
Secretary of State

State of Oregon

DEPARTMENT OF REVENUE

Property Tax Exemptions



Audits Division

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Auditing for a Better Oregon

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This report reviews selected property tax exemptions to determine whether the Department of Revenue has systems in place to best ensure that only eligible property is exempted from taxation.

Oregon statutes allow more than 40 exemption programs. For the 1995-96 tax year, the department reported more than 124,000 exempt properties valued at more than \$25.6 billion statewide. The total assessed value of property for this time period was \$170.9 billion.

Audit results indicate that 41 of the 154 exemptions examined did not meet all of the statutory and rule requirements to qualify for an exemption during the 1995-96 tax year. This report recommends that the department take additional steps to better ensure that all property that should be included on the tax rolls is included.

OREGON AUDITS DIVISION

John N. Lattimer
Director

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SUMMARY

PURPOSE

Recent ballot measures passed by Oregon citizens have placed limits on property tax rates and on overall property taxes collectible. As a result, programs supported by property taxes could experience a loss of funds when property that should be taxed is not included on the tax rolls. The purpose of this audit is to determine whether systems are in place to best ensure that only eligible property is exempted from taxation.

BACKGROUND

State statutes provide for more than 40 types of exemptions that remove real and personal property values from the tax rolls. For the 1995-96 tax year, properties valued at more than \$25.6 billion were exempted from taxation. A majority of the exempted property (76 percent) is public (i.e. government and school district property). The rest is removed from the tax rolls for various purposes, such as exemptions for fraternal and charitable organizations and exemptions to attract businesses to areas to stimulate employment, business, and industrial growth (enterprise zone exemptions).

RESULTS IN BRIEF

We found that not all property that should be taxed is included on the tax rolls. We found that 25 of 62 enterprise zone exemptions (40 percent) and 16 of 92 fraternal and charitable organizations (17 percent) did not meet all of the statutory and rule requirements for exemption. Failing to meet any one of the requirements cited in this report is grounds for disqualification from exemption under the statutes and rules in effect during our audit period. (See page 16 for details on enterprise zone requirements not met and page 28 for details on fraternal and charitable requirements not met.) These 41 exemptions removed more than \$19.2 million from the tax rolls.

For the 1995-96 tax year, we estimate that properties valued at \$147.2 million received a fraternal, charitable, or enterprise zone property tax exemption even though they did not meet all of the requirements. As a result, we estimate, local governments lost approximately \$381,000, and the state and other taxpayers paid an additional

\$1.69 million that would have been collected from these property owners.

RECOMMENDATIONS We recommend that the Department of Revenue use its rulemaking and oversight authority to assist the counties in developing and implementing policies and procedures to better ensure that only those properties that qualify for exemption are exempt from taxation. In addition, we recommend that the Oregon Legislative Assembly review exemption programs for their relevance in today's economic environment.

AGENCY RESPONSE The Department of Revenue generally agrees with the conclusions and recommendations in this report.

INTRODUCTION

HISTORICAL PERSPECTIVE OF PROPERTY TAX EXEMPTIONS

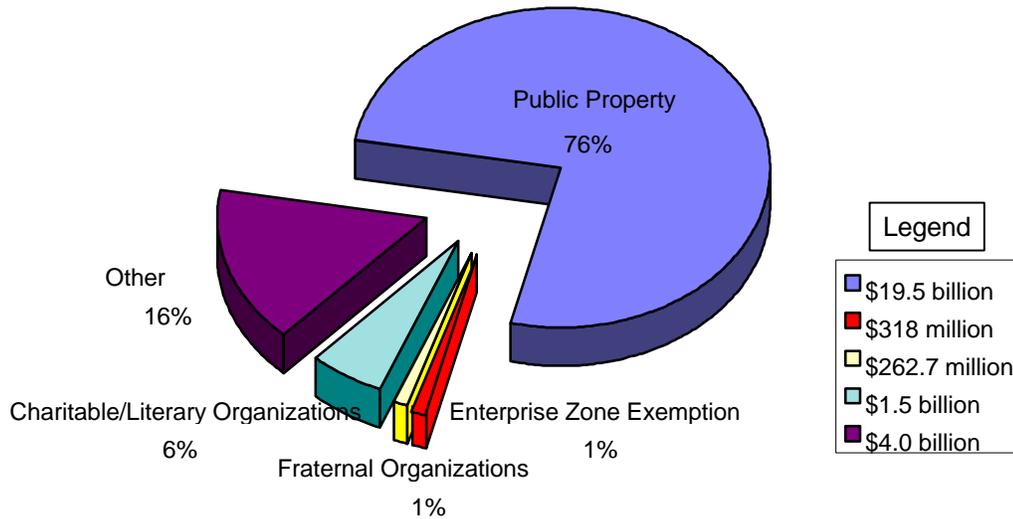
The property tax is Oregon's oldest tax. From the time of statehood in 1859 until the 1920s, property taxes funded both state and local government functions. In 1929, the Oregon Legislative Assembly enacted personal and corporate income taxes for the purpose of providing property tax relief. Until 1942, when state property taxes were eliminated altogether, revenue from both income taxes were used to offset state property taxes. Since 1942, property taxes have been imposed primarily to fund local government activities, including school districts, fire districts, ports, and other special districts, in addition to county and city government functions.

Oregon Revised Statutes (ORS) provide for more than 40 types of exemptions that remove real and personal property value from the tax rolls. Among the exemptions allowed are those for literary, benevolent, charitable, and scientific institutions; fraternal organizations; religious organizations; burial grounds and cemeteries; qualified property within enterprise zones; low-income housing; pollution control facilities; student housing; and natural heritage conservation areas. A list of exemptions and the reported amounts for tax year 1995-96 can be found in Appendix B.

For the tax year 1995-96, the Department of Revenue reported the total assessed value of property in Oregon to be approximately \$170.9 billion, with exempted property values totaling more than \$25.6 billion statewide. Approximately \$19.5 billion, or 76 percent, of the exempted amount is public property. Public property includes federal, state, county, and city buildings and school districts. Nonpublic property represents 24 percent of the total exempt value statewide, or approximately \$6.1 billion. The chart on page 2 illustrates the value of exempted property statewide for public properties, enterprise zones, fraternal organizations, charitable and literary organizations, and all other exempted properties as a percentage of the total exempted property value

statewide. This audit reports on enterprise zone exemptions and fraternal and charitable organization exemptions.

Percentage of Exempted Property Values Statewide



ENTERPRISE ZONE EXEMPTIONS

The enterprise zone exemption program was enacted by the Oregon Legislative Assembly in 1985. Its purpose is to stimulate employment, business, and industrial growth in areas that need the particular attention of government by providing tax incentives to help attract private business investment. Initially the exemption period was a five-year phasedown with 100 percent of the taxable property exempt in the first year and 20 percent in the fifth year. The current three-year exemption was adopted in 1989 along with a major rewrite of the statutes, referred to as the Enterprise Zone Act of 1989. If at any time during the three-year exemption period the property is disqualified, all prior exempt taxes must be repaid. Also, if the business firm or owner fails to give notice that the property is disqualified, a penalty equal to 20 percent of the amount exempted is added to the amount to be repaid.

The Act states that qualified property owned or leased by a qualified business firm in an enterprise zone is exempt

from property taxes for three years; the exemption can be extended as long as five years when certain requirements are met.

A business firm is qualified if the firm:

- Receives at least 75 percent of its annual gross receipts from activity within the zone and produces products or services (assembly, fabrication, storage, etc.) for other businesses.
- Owns or leases property within a zone that is part of the business operation.
- Increases employment by 10 percent if it is an existing firm or hires one or more employees if it is a new firm.
- Does not diminish employment outside the zone and does not substantially decrease employment inside the zone in years two and three of the exemption period.

Qualified property includes the following:

- A new building or structure with a cost of \$25,000 or more.
- An addition to or modification of an existing building or structure, if the total cost is at least \$25,000 in one tax year.
- Any real property, machinery, or equipment, whether new, used, or reconditioned, that is newly purchased, leased, or transferred into the enterprise zone from outside the county within which the zone is located and is installed in property owned or leased by a qualified business firm.
- Any single item of personal property, machinery or equipment, whether new, used, or reconditioned, that is newly purchased, leased or transferred into the enterprise zone from outside the county within which the zone is located and is installed in property owned or leased by a qualified business firm and:
 - ◊ That has a cost of at least \$1,000 if the property is used exclusively for producing tangible goods, or

- ◇ That has a cost of at least \$50,000.
- A building leased from a governmental body.

Property not qualifying includes land and self-propelled motorized vehicles, and otherwise qualified property that was:

- Located inside the enterprise zone prior to the designation of the enterprise zone
- In use or occupancy within the zone for more than 12 months by July 1 preceding the first tax year for which an application for exemption is made.
- Not in use or occupancy in the tax year immediately following completion of construction, addition, modification, or installation.
- Constructed, modified, or installed after termination of an enterprise zone.

Cities and counties apply for areas to be designated as enterprise zones, and the Oregon Economic Development Department approves the designated zones. Property owners then apply for property tax exemptions within the enterprise zones, which are granted by the county assessors.

For the 1995-96 tax year, property values granted enterprise zone exemptions accounted for approximately 5.2 percent of the total nonpublic property exempted in the state, or approximately \$318 million.

FRATERNAL ORGANIZATION EXEMPTIONS

According to a June 1994 report issued by the Legislative Revenue Office, prior to 1961, receiving a property tax exemption as a fraternal organization depended on what county the organization filed application in. According to the report, “in some counties, assessors felt fraternal organizations had enough of a ‘benevolent and charitable’ purpose to qualify them for exemption under [charitable exemption statutes]. In other counties assessors denied

property tax exemptions.”¹ The 1961 Oregon Legislative Assembly enacted a specific exemption for fraternal organizations to establish uniform treatment by assessors. In this legislation, the following organizations are specifically listed as qualifying for the exemption: the State Grange, American Legion, Veterans of Foreign Wars, Eagles, Elks, Masons, Moose, Odd Fellows, Knights of Pythias, and Knights of Columbus.

