

Internal Audit Department

O R A N G E C O U N T Y
6th Largest County in the USA

Internal Control Audit: TREASURER-TAX COLLECTOR – \$5.3 BILLION TAX COLLECTION AND CASH RECEIPT PROCESSES

For the Period July 1, 2009
through June 30, 2010

Critical
Impact
Audit

\$5.3 BILLION IN TAX
COLLECTIONS AND CASH
RECEIPTS PROCESSED
ANNUALLY

At the direction of the Board of Supervisors, we audited the Treasurer-Tax Collector Tax Collection and Cash Receipt processes and the controls regarding tax refunds and the cancellation of penalties charged for late payments on property taxes. We found controls were adequate to ensure Tax Collections and Cash Receipts were received, recorded, deposited, and reconciled timely, completely and accurately.

However, we noted significant improvements are required in the controls over penalty cancellations charged for late payments of property taxes. We identified five (5) Significant Control Weaknesses to improve penalty cancellation controls and processes.

In addition, we identified three (3) Control Findings for approving penalty cancellations and tax refunds, and accountability over “trouble checks;” two (2) Control Findings for efficiency/effectiveness issues; and three (3) Control Findings for issues concerning a bankruptcy interest fund, parking expenditures, and calculations of fees charged by the Treasurer-Tax Collector.

AUDIT NO: 2954
REPORT DATE: FEBRUARY 15, 2011

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RISK BASED AUDITING

GAO & IIA Peer Review Compliant – 2001, 2004, 2007, 2010



American Institute of Certified Public Accountants Award to Dr. Peter Hughes as 2010 Outstanding CPA of the Year for Local Government



2009 Association of Certified Fraud Examiners’ Hubbard Award to Dr. Peter Hughes for the Most Outstanding Article of the Year – Ethics Pays



2008 Association of Local Government Auditors’ Bronze Website Award



2005 Institute of Internal Auditors’ Award for Recognition of Commitment to Professional Excellence, Quality, and Outreach

 ORANGE COUNTY BOARD OF SUPERVISORS'
Internal Audit Department

GAO & IIA Peer Review Compliant - 2001, 2004, 2007, 2010

Providing Facts and Perspectives Countywide

RISK BASED AUDITING

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Letter from Dr. Peter Hughes, CPA

Transmittal Letter



Audit No. 2954 February 15, 2011

TO: Members, Board of Supervisors
Shari L. Freidenrich, Treasurer-Tax Collector

FROM: Dr. Peter Hughes, CPA, Director
Internal Audit Department

SUBJECT: Internal Control Audit: Treasurer-Tax
Collector – \$5.3 Billion Tax Collection and
Cash Receipt Processes

We have completed an Internal Control Audit of the Treasurer-Tax Collector Tax Collection and Cash Receipt Processes and the controls regarding tax refunds and the cancellation of penalties charged for late payments on property taxes for the period July 1, 2009 through June 30, 2010. We audited tax collections and cash receipts processed during April 2010 when the 2nd secured property tax installment payments were due. We performed this audit as directed by the Board of Supervisors on March 16, 2010 and in accordance with our *FY 2010-11 Audit Plan and Risk Assessment* approved by the Audit Oversight Committee and the Board of Supervisors. Our final report is attached for your review.

Please note we have a structured and rigorous **Follow-Up Audit** process in response to recommendations and suggestions made by the Audit Oversight Committee (AOC) and the Board of Supervisors (BOS). As a matter of policy, our **first Follow-Up Audit** will begin at six months from the official release of the report. A copy of all our Follow-Up Audit reports is provided to the BOS as well as to all those individuals indicated on our standard routing distribution list.

The AOC and BOS expect that audit recommendations will typically be implemented within six months and often sooner for significant and higher risk issues. Our **second Follow-Up Audit** will begin at six months from the release of the first Follow-Up Audit report, by which time **all** audit recommendations are expected to be addressed and implemented.

At the request of the AOC, we are to bring to their attention any audit recommendations we find still not implemented or mitigated after the second Follow-Up Audit. The AOC requests that such open issues appear on the agenda at their next scheduled meeting for discussion.

Letter from Dr. Peter Hughes, CPA

We have attached a **Follow-Up Audit Report Form**. Your department should complete this template as our audit recommendations are implemented. When we perform our first Follow-Up Audit approximately six months from the date of this report, we will need to obtain the completed document to facilitate our review.

Each month I submit an **Audit Status Report** to the BOS where I detail any material and significant audit findings released in reports during the prior month and the implementation status of audit recommendations as disclosed by our Follow-Up Audits. Accordingly, the results of this audit will be included in a future status report to the BOS.

As always, the Internal Audit Department is available to partner with your staff so that they can successfully implement or mitigate difficult audit recommendations. Please feel free to call me should you wish to discuss any aspect of our audit report or recommendations.

Additionally, we will request your department complete a **Customer Survey** of Audit Services. You will receive the survey shortly after the distribution of our final report.

ATTACHMENTS

Other recipients of this report are listed on the **OC Internal Auditor's Report** on page 5.

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Audit No. 2954

February 15, 2011

Audit Highlight

-Good News-

We found controls were adequate to ensure Tax Collections and Cash Receipts were received, recorded, deposited, and reconciled timely, completely and accurately.

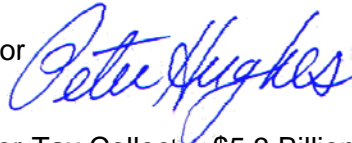
We also found controls were adequate over all other types of tax payment methods, such as payments received via the Remittance Processing System (mail payments), credit card payments, internet payments, electronic fund transfers and bank payments.

-Improvements Needed-

Significant improvements are needed regarding cancellation of penalties charged for late tax payments. We found **five Significant Control Weaknesses** and made recommendations to improve controls and processes in this area.

We also identified **three Control Findings** for approving penalty cancellations/tax refunds, and improving accountability over "trouble checks;" **two Control Findings** for efficiency/effectiveness issues; and **three Control Findings** for issues concerning a bankruptcy interest fund, parking expenditures, and calculation of fees charged by the Treasurer-Tax Collector.

TO: Members, Board of Supervisors
Shari L. Freidenrich, Treasurer-Tax Collector

FROM: Dr. Peter Hughes, CPA, Director
Internal Audit Department 

SUBJECT: Internal Control Audit: Treasurer-Tax Collector \$5.3 Billion
Tax Collection and Cash Receipt Processes

OBJECTIVES

By direction of the Board of Supervisors, the Internal Audit Department conducted an Internal Control Audit of the Treasurer-Tax Collector's Tax Collection and Cash Receipt processes and the internal controls involved with penalty cancellations and tax refunds.

Our audit included evaluating the adequacy and integrity of internal controls; ensuring compliance with Treasurer-Tax Collector and County policies; the California Revenue & Taxation Code; inquiring about fraud prevention and detection programs and policies, and examining processes within the department for issues related to efficiencies and effectiveness.

Our audit was conducted in conformance with professional standards established by the Institute of Internal Auditors. The five objectives of this audit were to:

1. Evaluate controls to ensure Tax Collections and Cash Receipts are received, recorded, deposited, and reconciled timely, completely, and accurately.
2. Evaluate controls over Penalty Cancellations and Tax Refunds to ensure these obtained proper authorization and followed policy compliance.
3. Ensure Tax Collections and Cash Receipts are safeguarded from receipt until deposit, including testing vault procedures; ensuring transfers of accountability are documented; and ensuring adequate segregation of duties.
4. Evaluate controls over all other types of tax payment methods, such as payments received via the Remittance Processing System (mail payments), credit card payments, internet payments, electronic fund transfers, and bank payments.
5. Determine if Tax Collection and Cash Receipt processes are efficient and effective (no significant backlogs, duplication of work, or manual processes that could be automated).
6. Evaluate other issues concerning a bankruptcy interest fund, parking validations, and fee calculations that came to our attention.



