

Office of
LEGISLATIVE AUDITOR GENERAL
State of Utah

REPORT NUMBER 2002-07

November 2002

**A Performance Audit
of Collecting
Transportation-related Revenue**



The Tax Commission collects multiple fees and taxes which are sent as revenue to the state Transportation Fund. Our audit of these revenues had two objectives: (1) to validate the reported cost of collecting these transportation-related fees and taxes; and, (2) to examine options for recovering the collection costs. The Legislature faces a policy decision of how to recover these collection costs. This audit presents some viable options for funding the Tax Commission's expenses for transportation-related revenue collections:

- **New Revenues** — Collect new revenues generated by raising vehicle registration and title fees (comparable to other states), with the increase being retained by DMV and dedicated to cost recovery, or
- **Transportation Fund Revenues** — Continue to fund the costs with increased allocations from the Transportation Fund, as implied in existing law, or
- **General Fund Revenues** — Use an increase of General Fund appropriations to fund costs, based on historical precedent of the past 10 years.

For FY 2003, DMV funding was cut from the General Fund. It was later restored with one-time funds. As a result, DMV has a shortfall of between \$3.7 and \$4 million for FY 2004.

During the Fifth Special Session of 2002, the fiscal year 2003 General Fund appropriation to the Tax Commission was cut back and the Division of Motor Vehicles' (DMV's) budget was reduced by \$5 million. In that

same special session of 2002, the Legislature restored the \$5 million of funding to the Tax Commission with a one-time appropriation of \$4 million from the General Fund and an ongoing appropriation of \$1 million from the Transportation Fund. But, this left a potential ongoing funding shortfall of \$4 million for fiscal year 2004.

Facing a fiscal year 2004 budget reduction this large, Tax Commission executives said that the DMV would not be able to operate as currently configured; it would not be able to offer the same level of motor vehicle services statewide and some DMV offices would be closed. If offices were closed, **Utah Code** gives the counties the option to perform DMV functions, but the state would have to reimburse the counties. So, closing offices would not fully resolve the issue of the budget shortfall.

We reviewed the total applicable collection costs for fiscal year 2002 and deducted the dedicated credits (a portion of the fees retained to offset collection costs) to come up with the net collection costs. Assuming that collection costs will be the same or greater for fiscal year 2003, and deducting the Transportation Fund transfers of \$5.8 million, an adjusted funding shortfall of \$3.7 million exists. Figure 1 identifies this additional ongoing funding needed by the Tax Commission to collect the transportation-related fees and taxes.

At least \$3.7 million in ongoing funding is needed for FY 2004 to restore transportation-related collection programs.

Figure 1. Additional Ongoing Funding Needed to Collect Transportation-related Fees and Taxes. Due to a drop in General Funds, about \$3.7 million is needed to meet costs.

Explanation	Amount
FY 2002 Total Transportation Fund Related Collection Costs ¹ .	\$14,299,100
Less Funding from Dedicated Credits	<u>(4,757,200)</u>
Net Collection Costs	9,541,900
Less FY 2003 Transportation Fund Appropriation ² .	(5,857,400)
ADDITIONAL ONGOING FUNDING NEEDED	<u>\$3,684,500</u>

1. See Figure 2 for a breakdown of these costs by Tax Commission divisions.

2. During the Fifth Special Session of 2002, the ongoing Transportation Fund appropriation was increased from \$4.8 million to \$5.8 million for the Tax Commission.

Although the budget shortfall was actually restored with \$4 million of one-time funding, our review of costs shows conservatively that at least an additional \$3.7 million of revenue is needed on an ongoing basis to fund

the collection of transportation taxes. Figure 1 does not include the allocated portion of indirect administrative costs of nearly \$1.3 million which we recommend not be included as part of the total collection costs.

Direct Costs Were Reviewed

The DMV and several divisions within the Tax Commission contribute directly to the collection of transportation-related taxes and fees which are deposited into the Transportation Fund. As part of our assignment to review the recent funding shortfall, we conducted a limited review of the DMV budget and related costs from other divisions. We examined expenditures for fiscal year 2002 and verified that the costs listed are directly related to the collection of revenues that feed the Transportation Fund. However, we did not attempt to evaluate the efficiency of revenue collection processes. These costs, identified in Figure 2, were estimated to be about \$14.3 million for fiscal year 2002.

Our review shows the total direct costs of transportation-related fees and tax collection to be \$14.3 million.