In order for any other organization to receive a fraternal organization property tax exemption, statutes require that the organization:

- Be organized as a corporation not for profit;
- Be not solely a social club but established under the lodge system with a ritualistic form of work and a representative form of government;
- Regularly engage in or provide financial support for some form of benevolent or charitable activity with the purpose of doing good for others rather than for the convenience of its members;
- Not distribute income to its members, directors, or officers;
- Not pay any member, officer, agent, or employee, in the form of salary or other compensation, an amount beyond that which is just and reasonable compensation commonly paid for such services and which has been fixed and approved by the members, directors, or other governing body of the corporation; and
- Not be a college fraternity or sorority.

For counties to grant a fraternal property tax exemption, statutes require that the organization request the exemption in writing. The statutes further require, if there is a change in ownership or use of the property, that a new statement of exemption, or application, be filed. The number of fraternal organization exemptions reported by the counties to the department increased 115 percent (from 658 accounts to 1,412 accounts) from fiscal year

¹ Legislative Revenue Office, *Oregon Tax Expenditures*, pp. 14-17.

1993-94 through fiscal year 1995-96, with an increase in property value of approximately 54 percent (from \$170.5 million to \$262.7 million).

Properties granted exemptions as fraternal organizations for the 1995-96 tax year account for 4.3 percent, or approximately \$262.7 million, of the total nonpublic exempted property in the state.

CHARITABLE ORGANIZATION EXEMPTIONS

The first statute granting exemption to charitable organizations was enacted in 1854. Although there have been subsequent amendments to some of the details, the original wording of the main exemption remains intact. According to statutes, there are two tests to qualify for exemption. First, the institution must be a charitable organization. Second, the property must be “actually and exclusively occupied or used” to further the exempt purpose of the institution.

For counties to grant a charitable property tax exemption, statutes require that the organization request the exemption in writing. It further requires, if there is a change in ownership or use of the property, that a new statement of exemption, or application, be filed.

Property values granted exemptions as charitable/literary organizations for the 1995-96 tax year account for 24.7 percent, or approximately \$1.5 billion, of the nonpublic property exempted in the state.

ROLES AND RESPONSIBILITIES

Department of Revenue Responsibilities

Oregon’s property tax program is found in ORS chapters 305 through 312. According to ORS chapter 306.115(1), “The Department of Revenue shall exercise general supervision and control over the system of property

taxation throughout the state.” It further states, “The department may do any act or give any order to any public officer or employee that the department deems necessary in the administration of the property tax laws so that all properties are taxed or are exempted from taxation according to the statutes and Constitutions of the State of Oregon and of the United States.” [Emphasis added.]

The department has broad authority and control over the exemption program, while ongoing administration of the program occurs at the county level. In addition to providing general supervision and control, the department is required by statute to construe and enforce all state tax and revenue laws, including ensuring compliance of public officers with laws and orders affecting property taxes. In pursuit of this goal, the department has the authority and responsibility to examine and test the work of county assessors at any time, and may issue an order directing the public officer or employee to comply with such laws and rules. The department is also responsible for providing in-service training to assessors as is expedient and beneficial to the needs of the state. The statutes further indicate that the department shall issue regulations, bulletins, manuals, instructions, and directions to county assessors as to the methods best calculated to secure uniformity according to law in the system of assessment and collection of taxes. Prior to July 1, 1997, the statutes required the department to conduct a performance review of each county’s operations no less frequently than once every six years.

In addition to having broad authority over exemption programs in general, the department has additional responsibilities under the Enterprise Zone Act of 1989. The Act directs the department to adopt any rules considered necessary to administer the enterprise zone exemption program; assist the Oregon Economic Development Department (OEDD), county assessors, and sponsors of enterprise zones in precertifying eligible business firms; assist eligible business firms in obtaining benefits of applicable tax incentive or inducement programs; prepare forms and worksheets to be used by eligible business firms applying for precertification or by precertified firms applying for property tax exemption; and submit a written report to the OEDD describing actions taken by the department, number of jobs created, value of investments in qualified property, and other

information considered necessary by the department or required by the OEDD. Prior to July 1, 1997, the statutes also required that the department receive a copy of all exemption applications from the counties.

County Assessor Responsibilities

Oregon Revised Statutes provide for receipt of exemption requests by county assessors. The department, through its supervisory authority, has further defined county assessors' roles to include routine administration of exemption programs, such as review of applications, review of applicable property, and determination of an organization's compliance with qualifications for exemption.

State statutes also establish county assessor responsibilities required under the Enterprise Zone Act. The Act directs the assessor of a county within which an enterprise zone is located to assist the local zone sponsor and eligible or precertified business firms in determining whether property will qualify for property tax exemption under the Act; process applications from precertified business firms for property tax exemptions under the Act; take necessary action when a business firm or property is no longer qualified for the property tax exemption; and submit a written report to the department describing actions taken by the assessor, the number of jobs created, the value of investments in qualified property, and other information considered necessary by the assessor or required by the department.

Other Parties Responsible for Enterprise Zones

The OEDD shares responsibility with the Department of Revenue for the enterprise zone program in general. State statutes provide that the OEDD shall adopt rules considered necessary in administering the designation of enterprise zones within the state; assist a sponsor of an enterprise zone in its efforts to retain, expand, start, or recruit eligible business firms; assist an eligible business firm in obtaining the benefits of applicable incentive or inducement programs authorized by Oregon law; and assist in implementing first-source hiring agreements by

publicly funded job training providers with precertified and qualified business firms.

Further, statutes charge local zone sponsors (the city or county that applied for and received approval of an enterprise zone) with additional responsibilities under the Act. Statutes provide that the sponsor of an enterprise zone shall appoint a local zone manager; provide local tax incentives and local regulatory flexibility to precertified or qualified business firms; process applications from eligible business firms for precertification; assist the county assessor in reviewing tax exemption applications; prepare, implement, and annually update a plan for marketing the enterprise zone; manage the enterprise zone in accordance with state statutes; identify property available for sale or lease to eligible business firms; and prepare indices of street addresses, tax lot numbers, or other information to facilitate the identification of land inside an urban enterprise zone.

RECENT LEGISLATION

The 1997 Oregon Legislative Assembly made several changes to statutes that will have a direct impact on the property tax program statewide. House Bill 2049 repealed the law that required the Department of Revenue to conduct performance reviews of county assessment and taxation functions at least once every six years. House Bill 2143 made several changes to the Enterprise Zone Act. Notably, it granted rulemaking authority to the OEDD for the entire Enterprise Zone Act, including those laws relating to the property tax exemption. Previously the Department of Revenue had sole rulemaking authority for those laws relating to administration of the enterprise zone exemption. Under HB 2143, the Department of Revenue maintains joint authority with OEDD to make rules deemed necessary for administration of these laws with the exception of the laws pertaining to exemptions for certain leased property; qualifications for exemption; eligibility; and hiring requirements. OEDD now has sole rulemaking authority for these portions of the Act. This bill also repealed the requirement that copies of all enterprise zone precertification and exemption applications be sent to the Department of Revenue.

These changes are noteworthy for the following reasons. First, changes made by HB 2049 are important because the performance reviews were used by the department as a mechanism to correct errors and train county personnel. Budget cuts at both the state and county levels in recent years severely reduced the number of employees available to conduct such reviews. Second, changes made by HB 2143 are important because the OEDD and the Department of Revenue have different missions. The OEDD helps communities and businesses create better jobs and improve their economic opportunities and quality of life. The Department of Revenue makes tax systems work effectively to fund services for Oregonians. The rulemaking authority provided to the department allowed it to act as a watchdog to ensure that only appropriate exemptions were granted. Because HB 2143 did pass, this role was removed from the Department of Revenue. Third, when the department received copies of enterprise zone exemption applications, it allowed the department's personnel to monitor exemptions granted within the six-year performance review cycle (which, as noted above, is also no longer required). Most enterprise zone exemptions expire after three years; therefore, the receipt and review of applications served as an interim review.

Also, Oregon voters passed Measure 50, a property tax reduction measure, in May 1997. Subsequently, the Legislature passed Senate Bill 1215 in an effort to guide the department, as well as the counties, in implementing the measure. The effects of this measure and corresponding legislation as related to those areas discussed in this report are briefly outlined as follows:

- Senate Bill 1215 defines the maximum assessed value for a property as each property's 1995-96 real market value less 10 percent. The bill goes on to indicate that the assessed value for the tax year beginning July 1, 1997, shall be the lesser of the maximum assessed value or the real market value of the property. The assessed value for subsequent tax years cannot increase more than three percent each year.
- The primary result of Senate Bill 1215 is a change in the type of taxing authority that a taxing district holds. Rather than the current levy system, the districts will now operate under a permanent rate system.

Department personnel indicate that because of the fixed rate, along with fairly predictable assessed values, local governments may be better able to forecast and budget.

- Rather than a fluctuating tax rate based on assessed value levels, a permanent rate will be set. Therefore, inappropriate exemptions could result in actual dollar losses to local governments.
- Maximum tax rate limits initially enacted under Measure 5, passed by the voters in 1990, are still in effect under the new measure. These limits are \$5 per \$1,000 real market value for education and \$10 per \$1,000 real market value for other government services.
- Bonds and other voter approved exceptions are still “exempt” from constitutional rate limits.

The state’s general fund must continue to replace revenue lost by schools because of the rate limitations. The amount replaced shall not be less than the total replaced for the 1997-98 tax year.²

SCOPE AND METHODOLOGY

The scope of the audit included a review of real and personal property tax exemptions granted to businesses and organizations throughout the state of Oregon. The main objective of the audit was to evaluate the controls at the Department of Revenue related to managing real and personal property tax exemptions.