BACKGROUND

On March 16, 2010, the Board of Supervisors delegated the investment authority and functions from the elected Treasurer-Tax Collector to the Chief Financial Officer (CFO) in the County Executive Office and authorized the CFO "...to assume that authority and approve other directions necessary to implement this action..." This action was taken in response to a U.S. Bankruptcy Judge's ruling in March 2010 against the elected Treasurer-Tax Collector where the judge found he had breached his fiduciary duty with the trust of the bankrupt Fruehauf Trailer Corporation. The Board of Supervisors, citing concerns with the tax collection and cash receipting functions remaining with the Treasurer-Tax Collector, directed the "Internal Auditor to audit the Treasurer-Tax Collector's Tax Collections and Cash Receipts policies."

The Treasurer-Tax Collector department is comprised of the following sections/divisions:

- **Administrative Executive Management:** includes the elected Treasurer-Tax Collector, two Executive Assistants and clerical support. Also includes three Assistant T-TC management positions and provides administrative functions such as budget, human resources, payroll, and procurement. Business Process Improvement and Information Technology are also under this section.
- **Treasurer Division:** includes Investments, Accounting, Cash Management, and Compliance sections. This function was recently delegated to the Chief Financial Officer.
- **Tax Collector Division:** includes cashiering operations for tax collections, the Remittance Processing Section for mail payments, a Bankruptcy section for taxpayers that have declared bankruptcy, a Redemption section for prior year's taxes, a Delinquent Collections section for pursuing past due taxes, and a Tax Information unit. The Remittance Processing Section and cashiering operations have been moved organizationally and now report to the Chief Assistant Treasurer-Tax Collector, who reports to the Chief Financial Officer.

Sources of Tax Collections

The Treasurer-Tax Collector Cashiering Section receives and processes tax payments **over-the-counter** (OTC) in which payments are entered into the cashiering system. The Remittance Processing Section receives and processes tax payments made by **mail**. Other tax payment methods include **credit card payments (OTC, phone and Web), electronic fund transfers (EFTs), Automatic Clearinghouse (ACH) debits, and payments sent from banks for tax receivables and for CORTAC (mortgage impound accounts)**. For FY 2008-09, the Treasurer-Tax Collector received about **\$5.3 billion** in tax collections and cash receipts.

SCOPE

Our audit evaluated internal controls and processes over Tax Collections and Cash Receipts in the Treasurer-Tax Collector from July 1, 2009 through June 30, 2010. Our scope included the following areas:

- We observed and tested a sample of tax collections and cash receipts on April 9th and 12th, 2010, which were the days before and after the April 10th due date for the 2nd secured property tax installment payment. This tax deadline is one of two busy periods for tax collections, the other being every December 10th.



- We tested and validated 100% of tax collections and cash receipts received on April 9th and 12th by agreeing collection detail records and cashiering reports to bank deposit records. We also tested reconciliations of the cash drawers and vault contents to amounts recorded in the cashiering system and in County records.
- We observed and tested a sample of mail payments received via the Remittance Processing section where tax collections are received and processed.
- We tested and validated all other types of payment methods for tax collections, such as credit cards, EFTs, bank receivables and impounds, and web based payments.
- We observed and tested controls to safeguard tax collections and receipts; such as, segregation of duties; establishing accountability when monies are transferred between employees; restricting access to the cash cage and vault; and cash drawer and vault balancing procedures to ensure bank deposits are accurate and complete.
- We audited tax refund and penalty cancellation controls to ensure they are in compliance with all legal requirements and were properly authorized.
- We conducted 10 interviews with management and staff about the risk of fraud; communicating ethical behavior; programs and controls to prevent/detect fraud; and to discover if actual, alleged, or suspected fraud has been observed.
- We evaluated the efficiency/effectiveness of tax collections and cash receipts for significant backlogs, duplicated work, or manual processes that could be automated.

SCOPE EXCLUSIONS

Our audit scope did not cover the following areas:

- Prior Year Taxes and Delinquent Payments: Although we obtained an understanding of prior year tax payments and delinquent payments, we only included current year tax collections refunds, and penalty cancellations in this audit. Prior year payments and delinquent payments are addressed in a separate Tax Redemption Office audit that we conduct every three years.
- Cashiering System and Assessment Tax System (ATS) Controls: We did not include a review of cashiering system controls or ATS controls in this audit. Other audits have been conducted on these systems, including a recent audit of the Treasurer-Tax Collector's electronic funds transfer processes and systems (Audit No. 2821).
- Treasury Investment Function: We did not include a review of the investment function except for cashiering and remittance processing.

SUMMARY CONCLUSION

The following shows the results of our audit. See further discussion in the *Detailed Findings, Recommendations and Management Responses* section of this report. See *Attachment A* for a description of Report Item Classifications.



▶ **Objective #1** – Evaluate controls to ensure Tax Collections and Cash Receipts are received, recorded, deposited, and reconciled timely, completely, and accurately.

▶ **Results:** We found controls are adequate and effective to provide reasonable assurance that tax payments are received, recorded, deposited, and reconciled timely, completely and accurately in all material regards. No exceptions were noted. **As such, we have no recommendations under this objective.**

▶ **Objective #2** – Evaluate controls over Penalty Cancellations and Tax Refunds to ensure these obtained proper authorization and policy compliance.

▶ **Results:** We identified **five (5) Significant Control Weaknesses** and **two (2) Control Findings** to improve controls and processes over penalty cancellations and tax refunds. (See Finding Nos. 1 through 7 below).

▶ **Objective #3** – Ensure that Tax Collections and Cash Receipts are safeguarded from receipt until deposited, including testing of vault procedures; ensuring transfers of accountability are documented; and ensuring adequate segregation of duties.

▶ **Results:** We found that controls over tax collections and cash receipts are adequate and effective to provide reasonable assurance the receipts are properly safeguarded in all material regards, including compliance with vault procedures, documented transfers of accountability, and proper segregation of duties. We noted an exception concerning “trouble checks” in the Remittance Processing Section where we identify **one (1) Control Finding** to improve controls. (See Finding No. 8 below.)

▶ **Objective #4** – Evaluate controls over all other types of tax payment methods such as payments received via Remittance Processing System (mail payments), credit card payments, internet payments, electronic fund transfers, and bank payments.

▶ **Results:** We found that controls are adequate and effective to provide reasonable assurance that other methods for tax payments were recorded, deposited, and reconciled timely, completely, and are safeguarded until deposited in all material regards. No exceptions were noted. **As such, we have no recommendations under this objective.**

▶ **Objective #5** – Determine if the Tax Collection and Cash Receipts processes are efficient and effective (no significant backlogs, duplication of work, or manual processes that could be automated).

▶ **Results:** We found tax collection and cash receipt processes are efficient and effective with no backlogs, duplication of work or manual processes that could benefit from automation. We identified **two (2) Control Findings** to evaluate the benefit of opening for tax collections on Saturdays, and the policy for accepting and/or rejecting partial/short tax payments. (See Finding Nos. 9 and 10 below.)

▶ **Other Issues Brought to Our Attention:** Issues concerning a bankruptcy interest fund, expenses for parking validations, and fee calculations were identified during the audit when conducting interviews of Treasurer-Tax Collector management and staff.

