

**REVIEW OF LOCAL BUSINESS TAX REVENUES**

**NOVEMBER 2009**




**CITY AUDITOR'S OFFICE  
CITY OF GAINESVILLE, FLORIDA**

*City of*  
**Gainesville**

*Inter-Office Communication*

November 30, 2009

**TO:** Audit, Finance and Legislative Committee  
Mayor Pegeen Hanrahan, Chair  
Mayor-Commissioner Pro Tem Scherwin Henry, Member

**FROM:**   
Brent Godshalk, City Auditor

**SUBJECT:** Review of Local Business Tax Revenues

**Recommendation**

The Audit, Finance and Legislative Committee recommend that the City Commission:

- 1) Accept the City Auditor's report and the response from the City Manager, and
- 2) Instruct the City Auditor to conduct a follow-up review on recommendations made and report the results to the Audit, Finance and Legislative Committee.

**Explanation**

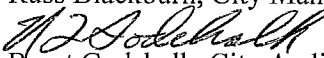
In accordance with our Annual Audit Plan, we have completed a Review of Local Business Tax Revenues. Our report, which includes a response from the City Manager, is attached for your review.

We request that the Committee recommend the City Commission accept our report and the management response. Also, in accordance with City Commission Resolution 970187, Section 10, Responsibilities for Follow-up on Audits, we request that the Committee recommend the City Commission instruct the City Auditor to conduct a follow-up review on recommendations made and report the results to the Audit, Finance and Legislative Committee.

*City of*  
**Gainesville**

*Inter-Office Communication*

November 23, 2009

**TO:** Russ Blackburn, City Manager  
**FROM:**   
Brent Godshalk, City Auditor  
**SUBJECT:** Review of Local Business Tax Revenues

In accordance with our Annual Audit Plan, we have completed a Review of Local Business Tax Revenues. During our review, we interviewed key personnel, analyzed financial and operating information and tested management controls. The primary objective of this audit was to evaluate the adequacy of management controls over the billing and collection of local business tax revenues.

Based on our review, we believe that the Budget and Finance Department has adequate internal controls in place over the billing and collection of local business tax revenues. Management has also established documented policies and procedures related to business tax collections and have implemented initiatives related to providing electronic billing and payment processes.

The attached draft report provides several recommendations we believe will assist management in strengthening the process of billing and collecting local business taxes. Our recommendations for improvement were reviewed with Treasurer Audrey Lewis during our exit conference held on October 27<sup>th</sup>. Since that time, Audrey has worked with Staff Auditor Brecka Anderson to finalize any necessary edits to our report and to provide written management responses to our recommendations. I would like to acknowledge Audrey and the members of the Treasury Division for their cooperation during our review.

Please review the attached written report, which documents our audit recommendations and the responses from the Budget and Finance Department, and let me know if you have any questions, comments or concerns with the information presented. Our final report, including the management responses, will then be submitted to the City Commission's Audit, Finance and Legislative Committee for review and approval. The next meeting is currently scheduled for November 30, 2009. Until that time, this draft report and your draft response are exempt from Florida's public records law.

Thank you to you and your staff for making this a productive process.

cc: Becky Rountree, Administrative Services Director  
Mark Benton, Finance Director  
Audrey Lewis, Treasurer  
Brecka Anderson, Staff Auditor

## OBJECTIVES, SCOPE AND METHODOLOGY

In accordance with our Annual Audit Plan, the City Auditor's Office completed a Review of Local Business Tax Revenues. The primary objective of this audit was to evaluate the adequacy of management controls over the billing and collection of local business tax revenues and to test business tax billing and revenue transactions for compliance with applicable laws, policies and procedures. Our procedures included interviewing key personnel, analyzing billing and collection information and testing management controls. The scope of our review was generally for local business tax billings and collections during fiscal years 2007 and 2008.

As for all of our audits, we conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Based on the results of our review, we have prepared several recommendations for improvement in the process of billing and collecting local business taxes, which were discussed with management. These recommendations, as well as management's written response, can be found in the following sections of this report.

## BACKGROUND INFORMATION

Chapter 205 of Florida Statutes authorizes the governing body of an incorporated municipality to levy, by appropriate resolution or ordinance, a business tax for the privilege of engaging in or managing any business, profession, or occupation within its jurisdiction. Accordingly, the City of Gainesville, through Section 25 of the Gainesville Code of Ordinances, levies a local business tax (formerly known as occupational licenses) for the privilege of engaging in or managing any business, profession or occupation within the city limits.

### *Levying Process*

Local Business Taxes are determined by preset business categories. Each business is categorized by the type of services or products offered. The amount of taxes levied may also depend upon the total number of employees or amount of inventory maintained by the business. For instance, Figure 1 below details applicable taxes for merchants in retail. The applicable amount of business tax levied depends on the cost value of inventory for the business at the most recent fiscal year end prior to June 1. For example, a clothing store with \$53,000 in inventory cost would pay \$262.50 in business taxes for the corresponding fiscal year.

