

STATE OF FLORIDA AUDITOR GENERAL

Performance Audit

DEPARTMENT OF REVENUE

Administration of the Ad Valorem Tax Program



Sherrill F. Norman, CPA
Auditor General

Head of the Department of Revenue and the Executive Director

Pursuant to Section 20.21(1), Florida Statutes, the head of the Department of Revenue is the Governor and Cabinet, which includes the Attorney General, Chief Financial Officer, and the Commissioner of Agriculture. Pursuant to Section 20.05(1)(g), Florida Statutes, the Governor and Cabinet are responsible for employing an Executive Director of the Department of Revenue. Marshall Stranburg served as the Executive Director during the 2013 and 2014 in-depth reviews.

The team leader was Mark A. Hesoun and the audit was supervised by Michael J. Gomez, CPA.

Please address inquiries regarding this report to Marilyn D. Rosetti, CPA, Audit Manager, by e-mail at marilynrosetti@aud.state.fl.us or by telephone at (850) 412-2881.

This report and other reports prepared by the Auditor General are available at:

www.myflorida.com/audgen

Printed copies of our reports may be requested by contacting us at:

State of Florida Auditor General

Claude Pepper Building, Suite G74 • 111 West Madison Street • Tallahassee, FL 32399-1450 • (850) 412-2722

DEPARTMENT OF REVENUE

Administration of the Ad Valorem Tax Program

SUMMARY

This performance audit focused on the Department of Revenue's (Department's) administration of the Ad Valorem Tax Program related to the ad valorem tax rolls, and included a follow-up on findings noted in our report No. 2013-034. Our audit disclosed the following:

In-Depth Reviews

Finding 1: As similarly noted in our report No. 2013-034, Department appraisal records did not always reasonably support property value estimates.

Finding 2: The Department analyzed some multifamily residential properties in a manner inconsistent with State law.

Finding 3: Contrary to State law, personal property values reported to the Department on county assessment rolls were not included in the Department's in-depth reviews.

Other Property Oversight Issues

Finding 4: The Department's policy of allowing county property appraisers, when deriving just valuation, to adjust net proceeds by up to 15 percent without justification or documentation had no documented basis.

Finding 5: Contrary to State law, the Department did not maintain a current property tax administration manual with up-to-date guidelines.

Certification Programs

Finding 6: Department procedures for the administration of the Certification Program Trust Fund needed improvement.

BACKGROUND

Pursuant to State law,¹ the Department of Revenue (Department) is responsible for the general supervision of the assessment and valuation of property so that all property is placed on the tax rolls and is valued according to its just valuation, as required by the State Constitution. The Department is also responsible for the supervision over tax collection and all other aspects of the administration of such taxes, primarily assisting county officers in the assessment and collection functions, with particular emphasis on the more technical aspects. In this regard, the Department conducts training to upgrade the assessment skills of both State and local assessment personnel. Additionally, State law requires the Department to:

¹ Section 195.002, Florida Statutes.

- Prescribe reasonable rules and regulations for the assessment and collection of taxes, which are to be followed by property appraisers, tax collectors, clerks of the circuit court, and value adjustment boards.²
- Promulgate rules and regulations for the exchange of information among the Department, property appraisers, tax collectors, the Auditor General, and the Office of Program Policy Analysis and Government Accountability.³
- Establish and promulgate standard measures of value, consistent with those standards provided by State law, to be used by property appraisers in all counties, including taxing districts, to assist them in arriving at assessments of all property.⁴
- Conduct research and maintain accurate tabulations of data and conditions existing as to ad valorem taxation. Annually publish such data as may be appropriate to facilitate fiscal policymaking, and annually make such recommendations to the Legislature as are necessary to ensure that property is valued according to its just value and is equitably taxed throughout the State.⁵
- Prepare and maintain a current manual of instructions for officials connected with the administration of property taxes.⁶
- Promulgate uniform definitions for all classifications of property.⁷
- Annually determine whether counties and municipalities are assessing the real and tangible personal property within their jurisdiction in accordance with State law.⁸
- Issue a notice to any property appraiser who the Executive Director has determined has one or more classes of property listed on the assessment rolls in a manner inconsistent with the requirements of State law, or is otherwise not assessing property in accordance with State law.⁹
- Review the assessment rolls of each county and conduct, at least every 2 years, an in-depth review of the assessment rolls of each county.¹⁰

FINDINGS AND RECOMMENDATIONS

IN-DEPTH REVIEWS

As noted in the **BACKGROUND** section, the Department must review the assessment rolls of each county and conduct, at least every 2 years, an in-depth review of the assessment rolls of each county. The results of the in-depth reviews are to include all statistical and analytical measures computed for the real property assessment roll as a whole, the personal property assessment roll as a whole, and independently for the following seven classes of real property, commonly referred to as strata, established in State law:¹¹

² Section 195.027(1), Florida Statutes.

³ Section 195.084(1), Florida Statutes.

⁴ Section 195.032, Florida Statutes.

⁵ Section 195.052, Florida Statutes.

⁶ Section 195.062, Florida Statutes.

⁷ Section 195.073, Florida Statutes.

⁸ Section 195.101, Florida Statutes.

⁹ Section 195.097(1)(a), Florida Statutes.

¹⁰ Section 195.096(1) and (2), Florida Statutes.

¹¹ Section 195.096(3)(a), Florida Statutes.