We limited our review to the following types of exemptions: enterprise zone exemptions and fraternal and charitable organization exemptions. In general, our review covered the period of July 1, 1995, through June 30, 1996. (See Appendix A for the specific methodology we used to limit our review and how data were retrieved.)

² State assistance for K-12 education is now the single largest expenditure of state general funds.

To select our samples and to estimate the total impact of exemptions that did not meet all of the requirements for exemption, we relied extensively on computer-processed data contained in the county assessors' data files. Though we found some errors in this data, the errors did not impact our conclusions or our recommendations.

To evaluate the controls at the department related to managing real and personal property tax exemptions, we reviewed applicable laws and regulations related to the oversight of property tax exemptions. We also examined administrative rules and other policies and procedures established by the department for counties to follow when exempting property. We examined statewide performance reviews completed by the department to determine the depth of the review conducted, the findings, and the follow-up actions when findings were noted. We interviewed responsible department and county personnel to determine how property becomes exempted; how exemptions that expire are adjusted on the rolls in a timely manner; what controls are in place to ensure adequate review of all exempted property; and what, if any, obstacles or disincentives exist that may limit effective management of exemption programs. To determine whether the department needs to strengthen its monitoring and oversight, we determined the extent to which exempted property did not meet requirements for exemption during tax year 1995-96 and the effects of those exemptions.

To determine whether property exempted met the statutory or rule requirements for the exemption, we reviewed pertinent laws and regulations, policies and procedures, and the history of changes to specific exemption types. We selected and tested 62 enterprise zone exemptions and 92 fraternal and charitable exemptions against the established criteria (see Appendix A for the specific methodology we used to select the sample items). We reviewed supporting documentation at both the department and county levels. We also interviewed department and county staff to evaluate the process used to determine whether or not a specific property or organization met the applicable exemption criteria.

To quantify the dollar effects when exemptions were granted that did not meet all of the statutory or rule

requirements, we identified the total real market value associated with those exemptions for the 1995-96 tax year. We then projected this value to the entire population of enterprise zone and fraternal and charitable organization exemptions reported to us. We identified the tax rates for each of the code areas in which the exempted properties that did not meet all requirements were located, and determined the amount of property taxes that should have been imposed on the property for the 1995-96 tax year. We then analyzed what effect not imposing these taxes had on other property owners throughout the state, as well as on the state general fund.

This audit was conducted according to generally accepted government auditing standards. We limited our review to those areas specified in this section of the report.

AUDIT RESULTS

ENTERPRISE ZONE EXEMPTIONS

In 1985, the Oregon Legislative Assembly determined that the health, safety, and welfare of the people of Oregon are dependent on the continued encouragement, development, growth, and expansion of employment, business, industry, and commerce within the state, and that there are certain depressed areas in the state that need the particular attention of government to help attract private business investment into these areas. The Oregon Enterprise Zone Act was created to stimulate employment, business, and industrial growth in the depressed areas of Oregon by providing tax incentives. The 1985 Act has since been replaced by the Enterprise Zone Act of 1989. Until 1997, the purpose remained unchanged. Recent legislation added the need to help resident businesses to reinvest and grow.

A qualified business firm can receive a property tax exemption for its qualified property located in an enterprise zone when certain conditions are met. For example, the business firm qualifies for exemption if the firm:

- Is an eligible business firm as defined by statutes;
- Has business operations located inside an enterprise zone;
- Owns or leases qualified property located inside an enterprise zone;
- Satisfies the hiring requirements;
- Did not diminish employment outside the enterprise zone;
- Did not substantially curtail employment within the enterprise zone;
- Complies with all local, state, and federal laws applicable to the firm's business; and

- Complies with all additional conditions for precertification imposed by an enterprise zone sponsor.

The exemption is available for three tax years, and may be extended for as long as two subsequent tax years with zone sponsor approval when additional conditions are met.

Exemptions Granted That Do Not Meet All Statutory and Rule Requirements

Of the 62 enterprise zone property tax exemptions tested, we found that 25 (40 percent) did not meet all of the statutory and rule requirements necessary to receive an enterprise zone property tax exemption. For these 25 exemptions, property valued at more than \$16.9 million was exempted for the 1995-96 tax year. The requirements that were not met fall into four categories: improper precertification, ineligible property, first-source hiring agreements not entered into, and annual statements of compliance not filed. Failing to meet any one of these requirements is grounds for disqualification from exemption under the statutes and rules in effect during our audit period. The table below summarizes our testing results and shows for each of the four categories, the number of exemptions that did not meet the statutory or rule requirement and the value of the exempted properties. [Note: Summary of results will not total 25 exemptions because some exemptions failed more than one category.]

ENTERPRISE ZONE TESTING RESULTS

Statutory or Rule Requirement Not Met	Number of Exemptions (Firms)	Exempted Property Value
Improper Precertification	6 Exemptions (6 Firms)	\$8,262,580
Ineligible Property	5 Exemptions (5 Firms)	\$87,580
First-Source Hiring Agreements Not Entered Into	12 Exemptions (12 Firms)	\$9,845,540
Annual Statements of Compliance Not Filed	7 Exemptions (5 Firms)	\$2,075,814

Improper Precertification

Six business firms were granted property tax exemptions when they did not precertify their investments prior to commencing construction, modification, or installation of qualified property in the zone as required by statute. The property value exempted for these six firms totaled \$8,262,580.

Precertification is a process in which a business firm is required to complete and submit a precertification application to the local zone manager before any physical work begins at a site in the enterprise zone and before hiring eligible employees. The precertification application includes a description of the nature of the firm's business operations in the enterprise zone, a description and estimated cost or value of the qualified property to be constructed, modified, or installed in the enterprise zone, an estimate of the number of employees that will be hired by the firm, and a commitment to meet all other requirements as prescribed by statute.

Precertification protects the business firm because it helps ensure that the business firm has the correct knowledge of the enterprise zone and its requirements before making investments and it gives the firm "some assurance" that it will qualify for an exemption on the property in which it is investing. Precertification also protects the state's interest because it helps ensure that the business firm has committed to the employment requirements and that its operations meet the requirements for eligibility.

Precertification also helps to ensure that the property tax exemption encouraged the investment, that is, the investment did not take place prior to the precertification or the establishment of the enterprise zone. When the precertification requirements are not met, and there are no circumstances whereby the Department of Revenue might waive the precertification, the department and the county are required to disallow the exemption. In some cases, this disallowance did not happen. For example:

- In one county, exemptions were granted to two business firms that began construction prior to the business firms' filing a precertification application. In one case, construction started approximately four months prior to the filing of the application for precertification. In the other case, construction started prior to the zone designation. State statutes

specifically exclude both of these situations from tax exemption. Although there may have been extenuating circumstances that would allow the department to waive the precertification for these two business firms, it did not do so. The property value exempted for these two firms totaled \$5,905,730 for the 1995-96 tax year.

- In another county, exemptions were granted to two business firms that also did not precertify their investment prior to commencing construction. These two business firms leased office space from the owner of a commercial office complex. Construction of this complex was well under way prior to the filing of either precertification application. While county staff indicate that a precertification was filed in each case prior to construction of the area occupied by each specific tenant, the business firms should have received exemption for only that portion of the construction started after precertification and attributable to their moving into the space. One firm received an exemption of \$151,070 for the 1995-96 tax year even though only \$2,188 in improvements were attributable to completion of its portion of the building.

During the 1995-96 tax year, department and county staff allowed exemptions for properties such as the above based on an Oregon Economic Development Department (OEDD) administrative rule and a 1995 letter of advice from the Department of Justice. During our review, we questioned this interpretation of the law. From our discussions with department and county staff, it became apparent that further clarification was needed. A February 3, 1998 letter of advice from the Department of Justice reverses the conclusion of the 1995 letter and points out some potential inconsistencies with the OEDD administrative rule. The 1998 letter concludes that a building is qualified for an exemption only when the lessee applies for precertification before the commencement of construction. To help relieve some of the confusion in this area, it would be beneficial to clarify this issue in both statute and administrative rule.

Ineligible Property

Ineligible property was included in the exempt property value for five of the exemptions granted. The statutes specifically state that personal property must have a cost of at least \$1,000 and be used exclusively for producing tangible goods or, if it is not used exclusively for producing tangible goods, must have a cost of at least \$50,000 to be considered qualified property. They further identify self-propelled motor vehicles as ineligible property. We found self-propelled motor vehicles, personal property with an original cost of less than \$1,000, and personal property with a cost of less than \$50,000 not used exclusively to produce tangible goods included in the exempted value. The five business firms received property tax exemptions on ineligible property totaling \$87,580 for the 1995-96 tax year.

First-Source Hiring Agreements Not Entered Into

In addition, 12 firms were granted exemptions although the county granting the exemption had no evidence indicating that a first-source hiring agreement had been entered into by the firm. According to statutes, the business firm is not a qualified business firm eligible for a property tax exemption if the firm has not entered into a properly executed first-source hiring agreement for the period of exemption. According to a letter of advice from the Department of Justice, if the firm does not submit evidence that they have entered into a first-source hiring agreement with their application, the assessor may not grant the exemption.

The Oregon Legislative Assembly established that one of its basic premises for enacting the enterprise zone program includes stimulating employment in areas that need the particular attention of government to help attract private business investment. As a method for ensuring that local residents would be considered for positions created by the enterprise zone development, they also mandated that the business firm enter into a first-source hiring agreement with a publicly funded job training provider for the period of property tax exemption. First-source hiring agreements are important because they are the best evidence that the business firm is complying with this hiring requirement criteria established by statute. After we notified the county assessors we found no

evidence that first-source hiring agreements had been entered into for the 12 firms, two of the business firms entered an agreement and copies were forwarded to us. A total property value of \$9,845,540 was exempted for the 1995-96 tax year for these 12 firms.

