# LEGISLATIVE AUDIT COMMISSION

Review of
Department of Revenue
Two Years Ended June 30, 2014

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**REVIEW: 4455**
**ILLINOIS DEPARTMENT OF REVENUE**
**TWO YEARS ENDED JUNE 30, 2014**

**FINDINGS/RECOMMENDATIONS - 14**

**IMPLEMENTED - 6**
**ACCEPTED AND PARTIALLY IMPLEMENTED - 8**

**REPEATED RECOMMENDATIONS - 9**

**PRIOR AUDIT FINDINGS/RECOMMENDATIONS - 21**

This review summarizes the auditors' reports on the Illinois Department of Revenue, filed with the Legislative Audit Commission May 28, 2015. The auditors conducted a compliance examination for the two years ended June 30, 2014 and a financial audit for the year ended June 30, 2014 in accordance with *Government Auditing Standards* and State law. Auditors stated the financial statements were fairly presented.

The Department of Revenue is empowered to administer, collect, enforce, and determine the distribution of the taxes imposed by the State's major tax acts. The Department also administers and oversees the operations of the Liquor Control Commission. Effective July 1, 2009, the Department of Revenue transferred all functions of the Gaming Board and the Racing Board to their respective agencies. As of July 1, 2011, Lottery operations transitioned to a private manager and on October 15, 2011 all remaining Lottery functions were transferred from the Department of Revenue to the Department of the Lottery.

The Department collected approximately 79% of the receipts deposited into the General Revenue Fund for FY13 and FY14. A significant portion of the Department's total effort relates to the collection of the Retailers' Occupation Tax (ROT) and related taxes, income taxes, and personal property replacement taxes. The revenue collected from these sources approximated 88% of taxes collected by the Department for FY14 and FY13. The remaining 12% of the Department's revenue was derived from the collection of 26 other taxes. In addition to collecting State taxes, the Department collects some taxes on behalf of local governments, and administers the Senior Citizens' and Disabled Persons' Property Tax Relief Act and the Additional Tax Relief Act.

The Director of the Department during the audit period and since February 2003 was Mr. Brian Hamer. Ms. Constance Beard began serving as Director in January 2015 and currently serves in that position. For the previous 17 years, Ms. Beard, a licensed attorney, was the founding Executive Director of the Illinois Chamber's Tax Institute.

The average number of employees at June 30 was:

| | FY14 | FY13 | FY12 |
|---|---|---|---|
| Tax Administration | 1,628 | 1,544 | 1,599 |
| Shared Services | 27 | 29 | 25 |
| Liquor Control Commission | 43 | 44 | 43 |
| **TOTAL** | **1,698** | **1,617** | **1,667** |

## Service Efforts and Accomplishments

Appendix A contains service efforts and accomplishments of the Department of Revenue as well as the Liquor Control Commission.

## Expenditures From Appropriations

The General Assembly appropriated $764,114,700 to the Department in FY14 from 24 funds. The Department had expenditures of $641,795,943 in FY14 compared to $592,656,665 in FY13, an increase of almost $49.2 million, or 8.3%. Some of the significant changes in fund expenditures were as follows:

- $22.3 million increase in the Illinois Affordable Housing Trust Fund due to a $10 million payment for the Illinois Housing Development Authority upon an accounting error by IHDA, greater revenue expenditures of $8.2 million, and a one-time payment of $5 million for the new Welcome Home Illinois Program;
- $21 million decrease in the Illinois Tax Increment Fund due to final expenditures for the Tax Increment Financing Program being paid in FY13 and no expenditures during FY14;
- $17.6 million increase in the Local Government Video Gaming Distributive Fund due to an increase in video gaming income;
- $8.2 million increase in the Rental Housing Support Program Fund due to an increase in Awards and Grants;
- $7.6 million increase in the Federal HOME Investment Trust Fund due to carry over of FY13 funds for additional projects;
- $7.3 million increase in the Abandoned Residential Property Municipality Relief Fund due to the establishment of the fund.

Appendix B summarizes the appropriations and expenditures by object for the period under review. Lapse period expenditures in FY14 were about $84.2 million, or 13.2% of total expenditures.

## Cash Receipts

Appendix C summarizes cash receipts of the Department for the year under review. Cash receipts were $41.5 billion in FY14 compared to $40.9 billion in FY13, an increase of $0.6

billion, or 1.5%. Most of the increase in FY14 was due to an increase in sales tax income. Other changes included:

- Sales tax receipts increased $594 million;
- Taxes collected on public utilities decreased $81 million;
- Motor Fuel taxes increased $34 million; and
- Taxes collected on the sale of cigarettes increased $28 million.

## Taxes Receivable Balances

Appendix D is a summary of taxes receivable balances. Net taxes receivable increased from $1,166,202,000 at June 30, 2013 to $1,211,455,000 at June 30, 2014. These taxes are due from individuals, corporations, and businesses. In FY14, approximately $705 million of $1.9 billion in total taxes receivable was considered uncollectible.

## Property Report

Appendix E is a summary of changes in State property for FY14 and FY13. Total property decreased from $13,026,705 at July 1, 2012 to $11,891,011 at June 30, 2014. Equipment comprised $11.86 million of total property in FY14.

## Accountants' Findings and Recommendations

Condensed below are the 14 findings and recommendations presented in the reports. There were nine repeated recommendations. Responses to the recommendations are classified based on updated information provided by Barb Ringler, Chief Internal Auditor, via electronic mail on April 12, 2016.

## Accepted or Implemented

1. **Take steps to improve the review process of the underlying data that helps compile the financial statements. In addition, work with the appropriate parties to establish an accounting/financial reporting system that is integrated with its operational systems to: 1) reduce errors associated with manual intervention in converting data; and 2) improve upon the timeliness in preparing and reporting required financial information. (Repeated-2012)**

**<u>Finding</u>**: The Department's initial year-end financial reporting (GAAP) to the Illinois Office of the Comptroller contained inaccuracies. The issues associated with the inaccuracies, if not detected and corrected, could misstate the Department's financial statements and impact the

Statewide financial statements prepared by the Illinois Office of the Comptroller.