- Residential property that consists of one primary living unit, including, but not limited to, single-family residences, condominiums, cooperatives, and mobile homes.
- Residential property that consists of two or more primary living units.
- Agricultural, high-water recharge, historic property used for commercial or certain nonprofit purposes, and other use-valued property.
- Vacant lots.
- Nonagricultural acreage and other undeveloped parcels.
- Improved commercial and industrial property.
- Taxable institutional or governmental, utility, locally assessed railroad, oil, gas and mineral land, subsurface rights, and other real property.

The Department's published standards for tax roll approval require that a county's assessment for an individual stratum, and in total, be at least 90 percent of market value (i.e., a 90-percent level of assessment). Pursuant to State law,¹² when one or more of these strata of real property listed on the assessment rolls are inconsistent with these requirements, the Department is to issue a notice to the applicable county property appraiser describing the necessary corrections. If the corrections are not made, the Department will disapprove the assessment roll and begin the process outlined in State law¹³ for an interim assessment roll.

For the conduct of in-depth reviews, the Department uses the sales-ratio methodology, the appraisal-ratio methodology, or a combination of the two. The sales-ratio methodology is utilized in value groups of strata with adequate sales data. Value groups are subgroups of strata arrayed by value and divided into quartiles by parcel count that provide a more detailed analysis of representative properties within each stratum. In the value groups of strata with inadequate sales data, the appraisal-ratio methodology is used either exclusively or to supplement the sales-ratio methodology.

For the 2013 and 2014 in-depth reviews for some strata, the Department used time-trended sales from up to 36 months prior to January 1 of the in-depth review year to obtain a sufficient number of sale samples for analyzing the various strata and value groups. Time-trended sales analysis, which is also referred to as sales-ratio trend analysis, is a method that tracks sales ratios (or their reciprocals) over time.¹⁴ Using this analysis, the Department could reduce its reliance on independent appraisals, which are more labor-intensive than using sale samples.

Using the appraisal-ratio methodology, Department staff perform individual appraisals on a random sample of parcels in various strata and value groups, and compare their value estimates with the county property appraisers' values to determine whether the values are reasonable and within specified thresholds. To determine estimated market values of property, Department staff use the following approaches described in *The Appraisal of Real Estate*:¹⁵

- **Sales Comparison Approach.** This approach estimates the market value of property based on recent sales of comparable properties, with appropriate quantitative or qualitative adjustments to

¹² Section 195.097, Florida Statutes.

¹³ Section 193.1145, Florida Statutes.

¹⁴ International Association of Assessing Officers publication, *Mass Appraisal of Real Property*.

¹⁵ Appraisal Institute's publication, *The Appraisal of Real Estate*, 14th Edition.

the comparable properties for any value-influencing dissimilarity between the property and comparable properties. The value indicators for each comparable sale are then reconciled to arrive at the estimated value of the property.

- **Cost Approach.** This approach estimates the current cost to construct a reproduction of (or replacement for) the existing structure, including a profit or entrepreneurial incentive; deducting depreciation from the total cost; and adding the estimated land value. If applicable, other adjustments may be made to the indicated value if a different partial interest is being valued. To estimate improvement costs as of the date of value, Department appraisers utilized a third-party national valuation service.
- **Income Approach – Direct Capitalization.** This approach uses a market-derived (based on similar properties) estimate of one year’s potential gross income, a deduction for vacancy and collection loss, and a deduction for operating expenses, resulting in net operating income that is capitalized into value using an appropriate capitalization rate that reflects one year’s anticipated risk and return characteristics.

When one class (stratum) of real property constitutes less than 5 percent of a county’s total assessed value of all real property on the previous assessment roll, the Department may combine it with one or more other strata of real property for purposes of the in-depth review or use the weighted average of the other strata for purposes of calculating the level of assessment for all real property in a county.¹⁶ Table 1 summarizes the number of sale and appraisal sample items, by stratum, for all counties subject to a 2013 or 2014 in-depth review. Strata 2, 5, and 7 each constituted less than 5 percent of the value of the tax roll for each county and, therefore, were not studied.

**Table 1
Sale and Appraisal Sample Items by Stratum**

Stratum	2013			2014		
	Qualified Sales ^a	Appraisals	Total	Qualified Sales ^a	Appraisals	Total
1	114,989	34	115,023	117,515	138	117,653
3	-	451	451	-	543	543
4	1,400	209	1,609	2,452	198	2,650
6	765	962	1,727	618	686	1,304
Totals	<u>117,154</u>	<u>1,656</u>	<u>118,810</u>	<u>120,585</u>	<u>1,565</u>	<u>122,150</u>

^a Includes time-trended sales for strata 1 and 4.

When the Department’s in-depth review is complete, each county property appraiser may review with Department staff each appraisal sample item utilized in the study and sales qualifications exceptions. After the review, a summary report is produced indicating the results of the in-depth review, which is used in the tax roll approval process. The Department certifies estimated levels of assessment for each county and Statewide to the Commissioner of Education for use in the equalization of required local effort funding for school districts.

¹⁶ Section 195.096(3)(a), Florida Statutes.

Finding 1: Appraisal-Ratio Studies

As indicated in Table 1, appraisals were used extensively in the Department's ratio studies of strata 3, 4, and 6 for the 2013 and 2014 in-depth reviews. Department guidelines¹⁷ provide that all data used in the appraisal and review processes must be as complete, accurate, and consistent as possible.

