STATE OF ILLINOIS
DEPARTMENT OF HEALTHCARE AND FAMILY SERVICES

FINANCIAL AUDIT

For the Year Ended June 30, 2016

Performed as Special Assistant Auditors
for the Auditor General, State of Illinois

STATE OF ILLINOIS
DEPARTMENT OF HEALTHCARE AND FAMILY SERVICES

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For the Year Ended June 30, 2016

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STATE OF ILLINOIS
DEPARTMENT OF HEALTHCARE AND FAMILY SERVICES

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AGENCY OFFICIALS

Director	Felicia Norwood
Assistant Director	Vacant
Deputy Directors	
Community Outreach	Vacant
Administrative Operations	Richard Foxman
Human Resources	Vacant
Strategic Planning	Michael Taylor
General Counsel	Mollie Zito
Inspector General	Bradley Hart
Administrators	
Division of Child Support Services	Pamela Lowry
Division of Finance	Michael Casey
Division of Medical Programs	Vacant (through 7/31/15) Teresa Hursey (Acting 8/1/15 – Current)
Division of Personnel and Administrative Services	Terri Shawgo
Chiefs	
Office of Legislative Affairs	Shawn McGady
Office of Fiscal Management	Jack Dodds
Office of Information Services	Vacant (through 8/31/15) Julie Hagele (9/1/15 – Current)

Department administrative offices are located at:

201 South Grand Avenue East
Springfield, IL 62763

2200 Churchill Road
Springfield, IL 62702

401 S. Clinton
Chicago, IL 60607

FINANCIAL STATEMENT REPORT

SUMMARY

The audit of the accompanying financial statements of the State of Illinois, Department of Healthcare and Family Services (Department) was performed by Sikich LLP.

Based on their audit, the auditors expressed an unmodified opinion on the Department's basic financial statements.

SUMMARY OF FINDINGS

The auditors identified matters involving the Department's internal control over financial reporting that they considered to be material weaknesses. The material weaknesses are described in the accompanying Schedule of Findings on pages 45-53 of this report as items 2016-001 (Inaccurate determination of eligibility), 2016-002 (Lack of control over the Integrated Eligibility System), 2016-003 (Lack of adequate controls over the review of internal controls over service providers) and 2016-004 (Financial statement preparation).

EXIT CONFERENCE

The findings and recommendations appearing in this report were discussed with Department personnel and the Department waived an exit conference.

The responses to the recommendations were provided by Felicia F. Norwood, Director, in correspondence dated February 21, 2017.

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Decatur, Illinois 62523

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INDEPENDENT AUDITOR'S REPORT

Honorable Frank J. Mautino
Auditor General
State of Illinois

Report on the Financial Statements

As Special Assistant Auditors for the Auditor General, we have audited the accompanying financial statements of the governmental activities, the major fund, and the aggregate remaining fund information of the State of Illinois, Department of Healthcare and Family Services, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the State of Illinois, Department of Healthcare and Family Services' basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial 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 financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the major fund, and the aggregate remaining fund information for the State of Illinois, Department of Healthcare and Family Services, as of June 30, 2016, and the respective changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 2, the financial statements of the State of Illinois, Department of Healthcare and Family Services are intended to present the financial position and the changes in financial position of only that portion of the governmental activities, the major fund, and the aggregate remaining fund information of the State that is attributable to the transactions of the State of Illinois, Department of Healthcare and Family Services. They do not purport to, and do not, present fairly the financial position of the State of Illinois as of June 30, 2016, and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

As discussed in Note 14 to the financial statements, the State of Illinois, Department of Healthcare and Family Services' financial statements have been restated, as of July 1, 2015, to correct prior year misstatements. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Management has omitted management's discussion and analysis and budgetary comparison information for any of its funds and related pension and other postemployment benefit information for its Department-wide financial statements that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the State of Illinois, Department of Healthcare and Family Services' basic financial statements. The combining General Fund schedules and nonmajor and agency funds financial statements are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The combining General Fund schedules and nonmajor and agency funds financial statements are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the accompanying combining General Fund schedules and nonmajor and agency funds financial statements are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated February 21, 2017 on our consideration of the State of Illinois, Department of Healthcare and Family Services' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the State of Illinois, Department of Healthcare and Family Services' internal control over financial reporting and compliance.

Restricted Use of this Auditor's Report

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, the Comptroller, and Department management and is not intended to be and should not be used by anyone other than these specified parties.

SIGNED ORIGINAL ON FILE

Decatur, Illinois
February 21, 2017

Statement of Net Position and Governmental Funds Balance Sheet

June 30, 2016 (Expressed in Thousands)

	General Fund	Other Nonmajor Funds	Total Governmental Funds	Adjustments	Statement of Net Position
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES					
Unexpended appropriations	$ 1,213,340	$ 122,392	$ 1,335,732	$ -	$ 1,335,732
Cash equity with State Treasurer	926,471	18,553	945,024	-	945,024
Cash and cash equivalents	9,888	-	9,888	-	9,888
Securities lending collateral equity with State Treasurer	99,711	1,211	100,922	-	100,922
Due from other government - federal	1,174,964	113,526	1,288,490	-	1,288,490
Due from other government - local	83,768	-	83,768	-	83,768
Taxes receivable, net	38,394	-	38,394	-	38,394
Other receivables, net	454,592	9,289	463,881	-	463,881
Due from other Department funds	49	-	49	(49)	-
Due from other State funds	4,950	340	5,290	-	5,290
Due from State of Illinois component units	5,448	-	5,448	-	5,448
Prepaid expenses	-	-	-	379	379
Capital assets not being depreciated	-	-	-	85,878	85,878
Capital assets being depreciated, net	-	-	-	2,179	2,179
Total assets	4,011,575	265,311	4,276,886	88,387	4,365,273
Deferred outflows of resources - SERS pensions	-	-	-	140,206	140,206
Total assets and deferred outflows of resources	$ 4,011,575	$ 265,311	$ 4,276,886	228,593	4,505,479
LIABILITIES AND DEFERRED INFLOWS OF RESOURCES					
Accounts payable and accrued liabilities	$ 2,324,510	$ 149,426	$ 2,473,936	-	2,473,936
Due to other government - federal	447,556	5,575	453,131	-	453,131
Due to other government - local	207,685	27,833	235,518	-	235,518
Due to other State fiduciary funds	473	1,066	1,539	-	1,539
Due to other Department funds	-	49	49	(49)	-
Due to other State funds	37,751	18,785	56,536	-	56,536
Due to State of Illinois component units	50,318	1,869	52,187	-	52,187
Unearned revenue	75	-	75	-	75
Obligations under securities lending of State Treasurer	99,711	1,211	100,922	-	100,922
Long-term obligations:					
Due within one year	-	-	-	997	997
Due subsequent to one year	-	-	-	9,622	9,622
Net pension liability - SERS	-	-	-	1,011,915	1,011,915
Total liabilities	3,168,079	205,814	3,373,893	1,022,485	4,396,378

Statement of Net Position and Governmental Funds Balance Sheet

June 30, 2016 (Expressed in Thousands)

	General Fund	Other Nonmajor Funds	Total Governmental Funds	Adjustments	Statement of Net Position
Unavailable revenue - Federal operating grants	$ 768,356	$ 23,427	$ 791,783	$ (791,783)	$ -
Unavailable revenue - License and fees	884	248	1,132	(1,132)	-
Unavailable revenue - Medical provider assessment tax	3,899	-	3,899	(3,899)	-
Unavailable revenue - Other taxes	1,137	-	1,137	(1,137)	-
Unavailable revenue - Other operating grants	81,179	-	81,179	(81,179)	-
Unavailable revenue - Other revenues	16,055	-	16,055	(16,055)	-
Deferred inflows of resources - SERS pensions	-	-	-	68,497	68,497
Total deferred inflows of resources	871,510	23,675	895,185	(826,688)	68,497
Total liabilities and deferred inflows of resources	4,039,589	229,489	4,269,078	195,797	4,464,875
FUND BALANCES (DEFICITS)/NET POSITION					
Restricted for health and social services	-	-	-	-	-
Committed for health and social services	824,419	43,198	867,617	(867,617)	-
Unassigned	(852,433)	(7,376)	(859,809)	859,809	-
Net investment in capital assets	-	-	-	88,046	88,046
Restricted net position	-	-	-	-	-
Unrestricted net position	-	-	-	(47,442)	(47,442)
Total fund balances (deficits)/net position	(28,014)	35,822	7,808	$ 32,796	$ 40,604
Total liabilities, deferred inflows of resources and fund balances (deficits)	$ 4,011,575	$ 265,311	$ 4,276,886		

The accompanying notes to the financial statements are an integral part of this statement.

State of Illinois
Department of Healthcare and Family Services
Reconciliation of Governmental Funds Balance Sheet
to Statement of Net Position
June 30, 2016
(Expressed in Thousands)

Total fund balances (deficits)-governmental funds	$	7,808
Amounts reported for governmental activities in the Statement of Net Position are different because:		
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.		88,057
Prepaid expenses for governmental activities are current uses of financial resources for funds.		379
Revenues in the Statement of Activities that do not provide current financial resources are deferred in the funds.		895,185
Deferred outflows of resources related to pension liability are not reported in the governmental funds since they do not provide current financial resources.		140,206
Deferred inflows of resources related to pension liability are not reported in the governmental funds since they do not use current financial resources.		(68,497)
Some liabilities reported in the Statement of Net Position do not require the use of current financial resources and, therefore, are not reported as liabilities in governmental funds. These activities consist of:		
Capital lease obligations		(11)
Compensated absences		(10,608)
Net pension liability - SERS		(1,011,915)
Net position of governmental activities	$	40,604

The accompanying notes to the financial statements are an integral part of this statement.

Statement of Activities and Governmental Revenues, Expenditures, and Changes in Fund Balances

For the Year Ended June 30, 2016 (Expressed in Thousands)

	General Fund	Other Nonmajor Funds	Total Governmental Funds	Adjustments	Statement of Activities
Expenditures/expenses:					
Health and social services	$ 16,464,859	$ 312,126	$ 16,776,985	$ 70,378	$ 16,847,363
Debt service principal	24	8	32	(32)	-
Debt service interest	13	3	16	-	16
Capital outlays	24,810	-	24,810	(24,810)	-
Total expenditures/expenses	16,489,706	312,137	16,801,843	45,536	16,847,379
Program revenues:					
Charges for services:					
Licenses and fees	28,777	1,476	30,253	(1,559)	28,694
Other	-	13,419	13,419	-	13,419
Total charges for services	28,777	14,895	43,672	(1,559)	42,113
Operating grant revenue:					
Federal	10,445,581	196,507	10,642,088	(281,308)	10,360,780
Other	966,304	-	966,304	43,893	1,010,197
Total operating grant revenue	11,411,885	196,507	11,608,392	(237,415)	11,370,977
Net program revenues (expenses)	(5,049,044)	(100,735)	(5,149,779)	(284,510)	(5,434,289)
General revenues:					
Interest and investment income	1,429	17	1,446	-	1,446
Medical provider assesment tax	1,375,891	-	1,375,891	237	1,376,128
Other taxes	435,233	-	435,233	412	435,645
Other	49,808	-	49,808	(17,774)	32,034
Total general revenues	1,862,361	17	1,862,378	(17,125)	1,845,253
Other sources (uses):					
Appropriations from State resources	7,141,509	200,600	7,342,109	30,174	7,372,283
Lapsed appropriations	(1,139,465)	(65,026)	(1,204,491)	-	(1,204,491)
Receipts collected and transmitted to State Treasury	(2,823,610)	(16,862)	(2,840,472)	-	(2,840,472)
Capital transfers from other State agencies	-	-	-	6,479	6,479
Amount of SAMS transfers-in	(80,000)	-	(80,000)	-	(80,000)
Amount of SAMS transfers-out	45,000	-	45,000	-	45,000
Transfers-in	10,324	-	10,324	-	10,324
Transfers-out	(40,000)	-	(40,000)	-	(40,000)
Total other sources (uses)	3,113,758	118,712	3,232,470	36,653	3,269,123
Change in fund balances/net position	(72,925)	17,994	(54,931)	(264,982)	(319,913)
Fund balances (deficits)/net position, July 1, 2015, as restated	44,911	17,828	62,739	297,778	360,517
Fund balances (deficits)/net position, June 30, 2016	$ (28,014)	$ 35,822	$ 7,808	$ 32,796	$ 40,604

The accompanying notes to the financial statements are an integral part of this statement.

