STATE OF LOUISIANA

Department of Revenue
State of Louisiana
Baton Rouge, Louisiana

February 18, 2004

LEGISLATIVE AUDITOR

DIRECTOR OF FINANCIAL AND COMPLIANCE AUDIT

Albert J. Robinson, Jr., CPA

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DEPARTMENT OF REVENUE
STATE OF LOUISIANA
Baton Rouge, Louisiana

Management Letter
Dated February 9, 2004

Under the provisions of state law, this report is a public document. A copy of this report has been submitted to the Governor, to the Attorney General, and to other public officials as required by state law. A copy of this report has been made available for public inspection at the Baton Rouge office of the Legislative Auditor.

February 18, 2004

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February 9, 2004

DEPARTMENT OF REVENUE
STATE OF LOUISIANA
Baton Rouge, Louisiana

As part of our audit of the State of Louisiana's financial statements for the year ended June 30, 2003, we considered the Department of Revenue's internal control over financial reporting; we examined evidence supporting certain accounts and balances material to the State of Louisiana's financial statements; and we tested the department's compliance with laws and regulations that could have a direct and material effect on the State of Louisiana's financial statements as required by *Government Auditing Standards*.

The Annual Fiscal Report of the Department of Revenue is not audited or reviewed by us, and, accordingly, we do not express an opinion on that report. The department's accounts are an integral part of the State of Louisiana's financial statements, upon which the Louisiana Legislative Auditor expresses opinions.

In our prior management letter on the Department of Revenue for the year ended June 30, 2002, we reported 12 findings. The current year status of these findings is listed below.

Resolved by Management:

- Lack of Support for Receivables
- No Enforcement of Electronic Funds Transfer for Certain Tax Payments
- Information System User Access Not Effectively Monitored
- Payroll/Personnel Internal Control Weaknesses

Not Resolved by Management:

- Information Systems Control Weaknesses
- Accounting Records and Reports Not Reconciled to Tax Information Database
- Lack of Control Within On-Line Error Resolution (OLER) System
- Financial Statement Information Not Properly Prepared
- Weaknesses in Controls Over Protested Tax Balances
- Insufficient Collection Effort for Tax Assessments

- Insufficient Control Over Refund Approval Process

- Tax Collections Not Deposited Timely

Based on the application of the procedures referred to previously, all significant findings are included in this letter for management's consideration. All findings included in this management letter that are required to be reported by *Government Auditing Standards* will also be included in the State of Louisiana's Single Audit Report for the year ended June 30, 2003.

Information Systems Control Weaknesses

For the second consecutive year, the Department of Revenue did not have adequate internal control over the information system (IS) functions that could affect the integrity of programs, processing, data, and financial reports for the Uniform Accounts Receivable (UAR) System. To ensure that the processing of transactions and financial data is performed according to management's design, good internal control requires the following:

- Responsibilities and mechanisms for developing, monitoring, modifying, and controlling information systems should be clear and well documented.

- Controls over application systems should be adequate to ensure accuracy of financial reporting requirements.

- System controls should be adequate to ensure that unauthorized or erroneous changes to tax records are not made.

During our test of transactions processed through the UAR, the following control deficiencies were noted:

- Financial information generated by the UAR System is not reliable. During the test of transactions, various truncation errors were noted on system screens, which resulted in inaccurate information used by employees to research taxpayer information and in financial reporting. For example, a truncation error for delinquent penalties caused 14 taxpayer accounts to be understated by $2.1 million.

- There is a lack of explicit, written identification of the business requirements of the system and lack of standardized, comprehensive documentation sufficient to meet the needs of technical and user support personnel to include contents of reports generated and the control procedures the user should employ when reviewing the reports for accuracy.

- Taxpayer accounts are purged when an account has the "maximum" number of transactions allowable or has the maximum number of accounts receivable records allowable and the account has become "full," meaning no space is available to post other transactions. When purged, the taxpayer accounts are stored in the department's archival system (RDARS). Transactions that remain in active status must be reentered into the mainframe. No supervisory review or approval is done to ensure that employees reenter the necessary data to keep taxpayer accounts active and current. The department cannot determine how many active account transactions exist in the RDARS.

- The system does not have sufficient edit checks to ensure that the amounts being refunded have actually been received and are reasonable. Two refund checks ($55 million and $48 million) for excise taxes were generated in error because the returns were keyed incorrectly into the system. These errors were caught through a manual review of a system-generated report that listed refunds to be paid.

The programs, their business requirements, and technical and user documentation were developed many years ago. The department limited work on the existing tax system several years ago because of its efforts to design and implement a new tax accounting system.

Failure to establish adequate internal control increases the risk that data could be accessed and modified without proper authorization, review, and approval; that data integrity could be impaired; and that errors or fraud could occur and not be detected for those taxes still accounted for on the UAR System. In addition, inaccurate or incomplete data and reports from the information system may result in materially incorrect financial data, impede collection efforts, and result in taxpayer complaints.

Even though the department is implementing a new tax accounting system, it still needs to establish and maintain adequate internal controls over the UAR System activities to ensure the integrity of data and financial reporting for those taxes that are still maintained in this system. Management substantially concurred with the finding and recommendation but did contend that RDARS is not meant to be used to store active account transactions (see Appendix A, pages 1-2).

Additional Comments: Although RDARS is not meant to be used to store active account transactions, such transactions have, in the past, been erroneously moved to RDARS. Without appropriate supervisory review, management cannot reasonably ensure that these active account transactions are properly restored on the mainframe.

Weaknesses in GenTax System

The Department of Revenue does not have sufficient internal control over the new tax accounting system (GenTax) functions, which could affect the integrity of processing, financial data, and financial reporting. The first phase of GenTax went on-line effective February 1, 2003, when the accounting for individual withholding, international fuel tax agreement, and beer taxes were moved to the system. An adequate system of internal control requires that the program has adequate written system documentation, has system reconciliation procedures, and be able to provide accurate system information in a timely manner. For the fiscal year ended June 30, 2003, GenTax processed approximately $115.8 million of tax collections, as well as other transactions, during the period February 1, 2003, to June 30, 2003.

IS general controls include controls over (1) organization and management of IS activities; (2) application systems development, installation, and maintenance; (3) systems software support; (4) computer operations, including backup and disaster recovery; (5) security administration policies and procedures; (6) logical security; and (7) internal audit of IS activities. Good IS general controls are necessary to preserve the integrity of the system and to provide reliance on the results, especially financial information, produced by the system. IS application controls include control procedures over input, processing, and output of data. Good IS application controls are necessary to ensure that the processing of transactions is performed in accordance with management's design and intent.

During a review of the GenTax System for the fiscal year ended June 30, 2003, the following control deficiencies were noted:

- The department had not adequately documented controls relating to the GenTax data structure, which consists of many data tables. The department could provide only limited technical system documentation on the functions, processes and interrelationships of each GenTax module. The department's IT division did not have sufficient knowledge of the new system to answer many questions. In most instances, the auditors were directed to the vendor for answers concerning general and application controls over logical security, input, processing, and output of data.