As the Department's in-depth review relied, in part, on appraisals of sampled properties, we tested Department appraisals for strata 4 and 6. We excluded stratum 3 (primarily agricultural property), which was assessed based on use rather than market value appraisals. To determine whether the Department's appraisals were consistent with applicable generally accepted appraisal practices and Department policies, procedures, and guidelines, we reviewed 60 Department appraisals, including 15 Department appraisals each in Escambia and Hernando Counties (2013 in-depth review) and 15 appraisals each in Gilchrist and Putnam Counties (2014 in-depth review). For the 60 appraisals reviewed, the Department used the sales comparison approach exclusively for 25 appraisals, the cost approach exclusively for 24 appraisals, a combination of the sales comparison and cost approaches for 6 appraisals, and the income approach for 5 appraisals.

Our review disclosed that Department appraisal records did not always reasonably support the value estimates for properties. For example:

- One appraisal in Gilchrist County valued a rural vacant tract measuring 30 feet wide by 1,320 feet deep. The appraiser described it as being a residential tract of adequate size and shape with good overall utility and marketability as a residential property and analyzed it as being comparable in functional utility to the three normally shaped residential tracts used as comparables. However, the appraiser's analysis did not acknowledge the unlikely development potential of this tract for residential purposes due to its extreme narrow dimensions.
- For an appraisal in Putnam County, the appraiser used an incorrect site size of 176,474 square feet in the site value calculation, instead of the actual site size of 17,674 square feet as stated in the appraisal. This error caused the site value conclusion of \$70,590 to be overstated by \$63,520.
- For another appraisal in Putnam County, the appraiser only included 5,038 square feet (50 percent) of the total 10,085 square feet of building area to determine the depreciated cost of the improvements, using the cost approach, with no mention of the omitted 5,047 square feet. Had the total square footage been considered, the value conclusion would have been \$457,000, or \$226,000 more than the appraiser's calculation.
- In the land valuation section of two appraisals in Hernando County, and the corresponding sale verification data sheet, there was a material omission of 24 acres from the size of a land sale, which may have had a material impact on the property value conclusion. The appraiser identified the land sale size as 4.46 acres, rather than 28.46 acres as reported on the deed. Although the sale included two adjacent parcels, the appraiser only acknowledged one parcel in the transaction, overstating the price per square foot and likely affecting the value conclusion.
- For two appraisals in Escambia County, there were inconsistent or incorrect statements of the highest and best use of the subject property. One appraisal indicated the highest and best use was its current use, a parking lot, while elsewhere the highest and best use was stated to be a medical facility. In the other appraisal, while the subject property was a fast food restaurant, in two places the highest and best use was stated to be "its current use as a warehouse." As such,

¹⁷ Section 2.6 of the Department's *Real Property Field Manual*.

the basis for the conclusion of each appraisal was not readily apparent since the statements on the highest and best use of the subject property were inconsistent.

- For an appraisal in Gilchrist County, there were inconsistencies between the sales comparison grid and the narrative analysis of the sales. For example, there were inconsistencies for the location, age, condition, gross building area, and traffic count elements of one of the comparable sales. The concluded value per square foot was also inconsistent between the sales comparison grid and narrative analysis.
- For three appraisals in Hernando County, the appraiser used an improved sale in the land valuation analyses with no discussions or adjustments for the improvements (a cellular telephone tower, communications building, and associated improvements). In two of these analyses, the appraiser gave primary weight to this sale, which may have impacted the value conclusion.
- Thirty-one appraisals for properties in Escambia, Gilchrist, and Hernando Counties included unsupported size adjustments using the sales comparison approach. Twenty-nine of the appraisals reported the support as being the economies of scale theory, which implies that smaller properties typically sell for more per square foot than larger properties with all other elements being equal, and two did not report any basis for the support. However, none of these size adjustments included market evidence for support.

Without complete, accurate, consistent, and relevant analyses and conclusions to support appraisals, the Department's ability to properly evaluate tax rolls may be limited and property tax assessments may be incorrect. A similar finding was noted in our report No. 2013-034.

Recommendation: The Department should ensure that all appraisals are adequately documented and supported by complete, accurate, consistent, and relevant analyses and conclusions.

Finding 2: Multifamily Properties

As previously discussed, in reviewing the property assessment rolls of each county, the Department is to conduct in-depth reviews of real property classes, or strata, which constitute 5 percent or more of the county's total assessed value of real property on the previous assessment roll. Furthermore, residential properties that consist of two or more primary living units are to be included in stratum 2 for in-depth review purposes.¹⁸

Our review of properties included in each stratum for the 2013 and 2014 in-depth reviews disclosed that, contrary to State law, the Department included multifamily residential properties with ten or more primary living units in stratum 6 (commercial and industrial property) rather than stratum 2 (residential property that consists of two or more primary living units). As a result, stratum 2 comprised less than 5 percent of the value of the tax rolls for each county and, therefore, was not studied in the in-depth reviews. Further, the Department attributed a greater emphasis to stratum 6 than intended by State law.

Department personnel indicated that larger multifamily residential properties were reclassified from stratum 2 to stratum 6 because, in their opinion, they are viewed by buyers and sellers as commercial properties. However, Department records did not evidence the legal basis upon which the property reclassifications were made for in-depth review purposes.

