

SPRINGFIELD OFFICE:
ILES PARK PLAZA
740 EAST ASH · 62703-3154
PHONE: 217/782-6046
FAX: 217/785-8222



CHICAGO OFFICE:
STATE OF ILLINOIS CENTER · SUITE 4-100
100 WEST RANDOLPH STREET · 60601
PHONE: 312/814-4000
FAX: 312/814-4006

OFFICE OF THE AUDITOR GENERAL
WILLIAM G. HOLLAND

REPORT DIGEST

**DEPARTMENT OF CORRECTIONS
CORRECTIONAL INDUSTRIES
FINANCIAL AUDIT
For the One Year Ended June 30, 1994
AND
COMPLIANCE AUDIT
For the Two Years Ended June 30, 1994**

5-94-43400-10

SYNOPSIS

- Correctional Industries distributed, free of charge, \$64,652 in finished goods. Typically, the free merchandise included items such as golf shirts, tee shirts, sweatshirts, ball caps, jackets, towels, and legal pad holders. According to management, many of these items were given away as promotional samples at golf outings and at charitable and community events throughout the State. The Department policy regarding these cost-free distributions of finished goods samples was inadequate and was not always followed.
- The Department did not collect Retailers' Occupation Tax (sales tax) on sales to non-governmental and other non-exempt organizations. Most of the Correctional Industries' sales appear to have been made to governmental and not-for-profit organizations which are tax-exempt under Illinois law. However, we noted some sales which were made to organizations which were not tax-exempt organizations (i.e., motorcycle clubs and fraternal organizations). As a result of this finding, Correctional Industries has requested an official opinion from the Illinois Department of Revenue to determine the tax status of these sales.

{Expenditures and Activity Measures are summarized on the reverse page.}

INTERNET ADDRESS: AUDITOR.GENERAL@ACCESSIL.COM

RECYCLED PAPER · SOYBEAN INKS

ILLINOIS DEPARTMENT OF CORRECTIONS
CORRECTIONAL INDUSTRIES
FINANCIAL AND COMPLIANCE AUDIT
FOR THE PERIOD ENDED JUNE 30, 1994

OPERATING STATISTICS	FY 1994	FY 1993	FY 1992
● Net Sales	\$36,077,888	\$38,100,012	\$33,184,641
● Cost of Sales	<u>\$32,109,947</u>	<u>\$32,308,173</u>	<u>\$28,209,625</u>
● Gross Profit (Loss)	\$3,967,941	\$5,791,839	\$4,975,025
Selling, General and Administrative Expenditures	<u>5,243,001</u>	<u>4,636,081</u>	<u>4,018,176</u>
Operating Profit (Loss)	\$(1,275,060)	\$1,155,758	\$956,849
Other, Net	<u>(14,446)</u>	<u>21,926</u>	<u>507,293</u>
● Net Profit (Loss)	\$(1,289,506)	\$1,177,684	\$1,464,142
Beginning Retained Earnings	16,958,116	15,780,432	16,160,739
Transfers into General Revenue Fund	<u>--</u>	<u>--</u>	<u>(1,844,449)</u>
● Ending Retained Earnings	<u>\$15,668,610</u>	<u>\$16,958,116</u>	<u>\$15,780,432</u>
KEY BALANCE SHEET ACCOUNTS, AS OF JUNE 30,	1994	1993	1992
Accounts Receivable	\$6,771,143	\$6,251,243	\$6,460,815
Inventories	\$9,800,078	\$7,535,550	\$8,892,250
Property, Equipment and Livestock, Net of Depreciation	\$8,564,276	\$7,837,748	\$8,349,032
● Average Number of Employees	192	181	171
Average Number of Inmate Workers	1,468	1,376	d.n.a.
d.n.a. - Data not readily available			

CORRECTIONAL INDUSTRIES' CHIEF ADMINISTRATIVE OFFICER

During Audit Period: Ronald L. Parish
Currently: Ronald L. Parish

INTRODUCTION

This is the audit of the Correctional Industries, a component of the adult division of the Illinois Department of Corrections. Correctional Industries operates manufacturing, service and agricultural industries within the adult correctional centers. Its purpose is to replicate a free world work environment to the greatest extent possible, while operating within a budget that does not exceed income, maximizing the number of inmate assignments, and providing customers quality goods and services at a competitive price.