State of Illinois
Department of Healthcare and Family Services
Reconciliation of Statement of Revenues, Expenditures and Changes in Fund Balances of Governmental Funds to Statement of Activities
For the Year Ended June 30, 2016
(Expressed in Thousands)

Net change in fund balances - governmental funds	$ (54,931)
Amounts reported for governmental activities in the Statement of Activities are different because:	
Governmental funds report capital outlays as expenditures while governmental activities report depreciation expense to allocate those expenditures over the life of the assets. This is the amount by which capital outlays exceeded depreciation in the current period.	23,832
Some capital assets were transferred in from other State agencies and, therefore, were transferred at no cost.	6,479
Prepaid expenses in the Statement of Activities are not reported as expenses in governmental funds.	(255)
Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenues in the funds. This amount represents the decrease in unavailable revenue over the prior year.	(256,099)
Deferred inflows of resources related to pension liability in the Statement of Activities that do not use current financial resources are not reported in the governmental funds. This amount represents the increase in deferred inflows over the prior year.	(29,261)
Deferred outflows of resources related to pension liability in the Statement of Activities that do not provide current financial resources are not reported in the governmental funds. This amount represents the decrease in deferred outflows over the prior year.	(19,157)
Some expenses reported in the Statement of Activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. Also, some expenditures reported in governmental funds decrease the amount of certain long-term liabilities reported on the Statement of Net Position and are therefore reported as expenses in the Statement of Activities. These include:	
Decrease in compensated absences obligation	666
Decrease in capital lease obligation	32
Decrease in net pension liability - SERS	8,781
Change in net position of governmental activities	$ (319,913)

The accompanying notes to the financial statements are an integral part of this statement.

State of Illinois

Department of Healthcare and Family Services

Statement of Fiduciary Net Position

June 30, 2016 (Expressed in Thousands)

		Agency Funds
ASSETS		
Cash equity with State Treasurer	$	16,697
Cash and cash equivalents		1,688
Other receivables, net		207,079
Due from other State funds		1
Total assets	$	225,465
LIABILITIES		
Accounts payable and accrued liabilities	$	19,496
Other liabilities		205,969
Total liabilities	$	225,465

The accompanying notes to the financial statements are an integral part of this statement.

(1) Organization

The Department of Healthcare and Family Services (Department) is a part of the executive branch of government of the State of Illinois (State) and operates under the authority of and review by the Illinois General Assembly. The Department operates under a budget approved by the General Assembly in which resources primarily from the State's General Revenue Fund are appropriated for the use of the Department. Activities of the Department are subject to the authority of the Office of the Governor, the State's chief executive officer, and other departments of the executive and legislative branches of government (such as the Department of Central Management Services, the Governor's Office of Management and Budget, the State Treasurer's Office, and the State Comptroller's Office) as defined by the Illinois General Assembly. All funds appropriated to the Department and all other cash received are under the custody and control of the State Treasurer, with the exception of the Child Support Enforcement Trust Fund – SDU.

The Department is organized to provide for the improvement of the lives of Illinois' families through healthcare coverage and child support enforcement.

(2) Summary of Significant Accounting Policies

The financial statements of the Department have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP), as prescribed by the Governmental Accounting Standards Board (GASB). To facilitate the understanding of data included in the financial statements, summarized below are the more significant accounting policies.

(a) Financial Reporting Entity

As defined by GAAP, the financial reporting entity consists of a primary government, as well as its component units, which are legally separate organizations for which the elected officials of the primary government are financially accountable. Financial accountability is defined as:

1) Appointment of a voting majority of the component unit's board and either (a) the primary government's ability to impose its will, or (b) the possibility that the component unit will provide a financial benefit to or impose a financial burden on the primary government; or

2) Fiscal dependence on the primary government and the possibility that the component unit will provide a financial benefit to or impose a financial burden on the primary government.

Based upon the required criteria, the Department has no component units and is not a component unit of any other entity. However, because the Department is not legally separate from the State of Illinois, the financial statements of the Department are included in the financial statements of the State of Illinois. The State of Illinois' Comprehensive Annual Financial Report may be obtained by writing to the State Comptroller's Office, Division of Financial Reporting, 325 West Adams Street, Springfield, Illinois, 62704-1871.

(b) Basis of Presentation

The financial statements of the State of Illinois, Department of Healthcare and Family Services, are intended to present the financial position and the changes in financial position of only that portion of the governmental activities, major fund, and the aggregate remaining fund information of the State of Illinois that is attributable to the transactions of the Department. They do not purport to, and do not, present fairly the financial position of the State of Illinois as of June 30, 2016, and the changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The financial activities of the Department, which consist only of governmental activities, are reported under the health and social services function in the State of Illinois' Comprehensive Annual Financial Report. For reporting purposes, the Department has combined the fund and government-wide financial statements using a columnar format that reconciles individual line items of the fund financial data to government-wide data in a separate column. A brief description of the Department's government-wide and fund financial statements is as follows:

Government-wide Statements. The government-wide statement of net position and statement of activities report the overall financial activity of the Department, excluding fiduciary activities. Eliminations have been made to minimize the double-counting of internal activities of the Department. The financial activities of the Department consist of governmental activities, which are generally financed through taxes and intergovernmental revenues.

The statement of net position presents the assets, deferred outflows of resources, liabilities and deferred inflows of resources of the Department's governmental activities with the difference being reported as net position. The assets and liabilities are presented in order of their relative liquidity by class of asset or liability with liabilities whose average maturities are greater than one year reported in two components – the amount due within one year and the amount due in more than one year.

The statement of activities presents a comparison between direct expenses and program revenues for the functions of the Department's governmental activities. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include (a) charges paid by the recipients of goods or services offered by the programs and (b) grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues.

Fund Financial Statements. The fund financial statements provide information about the Department's funds, including fiduciary funds. Separate statements for each fund category – governmental and fiduciary – are presented. The emphasis on fund financial statements is the major governmental fund, which is displayed in a separate column. All remaining governmental funds are aggregated and reported as nonmajor funds.

The Department administers the following major governmental fund (or portions thereof in the case of shared funds – see note 2 (d)) of the State:

> **General** – This is the State's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund. The services which are administered by the Department and accounted for in the General Fund include, among others, promoting access to quality healthcare and child support. Certain resources obtained from federal grants and used to support general governmental activities are accounted for in the General Fund consistent with applicable legal requirements. The Department's portion of the General Fund is composed of seven primary sub-accounts (General Revenue, U of I Hospital Services, County Provider Trust, Long-Term Care Provider, Hospital Provider, Drug Rebate and Healthcare Provider Relief) and nine secondary sub-accounts.

Additionally, the Department reports the following fund types:

Governmental Fund Types:

> **Special Revenue** – These funds account for transactions related to resources obtained from specific revenue sources that are restricted or committed to expenditures for specific purposes other than debt service or capital projects.

Fiduciary Fund Types:

Agency – These funds account for transactions related to assets collected by the Department, acting in the capacity of an agent, for distribution to other governmental units or designated beneficiaries.

(c) Measurement Focus and Basis of Accounting

The government-wide and fiduciary fund financial statements are reported using the economic resources measurement focus (except for agency funds which do not have a measurement focus) and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flow takes place. Non-exchange transactions, in which the Department gives (or receives) value without directly receiving (or giving) equal value in exchange, include nursing home assessments, hospital assessments and intergovernmental grants. On an accrual basis, revenues from the nursing home assessments are recognized in the fiscal year in which the underlying exchange transaction occurs. Revenue from grants, entitlements, and similar items are recognized in the fiscal year in which all eligibility requirements imposed by the provider have been met.

Governmental funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collected within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the State considers revenues to be available if they are collected within 60 days of the end of the current fiscal year. Expenditures generally are recorded when the liability is incurred, as under accrual accounting. However, principal and interest on formal debt issues, claims and judgments, and compensated absences are recorded only when the payment is due. Capital asset acquisitions are reported as expenditures in governmental funds. Proceeds of general long-term debt and acquisitions under capital leases are reported as other financing sources.

Significant revenue sources which are susceptible to accrual include the nursing home assessment, hospital assessments, federal matching revenues, drug rebates, intergovernmental transfer agreement revenues, and child support. Other miscellaneous revenue sources are considered to be measurable and available only when cash is received.

(d) Shared Fund Presentation

The financial statement presentation for the General Revenue, Care Provider for Persons with Developmental Disabilities, and Trauma Center Accounts of the General Fund, the Department of Corrections Reimbursement and Education Fund, and the Tobacco Settlement Recovery Fund, nonmajor governmental funds, represent only the portion of the shared fund that can be directly attributed to the operations of the Department. Financial statements for total fund operations of the shared State funds are presented in the State of Illinois' Comprehensive Annual Financial Report.

In presenting these financial statements, certain unique accounts are used for the presentation of shared funds. The following accounts are used in these financial statements to present the Department's portion of shared funds:

Unexpended Appropriations

This "asset" account represents lapse period warrants issued between July and September for fiscal year 2016, in accordance with the Statewide Accounting Management System (SAMS) records, plus any liabilities relating to obligations re-appropriated to the subsequent fiscal year.

Appropriations from State Resources

The "other financing source" account represents the final legally adopted appropriation according to SAMS records. In fiscal year 2016, the Department did not receive an appropriation from the General Assembly for General Revenue Fund spending. The appropriation amount included in the financial statements was derived from the consent decrees *Beeks v. Bradley* (Case No. 92 C 4204) and *Memisovski v. Maram* (Case No. 92 C 1982) issued by the United States District Court for the Northern District of Illinois Eastern Division (Case Numbers 92 C 1982 and 92 C 4204). The order required the Department to continue to pay all Medicaid providers to ensure access to medical services for Illinois' Medicaid clients.

Lapsed Appropriations

Lapsed appropriations are the legally adopted appropriations less net warrants issued for the 15 month period from July to September of the following year and re-appropriations to subsequent years according to SAMS records. Lapsed appropriations for certain Medicaid expenditures are the legally adopted appropriations less net warrants issued for the 16 month period from July to October of the following year.

Receipts Collected and Transmitted to State Treasury

This "other financing use" account represents all cash receipts received during the fiscal year from SAMS records.

Amount of SAMS Transfers-In

This "other financing use" account represents cash transfers made by the Office of the Comptroller in accordance with statutory provisions to the corresponding fund during the fiscal year per SAMS records in which the Department did not make a deposit into the State Treasury.

Amount of SAMS Transfers-Out

This "other financing source" account represents cash transfers made by the Office of the Comptroller in accordance with statutory provision from the corresponding fund during the fiscal year per SAMS records in which a legally adopted appropriation was not charged.

(e) Eliminations

Eliminations have been made in the government-wide statement of net position to minimize the "grossing-up" effect on assets and liabilities within the governmental activities column of the Department. As a result, amounts reported in the governmental funds balance sheet as interdepartmental interfund receivables and payables have been eliminated in the government-wide statement of net position. Amounts reported in the governmental funds balance sheet as receivable from or payable to fiduciary funds have been included in the government-wide statement of net position as receivable from and payable to external parties, rather than as internal balances.

(f) Cash and Cash Equivalents

Cash equivalents are defined as short-term, highly liquid investments readily convertible to cash with maturities of less than 90 days at the time of purchase. Cash and cash equivalents include cash on hand and cash in banks for locally held funds.

(g) Investments

Investments are reported at fair value.

(h) Interfund Transactions and Transactions with State of Illinois Component Units

The Department has the following types of interfund transactions between Department funds and funds of other State Agencies:

***Services provided and used* –** sales and purchases of goods and services between funds for a price approximating their external exchange value. Interfund services provided and used are reported as revenues in seller funds and expenditures or expenses in purchaser funds. Unpaid amounts are reported as interfund receivables and payables in the governmental funds balance sheet and the government-wide statement of net position.

***Reimbursements* –** repayments from the funds responsible for particular expenditures or expenses to the funds that initially paid for them. Reimbursements are reported as expenditures in the reimbursing fund and as a reduction of expenditures in the reimbursed fund.

Transfers – flows of assets (such as cash or goods) without equivalent flows of assets in return and without a requirement for repayment. In governmental funds, transfers are reported as other financing uses in the funds making transfers and as other financing sources in the funds receiving transfers.

The Department also has activity with the University of Illinois, a State of Illinois component unit, for medical programs and intergovernmental transfer agreements administered by the University.

(i) Capital Assets

Capital assets, which includes property, plant, and equipment and intangible assets, are reported at cost or estimated historical cost based on appraisals. Contributed assets are reported at acquisition value at the time received. Capital assets are depreciated and amortized using the straight-line method. Intangible assets (purchased computer software and internally generated computer software) are assets that do not have a physical existence, are nonfinancial in nature, are not in a monetary form, and have a useful life of over one year.

Capitalization thresholds and the estimated useful lives are as follows:

Capital Asset Category	Capitalization Threshold	Estimated Useful Life (in Years)
Equipment	$ 5,000	3-10
Purchased Computer Software	$ 25,000	3-5
Internally Generated Computer Software	$1,000,000	5-20

(j) Deferred Outflows/Inflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net assets that applies to a future period(s) and so will not be recognized as an outflow of resources (expense) until then. In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net assets that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The Department has recorded deferred outflows and inflows of resources in the government-wide financial statements in connection with the liability of net pension liability reported and explained in Note 8. Unavailable revenues in governmental funds include receivables not "available" to finance the current period.

