



CITY OF RICHMOND

Office of the City Auditor

DATE: April 2, 2024

TO: Mr. Lincoln Saunders
Chief Administrative Officer

FROM: Riad Ali
City Auditor

SUBJECT: Non-Audit Services: Meals Tax Delinquent Notifications

The City Auditor's Office reviewed the delinquent meals tax account notification process from July 12, 2022, through February 13, 2024. The review was requested by the City Council and is based on unaudited data from the Department of Finance.

In agreement with management, we performed the following tasks:

- Quantified the number and dollar amount of current delinquent meals tax accounts; and
- Determined if the account holders received partial payment letters informing them of the delinquency since implementing the partial payment letter process.

We attempted to quantify the number and dollar amount of current delinquent personal property tax accounts and determine if the Department of Finance sent the account holders delinquent notifications since the implementation of RVAPay. However, the personal property tax billings have not been processed through RVAPay yet, so this analysis cannot be performed at this time.

This document provides a summary of the delinquent meals tax information. This review was completed as a non-audit service and does not constitute an audit conducted under Generally Accepted Government Auditing Standards (GAGAS). A full audit conducted under GAGAS is planned to be initiated once RVAPay is implemented for the meals tax program. We want to thank the Department of Finance for their assistance and cooperation. Please contact us if you have any questions regarding this information.

cc: The Richmond Audit Committee
The Richmond City Council
Ms. Sabrina Joy-Hogg, DCAO Finance and Administration
Ms. Sheila White, Director of Finance

Background

Meals tax is a self-reported consumer (trust) tax paid for prepared foods and beverages. The City's meals tax rate is 7.5%, which became effective July 1, 2018. Establishments that sell prepared foods must collect and remit meals taxes to the City by the 20th of each month. Taxes are due on the next business day if the 20th falls on a weekend or City holiday. Returns must be filed even if taxes are not due. Establishments are awarded a 3% seller's commission for collecting, reporting, and remitting taxes in full by the due date. The City collected approximately \$52 million in meals taxes in Fiscal Year (FY) 2023, representing nearly 8% of the general government tax revenues.

For the period reviewed, the Department of Finance, in accordance with Virginia Code 58.1-3913, posted tax payments to the most delinquent account first. As such, if an establishment remitted meals taxes for the current month but had an outstanding balance, Finance first posted the payment to the outstanding balance. If the remitted payment was insufficient to cover the delinquent amount and the current month, the current month would become delinquent, accrue a penalty and interest, and the seller's commission cannot be taken. This delinquency pattern would continue until the establishment resolved the outstanding balance.

Also, in the period reviewed, a ten percent (10%) one-time penalty and simple interest at a rate of 10% annually were applied to meals tax accounts for remitting taxes after the due date. Failure to file and remit the meals taxes is a Class 1 Misdemeanor, punishable by up to one year in prison and/or a \$2,500 fine. It may also result in a criminal summons, business license denial, and delinquent collection efforts, including tax liens.

Delinquency Notification

The Department of Finance implemented a process to communicate outstanding account balances to businesses in June 2022. Partial payment letters were mailed to businesses that remit insufficient payments to cover account balances. The first batch of letters was mailed in July 2022, confirming receipt of payments and indicating

outstanding balances. Before this, business owners were only notified about their outstanding balances if they inquired or if tax audit, enforcement, or delinquent collection efforts were initiated. As a result, some businesses were unaware of their outstanding balances, incurring penalties, fees, and accruing interest.

The partial payment letter does not provide a detailed breakdown of the total amount due. Also, the reported account balances are not net of any account credits. The Department of Finance stopped including the account balances in the letters starting mid-June 2023.

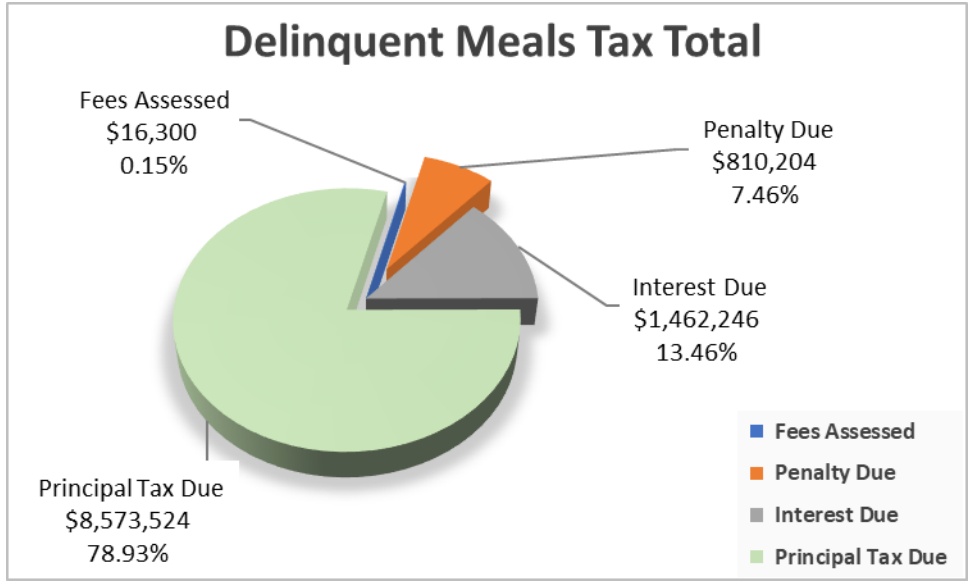
Methodology

- Obtained a listing of meals tax billings as of the report run date of February 27, 2024, and calculated the amount due for each bill. The auditor summarized the bills by property identification number to quantify the total delinquent amount per account.
- Obtained Partial Payment Letter files and supporting documentation from the Department of Finance. The individual letter files were combined into a single document and compared to the delinquent meals tax accounts to identify which businesses received partial payment letters between July 2022 and February 2024.
- Reviewed the partial payment letter files and supporting documentation to identify potential explanations for why letters were not issued to some of the businesses.

