

STATE OF CONNECTICUT

**AUDITORS' REPORT
DEPARTMENT OF REVENUE SERVICES
FOR THE FISCAL YEAR ENDED JUNE 30, 2000**

**AUDITORS OF PUBLIC ACCOUNTS
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July 24, 2002

**AUDITORS' REPORT
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FOR THE FISCAL YEAR ENDED JUNE 30, 2000**

We have examined the financial records of the Department of Revenue Services for the fiscal year ended June 30, 2000.

Financial statements pertaining to the operations and activities of the Department of Revenue Services for the fiscal year ended June 30, 2000, are presented and audited on a Statewide Single Audit basis to include all State agencies and funds. This audit examination has been limited to assessing compliance with several provisions of financial related laws, regulations and contracts, and evaluating internal control structure policies and procedures established to ensure such compliance.

This report on that examination consists of the Comments, Condition of Records, Recommendations and Certification which follow:

COMMENTS

FOREWORD:

The Department of Revenue Services operates principally under provisions of Title 12 (Taxation), Chapters 201, 202 and 207 - 229, of the General Statutes. The Department is responsible for administering and ensuring compliance with applicable provisions of this Title and certain other statutes related to the assessment and collection of taxes. Major functions of the Department include collecting and processing tax revenues, developing tax regulations and providing information and services to taxpayers.

Records pertaining to sales taxes collected by the Department of Motor Vehicles but credited to the Department of Revenue Services are examined as part of our audit examination of the Department of Motor Vehicles.

Section 12-1a of the General Statutes provides that the Department is under the direction of a Commissioner of Revenue Services. Gene Gavin served as Commissioner through the audited period. Fred H. Lovegrove, Jr. served as Deputy Commissioner through the audited period.

Legislative Changes:

Notable legislative changes, which took effect during the audited period, are presented below:

- **Public Act 99-48** – Section 1 of the Act amended Section 12-39aa of the General Statutes to allow taxpayers to file returns using certain designated private delivery services, in addition to the United States Postal Service, with the assurance that a return mailed on time will be considered filed on time. This Act which is effective May 27, 1999, is applicable to returns filed on or after October 1, 1999.
- **Public Act 99-109** – Sections 1 and 2 amended Section 12-302 and 12-303 of the General Statutes respectively, by prohibiting distributors and dealers from the stamping and sale of gray market cigarettes; which are cigarettes manufactured for export only, but sold domestically, effective July 1, 1999.
- **Public Act 99-173** – Sections 3 and 4 provide a \$50 sales tax rebate to individuals (\$100 to married couples filing jointly). This Act is effective from its passage, June 23, 1999.
- **Public Act 99-173** – Section 21 amends Section 12-412 subdivision (60) of the General Statutes to extend Sales & Use Tax exemption to vessels purchased by non residents who will not register vessels within the State. This Act is effective from its passage, June 23, 1999 and applicable to sales occurring on or after July 1, 1999.
- **Public Act 99-173** – Section 27 amends Section 12-412 subdivisions (101),(102) and (105) of the General Statutes to extend Sales & Use Tax exemptions to sales of firearm safety devices, bicycle helmets, and shoe repair services. This Act is effective from its passage, June 23, 1999 and applicable to sales occurring on or after July 1, 1999.
- **Public Act 99-173** – Section 39 amends Section 12-217 subsection (a) of the General Statutes to allow businesses a deduction from gross income for the capital gain realized on the sale of land to the State, a political subdivision of the State, or any non-profit land conservation organization, if the land is to be permanently preserved as protected open space. This Act is applicable to income years commencing on or after January 1, 1999 and is effective from its passage, June 23, 1999.
- **Public Act 00-170** – Section 9 amends Section 12-263b of the General Statutes by repealing the Hospital Gross Earnings Tax for calendar quarters commencing April 1 2000, effective May 26, 2000.

