# Executive Summary

Audit report 2003-04, Property Taxation, was originally issued in September, 2003 and management action plans with implementation dates were included in the report. In September, 2005, Internal Audit followed up the report to determine that appropriate and timely actions had been taken. Of the seventeen (17) individual recommendations made in the original report, eight (8) have been completed, four (4) are still in progress, two (2) have been initiated, two (2) are incomplete and one (1) is no longer applicable.
BACKGROUND:

Audit report 2003-04, Property Taxation, was originally issued in September, 2003. The report indicated several recommendations to strengthen internal controls, to comply with approved policies and procedures and to safeguard assets.

It is normal practice for Internal Audit to conduct follow up reviews within a 12-18 month period following issuance of the original report in order to determine whether action plans committed to by departmental management have been implemented. In September, 2005, Internal Audit followed up the report to confirm appropriate and timely actions had been taken.

ANALYSIS/RATIONALE:

The report attached as Appendix “A” contains the first three columns as originally reported in Audit Report 2003-04 along with an added fourth column indicating Internal Audit’s follow up comments.

Eight (8) of the seventeen (17) individual recommendations have been fully implemented. One (1) recommendation is no longer applicable as the process is no longer performed.

Two (2) recommendations have been initiated but without any substantial progress. Written policies are to be developed and the expected completion date is mid 2006. Although reports from Building and Licensing are forwarded to MPAC, changes to the MPAC computer system in regard to developing a common electronic file layout is not anticipated until mid 2006. The integration of two internal computer systems (Amanda and Vailtech) has not proceeded although it has been included in IT’s strategy and business plan.

Two (2) recommendations are incomplete. One is in regard to the processing of tax payments. In order to expedite the processing and deposit of cheques, staff still need to investigate the feasibility of transferring the RPS machine back to City Hall. The other outstanding recommendation requires an interface or integration between the Vailtech and PeopleSoft systems in the Revenue Division. To date, this has not occurred.

The implementation of the balance of the recommendations (i.e. four (4)) is in progress.

(1) In regard to Federal and Provincial properties deemed exempt from penalties or interest on delayed payment of taxes, staff have made attempts to have better working relationships with the Federal and Provincial property managers in recovering many of the payments outstanding from prior years.
(2) The Taxation Division has been more aggressive in its efforts to recover taxes and other debts through the issuance of more letters to delinquent taxpayers and escalated tax registrations. Most of the contaminated properties identified in the original audit have been sold for even partial recovery of taxes ($1.5 million of $9.4 million owing).

(3) Although hierarchical levels for processing and approval of tax refunds and reversal recordings is practised, a formal procedure is not expected until the fall of 2006.

(4) A list of City-owned rented properties has been developed to ensure appropriate taxation but the information on the list needs to be updated through consultation with the Real Estate Division.

**ALTERNATIVES FOR CONSIDERATION:**

Not applicable

**FINANCIAL/STAFFING/LEGAL IMPLICATIONS:**

**Financial**

Taxes (payments in lieu) from the Provincial and Federal properties that remain outstanding for long periods of time and delays in communicating assessment changes to properties by MPAC are losses to the current revenue stream.

**Staffing**

None

**Legal**

Not applicable

**POLICIES AFFECTING PROPOSAL:**

Some of the management action plans and subsequent actions involve the preparation and approval of written policies that are expected by mid 2006.

**RELEVANT CONSULTATION:**

The results of the follow up were discussed with the staff of Corporate Services whose responsibilities include the administration and management of property taxation.
CITY STRATEGIC COMMITMENT:

By evaluating the “Triple Bottom Line”, (community, environment, economic implications) we can make choices that create value across all three bottom lines, moving us closer to our vision for a sustainable community, and Provincial interests.

Evaluate the implications of your recommendations by indicating and completing the sections below. Consider both short-term and long-term implications.