**Accepted or Implemented – continued**

Auditors noted errors regarding the reporting of financial information. A summary of some of the errors identified are as follows:

- During the audit, the Department identified a reciprocal agreement with another state that was not being properly recorded in its financial statements. The Department received a check from the other state in December 2013 for the 2012 tax year. The taxes receivable and unavailable revenue in the General Fund and the taxes receivable and income tax revenues in the governmental activities were understated in the prior year for the amount of the December 2013 check and the estimate of income taxes to be received relating to January through June 2013 totaling $122 million. The Department reported a restatement to the government-wide beginning net position for the understatement of taxes receivable. As the Department also received a check in December 2014, the Department notified the Illinois Office of the Comptroller and requested journal entries to be made to three of the Department's closed GAAP Reporting Packages for the total amount of $122 million.

  Department personnel stated the annual cash transaction never came to the attention of the Financial Control Bureau because the reciprocal state payment was processed as a timely filed current year income tax in December of each year.

- During the audit, it was noted the Department did not update the percentages used to properly allocate the corporate income tax activity between corporate income tax and personal property replacement tax for year-end adjustments to taxes receivable and unearned revenue for FY13 and FY14. Therefore, in FY13 the General Fund taxes receivable balance was overstated by $1.5 million and the unearned revenue was understated by $24 million for a total overstatement of income tax revenue of $25.5 million. In FY13, the Personal Property Tax Replacement Fund taxes receivable balance was understated by $1.5 million and the unearned revenue was overstated by $24 million for a total understatement of income tax revenue of $25.5 million. The Department reported a restatement to the General Fund and the Personal Property Tax Replacement Fund beginning fund balances for the misstatement in income tax revenue in the prior year. In FY14, the General Fund taxes receivable balance was understated by $2.8 million and the unearned revenue was understated by $27.7 million for a net overstatement of income tax revenue of $24.9 million. In FY14, the Personal Property Tax Replacement Fund taxes receivable balance was overstated by $2.8 million and the unearned revenue was overstated by $27.7 million for a net understatement of income tax revenue of $24.9 million. The Department adjusted three fund GAAP Reporting forms and included the updated balances in the financial statements.

  Department personnel stated the error in the percentages used was due to percentages not being properly updated in spreadsheets used to calculate the year-end adjustments during the GAAP Package preparation process.

- Auditors noted errors in the Department's calculation of transfers from the General

Revenue Fund to the Local Government Distributive Fund during the fiscal year. During the May 2014 transfer calculation, the individual income tax and the business income taxes were transposed, overstating the transfer to the Local Government Distributive Fund by $14.6 million. During the July 2014 transfer calculation the receipts transferred from the Protest Fund were misstated which understated the transfer by $106 thousand. Therefore, the transfers from the General Revenue Fund to the Local Government Distributive Fund were overstated by $14.5 million in FY14. The misstatement was not considered material at the fund level by the Department and the financial statements were not corrected as of June 30, 2014. However, the Department indicated the overstatement was corrected in the transfers from the General Revenue Fund to the Local Government Distributive Fund in January 2015.

Department personnel stated the error in the transfer calculations was the result of human error.

- During testing of the Department's taxes receivable, it was noted the Department did not perform an analysis of the percentages used in the calculation of uncollectible taxes receivable balances during the fiscal year. As the Department reports $2.7 billion in taxes receivable and a $916 million allowance for uncollectible taxes, a small change to the allowance percentages could have a material impact on the Department's financial statements and could cause the net taxes receivable balances to be misstated.

  Department personnel stated GenTax was a multi-year, multi-system conversion project that is still ongoing. The Department is planning to update the analysis after the last rollout of the final taxes and general ledger implementation planned for July 1, 2015. The Department indicated this will be a substantial project that takes a significant amount of planning and programming.

- During testing of the Department's accounts receivable from income tax accounts, Business, Withholding, and Individual, auditors noted exceptions with certain accounts. Auditor testing identified five Business Income Tax accounts that had errors: a) two errors were the result of interest not being properly calculated; b) two errors were the result of penalties not calculated correctly; and c) one error was the result of an electronic funds transfer (EFT) payment being posted to the wrong FEIN prior to year-end but not applied to the correct account until after year end. The net effect of the above noted errors resulted in accounts receivable for those specific accounts being overstated by $392,035.

  The errors noted above as well as other errors identified in testing accounts receivable associated with Individual Income Tax were projected to the entire billed income tax receivable populations, and the projected estimated overstatement for the populations as a whole was $5.3 million. The adjustment was not considered material by the Department and no adjustment was made to the financial statements.

  Department personnel stated the errors noted by the auditors were the result of an error in the system not calculating interest appropriately for years before 2010 and human errors due to manual calculations being performed by Department personnel. Department personnel noted they continually strive for perfection, but a certain amount of errors will always be inherent in such a complex operating environment.

- During testing of the Department's taxes receivable for Business Income Tax and sales (ROT) tax accounts, auditors noted taxpayer legal settlements and audits that appeared to be completed before the fiscal year end that had not been entered into GenTax. As the taxpayer accounts were not updated within GenTax, the accounts had the potential to affect the year end accounts receivable and refunds payable balances.

  Department personnel noted the Audit Bureau's Review and Perfection Division had been short staffed for years, resulting in a backlog. It was further noted existing staff from other areas have been temporarily assigned to reduce the backlog and the Department is expecting to fill open positions.

**Updated Response:** Accepted and partially implemented. The Department has corrected nine out of ten issues (90%) associated with this finding and recommendation, as was evidenced by the FY15 Financial Audit. Preparing an analysis of the percentages used to calculate uncollectible taxes receivable is the remaining issue to be corrected, which will be implemented by June 30, 2016.

**2. Ensure taxpayer information is adequately protected during both business and non-business hours from potential unauthorized access as mandated by State statute and IRS Publication 1075. (Repeated-2010)**

**Finding:** The Department has not completely implemented controls and safeguards over processing taxpayer information. During FY14, the Department processed 18 million tax receipt documents throughout its facilities, totaling $40 billion.