- The department had not developed, implemented, or documented procedures to reconcile accounting records to the source data contained in GenTax and to identify missing, incomplete, and inaccurate tax information for system-generated transactions, transactions initiated through on-line error resolution, and electronic funds transfer payments. The lack of documented procedures results in the risk of undetected errors or fraud and provides no assurance that system-generated reports or underlying data are correct.

- The department could not provide a complete copy of a GenTax User Manual or a detailed description of the transaction types. Therefore, for seven of 17 items (41%) tested totaling $9,183,884, it could not be determined whether the transactions were coded properly. In addition, for these same items, it could not be determined whether an appropriate supervisor approved the on-line error resolution of these items. The department has over 200 employees with access to GenTax.

- A $2.2 million sales tax payment was incorrectly sent to the GenTax System for processing even though the sales tax module was not yet on-line in the system. In addition, this payment was posted to an account that could be manipulated by the Director of Operations.

- The department does not have adequate security procedures to ensure that access to hardware, software, and data is limited to the business need of employees and that authorized users are assigned individual user IDs. We noted the following:

    - Management information system programming personnel have access to production software and hardware within the Data Control center and at the department's off-site operations at the Department of Public Safety.

    - One database administrator is also an authorized system administrator. This combination of access rights grants to one individual the power to alter virtually anything in the GenTax System.

    - A single user ID for the structured query language (SQL) server used for all GenTax database servers is shared among several database administrators.

    - A single user ID and password for providing access to the firewall is shared by more than one administrator.

- The department does not have an IS auditor. Adequate internal control requires periodic reviews of the IS division's general and application controls by an IS auditor. The IS auditor position has been vacant since May 2002. The absence of an IS auditor means that no one independent of the IS division is assessing the adequacy of IS controls.

- In addition, the department does not have a written business continuity or disaster recovery plan.

These conditions occurred because the department is implementing the GenTax System in phases over a three-year period. Control deficiencies could affect the integrity of programs, processing, and data. As a result, risk exists that GenTax programs and data could be accessed and modified without proper authorization, review, and approval; that errors or fraud could occur and not be detected; and that a disaster could occur and the system may not be able to fully recover lost programs and data.

Management should establish adequate IS procedures and controls over the GenTax System to ensure the integrity of programs, processing, and data. Management should also ensure that the system has proper disaster recovery and reconciliation procedures and is able to provide accurate information in a timely manner. Management did not concur that there is insufficient control over the GenTax System. However, management concurred with the various control deficiencies and recommendations, except for the parts regarding adequate documentation of controls relating to the GenTax data structure and the inadequate security procedures over access to hardware, software, and data (see Appendix A, pages 3-5).

Additional Comments: Although management did not concur that there is inadequate control over the GenTax System and only partially concurred with some of the deficiencies noted, management has taken a position in its corrective action plan to strengthen the deficiencies noted in the above finding.

Lack of Control Within On-line Error Resolution (OLER) System

For the second consecutive year, the Department of Revenue does not have adequate control procedures and an adequate audit trail over the OLER to ensure that transactions are valid, authorized, and correctly entered into the department's tax information system. Transactions should be initiated and controlled with the general and specific authorizations of management. An audit trail should be maintained that allows tracing the path of any transaction from inception to final disposition and internal controls should ensure that transactions are reviewed and approved by an appropriate supervisor so that errors and/or fraud are detected timely.

The department has over 400 employees with access to OLER. These employees have the ability to make corrections, changes, or other adjustments to taxpayer accounts without review by an appropriate supervisor.

In addition, a test of 16 randomly selected transactions that required entry into OLER revealed the following control deficiencies:

1. Fifteen of the 16 transactions (94%) were not reviewed or approved by an appropriate supervisor.

2. Taxpayer payments may not be posted accurately and timely to the taxpayer's account as to the proper tax type (i.e., sales, income, et cetera) and tax period. For example, a $5,310,505 electronic fund transfer (EFT) tax payment was posted on January 21, 2003, to sales taxes instead of to gasoline and special fuels taxes. On February 13, 2003, a correcting entry was made to place $4,976,164 in the taxpayers' special fuels account and $334,341 in the gasoline account; however the correct amounts were placed in the wrong accounts. On April 2, 2003, another correcting entry was made to place the correct amounts in the correct accounts.

The department does not have written policies and procedures that require appropriate supervisory approval and a periodic reconciliation between edit/error reports to ensure the completeness and accuracy of data entered into the department's tax information system.

Annually, the department collects approximately $6 billion of state revenues. The lack of adequate internal control over the on-line error resolution process may result in inaccuracies in system data and reports and errors and/or fraud could occur and not be detected in a timely manner. In addition, management cannot be certain that financial statement amounts are fairly presented when transactions are not posted accurately and timely.

Management should establish written policies and procedures that ensure an adequate audit trail is established, transactions are reviewed and approved by an appropriate supervisor, and a periodic reconciliation between edit/error reports is performed to ensure the completeness and accuracy of the mainframe date. Management partially concurred with the finding and outlined a plan of corrective action (see Appendix A, page 6).

Financial Statement Information Not Properly Prepared

For the second consecutive year, the Department of Revenue did not submit an accurate and complete Annual Fiscal Report (AFR) to the Division of Administration by the prescribed due date. Louisiana Revised Statute 39:79 authorizes the commissioner of administration to establish the format for reporting each agency's financial information. The Office of Statewide Reporting and Accounting Policy (OSRAP) designed an AFR to obtain this information and requires a signed affidavit from each agency that the financial statements present fairly the financial information of the agency. OSRAP uses the department's AFR during its compilation of the state's annual financial report. The completed AFR was due to OSRAP on August 29, 2003. Good internal control requires adequate procedures to accurately and completely record, process, and summarize financial data needed to prepare accurate and timely financial statements. The department's AFR that was submitted on September 2, 2003, included the following errors:

Noncurrent Receivables

Receivables were overstated by at least $16.3 million because of the following:

- Tax payments totaling $4.6 million that were received before June 30, 2003, were included in the department's revenues as of June 30, 2003, and included again as receivables because the payments were not posted to taxpayers accounts until after year-end.

- Income withholding taxes were overstated by $4.7 million because of duplicate receivables in the amount reported.

- For taxpayer accounts over $100,000, receivables were overstated by $3.1 million because the department failed to provide adequate written instructions to the Tax Divisions regarding procedures to ensure the accuracy of accounts receivables greater than $100,000.

- Receivables from proposed assessments were overstated by $3.9 million because taxpayers included cents on their tax return forms. The tax return forms require the taxpayers to round amounts either up or down to the nearest dollar. However, the department recorded cents as dollars for these receivables.

- The accrual for interest and penalties overstated the gross receivables balance and the allowance for doubtful accounts. Interest and penalties continued to accrue on taxpayer accounts beyond the fiscal year-end because the department has not developed a methodology to accurately record and report interest and penalties at year-end.

- In its computation of individual income tax receivables from proposed assessments, the department used the amount collected for withholding taxes during the 45-day close period in fiscal year 2002 rather than the amount collected during the close period in fiscal year 2003. The department was unable to obtain the fiscal year 2003 amount from the new tax system (GenTax).