(k) Compensated Absences

The liability for compensated absences reported in the government-wide statement of net position consists of unpaid, accumulated vacation and sick leave balances for Department employees. A liability for these amounts is reported in governmental funds only if they have matured, for example, as a result of employee resignations and retirements. The liability has been calculated using the vesting method, in which leave amounts for both employees who currently are eligible to receive termination payments and other employees who are expected to become eligible in the future to receive such payments upon termination are included. The liability has been calculated based on the employees' current salary level and includes salary related cost (e.g., Social Security and Medicare taxes).

Legislation that became effective January 1, 1998 capped the paid sick leave for all State Employees' Retirement System members at December 31, 1997. Employees continue to accrue twelve sick days per year, but will not receive monetary compensation for any additional time earned after December 31, 1997. Sick days earned between 1984 and December 31, 1997 (with a 50% cash value) would only be used after all days with no cash value are depleted. Any sick days earned and unused after December 31, 1997 will be converted to service time for purposes of calculating employee pension benefits.

(l) Pensions

In accordance with the Department's adoption of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27,* and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68*, the net pension liability, deferred outflows of resources, deferred inflows of resources and pension expense have been recognized in the government-wide financial statements.

The net pension liability is calculated as the difference between the actuarially calculated value of the projected benefit payments attributed to past periods of service and the plan's fiduciary net position. The total pension expense is comprised of the service cost or actuarial present value of projected benefit payments attributed to the valuation year, interest on the total pension liability, plan administrative expenses, current year benefit changes, and other changes in plan fiduciary net position less employee contributions and projected earnings on plan investments. Additionally, the total pension expense includes the annual recognition of outflows and inflows of resources due to pension assets and liabilities.

For purposes of measuring the net pension liability, deferred outflows of resources, deferred inflows of resources, pension expense and expenditures associated with the Department's contribution requirements, information about the fiduciary net position of the plan and additions to/deductions from the plan's fiduciary net position have been determined on the same basis as they are reported within the separately issued plan financial statements. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with terms of the plan. Investments are reported at fair value.

(m) Fund Balances

In the fund financial statements, governmental funds report fund balances in the following categories:

Nonspendable- This consists of amounts that cannot be spent because they are either a) not in spendable form or b) legally or contractually required to be maintained intact.

Restricted- This consists of amounts that are restricted to specific purposes, that is, when constraints placed on the use of resources are either: a) externally imposed by creditors, grantors, contributors, or laws or regulations of other governments or b) imposed by law through constitutional provisions or enabling legislation.

Committed- This consists of amounts that can only be used for specific purposes pursuant to constraints imposed by formal action of the Department's highest level of decision-making authority. Committed amounts cannot be used for any other purpose unless the Department removes or changes the specified use by taking the same type of action it employed to previously commit those amounts. The Department's highest level of decision-making authority rests with the Illinois State legislature and the Governor. The State passes "Public Acts" to commit their fund balances.

Assigned- This consists of net amounts that are constrained by the Department's intent to be used for specific purposes, but that are neither restricted nor committed.

Unassigned- This consists of residual fund balance that has not been restricted, committed, or assigned within the General Fund and deficit fund balances of other governmental funds.

In the General Fund, it is the Department's policy to consider restricted resources to have been spent first when an expenditure is incurred for which both restricted and unrestricted (i.e. committed, assigned or unassigned) fund balances are available, followed by committed and then assigned fund balances. Unassigned amounts are used only after the other resources have been used.

In other governmental funds (special revenue), it is the Department's policy to consider restricted resources to have been spent last. When an expenditure is incurred for purposes for which both restricted and unrestricted fund balances are available, the Department first utilizes any assigned amounts, followed by committed and then restricted amounts.

(n) Net Position

In the government-wide statement of net position, net position is displayed in three components as follows:

Net investment in capital assets – This consists of capital assets, net of accumulated depreciation less the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.

Restricted – This consists of net position that is legally restricted by outside parties or by law through constitutional provisions or enabling legislation. When both restricted and unrestricted resources are available for use, generally it is the State's policy to use restricted resources first, then unrestricted resources when they are needed.

Unrestricted – This consists of net position that does not meet the definition of "restricted" or "net investment in capital assets."

(o) Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, deferred outflows of resources, liabilities, deferred inflows of resources, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(p) Adoption of New Accounting Pronouncements

Effective for the year ending June 30, 2016, the Department adopted the following GASB statements:

- GASB Statement No. 72, *Fair Value Measurement and Application*, which addresses accounting and financial reporting issues related to fair value measurements and provides guidance for determining a fair value measurement for financial reporting purposes. This statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. The implementation of this statement had no financial impact on the Department's net position or results of operations.

- The Department adopted the portion of GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68,* which is intended to improve usefulness of information about pensions included in the general purpose external financial reports of state and local governments for making decisions and assessing accountability for pensions that are within the scope of GASB Statement No. 67 and GASB Statement No. 68. The implementation of this statement had no financial impact on the Department's net position or results of operations.

- GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, which is intended to improve financial reporting for governments by establishing a framework for the evaluation of accounting guidance that will result in governments applying that guidance with less variation. This statement will improve the usefulness of financial statement information for making decisions and assessing accountability and enhance the comparability of financial statement information among governments. This statement also is intended to improve implementation guidance by elevating its authoritative status to a level that requires it be exposed for a period of broad public comment prior to issuance, as is done for other GASB pronouncements. The implementation of this statement had no financial impact on the Department's net position or results of operations.

- GASB Statement No. 79, *Certain External Investment Pools and Pool Participants,* which is intended to improve financial reporting for governments by superseding the accounting and financial reporting standards for 2a7-like external investment pools. This statement documents the criteria for qualifying external investment pools to elect to measure all of their investments at amortized cost. The implementation of this statement had no financial impact on the Department's net position or results of operations.

(q) Future Adoption of GASB Statements

Effective for the year ending June 30, 2017, the Department will adopt the following GASB statements:

- The portion of GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That are Not Within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68,* which addresses accounting and financial reporting by employers and governmental non-employer contributing entities for pensions that are not within the scope of GASB Statement No. 68.

- GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* which replaces GASB Statement No. 43, addresses the financial reports of defined other postemployment benefit (OPEB) plans that are administered through trusts that meet specified criteria. This statement follows the framework for financial reporting of defined benefit OPEB plans in GASB Statement No. 45 by requiring a statement of fiduciary net position and a statement of changes in fiduciary net position. This statement requires more extensive note disclosures and required supplementary information (RSI) related to the measurement of the OPEB liabilities for which assets have been accumulated, including information about the annual money-weighted rates of return on plan investments. GASB Statement No. 74 also sets forth note disclosure requirements for defined contribution OPEB plans.

- GASB Statement No. 77, *Tax Abatement Disclosures*, which is intended to improve financial reporting by requiring disclosure of tax abatement information about a reporting government's own tax abatement agreements and those that are entered into by other governments and that reduce the reporting government's tax revenues.

- GASB Statement No. 78, *Pensions Provided through Certain Multi-Employer Defined Benefit Pension Plans*, which addresses a practice issue regarding the scope and applicability of GASB Statement No. 68. This issue is associated with pensions provided through certain multiple-employer defined benefit pension plans and to state or local government employers whose employees are provided with such pensions. This statement amends the scope and applicability of GASB Statement 68 to exclude pensions provided to employees of state or local governmental employers through a cost–sharing multiple-employer defined benefit pension plan that is not a state or local governmental pension plan, is used to provide defined benefit pensions both to employees of state or local governmental employers and to employees of employers that are not state or local governmental employers, and has no predominant state or local governmental employer (either individually or collectively with other state or local governmental employers that provide pension through the pension plan). This statement establishes requirements for recognition and measurement of pension expense, expenditures, and liabilities; note disclosures; and required supplementary information for pensions that have the characteristics described above.

- GASB Statement No. 80, *Blending Requirements for Certain Component Units – an amendment of GASB Statement No. 14* which amends the blending requirements for the financial statement presentation of component units of all state and local governments. The additional criterion requires blending of a component unit incorporated as a not-for-profit corporation in which the primary government is the sole corporate member.

- GASB Statement No. 82, *Pension Issues – an amendment of GASB Statements No. 67, No. 68, and No. 73*, which addresses certain issues that have been raised with respect to Statements No. 67, *Financial Reporting for Pension Plans*, No. 68, *Accounting and Financial Reporting for Pensions*, and No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. Specifically, this statement addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements.

Effective for the year ending June 30, 2018, the Department will adopt the following GASB statements:

- GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* replaces the requirements of GASB Statement No. 45 and requires governments to report a liability on the face of the financial statements for the OPEB they provide. This statement requires governments in all types of OPEB plans to present more extensive note disclosures and RSI about their

OPEB liabilities. Among the new note disclosures is a description of the effect on the reported OPEB liability of using a discount rate and a healthcare cost trend rate that are one percentage point higher and one percentage point lower than assumed by the government. The new RSI includes a schedule showing the causes of increases and decreases in the OPEB liability and a schedule comparing a government's actual OPEB contributions to its contribution requirements.

- GASB Statement No. 81, *Irrevocable Split-Interest Agreements*, which is intended to meet the objective of improving accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement.

The Department has not yet determined the impact of adopting these statements on its financial statements.

(3) Deposits and Investments

(a) Deposits

The State Treasurer is the custodian of the State's cash and cash equivalents for funds maintained in the State Treasury. Deposits in the custody of the State Treasurer are pooled and invested with other State funds in accordance with the Deposit of State Moneys Act of the Illinois Compiled Statutes (15 ILCS 520/11). Funds held by the State Treasurer have not been categorized as to credit risk because the Department does not own individual securities. Detail on the nature of these deposits and investments are available within the State of Illinois' Comprehensive Annual Financial Report.

Cash on deposit for locally held funds of fiduciary activities had carrying amounts and bank balances of $1.688 million and $11.346 million, respectively, at June 30, 2016. Balances in excess of FDIC depository insurance were covered by collateral held by an agent in the Department's name.

(b) Investments

Section 2 of the Public Funds Investment Act limits the State's investments outside the State Treasury to securities of the U.S. government or its agencies, short-term obligations of domestic corporations exceeding $500 million in assets that are rated in the three highest categories by at least two nationally recognized statistical ratings organizations not to exceed ten percent of the domestic corporations outstanding obligations, money market mutual funds invested in the U.S. government and/or its agencies, and repurchase agreements securities of the U.S. government or its agencies or money market mutual funds invested in the U.S. government or its agencies. Investments of public funds in a Public Treasurers' Investment Pool created under Section 17 of the State Treasurer Act are also permitted.

As of June 30, 2016, the Department had the following investments outside of the State Treasury:

	Fair Value (Thousands)	Weighted Average Maturity (Years)
Governmental Activities		
Illinois Public Treasurer's Investment Pool	$9,888	0.122
Total fixed income investments	$9,888	

Interest Rate Risk: The Department does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk: The Department does not have a formal investment policy that limits investment choices. The Illinois Public Treasurers' Investment Pool were rated AAAm by Standard & Poor's.

(c) Reconciliation to Statement of Net Position and Statement of Fiduciary Net Position

The Statement of Net Position and the Statement of Fiduciary Net Position account cash and cash equivalents contains certain short-term investments (included as investments above) to reflect their liquidity. A reconciliation (amounts expressed in thousands) follows:

	Deposits	Investments
Governmental Activities		
Amount per note	$ -	$ 9,888
Cash equivalents	9,888	(9,888)
Amounts per Statement of Net Position	$ 9,888	$ -
Fiduciary Funds		
Cash on deposit	$ 11,346	$ -
Outstanding checks	(9,658)	-
Amounts per Statement of Fiduciary Net Position	$ 1,688	$ -

(4) Accounts Receivable

(a) Taxes Receivable

Taxes receivable (amounts expressed in thousands) at June 30, 2016 are as follows:

	General Fund
Taxes receivable	$ 52,714
Less: allowance for uncollectible taxes	(14,320)
Taxes receivable, net	$ 38,394

(b) Other Receivables

Other receivables (amounts expressed in thousands) at June 30, 2016 are as follows:

	General Fund	Nonmajor Governmental Funds	Fiduciary Funds
Other receivables	$ 546,478	$ 735,178	$4,978,601
Less: allowance for uncollectible accounts	(91,886)	(725,889)	(4,771,522)
Other receivables, net	$ 454,592	$ 9,289	$ 207,079

(5) Interfund Balances and Activity

(a) Balances due to/from Other Funds

The following balances (amounts expressed in thousands) at June 30, 2016 represent amounts due from Department funds and other State funds.

	Due from		
Fund	**Other Department Funds**	**Other State Funds**	**Description/Purpose**
General	$ 49	$ 4,950	Due from other Department funds and other State Funds for subgrants received.
Nonmajor governmental funds	-	340	Due from other State Funds for subgrants received.
Fiduciary funds	-	1	Due from other State Funds for subgrants received.
	$ 49	$ 5,291	

The following balances (amounts expressed in thousands) at June 30, 2016 represent amounts due to Department funds, other State funds and other State fiduciary funds for purchases of services.

