



THE CITY OF SAN DIEGO  
**REPORT TO THE CITY COUNCIL**

DATE ISSUED: April 7, 2014 REPORT NO: 14-033  
ATTENTION: Budget and Government Efficiency Committee  
Agenda of April 16, 2014  
SUBJECT: Sales, Use, and Property Tax Audit and Recovery, and Information  
Services  
REFERENCE: None

REQUESTED ACTIONS:

Authorize the one-year agreement with four additional one-year option periods between the City and HdL Companies to provide sales, use, and property tax audit and recovery, and information services for a contingency fee on new sales, use, and property tax revenue recovered by the consultant.

Authorize HdL Companies to examine, on the City's behalf, confidential taxpayer information contained in the records of the State Board of Equalization (BOE) per the requirements contained in the State of California Revenue and Taxation Code.

Authorize the Mayor, the Chief Operating Officer, the Chief Financial Officer, or other officer or employee of the City as designated to the BOE in writing by the Mayor, the Chief Operating Officer or the Chief Financial Officer to represent the City with authority to examine BOE records pertaining to sales and use taxes collected for the City by the BOE and for purposes related to the governmental functions of the City.

STAFF RECOMMENDATION:

Approve the requested actions.

SUMMARY:

**I. Background**

In 1991, the City Council approved an agreement with Municipal Revenue Consultants (subsequently renamed to Municipal Revenue Advisors, to MBIA MuniServices, and finally to MuniServices, LLC) to provide sales and use tax and information services. In 1997, the City Council approved the renewal of an agreement with MuniServices, LLC (MuniServices), which incorporated the provisions of a previous contract and included new revenue enhancement services. From 1997 to 2003, MuniServices had been retained as a sole source consultant to the City. In 2003 and 2008, the City issued Requests for Proposals (RFP) and MuniServices was

selected as the City's consultant based on the best value and the lowest bid. The City's agreement with MuniServices expired on March 23, 2014.

In September 2013, the City issued an RFP for the sales, use, and property tax audit and recovery, and information services that included the following:

- Sales and Use Tax Audit
- Sales Tax Analysis and Sales Tax Analysis Query System
- Property Tax Audit
- Geo-Area Database
- Property Tax Database

The City received two responses to this RFP. Both proposers were qualified to handle the required services for the City. By evaluating technical qualifications and the pricing of the proposals, HdL Companies (HdL) was selected based on the best value which included technical qualifications and the lowest bid. The original bids submitted by both companies were competitive and responsive, and both companies were given the opportunity to submit a Best and Final Offer (BFO) for this RFP. HdL's BFO had lower costs compared to the competitor.

Previously, the City Council authorized the sales and use tax consultant to review confidential BOE taxpayer information on the City's behalf per the requirements of the State Of California Revenue and Taxation Code. The BOE maintains agreements for the reciprocal exchange or release of information (including personal or confidential information) with state agencies, other states, local government agencies, the federal government, and private contractors, permitting disclosure of information contained in the files and records of the agencies (subject to the restrictions prescribed in the agreements or provided by statutes or regulations).

## **II. Discussion**

### **Sales and Use Tax Audits**

The purpose of the consultant's sales and use tax audit and recovery services is to maximize the City's sales and use tax revenues and minimize lost sales and use tax revenues by detecting and documenting misallocations of sales and use tax activity within the time limitations of administrative recoverability. Per state law, once a sales tax appeal is filed with the BOE, the "date of knowledge" is established and cities may recover misallocated sales tax a maximum of three quarters prior to the established date of knowledge and all forward quarters. It is common practice among jurisdictions including the City of Los Angeles, City of Oakland, City of Sacramento, San Diego County, and others to use sales tax audit consultants for this purpose. The services provided by the consultant include different types of sales tax audits as described below:

- Sales misreported as "use tax" transactions that are distributed to State and county pools rather than to "point of sale" for the City;
- "Points of sale" misreported to other locations outside the City rather than to the location within the City where principal negotiations or orders are initiated;

- Internet orders allocated to billing or switching equipment sites rather than the location of human intervention;
- Misallocations occurring due to sales from multiple retail outlets, order desks, or offices are credited to a single location outside the incorporated area rather than to sub outlets located within the City boundaries;
- New registrations, accounting adjustments and additional State sales tax assessments that are miscoded to other jurisdictions or to allocation pools;
- Individual “use tax” transactions exceeding \$500,000 that are reported to the pools rather than “point-of-use”;
- Erroneous distribution of the sales of construction material and fixtures to allocation pools because the sales are misidentified as installation rather than “over-the-counter” sales;
- Failure to designate in-state warehouses as “point of sale” for orders placed or negotiated outside of California;
- Misallocations that occur due to zip code, boundary, or other jurisdictional inconsistencies or because of failure of new addresses to be picked up in the BOE registration rolls; and
- Misallocations by companies that self impose “use tax” for materials taken out of inventory and misreport the usage as taking place at locations other than the City.

