

Internal Audit Department

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

FIRST FOLLOW-UP AUDIT: INTERNAL CONTROL AUDIT TREASURER-TAX COLLECTOR – \$5.3 BILLION TAX COLLECTION AND CASH RECEIPT PROCESSES

ORIGINAL AUDIT No. 2954

AS OF DECEMBER 31, 2011

Our First Follow-Up Audit found that the Treasurer-Tax Collector fully implemented eleven (11) recommendations, one (1) recommendation is in process, and one (1) recommendation has been closed from our original audit report dated February 15, 2011. The Treasurer-Tax Collector collects approximately \$5.3 billion in taxes annually.

AUDIT NO: 1130-A
REPORT DATE: MARCH 22, 2012

Director: Dr. Peter Hughes, Ph.D., CPA
Deputy Director: Eli Littner, CPA, CIA
Senior Audit Manager: Michael Goodwin, CPA, CIA
Senior Internal Auditor: Susan Nestor, CPA, CIA

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

GRC (Government, Risk & Compliance) Group 2010 Award to IAD as MVP in Risk Management



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 to IAD 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

Dr. Peter Hughes **Ph.D., MBA, CPA, CCEP, CITP, CIA, CFE, CFF**
Director Certified Compliance & Ethics Professional (CCEP)
 Certified Information Technology Professional (CITP)
 Certified Internal Auditor (CIA)
 Certified Fraud Examiner (CFE)
 Certified in Financial Forensics (CFF)
 E-mail: peter.hughes@iad.ocgov.com

Eli Littner **CPA, CIA, CFE, CFS, CISA**
 Deputy Director Certified Fraud Specialist (CFS)
 Certified Information Systems Auditor (CISA)

Michael Goodwin **CPA, CIA**
 Senior Audit Manager

Alan Marcum **MBA, CPA, CIA, CFE**
 Senior Audit Manager

Autumn McKinney **CPA, CIA, CISA, CGFM**
 Senior Audit Manager Certified Government Financial Manager (CGFM)

Hall of Finance & Records

12 Civic Center Plaza, Room 232
 Santa Ana, CA 92701

Phone: (714) 834-5475

Fax: (714) 834-2880

To access and view audit reports or obtain additional information about the OC Internal Audit Department, visit our website: www.ocgov.com/audit



OC Fraud Hotline (714) 834-3608

Letter from Dr. Peter Hughes, CPA



Transmittal Letter



Audit No. 1130-A March 22, 2012

TO: Shari L. Freidenrich
Treasurer-Tax Collector

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

SUBJECT: First Follow-Up Audit: Internal Control Audit
Treasurer-Tax Collector – \$5.3 Billion Tax
Collection and Cash Receipt Processes,
Original Audit No. 2954, Issued February
15, 2011

We have completed a First Follow-Up Audit of internal controls over the Treasurer-Tax Collector's Tax Collection and Cash Receipt Processes. Our audit was limited to reviewing, as of December 31, 2011, actions taken to implement the **thirteen (13) recommendations** from our original audit. We conducted this First Follow-Up Audit in accordance with the *FY 11-12 Audit Plan and Risk Assessment* approved by the Audit Oversight Committee and Board of Supervisors (BOS).

The results of our First Follow-Up Audit are discussed in the **OC Internal Auditor's Report** following this transmittal letter. Our First Follow-Up Audit found that the Treasurer-Tax Collector implemented eleven (11) recommendations, one (1) recommendation is in-process, and one (1) recommendation has been closed. As such, a Second Follow-Up Audit will be conducted approximately six months from the date of this report.

Each month I submit an **Audit Status Report** to the BOS where I detail any critical and significant control weaknesses 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.

Other recipients of this report are listed on the **OC Internal Auditor's Report** on page 6.

