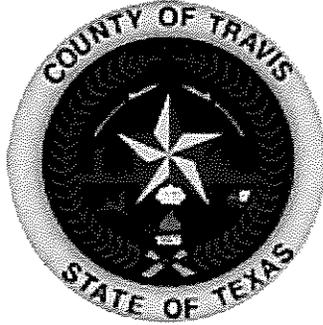


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To : Bruce Elfant
Travis County Tax Assessor/Collector

From: Nicki Riley, CPA 
Travis County Auditor

Date: April 27, 2018

Subject: Auto Title Services Even-Trade/Exempt Transaction Data Analysis

The Risk Evaluation and Consulting Division (REC) of the Travis County Auditor's Office has performed an analysis of the motor vehicle transaction data collected through the Texas Department of Motor Vehicles (TXDMV) Registration and Title System (RTS). The objective of this data analysis was to investigate the anomalies that were discovered when analyzing title transactions entered into RTS by Auto Title Services (ATS). ATS is a third party business that has contracted with the Travis County Tax Assessor/Collector's Office to perform vehicle registration and title services for the Tax Office as its agent.

Our review focused on even-trade and exempt salvage transactions performed by ATS. We performed an exploratory analysis to obtain an understanding of the data and to discover any unusual relationships.

Summary of items noted:

During the period September 25, 2015 to May 15, 2017, ATS performed 456 even trade transactions, 24% of the 1,842 even trades performed throughout Travis County in that period. Of these, 383 (84%) were completed in a six-week period ending November 9, 2015. All but seven (1%) of these 456 transactions appear to have been inappropriate or incorrectly recorded for various reasons. We estimate that over \$127,500 in vehicles sales taxes payable to the Texas State Comptroller was not collected for these transactions.

From June 2016 to May 2017, ATS processed 1,201 sale tax-exempt transactions related to salvage titles. This was 91% of the total exemptions of this type issued throughout the County for that period. It appears that from 701 to 1,187 of these tax-exempt transactions were handled incorrectly, although further verification with dealer records is required to conclusively verify this. If the applicable sales taxes were not collected at the dealerships, we estimate that \$540,498 to

\$926,568 in vehicle sales taxes due to the State Comptroller was not collected for these transactions.

Please see the Review Methodology/Details section attached to this memo, as well as Attachments A and B, for more details. Note that the TXDMV suspended ATS' access to the RTS system in May of 2017; this suspension is still in place. Please let us know if you have any questions or if we can be of assistance in this matter going forward.

REPORT DISTRIBUTION

Sarah Eckhardt, Travis County Judge

David Escamilla, Travis County Attorney

Peter Einhorn, Chief of Staff for Travis County Judge

REVIEW METHODOLOGY/DETAILS

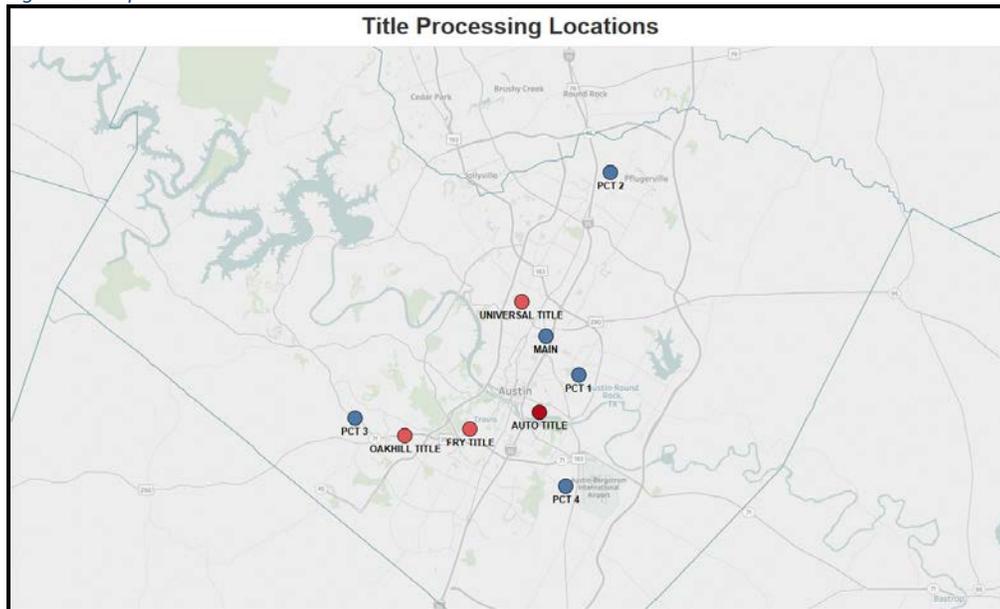
This examination included an analysis of the data collected by RTS for motor vehicle (MV) registrations, title transactions, collection of sales tax related to the sale or transfer of motor vehicles, issuance of temporary permits and handicap placards, as well as other motor vehicle-related transactions. Our analysis was based on applying sampling procedures and analytical models to RTS records. The scope of this examination included an examination of the transactions entered into RTS by all users identified to conduct business for Travis County during the three years ending October 1, 2017.

