State of Illinois
Department of Revenue

Financial Audit
For the Year Ended June 30, 2011

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

Table of Contents

State of Illinois
Department of Revenue

Agency Officials
For the Year Ended June 30, 2011

Director	Brian A. Hamer
Assistant Director	Vacant
Associate Director	Vacant (2/1/12 – Current)
	Jodie Winnett (7/1/10 – 1/31/12)
Chief of Staff	Lainie Krozel
Chief Fiscal Officer	David Hunt
Lottery	Michael Jones (10/10/11 – Current)
	Jodie Winnett (Acting through 10/10/11)
Liquor Control Commission	Gloria Materre (3/21/11 – Current)
	Lainie Krozel (7/1/10 – 3/20/11)
Program Administrators:	
Administrative Services	Angela Oxley
Account Processing	O. Wayne Richie
Information Technology	Elizabeth Malloy (1/15/12 – Current)
	Vacant (1/1/12 – 1/14/12)
	Rebecca Moore (12/1/09 – 12/31/11)
Tax Enforcement	John Chambers
Audit	Dan Hall
Policy and Communications Office	Michael Klemens
Chief Information Security Officer	Brad Boroff (3/1/12 – Current)
	(position established 3/1/12)
General Counsel	Gail Niemann (11/14/11 – Current)
	Agostino Lorenzini (Acting 7/1/11 – 11/13/11)
	John McCaffrey (Retired 6/30/11)
Chief Internal Auditor	Douglas Hathhorn (8/2/2010 – Current)
	Vacant (through 8/1/2010)
Managers:	
Financial Control Bureau	Matthew Couturiaux (8/16/11 – Current)
	Vacant (9/1/10 – 8/15/11)
	Larry Lascody, Jr. (7/1/10 – 8/31/10)
Returns and Deposit	Patti Walbaum
Administrative and Regulatory Shared Services Center:	
Director	Vacant (7/1/10 – Current)
Chief Fiscal Officer	Melinda Westwater (5/16/11 – Current)
	Dave Hunt (Acting 2/16/11 – 5/15/11)
	Marvin Becker (7/1/10 – 2/15/11)
Customer Service Liasion	Dave Klintworth
Human Resources Director	Matthew Bilinsky – Acting (12/1/11 – Current)
	Jeanine Hamm (7/1/10 – 11/30/11)
Administrative Director	Vacant
Lottery Control Board Members	Irv Smith
(as of June 30, 2011)	Jonathan Stein
	Vacant
	Vacant
	Vacant
Liquor Control Board Members	Stephen Schnorf
(as of June 30, 2011)	Sam Esteban
	Amy Kurson
	Michael F. McMahon
	Donald G. O'Connell
	James Pandolfi
	Charles Scholz

State of Illinois
Department of Revenue

Financial Statement Report

Summary

The audit of the accompanying basic financial statements of the State of Illinois, Department of Revenue (Department), was performed by McGladrey LLP. Based on their audit, the auditors expressed an unqualified 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 and significant deficiencies. The material weaknesses are described in the accompanying Schedule listed in the table of contents as findings 11-1 and 11-2. The significant deficiencies are described in the accompanying Schedule of Findings listed in the table of contents as findings 11-3 through 11-12.

Item No.	Page	Description	Finding Type
11-1	60	Increased Levels of Unprocessed Taxpayer Information	Material Weakness
11-2	63	Fund Balance Deficit Exceeding $1.6 Billion	Material Weakness
11-3	66	Service Organization Internal Control Reports Not Obtained	Significant Deficiency
11-4	67	Reconciliations of Hotel Operators' Occupation Tax Allocations	Significant Deficiency
11-5	68	Weaknesses in the Processes over Sales and Use Tax Allocations	Significant Deficiency
11-6	71	Weaknesses in Receipt Processing and Taxpayer Information	Significant Deficiency
11-7	73	Inadequate Control over Illinois Sports Facilities Authority Funds	Significanty Deficiency
11-8	75	Exceptions in Income Tax Refunds Payable Balances at Year-End	Significant Deficiency
11-9	77	Noncompliance with Provisions of the Illinois Income Tax Act and State Revenue Sharing Act	Significant Deficiency
11-10	80	Weaknesses in Controls over the Deposit of Sales and Use Tax Receipts	Significant Deficiency
11-11	84	Year-End Cash Balances Not Properly Recorded	Significant Deficiency
11-12	86	Weaknesses in Internal Controls over Taxpayer Accounts	Significant Deficiency
		Prior Findings Not Repeated	
A.	90	Year-end Reporting Procedures for Receivables Not Followed	
B.	90	Year-end Accounting Estimate Not Prepared Accurately	
C.	90	Year-end Receivable Not Propery Allocated	
D.	90	Certain Year-end Receivables Not Valid	
E.	90	Noncompliance with the Public Utilities Revenue Act	
F.	91	Inadequate Controls over Taxes Collected for Local Governments	

Exit Conference

The findings and recommendations appearing in this report were discussed with Department personnel at an exit conference on May 22, 2012. Attending were:

Department of Revenue	
Brian Hamer	Director
Gail Niemaun	General Counsel
Matthew Couturiaux	FCB Manager
Jose Borjon	Audit Liaison
Paul Caselton	Deputy General Counsel
Brenda Towers	Local Tax Allocation Division Manager
Angela Oxley	Administrative Services
Wayne Richie	APA Manager
Douglas Hatthorn	Chief Internal Auditor
Dan Hall	Audit Bureau Manager
Melinda Westwater	CFO ARSSC
Lainie Krozel	Chief of Staff
Dave Hunt	Chief Fiscal Officer
Michael Klemens	Manager Policy and Communications
McGladrey LLP	
Linda Abernethy	Partner
Bill Sarb	Senior Associate
Office of the Auditor General	
Paul Usherwood	Audit Manager
Daniel J. Nugent	Audit Manager
Jennifer Cicci	Audit Manager
Janis Van Durme	Audit Supervisor

The responses to the recommendations were provided by Brian A. Hamer, Director, in an email dated May 29, 2012.

McGladrey

Independent Auditors' Report

Honorable William G. Holland
Auditor General
State of Illinois

As Special Assistant Auditors for the Auditor General, we have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State of Illinois, Department of Revenue, as of and for the year ended June 30, 2011, which collectively comprise the State of Illinois, Department of Revenue's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the State of Illinois, Department of Revenue's management. 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 of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing 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 over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 2, the financial statements of the State of Illinois, Department of Revenue are intended to present the financial position and changes in financial position and cash flows, where applicable, of only that portion of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State that is attributable to the transactions of the State of Illinois, Department of Revenue. They do not purport to, and do not, present fairly the financial position of the State of Illinois as of June 30, 2011, and its changes in financial position including cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 11, the Department has the following significant fund deficits as of June 30, 2011; General Fund, $1.6 billion, and Personal Property Tax Replacement Fund (non-major special revenue fund) $386 million. The Department's plan to eliminate these deficits is highly dependent on the collection and allocation of future State revenues to the Department.

As discussed in Note 14, as of July 1, 2010, the Department adopted the reporting and disclosure requirements of Governmental Accounting Standards Board Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State of Illinois, Department of Revenue, as of June 30, 2011, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated May 30, 2012 on our consideration of the State of Illinois, Department of Revenue's 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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The State of Illinois, Department of Revenue has not presented a management's discussion and analysis and budgetary comparison information for the General Fund that accounting principles generally accepted in the United States of America has determined is necessary to supplement, although not required to be part of, the basic financial statements.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the State of Illinois, Department of Revenue's basic financial statements. The combining statements and schedules listed as supplementary information in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. The combining statements and schedules listed as supplementary information in the table of contents have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

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.