RÉSUMÉ OF OPERATIONS:

General Fund Revenues and Receipts:

General Fund tax revenues, license fees and all other revenues and non-revenue receipts totaled \$8,325,337,561 during the 1999-2000 fiscal year. General Fund tax revenue included in those amounts, recorded on the accrual basis, totaled \$8,992,373,561. Revenues other than taxes included payments for licenses to collect sales and use tax and to sell cigarettes and tobacco products, serving fees and costs related to tax warrants, expenditure refunds and Federal funding.

General Fund tax refunds, budgeted as reductions of tax revenues, were \$831,960,203, for the 1999-2000 fiscal year, and were paid from miscellaneous appropriations administered by the Department. Non-tax refunds totalled \$11,568 during the same period. As noted above, Public Act 99-173 established a “sales tax rebate” program. Of the amount presented as tax refunds, \$115,612,725 represented amounts appropriated for sales tax rebate checks. During the prior fiscal year, \$75,352,767 was appropriated for a rebate program.

A summary of tax revenues, net of refunds, compared to the previous fiscal year, is presented below:

(Millions)	<u>1999-2000</u>	<u>1998 – 1999</u>
Personal income	\$ 3,641	\$ 3,317
Sales and use	3,083	2,922
Corporations	405	451
Succession taxes	238	250
Public service companies	203	198
Insurance companies	147	147
Hospital gross earnings	68	126
Cigarettes/tobacco	121	122
Petroleum companies	62	33
Real estate/controlling interest	114	106
Alcoholic beverages	41	40
All other taxes	<u>36</u>	<u>37</u>
Total	<u>\$ 8,159</u>	<u>\$ 7,749</u>

As presented by the above analysis, net General Fund tax revenues increased by 5.3 percent over the preceding fiscal year. This increase was primarily due to rises in sales and use, and income tax receipts offset in part by decreases in corporate and hospital gross earnings tax receipts. Revenues from sales and use, and income tax receipts accounted for approximately 82.4 percent of tax revenues in total.

General Fund Expenditures:

A summary of General Fund expenditures from Department appropriations, compared to the previous fiscal year, is presented below:

	<u>1999-2000</u>	<u>1998-1999</u>
Personal services	\$ 45,137,532	\$ 42,383,713
Contractual services	9,465,416	8,576,597
Commodities	799,344	1,059,895
Sundry charges	57,536	100,116
Total Operating Accounts	<u>55,459,828</u>	<u>52,120,321</u>
Tax Refunds	831,971,772	720,344,225
Other Refunds		8,312
Total Budgeted Accounts	<u>887,431,600</u>	<u>772,472,858</u>
Restricted Appropriations	<u>316,869</u>	<u>170,669</u>
Totals	<u>\$887,748,469</u>	<u>\$772,643,527</u>

As presented above, operating expenditures remained fairly constant through the audited period. The increase in tax refunds was primarily attributable to income tax refunds, with a portion of that increase being due to sales tax rebates, as explained above.

The number of filled Department positions increased during the audited period, from an average of 883 for the 1998-1999 fiscal year to 910 for the 1999-2000 fiscal year. A summary of those averages is presented below.

	<u>1999-2000</u>	<u>1998-1999</u>
Full-time	811	803
Part-time or intermittent	25	16
Temporary or durational	<u>74</u>	<u>64</u>
Total	<u>910</u>	<u>883</u>

Special Transportation Fund:

In accordance with provisions of Section 13b-61 of the General Statutes, motor fuel taxes and related fees collected by the Department pursuant to Chapters 221 and 222 of the General Statutes were deposited to the Special Transportation Fund.

Special Transportation Fund tax revenues for the Department, recorded on an accrual basis, totaled \$531,445,928 during the 1999-2000 fiscal year. Motor carrier registration fees totaled \$310,158 during that same period.

Special Transportation Fund tax refunds, budgeted as reductions of tax revenues, totaled \$5,397,676 for the 1999-2000 fiscal year, and were paid from a miscellaneous appropriation administered by the Department.