The TXDMV provides RTS to tax offices across the state for the purposes of consistently calculating, tracking, and accounting for vehicle title and registration transactions. TXDMV also collects and maintains the data accumulated by RTS. The local entities using this system have little input on its design, functionality, and controls; however, a limited number of system settings can be locally administered, some of which can be utilized for internal control purposes.

Background

Texas residents are responsible for titling and registering their motor vehicles with the Texas Department of Motor Vehicles as required by Sections 501 and 502 of the Transportation Code “Certificate of Title Act” and “Registration of Vehicles.” The Travis County Tax Assessor/Collector’s Office is responsible for collecting vehicle taxes and fees. This office has approximately 46 staff members trained to process these transactions, including title transfers, motor vehicle licenses, registrations, and miscellaneous fees. There are five Travis County locations where title transactions are processed, along with four contracted title companies, as detailed below (Figure 1):

Figure 1: Map



The purpose of titling a vehicle is to reduce motor vehicle theft, the import of stolen vehicles into the state, and the sale of encumbered vehicles without the disclosure of a lien on the vehicle. The

Motor Vehicle Title Division of the Tax Office collects fees for vehicle title applications, rebuilt salvage vehicles, bonded title applications, title fees, and sales taxes. Title transactions are processed through RTS, which is a point-of-sale system that allows the data to be entered by the Tax Office staff at the time the transaction occurs.

Even-trade Transactions

We initially reviewed even-trade transactions, which occur when two parties agree to exchange vehicles they determine to be of equal value, and no funds or other considerations are included in the trade. Because the values are equal, no sales taxes are due by either party included in the transaction, and only a \$5 fee is charged for this transaction. Because of the nature of these transactions, they are advantageous from a tax perspective to the parties transferring vehicles, but they should be relatively rare.

When a vehicle is registered in relation to an even-trade transaction, the clerk performing the transaction should verify the Vehicle Identification Numbers (VINs) for both vehicles in the even-trade transaction in RTS. This review should verify that: a) the VINs are valid and b) the vehicle being traded away is currently titled under the name of one of the parties to the even-trade transaction. While this process does not fully verify the reasonableness of the even trade, this control should be helpful in limiting the number of invalid/fraudulent even trades.