McGladrey LLP

Schaumburg, Illinois
May 30, 2012

State of Illinois
Department of Revenue

Statement of Net Assets

June 30, 2011 (Expressed in Thousands)

	Governmental Activities	Business-type Activities	Total
ASSETS			
Unexpended appropriations	$ 29,703	$ -	$ 29,703
Cash equity in State Treasury	1,300,674	36,522	1,337,196
Cash and cash equivalents	3	6,278	6,281
Securities lending collateral with State Treasurer	54,382	-	54,382
Investments	-	525	525
Taxes receivable, net	1,309,641	-	1,309,641
Intergovernmental receivables	200	-	200
Other receivables, net of allowance of $231 and $7,706 for governmental and business-type activities, respectively	17,959	13,362	31,321
Due from Department fiduciary funds	-	328	328
Due from Department funds	(101,659)	101,659	-
Due from State funds	151,322	-	151,322
Loans and notes receivable, long-term	36,685	-	36,685
Due from State of Illinois component units	327,833	-	327,833
Inventories	379	248	627
Prepaid expenses	-	120	120
Capital assets being depreciated/amortized, net	10,219	269	10,488
Total assets	3,137,341	159,311	3,296,652
LIABILITIES			
Accounts payable and accrued liabilities	377,218	118,280	495,498
Income tax refunds payable	1,669,732	-	1,669,732
Intergovernmental payables	1,141,650	-	1,141,650
Obligations under securities lending - State Treasurer	54,382	-	54,382
Due to Department fiduciary funds	84,189	-	84,189
Due to other State fiduciary funds	416	-	416
Due to other State funds	485,581	414	485,995
Due to State of Illinois component units	36	-	36
Unearned revenue	588,794	3,785	592,579
Long-term obligations:			
Portion due or payable within one year	1,100	156	1,256
Portion due or payable after one year	14,852	1,785	16,637
Total liabilities	4,417,950	124,420	4,542,370
NET ASSETS			
Invested in capital assets	10,219	269	10,488
Restricted for education	-	34,622	34,622
Restricted - other	12,133	-	12,133
Unrestricted net assets	(1,302,961)	-	(1,302,961)
Total net assets	$ (1,280,609)	$ 34,891	$ (1,245,718)

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

State of Illinois

Department of Revenue

Statement of Activities

For the Year Ended June 30, 2011 (Expressed in Thousands)

		Program Revenues		Net (Expense) Revenues and Changes in Net Assets		
Functions/Programs	**Expenses**	**Charges for Services**	**Operating Grants and Contributions**	**Governmental Activities**	**Business-type Activities**	**Total**
Governmental activities						
General government	$ 245,308	$ 47,412	$ 526	$ (197,370)	$ -	$ (197,370)
Health and social services	120	-	-	(120)	-	(120)
Employment and economic development	5,625	-	-	(5,625)	-	(5,625)
Environment and business regulation	6,015	-	-	(6,015)	-	(6,015)
Intergovernmental-revenue sharing	4,528,346	-	-	(4,528,346)	-	(4,528,346)
Total governmental activities	4,785,414	47,412	526	(4,737,476)	-	(4,737,476)
Business-type activities						
Lottery	1,601,387	2,269,675	-		668,288	668,288
Total Department	$ 6,386,801	$ 2,317,087	$ 526			
General revenues						
Taxes:						
Income taxes				14,385,267	-	14,385,267
Sales taxes				9,423,018	-	9,423,018
Motor fuel taxes				1,302,294	-	1,302,294
Public utility taxes				1,488,768	-	1,488,768
Other taxes				1,008,094	-	1,008,094
Interest and investment income				13,880	-	13,880
Other revenues (expenses)				37,407	-	37,407
Appropriations from State Resources				249,507	-	249,507
Lapsed appropriations				(51,216)	-	(51,216)
Receipts collected and transmitted to State Treasury				(22,287,709)	-	(22,287,709)
Amount of SAMS transfers-in				(2,372,413)	-	(2,372,413)
Amount of SAMS transfers-out				1,557,941	-	1,557,941
Transfers-in				821,086	-	821,086
Transfers-out				(435,249)	(668,288)	(1,103,537)
Total general revenues and transfers				5,140,675	(668,288)	4,472,387
Change in net assets				403,199	-	403,199
Net assets, July 1, 2010				(1,683,808)	34,891	(1,648,917)
Net assets, June 30, 2011				$ (1,280,609)	$ 34,891	$ (1,245,718)

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

State of Illinois
Department of Revenue

Balance Sheet - Governmental Funds

June 30, 2011 (Expressed in Thousands)

	General Fund	Nonmajor funds	Total Governmental Funds
ASSETS			
Unexpended appropriations	$ 23,800	$ 5,903	$ 29,703
Cash equity in State Treasury	634,868	665,806	1,300,674
Cash and cash equivalents	-	3	3
Securities lending collateral with State Treasurer	33	54,349	54,382
Taxes receivables, net	973,709	335,932	1,309,641
Intergovernmental receivables	200	-	200
Other receivables, net of allowance of $231	-	17,959	17,959
Due from other Department funds	279,107	406,975	686,082
Due from other State funds	4,055	147,267	151,322
Loans and notes receivable, long-term	-	36,685	36,685
Due from State of Illinois component units	-	327,833	327,833
Inventories	379	-	379
Total assets	$ 1,916,151	$ 1,998,712	$ 3,914,863
LIABILITIES			
Accounts payable and accrued liabilities	$ 300,848	$ 76,370	$ 377,218
Income tax refunds payable	1,669,732	-	1,669,732
Intergovernmental payables	19,435	1,122,215	1,141,650
Obligations under securities lending - State Treasurer	33	54,349	54,382
Due to other Department fiduciary funds	55,763	28,426	84,189
Due to other State fiduciary funds	-	416	416
Due to other Department funds	456,690	331,051	787,741
Due to other State funds	482,278	3,303	485,581
Due to State of Illinois component units	36	-	36
Unavailable revenue	125,093	39,833	164,926
Unearned revenue	446,831	141,963	588,794
Total liabilities	3,556,739	1,797,926	5,354,665
FUND BALANCES (DEFICITS)			
Nonspendable (inventories)	379	-	379
Nonspendable (long-term loans receivable)	-	36,685	36,685
Restricted	-	12,133	12,133
Committed	308,768	548,289	857,057
Unassigned	(1,949,735)	(396,321)	(2,346,056)
Total fund balances (deficits)	(1,640,588)	200,786	(1,439,802)
Total liabilities and fund balances (deficits)	$ 1,916,151	$ 1,998,712	$ 3,914,863

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

State of Illinois
Department of Revenue
Reconciliation of Governmental Funds Balance Sheet
to Statement of Net Assets
June 30, 2011
(Expressed in Thousands)

Total fund balances-governmental funds	$	(1,439,802)
Amounts reported for governmental activities in the Statement of Net Assets are different because:		
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.		10,219
Revenues in the Statement of Activities that do not provide current financial resources are deferred in the funds.		164,926
Some liabilities reported in the Statement of Net Assets do not require the use of current financial resources and therefore are not reported as liabilities in governmental funds. These activities consist of:		
Compensated absences		(15,952)
Net assets of governmental activities	$	(1,280,609)

State of Illinois
Department of Revenue

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

For the Year Ended June 30, 2011 (Expressed in Thousands)

	General Fund	Nonmajor funds	Total Governmental Funds
REVENUES			
Federal operating grants	$ -	$ 526	$ 526
Income taxes	12,391,402	1,996,729	14,388,131
Sales taxes	6,850,133	2,580,692	9,430,825
Motor fuel taxes	-	1,299,397	1,299,397
Public utility taxes	1,121,156	368,635	1,489,791
Other taxes	761,707	247,977	1,009,684
Licenses and fees	5,274	38,453	43,727
Other charges for services	3,683	2	3,685
Interest and other investment income	-	3,709	3,709
Other	3,285	34,116	37,401
Total revenues	21,136,640	6,570,236	27,706,876
EXPENDITURES			
General government	148,790	95,232	244,022
Health and social services	-	120	120
Employment and economic development	5,625	-	5,625
Environment and business regulation	-	6,015	6,015
Intergovernmental	-	4,528,346	4,528,346
Capital outlays	3,259	2,839	6,098
Total expenditures	157,674	4,632,552	4,790,226
Excess (deficiency) of revenues over (under) expenditures	20,978,966	1,937,684	22,916,650
OTHER SOURCES (USES) OF FINANCIAL RESOURCES			
Appropriations from State resources	139,092	110,415	249,507
Lapsed appropriations	(5,539)	(45,677)	(51,216)
Receipts collected and transmitted to State Treasury	(20,129,111)	(2,158,598)	(22,287,709)
Amount of SAMS Transfers-in	(2,334,613)	(37,800)	(2,372,413)
Amount of SAMS Transfers-out	1,556,349	1,592	1,557,941
Transfers-in	671,704	149,382	821,086
Transfers-out	(390,228)	(45,021)	(435,249)
Net other sources (uses) of financial resources	(20,492,346)	(2,025,707)	(22,518,053)
Net change in fund balances	486,620	(88,023)	398,597
Fund balances (deficits), July 1, 2010, as restated	(2,127,306)	288,809	(1,838,497)
Increase for changes in inventories	98	-	98
FUND BALANCES (DEFICITS), JUNE 30, 2011	$ (1,640,588)	$ 200,786	$ (1,439,802)

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

State of Illinois
Department of Revenue
Reconciliation of Statement of Revenues, Expenditures and Changes in Fund Balances of Governmental Funds to Statement of Activities
For the Year Ended June 30, 2011
(Expressed in Thousands)

Net change in fund balances	$ 398,597
Change in inventories	98
	398,695
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/amortization expense to allocate those expenditures over the life of the assets. This is the amount by which capital outlays ($6,096) exceeded depreciation/amortization ($1,489) in the current period.	4,607
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.	(210)
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.	
Decrease in compensated absences obligation	107
Change in net assets of governmental activities	$ 403,199

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

State of Illinois
Department of Revenue

Statement of Net Assets - Proprietary Funds

June 30, 2011 (Expressed in Thousands)