Table of Contents



*First Follow-Up Audit:
Internal Control Audit -Treasurer-Tax Collector
\$5.3 Billion Tax Collection and Cash Receipt Processes
Audit No. 1130-A*

As of December 31, 2011

Transmittal Letter	i
OC Internal Auditor's Report	1

OC Internal Auditor's Report



Audit No. 1130-A

March 22, 2012

TO: Shari L. Freidenrich
Treasurer-Tax Collector

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

SUBJECT: First Follow-Up: Internal Control Audit of Treasurer-Tax Collector –
\$5.3 Billion Tax Collection and Cash Receipt Processes
Original Audit No. 2954, Issued February 15, 2011

Scope of Review

We completed a First Follow-Up Audit of the Treasurer-Tax Collector's Tax Collection and Cash Receipt processes and internal controls. Our audit was limited to reviewing actions taken as of December 31, 2011 to implement the **thirteen (13) recommendations** in our original audit report.

Background

We conducted the original Internal Control Audit by direction of the Board of Supervisors. The 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.

The original audit identified **five (5) Significant Control Weaknesses** and **eight (8) Control Findings** resulting in thirteen (13) recommendations pertaining to penalty cancellation controls and processes; approving penalty cancellations and tax refunds; accountability over "trouble checks," efficiency/effectiveness issues; issues concerning a bankruptcy interest fund, parking expenditures, and calculations of fees charged by the Treasurer-Tax Collector.

Results

Our First Follow-Up Audit indicated the Treasurer-Tax Collector **fully implemented eleven (11) recommendations, one (1) recommendation is in-process, and one (1) recommendation has been closed from our original audit.**

Based on the Follow-Up Audit we conducted, the following is the implementation status of the thirteen (13) original recommendations.

1. **Management Intervention in Approving Penalty Cancellations (Control Finding)**

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.

Current Status: Implemented. We found that the Treasurer-Tax Collector took appropriate corrective action by updating the penalty cancellation policy, procedures and forms to be consistent with, and limited to, those circumstances outlined in the Revenue and Taxation Code.



We compared the updated penalty cancellation policy, procedures and forms to the California Revenue and Taxation Codes pertaining to penalty cancellations and found the documentation to be consistent with the Code. In addition, we tested a sample of penalty cancellations and found that penalty cancellation forms were completed and authorized by the appropriate level of management, and the justification met the Treasurer-Tax Collector's criteria for cancellation per the policy. We also noted one instance when County Counsel was consulted on a penalty cancellation request. Because the Treasurer-Tax Collector updated the penalty cancellation policy and procedures, and obtains clarification from County Counsel as needed, we consider this recommendation to be implemented.

2. **Penalties Canceled Based on Single Authorization** (Significant Control Weakness)

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.

Current Status: **Implemented.** The Treasurer-Tax Collector took appropriate corrective action by updating penalty cancellation policy and procedures for supervisory reviews and management approvals on the penalty cancellation forms. Dollar thresholds were established for staff members authorized to approve penalty cancellations, with the Treasurer Tax Collector and Chief Assistant Treasurer-Tax Collector having the authority to approve penalty cancellations at any amount. We tested a sample of penalty cancellations and found that each penalty cancellation form was authorized by the appropriate level of management. Because corrective action was taken by establishing dollar thresholds for approval of penalty cancellations, we consider this recommendation to be implemented.

3. **Penalty Cancellation Forms Not Consistently Prepared** (Significant Control Weakness)

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

Current Status: **Implemented.** The Treasurer-Tax Collector took appropriate corrective action by updating the penalty cancellation policy and procedures to provide adequate controls and appropriate levels of supervisory review and management approvals on the penalty cancellation forms. The policy requires that a *Request and Authorization for Penalty Cancellation* form be completed for all penalty cancellations. We tested a sample of penalty cancellations and found that penalty cancellation forms were completed and properly approved. Because we found no exceptions, we consider this recommendation to be implemented.