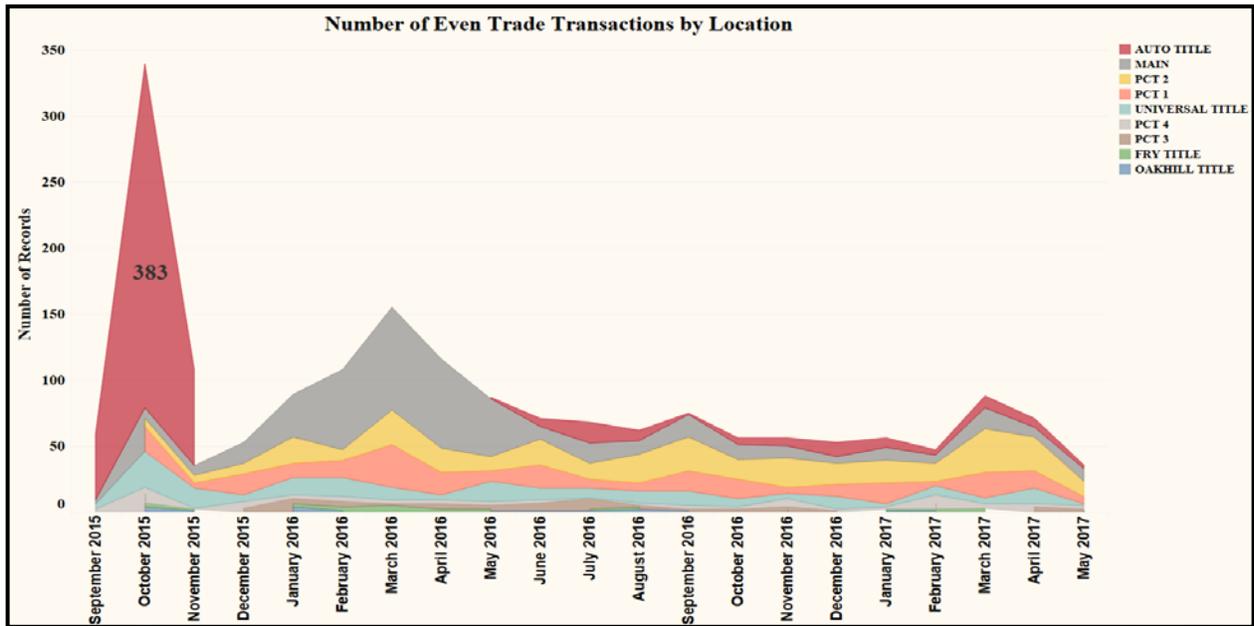
The data set we analyzed contains transaction data starting September 25, 2015 and ending January 31, 2018. We were informed that the TXDMV had suspended Auto Title Services May of 2017, so we filtered the data to include all transactions up to May 15, 2017, to prevent any inconsistencies with the data and our results. We then summarized the transactions by location to understand the volume of even-trade transactions completed by each location (Table 1 below).

Table 1: Even-Trade Transaction Summary

Location	Total Transactions
Auto Title Services	456
Main Tax Office	443
Pct 2 Tax Office	336
Pct 1 Tax Office	252
Universal Title Services	190
Pct 4 Tax Office	62
Pct 3 Tax Office	57
Fry Title Services	27
Oak Hill Title Services	19
TOTAL	1,842

From our analysis, we determined Auto Title Services completed an unusually high volume of even-trade transactions. Of the 1,842 even-trade transactions completed during this period, Auto Title Services completed 456 (24%). Of these, 383 (84%) were completed during a six-week period starting September 25, 2015 and ending November 9, 2015 (See Graph 1 on following page). On the heels of this large quantity of even trades, the TXDMV suspended Auto Title’s access to RTS from December 2015 to May 2016.

Graph 1: Even-Trade Transactions



Our next step was to examine the 456 even trades performed by ATS in detail. We first verified the VIN numbers for both vehicles in the even-trade transaction, noting that the VIN for the “traded away” vehicle was invalid for 41 (9%) transactions. As stated above, the clerk posting the even trade should be verifying the VIN for the traded-away vehicle; thus there is no logical reason for such a large number of invalid VINs being entered into RTS.

For 105 (23%) of the “traded away” vehicles, the applicable vehicles were later re-registered by the parties that supposedly traded them away. Based on this, it appears the even-trade transactions did not actually occur and a normal vehicle purchase without a trade actually happened. We researched the remaining 303 (66%) VINs to verify the traded vehicles were properly registered and found that no Travis County data was available for any of these vehicles.

Since our dataset was limited to only Travis County transactions, we determined that the owners of these 303 VINs likely resided in another county. To verify this, we remitted a sample of 10 transactions to the TXDMV for further review. They verified that the trading parties in these 10 transactions did reside outside of Travis County and that none of the 10 “traded away” vehicles in question were actually traded by the party applying for the even trade. In addition, TXDMV rules prevent titling vehicles for residents of other counties except under very specific conditions. It is unlikely that any of these 303 even trades for out-of-county residents should have been recorded in Travis County.

For these 456 transactions, we also found the same VIN was used in multiple even-trade transactions 14 (3%) times and the same owner was involved in multiple even-trade transactions in 30 (7%) instances. Given the rarity of even-trade transactions, it is extremely unlikely the same vehicles or vehicle owners would be involved in legitimate even-trade transactions at these rates.

