

GOVERNMENT OF THE DISTRICT OF COLUMBIA
Office of the Chief Financial Officer



Office of Integrity and Oversight

MEMORANDUM

TO: Stephen M. Cordi, Deputy Chief Financial Officer
Office of Tax and Revenue

Lasana Mack, Deputy Chief Financial Officer/Treasurer
Office of Finance and Treasury

Anthony Pompa, Deputy Chief Financial Officer
Office of Financial Operations and Systems

FROM: William J. DiVello, Executive Director
Office of Integrity and Oversight *William J. DiVello*

DATE: August 2, 2010

SUBJECT: Final Report on the Review of Income Tax Secured Bond Fund at OTR and Related Agencies (**Report No.: IA:OTR:2911-C15**)

This final report summarizes the results of the Office of Integrity and Oversight's (OIO) Review of Income Tax Secured Bond Fund at the Office of Tax and Revenue (OTR) and Related Agencies. The purpose of this audit was to examine and evaluate the adequacy of internal controls over the revenue collection and deposit process to ensure that internal controls are working as designed and functioning properly; assess the efficiency of the process; and also to assess the risk of fraud and misappropriation of District funds.

This report contains seven findings detailing the conditions we found during our audit. Overall, we found that dedicated revenues collected and reported by the Returns Processing Administration's (RPA) Receipt and Control Unit, lockbox contractors, and via electronic fund transfers are generally deposited in designated bank accounts and posted in appropriate accounts in the District's System of Accounting and Reporting (SOAR). The dedicated revenues are then transferred to accounts designated for the payment of principal and interest due to bondholders with the balance transferred to the general fund as required. However, we noted opportunities for the OCFO to strengthen controls surrounding the receipt and reconciliation of dedicated funds.

The Office of Tax and Revenue, Office of Finance & Treasury, and Office of Financial Operations and Systems acknowledged and agreed with our findings and recommendations and provided corrective action steps to address the issues noted. The agency planned actions are responsive to the issues we identified.

Should you have any questions on the final report or need additional information, please contact me, at (202) 442-6433 or a member of your staff may contact Tisha Edwards, Senior Audit Manager, at (202) 442-6446.

Attachments

cc: Natwar M. Gandhi, Chief Financial Officer, Government of the District of Columbia
Angell Jacobs, Chief of Staff, OCFO
Glen Groff, Director of Operations, OTR

**GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE CHIEF FINANCIAL OFFICER
OFFICE OF INTEGRITY AND OVERSIGHT**

**AUDIT OF THE INCOME TAX
SECURED BOND FUND
AT THE OTR AND RELATED AGENCIES
FOR THE PERIOD
MARCH 23, 2009 THROUGH JUNE 30, 2009**



FINAL REPORT

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AUDIT OF INCOME TAX SECURED BOND FUND
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Executive Summary

Pursuant to the annual work plan of the Office of Integrity and Oversight (OIO), the internal auditors performed an audit of the Income Tax Secured Bond Fund for the period March 23, 2009, through June 30, 2009. The purpose of this audit was to examine and evaluate the adequacy of internal controls over the revenue collection and deposit process to ensure that internal controls are working as designed and functioning properly; assess the efficiency of the process; and also to assess the risk of fraud and misappropriation of District funds.

The Income Tax Secured Bond Fund (Fund) was established pursuant to the Income Tax Secured Bond Authorization Act of 2008 (D.C. Code §47-340.26-36) as a fund separate from the general fund for the collection of tax revenues dedicated for the payment of interest and principal of bonds issued for the financing of capital projects. These dedicated revenues consist of business franchise (corporate and unincorporated) and individual income taxes accompanying annual income tax returns (final payments), estimated quarterly payments (declarations) and income taxes withheld from employees' wages by employers (withholdings). These dedicated revenues are received in designated post office boxes and collected by the Office of Tax and Revenue (OTR) and by lockbox contractors; they are also received via electronic funds transfer.

Results

Overall, we found that dedicated revenues collected and reported by the Returns Processing Administration's (RPA) Receipt and Control Unit, lockbox contractors and via electronic fund transfers are generally deposited in designated bank accounts and posted in appropriate accounts in the District's System of Accounting and Reporting (SOAR). The dedicated revenues are then transferred to accounts designated for the payment of principal and interest due to bondholders with the balance transferred to the general fund as required.

Our audit however revealed opportunities for the OCFO to strengthen controls surrounding the receipt and reconciliation of dedicated funds within the RPA's Receipt and Control Unit. Our audit also noted several deficiencies such as, deposit delays within the RPA Receipt and Control Unit; inadequate security controls over the area where tax collections are processed to monitor all operations and to prevent the accidental or intentional misplacement of tax collections; weak reconciliation controls and coordination between OTR and the Office of Financial Operations and Systems (OFOS); duplicate transfers of individual income taxes received via electronic funds transfers in bank ID 882 totaling \$6.4 million for the period; OTR's failure to provide the third party vendor with new instructions on where to deposit individual income taxes; and lack of coordination between the various administrations within OTR to ensure implementation of the bond fund.

Finally, we found no evidence of whether OTR and/or OFT are monitoring bank transfers of dedicated revenues performed daily by banks based on the amount deposited, net of returned items. Once transferred, banks notify OFT for the recording of transfers in SOAR. We inquired from OFT officials who responded that no one is responsible for verification of transfers and that

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no documentation is maintained evidencing that the amounts transferred agree with amounts deposited, net of returned items.

Summary of Findings:

1. RPA's Receipt And Control Unit: We found no evidence of supervisory reviews of the processing of mail including envelopes containing tax payments by RPA's Receipt and Control Unit. We also found that RPA's Receipt and Control Unit lacks controls to ensure that all tax payments received are deposited completely in designated bank accounts. In addition, we found that the functions of scanning, balancing, and coding of tax payments are performed by the same individual, increasing the risk of errors in coding not detected and timely corrected.
2. Physical Security Controls: We found that security controls over the Receipt and Control area, where in-house tax collections including dedicated revenues are processed needs improvement to adequately monitor all operations and to prevent tax collections from being accidentally or intentionally misplaced. We also observed that the Mail and Extraction areas are not separated and staff from Extraction have access to the Mail area to pick up mail for processing where envelopes containing tax payments remain unsecured and unattended before they are placed in a machine that sorts and counts mail for processing.
3. Guidelines for Bank Deposits: We found that the lack of deposit guidelines at RPA's Receipt and Control Unit is a contributing factor to the wide disparity in the number of business days from receipt to the deposit of tax payments in designated bank accounts. Our test work found that 13 of the 45 bank deposits reviewed, tax payment receipts were delayed from 1 to 50 business days after receipts before deposited (see *Exhibit 1*).
4. Combo Payments Containing Dedicated and Non-dedicated Revenues: The Remittance & Deposit unit may receive one check from a taxpayer that is for payment of multiple tax types. This is referred to as a combo payment. While there is a policy in place to handle these payments, our review found that non-dedicated revenues totaling \$520,710 were incorrectly deposited in bank ID 872 for dedicated revenues and ultimately to the revenue holding account (Bank ID 882) (see *Exhibit 2*).
5. OFOS' Monthly Bank Reconciliation Directive: We found no evidence that OTR submitted monthly bank reconciliation reports to the Office of Financial Operations and Systems in accordance with directive issued by the Deputy Chief Financial Officer for Financial Operations and Systems. Due to OTR's failure to submit required reports, OFOS continued performing bank reconciliations on OTR bank accounts through an undocumented process which lacked timeframes for OTR to resolve reconciling items (see *Attachment A*). We also found deficiencies with supervisory reviews of bank reconciliations performed by OFOS.
6. Resolving Unreconciled Items: We found that RAA's documented procedures ensuring that all revenue and deposit transactions are reconciled, did not include requirements for the

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timely resolution of differences in ITS. Additionally, the new process established by Returns Processing Administration, in which bank reconciliations performed by the OFOS and OTR's Revenue Accounting Administration (previously sent directly to responsible officials) are now sent to officials with RPA before they are forwarded to employees responsible for the resolution of reconciling items instigate delays in the resolution process.

7. Monitoring Bank Transfers: We found no evidence that OTR is performing reconciliations of transfers of dedicated revenues deposited in designated bank accounts established for the payment of interest and principal due to bondholders. We also found no evidence that OTR and/or OFT are monitoring bank transfers (see *Exhibit 3*).