Figure 2. Direct Costs of Collecting Transportation-related Fees and Taxes at the Utah State Tax Commission’s Divisions.

Tax Commission Division	Direct Costs
Administration (accounting)	\$ 159,600
Auditing	563,200
Technology Management	2,001,200
Processing	929,100
Taxpayer Services (customer service and delinquent collections)	123,600
Property Tax	0
Motor Vehicle Enforcement Division	0
Division of Motor Vehicles (transportation-related)	10,522,400
TOTAL	<u>\$ 14,299,100</u>

Figure 2 also shows that DMV accounts for about \$10.5 million, more than 73 percent, of the total costs associated with the Transportation Fund. The remaining \$3.8 million are costs associated with the collection of fuel taxes and services supporting DMV and fuel tax operations.

The Tax Commission collects revenues totaling \$554.2 million associated with the Transportation Fund and other DMV collections, according to fiscal year 2001 data provided by the Tax Commission. These revenues consist of \$53.9 million for the General Fund, \$388.2 million for the Transportation Fund, and \$112.1 million for the counties.

There are transactions performed by DMV that benefit other agencies which are not wholly related to the Transportation Fund. A significant function of DMV is not only to collect fees and taxes for the Transportation Fund, the counties, and the state General Fund, but also to register and license vehicles. The registration and licensing of vehicles clearly serves state and local public safety. Some users of the Transportation Fund believe that related collection costs should be divided more fairly among other agencies receiving benefits (for example law enforcement and counties).

However, in 1994 our office did a detailed time and motion study which determined the amount the counties should pay DMV for services provided. County payments for DMV services are reported as part of the dedicated credits reflected in figures within this report. This study has been updated by DMV to account for cost-of-living increases and the new motor vehicle system and should be an accurate reflection of costs. Determining other related costs of registration and licensing that may benefit law enforcement would be difficult and beyond the scope of this audit.

Costs Are Difficult to Separate

The DMV's operational costs are a result of transactions associated with the collection of various taxes and the regulation and licensing of motor vehicles. Numerous transactions are performed at each of the DMV offices throughout the state. The majority of these transactions are vehicle registrations and/or title transfers. The registration and title transfer are separate transactions, but both transactions are completed by the same staff using different computer strokes.

DMV costs are further complicated because collections from each transaction go to different users. For example, the vehicle registration transaction is used to collect taxes and fees for the users of the Transportation Fund as well as county assessed fees. The title transfer is

Registration and title transactions are coupled with other fee collections making it difficult to separate costs.

Costs are difficult to separate because the DMV collects for entities other than Transportation.

used to collect fees for the Transportation Fund and sales taxes for both the state and the counties. Finally, fees and taxes collected by DMV for the Transportation Fund can be credited to as many as 12 different revenue accounts.

While collecting these taxes and fees, which benefit numerous users, DMV also issues vehicle registrations and titles which benefits local and state public safety and insurance companies. The determination of what costs belong to which agency is a judgment call and depends upon how one wants to assign cost. In our opinion, the assignment of DMV costs are best determined as a matter of policy by the Legislature.

Legislative Options Exist for Cost Recovery

The Legislature has options for recovering the currently-unfunded portion of collection costs of transportation-related fees and taxes at the Tax Commission. Traditionally, DMV and other division costs have been provided from the Transportation Fund, General Fund, and from dedicated credits. As mentioned, recent strains on the General Fund led to \$5 million from the General Fund being converted to \$4 million in one-time funds and a \$1 million increase to transportation fund transfers to the Tax Commission. This section of the report presents policy alternatives the Legislature can consider to meet the \$3.7 million funding shortfall for fiscal year 2004.

Figure 3 summarizes the three options we present, along with the corresponding affected entities.

There are options for funding the collection costs:

- Raise DMV fees comparable to other states' fees.
 - Increase Transportation Funds.
 - Increase General Funds.
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Figure 3. The Legislature has Options for Addressing the Unfunded \$3.7 Million Needed by the Tax Commission for Collecting Transportation-related Fees and Taxes.

Funding Option	Affected Entity
1. Raise select DMV fees, (comparable to other states' fees) to be dedicated to cost recovery.	Utah vehicle users
2. Increase ongoing funds from the Transportation Fund	Department of Transportation
3. Increase General Fund revenues	General Fund

In short, each of the three options has a viable argument. In Option 1, fees could be increased, which gives the Legislature the benefit of added revenue in the form of dedicated credits. In Option 2, it could be argued that the **Utah Constitution** and the **Utah Code** allow for cost recovery through the Transportation Fund. In Option 3, the Legislature has set historical precedence by relying on the General Fund more and more over the past ten years to pay the costs of collecting transportation-related fees and taxes.