		Nonmajor Enterprise Fund
		State Lottery 0711
ASSETS		
Cash equity in State Treasury	$	36,522
Cash and cash equivalents		6,278
Investments, short-term		59
Other receivables, net of allowance of $7,706		13,362
Due from other Department fiduciary funds		328
Due from other Department funds		101,659
Inventories		248
Prepaid expenses		120
Total current assets		158,576
Investments		466
Capital assets being depreciated, net		269
Total assets		159,311
LIABILITIES		
Accounts payable and accrued liabilities		118,280
Due to other State funds		414
Unearned revenue		3,785
Current portion of long-term obligations		156
Total current liabilities		122,635
Noncurrent portion of long-term obligations		1,785
Total liabilities		124,420
NET ASSETS		
Invested in capital assets		269
Restricted for education		34,622
Total net assets	$	34,891

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

State of Illinois
Department of Revenue

Statement of Revenues, Expenses and Changes in Fund Net Assets - Proprietary Funds

For the Year Ended June 30, 2011 (Expressed in Thousands)

	Nonmajor Enterprise Fund State Lottery 0711
OPERATING REVENUES	
Charges for sales and services	$ 2,264,685
Other	4,990
Total operating revenues	2,269,675
OPERATING EXPENSES	
Cost of sales and services	160,910
Prizes and claims	1,368,472
General and administrative	71,857
Depreciation	148
Total operating expenses	1,601,387
Income before transfers	668,288
Transfers-out	(668,288)
Net income	-
Net assets, July 1, 2010	34,891
NET ASSETS, JUNE 30, 2011	$ 34,891

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

State of Illinois
Department of Revenue

Statement of Cash Flows - Proprietary Funds

For the Year Ended June 30, 2011 (Expressed in Thousands)

	Nonmajor Enterprise Fund State Lottery 0711
CASH FLOWS FROM OPERATING ACTIVITIES	
Cash received from sales and services (net of $227,419 cash prizes paid by agents and $29,684 commissions retained by agents)	$ 1,155,015
Cash payments to employees for services	(134,668)
Cash payments for lottery prizes	(326,909)
Cash receipts from other operating activities	4,990
Net cash provided by operating activities	698,428
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
Transfers-out to other funds	(722,987)
Net cash (used) by noncapital financing activities	(722,987)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Acquisition and construction of capital assets	(6)
Net cash (used) by capital and related financing activities	(6)
Net (decrease) in cash and cash equivalents	(24,565)
Cash and cash equivalents, July 1, 2010	67,365
CASH AND CASH EQUIVALENTS, JUNE 30, 2011	$ 42,800
Reconciliation of cash and cash equivalents to the statement of net assets:	
Total cash and cash equivalents per the statement of net assets	$ 6,278
Add: Cash equity with State Treasurer	36,522
CASH AND CASH EQUIVALENTS, JUNE 30, 2011	$ 42,800

(Continued)

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

Statement of Cash Flows - Proprietary Funds - Continued

For the Year Ended June 30, 2011 (Expressed in Thousands)

	Nonmajor Enterprise Fund State Lottery 0711
Reconciliation of operating income to net cash provided by operating activities:	
OPERATING INCOME	$ 668,288
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	148
Provision for uncollectible accounts	1,046
Changes in assets and liabilities:	
(Increase) decrease in accounts receivable	(8,732)
(Increase) decrease in due from other funds	(208)
(Increase) decrease in inventory	409
(Increase) decrease in prepaid expenses	(52)
Increase (decrease) in accounts payable and accrued liabilities	38,928
Increase (decrease) in intergovernmental payables	(31)
Increase (decrease) in due to other funds	(2,254)
Increase (decrease) in due to component units	(3)
Increase (decrease) in unearned revenues	846
Increase (decrease) in other liabilities	43
Total adjustments	30,140
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 698,428
NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES	
Transfer of assets from (to) other state funds	($19)

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

State of Illinois
Department of Revenue

Statement of Fiduciary Net Assets

June 30, 2011 (Expressed in Thousands)

	Investment Trust Fund: Deferred Prize Winners Trust Fund 0978	Agency Funds
ASSETS		
Cash equity in State Treasury	$ 491	$ 458,428
Cash and cash equivalents	-	2,807
Securities lending collateral with State Treasurer	-	130,878
Investments - US Treasury zero coupon securities	370,719	-
Taxes receivable, net	-	126,921
Other receivables,net	-	148
Due from other Department funds	-	84,189
Total assets	371,210	$ 803,371
LIABILITIES		
Accounts payable and accrued liabilities	-	$ 8,054
Intergovernmental payables	-	661,587
Due to other Department funds	328	-
Obligations under securities lending - State Treasurer	-	130,878
Other liabilities	163	2,852
Total liabilities	491	$ 803,371
NET ASSETS		
Held in trust for prizewinners	370,719	
Total net assets	$ 370,719	

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

State of Illinois

Department of Revenue

Statement of Changes in Fiduciary Net Assets

For the Year Ended June 30, 2011 (Expressed in Thousands)

	Investment Trust Fund
	Deferred Prize Winners Trust Fund 0978
ADDITIONS:	
Investment earnings:	
Interest, dividends and other investment income	$ 22,975
Net increase (decrease) in the fair value of investments	(18,690)
Net investment income	4,285
Individual account transactions:	
Shares sold	25,477
Shares redeemed	(91,011)
Net individual account transactions	(65,534)
Net additions	(61,249)
Net assets, July 1, 2010	431,968
Net assets, JUNE 30, 2011	$ 370,719

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

(1) Organization

The Department of Revenue (the 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 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 Surety Bond Fund, the Lottery Agent Security Deposits Fund, and the Evidence Fund.

The Department is organized to provide for administering, collecting, enforcing and determining distribution of the taxes imposed by the State's major tax acts. The Department also administers and oversees the operations of the Illinois Lottery and the Liquor Control Commission.

(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 dependency 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 Revenue, are intended to present the financial position, changes in financial position, and cash flows of only that portion of the governmental activities, each major governmental fund of the State of Illinois, the enterprise 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, 2011 the changes in financial position for the year then ended, and the cash flows in conformity with accounting principles generally accepted in the United States of America.

***Government-wide Statements*.** The government-wide statement of net assets 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. These statements distinguish between the *governmental* and *business-type* activities of the Department. Governmental activities generally are financed through taxes, intergovernmental revenues, and other nonexchange transactions. Business-type activities are financed in whole or in part by fees charged to external parties.

The statement of net assets presents the assets and liabilities of the Department's governmental and business-type activities with the difference being reported as net assets. 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 different business-type activities of the Department and for each function of the Department's governmental activities. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include charges paid by the recipients of goods or services offered by the programs. 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, proprietary, and fiduciary - are presented. The emphasis on fund financial statements is on major governmental and enterprise funds, each displayed in a separate column. All remaining governmental and enterprise funds are aggregated and reported as nonmajor funds.

Proprietary fund operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal value. Nonoperating revenues, such as subsidies and investment earnings, result from nonexchange transactions or ancillary activities.

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 Department's portion of the General Fund is composed of a primary sub-account (General Revenue) and eight secondary sub-accounts (Common School Special, Education Assistance, Illinois Sports Facility, Income Tax Refund, Common School, Predatory Lending Database Program, Municipal Economic Development and Capital Projects). The services which are administered by the Department and accounted for in the general fund include, among others, general government services.

Additionally, the Department administers the following fund types:

Governmental Fund Types:

Special Revenue – These funds account for resources obtained from specific revenue sources that are legally restricted to expenditures for specified purposes. Special revenue funds account for, among other things, taxes levied with statutorily defined distributions, federal grant programs and other resources restricted as to purpose.

Proprietary Fund Types:

Enterprise – The State Lottery Fund accounts for operations of the State Lottery in which the net proceeds are used for the support of the State's Common School Fund.

Fiduciary Fund Types:

Investment Trust – The Deferred Lottery Prizewinners Trust Fund accounts for the external portion of investment pools made on behalf of Lottery prizewinners.

Agency – These funds account for assets held 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, proprietary, and fiduciary fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when they are estimated to have been earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flow takes place. Nonexchange transactions, in which the Department gives (or receives) value without directly receiving (or giving) equal value in exchange, include income and replacement, sales, motor fuel, and excise taxes. On an accrual basis, revenues from these taxes 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 collectible 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.

In accordance with Governmental Accounting Standards Board Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, recognition of nonexchange transactions in the financial statements is required unless the transactions are not measurable (reasonably estimable) or are not probable of collection. In this regard, the Department annually has an inventory of returns (primarily income tax and sales tax), that are in various stages of processing at year-end and through the date of issuing the financial statements ("unperfected returns"). Cash receipts and revenue associated with these unperfected returns are generally recorded in the General Fund. As of June 30, 2011, unperfected returns were approximately $4.7 billion. Potential receivables and/or refunds that may result upon perfecting the returns cannot be reasonably estimated and are not recorded. Additionally, upon perfecting the returns, cash allocations to other governmental and fiduciary funds will be required and are expected to be material.