- **Community Well-Being is enhanced.**  
  - [ ] Yes  
  - [x] No

- **Environmental Well-Being is enhanced.**  
  - [ ] Yes  
  - [x] No

- **Economic Well-Being is enhanced.**  
  - [x] Yes  
  - [ ] No

City Council’s strategic commitment to “Best Practices – Best Value” under “A City That Spends Wisely and Invests Strategically” is addressed through audits and reviews and their subsequent follow up to ensure controls are in place to protect the assets of the City and promote efficient, effective and economic services and programs.

- **Does the option you are recommending create value across all three bottom lines?**  
  - [ ] Yes  
  - [x] No

- **Do the options you are recommending make Hamilton a City of choice for high performance public servants?**  
  - [ ] Yes  
  - [x] No

:dt
Attachment – Appendix “A”
### CITY OF HAMILTON
### INTERNAL AUDIT REPORT 2003-04
### PROPERTY TAXATION
### FOLLOW UP

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<td>1.</td>
<td><strong>Tax Billings and Adjustments</strong></td>
<td>That decisions that might materially affect either past or current tax revenues be taken after a) assessing their total impact; b) making complete disclosure of the facts; and c) obtaining and documenting approval from the appropriate authority(ies) to whom such disclosure is required to be made.</td>
<td>Agree. From now on, the circumstances surrounding any decision that might materially affect taxation revenues will be disclosed with its full impact to Council in the annual capping report or other similar document. However, staff would like to point out that corrective measures were taken to ensure the accuracy of the capping computations for 2002. During 1998 to 2001, some taxpayers were billed erroneous capping adjustments due to the frequent, significant changes in the environment under which the staff operated. Such adjustments were not recorded by staff on the assumption that with the passage of time and increase in tax rates in the future, these differences would work themselves out of the equation. However, these assumed reversals of past errors did not transpire because of changes in the related legislation in 2001 and Council's decision to introduce Business Tax Reductions. When the Division approached the Provincial staff with the dilemma, they were informally advised to make the necessary adjustments without further legislative amendments.</td>
<td>Complete. The computation of capping amounts has now become more standardized. The Budget section prepares a tax policy options report that outlines how much capping will cost the City and how much the City is prepared to claw back as part of the Business Tax Retention plan. The difference between the two is the impact of capping on the levy. Since this is part of the Budget process, Council is kept apprised of tax revenue decisions.</td>
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In the case of two properties, it was ascertained that problems in 2000 and 2001 computations for capping amounts led to significantly excessive capping credits being given to certain taxpayers. Internal Audit ascertained that these errors arose due to a cumulative effect of a) errors in the "Frozen Assessment Listings" provided by the Assessment Corporation in 1998; and b) the use of the Provincial capping tool (OPTA) which proved inadequate in meeting the Region's (pre-amalgamation) needs and did not accommodate graduated tax rates/banding. It should also be noted that the province introduced numerous legislative changes in quick succession during this period which caused much upheaval in the area.

While the division was aware of the existence of such problems, it did not pursue recoveries from properties that were either charged lower taxes, or, were given extra capping credits on account of such errors. The legislation allowed the City an opportunity (expired now) to correct errors in the year 2000 & 2001 tax bills for such cases. While the total loss suffered due to extra capping credits can be ascertained only after conducting a thorough exercise, such losses in case of only the two properties mentioned above equaled $238,292.

Formula anomalies in the capping calculation were rectified in 2002 and the capping amounts for the year were correctly ascertained and charged. However, the impact of such errors on the past revenues was not ascertained and thus, no corrective action was initiated to effect recoveries for under-billing. In fact, a 2002 report to Council mentioned such errors as being one of the contributory reasons for the decrease in capping losses in 2002, indicating that their impact in the previous years was significant enough to cause such variations.