Refunds Payable

Refunds payable were overstated in the annual fiscal report by $20.5 million because of the following:

- A total of $14.2 million of refunds residing on tax systems relating to business taxes were included twice. In addition, approximately $0.6 million of individual income tax system refunds were not recorded as payable.

- The department incorrectly included as refunds payable $7.1 million for such items as a payment made under protest, system input errors, and including interest accrued after June 30, 2003.

- The department did not include $1.9 million of refunds residing on side systems throughout the department, interest paid on those refunds, and some July refund payments that were manually processed as refunds payable.

- A total of $1.8 million of duplicate refunds payable that resulted from a programming error in a report generated from the new tax system (GenTax) were recorded as payable.

- Management has failed to develop a methodology to record the interest due to taxpayers on refunds payable in the annual financial report.

- Management has not developed procedures to include in refunds payable amounts from protested tax balances when the lawsuits are settled as of year-end.

- Management has not developed and communicated formal written procedures for the compilation of Refunds Payable and has not developed an adequate review process to ensure that the Refunds Payable footnote disclosure is materially correct.

Accounting Records and Reports Not Reconciled to Mainframe

- The Controller's Division does not perform an adequate reconciliation between the accounting records and the related mainframe databases to ensure that all items and adjustments have been accounted for when determining the accrual amounts at June 30.

- The Controller's Division does not reconcile the amounts recorded as collections in the Integrated Statewide Information System (ISIS) with the department's tax information databases to ensure that all amounts reported as collected on the tax information databases represent actual collections. For example, our review of ISIS journal vouchers showed that the State Treasurer's Office incorrectly moved $5.4 million of Severance Tax collections to the Mineral Revenue Audit and Settlement Fund. This caused total collections for the department to be understated in its AFR.

Management agreed to correct the material misstatements that we detected but has not established detailed written procedures for the compilation and maintenance of supporting documentation of financial statement amounts. In addition, management lacks procedures for reconciling and correcting discrepancies between accounting records and the tax information databases.

Management should establish a formal written compilation process that requires the maintenance of adequate reports and supporting documentation and the performance of analytical procedures to detect and correct errors before submission of the AFR to the Division of Administration. In addition, management should develop, implement, and document procedures to ensure that accounting records, as well as the information in the department's tax information databases, are accurate and complete. Management partially concurred with the finding regarding the reconciliation between accounting records and the related mainframe databases. Management did not concur with the finding regarding the reconciliation of collections recorded in ISIS to the department's tax information databases indicating that the two systems will never agree exactly because of timing differences (see Appendix A, pages 7-8).

Additional Comments: The reconciliation between accounting records and the related mainframe databases does not need to be to the exact amount. Instead, it can be used to determine if all large items and adjustments have been identified to ensure that the accrual amounts at June 30 are materially correct.

The Operations, Taxpayer Services, and Controller's divisions perform their reconciliation of collections recorded in ISIS to the department's tax information databases daily. These reconciliations do not account for any adjustments or reclassifications of tax collections that can occur at a later date, especially such transactions occurring in ISIS. If a reconciliation of the monthly collection data to ISIS had been performed, the ISIS journal voucher incorrectly moving $5.4 million of Severance Tax collections to the Mineral Revenue Audit and Settlement Fund could have been detected and corrected in a timely manner.

Weaknesses in Controls Over Protested Tax Balances

For the fifth consecutive year, the Department of Revenue did not reconcile the balances of protested taxes actually collected and recorded by the Controller's Division and the

Taxpayer Services Division with the balances recorded in the Legal Division's Tax Claims and Litigation Tracking System. Good internal control would ensure that protested tax balances in the Legal Division's records reconcile to those in the Controller's Division and the Taxpayer Services Division.

The department's established procedure has been to require a quarterly reconciliation among the Controller's Division, the Taxpayer Services Division, and the Legal Division to verify that payments received under protest have been properly recorded by each division. Each division keeps a subsidiary record of taxes paid under protest. According to the Controller's Division, the balance of taxes paid under protest at June 30, 2003, totals $159.1 million. Audit procedures revealed the following:

1. No reconciliations were performed for the quarters ended September 30, 2002, and December 31, 2002.

2. For the quarters ended March 31 and June 30, 2003, the department only reconciled the balances of the Controller's and the Taxpayer Services divisions.

Management did not enforce the established procedure that requires quarterly reconciliations of protested tax balances among the Controller's Division, Taxpayer Services Division, and the Legal Division. The lack of timely reconciliations increases the risk that error or fraud may occur and not be detected in a timely manner.

Management should take steps to ensure that all quarterly reconciliations are performed and that the information provided by the Legal Division includes the dollar amount contained in each lawsuit. Management concurred with the finding and outlined a plan of corrective action (see Appendix A, page 9).

Insufficient Collection Effort for Taxes Owed

For the fourth consecutive year, the Department of Revenue did not enforce its procedures that were designed to ensure effective collection efforts for tax assessments as well as the payment of taxes by department employees. The department's *Policies and Procedures Manual* (PPM), *Collection Division Desk Manual,* and the *Field Services Manual* discuss the procedures that should be followed when the department issues final assessments to taxpayers. Final assessments apply when a taxpayer has filed a return but has not made any payment; proper payment was not made (i.e., NSF check) based on a return; or an audit or examination identifies taxes due. A final assessment also occurs when the taxpayer does not file a return and the department assesses a tax, and the taxpayer fails to remit payment or file an appeal within the prescribed amount of time. In addition, Louisiana Revised Statute 47:31 requires every person (or the person's estate) residing within the state to pay a tax on net income and the department's

Standards of Conduct Section 23 requires all employees to comply with all applicable requirements of state tax laws and filing requirements.

Our review of the department's procedures regarding collection efforts for taxes owed to the state disclosed the following:

1. The department does not follow its policies and procedures to ensure that refunds are not issued to individual taxpayers whose businesses accounts have been placed in uncollectible status.

2. The department uses computerized work queues to prioritize accounts assigned for collection effort. The work queues are ineffective for ensuring that the oldest and largest accounts are given priority, resulting in some accounts remaining in active status for over 10 years. In addition, these queues can be turned off and on by supervisors.

3. The department does not provide adequate documentation to verify that all attempts to effect collection have been completed before an account is deemed uncollectible. In addition, the notes section of the taxpayer's electronic files does not adequately document the reasons/information to justify their uncollectible status and/or to provide an adequate audit trail for final assessments placed in uncollectible status.

4. In accordance with PPM 30.17, the department only bills taxpayers for amounts due that exceed $9.99 for each tax period. The policy states that the use of this amount will be periodically reviewed and appropriate recommendations will be made to management concerning the raising or lowering of this billing tolerance. The current policy has been in effect since November 1, 1988, when the cost of issuing and collecting a bill was determined to be $9.33.

5. The department has failed to monitor the tax filing status of its employees on a timely basis. As of October 22, 2003, the department has not performed the yearly review for the 2001 tax year. In addition, 26 employees of the department took part in the Tax Amnesty Program held in October 2001. These employees paid $13,557 in back taxes.