**Figure 1**

<b>Cost Value of Inventory</b>	<b>Business Tax</b>
0 to \$5,000.00	52.50
\$5,001 to \$10,000	105.00
\$10,001 to \$20,000	157.50
\$20,001 to \$50,000	210.00
\$50,001 to \$100,000	262.50
\$100,001 to \$300,000	315.00
\$300,001 to \$500,000	420.00
Over \$500,000	525.00

### *Business Tax Exemptions*

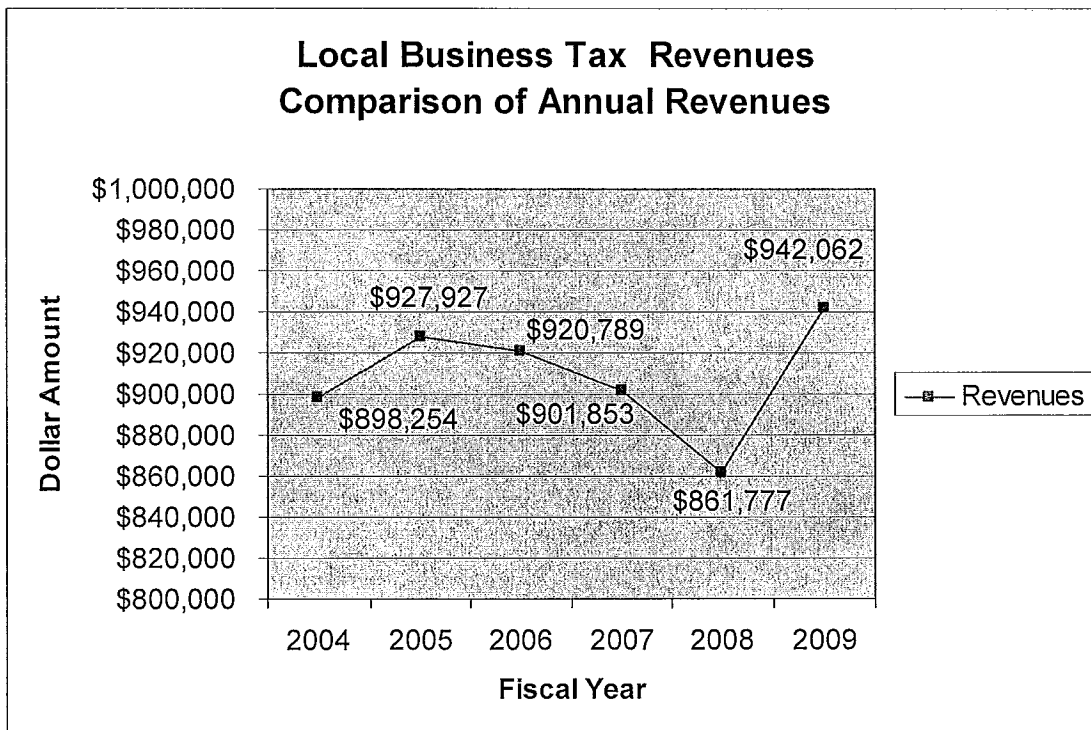
Exemptions from paying business taxes are generally provided by City ordinance for disabled persons, widows or widowers with minor dependents and persons 65 years of age and older, provided these persons live in Alachua County, employ one or less employee and use their own capital that is not in excess of \$1,000. Exemptions are also provided under specific circumstances to other categories such as veterans of war, college and high school students and employees of the University of Florida not holding themselves out to the public as available for practice of their professions.

Additionally, all persons who conduct their business, profession, or occupation at a permanent business location or branch office located in an area designated as an enterprise zone are exempt from 50 percent of the local business tax.

### *Annual Revenues*

Local business tax revenues are invoiced and collected by the Treasury Division of the City's Budget and Finance Department. Revenues are recorded in the General Fund and averaged approximately \$900,000 annually from fiscal year 2004 through 2009. As reflected in Figure 2 below, the City experienced a downward trend in business tax revenues in fiscal years 2006, 2007 and 2008, rebounding in fiscal year 2009. Some of the decline in revenues can be attributable to a reduction in field collection activities by the division, resulting from retirement and employee turnover. Local economic conditions have also contributed to this decline.

**Figure 2**



## ISSUE #1

### Identifying Businesses Required To Pay Local Business Taxes

#### Discussion

In order to evaluate the effectiveness of management's process of identifying businesses operating within city limits and required to pay a business tax to the City, we tested a random sample of business accounts within Gainesville city limits purchasing electricity from Gainesville Regional Utilities. We noted that six of the 359 businesses tested, or approximately 2% of our sample, had not been identified within the City's business tax system.

In evaluating the cause of this condition, we noted that management had lost one of their two local business tax field collectors due to a retirement and subsequent budget cuts in fiscal year 2007 and were unable to focus adequate resources in this area until a new collector was hired in late fiscal year 2008.

We also reviewed 12 businesses within the City's business tax system with the highest annual business tax, each equal to or exceeding \$1,500. We noted that most of these businesses were insurance companies and discovered that they had been contesting whether they were required to pay local business taxes due to not having office locations within Gainesville.