No documentation was available that indicated either the approval or the basis for the adoption of such a practice.
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<td>2.</td>
<td>Capping adjustments were verified and the following were observed:</td>
<td>That internal procedures be developed to ensure that capping adjustments are recorded completely and accurately.</td>
<td>Agree. Starting from 2004, the Division will make capping adjustments for properties affected by supplementary rolls based on the information available. The Division, depending on its staff resources, will also initiate follow-up action to ensure that comparative assessments are received from the Assessment Corporation where these are delayed beyond six months.</td>
<td>Initiated. At present, Appeals staff continue to review the properties issued supplementary assessments and make corrections for capping adjustments. In cases where the supplementary value is less than 50% of the original assessment, the supplement is capped at the same rate as the original tax (i.e. if they are capped at 10% of their current tax, the supplementary assessment is also capped at 10%). If the properties are new or if the supplementary assessments' value is 50% or greater than the current value, staff obtain comparables from MPAC. This is performed as required. The Director of Taxation has indicated that formal written policies will be developed by mid 2006.</td>
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<td>3.</td>
<td>Federal and Provincial properties have been designated by staff as exempt from penalties or interest on delayed payments of taxes. The basis for granting such exemption to these properties could not be specifically ascertained other than staff's opinion that such actions would prove futile and possibly further delay payments.</td>
<td>That staff continue to pursue an accelerated payment process with Federal and Provincial officials.</td>
<td>Agree.</td>
<td>In progress. Staff have made attempts to have better working relationships with the Federal and Provincial property managers. There has been some success in recovering many of the payments outstanding from prior years. Summary reports are sent to the property managers as required and they sometimes make partial payments. However, neither the Federal nor Provincial property managers can be forced to pay penalties and/or interest as these are perceived as payments in lieu rather than taxes.</td>
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<td>4.</td>
<td>Taxes levied are based on the assessment rolls, the accuracy of which is the primary responsibility of the Assessment Corporation. On receipt, the roll is also analyzed by City divisions to ensure reasonableness. However, the following types of analyses which would further enhance the effectiveness of such monitoring are not presently being carried out:</td>
<td>That properties classified as exempt, non-billable or vacant be regularly reviewed on test basis to ensure the reasonableness of their assessment under such classifications, especially for occurrences of a material or significant nature. A simple comparative spreadsheet compiled from readily available data would highlight the vacant property sub-classes experiencing significant variations from year to year.</td>
<td>Agree. Commencing 2004, the Division will determine internal or external staffing resources to specifically carry out detailed ‘Assessment Reviews’.</td>
<td>Complete. As part of the interim taxes billing procedures, the Senior Financial Analyst in the Taxation Division runs reports that show any property that has had a class change from one year to the next. When necessary, such changes are verified with the Assessment Corporation.</td>
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<td>• List of exempt properties be reviewed on test basis for changes in their ownership or usage, etc. Identification of changes that do not meet the exemption criteria would ensure taxation of such properties.</td>
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<td>Once a year, MPAC sends its New Non-Billable lists which note properties that are newly classified as non-billable, exempt or vacant to the City. The Senior Financial Analyst reviews the lists to verify the reasonableness of properties included.</td>
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<td>• Properties that record significant increases in vacancies be reviewed for the appropriateness of such assessment. Classifying a property as vacant necessitates a rebate of 30-35% from the amount of taxes that would be paid otherwise.</td>
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<td>Initiated. Monthly reports of the completed construction are received by Taxation from Building and Licensing and forwarded onto MPAC.</td>
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<td>• Supplementary rolls arise due to delayed assessments of changes to properties by the Assessment Corporation. Retrospective taxation of such assessments is limited to the two years that immediately precede the taxation year. The City may thus suffer absolute revenue losses and delayed taxation. While such absolute loss could not be ascertained, the 2002 supplementary rolls cumulatively lead to a total retrospective levy of $1.5m. The Revenues Division has identified a reporting mechanism through the integration of the information on the Amanda and Vailtech systems to seek proactive taxation of such properties; however, such interface remains to be established.</td>
<td>That a reporting system, either through the integration of the information on the Amanda and Vailtech systems or through some other mechanism that may be developed with the cooperation of the Building &amp; Licensing Division, be developed to proactively seek assessment and taxation of new constructions and sub-divisions.</td>
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<td>MPAC is in the process of changing its system. It is working with the Building Division to develop a common electronic file layout. This is expected no sooner than mid 2006.</td>