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 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 income and replacement taxes, sales taxes, public utility taxes, motor fuel taxes, other taxes, tax penalties, and interest. The tax revenues are recorded by the State as taxpayers earn income (personal income tax, corporate income tax, and other taxes), as sales are made (sales taxes, public utility taxes, motor fuel taxes, and other taxes), or as the taxable event occurs (other taxes) net of estimated overpayments and amounts not expected to be collected.

Taxpayers can elect to receive a refund of tax overpayments (refunds payable), or carry–forward those overpayments to be applied to tax liabilities of the next year (deferred revenue). All liabilities pertaining to tax overpayments (refunds payable and deferred revenue) are estimated based on a combination of actual data and historical trends.

All other revenue sources including fines, licenses, and other miscellaneous revenues are considered to be measurable and available only when cash is received. Estimates are used to assign estimated tax payments received or refunds applied to future tax periods for individual and corporate income taxes to the proper fiscal year.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. The State also has the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The State has elected not to follow subsequent private-sector guidance as it relates to the Department's operations.

(d) Shared Fund Presentation

The financial statement presentation for the General Revenue Fund, Education Assistance Fund, Motor Fuel Tax Fund, Public Utility Fund, Underground Storage Tank Fund, Illinois Gaming Law Enforcement Fund, Emergency Public Health Fund, Used Tire Management Fund, Natural Areas Acquisition Fund, Open Space Lands Acquisition and Development Fund, Common School Fund, Drycleaner Environment Response Trust Fund, Supplemental Low Income Energy Assistance Fund, Renewable Energy Resources Trust Fund, School Infrastructure Fund, International Tourism Fund, Capital Projects Fund, Build Illinois Fund, and Local Tourism Fund 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 August annually 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

This “other financing source” account represents the final legally adopted appropriation according to SAMS records.

Lapsed Appropriations

Lapsed appropriations are the legally adopted appropriations less net warrants issued for the 14 month period from July to August of the following year and re-appropriations to subsequent years according to SAMS records. For State fiscal year 2011, the Illinois General Assembly extended the lapse period from August 31 to December 31, 2011 to allow for the liquidation of all expenditure transactions for the 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 assets 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 assets. Amounts reported in the governmental funds balance sheet and proprietary statement of net assets as receivable from or payable to fiduciary funds have been included in the government-wide statement of net assets 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 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) Inventories

Inventories, consisting primarily of lottery tickets and postage and printing supplies, are valued at cost, principally on the first-in, first-out (FIFO) method. Significant inventories of governmental funds are recorded as expenditures when consumed rather than when purchased.

(i) Prepaid items

Payments made to vendors for services that will benefit periods beyond the date of this report are recorded as prepaid items on the government-wide statement of net assets.

(j) Interfund Transactions

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 or the government-wide and proprietary fund statements of net assets.

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. In proprietary funds, transfers are reported after nonoperating revenues and expenses.

(k) Capital and Intangible Assets

Capital assets, which consist of equipment, automobiles and internally developed computer software, are reported at cost. Contributed assets are reported at estimated fair value at the time received. Capital assets are depreciated/amortized using the straight-line method. The capitalization threshold for capital assets is $5,000 and the estimated useful life is 3-15 years.

(l) Compensated Absences

The liability for compensated absences reported in the government-wide and proprietary fund statements of net assets 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 costs (e.g., social security and Medicare tax).

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 January 1, 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.

(m) Fund Balances

Effective July 1, 2010, the Department adopted the provisions of Governmental Accounting Standards Board Statement No. 54 (GASB 54), *Fund Balance Reporting and Governmental Fund Type Definitions*. This statement established fund balance classifications that comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in the governmental funds. In addition, GASB 54 modified certain fund type definitions. Pursuant to this guidance, the Department was required to report fund balances previously reported as nonmajor special revenue funds, as part of the general fund. As a result, the Department restated its beginning fund balance in the general fund by $950 thousand in order to properly reflect the reclassification of funds previously reported as special revenue funds.

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.

Within the governmental fund types, the Department's fund balances are reported in one of the following classifications:

Nonspendable – includes 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 – includes amounts that are restricted to specific purposes, that is, when constraints placed on the use of resources are either: a) externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments; or b) imposed by law through constitutional provisions or enabling legislation.

Committed – includes 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 – includes amounts that are constrained by the Department's *intent* to be used for specific purposes, but that are neither restricted nor committed. Intent is expressed by: a) the State legislature itself; or b) a body or official to which the State has delegated the authority to assign amounts to be used for specific purposes. The State has not delegated authority to any other body or official to assign amounts for a specific purpose within the General Fund. Within the other governmental fund types (special revenue, debt service, capital projects) resources are assigned in accordance with the established fund purpose and approved appropriation. Residual fund balances in these fund types that are not restricted or committed are reported as assigned.

Unassigned – includes the residual fund balance that has not been restricted, committed, or assigned within the general fund and deficit fund balances of other governmental funds.

(n) Net Assets

In the government-wide and proprietary fund statements of net assets, equity is displayed in three components as follows:

Invested in Capital Assets – This consists of capital assets, net of accumulated depreciation and amortization.

Restricted – This consists of net assets that are 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 assets that do not meet the definition of "restricted" or "invested 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 and liabilities 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) Future Adoption of GASB Statements

GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, will be effective for the Department beginning with its year end June 30, 2013. The objective of the Statement is to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements.

GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* will be effective for the Department beginning with its year end June 30, 2013. The objective of this statement is to provide financial reporting guidance for deferred outflows and inflows of resources and to rename the residual measure from "Net Assets" to "Net Position".

The Department has not yet determined the impact these statements will have on financial reporting.

(3) Deposits and Investments

The State Treasurer is the custodian of the Department's deposits and investments for funds maintained in the State Treasury. These amounts are classified as "Cash equity in State Treasury", and "Securities Lending Collateral Equity with State Treasurer" on the Statement of Net Assets and Balance Sheets. The Department independently manages deposits and investments maintained outside the State Treasury.

(a) Deposits

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 is available within the State of Illinois' Comprehensive Annual Financial Report.

(b) Investments

As of June 30, 2011, the Department had the following investments outside of the State Treasury:

	Fair Value (Thousands)	Weighted Average Maturity (Years)
Enterprise Funds		
Annuities	$ 525	5.449
Fiduciary Funds		
U.S. Treasury zero coupon securities	370,719	5.333

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: Prior to July 30, 1985, the Department did not have a formal investment policy that limited investment choices. Subsequent to July 30, 1985, the Department is limited to investing in direct obligations of the United States of America or backed by the full faith and credit of the United States of America. The Department's investments in annuities are not rated.

(c) Securities Lending Transactions

Under the authority of the Treasurer's published investment policy that was developed in accordance with the State statute, 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 Group to lend the State Treasurer's securities to broker-dealers and banks pursuant to a form of loan agreement.

During fiscal year 2011, Deutsche Bank Group lent 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 aggregate market value of the loaned securities. Loans are marked to market daily. If the market value of collateral falls below 100%, the borrower must provide additional collateral to raise the market value to 100%.

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

During the fiscal year, 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 Group 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 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.

In accordance with GASB Statement No. 28, paragraph 9, the Office of the State Treasurer has allocated the assets and obligations at June 30, 2011 arising from securities lending agreements to the various funds of the State. The total allocated to the Department was $185.260 million at June 30, 2011 including $130.878 million allocated to agency funds administered by the Department.

(4) Taxes Receivable

Taxes receivable (amounts expressed in thousands) at June 30, 2011 are as follows:

	General Fund	Nonmajor Governmental Funds	Fiduciary Funds
Taxes receivable:			
Income	$ 849,977	$ 87,258	$ -
Sales	699,104	228,266	193,315
Motor fuel tax	-	134,657	-
Public utility	11,742	8,085	1,768
Other	75,595	17,289	7,023
Total taxes receivable	$ 1,636,418	$ 475,555	$ 202,106
Less: allowance for uncollectible taxes	$ 662,709	$ 139,623	$ 75,185
Taxes receivable, net	$ 973,709	$ 335,932	$ 126,921

(5) Loans and Notes Receivable

The Senior Citizen Real Estate Tax Deferral program is a tax-relief program that works like a loan. It allows qualified seniors to defer all or part of their taxes and special assessments on their primary home. The loan, which comes from the State of Illinois, is re-paid when the property is sold, or upon the death of the participant.

Loans receivable (amounts expressed in thousands) at June 30, 2011 are as follows:

	Nonmajor Governmental Funds
Senior Citizens Real Estate Deferred Tax	$ 36,685

(6) Interfund Balances and Activity

(a) Balances Due from/to Other Funds

The following balances (amounts expressed in thousands) at June 30, 2011 represent amounts due from other Department and other State funds.