During testing auditors noted instances in which the Department's internal controls to protect taxpayer information contained weaknesses in certain physical safeguards to control access to areas within the Department as well as the storage of taxpayer information. Department staff confirmed to the auditors they were not aware of any specific instances of loss of confidential information due to the identified weaknesses in physical safeguards.

Department personnel stated they continue to make improvements over the areas of protection of taxpayer records. In addition, it was noted they are working with recommendations from their Security Consultant to enact the recommendations as funding becomes available.

**Updated Response:** Accepted and partially implemented. The Department has worked diligently on plans to adequately protect all taxpayer information, and had started the physical work in FY15, such as installing locking bars and padlocks at all district offices and the JRTC. In addition, security equipment for cameras and turnstiles have been purchased, as well as approximately one-third of the garage doors needed to secure taxpayer files. However, because of lack of an FY16 budget, the work had to stop, and therefore, we have not been able to complete the modifications as planned. Once a budget is passed, work will continue.

**3. Integrate the applicable systems from the various areas to reconcile detail return information with deposit information to reduce the reliance on staff to perform the complex calculations on multiple spreadsheets. (Repeated-2011)**

**Finding:** Auditors noted weaknesses in the Department's internal control over the deposit, allocation, and distribution of receipts from sales and use taxes (Retailers' Occupation Tax or ROT).

During FY14, the Department deposited approximately $13 billion in ROT receipts into the State Treasury. As cash is collected daily, the Department allocates 98% of receipts to various State and local government funds based upon a biannual estimate. For the remaining 2% of receipts, the Department sets aside these collections (2% reserve) in order to have sufficient funds to "true-up" the various local government funds once the ROT returns are perfected and the correct/final local government allocations are known.

The Department's receipt allocation process is a manual paper process involving data amassed from several sources with complex calculations on multiple spreadsheets. It relies on interaction between various areas within the Department that are responsible for portions of the ROT tax deposit and allocation process. The source data needed for the process is partially obtained by two different divisions within the Department and from records from the Office of the State Comptroller. The structure creates additional risk of error and miscommunication.

As a result of these limitations, the cash receipts and revenue associated with the unperfected returns from the 2% reserve are generally recorded in the State's General Fund. Upon perfecting the returns, cash allocations to other governmental and fiduciary funds will be required and could be material. Further, due to the current cash allocation process limiting the accuracy of each individual fund's cash balance at a point in time, it also limits the State Treasurer's ability to accurately allocate interest due to various local government funds.

Regarding the exceptions noted in this engagement, Department personnel stated without legislative approval for significant investments into system upgrades and mandatory electronic filing, the Department lacks the information and system capability to allow for precisely allocating all receipts when they are initially received. The true-up of funds is merely a timing issue and the variances to fund balances, including interest allocations, is not deemed material by the Department.

**Updated Response:** Implemented. The receipt deposit, allocation and distribution process for sales and use taxes was integrated into GenTax on March 1, 2016, and is working well.

**Accepted or Implemented – continued**

**4. Establish a documented process over the administration of GenTax users. Additionally, maintain documentation of the authorization of access, periodically review the access rights of all users, and timely deactivate separated employee accounts.**

**In addition, ensure required background checks are properly and timely completed, including those for individuals with access to GenTax. (Repeated-2010)**

**<u>Finding</u>:** The Department continued to lack adequate security controls over the GenTax system and data.

The Department utilizes GenTax to carry out its mission as "chief tax collector for the State of Illinois." GenTax maintains confidential and personal information on all individuals who pay taxes to the State of Illinois.

Since FY10, auditors have noted weaknesses in the controls over the security of GenTax. During the current examination testing, auditors noted:

- The Department did not have a documented process for the administration of access rights.

- Access rights for individuals who separated employment from the Department were not always timely deactivated. Auditors noted nine of 21 separated individuals tested were deactivated from nine to 969 days after separation.

- For four of 32 individuals with access to GenTax, the Department did not provide documentation to support the required background checks had been completed. Additionally, three of these four individuals had administrative access rights to the computer servers in which the GenTax System and data reside.

- The Department could not provide an explanation as to why 29 of 33 individuals had access to GenTax and data.

- The Department could not provide documentation authorizing four of 17 individuals access to GenTax.

Department management stated the Department has a process for administration of access rights and deactivation of access to GenTax, but that process is not formally documented.

**<u>Updated Response</u>:** Accepted and partially implemented. Three of six (50%) of the audit issues have been resolved. A documented process over the administration of GenTax users is anticipated to be completed by June 30, 2016. An "Exit Interview" form is being developed that will standardize the notification for deactivation of security rights. The anticipated date for finalization is June 30, 2016. The Department has been retaining documentation of the authorization of access, reviewing access rights of all users, and properly and timely completing required background checks for individuals with access to GenTax since November 2015.

5. **Ensure the change management process is effectively controlled and documented. Also, ensure all changes adhere to the Department change control standards.**

   **In addition, restrict programmer access to all production programs and data. If programmer access is necessary in some situations, establish and enforce compensating controls to ensure appropriate management oversight and approval of changes. (Repeated-2008)**

**Finding:** The Department lacked adequate controls over the change management process. Auditors noted the Department had developed standards, processes and procedures to control the change process over the enterprise wide tax system (GenTax); however, the standards were not consistently followed and did not address requirements for approving, testing, documentation and post implementation reviews.

In addition, the auditors tested 30 completed change requests to GenTax, noting:

- Testing documentation was not always maintained,
- Approvals to move the change to the Production environment were not maintained,
- Migration Checklists were not maintained, and
- Requirements to verify changes after the move to the Production environment were not completed.

Additionally, it was noted the Department's programmers had access to the production environment in order to complete changes.

Department officials stated change control standards were not consistently followed due to managerial oversight.

**Updated Response:** Accepted and partially implemented. One of seven of the audit issues has been resolved. Programmers' access to production data was removed August 3, 2015. All other portions of the recommendation have been given appropriate attention and the target date to implement the new procedures is April 30, 2016.