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<td>The integration of the Building and Licensing’s Amanda system with Taxation’s Vailtech system has not proceeded. IT has identified this project in its strategy and business plan but has not identified the resources required or a time frame for its completion.</td>
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| 5. | The division did not have a ready listing of all City owned properties that have been rented out. In the absence of such a list, Internal Audit could not ensure that such properties had been taxed completely and accurately. | That a list of City-owned rented properties be requested from the Real Estates and Property Management Section. The taxation of such properties should then be reviewed.                                                                                                                                 | Agree.  
The Revenue Division has been requesting such a list for some time. Staff have observed situations in the past where taxes from leased out City properties remained outstanding after being correctly assessed and taxed.  
The Division has stressed the need to ensure that leases on city owned properties include provisions for payment of taxes by the tenant or that the lease rent is sufficient to also cover such taxes borne by the operating departments. While in most cases such provisions are made, there has been a void in communication of this information to the tax section.  
The Real Estate Division will be contacted again to request provision of this information. | In progress.  
A list of City-owned rented properties has been developed with input from the Real Estate and Property Management Section.  
The taxation of such properties is reviewed by the Supervisor of Accounts Receivable in Corporate Services. However, the Taxation Division needs to work with the Real Estate Division to ensure that the listing is current and up to date. |
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<td>6.</td>
<td>Collection of Taxes</td>
<td>The following control weaknesses in the Class Cash (POS) system used to record cash receipts were noted:</td>
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<td>• The validity of the refunds recorded by cashiers is not verified. This allows for an opportunity to misappropriate collections.</td>
<td>Agree.</td>
<td>Complete. With the implementation of the new POS system, the Cashiers must take refunds to the Customer Service Officer for their approval. The Cash Receipts Procedure was updated to reflect this in February 2005. The new system allows previewing of the reports rather than pre-closing.</td>
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<td>Further, permitting a 'pre-close' verification of the batch or its closure on the next day when it is independently verified by another staff, allows the cashiers to 'balance' their cash with the system totals. Though such practices provide flexibility and convenience, when coupled with the observation in the previous paragraph, they pose significant control risks.</td>
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<td>• The validity of each refund or void/cancelled transaction be reviewed for supporting detail. Alternatively, the authority to process refunds or record void transactions be given only to the supervisors to ensure appropriate segregation of duties.</td>
<td>Agree.</td>
<td>Complete.</td>
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<td>That the numerical sequence of the Class Cash system batches be verified to ensure completeness in accounting.</td>
<td>Agree.</td>
<td>Complete. (Alternate provided.) The new POS System was put into service in May 2004. In this new POS system, the numeric sequence can no longer be used to ascertain completeness in accounting as each user on the POS system automatically receives the next available &quot;reset number&quot;. Completeness is now ensured by balancing payments received to various reports generated by the system: i.e. the Drawer Balance Report and the Group Item Sales Report.</td>
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<td>That the numerical sequence of the Class Cash system was not verified to ensure completeness with their recording on the Vailtech system. This allows for an opportunity to misappropriate cash from unrecorded batches.</td>
<td>Agree.</td>
<td>Incomplete. Although there is an extra pick up of the tax installment cheques from City Hall on the installment due date, the processing of payments is not as efficient because of the time required to transport the cheques to Glanbrook. In order to expedite the processing and deposit of cheques, the Taxation division would like to transfer the RPS processing machine back to City Hall. In order to expedite the processing and deposit of cheques, the Taxation Division would like to investigate the feasibility of transferring the RPS processing machine back to City Hall.</td>
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<td>The possibility of such misappropriation is further increased since audit totals provided by the Class Cash system are not utilized to check transactions recorded. ‘Audit totals’ is a standard control feature that provides additional assurance against transactions that may be recorded outside the batches reported.</td>
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<td>That the cost of delays in deposit and the resultant custodial risk be evaluated against the costs of additional resources required to expedite processing and depositing of cheques around tax installment dates.</td>
<td>Agree.</td>
<td>Incomplete. During the 2004 budget process the Customer Service and the Budgets, Taxation and Policy Divisions are looking at measures to minimize the delays in the processing of cheques through the Glanbrook Municipal Service Centre</td>
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## Observations of Existing System