	Due to		
Fund	**Other Department Funds**	**Other State Funds**	**Other State Fiduciary Funds**
General	$ -	$ 37,751	$ 473
Nonmajor governmental funds	49	18,785	1,066
	$ 49	$ 56,536	$ 1,539

(b) Transfers to/from Other Funds

Interfund transfers in (amounts expressed in thousands) for the year ended June 30, 2016 were as follows:

Fund	Transfers In from Other State Funds	Description/Purpose
General	$ 10,324	Transfer from other State agencies' General Fund.
	$ 10,324	

Interfund transfers out (amounts expressed in thousands) for the year ended June 30, 2016 were as follows:

Fund	Transfers Out to Other State Funds	Description/Purpose
General	$ 40,000	Transfers to other State agencies' funds per State appropriation.
	$ 40,000	

(c) *Balances Due to/from State of Illinois Component Units*

The following balances (amounts expressed in thousands) at June 30, 2016 represent amounts due from State of Illinois Component Units to the General Fund for intergovernmental agreement reimbursements.

	Due From
Component Unit	General Fund
Southern Illinois University	$ 1,911
University of Illinois	3,537
	$ 5,448

The following balances (amounts expressed in thousands) at June 30, 2016 represent amounts due to State of Illinois Component Units for medical reimbursements.

	Due To	
Component Unit	General Fund	Nonmajor Governmental Funds
Illinois State University	$ 9	$ 1
Northern Illinois University	1,186	46
Illinois Toll Highway Authority	1	-
Illinois Housing Develop Authority	-	63
Southern Illinois University	6,691	-
University of Illinois	42,431	1,759
	$ 50,318	$ 1,869

(6) Capital Assets

Capital asset activity (amounts expressed in thousands) for the year ended June 30, 2016 is as follows:

	Balance July 1, 2015	Additions	Deletions	Net Transfers	Balance June 30, 2016
Governmental Activities:					
Capital assets not being depreciated/amortized:					
Internally generated intangible assets in development	$ 54,589	$ 24,810	$ -	$ 6,479	$ 85,878
Total capital assets not being depreciated/amortized:	54,589	24,810	-	6,479	85,878
Capital assets being depreciated:					
Equipment	5,549	-	54	-	5,495
Non-internally generated software	2,878	-	-	-	2,878
Less accumulated depreciation:					
Equipment	4,036	407	54	-	4,389
Non-internally generated software	1,234	571	-	-	1,805
Total capital assets being depreciated, net	3,157	(978)	-	-	2,179
Governmental activity capital assets, net	$ 57,746	$ 23,832	$ -	$ 6,479	$ 88,057

Depreciation expense for governmental activities (amounts expressed in thousands) for the year ended June 30, 2016 was charged as follows:

Health and social services	$ 978

(7) Long-Term Obligations

Changes in Long-Term Obligations

Changes in long-term obligations (amounts expressed in thousands) for the year ended June 30, 2016 was as follows:

	Balance July 1, 2015	Additions	Deletions	Balance June 30, 2016	Amounts Due Within One Year
Governmental Activities:					
Compensated absences	$ 11,274	$ 11,334	$ 12,000	$ 10,608	$ 986
Capital Leases	43	-	32	11	11
Net Pension Liability	1,020,696	-	8,781	1,011,915	-
Total governmental Activities	$ 1,032,013	$ 11,334	$ 20,813	$ 1,022,534	$ 997

Compensated absences will be liquidated by the applicable governmental funds that account for the salaries and wages of the related employees. Net pension liabilities will be liquidated through the General Revenue Fund, and the special revenue funds that report wages. The capital lease obligations will be liquidated primarily by the General Revenue Fund.

Capital Leases

The Department has acquired certain office equipment through capital lease arrangements. Future debt service requirements under capital leases (amounts expressed in thousands) at June 30, 2016 were as follows:

Year Ending June 30,	Principal	Interest	Total
2017	$ 11	$ 1	$ 12
	$ 11	$ 1	$ 12

(8) Defined Benefit Pension Plan

Plan Description. Substantially all of the Department's full-time employees who are not eligible for participation in another state-sponsored retirement plan participate in the State Employees' Retirement System (SERS), which is a single-employer defined benefit pension trust fund in the State of Illinois reporting entity. SERS is governed by article 14 of the Illinois Pension Code (40 ILCS 5/1, et al.). The plan consists of two tiers of contribution requirements and benefit levels based on when an employee was hired. Members who first become an employee and participate under any of the State's retirement plans on or after January 1, 2011 are members of Tier 2, while Tier 1 consists of employees hired before January 1, 2011 or those who have service credit prior to January 1, 2011. The provisions below apply to both Tier 1 and 2 members, except where noted. The SERS issues a separate CAFR available at www.srs.illinois.gov or that may be obtained by writing to the SERS, 2101 South Veterans Parkway, Springfield, Illinois, 62794-9255.

Benefit Provisions. SERS provides retirement benefits based on the member's final average compensation and the number of years of credited service that have been established. The retirement benefit formula available to general State employees is 1.67% for each year of covered service and 2.2% for each year of non-covered service. The maximum retirement annuity payable is 75% of final average compensation as calculated under the regular formula. The minimum monthly retirement annuity payable is $15.00 for each year of covered employment and $25.00 for each year of non-covered employment.

Participants in SERS under the regular formula Tier 1 and Tier 2 receive the following levels of benefits based on the respective age and years of service credits.

<table>
<tr><th>Regular Formula Tier 1</th><th>Regular Formula Tier 2</th></tr>
<tr><td>A member must have a minimum of eight years of service credit and may retire at:

• Age 60, with 8 years of service credit.
• Any age, when the member's age (years & whole months) plus years of service credit (years & whole months) equal 85 years (1,020 months) (Rule of 85) with eight years of credited service.
• Between ages 55-60 with 25-30 years of service credit (reduced 1/2 of 1% for each month under age 60).</td><td>A member must have a minimum of 10 years of credited service and may retire at:
• Age 67, with 10 years of credited service.
• Between ages 62-67 with 10 years of credited service (reduced 1/2 of 1% for each month under age 67).

The retirement benefit is based on final average compensation and credited service. For regular formula employees, final average compensation is the average of the 96 highest consecutive months of service within the last 120 months of service. The retirement benefit is calculated on a maximum salary of $106,800.</td></tr>
</table>

The retirement benefit is based on final average compensation and credited service. Final average compensation is the 48 highest consecutive months of service within the last 120 months of service. Under the Rule of 85, a member is eligible for the first 3% increase on January 1 following the first full year of retirement, even if the member is not age 60. If the member retires at age 60 or older, he/she will receive a 3% pension increase every year on January 1, following the first full year of retirement. If the member retires before age 60 with a reduced retirement benefit, he/she will receive a 3% pension increase every January 1 after the member turns age 60 and has been retired at least one full year. These pension increases are not limited by the 75% maximum.	This amount increases annually by 3% or one-half of the Consumer Price Index, whichever is less. If the member retires at age 67 or older, he/she will receive a pension increase of 3% or one-half of the Consumer Price Index for the preceding calendar year, whichever is less, every year on January 1, following the first full year of retirement. The calendar year 2015 rate is $111,572. If the member retires before age 67 with a reduced retirement benefit, he/she will receive a pension increase of 3% or one-half of the Consumer Price Index for the preceding calendar year, whichever is less, every January 1 after the member turns age 67 and has been retired at least one full year. These pension increases are not limited by the 75% maximum.

Additionally, the Plan provides an alternative retirement formula for State employees in high-risk jobs, such as State policemen, fire fighters, and security employees. Employees qualifying for benefits under the alternative formula may retire at an earlier age depending on membership in Tier 1 or Tier 2. The retirement formula is 2.5% for each year of covered service and 3.0% for each year of non-covered service. The maximum retirement annuity payable is 80% of final average compensation as calculated under the alternative formula.

SERS also provides occupational and non-occupational (including temporary) disability benefits. To be eligible for non-occupational (including temporary) disability benefits, an employee must have at least eighteen months of credited service to the System. The non-occupational (including temporary) disability benefit is equal to 50% of the monthly rate of compensation of the employee on the date of removal from the payroll. Occupational disability benefits are provided when the member becomes disabled as a direct result of injuries or diseases arising out of and in the course of State employment. The monthly benefit is equal to 75% of the monthly rate of compensation on the date of removal from the payroll. This benefit amount is reduced by Workers' Compensation or payments under the Occupational Diseases Act.

Occupational and non-occupational death benefits are also available through the System. Certain non-occupational death benefits vest after eighteen months of credited service. Occupational death benefits are provided from the date of employment.

Contributions. Contribution requirements of active employees and the State are established in accordance with Chapter 40, section 5/14-133 of the Illinois Compiled Statutes. Member contributions are based on fixed percentages of covered payroll ranging between 4.00% and 12.50%. Employee contributions are fully refundable, without interest, upon withdrawal from State employment. Tier 1 members contribute based on total annual compensation. Tier 2 members contribute based on an annual compensation rate not to exceed $106,800 with limitations for future years increased by the lessor of 3% or one-half of the annual percentage increase in the Consumer Price Index. For 2016, this amount was $111,572.

The State is required to make payment for the required departmental employer contributions, all allowances, annuities, any benefits granted under Chapter 40, Article 5/14 of the ILCS and all administrative expenses of the System to the extent specified in the ILCS. State law provides that the employer contribution rate be determined based upon the results of each annual actuarial valuation.

For fiscal year 2016, the required employer contributions were computed in accordance with the State's funding plan. This funding legislation provides for a systematic 50-year funding plan with an ultimate goal to achieve 90% funding of the plan's liabilities. In addition, the funding plan provided for a 15-year phase-in period to allow the State to adapt to the increased financial commitment. Since the 15-year phase-in period ended June 30, 2010, the State's contribution will remain at a level percentage of payroll for the next 35 years until the 90% funded level is achieved. For fiscal year 2016, the employer contribution rate was 45.598%. The Department's contribution amount for fiscal year 2016 was $36.848 million.

Pension liability, deferred outflows of resources, deferred inflows of resources and expense related to pensions. At June 30, 2016, the Department reported a liability of $1,011.915 million for its proportionate share of the State's net pension liability for SERS on the statement of net position. The net pension liability was measured as of June 30, 2015 (current year measurement date), and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The Department's portion of the net pension liability was based on the Department's proportion of employer contributions relative to all employer contributions made to the plan during the year ended June 30, 2015. As of the current year measurement date of June 30, 2015, the Department's proportion was 3.6129%, which was a decrease of .153% from its proportion measured as of the prior year measurement date of June 30, 2014.

For the year ended June 30, 2016, the Department recognized pension expense of $106.659 million. At June 30, 2016, the Department reported deferred outflows and deferred inflows of resources related to the pension liability from the following sources (amounts expressed in thousands):

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ 3,078	$ 13,137
Changes of assumptions	74,241	-
Net difference between projected and actual investment earnings on pension plan investments	-	15,326
Changes in proportion	26,039	40,033
Department contributions subsequent to the measurement date	36,848	-
Total	$ 140,206	$ 68,497

$36.848 million reported as deferred outflows of resources related to pensions resulting from Department contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2017. Other amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized as pension expense as follows (amounts expressed in thousands):

Year ended June 30,	
2017	$ 16,975
2018	16,975
2019	3,683
2020	(2,772)
Total	$ 34,862

Actuarial Methods and Assumptions. The total pension liability was determined by an actuarial valuation as of June 30, 2015, using the following actuarial assumptions, applied to all periods included in the measurement:

Mortality: 105 percent of the RP2014 Healthy Annuitant mortality table, sex distinct, with rates projected to 2015.

Inflation: 3.0%

Investment Rate of Return: 7.25%, net of pension plan investment expense, including inflation.

Salary increases: Salary increase rates based on age related productivity and merit rates plus inflation.

Post-retirement benefit increases of 3.00%, compounded, for Tier 1 and the lessor of 3.00% or one-half of the annual increase in the Consumer Price Index for Tier 2.

Retirement Age: Experience-based table of rates specific to the type of eligibility condition. Table was last updated for the June 30, 2014, valuation pursuant to an experience study of the period July 1, 2009 to June 30, 2013.

The long-term expected real rate of return on pension plan investments was determined based on the simulated average 10-year annualized geometric return for each major asset class. These returns are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage. For each major asset class that is included in the pension plan's target asset allocation, calculated as of the measurement date of June 30, 2015, the best estimates of the geometric real rates of return as summarized in the following table:

Asset Class	**Target Allocation**	**Long-Term Expected Real Rate of Return**
U.S. Equity	30%	5.69%
Fixed Income	20%	1.62%
Hedge Funds	10%	4.00%
International Equity	20%	6.23%
Real Estate	10%	5.50%
Infrastructure	5%	6.00%
Private Equity	5%	10.10%
Total	**100%**	**5.03%**

Discount Rate. A discount rate of 7.02% was used to measure the total pension liability as of the measurement date of June 30, 2015 as compared to a discount rate of 7.09% used to measure the total pension liability as of the prior year measurement date. The June 30, 2015 single blended discount rate was based on the expected rate of return on pension plan investments of 7.25% and a municipal bond rate of 3.80%, based on an index of 20 year general obligation bonds with an average AA credit rating as published by the Federal Reserve. The projection of cash flows used to determine this single discount rate assumed that plan member contributions will be made at the current contribution rate and that contributions will be made based on the statutorily required rates under Illinois law. Based on these assumptions, the pension plan's fiduciary net position and future contributions will be sufficient to finance the benefit payments through the year 2067. As a result, the long-term expected rate of return on pension plan investments was applied to projected benefit payments through the year 2067, and the municipal bond rate was applied to all benefit payments after that date.