**Accepted or Implemented – continued**

6. **Upgrade disaster contingency plans to address the current environment, including the enterprise wide tax system (GenTax). Also, ensure the contingency plans include details specific to the recovery applications and data. In addition, test the contingency plans annually and continually update the plans to reflect environmental changes and improvements identified from tests. (Repeated-2006)**

**Finding:** The Department continued to have inadequate planning or testing for the recovery of its applications or data.

The Department carries out its mission as the "chief tax collector" for the State of Illinois through the use of Information Technology. The Department is reliant upon approximately 111 applications in order to support their mission. The Department's disaster contingency plans had not been updated and had not been tested to ensure timely recovery of applications and data.

In 2006, the Department contracted with a vendor for the development of the enterprise wide tax system (GenTax). As part of the contract, the vendor was to develop a disaster contingency plan. However, such a plan still has not been developed. During FY14, approximately 12.5 million taxpayer returns had been processed through GenTax.

Department personnel stated the applications and data are housed and maintained by the Department of Central Management Services (CMS). Despite ongoing efforts, CMS has not provided the Department with the necessary recovery capabilities to allow it to finalize its disaster recovery plan.

**Updated Response:** Accepted and partially implemented. The Department is making progress on documenting and verifying all its systems and grouping them in order to be addressed on CMS's Business Reference Model (BRM) and the new Business Application Rationalization (BAR). In addition, all the Department's data is backed up and stored daily at the Alternative Data Center (ADC) in Oak Brook, IL. The Department has used the backup for GenTax to restore the environment in the past, but not within the last year. The Information Technology area has plans to work with CMS to do this again.

7. **Obtain and use the most up-to-date death file record to help ensure refunds paid to individuals are appropriate; develop a formal process to document monitoring of taxpayer account activity and actions taken by management to address issues noted and; develop and formalize business rules setting forth the Department's process for account offsets across tax types.**

**Finding:** While testing various areas within the Department, auditors identified issues with monitoring refunds to deceased taxpayers as well as documenting reviews of taxpayer accounts in process. In addition, auditors noted a lack of policies and procedures (business rules) related to the Department's internal offset program.

- Auditors identified 8,759 individuals who received income tax refunds totaling $8.4 million. Auditors noted as a result of their testing the Department had not been using the most up-to-date Social Security Administration death record file. While there are legitimate reasons for refunds to taxpayers identified as being deceased, auditors noted approximately 200 questionable refunds which were communicated to the Department for follow-up.

  Department management stated due to procurement issues, the contract to obtain the death master file update was not completed timely.

- Auditors noted the Department did not have a formal process to document actions taken for the monitoring of indicators placed on taxpayer accounts. The Department places various indicators on taxpayer accounts for a variety of reasons: information has been received and needing to be worked; the account should not be processed further until specific information or activity is completed; etc. During testing of the inventory of taxpayer accounts with such indicators at June 30, auditors noted the number of taxpayer accounts with such indicators had significantly increased from 37,850 in FY12 to 66,973 in FY14.

  During discussion with the Department's Processing Division, it was noted weekly inventory reports indicating taxpayer information waiting to be worked was produced and provided to management; however, there was no documentation of a formal review and any actions taken based on the review of these reports. In addition, other divisions indicated they did not have processes in place to monitor such account activity in GenTax.

  Department management stated although they have processes in place to monitor indicators, these processes are not completely documented nor are they comprehensive enough to track all possible uses for each indicator. The Department failed to update these processes to coincide with its growing dependence on technology.

- During testing of business income tax accounts, the auditors noted the Department used informal criteria for determining and developing the process of when to offset income tax overpayments against other tax liabilities. The Department had not established written formal business rules for these transactions.

  Department management stated business rules were relayed to the programmers during the development of the various implementation phases of GenTax. Modification to the initial business rules are reflected in the change requests (SQRs), which are the official change vehicle for production activity.

**Updated Response:** Implemented. An upgraded version of the Social Security Administration's death record file was purchased and has been in use since August 2015. The process for review and monitoring of indicators placed on taxpayer accounts has been formally and comprehensively documented. Formal business rules have been documented

**Accepted or Implemented – continued**

for the offsetting of income tax overpayments against other tax liabilities as of November 2015. Review of weekly inventory reports and any actions taken by those reviews are also being documented.

8. **Devote sufficient resources to develop an effective internal audit program such that all planned audits are performed within the designated time period in accordance with the Act. (Repeated-2012)**

**Finding:** The Department's Office of Internal Audit (OIA) did not comply with the Fiscal Control and Internal Auditing Act (FCIAA).

Based on auditor testing, OIA did not meet FCIAA coverage for the two year examination period. The Department has recognized and documented in their FY13 and FY14 Annual Reports that they do not have adequate staffing levels within the OIA to perform the work to be in compliance with the Act.

The OIA Audit Plan for FY13 identified 11 high risk audits and projects to be performed during the fiscal year. OIA postponed four and cancelled one of these, representing 36% of the original budgeted hours scheduled to be performed during FY13. Three additional audits and projects were added to the plan during the year, of which one was subsequently postponed. The two remaining additions replaced 13% of the budgeted hours not used in the original plan.

The OIA Audit Plan for FY14 identified eight high risk audits and projects to be performed during the fiscal year. OIA postponed two of these, representing 38% of the original budgeted hours scheduled to be performed during FY14. Nine additional audits and projects were added to the plan during the year; however, OIA does not have documentation of the effort and resources utilized to complete these audits and projects.

Furthermore, documentation could not be provided on how the Audit Plan was developed and how the initial population of audits were identified in relation to a risk assessment matrix prepared by the Department.

Department personnel stated the noncompliance with FCIAA requirements is due to inconsistent leadership of the Internal Audit Division.

**Updated Response:** Implemented. An effective internal audit program has been developed and all major systems of internal accounting and administrative control have been included in the Two-Year Audit Plan, in accordance with the Fiscal Control and Internal Auditing Act. The Plan is being followed, is current, and is on track to be completed timely.

**9. Annually send a formal notice to those employees whose jobs involve travel to remind them of the requirement and importance of filing internally and externally required accident reports in a timely manner. In addition, enforce vehicle maintenance schedules. (Repeated-2012)**

**Finding:** Auditors noted Department employees did not timely report all accidents involving State/Department vehicles and the Department was not ensuring all personally assigned and pool vehicles were being adequately maintained.