▶ **Results:** We identified **three (3) Control Findings** to address issues concerning use of bankruptcy interest, expenses for parking validations, and fee calculations. (See Finding Nos. 11 through 13 below.)



Management's Responsibilities for Internal Controls

In accordance with the Auditor-Controller's County Accounting Manual section S-2 *Internal Control Systems*, "All County departments/agencies shall maintain effective internal control systems as an integral part of their management practices. This is because management has primary responsibility for establishing and maintaining the internal control system. All levels of management must be involved in assessing and strengthening internal controls." **Control systems shall be continuously evaluated (by Management) and weaknesses, when detected, must be promptly corrected.** The criteria for evaluating an entity's internal control structure is the Committee of Sponsoring Organizations (COSO) control framework. Our Internal Control Audit enhances and complements, but does not substitute for the Treasurer-Tax Collector's continuing emphasis on control activities and self-assessment of control risks.

Inherent Limitations in Any System of Internal Control

Because of inherent limitations in any system of internal controls, errors or irregularities may nevertheless occur and not be detected. Specific examples of limitations include, but are not limited to, resource constraints, unintentional errors, management override, circumvention by collusion, and poor judgment. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or the degree of compliance with the procedures may deteriorate. Accordingly, our audit would not necessarily disclose all weaknesses in the Treasurer-Tax Collector's operating procedures, accounting practices, and compliance with County policy.

Acknowledgment

We appreciate the courtesy extended to us by the Treasurer-Tax Collector and staff during our audit. If we can be of further assistance, please contact me directly; or Eli Littner, Deputy Director at 834-5899; or Michael Goodwin, Senior Audit Manager at 834-6066.

Attachments

Distribution Pursuant to Audit Oversight Committee Procedure No. 1:

Members, Board of Supervisors
Members, Audit Oversight Committee
Thomas G. Mauk, County Executive Officer
Bob Franz, Deputy CEO, Chief Financial Officer
Paul Gorman, Chief Assistant Treasurer-Tax Collector
Jennifer Burkhart, Assistant Treasurer-Tax Collector
Kim Hansen, Cash Manager, Treasurer-Tax Collector
Daniel Puglia, Budget Manager, Treasurer-Tax Collector
Foreperson, Grand Jury
Darlene J. Bloom, Clerk of the Board of Supervisors



Audit Objective #1

Our objective was to evaluate controls to ensure Tax Collections and Cash Receipts are received, recorded, deposited, and reconciled timely, completely, and accurately.

AUDIT STEPS AND RESULTS

Over-the-Counter Tax Collections

To accomplish this objective, we audited the 2nd installment of secured property taxes (due April 10th) that were received over-the-counter (OTC) and performed the following:

- ✓ Observed walk-in customers paying tax payments on April 8th and April 12th for the 2nd installment deadline of April 12th. We selected **twenty-five (25) tax payments totaling \$43,357** from the two days for testing.
- ✓ We traced and agreed the above payments to the taxpayer parcel and payment information to the T-TC cashiering and account detail reports, ensured the payments were recorded to the correct parcel number, and tested the accuracy of currency counters used in counting cash payments and deposits. For the two (2) sample days, we also observed that:
 1. Tax payments were scanned, restrictively endorsed, and imaged upon receipt.
 2. Cashiers cannot observe their drawer balances minimizing the risk of loss or theft.
 3. Only a limited number of supervisors/managers can void transactions.
 4. Transfer of accountability of cash receipts and checks is documented in writing.
 5. Cash handling duties were properly segregated to avoid incompatible duties.
 6. Cash counts and cashier closing procedures were performed as required.
 7. Tax collections and cash receipts agreed to daily bank deposits.
 8. Daily reconciliations were performed to account for all collections and deposits.
- ✓ See [Audit Objective No. 3](#) regarding additional audit steps we performed related to this objective.

CONCLUSION

We found controls are adequate and effective to provide reasonable assurance that tax payments are received, recorded, deposited, and reconciled timely, completely and accurately in all material regards. No exceptions were noted in our observation and testing of tax payments for the two (2) sample days.

DETAILED AUDIT FINDINGS AND RECOMMENDATIONS

We have no audit findings or audit recommendations under Audit Objective #1.



Audit Objective #2

Our objective was to evaluate controls over Penalty Cancellations and Tax Refunds to ensure these obtained proper authorization and policy compliance.

AUDIT STEPS AND RESULTS

Penalty Cancellations and Tax Refunds

We audited controls to determine whether penalty cancellations and tax refunds are appropriate, properly authorized, accurate, and made in full compliance with the California Revenue & Taxation Code. We reviewed internal written policies, procedures, and guidelines; we obtained lists of employees authorized to make tax refunds and penalty cancellations; and reviewed the related criteria in the Revenue & Taxation Code.

Penalty Cancellations: The penalty amount for current year late tax payments is 10% annually. The penalty amount assessed for prior year (redemption) late tax payments is 1.5% of the defaulted amount calculated monthly which equates to an 18% per year interest charge. The Treasurer-Tax Collector uses criteria under Revenue & Taxation Code *Section 4985.2* to approve penalty cancellations in the following instances:

- (a) Failure to make a timely payment is due to reasonable cause and circumstance beyond the taxpayer's control, and occurred notwithstanding the exercise of ordinary care in the absence of willful neglect, provided the principal for the proper amount of the tax due is made....
- (b) There was an inadvertent error made in the amount of payment made by the taxpayer, provided the principal payment for the proper amount of the tax due is made within 10 days after the notice of shortage is mailed by the tax collector.
- (c) The cancellation was ordered by a local, state, or federal court.

For FY 2009-10, the following penalty cancellations were processed based on reports generated from Assessment Tax System (ATS):

- Current Year Secured: **21,382 penalty cancellations totaling \$1,491,359**
- Current Year Unsecured: (ATS could not readily provide this information)
- Redemption (delinquent): **3,667 penalty cancellations totaling \$1,088,017**
- Bankruptcy: (ATS could not readily provide this information)

Note: Because of system limitations, we could not obtain a total count or dollar amount of penalty cancellations. We estimated that there was approximately **\$7,440,575** in refunded penalties (see below under Tax Refunds), but this does not include penalties that were cancelled but were not paid, and did not result in a refund.

For testing, we obtained **three (3) penalty cancellations totaling \$382,866** that the Treasurer-Tax Collector was personally involved in authorizing. We also requested the following **six (6) penalty cancellations**. Our findings are noted below:

- #93 06-000037 for **\$20,668**, dated 11/10/09 - (Bankruptcy)
- #93 07-013599 for **\$298,500**, dated 2/17/10 - (Bankruptcy)
- #93 07-021321 for **\$28,985**, dated 7/16/09 - (Redemption)
- #93 08-027097 for **\$14,783**, dated 10/3/09 - (Redemption)
- #93 08-028104 for **\$4,894**, dated 9/10/09 - (Redemption)
- #93 08-028105 for **\$4,894**, dated 9/8/09 - (Redemption)

Detailed Results, Findings, Recommendations and Management Responses



Tax Refunds: Refunds are made to taxpayers when the following “events” are established in ATS. ATS automatically processes the refunds based on the event and generates reports showing the tax refunds for management review.

- Duplicate payments – when installments are paid more than once.
- Overpayments – amount paid is in excess of installment due.
- Corrected bill – when a taxpayer pays the full tax amount, then appeals to have assessed value of property lowered. If approved, the assessed value is lowered resulting in a lower tax and a refund to the taxpayer.
- Roll corrections – when the Assessor adjusts the tax roll to a lower amount, the event creates a refund.
- Underpayments – when an installment payment is less than the amount due. The short or partial payment is not processed but refunded instead.

