

County of Solano
Office of the Auditor-Controller



**Audit of the Property Tax Redemption Process
July 1, 2008 through June 30, 2011**

March 1, 2012

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INTRODUCTION

In accordance with the Fiscal Year 2011/12 Audit Plan for the Internal Audit Division, we conducted an audit of the Property Tax Redemption Process.

OBJECTIVE

Our objective was to evaluate the Property Tax Redemption Process from July 1, 2008 through June 30, 2011, pursuant to Revenue and Taxation Code §§ 4101 through 4379. As part of obtaining reasonable assurance about the accuracy of redemption collection records and accounts, we performed tests of collection records, penalty and interest calculations, and account reconciliations.

BACKGROUND

Parcels on which the amounts due (e.g., taxes, assessments, penalties, and costs) are not fully paid by the close of business on the last day of the fiscal year, are by operation of law, declared tax-defaulted and transferred to the redemption roll. The declaration of default opens a waiting period, during which the defaulted taxes, penalties, and costs accumulate until redeemed.

Tax records are maintained within the Solano County Integrated Property System (SCIPS) administered by the Department of Information Technology. At the close of each fiscal year, SCIPS automatically generates a report of tax-defaulted properties. The Auditor-Controller's Office (ACO) uses this SCIPS report to move defaulted supplemental and secured taxes receivable to the redemption roll. After tax-defaulted properties are transferred to the redemption roll, the Treasurer-Tax Collector's Office (TCO) is charged with collecting delinquent taxes, penalties, interests, and costs.

The Treasurer-Tax Collector is responsible for managing redemption records and accounts which include billing, collecting, and accounting for all defaulted property taxes. The act of redemption involves the payment of defaulted property tax amounts and related penalties, fees, and costs. Any tax-defaulted property may be redeemed until the right of redemption is terminated. A property owner may choose to redeem the property by paying defaulted property tax in full or in installments.

An installment plan may be instituted or reinstated on tax-defaulted property until 5 p.m. on the last business day prior to the date when the Tax Collector obtains the power to sell the property (R&T Code §4217). The amount owed for parcels under installment pay plans totaled approximately \$1.1 million at June 30, 2009, \$1.5 million at June 30, 2010, and \$2 million at June 30, 2011.

The Tax Collector's Office submits a certified monthly report of collections to the Auditor-Controller's Office. The Auditor-Controller's Office uses this report to relieve the taxes receivable accounts and transfer interest and penalties to the Tax Loss Reserve Fund.

For the period of July 2008 through June 2011, defaulted property taxes transferred to the redemption roll and collections of redemption taxes, penalties, interests, and costs were as follows:

REDEMPTION RECEIVABLE AND COLLECTIONS

For fiscal years ended June 30, 2009, 2010 & 2011

	<u>FY 2008/09</u>	<u>FY 2009/10</u>	<u>FY 2010/11</u>
Beginning Balance	\$ 17,822,178.00	\$ 19,768,078.90	\$ 18,359,263.96
Add/Less:			
Delinquent Taxes Transfers	43,298,241.68	31,381,833.02	17,604,063.53
Collections/Cancellations	(41,352,340.78)	(32,790,647.96)	(20,062,650.90)
Ending Balance *	<u>\$ 19,768,078.90</u>	<u>\$ 18,359,263.96</u>	<u>\$ 15,900,676.59</u>

* Amounts include payments made under Installment Pay and Secured Bankruptcy Payment plans.

In addition, the TCO conducts public auctions and sealed bid sales on tax-defaulted properties. Two chapters in Part 6 of Division 1 of the Revenue & Taxation Code provide for the sale of tax-defaulted properties by the Tax Collector. The Tax Collector has the authority to sell tax-defaulted property. Written approval of the Board of Supervisors is required to sell property at public auction or by sealed bid (R&T Code §3692) to the highest bidder at the time and place fixed for sale. Approval of the Board of Supervisors and authorization by the State Controller is required to complete sales to public agencies or nonprofit organizations. Parcels approved for sale for the period of July 2008 through June 2011 were as follows:

