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Property Tax Exemptions

April 6, 2018



**City of Fort Worth
Department of Internal Audit**

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The Property Tax Exemptions Audit was conducted as part of the FY2017 Annual Audit Plan. The City Manager's Office requested the audit due to a concern that historic site tax exemptions were being calculated incorrectly.

Audit Objectives

The objectives of this audit were to determine whether:

- tax exemptions claimed were adequately supported and calculated accurately;
- tax exemptions were made in accordance with the intent of Mayor and Council actions;
- forms (used to request historic site tax exemptions) conform to applicable City ordinances;
- City ordinances are within the confines of Texas state law; and,
- eligible exemptions are codified.

Audit Scope

Our audit covered FY2016 and FY2017 property tax exemptions, with prior year research as needed.

Opportunities for Improvement

Improved monitoring of exemptions applied by the appraisal districts

Improved documentation for the historic exemption process

Revised forms and utilization of checklist(s) for historic exemptions

Timely notification to appraisal districts regarding re-platted exempt properties

Clear requirements within the historic exemption ordinance

Executive Summary

While the concern within the City Manager's Office was the calculation of historic site tax exemptions, we expanded our audit coverage to include:

- **General Homestead Exemptions** – exempt 20% of the appraised value of a property owner's principal residence;
- **Age 65 and Over Exemption & Tax Ceiling** – provide an additional \$40,000.00 exemption, and establish a tax ceiling at that level;
- **Neighborhood Empowerment Zone (NEZ) Abatements** – provide for non-taxation on the increase in improvement value for five years, in return for investment in new property;
- **Historic & Cultural Landmark Exemptions** – provide for the taxable value of the land and improvements to stay at pre-rehabilitation "base year" value for 10 years; and,
- **Highly Significant Endangered Exemptions** – provide that the improvements are not taxed, but land is taxed at the base year value for up to 15 years.

Based on our audit results, we found that exemption calculation errors resulted in tax under and overpayments. In addition, we concluded that City staff sometimes submitted information to the Mayor and Council that was inconsistent with that submitted to the Tarrant Appraisal District (TAD). There was also one instance where a historic exemption was not submitted for Mayor and Council approval as was required. In addition, one refund was processed based on six years instead of the five-year maximum.

We identified general homestead exemptions applied to properties where owner residency was questionable. For example, some properties appeared to be rental property or demolished. We also identified instances where more than one property with an exemption had the same owner name and address. Exemptions that appear questionable may be valid in specific circumstances. The questioned exemptions were sent to TAD for further review.

The Department of Internal Audit identified properties, with age 65 and over exemption and tax ceilings that were in the name of an estate. We concluded that NEZ abatements were erroneously applied to 10 properties for six years (instead of the five-year maximum), with approximately \$34,323.00 in City taxes abated for the sixth year.

Under Texas State law, appraisal districts have the responsibility to process exemption applications, determine eligibility, and calculate exemptions. The City notifies the appraisal districts about historic property tax exemptions and NEZ abatements; however, the property owner is responsible for applying to the appraisal district on a yearly basis to maintain the exemption. For other exemptions, the property owner applies directly to the appraisal district.

The Department of Internal Audit referred 829 properties to TAD for follow-up, including 290 accounts that were not billed as of December 2017/January 2018. As of the end of our audit fieldwork, TAD had processed exemption adjustments and/or Tarrant County had billed 362 accounts, totaling approximately \$1,187,376.00. TAD indicated that pending protests and exemption applications delayed billing for many of these properties.



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Methodology

To achieve the audit objectives, the Department of Internal Audit:

- interviewed City, Tarrant County, Tarrant Appraisal District, and Denton Central Appraisal District personnel, along with Dallas and Travis County Central Appraisal District personnel;
- reviewed City ordinances and state law;
- downloaded and analyzed TAD and Denton Central Appraisal district data;
- queried data files provided by Tarrant County;
- used on-line and other data sources to verify property owners' residences and eligibility for exemptions;
- reviewed on-line newspaper obituaries;
- recalculated exemptions;
- reviewed supporting documents for historic exemptions and NEZ abatements;
- reviewed exemptions granted by other cities;
- verified Mayor and Council approval for exemptions; and,
- evaluated City internal controls related to property tax exemptions.

We conducted this 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.