A summary of tax revenues, net of refunds, for the audited period is presented below:

(Millions)	<u>1999-2000</u>	<u>1998-1999</u>
Motor fuel tax	\$ 447	\$ 444
Special motor fuel tax	44	42
Petroleum Companies	27	15
Motor carrier tax	8	8
Total	<u>\$ 526</u>	<u>\$ 509</u>

As presented by the analysis, net Special Transportation Fund tax revenues, which totaled approximately \$509,000,000 during the 1998-1999 fiscal year, increased slightly during the 1999-2000 fiscal year. The increase was primarily due to the increase in revenue generated by companies distributing petroleum products in Connecticut.

Pending Receipts Fund:

During the audited year, the Department conducted financial activity in an account of the State's Pending Receipts Fund. Receipts deposited to this account totaled \$24,013,613 during the fiscal year. Receipts included transfers from the General Fund of room occupancy sales taxes payable pursuant to Section 32-305 of the General Statutes, security bonds required from taxpayers, and collection of New York State sales taxes pursuant to a reciprocal enforcement agreement with New York.

Disbursements totaled \$23,395,557 during the audited fiscal year. These amounts were disbursed to the appropriate recipients of the activities described above.

Audit Assessments:

Audits were conducted by examiners within the Audit Division to ensure taxpayer compliance, as regards the filing of returns and the remitting of tax payments. Assessments were generated as a result of both office and field audit efforts. Based upon statistics provided by the Audit Division, assessments totaled \$307,647,483, for the fiscal year ended June 30, 2000. A summary of assessments by tax type for the audited year compared to the previous fiscal year, as provided by the Audit Division, is presented below:

(Millions)	<u>1999-2000</u>	<u>1998 – 1999</u>
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Auditors of Public Accounts

Corporation	\$ 100.7	\$ 89.0
Sales and use	110.1	94.2
Personal	59.6	48.3
Excise	3.9	5.1
Public service	32.4	40.9
Admissions, cabaret and dues	.9	.7
Total	<u>\$ 307.6</u>	<u>\$ 278.2</u>

Appellate Division:

The Department's Appellate Division administered appeals from taxpayers disputing audit assessments. Following written protests, hearings with taxpayers are held. Based upon information presented, appellate decisions are made concerning the validity of assessments. Further appeal is available to a taxpayer by means of litigation.

Appellate Division activity reports, reflecting resolution activity during the audited fiscal year, as compared to the prior fiscal year, is presented below. Revisions resulted from both court and Appellate Division decisions.

	<u>1999-2000</u>	<u>1998-1999</u>
Cases resolved	1217	1074
Original assessments	\$ 79,869,584	\$ 106,348,102
Revised assessments	<u>36,148,911</u>	<u>54,950,384</u>
Assessment reductions	<u>\$ 43,720,673</u>	<u>\$ 51,397,718</u>
Percentage reduction	54 %	48 %

Accounts Receivable:

Accounts receivable of the Department emanate from various sources, including audit assessments, delinquency assessments, penalty and interest charges, and returns filed without remittances or filed with an underpayment of tax liability. A summary of accounts receivable as of June 30, 2000, as compared to the prior fiscal year end, is presented below.

	<u>June 30, 2000</u>	<u>June 30, 1999</u>
Business and miscellaneous taxes	\$ 230,695,027	\$ 218,503,330
Income tax	120,125,073	86,450,608
Inheritance tax	<u>4,449,683</u>	<u>5,540,590</u>
Total	\$ 355,269,783	\$ 310,494,528
Provisions for uncollectable	<u>(146,022,612)</u>	<u>(103,758,021)</u>
Net accounts receivable	<u>\$ 209,247,171</u>	<u>\$ 206,736,507</u>

It should be noted that some of the receivable amounts presented above include amounts received and presented within our analysis of receipts, but for which related tax returns had not been filed, at fiscal years' end. The receivable balances presented reflect reductions for payments that were made on account by taxpayers to avoid the continued accrual of interest on assessments under protest. The amounts of such payments on account were \$29,750,863 and \$36,674,197 at June 30, 1999 and 2000, respectively. Additionally, agency records presented credits due taxpayers (refunds payable or deferred revenues) in the amount of \$31,890,944 and \$63,631,033 at June 30, 1999 and 2000, respectively. The provision for the amounts deemed uncollectable is based on estimates of appellate and court reductions, abatements and other cancellations.