- Fiscal year 2008/09, 28 parcels were approved for sale. Of the 28 parcels offered, 21 were redeemed prior to sale, 6 parcels were withdrawn and 1 parcel was sold. The Tax Collector recovered approximately \$440,000 in taxes, penalties, interest and fees.
- Fiscal year 2009/10, 51 parcels were approved for sale. Of the 51 parcels offered, 30 were redeemed, 10 parcels were withdrawn, 4 parcels were sold and 7 parcels did not receive any bids. The Tax Collector recovered approximately \$496,000 in taxes, penalties, interests and fees.
- Fiscal year 2010/11, 50 parcels were approved for sale. Of the 50 parcels offered, 35 were redeemed, 4 parcels were withdrawn, 5 parcels were sold, 5 parcels did not receive any bids and 1 parcel filed for bankruptcy. The Tax Collector recovered approximately \$202,000 in taxes, penalties, interests and fees.

SCOPE & METHODOLOGY

Part 7, Chapter 1, Section 4108.5 of the Revenue and Taxation Code requires an audit once every three years of the records and accounts of the Property Tax Redemption Process. Our audit involved a review of the redemption records and accounts from July 1, 2008 through June 30, 2011, to determine compliance with R&T Code §§ 4101 through 4379. Our audit also included a review of the information systems used in the redemption process managed by the Department of Information and Technology (DoIT). Our audit methodology included inquiry, auditor observation, testing the records and accounts of redemption collections, and reviewing compliance with laws regulations for redemption activities. Specifically, we:

- Verified redemption amounts and fees were appropriately charged and collected;

- Reviewed the appropriateness of certificates of redemption;
- Verified accounts and records of property tax receivables transferred to redemption;
- Verified the Treasurer-Tax Collector properly accounted for monies collected to the Auditor-Controller;
- Determined whether the abstracts lists (i.e., records of redemption) were adequately maintained; and
- Determined whether Redemption Installment and Bankruptcy Trust monies were accounted for properly.

Our review was conducted in accordance with the *International Standards for the Professional Practice of Internal Auditing*.

In any system of internal controls inherent limitations exist which may result in errors or irregularities occurring and not being detected. Limitations may include, but are not limited to, resource constraints, management override, and circumvention of internal controls by collusion. Further, projection of any evaluation of the internal controls to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies and procedures. Accordingly, our review would not necessarily disclose all weaknesses in the operating procedures, accounting practices and compliance with County policy.

CONCLUSION

Overall, we found the Property Tax Redemption Process generally is in compliance with R&T Code §§ 4101 through 4379. Further, we determined collection reports were promptly reported to the Auditor-Controller by the Tax Collector and certificates of redemption were adequately maintained and met content requirements. However, our audit disclosed several areas where corrective action is needed to improve the internal controls over the redemption process. The Tax Collector's Office, Auditor-Controller's Office, and Department of Information Technology initiated corrective action during the audit as noted in the management responses at Findings and Recommendations section. Following are details of the areas where improvements were needed:

1. Due to inaccuracies in the Bankruptcy Pay reports and the inability to generate year-end reports for both Installment Pay and Bankruptcy Pay plans, the Tax Collector's Office could not adequately monitor parcels under Installment Pay and Bankruptcy Pay Plans. As such the TCO relied on summary report totals without the detail reports. Without accurate detail reports, the TCO could not adequately monitor status of Installment Pay and Bankruptcy Pay Plans without looking at individual account details.
2. In our review of the Property Tax division's monthly reconciliation, unresolved variances between the general ledger IFAS (control account) and the SCIPS system (subsidiary account) were noted. The net unresolved variances for prior year Tax Receivable and Due To Other accounts were \$456,959.
3. SCIPS system issues reported to the Department of Information Technology are not always resolved in a timely manner.
4. Preventive controls are not in place to prevent unauthorized access and/or changes to SCIPS generated system reports utilized by the Tax Collector's Office.

5. Password security controls in accessing the SCIPS system do not ensure user passwords remain confidential to the individual user.
6. Redemption report used to determine payoff for taxes owed contained incorrect payoff dates which may result in under or overpayment of taxes.

The following pages provide a detailed description of the findings and the related recommendations. These recommendations will assist the departments to improve internal control for the accountability over the redemption process.