4. **Excessive Staff Have Access to Cancel Penalties in ATS** (Significant Control Weakness)

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

Current Status: **Implemented.** During the original audit, thirty-six (36) staff had authorization to process penalty cancellations. The Treasurer-Tax Collector reduced the number of staff processing penalty cancellations to fifteen (15). For approving penalty cancellations, the number of staff was reduced from eleven (11) to nine (9). The listing of *Staff Authorized to Process Online Penalty Cancellations* was also revised since the original audit. Because corrective action was taken on the number of staff that process and approve penalty cancellations, we consider this recommendation to be implemented.



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

Current Status: Implemented. Treasurer-Tax Collector management determined it is not cost-effective to modify ATS due to prioritization of resources on the PTMS project. We reviewed Property Tax Management System (PTMS) design documentation for the Penalty Cancellation module. The design documentation included a requirements summary, system use case, and a low level screen design for report search capability. Based on our review of this documentation, we saw that a module has been designed to improve management reporting of property tax penalty cancellations, including the ability to retrieve and review the entire population of penalty cancellations that have been completed. In addition, the reports will be retained in accordance with the records retention policy. Although PTMS has not been implemented, the intent of the recommendation to ensure management reports will be generated has been met. Therefore, we consider this recommendation to be implemented.

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

Current Status: Implemented. Treasurer-Tax Collector management determined it is not cost-effective to modify the current Assessment Tax System (ATS) due to prioritization of resources on the PTMS project. We reviewed PTMS design documentation for the Penalty Cancellation module. Penalty cancellation audit trails are addressed in the design documentation that provides management the capability to generate, monitor and review penalty cancellations. Although PTMS has not yet been implemented, the intent of the recommendation to ensure there are planned audit trails in the new system has been met. Therefore, we consider this recommendation to be implemented.

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

Current Status: Implemented. Treasurer-Tax Collector management determined it is not cost-effective to modify ATS due to prioritization of resources on the PTMS project. We reviewed PTMS design documentation for the Penalty Cancellation module. Based on our review of the requirements summary documentation, we noted the design of the system will enable on-line review and management approval of penalty cancellations. Although PTMS has not yet been implemented, the intent of the recommendation to have planned online processing and supervisory approval has been met in the system design documentation. Therefore, we consider this recommendation to be implemented.



8. Controls Over "Trouble Checks" (Control Finding)

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.

Current Status: **Implemented.** The Treasurer-Tax Collector implemented an exception mail (trouble checks) process within the Remittance Processing Section to provide the necessary accountability and safeguarding of checks until final disposition of the monies is determined. Additional controls now include logging and scanning of trouble checks, email notifications to groups responsible for researching the checks, and use of spreadsheets to track the checks through disposition. We observed the daily exception mail process in the Remittance Processing Section and found that "trouble checks" were accounted for and safeguarded until the disposition of the monies was determined. We tested a sample of trouble checks and found that the final disposition of the monies was appropriate. Because corrective actions were taken, we consider this recommendation to be implemented.

9. Opening for Tax Collections on Saturday (Control Finding)

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

Current Status: **Implemented.** The Treasurer-Tax Collector discontinued the opening of the office on Saturdays when tax payments are due the following Monday. We observed that the Treasurer-Tax Collector website informs taxpayers that if the tax due date falls on Saturday, Sunday or legal holiday, taxes are due on the next business day. The site also notifies taxpayers that the office is open Monday through Friday. Because the Treasurer-Tax Collector discontinued opening the office on Saturdays, we consider this recommendation to be implemented.

10. Acceptance of Partial/Short Tax Payments (Control Finding)

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

Current Status: **Closed.** Treasurer-Tax Collector management determined it is not cost-effective to modify ATS for partial/short tax payments due to prioritization of resources on the PTMS project. ATS currently has modules for Unsecured and Redemption (prior year defaulted taxes) to process and account for Payment Arrangements, 4-Pay and 5-Pay Plans established under Revenue & Taxation Code. However, our review of PTMS design documentation found that the current design does not provide for short or partial payments for secured tax payments.