Penalty Waivers:

Provisions of certain statutes impose penalties for failure to satisfy taxes due within specified times. The Commissioner of Revenue Services is authorized to waive penalties, subject to the provisions of Section 12-3a of the General Statutes, in cases where the failure to pay the tax was due to reasonable cause and was not intentional or due to neglect. Section 12-3a requires approval of a Tax Review Committee, comprised of the Commissioner of Revenue Services, the Secretary of the Office of Policy and Management and the State Comptroller, for all penalty waivers over \$500.

A summary of penalty waiver activity during the audited fiscal year, as compared to the prior fiscal year, as provided by the Department, follows:

	<u>Waiver Requests</u>		<u>Rejected Waivers</u>		<u>Approved Waivers</u>	
	<u>Cases</u>	<u>Penalties</u>	<u>Cases</u>	<u>Penalties</u>	<u>Cases</u>	<u>Penalties</u>
1998-1999	9,511	\$3,657,766	1,147	\$1,432,458	8,364	\$2,225,308
1999-2000	8,538	\$3,055,481	1,423	\$1,481,525	7,115	\$1,573,956

Collections and Enforcement Division:

The Collections and Enforcement Division is comprised of revenue agents who pursue collections through direct contact with taxpayers, field agents who issue tax warrants to delinquent taxpayers, hearing officers who provide an initial hearing process for delinquent taxpayers and enforcement agents who investigate cases involving tax evasion. Records of the Collections and Enforcement Division presented revenues collected by the Division to be \$124,334,525 during the fiscal year.

The Division, as provided by Section 12-39 of the General Statutes, is also responsible for the identification of accounts subject to abatement. The Commissioner, upon the approval of an Abatement Review Committee, may abate any tax payable to the State which has been present on its suspense tax book for seven years and determined to be uncollectible. During the audited period, there were no abatements executed under this Section.

It is a practice of the Department to remove from its active accounts receivable file, accounts considered to be uncollectible but which have yet to be included on abatement approval requests. This is due to the statutorily required seven year waiting period. During the 1999-2000 fiscal year, accounts totaling \$16,142,380 were referred to this status.

The Department also utilizes a separate suspense tax status to identify accounts receivable deemed to be temporarily uncollectible. Transfers to this status totaled \$2,467,793 during the fiscal year. The majority of accounts receivable placed in this status involve circumstances where liens or pending litigation have been pursued, which would indicate that collection at a future time may be possible.

CONDITION OF RECORDS

Inadequate Controls Over Receipts

Criteria: Receipts should be deposited in a timely manner in accordance with Section 4-32 of the General Statutes. Section 4-32 of the General Statutes generally requires that any State agency receiving any money or revenues for the State amounting to more than \$500 shall deposit such receipts in depositories designated by the State Treasurer within 24 hours of receipt. The State Treasurer waives this requirement in certain specified instances. The State Comptroller provides for the use of pending receipts in cases where monies are received by State agencies and held in suspense until the final disposition is determined.

Condition: Our test of 24 checks totaling \$98,920 disclosed that ten checks totaling \$24,220 were deposited at least one business day late, five checks totaling \$64,249 were deposited at least three business days late, four checks totaling \$3,743 were deposited at least four business days late, one check in the amount of \$612 was deposited at least nine business days late and two checks totaling \$4,834 were deposited at least 11 business days late. The checks were all located in open bins in the processing unit. They were not secured at night. In all, 22 of 24 checks sampled were deposited between one and 11 days late.