Annual Statements of Compliance Not Filed

Finally, we found five business firms failed to file with the county annual statements of compliance for the 1995-96 tax year for seven exemptions granted. The department requires that a business firm file an annual statement of compliance with the county for each exemption granted. According to a letter of advice from the Department of Justice, the annual filing of a statement of compliance is a precondition to the continued receipt of the exemption. If the business firm fails to meet this requirement, the assessor is required to disqualify the firm from exemption. The annual statements of compliance are important in determining that business firms meet the hiring requirements necessary to avoid disqualification. We also noted the county did not always follow up when a firm failed to file a statement for exemptions that expired at the end of the 1995-96 tax year. A total property value of \$2,075,814 was exempted for the 1995-96 tax year for the five firms.

**Effect of Granting Exemptions
That Do Not Meet
Requirements**

For the 25 properties that did not meet all of the statutory and rule requirements necessary to receive an enterprise zone exemption, property valued at more than \$16.9 million was excluded from the base assessed value calculation for the 1995-96 tax year. If the amount had been included in the base assessed value calculation, approximately \$260,000 in taxes could have been collected from these property owners. Given the tax system at the time of our review, the state and other taxpayers picked up a portion of the lost revenue. The actual dollar loss to local governments for other government programs and services for these 25 exemptions was approximately \$43,000.

When these findings are projected to the entire population of enterprise zone exemptions in effect for the 1995-96

tax year, approximately \$595,000 in taxes could have been collected from owners of property who did not meet all of the requirements for exemption. The state and other taxpayers picked up an estimated \$497,000 of the lost revenue. Further, the actual dollar loss to local governments was an estimated \$97,000.

According to information compiled by the department, the total real market value exempted for enterprise zones during the 1996-97 tax year is \$1.1 billion. This is more than a 234 percent increase from the total amount exempted during the 1995-96 tax year. With the rapidly increasing dollar amount of exempted property, it is important that adequate supervisory review and oversight be in place to ensure that the exemptions are appropriate.

Exemptions Granted Without Adequate Information

During the course of our audit we also found that counties granted a majority of the exemptions examined without obtaining or validating information needed to make appropriate granting decisions. For example:

- We found 12 instances in which the department did not receive copies of exemption applications as required by statute for firms granted enterprise zone property tax exemption prior to June 30, 1996. The receipt of these applications made it possible for the department to easily monitor and review individual exemptions to ensure they were appropriate. It should be noted that the 1997 Oregon Legislative Assembly revoked the requirement that the department receive a copy of the exemption applications.
- In 26 instances the first-source hiring agreement did not cover the period of exemption as required by statute. The Enterprise Zone Act of 1989 required that a first-source hiring agreement be entered into for the period between precertification and March 1 following the calendar year in which the investment in qualified property was completed. The 1993 Legislative Assembly modified the requirement to say, "A precertified business firm shall enter into a first-source hiring agreement...for the period of property tax exemption." This same language currently stands in ORS 285.605(1). We did not

count as an exception those business firms that precertified or applied for exemption prior to or just as the laws changed in 1993.

- In six instances evidence such as city or county ordinance of the intent to exempt motel property was not located in the department's files. An enterprise zone exemption is available to hotel, motel, or destination resort property under ORS 285.610. One of the requirements of this statute is that the department be notified in writing of the applicable zone sponsor's desire to exempt hotel, motel, and destination resort property. No evidence was found at the department of the intent to exempt this type of property. We were able to obtain from zone managers copies of the city or county ordinances for two properties. After notifying the county assessors that we did not find evidence for the other four properties, county assessors obtained copies of ordinances from a zone manager and another county office for three of the properties. One ordinance was never found.
- In 18 instances the application for exemption was not signed by all appropriate parties. Also, in 24 instances information was missing on either the precertification or the exemption application. The legality of the documents could be questioned when complete information on exemption documents, as well as a signature by all appropriate parties, is not obtained.
- In 39 instances physical inspections or verifications of the property listed for exemption were not completed. In one case, a firm did not identify individual items for exemption on its real property return; rather, the firm made a blanket statement indicating that the total value of the property was \$195,741. This amount was used in the exempt value calculation.

The department and counties reported that actual physical appraisals on a specific property are required only once every six years. They use industrial property returns, real property returns, and personal property returns between appraisals to identify changes to the property. We found that this is true for the industrial accounts handled by the department, but some (not all) counties complete a physical inspection

and appraisal of all new construction and additions to real property as they occur. When physical inspection and appraisal of property is not completed prior to granting an exemption, it leaves the door open for exemption of ineligible property and unrepresentative real market values of property exempted.

- In 51 instances verification of information such as the percentage of gross receipts obtained from eligible activities was not completed. In addition, verifications of employment increases and decreases were not completed for 56 of the exemptions examined. Several counties reported that attempts to verify the employment numbers with an independent source such as an employment office are futile. One county employee stated that he was informed by an employment office that all employment records are confidential. Some counties may be unaware that the department has access to obtain employment information from the Employment Department under ORS 657.665.

The importance of such verification was demonstrated by the department itself in a performance review report published in January 1993. The department noted that the county did not always obtain verification that 75 percent of the firm's gross receipts were from eligible activities. As a result of the review, it was discovered that one company completed only eight percent of its business in eligible activities. The result was an exemption granted in error. The department recommended that the county revoke the exemption and add the property back to the tax rolls.

In another example, one firm reported 40 employees at the time of precertification and 49 at the time of application. Subsequently, annual statements of compliance reported that employment had decreased to 42, a level that would indicate the firm was no longer in compliance with hiring requirements. After several months of correspondence between the county and the firm, it was discovered that initial employment figures had included part-time and seasonal workers in addition to the eligible fulltime, permanent employees. According to statute, only permanent, full-time employees are eligible to count

toward hiring requirements. Because verification of employment at the time of precertification and application was not obtained, it is impossible to determine if this firm actually qualifies for exemption. Employment numbers are included annually in the department's *Annual Enterprise Zone Tax Exemption Data* report. Because employment was not verified for 56 of the 62 exemptions reviewed, the information contained in the report may be inaccurate. In addition, we noted five instances in which inaccurate real market values were reported to the department for inclusion in the report.

The granting of an inappropriate exemption can result when verification of information such as gross receipts and hiring requirements is not performed at the time of application, or as reported on annual statements of compliance. Also, when inaccurate values are reported on the department's *Annual Enterprise Zone Tax Exemption Data* report, users of the information, including other state agencies and the legislature, make decisions based on inaccurate information.

Overall Supervision and Operations Related to the Enterprise Zone Property Tax Exemption Program

The department has not used its rulemaking authority to establish sufficient policies and procedures for enterprise zone property tax exemptions. The department issues an exemption manual to county assessors to provide guidance on procedures to use when granting exemptions and to help define terms and interpret statutes. The department, however, has not included enterprise zone exemptions in this manual. In addition, the *Oregon Administrative Rules* established for this program do not address procedural issues, such as what should be done by the county assessors during the exemption review and approval process. Further, the department has not established adequate policies and procedures for its own staff to follow related to the review and supervisory control of enterprise zone precertification and exemption materials.

The department stated that the *Oregon Enterprise Zones* publication available to interested businesses is considered the procedures manual for the counties. This publication is co-sponsored by the Department of Revenue and the Oregon Economic Development Department. It contains information that the department and OEDD believe a business firm must know in order to apply for the exemption. It is not adequate for use as a procedures manual because it does not explain the steps that should be taken during the exemption review and approval process.

Most of the counties interviewed during our review indicated that training provided by the Department of Revenue related to the enterprise zone exemption program is minimal. The department has indicated that training is provided in conjunction with the OEDD. Counties, however, noted that any training provided was clearly administered by OEDD and training issues were presented as they related to OEDD's objectives, not the department's.

One county employee noted that pertinent information, such as legal rulings, opinions, and orders, were once circulated by the department to aid counties in determining standards and procedures for enterprise zone exemptions. He noted, however, that the information is not provided as frequently as it was in the past.

RECOMMENDATIONS

We recommend the department develop and implement a system that best ensures that enterprise zone property tax exemptions throughout the state are appropriately granted. Specifically, we recommend that the department do the following:

1. Work with county assessors to develop and implement policies and procedures for counties to follow when processing enterprise zone exemption applications. The department should consider including policies and procedures that address the following issues:
 - Precertification review;
 - Verification of the 75 percent gross receipts test;

- Verification of hiring and employment requirements;
- Development of appraisal procedures for both real and personal enterprise zone property;
- Verification of compliance with property qualifications;
- Verification of information contained in the annual statement of compliance;
- Verification of compliance with extended abatement criteria; and
- Development of standards for annual enterprise zone data reported to the department for inclusion in its report to OEDD.

In addition, the department should establish policies and procedures for its own staff to follow related to:

- The review and supervisory control of enterprise zone precertification and exemption materials;
 - The granting of precertification waivers, including both circumstances deemed eligible for a waiver and the appropriate time period during which a waiver should be granted;
 - Appraisal procedures for real and personal enterprise zone property; and
 - Reporting and information gathering standards for annual enterprise zone data reported to OEDD.
2. Increase supervision and control over counties' granting of enterprise zone property tax exemptions, where possible, to help ensure that exemptions are consistently granted according to applicable laws and regulations. To accomplish this, the department should establish a system of periodic reviews of county programs to provide training and feedback to county staff and to ensure that established policies and procedures are being followed.
 3. Increase its efforts to provide enterprise zone exemption training to the county assessor's offices. As a part of this training, the department should include the enterprise zone exemption program in the exemption manual published by the department, and recommence distribution of pertinent information to the counties to aid them in making exemption decisions.

4. In consultation with the Oregon Economic Development Department and other pertinent parties, introduce legislation to clarify enterprise zone exemption statutes so that (a) it is clear what requirements an organization must meet to qualify for exemption and (b) it is clear who is responsible for ensuring that the requirements are met.