There is a fourth approach which is not viable for the current situation—it is to split collection costs among the various benefactors of the Transportation Fund. We do not present this approach here because it would require more analysis than this limited-scope audit could provide. Essentially, costs of the program could be spread among the benefactors according to the percent of revenue received, or costs could be spread according to actual services rendered. The second approach would require a more detailed analysis. In our opinion, neither of these options of splitting collection cost among the benefactors of the Transportation Fund are as viable as the first three options presented in this report. Our primary concern is that splitting the collections costs will result in either the counties having to pay a disproportionate share based on revenues, or the necessary data needed to determine a fair split not being available for the 2004 General Session.

Cost Recovery Could Come From Increased DMV Fees

Additional revenues could be raised through a moderate increase in vehicle registration and title fees. Vehicle registration fees have not been increased since 1997 and title fees have not been increased since 1991.

Increasing vehicle registration fees and title fees would provide needed funding for cost recovery.

When compared to other western states, Utah’s fees for comparable vehicles are relatively low. There are so many variables affecting the fee amounts in other states that to look at fees in general would not be accurate. Consequently, we chose to review the actual fees for a sample of comparable vehicles.

Based on our fee comparisons, Utah’s vehicle registration fee could have a moderate increase and still be under the average registration fee for the surrounding states. For our comparison, we chose the most popular vehicles in the four major vehicle classes. We researched the fees for two different years so that each state had an average of eight vehicle scenarios. This comparison is summarized in Figure 4.

Utah vehicle registration fees are below the average of other western states.

Figure 4. Utah is Below the Average of Western States for Motor Vehicle Registration. The figures from other states are a compiled average of eight registration scenarios of four popular vehicles in the major vehicle categories (Passenger, SUV, Light Truck, Full-size Truck) for two years (2001 and 1996).

State	Average Fee
Arizona ¹	\$ 8.00
California	29.00
Idaho	36.00
Montana ²	18.75
Nevada	33.00
New Mexico	36.00
Oregon ³	15.00
Washington	33.75
Wyoming ⁴	<u>20.00</u>
Average of Other States	\$ 25.50
UTAH	21.00
Difference	\$ 4.50

1. Arizona’s registration fee is low because it is offset by an in-lieu fee—the “Vehicle Licensing Tax” collected as part of the registration fee.
2. Montana’s fee is lower than Utah but there are no fees in-lieu like Arizona.
3. Oregon has lower fees, but officials say they rely on a highway “wear and tear” fee (based on weight), which most states have abandoned, and also have a higher fuel tax relative to some western states.
4. Wyoming counties may be asking the Legislature for a \$3.00 per transaction fee, which could raise rates, according to one county treasurer’s office.

Utah's fee of \$21 is significantly lower than five of the nine western states. However, two of the four states with fees lower than Utah's have other related taxes that support the registration process. Also, one of the four states may be raising its fee this year, leaving only one state with a lower fee than Utah. The modest increase recommended in this report would still leave Utah's registration fee among the lowest of western states.

In addition to registration fees, a comparison of Utah's original title fee and duplicate title fee with that of other western states shows that Utah's fees are about \$4 lower than the average of surrounding states. This comparison, shown in Figure 5, suggests that fees for all titles could be increased.

Figure 5. Utah is Below the Average of Western States for Motor Vehicle Title and Duplicate Title Fees. Utah's original title fees are about \$4 under the average and duplicate title fees are about \$4.50 under the average of other states.

State	Original Title Fee	Duplicate Title Fee
Arizona	\$ 4.00	\$ 4.00
California	10.00	7.00
Colorado	6.50	7.50
Idaho	8.00	8.00
Montana	5.00	3.00
Nevada	20.00	20.00
New Mexico	4.50	15.00
Oregon	30.00	30.00
Washington	5.25	5.25
Wyoming	<u>6.00</u>	<u>6.00</u>
Average of Other States	\$ 9.93	\$ 10.58
UTAH	6.00	6.00
Difference	\$ 3.93	\$ 4.58

Fee Source: N.A.D.A. Title & Registration Text Book—The Title and Registration Book of the National Automobile Dealers Association, 2002

Based on higher fees in other western states, Utah's title fees could be increased.