For FY 09-10, we determined there were **89,689 miscellaneous tax refunds** issued totaling **\$148,811,489**. Miscellaneous tax refunds are comprised of penalty cancellations, Assessor roll corrections, payments on the wrong parcels, duplicate payments, overpayments, and short payments. We were informed that about 5% or less of the total refunds are from penalty cancellations (5% of \$148,811,489 = **\$7,440,575**), but this was provided as an estimated amount because the current ATS system could not provide a report of all penalty cancellations.

We tested **twenty (20) tax refunds totaling \$242,374**. No exceptions were noted except that there is currently no ATS online approval process for tax refunds (see Finding No. 7).

CONCLUSION

Significant improvements in the controls and process are required for penalty cancellations. We identified **five (5) Significant Control Weaknesses** and **two (2) Control Findings** to improve controls and processes. Areas needing improvement include authorizing cancellations, ATS access controls, supervisory reviews, and audit trails and management reports to validate penalty cancellations are made in full compliance with the Revenue & Taxation Code. Our findings are as follows:

DETAILED AUDIT FINDINGS AND RECOMMENDATIONS

Finding No. 1 – Management Intervention in Approving Penalty Cancellations (Control Finding)

The Treasurer-Tax Collector approved two penalty cancellations after being removed from the list of authorized individuals to approve such cancellations. The penalty cancellations were for **\$280** and **\$11,514**.

The Treasurer-Tax Collector is authorized under Revenue and Taxation Code section 4985.2 to cancel delinquent tax penalties where certain defined statutory criteria are met. The Treasurer-Tax Collector’s policy authorized identified Treasurer-Tax Collector department (T-TC) officials, including the Treasurer-Tax Collector, to review and cancel penalties. From July 1, 2009 until the end of his term, the Treasurer-Tax Collector was not included on the list of officials who would review and cancel penalties. When the Treasurer-Tax Collector delegates approval authority to staff, he/she retains final authority to make the decision because of the legislative grant of this authority. In regard to this authority, penalties should only be cancelled if the reasons fully comply with the code.



After July 1, 2009, authorized T-TC officials denied requests for penalty cancellations of **\$280** and **\$11,514** because they did not believe the penalties met the criteria of section 4985.2. The Treasurer-Tax Collector intervened and canceled the penalties. Also after July 1, 2009, we noted efforts by the Treasurer-Tax Collector to approve a penalty cancellation for **\$371,072** where T-TC employees did not believe it met the statutory criteria for a penalty cancellation. However, this penalty cancellation was not ultimately approved or processed.

Recommendation No. 1

The Treasurer-Tax Collector and staff with delegated authority to cancel penalties ensure that penalty cancellations are made only when compliant with the Revenue & Taxation Code. If there is uncertainty in the criteria or their application, a County Counsel opinion should be obtained for further clarification.

Treasurer-Tax Collector Management Response:

Concur. The new Treasurer-Tax Collector's term started January 3, 2011 and she will be updating current penalty cancellation procedures so that they are consistent with and limited to those circumstances outlined in the Revenue and Taxation Code. The Treasurer-Tax Collector will complete the review and implement the revised policy, procedure and forms by March 31, 2011.

Finding No. 2 – Penalties Canceled Based on Single Authorization (Significant Control Weakness)

Penalty cancellations are authorized by individual staff based on the dollar amount of the cancellations. No additional authorized signatures based on dollar thresholds were required on the manual penalty cancellation forms.

Because of the high volume and large dollar amounts of penalty cancellations, we believe a single authorization is insufficient as an internal control. Thresholds should be established to require additional supervisory/management approvals based on the dollar amount. High-dollar penalty cancellations should require authorization by a higher level of management, such as the Chief Assistant Treasurer-Tax Collector or Treasurer-Tax Collector. Management should determine the appropriate dollar thresholds requiring additional approvals based on the volume of cancellations and staffing resources.

Recommendation No. 2

The Treasurer-Tax Collector establish dollar thresholds for requiring additional supervisory and management approvals for all penalty cancellations. For high-dollar transactions, a third level of authorization should be required by either the Chief Assistant Treasurer-Tax Collector or the Treasurer-Tax Collector.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector is updating the penalty cancellation policy, procedures and forms to provide adequate controls and appropriate levels of supervisory review and management approvals on the penalty cancellation forms. The Treasurer-Tax Collector will complete the review and implement the revised policy, procedures and forms by March 31, 2011.



Finding No. 3 – Penalty Cancellation Forms Not Consistently Prepared (Significant Control Weakness)

Our testing disclosed that manual *Request and Authorization for Penalty Cancellation* forms were not consistently prepared for each penalty cancellation. Our testing of **nine (9) penalty cancellations found that four (4) did not have a penalty cancellation form** to authorize the cancellation.

Different forms are used for current and prior year penalty cancellations. Both forms show the amount of the penalty, reason codes and descriptions (based on Revenue & Taxation Code criteria), signature lines for processing, authorization or denial, and any detailed comments. We believe these forms should be prepared for all penalty cancellations to establish accountability for preparing, reviewing and authorizing the cancellation.

Recommendation No. 3

The Treasurer-Tax Collector ensure that a *Request and Authorization for Penalty Cancellation* form be completed for all penalty cancellations.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector is updating the penalty cancellation policy, procedures and forms and updating the form to ensure there are adequate controls and proper documentation and approvals for all penalty cancellations. The Treasurer-Tax Collector will complete the review and implement the revised policy, procedures and forms by March 31, 2011.

Finding No. 4 – Excessive Staff Have Access to Cancel Penalties in ATS (Significant Control Weakness)

We noted that excessive staff are authorized to process penalty cancellations or refunds within ATS. Currently **nineteen (19) staff** can unilaterally process and grant current year secured penalty cancellations, **three (3) staff** can unilaterally process and grant prior year/redemption penalty cancellations, and **fourteen (14) staff** can unilaterally process and grant unsecured penalty cancellations.

Access and ability to process penalty cancellations should be restricted to those individuals with the job requirements to do so. Additionally, we note in our other findings the lack of management reports and audit trails in ATS for all penalty cancellations processed. Furthermore, there is no online approval feature for penalty cancellations in ATS. When system limitations are combined with numerous users who can each unilaterally access and grant penalty cancellations, the risk increases for unauthorized penalty cancellations with a small chance of discovery.

Recommendation No. 4

The Treasurer-Tax Collector evaluate the number of staff needed to process penalty cancellations and refunds and limit this function to only staff with those job responsibilities.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector is updating the penalty cancellation policy, procedures and forms to ensure proper segregation of duties consistent with staff job responsibilities. The Treasurer-Tax Collector will complete the review and implement the revised policy, procedures and forms by March 31, 2011.



Finding No. 5 – No Reports and Limited Reviews of Penalty Cancellations in ATS (Significant Control Weakness)

Management cannot generate either a partial or complete listing of penalty cancellations from ATS. Thus, management does not have a record indicating the total number, dollar amount, or name of taxpayer for penalty cancellations subject to management review. In addition, management currently only reviews a sample of penalty cancellations. Moreover, this sample is not statistically valid and the sample may or may not identify large and potentially noncompliant penalty cancellations.

When sampled penalty cancellations are reviewed, the process is completed by the section Supervisor (Redemption, Unsecured or Bankruptcy sections) through a review of a “PD30” screen in ATS. The supervisor must “screen print” each page. The supervisor prints the screens, notes which items were reviewed, and maintains the reviewed screen prints in a binder.