FRATERNAL AND CHARITABLE ORGANIZATION EXEMPTIONS

In 1961, the Oregon Legislative Assembly determined that counties were not consistently granting property tax exemptions to fraternal organizations statewide. To correct this inconsistency, the Oregon Legislative Assembly enacted statutes that define fraternal organizations and specifically name certain organizations as qualifying organizations. Included in these groups are the Masons, Knights of Pythias, Knights of Columbus, Benevolent and Protective Order of Elks, Fraternal Order of Eagles, Loyal Order of the Moose, Independent Order of the Odd Fellows, Oregon State Grange, American Legion, and Veterans of Foreign Wars.

Laws exempting property taxes for charitable organizations were first enacted in 1854. Since that time, laws have remained relatively unchanged. The purpose for creating the exemption appears to be to subsidize organizations providing services that state or local government might otherwise need to provide. This exemption applies to many types of private nonprofit organizations. Examples are hospitals, social services, museums, youth and athletic groups, summer camps, and conservation groups.

Exemptions Granted That Do Not Meet All Statutory and Rule Requirements

Of the 92 fraternal and charitable property tax exemptions tested, we identified 16 (17 percent) that do not meet all of the applicable statutory and administrative rule requirements for exemption. The total value recorded on individual tax account records for these 16 properties was

\$2.3 million for the 1995-96 tax year. The requirements that were not met fall into three categories: change in ownership or use, ineligible organizations, and insufficient activities. The table below summarizes our testing results and shows for each of the three categories, the number of exemptions that did not meet the statutory or rule requirement and the value of the exempted properties. [Note: Summary of results will not total 16 exemptions because some exemptions failed more than one category.]

FRATERNAL AND CHARITABLE TESTING RESULTS

Statutory or Rule Requirement Not Met	Number of Exemptions (Organizations)	Exempted Property Value
Change in Ownership or Use	12 Exemptions (10 Organizations)	\$1,579,902
Ineligible Organizations	2 Exemptions (2 Organizations)	\$396,570
Insufficient Activities	5 Exemptions (4 Organizations)	\$717,730

Change in Ownership or Use

Twelve organizations have not filed a new application for charitable exemption even though there has been a change in ownership or a change in use of the property. In several cases, the current property use may not permit exemption. For example:

- An organization providing residential habilitation and training for developmentally disabled people continues to receive an exemption on 9.08 acres of owned property even though it no longer owns the site. As reported by an administrator of this organization, the property was leased to two other organizations in 1994, except for 3,570 square feet used as office space. The administrator also stated that the entire property was sold in 1997, and the organization now leases back the 3,570 square feet from the new owner. Not only did the original property owner fail to submit a new application to the county in 1994 for a change in use of the property, we found no applications from the two other organizations. The county computer record does not

indicate a real market value for this property. According to the 1973 Application for Property Tax Exemption, however, the market value was approximately \$1.3 million. Furthermore, the assessor's office reported to us that the property sold for \$758,422 in February 1997.

- An organization is receiving an exemption on property purchased from a previously eligible owner without submitting a new application attesting to the new organization's qualifications. Further, the use of this property changed from a medical services clinic to a family resource center and does not appear to qualify for exemption. A total property value of \$99,740 was exempted from the property tax rolls for the 1995-96 tax year.
- An organization continues to receive an exemption for property even though it no longer uses the property. Since July 1, 1993, the property has been rented to an organization that does not appear to meet eligibility requirements for exemption. A total property value of \$82,000 was exempted from the property tax rolls for the 1995-96 tax year.
- An organization continues to receive a property tax exemption for a vacant lot. The original application filed in 1989 requested an exemption for all lots owned by the organization. This application indicated that all lots were under construction. In December 1991, the county physically inspected the property and determined it was undeveloped land, but exempt status has not been revoked. A total property value of \$9,090 was exempted from the tax rolls for the 1995-96 tax year.

Through our discussions with department and county assessor staff, we have found that the definition of what constitutes a "change in use" is not immediately clear. According to a letter of advice from the Department of Justice, the interpretation of "change in use" that appears most consistent with legislative intent is that a new application must be filed whenever there is a substantial change of use from the purposes set forth in the application for which the current exemption was granted. While the new use of properties may still qualify for exemption, organizations are required to file new

applications so that the new use can be reviewed to ensure that they do in fact continue to qualify. Failure to file a new application when there is a change in use is grounds for disqualification from exemption.

All of the exemptions that we identified as exceptions due to a change in use of the property were due to the fact that the organizations' use of the property at the time of our review was substantially different than that stated on their exemption applications. For example, a 1994 application for one organization stated that the property was going to be used as a coffee shop to provide employment and training opportunities for developmentally disabled individuals; however, at the time of our review in 1997, the property was empty and was never used for the stated purpose. To help relieve some of the confusion in this area, it would be beneficial to clarify in statute or administrative rule what constitutes a "change in use."

Ineligible Organizations

Two organizations continue to receive exemption as fraternal organizations even though they do not meet eligibility requirements. Fraternal organizations are considered eligible if (a) they are specifically listed in statute, or (b) they meet the statutory requirements. One of the statutory requirements is that an eligible fraternal organization be a corporation that "is not solely a social club but is established under a lodge system with a ritualistic form of work and representative form of government." Examples of ineligible organizations include the following:

- An organization receiving an exemption as a fraternal organization is not an incorporated organization performing charitable work. A total property value of \$218,070 was exempted from the property tax rolls for the 1995-96 tax year.
- Another organization is receiving a property tax exemption as a fraternal organization even though it does not own, lease, or occupy the property being exempted, does not meet the statutory definition of a fraternal organization, and disbanded in 1990. The owner of the property has not notified the county of a change in use. A total property value of \$178,500 was

exempted from the property tax rolls for the 1995-96 tax year.

Neither of the above organizations is specified in statute as an eligible fraternal organization.

Insufficient Activities

Five organizations with limited public benefit or charitable activities are receiving exemption. State statutes require that the exempted property be actually and exclusively occupied or used in the charitable work carried on by the organization. In its administrative rules, the department further requires that: (a) “any organization claiming the benefit of property tax exemption under ORS 307.130, as a charitable institution, must have charity as its primary, if not sole, object and must be performing in a manner that furthers that object”; and (b) “the activity conducted by the charitable institution must be for the direct good or benefit of the public or community at large.” According to the department’s rules, “An organization established primarily for the benefit of its members is not a qualifying charity.” Examples of insufficient activities include the following:

- One organization receives an exemption for a building it rents to other clubs and organizations for meetings, receptions, and other functions. Although the organization itself was involved in actual charitable work when it applied for exemption in 1927, its sole purpose today is to provide a place for other organizations to meet. This account may also be an example of a change in use that has not yet been reported. A total property value of \$267,970 was exempted from the tax rolls for the 1995-96 tax year.
- An organization receives an exemption for a building it leases to another organization. The lessee uses the building as a lounge and meeting hall. The lessee also rents the building to individuals and other charitable organizations 20 percent of the time. Renting space to other charitable organizations does not constitute charitable work. In 1995, approximately \$304,000 in property was exempted from the tax rolls.

**Effects of Granting Exemptions
That Do Not Meet
Requirements**

For the 1995-96 tax year, the 16 exemptions above represent a total property value of more than \$2 million. If this amount had been included in the base assessed value calculation, approximately \$31,000 in taxes could have been collected from the 14 property owners. Given the tax system in effect at the time of our review, the state and other taxpayers picked up a portion of the lost revenue. The actual dollar loss to local governments for these 16 exemptions was approximately \$6,042.

When these findings are projected to the entire population of fraternal and charitable exemptions in effect for the 1995-96 tax year, we estimate that \$1.5 million in taxes could have been collected from owners of property who did not meet the statutory and rule requirements for exemption that were in effect during our audit period. The state and other taxpayers picked up an estimated \$1.1 million of the lost revenue. Further, the actual dollar loss to local governments was an estimated \$280,000. It should be noted that these projected dollar amounts are based on property values that are more than likely less than market value. Many of the properties receiving an exemption have not been physically reappraised in the past six years and in some counties these properties are not reappraised at all. For example, in one county exempt properties are not reappraised and as a result, more than half the exempt properties are carried on the computer records at a zero dollar value. Thus, we not only were unable to obtain a dollar value for some of the properties included in our population.

**Exemptions Granted Without
Adequate Information**

During the course of our review we also found that counties grant exemptions without obtaining and validating information needed to make appropriate granting decisions. For a majority of the exemptions tested (includes the 16 mentioned above), the exemption files at the county did not contain enough evidence or supporting documentation for us to determine that the exemption was appropriate. Using the exemption files at the county, we found the following:

- 65 instances in which there was no evidence of the organization’s separate accounting of funds;
- 63 instances in which the documentation of the organization’s charitable activities was insufficient;
- 18 instances in which the documentation of property use was insufficient;
- 15 instances in which there was no evidence the application was approved; and
- 10 instances in which there was no evidence of the organization’s incorporated status.

For us to determine that the 70 accounts might qualify for exemption, we requested that organizations provide us with the information we would expect to find in the county exemption files, such as articles of incorporation, evidence of charitableness, and evidence of how the property is used. Based on the additional information provided by the organizations, we determined that 49 of the 92 accounts were appropriately exempted from taxation. In addition to the 16 accounts previously mentioned as being exempted even though they did not meet all of the requirements for exemption, however, we identified 23 accounts for which exemption remains questionable, even after we received the additional documentation from the organizations. Four accounts were miscoded as charitable accounts.

Overall Supervision and Operations Related to the Fraternal and Charitable Organization Exemption Program

The property tax exemption program for fraternal and charitable organizations is largely a self-reporting program. Organizations are expected to notify the county when significant changes occur. Our testing indicates that this self-reporting has not been sufficient to ensure that all property that should be included on the tax rolls is included.

The department, in its supervisory and oversight role, has not taken adequate measures to ensure that appropriate

policies and procedures are developed and implemented at the county level to provide for equality and uniformity in granting fraternal and charitable property tax exemptions. Although the department has an exemption manual, it does not provide guidelines on:

- How to document and verify that all requirements are met for each exempt account;
- The need for documenting the approval of an exempt account in writing;
- Reporting and information-gathering standards for the department's annual property tax statistics report; and
- Definitions and procedures for approving the four types of exempt institutions under ORS 307.130: literary, benevolent, charitable, and scientific.