Although most established procedures appear adequate, the department's failure to implement those procedures and aggressively pursue the collection of taxes allows businesses and business owners that are delinquent to continue to operate in the State of Louisiana. In addition, by not monitoring the tax filing status of its employees timely, the department cannot ensure that its own employees are paying their taxes in accordance with the department's Standards of Conduct Section 23 and state law. Furthermore, at June 30, 2003, the department records reflect that over $149.7 million in uncollected taxes are due to the state, of which over $69.7 million has been outstanding for over one year but less than five years.

Management should implement and/or update its policies and procedures to ensure that an effective and adequate collection effort is made to collect all taxes due to the State of Louisiana. Management partially concurred with the finding and recommendation, except management did not concur with the lack of timely monitoring of employees' tax status (see Appendix A, pages 10-11).

Additional Comments: Based upon the evidence provided as of October 22, 2003, the department's review of employees' 2001 tax returns was not performed timely.

Insufficient Control Over Refund Approval Process

For the second consecutive year, the Department of Revenue does not have sufficient control procedures to ensure that taxpayer refunds are valid and properly approved before issuance and that interest is paid in accordance with state law. The department's Policies and Procedures Memorandum (PPM) 30.1.2 titled "Refund Review and Approval Procedures" establishes the review and approval procedures for issuing refunds of $20,000 or more, excluding interest. PPM 30.1.2 Subsection 4d allows for seven exceptions to the approval signature requirements. If a refund is due as a result of any of the noted exceptions, the refund can be issued to the taxpayer after being reviewed by only one employee of the department. In addition, Louisiana Revised Statutes 47:115(A) (3) and 47:1624(A) require the department to pay interest on certain amounts refunded or credited to taxpayers and state how the interest due shall be computed.

We tested 20 refunds totaling $28,112,502 that were issued during fiscal year 2003. The test of those refunds revealed the following control deficiencies:

- Three of the 20 refunds (15%) totaling $5.5 million were issued by an employee without any supervisory approval in accordance with the exceptions allowed by PPM 30.1.2. These refunds were for $50,405; $191,958; and $5,283,993.

- Eleven of 20 refunds (55%) did not include interest due of approximately $159,000 as required by state law.

Management has not considered the potential adverse effect the control deficiency over the refund approval process may have on the financial statements and the revenues of the State of Louisiana. In addition, the department does not ensure that the laws regarding the payment of interest on refunds is consistently applied. Failure to require supervisory review and approval to all large refunds increases the risk that errors and/or fraud could occur and not be timely detected and corrected. Failure to include interest on all eligible refunds underpays the taxpayer, overstates revenue collections, and subjects the department to noncompliance with state laws.

The department should reevaluate PPM 30.1.2 and require supervisory review and approval for all large dollar refunds issued. Also, the department should ensure that interest is paid on all refunds and credits as required by state law. Management did not concur with the finding and recommendation regarding the refunds issued. Management partially concurred with the finding and recommendation regarding the interest on refunds (see Appendix A, pages 12-13).

Additional Comments: The refunds issued under the exceptions in PPM 30.1.2 were issued by an employee without any supervisory review and approval. If the steps in the refund process for large dollar refunds are not reviewed timely by a knowledgeable supervisor, the state's assets are at risk.

Tax Collections Not Deposited Timely

For the sixth consecutive year, the Department of Revenue did not comply with state law for timely deposits of tax collections for major state revenues. Article 7, Section 9 of the Louisiana Constitution requires that all money received by state agencies shall be deposited in the State Treasury immediately upon receipt. The *Division of Administration and State Treasurer Policies and Procedures Manual* defines immediately as "within 24 hours of receipt." In addition, good internal control requires that collections received by the department be deposited timely to properly safeguard assets.

An analysis of tax information data that was supplied by the department revealed that 103,958 of the 110,183 batch headers (94.4%) were not deposited timely. A batch header is a summary of the information in a batch that includes total dollar amount; date of returns, payments, or declarations received by the department; date of deposit to the bank; and number of documents in the batch. The total amount not deposited timely accounted for $1.49 billion of the $6.28 billion (23.7%) deposited for fiscal year 2003. These deposits ranged from one to 60 days late, for an average of 8 days late.

This condition is the result of inefficient methods of processing tax returns and remittances. In addition, the department has not fully implemented an adequate method of monitoring the effectiveness of its system for depositing tax payments. Consequently, the department has an increased risk that untimely deposits will be susceptible to loss and/or theft. In addition, by not making deposits in a timely manner, the state's Treasury Department is hindered from earning interest on these collections. If deposits had been made within one day of receipt, the state could have earned approximately $470,868 in interest, assuming a simple interest rate of 1.80%.

Management should review current procedures and identify changes that can be made to enhance its compliance with the Louisiana Constitution relative to timely deposits in the state's Treasury Department accounts. Management concurred with the finding and outlined a plan of corrective action (see Appendix A, pages 14-15).

Incorrect Deposit of Monies Into Sports Facility Assistance Fund

During fiscal year 2003, the Department of Revenue incorrectly deposited income taxes received from resident professional athletes into the Sports Facility Assistance Fund. Louisiana Revised Statute 39:100.1 provides that the income taxes collected by the state that are attributable to the income of nonresident professional athletes and professional sports franchises that is earned in Louisiana is to be deposited into the Sports Facility Assistance Fund. In addition, the monies in the fund are to be appropriated to the facility, course, stadium, or arena at which nonresident professional athletes and professional sports franchises earned income in Louisiana.

For two of 12 (17%) of the professional athletes' returns tested, the Department of Revenue incorrectly determined these athletes to be nonresidents and distributed the $112,560 they paid in income taxes to the Sports Facility Assistance Fund.

This situation occurred because the department's procedures for determining the residency status of professional athletes earning income in Louisiana are deficient. For determining residency status, the department does not consider the addresses provided by the athlete or the information on copies of tax returns submitted to other states where those returns clearly state that the taxpayer is a resident of Louisiana. Instead, the department relies on the address provided by the professional athletic organization to determine if the athlete is a resident or nonresident.

The department should revise its procedures to include the consideration of the various states' tax returns submitted by professional athletes to aid in establishing the athletes' state of residency. Management concurred with the finding and recommendation and outlined a plan of corrective action (see Appendix A, page 16).

Additional Information for Consideration

The Office of Inspector General issued a report dated April 17, 2003, on the Louisiana Tax Commission. The report noted that a former member of the commission (1) accepted gratuities from a company that did business before the commission, (2) was a substantial owner of a business that leased space to companies whose business falls under the jurisdiction of the commission, and (3) submitted travel expense claims that were questionable because of lack of documentation supporting the purpose and business necessity of the trips. In addition, the report states the Tax Commission ". . . routinely conducted commission meetings in violation of the state's open meetings law, failing to post a notice or an agenda, and thereby effectively denying the public access." Copies of the Inspector General's report can be accessed on the Internet at www.state.la.us/oig/inspector.htm.

The recommendations in this letter represent, in our judgment, those most likely to bring about beneficial improvements to the operations of the department. The varying nature of the recommendations, their implementation costs, and their potential impact on the operations of the department should be considered in reaching decisions on courses of action. Findings relating to the department's compliance with applicable laws and regulations should be addressed immediately by management.

This letter is intended for the information and use of the department and its management and is not intended to be, and should not be, used by anyone other than these specified parties. Under Louisiana Revised Statute 24:513, this letter is a public document, and it has been distributed to appropriate public officials.