Recommendation No. 5

The Treasurer-Tax Collector ensure the new Property Tax Management System (PTMS) generates the necessary management reports that include a listing of the entire population of penalty cancellations. These reports should enable management to review all penalty cancellations. Additionally, the reports should be retained in accordance with the County record retention policy.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector will ensure the new Property Tax Management System (PTMS) generates the necessary reports that include a listing of the entire population of penalty cancellations. The reports will enable management review and be retained in accordance with the County record retention policy. In the interim, as PTMS will not be live until 2012, the Treasurer-Tax Collector will implement a process of randomly checking penalty cancellations as part of the new policy unless the system can generate reports. This is already in place for Redemptions and will be expanded for all waivers.

Finding No. 6 – No Audit Trails in ATS for Certain Penalty Cancellations (Significant Control Weakness)

Penalties canceled for installment payment accounts (known as “five pay”), defaulted five pays, and unsecured taxes do not leave an audit trail within ATS. Noncompliant cancellations could be processed and not detected. In addition, these types of penalty cancellations are also not reviewed by management. Moreover, when certain accounts have been paid, the transaction history is automatically deleted from ATS. Without audit trails, the risk increases in processing unauthorized or non-compliant penalty cancellations without being detected. Although it may not be feasible to address this issue in ATS, it should be a feature of new PTMS system currently under development.

Recommendation No. 6

The Treasurer-Tax Collector explore ways to develop or identify a process that captures 100% of the penalty cancellations to enable a thorough review to ensure their propriety. Additionally, the Treasurer-Tax Collector needs to ensure that audit trails are built into PTMS system and retained for all types of transactions, including the above described penalty cancellations, for purposes of monitoring and management reviews.



Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector will ensure that audit trails are built into the PTMS system and retained for all types of transactions, including penalty cancellations, for purposes of monitoring and management reviews. Collections Management has determined a process to capture 100% is not cost-effective to write in the current ATS system due to prioritization of resources focused on the PTMS project. Collections Management will update the written policy so that all penalty waivers are approved by a supervisor and randomly check for compliance in the interim.

Finding No. 7 – No ATS Online Approval of Penalty Cancellations and Tax Refunds (Control Finding)

Online supervisory approval of penalty cancellations and tax refunds was not a feature of ATS. A review of penalty cancellations is completed on a manual *Request and Authorization for Penalty Cancellation* form by selecting a sample of canceled penalties after they have been authorized. The same applies to tax refunds, except there are hardcopy documents that are reviewed after the refunds are approved. Supervisory reviews performed after the approvals are made are not effective in preventing inappropriate cancellations and refunds. Online approval of penalty cancellations and tax refunds will help to prevent inappropriate cancellations and refunds.

Recommendation No. 7

The Treasurer-Tax Collector ensure online supervisory approval of penalty cancellations and tax refunds is built into the PTMS system upgrade to enable a thorough review to ensure their propriety.

Treasurer-Tax Collector Management Response:

Concur. With the current ATS system being replaced by PTMS in the next 18 months, all experienced Treasurer-Tax Collector and Auditor-Controller programmers and contractors are being fully utilized. The current system was developed in 1987 and is now over 23 years old. IDEAL, the programming language used to code ATS, is now obsolete and has reached the end of its support life. Its vendor, Computer Associates, has stopped providing product support updates including much-needed fixes and interoperability mechanisms to adapt to newer technology. It is not cost effective to locate programmers and train them on the current ATS system to write any new code.

The Treasurer-Tax Collector will plan to add online supervisor approval of penalty cancellations and tax refunds into the PTMS system to enable a thorough review to ensure their propriety. Collections Management will update the written policy so that all penalty waivers are approved by a supervisor and randomly check for compliance in the interim.

Audit Objective #3

Our objective was to ensure that Tax Collections and Cash Receipts are safeguarded from receipt until deposited, including testing of vault procedures; ensuring transfers of accountability are documented; and ensuring adequate segregation of duties. To accomplish this objective, we observed and tested the controls that help safeguard tax collections and cash receipts.



AUDIT STEPS AND RESULTS

- Segregation of duties is adequate for staff responsible for the receipting, recording, depositing and reconciling of tax collections and cash receipts. In addition, we observed staff with no other cash handling responsibilities were assigned to help with the processing of payments during the peak tax season.
- Transfer of accountability is established when monies are exchanged between employees, during cash counts, and for daily opening/closing of cashier drawers. We noted one exception concerning mail payments and “trouble checks” received in the Remittance Processing Section discussed below in Finding No.8.
- Restrictive endorsement and imaging of check payments is performed by the cashiering system at the time of payment to the cashiers.
- Vault cash counts are conducted daily using currency counters to ensure the \$30,000 limit is not exceeded and any excess monies are deposited as required by the T-TC’s cash count procedures. No exceptions were noted on the Vault Balance Reports for the two days we tested.
- Counter cash counts are performed daily using currency counters. To ensure the accuracy of the counters, we observed the counters detected “strangers” several times during our observation. A “stranger” is a bill not of the same denomination being counted that is detected and removed during the count. Based on our observation, the currency counters appeared to be working properly.
- Voiding of payments is restricted to four supervisors/managers in the Cashiering and Remittance sections. Daily reports of voids are generated and reviewed by a supervisor.

CONCLUSION

We found that the controls are adequate over tax collections and cash receipts to provide reasonable assurance the receipts are properly safeguarded in all material regards, except for one finding concerning “trouble checks” in the Remittance Processing Section. The following is where processes and controls should be enhanced:

DETAILED AUDIT FINDING AND RECOMMENDATION

Finding No. 8 – Controls Over “Trouble Checks” (Control Finding)

There is a lack of accountability over “trouble checks” when the Remittance Processing Section distributes the checks to staff to research the appropriate application of tax payments.

The Remittance Processing Section (Remittance) processes all tax payments made by mail. Checks received in the mail with inadequate information for applying the payment (e.g., missing payment stub) are collected and identified as “trouble checks.” “Trouble checks” cannot be processed through the Remittance Processing System (RPS) as they require additional research to determine the appropriate application of the tax payment.



“Trouble checks” are accumulated daily and given to staff in either Remittance, or staff outside of the Remittance in either the Redemption or Bankruptcy units.

We noted there is no log prepared for “trouble checks” or accountability over checks leaving RPS. We were told a log of “trouble checks” is not maintained due to the volume received (**approximately 8,200 per year**).

Accountability should be established for all checks pulled for research to avoid loss or misappropriation. One option to consider is to have Remittance make a copy of the “trouble checks” for purposes of research, and deposit the actual checks into a suspense account upon receipt. This would ensure monies are accounted for and safeguarded.

Recommendation No. 8

The Treasurer-Tax Collector evaluate ways to maintain accountability and safeguard “trouble checks” received in the Remittance Processing Section. One option is to immediately deposit the trouble checks into suspense at the time of receipt to ensure they are safeguarded.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector is in discussions with our remittance processing vendor concerning a system upgrade to process “trouble checks” online while retaining accountability and safeguarding the checks in the Remittance Processing Section. In the interim treasury management will implement a manual system to maintain accountability and safeguard “trouble checks”. We expect to implement the manual system by March 31, 2011.

Audit Objective #4

Our objective was to evaluate controls over all other types of tax payment methods such as mail payments processed through the Remittance Processing System, credit card payments, internet payments, electronic fund transfers, and bank payments. To accomplish our objective, we tested a total of **\$344,315,829** in tax payments.