Sensitivity of the Net Pension Liability to Changes in the Discount Rate. The net pension liability for the plan was calculated using the stated discount rate, as well as what the net pension liability would be if it were calculated using a discount rate that is 1-percentage point lower or 1-percentage point higher than the current rate as shown below (amounts expressed in thousands):

	1% Decrease 6.02%	Discount Rate 7.02%	1% Increase 8.02%
Department's Proportionate Share of the Net Pension Liability	$ 1,218,178	$ 1,011,915	$ 840,701

Payables to the pension plan. At June 30, 2016, the Department reported a payable of $1.539 million to SERS for the outstanding amount of contributions to the pension plans required for the year ended June 30, 2016.

(9) Postemployment Benefits

The State provides health, dental, vision, and life insurance benefits for retirees and their dependents in a program administered by the Department of Central Management Services. Substantially all State employees become eligible for these other postemployment benefits ("OPEB") if they eventually become annuitants of one of the State sponsored pension plans.

The health, dental, and vision benefits provided to and contribution amounts required from annuitants are the result of collective bargaining between the State and the various unions representing the State's and the university component units' employees in accordance with the limitations established in the Act. Therefore, the benefits provided and contribution amounts are subject to periodic change. Annuitants may be required to contribute towards health, dental and vision benefits with the amount based on factors such as date of retirement, years of credited service with the State, whether the annuitant is covered by Medicare, and whether the annuitant has chosen a managed health care plan. Annuitants who retired prior to January 1, 1998, and who are vested in the State Employees Retirement System do not contribute towards health, dental and vision benefits. For annuitants who retired on or after January 1, 1998, the annuitant's contribution amount is reduced five percent for each year of credited service with the State allowing those annuitants with twenty or more years of credited service to not have to contribute towards health, dental and vision benefits. The State also provides life insurance benefits for annuitants equal to their annual salary as of the last day of employment until age 60, at which time the benefit amount becomes $5,000.

The total cost of the State's portion of health, dental, vision, and life insurance benefits of all members, including post-employment health, dental, vision, and life insurance benefits, is recognized as expenditure by the State in the Illinois Comprehensive Annual Financial Report. The State finances the costs on a pay-as-you-go basis. The total costs incurred for health, dental, vision, and life insurance benefits are not separated by department or component unit for annuitants and their dependents nor active employees and their dependents.

A summary of post-employment benefits provisions, changes in benefit provisions, employee eligibility requirements including eligibility for vesting, and the authority under which benefit provisions are established are included as an integral part of the financial statements of the Department of Central Management Services. A copy of the financial statements of the Department of Central Management Services may be obtained by writing to the Department of Central Management Services, 715 Stratton Building, 401 South Spring Street, Springfield, Illinois, 62606-4100.

(10) Fund Deficits

The following funds had a deficit balance at June 30, 2016 (amounts expressed in thousands):

		Fund Deficit
Major Governmental Funds:		
General Revenue Fund (0001)	$	28,014
Nonmajor Governmental Funds:		7,376
Child Support Administrative Fund (0757)		

The deficits are expected to be recovered from future years' State appropriations and federal funds.

(11) Risk Management

The Department is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; workers compensation and natural disasters. The State retains the risk of loss (i.e., self-insured) for these risks except computer equipment insurance purchased by the Department.

Liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported (IBNR). Claims liabilities are based upon the estimated ultimate cost of settling the claims including specific, incremental claim adjustment expenses, salvage, and subrogation and considering the effects of inflation and recent claim settlement trends including frequency and amount of payouts and other economic and social factors.

The Department's risk management activities for self-insurance, unemployment insurance and workers' compensation are financed through appropriations to the Illinois Department of Central Management Services and are accounted for in the General Fund of the State. The claims are not considered to be a liability of the Department, and accordingly, have not been reported in the Department's financial statements for the year ended June 30, 2016.

(12) Commitments and Contingencies

(a) Operating Leases

The Department leases equipment, buildings and office space under terms of noncancelable operating lease agreements not extending past the end of the fiscal year, that require the Department to make minimum lease payments plus pay a pro rata share of certain operating costs. Rent expense under operating leases was $4.8 million for the year ended June 30, 2016.

(b) Federal Funding

In October 2004, the U.S. Department of Health and Human Services Office of Inspector General (OIG) issued its reports, "Review of Illinois Medicaid Disproportionate Share Hospital Payments to the University of Illinois at Chicago Hospital" and "Review of Illinois Medicaid Disproportionate Share Hospital Payments to Mount Sinai Hospital of Chicago". The reports recommended that the State refund $140.282 million and $4.516 million respectively, in FFP to the federal government because of alleged overpayment to the hospitals of $280.6 million and $9.032 million above the hospital-specific limitation on Disproportionate Share Hospital (DSH) payments to the hospitals during State FY 1997-2000. The State has strongly disagreed with the OIG's findings. The Centers for Medicare and Medicaid Services (CMS) concurred with the audit finding but stated "we interpret this recommendation as a prospective resolution and not a requirement to recoup any Federal payments associated with these findings". After approximately 12 years of no official action, in July 2016, the State received a formal disallowance from CMS for these two audits. It is the State's position that it has followed CMS published guidelines, and its methodology for calculating the hospital-specific limitation has consistently been approved by CMS. The State is in the process of appealing the matter.

The Department receives other federal grants which are subject to review and audit by federal grantor agencies. Certain costs could be questioned as not being an eligible expenditure under the terms of the grants. At June 30, 2016, other than identified above, there were no material questioned costs that have not been resolved with the federal awarding agencies. However, questioned costs could still be identified during audits to be conducted in the future. Management of the Department believes there will be no material adjustments to the federal grants and, accordingly, has not recorded a provision for possible repayment.

(c) Litigation

A class action lawsuit existed at June 30, 2016 consisting of all past, present, and future participants in the Medically Fragile and Technology Dependent (MFTD) Medicaid Waiver for Children. The suit seeks to not have the individual's services reduced solely because the individual "ages-out" of the waiver at twenty-one upon being referred to a program with different service levels than the MFTD. An estimate of the possible loss cannot be made.

A class action lawsuit existed at June 30, 2016. This is a class action brought on behalf of children who receive home-based skilled nursing services through the Department's Nursing and Personal Care Services (NPCS) program. The suit argues the Department has engaged in a systematic effort to unfairly reduce or deny their approved services of affected NPCS participants. An estimate of the possible loss cannot be made.

A class action lawsuit existed at June 30, 2016. This lawsuit seeks class certification for "all recipients of Medicaid in the State of Illinois with behavioral or emotional disorders under the age of twenty-one who are not receiving medically necessary home and community-based services to treat or ameliorate their disorders, and are currently segregated, or who have been segregated or at risk of segregation for the purpose of receiving treatment and services and who would not oppose community services." The Plaintiffs explicitly seek to require the provision of appropriate services and support to qualified persons in the community. It may also seek to require residential treatment of children in Psychiatric Residential Treatment Facilities (PRTFs) under Early, Periodic, Screening, Diagnosis, & Treatment (EPSDT). An estimate of the possible loss cannot be made.

A class action lawsuit existed at June 30, 2016. This is a class action brought on behalf of children who have been approved for in-home shift nursing services, but who are not receiving shift nursing at the level approved. The suit seeks to require that all steps necessary be taken to ensure class members receive all nursing services for which they are approved. An estimate of the possible loss cannot be made.

(13) Securities Lending Transactions

The State Treasurer lends securities to broker-dealers and other entities for collateral that will be returned for the same securities in the future. The State Treasurer has, through a Securities Lending Agreement, authorized Deutsche Bank AG to lend the State Treasurer's securities to broker-dealers and banks pursuant to a form of loan agreement.

During fiscal year 2016, Deutsche Bank AG lent U.S. Treasury and U.S. Agency securities and received as collateral U.S. dollar denominated cash. Borrowers were required to deliver collateral for each loan equal to at least 100% of the aggregated fair value of the loaned securities. Loans are marked to market daily. If the fair value of collateral falls below 100%, the borrower must provide additional collateral to raise the fair value to 100%.

The State Treasurer did not impose any restrictions on loan amounts of available and eligible securities during fiscal year 2016. In the event of borrower default, Deutsche Bank AG provides the State Treasurer with counterparty default indemnification. In addition, Deutsche Bank AG is obligated to indemnify the State Treasurer if Deutsche Bank AG loses any securities, collateral or investments of the State Treasurer in Deutsche Bank AG's custody. Moreover, there were no losses during fiscal year 2016 resulting from a default of the borrowers or Deutsche Bank AG.

During fiscal year 2016, the State Treasurer and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested in repurchase agreements with approved counterparties collateralized with securities approved by Deutsche Bank AG and marked to market daily at no less than 102%. Because the loans are terminable at will, their duration did not generally match the duration of the investments made with the cash collateral. The State Treasurer had no credit risk as a result of its securities lending program as the collateral held exceeded the fair value of the securities lent. The securities lending collateral invested in repurchase agreements and the fair value of securities on loan for the State Treasurer as of June 30, 2016 were $2,603,015,000 and $2,587,869,617, respectively.

In accordance with GASB Statement No. 28, paragraph 9, the Office of the State Treasurer has allocated the assets and obligations at June 30, 2016 arising from securities lending agreements to the various funds of the State. The total allocated to the Department at June 30, 2016 was $100.922 million for governmental activities.

(14) Prior Period Adjustment

The Agency's financial statements have been restated as of July 1, 2015. During the implementation of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27* in the prior year, the amount reported as net pension liability – SERS was understated by $35.181 million and therefore net position was overstated. In addition, the Department discovered that between April 1, 2009 and June 30, 2015, medical costs covered under Title XIX were incorrectly claimed as Title XXI costs. Due to the difference in federal financial participation (FFP) rates between the programs, it was determined $81.897 million was due to the federal government as of June 30, 2015, resulting in an overstatement of fund balance and net position. As a result of these issues, the financial statements have been restated as of July 1, 2015, as shown in the table below.

	General Fund (Thousands)	Governmental Activities (Thousands)
Fund balance/net position, July 1, 2015, as previously reported	$ 126,808	$ 477,595
Adjustment to net pension liability – SERS	-	(35,181)
Adjustment to amount due to federal government	(81,897)	(81,897)
Fund balance/net position, July 1, 2015, as restated	$ 44,911	$ 360,517

(15) Subsequent Event

The Department is part of the executive branch of government and operates under a budget where resources are appropriated for the use of the Department. As of the date these financial statements were available to be issued, the State of Illinois had adopted a six-month budget for fiscal year 2017. The partial year "stopgap" budget was signed into law on June 30, 2016 and provides funding for six months through December 2016. Payments to

Department employees for work performed and medical assistance payments will be paid from the six month budget, but will be paid from court orders if a budget is not passed for the remainder of the year.