This matter was reported by us to the Governor and other State Officials in a letter dated September 26, 2001.

Effect: Revenues may not be deposited in the Agency's bank account in a timely manner. Delays in deposit result in a loss of revenue to the State. Checks left in an unsecured area may be lost.

Cause: The Department of Revenue Services opens and sorts incoming payments and returns. Priority is given to the remittances that are complete and in agreement with the return filed. In an effort to deposit as much as possible as quickly as possible, these returns are processed first. The returns that present an exception are set aside in the various exception baskets. The exception work is not given priority. When time permits, the exception work is reviewed and the remittance forwarded to the deposit unit when the problem is resolved. The checks remain with the correspondence pertaining to the payment until the problem is resolved. The Pending Receipts Fund is not routinely utilized for exception work.

In addition, the checks associated with the "clean" returns may not

be deposited within the 24 hours allowed. Due to the cost associated with data entry the Agency accumulates checks until they have enough to complete a batch. On Wednesday and Friday mornings the Agency gathers all checks that have not yet been deposited and deposits them. The accumulation of checks in this manner may result in a check not being deposited in a timely manner.

Recommendation: The Department should improve its internal control over receipts and implement procedures to ensure receipts are deposited promptly in compliance with statutory requirements. (See Recommendation 1.)

Agency Response: “We agree with this finding in part. The Auditors of Public Accounts specifically cited 22 checks deposited between one and eleven days late. Of the more than five million tax returns processed every year through Department of Revenue Service (DRS), the twenty-two late deposits in question were identified by DRS staff as “exception returns” upon receipt. An “exception return” is one which requires research, and in most cases, communications with the individual taxpayer to resolve an issue before processing. To meet peak tax season processing demands, DRS established business rules to prevent exception returns from becoming a bottleneck to the entire system.

Additionally, the Office of the Treasurer has granted a waiver to DRS for certain returns, including exception returns, under Section 4-32 of the Connecticut General Statutes, which would otherwise require that deposits be made within 24 hours of receipt. Of the 22 incidents cited by the Auditors, our records indicate that four of these deposits do not conform to the waiver granted by the Office of the Treasurer. DRS Operation Division staff have been reminded to comply with established business rules.”

Auditors’ Concluding Comment:

Our receipt test of 24 checks was not performed on peak tax season receipts and does not meet the requirements of the deposit waiver granted by the State Treasurer. The Department did not utilize the Pending Receipts Fund for the receipts tested and does not routinely utilize the Pending Receipts Fund for exception work.

Collection and Reporting of Revenue

Criteria: Section 12-719 of the General Statutes requires a person to make and file a tax return and pay any tax due thereon on or before the date fixed for filing such return.

Receipts received by certified mail should be accounted for and deposited to the accounts of the State of Connecticut as required by Section 4-32 of the General Statutes.

Condition: Tax returns and tax payments that were sent by certified mail during April 2000 were not received by the Department of Revenue Services in a timely manner. A problem with the processing of certified mail by the United States Postal Service (USPS) caused 46,270 pieces of mail to be delivered late. An employee of the Department of Revenue Services (DRS) noticed a problem with the mail service. A representative of the USPS acknowledged the problem. The Department subsequently received the mail, over a four day period. Department employees noted that the majority of the mail was postmarked prior to the due date for a personal return (April 18, 2000).

Revenue information used in the State budget process was underestimated due to the lack of inclusion of tax payments sent by certified mail.

Effect: Receipts were not received in a timely manner. The State budget was approved based on inaccurate underestimated information.

Cause: The United States Postal Service was not able to handle the volume of mail addressed to DRS. A representative of the USPS located bags of unprocessed mail addressed to DRS on the floor of the Post Office in Hartford.