Recommendations

Our recommendations are presented in the respective sections of this report.

Agency Response:

The Office of Tax and Revenue (OTR), Office of Financial Operations and Systems (OFOS) and Office of Finance & Treasury (OFT) concurred with the findings and recommendations noted herein. See complete agency responses at Attachment B.

OIO Auditor Evaluation:

The agency planned actions are responsive to the issues we identified, and when fully implemented should satisfy the intent of our recommendations.

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BACKGROUND

The Income Tax Secured Bond Fund (Fund) was established pursuant the Income Tax Secured Bond Authorization Act of 2008 (D.C. Code §47-340.26-36) as a fund separate from the general fund for the collection of tax revenues dedicated for the payment of interest and principal of bonds issued for the financing of capital projects. These dedicated revenues consist of business franchise (corporate and unincorporated) and individual income taxes accompanying annual income tax returns (final payments), estimated quarterly payments (declarations) and income taxes withheld from employees' wages by employers (withholdings). These dedicated revenues are received in designated post office boxes and collected by the Office of Tax and Revenue (OTR) and by lockbox contractors; as well as via electronic funds transfer.

The Official Statement, prepared in connection with the issuance and sale of Fund bonds, describes the collection of dedicated revenues and payment of interest and principal on bonds. Beginning March 2009, dedicated revenues are to be deposited daily into Collection Accounts maintained by the Collection Agent (Wachovia bank) and transferred daily to the Revenue Account maintained by the Trustee (Wells Fargo bank ID 882). The following are bank IDs for Collection Accounts:

- OTR In-House – Bank ID 872 for all dedicated revenues
- Electronic Funds Transfers – Bank ID 725 for all dedicated revenues
- Lockbox Contractor
 - Bank ID 217 for Withholdings
 - Bank ID 229 for Individual Income Taxes
 - Bank ID 405 for Business Franchise Taxes

In months other than April, May and June, dedicated revenues deposited into bank ID 882 are transferred daily to the DC Custodial Account (Bank of America bank ID 200). Beginning with the first day of each month in April, May and June, dedicated revenues are retained in bank ID 882 until 1/3 of the amount due (\$39 million for fiscal year 2009) for the payment of principal and interest in December and interest in June of the following year is accumulated and transferred to the Accumulation Account (Wells Fargo bank ID 883). Once that amount has been reached (\$13 million each month in April, May, and June), dedicated revenues continue to be transferred to bank ID 200.

Processing of Dedicated Revenues

Dedicated revenues collected in-house by OTR are processed and prepared for deposit by OTR's Returns Processing Administration (RPA) and picked up daily by an armored car company for transportation and deposit into Collection Account bank ID 872 at Wachovia Bank. Lockbox contractors process and deposit revenues directly into Collection Accounts bank IDs 217, 229, and 405 and, separately, send related tax information daily to OTR's Tax Systems Group (TSG) formerly known as Information Systems Administration (ISA) in electronic form for uploading into OTR's Integrated Tax System (ITS). At the inception of the secured fund, electronic funds

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transfers for all tax types including dedicated revenues were first deposited directly into bank ID 406 then transferred to bank IDs 725. Beginning September 2009, they are deposited directly into bank ID 725. Electronic taxpayer information is also received by TSG and uploaded into ITS.

The accounting for the dedicated revenues involves several OCFO agencies. In addition to the processing and depositing of dedicated revenues by OTR's RPA and lockbox contractors, the Office of Finance and Treasury(OFT) records transfers of dedicated revenues between bank accounts in the District's System of Accounting and Reporting (SOAR). OTR's Revenue Accounting Administration (RAA) and the Office of Financial Operations and Systems (OFOS) perform bank reconciliations; and the OCFO's Office of Revenue Analysis (ORA) produces annual revenue projections and performs monthly comparisons between estimated revenues with actual and investigates variances.

Tax Collections Processed by OTR (In-house)

Daily, staff with RPA's Receipt and Control Unit collects from designated post office boxes envelopes containing tax returns and tax payments and brings them to OTR for processing. Once at OTR, the contents are removed from envelopes by staff with the Extraction unit and sorted by the tax type (individual or business franchise) and whether or not they contain tax payments. Tax returns that do not contain tax payments are forwarded to the Code and Edit unit for review, and then forwarded to the Document Preparation unit for preparation, and to Scanning Unit for scanning in the Integrated Data Capture System (IDCS).

Envelopes with tax payments are further sorted by whether or not they are accompanied by a tax return and/or tax payment voucher containing taxpayer information including the taxpayer's name, taxpayer identification number, tax type, and tax year. Tax payments without a tax return or a payment voucher (unclean) are forwarded to the Payment Perfection unit for research and for the generation of a payment voucher (for tax years 2006 to the present) or a keypunch document (tax year 2005 and earlier). Tax payments with payment vouchers identifying the taxpayer (clean) are forwarded to the Code and Edit unit for review and for verification that the amount of the payment agrees with the tax liability in tax returns and with the payment voucher.

Clean payments with payment vouchers verified by the Code and Edit unit are forwarded to the Remittance Deposit unit for review and for scanning in the NCR machine, a subsystem of IDCS. Unclean payments with keypunch documents generated by the Payment Perfection unit are forwarded to the Document Preparation unit for review and preparation, then to the Scanning Unit for scanning into BankTec, another subsystem of IDCS that processes letter size (8 ½ by 11 inches) documents. Once scanned, unclean payments and keypunch documents are forwarded to the Remittance Deposit Unit. After scanning, staff with the Remittance Deposit unit codes tax payments in NCR, prepares deposit tickets for deposit into bank ID 872 and generates reports for the preparation of vouchers for recording in SOAR. Tax returns and tax payments scanned in IDCS are uploaded daily to ITS.

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Tax Collections Processed by Lockbox Contractors and Electronic Funds Transfers

Lockbox contractors send through secured transmissions taxpayer information associated with tax payments processed daily and deposited into Collection Accounts to ISA for uploading in ITS. The following day, lockbox contractors send via courier deposit information to RPA's Accounting and Reconciliation for the preparation of vouchers for the recording in SOAR.

RPA's Accounting and Reconciliation unit is responsible for recording in SOAR tax collections processed by lockbox contractors and electronic funds transfers. RPA's Accounting and Reconciliation unit also periodically reviews bank activity and investigates and records in SOAR debits and credits posted to bank accounts. In addition, they are responsible for the resolution of reconciling items in bank reconciliations performed by the Office of Financial Operations and Systems (OFOS) and OTR's RAA. To investigate bank debits and credits and resolve reconciling items, RPA's Accounting and Reconciliation Unit previously spoke directly with bank representatives. However, on or around August 2009, RPA requested that inquiries of bank information be channeled through officials with RPA before is forwarded to the bank's COTR and finally to banks for research.

Electronic Funds Transfers: Electronic funds transfers are deposited directly into respective Collection Accounts with tax payment information and also sent to TSG for uploading into ITS. The following day, RPA's Accounting and Reconciliation Unit prepares the vouchers for the recording in SOAR.

Prior to the establishment of the Fund, electronic funds transfers of all tax types including dedicated revenues were deposited into bank ID 406 then transferred to respective bank IDs, and dedicated revenues are transferred to Custodial Account bank ID 200. In March 2009, when the Fund was created, bank ID 725 was established for the deposit of electronic funds transfers of dedicated revenues. The deposits into bank ID 725, however, did not occur as anticipated but individual income taxes, a source of dedicated revenues, were deposited into bank ID 229 while franchise business taxes (corporate and unincorporated) continued to be deposited into bank ID 406 through the end of August 2009. To record the deposits in SOAR, RPA's Accounting and Reconciliation Unit first identifies the bank account and related tax type posted to ITS for entry of electronic funds transfers in the appropriate bank ID and agency object in SOAR. RPA's Accounting and Reconciliation Unit was recording individual income taxes to bank ID 229 and franchise business taxes to bank ID 406 based on the bank account where they were deposited.

Separately and to compensate for this deficiency, RPA's Systems and Forms Unit, during the period from March to the end of August 2009, manually segregated, reports of electronic funds posted to ITS, dedicated revenues from other tax types and e-mailed the modified reports to the bank requesting the transfer of dedicated revenues from bank ID 406 to bank ID 725. However, because officials with RPA's Systems and Form were not aware that individual income taxes were not being deposited into bank ID 406 but instead directly into bank ID 229; the requests e-mailed to the bank effectively caused the duplicate transfer of individual income taxes to bank

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ID 882, once through bank ID 229 and the other through bank ID 406. Beginning in September 2009, electronic funds transfers for dedicated revenues are deposited directly to bank ID 725.