	Due from			
Fund	**Other Department Funds**	**Other State Funds**	**Other Department Fiduciary Funds**	**Description/Purpose**
General	$ 279,107	$ 4,055	$ -	Due from other Department funds pursuant to statutory tax allocations and for administrative cost reimbursements, and due from other State funds pursuant to statutory tax allocations.
Nonmajor governmental funds	406,975	147,267	-	Due from other Department funds pursuant to statutory tax allocations, administrative cost reimbursements, and allocation of lottery proceeds and from other State fund for advances of services purchased.
Lottery	101,659	-	328	Due from General Fund for cumulative overpayment of lottery profits, and from other Department fiduciary funds for unclaimed lottery prizes.
Fiduciary Funds	84,189	-	-	Due from other Department funds pursuant to statutory tax allocations.
	$ 871,930	$ 151,322	$ 328	

The following balances (amounts expressed in thousands) at June 30, 2011 represent amounts due to other Department and other State funds

	Due to				
Fund	**Other Department Funds**	**Other State Funds**	**Other Department Fiduciary Funds**	**Other State Fiduciary Funds**	**Description/Purpose**
General	$ 456,690	$ 482,278	$ 55,763	$ -	Due to other Department funds and other Department fiduciary funds pursuant to statutory tax allocations and cumulative overpayment of lottery profits and due to other State funds for administrative expenses.
Nonmajor governmental funds	331,051	3,303	28,426	416	Due to other Department funds and other State funds pursuant to statutory tax and fee allocations, for administrative cost reimbursements, and for administrative expenses, other Department fiduciary funds pursuant to statutory tax allocations, and to other State fiduciary funds for payment of retirement benefits.
Lottery	-	414	-	-	Due to other State funds for allocation of lottery proceeds.
Fiduciary Funds	328	-	-	-	Due to Lottery Fund for unclaimed lottery prizes.
	$ 788,069	$ 485,995	$ 84,189	$ 416	

(b) Transfers from/to Other Funds

Interfund transfers in (amounts expressed in thousands) for the year ended June 30, 2011, were as follows:

	Transfers in from		
Fund	**Other Department Funds**	**Other State Funds**	**Description/Purpose**
General	$ 671,457	$ 247	Transfers from Lottery Fund for lottery profits and other Department funds and other State funds pursuant to statutory tax allocations.
Nonmajor governmental funds	149,382	-	Transfers from other Department funds pursuant to statutory tax allocations.
	$ 820,839	$ 247	

Interfund transfers out (amounts expressed in thousands) for the year ended June 30, 2011, were as follows:

	Transfers out to		
Fund	**Other Department Funds**	**Other State Funds**	**Description/Purpose**
General	$ 111,582	$ 278,646	Transfers to other Department funds and other State funds pursuant to statutory tax allocations.
Nonmajor governmental funds	45,021	-	Transfers to other Department funds pursuant to statutory tax allocations.
Lottery Fund	664,236	4,052	Transfers to General Fund for lottery profits and to other State funds for budget shortfalls.
	$ 820,839	$ 282,698	

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

The Illinois Housing Development Authority owes the Department's nonmajor governmental funds $327.833 million at June 30, 2011 for advances on loan programs. The General Fund owes $36 thousand at June 30, 2011 to State of Illinois Component Units for reimbursements for expenses incurred.

(7) Capital and Intangible Assets

Capital asset activity (amounts expressed in thousands) for the year ended June 30, 2011 was as follows:

	Balance July 1, 2010	Additions	Deletions	Net Transfers	Balance June 30, 2011
Governmental activities:					
Capital assets being depreciated/amortized:					
Equipment	$ 5,418	$ 311	$ (50)	$ (174)	$ 5,505
Internally generated computer software	5,114	5,785	-	-	10,899
Total capital and intangible assets being depreciated/ amortized	10,532	6,096	(50)	(174)	16,404
Less accumulated depreciation/amortization:					
Equipment	4,409	399	(50)	(174)	4,584
Internally generated computer software	511	1,090	-	-	1,601
Total accumulated depreciation/amortization	4,920	1,489	(50)	(174)	6,185
Total Governmental activity capital assets, net	$ 5,612	$ 4,607	$ -	$ -	$ 10,219

	Balance July 1, 2010	Additions	Deletions	Net Transfers	Balance June 30, 2011
Business-type activities:					
Capital assets being depreciated:					
Equipment	$ 2,142	$ 6	$ (19)	$ (96)	$ 2,033
Less accumulated depreciation:					
Equipment	1,731	148	(19)	(96)	1,764
Business-type activity capital assets, net	$ 411	$ (142)	$ -	$ -	$ 269

Depreciation/amortization expense for governmental activities (amounts expressed in thousands) for the year ended June 30, 2011 was charged to functions as follows:

General government	$ 1,489

(8) Long-Term Obligations

(a) Changes in Long-Term Obligations

Changes in long-term obligations (amounts expressed in thousands) for the year ended June 30, 2011 were as follows:

	Balance July 1, 2010	Additions	Deletions	Balance June 30, 2011	Amounts Due Within One Year
Governmental activities:					
Compensated Absences	$ 16,059	$ 10,082	$ 10,189	$15,952	$ 1,100
Total governmental activities	$ 16,059	$ 10,082	$ 10,189	$15,952	$ 1,100
Business-type activities:					
Compensated Absences	$ 1,373	$ 867	$ 824	$ 1,416	$ 97
Obligations to Lottery prizewinners	559	32	66	525	59
Total business-type activities	$ 1,932	$ 899	$ 890	$ 1,941	$ 156

Compensated absences will be liquidated by the applicable governmental funds that account for the salaries and wages of the related employees.

(b) Obligations to Lottery Prize Winners

The State has obligations to certain lottery prize winners for awards payable in annual installments ranging from nineteen years to the life of the prize winner, with the first payment being made after the claim is presented for payment. In addition, the State has fulfilled its obligations for certain other prize winners through the purchase of annuities under group contracts.

For certain prize winners, annuities were purchased in the name of the State for which the State has retained the rights of ownership. Effective July 30, 1985, State law provides that the State Treasurer, with the consent of the Director of Revenue, may contract to invest in securities, which provide payments corresponding to the Lottery's obligation to these winners. The present value of these annuities and the related liabilities owed to prize winners, $525 thousand, have been reported in the financial statements of the State Lottery Fund, a nonmajor enterprise fund.

In addition to the prize obligations discussed above, the State has provided for other payments corresponding to the Lottery's obligation to prize winners through the purchase of direct obligations of the federal government, primarily in the form of United States Treasury zero coupon bonds.

As established by State law, such securities shall be maintained in the Deferred Lottery Prize Winners Trust Fund, a special trust fund separate and apart from all public money or funds of the State. These investments are purchased in amounts to provide for annual annuity payments to the prize winner(s) of each qualifying individual drawing. Since these monies are invested by the State on behalf of external legally separate entities (the prize winners), with specific investments being acquired for these individual entities for which the income from and changes in the value of the investments affect only the prize winners for whom they were acquired, in accordance with the provisions of GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools, the Deferred Lottery Prize Winners Trust Fund* is reported as an investment trust fund. The investments of the fund were $370.719 million at June 30, 2011, and the net assets are reported as held in trust for prizewinners.

(9) Pension Plan

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 pension trust fund in the State of Illinois reporting entity. The SERS is a single-employer defined benefit public employee retirement system (PERS) in which State employees participate, except those covered by the State Universities, Teachers', General Assembly, and Judges' Retirement Systems. The financial position and results of operations of the SERS are included in the State of Illinois' Comprehensive Annual Financial Report (CAFR) for the year ended June 30, 2011. The SERS issues a separate CAFR that may be obtained by writing to the SERS, 2101 South Veterans Parkway, Springfield, Illinois, 62794-9255.

A summary of SERS benefit 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 SERS' CAFR. Also included is a discussion of employer and employee obligations to contribute and the authority under which those obligations are established.

The Department pays employer retirement contributions based upon an actuarially determined percentage of their payrolls. For fiscal year 2011, the employer contribution rate was 27.988%. Effective for pay periods beginning after December 31, 1991, the State opted to pay the employee portion of retirement for most State agencies (including the Department) with employees covered by the State Employees' and Teachers' Retirement Systems.

However, effective with the fiscal year 2004 budget, the State opted to stop paying the portion or a part of the portion of retirement for many State agencies (including the Department) for certain classes of employees covered by the State Employees' and Teachers' Retirement Systems. The pickup, when applicable, is subject to sufficient annual appropriations and those employees covered may vary across employee groups and State agencies.

(10) Post-employment Benefits

The State provides health, dental, vision, and life insurance benefits for retirees and their dependents in a program administered by the Department of Healthcare and Family Services along with the Department of Central Management Services. Substantially all State employees become eligible for post-employment benefits if they eventually become annuitants of one of the State sponsored pension plans. Health, dental, and vision benefits include basic benefits for annuitants and dependents under the State's self-insurance plan and insurance contracts currently in force. 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. Annuitants also receive life insurance coverage equal to the annual salary of the last day of employment until age 60, at which time the benefit 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 an expense 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 benefit 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 Healthcare and Family Services. A copy of the financial statements of the Department of Healthcare and Family Services may be obtained by writing to the Department of Healthcare and Family Services, 201 South Grand Ave., Springfield, Illinois, 62763-3838.