AUDIT STEPS AND RESULTS

- ✓ For mail payments received in Remittance Processing, we selected **mail payments for two days totaling \$50,339,043** for testing. We verified checks were restrictively endorsed, imaged, and safeguarded until deposited. We agreed amounts to remittance reports, deposit orders, daily balancing and summary reports and application to the tax payment. No exceptions were noted except for accountability over what are known as “trouble checks” ([see Finding No. 8 above](#)).
- ✓ For credit card payments made from the internet and/or by phone (IVR), we selected **receipts for two days totaling \$15,557,019** for testing. We traced and agreed the tax payments to various CAPS+ reports, Wells Fargo EDI Payment Detail reports, and to ATS reports showing the application of the tax payments. No exceptions were noted.
- ✓ For CORTAC payments received from the banks from taxpayer impound accounts, we selected **two tax payments totaling \$218,548,835** for testing. We traced and agreed the tax payments to various CAPS+ reports, bank EFT Activity download, and ATS collection reports showing the application of the tax payments. No exceptions were noted.

Detailed Results, Findings, Recommendations and Management Responses



- ✓ For Automated Clearinghouse (ACH) payments from home banking payment files where the County is authorized to access the tax payments, we selected **ACH payments for two days totaling \$55,476,561** for testing. We traced and agreed the tax payments to various CAPS+ reports, bank confirmation reports, and ACH WEB files confirming the application of the tax payments. No exceptions were noted.
- ✓ For Receivable Manager payments received from home banking files where the taxpayer instructs the bank to make the tax payments, we selected **payments for two days totaling \$4,394,371** for testing. We traced and agreed the tax payments to various CAPS+ reports, Tax Collector EFT activity reports, and Receivable Manager file reports confirming the application of the tax payments. No exceptions were noted.

CONCLUSION

We found that controls are adequate and effective to provide reasonable assurance that other methods of tax payments were recorded, deposited, and reconciled timely, completely, and accurately, and are safeguarded until deposited in all material regards. No exceptions were noted.

DETAILED AUDIT FINDINGS AND RECOMMENDATIONS

We have no audit findings or recommendations under this objective.

Audit Objective # 5

Process Efficiency/Effectiveness

Our objective was to determine if Tax Collection and Cash Receipt processes are efficient and effective (no significant backlogs, duplication of work, or manual processes that could be automated).

AUDIT STEPS AND RESULTS

We observed all key processes, conducted key interviews with management and staff and analyzed workflow processing and noted staff appeared knowledgeable, trained, organized and supervised.

CONCLUSION

We did not find any instances of significant backlogs, duplication of work, or manual processes that could benefit from automation. We do offer two recommendations for management's evaluation and consideration concerning process efficiency and effectiveness.

DETAILED AUDIT FINDINGS AND RECOMMENDATIONS

Finding No. 9 – Opening for Tax Collections on Saturday (Control Finding)

The Treasurer-Tax Collector opened on Saturday, April 10th to allow taxpayers to make tax payments due the following Monday. Seven employees, including a Sheriff Deputy assigned to the Treasurer-Tax Collector, were paid overtime to operate the office, even though a payment drop box that allows taxpayers to submit payments after hours is available. We were informed only a limited number of payments were received by staying open Saturday.



Since there is a payment drop box that allows taxpayers to submit payments after hours, and the Revenue & Taxation Code specifically extends the tax payment deadlines when the deadline occurs on a weekend or holiday, the Treasurer-Tax Collector should consider conducting an analysis to determine whether opening on Saturday is cost-effective.

Recommendation No. 9

The Treasurer-Tax Collector should analyze the cost/benefit of opening the office on Saturday when tax payments are due the following Monday.

Treasurer-Tax Collector Management Response:

Concur. With additional online payment options available and a payment drop box for after-hour payments, the Treasurer-Tax Collector discontinued the opening of the office on Saturday effective December 2010.

Finding No. 10 – Acceptance of Partial/Short Tax Payments (Control Finding)

During our annual Risk Assessment, the Chair of the Board of Supervisors inquired about the Treasurer-Tax Collector's policy on accepting partial tax payments because it was brought to the Board's attention that the policy was not to accept partial payments. A partial, or short, payment occurs when a taxpayer pays less than the tax amount due.

We inquired about the Treasurer-Tax Collector's policy on accepting partial/short payments. For **secured property taxes**, which are the majority of the taxes, the policy is not to accept partial/short payments. We were told this is practiced throughout California. Remittance staff indicated the volume and required accounting for these payments would significantly increase their workload. There is, however, a process by which installment plans can be established for taxpayers. We found no requirement in the Revenue & Taxation Code pertaining to partial/short payments except for the option of offering installment plans.

When short/partial payments are received, the payment is deposited temporarily into a suspense account and a letter is sent to the taxpayer indicating they have 30 days to pay the remaining balance or the prior payment will be returned. If no payment is received, the T-TC processes a refund in the amount of the short/partial payment.

For **unsecured taxes**, the Treasurer-Tax Collector's policy is to accept partial/short payments because they occur less frequently. Partial payments for unsecured taxes are deposited and apportioned, and the payment is applied to the taxpayer's account. The Treasurer-Tax Collector sends out "short" letters with a new tax payment stub with the revised balance due. The process of sending out short letters was audited in the Tax Redemption Officer audit (Audit No. 2812) performed by the OC Board of Supervisors' Internal Audit Department.

The above policy for accepting partial payment of secured and unsecured taxes seems reasonable and practicable. If the Board so desires, the Treasurer-Tax Collector should evaluate the feasibility and cost/benefit of accepting partial/short payments for secured taxes. Depending on the outcome of the analysis, the Board can decide whether this policy should be revised and take appropriate action to do so.



Recommendation No. 10

The Treasurer-Tax Collector evaluate if further analysis should be performed on whether partial/short tax payments for secured taxes should be accepted.

Treasurer-Tax Collector Management Response:

Concur. With the current ATS system being replaced by PTMS in the next 18 months, all experienced Treasurer-Tax Collector and Auditor-Controller programmers and contractors are being fully utilized. The current system was developed in 1987 and is now 21 years old. IDEAL, the programming language used to code ATS, is now obsolete and has reached the end of its support life. Its vendor, Computer Associates, has stopped providing product support updates including much-needed fixes and interoperability mechanisms to adapt to newer technology. It is not cost effective to locate programmers and train them on the current ATS system to write any new code. The ability to accept partial/short payments will be a requested feature of the PTMS project under development.

A short payment relates to the inadvertent error made by a taxpayer in making taxes. These are deposited to a suspense account and held for a short time until the taxpayer is notified and proper remittance is made or the amount is refunded.

A partial payment refers to an intentional series of payments that are held for an extended period of time until the balance of the installment is received. Because the secured module of ATS does not have the ability to process and account for this type of payment plan option for current secured taxes, our policy is not to accept them.

As reported by Internal Audit, Revenue & Taxation Code 4143 on this subject is optional and requires Board approval to accept partial payments on current year taxes prior to the default date of June 30.

The Unsecured and Redemption (prior year defaulted taxes) modules within ATS have established functionality to process and account for Payment Arrangements, 4-Pay and 5-Pay Plans established under Revenue & Taxation Code.

Collections Management will evaluate various options for partial payments processes including the CAPS+ Accounts Receivable module and the module for Payment Arrangements for Unsecured and Redemption. If any option is cost-effective, a request to the Board of Supervisors will be made to accept these payments and implement the selected option.



Other Issues Brought to Our Attention:

The following are issues brought to our attention during the audit when conducting our interviews of Treasurer-Tax Collector management and staff.

Finding No. 11 – Use of Bankruptcy Interest (Control Finding)

The Treasurer-Tax Collector asked his staff to charge an administrative fee/interest on bankrupt taxpayer accounts. A concern was raised about the appropriateness and a County Counsel opinion was requested and received on August 16, 2007, regarding usage of interest approved and collected through the Bankruptcy Court. The opinion discussed what could be done with such interest and whether the interest can be used for cost recovery, specifically to defray administrative costs.

