



County of San Diego, California

Auditor and Controller

*Final
Report*

Follow-Up Audit of the Property Tax Collection and Refund Process

Office of **A**udits & **A**dvisory **S**ervices

**August 2009
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COUNTY OF SAN DIEGO

INTER-DEPARTMENTAL CORRESPONDENCE

August 17, 2009

TO: Daniel V. McAllister
Treasurer-Tax Collector

FROM: Kenneth J. Mory
Chief of Audits

FINAL REPORT: FOLLOW-UP AUDIT OF THE PROPERTY TAX COLLECTION AND REFUND PROCESS

Enclosed is our report on the Follow-up Audit of the Property Tax Collection and Refund Process. As there are no recommendations in the report, no audit response is required.

Thank you for the courtesousness and cooperation extended to the Office of Audits & Advisory Services during the course of the audit.

If you have any immediate concerns about the report, please contact me at (858) 495-5662.


KENNETH J. MORY
Chief of Audits

AUD:TP:aps

Enclosure

c: Donald F. Steuer, Chief Financial Officer
Tracy M. Sandoval, Assistant Chief Financial Officer/Auditor and Controller
Ebony N. Shelton, Group Finance Director

BACKGROUND

From FY 2005-06 to the present, three audits and one review related to the property tax refund process have been conducted. In FY 2005-06, a Grand Jury (GJ) audit was conducted of the Treasurer-Tax Collector (T-TC) tax refund program. In October 2005, Macias Consulting, Inc. (Macias) performed a review of the property tax overpayment and escheatment processes. Subsequently, in 2008, the Office of Audits & Advisory Services (OAAS) conducted an audit of the property tax collection and refund process. Last, as requested by the Treasurer-Tax Collector, in 2009, Kessler International (Kessler) conducted a forensic audit of the property tax trust refund database. The report titles, dates, and objectives are provided in Appendix A.

AUDIT SCOPE AND LIMITATIONS

At the request of the T-TC, OAAS completed a follow-up to the audits and review indicated above. The objective was to determine whether the T-TC implemented the recommendations or alternative solutions to address the findings included in the GJ, Macias, OAAS, and Kessler engagements.

This audit was conducted in accordance with auditing standards prescribed by the Institute of Internal Auditors, Inc., as required by California Government Code, Section 1236.

METHODOLOGY

OAAS implemented a multi-faceted methodology to conduct the audit. The following briefly highlights the methods used:

- Performed a review of all findings and recommendations included in each engagement;
- Reviewed the Department's response describing the status of each recommendation;
- Assessed recommendations to determine if they were reasonable, applicable, and feasible (RAF);
- Verified through observation and inspection whether recommendations reported as implemented were actually implemented;
- Identified the reasons why implementation has not occurred for those recommendations reported as outstanding; and
- Evaluated whether the approach proposed by the T-TC for reconciling the TrustRef system to the County's Oracle General Ledger (GL) is reasonable.

AUDIT RESULTS

OAAS identified a total of 46 recommendations as reported by the engagements performed by the GJ, Macias, OAAS, and Kessler. There were 11 recommendations in the Kessler report assessed as not reasonable, not feasible, or redundant to those in the three prior engagements. Audit work found that 23 of the remaining 35 recommendations have been implemented by the T-TC, while 12 open recommendations are in progress with implementation expected by December 2009.

Half of the open recommendations were directly related to findings regarding records maintained in the TrustRef system and the inability to reconcile the system to the general

ledger. The reconciliation and baseline procedure proposed by the T-TC was determined to be a reasonable approach and responsive to audit recommendations.

**Observation I: Some Recommendations Redundant,
Not Feasible, or Not Reasonable**

OAAS identified a total of 46 recommendations as reported by the engagements performed by the GJ, Macias, OAAS, and Kessler. OAAS assessed these recommendations to determine whether they were RAF (fully or in part) and that they represented a unique recommendation requiring some level of action or response. All 21 recommendations contained within the GJ, Macias, and OAAS engagements were determined to be RAF and unique. However, from the 25 recommendations identified in the Kessler report, 11 (44%) were assessed as not reasonable, not feasible, or redundant to those in the three prior engagements. These recommendations were excluded from the implementation status review and will not be included in future recommendation follow-up activity. Additionally, six recommendations were classified as partially RAF. In these cases, while implementation of the exact wording of the recommendation was not considered reasonable and/or feasible, the recommendations addressed findings and risk areas where an alternative action was appropriate. These recommendations are included in the implementation status sheet.