Conclusion: The Department of Revenue Services has employed additional procedures including frequent visits to the Post Office to better monitor Department mail delivery and improve revenue accountability. Tax returns and tax payments that were sent by certified mail during April 2001 were received by the Department of Revenue Services in a timely manner.

Procurement Process – Personal Service Agreements:

Criteria: Section 4-98 of the General Statutes states that no State agency shall incur an obligation of State funds without properly executing a valid commitment document.

Section 4-213 of the General Statutes states that no State agency may hire a personal service contractor without executing a personal service agreement.

Condition: Our review of DRS General Fund expenditures noted seven transactions totalling \$6,210,104 in which data processing consulting services were committed by a purchase order instead of a personal service agreement as required.

Effect: The use of a purchase order (instead of a personal service agreement) to engage personal service contractors circumvents statutory approval processes within the Offices of Policy and Management and the Attorney General, and does not necessarily afford the desired level of assurance that all terms included in the Statement of Work are part of the purchase agreement.

Cause: The policy in place regarding data processing consultants is contrary to Section 4-213 of the General Statutes.

Recommendation: The Department should improve controls over the procurement process to insure that all statutory requirements pertaining to personal service agreements are adhered to. (See Recommendation 2.)

Agency Response: “We agree with this finding in part. The Department of Revenue Service (DRS) used a purchase order to engage data processing consultants. However, these contracts were all associated with the Department of Revenue Service (DRS) Y2K remediation effort. The DRS utilized the procurement process dictated by the Department of Information Technology (DOIT) Y2K office, following the DOIT policies and procedures for data processing consultant services.”

Auditors’ Concluding Comment: Although we acknowledge that DRS utilized the procurement process dictated by the Department of Information Technology (DOIT), we note that the process is inconsistent with statutory provisions and was not necessarily in the best interests of the State. It is DRS that is held responsible for adherence to applicable General Statutes when expending their appropriated funds.

Payment Process – Duplicate Payment:

Criteria: The State Accounting Manual mandates accounting and preparatory requirements that must be met by State Agencies. The Manual requires that payments to vendors be made from an original vendor invoice. The invoice should be properly authorized and the receipt of goods verified. In addition, the Manual also details how commitment documents for leases should be completed, specifically, that the lease indicator is a required

element.

Condition: A payment was processed from a contract instead of an original vendor invoice. The payment resulted in a duplicate payment to the vendor.

A purchase order completed for the long-term lease of equipment did not have the “lease type” entered in the appropriate space. A further review of related lease documents revealed that 33 documents did not have the “lease type” entered.

Effect: The processing of a payment from a document other than an original vendor invoice resulted in a duplicate payment to the vendor.

The completion of the lease indicator is crucial for the generation of accurate reports that are integral to annual financial reports.

Cause: The duplicate payment was the result of a payment being made from a contract instead of from a properly authorized original vendor invoice.

We were not able to determine why the lease indicator was not entered.

Recommendation: The Department should improve controls over the payment process to insure that commitments and expenditures are processed in accordance with established requirements. (See Recommendation 3.)

Agency Response: “We agree with this finding. The Auditors of Public Accounts (APA) are correct in their findings that the copier lease they examined did not have a character in the appropriate space. The character that should have been entered in this field is "O", as this lease was a non-capital lease. The Business Office incorrectly prepared this and subsequent copier lease purchase orders. It has now added the proper "O" designation on all 33 documents and will continue to do so in the future.

The duplicate payment occurred as a result of payment being made from a Contract Confirmation statement rather than an invoice - both of which are very similar in appearance. This incident was previously documented in detail to the Comptrollers Office in June of 2000. A review of the monthly Comptrollers post audit results will indicate that this is an isolated incident.”