Upon receiving the opinion, the Treasurer-Tax Collector continued to collect interest from bankrupt taxpayers. However, the interest charges did not get apportioned with the tax payments for the years 2007~2009. **As of October 31, 2009, there was \$120,605 in bankruptcy interest** held in the 904 suspense account. We verified that the Treasurer-Tax Collector began apportioning the interest; however, because ATS lacks audit trails, there were difficulties in determining the interest charges from prior years because the parcel records are not on file. This required staff to research hardcopy records to apportion the interest. **As of 6/30/10, the balance was reduced to \$55,901.** Beginning in 2010, the Treasurer-Tax Collector discontinued collecting the bankruptcy interest, and is in the process of apportioning the remaining interest held in suspense.

We found no evidence to support that bankruptcy interest was recorded as revenue to offset administrative costs. The Treasurer-Tax Collector took appropriate action to apportion bankruptcy interest; however, it was about two years after receiving the County Counsel opinion.

Recommendation No.11

The Treasurer-Tax Collector continue to apportion bankruptcy interest as expeditiously as possible.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector completed this process as of January 27, 2011.

Finding No. 12 – Excessive Parking Validations (Control Finding)

Concerns were expressed that the Deputy Treasurer and one Executive Assistant have parking cards that grant them roof parking at the Civic Center; however, they instead park in a public pay lot closer to the Treasurer-Tax Collector office and have their parking validated, resulting in unnecessary parking expenditures. Another similar assertion was made involving two Treasurer-Tax Collector managers who park in the public pay lot and have validated their own parking for the past several years.

We obtained information from the Treasurer-Tax Collector and from OC Public Works Parking Administration (OCPW Parking) showing all parking cards assigned to employees. Parking cards are provided to departments at no cost and allow employees free parking. We confirmed with OCPW Parking that all departments using the **Civic Center Garage** and **Lot 2** (The Pit) have a shortage of cards due to limited parking spaces.

Detailed Results, Findings, Recommendations and Management Responses



The Treasurer-Tax Collector has 101 employees and is allocated 93 parking cards by OCPW Parking. Of the 101 employees, five are Extra Help and two are Interns. Two Treasurer-Tax Collector employees were transferred to the Auditor-Controller with their assigned parking, leaving the **Treasurer-Tax Collector with 99 employees and 91 available parking cards.**

To compensate for the shortage of eight parking cards, Treasurer-Tax Collector management found four employees that did not need parking cards (i.e., employees who carpool and do not drive), and provided the cards to the Extra Help staff. Because the Interns work part-time, and the Deputy Treasurer and Executive Assistant are in and out of the office, it was a management decision to allow those individuals to have their parking validated (in the pay lot near Building 16) to compensate for the other four cards.

We also reviewed the Treasurer-Tax Collector's two Parking Validations Logs for the period December 9, 2009 through July 22, 2010 (one for the Interns and Extra Help, and one for visitors, the Deputy Treasurer and the Executive Assistant). We found that the employees who were allowed to validate parking did not also have assigned parking cards. We did note that access to the validation stamp and logs were not restricted, and that employees self-validate their parking (i.e., sign the log and utilize the department stamp to validate their own tickets.)

Recommendation No.12

The Treasurer-Tax Collector restrict access to the parking validation logs and stamps and have a designated individual responsible for maintaining them and validating parking.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector has restricted access to the parking validation logs and stamps and has designated an individual responsible for maintaining the logs and validating parking. Management will be reviewing the log and report on a monthly basis to ensure compliance with the policy.

Finding No. 13 – Errors in Fee Calculations (Control Finding)

The fees charged for the Delinquent Unsecured Tax Fee (\$75) and Delinquent Tax Fee (\$23) are inflated by 25% due to an error in the fee calculations. The errors resulted in an allocation of staff time being counted twice.

We noted these fees were implemented at different times and the calculations did not necessarily take into account certain employee salaries already recovered through the other fees. We reviewed an analysis of fees performed by Treasurer-Tax Collector staff and confirmed that was the case, resulting in a 25% overstatement of salaries in the fee calculations.

Recommendation No.13

The Treasurer-Tax Collector update their Delinquent Unsecured and Delinquent Tax fee studies and prepare fee revisions as necessary.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector is updating the Department's Indirect Cost Rate Study and the Delinquent Unsecured and Delinquent Tax fee studies. Management expects to complete the update and fee studies by September 30, 2011.



ATTACHMENT A: Report Item Classifications

For purposes of reporting our audit observations and recommendations, we will classify audit report items into three distinct categories:

▶ **Critical Control Weaknesses:**

Serious audit findings or a combination of Significant Control Weaknesses that represent critical exceptions to the audit objective(s) and/or business goals. Management is expected to address Critical Control Weaknesses brought to their attention immediately.

▶ **Significant Control Weaknesses:**

Audit findings or a combination of Control Findings that represent a significant deficiency in the design or operation of internal controls. Significant Control Weaknesses generally will require prompt corrective actions.

▶ **Control Findings:**

Audit findings concerning internal controls, compliance issues, or efficiency/effectiveness issues that require management's corrective action to implement or enhance processes and internal controls. Control Findings are expected to be addressed within our follow-up process of six months, but no later than twelve months.



ATTACHMENT B: Treasurer-Tax Collector Management Responses



OFFICE OF THE TREASURER-TAX COLLECTOR

SHARI L. FREIDENRICH, CPA

RECEIVED
INTERNAL AUDIT DEPARTMENT

HALL OF FINANCE & RECORDS
11 CIVIC CENTER PLAZA, SUITE G76
SANTA ANA, CA 92701

2011 FEB 10 PM 1:18

INTERDEPARTMENTAL COMMUNICATION

TO: DR. PETER HUGHES, MBA, CPA, CIA

CC: MICHAEL GOODWIN, INTERNAL AUDIT
PAUL GORMAN, JENNIFER BURKHART, TTC

FROM: SHARI L. FREIDENRICH, CPA, CCMT, CPFA, CPFM *SW*

DATE: 2/9/2011

SUBJECT: RESPONSE TO DRAFT REPORT ON THE INTERNAL CONTROL AUDIT OF THE
TREASURER-TAX COLLECTOR \$5.3 BILLION TAX COLLECTION AND CASH RECEIPT
PROCESSES FOR THE PERIOD JULY 1, 2009 THROUGH JUNE 30, 2010

Pursuant to Audit Oversight Committee Administrative Procedure No. 1, we have prepared our response to the Draft Report on the Internal Control Audit of the Treasurer-Tax Collector - \$5.3 Billion Tax Collection and Cash Receipt Processes for the period July 1, 2009 through June 30, 2010. The recommendation numbers used in your report reference our response.

Recommendation No. 1

Treasurer-Tax Collector and staff with delegated authority to cancel penalties ensure that penalty cancellations are made in only when compliant with the Revenue & Taxation Code. If there is uncertainty in the criteria or their application, a County Counsel opinion should be obtained for further clarification.

Treasurer-Tax Collector Management Response:

Concur. The new Treasurer-Tax Collector's term started January 3, 2011 and she will be updating current penalty cancellation procedures so that they are consistent with and limited to those circumstances outlined in the Revenue and Taxation Code. The Treasurer-Tax Collector will complete the review and implement the revised policy, procedures and forms by March 31, 2011.

Recommendation No. 2

The Treasurer-Tax Collector establish dollar thresholds for requiring additional supervisory and management approvals for all penalty cancellations. For high-dollar transactions, a third level of authorization should be required by either the Chief Assistant Treasurer-Tax Collector or the Treasurer-Tax Collector.



