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December 2015

Erie County Office of County Clerk
Audit of Mortgage Recording Tax – Niagara Frontier Transportation Authority
April 1, 2015 thru September 30, 2015

STEFAN I. MYCHAJLIW
ERIE COUNTY COMPTROLLER

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December 28, 2015

Erie County Legislature
92 Franklin Street 4th Floor
Buffalo, New York 14202

Dear Honorable Members:

The Erie County Comptroller's Office has completed a limited scope audit of the Erie County Office of County Clerk's (OCC) mortgage recording tax with respect to the Niagara Frontier Transportation Authority (NFTA) for the six month period of April 1, 2015 through September 30, 2015.

Our objectives were to:

- Understand and document the mortgage recording process.
- Determine that the New Vision software provided an accurate systematic calculation of the mortgage recording tax on mortgages submitted for recording.
- Determine that NFTA was paid on a timely basis and payment amount was correct.

To accomplish these objectives, we examined original mortgage documents, confirmed automated bank transactions, observed the mortgage recording process, and performed recalculations of the mortgage recordings tax during our limited scope period.

We conducted our audit in accordance with Generally Accepted Government Auditing Standards. Such standards require that we plan and perform our audit to adequately assess those operations of the OCC that are included within our audit scope. We believe that our audit provides a reasonable basis for our findings, conclusions and recommendations.

Table of Contents

BACKGROUND....4

EXECUTIVE SUMMARY....5

AUDIT FINDINGS....5

AUDIT COMMENTS....6

EXIT CONFERENCE....7

APPENDIX A Response to External Risk Assessment....8

APPENDIX B County Clerk's Response....8

BACKGROUND

New York State Tax Law Section 253 and 253-1a states:

"Mortgage tax includes a Basic Tax of $.50 for each $100 of principal obligation secured, a Special Additional Tax of $.25 for each $100 of principal obligation secured (253-1a), both of which apply in all counties, and, in a number of counties, an Additional Tax of $.25.

Tax Law 253-1a requires that the Special Additional Tax be paid by the lender when the mortgaged property is principally improved, or it is to be improved, by a 1-6 family dwelling with separate cooking facilities, or when the mortgagor is a not-for-profit organization no part of the net earnings of which ensure to the benefits of any officer, director or member and which is exempt from taxation under IRC Section 501.

There is case law holding that Special Additional Tax need not be paid by a federally chartered savings association, including federal savings banks, and the Department continues to take the position, notwithstanding a decision in 2010 by the Supreme Court, New York County, that the Special Additional Tax is not payable on mortgage given to a federal credit union on real property principally improved or to be improved by one or more structures containing the aggregate not more than six residential dwelling units, each having its own separate cooking facilities. The Special Additional Tax is not payable at on a mortgage on such a property made to a New York State chartered credit union.

Under Tax Law Section 253, when the mortgage is a natural person, a mortgage on real property with six or less residential dwellings units is exempt from payment of the Special Additional Tax.

An affidavit must be submitted to the recording officer claiming the Special Additional Tax exemption."

New York Tax law Section 1432 Deposit and Disposition of Revenue states:

"Such local law shall also provide that an officer of the county shall pay to the Niagara Frontier Transportation Authority all revenue deposited under this section. Such payments shall be made on the tenth day of each month for the preceding month."

The Erie County Clerk is the official repository for public records relating to business, property ownership (land records) and court cases. This audit has focused on the area that processes land records.

The vast majority of the revenues collected by OCC are paid out to the State and local municipalities.

EXECUTIVE SUMMARY

In our opinion, the OCC's staff properly accounted for the mortgage recording tax revenues collected as well as consistently verified the exemption affidavits submitted with the mortgages. Additionally, the New Vision software calculated the mortgage recording tax correctly based on data inputted by the cashiers. The software appropriately apportioned the correct percentages of the mortgage recording tax revenues collected to various recipients. Furthermore, we noted management accurately and efficiently disbursed the tax monies owed to NFTA in a timely manner.

No significant matters are affecting compliance with applicable laws, rules, or procedures came to our attention. Our audit was performed for the objectives described. Our consideration of internal controls was for the limited purpose of the audit. However, material weaknesses may exist that have not been identified with respect to areas of operation not reviewed.

AUDIT FINDINGS

I. Valid Exemptions from Special Additional Tax - NFTA

We randomly tested 25 mortgage recording transactions with a zero amount in the MT NFTA column of the daily reports from June 2015. The days we randomly chose were: June 1st, 10th, 17th, 19th, and June 22nd. We observed the original documentation online and verified the required affidavit necessary for that particular mortgage to be exempt from paying the Special Additional Tax – NFTA at the time of its recording was valid. Furthermore, we noted the exemption reason and proper affidavit form number.