Between 1995 and 1997, the department provided one comprehensive training class that included training on exemptions. Only 14 of the 36 counties were represented at the 1996 training session. Most of the counties we interviewed indicated that the main interaction with the department in this area is through self-initiated phone calls to the department requesting assistance in handling individual accounts. One county noted that in the past the department circulated pertinent information, such as examples of court cases, opinions, and orders. This county, however, indicated that the information is not provided as frequently as it was in the past.

The statutes do not require periodic review of the exempt organization's current status. Therefore, an application that was submitted and approved many years ago is still considered active and valid today. We found information in one exempt file dating back to 1883. If organizations were periodically reminded of the requirement to reapply when there is a change in ownership or use of the property or were required to reapply for property tax exemptions on a periodic basis, the information in the county files would be more current and complete. This would also provide county staff with information that would allow them to periodically review and reassess the exempt status of these organizations.

In the past six to 10 years, significant cutbacks in staffing have occurred both at the department and in the county offices. With these cutbacks came a prioritization of responsibilities. In talking with both department staff and county assessment and taxation staff, we found that a decision was made that the exemption program should have a very low priority. We found that most counties have less than the equivalent of a half-time employee assigned to this area.

RECOMMENDATIONS

We recommend the department develop and implement a system that best ensures that fraternal and charitable organization property tax exemptions are appropriately granted. Specifically, we recommend that the department do the following:

1. Work with county assessors to establish and implement policies and procedures that will better ensure that only appropriate exemptions are granted. These policies and procedures should include the following:
 - who will process the application and obtain additional information,
 - what information needs to be verified on the application,
 - what additional information is required,
 - how to verify and document the additional information,
 - who will be responsible for reviewing the account, and
 - how often the account will be reviewed.
2. Increase supervision and control over counties' granting of fraternal and charitable property tax exemption, where possible, to help ensure that exemptions are consistently granted according to applicable laws and regulations. To accomplish this, the department should establish a system of periodic reviews of county programs to provide training and feedback to county staff and to ensure that established policies and procedures are being followed.

3. Provide training to counties on a periodic basis. This training should include a review of the documentation required before an exemption can be granted and how to collect and review the information.
4. Consider introducing legislation that would require all organizations to periodically submit updated application materials so that the information in the county files remains current and so that county assessors have an opportunity to periodically review and reassess the appropriateness of exemptions.
5. Consider introducing legislation or drafting an administrative rule to clarify what constitutes a “change in use” of a property.

OTHER MATTERS

In the course of our audit work, we identified other issues related to enterprise zone, fraternal, and charitable exemptions that warrant the attention of both the Department of Revenue and the Oregon Legislative Assembly. These issues relate to whether the intent of the applicable statutes is being met, and whether the department has the authority or resources available to ensure compliance with all areas of these same statutes.

ENTERPRISE ZONE EXEMPTIONS

Exemptions Granted That May Not Meet the Intent of the Enterprise Zone Act

Our review found that the owners of millions of dollars' worth of property are being granted tax exemptions for property uses that may not meet the intent of the enterprise zone property tax exemption program. For example, the Legislative Assembly states, in ORS 285.573, that "the health, safety and welfare of the people of this state are dependent upon the continued encouragement, development, growth and expansion of employment, business, industry and commerce within the state, and that there are areas in the state that need the particular attention of government to help attract private business investment." They further state that it is "the purpose of ORS 285.560 to 285.620 [the Oregon Enterprise Zone Act of 1989] to stimulate employment, business and industrial growth...by providing assistance to businesses and industries and by providing tax incentives in those areas." Some enterprise zone property tax exemptions are being granted that may not meet the intent of this Act.

We reviewed 62 enterprise zone exemptions and found five exemptions granted to businesses who hired just one employee. In addition, 13 exemptions were granted to businesses where employment was increased by five or fewer employees, and another 12 exemptions where employment increased by 10 or fewer. For 1995-96, these 30 properties were valued at \$12,574,686.

In one case, a firm received an exemption although it admitted it closed or curtailed operations in another county more than 30 miles from the enterprise zone in which it made the request for exemption. Although ORS 285.600(4) indicates that this would constitute disqualification for exemption if employment in the area that operations were moved from was substantially diminished, the statute does not clearly define diminished employment. Consequently, the department has defined “diminished employment” in such a manner that it would be nearly impossible for a firm to be disqualified based on this criteria. For 1995-96, this property was valued at \$3,989,430.

In three cases, exemptions were granted to firms that did not increase employment or that decreased overall employment. For example, one firm entered into an agreement in 1989 that allowed it to receive an exemption even though the firm would decrease employment. It was the position of the firm that without the agreement and exemption on necessary investments, the firm was in danger of closing and therefore impacting the overall economic stability of the community. This threat was eliminated just after the ordinance was passed. Subsequently, the firm received exemption on millions of dollars’ worth of property over a period of six years, while decreasing overall employment. The 1995-96 value of exempt property for this firm was \$12,550,710.

The Enterprise Zone Act was ultimately revised to allow a firm that makes an investment of \$25 million or more to receive an exemption on that property without an increase in employment, and at times with a decrease in employment. Another firm, a well-established business in Oregon, received property tax exemptions in this manner. The 1995-96 value of enterprise zone exempt property for this firm was \$69,324,880.

**Exemptions Granted Because
of Misinformation Provided
by Other Agency**

In some cases, exemptions that would not meet statutory requirements were granted or precertification requirements were waived based on promises or inappropriate information presented to enterprise zone applicants by state and local economic development staff.

One county representative indicated that there was a problem with a past zone manager making promises to firms and giving them inadequate or inaccurate information that resulted in problems with granting the exemptions. In another county, a firm submitted an application for exemption more than three months after the filing deadline. The application was denied by the assessor's office and subsequently appealed by the firm. The zone manager supported the firm's appeal, indicating that he was guilty of providing misinformation to the firm. Ultimately, the appeal was decided in the firm's favor based on this misinformation provided by the zone manager.

Requirements Placed on Department May Be Impossible to Complete

In addition to the above concerns, we found that some requirements placed on the department under the administration of this program may be impossible to complete. For example, business firms must be in compliance with local, state, and federal laws when applying for exemption. It is beyond the ability of the department and local tax assessors to have knowledge of all laws that pertain to each business in order to determine that the business is indeed in compliance, and yet it is a statutory requirement for enterprise zone exemptions.

Other requirements, though not impossible, would require increased staffing levels at both the department and local county assessor's offices for effective administration.

- Ongoing monitoring of employment levels at enterprise zone businesses goes beyond the normal scope of the department or county assessor responsibility, yet it is a requirement for appropriate exemption of an applicant. Verification could be made through cooperation with other state agencies. For the most part, however, these other agencies, such as the Employment Department, will not provide or confirm the applicable information when requested.
- Verification that 75 percent of an enterprise zone business's annual gross receipts within the applicable enterprise zone are received from eligible activities goes beyond the normal scope of the department or

county assessor responsibility, yet it is a requirement for appropriate exemption of an applicant.

FRATERNAL AND CHARITABLE ORGANIZATION EXEMPTIONS

Degree of Charitable Activity Being Questioned

As we reviewed the 92 exempt fraternal and charitable property accounts in our sample, we noted that these exemptions were being granted to organizations for a variety of activities. Though these exemptions may be allowed under statute, the purpose and activities of the organizations receiving the exemptions and how the properties are being used by the organizations may not be what was intended by the program. The following items describe a sample of the organizations and types of activities that are currently being exempted as charitable:

- An organization whose purpose is to promote education about the nature of consciousness. The sampled property account is a residential home in the Portland area. It is exempted as the organization's office.
- An organization is receiving a 100 percent exemption on its property that is currently being used as a museum. This museum is open three days a week only when there is a traveling display. Traveling displays last only a couple of months and are available to the museum three to four times a year. The display at the time of our review was an exhibit of recycled materials that have been turned into rugs. There is no regular display.
- Another organization is receiving an exemption for operating a museum. This museum is open to the public for four hours once a month by appointment. The organization estimates it has five to six visitors each month.

- An organization is receiving a charitable exemption for operating a wilderness summer camp program. Activities of the program include hiking, gardening, camping, botanical studies, and wilderness preservation studies. Participants in this program are limited to those interested in the religious teachings of the organization.
- A private college is receiving a charitable exemption on its property, including the property account that we sampled, which is being used as a storage location for grounds maintenance material and a grounds material recycling depot.
- An organization operates a long-term care facility and provides assisted living for aged and frail people. The applicants for permanent admission must be of a specified nationality.
- An organization is receiving an exemption for a lodge at Mount Hood where members learn the skills of snow camping, inner tubing, snowshoeing, and cross-country skiing. Use of the lodge is limited to members of the organization, and the lodge is not operated for public benefit.
- An organization is receiving an exemption for a house that contains literature on Russian subjects and an area dedicated for prayer. The director of the organization resides on the property.
- A hospital is receiving an exemption on most of its property, including the property account in our sample, which appears to be used as a lounge related to the hospital's facilities. The facilities include a racquetball court, exercise room, and swimming pool.

**Property Tax Exemptions
for Hospitals Are Being
Challenged**

The charitable property tax exemption granted to hospitals is currently being challenged in Multnomah County. Multnomah County's legal counsel is currently deciding whether to approve property tax exemptions for hospitals currently under review. The basis for the legal petition is that four nonprofit hospitals in the Portland

area were granted property tax exemptions as charitable organizations and they may not possess the degree of charitable giving sufficient to qualify for property tax exemption. Multnomah County does not expect a final decision on this issue for two years or so because of anticipated appeals.