Bank Transfers

Transfers of dedicated revenues are made daily by Wachovia bank from Collection Accounts (bank IDs 217, 229, 405, 725, and 872) to the Revenue Account maintained by Wells Fargo Revenue Account (bank ID 882). The results of our inquiries suggest that these bank transfers are made independently by Wachovia based on the amounts of deposits net of returned items. Wachovia bank e-mails daily notifications to officials with the Office of Finance and Treasury (OFT) for the preparation of vouchers for the recording of bank transfers in SOAR.

Bank Reconciliations

Monthly, OTR's Revenue Accounting Administration (RAA) performs reconciliations of *bank deposits* by comparing deposits between bank statements, SOAR, and ITS. Completed deposit reconciliations are sent to OTR's Returns Processing Administration for resolution of reconciling items for the current period only. Also, RAA follows up with RPA on the resolution of unreconciled items from prior periods.

The Office of Financial Operations and Systems (OFOS) perform reconciliations of *all bank activity* by comparing deposits and transfers in bank statements with SOAR. Unlike deposit reconciliations prepared by RAA, bank reconciliations prepared by OFOS list unreconciled items from prior periods. OFOS also follows up with both RPA and RAA on the resolution of reconciling items.

Revenue Projections

The ORA prepares annual estimates of tax revenues including dedicated revenues by analyzing national as well as local economic trends, among others. The ORA also performs monthly comparisons of revenue estimates with revenues collected, investigate abnormal variances, and when necessary, adjust projected revenues.

OBJECTIVES, SCOPE AND METHODOLOGY

The objectives of this audit were to:

- Assess whether the existing controls over the income tax payment process are adequate, and are operating effectively;
- Ensure that all tax payments received during the period under review were processed and deposited promptly;
- Verify whether all tax payments collected are properly recorded in SOAR and promptly deposited by RPA;

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- Compare the projected revenue to actual revenue to determine any variances;
- Determine whether reconciliations of deposits between bank accounts, SOAR, and ITS are being performed by RAA on a monthly basis;
- Determine whether reconciliations of bank activity between SOAR and Bank Accounts are being performed by OFOS on a monthly basis; and
- Verify whether remittances deposited daily in Wachovia bank accounts related to the Fund are transferred to Wells Fargo account and that Wells Fargo transfers those remittances to Bank of America custodial account except for amounts retained in April, May and June to cover the principal and interest due to bondholders.

To accomplish our objectives, we interviewed appropriate District officials at selected agencies, reviewed pertinent supporting documents and applicable policies and procedures, obtained data from SOAR, identified the authority for the Income Tax Secured Bond Fund and related documentation, and reviewed bank transfers to ensure they are accurate and net of returned items, selected a sample of dedicated revenues processed and deposited by RPA's Receipt and Control unit, and determined whether recorded properly and deposited promptly, and reviewed bank reconciliations performed by OFOS and RAA to determine whether performed on monthly basis. We also inquired of officials with:

- Returns Processing Administration's Receipt and Control and documented their procedures for the processing and depositing tax payments received including dedicated revenues;
- responsibility for security controls over the area where tax payments including dedicated revenues are processed;
- RPA's Accounting and Reconciliation and documented their recording in SOAR of dedicated revenues processed and deposited by lockbox contractors and those received via electronic funds transfers;
- the Office of Revenue Analysis and documented their procedures for revenue projections, how they compare revenue estimates with actual, and how they investigate variances;
- the Office of Financial Operations and Systems and OTR's Revenue Accounting Administration and documented their preparation of bank reconciliations (OFOS) and deposit reconciliations (RAA); and
- the Office of Finance and Treasury and documented their recording of bank transfers between accounts used to deposit dedicated revenues and accounts used for the payment of interest and principal due to bondholders.

RESULTS OF AUDIT

We found that dedicated revenues are generally deposited by RPA's Receipt and Control Unit into designated bank accounts and recorded in the appropriate accounts in SOAR. We also found that dedicated revenues both received and processed by lockbox contractors and via electronic funds transfers are generally deposited in designated bank accounts and recorded in

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appropriate accounts in SOAR. Dedicated revenues are then transferred to accounts designated for the payment of principal and interest due to bondholders with the balance transferred to the general fund.

We found however several internal controls weaknesses that OTR management needs to improve on such as: controls within RPA's Receipt and Control are not adequate to ensure that dedicated funds are processed properly and deposited completely in designated bank accounts; lack of deposit guidelines at RPA's Receipt and Control Unit is a contributing factor to the wide disparity in the number of business days from receipt to the depositing of tax payments in Collection Accounts that ranged from one to 50 business days after received; inadequate security controls over the area where tax collections are processed to monitor all operations and to prevent tax collections from being accidentally or intentionally misplaced.

In addition, we found no evidence that the Office of Tax and Revenue submitted required monthly bank reconciliation reports in accordance with a directive that requires all CFO offices to submit them monthly to the Office of Financial Operations and Systems. Due to OTR's failure to submit these required reports, OFOS continued preparing bank reconciliations on OTR bank accounts through an undocumented process which lacked timeframes for OTR to resolve reconciling items. We also found deficiencies with supervisory reviews of bank reconciliations performed by OFOS. Similarly, we found that the procedures for preparing deposit reconciliations by the Revenue Accounting Administration does not include requirements for the timely resolution of differences in OTR's Integrated Tax System.

Further, we found no evidence that the OCFO is reconciling transfers of dedicated revenues from Collection Accounts to the Revenue Account (bank ID 882). During our reconciliation of bank transfers, we found duplicate transfers of individual income taxes received via electronic funds transfers into bank ID 882 totaling \$6.4 million for the period of our review. OTR failure to provide the third party vendor with new instructions on where to deposit individual income taxes contributed to these duplicate transfers. The lack of coordination within RPA's units was another contributing factor. We also found no evidence of whether OTR and/or OFT are monitoring bank transfers. Transfers of dedicated revenues are performed daily by banks based on the amount deposited, net of returned items. Once transferred, banks notify OFT for the recording of transfers in SOAR. We inquired of OFT officials who responded that no one is responsible for verification of transfers or that documentation is maintained evidencing a verification that the amounts transferred agree with amounts deposited net of returned items.

Finally, the new process established by Returns Processing Administration for the receipt and distribution of bank reconciliations and for the handling of inquiries for the timely resolution of reconciling items needs to be streamlined. The additional steps extend the time, sometimes for several months, for obtaining bank information for the timely resolution of reconciling items.

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FINDINGS

1. RPA's Receipt And Control Unit

In our walkthrough and testing of the in-house process, we found no evidence of supervisory reviews of the processing of mail by RPA's Receipt and Control Unit, especially over returns with tax payments; over the manual generation of payment vouchers when not included with tax payments; over the scanning, balancing, coding of tax payments; and over the preparation of tax payments for deposit. There was a lack of tracking of returns from receipt to final disposition to ensure all items received are processed, and a lack of segregation of duties in the deposit area.

a. Lack of Supervisory Review

Specifically, we noted that supervisors do not review the work of staff persons to ensure items are processed accurately. Staff with the Extraction Unit removes tax returns and tax payments from envelopes mailed by taxpayers and batch them for review by Code and Edit or for research by Payment Perfection when received with no taxpayer information. The Code, Edit and Payment Perfection Unit, after taxpayer information has been identified, forward tax payments to the Remittance Deposit Unit for scanning, coding, and preparation for deposit. The preparation of bank deposits is a manually-intensive process requiring that tax payments scanned and uploaded to spreadsheets be separated by tax type and by bank. All of these functions are performed with no evidence of supervisory review.

During our review of deposits selected for testing, we found fourteen deposits for tax types other than dedicated revenues totaling \$520,710 were incorrectly recorded in SOAR bank ID 872. As of the date of this report, RPA had not responded to our request for explanation for these incorrect entries.

b. Lack of Tracking of returns.

Returns and payments are not tracked from receipt to final disposition. The RPA's Receipt and Control Unit lacks a tracking mechanism to ensure that all tax payments received are deposited completely in designated bank accounts. While staff with Extraction, Code and Edit, Payment Perfection, and Remittance Deposits each maintains logs with daily counts of mail processed and forward them to supervisors who first reconcile their numbers with each other before submitting them to the Chief, Receipts and Control and other officials with RPA we found no evidence that the logs are used to ensure that all tax payments received are deposited. Instead, they are used to monitor staff production and to plan for staffing levels.

