Executive Summary

Homestead Tax Deduction Program Deficiencies May Have Caused the District to Lose As Much As $44.7 Million During Fiscal Years 1998 Through 2000
(DCA Report 102 - Issued November 19, 2001)

PURPOSE

Pursuant to Public Law 93-198, Section 455, the District of Columbia Auditor reviewed the operations of the Homestead Tax Deduction Program managed by the Office of the Chief Financial Officer’s Office of Tax and Revenue.

CONCLUSION

The District of Columbia may have lost approximately $44.7 million in real property tax revenue during the review period, excluding penalties of approximately $8 million or more, because the Office of Tax and Revenue (OTR) did not properly and aggressively manage the Homestead Tax Deduction Program (the Program) during the period covered by this audit. Penalties were not factored into the Auditor’s lost revenue estimate because OTR may opt to waive a presently undetermined amount of such penalties that were the result of OTR’s internal management deficiencies.

The Homestead Tax Deduction Program was established to provide homestead and senior citizen property tax reductions to qualified residential real property owners. The desired results or benefits for which this Program was established were not sufficiently achieved during the three-year period covered by this audit. It is the Auditor’s opinion that this was due in significant part to a lack of effective managerial oversight and direction, in addition to ineffective manual and automated processes used by OTR for granting, revoking, monitoring and calculating these tax reductions. The processes were not fully automated and lacked adequate internal controls to ensure that the tax reductions were properly granted for eligible properties and promptly terminated for ineligible properties.

Although OTR made substantial improvements in the administration of the Homestead Tax Deduction Program prior to, and during the three-year period under audit, the Auditor found that the methodology used by OTR still lacked adequate, effective internal controls to ensure full compliance with the law. Homestead and senior citizen tax reduction applications were not in
OTR’s records for a significant number of property owners that received these reductions, and data on some tax reduction applications in OTR’s records were not adequately screened and validated before tax reductions were granted. In other words, eligibility was often not determined before owner’s received tax reductions. Additionally, because of onerous, inefficient manual and automated processes, annual compliance audits of each property, or even a significant percentage of properties in the Homestead Tax Deduction Program, were not conducted in accordance with OTR’s Homestead Audit Unit’s strategic plan. Consequently, owners received tax reductions on ineligible properties that might have been detected if all or a significant number of properties had undergone periodic reviews. Further, complete rules and regulations were not published to ensure that the public was fully informed about the legal requirements for participating in the Program. As a result, many owners may not have known that they were required to notify OTR when a property became ineligible for the homestead and senior citizen tax reductions.

The conditions discussed above are indicia of OTR’s mismanagement of the Homestead Tax Deduction Program during the period covered by this audit. Consequently, property owners may have received homestead and senior citizen tax reductions even though the owners may not have occupied the property. Some owners appeared to have received the deduction on multiple properties at the same time. Additionally, other owners appeared to have received tax reductions that were brought forward from prior property owners. Further, corporations and businesses, ineligible for the Program, appear to have received the homestead tax reduction on residential properties. Program mismanagement, and general failure to adhere to the requirements of the law regarding homestead and senior citizen tax reductions, placed the District at great risk of failing to collect millions of dollars in residential real property taxes.

The Office of the Chief Financial Officer (OCFO) concurred with the Auditor’s conclusion that the Homestead Tax Deduction Program needs improvement, agreed with the “spirit” of the Auditor’s recommendations, and conceded that as much as $19 million in potential revenue is still materially affected by inadequate administration of the program. The OCFO also conceded that the material difference between the Auditor’s and OCFO’s estimated revenue losses arises primarily from the fact that the Auditor included losses from properties participating in the program without an application and the OCFO did not include those properties.
FINDINGS

1. The Office of Tax and Revenue did not always ensure that owners were qualified to receive homestead and senior citizen tax reductions before granting tax reductions.

2. OTR did not accurately calculate tax reductions when property ownership changed.

3. Improvements are needed in the number and quality of property eligibility audits conducted.

4. Written standard policies, procedures and rules governing the Homestead Tax Deduction Program were not finalized.

5. Fiscal Year 2001 legislation may permit continuing tax reductions on ineligible properties beyond fiscal year 2001.

RECOMMENDATIONS

1. The Homestead Application Database should be modified to perform additional edits before homestead and senior citizen tax reductions are granted.

2. All OTR computer systems used in the eligibility determination process should utilize common identification numbers, such as social security numbers and tax identification numbers, assigned to real property owners and co-owners for effective automated data matching.

3. OTR should develop a mechanism to automate data matching, with assistance from the District’s Chief Technology Officer, from the Homestead Application Database to computer systems in other District agencies using social security numbers and federal tax identification numbers.

4. OTR should develop guidelines, with assistance from the District’s Chief Technology Officer, to standardize the format for entering names and addresses into all computer systems available for use in the process of determining eligibility for the homestead tax deduction and senior citizen tax relief.

5. OTR should ensure that tax reductions are granted only after an application has been filed and eligibility has been definitively determined.
6. OTR should program the property tax billing system to automatically terminate tax reductions on properties when ownership changes, thereby forcing new owners to file an application to receive property tax reductions.

7. OTR should program the tax billing system to prorate tax reductions on a monthly basis when applications are received in accordance with the law.

8. OTR must enhance the Homestead Audit Unit’s resources and automate the data matching steps of the audit process to reduce the time required to perform each audit.

9. The Manager of the Homestead Audit Unit must maintain a list of audit properties and the results and statistics on property compliance audits conducted annually.

10. OTR officials should develop performance measures for the Homestead Audit Unit relative to homestead and senior citizen property tax reduction audits for inclusion in OTR’s annual performance plan.

11. The Deputy Chief Financial Officer for OTR must immediately finalize all policies and procedures relative to the Homestead Tax Deduction Program. Further, regulations must be promulgated in the District of Columbia Municipal Regulations setting forth all the requirements for participating in the Program.

12. The Deputy Chief Financial Officer for OTR should immediately develop the staff and technical resources necessary to ensure that every Class 1 Property is periodically audited, and ineligible properties are promptly removed from the Homestead Tax Deduction Program.

13. OTR must collect all real property taxes, penalties and interest resulting from property owners improperly receiving homestead and senior citizen tax reductions in violation of District law.