### Tax-Refunds

Tax-refunds are initiated and executed by staff without specific approvals from senior management. In a particular instance, refunds worth $1.1m were initiated by a single staff member. While Internal Audit ascertained the validity of the amount so refunded, the lack of management review and approval leaves the system open to manipulation.

### Recommendation for Strengthening System

That detailed procedures over the processing and approval of tax-refunds and the recording of tax-refund reversals be documented and implemented. Hierarchical authority over the approval of underlying adjustments and the refunds should be instituted for improved controls.

### Management Action Plan

Agree. Hierarchical levels of authority over tax refunds determined on the basis of the approval limits established under the Corporate Purchasing Policies are being considered for implementation by the Division before the start of 2004.

### Follow Up (September 2005)

In progress. There is a formal hierarchical structure in place that must be followed when issuing tax refunds. Written notice of MPAC or Assessment Review Board (ARB) decisions are obtained from MPAC’s website by Appeals staff. The assessment change reported in the notice is recorded in Vailtech, and with the notice as back up, approval of the change in Vailtech is obtained from one of the three senior employees in the section (the Director of Taxation, the Manager of Tax Accounting, or the Manager of Customer Service). Vailtech then utilizes the lower assessed value to adjust the municipal taxes. The resulting credit is then applied to the property owner’s account or a refund is issued at the property owner’s request. In addition, the General Manager of Finance, the City Manager and Council are informed of any large refunds through the budget variance report.

The reduction or elimination of the penalty and interest portion of the refund are also approved, in practice, by one of the three senior employees of the section.

However, the procedure drafted by the Director does not mention these levels of authorization. The finalized procedure is expected by the fall of 2006.
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<td>8.</td>
<td><strong>Tax-Sales</strong></td>
<td>That, after considering the social obligations and the broader ramifications of tax-sales, an effective, more aggressive action plan to initiate collections from properties that are delinquent in the payment of their taxes and other dues be developed, documented and implemented.</td>
<td>Agree. The Division’s tax registration activities over the past three years have already been much more aggressive than those of any of the former municipalities. This is evidenced by the significant reduction in total arrears that has been seen over the past three years. Attempts will be made to take closer looks at those properties where the tax arrears are approaching the value of the property. Staff feel that 200 registrations per year is a good target. However, if set a higher target additional staffing would be required.</td>
<td>In progress. The Taxation Division has been more aggressive in its efforts to recover taxes and other debts by issuing more letters to delinquent taxpayers. A review of the Vaittech database indicates that since the conclusion of the audit in the fall of 2003, the number of tax arrears registrations have increased. There were 200 tax registrations in 2003, 210 in 2004, and 234 as of September 15, 2005. The remaining outstanding debt from 2002 and earlier totals $10.7 million for 1,305 properties. (This compares to 2,256 properties and $48.4 million in April 2003.) Of the 19 contaminated properties identified in 2003, 18 have been sold. The $8.8 million outstanding in 2003 had grown to $9.4 million, of which $1.5 million was recovered. In addition, other Brownfield sites with unpaid taxes have been sold.</td>
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## 9. Recent amendments to the Municipal Act

Recent amendments to the Municipal Act with effect from January 01, 2003 prohibit partial receipts of the ‘cancellation price’ for properties that have been registered for tax arrears, excepting such cases where 'extension agreements' have been executed. Execution of such agreements has to be approved under Council by-laws. However, it was observed that partial payments from registered properties continue to be accepted without proper extension agreements. That, in view of the recent amendments to the governing legislation, the division review its practice of acceptance of partial payments of the cancellation price from properties that have been registered for tax arrears and amend the policies and procedures as necessary. If the acceptance of partial payments continues in certain cases, extension arrangements should be executed in the manner legislated after being approved by Council. Agree. The staff exercises its responsibility to collect taxes with due regard for social implications of their actions. Therefore, partial payments may be accepted from taxpayers making efforts to clear their taxes and other dues. However, in such cases, commencing from December 2003, the staff agrees to either 'de-register' the properties or to execute formal extension agreements within a period of three months from the date of finalizing such agreement with the taxpayers.