**Observation II: All Reasonable, Applicable, and Feasible Recommendations
Have Been Implemented or Are in Progress**

Audit work verified that all 35 recommendations assessed as RAF or partially RAF were either implemented or are in progress as shown in the table below.

Summary	No. of Recommendation	Implementation Status		
		Implemented	In Progress	Reference Number ¹
Grand Jury Audit Report (Appendix B)	4	4	-	-
Macias Audit Report (Appendix C)	12	11	1	M10a
OAAS Audit Report (Appendix D)	5	3	2	O1, O5
Kessler's Report (Appendix E)	14	5	9	K1, K5, K6, K9, K11, K16, K20, K22, K25
Total	35	23	12	
Percentage		65.7%	34.3%	

¹ Reference numbers relate to the recommendation number of each engagement as shown in Appendices B, C, D, and E. GJ=Grand Jury, M=Macias, O=OAAS, and K=Kessler.

Recommendations In Progress - Of the 12 recommendations in progress, six (50%) are addressed by the escheatment and baseline reconciliation process discussed in Observation III. The remaining six recommendations and implementation dates are shown in the table below.

Recommendation - Action/Activity	Planned Implementation Date	Reference Number
Implementation of a security maintenance policy	9/30/2009	K16
Implementation of database programming to alert the issuer of any monies due to the County before issuing refunds to the taxpayer	9/30/2009	K6
Staff training on the newly issued TrustRef desk manual	9/30/2009	K22
Performance of a risk-based review of refund activity specified in audit findings as requiring reconciliation ² to determine whether refunds were properly issued and received by the rightful recipients	8/31/2009	K1, K25
Completion of financial reporting procedure documentation ³	11/30/2009	O5

Observation III: Proposed Solution to Reconcile the TrustRef Database to the General Ledger Determined to be Reasonable

OAAS reviewed the T-TC proposed solution to reconcile the TrustRef database to the GL and determined the approach to be reasonable. The OAAS audit in 2008 found that the T-TC was unable to perform a cumulative reconciliation between the TrustRef database and the GL. T-TC management took action and hired Kessler to identify a baseline and reconcile the balance to the GL. Due to some data discrepancies identified by Kessler, they did not provide the reconciliation of the TrustRef database to the GL. According to the Kessler report, they were unable to rely on the information provided by the T-TC; therefore, they did not perform the reconciliation of the TrustRef database to the GL. As a result, the T-TC developed an alternate solution that includes the following steps (See also Appendix F for a flowchart of the procedural steps):

- Segregate records older than June 30, 2004;
- Perform an escheatment – invalid records will be excluded from this process in accordance with existing escheatment procedures (includes documentation of attempts to locate refund recipients); and
- Adjust/balance TrustRef and the GL.

Note: Due to the lack of integrity of the archive database, this reconciliation will include only current TrustRef records as compared to the GL.

² In lieu of a full reconciliation of transactions as recommended (not feasible), it was agreed that a risk-based sample would be utilized to trace selected refunds back to source data.

³ Draft documentation is pending assessment by T-TC CAFR external auditor for completeness and adequacy.

Appendix A
Audits and Reviews Since 2005

Report Title	Purpose or Objective of the Engagement
<p>Grand Jury Audit, <i>The San Diego County Treasure/Tax Collector Tax Refund Program</i>, issued 2005.</p>	<p>The Grand Jury focused on the following issues:</p> <ul style="list-style-type: none"> • Refund procedures used by County Treasurer/Tax Collector; • The most recent refunds distributed to taxpayers; • Minimum refund amount; • Procedures used to locate eligible taxpayers whose address of record may be invalid; and • Tax bill format.
<p>Macias Consulting Group, Inc. (MCG) Review, <i>County of San Diego Treasurer-Tax Collector Property Tax Refund for Overpayment and Escheatment Protocols Validation</i>, issued October 17, 2005.</p>	<p>MCG's objectives were to:</p> <ul style="list-style-type: none"> • Determine the reasonableness of County policies and methods for issuing funds owed to property owners; • Validate escheatment reporting carried out; and • Develop or upgrade property tax refund and escheatment protocols.
<p>County of San Diego Office of Audits & Advisory Services, <i>Property Tax Collection and Refund Process Audit</i>, issued January 31, 2008.</p>	<p>This audit was in response to specific areas of concern related to the property tax collection and refund process, including:</p> <ul style="list-style-type: none"> • Reporting accuracy and completeness of reconciliations; • Negative account balances (collections due); • Refunds on returned property tax payments (non-sufficient funds); and • Data integrity and completeness of subsidiary records in the Trust Refund (TrustRef) system.
<p>Kessler International, <i>Forensic Audit of the Treasurer-Tax Collector Property Tax Trust Refund Database</i>, issued March 25, 2009.</p>	<p>The objectives of the engagement were to:</p> <ul style="list-style-type: none"> • Perform an assessment of the (TrustRef) system's exposure to (or evidence of) fraud; • Assess whether the condition of the current, archived, and backed up data is sufficient to perform and complete a cumulative reconciliation to the general ledger; • Complete the cumulative reconciliation; or • If a cumulative reconciliation cannot be performed, recommend a procedure and criteria for establishing a baseline.