#### Conclusion

In our opinion, some of the decrease in local business tax revenue noted for fiscal year 2008 was due to the following issues:

- The Treasury Division was unable to actively identify and collect local business taxes as efficiently as in prior years during fiscal year 2008 due to the vacant Field Collector position.
- Customer tax statements were delayed due to issues related to implementing the local business tax online payment system.
- Beginning in fiscal year 2008, local business tax statements were sent to some customers via e-mail only. Some businesses indicated that they did not receive the e-mails due to spam filters and not utilizing their e-mail accounts on a consistent basis.

The City forgoes revenues such as potential earned interest when outstanding local business taxes are not collected timely. Additionally, the City spends more money pursuing non-paying or late-paying customers through staff time, office supplies and postage costs.

#### Recommendation

We recommend management:

- Implement an action plan to increase revenue collection activity. During our review, Billing and Collections hired a Field Collector to increase collection activity.
- Revise local business tax billing procedures to ensure that businesses are identified and notified appropriately and timely.
- Resolve the issue of non-payment by the businesses noted above as soon as possible.

### **Management's Response**

Management concurs that several issues converged to make 2008 a less effective year than normal related to business tax collections. Prior to 2008, the Budget & Finance Department had two full-time Field Collector positions. During 2008 one of these positions was eliminated as part of the department's budget reductions, and the performance of the remaining collector deteriorated to the point that the individual is no longer with the organization. As noted by the City Auditor, a new Field Collector was hired and collections are back on track.

There have been issues to overcome associated with the transition to the online payment system, and we continue to work through those issues. Notification processes were expanded to include a postcard in addition to the e-mail notifications provided to businesses.

## ISSUE #2

### Collecting Business Taxes and Late Payment Penalties

#### Discussion

The City's local business tax ordinance provides for delinquent fees and penalties for business taxes not renewed by the established due date. Additionally, any person who engages in business, but does not pay their local business tax within 180 days after the initial notice, is subject to a \$250.00 penalty and may be subject to civil actions and penalties.

Billing and Collections staff generally apply late fees to businesses whose business tax payments are not received by September 30 of each fiscal year. The amount of the late fees is staggered depending on the lateness of the payment, as noted in Figure 3 below.

**Figure 3**

Payment Period	Fee
After October 1	10%
After November 1	15%
After December 1	20%
After January 1	25%
After 180 days	\$250 penalty plus prior fees

In fiscal year 2008, the Treasury Division was involved in implementing E payment options for business taxes and did not include statements of business tax late fees on late notices mailed to customers, other than notice of the impending \$250 penalty if not paid within 180 days.

#### Conclusion

In fiscal year 2008, the City did not collect late fees that would otherwise have been due. An estimate of lost revenues could not be determined. This was corrected for fiscal year 2009.

#### Recommendation

We recommend management enhance procedures to ensure that all appropriate local business tax late fees and penalties are included on correspondences such as late notices.

#### Management's Response

Management concurs. Due to the relatively large number of businesses that reported that they did not receive notification of the business tax due, and the wording of the language on late notices, certain late fees were not pursued in the same manner as previous years. These notification issues have been addressed.



## ISSUE #3

### Controls Over City Assets and Receivables

#### Discussion

##### *Physical Controls Over City Assets*

City assets, including monies for deposit, are stored within the city vault, which is located within the vault room. The vault often remains unlocked during business hours. However, a door secures the vault room with entry restricted to those granted security card access.

During our review, we noted that two former employees and eight current Budget and Finance Department employees with responsibilities for journal entries and/or bank reconciliations had security access to the vault room. Although, no theft was discovered, employees with duties directly impacting accounting journals or bank reconciliations should not have access to physical monies.

##### *Check Documentation and Endorsement*

Businesses often remitted their business taxes using paper checks either by mail or by physically bringing the check to the Treasury Division of the Budget and Finance Department. During our review, we noted that some incoming business tax checks were not deposited promptly upon receipt. We noted that one check was not deposited for at least 45 days while awaiting additional paperwork from the customer.

Good accounting practices suggest the existence of adequate controls to ensure that checks are restrictively endorsed upon receipt and deposited in a timely manner. Potentially lost or diverted checks could go undetected due to the lack of endorsement or documentation.

#### Conclusion

In our opinion, the vault access and undocumented checks issues were due to the following weaknesses in internal control, respectively:

- There was not an adequate review when assigning ID card access.
- Daily processes did not allow sufficient time to endorse and document each check during business tax busy season.

#### Recommendation

We recommend management:

- Periodically review vault door access to ensure that employee duties do not conflict in order to protect city assets. During our review, management requested removal of vault room door access for the two former employees and the eight employees with conflicting duties.
- Enhance procedures to ensure that checks are restrictively endorsed upon receipt and are deposited in a timely manner.

**Management's Response**

Management concurs. Apparently the default setting for the security access for certain Accounting personnel provided access to the vault area, a fact of which these personnel were not even aware. As the City Auditor indicated this issue has been addressed, and we will periodically review access to the vault door to maintain appropriate security.

Occasionally checks for business tax payment are held while issues associated with the taxes they are meant to cover (prior year taxes, late fees, etc) are resolved, but we concur with the City Auditor that checks should be endorsed in a timely manner and we will continue to enhance our procedures to ensure that this is the case.