During the engagement period, Department employees were involved in 18 motor vehicle accidents while driving on State business. Auditors noted exceptions concerning four of the 18 (22%) accidents as follows:

- Three of 18 were not reported to the Department's Administrative Services Division of Operational Special Services (OPSS) in accordance with the Department's policy within 48 hours of the accidents, not including weekends and holidays. The accident reports were one to two days late.

- One of 18 accidents was not communicated to the Department of Transportation by the employee.

During testing of maintenance records for 25 vehicles in operation at the Department during the engagement period, auditors noted the following exceptions:

- Tire rotations did not occur for 13 of 25 vehicles as required. Five vehicles exceeded both the 12-month requirement by one to eight months and the mileage requirements by 5,009 to 17,749 miles.

- Oil changes did not occur as required for nine of 25 vehicles.

- Five of 25 vehicles were missing the approval by the driver certifying costs and mileage in one or more monthly Automotive Cost Report/Vehicle Log.

- One of 25 vehicles was reported with the incorrect license plate number on the monthly maintenance log.

Related to the accident reporting exceptions noted in the current engagement, Department personnel stated the accidents not reported within 48 hours were due to oversight and the accident not reported to IDOT was due to an old form with an incorrect address being used. In addition, Department personnel stated the current engagement period vehicle maintenance exceptions were due to oversight and a lack of documentation by DCMS for work completed.

**Updated Response:** Implemented. Fleet Management clerical staff emails drivers concerning maintenance discrepancies when they review the Maintenance Section of the drivers' monthly Automotive Cost Reports that are turned in with the first two weeks of the following month. They also email the drivers reminders when they are close to the mileage or months due for maintenance.

**Accepted or Implemented – continued**

**10. Ensure employee performance evaluations are performed in a timely manner. In addition, maintain accurate and approved overtime and leave records for all employees. (Repeated-2007)**

**<u>Finding</u>:** The Department did not ensure all required processes were followed and required forms and documents were completed and/or retained in the administration of their payroll and timekeeping functions. During testing, auditors noted:

- The Department did not perform employee performance evaluations as required.

  Auditors tested the evaluations required for 40 employees during the engagement period. For these employees, 84 total evaluations should have been performed during the engagement period. Of the 84 evaluations tested, the auditors noted:

  - Thirty-seven annual evaluations were not completed within 30 days of evaluation period end, ranging from 31 to 532 days late.

  - Two probationary evaluations were not signed by the employees within 30 days of evaluation period end, ranging from 395 and 410 days late.

  - Four evaluations were not on file and available for review.

  - One evaluation for FY13 was completed on March 4, 2013, 119 days before the evaluation period ended on June 30, 2013. It was also noted the evaluation period immediately before, July 1, 2011 through June 30, 2012, was signed on the same date as the FY13 evaluation.

  Department personnel stated they were unable to complete the evaluations within 30 days due to the lack of staff and resources required for the Department to prioritize demands.

- Department personnel did not complete required overtime approval forms correctly. The Department paid $685,632 during FY13 and $670,277 during FY14 to employees for overtime. During testing of 40 employees who worked overtime, auditors noted exceptions pertaining to 16 of the 40 employees tested:

  - One or more timesheets were not provided to the auditors for three employees.

  - One or more Overtime Report Forms could not be located for two employees.

  - One Overtime Report Form included actual hours worked but was signed by the employee and supervisor prior to the overtime being worked for one (3%) employee.

  - One or more overtime requests were submitted and/or approved one to seven days after the overtime was worked for 10 (25%) employees.

Department personnel stated requests for overtime did not always include documentation of verbal approval or identify overtime as an emergency due to oversight.

- Auditors noted exceptions in testing the Department's timekeeping records, exceptions were noted for 21 of 40 employees tested, with multiple exceptions regarding some employees.

  - Twelve CTAS reports were signed one to 295 days late by the Timekeeper, Employee and/or Division Manager.

  - Two employees had Employee Leave Requests submitted 15 and 269 days late.
  - One employee had an Employee Leave Request that was missing the signature and date of the Supervisor.

  - Two CTAS reports were missing both the signature and date of the Timekeeper, Employee and/or Division Manager.

  - One CTAS report did not show the proper amount of leave time taken.

  - Three CTAS reports could not be located.

  - One employee signed in on the time sheet 2.5 hours after her shift began and no Request for Leave was submitted.

  - One employee did not properly complete his time sheet. He failed to sign out on one day of the tested pay period.

  Department personnel stated the noted exceptions were due to human error and lack of a Department policy specifying the exact number of days for CTAS reports to be signed and returned to timekeepers.

- In testing various areas, auditors perform procedures to determine the Department's controls over access, physical and computer, as well as over State property are functioning when employees separate from the Department. Auditors made requests to the Department for a listing of employees that had separated from, or were no longer working for, the Department. Auditors received four different reports. After auditor review, each report provided either contained individuals that were still employed by the Department, or omitted individuals known to have separated from the Department. Auditors were able to perform testing by gathering the needed information from all the reports. The Department should be able to efficiently and effectively produce one report of employees separated from the Department.

  Department personnel stated Department staff misunderstood the auditor's requests.

**Accepted or Implemented – continued**

In response to this finding from the previous engagement, the Department stated it would continue to inform managers and supervisors of evaluations due and also remind timekeepers, employees, and managers that all CTAS reports must be signed, as required by timekeeping policy. The Department stated the issues noted by the auditors in the previous engagement were more form over substance. Finally, the Department responded that the new eTime paperless system it was preparing to transition to in FY13 should mitigate the issues noted by the auditors as the records for leave requests and overtime would be paperless, the system would be integrated into CTAS, and all records electronically maintained.

**Updated Response:** Partially implemented. Three of four (75%) of the audit issues have been corrected. An employee has been tasked to follow up with all areas of the Department to monitor overdue evaluations, and is proactively sending out reminders for upcoming performance evaluation due dates. The Department has also been working to ensure that accurate and approved overtime and leave records for all employees are maintained.