Audit Results

The Department of Internal Audit confirmed that historic site tax exemptions were sometimes erroneously calculated. We concluded that miscalculations resulted from the City’s ordinance being unclear regarding the calculation methodology for historic site tax exemptions; miscommunication between City of Fort Worth staff and TAD; and, the erroneous use by TAD of prior year property values, etc.

On December 12, 2017, the Department of Internal Audit presented interim audit results to the City of Fort Worth’s Audit Committee. Interim reporting was considered necessary to provide City management and the Audit Committee with information considered helpful when making necessary revisions to the City ordinance, and to allow management the opportunity to correct some property tax errors during the current property tax year.

Since our interim report, the Department of Internal Audit conducted additional testing. As of January 27, 2018, our results are as follows.

Audit Exceptions Summary

Category	Total Count	Exception Summary					
		Interim Tested		Referred to TAD		Corrected/Billed ¹	
		Count	Estimated Amount	Count	Estimated Amount	Count	Amount
Historic Site	381	381	\$76,853	125	\$76,853	TBD ²	TBD ²
General Homestead	137,907	121	\$19,727	330	\$76,502	26	\$13,918
65 and Older Years of Age ³	35,680	74	\$25,102	74	\$25,102	56	\$58,713
NEZ Abatements	95	52	\$34,323	10	\$34,323	1	\$6,985
Exemptions subtotal	174,063	628	\$156,005	539	\$212,780	83	\$79,616
Residential property (2017 tax)	244,055	254	\$338,870	254	\$338,870	244	\$321,804
Commercial property (2017 tax) ⁴	28,614	0	\$0	36	\$830,179	35	\$785,956
Unbilled subtotal	272,669	254	\$338,870	290	\$1,169,049	279	\$1,107,760
Totals	446,732	882	\$494,875	829	\$1,381,829	362	\$1,187,376

Note: 1 Billed as of January 27, 2018. TAD had not reviewed all exemptions at the time of this report. Exemptions identified as questioned and forwarded to TAD for review may have been found to be valid.

2 Historic exemption calculation errors identified may require more research and legal review, prior to determining amounts collectible.

3 TAD removed 65 years and older exemption and tax ceilings in the name of an estate. However, the corrections included multiple years, resulting in a larger billed amount, but fewer accounts.

4 The initial audit testing scope did not include a search for unbilled accounts. Subsequent to the initial testing, we identified unbilled accounts that were researched and referred to TAD.

Amounts represent: City of Fort Worth taxes only; do not include taxes for school districts or other taxing entities; and include 2016 taxes that were due no later than January 31, 2017, unless stated otherwise.



Historic Property Tax Exemptions: We identified the following historic property tax exemptions errors:

- exemptions renewed by TAD without a required annual application [22 properties];
- multiple calculation errors, resulting in net tax underpayments;
- one (1) property received an exemption after obtaining approval from the Historic and Cultural Landmarks Commission, but without Mayor and Council approval;
- one (1) property received a refund for six years, although the law specifies a five-year maximum, resulting in an over refund of approximately \$73,102.00;
- differences existed between pre-rehab (base year) values approved by the Mayor and Council, and the values communicated to TAD [six (6) properties];
- property exemptions that were continued after the term expired [three (3) properties]; and,
- different exemption expiration dates sent to TAD for the same property.

We also concluded that the method used to calculate homestead exemptions (when combined with the method used to calculate historic property tax exemptions) results in a decrease in the tax levy as the property value increases. (See Exhibit I) This result is not consistent with the intent of the historic exemption, which is to prevent an increase in assessed value for the exemption term. Tarrant County and TAD personnel stated that historic exemption tax reductions are included in the permanent tax ceiling for properties with a 65 and over exemption and tax ceiling.

The historic site tax ordinance is codified and consistent with state law. However, revisions are necessary to clarify certain provisions. For example, the ordinance should clarify the number of years that may lapse between the application or rehabilitation and the application for tax exemption along with the extent to which additions to existing structures are eligible. TAD personnel agreed that the historic property tax exemption calculations could be changed to reflect the intent of the exemption.