Matching of Tax Information

- Criteria:* Section 12-707 of the General Statutes states that each employer required to deduct and withhold tax shall be liable for such tax and shall file a withholding return.
- Section 12-732 of the General Statutes states that if any tax has been overpaid, the taxpayer may file a claim for refund in writing with the Commissioner.
- The State Accounting Manual states that when a General Fund item must be refunded it is not recorded as a reduction of revenue but as an expenditure.
- Good internal controls require that claims presented for payment be supported by adequate documentation and verified for accuracy.
- The W-2 wage and tax statement reports tax filer income information and the corresponding amount of tax withheld, if any. W-2 statements are attached to the filers' tax return by the filer.
- Condition:* The withholding information submitted with personal income tax returns is not being verified for accuracy and checked to other sources by the Department prior to the issuance of tax refunds.
- Effect:* Tax refund payments are generated prior to tax withholding comparison and matching procedures. The State of Connecticut may not be adequately protected against error or possible fraud.
- Cause:* The Department does not have a procedure or program in place that compares and matches amounts reported as withheld on an employer's record to that reported by the employee as withheld on the W-2 statement filed with the employee's tax return.
- Recommendation:* The Department of Revenue Services should develop and implement additional procedures to examine and verify personal income tax information supporting tax withheld prior to the issuance of tax refund payments. (See Recommendation 4.)
- Agency Response:* "We disagree with this finding. The Department of Revenue Service (DRS) has in place many inspection procedures to ensure that returns are accurately filed. Tax returns and W-2s are reconciled when filed. The inspection procedures continue to be refined based upon our own experiences, and the exchange of information between other States and other State Agencies. The DRS has additional security measures in place that have proven

effective in monitoring fraud. This includes a “backend process” to validate discrepancies. Furthermore, a new training program was provided to staff this past year.

Based upon the security procedures in place and results of a prior internal study on this very issue, the DRS is confident that the State of Connecticut is adequately protected against fraud.

The DRS along with several other states is actively participating in the development of a new Federal program that we anticipate will provide an additional source of information for the DRS to utilize.

As explained to the Auditors of Public Accounts, no State can afford to capture this information and reconcile on the front-end of the process, due to the time and monetary constraints. The current cost to data capture this information is in excess of \$2,000,000 annually. However, the DRS will consider a budget option for this in the future.”

*Auditors’ Concluding
Comment:*

Although the DRS performs procedures to reconcile filer tax returns and filer W-2 statements, procedures are not performed to reconcile the filer W-2 statement that accompanies the filer’s tax return to employer records, prior to the issuance of tax refund payments. Inaccurate W-2 statement information due to error or fraud may go undetected.

RECOMMENDATIONS

Our prior report on the fiscal year ended June 30, 1999, contained no recommendations.

Current Audit Recommendations:

1. **The Department of Revenue Services should improve its internal control over receipts and implement procedures to ensure receipts are deposited promptly in compliance with statutory requirements.**

Comment:

Our examination of the DRS receipts revealed that receipts over \$500 were held in excess of 24 hours, for periods ranging from one day to 11 business days. Such delays reduce the opportunity for the State Treasurer to invest idle money.

This matter was reported by us to the Governor and others in a letter dated September 26, 2001.

2. **The Department of Revenue Services should improve controls over the procurement process to insure that all statutory requirements pertaining to personal service agreements are adhered to.**

Comment:

Consulting services were engaged by way of a purchase order rather than a personal service agreement as required by Section 4-213 of the General Statutes.

3. **The Department of Revenue Services should improve controls over the payment process to insure that commitments and expenditures are processed in accordance with established requirements.**

Comment:

A duplicate payment to a vendor resulted when a payment was made from a contract instead of an original vendor invoice.

4. **The Department of Revenue Services should develop and implement additional procedures to examine and verify personal income tax information supporting tax withheld prior to the issuance of tax refund payments.**

Comment:

Tax refund payments are issued prior to confirmation that claims presented for payment are supported by documentation that has been verified for accuracy.