Utah's original title fee of \$6 is the same or lower than six of ten western states. Also, Utah's duplicate title fee of \$6 is the same or lower than seven of ten western states. With a moderate recommended increase of \$1.50 for all types of titles, Utah's title fee would still be below four of the ten western states, and significantly below the average of ten western states.

Therefore, an increase of all title fees by \$1.50 (from \$6 to \$7.50) and an increase of vehicle registration by \$1.50 would provide the revenues needed to replace the General Fund reductions made during the Fifth Special Session of 2002.

We chose \$1.50 in each category to simplify the model and because it represents a moderate increase in both areas, rather than significant increases in either fees or titles. Under this option, the DMV would be able to continue operations without an increase to the General Fund or the Transportation Fund. Because the increase in fee amounts would be enacted to help pay for the costs of collection, the revenue from the increase should be a dedicated credit to DMV, as opposed to being sent to the Transportation Fund and then allocated back to the DMV.

Although numerous other fee increase options exist, for the purposes of this report, we offer the model shown in Figure 6 as an example.

Figure 6. The Legislature Could Increase Motor Vehicle Fees to Meet the \$3.7 Million Shortfall in the Division of Motor Vehicles. Our comparisons in Figures 4 and 5 show that Utah could moderately raise selected motor vehicle fees and still remain comparable to other western states. (Note: Fee increases are merely suggested amounts calculated to roughly meet the needed funding amount.)

The Tax Commission could raise \$3.9 million by increasing vehicle registration fees and title fees by \$1.50 each.

Fee Increase	Applicable Unit	Totals (Fee x Unit)
Motor Vehicle Registration	FY 2003 Estimated "On Highway" Vehicles	
\$1.50	1,946,020	\$2,919,030
All Types of Titles ¹	FY 2002 Actual Titles Issued (All Types) ¹	
\$1.50	662,831	994,247
Estimated Total New Revenue:		<u>\$ 3,913,277</u>

1. Includes original titles, duplicate titles, new lien titles and salvage titles.

Earlier we mentioned that we did not include an additional \$1.3 million of indirect overhead cost attributed to the cost of collecting transportation -related fees and taxes at the Tax Commission. However, if registration fees were raised by \$2.10 (instead of the \$1.50 shown in Figure 6) total new revenue would increase to \$5 million. This increase could fund the overhead costs currently being met with General Funds.

Cost Recovery Could Come From Increased Transportation Funds

According to legislative general counsel, **Utah Constitution**, Article XIII Section 13 provides that costs of collection and administration of the revenues going into the Transportation Fund may be taken from the Transportation Fund:

“The proceeds from the imposition of any license tax, registration fee, driver education tax, or other charge related to the operation of any motor vehicle upon any public highway in this State, and the proceeds from the imposition of any excise tax on gasoline or other liquid motor fuels used for propelling such vehicle, except for statutory refunds and adjustments allowed thereunder and *for costs of collection and administration*, shall be used exclusively for highway purposes . . . (emphasis added).”

The statutes also appear to provide support of the collection costs coming out of the Transportation Fund. **Utah Code 41-1a-1201(2)** states that “. . . all fees collected under this part [‘Part 12 Fee and Tax Requirements’] shall be deposited in the Transportation Fund.” Included in these deposited fees is motor vehicle registration and title fees. **Utah Code 41-1a-1201(5)** continues by stating that “. . . the expenses of the commission [Tax Commission] in enforcing and administering this part shall be provided for by legislative appropriation from the revenues of the Transportation Fund.”

Concerning transportation-related fuels, the Motor and Special Fuel Tax Act similarly provides that “. . . An appropriation from the Transportation Fund shall be made to the commission [Tax Commission] to cover expenses incurred in the administration and enforcement of the collection of the motor fuel tax, [the special fuel tax, and aviation fuel tax].” (See **Utah Code 59-13-201(5)(b)**, **59-13-301(7)(a)**, and **59-13-402(1)(b)**.)

Utah Constitution and statutes may infer that cost recovery should come through the Transportation Fund.

One aspect the Legislature may want to reconsider in connection with the Transportation Fund is something similar to the failed language from an early draft of Senate Bill 5003 presented in the 2002 Fifth Special Session. This language stated,

“An amount may be appropriated or transferred from the Transportation Fund to the State Tax Commission for collection costs not to exceed 2.5% of the total Transportation Fund Revenue collected by the State Tax Commission in the previous fiscal year.”