¹⁸ Section 195.096(3)(a), Florida Statutes.

Recommendation: The Department should include multifamily residential properties in stratum 2, as required by State law, or document the legal basis upon which the property reclassifications were made for in-depth review purposes.

Finding 3: Review of Personal Property Assessment Rolls

State law¹⁹ provides that county property assessment rolls include taxable values for both real property and personal property and are subject to review by the Department. The Department must publish the results of the reviews, which are to include all statistical and analytical measures prescribed by State law for the personal property assessment roll as a whole. In addition, State law²⁰ requires the Department to annually certify to the Commissioner of Education (DOE) certain data on taxable values (including personal property) for school funding purposes.

Our review of Department procedures for reviewing personal property disclosed that such procedures were limited to verification (i.e., mathematical accuracy, completeness, etc.) of the data received from the county property appraisers and did not include statistical and analytical measures of the personal property assessments in the in-depth reviews. Department personnel indicated that, based on a 1997 court case, the Department was not mandated by State law to review personal property. However, our review of the court-related documentation did not identify any language that would negate the Department's responsibility to review the personal property assessment roll as a whole for each county (i.e., to review the reasonableness and credibility of the personal property values in each county).

Although personal property is a small portion (8 percent) of the Statewide property assessment roll,²¹ personal property is significant to some individual counties. For example, for the 2014 tax year, there were 16 counties where the percentage of personal property to total property ranged from 22 percent (Madison County) to 53 percent (Hamilton County), with an average of 30 percent. When a significant portion of a county's property assessment roll is excluded from the Department's in-depth reviews, the results of such reviews may not adequately support the information certified to the DOE for school funding purposes.

Recommendation: The Department should include personal property in its in-depth reviews as required by State law.

OTHER PROPERTY OVERSIGHT ISSUES

Finding 4: Adjustments for the 8th Factor

State law²² provides for the just valuation of property by requiring county property appraisers to consider eight factors when deriving just value. The 8th factor is defined in law as "the net proceeds of the sale of the property, as received by the seller, after deduction of all the usual and reasonable fees and costs of the sale, including the costs and expenses of financing, and allowance for unconventional or atypical

¹⁹ Section 195.096(1) and (3)(a), Florida Statutes.

²⁰ Section 1011.62(4), Florida Statutes.

²¹ 2014 Taxable Value of all Property Types from the Department's Property Tax Data Portal.

²² Section 193.011, Florida Statutes.

terms of financing arrangements. When the net proceeds of the sale of any property are utilized, directly or indirectly, in the determination of just valuation of realty of the sold parcel or any other parcel . . . the property appraiser, for the purposes of such determination, shall exclude any portion of such net proceeds attributable to payments for household furnishings or other items of personal property.”²³

Since 1982, Department rules²⁴ have required county property appraisers to only justify or document any 8th factor adjustments exceeding 15 percent and Department records did not evidence the basis for this percentage. In the 3 decades since 1982, many usual and reasonable fees and costs of the sale, as well as costs of financing, have likely changed. For example, the tax on real property deeds conveyed to a purchaser is considered a cost of the sale and, in 1982, the tax was 45 cents per \$100 of the consideration given (i.e., sales price), whereas the current tax is 70 cents per \$100 of the consideration given, an increase of 56 percent.

In 2011, the Department prepared an *Eighth Criterion Feasibility Report (Report)* wherein the Department listed the difficulties of conducting a study to support 8th factor adjustments. The listed difficulties included an unwillingness of the public to share personal financial information, the lack of statutory provisions compelling marketplace participants to respond to requests for such information, incomplete or inaccurate data for expenses paid outside the closing process, and resource infeasibility for the Department and county property appraisers. The *Report* concluded that the Department’s current practice of requiring counties to provide support data and statistical analysis for adjustments exceeding 15 percent was the most efficient option.

Our review of the 8th factor adjustments reported to the Department for the 2013 and 2014 property assessment rolls disclosed that 65 of the 67 county property appraisers (97 percent) deducted 15 percent from all recorded selling prices. The remaining 2 property appraisers reported varying adjustments as the Alachua County Property Appraiser reported total adjustments of 5 to 15 percent for each of the 2013 and 2014 tax years, and the Broward County Property Appraiser reported total adjustments of 8 to 11 percent for the 2013 tax year and 10 percent for the 2014 tax year. Both County Property Appraisers indicated that the percentages used were based on limited market surveys that included consideration of buyer and seller costs.

Use of an adjustment not representing actual fees and costs of sale could have a significant fiscal impact on school funding and local government revenues, as property values are considered in these revenue projections. Accordingly, it is important for county property appraisers to utilize factual information to arrive at accurate 8th factor adjustments and for the Department to utilize such information to determine whether the adjustments are reasonable, supportable, and accurately represent the marketplace.

Recommendation: So that county property appraisers and the Department have the information necessary to accurately calculate 8th factor adjustments, the Legislature should consider enacting legislation to require disclosure of the data elements to be considered in 8th factor adjustments. In the interim, the Department, in consultation with the county property appraisers, should ensure that the basis for 8th factor adjustments made by county property appraisers are reasonable, supportable, and accurately represent the marketplace.

²³ Section 193.011(8), Florida Statutes.

²⁴ Department Rule 12D-8.002(4), Florida Administrative Code.

