

**CITY OF HAMILTON
PERFORMANCE AUDIT REPORT 2013-14
UNLICENSED BUSINESSES**

Background

The City of Hamilton website identifies "the primary purpose of a license is to protect the health and safety of the public who use the service. It also helps ensure consistency for business owners and customers."

Part IV of the *Municipal Act, 2001* allows for the enactment of by-laws to license, regulate and govern businesses and to impose conditions on the obtaining, holding and keeping of licenses to carry on such businesses.

The City of Hamilton has a Licensing By-law (By-law #07-170, including subsequent amendments) that provides the rules and regulations for all business categories including establishment licenses.

One of the initial projects approved by Council in April, 2013 for the Value for Money Audit program was the review for unlicensed businesses.

Objectives

Most businesses in Hamilton require a license to operate legally. Additional revenue may be realized by identifying unlicensed businesses. Unlicensed businesses include:

- Businesses that are currently operating within the City that have not obtained a proper business license; and
- Businesses that have not renewed their business licenses but continue to operate without a current business license.

The objectives of this review were:

- To identify other potential databases from other City of Hamilton operations that capture business names, addresses or owners to compare against the Licensing database;
- To identify businesses that are recorded on other City of Hamilton databases but are not captured in the Licensing database; and
- To calculate the potential revenue opportunities that may be realized if the unlicensed businesses were to become licensed.

Scope

The selection of business license categories was based upon those categories with:

- The greatest number of existing businesses;
- The largest total current revenue; and,
- The availability to access other databases to obtain comparative data to match against the Licensing database.

The resulting four categories selected were public garages, aesthetic services, eating establishments and food shops and cigarette and tobacco retailers.

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Methodology

The work that was performed by Audit Services involved comparisons of the Licensing database against other City of Hamilton databases that capture comparable data with respect to the identification of businesses in the license categories that were reviewed. These comparisons were done through both a manual matching process and through the use of the capabilities within Excel software.

More specifically, the work included:

1. The identification of other City activities and their respective databases suitable for comparison against the Licensing database:
 - Areas with comparative data were Public Health, Fire Services and Taxation;
 - The database information was obtained in an Excel format for ease of analysis; and
 - Comparable fields that may be compared against the Licensing database were determined.

2. Data comparison:
 - Manually compare:
 - Public Garage – Fire versus Licensing
 - Personal Aesthetic Services – Public Health versus Licensing
 - Use of the capabilities in Excel to perform comparisons:
 - Public Garage – Fire versus Licensing
 - Public Garage – Taxation versus Licensing
 - Personal Aesthetic Services – Public Health versus Licensing
 - Eating Establishments and Food Shops – Public Health versus Licensing
 - Eating Establishments and Food Shops – Fire versus Licensing
 - Eating Establishments and Food Shops – Taxation versus Licensing
 - Cigarette/Tobacco Sales – Public Health (Convenience Stores) versus Licensing
 - Cigarette/Tobacco Sales – Tobacco Information System versus Licensing
 - For Eating Establishments, potential duplicate unlicensed businesses identified in both Public Health, Fire and/or Taxation were eliminated.
 - For Cigarette/Tobacco, potential duplicate unlicensed businesses identified in both Public Health (Convenience Stores) and the Tobacco Information System were eliminated.

Audit Services conducted this audit in conformity with the *International Standards for the Professional Practice of Internal Auditing*. These standards require that Audit Services plan and perform the audit to obtain sufficient, appropriate evidence to support the findings and conclusions based on the audit objectives. Audit Services believes that the work performed provides a reasonable basis for the audit findings and conclusions.

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Findings

The testing identified a considerable number of businesses that were in operation per inspections performed by Fire Services and Public Health (Food Safety, Personal Services and Tobacco Control) and via the Tax Roll of Taxation Services. However, several of these businesses were not included in the Licensing database and, therefore, were potentially operating without a proper license.

The results of the fieldwork are summarized below.

Per the Licensing database received on May 27, 2013, there were 4,014 establishment licenses issued. The following table provides a perspective on the number of active business licenses issued as of May 27, 2013 for the four license categories selected for review.

TABLE 1

Business License Category	Number of Licenses as of May 27, 2013	License Category as a Percentage of the Total Establishment Licenses Issued
Public Garages	755	18.8%
Aesthetic Services	585	14.6%
Eating Establishments and Food Shops	1,075	26.8%
Cigarette/Tobacco	572	14.3%
TOTAL	2,987	74.5%

The review found **684** businesses that did not appear to be licensed which could result in a **potential gross revenue opportunity of \$129,849** if they were all to become properly licensed at the current license fee rates.

Additional potential gross revenue could also be generated from:

- New license set-up fee of \$60.00 per license, generating as much as an additional **\$41,040 in one-time revenue.**
- Mandatory inspections required for any unlicensed businesses such as eating establishments that appeared on the Health database but not on the Fire database or vice versa. These additional inspection fees would be generated annually, bi-annually or every three years, as required. The related additional revenue was not calculated as part of this review.