Respectfully submitted,

Grover C. Austin, CPA
First Assistant Legislative Auditor

RT:STD:THC:ss

[REVENUE03]

Appendix A

Management's Corrective Action Plans and Responses to the Findings and Recommendations

LDR
Louisiana Department of Revenue

January 27, 2004

Mr. Grover Austin, CPA
First Assistant Legislative Auditor
Office of the Legislative Auditor
P.O. Box 94397
Baton Rouge, LA 70804-9397

RE: Information Systems Control Weaknesses

Dear Mr. Austin:

Regarding the Uniform Accounts Receivable System (UAR), we **concur in part** that some documentation of changes to this System is inadequate and that the existing Legacy "system" has limitations. Controls do exist to ensure the authorization and accuracy of computer program changes to this and all systems. Each change is initiated with an approved Service Request and entered into an assignment tracking system until complete. An entry is made in the Modification History of the computer program for every change documenting: the change made, the date of the change, who made the change, and who authorized it. In addition, a quality assurance review process is conducted for each change verifying that certain actions were taken and certain procedures were followed.

Specific responses to the items in this Finding are listed below:

- We **concur** that some financial information generated by the UAR System must be reviewed and adjusted for the information to be reliable. As noted in this Finding, the UAR and other Systems were developed many years ago and are currently being replaced by the new GenTax (DELTA) System which offers vast improvements in accounting for all Receivables.

- We **concur** that some System-generated reports lack specific, written business requirements as well as appropriate documentation to enhance their use by Department personnel. Through the years, most reports were generated on an "as-needed" basis by various managers and executive staff. As DELTA is developed, so are the rationale, documentation, and control procedures of all reports.

- We **concur in part** that there is limited review by supervisors of the data reentered from the Department's archival system (RDARS). Legacy "system" limitations require manual intervention once an account is "full". The account and/or older transactions are first "purged" from the System followed by identifying and restoring those "active" transactions by manual review if such restoration is appropriate. The RDARS is an archival media and is used as a reference for recreating the account and for historical record. It is not used to store active accounts.

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Grover Austin, CPA
January 27, 2004

- We **concur** that this antiquated System is lacking in functionality. That's why procedures include various reviews and manual controls. To strengthen the controls on the issuance of refunds, UAR has been changed to allow sufficient time for a review to occur on all refunds over $100. Once the review timeframe (28 days) has lapsed, an automatic hold is put on the affected tax period. Once the refund is verified and all approval requirements are met, the refund will not print until a manual release is keyed to the System.

Within available resources, the Department will continue to do everything possible to maintain adequate internal controls over the UAR System to ensure the integrity of data and financial reporting.

Sincerely,

Stephen Hymel

Stephen Hymel
Undersecretary

Cc: Cynthia Bridges
Gwen Scott
Joy Shrum
Phyllis Perry
Greg Montagnino

LDR
Louisiana Department of Revenue

January 23, 2004

Mr. Grover Austin, CPA
First Assistant Legislative Auditor
Office of the Legislative Auditor
P.O. Box 94397
Baton Rouge, LA 70804-9397

RE: Weaknesses in GenTax System

Dear Mr. Austin:

The Louisiana Department of Revenue (LDR) began its project for a new integrated tax system in May, 2002. This new system's main component is the GenTax software package created by Fast Enterprises, LLC. The customized version of GenTax being developed for the twenty (20) largest revenue-producing taxes in Louisiana is called DELTA: "Defining Excellence in Louisiana Tax Administration".

We **do not concur** that there is insufficient internal control over the new tax accounting system (GenTax) functions. We **concur in part** that the Department's system of input, processing, and output controls for ensuring integrity of the GenTax System (and the existing Legacy "System") databases has been and continues to be an area of concern during this time of conversion and migration to the GenTax (DELTA) system.

In undertaking the DELTA project, LDR recognized the need to quickly demonstrate the viability of GenTax as a high-quality, tax administration product. The Department's choice of a rapid development methodology met several desirable goals. Among those goals were quick implementation, specific deliverables and deadlines, and the transferring of the majority of the implementation risks to the vendor. While this approach achieved several positive results, it required a heavy reliance on the expertise of vendor personnel in the earlier stages of the project such as Phase 1 covered in this audit. Although substantial dependence on the vendor is still necessary, LDR staff is steadily acquiring this expertise as each phase is completed. The contract stipulates five (5) phases. In addition, an independent project manager has been used from the start to oversee activity and evaluate risks.

The Department recognizes the need to continually review and update its accounting and control procedures to keep pace with the increasing technological advances it has undertaken in its efforts to modernize aging tax systems and improve customer services. This effort represents a major undertaking as LDR upgrades from a mainframe-based Legacy system to a "Windows"-based software package (GenTax) for tax administration. This change involves significant differences in the methods used for tax processing. It is likely that some accounting and control procedures must be modified. Efforts have begun to identify and address this need. These efforts will continue and become progressively more detailed throughout the course of this three-year project as each phase results in increasing expertise from the LDR staff.

With the implementation of this new tax system, LDR must review and adjust its accountability controls to reflect the new environment. Processes that were satisfactory in the Legacy system may no longer apply. In some instances, opportunities are surfacing for even more effective controls within the new system. LDR envisions forming a team to review these processes, validate that the existing processes are still effective, or recommend improvements where appropriate.

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Grover Austin, CPA
January 23, 2003

The rapid-development nature of the DELTA project limits the amount of time and resources that can presently be devoted to an overall review of LDR's accountability controls as they relate to the new system. In addition, LDR personnel (both IT employees and business unit representatives) are still learning and do not yet have a comprehensive understanding of the complexities of the GenTax system to conduct such an analysis independently. Contractual obligations in getting taxes converted into GenTax from the DORT Legacy system restricts the time and effort that the contractor (FAST Enterprises) can devote to such a review. As expertise continues to develop among the LDR staff, this knowledge will be used for an increasingly more indepth assessment of the System's accounting and control procedures. While it will be challenging for LDR to allocate sufficient resources to complete this activity, work on independent components of the system of controls will continue throughout the project. The overall review of monitoring and control procedures will incorporate this work. In addition, the Secretary has directed that each Division begin updating all existing process maps to reflect changes resulting from GenTax. The re-mapping of business processes will continue to be given a high priority with emphasis on controls points in these processes.

Comprehensive documentation of the system is a recognized need. Initiatives are underway to improve this documentation in the following areas:

- Cataloging of GenTax reports and providing details on the purpose and the description of the data for each report.
- Technical documentation.
- Application documentation.

A major effort to compile technical documentation for LDR use has begun and is outlined in the DELTA project's *Technical Knowledge Transfer and Documentation Plan*, published and accepted on August 30, 2003. An LDR IT manager and technician have been assigned the task of organizing and archiving all DELTA project technical documentation. A strategy has been selected and work is in progress. Fast Enterprises will also be committing a resource person to this effort.