We also reviewed each valid VIN for both sides of all 456 even trades in the Standard Presumptive Value (SPV) calculator located on the TXDMV¹ website. From this, we were able to determine the standard value of both vehicles in each transaction. We noted that in 381 (84%) instances, the difference in standard value between the two exceeded 20%. While SPV does not take into account the actual condition of the vehicles in question, 84% of these trades exceeding a 20% differential appears unreasonable. Table 2 below details the above findings by transaction type; taxes due are based on the SPV for the vehicle at the time of the even-trade transaction:

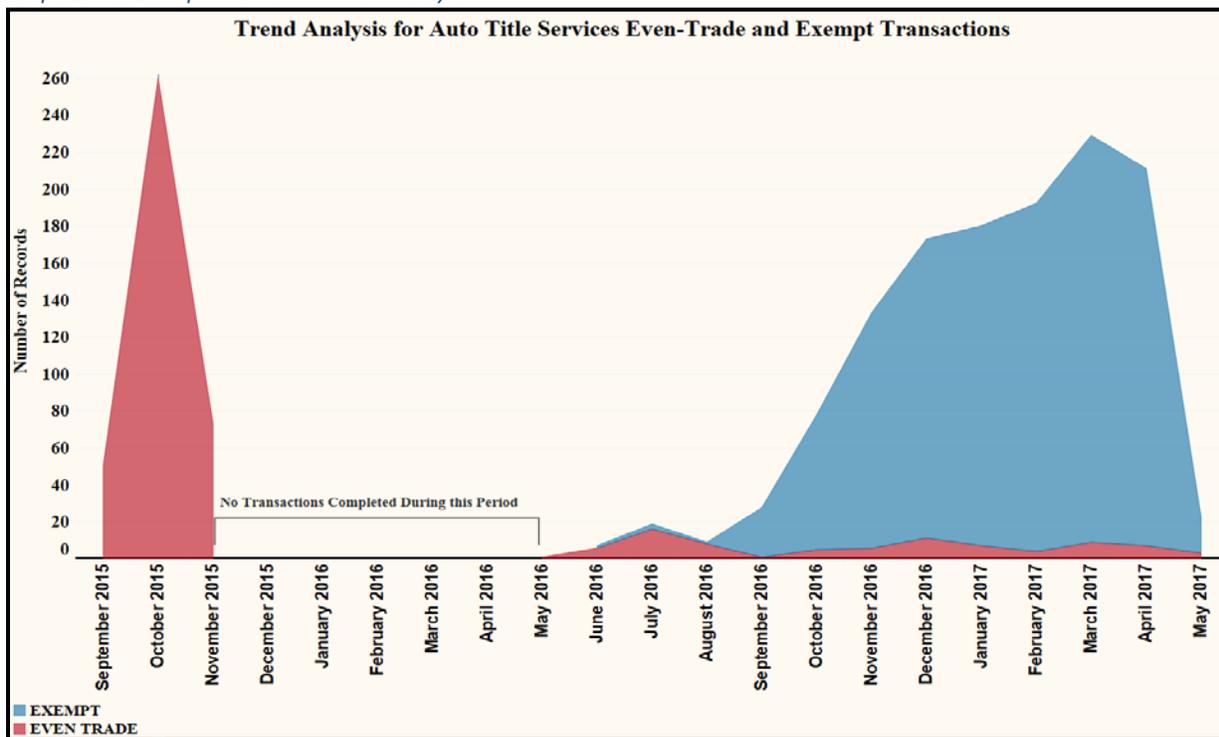
Table 2: Transaction Type Summary

Transaction Type	Total Transactions	20% Value Difference	Est Tax Due
Traded	7		\$35
Invalid VIN	41	40	\$18,507
Not Traded	105	74	\$29,672
No Information	303	267	\$79,741
TOTAL	456	381	\$127,920

Exempt Transactions

As stated above, ATS received a six-month suspension by the TXDMV from December 2015 to May 2016. After their reinstatement, Auto Title completed significantly fewer even-trade transactions. However, Auto Title completed an unusually high volume of exempt transactions after their suspension (See Graph 2 below). Based on this, we also reviewed these exempt transactions, which are utilized when a customer qualifies for a waiver of vehicle sales taxes under certain circumstances defined by the Texas State Comptroller.