Combining Schedule of Accounts - General Fund

June 30, 2016 (Expressed in Thousands)

	General Revenue 0001	U of I Hospital Services 0136	County Provider Trust 0329	Care Provider for Persons with DD 0344	Long-Term Care Provider 0345	Hospital Provider 0346	Special Education Medicaid Matching 0355	Trauma Center 0397	Public Aid Recoveries Trust 0421
ASSETS									
Unexpended appropriations	$ 1,210,902	$ -	$ -	$ 22	$ -	$ -	$ -	$ 2,416	$ -
Cash equity with State Treasurer	989	30,831	15,318	-	35,204	183,118	-	-	358,738
Cash and cash equivalents	9,888	-	-	-	-	-	-	-	-
Securities lending collateral equity with State Treasurer	-	5,358	3,065	-	7,969	46,402	-	-	-
Due from other government - federal	317,096	26,300	50,230	8,785	66,591	226,768	40,628	1,571	30,396
Due from other government - local	-	-	83,757	-	-	-	11	-	-
Taxes receivable, net	-	-	-	386	30,266	5,099	-	-	-
Other receivables, net	3,895	10	6	-	14	83	-	-	387,714
Due from other Department funds	49	-	-	-	-	-	-	-	-
Due from other State funds	39	-	-	-	27	-	-	-	713
Due from State of Illinois component units	-	3,537	-	-	-	-	-	-	-
Total assets	$ 1,542,858	$ 66,036	$ 152,376	$ 9,193	$ 140,071	$ 461,470	$ 40,639	$ 3,987	$ 777,561
LIABILITIES AND DEFERRED INFLOWS OF RESOURCES									
Accounts payable and accrued liabilities	$ 1,749,874	$ -	$ 96	$ 19	$ 128,043	$ 227,317	$ 20	$ 2,088	$ 28,144
Due to other government - federal	203,723	-	7	-	1,706	2,071	-	-	66
Due to other government - local	10,113	-	149,127	-	2,261	-	40,619	328	3,802
Due to other State fiduciary funds	-	-	44	2	10	-	-	-	411
Due to other Department funds	552	-	-	-	-	-	-	-	663,572
Due to other State funds	10,385	-	37	1	82	-	-	-	9,193
Due to State of Illinois component units	13,017	25,791	-	-	-	-	-	-	2,757
Unearned revenue	-	-	-	-	-	-	-	-	-
Obligations under securities lending of State Treasurer	-	5,358	3,065	-	7,969	46,402	-	-	-
Total liabilities	1,987,664	31,149	152,376	22	140,071	275,790	40,639	2,416	707,945
Unavailable revenue - Federal operating grants	206,655	24,560	13,452	8,785	51,677	226,200	6,879	341	939
Unavailable revenue - License and fees	883	-	-	-	-	-	-	-	-
Unavailable revenue - Medical provider assessment tax	-	-	-	-	3,899	-	-	-	-
Unavailable revenue - Other taxes	-	-	-	-	279	-	-	-	-
Unavailable revenue - Other operating grants	-	3,537	75,731	-	-	-	-	-	-
Unavailable revenue - Other revenues	962	-	-	-	-	-	-	-	-
Total deferred inflows of resources	208,500	28,097	89,183	8,785	55,855	226,200	6,879	341	939
Total liabilities and deferred inflows of resources	2,196,164	59,246	241,559	8,807	195,926	501,990	47,518	2,757	708,884
FUND BALANCES (DEFICITS)									
Restricted for health and social services	-	-	-	-	-	-	-	-	-
Committed for health and social services	-	6,790	-	386	-	-	-	1,230	68,677
Unassigned	(653,306)	-	(89,183)	-	(55,855)	(40,520)	(6,879)	-	-
Total fund balances (deficits)	(653,306)	6,790	(89,183)	386	(55,855)	(40,520)	(6,879)	1,230	68,677
Total liabilities, deferred inflows of resources and fund balances (deficits)	$ 1,542,858	$ 66,036	$ 152,376	$ 9,193	$ 140,071	$ 461,470	$ 40,639	$ 3,987	$ 777,561

State of Illinois

Department of Healthcare and Family Services

Combining Schedule of Accounts - General Fund

June 30, 2016 (Expressed in Thousands)

	Electronic Health Record Incentive 0503	Juvenile Rehab Services Medicaid Matching 0575	Medical Interagency Program 0720	Drug Rebate 0728	Medicaid Buy-in Program Revolving 0740	Healthcare Provider Relief 0793	Medical Special Purposes Trust 0808	Eliminations	Total
ASSETS									
Unexpended appropriations	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 1,213,340
Cash equity with State Treasurer	4,297	6	7,754	50,655	837	233,346	5,378	-	926,471
Cash and cash equivalents	-	-	-	-	-	-	-	-	9,888
Securities lending collateral equity with State Treasurer	-	-	837	13,408	213	22,459	-	-	99,711
Due from other government - federal	-	91	5,323	413	-	399,437	1,335	-	1,174,964
Due from other government - local	-	-	-	-	-	-	-	-	83,768
Taxes receivable, net	-	-	-	-	-	2,643	-	-	38,394
Other receivables, net	-	-	2	24	60	62,784	-	-	454,592
Due from other Department funds	-	-	552	663,572	-	-	-	(664,124)	49
Due from other State funds	-	-	4,171	-	-	-	-	-	4,950
Due from State of Illinois component units	-	-	1,911	-	-	-	-	-	5,448
Total assets	$ 4,297	$ 97	$ 20,550	$ 728,072	$ 1,110	$ 720,669	$ 6,713	$ (664,124)	$ 4,011,575
LIABILITIES AND DEFERRED INFLOWS OF RESOURCES									
Accounts payable and accrued liabilities	$ 3,808	$ -	$ 12,500	$ 88,396	$ 13	$ 83,311	$ 881	$ -	$ 2,324,510
Due to other government - federal	-	-	-	239,981	1	-	1	-	447,556
Due to other government - local	251	97	455	-	-	632	-	-	207,685
Due to other State fiduciary funds	-	-	-	-	6	-	-	-	473
Due to other Department funds	-	-	-	-	-	-	-	(664,124)	-
Due to other State funds	-	-	-	-	4	18,039	10	-	37,751
Due to State of Illinois component units	238	-	6,758	28	-	1,040	689	-	50,318
Unearned revenue	-	-	-	-	-	-	75	-	75
Obligations under securities lending of State Treasurer	-	-	837	13,408	213	22,459	-	-	99,711
Total liabilities	4,297	97	20,550	341,813	237	125,481	1,656	(664,124)	3,168,079
Unavailable revenue - Federal operating grants	-	90	4,689	413	-	222,731	945	-	768,356
Unavailable revenue - License and fees	-	-	-	-	1	-	-	-	884
Unavailable revenue - Medical provider assessment tax	-	-	-	-	-	-	-	-	3,899
Unavailable revenue - Other taxes	-	-	-	-	-	858	-	-	1,137
Unavailable revenue - Other operating grants	-	-	1,911	-	-	-	-	-	81,179
Unavailable revenue - Other revenues	-	-	-	-	-	15,093	-	-	16,055
Total deferred inflows of resources	-	90	6,600	413	1	238,682	945	-	871,510
Total liabilities and deferred inflows of resources	4,297	187	27,150	342,226	238	364,163	2,601	(664,124)	4,039,589
FUND BALANCES (DEFICITS)									
Restricted for health and social services	-	-	-	-	-	-	-	-	-
Committed for health and social services	-	-	-	385,846	872	356,506	4,112	-	824,419
Unassigned	-	(90)	(6,600)	-	-	-	-	-	(852,433)
Total fund balances (deficits)	-	(90)	(6,600)	385,846	872	356,506	4,112	-	(28,014)
Total liabilities, deferred inflows of resources and fund balances (deficits)	$ 4,297	$ 97	$ 20,550	$ 728,072	$ 1,110	$ 720,669	$ 6,713	$ (664,124)	$ 4,011,575

State of Illinois
Department of Healthcare and Family Services

Combining Schedule of Revenues, Expenditures and Changes in Fund Balance - General Fund

For the Year Ended June 30, 2016 (Expressed in Thousands)

	General Revenue 0001	U of I Hospital Services 0136	County Provider Trust 0329	Care Provider for Persons with DD 0344	Long-Term Care Provider 0345	Hospital Provider 0346	Special Education Medicaid Matching 0355	Trauma Center 0397	Public Aid Recoveries Trust 0421
REVENUES									
Operating grants - federal	$ 3,205,697	$ 79,957	$ 1,408,910	$ 15,565	$ 177,311	$ 1,496,759	$ 160,028	$ 4,632	$ 91,315
Other operating grants	243,700	18,255	702,149	-	-	-	-	-	-
Licenses and fees	28,107	-	-	-	-	-	-	-	-
Other charges for services	-	-	-	-	-	-	-	-	48,258
Interest and other investment income	3	67	54	-	124	660	-	-	-
Medical provider assessment tax	-	-	-	17,537	173,012	1,185,342	-	-	-
Other taxes	-	-	-	-	18,828	-	-	-	-
Other	3,046	-	-	-	-	-	-	-	-
Total revenues	3,480,553	98,279	2,111,113	33,102	369,275	2,682,761	160,028	4,632	139,573
EXPENDITURES									
Health and social services	6,490,178	128,244	2,117,408	206	390,179	2,669,819	166,907	9,094	138,003
Debt service principal	16	-	-	-	-	-	-	-	-
Debt service interest	9	-	-	-	-	-	-	-	-
Capital outlays	2,723	-	-	-	-	-	-	-	190
Total expenditures	6,492,926	128,244	2,117,408	206	390,179	2,669,819	166,907	9,094	138,193
Excess (deficiency) of revenues over (under) expenditures	(3,012,373)	(29,965)	(6,295)	32,896	(20,904)	12,942	(6,879)	(4,462)	1,380
OTHER SOURCES (USES) OF FINANCIAL RESOURCES									
Appropriations from State resources	7,125,304	-	-	1,205	-	-	-	15,000	-
Lapsed appropriations	(1,132,546)	-	-	(1,013)	-	-	-	(5,906)	-
Receipts collected and transmitted to State Treasury	(2,784,798)	-	-	(34,222)	-	-	-	(4,590)	-
Amount of SAMS transfers-in	(80,000)	-	-	-	-	-	-	-	-
Amount of SAMS transfers-out	45,000	-	-	-	-	-	-	-	-
Transfers-in	80,000	45,000	-	-	30,000	-	-	-	-
Transfers-out	(36,678)	-	-	-	(20,000)	(180,000)	-	-	-
Net other sources (uses) of financial resources	3,216,282	45,000	-	(34,030)	10,000	(180,000)	-	4,504	-
Net change in fund balances	203,909	15,035	(6,295)	(1,134)	(10,904)	(167,058)	(6,879)	42	1,380
Fund balances (deficits), July 1, 2015	(857,215)	(8,245)	(82,888)	1,520	(44,951)	126,538	-	1,188	67,297
FUND BALANCES (DEFICITS), JUNE 30, 2016	$ (653,306)	$ 6,790	$ (89,183)	$ 386	$ (55,855)	$ (40,520)	$ (6,879)	$ 1,230	$ 68,677

State of Illinois
Department of Healthcare and Family Services

Combining Schedule of Revenues, Expenditures and Changes in Fund Balance - General Fund

For the Year Ended June 30, 2016 (Expressed in Thousands)

	Electronic Health Record Incentive 0503	Juvenile Rehab Services Medicaid Matching 0575	Medical Interagency Program 0720	Drug Rebate 0728	Medicaid Buy-in Program Revolving 0740	Healthcare Provider Relief 0793	Medical Special Purposes Trust 0808	Eliminations	Total
REVENUES									
Operating grants - federal	$ 36,107	$ 116	$ 25,475	$ (2,138)	$ -	$ 3,744,198	$ 1,649	$ -	$ 10,445,581
Other operating grants	-	-	2,175	-	-	-	25	-	966,304
Licenses and fees	-	-	-	-	670	-	-	-	28,777
Other charges for services	-	-	-	-	-	-	-	(48,258)	-
Interest and other investment income	-	-	34	246	3	238	-	-	1,429
Medical provider assessment tax	-	-	-	-	-	-	-	-	1,375,891
Other taxes	-	-	-	-	-	416,405	-	-	435,233
Other	-	-	-	-	-	46,762	-	-	49,808
Total revenues	36,107	116	27,684	(1,892)	673	4,207,603	1,674	(48,258)	13,303,023
EXPENDITURES									
Health and social services	36,107	111	40,778	(95,323)	217	4,419,249	1,940	(48,258)	16,464,859
Debt service principal	-	-	-	-	-	8	-	-	24
Debt service interest	-	-	-	-	-	4	-	-	13
Capital outlays	-	-	-	-	231	21,468	198	-	24,810
Total expenditures	36,107	111	40,778	(95,323)	448	4,440,729	2,138	(48,258)	16,489,706
Excess (deficiency) of revenues over (under) expenditures	-	5	(13,094)	93,431	225	(233,126)	(464)	-	(3,186,683)
OTHER SOURCES (USES) OF FINANCIAL RESOURCES									
Appropriations from State resources	-	-	-	-	-	-	-	-	7,141,509
Lapsed appropriations	-	-	-	-	-	-	-	-	(1,139,465)
Receipts collected and transmitted to State Treasury	-	-	-	-	-	-	-	-	(2,823,610)
Amount of SAMS transfers-in	-	-	-	-	-	-	-	-	(80,000)
Amount of SAMS transfers-out	-	-	-	-	-	-	-	-	45,000
Transfers-in	-	-	2,002	-	-	50,000	-	(196,678)	10,324
Transfers-out	-	-	-	-	-	-	-	196,678	(40,000)
Net other sources (uses) of financial resources	-	-	2,002	-	-	50,000	-	-	3,113,758
Net change in fund balances	-	5	(11,092)	93,431	225	(183,126)	(464)	-	(72,925)
Fund balances (deficits), July 1, 2015	-	(95)	4,492	292,415	647	539,632	4,576	-	44,911
FUND BALANCES (DEFICITS), JUNE 30, 2016	$ -	$ (90)	$ (6,600)	$ 385,846	$ 872	$ 356,506	$ 4,112	$ -	$ (28,014)

State of Illinois

Department of Healthcare and Family Services

Combining Balance Sheet - Nonmajor Governmental Funds

June 30, 2016 (Expressed in Thousands)