We **concur** that at the time of the audit, reconciliation procedures were not completely functional. However, currently such procedures are implemented and will be formally documented and refined as needed as the project progresses. The Operations Division reconciles *the Daily Collection Report* (non-EFT deposit by tax) to the GenTax *Batch Success Report*. This reconciliation verifies that the money deposited has been posted by GenTax. The Operations Division then reconciles the *Daily Reconciliation Report* to the *Daily Collection Report* to verify that the money has been posted to the appropriate tax. Corrections in these reconciliations are initiated as needed by Operations employees.

The *Daily Collection Report* is furnished to the Controllers Division to post in ISIS. Controllers uses the *Daily Collection Report* provided by Operations and the *EFT Report* provided by IS to post to the in-house ledger and ISIS. The in-house ledger also includes other reconciled data such as NSF information, bank errors, and reallocations. ISIS and the in-house ledger are reconciled on a monthly basis. Each month Controllers also reconciles total EFT payments from ISIS to Controllers EFT records.

We **concur** that at the time of the audit, a GenTax User Manual was not up-to-date. However, the basics of and framework for a detailed Users Manual has been created and is in use. This manual will continue to be enhanced and refined as the project progresses.

Grover Austin, CPA
January 23, 2003

We **do not concur** that the Department lacks adequate security procedures to ensure appropriate access to hardware, software, and data. However, several activities are planned to validate and/or strengthen this security. These actions include a third party security vulnerability assessment in conjunction with the State's Office of Information Technology, a network intrusion testing assessment, and a review of all IT services provided by LDR groups to determine the best placement of those services in the organization. In addition, a review of all ID's for system administration, database administration, and security administration will be conducted. A review of all security groups within GenTax will also be done to verify that access is limited appropriately.

We **concur** that the Department has not yet employed an IT auditor. LDR has been working with the Department of Civil Service for many months to establish an appropriate job classification and description that meets the needs of our Internal Audit and IT Divisions. Thus far we have not been able to establish such a position but will continue to pursue hiring an IT Auditor.

We **concur** that the Department does not have in place a written business continuity or disaster recovery plan. However, we do have in place many of the components of such a plan. The State Office of Information Technology (OIT) is currently devising the requirements of such a plan for all State agencies and has procured software which will be made available to agencies to assist in achieving this objective. LDR intends to combine our efforts with OIT and other agencies to build a written plan and fully implement it. The Department has requested funding for this project for Fiscal Year 04-05

In summary, LDR is moving through a major transition as it upgrades its technology in the area of tax administration. During this transition the Department will mitigate risk by relying on the expertise of vendor personnel who are contractually obligated to protect the integrity of the tax system as well as assigning full-time agency staff to oversee project activity and using the services of an independent project manager. LDR staff has also been assigned full-time to learn the details of the System and to document these details as they relate to Louisiana. Rules and procedures of the past will also be scrutinized and revised when necessary. As the project moves closer to completion, LDR remains on schedule to successfully update its tax processing technology in an effective and secure manner which will significantly benefit the State in its revenue collection efforts.

The contact person for appropriate corrective actions is Greg Montagnino.

Sincerely,

Stephen Hymel

Stephen Hymel,
Undersecretary

Cc: Cynthia Bridges
Greg Montagnino
Phyllis Perry
James Greeson

LDR
Louisiana Department of Revenue

January 23, 3004

Mr. Grover Austin, CPA
First Assistant Legislative Auditor
Office of the Legislative Auditor
P.O. Box 94397
Baton Rouge, LA 70804-9397

RE: Lack of Control Within Online Error Resolution System

Dear Mr. Austin:

The Online Error Resolution (OLER) System was developed in the late 1980's in an attempt to improve the error correction process for taxpayer errors and keypunch errors. Prior to OLER the process was overly labor-intensive and time-consuming and this resulted in an unacceptable delay in the processing of many tax returns and refunds. Since instituting OLER the Department has attempted to balance the need for adequate control and review with the demand of citizen taxpayers and others for more timely processing of returns and refunds. Review is mandatory for certain adjustments. Under the Legacy and GenTax Systems, audit trails do exist that allow us to determine the employee who worked the account and what adjustments were made to the account. The Department continues to work toward improving the integrity and accuracy of taxpayer records.

The following are responses to the specific issues raised in the Finding:

- We **concur in part** with this item. Due to the large number of on-line transactions, relatively high employee-to-supervisor ratio, significant limitations of the Legacy system, and limited personnel and financial resources, it is not feasible to institute measures to review all or even a majority of transactions especially prior to the transaction's completion. The new GenTax system being customized for Louisiana will allow the Department to more readily review such transactions. Eventually an optimum number of transactions will be reviewed and a selected sampling developed to continue to ensure the integrity of taxpayer data.

- We **concur in part** with this item. Because of the limitations of the Legacy system it may take several months for an error of a specific posting to be discovered and corrected. In the current "system", should the incorrect posting failure-to-post error result in an overpayment, the potential refund is reviewed through our normal review process and the necessary adjustments made to the posting error. Should a billing be erroneously issued, we would, upon notification, make the necessary adjustment to reflect the correct liability. With the use of GenTax, payments that have been reversed but not applied will be identified through an automated system as well as payments that have been moved but have no matching liability. As the Department migrates to this new System, more timely and more frequent reviews will occur.

Sincerely,

Stephen Hymel

Stephen Hymel
Undersecretary

Cc: Cynthia Bridges
Kenneth Comeaux
Gwen Scott
Phyllis Perry
Barbara Roe

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LDR
Louisiana Department of Revenue

January 16, 2004

Mr. Grover Austin, CPA
First Assistant Legislative Auditor
Office of the Legislative Auditor
P.O. Box 94397
Baton Rouge, LA 70804-9397

RE: Financial Statement Information Not Properly Prepared

Dear Mr. Austin:

Noncurrent Receivables and Refunds Payable

We concur that the receivable and refunds payable figures reported on the Annual Fiscal Report (AFR) understated revenue by a net $4.2 million. The understatement of revenue was due to a variety of circumstances (e.g. some tax payments received at June 30, 2003 were not processed in time to be included on the receivable reports, programming errors caused some duplicate receivable and payable amounts to be reported and some escrow payments to be erroneously included as refunds payable, some data entry errors in processing tax returns went undetected, and a compilation error was made in calculating manual refunds payable).

Accounting Records and Reports Not Reconciled to Mainframe

We **concur in part** with this finding. We agree that ideally the accounting records (ISIS) and the mainframe database (Legacy system) should contain the same collection, refund and revenue adjustment data to ensure accrual amounts are reasonably accurate; however, the Legacy system was developed over 25 years ago and is an antiquated system with many limitations. The Legacy system was not designed to provide a means of reconciling its information to an external financial accounting system, such as ISIS. In addition, deposit data processed through the Operations Division is not necessarily loaded into the Legacy system the same day the funds are deposited into ISIS because deposit data must first be keyed and balanced by Operations. It may take several days or weeks for the deposit information to be posted to the Legacy system; therefore, ISIS and the Legacy system will never be in agreement because of these major timing differences. In order to accomplish the reconciliation as recommended in the audit finding, new processes would have to be developed and implemented in the Operations Division and a large amount of computer programming would also be required, which would be very time-consuming and costly.