(11) Fund Balance

(a) Categories

At June 30, 2011, the Department's fund balances were classified as follows:

	General Fund	Nonmajor Special Revenue Funds	Total
Nonspendable:			
Inventory	$ 379	$ -	$ 379
Long-term Loans Receivable	-	36,685	36,685
Total Nonspendable	$ 379	$ 36,685	$ 37,064
Restricted purpose:			
General Government	$ -	$ 12,133	$ 12,133
Committed purpose:			
General Government	$ 160,723	$ 106,456	$ 267,179
Health and Social Services	-	375,315	375,315
Employment and Economic Development	-	4,936	4,936
Environment and Business Regulation	950	17,636	18,586
Education	147,095	-	147,095
Capital outlay	-	43,946	43,946
Total Committed	$ 308,768	$ 548,289	$ 857,057
Total Unassigned	$ (1,949,735)	$ (396,321)	$ (2,346,056)
Total fund balances	$ (1,640,588)	$ 200,786	$ (1,439,802)

(b) Fund Deficits

The General Fund ($1.641 billion) and the Illinois Gaming Law Enforcement ($441 thousand), State & Local Sales Tax Reform ($2.353 million), School Infrastructure ($1.206 million), Local Government Tax ($5.357 million), Illinois Tax Increment ($1.279 million), and Personal Property Tax Replacement Fund ($385.685 million), nonmajor governmental funds, had fund deficits at June 30, 2011. The fund deficit in the General Fund will be eliminated through the collection and allocation of future State revenues to the Department. The fund deficits in the State & Local Sales Tax Reform, County & Mass Transit, and the Local Government Tax funds will be eliminated by future recognition of earned but unavailable revenues. The fund deficit of the Illinois Gaming Law Enforcement, Illinois Tax Increment, and the Personal Property Tax Replacement funds will be eliminated through future revenues earned.

(12) 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.

The Department's risk management activities 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, 2011.

(13) Commitments and Contingencies

(a) Operating leases

The Department leases certain office space under annual agreements which require the Department to make minimum lease payments. Rent expense under operating leases was $8.703 million for the year ended June 30, 2011.

(b) Litigation

The Department is routinely involved in a number of legal proceedings and claims that cover a wide range of matters. In the opinion of management, the outcome of these matters is not expected to have any material adverse effect on the financial position or results of operations of the Department.

(14) Restatement for Implementation of New Accounting Standard

As shown in the following table, the financial statements of the Department have been restated for the implementation of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*. The Illinois Sports Facility Fund (225), the Predatory Lending Database Program Fund (478), and the Municipal Economic Development Fund (650) were presented as nonmajor special revenue funds in previous years but were reclassified to the General Fund based upon criteria of GASB Statement No. 54.

	General Fund	Nonmajor Governmental Funds
Fund Balance, June 30, 2010, as previously reported	$ (2,128,256)	$ 289,759
Implementation of GASB 54	950	(950)
Fund Balance, July 1, 2010, as restated	$ (2,127,306)	$ 288,809

(15) Subsequent Events

Effective October 15, 2011, the Department transferred all functions performed for the Illinois Lottery and all associated powers, duties, rights and responsibilities to the Illinois Department of Lottery in accordance with Public Act 97-0464.

State of Illinois

Department of Revenue

Combining Schedule of Accounts - General Fund

June 30, 2011 (Expressed in Thousands)

	General Revenue Account 0001	Common School Special 0005	Education Assistance 0007	Illinois Sports Facility 0225	Income Tax Refund 0278	Common School 0412	Predatory Lending Database Program 0478	Municipal Economic Development 0650	Capital Projects 0694	Elimin-ations	Total
ASSETS											
Unexpended appropriation	$ 23,800	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 23,800
Cash equity in State Treasury	319,406	98,926	12,862	5,762	51,953	4,988	300	91	140,580	-	634,868
Securities lending collateral with State Treasurer	-	-	-	-	-	-	-	33	-	-	33
Taxes receivable, net	757,917	99,967	30,129	4,513	59,450	1,245	-	1	20,487	-	973,709
Intergovernmental receivables	-	-	-	-	200	-	-	-	-	-	200
Due from other Department funds	110,090	-	5,390	625	163,002	-	-	-	-	-	279,107
Due from other State funds	-	-	-	3,200	-	-	650	205	-	-	4,055
Inventories	379	-	-	-	-	-	-	-	-	-	379
Total assets	$ 1,211,592	$ 198,893	$ 48,381	$ 14,100	$ 274,605	$ 6,233	$ 950	$ 330	$ 161,067	$ -	$ 1,916,151
LIABILITIES											
Accounts payable and accrued liabilities	$ 237,668	$ 58,810	$ -	$ -	$ -	$ 4,174	$ -	$ 196	$ -	$ -	$ 300,848
Income tax refunds payable	-	-	-	-	1,669,732	-	-	-	-	-	1,669,732
Intergovernmental payables	5,235	-	-	14,100	-	-	-	100	-	-	19,435
Obligations under securities lending - State Treasurer	-	-	-	-	-	-	-	33	-	-	33
Due to other Department fiduciary funds	55,763	-	-	-	-	-	-	-	-	-	55,763
Due to other Department funds	355,031	-	-	-	-	101,659	-	-	-	-	456,690
Due to other State funds	482,278	-	-	-	-	-	-	-	-	-	482,278
Due to State of Illinois component units	36	-	-	-	-	-	-	-	-	-	36
Unavailable revenue	96,977	9,294	6,510	-	11,852	115	-	1	344	-	125,093
Unearned revenue	324,635	-	25,565	-	96,631	-	-	-	-	-	446,831
Total liabilities	1,557,623	68,104	32,075	14,100	1,778,215	105,948	-	330	344	-	3,556,739
FUND BALANCES (DEFICITS)											
Nonspendable - Inventory	379	-	-	-	-	-	-	-	-	-	379
Committed	-	130,789	16,306	-	-	-	950	-	160,723	-	308,768
Unassigned	(346,410)	-	-	-	(1,503,610)	(99,715)	-	-	-	-	(1,949,735)
Total fund balances (deficits)	(346,031)	130,789	16,306	-	(1,503,610)	(99,715)	950	-	160,723	-	(1,640,588)
Total liabilities and fund balances (deficits)	$ 1,211,592	$ 198,893	$ 48,381	$ 14,100	$ 274,605	$ 6,233	$ 950	$ 330	$ 161,067	$ -	$ 1,916,151

State of Illinois

Department of Revenue

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

For the Year Ended June 30, 2011 (Expressed in Thousands)

	General Revenue Account 0001	Common School Special 0005	Education Assistance 0007	Illinois Sports Facility 0225	Income Tax Refund 0278	Common School 0412	Predatory Lending Database Program 0478	Municipal Economic Develop-ment 0650	Capital Projects 0694	Elimin-ations	Total
REVENUES											
Income taxes	$ 11,330,683	$ -	$ 974,747	$ -	$ (30,497)	$ 116,469	$ -	$ -	$ -	$ -	$ 12,391,402
Sales taxes	5,021,918	1,714,745	-	-	-	61,447	-	-	52,023	-	6,850,133
Public utility taxes	1,005,600	-	-	-	-	115,473	-	83	-	-	1,121,156
Other taxes	459,857	-	-	-	-	118,591	-	-	183,259	-	761,707
Licenses and fees	5,045	-	-	-	-	229	-	-	-	-	5,274
Other charges for services	3,683	-	-	-	-	-	-	-	-	-	3,683
Other	3,285	-	-	-	-	-	-	-	-	-	3,285
Total revenues	17,830,071	1,714,745	974,747	-	(30,497)	412,209	-	83	235,282	-	21,136,640
EXPENDITURES											
General government	168,460	-	-	-	(20,000)	-	-	330	-	-	148,790
Employment and economic development	-	-	-	5,625	-	-	-	-	-	-	5,625
Capital outlay	3,259	-	-	-	-	-	-	-	-	-	3,259
Total expenditures	171,719	-	-	5,625	(20,000)	-	-	330	-	-	157,674
Excess (deficiency) of revenues over (under) expenditures	17,658,352	1,714,745	974,747	(5,625)	(10,497)	412,209	-	(247)	235,282	-	20,978,966
OTHER SOURCES (USES) OF FINANCIAL RESOURCES											
Appropriations from State resources	139,092	-	-	-	-	-	-	-	-	-	139,092
Lapsed appropriations	(5,539)	-	-	-	-	-	-	-	-	-	(5,539)
Receipts collected and transmitted to State Treasury	(18,594,630)	-	(954,554)	-	-	(416,217)	-	-	(163,710)	-	(20,129,111)
Amount of SAMS transfers-in	(2,334)	-	-	-	-	(2,332,279)	-	-	-	-	(2,334,613)
Amount of SAMS transfers-out	1,556,349	-	-	-	-	-	-	-	-	-	1,556,349
Transfers-in	1,596	-	-	5,625	-	2,310,515	-	247	54,125	(1,700,404)	671,704
Transfers-out	(277,276)	(1,700,404)	-	-	(112,952)	-	-	-	-	1,700,404	(390,228)
Net other sources (uses) of financial resources	(17,182,742)	(1,700,404)	(954,554)	5,625	(112,952)	(437,981)	-	247	(109,585)	-	(20,492,346)
Net change in fund balances	475,610	14,341	20,193	-	(123,449)	(25,772)	-	-	125,697	-	486,620
FUND BALANCES (DEFICITS)											
July 1, 2010, as restated	(821,739)	116,448	(3,887)	-	(1,380,161)	(73,943)	950	-	35,026	-	(2,127,306)
Decrease for changes in inventories	98	-	-	-	-	-	-	-	-	-	98
JUNE 30, 2011	$ (346,031)	$ 130,789	$ 16,306	$ -	$ (1,503,610)	$ (99,715)	$ 950	$ -	$ 160,723	$ -	$ (1,640,588)