The departments' responses to the recommendations and a brief summary of the plan for corrective action are included in the accompanying schedule of findings and recommendations. The responses are the opinion of management and have not been subject to audit procedures or verification by the Auditor-Controller. All findings and recommendations are subject to the Auditor-Controller's follow-up review process.

Audit of Property Tax Redemption Process
July 1, 2008 through June 30, 2011
FINDINGS AND RECOMMENDATIONS

Treasurer-Tax Collector's Office (TCO)

1. Due to inaccuracies in the Bankruptcy Pay reports and the inability to generate year-end reports for both Installment Pay and Bankruptcy Pay plans, the Tax Collector's Office could not adequately monitor parcels under Installment Pay and Bankruptcy Pay Plans.

Condition:

Due to inaccuracies in the Bankruptcy Pay reports and the inability to generate year-end reports for both Installment Pay and Bankruptcy Pay plans, the department could not adequately monitor parcels under Installment Pay and Bankruptcy Pay Plans. As such the department relied on summary report totals without the detail reports. Without accurate detail reports, the TCO could not adequately monitor status of Installment Pay and Bankruptcy Pay Plans without looking at individual account details.

Criteria:

Proper monitoring is essential for an effective internal control system to ensure:

- The accuracy and validity of the entries and balances
- The records are accurately recorded
- To resolve discrepancies in a timely manner

Cause:

- The Bankruptcy Pay Plan report was programmed incorrectly by SCIPS/DoIT. The report contained parcels not in bankruptcy and/or parcels subject to installment pay plans.
- Detail reports for Installment Pay Plans and Bankruptcy Pay Plan cannot be generated for the fiscal year-ends under review.

Effect:

Without accurate detail reports, the TCO could not adequately monitor status of Installment and Bankruptcy Pay Plans without looking at individual account details. As such, we could not properly determine the accuracy of the totals for Installment and Bankruptcy Pay Plans.

Recommendations:

- A. Work with DoIT to correct the reports for the Installment Pay Plan and Bankruptcy Pay accounts.
- B. Reconcile and monitor monthly the detail report for Installment Pay Plans and Bankruptcy payments to the summary recap report and resolve variances, if any.

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FINDINGS AND RECOMMENDATIONS, Continued

Management Response:

The Tax Collector concurs with the finding.

SCIPS/DoIT has made the required corrections to the Redemption Installment Pay Plan monitor reports in the SCIPS system and the reports are generated timely. The TCO has submitted a request to SCIPS/DoIT to resolve all problems and make the necessary corrections to the Redemption Bankruptcy Information report. The TCO expect the completion of this request to be completed by SCIPS/DoIT within the next 60 days.

The TCO has a reconciliation process in place where as we completed daily reconciliations of the Redemption collections using the SCIPS Redemption Collections Recap reports. The TCO has implemented a Month End Installment Pay Plan Reconciliation that reconciles and monitors the secured redemption pay plans. The TCO will implement a Month End Redemption Bankruptcy Reconciliation once SCIPS has completed the requested corrections to the Redemption Bankruptcy Information report.

These improvements will now allow us to properly reconcile using the SCIPS system.

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FINDINGS AND RECOMMENDATIONS, Continued

Auditor-Controller's Office (ACO)

2. Unresolved variances between the general ledger (IFAS) and the SCIPS system were noted.

Condition:

In our review of the Property Tax division's monthly reconciliation of the Taxes Receivable and Due to Others accounts, we noted variances between IFAS and the SCIPS system were carried forward and not resolved in a timely manner. The net unresolved variances for prior year Tax Receivable and Due To Other accounts were \$456,959.

Criteria:

Sound internal control requires unresolved variances are resolved in a timely manner (within the accounting period).

Cause:

The Property Tax and Grant division personnel were aware of the variances. Management identified the lack of resources and time as two factors of why the variances remained unresolved.

Effect:

Without the timely identification of the unresolved variances, the Accounts Receivable and Due to Other accounts appear misstated.

Recommendations:

- A. Resolve identified variances for all redemption receivable and Due to Other accounts.