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Mr. Grover Austin, CPA
January 15, 2004

We **do not concur** with the part of the finding that states amounts recorded as collections are not reconciled to the new integrated tax system database (GenTax system). The Operations Division processes all tax payments made by paper check and generates a deposit detail batch report and batch file that are used to post to both the ISIS system and the GenTax system. The Controllers Division ensures that the batches of payments are posted correctly in ISIS and the Operations Division ensures (reconciles) that the batches of payments are posted correctly in the GenTax system. Tax payments received by LDR through electronic funds transfer are posted to the ISIS system and the GenTax system using the same data. The Controllers Division ensures that the EFT payments are posted correctly in ISIS and the Taxpayer Services Division ensures (reconciles) that the EFT payments are posted correctly in the GenTax system. In our opinion, performing additional reconciliations between the summary revenue data in ISIS and the GenTax system would be redundant and extremely costly.

Corrective Action Planned

The receivable and payable reports containing programming errors will be corrected and more detailed written procedures for compiling the AFR will be developed under the GenTax system. We will implement additional analytical procedures that should help to detect and correct data entry errors made in processing tax returns and payments that directly affect the receivable and payable reports used to compile the AFR. The persons responsible for such corrective action are Dale LeJeune and Margaret Roubique of the Controllers Division.

Sincerely,

Stephen J. Hymel
Stephen J. Hymel
Undersecretary

Cc: Cynthia Bridges
Dale LeJeune
Phyllis Perry

LDR
Louisiana Department of Revenue

January 4, 2004

Mr. Grover Austin, CPA
First Assistant Legislative Auditor
Office of the Legislative Auditor
P.O. Box 94397
Baton Rouge, LA 70804-9397

RE: Weaknesses in Controls Over Protested Tax Balances

1. We concur that for quarters ended September 30, 2002 and December 31, 2002, no reconciliations were performed since the escrow records involving Protested Tax Balances were being restructured and a shared database was being developed.

2. We concur that for quarters ended March 31, 2003 and June 30, 2003, the Taxpayer Services Division and Controllers Division successfully reconciled its balances. Although no formal reconciliation was completed with the Legal Division ("Legal"), Legal did takes steps to verify the dollar amounts shown and the status of lawsuits pertaining to those amounts. Specifically, Legal now performs a monthly review of the escrow reports and maintains a separate log for payment made on protested tax balances. Legal has revised its "agreement to abide" procedure to ensure proper tracking of subsequent payments under protest.

As of this date, the Legal Division has reviewed and updated all accounts listed in the existing Escrow database for such Protested Tax Balances. The Controllers Division and Taxpayer Services Division will now work with Legal to reconcile any discrepancies for the next quarterly report. Persons responsible for such corrective actions include Dale Lejeune/Controllers Division, Rickey Hebert/Taxpayer Services Division, and Shone Pierre/Legal Division.

Sincerely,

Stephen Hymel

Stephen Hymel
Undersecretary

Cc: Cynthia Bridges
Dale Lejeune
Rickey Hebert
Shone Pierre
Kimberly Robinson
Gwen Scott

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LDR
Louisiana Department of Revenue

January 20, 2004

Mr. Grover Austin, CPA
First Assistant Legislative Auditor
Office of the Legislative Auditor
P.O. Box 94397
Baton Rouge, LA 70804-9397

RE: Insufficient Collection of Taxes Owed

Dear Mr. Austin:

1. We **concur in part** with this finding. The process of flagging individual tax accounts that have business tax liabilities is a manual process and completed only once a year. The business tax master file in the Legacy and GenTax Systems and the Individual Income tax master file are not interactive. Sales and Withholding taxes have been converted to GenTax while the Individual Income tax master file is still in our Legacy system. Employees use a computer printout to physically enter garnishment codes on the Individual Income tax files only after verifying that the business owner and individual are one and the same through social security number verification.

   The Department feels that it is doing everything possible to follow this procedure within the two Systems. The process will improve with the conversion of the Individual Income tax files to GenTax scheduled for implementation in October, 2004. Please note that regardless of what system contains the business and individual tax files, a match of the taxpayer's accounts cannot be obtained unless valid, verified social security numbers match on both accounts; otherwise, the State will be subject to wrongful seizure action by taxpayers.

2. We **concur** with this finding. The issue of prioritizing accounts assigned for collection efforts is being addressed with the conversion to GenTax. The "Warrant Manager" in GenTax allows for the sorting of assignments by taxpayer, tax type, office assignment (region), account ID, risk factor, balance due, age, etc. There are 26 different "stages" of the assignments, i.e. levy pending, waiver pending, offer-in-compromise, Currently Not Collectible, assigned, etc. Through the Warrant Manager, cases will be easier to monitor and employees' actions on the files will be easy to follow. Eight taxes have been converted to GenTax thus far and Severance tax, Corporation Income and Franchise Taxes as well as Individual Income Tax are scheduled for conversion in 2004. Once these taxes are converted, all major taxes collected by the Department will be on one system and final assessments will be in the Warrant Manager.

3. We **concur in part** with this finding. Employees are continually reminded of the importance of documenting all of the collection action taken on an account. The Legacy System has limited space for notes and is not user-friendly for tracking such notations. With the conversion of more taxes to GenTax, it will be easier to record and monitor each action taken. In fact, some actions taken on assignments in the GenTax Warrant Manager will be automatically captured by way of the action stages built into that system.

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Grover Austin, CPA
January 20, 2004

4. We **concur in part** with this finding. A detailed cost study was performed after the close of fiscal year ending June 30, 2002. The study indicates the cost of issuing a 10-day, 15-day or 30-day billing notice is $12.56 and cost of issuing a 60-day notice is $14.92. Management has reviewed the analysis but an updated PPM has not been drafted since another cost analysis must be performed once the employees master the use of GenTax.

5. We **do not concur** with this finding. The review for all tax years through 2001 was completed in April, 2003. Letters were sent to employees on May 12, 2003. In fact, if their 2002 income tax returns was not on file at that time they were reminded of that although the return was not due. The review for all tax years through the 2002 tax year was begun in October, 2003 and completed in December 2003. Employees have been notified by email of the tax delinquencies.

   Because the employees of the Department of Revenue are held to a higher standard by Department management than other taxpayers regarding the filing and payment of income taxes, their income tax accounts are individually checked to ensure compliance above and beyond what is prescribed by statute, policy or standards. In addition, the accounts of all new employees are reviewed as part of the "New Employee Sign-In" with the Human Resources Division.

The Department is in agreement with your statement that 26 employees of the Department took advantage of the Tax Amnesty Program in 2001. The statute authorizing the program did not exclude Revenue employees or other State employees. Various circumstances can lead to employees owing taxes and being unable to pay them in a timely manner. While the Department holds its employees to a higher standard they are no different than the average citizen, in that, extenuating circumstances can and will affect their lives creating hardships.

