



STATE OF NEVADA
DEPARTMENT OF TAXATION

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January 19, 2016

Mr. Rajan O. Dhungana, Esq.
Sahara Legal Group
59 Damonte ranch Pkwy, STE B-550
Reno, Nevada 89521

Dear Mr. Dhungana:

The Department of Taxation has received your letter of October 26, 2015 on behalf of your client Jeffrey Church to the Committee on Local Government Finance ("CLGF"). The letter requests CLGF conduct an investigation into the appropriate taxing authorities and the recipients of the revenues from City of Reno Ballot Measure R-3 to see if there has been negligent or willful misappropriation of funds; or "at the very least" provide Mr. Church with information as to where and how the tax revenue is being appropriated. You further request that Mr. Church be notified in writing if CLGF will commence an investigation or take any relevant action regarding Mr. Church's request.

In addition to your letter, Mr. Church sent an email on October 27, 2015 transmitting your letter to the Department and additionally requested a legal opinion or confirmation that Attorney General Opinion (AGO) 2011-4 equally applies to the ballot measure R-3.

Background

The Department reviewed the City of Reno's Comprehensive Annual Financial Reports ("CAFR"). For example, Schedule 17 from the FY 2005-2006, FY 2008-2009, FY 2010-2011, and FY 2013-2014 CAFRs indicate the total number of authorized emergency fire personnel was 194 in 1997 compared to a high of 345 in FY 2010 and a decline to 192 in 2014. Similarly, fire prevention officers in FY 1997 totaled 16, increased over time to a high of 19 in FY 2009, and declined to 12 in 2014. The number of fire stations declined from 16 to 13 in the same period of time. *See Exhibit 1.*

The Department also requested the City of Reno supply information regarding the proceeds of the fire override tax levy and how it was appropriated by the City Council. In response, the City provided a table showing the complete history of the actual amounts received from the levy of the fire override since inception. In 1997-98, the amount received from the levy was \$2,399,992. The highest amount received was \$5,177,557 in FY 2009/10 and has declined since then to \$4,443,996 in FY 2014/15. *See Exhibit 2.*

The table also shows the actual expenses incurred by the Fire Department, which range from \$20,178,056 in FY 1997/98 to a high of \$51,586,489 in FY 2009/10. Expenses have declined

since then to \$40,622,244 in FY 2014/15. The fire override tax levy contributed an average of 10% of the total revenues required to cover Fire Department expenses, ranging from a low of 8% in FY 2003 to a high of 13% in FY 2000.

Audits of City of Reno Financial Statements

Mr. Church has appeared before CLGF several times during the public comment period requesting an investigation. See *Exhibit 3, CLGF Minutes, August 8, 2014; Minutes, February 6, 2015; Partial Draft of Minutes, October 27, 2015*. At the August 8, 2014 meeting, Chairman Leavitt responded that "prior to the next meeting, we will have a submission of the audit report from the City of Reno. The auditors have an obligation in their report to comment on matters relating to legal compliance in financial matters."

At the February 6, 2015 meeting of CLGF, the City of Reno reported on its financial condition. Mr. Church again requested a legal opinion on the City's use of the proceeds from Ballot Measure R-3. The Chairman asked Mr. Chisel, the City's chief financial officer, if the City had received the audit, and again stated "The auditors have the responsibility to comment on your legal compliance and financial compliance." The Chairman asked if there were any violations of statute stated in the audit. Mr. Chisel responded that there were no violations of statute. He also stated that the proceeds of all voter-approved overrides are directed to the fire or police departments as required. See *Exhibit 3, February 6, 2015 CLGF Minutes*.

In addition, Department staff has specifically reviewed the audits for the last five years in connection with Mr. Church's assertions. The findings of the auditors are critical because they use Government Auditing Standards which require the auditors to plan and perform the audit to obtain reasonable assurance about whether the basic financial statements are free from material misstatement. Department staff reviewed the audits looking for any reported material weakness or significant deficiency related to internal controls. The audit opinions for FY 2010 through 2015 indicate the basic financial statements of the City present fairly, in all material respects, the financial position of the governmental activities, the business-type activities, each major fund, and the respective changes in financial position in accordance with generally-accepted accounting principles.

Accounting for Restricted Use

At the February 6, 2015 meeting of CLGF, Mr. Church indicated he believed the R-3 Ballot Measure required the proceeds of the tax levy to be classified as a special revenue fund. The City does not have a separate special revenue fund for the Fire Department but instead includes it as part of the General Fund. I have enclosed Guidance Letter 15-002 which discusses special revenue and enterprise funds. The Guidance Letter was approved at the October 27, 2015 CLGF meeting. See *Exhibit 4*.

The Guidance Letter beginning at page 4 discusses the nature of a special revenue fund as required by Governmental Accounting Standards Board ("GASB") Statement No. 54, "Fund Balance Reporting and Governmental Fund Type Definitions." GASB Statement No. 54 states at Paragraph 31 that

The restricted or committed proceeds of specific revenue sources should be expected to continue to comprise a *substantial portion* of the inflows reported in the fund. Other resources (investment earnings and transfers from other funds, for example) also may be reported in the

fund if those resources are restricted, committed, or assigned to the specified purpose of the fund. Governments should discontinue reporting a special revenue fund, and instead report the fund's remaining resources in the general fund, if the government no longer expects that a substantial portion of the inflows will derive from restricted or committed revenue sources.