General Homestead Tax Exemptions: We queried the population of 137,907 properties with homestead exemptions and identified properties that appear to be ineligible. However, the appraisal district has responsibility to allow or deny eligibility. Questioned general homestead exemptions included:

- property owners with more than one exempt property [116 properties];
- properties where the owner address is outside the state of Texas [104 properties];
- properties where the owner appears to reside at a different property [98 properties];
- properties where the structure had been demolished [one property]; and/or,
- exempt property in the name of a business [11 properties].

Over 300 general homestead exemptions were questioned and referred to TAD. As of the end of audit fieldwork, TAD had begun the process of resolving the questioned exemptions, which could be a time-consuming task. TAD personnel stated that they review exemptions periodically for compliance and noted that exemptions that appear to be invalid may be appropriate in specific circumstances.

Age 65 and Over Exemption and Tax Ceiling: We identified properties in the name of an estate where the prior owner appeared to have been deceased for more than one year, with no identified surviving spouse. Subsequent inquiry indicated that TAD removed 54 of the questioned age 65 and over tax exemption and tax ceilings, equating to approximately \$25,102.00 for 2016 only. We noted that as TAD corrected the ineligible property accounts, additional amounts were removed for other years. It should be noted that based on the testing of a sample of properties, Internal Audit did not identify properties considered ineligible based on the age of the property owner or surviving spouse.



Neighborhood Empowerment Zone (NEZ) Abatements: We identified 10 properties that received abatements after the terms expired. Subsequent inquiry indicated that one of the 10 properties was “back-billed.” However, as of end of audit fieldwork, no changes had been made to the remaining nine properties. NEZ abatements would be included in the value used for the age 65 and over tax ceiling.

Another property did not receive the abatement for the initial year due to re-platting of the property, which resulted in a change in property account numbers.

Unbilled Property Accounts: During the review of exemptions, we identified three property accounts with no tax levy for 2017. With additional review, we identified an estimated \$338,870.00 in unbilled residential properties as of mid-December 2017, and an estimated \$830,179.00 in unbilled commercial properties as of January 20, 2018. A majority of the unbilled residential accounts identified were billed as of January 26, 2018, and a majority of the unbilled commercial accounts were billed by January 27, 2018. TAD personnel stated that accounts unbilled in December and January typically result from pending protests or delayed exemptions.



Recommendations

Recommendation 1. Management should follow up with TAD and/or Tarrant County regarding any unresolved, potential errors identified by Internal Audit.

Auditee Response: Concur.

Target Implementation Date: Complete

Responsibility: Planning & Development, Neighborhood Services, Performance & Budget

This would be the responsibility of the department with oversight of the exemption in question:

Historical Exemption – Planning & Development, Performance & Budget

NEZ Abatement – Neighborhood Services

Homestead, Age 65 and Over, and all other – Performance & Budget

Recommendation 2. Management should clarify ambiguities within the current historic exemption ordinance.

Auditee Response: Concur.

Target Implementation Date: Complete

Responsibility: Planning & Development

Recommendation 3. Management in conjunction with TAD, should revise the form used to communicate historic site exemptions to TAD.

Auditee Response: Concur.

Target Implementation Date: Complete

Responsibility: Planning & Development

Recommendation 4. Management should utilize a checklist to help verify the accuracy and completeness of information sent to TAD.

Auditee Response: Concur.

Target Implementation Date: Complete

Responsibility: Performance & Budget, Planning & Development



Recommendation 5. *Management should document historic site tax exemption procedures, and flowchart processes.*

Auditee Response: Concur.

Target Implementation Date: Complete

Responsibility: Planning & Development

Recommendation 6. *Management should enhance monitoring of historic, NEZ and other exemptions on a sample basis. (i.e. historic – mathematical accuracy, NEZ – term expiration).*

Auditee Response: Concur (Planning & Development Department), Concur (Neighborhood Services Department).

As part of its regular audit review of NEZ applications, Neighborhood Services will increase scrutiny on tax abatements as they approach expiration and will increase communication with TAD to ensure the tax abatements do not go beyond its intended life span.

Target Implementation Date: Completed for historic site tax exemptions and NEZs

Responsibility: Performance & Budget, Planning & Development, Neighborhood Services

Recommendation 7. *Management should annually review county assessment and tax records to ensure that Fort Worth properties were billed.*

Auditee Response: Concur.

Target Implementation Date: 4th calendar year quarter – when contract is up for renewal.