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c. Lack of Segregation of Duties

Additionally, we found that the functions of scanning, balancing (visual verification of tax payments scanned and the keying of tax payment amounts), and coding of tax payments are performed by the same individual.

The *Standards for Internal Control in the Federal Government* issued by the U.S. Government Accountability Office (GAO) provides the framework for the development and establishment of sound internal controls by federal agencies. Page 11 states that "Control activities occur at all levels of the entity. They include a wide range of diverse activities such as approvals, authorizations, verifications, reconciliations, performance reviews, maintenance of security, and the creation and maintenance of related records which provide evidence of execution of these activities as well as appropriate documentation." It also states on page 14 that "Key duties and responsibilities need to be divided or segregated among different people to reduce the risk of error or fraud."

The Chief, Receipt and Control, acknowledged that no supervisory reviews are performed but the work of employees who frequently commit errors is reviewed. The Supervisor, Remittance Deposits stated that she frequently observes the work of her employees and closely monitors large deposits although she admitted that the results of her review are not documented and she leaves no proof of her supervisory review. She also indicated that her preference is that the scanning, balancing, and coding of tax payments be segregated but that is not always the case.

The absence of supervisory reviews, or evidence that they were performed, may inadvertently foster an environment susceptible to errors and inaccuracies. In addition, the lack of a tracking mechanism to ensure that all tax payments received are deposited in respective bank accounts increases the risk of loss or misappropriation. The functions of scanning, balancing, and coding of tax payments performed by the same individual also increases the risk that errors in coding are not detected and corrected timely by another employee before they are deposited in bank accounts.

Recommendations:

We recommend that the RPA's Receipt and Control Chief:

- 1) Develop and establish documented procedures for periodic reviews by supervisors of all units involved in the processing of tax payments ensuring that they describe the documentation required to evidence the performance of supervisory reviews.
- 2) Determine the causes for tax types other than dedicated revenues recorded in SOAR bank ID 872. If incorrectly recorded, complete correcting entries and required transfers to respective accounts.

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- 3) Develop and establish a mechanism to track and account for each tax payment, from the time it is picked up from post offices to the time is deposited into designated bank accounts. Consider, for example, a process in which staff with Extractions runs an adding machine tape of all tax payments in the batch picked up from the Mail area, listing the dollar amount of each tax payment and number and dollar amount of all tax payments in the batch. Such a tape, initialed and dated by staff with Extractions, may be stapled to the Return Routing Transmittal accompanying the batch and used to track the movement of tax payments throughout all units responsible for processing the batch. Said tape may also be used to identify tax payments missing on the batch that may have been accidentally or intentionally misplaced.

- 4) Develop and establish documented procedures for assigning a different staff with Remittance Deposits to perform the scanning, balancing, and coding of tax payments. Ensure that those procedures include periodic comparisons of staff initialing designated fields on the DC – OTR Folder Summary Sheet to ensure compliance.

Agency Response:

The agency concurred with the finding and recommendations. As part of the planned actions, OTR will implement a batch tracking system and develop written procedures addressing internal control deficiencies noted.

OIO Auditor Evaluation:

The OTR planned actions are responsive to the issues we identified, and when fully implemented should satisfy the intent of our recommendations.

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2. Physical Security Controls

We found that physical security controls over the Receipt and Control area where in-house tax collections including dedicated revenues are processed, are not adequate to monitor all operations and to prevent tax collections from accidental or intentional misplacement. We noted a total of four cameras located in the area; one in the mail room, one in the Extractions area, one in the Code and Edit area, and another in the Remittance Deposit area. We also noted that access cards are used to access the mail room and the Code and Edit/Deposit Remittance areas. We inquired of the official with responsibility for the physical security over the area processing tax payments and were advised the following:

- There are blind spots that the cameras do not cover;
- The current equipment does not provide for storage of data beyond one week and deleted one week later;
- A number of employees with the Office of Management and Administration (OMA) have generic cards and just about everyone from the company providing security systems has access to the areas where tax collections are processed.

We also observed that the Mail and Extraction areas are not separated but staff from Extraction have access to the Mail area to pick up mail for processing. We also observed that the mail in bins collected from post offices, including those with tax payments, remains unsecured and unattended before is placed in a machine that sorts and count mail for processing. In addition, we observed that the employee responsible for collecting mail from post office stations does daily runs alone without the company of another staff or security personnel although we observed that the employee locks the vehicle each time he enters a building thus securing mail inside the vehicle.

GAO's *Standards for Internal Control in the Federal Government* state on page 5 that "An agency must establish physical control to secure and safeguard vulnerable assets. Examples include security for and limited access to assets such as cash, securities, inventories, and equipment which might be vulnerable to risk of loss or unauthorized use." Page 15 also states that "Access to resources and records should be limited to authorized individuals, and accountability for their custody and use should be assigned and maintained. Periodic comparison of resources with the recorded accountability should be made to help reduce the risk of errors, fraud, misuse, or unauthorized alteration."

When inquired of deficiencies with the security system, the official with responsibility for physical security over the area processing tax payments indicated that there are new plans for monitoring the system. Our request for copy of RPA's action plan addressing each security concern above and information of the new plan including milestones and date for completion, among others, however, has not been addressed.

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Deficiencies with the security system, including areas not covered by security cameras, retention of tapes for only one week before deletion, and the number of employees with access to the area where tax payments are processed raises serious concerns of the protection and integrity of tax payments. The unrestricted access to the Mail area where unsorted mail remains unsecured and unattended, especially by temporary staff hired to assist permanent employees during the busy tax season, compounded by deficiencies with security cameras increases the risk that tax payments may be accidentally or intentionally misplaced and not be detected. Finally, the transportation of mail including envelopes containing tax payments by one single person without the company of security personnel exposes the staff to unnecessary harm and the tax payments to loss or theft.

Recommendations:

As the OTR is scheduled to move to a new location in FY 2010, we recommend that Returns Processing Administration Director:

- 5) Assess the adequacy of the security system at the new location to determine the changes necessary to ensure the protection of tax payments from the time they are received until they are picked up by an armored car company for transportation and deposit into designated bank accounts. Include in said assessment a determination of the adequacy of the period for retaining tapes. Ensure to document the results of the assessment and corrective actions addressing deficiencies noted.
- 6) Make available for review copy of the new monitoring system process ensuring that it addresses each deficiency identified during the assessment of the current system and include, among others, milestones and dates for completion.
- 7) If separation of the Mail and Extraction areas is not feasible, consider establishing compensating controls to ensure that mail is secured and protected at all times.

Agency Response:

OTR concurred with the finding and recommendations. As part of planned actions, the unit will work with OCFO Logistics to ensure cameras are strategically located in the new building as well as an evaluation of the mail and extraction area.

OIO Auditor Evaluation:

The OTR planned actions are responsive to the issues we identified, and when fully implemented should satisfy the intent of our recommendations.

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3. Guidelines For Bank Deposits

We found that the lack of deposit guidelines at RPA's Receipt and Control Unit is a contributing factor to the wide disparity in the number of business days from receipt to the deposit of tax payments in designated bank accounts. Our test work found that 13 of the 45 bank deposits reviewed, tax payment receipts were delayed from 1 to 50 business days after receipts before deposited (see *Exhibit 1*). Tax payments received without taxpayer information which require additional research are a major reason for the extended period for deposit. We found, however, that RPA's Receipt and Control lacks procedures for depositing tax payment promptly and deferring the posting in the District's management information systems (SOAR and ITS) until the taxpayer information is identified.

Prompt deposit requirements applicable to the federal government require that agencies deposit money received "not later than the third day after the custodian receives the money" (31 U.S.C. §3302(c) (1)). The contract with the lockbox contractors, according to RPA officials, requires the depositing of tax payments within 24 hours of receipt.

According to officials with RPA's Receipt and Control, deposits are categorized based on the time tax payments are ready for deposit after receipt as follows:

- Prompt deposits – tax payments ready for deposit within 48 hours of receipt
- Non-prompt – tax payments that, because of delays caused by additional research when, for example, they are received without taxpayer information, cannot be deposited within 48 hours of receipt
- Discovery – tax payments resulting from collection efforts by OTR's Compliance Administration

But even those characterized as prompt deposits, are not consistently deposited within the established timeframe. Of the 13 deposits processed at RPA's Receipt and Control selected for testing, each containing several batches of dedicated revenues, we found that the average number of business days for depositing batches in 3 prompt deposits were 1.5, 12, and 17 business days after dedicated revenues were received.