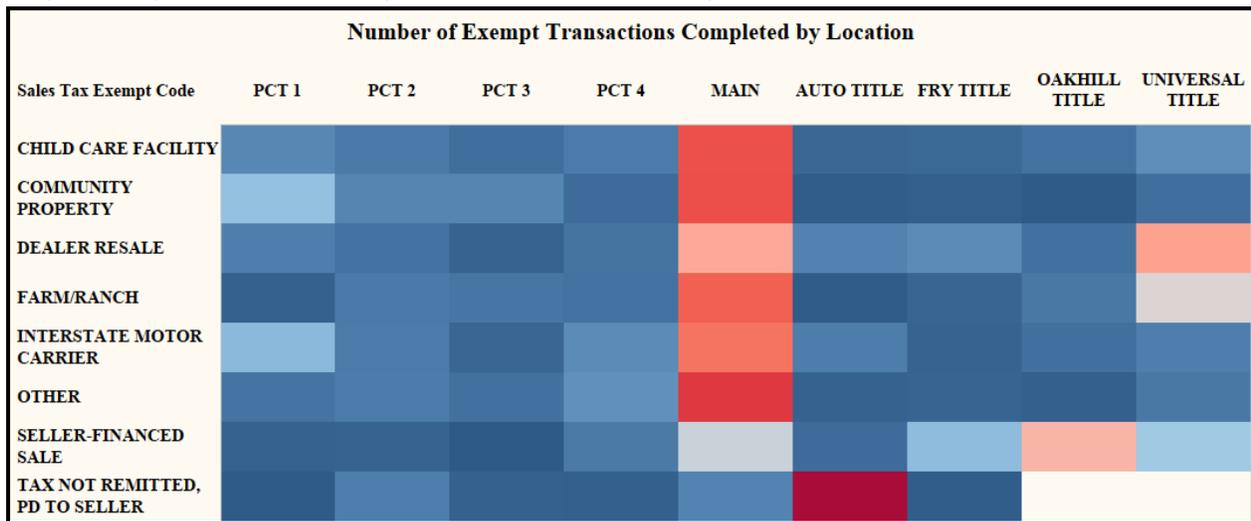
Graph 2: Tax Exempt Transaction Trend Analysis



¹ <http://www.txdmv.gov/spv-calculator>

According to the Motor Vehicle Sales Tax Manual, an employee or user must enter an exempt code when a transaction is deemed to be exempt. This code allows the DMV to track when each of the 17 exempt codes are used for exempt transactions. We first summarized exempt code transactions using a Heat Map to identify where most of the exempt code transactions occurred. A heat map is a two-dimensional representation of data in which values are represented by colors, providing an immediate visual frequency summary of the data. The colors used for the heat map provided on Graph 3 below range from a dark blue representing low transaction volume to a dark red representing a high volume. According to the heat map below, the Tax Office’s main location appears to have completed the most transactions for each of the top exempt codes, except for “Tax not Remitted, Paid to Seller” transactions, for which ATS issued by far the most.

Graph 3: Exempt Transaction Heat-Map (Period: October 1, 2015 to May 15, 2017)



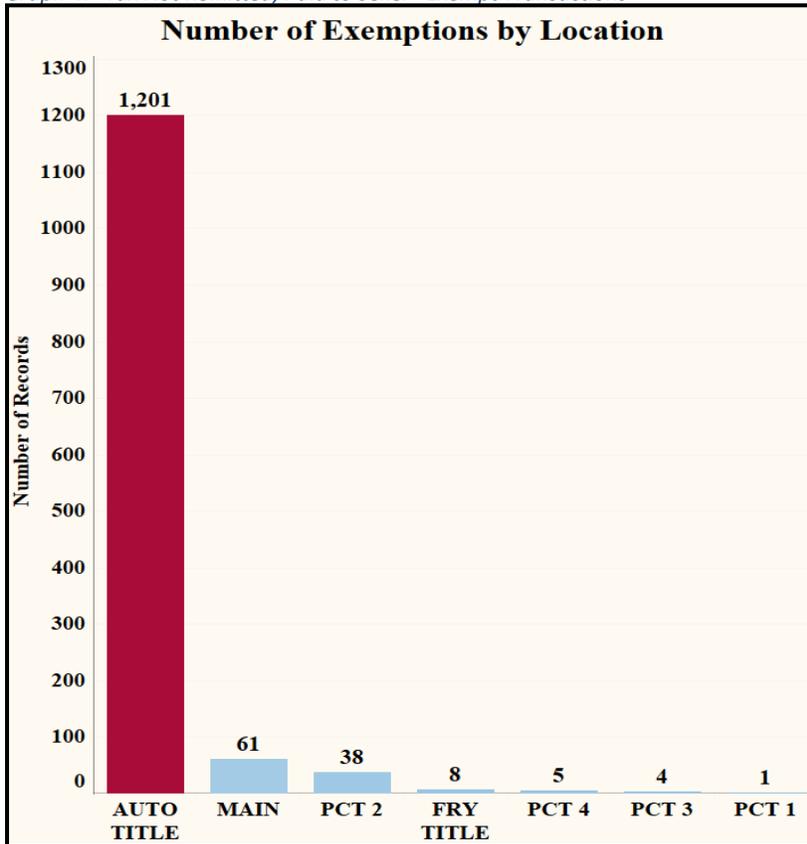
When the “Tax not Remitted, Paid to Seller” exemption code is used, the buyer is exempt from paying motor vehicle tax at the time the transaction occurred. Specifically, this exemption code is used when the vehicle is not road worthy (typically due to being wrecked) and has incurred a salvage title. In this state, the vehicle is considered personal property, and regular sales taxes (8.25%) are incurred and paid to the dealer when the vehicle is purchased.