Management Response:

We agree with the auditor's comments. However, due to lack of time, resources and complexity of the discrepancies noted, it took longer for us to resolve the issue. During the course of the audit, we conducted further analysis of the variances and final determination has been made. Proper adjustments were initiated and the discrepancies in all of the affected accounts in the Redemption Roll have now been resolved.

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FINDINGS AND RECOMMENDATIONS, Continued

Department of Information Technology (DoIT)/ SCIPS System

3. SCIPS system issues reported to the Department of Information Technology are not always resolved in a timely manner.

Condition:

The ACO and TCO rely heavily on reports generated by the SCIPS system. The departments utilize various reports to book redemption collections and receivables. If any problems are encountered with the reports, the departments are required to submit a Mantis Issue report that logs issues and assigns them to System Analyst.

In our review of Mantis issues submitted by the ACO and TCO, we determined system issues reported to SCIPS/DoIT were not resolved in a timely manner. We identified seven (7) major unresolved issues for FYs 2011, 2010 and 2009. Five (5) of the 7 issues remained unresolved for over 100 days. Issues included reports formatted incorrectly resulting in inaccurate data, missing reports, reports showing no records, etc.

In addition, we identified twelve (12) minor unresolved issues for FYs 2011, 2010 and 2009. Two (2) of these minor issues were unresolved for over 365 days.

Criteria:

Sound internal control requires system issues reported be identified, managed, and resolved timely. Issue management plays an important role in maintaining stability and efficiency of the system.

Cause:

Operational business cycle and/or other priority issues impact the availability of system development which extends the time duration resolving pending issues.

Effect:

Unresolved system issues can delay or prevent departments from maximizing the use of the system. For example, we identified an unresolved issue over 100 days regarding release of liens report. Based on the Mantis issue submitted, unsecured complex payments made in the system with liens needed to be released were not showing in the release of lien report listing. The report was showing "No records have met selection criteria." As a result, the department was unable to apply payments for a period of time, staff had to manually review all accounts paid in full, and manually prepare a release of lien for parcels paid.

Recommendations:

- A. Resolve all outstanding Mantis issues; prioritize issues over 100 days old.
- B. Establish proper control and oversight of Mantis issues submitted to ensure timely resolution.

Management Response:

The department concurs with the finding.

The department's review of the Mantis Issue reporting system revealed that the average incident closure rate over the past two years is 59.8 days. Most often, issues are closed in 5 days. Reviewing the ten issues open the longest revealed that two issues (338 & 649) have not been handled correctly; while the other eight issues are waiting on the end user, resolved, or delayed due to priorities shifting.

The current SCIPS system is the result of a 36 month migration project which successfully redeployed the existing legacy functionality to a modern hardware and software platform. At the same time, SCIPS replaced their manual, limited access, trouble reporting system with the current web-based bug tracking system (Mantis). This new issue tracking system allows the end user the ability to report, update, and track their issues throughout the process using a web browser. Reports showing "No records have met selection criteria" indicate one of two possible conditions: 1) it is a valid report; there are no records to report on the system or 2) a result of limited testing during the migration, where only the technical capability of a successful run completion was tested and the report content was not validated. Inaccurate reports are generally fixed fairly quickly unless there are data anomalies. Currently there are no reported issues concerning reports showing "No records have met selection criteria".

SCIPS has a process in place which works fairly well. Typically, the end user will start the process by reporting an issue using the Mantis Bug Tracker system which SCIPS adopted as the primary issue and project development tracking tool. Once entered into the system, a Senior Systems Analyst in the SCIPS division will evaluate the issue and either request clarifying information from the submitted or assign the issue to the appropriate analyst for resolution. If both parties fail to monitor their issue, it could remain unresolved for quite a while. In the past, the Monthly end-user meeting had time allotted to review Mantis issues as well as remind everyone on the number of items waiting for testing or feedback. Attendance at these meeting has fallen off lately; so, implementing a different process for monitoring and oversight may be required.

The department will work on implementing a different process for monitoring and oversight.

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FINDINGS AND RECOMMENDATIONS, Continued

4. Preventive controls are not in place to prevent unauthorized changes and/or access to SCIPS system generated reports.

Condition:

SCIPS generated reports utilized by the TCO are generated in word formats and controls are not in place to prevent unauthorized changes and/or inappropriate access to SCIPS system generated reports and its data.