Absent requirements establishing the number of days between receipt and deposit, tax payments including dedicated revenues may remain undeposited for excessive number of days, increasing the risk that they may be overlooked, forgotten, misplaced, or lost.

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Recommendations:

We recommend that the Returns Processing Administration Director:

- 8) Develop and establish guidelines establishing a maximum number of days tax payments including dedicated revenues should be deposited after received. Consider, among others, the guidelines established in the federal government.
- 9) Develop and establish documented procedures for the prompt depositing of tax payments received without taxpayer information (unclean) so that their depositing is not delayed while taxpayer information for posting is researched.

Agency Response:

OTR concurred with the finding and recommendations. As part of the corrective actions, OTR will revise the 2010 MOTR to ensure that guidelines for prompt deposit are clearly established and that reasonable exceptions for peak cycles are included.

OIO Auditor Evaluation:

The OTR planned actions are responsive to the issues we identified, and when fully implemented should satisfy the intent of our recommendations.

4. Combo Payments Containing Dedicated And Non-Dedicated Revenues

The Remittance & Deposit unit may receive one check from a taxpayer that is for payment of multiple tax types. This is referred to as a combo payment. With the introduction of dedicated revenues, a taxpayer may send in a check for dedicated and non-dedicated revenues which requires deposit into two separate banks.

While there is a policy in place to handle these payments our review found that non-dedicated revenues totaling \$520,710 were incorrectly deposited in bank ID 872 and ultimately to the revenue holding account(Bank ID 882) during the period of our review (see *Exhibit 2*). These funds were still not transferred to their respective bank IDs at the time of our testing. As a result of this oversight, these amounts were incorrectly made available for the payment of principal of interest due to bondholders.

GAO's *Standards for Internal Control in the Federal Government* states on page 15 that "Transactions should be promptly recorded to maintain their relevance and value to management in controlling operations and making decision." It continues by explaining that

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“control activities help to ensure that all transactions are completely and accurately recorded.”

Also on page 15, GAO’s *Standards for Internal Control in the Federal Government* states that “Internal controls and all transactions and other significant events need to be clearly documented, and the documentation should be readily available for examination. The documentation should appear in management directives, administrative policies, or operating manuals and may be in paper or electronic form. All documentation and records should be properly managed and maintained.”

RPA did not have written procedures available for our review; however, officials explained that staff processing combo payments is required to notify the supervisor, Remittance Deposits, when a deposit contains multiple tax types for the supervisor to forward the SOAR voucher to RPA’s Accounting and Reconciliation for the allocation to the appropriate bank IDs.

Recommendations:

We recommend that RPA’s Remittance Deposit Supervisor:

- 10) Remind staff under her supervision of their responsibility to alert of deposits that contain payments for multiple tax types. If necessary, consider providing copies of documented procedures and/or additional training.
- 11) Develop and establish a process to periodically review deposits to determine if staff under her responsibility is adhering to documented procedures for the processing of combo payments.

Agency Response:

The agency concurred with the finding and recommendations. The OTR RPA will provide refresher training on processing combo payments and continue to conduct review of deposits.

OIO Auditor Evaluation:

The OTR planned actions are responsive to the issues we identified, and when fully implemented should satisfy the intent of our recommendations.

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5. **OFOS' Monthly Bank Reconciliation Directive**

We found no evidence that OTR submitted monthly bank reconciliation reports to the Office of Financial Operations and Systems (OFOS) in accordance with the directive issued by the Deputy Chief Financial Officer for Financial Operations and Systems.

In a memorandum dated February 11, 2009, issued to all associate Chief Financial Officers, Agency Fiscal Officers, Agency Controllers, and Agency Financial Managers, the Deputy CFO, OFOS, stated that "Effective immediately, all agencies **must** prepare the bank reconciliation report within 10 business days of receiving the 'periodic report' from the bank or investment house **and** forward this monthly bank reconciliation report to OFOS Accounting Operations." It also states that "All unrecorded unreconciled items must be recorded in SOAR as part of the bank reconciliation process. The bank reconciliation report must show the document number for the reconciling items' journal voucher(s)." (See *Attachment A*)

According to officials with OTR's Revenue Accounting Administration, OTR received an exception from OFOS and was permitted to prepare *deposit* reconciliations only for all funds (except for business improvement districts). OFOS' exception, however, was not documented and RAA, on the date of this report, was still in the process of obtaining a formalized exemption from OFOS.

Due to OTR's failure to submit monthly bank reconciliation reports, OFOS continued preparing bank reconciliations for OTR's bank IDs through an undocumented process in which bank reconciliations are e-mailed to responsible officials requesting them to resolve reconciling items. This process lacks timeframes for agencies to resolve reconciling items and any corrective actions when agencies fail to comply with established timelines. We found, for example, reconciling items in bank reconciliations unreconciled since January 2008.

We also found deficiencies with supervisory reviews of OFOS' bank reconciliations. We noted, for example, that certain deposits were posted to SOAR but not reflected in bank statements and correctly listed as reconciling items in March 2009's bank reconciliation for bank ID 217, continued being listed as reconciling items in bank reconciliations for April, May, and June 2007 even though they cleared the bank in April 2009. The reviews of these bank reconciliations by the preparer's supervisor, evidenced by her signature, failed to detect these errors. We independently recreated these bank reconciliations and concluded that the bank reconciliations performed by OFOS contained plug numbers" in order to force bank reconciliations to reconcile. We inquired of the manager of OFOS' Cash Reconciliation Unit who admitted that she overlooked these errors.

Failure to submit required reports may cause OTR to be in non-compliance with directive requiring all agencies CFOs to submit monthly bank reconciliation reports to OFOS' Accounting Operations.

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Recommendations:

We recommend that the DCFO, Office of Tax and Revenue:

- 12) Ensure compliance with directive requiring officials with the Office of the Chief Financial Officer to submit monthly bank reconciliation reports to OFOS' Accounting Operations. If the exemption sought from OFOS is granted, we recommend that OTR develop and establish documented procedures incorporating relevant provision of the directive issued by the Deputy CFO for Financial Operation and Systems. For example, the third paragraph of the directive requires all unrecorded reconciling items be recorded in SOAR as part of the bank reconciliation process and to include the document number for the reconciling items' entry in SOAR.

We recommend the OTR's Returns Processing Administration Director:

- 13) Review bank reconciliations ensuring the prompt resolution of reconciling items that remain unreconciled.

We also recommend that OFOS' Cash Reconciliation Unit Supervisor:

- 14) Define its role in the new process established by the directive issued by the Deputy CFO, OFOS. If the purpose of the directive was to change from preparing bank reconciliation to reviewing monthly bank reconciliation reports, we recommend its officials to direct their efforts to ensure agencies' compliance with the directive. If OFOS' Cash Reconciliation Unit is to retain some responsibilities for preparing monthly bank reconciliations, we recommend its officials to develop and establish documented procedures for the preparation of bank reconciliation ensuring to include requirements for the timely resolution of reconciling items and for effective supervisory reviews.

Agency Response:

OTR and OFOS concurred with the finding and recommendations. OTR will formalize the reconciliation duties with OFOS and complete written procedures outlining specific responsibilities and timelines for completing deposit reconciliation in RAA. OFOS will develop a formal policy that documents the procedures for preparing a bank reconciliation as well as develop an assessment tool to measure agency compliance with reconciliation guidelines.

OIO Auditor Evaluation:

The OTR and OFOS planned actions are responsive to the issues we identified, and when fully implemented should satisfy the intent of our recommendations.

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6. Resolving Unreconciled Items

For our test work, we obtained Revenue Accounting Administration monthly and annual procedures for ensuring that all revenue and deposit transactions for the Office of Tax and Revenue are reconciled in the District's System of Accounting and Reporting (SOAR) and OTR's Integrated Tax System (ITS). This document, however, fails to provide requirements for the timely resolution of differences in ITS and follow up procedures to ensure reconciling items are promptly resolved. For example, we found reconciling items in ITS unreconciled for several months.