It should be noted that these dollar amounts are gross and any costs that might need to be incurred to carry out the licensing and inspection processes have not been calculated at this time.

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Most of the additional revenue garnered from licensing these businesses will be realized on an on-going basis to the City of Hamilton (as long as the businesses continue to operate) since the cost of renewing licenses is the same as the cost of obtaining new licenses.

TABLE 2

Business License Category	Number of Unlicensed Businesses Found	Unlicensed Businesses as a Percentage of the Total Number of Businesses in the Business License Category
Public Garages	153	16.9%
Aesthetic Services	168	22.3%
Eating Establishments and Food Shops	300	21.9%
Cigarette/Tobacco	63	10.0%
TOTAL	684	18.7%

TABLE 3

Business License Category	Business License Fee (1)	Number of Unlicensed Businesses Found (2)	Potential New Revenue (1)x(2)=(3)	2013 Actual Revenue (4)	Uncollected Revenue as a Percentage of Potential Total Revenue (3)/(3)+(4)
Public Garages	\$187	153	\$ 28,611	\$114,977	19.9%
Aesthetic Services	\$165	168	\$ 27,720	\$ 86,419	24.3%
Eating Establishments and Food Shops	\$164*	300	\$ 49,200	\$258,628	16.0%
Cigarette/Tobacco	\$386	63	\$ 24,318	\$156,334	13.5%
TOTAL		684	\$129,849	\$616,358	17.4%

* NOTE: There are three license fees for Eating Establishments depending on the type of business in this category. The majority of the unlicensed businesses do not sell alcohol so the lowest licencing fee of \$164 was applied for the calculation. Therefore, the potential revenue could actually be higher.

Two main stakeholder groups of Business Licensing should be considered.

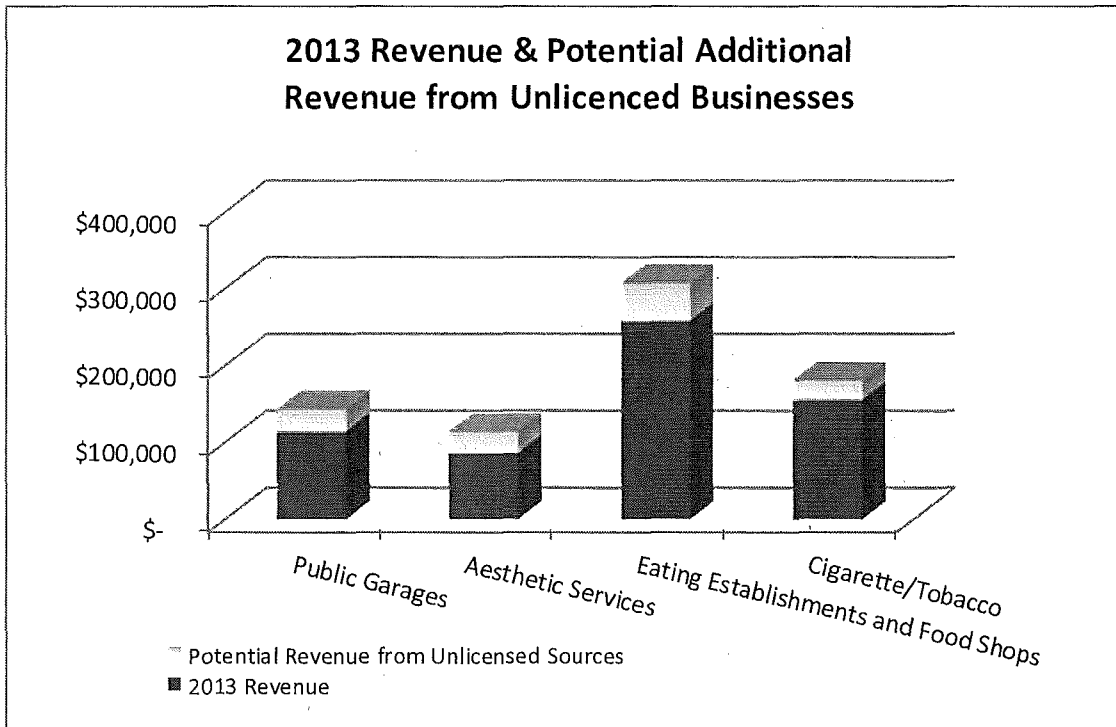
The citizens of Hamilton are interested in:

- Ensuring that the health and safety of those that use a particular service are protected; and
- Obtaining revenue from businesses that are operating such that the costs of running the Business Licensing office's services are appropriately recovered so that these costs are not borne by the general tax levy.

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Businesses that are currently compliant with the Licensing By-law need assurance that:

- There is not an unfair advantage provided to their competitors that are not properly licensed with respect to the costs of the licensing fees and various required inspection fees as well as avoidance of any potential costs to bring the businesses into compliance; and
- The reputation of their industry is not negatively impacted by businesses not monitored to ensure the health and safety of their customers.



