



OFFICE OF THE
STATE AUDITOR

Comment Period: In an effort to make our publications accurate and useful to our intended audience, we invite individuals who work for and with local government entities to read this draft and provide comment. The comment period is ongoing. Comments should be submitted to Seth Oveson at soveson@utah.gov.

Auditor Alert 2018-03 Draft - Revised

Date: October 23, 2018; Revised November 9, 2021

Subject: Government Fees

Overview

The Government Finance Officers Association (GFOA) makes the following recommendations concerning the use of fees as a method of financing governmental services¹:

1. Consider applicable laws and statutes before the implementation of specific fees.
2. Adopt formal policies regarding fees.
3. Calculate the full cost of providing a service in order to provide a basis for setting the fee.
4. Review and update fees periodically based on factors such as the impact of inflation, other cost increases, adequacy of cost recovery, use of services, and the competitiveness of current rates.
5. Utilize forecasting in ensuring that fees anticipate costs in providing the service.
6. Provide information on fees to the public.

Additionally, from the perspective of the Office of the State Auditor (Office):

1. Government entities must use a reasonable methodology for determining fees.
2. Government entities must track associated costs and revenues for each classification of fee imposed. For example, the revenue generated from fees for the community pool and the associated costs could be tracked together but they should be tracked separately from the revenues generated from fees for garbage disposal and their associated costs.
3. Fees may be less than actual (average per unit) cost, but not greater than.
 - a. In other words, a fee may be subsidized by the general fund but a fee should not generate excess revenue to fund activities unrelated to the fee.
 - b. The Office acknowledges certain situations in which state statute allows an assessment to generate excess revenue and provides for a mechanism for notification and transfer of those excess revenues.
4. In general, a fee may cover both direct and indirect costs of the associated activity, but a fee should not include costs that have already been paid for from other revenue sources.
 - a. For example, a fee should not include the associated cost of capital equipment or facilities that have been or are being paid for by a separate capital levy.
5. Any revenue collected from unauthorized fees should be promptly returned to those who paid those fees. The duty is on the governmental entity to return these unauthorized monies. The fee payer should not be required to request a refund.

A Fee Versus a Tax

Landmark court rulings have determined that the distinguishing attribute between taxes and fees is their use, not their name. To avoid imposing an unauthorized tax in the form of a fee, governments must use fee revenue “either to compensate the government for the provision of a specific service or benefit to the one paying the fee or to defray the government’s cost of regulating and policing a business or activity engaged in by the one paying the fee.”²

¹ gfoa.org/materials/establishing-government-charges-and-fees

² *V-1 Oil Co. v. Utah State Tax Comm’n*, 942 P.2d 906, 911 (Utah 1997), vacated in part on reh’g, 942 P.2d. 906 (Utah, Aug. 5, 1997).

From V-1 Oil v Utah State Tax Comm'n (1997):

"Generally speaking, a tax raises revenue for general governmental purposes, while a fee raises revenue either to compensate the government for the provision of a specific service or benefit to the one paying the fee or to defray the government's costs of regulating and policing a business or activity engaged in by the one paying the fee... [T]here are at least two broad types of fees: (i) a fee for service, i.e., a specific charge in return for a specific benefit to the one paying the fee, and (ii) a regulatory fee, i.e., a specific charge which defrays the government's cost of regulating and monitoring the class of entities paying the fee.

"To be a legitimate fee for service, the amount charged must bear a reasonable relationship to the services provided, the benefits received, or a need created by those who must actually pay the fee. This requirement is intended to prevent a fee from being used to generate excessive revenues and becoming indistinguishable from a tax. More specifically, for a fee for service to be reasonable, the total cost of the service so financed must fall equitably upon those who are similarly situated and in a just proportion to the benefits conferred. We do not insist on exact mathematical precision, however, in holding that a certain charge is a legitimate fee instead of a tax. The revenues raised by the fee may exceed the precise cost of providing the service to those paying the fee, yet the fee may be reasonable as long as its reasonableness can be determined in some other manner. The nature of the service or benefit provided may also make it difficult or impossible to distribute the services or benefits equally to all who pay the fee. For such a fee to be reasonable, we have directed that it should be fixed so as to be equitable in light of the relative benefits conferred as well as the relative burdens imposed. Id. Thus, if the fee bears no reasonable relationship to some need created by the one paying the fee...or if the services provided through the fee are not of "demonstrable benefit" to the one paying the fee...then the fee is likely to be unreasonable and, hence, illegitimate.

"...a regulatory fee must bear some reasonable relationship to the cost of the thing said to justify its imposition, in this instance, the costs of regulating the industry that pays the surcharge."

Additional Public Education Restrictions

The Utah Constitution (Article X, Section 2) states: "Public elementary and secondary schools shall be free, except the Legislature may authorize the imposition of fees in the secondary schools." The Office of the Legislative Auditor General recently released audit report 2018-09 titled "A Performance Audit of Secondary School Fees" (le.utah.gov/audit/18_09rpt.pdf). The audit provides evidence that various secondary schools have not fully complied with state statute related to "school fees".

A local education agency (LEA) should avoid any methodology for determining fees which could result in constitutional, statutory or regulatory concerns. For example, the Office would question the appropriateness of including teacher compensation costs when computing a school fee for a curricular class.

Since the calculation (and any approval) of a fee occurs prior to and independent of any application of a fee waiver, a fee may not be inflated for the actual or estimated cost of any fee waiver(s). A fee waiver should be paid from other appropriate sources.

See state statute and Utah State Board of Education rules for more information.