Legislation of this sort could recover costs from all of the component fees collected into the Transportation Fund. Currently, the transfer for cost recovery does not draw from many restricted accounts that were recently added to the Transportation Fund.

We called ten other western states for comparison and found a wide variety of funding models for motor vehicle services. Six of them rely on cost recovery from a transportation fund (or equivalent fund), or from retained collections. In Arizona, Oregon, and Washington—three of the six states—the registration fees are collected by the state motor vehicle agencies which are funded with transportation fund revenues. The other three of six states—California, Idaho, and Montana—fund their collections with retained portions of the registration fees, title fees, and other taxes collected, the remainder of which become state revenues.

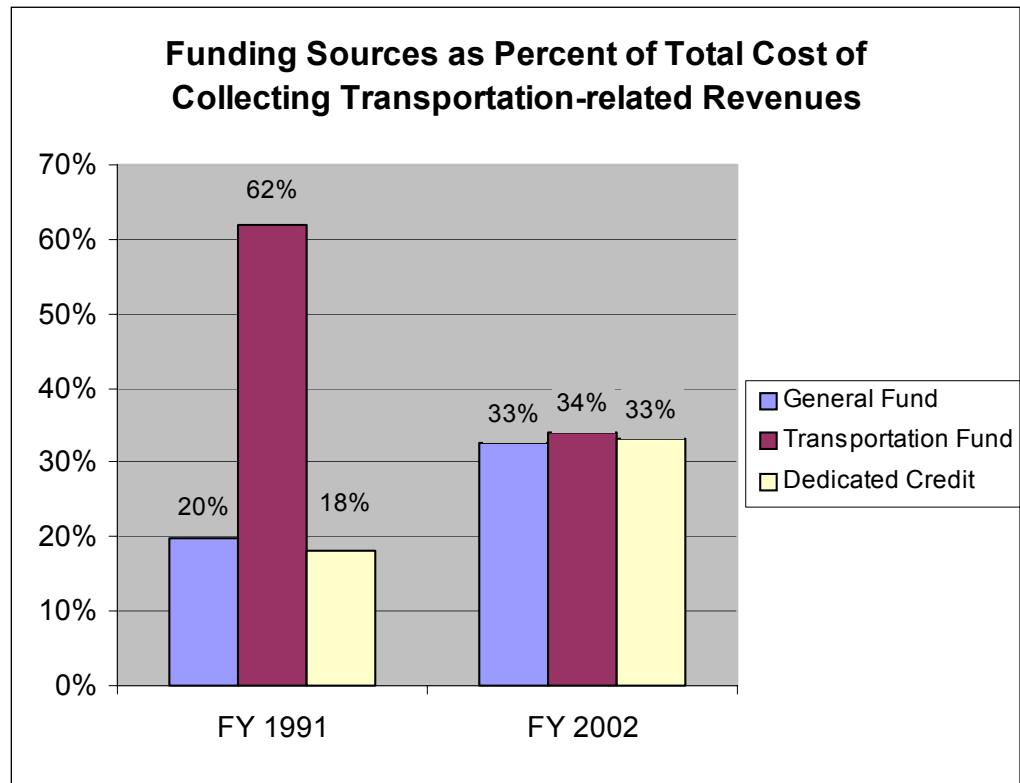
Cost Recovery Could Come From Increased General Funds

Increased cost recovery from the General Fund can be justified because the Legislature has historically funded costs of collecting transportation-related revenues from a mixture of General Funds, Transportation Funds, and dedicated credits. General Fund revenues have always been necessary because transfers from the Transportation Fund to the Tax Commission were legislatively capped at \$4.8 million in 1991. Over the years, as collection costs increased, General Fund revenues and dedicated credits funded increasingly greater portions of the costs, as shown in Figure 7.

Several other states pay for transportation-related fees and taxes through direct cost recovery or through their equivalent Transportation Funds.

The General Fund contributed increasingly to cost recovery of collecting transportation-related revenues because the Transportation Fund was limited.

Figure 7. As Costs of Collecting Transportation-related Revenues Increased There Was Greater Reliance on the General Fund Because of Limited Transportation Funds.



In fiscal year 1991, estimated collection costs were approximately \$7.8 million with 20 percent (\$1.6 million) being funded from the General Fund. By comparison, in fiscal year 2002, collection costs were \$14.3 million with 33 percent (\$4.7 million) being funded from the General Fund.