### **Property Tax Audits**

The purpose of the consultant’s property tax audit and recovery services is to identify, correct, and recover property tax errors including the following:

- Establish the county data set and reconcile the county annual property assessed valuation report to the County Assessor’s lien date rolls and identify discrepancies;
- Identify and correct errors through the performance of secured parcel and unsecured property audits;
- Prepare reports, and review and analyze the data in preparation for meeting with the City staff to discuss year over year changes and trending; and
- Ongoing analysis, appeal updates, transfer of ownership updates, remittance advance review, and budget projections.

The consultant would provide, if necessary, assistance with Recognized Obligation Payment Schedules (ROPS) for the Successor Agency and monitor the County distribution of Redevelopment Property Tax Trust Fund (RPTTF) revenues, tax sharing amounts to the City and taxing entities of the former redevelopment agency and allocation of residual and other revenues.

### **Geo-Coding**

The consultant will provide a Geo-coding database for the development of comprehensive reports that can illustrate specified areas of the City, such as community plan areas, Business Improvements Districts, and project areas. Reports and data exports can be generated by Geo-area in numerous configurations, such as by quarter, fiscal year, major industry group, and business type, address, and/or allocation amount.

### III. Summary

To provide these tax audit services using City staff, it would require full-time staff dedicated to sales, use, and property tax audits on a daily basis, including field audits of the City's commercial and industrial areas. It would also require resources from the City Attorney's Office to provide legal support as well as the development and maintenance of a software program for sales tax audits and Geo-coding. In addition, the City would not have access to other state and regionwide municipalities' tax data for analysis purposes. The consultant would have access to all statewide and countywide pool accounts and can see trends in the major businesses reporting sales taxes.

#### FISCAL CONSIDERATION(S):

The original bids submitted by both companies were very competitive and included price proposals of 18% contingency fee from MuniServices and 15% from HdL for sales and use tax audit service. For property tax audit service, MuniServices proposed a 25% contingency fee and HdL proposed a \$40,000 annual fee. The City's Evaluation Committee reviewed the financial impact of these proposals and offered both companies the opportunity to submit a BFO for this RFP. MuniServices lowered the sales and use tax audit contingency fee from 18% to 17% and property tax audit fee from 25% to 17%. HdL's BFO offered a tiered contingency fee structure (see below) for sales and use tax audit services and lowered the property tax audit fee from \$40,000 to \$36,000 annually. For individual petitions for high-value sales and use tax recoveries and significant one-time allocation adjustments, the City will pay HdL for recovered sales and use tax revenue based on a tiered contingency fee structure:

- 15% of the first \$1,000,000 of sales and use tax revenues recovered
- 10% for \$1,000,001 to \$2,500,000
- 5% for \$2,500,001 and higher

It should be noted that the City will pay HdL a contingency fee for retroactive back quarter reallocations and allocations received in the first six consecutive reporting quarters starting with the correction of the misallocation.

MuniServices generated on average approximately \$2-\$4 million in new (recovered) revenue per year for the City by performing the sales and use tax audit services and the City paid a contingency fee of 18% to the company. It is expected that HdL would continue to generate at least the same amount of new revenue per year for the City by performing these services.

By providing property tax audit services, MuniServices generated on average approximately \$350,000 in new revenue per year for the City, and it is expected that HdL would continue to generate at least the same amount of new revenue per year for the City by performing these services.

By selecting HdL as its consultant for sales, use, and property tax audit services, the City will save at least approximately \$80,000 annually as a result of a lower contingency fee for sales, use, and property tax audit services.

The City's sales and property tax annual budgets and projections include recovered revenues from these audit services.

Retaining a sales, use, and property tax consultant providing tax audit services will ensure that new (recovered) revenue is continuously generated by the City.

PREVIOUS COUNCIL and/or COMMITTEE ACTION: None

COMMUNITY PARTICIPATION AND PUBLIC OUTREACH EFFORTS: None

KEY STAKEHOLDERS AND PROJECTED IMPACTS: None



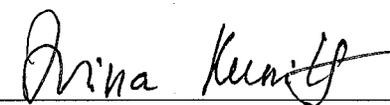
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