

# AUDITOR-CONTROLLER/ TREASURER/TAX COLLECTOR



COUNTY OF SAN BERNARDINO

- 222 West Hospitality Lane, Fourth Floor  
San Bernardino, CA 92415-0018 • (909) 387-8322 • Fax (909) 386-8830
- 172 West Third Street, First Floor  
San Bernardino, CA 92415-0360 • (909) 387-8308 • Fax (909) 387-6716

**LARRY WALKER**  
Auditor-Controller/  
Treasurer/Tax Collector

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**Oscar Valdez, Assistant Auditor-Controller**  
Auditor-Controller/Treasurer/Tax Collector  
222 W. Hospitality Ln, 4<sup>th</sup> Floor  
San Bernardino, CA 92415

## **SUBJECT: PROPERTY TAX SECTION REVIEW**

### **Introduction**

In compliance with Article V, Section 6, of the San Bernardino County Charter and the Board of Supervisor's Policy on Internal Operational Auditing, we have completed a review of the tax increment pass-through funding for redevelopment agencies within the County region. Our review was conducted in accordance with the International Standards for the Professional Practice of Internal Auditing established by the Institute of Internal Auditors.

### **Background**

The Auditor-Controller/Treasurer/Tax Collector-Property Tax Section (ATC PTS) compiles assessed valuations for all agencies; checks and proofs the tax rolls by code area; enters all penalties and corrections; maintains the tax charges against the County Tax Collector as well as sets and releases subdivision tax bonds; and apportions all property taxes to approximately 600 taxing entities Countywide. ATC PTS has a staff of 10 including two supervisors and a manager. The County of San Bernardino established agreements with the Redevelopment Agencies (RDA) to pass through property tax dollars to the affected tax entities. There are currently 27 redevelopment agencies within the County, 16 of which have negotiated pass-through agreements with the County.

ATC PTS identified errors affecting certain pass-through transactions in the fall of 2011. The Assistant Auditor-Controller over ATC PTS requested ATC IAS to perform an audit of the preventive and detective control activities of the ATC PTC function.

### **Objectives and Methodology**

Our overall objective was to determine whether the preventive and detective controls within ATC PTS are properly designed to ensure input is accurate, complete, and reflects the RDA agreements and amendments. We interviewed ATC PTS staff directly involved in the tax increment pass-through process and made observations on July 26, 2011 to gain an understanding of how the tax increment procedures are performed.

### **Conclusion**

Based on our observations and discussions with ATC PTS staff, we concluded that ATC PTS lacked sufficient preventive and detective controls to prevent errors from occurring within the tax increment pass-through process.

We sent a draft report to ATC PTS on October 12, 2011 and discussed our observations with management on October 26, 2011. ATC PTS's responses to our recommendations are included in this report.

### **Findings and Recommendations**

We have identified and listed the findings for this engagement, along with our recommendations for improvement.

#### **Finding 1: Improvement needed over written policies and procedures for the RDA tax increment process.**

As a component of the COSO Framework, the Control Environment serves as the cornerstone of an entity's overall internal control system as it sets the tone of the organization. The responsibilities of management are conveyed through the basic elements that make up the control environment, including developing and documenting policies and procedures. Comprehensive written policies and procedures serve as a department's primary reference tool for business processes, personnel responsibilities, departmental operations, and proper execution and recording of transactions. Additionally, policies and procedures can be used as an effective training resource for employees. ATC PTS has not established comprehensive written policies and procedures governing the RDA tax increment pass-through process. Therefore, neither management nor ATC PTS staff have an adequate reference source describing how the operations of the ATC PTS are to be executed.

Previous management did not fully document the policies and procedures that were instrumental to executing the RDA tax increment pass-through process. If ATC PTS continues to operate without sufficient documented policies and procedures, the following could potentially result:

- Inaccurate and unreliable financial records resulting from improper recording of transactions
- Inconsistent practices among ATC PTS staff
- Processing errors
- Inability to enforce employee accountability
- Less management oversight of ATC PTS's various operational functions, including quality assurance processes for work performed by ATC PTS staff
- Monitoring activities' impairment due to insufficient operational standards with which to align the day-to-day functions of the department

#### **Recommendation:**

We recommend that management develop and document all significant policies and procedures that encompass the overall RDA tax increment process. We further recommend that management communicate these policies and procedures to all ATC PTS personnel and ensure the resources are accessible to personnel at all times. ATC PTS personnel should also conduct periodic reviews/updates of policies and procedures due to changes in industry practices or regulatory codes. Additionally, an ongoing process should be used to reinforce the policies and procedures of the RDA tax increment process and documentation should be maintained showing employees' acceptance of their responsibilities.