The Guidance letter goes on to say at page 6 that:

"Substantial portion" of inflows is not defined in Statement No. 54, however, the Government Finance Officers Association has indicated "around 20 percent" is reasonable for justifying a special revenue fund; and it is a commonly used threshold. Local governments also need to consider factors such as past resource history, future resource expectations and unusual current year inflows such as debt proceeds.

Based on the GASB Statement No. 54 requirements, it does not appear that the City of Reno is required to establish a special revenue fund to account for the proceeds of the fire override tax levy. As noted above, the proceeds of the fire override levy constitute only about 10% of the total appropriations for the Fire Department.

Nevertheless, it is important to note that the proceeds of the fire override tax levy are restricted to the uses indicated in Ballot Measure R-3. Two GASB Statements make pronouncements on the subject.¹

First, Paragraph 34 of GASB Statement No. 34 states:

34. Net assets should be reported as restricted when constraints placed on net asset use are either:
- a. Externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments
 - b. Imposed by law through constitutional provisions or enabling legislation.

Further, GASB Statement No. 34, Paragraph 52 states:

All revenues are *general revenues* unless they are required to be reported as program revenues, as discussed in paragraphs 48 through 51. All taxes, even those that are levied for a specific purpose, are general revenues and should be reported by type of tax – for example, sales tax, property tax, franchise tax, income tax.

Thus, the fact that the source of revenue is from the reporting government's taxpayers, the revenue is always considered a general revenue, even if restricted to a specific program.

GASB Statement No. 54, Paragraph 8 similarly states that:

8. Fund balance should be reported as restricted when constraints placed on the use of resources are either:
- a. Externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments; or
 - b. Imposed by law through constitutional provisions or enabling legislation.

¹ GASB Statements may be found on the internet at <http://gasb.org/resources/ccurl/313/494/GASBS%2054.pdf> and <http://www.gasb.org/cs/BlobServer?blobkey=id&blobwhere=1175824063624&blobheader=application%2Fpdf&blobcol=urldata&blobtable=MungoBlobs>

GASB Statement No. 54, Paragraph 9 discusses *enabling legislation*. Enabling legislation:

Authorizes the government to assess, levy, charge, or otherwise mandate payment of resources (from external resource providers) and includes a legally enforceable requirement that those resources be used only for the specific purposes stipulated in the legislation.

Page 48 of the 2014-2015 City of Reno CAFR notes that governmental funds are classified in accordance with GASB Statement No. 54, *Fund Balance reporting and Governmental Fund Type Definitions*, including "restricted fund balances have constraints placed upon the use of the resources either by an external party or imposed by law through a constitutional provision or enabling legislation."

The fact that the proceeds of the fire override levy are restricted is further confirmed in the FY 2015 Budget Summary, Section III, Page 65 which specifically shows the Fire Station Override as restricted funds. See <http://www.reno.gov/home/showdocument?id=46631> . See also Exhibit 5.

Finally, the City notes in the FY 2015 CAFR at Page 49:

Prioritization and Use of Available Resources

When both restricted resources and other resources (i.e., committed, assigned and unassigned) can be used for the same purposes, it is the City's policy to use restricted resources first. Furthermore, when committed, assigned and unassigned resources can be used for the same purpose, it is the City's policy to use committed resources first, assigned second, and unassigned last.

Appropriation of Funds

NRS 354.598(4) states that "Upon the adoption of the final budget or the amendment of the budget in accordance with NRS 354.598005, the several amounts stated in it as proposed expenditures are appropriated for the purposes indicated in the budget."

Annually, the Department of Taxation ensures that the adoption of the budget is in compliance with state law. Each local government supplies the Department of Taxation with a copy of the final budget as adopted by the governing body. The document is signed by a majority of the governing body and information showing how the public was noticed about the budget must also be submitted.

At the Department's request, the City supplied a copy of the resolution adopting each budget since inception of the levy of the fire override. If you desire copies, please advise. The Department did not find any evidence of misappropriation of funds.

Request for Legal Opinion

The Department has consulted with the Attorney General's office with regard to the application of AGO 2011-4 to Ballot Measure R-3. We are advised that AGO 2011-4 does not apply to the City of Reno. AGO 2011-4 references AB 418 which was a bill passed specifically for Clark County and relates to sales and use taxes. Ballot Measure R-3 relates to property taxes for the City of Reno.

Further, the Department has also reviewed the letter you received from the Reno City Attorney dated March 13, 2015 with regard to the question of whether the legal analysis regarding "supplantation" contained in AGO 2011-4 is applicable to the ballot measure. The City Attorney stated that the legal analysis regarding "supplantation" contained in AGO 2011-4 is not applicable to the ballot measure because the ballot measure is silent on supplantation. We agree the ballot measure is silent on supplantation. Finally, your comments on page 2 of your letter reference a Nevada Supreme Court decision regarding the interpretation of statutes. We are advised from the Attorney General's office that those comments about statutory interpretation are inapplicable to a ballot since it is not a statute.

Your client's request for CLGF to conduct an investigation will be placed on the next agenda of CLGF, which is scheduled to meet at the following time and place:

Date and Time of Meeting: January 26, 2016 9:00 a.m.

Gaming Control Board
Board Room
1919 College Parkway
Carson City, Nevada

Video Conference to:
Gaming Control Board
Grant Sawyer State Office Building
555 East Washington Avenue
Second Floor, Room 2450
Las Vegas, Nevada

At that time, the Department will recommend that staff could find no basis for a formal investigation, and that unless and until evidence of wrongdoing is brought forward, that a formal investigation not be initiated.

Sincerely,



Terry E. Rubald
Deputy Executive Director