## 10. Vailtech System

Security and the efficiency in the usage of the Vailtech Tax System was reviewed and it was noted that:

- Incompatibilities exist between the current job responsibilities and the access rights assigned to staff.
- Though the Vailtech system is capable of recording each and every procedure carried out to affect a tax sale, considerable information is not recorded on the system. This leads to an ineffectual use of the system and results in incomplete and inaccurate reporting therefrom.
- Significant duplication of efforts and documentation arises in the process of ensuring that the two systems, Vailtech and PeopleSoft, provide the same details. Integration of the two systems would remove such redundancies and inefficiencies.

That the access to the system processes in Vailtech be reviewed to ensure appropriate segregation of duties and levels of access rights. That complete details be recorded on Vailtech to ensure accurate and meaningful reports and analyses and prevent the possible loss of information due to its recording on personalized media. That the feasibility of integrating the PeopleSoft and Vailtech systems be investigated in order to increase efficiency and ensure consistency of the information presented.

Agree. The Division had requested an integration of the PeopleSoft and the Vailtech systems approximately a year ago. However, the integration was postponed until the implementation of PeopleSoft version 8.0. It was further delayed due to performance/implementation related issues under the new version of PeopleSoft. The Revenues Division will work with the PeopleSoft team to complete integration by the end of 2004.

Agree. User accounts that were provided with additional rights on the system to help with the implementation/upgrade of Vailtech have been suitably modified to reflect current responsibilities.

Agree. Effective immediately, staff agrees to make every effort to capture the complete details of tax-sale related transactions on the system for meaningful analyses.

Agree. Though the Vailtech system is capable of recording each and every procedure carried out to affect a tax sale, considerable information is not recorded on the system. This leads to an ineffectual use of the system and results in incomplete and inaccurate reporting therefrom. A random review of the access to Vailtech has been modified to restrict the capabilities of staff according to their job function. This was confirmed by a review of Vailtech Security Profiles.

Agree. Effective immediately, staff agrees to make every effort to capture the complete details of tax-sale related transactions on the system for meaningful analyses.

Complete. Though the Vailtech system is capable of recording each and every procedure carried out to affect a tax sale, considerable information is not recorded on the system. This leads to an ineffectual use of the system and results in incomplete and inaccurate reporting therefrom. A random review of the access to Vailtech has been modified to restrict the capabilities of staff according to their job function. This was confirmed by a review of Vailtech Security Profiles.

Complete. Effective immediately, staff agrees to make every effort to capture the complete details of tax-sale related transactions on the system for meaningful analyses.

Incomplete. There continues to be no interface or integration between Vailtech and PeopleSoft.
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| 11. | Other Issues  
It was observed that the master spreadsheet used to record phase-in adjustments during 2001 & 2002 was not password protected and could be accessed by anybody having access to the network drive that it resided on. | That access to softcopy files that determine the extent of a property's taxation be restricted. | Agree.  
The 2003 phase-in adjustments file is now password protected. | No longer applicable.  
The phase-in adjustments are no longer performed and the file is no longer on the network drive. |

| 12. | It was noted that inter-account balance transfers are being recorded without appropriate supporting confirmations from the taxpayers. | That inter-account balance transfers be recorded only after receipt of formal instructions from the taxpayers. These instructions should be retained in a proper manner. | Agree.  
The divisional practice is to record inter-account transfers on explicit written instructions of the property owner except in cases of data entry error or in regards to transfers between accounts under the same ownership. However, staff agrees to describe the relevant information regarding the process followed to justify the transfer in the form of a note. Such notes would be recorded either as part of the documentation or on the system in text format. | Complete.  
A random sampling of inter-account transfers demonstrates that, in the case of a data entry error, staff applies the payment to the proper account and maintains back up to support the tax rolls impacted. Further, in cases where the inter-account transfer is brought on by the owner’s request, supporting confirmation from the taxpayer is retained. |