Criteria:

Management uses a system generated report to make critical business decisions and to record entries in the general ledger. Sound internal control requires system-generated reports to be accurate and free from potential manual manipulations. Specific control procedures may include restrictions on user access to only allow the system functions needed to perform assigned duties and password-protect file to restrict access to system generated data.

Cause:

System program was formatted to generate report in an editable form.

Effect:

SCIPS system generated reports can be manipulated (e.g., delete amounts, parcels, taxpayer's information, etc.)

Recommendations:

- A. Implement security locks to the stored reports folder.
- B. Restrict user's access to only the system functions needed to perform assigned duties.
- C. Password-protect SCIPS system reports to restrict and prevent unauthorized changes.

Management Response:

The department concurs with the finding.

During the Property System migration, the decision was made to produce all reports previously printed on paper with electronically delivered reports. The default format selected was PDF which provides some level of protection from editing and the default delivery method was network storage. SCIPS produces reports in a number of output formats ranging from Email to PDF. Any report that was previously delivered by electronic means from the legacy system was not changed. Due to system limitations at the time, a fair number of reports are still generated from the Cobol programs and delivered in MSWord format. The folder security implemented allows for read-only access by the designated department and end-user. Reports can be manipulated; however they cannot be saved back to the stored report repository. Folders on the network typically have some level of security applied. A review of the current properties set on the stored reports folder revealed that with the exception of one group, all permissions are set to read only. The Auditor group is the only user group requiring a modification to remove the write capability from the stored reports folder. Analysis of the Auditor processes using the folder and the correction of the properties is expected to be completed by April 30, 2012.

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FINDINGS AND RECOMMENDATIONS, Continued

5. Password security controls in accessing the SCIPS system do not ensure user passwords remain confidential to the individual user.

Condition:

In order to access the SCIPS system, users are required to have a user ID and password. A secure user password ensures accountability to access and any changes made to the SCIPS system. Based on our review, we have determined SCIPS administrators have access to user passwords and user identifications. As such, user passwords are not confidential to individual users. In addition, password controls such as expiration after a predefined interval, are not in place.

Criteria:

Safeguarding access to passwords and user IDs is an important part of an internal control structure. A unique user ID and passwords ensures accountability to access and any changes made to the system.

Cause:

Passwords are established by the user; however they are manually input into the system by the SCIPS administrator.

Effect:

Password data in the SCIPS system is accessible to SCIPS administrators without restriction.

Recommendations:

- A. Require SCIPS passwords expire at predefined interval and users reset passwords.
- B. Ensure passwords are confidential and are not shared or accessible.

Management Response:

The department concurs with the finding.

The current SCIPS security model was migrated from the legacy system and as a result, does not meet the standards of today's information management systems. The security model will need to be redesigned to incorporate today's best practices. While this is a project on the SCIPS project list, existing priorities and resource constraints prohibit any significant attention to this effort. Departmental priorities have steered toward additional functionality and automation to counter the reduction of staff in the user Departments.

The department will work with the Auditor-Controller's Office and Tax Collector's Office to resolve this issue.

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FINDINGS AND RECOMMENDATIONS, Continued

6. Redemption report used to determine payoff for taxes owed contained incorrect payoff dates.

Condition:

Redemption report (microfiche) used to determine payoff for taxes owed contained incorrect payoff dates. Based on work performed, we determined 7 out of 15 reports tested incorrectly reported the payoff amount for the current year as payoff amount for the subsequent year.

Criteria:

Proper internal control requires controls put in place to ensure transactions are valid, and reported completely and accurately.

Cause:

The redemption report (microfiche) was programmed incorrectly.

Effect:

The data contained in the redemption report (microfiche) may cause confusion as to the correct payoff amount. Based on the data contained in the report, readers could potentially assume the taxpayer paid in advance which may result in under or overpayment of taxes.

Recommendation:

- A. Perform an independent review of the reports to help prevent the occurrence of erroneous data.

Management Response:

The department concurs with the finding.

The department and the Tax Collector's Office are working together to resolve this issue.