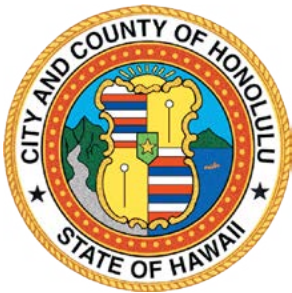




Office of the City Auditor



**City and County of
Honolulu
State of Hawai`i**

**Report to the Mayor
and the
City Council of Honolulu**

**Follow-Up on
Recommendations from
Report No. 12-03, *Audit
of the City's Real
Property Tax
Delinquency Collection***

**Report No. 19-04
November 2019**

**Follow-Up on Recommendations
from Report No. 12-03, *Audit
of the City's Real Property Tax
Delinquency Collection***

A Report to the
Mayor
and the
City Council
of Honolulu

Submitted by

THE CITY AUDITOR
CITY AND COUNTY
OF HONOLULU
STATE OF HAWAII

Report No. 19-04
November 2019

Follow-Up on Recommendations from Report No. 12-03, *Audit of the City's Real Property Tax Delinquency Collection*

November 2019

Background

The *Audit of the City's Real Property Tax Delinquency Collection* (Report 12-03, issued March 2012), was a self-initiated audit that addressed concerns about projected increases in delinquent receivables and inadequate reporting regarding the city's delinquent property tax collection program. The audit objective was to review and assess the city's real property tax delinquency collection process. To assess the program, we evaluated the effectiveness of management practices for collecting real property delinquent taxes.

In Report 12-03, the audit identified issues that prevented the city from reducing real property tax delinquencies through effective, timely, and efficient collection. A number of long-term, large dollar amount delinquencies were caused by the city's inability to collect from government-owned land lessees. The city received little or nothing in return for its resources and collection efforts because the city was limited in its options to collect from lessees and could not foreclose on government-owned property if its lessee failed to pay the city's assessed taxes. To facilitate collection of taxes and timely actions against lessees of government lands, the city would need to develop memoranda of agreements with other government entities for sharing lessee and lease information.

The audit also concluded that delinquent tax collection amounts for private properties were increasing because land owners were allowed to remain on payment plans indefinitely. We also found that the chronically delinquent knew how to avoid the foreclosure process by paying the minimum property tax amount necessary to avoid triggering the foreclosure process. In addition, improvements in city policies and procedures could improve delinquent tax collections and the accuracy of delinquency tax data. Establishing categories for written-off and uncollectible accounts and moving these accounts to a separate list could improve the accuracy of the delinquent tax totals. Establishing a list of written-off and uncollectible accounts could be used by city staff to deny city services and benefits to delinquent taxpayers and serve as an incentive to pay delinquent taxes, provided that due process, administrative, and appeal procedures related to the denial are in place.

The audit made 11 recommendations to improve delinquency collections. Since the original report was issued in 2012, our office has periodically monitored the status of the report's recommendation by requesting the Department of Budget and Fiscal Services (BFS) to report on the status of the audit recommendations. In the FY 2012, FY 2014 and FY 2017 status recommendation reports, we noted that BFS had not-started any of the 11 recommendations. Based on this and the period of time that has transpired since the audit was completed, we determined that a follow-up audit should be performed to verify that status of the outstanding recommendations.

The 11 outstanding audit recommendations included in this follow-up audit are:

For government landowners and lessees:

- 1. Negotiate a Memorandum of Agreement with the State of Hawai'i that provides for the timely exchange of lessee information on government lands and permits the city and county access to State of Hawai'i databases that allow the city staff to take timely actions in filing liens against delinquent lessees.*
- 2. Maintain a list of lessees of government-owned lands who are repeatedly delinquent for close monitoring and follow-up collection actions. The list should include information such as periods of chronic delinquency, personal or property lien status, private or government owned land, age of delinquency, and collection status.*
- 3. Place uncollectible and written off property taxes on a list of lessees that should be denied city services and benefits until the delinquent taxes are paid or arrangements made to repay the delinquent taxes.*
- 4. Develop policies, procedures, and time lines for the following - filing personal and/or property liens; terms and conditions for payment plans; terms and conditions for personal liens; classifying accounts as uncollectible; the proper disposition of uncollectible accounts; and the treatment of chronically delinquent taxpayers.*
- 5. Require the BFS staff to identify and report long term government land lessee delinquencies to the BFS Director that should be written off as uncollectible.*