Results

As of February 27, 2024, there were **673** delinquent meals tax accounts totaling approximately \$10.9 million.¹ The following chart shows the delinquent total by principal tax, interest, penalty, and fees.

¹ The total includes delinquent accounts with balances of \geq \$5 net of account credits and still in statute (billing years 2019 – 2024).



Source: Prepared by Auditor using tax data provided by the Department of Finance through 2/27/2024

As seen in the chart above, the majority of delinquent amounts are made up of the principal tax due while penalty, interest, and fees represent approximately 21% of the total delinquent amount. The table below shows the businesses with the highest amount due, including penalty and interest as of February 27, 2024:

Business	Principal Tax Due	Penalty Due	Interest Due	Total Amt Due
A	\$ 189,867	\$ 18,756	\$ 59,292	\$ 267,915
B	\$ 171,010	\$ 17,101	\$ 61,144	\$ 249,255
C	\$ 176,261	\$ 17,519	\$ 23,591	\$ 217,370
D	\$ 162,692	\$ 15,496	\$ 3,025	\$ 181,213
E	\$ 154,554	\$15,455	\$ 6,172	\$ 176,182

Source: Prepared by Auditor using tax data provided by the Department of Finance

As of February 13, 2024, **390** (58%) delinquent accounts, totaling approximately \$7 million, received at least one partial payment letter. The remaining **283** (42%) accounts, totaling approximately \$3.9 million, did not receive a letter. Of note, **98** of these

accounts were excluded from the partial payment letter process due to at least one of the following:

- Bankruptcy
- Payment plan
- Account under review
- Payment allocation
- Business did not make a payment.

In addition to the partial payment letters, delinquent account holders may have been notified through the delinquent collections or tax enforcement processes. Analyzing these processes is beyond the scope of this request.

The City's Commitment

Richmond restaurant owners have come forward to share their experiences and the impact that recent meals tax collections have had on their businesses and lives. In response, the City Council and City Administration have taken the below actions to address the ongoing concerns and improve the collection and application of meals tax payments.

Changes Made

As part of this review, the City Auditor's Office verified that the City has begun to institute the following changes:

- On February 12, 2024, the City Council adopted Ordinance 2024-024 to modify the application of tax payments. The Department of Finance will now apply tax payments to the current tax period for the tax type paid instead of the most delinquent account. Any excess funds from payments will be applied to the oldest delinquent local account after the current liability is paid.
- On February 26, 2024, the City Administration announced that the Department of Finance's Payment Allocation Review Committee is reviewing meals tax accounts with outstanding balances as of March 1, 2024. The businesses will be

notified via mail. A penalty and interest freeze were placed on the accounts under review to prevent the businesses from incurring additional costs during the review process. The Department of Finance aims to complete and communicate the review results by July 1, 2024.

- The City introduced the following measures to facilitate collaboration with businesses:
 - A secure website for businesses to submit appeal forms.
 - A dedicated email address so businesses can communicate concerns about the Meals Tax to the Department of Finance.
 - A Payment Allocation Review Committee charged with the task of manually evaluating cases.
 - As of February 28, 2024, hours for the City Hall Finance Office (1st floor) were changed to allow more time to review cases. The City Hall Finance Office closes on Wednesdays at noon.

- The Department of Finance held a career fair on March 7, 2024, to recruit and hire individuals to fill the Department's vacant positions. Per City Administration, conditional offers were extended for 23 open vacancies.

Ongoing Efforts

As part of this review, management informed the City Auditor's Office of the following ongoing initiatives and commitments:

- Per the Director of Finance, businesses were notified that their meals tax accounts are being reviewed and formal notification letters were issued on March 22, 2024.

- The City is organizing a series of Business Cafés to provide real-time assistance and answer questions from business owners regarding their immediate concerns.

- The City hosted a BizConnect Expo on March 11, 2024, that allowed businesses to connect with various City departments and local and regional business support partners.
- Implement RVA Pay, an automated payment system that allows businesses and residents to view accounts, make payments, and access real-time billing information. City Administration adjusted the module implementation schedule to prioritize on the business module to address the businesses' concerns. Per the Director of Finance, a Business Advisory Council will advise the City on the build-out of the RVA Pay system.

Recommendations

The City Auditor's Office will not issue any additional recommendations as the City is already committed to the process of informing delinquent account holders of their outstanding balance. As requested by City Council, City Administration, and the Director of Finance, the City Auditor's Office will audit the meals tax program after RVAPay is implemented.