

*Internal Audit Report*

**DEPARTMENT OF FINANCE  
PAYMENT IN LIEU OF  
TAXES AGREEMENTS AUDIT  
JANUARY 2020**

*Office of the County Auditor*





## OFFICE OF THE COUNTY AUDITOR

Craig Glendenning, CPA  
County Auditor

January 2020

The Honorable Members of the County Council  
The Honorable Calvin Ball, County Executive

Pursuant to Section 212 of the Howard County Charter and Council Resolution 22-1985, we have conducted an audit of the payments and monitoring of Payment in Lieu of Taxes (PILOT) agreements entered into by the County. Our audit disclosed that the Department of Finance did not have formal policies to monitor the payments and ensure that payments were made timely and in the appropriate amount. For example, as of September 2019, one property owner had not made the required PILOT payments for Calendar Years 2016, 2017, and 2018 in amounts totaling \$187,000.

This report has been reviewed with the Chief Administrative Officer and we have included the Administration's response. We wish to express our gratitude to the Department of Finance for the cooperation and assistance extended to us during the course of this engagement.

A handwritten signature in blue ink, appearing to read "Craig Glendenning".

Craig Glendenning, CPA  
County Auditor

## BACKGROUND

Payment in Lieu of Taxes (PILOT) agreements are a mechanism used by local governments and developers to encourage specific types of developments or projects (such as affordable housing). Use of a PILOT agreement is meant to allow projects to go ahead when they otherwise might not be able to based on considerations such as cost of the project. These agreements provide the developer with financial relief in the form of waived local property taxes (and sometimes other local taxes) for a specified period. Developers are usually required to pay a minimum PILOT amount along with State taxes and any local taxes not waived. In addition, PILOT agreements require additional amounts due dependent on the financial conditions of the project.

All PILOT agreements entered into by the County must be approved by the Council as required for multi-year agreements. Property owners under such agreements make payments annually to the Department of Finance (Finance). In addition, Finance receives certain financial information annually as required by each agreement. As of August 2019, Finance monitored 30 PILOT agreements. For the 2019 tax year, the County received PILOT payments totaling \$640,000. The property tax credits provided totaled \$1.4 million.

## FINDINGS, COMMENTS, AND RECOMMENDATIONS

### **Finding 1**

**The Department of Finance did not have procedures in place to monitor PILOT agreements and payments. As a result, Finance failed to collect \$187,027 from one property owner over the last three years.**

Finance did not have procedures in place to ensure that property owners with approved PILOT agreements made payments in accordance with the agreements. In addition, Finance did not assess penalties for late payment. Our test of nine payments and agreements related to Calendar Year 2018 found the following:

- Finance did not receive a Calendar Year 2018 payment from one PILOT property owner totaling \$65,240. According to the financial report, the property owner also did not remit payments for Calendar Years 2016 and 2017. The payments due to the County totaled \$187,027 for the three years.
- Although PILOT agreements provide for the imposition of penalties for late payment up to and including the termination of the agreement and payment of real property taxes due for the preceding year, Finance did not assess any penalties for late payments for the items we tested. For example, one payment totaling \$10,109 due April 1, 2019, was not received until August 16, 2019, and Finance did not send overdue notices or take other action to collect the amount due.

- Four financial reports did not contain adequate detailed calculations to determine if the owner owed amounts in addition to the minimum payment as required by the agreements.

***We recommend that Finance develop and implement procedures to monitor PILOT agreements including:***

- ***Developing procedures to track payments and assess past due penalties when applicable, including the \$187,027 noted above;***
- ***Ensuring payments agree to the supporting financial reports; and***
- ***Reviewing financial reports for sufficient detailed information to ensure that payment was in the proper amount.***

*Administration's Response:*

The Department of Finance concurs. Procedures are in place for PILOT revenue tracking, calculation, verification, and collection. Additionally, the County has collected the revenue and interest for the PILOT agreements listed. Specifically, \$246,207.01 has been received for the PILOT described in bullet #1 and \$5,262.72 for the PILOT described in bullet #2.

## **ADDITIONAL COMMENT**

The Applied Physics Laboratory (APL) is a not-for-profit, Johns Hopkins affiliated research center serving as a technical resource for the Department of Defense, NASA, and other government agencies. Although it is exempt from paying property and fire tax – and therefore technically not a PILOT - the County entered into the agreement with APL in October 1972 which states that “*it is recognized that the laboratory requires various services which would ordinarily be supported in part by the very property taxes from which it is exempt.*” The County accounts for the payments received as PILOT in its financial records, considering they are receiving a payment rather than taxes.

While the agreement provides a methodology for calculating payment for services that APL receives from the County, it has not been reviewed for 48 years. Therefore, there is no assurance that the payment the County receives from APL, which totaled \$900,000 in Fiscal Year 2019, adequately compensates the County for the services APL receives.

***We recommend the County Administration review the 48-year-old PILOT agreement and ensure that APL is paying the County for services that the County provides.***

***We also recommend that the County review the agreement on a periodic basis and submit it to the County Council for review.***

*Administration's Response:*

County Administration acknowledges and agrees with the recommendation to periodically review the agreement and share with the Council as appropriate.

As noted by the auditor, APL is exempt from taxes by State law. The long-standing agreement is carefully constructed to maintain its relevance over time by linking APL's contribution to the current County budget - the first payment in 1973 was \$63,166, and for tax year 2019 was \$1,057,302. The County values APL's significant achievements, community involvement, economic presence and voluntary payment.

## **AUDIT SCOPE, OBJECTIVES AND METHODOLOGY**

We conducted a performance audit of Payment in Lieu of Taxes (PILOT) agreements including monitoring of payments and related financial information.

We conducted our audit in accordance with generally accepted government auditing standards prescribed by the Comptroller General of the United States. Those standards require us to plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence we obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objectives of our audit were to:

1. Determine the adequacy of procedures and controls established to monitor PILOT agreements.
2. Ensure that agreements were properly approved.
3. Ensure that payments made were in accordance with the related agreements.

To accomplish our objectives, we met with the Department of Finance (Finance) staff responsible for monitoring and record keeping of PILOT agreements. We reviewed agreement documents and County Council resolutions. We performed tests designed to determine adherence to the PILOT agreements with regards to payments amounts and required financial reporting. Generally, transactions were selected for testing based on auditor judgment, which primarily considers risk. Unless otherwise specifically indicated, neither statistical nor non-statistical audit sampling was used to select the transactions tested. Therefore, the results of the tests cannot be used to project those results to the entire population from which the test items were selected.

Management is responsible for establishing and maintaining effective internal control. Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate. We conducted our field work from August 2019 to September 2019. The Administration's responses to our finding and recommendations are included in this report.

**AUDIT TEAM**

**Edward L. Shulder, CPA**  
Deputy County Auditor