For private property owners:






- 6. Maintain a list of private landowners who are repeatedly delinquent for close monitoring and follow-up collection actions. The list should include information such as the periods of chronic delinquency, lien status, private or government owned land, age of delinquency, and collection status.*
- 7. Segregate the list of delinquent property taxes for privately owned real estate from government lands; age the delinquent accounts so city staff can identify long term delinquencies that are unlikely to be collected; and require the city staff to identify and report to the BFS Director any long term, private landowner delinquencies that should be classified as uncollectible.*
- 8. Establish policies, procedures and timelines that limit the number of years for payment plans and require staff to take more timely action on foreclosures and other actions that protect the city's interests. The policies, procedures, and time lines should include the following – collecting and processing annual real property taxes, filing property liens; terms and conditions for payment plans; terms and conditions for foreclosure actions; classifying accounts as uncollectible; the proper disposition of uncollectible accounts; and the treatment of chronically delinquent taxpayers.*
- 9. Establish an ordinance that allows the city to fine and deny services to delinquent taxpayers as an incentive to pay delinquent taxes. The ordinance should include due process administrative and appeal procedures related to the denial of the city services.*

To improve collection policies and procedures, BFS should:

10. Establish policies, procedures, and time lines for: identifying and classifying accounts as uncollectible after two years; removing uncollectible accounts from the collections lists; transferring accounts to an uncollectible accounts list; writing off the uncollectible accounts; limiting the number of years for payment plans; taking timely actions on foreclosures and delinquent accounts that protect the city's interests; and handling long-term and repeat delinquent taxpayers.
11. Establish and maintain a list of taxpayers with uncollectible and written off accounts for monitoring and follow-up actions.

Audit Results

We found that 8 of the 11 outstanding recommendations have been completed, 1 is in process, and 2 were dropped:

 Completed 8	 Resolved --	 In Process 1	 Not Started --	 Dropped 2
Agency has fully implemented the audit recommendation.	Although agency did not implement the audit recommendation, it implemented an alternative solution that fully addressed the applicable audit finding or risk.	Agency started or has partially implemented the audit recommendation.	Agency has not begun implementation of the recommendation.	Agency has no plan to implement the recommendation; the risk associated with the recommendation no longer exists, or is no longer applicable.

The following details the audit recommendations made and the status of each recommendation based on our review.

Recommendation 1



Negotiate a Memorandum of Agreement with the State of Hawai'i that provides for the timely exchange of lessee information on government lands and permits the city and county access to State of Hawai'i databases that allow the city staff to take timely actions in filing liens against delinquent lessees.

STATUS UPDATE

Management made efforts to obtain information from the state. On September 19, 2012, the former governor issued an Executive Memorandum requesting that the state provide the city with timely information regarding non-residential leases with commercial tenants that have a term in excess of one year. The memorandum specifies that all state agencies that issue leases, licenses, permits, or other dispositions for non-residential real property to tenants who will use the property for

commercial purposes, where the lease continue a period of one year or more, shall provide the city and counties worksheet information on an annual basis by September 30th of each year. According to BFS, since 2013, the state has not upheld its commitment to provide annual worksheets and timely information to the city.

NEXT STEPS

We recommend that BFS work with the state to ensure compliance with the memorandum. Absent timely and accurate delinquency information, the city remains unable to effectively collect back payments and penalties from government-owned land lessees.