Combining Balance Sheet - Nonmajor Governmental Funds

June 30, 2011 (Expressed in Thousands)

	Special Revenue							
	Motor Fuel Tax 0012	Public Utility 0059	Underground Storage Tank 0072	Illinois Gaming Law Enforcement 0085	IDOR Federal Trust 0140	Rental Housing Support Program 0150	State & Local Sales Tax Reform 0186	RTA Occupation and Use Tax Replacement 0187
ASSETS								
Unexpended appropriations	$ 5,789	$ -	$ -	$ 114	$ -	$ -	$ -	$ -
Cash equity in State Treasury	757	1,591	-	23	376	12,796	51,112	-
Cash and cash equivalents	-	-	-	-	-	-	-	-
Securities lending collateral with State Treasurer	-	-	-	-	-	-	-	-
Taxes receivable, net	104,385	1	6,361	562	-	-	15,517	-
Other receivables, net	-	3,823	-	-	-	-	-	-
Due from other Department funds	-	-	-	-	-	-	-	6,542
Due from other State funds	-	-	-	-	-	5,857	-	-
Loans and notes receivable, long-term	-	-	-	-	-	-	-	-
Due from State of Illinois component units	-	-	-	-	-	-	-	-
Total assets	$ 110,931	$ 5,415	$ 6,361	$ 699	$ 376	$ 18,653	$ 66,629	$ 6,542
LIABILITIES								
Accounts payable and accrued liabilities	$ 9,627	$ 21	$ -	$ 41	$ 6	$ 6,930	$ -	$ -
Intergovernmental payables	230	-	239	980	-	-	14,685	6,542
Obligations under securities lending - State Treasurer	-	-	-	-	-	-	-	-
Due to other Department fiduciary funds	-	-	-	-	-	-	-	-
Due to other State fiduciary funds	245	-	-	4	-	-	-	-
Due to other Department funds	-	-	-	-	-	-	51,944	-
Due to other State funds	2,461	-	-	95	-	-	-	-
Unavailable revenue	5,666	1	512	20	-	-	2,353	-
Unearned revenue	-	-	-	-	-	-	-	-
Total liabilities	18,229	22	751	1,140	6	6,930	68,982	6,542
FUND BALANCES (DEFICITS)								
Nonspendable (long-term loans receivable)	-	-	-	-	-	-	-	-
Restricted	-	-	-	-	370	11,723	-	-
Committed	92,702	5,393	5,610	-	-	-	-	-
Unassigned	-	-	-	(441)	-	-	(2,353)	-
Total fund balances (deficits)	92,702	5,393	5,610	(441)	370	11,723	(2,353)	-
Total liabilities and fund balances (deficits)	$ 110,931	$ 5,415	$ 6,361	$ 699	$ 376	$ 18,653	$ 66,629	$ 6,542

(Continued)

State of Illinois
Department of Revenue

Combining Balance Sheet - Nonmajor Governmental Funds - Continued

June 30, 2011 (Expressed in Thousands)

	Special Revenue							
	County & Mass Transit 0188	Local Govt Tax 0189	Emergency Public Health 0240	Debt Collection 0279	Illinois Tax Increment 0281	Illinois Affordable Housing Trust 286	Used Tire Management 0294	Natural Areas Acquisition 0298
ASSETS								
Unexpended appropriations	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Cash equity in State Treasury	60,538	193,750	-	13	3,502	12,029	-	210
Cash and cash equivalents	-	-	-	-	-	-	-	-
Securities lending collateral with State Treasurer	-	-	-	-	840	4,127	-	-
Taxes receivable, net	18,701	90,955	-	-	1,145	-	-	-
Other receivables, net	-	-	750		1	5	2,856	-
Due from other Department funds	3,480	-	-	-	-	-	-	-
Due from other State funds	-	100,000	-	27	-	27,023	-	-
Loans and notes receivable, long-term	-	-	-	-	-	-	-	-
Due from State of Illinois component units	-	-	-	-	-	327,833	-	-
Total assets	$ 82,719	$ 384,705	$ 750	$ 40	$ 5,488	$ 371,017	$ 2,856	$ 210
LIABILITIES								
Accounts payable and accrued liabilities	$ -	$ -	$ -	$ -	$ 816	$ -	$ -	$ -
Intergovernmental payables	52,901	343,462	-	-	4,999	-	-	-
Obligations under securities lending - State Treasurer	-	-	-	-	840	4,127	-	-
Due to other Department fiduciary funds	28,426	-	-	-	-	-	-	-
Due to other State fiduciary funds	-	-	-	-	3	-	-	-
Due to other Department funds	-	41,243	-	-	-	-	400	-
Due to other State funds	-	-	-	-	3	-	-	-
Unavailable revenue	1,392	5,357	16	-	106	-	67	-
Unearned revenue	-	-	-	-	-	-	-	-
Total liabilities	82,719	390,062	16	-	6,767	4,127	467	-
FUND BALANCES (DEFICITS)								
Nonspendable (long-term loans receivable)	-	-	-	-	-	-	-	-
Restricted	-	-	-	40	-	-	-	-
Committed	-	-	734	-	-	366,890	2,389	210
Unassigned	-	(5,357)	-	-	(1,279)	-	-	-
Total fund balances (deficits)	-	(5,357)	734	40	(1,279)	366,890	2,389	210
Total liabilities and fund balances (deficits)	$ 82,719	$ 384,705	$ 750	$ 40	$ 5,488	$ 371,017	$ 2,856	$ 210

(Continued)

Combining Balance Sheet - Nonmajor Governmental Funds - Continued

June 30, 2011 (Expressed in Thousands)

	Special Revenue						
	Open Space Lands Acquisition & Development 0299	Tax Compliance and Administration 0384	Local Government Distributive 0515	Drycleaner Environmental Response 0548	Supplemental Low Income Energy Assistance 0550	Renewable Energy Resource 0564	School Infrastructure 0568
ASSETS							
Unexpended appropriations	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Cash equity in State Treasury	489	2,475	56	-	-	-	2,206
Cash and cash equivalents	-	-	-	-	-	-	-
Securities lending collateral with State Treasurer	-	-	-	-	-	-	-
Taxes receivable, net	-	718	-	127	4,744	-	503
Other receivables, net	-	1	-	-	-	296	-
Due from other Department funds	-	-	387,503	-	-	-	-
Due from other State funds	-	12,805	-	-	-	-	-
Loans and notes receivable, long-term	-	-	-	-	-	-	-
Due from State of Illinois component units	-	-	-	-	-	-	-
Total assets	$ 489	$ 15,999	$ 387,559	$ 127	$ 4,744	$ 296	$ 2,709
LIABILITIES							
Accounts payable and accrued liabilities	$ -	$ 157	$ -	$ -	$ -	$ -	$ 3,819
Intergovernmental payables	-	5	386,934	-	-	-	-
Obligations under securities lending - State Treasurer	-	-	-	-	-	-	-
Due to other Department fiduciary funds	-	-	-	-	-	-	-
Due to other State fiduciary funds	-	20	-	-	-	-	-
Due to other Department funds	-	-	625	-	-	-	-
Due to other State funds	-	64	-	-	-	-	-
Unavailable revenue	-	145	-	-	-	-	96
Unearned revenue	-	-	-	-	-	-	-
Total liabilities	-	391	387,559	-	-	-	3,915
FUND BALANCES (DEFICITS)							
Nonspendable (long-term loans receivable)	-	-	-	-	-	-	-
Restricted	-	-	-	-	-	-	-
Committed	489	15,608	-	127	4,744	296	-
Unassigned	-	-	-	-	-	-	(1,206)
Total fund balances (deficits)	489	15,608	-	127	4,744	296	(1,206)
Total liabilities and fund balances (deficits)	$ 489	$ 15,999	$ 387,559	$ 127	$ 4,744	$ 296	$ 2,709