**Appendix B
OAAAS Analysis – 2005 Grand Jury Audit**

Related Findings:

- a) Inadequate written policies and procedures for refunding overpaid property taxes.
- b) A backlog of over 11,000 refunds that remains unclaimed for tax years 1996 through 2002.
- c) The current policy of processing refunds that exceed \$6 adds unnecessary expense to the administrative cost of making refunds.
- d) The format of the Supplemental Tax Bill is not easily understood and may be confusing to many people.

Control #	Recommendation	T-TC's Response To Audit Recommendation Status	OAAAS Comments and Observations	Implementation Status (Planned Date)
GJ06-01	Expedite the completion of written policies and procedures for processing refunds.	The recommendation has been implemented. In December 2005, the Treasurer-Tax Collector completed and implemented formal written policies and procedures for: - Tax Refunds for Overpayment - Escheatment Process The Treasurer-Tax Collector will continue to update all department policies and procedures.	Agrees. Verified implementation of policies and posting of policies to the intranet.	Implemented
GJ06-02	Issue refunds for all tax years prior to 2001 as soon as is practicable.	The recommendation has been implemented. Since August 2005, the Treasurer-Tax Collector has refunded \$1.381 million for overpayments made in tax years 1996 through 2002, with a remaining balance of \$1.012 million. The Treasurer-Tax Collector continues to issue refunds on a 2-week cycle and will continue to work diligently to process all outstanding refunds.	Agrees Supporting data for refund totals relevant to the recommendation could not be provided. However, Treasurer-Tax Collector subsequently provided overall refund data from FY2004-05 that showed a substantial increase in refund activity correlating to the period following the recommendation.	Implemented
GJ06-03	Evaluate the cost savings to the Treasurer-Tax Collector's office if the minimum refund amount is increased from \$6.00 to \$10.00 as authorized by the Revenue and Taxation Code.	The recommendation has been implemented. The Treasurer-Tax Collector initiated a change in its property tax system to increase the minimum refund amount from \$6.00 to \$10.00 effective January 1, 2006.	Agrees Verified implementation of the change in minimum refund amount to \$10.	Implemented
GJ06-04	Revise the Supplemental Tax Bill format to highlight the taxpayer's eligibility and amount of the refund.	The recommendation has been implemented. The Treasurer-Tax Collector has redesigned the Supplemental Tax Bill to conform to the format established with the annual secured property tax bill. The information on the back of the bill and on the insert explains that a negative supplemental bill means that the taxpayer is receiving a refund which is included in the mailing.	Agrees Verified the revisions made to the supplemental tax bill.	Implemented

**Appendix C
OAAS Analysis – Macias Consulting Group Report (October 17, 2005)**

Related Findings:

- a) Customer service strategies and response time improvements.
- b) Inadequate documentation and training on policies, procedures, and user guides.
- c) Backlog, inadequate staffing.
- d) IT project management controls.

Control #	Recommendation	T-TC's Response To Audit Recommendation Status	OAAS Comments and Observations	Implementation Status (Planned Date)
M1	Conduct a review of the T-TC long-term strategies and supporting structure to identify innovations to improve customer service and timely and effective processing of tax-related transactions.	T-TC remains committed to continuous improvements in the areas of customer service and operational efficiency. This commitment has resulted in the automation of the exception payment process. Rejected payments are made available to the exception processors electronically. The processors reconcile the payments, determine the appropriate disposition for the payment and generate the required correspondence online. The efficiencies gained include a 70 percent decrease in resources processing exception payments during the peak periods, faster notification to taxpayers of payment discrepancies and increased security of property tax payments. T-TC also participates with the Assessor/Recorder/ County Clerk in conducting educational tours of the T-TC's Office for real estate and title company agencies in order to educate attendees about property tax billing and collection. Finally, T-TC conducts annual training sessions for its staff to stay up to date and knowledgeable in TTC functions as well as routinely used Revenue and Taxation Codes.	<u>Agrees.</u> Customer focus customer initiatives verified in OAAS 2008 report.	Implemented
M2	Determine total processes cycle time and address problems contributing to any process delays.	T-TC has completed policies and procedures for processing refund overpayments and has conducted staff training. T-TC will conduct annual training sessions to review the policies and procedures. A Trustee user guide has been established for TrustRef users.	<u>Agrees.</u> Verified policy implementation, including training in procedures and user training of TrustRef system.	Implemented
M3	Fill accounting vacant positions to address current backlog.	All vacant accounting positions have been filled.	<u>Agrees.</u> Verified decrease in vacancies and	Implemented