The purpose for which a hospital operates today may be different from the purpose it had when it was first organized. As stated in a letter from an attorney to the director of the Multnomah County Division of Assessment and Taxation dated October 13, 1995, "...hospitals are business operations providing a venue for the medical profession to practice its trade, managed by professionals whose role it is to ensure that revenues exceed expenses. Whatever reasons may have justified tax exemptions for the hospitals when they were first organized have long since evaporated. The hospitals can no longer justify their exemptions from either a statistical or a social policy standpoint."

Our random sample included 13 hospital properties statewide having a total property value of \$9,425,680. The properties are owned by the following hospitals: Sisters of Providence in Oregon, Portland Adventist Medical Center, Legacy Emanuel Hospital and Health Center, PeaceHealth d.b.a. Peace Harbor Hospital, PeaceHealth d.b.a. Western Lane Hospital, PeaceHealth d.b.a. Sacred Heart Hospital, Cottage Grove Hospital, Rogue Valley Medical Center, Providence Medford Medical Center, Salem Hospital, and Albany General Hospital. One of these hospitals reported a total revenue of approximately \$164,620,000 for fiscal year 1996. Its direct charity care write-offs for the same period was approximately \$2,106,000, roughly one percent of the total revenue.

Because of decisions pending in Multnomah County, we did not determine the appropriateness of the charitable exemptions granted to the above organizations. We did find, however, that the county assessor is granting exemptions to these organizations without sufficient evidence to determine that they are charitable.

**List of Fraternal Organizations
Should Be Revisited**

The statute defining a fraternal organization lists the following specific organizations that are considered fraternal:

- Masons;
- Knights of Pythias;
- Knights of Columbus;
- Benevolent and Protective Order of Elks;
- Fraternal Order of Eagles;
- Loyal Order of the Moose;
- Independent Order of the Odd Fellows;
- Oregon State Grange;
- American Legion; and
- Veterans of Foreign Wars.

The grand and subordinate lodges of those organizations are exempt from property tax by statute and are therefore not required to engage in activities that benefit nonmembers. For the fraternal organizations exempt by statute that were selected in our sample, we attempted to review information regarding their charitable activities. Though most of the fraternal organizations were able to note some charitable activities, the extent of these activities was unclear. For example, a subordinate lodge of one organization submitted information to us indicating that the organization has limited charitable activities. According to the organization's 1996 check register, only \$23 went to charitable purposes for the entire year.

**Government Funded
Organizations**

Government funded organizations are being exempted as charitable organizations when in fact they have no evidence of charitable work being performed. Our audit found that counties are granting exemptions to organizations such as group homes for developmentally disabled citizens and other rehabilitation training facilities based on their not-for-profit 501-C filing with the federal government. We also found that the counties granted these exemptions because they believe these organizations are "relieving a burden" for the community at large. The statutes, however, specifically state that "relieving a burden" alone is not sufficient grounds to grant the

organization an exemption as a charitable organization. Statutes state that the organization must also perform a degree of charitable work.

Our audit sample included properties of several group homes for developmentally disabled citizens and other rehabilitation training facilities, schools, and universities. We found no evidence that these organizations are performing charitable work. Although these organizations have nonprofit status with the federal government, and they may be “relieving a burden” for the government, their exemption as a charitable organization is questionable.

Definitions

ORS 307.130 is specific to property owned or being purchased by incorporated literary, benevolent, charitable, and scientific institutions, and ORS 307.140 is specific to religious organizations. The statutes, however, do not define the terms literary, benevolent, charitable, and scientific institutions or religious organizations. The department has provided definitions only for some of these types of organizations.

Organizations applying for exemption may not know the appropriate type of exemption for which they qualify. We found that counties are classifying as charitable organizations some organizations applying for exemption as religious organizations. When we examined documentation for one organization, it was questionable that the organization would qualify for exemption as either a charitable or a religious organization. Further, the county granted the exemption as a charitable organization without determining the degree of charitableness of the organization.

Partial vs. Full Exemptions

Our audit found that counties are not consistent in granting fraternal and charitable organizations exemptions for only that portion of a property actually used for charitable work. We found one organization that received a full exemption for a residential property used as a research center even though the owner also resided at the residence. Another organization received only a partial exemption for property it owns.

RECOMMENDATION

We recommend that the Legislature consider the above concerns and conduct a review of the applicable statutes to ensure that the administration of the program is appropriately designed to allow the granting of only those exemptions that meet the intent of the Legislative Assembly. In addition, the department should review administrative rules to ensure that the intent of the Legislative Assembly is being carried out and only appropriate exemptions are being granted.

REPORT DISTRIBUTION

This report is public record and is intended for the information of the Oregon Department of Revenue management, the governor of the state of Oregon, the Oregon Legislative Assembly, and all other interested parties.

COMMENDATION

The courtesies and cooperation extended by the officials and employees of the Oregon Department of Revenue and the county assessor's offices during the course of our audit were very commendable and sincerely appreciated.

AUDIT TEAM

Cathy Pollino, Deputy Director
Margaret Kane, CPA
Marlene Hartinger
Cora Bristow
Ann Takamura
Pam Stroebel

APPENDIX A

AUDIT SCOPE AND METHODOLOGY

We determined that the audit period would be the tax year from July 1, 1995, through June 30, 1996. This was the most recent period for which exemption data from the counties was compiled.

According to information provided in the department's *Oregon Property Tax Statistics: Fiscal Year 1995-96*, "Summary of Exempt Value of Fully and Partially Exempt Property, FY 1995-96, Table C.1," during our audit period 80 percent of the total property values exempted statewide, excluding public exemptions, fell in eight counties: Multnomah (37%), Washington (12%), Lane (11%), Clackamas (10%), Jackson (3%), Marion (3%), Benton (2.6%), and Linn (2.4%). We decided to limit our audit to these eight counties. (This was later modified for enterprise zone exemptions as the data in Table C.1 did not include all the exemptions for our audit period. See the sample selection methodology for enterprise zone exemptions below.)

In Table C.1, exemptions are categorized into public exemptions, social welfare exemptions, or business/housing/miscellaneous exemptions. Within the social welfare exemptions are fraternal organizations, literary/charitable organizations, religious organizations, burial grounds, and all other social welfare exemptions. Within the business/housing/miscellaneous exemptions are veterans exemptions, historic property, enterprise zones, commercial under construction, and all other business/housing exemptions.

After reviewing the *Oregon Revised Statutes* requirements for each of these exemption groups, we determined only the following exemption types had sufficient criteria against which we could apply specific audit procedures to accomplish our objectives: fraternal organizations; literary, charitable, benevolent, and scientific organizations; and enterprise zone exemptions.

SAMPLE SELECTION METHODOLOGY

In order to select a statistically sound and defensible random sample for testing, the following sample selection methodology was used.

Enterprise Zone Exemptions

The Department of Revenue's *1995 Enterprise Zone Tax Exemption Data* report identified 157 enterprise zone exemptions in 18 counties statewide for the period July 1, 1995, through June 30, 1996.³ The 157 exemptions had an exempted value of \$318,144,331. Using the *Statistical Sampling Program for Auditing and Accounting* developed by Herbert Arkin, Berard M. Baruch College, and Ronald C. Arkin, University of Massachusetts, we determined that the appropriate sample size was 60 exemptions:

Population size:	157 exemptions
Confidence Coefficient	90% (1.645)
Desired Precision	5%
Expected Rate of Occurrence	10%
Minimum Sample Size	60 (approx. 38% of 157)

Using a random number table, we identified the first 60 numbers corresponding to our parameters of 1 through 157. In the case of duplicates, replacement was as follows: the second number (or duplicate) was replaced by the next number from the table; an additional number was identified from the point where the first 60 numbers ended; and this number was added to the bottom of the list. This system was repeated until all 60 exemptions were selected only once. The exemptions selected for testing were in 17 counties. The exempted value of the 60 exemptions is \$138,588,832 (approximately 44 percent of the total exempted dollars).

During testing, we found that two of the exemptions reported in the department's report were actually multiple exemptions for the business firm. We tested each

³ Exemption data in the department's *Oregon Property Tax Statistics, Fiscal Year 1995-96*, Table C.4 indicates 131 exemptions.

exemption individually. In all, we tested 62 exemptions; the total exempted value did not change.

Fraternal and Charitable Exemptions

The department's Oregon Property Tax Statistics: Fiscal Year 1995-96, "Exempt Value of Social Welfare Exemptions for Fiscal Year 1995-96" identified 2,673 fraternal and charitable organization (FCO) exemptions granted in the eight counties: Multnomah, Washington, Lane, Clackamas, Jackson, Marion, Benton, and Linn. The department compiles this number from annual reports submitted by counties to the department each December. When we requested the detailed documentation from the county to support the department's summary numbers, the counties, except for Lane County, indicated that the detailed information did not exist to support the reported numbers. (Note: the department does not require supporting documentation be submitted with reports from counties.) Several counties stated that because they have an "on-line" system in which updated information continuously replaces historical data, past detailed data are unavailable. These counties also noted that the reports are created using summary data. Because the detailed information supporting the numbers reported was not available, we requested that the counties provide us with the best information available. Six of the eight counties' data included some exemptions granted after our audit period. Also, exemptions that were active during the audit period but removed between June 30, 1996, and the time the information was collected for our sample were not included in the information provided by the counties.

Using the county data, we identified and compiled a list of 2,540 fraternal and charitable organization exemptions with an exempted value of \$1,558,333,612. (Note: The dollar value identified here is not the real market value of the property. The department stated to us, and it was confirmed by several counties, that the counties are not to expend resources on these exemptions. Therefore, in some cases, reappraisals have not been completed once every six years as required by statute. In Washington County, due to past computer problems, only the most recent exemptions show a property value other than zero on the system. Because our report is not on valuation, this issue was not addressed unless the account was

selected for testing in our audit.) County data was sorted from the highest dollar percentage county to the smallest dollar percentage county, in account, or map and tax lot, order within the county.