	Special Revenue					
	Provider Inquiry Trust 0341	Money Follows the Person Budget Transfer 0522	Department of Corrections Reimbursement and Education 0523	Tobacco Settlement Recovery 0733	Child Support Administrative 0757	Total
ASSETS						
Unexpended appropriations	$ -	$ -	$ -	$ 122,392	$ -	$ 122,392
Cash equity with State Treasurer	1,701	4,576	-	-	12,276	18,553
Securities lending collateral equity with State Treasurer	-	1,211	-	-	-	1,211
Due from other government - federal	-	3,164	9	78,546	31,807	113,526
Other receivables, net	393	2	-	-	8,894	9,289
Due from other State funds	-	340	-	-	-	340
Total assets	$ 2,094	$ 9,293	$ 9	$ 200,938	$ 52,977	$ 265,311
LIABILITIES AND DEFERRED INFLOWS OF RESOURCES						
Accounts payable and accrued liabilities	$ -	$ 335	$ -	$ 137,406	$ 11,685	$ 149,426
Due to other government - federal	-	-	-	-	5,575	5,575
Due to other government - local	-	-	-	4,087	23,746	27,833
Due to other State fiduciary funds	-	-	-	-	1,066	1,066
Due to other Department funds	-	-	-	-	49	49
Due to other State funds	593	-	-	247	17,945	18,785
Due to State of Illinois component units	-	1,521	-	348	-	1,869
Obligations under securities lending of State Treasurer	-	1,211	-	-	-	1,211
Total liabilities	593	3,067	-	142,088	60,066	205,814
Unavailable revenue - Federal operating grants	-	1,856	9	21,275	287	23,427
Unavailable revenue - License and fees	248	-	-	-	-	248
Total deferred inflows of resources	248	1,856	9	21,275	287	23,675
Total liabilities and deferred inflows of resources	841	4,923	9	163,363	60,353	229,489
FUND BALANCES (DEFICITS)						
Committed for health and social services	1,253	4,370	-	37,575	-	43,198
Unassigned	-	-	-	-	(7,376)	(7,376)
Total fund balances (deficits)	1,253	4,370	-	37,575	(7,376)	35,822
Total liabilities, deferred inflows of resources and fund balances (deficits)	$ 2,094	$ 9,293	$ 9	$ 200,938	$ 52,977	$ 265,311

Combining Statement of Revenues, Expenditures and Changes in Fund Balances - Nonmajor Governmental Funds

For the Year Ended June 30, 2016 (Expressed in Thousands)

	Special Revenue					
	Provider Inquiry Trust 0341	Money Follows the Person Budget Transfer 0522	Department of Corrections Reimbursement and Education 0523	Tobacco Settlement Recovery 0733	Child Support Administrative 0757	Total
REVENUES						
Operating grants - federal	$ -	$ 3,138	$ 1,154	$ 75,314	$ 116,901	$ 196,507
License and fees	1,476	-	-	-	-	1,476
Other charges for services	-	-	-	-	13,419	13,419
Interest and other investment income	-	17	-	-	-	17
Total revenues	1,476	3,155	1,154	75,314	130,320	211,419
EXPENDITURES						
Health and social services	593	1,841	-	146,454	163,238	312,126
Debt service principal	-	-	-	-	8	8
Debt service interest	-	-	-	-	3	3
Total expenditures	593	1,841	-	146,454	163,249	312,137
Excess (deficiency) of revenues over (under) expenditures	883	1,314	1,154	(71,140)	(32,929)	(100,718)
OTHER SOURCES (USES) OF FINANCIAL RESOURCES						
Appropriations from State resources	-	-	-	200,600	-	200,600
Lapsed appropriations	-	-	-	(65,026)	-	(65,026)
Receipts collected and transmitted to State Treasury	-	-	(1,154)	(15,708)	-	(16,862)
Transfers-in	-	-	-	-	-	-
Transfers-out	-	-	-	-	-	-
Net other sources (uses) of financial resources	-	-	(1,154)	119,866	-	118,712
Net change in fund balances	883	1,314	-	48,726	(32,929)	17,994
Fund balances (deficits), July 1, 2015	370	3,056	-	(11,151)	25,553	17,828
FUND BALANCES (DEFICITS), JUNE 30, 2016	$ 1,253	$ 4,370	$ -	$ 37,575	$ (7,376)	$ 35,822

Combining Statement of Fiduciary Net Position - Agency Funds

June 30, 2016 (Expressed in Thousands)

	Child Support Enforcement Trust 0957	Child Support Enforcement Trust - SDU 2957	Total
ASSETS			
Cash equity with State Treasurer	$ 16,697	$ -	$ 16,697
Cash and cash equivalents	186	1,502	1,688
Other receivables, net	207,043	36	207,079
Due from other State funds	1	-	1
Total assets	$ 223,927	$ 1,538	$ 225,465
LIABILITIES			
Accounts payable and accrued liabilities	$ 17,958	$ 1,538	$ 19,496
Other liabilities	205,969	-	205,969
Total liabilities	$ 223,927	$ 1,538	$ 225,465

State of Illinois

Department of Healthcare and Family Services

Combining Statement of Changes in Assets and Liabilities - Agency Funds

For the Year Ended June 30, 2016 (Expressed in Thousands)

	Balance at July 1, 2015	Additions	Deletions	Balance at June 30, 2016
Child Support Enforcement Trust (0957)				
ASSETS				
Cash equity with State Treasurer	$ 15,492	$ 144,806	$ 143,601	$ 16,697
Cash and cash equivalents	634	82,753	83,201	186
Other receivables, net	207,149	144,699	144,805	207,043
Due from other State funds	-	2	1	1
Total assets	$ 223,275	$ 372,260	$ 371,608	$ 223,927
LIABILITIES				
Accounts payable and accrued liabilities	$ 16,460	$ 11,615	$ 10,117	$ 17,958
Other liabilities	206,815	215,839	216,685	205,969
Total liabilities	$ 223,275	$ 227,454	$ 226,802	$ 223,927
Child Support Enforcement Trust - SDU (2957)				
ASSETS				
Cash and cash equivalents	$ 1,389	$ 1,213,462	$ 1,213,349	$ 1,502
Other receivables, net	61	291	316	36
Total assets	$ 1,450	$ 1,213,753	$ 1,213,665	$ 1,538
LIABILITIES				
Accounts payable and accrued liabilities	$ 1,450	$ 1,213,437	$ 1,213,349	$ 1,538
Total liabilities	$ 1,450	$ 1,213,437	$ 1,213,349	$ 1,538
Total				
ASSETS				
Cash equity with State Treasurer	$ 15,492	$ 144,806	$ 143,601	$ 16,697
Cash and cash equivalents	2,023	1,296,215	1,296,550	1,688
Other receivables, net	207,210	144,990	145,121	207,079
Due from other State funds	-	2	1	1
Total assets	$ 224,725	$ 1,586,013	$ 1,585,273	$ 225,465
LIABILITIES				
Accounts payable and accrued liabilities	$ 17,910	$ 1,225,052	$ 1,223,466	$ 19,496
Other liabilities	206,815	215,839	216,685	205,969
Total liabilities	$ 224,725	$ 1,440,891	$ 1,440,151	$ 225,465

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Honorable Frank J. Mautino
Auditor General
State of Illinois

As Special Assistant Auditors for the Auditor General, we have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the major fund, and the aggregate remaining fund information of the State of Illinois, Department of Healthcare and Family Services, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the State of Illinois, Department of Healthcare and Family Services' basic financial statements, and have issued our report thereon dated February 21, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the State of Illinois, Department of Healthcare and Family Services' internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the State of Illinois, Department of Healthcare and Family Services' internal control. Accordingly, we do not express an opinion on the effectiveness of the State of Illinois, Department of Healthcare and Family Services' internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings as items 2016-001 through 2016-004 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State of Illinois, Department of Healthcare and Family Services' financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings as items 2016-001 through 2016-004.

State of Illinois, Department of Healthcare and Family Services' and State of Illinois, Department of Human Services' Responses to Findings

The State of Illinois, Department of Healthcare and Family Services' and the State of Illinois, Department of Human Services' (Departments) responses to findings 2016-001 and 2016-002 identified in our audit are described in the accompanying schedule of findings. The Departments' responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the responses.

State of Illinois, Department of Healthcare and Family Services' Responses to Findings

The State of Illinois, Department of Healthcare and Family Services' responses to findings 2016-003 and 2016-004 identified in our audit are described in the accompanying schedule of findings. The State of Illinois, Department of Healthcare and Family Services' responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the responses.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the State of Illinois, Department of Healthcare and Family Services' internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the State of Illinois, Department of Healthcare and Family Services' internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

SIGNED ORIGINAL ON FILE

Decatur, Illinois
February 21, 2017

CURRENT FINDINGS
(GOVERNMENT AUDITING STANDARDS)

2016-001 **FINDING** (Inaccurate determination of eligibility)

The Department of Healthcare and Family Services and the Department of Human Services (Departments) lacked internal controls over the operation of the State of Illinois' Integrated Eligibility System (IES) to sufficiently prevent or detect defects that caused inaccurate determinations of eligibility.

In October 2013, the Departments implemented IES, which is utilized for the intake of applications and the determination of eligibility for the State's human service programs.

Based on Departments' information, from July 1, 2015 through June 30, 2016, the Departments had:

Applications submitted via IES	752,556
Applications approved via IES	551,681
Expenditures associated with applications approved via IES	$1,363,290,037

In order to obtain social services, individuals are evaluated on many financial and non-financial criteria. To test the accuracy of IES' determination of eligibility for benefits, the auditors selected the non-financial eligibility criteria (residency, citizenship, and social security information) for detailed testing.

The auditors received from the Departments a dataset of all applications submitted via IES from July 1, 2015 through June 30, 2016. Although the auditors could not verify the completeness and accuracy of the information, they tested all individuals who were approved to determine if they were properly approved based on the eligibility criteria selected for testing. The testing identified multiple defects which resulted in 2,198 distinct cases being improperly approved for certain programs. Specifically, individuals were approved:

- without meeting immigration requirements,
- without verification of citizenship,
- without verification of residencies,
- without valid SSNs or documentation of submitted SSN applications, and
- for individuals who were not citizens and who did not provide other acceptable alternate information (i.e.; legal permanent residents, refugees, etc).

As a result of the defects identified, inappropriate expenditures were made to or on-behalf of individuals for fiscal year 2016, totaling:

- Department of Healthcare and Family Services - $7,653,327
- Department of Human Services - $350,258

Based upon the non-financial eligibility criteria tested, the noted total expenditures made in error were not considered material by either Department with respect to their financial statements, and therefore, no adjustments were made.

According to Department management, changes were implemented in late May 2016, in order to rectify errors noted in the prior year audit (Finding 2015-002) and the errors noted above.

In addition, the auditors selected a random sample of 60 cases to determine if they had been properly approved based on all eligibility factors (both financial and non-financial). In order to conduct the testing, the auditors worked with the Departments to review each case within IES. The results of the testing were as the follows:

- Income in which IES utilized to determine eligibility was not supported in eight of the cases (13%),
- Citizenship was not verified in three of the cases (5%),
- Residency was not verified in two of the cases (3%), and
- Application was not signed by an applicant in one of the cases (2%).

Based on the above results, the auditors could not determine the accuracy of the Departments' eligibility determination for 14 of the 60 cases selected (23%). The FY16 expenditure amount associated with the 14 cases in error was $75,764. The Departments stated the errors were the result of caseworker error.

The Illinois Public Aid Code (Code) (305 ILCS 5) requires individuals to provide information related to their citizenship, residencies and SSNs. The Code also requires the Departments to verify, via a third party, the information provided by the individuals.

The State Records Act (5 ILCS 160/8) requires the head of each agency to preserve records containing adequate and proper documentation of the organization, functions, policies, decisions, procedures, and essential transaction of the agency designed to furnish information to protect the legal and financial rights of the State and of persons directly affected by the agency's activities.

Finally, the Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) states all agencies are to establish and maintain a system of internal fiscal and administrative controls, which shall provide assurance that: (1) resources are utilized efficiently, effectively, and in compliance with applicable laws; and (2) obligations and costs are in compliance with applicable laws.

Departments' management stated the exceptions noted can be attributed to the complexity of the federal laws governing each program's eligibility rules. Additionally, the eligibility rules for medical programs were changing while IES was being designed and built because the Federal Centers for Medicare and Medicaid Services continued issuing guidance and promulgating regulations. The exceptions identified during testing of the sixty cases were attributable solely to caseworker error and were not the result of any type of errors or calculations attributable to IES.

By inaccurately determining eligibility, the Departments have incurred and may continue to incur expenditures for ineligible individuals. Furthermore, due to the errors being the responsibility of the Departments, a decision was made not to recover the inappropriate payments. (Finding Code No. 2016-001, 2015-002)

RECOMMENDATION

We recommend the Departments implement adequate controls over the operations of IES to provide a high level of assurance that all defects are rectified in a timely manner. We also recommend the Departments evaluate all eligibility criteria within IES so that cases are properly approved and caseworkers are properly trained to obtain and retain documentation in support of case eligibility determinations.