Finding 5: Property Tax Administration Manual

State law²⁵ requires the Department to prepare and maintain a current manual of instructions for county property appraisers and other officials connected with the administration of property taxes. The manual must contain all rules and regulations, standard measures of value, forms, and instructions relating to the use of forms and maps. Guidelines associated with standard measures of value may be updated annually to incorporate new market data, technical changes, changes indicated by established decisions of the Supreme Court, and other changes relevant to appropriate assessment practices or standard measurement of value.

As part of our audit, we reviewed the Department's *Manual of Instructions and Guidelines (Manual)* located on the Department's Web site and found that portions of the *Manual* had not been updated in several years. For example, the Department had not updated the *Real Property Appraisal Guidelines* since 2002, and, therefore, those *Guidelines* did not include subsequent statutory changes regarding the highest and best use considerations. Additionally, the Department issued the most recent *Tangible Personal Property Appraisal Guidelines* in 1997 and the *Classified Use Real Property Guidelines* in 1982. Considering that county property appraisers and other interested parties rely on information contained in the *Manual* for the proper administration of property taxes, and the possible consequences of outdated guidance, it is important that the *Manual* be up to date.

Department personnel indicated that delays in updating the *Manual* were due to resource constraints and the need to promulgate new rules and forms for recently enacted legislation. Subsequent to our inquiry, the Department implemented a policy requiring legal staff to review all guidelines annually upon completion of each Legislative Session.

Recommendation: The Department should continue efforts to maintain a current *Manual* and annually update guidelines, as appropriate, in accordance with State law.

CERTIFICATION PROGRAMS

State law²⁶ requires the Department to establish and maintain certification programs for property appraisers and tax collectors. State law authorizes the Department to establish by rule committees on admissions and certification, incur reasonable program expenses, and charge tuition, examination, certification, and recertification fees.²⁷ To obtain certification, a person must complete an application; pay a fee; have at least 2 years of experience in a Florida property appraiser's office, a Florida tax collector's office, or with the Department; attend a number of approved courses; and pass written course examinations. Each property appraiser and tax collector who has been timely designated as certified by the Department receives an additional \$2,000 annual special qualification salary.

²⁵ Section 195.062, Florida Statutes.

²⁶ Sections 145.10(2)(a) and 145.11(2)(a), Florida Statutes.

²⁷ Section 195.002(2), Florida Statutes.

Finding 6: Administration of the Certification Program Trust Fund

State law²⁸ establishes the Certification Program Trust Fund (Trust Fund) and requires the Department to use the Trust Fund to account for fees and expenses associated with administering the certification programs and those associated with the aid and assistance activity of providing aerial photographs and non-property ownership maps to county property appraisers. The Department must establish separate accounts within the Trust Fund for property appraisers, tax collectors, and aerial photography.

As part of our audit, we evaluated the Department's administration of the Trust Fund and found that improvements in Department procedures were needed. Specifically:

- **Collection Controls.** A Training Specialist was responsible for receiving checks and associated documentation, recording the information in the Learning Management and Sunrise Systems (Systems),²⁹ batching checks for deposit, and providing deposit information to the budget office. Although the deposits were delivered to the bank by another employee, the Training Specialist was in a position to conceal collections without detection since an independent reconciliation was not performed between the accounting records and the Systems. Additionally, although the checks were logged by another employee when initially received by the Department, the check log was not reconciled to the accounting records, the Systems, or the bank deposits. On average, during the period July 2012 through June 2015, the Department annually deposited in the Trust Fund certification and tuition fees totaling \$291,510. Our tests did not disclose any errors or fraud associated with this control deficiency; however, given the inadequate separation of duties and lack of compensating controls, there is an increased risk that errors or fraud could occur and not be timely detected.
- **Service Charge Allocations.** State law³⁰ requires certain State trust funds to quarterly contribute to the State General Revenue Fund a service charge of 8 percent of all revenues deposited. This requirement is applicable to certain certification program revenues collected and deposited in the Trust Fund and, until 2012, was applicable to aerial photography fees. Our review disclosed that the Department appropriately transferred the total service charge amounts from the Trust Fund to the State General Revenue Fund; however, the Department did not always allocate the proper service charge amounts among the separate property appraiser, tax collector, and aerial photography accounts within the Trust Fund. For example, of the seven service charge allocations made during the period January 2013 through December 2014, we noted four totaling \$46,373 in which the allocation methodology did not reflect the proper proportion of fees deposited, causing the tax collector account and the aerial photography account to be overcharged by \$10,855 and \$6,328, respectively, while the property appraiser account was undercharged by \$17,183.

Department personnel indicated that the tax collector and aerial photography accounts were overcharged because the accounts had larger balances and could absorb a greater portion of the service charge. However, to ensure that accurate, separate account balances are maintained, service charge allocations should be based on the proportion of applicable fees deposited for a particular program in relation to the total fees deposited. Subsequent to our inquiry, in April 2015, the Department made some of the corrections to the account balances; however, additional corrections totaling \$16,835 were needed as a result of service charge credits due to the Trust Fund from the State General Revenue Fund.

²⁸ Sections 195.002(2) and 195.022, Florida Statutes.

²⁹ The Learning Management and Sunrise Systems were used to register students for classes and issue certificates of class completion, as well as professional certifications.

³⁰ Section 215.20(1), Florida Statutes.