INDEPENDENT AUDITORS' CERTIFICATION

As required by Section 2-90 of the General Statutes we have audited the books and accounts of the Department of Revenue Services for the fiscal year ended June 30, 2000. This audit was primarily limited to performing tests of the Agency's compliance with certain provisions of laws, regulations, contracts and grants, and to understanding and evaluating the effectiveness of the Agency's internal control policies and procedures for ensuring that (1) the provisions of certain laws, regulations, contracts and grants applicable to the Agency are complied with, (2) the financial transactions of the Agency are properly recorded, processed, summarized and reported on consistent with management's authorization, and (3) the assets of the Agency are safeguarded against loss or unauthorized use. The financial statement audit of the Department of Revenue Services for the fiscal year ended June 30, 2000, is included as a part of our Statewide Single Audit of the State of Connecticut for that fiscal year.

We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial-related audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Department of Revenue Services complied in all material or significant respects with the provisions of certain laws, regulations, contracts and grants and to obtain a sufficient understanding of the internal control to plan the audit and determine the nature, timing and extent of tests to be performed during the conduct of the audit.

Compliance:

Compliance with the requirements of laws, regulations, contracts and grants applicable to the Department of Revenue Services is the responsibility of the Department of Revenue Services' management.

As part of obtaining reasonable assurance about whether the Agency complied with laws, regulations, contracts, and grants, noncompliance with which could result in significant unauthorized, illegal, irregular or unsafe transactions or could have a direct and material effect on the results of the Agency's financial operations for the fiscal year ended June 30, 2000, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants. However, providing an opinion on compliance with these provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*. However, we noted certain immaterial or less than significant instances of noncompliance, which are described in the accompanying "Condition of Records" and "Recommendations" sections of this report.

Internal Control over Financial Operations, Safeguarding of Assets and Compliance:

The management of the Department of Revenue Services is responsible for establishing and maintaining effective internal control over its financial operations, safeguarding of assets, and compliance with the requirements of laws, regulations, contracts and grants applicable to the Agency. In planning and performing our audit, we considered the Agency's internal control over its financial operations, safeguarding of assets, and compliance with requirements that could have a material or significant effect on the Agency's financial operations in order to determine our auditing procedures for the purpose of evaluating the Department of Revenue Services' financial operations, safeguarding of assets, and compliance with certain provisions of laws, regulations, contracts and grants, and not to provide assurance on the internal control over those control objectives.

However, we noted certain matters involving the internal control over the Agency's financial operations, safeguarding of assets, and/or compliance that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control over the Agency's financial operations, safeguarding of assets, and/or compliance that, in our judgment, could adversely affect the Agency's ability to properly record, process, summarize and report financial data consistent with management's authorization, safeguard assets, and/or comply with certain provisions of laws, regulations, contracts, and grants. We believe the following finding represents a reportable condition: the issuance of tax refund payments prior to confirmation that claims presented for payment are supported by documentation that has been verified for accuracy.

A material or significant weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with certain provisions of laws, regulations, contracts, and grants or the requirements to safeguard assets that would be material in relation to the Agency's financial operations or noncompliance which could result in significant unauthorized, illegal, irregular or unsafe transactions to the Agency being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over the Agency's financial operations and over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material or significant weaknesses. However, we believe that the reportable condition described above is not a material or significant weakness.

We also noted other matters involving internal control over the Agency's financial operations and over compliance which are described in the accompanying "Condition of Records" and "Recommendations" sections of this report.

This report is intended for the information of the Governor, the State Comptroller, the Appropriations Committee of the General Assembly and the Legislative Committee on Program Review and Investigations. However, this report is a matter of public record and its distribution is not limited.

CONCLUSION

We wish to express our appreciation for the cooperation and courtesies extended to our representatives by the officials and staff of the Department of Revenues Services during the course of our examination.

Josepha M. Brusznicki
Principal Auditor

Approved:

Kevin P. Johnston
Auditor of Public Accounts

Robert G. Jaekle
Auditor of Public Accounts

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