The Treasurer-Tax Collector has indicated that although the original PTMS Needs Assessment did not include the ability to make partial payments, it was noted in the high-level design that this is a feature the Treasurer-Tax Collector wants to incorporate in the future. We were informed the database has been designed with the flexibility to develop partial payment capability similar to that which exists for unsecured tax bills. The analysis and funding of this post "go-live" request will be completed and requested to be approved by the Board of Supervisors after "go-live" so that partial payments will be accepted in the future. Because this is a feature that will be explored further after PTMS is implemented, we consider this recommendation closed.

11. Use of Bankruptcy Interest (Control Finding)

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



Current Status: Implemented. During the original audit, the Treasurer-Tax Collector held approximately \$55,900 in a bankruptcy interest fund that had not yet been apportioned to taxpayers as of June 30, 2010. Subsequent to the audit, the Treasurer-Tax Collector continued its efforts to identify eligible taxpayer accounts and apportion interest back to the taxpayers who were involved in bankruptcy. We were informed all bankruptcy interest had been apportioned, and we verified the bankruptcy interest fund balance was zero as of June 30, 2011. Because corrective actions were taken to apportion the remaining bankruptcy interest, we consider this recommendation to be implemented.

12. Excessive Parking Validations (Control Finding)

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.

Current Status: Implemented. The Treasurer-Tax Collector restricted access to the parking validation log and stamp, and designated responsibility for maintenance and validation of the logs to a single individual. Treasurer-Tax Collector staff no longer have access to parking logs. Staff without parking cards (due to a limit on the number of cards issued) were issued hangtags for Civic Center monthly parking lots; as a result, validation of staff parking is no longer required for Treasurer-Tax Collector employees. We reviewed the parking validation log subsequent to our original audit and noted that parking for visitors was appropriately validated. Because corrective action was taken, we consider this recommendation to be implemented.

13. Errors in Fee Calculations (Control Finding)

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

Current Status: In Process. In our original audit, the Delinquent Unsecured (DU) and Delinquent Secured (DS) fees were \$75 and \$23, respectively, calculated in May and July 2007. In those studies, some staff salaries were recovered in excess of actual costs, and some salary recoveries were for staff not involved in delinquent collections.

Fee studies were updated for the DU and DS fees; however, the Treasurer Tax Collector determined that additional statistics were needed to more accurately reflect the fee amounts to be charged. Because of the age of the data used, the statistics have dramatically changed with the economy and would not provide an accurate basis for the fee revisions. Staff has been directed to compile more current data, including some overhead amounts that are to be determined by the Auditor-Controller. The Treasurer Tax Collector indicated that they are not able to complete the fee study for approval by the Board of Supervisors prior to April 2012. Additional time is needed to complete a fee study and information is still pending from the Auditor-Controller. As such, we consider this recommendation in process.

Planned Action:

The Treasurer-Tax Collector plans to review the 2010-11 data along with the Indirect Cost rate, once it is finalized by the Auditor-Controller, to determine whether there will be a change in the calculated fee amounts for the Delinquent Secured and Delinquent Unsecured fees. Once the final data is available, the Treasurer-Tax Collector will take steps, if necessary, to change the fees and provide the information to Internal Audit. At this time, based on estimated costs, the fees are not expected to significantly change as delinquencies have decreased significantly, especially in the area of secured taxes.

OC Internal Auditor's Report



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.

Distribution Pursuant to Audit Oversight Committee Procedure No. 1:

Members, Board of Supervisors
Members, Audit Oversight Committee
Thomas G. Mauk, County Executive Officer
Ray Silver, Chief of Staff, Treasurer-Tax Collector
Paul Gorman, Chief Assistant Treasurer-Tax Collector
Jennifer Burkhart, Assistant Treasurer-Tax Collector
Robin Russell, Assistant Treasurer-Tax Collector, Administration
Daniel Puglia, Budget Manager, Treasurer-Tax Collector
Foreperson, Grand Jury
Susan Novak, Clerk of the Board of Supervisors