Control #	Recommendation	T-TC's Response To Audit Recommendation Status	OAS Comments and Observations	Implementation Status (Planned Date)
M4	Draft and adopt policies and procedures for the Tax Refund and Overpayment and Escheatment processes.	T-TC has adopted formal policies and procedures for the processing of property tax overpayments which includes the proper documentation for the validation of refunds. A research guide has also been established for the purpose of locating taxpayers to whom a refund is owed.	increase in accounting positions correlating to 2005 recommendation. Agrees. Verified procedure implementation.	Implemented
M5	Draft a research guideline that identifies a sequence for use of source data, due diligence, and documentation of research efforts.	A research guide for locating taxpayers has been completed.	Agrees. Verified implementation and use of returned warrant worksheet.	Implemented
M6	Develop procedures for carrying out research for the 2005 list of items pending escheatment to include third party review to assure these procedures have been followed.	T-TC completed the formal escheatment policy and procedure in November 2006.	Agrees. Verified implementation of escheatment procedure, which includes documentation of attempts to locate refund recipients prior to escheatment.	Implemented
M7	Draft a TrustRef system user manual that includes instructions on data entry, research capabilities to identify the best and most recent address for recipient, and report generation functionality.	The development of a TrustRef system user manual is in process.	Agrees. While the T-TC response indicated that work is still in progress, the Department did respond to the 2005 recommendation with a user guide (instructional handouts) and provided evidence that training had been conducted. Attendance/ Participation records could not be provided but training was confirmed via participant testimonial.	Implemented
M8	Require staff to read and sign off on the policies and procedures, research guideline, and user manual to acknowledge receipt and understanding.	An annual training for the TrustRef procedure is conducted.	Agrees. Attendance/Participation records could not be provided. Testimonial from Financial Division Manager indicated that annual training was conducted and sign-in sheets were utilized but not retained.	Implemented

Control #	Recommendation	T-TC's Response To Audit Recommendation Status	OAAAS Comments and Observations	Implementation Status (Planned Date)
M9	Provide training to all staff on the policies and procedures, guidelines, and user manual and post this documentation on the T-TC intranet.	An annual training of the TrustRef procedure is conducted.	Agrees. Testimonial of Financial Division Manager indicates that training was conducted on all recommendation elements annually, though training documentation/agendas were not retained. Procedural documentation posted to internet (a portion of the contents of a user/desk manual).	Implemented
M10a	Record appropriate account adjustments to write-off unidentifiable account variances.	Refer to management response to OAAAS Report No. A08-002 Finding I.	Agrees. This is addressed in implementation plan for recommendation O1.	In Progress (12/31/2009)
M10b	Conduct a review of TrustRef reports to determine whether reports meet user needs and to identify formatting enhancements to better their usefulness and to best identify the refund recipient.	Refer to management response to OAAAS Report No. A08-002 Finding I.	Agrees. While TrustRef reporting was not included in the T-TC response, reporting enhancements to TrustRef system were visually verified, including detail reporting screens, additional fields, and supporting information contained in each record screen.	Implemented
M11	Formalize policy and procedures for IT project management and oversight prior to initiation of new Treasurer database project planned for implementation in 2008, including change control, cost control, risk management, budget control, and schedule control.	T-TC IT staff utilize the comprehensive IT policies and procedures established by the County's Chief Technology Office. The CTO has also established a Project Management Plan which provides for change control, cost control, risk management, budget control and schedule control. T-TC has reviewed the feasibility of processing all checks. In compliance with Revenue and Taxation Codes, T-TC may not hold payments for application to future liabilities.	Agrees. Verified that entity level (County) controls exist for each area, including: NG change control, Business Requirement Documentation (BRD), and County Technology Office (CTO) procedures. The County Financial Risk Assessment and Control (FRAC) initiative includes an IT process control matrix with specific references to documented procedures.	Implemented