When titling the salvage vehicle under these circumstances, the buyer must provide the clerk a bill of sale as proof they paid the standard sales tax to the seller. If the bill of sale is not available, the buyer must pay motor vehicle sales tax (6.25%) at the time of the title transaction. The “Tax not Remitted, Paid to Seller” exemption code can only be used if both the vehicle is not functional or safe for road use and the party titling the vehicle can support that they paid the seller 8.25% sales tax. When a vehicle has been inspected and deemed road worthy, this exemption cannot be used. The vehicle is no longer personal property, and the entity issuing the title is responsible for collecting the standard vehicle sales taxes of 6.25%.

Upon noting that ATS performed such a significant number of “Tax not Remitted, Paid to Seller” exemptions, we quantified the number of these exemptions performed by location, using Graph 4

below. Overall, 1,318 “Tax not Remitted, Paid to Seller” exempt transactions were completed in the period, of which 1,201 (91%) were performed by ATS.

Graph 4: “Tax Not Remitted, Paid to Seller” Exempt Transactions



We performed a detailed review of these 1,201 exempt ATS salvage transactions, the details of which can be found in Table 3 below. Specifically, we noted that the vehicles for 701 (58%) of the 1,201 exempt transactions passed inspection prior to being sold. An additional 338 (28%) passed inspection within eight days of being sold, while 148 (12%) passed inspection over eight days after being sold, but prior to being titled. Fourteen transactions are likely to have been completed correctly.

Table 3: Exempt Transaction Summary

Transaction Details	Transaction Count	Est Tax Due .0625
Insp Date Before Sale	701	\$540,498
Insp Date within 8 days of sold date	338	\$270,249
Insp Date after 8 Days from Sold Date	148	\$115,821
Transaction Completed Correctly	14	0
TOTAL	1,201	\$926,568

Since this exemption cannot be used for “road ready” vehicles which have passed inspection, vehicle sales taxes should have been collected on most, if not all, of these 1,187 (1,201 - 14) transactions. Table 3 above includes an estimate of the sales taxes payable to the State comptroller for these exempt transactions using 6.25%. We based these estimates on the Standard Presumptive Value of a sample of 100 of these exempt vehicles.

It is possible that the dealers selling these salvage vehicles collected the 8.25% in sales taxes for some or all of these transactions. However, in the case of the 701 vehicles that passed inspection and were road worthy at the time of sale, the dealers would have been violating TXDMV regulations in collecting the 8.25%. Our office does not have the authority to obtain this information from the dealers, so a review by the State Comptroller’s Office would be necessary to verify that no 8.25% sales tax payments were collected.