We concluded there were no findings. The transactions tested had proper affidavits attached and warranted the exemption from the Special Additional Tax – NFTA. The zero amounts in the MT NFTA column for each transaction tested was correctly stated in the daily report.

II. Accounting for Mortgage Recording Tax Revenues

We tested each business day in the month of June. We verified that each end of the day revenue collection report summed up to the revenues reported for the month. Then we compared the total to the official Statement of Mortgages that were sent to the State Commissioner of Taxation and Finance and the Erie County Director of Finance.

We concluded that there were no findings. The June daily revenues collected tied to the monthly total that was ultimately disbursed to its recipients. In particular, we noted the NFTA revenues collected were disbursed accurately and for the total amount collected for the month.

III. Calculation of Mortgage Recording Tax

We randomly chose two transactions for each business day of June 2015. We obtained the original documentation in paper form. We recalculated the mortgage tax based on the original documentation then compared it to the New Vision systematic calculation that is done "behind the scenes" once the cashier enters the proper information into the system fields.

We concluded there were no findings. The New Vision software properly calculated the mortgage recording tax. In particular, it calculated the Special Additional Tax – NFTA accurately based on exempt or not exempt status.

IV. Disbursement of Mortgage Recording Tax Revenues

We verified that the NFTA disbursements made based on the official Statement of Mortgages Recorded reports for the six months in our limited scope period were executed and received in a timely manner as stated in the New York Tax Law Section 1432 as "payment shall be made on the tenth day of each month for the preceding month". Our evaluation of the M&T bank statements revealed detailed ACH transactions and provided documented proof of the electronic payments made to the NFTA.

We concluded that there were no findings. The Mortgage Recording Tax – Special Additional Tax portion was remitted to the NFTA during the first five days of the following month.

AUDIT COMMENTS

The recordkeeping software, New Vision, is not used by any other county clerk's office in New York State. This poses a possible risk that the software company will no longer support its New York version of New Vision for viability reasons. The OCC is currently in a five year contract for support services.

As a follow up to the internal control findings from the 2012 Audit, we noted weaknesses in the segregation of duties and management oversight with regards to the Deputy County Clerk - Finance position still exists. The Deputy is responsible for all bank deposits and reconciliations, internal and external wire transfers between the bank accounts and its monetary recipients. The Deputy continues to be responsible for initiating, processing and recording bank transactions. The Deputy prepares the monetary disbursements via ACH and check. There is little to no oversight or review by a senior staff member.

An effective system of internal controls requires segregation of duties. It is especially important that the functions of recording cash and checks, depositing receipts, initiating banking transactions, reconciling bank records, and maintaining accounting records be divided among several employees to reduce the risk of errors and fraudulent activities.

Management is responsible for the internal controls. Increased review of activities by a supervisor or other senior staff member can be a mitigating control where adequate segregation is not obtainable. Management should evaluate the control functions on a regular basis.

Our recommendations remain the same as the prior audit:

- Have another member of management prepare the bank reconciliations OR at least have someone sign off and date on the monthly bank reconciliations prepared by the Deputy.
- Require two signatures on checks issued.
- Establish a system of checks and balances in the office, whereby any transaction processed, recorded, or approved by one employee is reviewed by a supervisor or senior staff member.
- Cross-train staff so that in the absence of one individual, the duties can be performed by another.

RESULTS OF EXIT CONFERENCE

On December 31, 2015, an exit conference was held with the County Clerk – Christopher Jacobs, First Deputy County Clerk – Peggy Lagree and Deputy County Clerk – Thomas Christy where the contents of the report were discussed. Mr. Jacobs informed us of a Risk Assessment Report had been done by Tronconi Segarra & Associates which addressed some of our audit comments. We obtained a copy of the report for further review and consideration.

ERIE COUNTY COMPTROLLER'S OFFICE

cc: Hon. Mark C. Poloncarz, County Executive
Hon. Christopher L. Jacobs, County Clerk
Hon. Erie County Legislature
Robert W. Keating, Director of Budget and Management
Erie County Fiscal Stability Authority

APPENDIX A – Response to External Risk Assessment Report

We reviewed a report titled Risk Assessment - Cash Receipts/Revenue Collection Cycle Findings and Recommendations for the period January 1, 2011 through September 30, 2012. It was prepared by Tronconi Segarra & Associates Certified Public Accountants & Business Consultants.

We are in agreement with many of their findings and many of their recommendations. Our follow-up review included some of these as well. They used a much broader scope in reviewing the operations. The Clerk's response included some points that they have not yet implemented.

APPENDIX B – County Clerk's Response

On January 15th, 2016, our Office received a written response from the County Clerk's Office. On the next page we have provided the comments.