The fact that the General Fund contributes significantly to the DMV operations and transportation-related tax collections at the Tax Commission has been understood, if not supported, by the Legislature. After all, DMV provides valuable and needed services to the general public and to local governments, as well as to insurance companies, the Department of Public Safety, and other organizations that benefit from vehicle registrations.

According to **Utah Code 59-2-406(1)**, the collection of motor vehicle fees and taxes can be done, at the option of each county, by the Tax Commission or the county. Each county is allowed to have a DMV office which has been beneficial to county governments and to the vehicle

Because DMV functions benefit the counties and several different state entities, the Legislature could use more General Funds for cost recovery.

owners in each county. Also, having license plates on each vehicle has been critical to state and local law enforcement agencies statewide for identification, tracking and enforcement purposes. Because vehicle registrations and fee collections are so important to the public and to other agencies, and because the General Fund has historically supported the DMV operations, the Legislature could continue to provide some level of General Fund support for the DMV services.

Recommendation

1. We recommend the Legislature consider one of the options presented to restore the funding shortfall to the Tax Commission (Division of Motor Vehicles) for the collection of transportation-related revenues.

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Agency Response

November 11, 2002

Wayne L Welsh, CPA
Legislative Auditor General
130 State Capitol
Salt Lake City, Utah 84114-0151

Re: Legislative Auditor General Report 2002-07

Dear Wayne:

The Tax Commission appreciates the opportunity to respond to the above audit report on the Collection of Transportation-Related Revenue. We support the findings and recommendations. We appreciate the time and professionalism of your staff as they have conducted this audit.

The audit report provides for three ongoing funding options and the Tax Commission fully endorses each of the options as a viable solution to the budget shortfall. While details would have to be worked out for each option, each one could provide the ongoing funding that is required to continue ongoing programs.

We believe it would be helpful to provide additional background to others reading the report of the events of the Fifth Special Session of 2002 that lead to this potential shortfall in FY04. During that session, the Fiscal Analyst's Office recommended a change in the ongoing funding sources of the Tax Commission. This was related to questions that arose regarding the spending limitations imposed on Transportation Fund appropriations since 1991 (Utah Code 72-2-103) and other sections of code that indicate that Transportation Funds should be used to pay for the costs associated with the collection of those funds. This potential change in funding allocations is separate and distinct from the budget cuts that were imposed on all state agencies last year.

During appropriation meetings, the Fiscal Analyst's Office recommended a reduction in General Fund Appropriations with the intent to *replace* those funds with ongoing Transportation Funds. We have been told that several legislators were concerned with this change in funding sources. Since there was not adequate time to address the concerns during that short session, this audit was requested. At the close of that session, appropriations were made to keep the budget whole, with the \$5 million General Fund reduction being replaced with a \$1 million in ongoing Transportation Funds and \$4 million in one-time General Funds. The one-time funding that was used

Wayne L. Welsh
November 11, 2002
Page 2

to cover ongoing program costs is the amount that the audit is recommending 3 options for funding.

While the audit finds that \$3.7 million in additional costs are directly attributable to the collection of transportation-related funds, the ongoing reduction made during the session was \$4.0 million. We would ask that the final solution address the full amount of the reduction.

If ongoing funding is not restored, the reduction in state funding of transportation-related collection costs is equal to a 40% reduction (\$4 million of the current \$10 million in appropriated state funds). This is a sizable amount and if not funded with ongoing funds would result in significant impacts to the state's fuel tax and motor vehicle registration collection processes. Several Motor Vehicle offices would have to be closed and citizens would have to conduct business at fewer offices and with fewer staff. Significant lines would result at the remaining offices, and citizens would see much longer wait times when trying to complete their motor vehicle registration transactions. Other ongoing collection services would also be impacted to accommodate this large of a budget reduction.

Based on Utah Code 59-2-406, if county officials are not satisfied with the impact of the above situation, they may elect to do the combined motor vehicle registration work in their county. By statute, the state would be required to pay the counties for the costs associated with the state portion of the work, and ongoing funding would again be needed to pay the counties for doing the state's motor vehicle related work.

All three options presented in the report will provide the ongoing funding that is required for ongoing revenue administration and collection programs. We appreciate your efforts on this audit and will be requesting legislative support for implementing one of these options to restore ongoing funding.

Sincerely,

Barry C. Conover
Deputy Executive Director

cc: Rodney G. Marrelli, Executive Director
Pam Hendrickson, Chair
Bruce Johnson, Commissioner
Palmer DePaulis, Commissioner
Marc Johnson, Commissioner

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