RAA's procedure requires the monthly reconciliation of cash receipts but fails to provide the date when bank reconciliations should be submitted to the management of RAA for review. Bank reconciliations performed on deposits for all bank IDs used for dedicated revenues for the period of our review, revealed that bank reconciliations for bank ID 872 for the months of May and June 2009 had not been completed.

We found that the new process established by Returns Processing Administration, in which bank reconciliations performed by the Office of Financial Operations and Systems (OFOS) and OTR's Revenue Accounting Administration (RAA) previously sent directly to officials with RPA's Accounting and Reconciliation Unit for the resolution of reconciling items, are now sent to officials with RPA before they are forwarded to RPA's Accounting and Reconciliation. Similarly, inquiries of information necessary for the resolution of reconciling items previously handled by officials with RPA's Accounting and Reconciliation directly with bank representatives are now sent to officials with RPA before they are forwarded to banks for research. These additional steps extends the time, sometimes for several months, for obtaining bank information previously obtained immediately from the bank and necessary for the timely resolution of reconciling items. These concerns were voiced by officials with both RPA's Accounting and Reconciliation and OFOS.

The Treasury Financial Manual, issued by the Financial Management Service (FMS) within the U.S. Department of Treasury, provides policies and procedures for federal agencies to follow in carrying out their fiscal responsibilities. In its reconciliation procedures' webpage at <http://www.fms.treas.gov/fundbalance/procedure.html>, FMS requires agencies "to identify and clear differences within 2 months of occurrence." TFM's Volume I, Part 2, Chapter 5100, and Section 5125 also explain that "Unresolved differences compromise the reliability of [Fund Balance with Treasury] balances...and Treasury's published financial reports. This, in turn, compromises the overall integrity and status of the Government's financial position."

As noted in I TFM Part 2, Section 5125, unresolved reconciling items compromise financial information used for management's decisions as well as the integrity and status of the District's financial position.

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Recommendations:

We recommend that OTR's Revenue Accounting Administration Director:

- 15) Incorporate in its documented procedures for ensuring that all revenue and deposit transactions are reconciled, timeframes for the timely resolution of reconciling items in SOAR and ITS ensuring they include follow up procedures to ensure responsible officials are adhering to established guidelines. Consider, among others, the guidelines established in the federal government. Also, ensure to include deadlines for the completion and submission of deposit reconciliations to management of RAA for review.

We recommend also that the Returns Processing Administration Director:

- 16) Develop and establish documented procedures for the receipt and distribution of bank reconciliations to responsible officials and of inquiries of banks for the timely resolution of reconciling items, ensuring that they incorporate requirements for compliance with timeframes for the resolution of reconciling items established by OFOS and RAA.

Agency Response:

The OTR concurred with the finding and recommendations. The agency will develop a comprehensive strategy for reengineering the reconciliation process.

OIO Auditor Evaluation:

The OTR planned actions are responsive to the issues we identified, and when fully implemented should satisfy the intent of our recommendations.

7. Monitoring of Bank Transfers

We found no evidence that OTR is performing reconciliations of transfers of dedicated revenues from Collection Accounts to the Revenue Account (bank ID 882). The lack of reconciliations failed to detect duplicate transfers of *individual income taxes*, a source of dedicated revenues, totaling \$6.48 million to bank ID 882 (see *Exhibit 3*).

During our independent reconciliation of dedicated revenues received via electronic funds transfers recorded in SOAR's bank ID 406 with transfers to bank ID 725, we found that the amounts transferred to bank ID 725 during the period of our review exceeded dedicated revenues posted to bank ID 406 by \$6.63 million. In investigating the causes for the excess transfers, we traced the amounts of dedicated revenues in reports summarizing the posting of electronic funds transfers in ITS to the corresponding bank accounts, noting that *individual income taxes* were not deposited into bank ID 406 but into bank ID 229. The same reports, modified by RPA's Systems and Forms to segregate dedicated revenues from other tax types,

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were e-mailed to banks for the transfer of dedicated revenues from bank ID 406 to bank ID 725. For a more detailed discussion of transfers to bank ID 725, please refer to the Background section above under the caption *Processing of Dedicated Revenues*.

The modified reports requesting transfers from bank ID 406 to bank ID 725 incorrectly included amounts of *individual income taxes* that were deposited to bank ID 229. Because deposits in bank ID 229 are also transferred to bank ID 882, it resulted in the amounts of *individual income taxes* totaling \$6.48 million transferred twice to bank ID 882. Once through bank ID 725 and again through bank ID 229. The remaining difference of \$155,113 (\$6,632,824 minus \$6,477,711) is yet to be reconciled. Other tax types such as, sales and use taxes are also received via electronic funds and deposited into bank ID 406 before transferred to their respective bank IDs. The excess transfers to bank ID 725 effectively created shortages in other bank IDs although the deficits remain undetected given the lack of reconciliations of bank transfers.

We also found no evidence that OTR and/or OFT are monitoring bank transfers. After funds are transferred from bank ID 406 to bank ID 725, dedicated revenues are transferred to bank ID 882. This is also the case with dedicated revenues deposited into bank IDs 217, 229, 405, and 872. These transfers are performed daily by banks based on the amount deposited, net of returned items. Once transferred, banks notify OFT for the recording of transfers in SOAR.

We inquired of officials with OFT who responded that no one is responsible for verification of transfers or that documentation is maintained evidencing a verification that the amounts transferred agreed with amounts deposited net of returned items. We analyzed the bank transfers to bank ID 882 and noted that all bank accounts except for bank ID 405 retained \$50,000 each. In the case of bank ID 405, the amount transferred exceeded amounts deposited by \$50,000. We inquired of OFT officials who appeared unaware of these balances but forwarded our inquiries to bank officials who responded that this balance is retained to cover returned items in excess of deposits.

GAO's *Standards for Internal Control in the Federal Government* states on page 20 that "Internal control should generally be designed to assure that ongoing monitoring occurs in the course of normal operations. It is performed continually and is ingrained in the agency's operations. It includes regular management and supervisory activities, comparisons, reconciliations, and other actions people take in performing their duties."

In responding to our requests for explanation of these duplicate transfers, RPA indicated that OTR failure to provide the third party vendor with new instructions on where to deposit individual income taxes contributed to these duplicate transfers. The lack of coordination within RPA's units was another contributing factor. We noted, for example, that RPA's Accounting and Reconciliation was correctly posting in SOAR electronic funds transfers of individual income taxes into bank ID 229. RPA's Systems and Forms unit was under the incorrect impression that individual income taxes were being deposited into bank ID 406 and

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was transferring related amounts to bank ID 882 at the same time that the bank was transferring the same revenues to bank ID 882 from bank ID 229.

Although during our reconciliation of bank transfers to the Revenue Account we were able to account for all deposits into Collection Accounts, the lack of reconciliation and monitoring of bank transfers leaves the District vulnerable to errors and misappropriation of funds.

Recommendations:

We recommend that Returns Processing Administration Director:

- 17) Develop and establish documented procedures for the periodic reconciliations of bank transfers, especially of bank IDs related to dedicated revenues.
- 18) Research and reconciled the unreconciled difference of \$115,113 in excess transfers of dedicated revenues to bank ID 725.

We recommend also that the Office of Finance and Treasury Associate Treasurer for Cash and Investments:

- 19) Develop and establish documented procedures for the reviewing of bank transfers performed by bank, to ensure they reflect deposits net of returned items.

Agency Response:

OTR and OFT concur with the findings and recommendations. OTR noted that they discovered the duplicate transfers in October 2009 and took appropriate action. In addition, RAA and RPA will finalize procedures for reconciling the transfers to the secured account. OTR also plans to address the resolution of the excess transfers identified by OIO.

OIO Auditor Evaluation:

The OTR and OFT planned actions are responsive to the issues we identified, and when fully implemented should satisfy the intent of our recommendations.