- **Trust Fund Account Balances.** At June 30, 2015, the Trust Fund cash balance was \$646,956, which consisted of \$218,023 for the property appraiser program account, \$428,933 for the tax collector program account, and a zero balance for the aerial photography program account. Our tests indicated that, during the 3-year period July 2012 through June 2015, the Department collected average annual revenues of \$167,378 and \$136,098 for the property appraiser and tax collector program accounts, respectively, and incurred average annual expenses of \$156,217 and \$53,024 for the property appraiser and tax collector program accounts, respectively, producing a positive cash flow in the trust fund for those accounts. The expenses for the aerial photography program account generally matched the revenues for that account, so typically there was a zero cash balance for this account. For appropriate operation of the Trust Fund, it is important that the Department collect sufficient revenues (through a properly established fee structure) for each program to pay the associated expenses of the program.

The development of a budget that considers anticipated expenses and identifies a target cash balance for each program account within the Trust Fund is necessary for the proper establishment of a fee schedule. Our tests disclosed that the Department had neither identified a target cash balance for each program account nor set a fee structure based on anticipated expenses. When an appropriate account balance is not taken into consideration in setting fees, such fees could either be excessive or insufficient to the needs of the program. As evidenced by the June 30, 2015, cash balances, the program accounts appeared to be surplus to the needs of the programs, especially for the tax collector program. Department personnel indicated that excess cash balances may be needed in the future to cover expenses should school attendance decline significantly. However, the purpose for the Trust Fund is to pay the expenses related to the certification programs and aerial photography activity, not to accumulate large surplus cash balances in the Trust Fund.

Recommendation: The Department should enhance procedures to provide for an adequate separation of duties related to Trust Fund collections. Additionally, the Department should ensure that service charges are allocated to accounts within the Trust Fund based on the proportion of applicable program revenues deposited and that all necessary adjustments are made to the accounts for erroneous service charge allocations. Also, the Department should establish an appropriate fee schedule for each program account based on anticipated expenses and overall cash balance needs for each program account.

PRIOR AUDIT FOLLOW-UP

Except as discussed in Finding 1, the Department had taken corrective action for the applicable findings included in our report No. 2013-034.

RELATED INFORMATION

Findings noted in our information technology operational audit of the *Property Tax Oversight System* used by the Department in its administration of the Ad Valorem Tax Program are included in our report No. 2014-185, dated April 2014.

OBJECTIVES, SCOPE, AND METHODOLOGY

The Auditor General conducts audits of governmental entities to provide the Legislature, Florida's citizens, public entity management, and other stakeholders unbiased, timely, and relevant information for use in promoting government accountability and stewardship and improving government operations.

We conducted this performance audit from January 2014 to April 2015, and performed selected audit procedures through June 2015, 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.

An audit by its nature does not include a review of all records and actions of agency management, staff, and vendors, and as a consequence, cannot be relied upon to identify all instances of noncompliance, fraud, waste, abuse, or inefficiency.

The objectives of this performance audit were to:

- Evaluate management's performance in administering the Ad Valorem Tax Program, as described in Section 195.096, Florida Statutes, in accordance with applicable laws, rules, policies, and other guidelines.
- Evaluate the:
 - Effectiveness of established controls that are designed and placed in operation to promote and encourage the economy, efficiency, and effectiveness of the program;
 - Structure or design of the program to accomplish its goals and objectives;
 - Adequacy of the program to meet the needs identified by the Legislature;
 - Alternative methods of providing program services or products;
 - Goals, objectives, and performance measures used to monitor and report program accomplishments;
 - Accuracy or adequacy of public documents, reports, or requests prepared under the program; and
 - Compliance of the program with applicable laws, rules, policies, and other guidelines.
- Determine whether management had taken corrective actions, as appropriate, for findings included in our report No. 2013-034.
- Identify, pursuant to Section 11.45(7)(h), Florida Statutes, statutory and fiscal changes that may be included in the audit report or subsequently recommended to the Legislature.

This audit was designed to identify, for those programs, activities, or functions included within the scope of the audit, deficiencies in management's internal controls, instances of noncompliance with applicable laws, rules, regulations, contracts, grant agreements and other guidelines, and instances of inefficient or ineffective operational policies, procedures, or practices. The focus of this audit was to identify problems so that they may be corrected in such a way as to improve government accountability and efficiency and the stewardship of management. Professional judgment has been used in determining significance and audit risk and in selecting the particular transactions, legal compliance matters, records, and controls considered.

As described in more detail below, for those programs, activities, and functions included within the scope of our audit, our audit work included, but was not limited to, communicating to management and those charged with governance the scope, objectives, timing, overall methodology, and reporting of our audit; obtaining an understanding of the program, activity, or function; exercising professional judgment in

considering significance and audit risk in the design and execution of the research, interviews, tests, analyses, and other procedures included in the audit methodology; obtaining reasonable assurance of the overall sufficiency and appropriateness of the evidence gathered in support of our audit's findings and conclusions; and reporting on the results of the audit as required by governing laws and auditing standards.