Recommendation 2

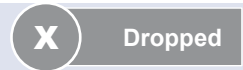


Maintain a list of lessees of government-owned lands who are repeatedly delinquent for close monitoring and follow-up collection actions. The list should include information such as periods of chronic delinquency, personal or property lien status, private or government owned land, age of delinquency, and collection status.

STATUS UPDATE

The current and delinquent age list detail reports allow collection staff to monitor delinquent accounts activity on a monthly basis. The report also identifies accounts that have been delinquent for more than two years and eligible to be written off. We found that collections staff sufficiently monitor detail reports and follow-up with the accounts on a monthly basis. Management provided us lists of current and delinquent accounts that included total amounts owed for taxes and penalties. Although the report does not list any period of chronic delinquency, personal or property lien status, private or government-owned land, age of delinquency, and collection status, we did find comparable information in the real property tax computerized information software. The system provided status of delinquent accounts and other information through the internal transaction notes and data. From the current and delinquent age list detail provided, we judgmentally sampled five delinquent accounts and verified that the correct status was noted in the tax computerized information software.

Recommendation 3



Place uncollectible and written off property taxes on a list of lessees that should be denied city services and benefits until the delinquent taxes are paid or arrangements made to repay the delinquent taxes.

STATUS UPDATE

Management will not implement this recommendation upon the advice of the city's Corporation Counsel. Corporation Counsel provided a legal memorandum to management dated February 13, 2012, in response to a request for an opinion on the issue of withholding services and benefits from delinquent real property taxpayers. The Corporation Counsel memorandum concluded: (1) the city may not withhold services from delinquent taxpayers absent statutory authority to do so; (2) ROH Chapter 8, Article 5 already provides statutory remedies for nonpayment of real property taxes, including a *paramount lien* on the subject property and the ability to seek non-judicial foreclosure

thereon; and (3) denial of city services to delinquent taxpayers may violate constitutional due process requirements.

Recommendation 4



Completed

Develop policies, procedures, and time lines for the following - filing personal and/or property liens; terms and conditions for payment plans; terms and conditions for personal liens; classifying accounts as uncollectible; the proper disposition of uncollectible accounts; and the treatment of chronically delinquent taxpayers.

STATUS UPDATE

Management has a comprehensive delinquent collection policies and procedures manual for the collection of delinquent real property taxes. The manual's second edition was revised in 2013. We reviewed the policies and procedures manual and conducted interviews with staff. We found that the revised policies and procedures, or current practices, generally addressed the audit recommendation with the following clarifications. We found that there is no policy or procedure concerning personal liens filing and its terms and conditions. According to management, the current ordinance does not give the department authority to file a personal lien on a taxpayer. Instead, management and staff follow the procedure and terms and conditions on issuing a paramount lien upon the property.

Regarding payment plan agreements, we found that the department does not follow the payment plan agreement process because it is an ineffective means to collect from the taxpayer. Payment plans are generally short term agreements requiring payments within six months and the city does not enter into long term repayment agreements due to the time constraints for collection.

Per the policy and procedure on classifying an account as *uncollectible*, the collector must ensure that all collection efforts have been exhausted. Specifically, the collector must have pursued all methods of contact and documentation before recommending the account as uncollectible. When an account is determined to be uncollectible, the account is submitted to management to be placed on the list of write-offs. The case is then forwarded to the director for approval. This is the same treatment for chronically delinquent taxpayers. Based on the review of the recent approval of the uncollectible delinquent taxes on May 30, 2019, we found that the department followed its process for identifying uncollectible accounts. For example, we observed approval accounts that have been delinquent for at least two years and a total write-off of \$100,999.59 was uncollectible.

Although the department did not fully establish policies and procedures for all topics referenced in the recommendation, we determined that the department made sufficient effort to review the areas of concern and took appropriate action where applicable.

Recommendation 5



Completed

Require the BFS staff to identify and report long term government land lessee delinquencies to the BFS Director that should be written off as uncollectible.