**11. Submit a corrected "Agency Workforce Report" for 2012 and 2013. In addition, ensure those preparing the "Agency Workforce Report" understand the definitions of each workforce category according to the interpretation outlined in the State Employment Records Act.**

**Finding:** The Department included inaccurate information in its "Agency Workforce Report" filed for FY12 and FY13.

The "Agency Workforce Reports" filed for FY12 and FY13 incorrectly included all union employees as contractual employees which is not a correct categorization. The Department discovered this error during its preparation of the 2014 "Agency Workforce Report." At the time of concluding the testing of this area, the Department had not submitted amended reports for 2012 and 2013 to the Illinois Office of the Secretary of State or the Governor's Office.

Department management stated former staff of the Department incorrectly interpreted "contractual employee" without consulting the Department's legal division on the proper interpretation. Upon the former staff's departure, the legal division found this mistake while completing the 2014 report and corrected it going forward.

**Updated Response:** Implemented. The corrected 2012 and 2013 "Agency Workforce Reports" were filed in September 2015. The employee now charged with preparing the "Agency Workforce Report" understands all definitions and has filed the Report correctly.

**12. Comply with statutory requirements or seek a legislative remedy as appropriate. Also, devote the resources to ensure the legal reviews and Contract Obligation Document (COD) submissions are performed within the time parameters outlined within the Memorandum of Understanding it has with the IHDA.**

**REVIEW: 4455**

**Finding:** The Department did not comply with various statutory mandates and a Memorandum of Understanding. During testing auditors noted the following:

- The Department did not use updated information and distributed payments from the Tennessee Valley Authority Local Trust Fund based upon the same percentages used in prior years without adjusting for changes in book value in FY13 or FY14, which caused underpayments and overpayments to certain counties.

  Department personnel stated the Tennessee Valley Authority did not send information regarding the book values for each county during FY13 or FY14. These documents were only provided to the Department after the auditor's request.

- Three of 28 International Fuel Tax Agreement (IFTA) payments tested were not certified to the Comptroller by the 15th day of the month, ranging from five to eight days late.

  The Department stated the delays in certification were an oversight.

- The Department's Unified Economic Development Budget (UEDB) submission to the General Assembly and the Department of Commerce and Economic Opportunity (DCEO) was not completed properly. The Department reported the aggregate amount of uncollected or diverted State tax revenues filed during a fiscal year; however, the Department was required to report detailed information for the preceding fiscal year. The Department completed the submission of the report on September 27, 2013 using data for returns filed during FY11. The report due on September 30, 2013 should have used data for returns filed during FY13.

  The Department stated the operational capabilities of the Department, i.e. filing dates, are limited by the timing of when taxpayers file tax returns, and the fiscal year data needed to comply with the statute is not yet available by the due date of the report.

- The Department has a Memorandum of Understanding (MOU) with the Illinois Housing Development Authority (IHDA) which sets forth the requirements for the distribution of funds from the Federal HOME Investment Trust Fund.

  During testing of distributions from the Federal HOME Investment Trust Fund, auditors noted the Department failed to conduct the legal review in a timely manner for nine of 25 payments tested, ranging from three to 37 days late. In addition, the Department failed to timely submit a Contractual Obligation Document (COD) to the Illinois Office of the Comptroller for three of 25 payments tested, ranging from 10 to 51 days late.

  The Department stated the exceptions were due to oversight and lack of staff.

**Updated Response:** Partially implemented. Five of six (83%) of the audit issues have been resolved. The legislative office has drafted language that will enable the Department to comply with the statutory reporting requirements in the Unified Economic Development Budget report. Currently, the required year-end data is not available by the due date of the report. This language will be included in the Department's technical omnibus bill. It will be attached to shell bill SB514. Legal reviews are being performed timely, and Contract Obligation Document (COD) submissions are also filed within the time parameters in the Memorandum of Understanding (MOU) with the Illinois Housing Development Authority (IHDA).

**13. Develop and implement oversight procedures for pull tab and jar game payments in order to identify errors prior to the distributions.**

**Finding:** The Department failed to comply with statutory requirements set forth in the Charitable Games Act and the Pull Tabs and Jar Games Act.

During testing of disbursements from the Illinois Gaming Law Enforcement Fund in FY13, auditors noted the Department issued payments for the correct number of licenses for pull tabs and jar games, but incorrectly used the FY12 rate per license causing a total underpayment of $88,475 to the Illinois Gaming Law Enforcement Fund. In addition, the Department incorrectly used both the FY12 number of and rate per licenses for charitable games causing a net overpayment of $24,702 to the Illinois Gaming Law Enforcement Fund.

In order to correct the FY13 underpayments made for pull tabs and jar games, the Department cancelled incorrect warrants, offset payments and issued supplemental vouchers in FY14 totaling $89,475. In order to correct some of the FY13 overpayments made for charitable games, the Department cancelled incorrect warrants, recovered some amounts from municipalities, and offset distributions/payments in FY14 totaling $5,269. Upon further review of the Department's errors, auditors identified total underpayments of $2,552 and total overpayments of $21,985 still to be recovered by the Department from multiple municipalities, for a net overpayment due to the Department of $19,433.

The Department stated the calculation of distributions is a manual process and the mistakes were the result of human error.

**Updated Response:** Implemented. The distributions and related calculations were incorporated into GenTax on June 28, 2015, and are working well.

**14. Ensure all taxpayer information is properly protected as required by federal and State law. Additionally, implement a security policy and perform a risk assessment to evaluate the computer environment and data that is maintained.**

**Finding:** The Department did not maintain adequate security control over the Information Technology environment.

**REVIEW: 4455**

In order to carry out its mission as "chief tax collector for the State of Illinois", the Department makes significant use of Information Technology, where they maintain confidential and sensitive taxpayer information. During testing, the auditors noted the following issues:

- Inadequate protection over transmitted information.
- Lack of protection over the Department's backups.
- Lack of completing a risk assessment of its computing environment.
- Lack of a security policy.