Our audit included selection and examination of various records and transactions from January 2013 through December 2014, and selected Department actions taken prior and subsequent thereto. Unless otherwise indicated in this report, these records and transactions were not selected with the intent of projecting the results, although we have presented for perspective, where practicable, information concerning relevant population value or size and quantifications relative to the items selected for examination. Specifically, we:

- Evaluated the adequacy of Department policies and procedures regarding the administration of the Ad Valorem Tax Program to determine whether the Department complied with applicable laws, rules, policies, and industry standards.
- Verified Department statistical calculations for one county to determine the reliability of the calculations used by Department staff to produce statistical measurements for county in-depth reviews.
- Examined all statistical and analytical measures computed by the Department in approving the real property assessment rolls for all counties for the 2013 and 2014 tax years to determine whether the Department verified the counties' tax rolls complied with applicable laws.
- Evaluated the statistical measurements of all 34 in-depth review counties in 2013 and all 33 in-depth review counties in 2014 to determine compliance with applicable laws, rules, policies, and industry standards. Also, we determined whether sample sizes for strata (property classifications) and value groups (property sub-classifications) within the strata were sufficiently representative of the population to enable meaningful statistical analyses of the in-depth review counties.
- Examined 60 of 190 Department appraisals and related documents from four in-depth review counties to determine compliance with industry practices, Department policies and requirements, and other guidelines.
- Examined records related to 190 properties selected by the Department for appraisal in four in-depth review counties to evaluate whether the selections were representative of the population. We also reviewed the voided appraisal samples from four in-depth review counties to determine whether the Department complied with established procedures for voiding and replacing appraisal samples.
- For 3 of the 34 in-depth review counties in 2013, and 4 of the 33 in-depth review counties in 2014, evaluated changes made to appraised values and corresponding documentation prepared subsequent to the final meeting between the Department and the county property appraisers at the conclusion of the appraisal process to determine compliance with State law.
- Evaluated the reasons provided and the documentation for the changes in sale qualification decisions for 2 of the 34 in-depth review counties in 2013, and 2 of the 33 in-depth review counties in 2014, to determine if the sale qualification actions were appropriate.
- Evaluated Department policies and procedures relating to the administration of the certified Florida property appraiser and certified Florida tax collector programs to determine whether the Department complied with requirements in applicable laws, rules, policies, and other guidelines.

- Tested transactions and program account balances within the Certification Program Trust Fund to determine whether the Department complied with requirements in applicable laws, rules, policies, and other guidelines.
- Tested 15 of the 67 property appraiser budgets and 15 of the 52 nonexempt tax collector budgets to determine whether Department budget reviews were conducted in accordance with applicable laws, rules, policies, and other guidelines.
- Communicated on an interim basis with applicable officials to ensure the timely resolution of issues involving controls and noncompliance.
- Performed various other auditing procedures, including analytical procedures, as necessary, to accomplish objectives of the audit.
- Prepared and submitted for management response the findings and recommendations that are included in this report and which describe the matters requiring corrective actions. Management's response is included in this report under the heading **MANAGEMENT'S RESPONSE**.

AUTHORITY

Pursuant to the provisions of Section 11.45(2)(h), Florida Statutes, I have directed that this report be prepared to present the results of our performance audit.



Sherrill F. Norman, CPA
Auditor General

MANAGEMENT'S RESPONSE



FLORIDA

Executive Director
Marshall Stranburg

Child Support
Ann Coffin
Director

General Tax Administration
Maria Johnson
Director

Property Tax Oversight
Dr. Maurice Gogarty
Director

Information Services
Damu Kuttikrishnan
Director

December 17, 2015

Ms. Sherrill F. Norman, CPA
Auditor General
Office of the Auditor General
G74 Claude Pepper Building
111 West Madison Street
Tallahassee, Florida 32399-1450

Dear Ms. Norman:

As required by section 11.45(4)(d), Florida Statutes, attached is the Department's response to the preliminary and tentative findings and recommendations related to your audit of the Administration of the Ad Valorem Tax Program.

We appreciate the professionalism displayed by your audit staff. If you have questions or need additional information, please contact Marie Walker, Director of Auditing, at 717-7598.

Sincerely,

Marshall Stranburg

MS/mw

Attachment

cc: Sharon Doredant, Inspector General
Marie Walker, Director of Auditing

Florida Department
of Revenue
Tallahassee,
Florida
32399-0100
<http://dor.myflorida.com/dor/>

Responses to Preliminary and Tentative Audit Findings
Department of Revenue Performance Audit:
Administration of the Ad Valorem Tax Program

In-Depth Reviews

Finding 1: As similarly noted in our report No. 2013-034, Department appraisal records did not always reasonably support property value estimates.

Recommendation: The Department should ensure that all appraisals are adequately documented and supported by complete, accurate, consistent, and relevant analyses and conclusions.

Response: The Department of Revenue (Department) agrees that it should comply with generally accepted appraisal practices, in part by producing real property appraisals that are adequately documented and supported by complete, accurate, consistent, and relevant analyses and conclusions. Data provided by the Auditor General clearly demonstrates that the quality of the Department's appraisals has significantly improved over the last five years. In this regard, the Department will continue to provide its appraisal personnel with additional training. In conjunction, the Department will continue to develop and implement sound procedures designed to improve the appraisal quality review process to ensure that appropriate appraisal standards and procedures are followed.

Finding 2: The Department analyzed some multifamily residential properties in a manner inconsistent with State law.

Recommendation: The Department should include multifamily residential properties in stratum 2, as required by State law, or document the legal basis upon which the property reclassifications were made for in-depth review purposes.