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EXHIBITS & ATTACHMENT

- Exhibit 1: Prompt Deposits and Correct Tax Type**
Exhibit 2: Non-Dedicated Revenues Incorrectly Posted in Bank ID 872
Exhibit 3: Duplicate Transfers of Electronic Fund Transfers to Bank IDs 882 and 725
- Attachment A: OFOS Memorandum on Monthly Bank Reconciliation Report.**
Attachment B: Agency Responses
-OTR
-OFOS
-OFT

GOVERNMENT OF THE DISTRICT OF COLUMBIA

Office of the Chief Financial Officer

Office of Tax and Revenue



Stephen M. Cordi
Deputy Chief Financial Officer

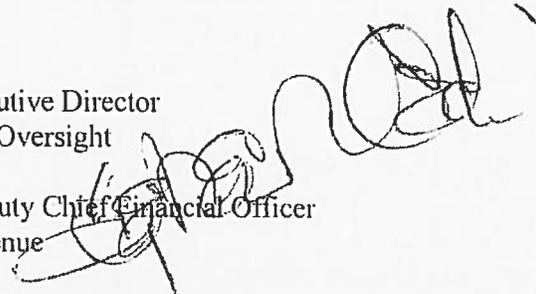
MEMORANDUM

TO: William DiVello, Executive Director
Office of Integrity and Oversight

FROM: Stephen M. Cordi, Deputy Chief Financial Officer
Office of Tax and Revenue

DATE: March 19, 2010

SUBJECT: Draft Report on the Review of Income Tax Secured Bond Fund at OTR and Related Agencies (Report No.: IA:OTR:2911-C15)



This memorandum serves as the response of the Office of Tax and Revenue (OTR) to the subject draft report. It reflects only the response of OTR, and does not attempt to respond to the recommendations made to OFOS, OFT or other offices within the OCFO.

Finding #1: Controls within RPA's Receipt and Control Unit are not Adequate.

Recommendations:

- 1) Develop and establish documented procedures for periodic reviews by supervisor of all units, ensuring that they describe the documentation required to evidence the performance of supervisory reviews.
- 2) Determine the causes for non-secure tax types recorded to the secure Bank ID (BID), and complete correcting entries.
- 3) Develop and establish a mechanism to track and account for each tax payment from the time it is picked up to the time it is deposited.
- 4) Develop procedures for ensuring proper segregation of duties in Remittance Deposits between scanning, balancing and encoding functions.

Response: Concur

- The Branch Chief of the Receipt and Control unit will update the 2010 MOTR requiring periodic reviews by the supervisor of the mail unit to ensure that mail extraction is performed accurately.

- RPA will work with RAA to identify erroneous deposits to the secured accounts and make timely correcting entries. If a root cause can be identified for these errors, RPA will make revisions to procedures and/or request system changes to prevent future occurrence. If the error is found to be caused by internal RPA procedure, the Branch Chief shall provide refresher training to the staff on procedures to reinforce awareness of the Income Tax Secured Bond Program and the impact to the District if pledge revenue is extracted and deposited incorrectly.
- RPA will draft a written request to OTR Executive team to purchase and implement a batch tracking system that would strengthen the controls surrounding the mail collection process in FY2010-11.
- The Branch Chief shall draft written procedures, so that when resources permit, different staff will be used to maintain a level of internal controls during the scanning, balancing, and coding of the tax revenue receipts.

Finding #2: Physical Security Controls Not Strengthened as Previously Recommended.

Recommendations:

- 5) Assess the adequacy of the security system in the new location to determine changes necessary to ensure protection of tax payments from receipt until they are picked up by an armored car, including adequacy of period for retaining tapes. Document the assessment and action plan.
- 6) Make available a copy of the new monitoring system process ensuring that it addresses each deficiency identified during the assessment.
- 7) If separation of the Mail and Extraction areas is not feasible, consider compensating controls to ensure that mail is secured at all times.

Response: Concur

- The Deputy Director and Branch Chief of the Receipts and Control unit will work with OCF/O Logistics to ensure security cameras are visible and strategically located in the new building to reduce the risk of fraud.
- RPA currently monitors security cameras and will continue this effort at the new building. The monitoring plan will be documented; including the retention period for tapes, and expectations will be made clear to supervisors and included in annual performance goals.
- Once RPA has relocated, we will evaluate who has access to the Mail and Extraction area and determine what controls may be implemented to limit the risk of returns being accidentally or intentionally misplaced.

Finding #3: Guidelines for Bank Deposits not Established Resulted in Deposit Delays at RPA's Remittance Deposit Unit.

Recommendations:

- 8) Develop guidelines establishing a maximum number of days within which tax payments should be deposited after receipt.
- 9) Develop procedures for the prompt deposit of tax payments received without taxpayer information (unclean) so that deposits are not delayed while the taxpayer information for posting is researched.

Response: Concur

- In reviewing the report and appendices, the late deposits identified had a receipt date of April 15th. While the prompt deposit standard does apply, RPA acknowledges that not all payments mailed/received on the individual income filing date can be deposited within the timeframe, based on the time involved to open all the mail that is counted as "received" on April 15th. With that in mind, the Branch Chief of the Receipt and Control unit will revise the 2010 MOTR to ensure that guidelines for prompt deposit are clearly established and that reasonable exceptions for peak cycles are included.
- The Branch Chief of the Receipts and Control unit will reevaluate the 2010 MOTR to determine if procedures for prompt depositing of tax payments received without taxpayer information (unclean) are clearly outlined. If not, the Branch Chief will make the necessary revisions so that it is clearly defined how to handle (unclean) receipts to meet the prompt deposit standard while research is ongoing in order to post the payment to the appropriate taxpayers account in ITS.

Finding #4: Combo Payments Containing Dedicated and Non-dedicated Revenues are not Processed Properly.

Recommendations:

- 10) Remind staff of responsibility to alert supervisor of deposits containing payments for multiple tax types and, if necessary, consider providing copies of documented procedures and/or additional training.
- 11) Develop a process to periodically review deposits to determine if staff is adhering to documented procedures for processing combo payments.

Response: Concur

- RPA will provide refresher training to the staff to include examples of combo type payments. Training aids will be developed and placed in the work area.
- The RPA Remittance Deposit Supervisor will conduct reviews of deposits. The manager is currently performing a 100% review of all deposits, which will detect any cases where combo payments may have been misapplied.

Finding #5: Non-compliance with OFOS' Monthly Bank Reconciliation Directive.

Recommendations:

- 12) Ensure compliance with OFOS' bank reconciliation directive. If OTR is exempted, OTR should establish documented procedures incorporating relevant provisions of the directive.
- 13) RPA should review bank reconciliations ensuring the prompt resolution of reconciling items that remain open.
- 14) OFOS specific recommendation

Response: Concur

- RAA prepares monthly bank deposit reconciliations and forwards them to RPA with a cover letter identifying reconciling items. It is RPA's duty to resolve the reconciling items. OTR will formalize the reconciliation duties with OFOS, and complete written procedures outlining specific responsibilities, deadlines and timeframes for completing deposit reconciliations in RAA. The timeframes for acceptable completion of

to finalize procedures to ensure that the necessary controls are in place. Since August 2009 RAA has monitored the implementation of the automated processes to ensure that there are no duplicate transfers to the Trustee account.

- RAA and RPA will finalize procedures for reconciling the transfers to the secured account.
- RAA and RPA will work together to ensure that the excess transfers identified by OIO are resolved.

reconciliations and resolution of outstanding items are currently included in the performance agreements of relevant RAA staff.

- RPA will develop written procedures for resolving reconciling items received from RAA.

Finding #6: Reconciling Items Are Not Resolved Timely.

Recommendations:

- 15) RAA should incorporate in its documented procedures for revenue and deposit reconciliations the timeframes for timely resolution of reconciling items and follow up procedures to ensure compliance. Also include deadlines for the completion and submission of deposit reconciliations to RAA management for review.
- 16) RPA should develop procedures for the receipt and distribution of bank reconciliations to responsible officials and for inquiries to banks for timely resolution of reconciling items, ensuring that they incorporate timeframes established by OFOS and RAA.

Response: Concur

- Currently, timeframes for RAA to complete reconciliations and resolve reconciling items are contained in the performance agreements for relevant staff. This would include submission to management for review. As procedures are updated, RAA will document the timeframes in the written procedures as well. However, many of the longstanding issues with the reconciliation process are impacted by staff resource levels and system constraints within ITS. RAA will work with RPA to investigate root causes for most reconciling items and develop specific solutions. Some items will continue to pose a challenge, based on system limitations (such as the problem of suspended or unprocessed batches) which contribute to the number of reconciling items that cannot be resolved until the deposits can be posted. A comprehensive strategy for reengineering this process will be completed by September 30, 2010. ,
- RPA and RAA are currently discussing improvements to the reconciliation process, including a realignment of responsibilities. This will be included in the revised procedures, to be completed by September 30th.

Finding #7: Failure to Monitor Bank Transfers Resulting in Duplicate Transfers.