Department management stated they believed the regularly conducted vulnerability scans performed by the Department of Central Management Services (CMS) on behalf of the Department were adequate.

**Updated Response:** Accepted and partially implemented. One of four (25%) of the audit issues has been corrected. The Department has encrypted all data at rest and at the router end in an effort to protect all taxpayer information. The draft Security Policy continues to be revised, with an estimated date of June 30, 2016 for finalization. CMS has provided a proposed overview of the risk assessment to be conducted by IBM.

## Emergency Purchases

The Illinois Procurement Code (30 ILCS 500/) states, "It is declared to be the policy of the State that the principles of competitive bidding and economical procurement practices shall be applicable to all purchases and contracts...." The law also recognizes that there will be emergency situations when it will be impossible to conduct bidding. It provides a general exemption when there exists a threat to public health or public safety, or when immediate expenditure is necessary for repairs to State property in order to protect against further loss of or damage to State Property, to prevent or minimize serious disruption in critical State services that affect health, safety, or collection of substantial State revenues, or to ensure the integrity of State records; provided, however that the term of the emergency purchase shall not exceed 90 days. A contract may be extended beyond 90 days if the chief procurement officer determines additional time is necessary and that the contract scope and duration are limited to the emergency. Prior to the execution of the extension, the chief procurement officer must hold a public hearing and provide written justification for all emergency contracts. Members of the public may present testimony.

Notice of all emergency procurement shall be provided to the Procurement Policy Board and published in the online electronic Bulletin no later than 3 business days after the contract is awarded. Notice of intent to extend an emergency contract shall be provided to the Procurement Policy Board and published in the online electronic Bulletin at least 14 days before the public hearing.

A chief procurement officer making such emergency purchases is required to file an affidavit with the Procurement Policy Board and the Auditor General. The affidavit is to set forth the circumstance requiring the emergency purchase. The Legislative Audit Commission receives quarterly reports of all emergency purchases from the Office of the Auditor General.

The Legislative Audit Commission is directed to review the purchases and to comment on abuses of the exemption.

The Department filed no affidavits for emergency purchases in FY14, and one affidavit for an emergency purchase in FY13 as follows:

- $36,792.81 for a one-time Threat Assessment Program review of the CMS computer and network environment.

## Headquarters Designations

The State Finance Act requires all State agencies to make semiannual headquarters reports to the Legislative Audit Commission. Each State agency is required to file reports of all its officers and employees for whom official headquarters have been designated at any location other than that at which official duties require them to spend the largest part of their working time.

In July of 2014, the Department indicated that 468 employees spent at least 50% of their time working at locations other than their official headquarters.

## APPENDIX A

## SERVICE EFFORTS AND ACCOMPLISHMENTS

| | FY14 | FY13 |
|---|---|---|
| **Administer State and Local Tax Laws** | | |
| Number of State and local taxes administered | 74 | 73 |
| State and local tax and fee collections | $ 41,493,000,000 | $ 41,009,000,000 |
| Number of tax return documents processed includes alternatively filed methods | 17,833,349 | 18,193,237 |
| Number of individual income tax returns processed | 6,143,408 | 5,946,121 |
| Number of individual income tax refunds issued | 3,738,865 | 3,219,241 |
| Delinquent tax debt cases closed | 615,645 | 400,584 |
| Delinquent tax debt collections | $ 643,346,000 | $ 617,657,000 |
| Number of phone calls answered on toll-free assistance lines | 1,066,474 | 1,057,132 |
| Number of individual income tax returns filed electronically | 4,867,534 | 4,698,563 |
| Percent of individual income tax returns filed electronically | 79.2% | 79% |
| Total tax and fee collections received via electronic fund transfers | $ 34,736,100,000 | 33,364,200,000 |
| | | |
| **Liquor Control Commission** | | |
| Inspections | 16,676 | 16,871 |
| Licenses Issued | 34,973 | 30,399 |
| Liquor inspections compliance rate | 64.0% | 63.3% |