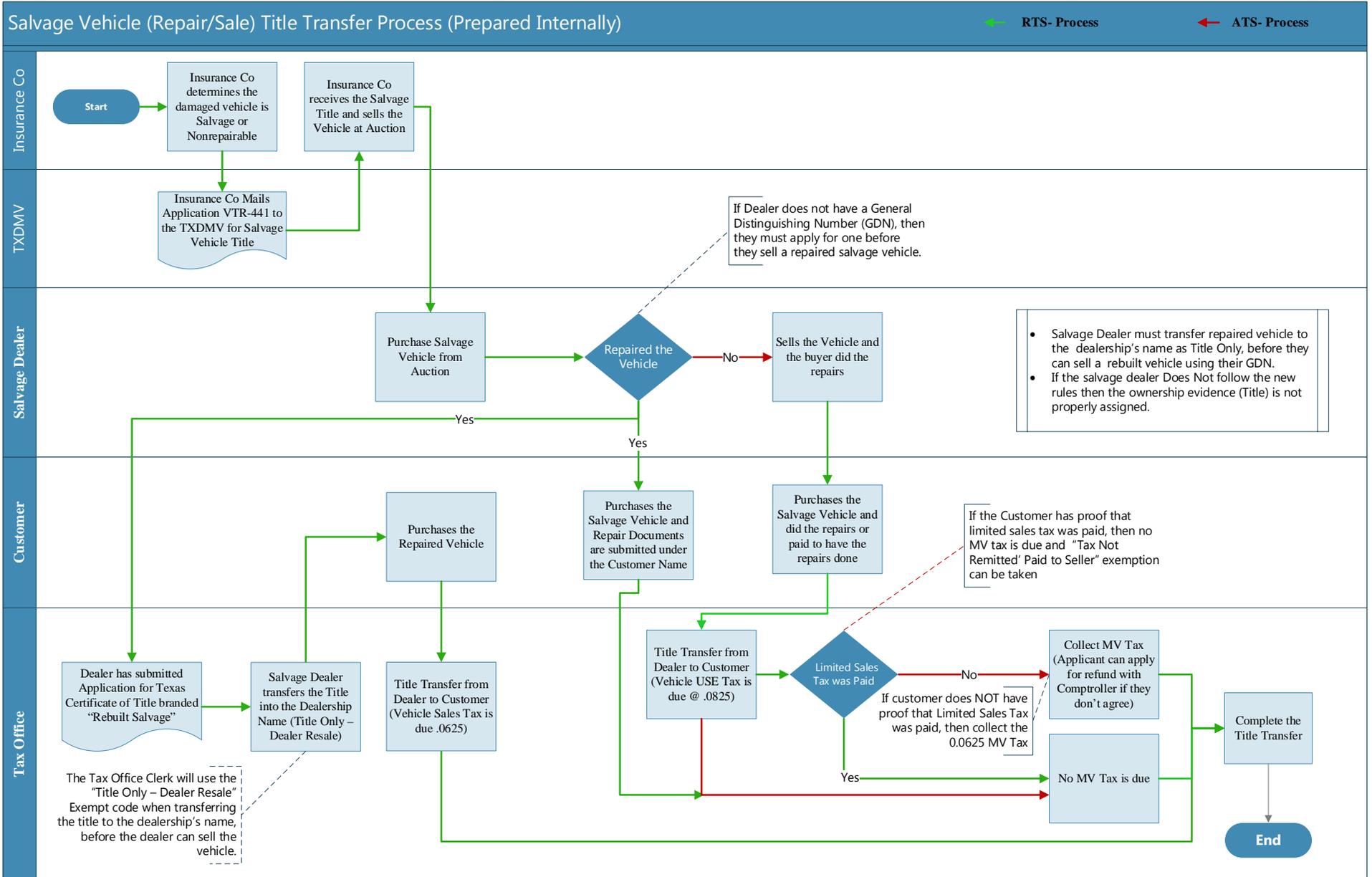
Note that for all 1,201 of the above transactions, ATS assessed a rebuilt title fee indicating that an application for a Texas “Rebuilt Salvage” title was submitted. However, according to the Transportation Code Sec. 501.100, a “*Texas Title branded Rebuilt Salvage is required when a salvage motor vehicle has been rebuilt and placed in an **operable** condition before selling or transferring ownership of the vehicle*” (emphasis added). For each of the road-worthy vehicles titled by ATS, the dealers should have obtained the rebuilt salvage title prior to the sale. Since this fee was assessed on the retail purchasers, these dealers also violated TXDMV regulations on these transactions.

We also plotted the owner addresses for these transactions, noting that a significant number of them related to parties residing outside of Travis County (See Appendix B.). As stated above, TXDMV rules prevent titling vehicles for residents of other counties except under very specific conditions. TXDMV regulations also require that dealers selling salvage vehicles be licensed to do so by the TXDMV. We noted that a number of the dealers for whom ATS titled salvage vehicles were either not licensed or had exceeded their annual limit of salvage sales. We are reporting these dealers to the TXDMV through their standard reporting mechanism.

Conclusion

There appear to be significant issues related to even-trade and exempt transactions posted by Auto Title Services before and after their services were initially suspended. In addition, a material amount of vehicle sales taxes are likely to have not been collected and remitted to the State.

APPENDIX A



APPENDIX B

Exempt Transactions by Seller Location