Responsibility: Budget will need to determine how this can be done and formulate a policy. Budget will work with FMS and Legal to review and update the contract with the County to make sure we can obtain the required and basic information and include current language for performing our own audits.

Recommendation 8. *Management should request that Tarrant County periodically provide a complete property billing file and ensure that future tax collection contracts include a requirement to provide a complete property billing file.*

Auditee Response: Concur.

Target Implementation Date: 4th calendar year quarter – when contract is up for renewal.

Responsibility: Budget will work with FMS and Legal to review and update the contract with the County to make sure we can obtain the required and basic information and include current language for performing our own audits.

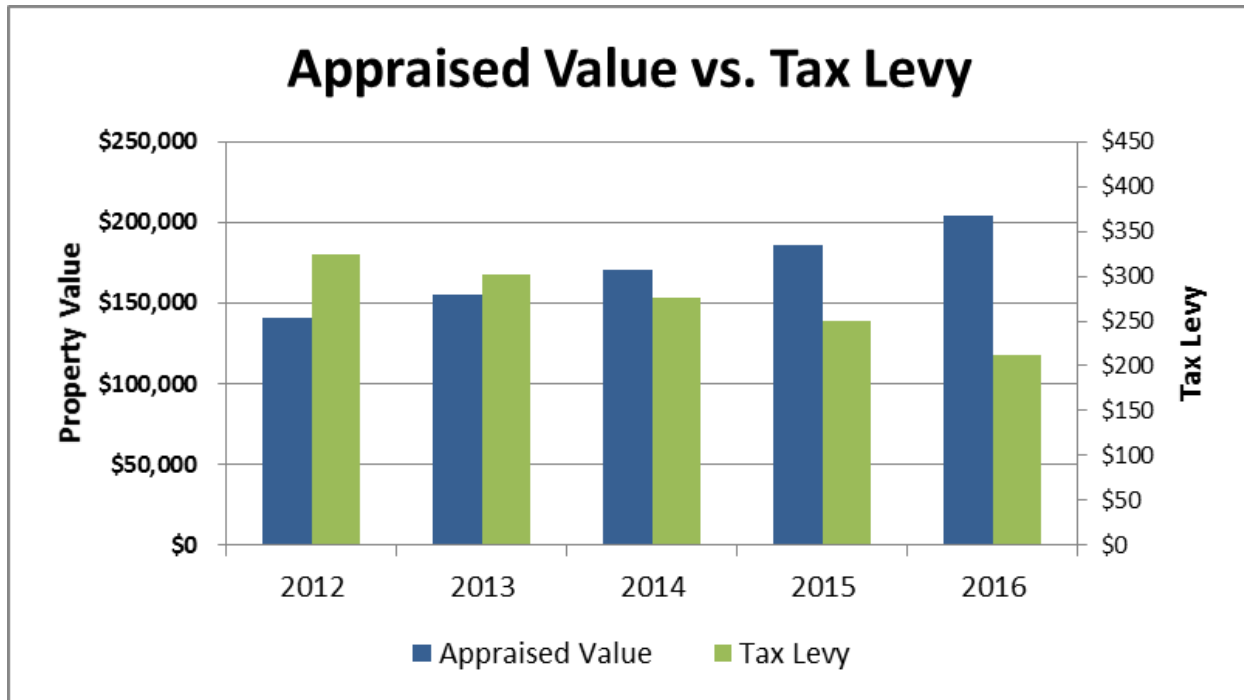


Acknowledgements

The Department of Internal Audit would like to thank the Planning & Development, Performance & Budget, and Neighborhood Services Departments, the City Attorney's Office, Tarrant Appraisal District, and Tarrant County personnel for their cooperation and assistance during this audit.

Exhibit I – Combined Historic & Homestead Exemptions

The graph below shows an example property with both historic and homestead exemptions. The effect of the current method of calculating the homestead exemption when combined with the method of calculating the historic exemption results in a reduced tax levy as the property value increases.



Source: TAD and Tarrant County Tax Data

The Appraised Value bars in the graph above show the appraised value of the property per the appraisal district, which increased each year.

The Tax Levy bars show that as the appraised value increased every year, the tax levy decreased. The tax rate remained the same except for a decrease of 2.3% in 2016. The effect appears contrary to the intent of the historic tax exemption ordinance, which is to maintain the appraised value at the pre-rehabilitation value for the term of the exemption.