STATUS UPDATE

We found that collection staff maintain current and delinquent age list detail reports. According to the department's policies and procedures, collectors must review their detail report, ensure that all collections efforts have been exhausted, and document internal notes before submitting to management for review and placement on the list of write-offs. We reviewed a listing dated June 24, 2019 that identified the uncollectible delinquent taxes for lessees of government-owned parcels for the director's write-off approval. The list identified a total of 57 government-owned parcels with a total of \$204,115.78 that was approved by the director for uncollectible delinquent taxes write-off. We confirmed with management that collection staff are involved with the process to review and recommend that uncollectible accounts be written-off. We judgmentally reviewed 10 government-owned land parcels from the approved write-off list and found that collection staff provided sufficient analyses and documentation on uncollectable accounts. We also verified our samples in the historical tax information database and confirmed that there are no other outstanding charges.

Recommendation 6



Maintain a list of private landowners who are repeatedly delinquent for close monitoring and follow-up collection actions. The list should include information such as the periods of chronic delinquency, lien status, private or government owned land, age of delinquency, and collection status.

STATUS UPDATE

Similar to our comments in recommendation 2, the delinquent collection staff maintain current and delinquent age list detail reports and monitor and follow-up on a monthly basis with taxpayers. The delinquent age list report is presented in the same form as the government-owned lease report which calculates the total taxes and penalties owed. Although the report does not list any period of chronic delinquency, personal or property lien status, private or government-owned land, age of delinquency, and collection status we did find comparable information in the real property tax computerized information software. The system provided status of delinquent accounts and other information through the internal transaction notes and data. From the current and delinquent age list details provided, we judgmentally sampled five delinquent accounts and verified that the correct status was noted in the tax computerized information software.

Recommendation 7



Segregate the list of delinquent property taxes for privately owned real estate from government lands; age the delinquent accounts so city staff can identify long term delinquencies that are unlikely to be collected; and require the city staff to identify and report to the BFS Director any long term, private landowner delinquencies that should be classified as uncollectible.

STATUS UPDATE

Similar to our comments in recommendations 2 and 6, the collection staff maintain a list of delinquent property tax account records and monitors payment progress. Based on our review, the current and delinquent age list detail record can be segregated for privately owned property from government-owned lands. We also reviewed the director's most recent approval list for

uncollectible delinquent taxes and found that the list distinguishes between private owners and government-owned lands.

Recommendation 8



Completed

Establish policies, procedures and timelines that limit the number of years for payment plans and require staff to take more timely action on foreclosures and other actions that protect the city's interests. The policies, procedures, and time lines should include the following – collecting and processing annual real property taxes, filing property liens; terms and conditions for payment plans; terms and conditions for foreclosure actions; classifying accounts as uncollectible; the proper disposition of uncollectible accounts; and the treatment of chronically delinquent taxpayers.

STATUS UPDATE

Similar to our comments in recommendation 4, we reviewed the policies and procedures for collecting and processing annual real property taxes; filing property liens; terms and conditions for payment plans; terms and condition for foreclosure actions; classifying accounts as uncollectible; the proper disposition of uncollectible accounts; and the treatment of chronically delinquent taxpayers. According to BFS management and staff, the department does not follow the terms and conditions for payment plans because it is not an effective collection tool. Rather, the department found that the use of processing foreclosures is more effective. According to BFS, in May 2018, the Treasury Division accelerated the foreclosure process for accounts two years delinquent rather than three years. Our review of May 2019 foreclosures found relatively few foreclosures compared to the total 290,000 taxable parcels. Foreclosures average less than 10 properties a year, or 1 in 29,000 parcels. Total foreclosure properties sold resulted in proceeds of \$738,681.

Recommendation 9



Dropped

Establish an ordinance that allows the city to fine and deny services to delinquent taxpayers as an incentive to pay delinquent taxes. The ordinance should include due process administrative and appeal procedures related to the denial of the city services.