Using the *Statistical Sampling Program for Auditing and Accounting*, we determined that the appropriate sample size was 92 exemptions:

Population size:	2,540 exemptions
Confidence Coefficient	90% (1.645)
Desired Precision	5%
Expected Rate of Occurrence	10%
Minimum Sample Size	92 (approx. 4% of 2,540)

Using a random number table, we identified the first 92 numbers corresponding to our parameters of 1 through 2,540. The exemptions selected for testing were in seven counties. The exempted value of the 92 exemptions is \$36,689,400 (approximately 2 percent of the total exempted dollars).

During testing, we found that four exemptions selected for testing did not occur during our audit period. We removed these items from our sample and replaced them with the next exemption account on the list that was applicable to our audit period. We also noted that some exemptions were miscoded as fraternal or charitable exemptions when they were actually other types of exemption. We removed these exemptions from our sample and replaced them in the same manner as those that did not occur in our audit period. In all, we tested 92 exemptions.

APPENDIX B

SUMMARY OF TAX EXEMPT PROPERTIES Tax Year 1995-96

Type of Exemption	ORS	Number of Exemptions Reported Statewide	Value Reported (in thousands)
<u>Business/Housing/Misc.</u>			
Veterans Exemptions	307.250 – 307.300	33,403	\$266,682
Historic Property	358.475 – 358.565	1,667	312,566
Enterprise Zones	285.597	131	317,775
Commercial Under Construction	307.340	32	571,245
All Other Business/Housing	various	2,092	361,023
TOTAL BUSINESS/HOUSING		37,325	\$1,829,291
<u>Social Welfare Exemptions</u>			
Fraternal Organizations	307.136	1,412	\$262,742
Literary/Charitable	307.130	2,488	1,487,050
Religious Organizations	307.140	6,862	2,010,492
Burial Grounds	307.150	1,034	153,119
**Not Identified — see note below	**	209	111,300
All Other Social Welfare	various	988	302,487
TOTAL SOCIAL WELFARE		12,993	\$4,327,190
<u>Public Exemptions</u>			
Federal	307.040	21,694	\$7,893,053
State	307.090	11,873	2,469,060
County/City	307.090	30,060	3,674,448
School Districts	307.090	5,392	4,246,468
Other Municipal Corporations	307.090	5,550	1,228,579
TOTAL PUBLIC EXEMPTIONS		74,569	\$19,511,608
TOTAL PROPERTY EXEMPTIONS STATEWIDE		124,887	\$25,668,089

** The amount in the total column on the department's table for social welfare exemptions is a higher value than the detail presented in the columns. In comparing one county's information report to the Department of Revenue's table, we found that the values for other categories not specifically identified were included only in the total value reported.

Source: Department of Revenue,
Oregon Property Tax Statistics for Fiscal Year 1995-96,
Tables C.2, C.3, and C.4.

AGENCY'S RESPONSE TO THE AUDIT REPORT



Oregon

John A. Kitzhaber, M.D., Governor

Department of Revenue

955 Center St NE
Salem OR 97310-2501

March 13, 1998

**John Lattimer, Director
Audits Division
Office of Secretary of State
255 Capitol Street NE, Suite 500
Salem, OR 97310**

Dear John:

Enclosed is the Department of Revenue's response to the Property Tax Exemption audit. I am also providing a computer disk (Microsoft Word) containing the response.

Thank you for the courtesy you and your staff have shown us during the conduct and conclusion of this audit. I hope that we can use it to improve the property tax exemption statutes and administrative processes.

Please advise my assistant, Joan Linn, of the date the audit will be released. Her telephone number is 945-8215.

Sincerely,

**Elizabeth Harchenko
Director**

Encl.

RESPONSE TO AUDIT

During 1995-96, the value of assessed and exempt properties in the Oregon property tax system exceeded \$200 billion. This audit reviewed about 1% of the value in the system. The audit concludes that 7% of the value of exempt property that was examined by the auditors should not have been exempt from tax. In almost all of the cases, the non-profit charitable organization or enterprise zone business had missed a step in the application process, or had failed to file documents needed to maintain their exempt status from year to year.

Over the years, when taxpayers have missed procedural steps in qualifying for these exemptions the legislature has regularly rescued them. We agree with the audit recommendations that it is time to form groups of interested parties to propose a clearer statutory framework to the next legislature. A simpler process will better serve both taxpayers and the system.

The Secretary of State's audit conclusions are correct. Most non-profit charitable organizations and enterprise zone businesses missed filing a document or missed the time for filing a document though they met all of the substantive requirements to qualify for an exemption. A few properties failed to meet substantive use or property eligibility requirements. The county assessors and their staff process exemption applications and decide whether to grant them. At times, the quality of this process is limited by the resources available to the assessors. For its part, the Department will improve procedure and training to keep county staff educated on the necessary requirements for exemption filings.

More importantly, the Department will work in partnership with the county assessors to clarify and simplify the exemption process requirements in the next legislative session so that taxpayers who qualify for exemptions don't inadvertently miss a step that would cause them to lose those exemptions. Likewise, the Department will work with the Oregon Economic Development Department, zone managers, county assessors and businesses to propose improvements to the enterprise zone statutes so they do not create traps for businesses that invest millions of dollars and create jobs for Oregonians.

RESPONSE TO AUDIT RECOMMENDATIONS

ENTERPRISE ZONE EXEMPTIONS

Recommendations: “We recommend the department develop and implement a system That best ensures that enterprise zone property tax exemptions throughout the state are appropriately granted. Specifically, we recommend that the department do the following:

1 Work with county assessors to develop and implement policies and procedures for counties to follow when processing enterprise zone exemption applications. The department should consider including policies and procedures that address the following issues:

- Precertification review;
- Verification of the 75 percent gross receipts test;
Verification of hiring and employment requirements;
Development of appraisal procedures for both real and personal enterprise zone property;
- Verification of compliance with property qualifications;
- Verification of information contained in the annual statement of compliance;
Verification of compliance with extended abatement criteria;
and
- Development of standards for annual enterprise zone data reported to the department for inclusion in its report to OEDD.

In addition, the department should establish policies and procedures for its own staff to follow related to:

- The review and supervisory control of enterprise zone precertification and exemption materials;
- The granting of precertification waivers, including both circumstances deemed eligible for a waiver and the appropriate time period during which a waiver should be granted;
- Appraisal procedures for real and personal enterprise zone property; and
- Reporting and information gathering standards for annual enterprise zone data reported to OEDD.”

Response	<p>The department’s work with county assessors is ongoing, although our presence in county offices has been seriously reduced in recent years. We will actively pursue contacts during the next two years to determine the procedures that exist in each county. We will develop standard procedures for county assessment staff to use for the various portions of the enterprise zone program that apply to property value and qualifications.</p> <p>The department will refine its internal policies and procedures as part of the regular rules and policy processes. We will emphasize those areas specifically addressed by this audit.</p>
Recommendation	<p>“2. Increase supervision and control over counties’ granting of enterprise zone property tax exemptions, where possible, to help ensure that exemptions are consistently granted according to applicable laws and regulations. To accomplish this, the department should establish a system of periodic reviews of county programs to provide training and feedback to county staff and to ensure that established policies and procedures are being followed.”</p>
Response	<p>The department’s two-year work plan for enterprise zones will increase the department’s presence in county offices to review program activities and make recommendations for corrective action or program enhancement.</p>
Recommendation	<p>“Increase its efforts to provide enterprise zone exemption training to the county assessors’ offices. As a part of this training, the department should include the enterprise zone exemption program in the exemption manual published by the department, and recommence distribution of pertinent information to the counties to aid them in making exemption decisions.”</p>
Response	<p>The department will increase its training efforts, coordinated with Oregon Economic Development Department staff as available. We will include the enterprise zone exemption program in the manual.</p>
Recommendation	<p>“In consultation with the Oregon Economic Development Department and other pertinent parties, introduce legislation to clarify enterprise zone exemption statutes so that (a) it is clear what requirements an organization must meet to qualify for exemption and (b) it is clear who is responsible for ensuring that the requirements are met.”</p>

Response The Department is already coordinating with OEDD to chose assessors, zone managers, companies, Oregon Economic Development Department staff and Department of Revenue staff to participate in a group that will create a legislative bill to streamline this exemption program.

FRATERNAL AND CHARITABLE EXEMPTIONS

Recommendation “We recommend the department develop and implement a system that best ensures that fraternal and charitable organization property tax exemptions are appropriately granted. Specifically, we recommend that the department do the following:

1. Work with county assessors to establish and implement policies and procedures that will better ensure that only appropriate exemptions are granted. These policies and procedures should include the following:
 - who will process the application and obtain additional information,
 - what information needs to be verified on the application,
 - what additional information is required,
 - how to verify and document the additional information,
 - who will be responsible for reviewing the account, and how often the account will be reviewed.”

Response We will work with the county assessors to implement policies and procedures that identify the necessary steps in the review process.

Recommendation 2. “Increase supervision and control over counties’ granting of fraternal and charitable property tax exemption, where possible, to help ensure that exemptions are consistently granted according to applicable laws and regulations. To accomplish this, the department should establish a system of periodic reviews of county programs to provide training and feedback to county staff and to ensure that established policies and procedures are being followed.”

Response The department will be regularly reviewing county programs to identify problems that require feedback for correction and statewide training for consistent application of the laws.

Recommendation	3. “Provide training to counties on a periodic basis. This training should include a review of the documentation required before an exemption can be granted and how to collect and review the information.”
Response	The Department will increase its training in this area to clarify the needed review and collection of information for these exemption applications.
Recommendation	“4. Consider introducing legislation that would require all organizations to periodically submit updated application materials so that the information in the county files remains current and so that county assessors have an opportunity to periodically review and reassess the appropriateness of exemptions.”
Response	The Department has already begun identifying assessors and representatives of charitable organizations to participate in a group that will create a legislative bill to improve the exemption process and ensure that the assessor has current information about the organization’s property and its use.
Recommendation	“5. Consider introducing legislation or drafting an administrative rule to clarify what constitutes a ‘change in use’ of a property.
Response	The group the Department is convening will address the issue of “change in use”.

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