There are over 300 businesses with multiple establishment licenses. The current practice for this licensing is to only charge the business the cost of the most expensive license involved in the multiple establishment license. However, additional costs are incurred by the City in managing and monitoring the establishments for each licensable activity performed by the business. There is an opportunity to collect additional revenues from such businesses.

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Recommendations

The implementation of the following recommendations may result in opportunities to realize additional licensing revenues within the authority of the *Municipal Act* and through full cost recovery using appropriate levels of licensing fees.

1. That Licensing investigate the discrepancies identified as a result of this review and initiate actions to license all businesses that are currently operating without a license.

Management Action Plan

Agreed in principle but not practical. Based on other safety related priorities and on the current staffing levels (internal administration as well as Licencing and Permit Officers), current workload and technology improvements required in the AMANDA database, this investigation and enforcement cannot be undertaken without additional FTEs – AMANDA support, Licencing and Permits Officers and Administrative staff. As noted in the report above, not all of the 684 potential business licenses are likely to be obtained due to use not permitted under zoning, Building Code constraints, criminal record checks, Public Health Inspection, Fire Inspection, etc. However, the determination can only be completed where staff resources are available to undertake the work.

2. That similar analysis as was performed in this review using existing software capabilities to uncover potentially unlicensed businesses be carried out annually.

Management Action Plan

Agreed in principle but not practical. Based on current staff levels (internal administration as well as Licencing and Permit Officers), current workload and technology improvements required in the AMANDA database, this investigation and enforcement cannot be undertaken without additional FTEs.

3. That a common address database be developed in conjunction with Licensing, Public Health, Fire Services and Taxation. Initial activities should include the use of common nomenclature to enable efficient search capabilities (e.g. using N for North, St. for Street, etc.). The recommended nomenclature changes should be incorporated into the future Amanda upgrade project. A common database employed by multiple users would provide more efficiencies throughout the City departments.

Management Action Plan

Disagreed. Each area has a database which is proprietary to their specific operational needs. Although there has been some data conversion for Hansen and AMANDA, it is understood that this is a corporate priority beyond that which can be resolved solely by Parking and By-law Services.

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4. That the cost recovery analysis be completed and, as a minimum, the license fees be increased according to the Business Licensing Fee Review Report presented to the Planning and Economic Development Committee on August 14, 2012. This action would continue to close the gap between the licensing expenses incurred and the revenue being collected in order to achieve full cost recovery in accordance with the provisions of the *Municipal Act, 2001*.

Management Action Plan

Agreed in principle. However, prior Council direction did not support full cost recovery for all business license fees. In March 2012, in response to a Council direction for business license fees to be based on full cost recovery, a report was presented to Planning Committee with the proposed fees. Planning Committee approved full cost recovery for 24 of 91 business license categories and directed staff to review a phase-in plan for the increase in fees. Recommendations for cost recovery of business license fees have been presented to Planning Committee on August 14, 2012, January 15, 2013 and September 17, 2013 which have resulted in the first three years of the five year equal fee increase phase-in having been approved. The last report also recommended holding off on any further increases until such time as this audit report was completed.

5. That the City of Hamilton consider eliminating the multiple establishment license type and require that businesses purchase licenses for each type of licensable activity that the businesses operate.

Management Action Plan:

Disagreed. This disagreement is based on the fact that this type of license (multiple establishment) was recently implemented (2009) and that there has been resistance to obtaining full cost recovery. A report was presented to Planning Committee in January 2009 which recommended to Council that multiple licenses for businesses associated with the same business only be charged the higher license fee and any inspections fees, with the exception of tobacco vendor license. Based on Council not approving full cost recovery of the business license fees for all categories and the Council discussion that the fees seem high for small businesses, it would be difficult to recommend the additional costs to a business at this time.

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Conclusion

In the detailed review of the top four Business and Establishment License category types, Audit Services found 684 businesses that appeared not to be properly licensed. Licensing these businesses at the current license rates could generate an additional \$129,849 in gross revenue plus \$41,040 in new license setup fees, totalling \$170,889. There are also opportunities to collect inspection fees by Fire Services for those businesses that were identified in the Public Health comparison testing and vice versa, where appropriate. These revenues would not be attributed to Licensing but would offset costs in the other respective departmental budgets. It should also be noted that the \$129,849 would be an annual recurring benefit to the City of Hamilton as the cost to renew a license is the same as the cost to obtain a new license. All new revenues are at gross and would have to be netted against any new costs to enforce the licensing as per the recommendations. It should also be noted that the City of Hamilton may not be able to issue a license to all of the identified unlicensed business as there may be issues of zoning (related to whether the business is permitted to operate at its current location), building (whether a building permit exists to establish the use at the site), proper corporate papers, criminal checks, etc.

There is also a potential for additional revenues if the City of Hamilton were to reconsider and modify its practice with respect to Multiple Establishment licenses i.e. require businesses to purchase licenses for each licensable activity that is carried out at an establishment instead of just one Multiple Establishment license.