STATUS UPDATE

Management will not take any further action on this recommendation upon advice of the city's Corporation Counsel memorandum dated February 13, 2012. The Corporation Counsel memorandum concluded: (1) the city may not withhold services from delinquent taxpayers absent statutory authority to do so; (2) ROH Chapter 8, Article 5 already provides statutory remedies for nonpayment of real property taxes, including a *paramount lien* on the subject property and the ability to seek non-judicial foreclosure thereon; and (3) denial of city services to delinquent taxpayers may violate constitutional due process requirements.

Recommendation 10



Completed

Establish policies, procedures, and time lines for: identifying and classifying accounts as uncollectible after two years; removing uncollectible accounts from the collections

lists; transferring accounts to an uncollectible accounts list; writing off the uncollectible accounts; limiting the number of years for payment plans; taking timely actions on foreclosures and delinquent accounts that protect the city's interests; and handling long-term and repeat delinquent taxpayers.

STATUS UPDATE

Based on our review of the policies, procedures and timelines we found that the department generally established policies and procedures for areas noted in the recommendation. We verified with management and staff that these policies and procedures are being followed. Based on discussion and review, we have determined that the efforts on the foreclosure process are more effective and improve the collection on delinquent accounts.

Recommendation 11



Completed

Establish and maintain a list of taxpayers with uncollectible and written off accounts for monitoring and follow-up actions.

STATUS UPDATE

Please refer to our comments in recommendations 2 and 6.

Appendix A

Audit Objectives, Scope, and Methodology

The objective of the follow-up audit is to determine whether Department of Budget and Fiscal Services' Real Property Tax Delinquency Collection Section has adequately addressed its open recommendations with corrective actions.

For this follow-up audit we reviewed the original audit and the available supporting documentation, interviewed management and staff, and requested supporting documentation to substantiate information provided. We conducted walkthrough sample observations and reviews of material pertinent to the follow-up audit. We also reviewed the *iasWorld* computerized information software and data in the individual property records search. We also reviewed pertinent sections of Chapter 8 Revised Ordinances of Honolulu related to Real Property Tax, and policies and procedures established by the delinquent real property tax collection.

During the audit we were not aware of any other investigations, audits or other work by other agencies that may have impacted our work. In addition, we did not become aware of any possible fraud, waste or abuse situations during the course of the audit relative to the audit objectives.

Our follow-up audit on the open recommendations made in Report No. 12-03 was conducted between May 2019 through September 2019 in accordance with generally accepted government auditing standards. These standards require that we plan and perform the audit to obtain sufficient and 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.

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Appendix B

Management Response

OFFICE OF THE MAYOR
CITY AND COUNTY OF HONOLULU

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KIRK CALDWELL
MAYOR



ROY K. AMEMIYA, JR.
MANAGING DIRECTOR
GEORGETTE T. DEEMER
DEPUTY MANAGING DIRECTOR

November 19, 2019

Mr. Troy Shimasaki
Acting City Auditor
Office of the City Auditor
City and County of Honolulu
1001 Kamokila Boulevard, Suite 216
Kapolei, Hawaii 96707

Dear Mr. Shimasaki:

Thank you for your November 8, 2019, letter and follow-up audit of the City's Real Property Tax Delinquency Collection. Budget and Fiscal Services (BFS) notes the cooperative working relationship with the City Auditor which began in 2012. In FY 2012, FY 2014 and FY 2017, BFS consistently noted that all 11 recommendations were resolved or closed.

BFS considers Recommendation 1 resolved and will not take further action as an Executive Memorandum of Agreement by the former governor was issued September 19, 2012. BFS continues to pursue resolutions with various State Agencies regarding the timely information on non-residential leases with commercial tenants whose lease terms are in excess of one year.

We appreciate that Recommendations 2 through 11 were completed or dropped by the City Auditor.

Should you have any questions, please feel free to contact Mr. Nelson H. Koyanagi, Jr., Director, Budget and Fiscal Services, at 768-3901.

Warm regards,


Roy K. Amemiya, Jr.
Managing Director

cc: Nelson H. Koyanagi Jr., Director
Budget and Fiscal Services

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