**Management's Response:**

We concur; management is currently in the process of developing and documenting all significant policies and procedures for the Property Tax Section (PTS). Although the current ruling by the Supreme Court of California on ABX1 26, RDA Dissolution Act, was upheld allowing the legislature to dissolve RDA's on February 1, 2012 there is still a need for the County Auditor-Controller to determine the amount of property taxes that would have been allocated to each RDA had they not been dissolved. Management is working closely with CALSACA's Property Tax Manager's group to develop uniform guidelines for the implementation of ABX1 26. Upon approval by the State Department of Finance (DOF) management will develop and document internal policies and procedures for PTS.

Management will communicate such policies and procedures verbally at weekly (ABX1 26 implementation) staff meetings and will be referred to the centralized location where the written policies and procedures may be accessed for reference when needed. Management attends property tax conferences, actively participates in property tax forums and in the Property Tax Managers Group Manual Committee to keep up with industry practices and regulatory changes. Updates will be made on policies and procedures and communicated to staff as needed. To reinforce the policies and procedures, PTS staff will play an active role in documenting and presenting the policies and procedures at staff meetings. In addition, management will incorporate the expectation of PTS staff to be familiar with policies and procedures approved and implemented by management in their Memo of Expectations (MOE), obtain documentation of MOE notice and maintain the MOE documenting employees' acceptance of their responsibilities in their personnel file.

Expected Date of Implementation: 06/30/2013

Due to pending clarification from the State DOF and ongoing changes that will be necessary to comply with ABX1 26 we do not anticipate comprehensive policies and procedures to be completed until 06/30/2013.

**Auditor's Response:**

ATC PTC's planned actions will correct the deficiencies noted in the finding.

**Finding 2: Improvements were needed in the RDA pass-through calculation process.**

Important responsibilities of management are to develop and maintain a control structure that is conducive for ATC PTS staff to accurately and efficiently fulfill the objectives of the organization. Additionally, the presence of a routine quality assurance process (i.e., performing variance analysis, reconciling system reports with source documents, etc.) would serve to strengthen management oversight of ATC PTS's operational functions. Through inquiries with ATC PTS staff on July 26, 2011, we discovered there was no certainty that all of the negotiated RDA agreements were filed in the Property Tax Section. Additionally, with regards to the agreements that were actually maintained in Property Tax, departmental staff could not ascertain whether or not the RDA files contained the most current agreements and/or amendments. We also observed RDA files stored in cubicles instead of storing them in the file cabinet. Therefore, we were unable to determine whether the formulas entered into the PIMS Auditor Tax Processing (PIAU) system were consistent with the information stated in the most current RDA agreements.

If the RDA agreements and/or amendments are not current and available for staff's reference, staff cannot verify that the information input in the PIAU system is accurate.

**Recommendation:**

To improve the RDA tax increment calculation process, we recommend that management:

- Ensure that the most current RDA agreements and amendments are kept within Property Tax for staff's use.
- Inquire with the pass-through agencies to acquire the most current pass-through agreements.
- Create and maintain a process to secure the agreements from loss but allow staff to review them when necessary for their job duties.
- Initiate and maintain an annual process in which the RDAs that use the County to allocate the pass-through agreements are contacted to verify that all new amendments were sent to Property Tax.
- Ensure that a higher-level staff member reconciles items processed through the PIAU system with the corresponding agreement on file.
- Develop and implement a procedure to compare two or more years of pass-through dollars for each subrecipient to look for unexpected changes in dollar amounts before the data is input into the PIAU system.

**Management's Response:**

We concur; there is a need to improve the RDA pass-through calculation process. Although the current ruling by the Supreme Court of California on ABX1 26, RDA Dissolution Act, was upheld allowing the legislature to dissolve RDA's on February 1, 2012 there is an even greater need to strengthen controls over RDA pass-through calculations due to the increased responsibilities for the County Auditor-Controller. County Auditor-Controller's will now be responsible for calculating and disbursing property tax revenues for all pass-through agreements held by recently dissolved RDA's.

Management is currently in the process of;

- Requesting and obtaining all current pass-through agreements from the Successor Agencies of the recently dissolved RDA's.
- Creating organized Successor Agency (physical and electronic) files. Pass-through agreements will be logged, indexed, scanned and filed upon receipt.
- Identifying a secure filing cabinet location for Successor Agency files. Implementing policies and procedures requiring staff to log out files when needed and prohibiting the removal of documents from files.
- Implementing procedures requiring PTS staff to reconcile Redevelopment Property Tax Trust Fund (RPTTF) on a semi-annual basis. Property tax revenue passed-through to entities per agreements will be identified in these reconciliations. The PTS Manager or Supervisor will be responsible for reviewing reconciliations for accuracy.
- PTS staff or designee will perform pass-through calculations and prepare estimates of amounts to be allocated and distributed to entities on May 1<sup>st</sup> and November 1<sup>st</sup> as required by ABX1 26. At this time a variance analysis will be done to compare current year and prior year data.