COUNTY OF ERIE

CHRISTOPHER L. JACOBS
COUNTY CLERK

ERIE COUNTY CLERK'S RESPONSE TO COMPTROLLER'S AUDIT OF MORTGAGE RECORDING TAX- NIAGARA FRONTIER TRANSPORTATION AUTHORITY APRIL 1, 2015 THRU SEPTEMBER 30, 2015

The Erie County Clerk is in receipt of the Comptroller's Audit referenced above. The Clerk respects the checks and balances that separation of government provides and openly and enthusiastically participated in fulfilling our obligation to provide all relevant information. We welcome ongoing and constructive dialogue that would improve the efficiency and accuracy of the operations of the Clerk's Office, not just during the formal audit process, but any time forward-thinking improvements are identified.

Following is our response to the audit for inclusion in your final report.

Executive Summary

The Clerk is pleased that within the original scope of the audit no findings were identified. We question the basis of the last sentence of the summary that states "material weaknesses may exist that have not been identified with respect to areas of operation not reviewed." This statement is purely conjectural, outside the scope of the audit, overly broad and not supported by sufficient facts or data.

Audit Findings

In areas examined within the scope of the audit, the audit concluded there were "no findings" in four areas:

I. Valid Exemptions from Special Additional Tax – NFTA.
II. Accounting for Mortgage Recording Tax Revenues.
III. Calculation of Mortgage Tax Recording Tax.
IV. Disbursement of Mortgage Recording Tax Revenues.

We agree that there were no adverse findings. In every area examined within the scope of the audit the auditors findings concluded that proper procedures were followed, transactions were calculated, accounted for, reported and disbursed accurately.

Background Information

For clarification to the point made in the audit, page 4, paragraph 4, the New York State Court of Appeals held in Hudson Valley Federal Credit Union vs New York State Department of Taxation and Finance, et al, 956 NYS2d 425 (2012) "federal credit union mortgages are NOT exempt from the State's [mortgage recording tax]." No discussion of the liability for, or distinction between, mortgage recording tax and the special additional mortgage recording tax is made by the Court. Because New York Law specifically exempts mortgages made to State chartered credit unions when the mortgaged premises consist of real property improved by a structure containing six residential dwelling units or less, each with separate cooking facilities (Tax §253.1-a(a)), the State Department of Taxation and Finance has taken the position that mortgages made to federal credit unions should be treated similarly to mortgages made to State chartered credit unions with regard to special additional mortgage recording tax. (See TSB-M-12(1)R).

Audit Comments

The audit states - "The recordkeeping software, New Vision, is not used by any other county clerk's office in New York State. This poses a possible risk that the software company will no longer support its New York version of New Vision for viability reasons, The OCC is currently in a five year contract for support services."

We question the relevance of this statement and accuracy of the conclusion. NewVision Systems Corporation has been in business since 1989. It provides software to approximately 30 counties in seven states. The Erie County Clerk's Office has utilized their software for recording, archiving and retrieval of our official records for almost 10 years. Erie County is on the same base software as all of their customers, which is designed to adapt to specific needs. In the last four years alone, we have benefited from technology improvements and advancements that have allowed Erie County to remain in the forefront on new initiatives in New York such as eRecording and eFiling at minimal cost to the County. Being the only county in New York utilizing NewVision has no bearing on the quality or viability of their services.

We take exception to comments regarding items included in a previous internal control audit issued by the Comptroller's Office in June 2012; those specific issues are outside the scope of this audit. The current very limited audit was not intended to afford the Comptroller's Office a second opportunity to opine upon matters not under consideration and without additional considered evaluation. We concurred with many of the recommendations made by the Comptroller in 2012 and not only implemented those changes, but took additional steps to ensure the integrity of our operations and financial accountability.

We engaged an independent accounting firm, Tronconi Segarra & Associates, to perform a Risk Assessment of the Cash Receipts/Revenue Collection Cycle of the Registrar Division. That report, issued in September 2012 and attached hereto, identified areas of risk and internal control recommendations. Included in that report were processes the Clerk's Office adopted to address the areas of risk identified. Notably, implementing a double entry accounting system, which was non-existent previously.

The Tronconi Segarra report was supplied to the Comptroller's Office at the beginning of the current audit; however, the auditors stated at the Exit Conference that no consultation or review was made in conjunction with the current audit.

We concur additional controls could be put in place to further segregate duties within the finance area and we will institute changes in the first quarter of 2016.

We want to thank the Comptroller's Office Audit Division for their work during this audit. As noted, the Clerk's Office has implemented many of the recommended corrective actions cited in previous audits by the County Comptroller and Tronconi Segarra and we take any review of our operations, policies and procedures seriously.

Respectfully submitted January 15, 2016.

CHRISTOPHER L. JACOBS
Erie County Clerk