FINDINGS, CONCLUSIONS, AND RECOMMENDATIONS

WEAKNESSES IN POLICY REGARDING COST-FREE DISTRIBUTIONS OF MERCHANDISE

Correctional Industries distributed, free of charge, finished goods valued at \$33,918 in fiscal year 1994 and \$30,734 in fiscal year 1993. According to personnel, the purpose of these cost-free distributions was to promote, to potential buyers, the use of Correctional Industries' products.

Our auditors analyzed the cost-free distributions from fiscal year 1994. Typically, the merchandise included items such as golf shirts, tee shirts, sweatshirts, ball caps, jackets, towels, and legal pad holders. Department personnel indicated that cost-free distributions made in 1993 were for similar types of merchandise.

Department personnel stated that many of these items were given away as promotional samples at golf outings and at charitable and community events throughout the State. We did not see evidence that the Department is authorized by statute to support charitable organizations and community events with Correctional Industries' resources. In addition, we question the need for cost-free distributions to State agencies and employees, since State agencies are already required by State law to buy Department merchandise.

The Department policy regarding the cost-free distributions of finished goods samples was inadequate and was not always followed. The Department had a written policy (dated 1982) which addressed the accounting, distribution, and approval of sample items. However, Correctional Industries did not always comply with these aspects of the policy. Also, the policy did not address the cost-free distribution of goods to charitable organizations or for community events. (Finding 1, page 10.)

Department officials accepted our recommendation and stated that they will update the Department's policy and will include guidelines for approving promotional distributions of merchandise for specific purposes.

FAILURE TO COLLECT RETAILERS' OCCUPATION TAX

The Department did not collect Retailers' Occupation Tax (sales tax) on sales to non-governmental and other non-exempt organizations. Most of the Correctional Industries' sales appear to have been made to governmental and not-for-profit organizations which are tax-exempt

under Illinois law. However, some sales were made to organizations which were not tax-exempt organizations (i.e., motorcycle clubs and fraternal organizations). The total possible sales tax not collected cannot be readily determined.

The Retailers' Occupation Tax Act defines retail sales and provides for exemptions for government or for charitable, religious, or educational purposes.

It is the Department's responsibility to establish procedures to determine if an organization is exempt from sales tax by obtaining the organization's active sales tax identification number.

We recommended the Department establish procedures to determine if an organization is subject to or exempt from Retailers' Occupation Tax and charge all taxes where applicable. (Finding 2, page 12.)

While looking into the requirements to implement our recommendation, Illinois Correctional Industries' officials became aware of an Illinois Administrative Code rule which states that sales made in the performance of a governmental function are exempt from the Retailers' Occupation Tax. Since Correctional Industries sells products manufactured through inmate labor pursuant to Statute, the Department of Corrections legal staff believe that all Correctional Industries' sales are tax-exempt. The Department has requested an official opinion from the Illinois Department of Revenue to determine the tax status of these sales.

OTHER FINDINGS

The remaining finding is considered less significant at this time and has been given appropriate attention by the Department. We will review progress towards the implementation of our recommendation in our next audit.

Responses were provided by Mr. Mark B. Krell, CIA, Chief Internal Auditor for the Department.

AUDITORS' OPINION

Our auditors state that the June 30, 1994 financial statements for the Correctional Industries are fairly presented.



WILLIAM G. HOLLAND, Auditor General

WGH:JHL:jr
April 25, 1995

SUMMARY OF AUDIT FINDINGS

<u>Number of</u>	<u>1994 Audit</u>	<u>1992 Audit</u>
Audit Findings	3	4
Repeated Audit Findings	0	0
Prior Recommendations Implemented or Not Repeated	4	1

SPECIAL ASSISTANT AUDITORS

Our special assistant auditors for this engagement were Sikich, Gardner & Co. , LLP.