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STATE COMPTROLLER



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September 18, 1998

Mr. Michael Urbach
Commissioner
Department of Taxation & Finance
W. A. Harriman State Office Campus
Building 9
Albany, NY 12227

Re: Report 98-F-24

Dear Mr. Urbach:

According to the State Comptroller's authority as set forth in Section 1, Article V of the State Constitution and Section 8, Article 2 of the State Finance Law, we have reviewed the actions taken by officials of the Department of Taxation and Finance (Department), as of July 31, 1998, to implement the recommendations included in our prior report, Report 96-S-9, entitled "Withholding Tax Revenues." Our prior report, which was issued on February 4, 1997, examined the Department's control over the receipt of withholding tax revenues at both the Department and the Chase Manhattan Bank (Bank).

Background

The Department administers the State's tax laws and serves as its general tax collection agency. The Department's Processing and Revenue Management Division (Division) administers the Withholding Tax program to ensure that employers appropriately deduct, report and submit employee wage withholdings in accordance with Article 22, Section 671 of the New York State Tax Law. For the 1997-98 State fiscal year, annual withholding tax collections totaled approximately \$19 billion from more than 425,000 employers. The Department contracts with the Bank to collect and process New York State withholding taxes. The majority of withholding tax collections are received directly by the Bank. The Department receives about \$60 million (.3 percent of total collections) and then forwards these collections to the Bank.

Article 22, Section 9 of the New York State Tax Law requires employers with annual withholding tax collections equal to or greater than \$400,000 to participate in the Department's PrompTax program (PrompTax). Under PrompTax, employers must submit their withholding tax

payments by using electronic funds transfer (EFT) or by using a certified check. Employers with lesser amounts of withholding tax collection can choose to participate in the PromptTax program if they meet certain Department requirements. PromptTax accounts for approximately 60 percent of all annual withholding tax revenues. Other than PromptTax withholding collections account for the remaining 40 percent of revenues. Employers who are not using PromptTax must submit paper tax returns in accordance with Department criteria.

Summary Conclusions

Our prior audit concluded that Department management had taken appropriate steps to ensure that daily withholding tax collections were properly received, documented and deposited. However, the prior audit found that certain Department and Bank internal control processes could be strengthened to better safeguard withholding tax revenues from loss or misuse.

Summary of Status of Prior Recommendations

Of the five prior audit recommendations, we found that the Department had implemented four recommendations and had not implemented one recommendation.

Follow-up Observations

Recommendation 1

Adequately separate duties among Unit staff who process withholding tax remittances for transmittal to Chase Manhattan Bank. Consider rotating withholding tax remittance processing responsibilities.

Status - Implemented

Agency Action - The Department has developed a plan for separating duties between staff and rotating those responsibilities on a weekly basis.

Recommendation 2

Maintain a control record of all checks and/or documents that are returned to taxpayers.

Status - Implemented

Agency Action - The Department developed a remittance control record to account for checks and/or documents sent to taxpayers.

Recommendation 3

Maintain a key distribution log and ensure only authorized staff have access to the file cabinet.

Status - Implemented

Agency Action - The keys to the file cabinets are no longer kept in an unlocked drawer with unlimited access. The supervisor of the unit is responsible for distributing the keys. A list of the authorized supervisors is maintained.

Recommendation 4

Ensure Chase Manhattan Bank establishes an adequate separation of duties for processing certified PromptTax checks.

Status - Not Implemented

Agency Action - Certified PromptTax checks continue to be processed by one individual. This one individual verifies check bankability, assigns deposit serial numbers, calculates and verifies check and return totals, prepares the credit memo for the deposit amount and forwards the checks for data entry. Department officials contended that although the process is performed by one bank employee, this individual is bonded and has the skill necessary to handle the specialized processing of these checks. Officials also believe that secondary security such as facility card access and surveillance cameras afford control.

Auditors' Comments - We continue to believe that separating duties for the processing of certified PromptTax checks is needed to help ensure that assets are adequately safeguarded.

Recommendation 5

In accordance with the State Finance Law, ensure EFT reversal transactions are remitted to OSC's Personal Income Tax Group for audit and approval.

Status - Implemented

Agency Action - Beginning November 1996, PromptTax requests for electronic funds transaction reversal have received pre-audit approval by OSC staff prior to the funds being returned to the transaction originator.

Major contributors to this report were Arthur F. Smith, Naomi Hoffman and Kevin Connolly.

We would appreciate your response to this report within 30 days, indicating any action planned or taken to address the unresolved matter discussed in this report. We also thank Department management and staff for the courtesies and cooperation extended to our auditors during this review.

Yours truly,

Jerry Barber
Audit Director

cc: Robert L. King