Recommendations:

- 17) RPA should develop procedures for the periodic reconciliations of bank transfers, especially of bank ID's related to dedicated revenues.
- 18) RPA should research and reconcile the unreconciled difference of \$115,113 in excess transfers of dedicated revenues to bank ID 725.
- 19) OFT specific recommendation

Response: Concur

- While OTR does not have the responsibility to reconcile BID 882, OTR does track the accounts that feed into it. Secured Bond transactions began in March of 2009, and many of the procedures for tracking these revenues were not in place at start up. However, RAA was reconciling the secured accounts, and noticed the duplicate transfers identified here in October. RPA was notified, and RAA took appropriate action through OFT to recover the duplicate payments. As with other reconciliation issues, RAA and RPA need

GOVERNMENT OF THE DISTRICT OF COLUMBIA
Office of the Chief Financial Officer



Bill K. Slack
Deputy Controller

Financial Operations
and Systems

MEMORANDUM

TO: William J. DiVello, Executive Director
Office of Integrity and Oversight

FROM: Bill K. Slack, Deputy Controller *Bill Slack*
Office of Financial Operations & Systems

DATE: June 30, 2010

SUBJECT: Response to draft report on Review of Income Tax Secured Bond Fund at
OTR and Related Agencies (Report No:IA:OTR:2911-C15)

The Office of Integrity and Oversight (OIO) recommended that OFOS' Cash Reconciliation Unit Supervisor

Define its role in the new process established by the directive issued by the Deputy CFO, OFOS. If the purpose of the directive was to change from preparing bank reconciliation to reviewing monthly bank reconciliation reports, we recommend its officials to direct their efforts to ensure agencies' compliance with the directive. If OFOS' Cash Reconciliation Unit is to retain some responsibilities for preparing monthly bank reconciliations, we recommend its officials to develop and establish documented procedures for the preparation of bank reconciliation ensuring to include requirements for the timely resolution of reconciling items and for effective supervisory reviews.

OFOS submits the following in response to that recommendation:

OFOS is currently developing a formal policy that documents the procedures for preparing bank reconciliation. In addition to the bank reconciliation procedures, OFOS is formulating an assessment tool to measure agency compliance with the timely resolution of reconciling items and effective supervisory review guidelines.

If you have any questions, please contact Tonja Lowe on 442-8250.

OFOS RESPONSE TO FINDING #5

Non-compliance With OFOS' Monthly Bank Reconciliation Directive

We found no evidence that OTR submitted monthly bank reconciliation reports to the Office of Financial Operations and Systems (OFOS) in accordance with the directive issued by the Deputy Chief Financial Officer for Financial Operations and Systems.

In a memorandum dated February 11, 2009, issued to all associate Chief Financial Officers, Agency Fiscal Officers, Agency Controllers, and Agency Financial Managers, the Deputy CFO, OFOS, stated that "Effective immediately, all agencies must prepare the bank reconciliation report within 10 business days of receiving the 'periodic report' from the bank or investment house and forward this monthly bank reconciliation report to OFOS Accounting Operations." It also states that "All unrecorded unreconciled items must be recorded in SOAR as part of the bank reconciliation process. The bank reconciliation report must show the document number for the reconciling items' journal voucher(s)." (See *Attachment A*)

According to officials with OTR's Revenue Accounting Administration, OTR received an exception from OFOS and was permitted to prepare *deposit* reconciliations only for all funds (except for business improvement districts). OFOS' exception, however, was not documented and RAA, on the date of this report, was still in the process of obtaining a formalized exemption from OFOS.

Due to OTR's failure to submit monthly bank: reconciliation reports, OFOS continued preparing bank: reconciliations for OTR's bank: IDs through an undocumented process in which bank: reconciliations are e-mailed to responsible officials requesting them to resolve reconciling items. This process lacks timeframes for agencies to resolve reconciling items and any corrective actions when agencies fail to comply with established timelines. We found, for example, reconciling items in bank: reconciliations unreconciled since January 2008.

We also found deficiencies with supervisory reviews of OFOS' bank: reconciliations. We noted, for example, that certain deposits were posted to SOAR but not reflected in bank statements and correctly listed as reconciling items in March 2009' s bank: reconciliation for bank: ID 217, continued being listed as reconciling items in bank: reconciliations for April, May, and June 2007 even though they cleared the bank: in April 2009. The reviews of these bank: reconciliations by the preparer's supervisor, evidenced by her signature, failed to detect these errors. We independently recreated these bank: reconciliations and concluded that the bank reconciliations performed by OFOS contained plug numbers" in order to force bank reconciliations to reconcile. We inquired of the manager of OFOS' Cash Reconciliation Unit who admitted that she overlooked these errors.

Failure to submit required reports may cause OTR to be in non-compliance with directive requiring all agencies CFOs to submit monthly bank reconciliation reports to OFOS' Accounting Operations.

Recommendations:

We recommend that the DCFO, Office of Tax and Revenue:

12) Ensure compliance with directive requiring officials with the Office of the Chief Financial Officer to submit monthly bank reconciliation reports to OFOS' Accounting Operations. If the exemption sought from OFOS is granted, we recommend that OTR develop and establish documented procedures incorporating relevant provision of the directive issued by the Deputy CFO for Financial Operation and Systems. For example, the third paragraph of the directive requires all unrecorded reconciling items be recorded in SOAR as part of the bank reconciliation process and to include the document number for the reconciling items' entry in SOAR.

We recommend the OTR's Returns Processing Administration Director:

13) Review bank reconciliations ensuring the prompt resolution of reconciling items that remain unreconciled.

We also recommend that OFOS' Cash Reconciliation Unit Supervisor:

14) Define its role in the new process established by the directive issued by the Deputy CFO, OFOS. If the purpose of the directive was to change from preparing bank reconciliation to reviewing monthly bank reconciliation reports, we recommend its officials to direct their efforts to ensure agencies' compliance with the directive. If OFOS' Cash Reconciliation Unit is to retain some responsibilities for preparing monthly bank reconciliations, we recommend its officials to develop and establish documented procedures for the preparation of bank reconciliation ensuring to include requirements for the timely resolution of reconciling items and for effective supervisory reviews.

OFOS Response:

OFOS is currently developing a formal policy that documents the procedures for preparing a bank reconciliation. In addition to the bank reconciliation procedures, OFOS is formulating an assessment tool to measure agency compliance with the timely resolution of reconciling items and effective supervisory review guidelines.

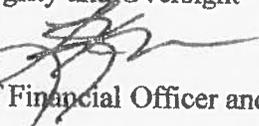
GOVERNMENT OF THE DISTRICT OF COLUMBIA
Office of the Chief Financial Officer



Office of Finance and Treasury

MEMORANDUM

TO: Tisha Edwards
Office of Integrity and Oversight

FROM: Lasana Mack 
Deputy Chief Financial Officer and Treasurer

DATE: June 22, 2010

SUBJECT: Response to Draft Report on the Review of Income Tax Secured Bond Fund at OTR and Related Agencies

This correspondence is to provide comments on the draft report transmitted by the Office of Integrity and Oversight on April 27, 2010 entitled "Draft Report on the Review of Income Tax Secured Bond Fund at OTR and Related Agencies," (Report No.: IA:OTR:2911-C15) The format of the response is to address each of the specific recommendations and considerations contained in the draft report.

Please find the following response from the Office of Finance and Treasury (OFT) to the OIO Recommendation:

In response to Finding No. 7, as indicated, OFT has the responsibility to record incoming transfers into BID 882, and OFT recognizes there were duplicate transfers into BID 882. The tax-related transfers into the accounts that are the sources of the transfers into BID 882, and the transfers into BID 882 itself, are the responsibility of OTR to manage and properly transfer. Consistent with the recommendations, there should be monthly account reconciliation procedures performed by OTR and OFOS, through which any discrepancies in amounts transferred and recorded into and out of these accounts should be reconciled and resolved. Since the electronic funds transfers into BID 882 are automatically generated by the financial institutions using a wire transfer, OFT believes that proper controls are in place at the financial institution to ensure that the payment out of one account is the same value that is posted into BID 882. However, consistent with the recommendations, OFT will perform periodic verification of the account balances to ensure that they are being maintained at the appropriate levels, and will periodically verify that the amounts received into BID 882 are consistent with the amount of these dedicated tax revenues that should be credited to this account. This will provide additional checks and balances on the process, enhancing the overall level of controls.