Response: The Department's study of large multifamily properties with more than nine (9) living units aligns with the International Association of Assessing Officer's (IAAO) current standard on ratio studies (2013), which appropriately categorize large apartments and apartment complexes within the income-producing property group. In addition, the Appraisal Institute also advocates for the use of differing valuation methodologies for large apartment complexes versus small multifamily residential properties. Because investor motivations and decisions are different for larger apartment properties than for smaller (2-9 living unit) multifamily properties, the Department has determined that the commercial stratum (6) is the most appropriate stratum in which to study these properties.

Section 195.096, F.S., does not clearly define the term "multifamily" to include larger apartment complexes and therefore neither affirm nor prohibit inclusion of these types of property among improved commercial properties (stratum 6) for purposes of in-depth study. By incorporating large apartment complexes in the commercial strata grouping

Responses to Preliminary and Tentative Audit Findings
Department of Revenue Performance Audit:
Administration of the Ad Valorem Tax Program

(stratum 6), the Department studied apartments in 66 counties across the state in 2015, as compared to only 10 counties in 2012, whereby apartments were studied as part of stratum 2. This equates to an additional \$58.8 billion of just value that was studied in 2015 as compared to 2012. Notwithstanding the Department's current determination, the Department may pursue statutory clarification in the future to further address this issue

Finding 3: Contrary to State law, personal property values reported to the Department on county assessment rolls were not included in the Department's in-depth reviews.

Recommendation: The Department should include personal property in its in-depth reviews as required by State law.

Response: Due to a lack of recorded selling prices and other data for tangible personal property (TPP) valuation, the Department uses the calculated real property level of assessment to infer the calculated level of assessment of tangible personal property. While it is not practicable to conduct in-depth reviews of TPP, the Program will begin to formulate a plan to perform TPP procedural reviews of all Florida counties over a two-year cycle.

In order to accomplish these procedural reviews, the Program must first complete the update of the TPP guidelines, which is currently underway. This update initiative will require approximately two years to complete. Once the TPP guidelines are brought up-to-date, we will begin to implement the TPP procedural review process. We expect these reviews to begin in 2018.

Other Property Oversight Issues

Finding 4: The Department's policy of allowing county property appraisers, when deriving just valuation, to adjust net proceeds by up to 15 percent without justification or documentation had no documented basis.

Recommendation: So that county property appraisers and the Department have the information necessary to accurately calculate 8th factor adjustments, the Legislature should consider enacting legislation to require disclosure of the data elements to be considered in 8th factor adjustments. In the interim, the Department, in consultation with the county property appraisers, should ensure that the basis for 8th factor adjustments made by county property appraisers are reasonable, supportable, and accurately represent the marketplace.

Responses to Preliminary and Tentative Audit Findings
Department of Revenue Performance Audit:
Administration of the Ad Valorem Tax Program

Response: The Department will implement any changes to the 8th criterion adopted by the Legislature. Notwithstanding the inherent difficulty in collecting financial information related to 8th criterion considerations, Florida's Property Appraisers have the responsibility of collecting and analyzing information necessary to determine all appropriate adjustments. As provided by Florida law, consideration of the net proceeds of sale must be made by the Property Appraiser, as with all other factors in section 193.011, F.S. Moreover, Rule 12D-8.002(4), F.A.C., specifies that if any reported 8th criterion percentage adjustment exceeds 15 percent, the Property Appraiser is required to submit complete, clear, and accurate documentation to the Department supporting the adjustment(s).

Finding 5: Contrary to State law, the Department did not maintain a current property tax administration manual with up-to-date guidelines.

Recommendation: The Department should continue efforts to maintain a current manual and annually update guidelines, as appropriate, in accordance with State law.

Response: As noted, the Department will update the Manual of Instructions for Property Appraisers and other officials connected with the administration of property taxes pursuant to the requirements of section 195.062, F.S. The Department will continue efforts to maintain a current Manual of Instructions and periodically update all of the manual's guidelines, as appropriate, in accordance with State law. The Program has already begun work on a draft of the real property guidelines and anticipates publication of said draft within approximately one year. However, completion of the Manual of Instructions in its entirety will require the hiring of additional personnel with the requisite appraisal, technical, and legal expertise. The expected delivery date of a completed Manual of Instructions is planned for 2019.

Certification Programs

Finding 6: Department procedures for the administration of the Certification Program Trust Fund needed improvement.

Recommendation: The Department should enhance procedures to provide for an adequate separation of duties related to Trust Fund collections. Additionally, the Department should ensure that service charges are allocated to accounts within the Trust Fund based on the proportion of applicable program revenues deposited and that all necessary adjustments are made to the accounts for erroneous service charge allocations. Also, the Department should establish an appropriate fee schedule for each

Responses to Preliminary and Tentative Audit Findings
Department of Revenue Performance Audit:
Administration of the Ad Valorem Tax Program

program account based on anticipated expenses and overall cash balance needs for each program account.

Response: The Department has enhanced its procedures to provide an adequate separation of duties related to Trust Fund collections. These procedures are outlined in two procedural documents: "Monthly Reports Procedures – How to Run Monthly Reports," and "Mail Processing Workflow Chart."

The Department will take the necessary steps to ensure that all service charges are properly allocated to accounts within the Trust Fund based on the proportion of applicable program revenues deposited. In addition, the Department will make certain that all necessary adjustments are made to account for any erroneous service charge allocations.

Last, the Department will establish annually an appropriate fee schedule for each program account based on anticipated expenses and determine cash balance targets for each program account.