Sincerely,

Stephen Hymel

Stephen Hymel
Undersecretary

Cc: Cynthia Bridges
Kenneth Comeaux
Phyllis Perry
Gwen Scott
Joy Shrum

LDR
Louisiana Department of Revenue

January 20. 2004

Mr. Grover Austin, CPA
First Assistant Legislative Auditor
Post Office Box 94397
Baton Rouge, LA 70804-9397

Dear Mr. Austin:

RE: Insufficient Control Over Refund Approval Process

We **do not concur** that PPM 30.1.2 does not include sufficient control over the refund approval process. As noted in last year's response to a similar finding, it is our belief that the Department does have sufficient control procedures to ensure that refunds are valid and appropriately approved before issuance. Of the three refunds identified in the finding as having been issued without any supervisory approval, it is noted that all were issued in accordance with the provisions of PPM 30.1.2 and none were determined to not be due to the taxpayer under the information available. As noted in the finding, our current policy allows seven exceptions to the refund review and approval process as set forth in that policy. The basis for these seven exceptions is explained below.

1) *Refunds of excise taxes on original tax returns for accounts secured by bond or other financial assurance or for taxpayer accounts that have qualified for waiver of the bond requirements.* These refunds result from the dealer pre-paying tax on motor fuel that is ultimately shipped out-of-state.

2) *Refunds of corporation income and franchise taxes resulting from overpayment of estimated tax payments by the corporation.* These refunds occur when a corporation pre-pays its taxes in excess of the amount ultimately determined to be due.

3) *Refunds of corporation income and franchise taxes resulting from credits for payment of ad valorem taxes.* These refunds occur when the credit for ad valorem taxes paid to political subdivisions on certain inventory items held by manufactures, distributors and retailers exceeds the amount of tax due. The statute governing these credits specifically provide for the refunding of any credit not used to offset a tax liability.

4) *Tentative refunds of corporation income tax.* A taxpayer may request a tentative refund from the application of a net operating loss carry back under the provisions of Louisiana Revised Statute §47:287.86(G). As provided by statute, the auditing of these tentative refunds is conducted after the refunds are issued.

5) *Refunds of individual income tax resulting from overpayment of estimated tax payments by the individual.* When the total of the pre-payments by a taxpayer for his estimated taxes is in excess of the actual taxes calculated to be due, a refund will be issued of the excess.

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Mr. Grover Austin, CPA
January 20, 2004

6) *Reimbursements of amounts remitted to the Department that have been determined to be owed to another agency and that are transferred to the other agency by interagency transfer.* This situation occurs when a taxpayer remits money to the Department of Revenue that belongs to another governmental agency. The funds are transferred to the appropriate agency.

7) *Duplicate or erroneous electronic fund transfers.* It is not uncommon for taxpayers to make errors when electronically transmitting their payments of taxes due. When this situation occurs, the respective divisions maintain proper documentation. Additional review and approval by the executive management would unnecessarily delay the issuance of the refund thereby placing the taxpayer in a potentially difficult situation monetarily.

As noted previously, an analysis of this process clearly indicates that sufficient controls are in place to protect the State from undue risks of erroneously issued refunds or issuance of fraudulent refunds. All steps in the refund process are documented and are available for review. Each of these exceptions involves routine overpayments and do not involve substantive tax issues. However, because of capabilities of the new GenTax system currently being implemented, the executive management team is considering revising the current policy to eliminate these exceptions.

Regarding the issuance of interest on refunds, we **concur in part** that refunds did not include interest due. Due to the limitations of the legacy computer system, interest on refunds was required to be calculated manually. To issue interest on all refunds would require a review of each refund regardless of amount and determination of the correct interest due, if any. The cost to the Department to have sufficient manpower to accomplish this task in a timely manner would be prohibitive and due to the longer delays in issuing the refunds, a significantly larger number of refunds would incur interest than might otherwise be required by statute. An interdepartmental procedure provides for the automatic calculation of interest on refunds that require manual review, which would generally be those refunds in an amount that required supervisory review and approval. Please note that refunds issued under the GenTax system automatically calculates and includes interest.

Sincerely,

Stephen Hymel

Stephen Hymel
Undersecretary

Cc: Cynthia Bridges
Kenneth Comeaux
Phyllis Perry
Barbara Roe

State of Louisiana
Department of Revenue

M. J. "Mike" Foster, Jr.
Governor

September 10, 2003

Cynthia Bridges
Secretary

Mr. Grover C. Austin, CPA
First Assistant Legislative Auditor
P. O. Box 94397
Baton Rouge, LA 70804-9397

Dear Mr. Austin:

RE: Tax Collections Not Deposited Timely

The Department of Revenue concurs with the finding concerning the timely deposit of collections. We agree that 76.30% of the funds collected are deposited timely. We further concur that the remaining 23.7% of funds, funds deposited manually, are deposited outside the 24-hour time frame.

Management recognizes that deposit of <u>all</u> funds within a 24-hour time frame is not cost effective. The Department's strategic plan calls for 75% of all funds to be deposited within 24 hours by the year 2006, and we have met that requirement this year. Management must balance the resources available among the objective to improve timely deposits and other strategic plan requirements, including processing returns and refunds timely, as well as the use of available funds for additional processing enhancements.

The Department of Revenue improved the percentage of funds deposited within 24 hours from 74.4% to 76.30% for this fiscal year. The average deposit time also improved by two days which indicates that our efforts to implement processing enhancements are achieving results. Additional methods for electronic and paper processing continue to be examined as part of the Department's continual improvement efforts to provide more timely deposits. Emphasis has been placed on the objective, and the achieved results are regularly posted to provide information on our performance to our employees.

The Department has long recognized the difficulties in obtaining statistical and monitoring information, and a "tax re-engineering" initiative is in process to implement a new system to provide better tracking information. The first phase of this program was implemented in February, 2003, with the second implementation in August, 2003. Other auxiliary systems continue to be refined to provide better monitoring information.

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The additional costs to achieve deposit of all funds within "24 hours of receipt" would exceed your calculated $470,868 of additional interest earned on deposited funds.

Janet Macmurdo, Director of the Operations Division, is the contact person regarding the corrective action plans for this finding.

If you have any questions, please contact my office at 219-2710.

Sincerely,

Stephen Hymel

Stephen J. Hymel
Undersecretary

Cc: Cynthia Bridges
Kenneth Comeaux
Phyllis Perry
Janet Macmurdo

State of Louisiana
Department of Revenue

M. J. "Mike" Foster, Jr.
Governor

Cynthia Bridges
Secretary

November 3, 2003

Mr. Grover C. Austin, CPA
First Assistant Legislative Auditor
P. O. Box 94397
Baton Rouge, LA 70804

Dear Mr. Austin:

Incorrect Deposit of Monies into the Sports Facility Assistance Fund

The Department concurs that two (2) of the returns were inappropriately classed as non-resident returns and the appropriate transfer of funds will be made.

In order to correct the situation in the future, a closer review of each "questionable" return (questionable with respect to actual domicile of the athlete) will be conducted prior to making a determination that the return has been filed by a non-resident professional athlete.

The review will consist of:

1) Examining the return for other states' returns
2) Inspecting attached returns for state of residency claim
3) If necessary, request from the taxpayer a copy of their federal return

If the above procedures do not yield a clear answer, the Department will contact the taxpayer and solicit information to make a proper determination of the taxpayer's domicile.

Sincerely

Stephen Hymel

Stephen J. Hymel
Undersecretary

Cc: Cynthia Bridges
Phyllis Perry
Gwen Scott
Clarence Lymon

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