ATTACHMENT B: Treasurer-Tax Collector Management Responses (continued)

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector is updating the penalty cancellation policy, procedures and forms to provide adequate controls and appropriate levels of supervisory review and management approvals on the penalty cancellation forms. The Treasurer-Tax Collector will complete the review and implement the revised policy, procedures and forms by March 31, 2011.

Recommendation No. 3

The Treasurer-Tax Collector ensure that a *Request and Authorization for Penalty Cancellation* form be completed for all penalty cancellations.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector is updating the penalty cancellation policy, procedures and forms and updating the form to ensure there are adequate controls and proper documentation and approvals for all penalty cancellations. The Treasurer-Tax Collector will complete the review and implement the revised policy, procedures, and forms by March 31, 2011.

Recommendation No. 4

The Treasurer-Tax Collector evaluate the number of staff needed to process penalty cancellations and refunds and limit this function to only staff with those job responsibilities.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector is updating the penalty cancellation policy, procedures and forms to ensure proper segregation of duties consistent with staff job responsibilities. The Treasurer-Tax Collector will complete the review and implement the revised policy by March 31, 2011.

Recommendation No. 5

The Treasurer-Tax Collector ensure the new Property Tax Management System (PTMS) generates the necessary management reports that include a listing of the entire population of penalty cancellations. These reports should enable management to review all penalty cancellations. Additionally, the reports should be retained in accordance with the County record retention policy.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector will ensure the new Property Tax Management System (PTMS) generates the necessary management reports that include a listing of the entire population of penalty cancellations. The reports will enable management review and be retained in accordance with the County record retention policy. In the interim, as PTMS will not be live until 2012, the Treasurer-Tax Collector will implement a process of randomly checking penalty cancellations as part of the new policy unless the system can generate reports. This is already in place for Redemptions and will be expanded for all waivers.



ATTACHMENT B: Treasurer-Tax Collector Management Responses (continued)

Recommendation No. 6

The Treasurer-Tax Collector explore ways to develop or identify a process that captures 100% of the penalty cancellations to enable a thorough review to ensure their propriety. Additionally, the Treasurer-Tax Collector needs to ensure that audit trails are built into PTMS system and retained for all types of transactions, including the above described penalty cancellations, for purposes of monitoring and management reviews.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector will ensure that audit trails are built into the PTMS system and retained for all types of transactions, including penalty cancellations, for purposes of monitoring and management reviews. Collections Management has determined a process to capture 100% is not cost-effective to write in the current ATS system due to a prioritization of resources focused on the PTMS project. Collections Management will update the written policy so that all penalty waivers are approved by a supervisor and randomly check for compliance in the interim.

Recommendation No. 7

The Treasurer-Tax Collector ensure online supervisory approval of penalty cancellations and tax refunds is built into the PTMS system upgrade to enable a thorough review to ensure their propriety.

Treasurer-Tax Collector Management Response:

Concur. With the current ATS system being replaced by PTMS in the next 18 months, all experienced Treasurer-Tax Collector and Auditor-Controller programmers and contractors are being fully utilized. The current system was developed in 1987 and is now over 23 years old. IDEAL, the programming language used to code ATS, is now obsolete and has reached the end of its support life. Its vendor, Computer Associates, has stopped providing product support updates including much-needed fixes and interoperability mechanisms to adapt to newer technology. It is not cost effective to locate programmers and train them on the current ATS system to write any new code.

The Treasurer-Tax Collector will plan to add online supervisory approval of penalty cancellations and tax refunds into the PTMS system to enable a thorough review to ensure their propriety. Collections Management will update the written policy so that all penalty waivers are approved by a supervisor and randomly check for compliance in the interim.

Recommendation No. 8

The Treasurer-Tax Collector evaluate ways to maintain accountability and safeguard "trouble checks" received in the Remittance Processing Section. One option is to immediately deposit the trouble checks into suspense at the time of receipt to ensure they are safeguarded.



ATTACHMENT B: Treasurer-Tax Collector Management Responses (continued)

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector is in discussions with our remittance processing vendor concerning a system upgrade to process "trouble checks" online while retaining accountability and safeguarding the checks in the Remittance Processing Section. In the interim treasury management will implement a manual system to maintain accountability and safeguard "trouble checks". We expect to implement the manual system by March 31, 2011.

Recommendation No. 9

The Treasurer-Tax Collector should analyze the cost/benefit of opening the office on Saturday when tax payments are due the following Monday.

Treasurer-Tax Collector Management Response:

Concur. With additional online payment options available and a payment drop box for after-hour payments, the Treasurer-Tax Collector discontinued the opening of the office on Saturday effective December 2010.

Recommendation No. 10

The Treasurer-Tax Collector evaluate if further analysis should be performed on whether partial/short tax payments for secured taxes should be accepted.

Treasurer-Tax Collector Management Response:

Concur. With the current ATS system being replaced by PTMS in the next 18 months, all experienced Treasurer-Tax Collector and Auditor-Controller programmers and contractors are being fully utilized. The current system was developed in 1987 and is now 21 years old. IDEAL, the programming language used to code ATS, is now obsolete and has reached the end of its support life. Its vendor, Computer Associates, has stopped providing product support updates including much-needed fixes and interoperability mechanisms to adapt to newer technology. It is not cost effective to locate programmers and train them on the current ATS system to write any new code. The ability to accept partial/short payments will be a requested feature of the PTMS project under development.

A short payment relates to the inadvertent error made by a taxpayer in making taxes. These are deposited to a suspense account and held for a short time until the taxpayer is notified and proper remittance is made or the amount is refunded.

A partial payment refers to an intentional series of payments that are held for an extended period of time until the balance of the installment is received. Because the secured module of ATS does not have the ability to process and account for this type of payment plan option for current secured taxes, our policy is not to accept them.

As reported by Internal Audit, Revenue & Taxation Code 4143 on this subject is optional and requires Board approval to accept partial payments on current year taxes prior to the default date of June 30.



ATTACHMENT B: Treasurer-Tax Collector Management Responses (continued)

The Unsecured and Redemption (prior year defaulted taxes) modules within ATS have established functionality to process and account for Payment Arrangements, 4-Pay and 5-Pay Plans established under Revenue & Taxation Code.

Collections management will evaluate various options for partial payments processes including the CAPS+ Accounts Receivable module and the module for Payment Arrangements for Unsecured and Redemption. If any option is cost-effective, a request to the Board of Supervisors will be made to accept these payments and implement the selected option.

Recommendation No.11

The Treasurer-Tax Collector continue to apportion bankruptcy interest as expeditiously as possible.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector completed this process as of January 27, 2011.

Recommendation No.12

The Treasurer-Tax Collector restrict access to the parking validation logs and stamps and have a designated individual responsible for maintaining them and validating parking.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector has restricted access to the parking validation logs and stamps and has designated an individual responsible for maintaining the logs and validating parking. Management will be reviewing the log and report on a monthly basis to assure compliance with the policy.

Recommendation No.13

The Treasurer-Tax Collector update their Delinquent Unsecured and Delinquent Tax fee studies and prepare fee revisions as necessary.

Treasurer-Tax Collector Management Response:

Concur. The Treasurer-Tax Collector is updating the Department's Indirect Cost Rate Study and the Delinquent Unsecured and Delinquent Tax fee studies. Management expects to complete the update and fee studies by September 30, 2011.

If you have additional questions or follow-up comments; please contact myself or Paul Gorman at 714-834-2288.