DEPARTMENTS' RESPONSE

The Departments accept the recommendation. Upon receiving the FY15 eligibility related audit findings, HFS and IDHS staff worked to resolve the system errors. The dataset exceptions were identified and the system errors with respect to SSN, citizenship, and residence were corrected late in FY16. Most of the errors identified in this audit about eligibility determinations related to SSN, citizenship, and residence occurred in the earlier months of FY16 before the resolutions were in place. The Departments will also continue on going training of caseworkers to ensure they are properly trained to obtain and retain documentation in support of case eligibility determinations.

2016-002 **FINDING** (Lack of control over the Integrated Eligibility System)

The Department of Healthcare and Family Services and the Department of Human Services (Departments) failed to implement adequate security, change management and recovery controls over the State's Integrated Eligibility System (IES). IES determined eligibility for 752,556 applications, with total claims of $1.363 billion being processed during FY16.

IES was developed to consolidate and modernize the State's eligibility functions and to comply with specific federal and State security standards, which was implemented on October 1, 2013.

In the prior audit, the auditors had determined the Departments had not implemented adequate controls over security, change management, and disaster recovery. During the current audit, the auditors determined the Departments had not taken appropriate corrective action to correct these weaknesses.

Access Security Control
In order to determine if access security controls were in place over IES, the auditors requested a listing of users, developers, and administrators. Over the course of the fieldwork, the Departments provided multiple iterations of the listings, which resulted in the auditors being unable to determine the completeness and accuracy of this information.

Based on the information provided by the Departments, the auditors identified individuals and developers with unneeded or inappropriate access rights. Furthermore, the Departments' own review noted issues with separation of duties, inappropriate access rights, security administration, and access rights documentation.

According to the Departments, during the development process for IES, "security functions and roles were developed without appropriate State security oversight."

Infrastructure Security
To assess security, the auditors requested detailed documentation regarding the information technology infrastructure where IES resides. The Departments provided multiple iterations of this information, which resulted in the auditors being unable to determine the completeness and accuracy of this information.

Based on information the Departments provided, the auditors identified servers running outdated operating systems, running outdated or lacking antivirus software, and not being backed up. In addition, the development vendor and subcontractor had administrative rights to the production environment and only one State employee had access to the IES production environment. Further, the Departments' own review noted issues with clear text security information, a lack of audit logs, vendor's inability to provide complete user listings, and device configuration and operational problems.

Change Management
The Departments had not developed change management policies and procedures for IES modifications. Additionally, a review by the Departments concluded the vendor and subcontractor made changes to IES that were not approved by the State.

Disaster Recovery
After the finalization of the auditor's fieldwork, the Departments provided a disaster recovery plan for IES. However, the plan did not indicate it had been reviewed and approved by the State and did not appear to depict the current IES environment. In addition, testing of IES had not been conducted to ensure it could be recovered in the event of an outage.

Although the Departments had contracted with a development vendor and subcontractor to maintain the IES environment, the State is responsible for the security and controls of the environment in which IES resides on.

The Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires State agencies to establish and maintain a system, or systems, of internal fiscal and administrative controls to ensure State's resources are used efficiently and effectively.

Generally accepted information technology guidance endorses the development of well-designed and well-managed controls to protect computer systems and data. Effective computer security controls provide for safeguarding systems and data, suitable change management procedures, and the formal development and testing of disaster recovery plans.

Department management stated the primary focus for launching Phase 1 of IES was on gaining approval from federal CMS to connect IES to the Federal Data Services Hub by October 1, 2013. Changes required addressing the control weaknesses have taken longer to develop and implement than anticipated.

Failure to implement and maintain adequate control may lead to improper changes, access, and security flaws, which could result in inaccurate data and availability issues. For related finding see 2016-001. (Finding Code No. 2016-002, 2015-003)

RECOMMENDATION

The Departments should establish and maintain adequate controls over the security, availability, integrity, and confidentiality of IES data. Specifically, the Departments should take action provide a high level of assurance that:

- IES security controls are adequately documented and comply with the required federal and State security standards.
- Access rights are appropriate, based on job duties, approved and documented, and periodically reviewed.
- State employees have proper access to the IES environment in order to monitor and track activities on the environment.
- All changes comply with approved change management procedures and are properly documented.
- An adequately developed and tested disaster contingency plan exists.

DEPARTMENTS' RESPONSE

The Departments accept the recommendation. Several of the control weaknesses identified during this audit were identified by state personnel and previously submitted to federal CMS in the IES Plan of Action and Milestones (POA&M). The POA&M includes estimated timeframes for resolution and some requirements have already been documented as well as the action taken to resolve the issues. The Departments will continue to work internally and with the vendor to resolve the deficiencies noted during this audit.

2016-003 **FINDING** (Lack of adequate controls over the review of internal controls over service providers)

The Department of Healthcare and Family Services (Department) did not obtain or conduct timely independent internal control reviews over its external service providers.

The Department utilized various external service providers to provide:

- Software used in the data matching and verification, process management, and reporting of client's eligibility redeterminations. The vendor processed 735,624 client redeterminations during the audit period.
- Administration and payment of claims for the enrollees of the State's Dental Program. The vendor processed claims totaling $224,075,231 during the audit period.
- An externally developed and hosted application which processed Medicaid Incentive Payment Program (eMIPP). During the audit period, $37,587,170 of eMIPPs payments were processed.
- Software utilized in the Integrated Eligibility System (IES) rules engine processes, which was utilized in the determination of client eligibility for State programs. During the audit period, IES processed 752,556 applications for benefits.
- An IT environment and telecommunication resources in which to host the Department's applications and data.

During testing, the auditor noted:

- The Department did not obtain Service Organization Control (SOC) reports or conduct independent internal control reviews of all the external service providers.
- Although the Department had received a SOC report from two of the external service providers, including the provider which processed dental program payments, an analysis of the reports had not been conducted.
- The external service provider which processed payments for one of the programs, utilized subcontractors in order to carry out their contractual duties. However, the Department had not performed an analysis to determine the need to obtain information as to the subservice organization's internal controls.
- All agreements between the Department and the external service providers did not contain a requirement for an independent review to be completed.

The Department is responsible for the design, implementation, and maintenance of internal controls related to information systems and operations to assure its critical and confidential data are adequately safeguarded. This responsibility is not limited due to the processes being outsourced.

Department management stated that due to multiple staffing changes at multiple levels in the agency, the requirement for an annual Service Organization Control report was inadvertently not included in the statement of work.

The Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires all State agencies to establish and maintain a system, or systems, of internal fiscal and administrative controls, which shall provide assurance that revenues, expenditures, and transfers of assets, resources, or funds applicable to operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the State's resources.

Without having obtained and reviewed a SOC report or another form of independent internal controls review, the Department does not have assurance the external service providers' or subservice organizations' internal controls are adequate to ensure program payments and claims are accurate and secure. (Finding Code No. 2016-003, 2015-004)

RECOMMENDATION

We recommend the Department obtain or perform independent reviews of internal controls associated with third party service providers at least annually.

The independent reviews should include an assessment of the following five key system attributes, as applicable:

- Security - The system is protected against both physical and logical unauthorized access.
- Availability - The system is available for operation and use as committed or agreed.
- Processing integrity - System processing is complete, accurate, timely and authorized.
- Confidentiality - Information designated as confidential is protected as committed or agreed.
- Privacy - Personal information is collected, used, retained, disclosed, and disposed of in conformity with Department requirements.

The Department should perform a timely review of the report, assess the effect of any noted deficiencies, and identify and implement any compensating controls. The Department's reviews and corrective actions taken by the service provider should be documented and maintained.

In addition, the Department should perform an analysis to determine the need to obtain information as to the subservice organization's internal controls and perform reviews as needed.

DEPARTMENT RESPONSE

The Department accepts the recommendation. Management will develop and implement a plan to ensure adequate controls over the review of service providers are established.

2016-004 **FINDING** (Financial statement preparation)

The Department of Healthcare and Family Services' (Department) year-end financial reporting in accordance with generally accepted accounting principles (GAAP) contained weaknesses and inaccuracies.

During our audit of the Department's financial statements, the auditors brought the following items to the Department's attention. The Department corrected each of these items accordingly.

- Fund balance for three funds was incorrectly classified as unassigned. The Care Provider for Persons with DD Fund, the Trauma Center Fund and the Tobacco Settlement Recovery Fund were special revenue funds with positive balances, and the fund balance of those funds should be classified as committed rather than unassigned.

- The Department's footnote disclosure regarding contingencies omitted a matter concerning disallowed costs totaling approximately $145 million (federal share of costs) for which the Department is in the process of appealing.

In addition, the Department identified the following items and corrected each of these accordingly.

- An error was noticed in the Department's prior year reporting of its net pension liability. As such the beginning of year net pension liability was understated $35.2 million, which required a year end adjustment by the Department to restate beginning of year net position in its government wide Statement of Net Position.

- Subsequent to June 30, 2016, but prior to the completion of this audit, the Department determined that certain costs were not claimed under the correct federal program due to incorrect logic in its electronic systems. Consequently, an adjustment by the Department was required to record a liability to the federal government as of June 30, 2016 for $124 million. Of the amount owed at June 30, 2016, an adjustment was necessary to restate/reduce beginning of year fund balance of the General Revenue Fund by $82 million for those errors that occurred from April 1, 2009 through June 30, 2015.

The following errors described below were identified during the audit of the Department's draft financial statements. The Department did not correct its financial statements for these errors. However, the errors were deemed immaterial to the financial statements taken as a whole and, therefore, did not result in a modification to the auditors opinion on the Department's financial statements.

- In making the year end entries for the Medical Interagency Program Fund, the Department omitted a $5,814,000 account receivable. As a result the assets and revenue for the fund were understated by $5,814,000. Additionally, the Department accrued a liability at year end in the amount of $287,000; however, the bill which was accrued had been previously paid. As a result the liabilities and expenditures were overstated by $287,000 in the Medical Interagency Program Fund as of June 30, 2016.

- Subsequent to its preparation of the year-end financial statements, the Department identified lapse period expenditures which were not included in the year-end calculation of the medical accrual for the Drug Rebate Fund; the Department excluded $500,000 for amounts owed for additional medical assistance. Consequently, the accrued liabilities and expenditures were understated by $500,000 in the Drug Rebate Fund as of June 30, 2016. As a result of the lapse period expenditures excluded from the Drug Rebate Fund, the calculation of the total accrued liabilities and expenditures in the General Revenue Fund were overstated by $500,000 as of June 30, 2016.

- During the testing of child support accounts receivable balances in the Child Support Enforcement Trust Fund, the auditors noted two cases with overstated balances at June 30, 2016 totaling $10,802,000. Although the Department had subsequently identified and corrected one of these errors totaling $10,075,000 within its case management system, the correction was not reflected in the Department's 2016 financial statements. Additionally, the auditors noted four accounts with errors as of June 30, 2016 resulting in a net understatement of amounts owed totaling $21,000.

The Fiscal Control and Internal Auditing Act (Act) (30 ILCS 10/3001) requires State agencies to establish and maintain a system of internal fiscal and administrative controls, which shall provide assurance that revenues, expenditures, and transfers of assets, resources, or funds applicable to operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the State's resources. Good internal control procedures require adequate management oversight and review of accounting policies and procedures as well as an overall review of financial reporting for accuracy and compliance with generally accepted accounting principles.

Department management stated the issues noted were due to human errors.

Weaknesses in the design or operation of internal controls could adversely affect the Department's ability to fulfill its responsibility to prepare accurate financial statements and could lead to future misstatements of the Statewide and Department's financial statements. (Finding Code No. 2016-004)

RECOMMENDATION

We recommend the Department implement internal control procedures to ensure its financial reporting is accurate by reviewing the source for, and both manual and electronic processing of, its underlying financial records.

DEPARTMENT RESPONSE

The Department accepts the recommendation. The Department is committed to accurate financial reporting, and will continue to assess the financial reporting process and related procedures and implement necessary internal control changes to improve the accuracy of the financial statements. Immediately following submission of the Fiscal Year 2016 GAAP Reporting Packages and financial statements, the Department began conducting meetings with individuals from various bureaus to ensure the Department's activities and the financial reporting impact of those activities was shared once again and understood between bureaus. The Department plans to continue these meetings and to implement a more robust review process involving individuals from the bureaus to facilitate financial reporting accuracy. In addition, the financial statement review checklist will be updated to cover areas not previously included in the checklist, thereby facilitating more detailed review.

PRIOR FINDINGS NOT REPEATED

A. FINDING (Lack of due diligence and project management over the Integrated Eligibility System)

During the prior audit, the Department of Healthcare and Family Services and the Department of Human Services (Departments) did not establish controls to conduct due diligence or ensure project management over the State of Illinois' Integrated Eligibility System (IES) development project.

During the current period, the Departments had not yet implemented phase two of IES. Upon completion of phase two, the auditors will review the Departments' controls over the development project (Finding Code No. 2015-001)