**APPENDIX B**

## Summary of Appropriations and Expenditures

| | FY14 | FY13 | FY12 |
|---|---|---|---|
| **APPROPRIATIONS** | **$ 764,114,700** | **$ 763,562,800** | **$ 933,591,883** |
| **Expenditures by Fund** | | | |
| General Revenue Fund | $ 109,354,284 | $ 108,455,392 | $ 123,329,991 |
| Motor Fuel Tax Fund | 59,497,707 | 61,777,588 | 67,182,640 |
| Underground Storage Tank Fund | 1,758,396 | 1,736,202 | 1,565,624 |
| Illinois Gaming Law Enforcement Fund | 1,645,834 | 1,512,074 | 1,702,014 |
| Home Rule Municipal ROT Fund | 605,593 | 488,241 | 1,106,711 |
| Federal Trust Fund | 145,565 | 155,496 | 88,405 |
| Rental Housing Support Program Fund | 18,863,017 | 10,634,786 | 14,038,399 |
| State and Local Sales Tax Reform Fund | 65,149,816 | 61,823,418 | 51,600,000 |
| RTA Occupation & Use Tax Replacement Fund | 31,536,416 | 30,560,309 | 26,000,000 |
| County Option Motor Fuel Tax Fund | 647,152 | 672,808 | 650,036 |
| Debt Collection Fund | 15,210 | 19,997 | 1,221 |
| Illinois Tax Increment Fund | - | 21,086,744 | 20,857,027 |
| Illinois Affordable Housing Trust Fund | 53,500,172 | 31,132,992 | 22,684,755 |
| Federal HOME Investment Trust Fund | 10,166,912 | 2,591,943 | 31,968,926 |
| Tax Compliance & Administration Fund | 9,633,307 | 9,508,507 | 3,673,858 |
| Predatory Lending Database Program Fund | 845,000 | - | 105,000 |
| Local Government Distributive Fund | 180,727,470 | 177,231,490 | 140,999,548 |
| State Lottery Fund | - | - | 95,699,973 |
| Personal Property Tax Replacement Fund | 52,040,701 | 51,593,062 | 37,793,997 |
| Dram Shop Fund | 7,970,455 | 8,609,130 | 7,007,324 |
| Video Gaming Distribution Fund | 21,316,783 | 3,735,470 | 6,991,295 |
| Foreclosure Prevention Program Fund | 3,432,581 | 2,949,548 | 5,096,940 |
| Sr. Citizen Real Estate Deferred Tax Fund | 5,571,278 | 6,381,468 | - |
| Abandoned Residential Property Relief Fund | 7,372,294 | - | - |
| Build Illinois Bond Fund | - | - | 34,220,000 |
| **TOTAL** | **$ 641,795,943** | **$ 592,656,665** | **$ 694,363,684** |
| **Expenditures by Major Object** | | | |
| Personal services | $ 36,057,008 | $ 104,115,446 | 109,116,406 |
| Retirement, State | 14,559,927 | 12,915,076 | 12,294,242 |
| Social security | 2,605,316 | 7,502,754 | 7,863,510 |
| Group Insurance | 9,353,658 | 10,036,714 | 8,515,456 |
| Contractual services | 3,138,199 | 9,196,523 | 8,213,526 |
| Travel | 1,459,711 | 2,825,182 | 2,471,253 |
| Commodities | 66,619 | 675,121 | 611,333 |
| Printing | 141,710 | 442,501 | 462,275 |
| Equipment | - | 54,412 | 38,931 |
| EDP | 13,948,744 | 31,098,090 | 38,314,860 |
| Telecommunications | 1,492,231 | 2,522,611 | 2,272,099 |
| Operate auto equipment | 106,106 | 122,201 | 332,300 |
| Shared Services | 2,656,849 | 2,937,022 | 2,774,313 |
| Administration of certain programs | 17,259,307 | 16,729,597 | 38,157,300 |
| Lump sum | 1,397,383 | - | 41,211,295 |
| Awards & Grants | 384,691,680 | 356,154,367 | 304,703,188 |
| Refunds | 22,224,390 | 28,593,578 | 26,395,864 |
| Operations | 103,749,044 | 3,000,000 | - |
| Senior Citizen Deferred Tax Revolving Fund | 5,571,278 | 3,735,470 | - |
| Video Gaming Act | 21,316,783 | - | - |
| Governor's Discretionary appropriation | - | - | - |
| Lottery, Development Board, Prizes | - | - | 90,615,233 |
| **Total Expenditures** | **$ 641,795,943** | **$ 592,656,665** | **$ 694,363,384** |

**REVIEW: 4455**
**DEPARTMENT OF REVENUE**
**TWO YEARS ENDED JUNE 30, 2014**

**APPENDIX C**

## Summary of Cash Receipts

| | FY14 | FY13 | FY12 |
|---|---|---|---|
| **Receipts** | | | |
| Income Tax and fee collections | $ 23,473,570,973 | $ 23,490,696,383 | $ 21,180,192,738 |
| Sales: | | | |
| State, municipal, county, county water commission, RTA, MED, retailers' & service occupation use | 13,402,872,832 | 12,808,943,938 | 12,611,399,786 |
| Public utilities: | | | |
| Message, gas revenue, electric | 1,642,262,559 | 1,723,599,817 | 1,749,940,343 |
| Motor fuel | 1,225,728,873 | 1,191,781,262 | 1,222,013,645 |
| Other: | | | |
| Underground storage tanks | 70,810,482 | 68,703,436 | 69,588,533 |
| Cigarette & cigarette use | 878,774,759 | 850,382,469 | 608,997,557 |
| Racing privilege | 6,529,997 | 6,023,137 | 7,231,927 |
| Hotel operator & occupation | 343,097,412 | 329,945,219 | 309,311,789 |
| Liquor | 279,764,944 | 279,955,470 | 279,232,201 |
| Vehicle Use | 33,875,940 | 32,575,417 | 33,740,576 |
| Real estate transfer | 76,307,001 | 72,665,352 | 59,448,800 |
| Bingo | 1,878,804 | 2,029,347 | 2,134,821 |
| Coin operated amusement device | 1,162,755 | 1,472,943 | 1,740,379 |
| Automobile renting tax | 75,920,784 | 72,877,114 | 68,962,440 |
| Charitable games | 389,014 | 401,617 | 469,222 |
| Pull tabs & jar games | 4,159,931 | 4,954,491 | 4,591,451 |
| Solid Waste | 16,124 | 54,937 | 68,175 |
| Lottery | - | - | 318,030,827 |
| Liquor Control Commission | 15,311,162 | 14,388,888 | 13,689,493 |
| Senior citizens real estate tax deferral | 5,991,861 | 6,074,385 | 5,856,739 |
| Live adult entertainment | 405,997 | - | - |
| Miscellaneous collections | 1,220,095 | 3,451,367 | 3,690,490 |
| **Total Cash Receipts** | **$ 41,540,052,299** | **$ 40,960,976,989** | **$ 38,550,331,932** |

**APPENDIX D**

## Summary of Taxes Receivable Balances

| | At June 30 | |
|---|---|---|
| | **FY14** | **FY13** |
| Taxes receivable | | |
| Income | $ 1,276,085,000 | $ 1,185,543,000 |
| Sales | 606,853,000 | 675,830,000 |
| Motor Fuel | - | - |
| Public utility | 11,108,000 | 14,918,000 |
| Other | 22,369,000 | 51,075,000 |
| Total taxes receivable | 1,916,415,000 | 1,927,366,000 |
| Less allowance for uncollectible taxes | (704,960,000) | (761,164,000) |
| Taxes receivable, net | **$ 1,211,455,000** | **$ 1,166,202,000** |

# REVIEW: 4455
# DEPARTMENT OF REVENUE
# TWO YEARS ENDED JUNE 30, 2014

**APPENDIX E**

## Changes in State Property

| | FY14 | FY13 |
|---|---|---|
| **Beginning Balance** | **$ 12,501,377** | **$ 13,026,705** |
| Total Additions | 207,507 | 161,713 |
| Total Deductions | 46,190 | (87,037) |
| Net Transfers | (864,063) | (600,004) |
| **Ending Balance** | **$ 11,891,011** | **$ 12,501,377** |