(Continued)

Combining Balance Sheet -
Nonmajor Governmental Funds - Continued

June 30, 2011 (Expressed in Thousands)

	Special Revenue							
	International Tourism 0621	Personal Property Tax Replacement 0802	Dram Shop 0821	Senior Citizen Real Estate Deferred Tax 0930	Build Illinois 0960	Local Tourism 0969	Evidence Fund 1369	Total
ASSETS								
Unexpended appropriations	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 5,903
Cash equity in State Treasury	712	303,776	3,224	1,569	13,336	1,266	-	665,806
Cash and cash equivalents	-	-	-	-	-	-	3	3
Securities lending collateral with State Treasurer	-	49,382	-	-	-	-	-	54,349
Taxes receivable, net	1,138	53,420	-	-	35,660	1,995	-	335,932
Other receivables, net	-	56	-	10,171	-	-	-	17,959
Due from other Department funds	-	-	-	-	9,450	-	-	406,975
Due from other State funds	-	-	-	1,555	-	-	-	147,267
Loans and notes receivable, long-term	-	-	-	36,685	-	-	-	36,685
Due from State of Illinois component units	-	-	-	-	-	-	-	327,833
Total assets	$ 1,850	$ 406,634	$ 3,224	$ 49,980	$ 58,446	$ 3,261	$ 3	$ 1,998,712
LIABILITIES								
Accounts payable and accrued liabilities	$ 26	$ 40,635	$ 84	$ -	$ 14,160	$ 48	$ -	$ 76,370
Intergovernmental payables	-	311,061	-	177	-	-	-	1,122,215
Obligations under securities lending - State Treasurer	-	49,382	-	-	-	-	-	54,349
Due to other Department fiduciary funds	-	-	-	-	-	-	-	28,426
Due to other State fiduciary funds	-	143	1	-	-	-	-	416
Due to other Department funds	-	236,839	-	-	-	-	-	331,051
Due to other State funds	-	660	20	-	-	-	-	3,303
Unavailable revenue	47	11,636	-	10,171	2,194	54	-	39,833
Unearned revenue	-	141,963	-	-	-	-	-	141,963
Total liabilities	73	792,319	105	10,348	16,354	102	-	1,797,926
FUND BALANCES (DEFICITS)								
Nonspendable (long-term loans receivable)	-	-	-	36,685	-	-	-	36,685
Restricted	-	-	-	-	-	-	-	12,133
Committed	1,777	-	3,119	2,947	42,092	3,159	3	548,289
Unassigned	-	(385,685)	-	-	-	-	-	(396,321)
Total fund balances (deficits)	1,777	(385,685)	3,119	39,632	42,092	3,159	3	200,786
Total liabilities and fund balances (deficits)	$ 1,850	$ 406,634	$ 3,224	$ 49,980	$ 58,446	$ 3,261	$ 3	$ 1,998,712

State of Illinois

Department of Revenue

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

For the Year Ended June 30, 2011 (Expressed in Thousands)

	Special Revenue							
	Motor Fuel Tax 0012	Public Utility 0059	Underground Storage Tank 0072	Illinois Gaming Law Enforcement 0085	IDOR Federal Trust 0140	Rental Housing Support Program 0150	State & Local Sales Tax Reform 0186	RTA Occupation and Use Tax Replacement 0187
REVENUES								
Federal operating grants	$ 116	$ -	$ -	$ -	$ 369	$ -	$ -	$ -
Income taxes	-	-	-	-	-	-	-	-
Sales taxes	-	-	-	-	-	-	88,783	26,951
Motor fuel taxes	1,228,648	-	70,731	-	-	-	-	-
Public utility taxes, Net	-	8,585	-	-	-	-	-	-
Other taxes	-	-	-	2,616	-	18,233	-	-
License and fees	3,254	3,823	-	300	-	-	-	-
Other charges for services	2	-	-	-	-	-	-	-
Interest and other investment income	-	-	-	-	-	-	-	-
Other	-	-	-	-	-	-	-	-
Total revenues	1,232,020	12,408	70,731	2,916	369	18,233	88,783	26,951
EXPENDITURES								
General government	43,753	-	1,385	-	34	12,394	-	-
Health and social services	-	-	-	-	-	-	-	-
Environment and business regulation	-	-	-	-	-	-	-	-
Intergovernmental	-	-	-	1,697	-	-	52,015	26,951
Capital outlay	968	-	-	-	-	-	-	-
Total expenditures	44,721	-	1,385	1,697	34	12,394	52,015	26,951
Excess (deficiency) of revenues over (under) expenditures	1,187,299	12,408	69,346	1,219	335	5,839	36,768	-
OTHER SOURCES (USES) OF FINANCIAL RESOURCES								
Appropriations from State resources	106,667	-	1,487	2,261	-	-	-	-
Lapsed appropriations	(45,062)	-	(102)	(513)	-	-	-	-
Receipts collected and transmitted to State Treasury	(1,246,398)	(12,515)	(71,164)	(2,935)	-	-	-	-
Amount of SAMS transfers-in	-	-	-	-	-	-	-	-
Amount of SAMS transfers-out	-	-	-	-	-	-	-	-
Transfers-in	-	-	-	-	-	-	-	-
Transfers-out	-	-	-	-	-	-	(37,800)	-
Net other sources (uses) of financial resources	(1,184,793)	(12,515)	(69,779)	(1,187)	-	-	(37,800)	-
Net change in fund balances	2,506	(107)	(433)	32	335	5,839	(1,032)	-
Fund balances (deficits), July 1, 2010, as restated	90,196	5,500	6,043	(473)	35	5,884	(1,321)	-
FUND BALANCES (DEFICITS), JUNE 30, 2011	$ 92,702	$ 5,393	$ 5,610	$ (441)	$ 370	$ 11,723	$ (2,353)	$ -

(Continued)

State of Illinois
Department of Revenue

Combining Statement of Revenues,
Expenditures and Changes in Fund Balance -
Nonmajor Governmental Funds - Continued
For the Year Ended June 30, 2011 (Expressed in Thousands)

	Special Revenue							
	County & Mass Transit 0188	Local Govt Tax 0189	Emergency Public Health 0240	Debt Collection 0279	Illinois Tax Increment 0281	Illinois Affordable Housing Trust 286	Used Tire Management 0294	Natural Areas Acquisition 0298
REVENUES								
Federal operating grants	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Income taxes	-	-	-	-	-	-	-	-
Sales taxes	321,263	1,563,258	-	-	19,903	-	-	-
Motor fuel taxes	-	-	-	-	-	-	-	-
Public utility taxes, Net	-	-	-	-	-	-	-	-
Other taxes	-	-	-	-	-	19,403	-	5,821
License and fees	-	-	3,527	-	-	27	13,400	-
Other charges for services	-	-	-	-	-	-	-	-
Interest and other investment income	-	-	-	-	16	2,131	-	-
Other	-	-	-	8	-	-	-	-
Total revenues	321,263	1,563,258	3,527	8	19,919	21,561	13,400	5,821
EXPENDITURES								
General government	-	-	-	17	-	11,126	-	-
Health and social services	-	-	-	-	-	120	-	-
Environment and business regulation	-	-	-	-	-	-	-	-
Intergovernmental	319,471	1,561,580	-	-	19,716	-	-	-
Capital outlay	-	-	-	-	-	-	-	-
Total expenditures	319,471	1,561,580	-	17	19,716	11,246	-	-
Excess (deficiency) of revenues over (under) expenditures	1,792	1,678	3,527	(9)	203	10,315	13,400	5,821
OTHER SOURCES (USES) OF FINANCIAL RESOURCES								
Appropriations from State resources	-	-	-	-	-	-	-	-
Lapsed appropriations	-	-	-	-	-	-	-	-
Receipts collected and transmitted to State Treasury	-	-	(3,551)	-	-	-	(13,493)	(5,699)
Amount of SAMS transfers-in	-	-	-	-	-	-	-	-
Amount of SAMS transfers-out	-	-	-	-	-	-	1,592	-
Transfers-in	-	-	-	-	-	-	-	-
Transfers-out	-	-	-	-	-	-	(1,596)	-
Net other sources (uses) of financial resources	-	-	(3,551)	-	-	-	(13,497)	(5,699)
Net change in fund balances	1,792	1,678	(24)	(9)	203	10,315	(97)	122
Fund balances (deficits), July 1, 2010, as restated	(1,792)	(7,035)	758	49	(1,482)	356,575	2,486	88
FUND BALANCES (DEFICITS), JUNE 30, 2011	$ -	$ (5,357)	$ 734	$ 40	$ (1,279)	$ 366,890	$ 2,389	$ 210

(Continued)

State of Illinois

Department of Revenue

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

For the Year Ended June 30, 2011 (Expressed in Thousands)

	Special Revenue						
	Open Space Lands Acquisition & Development 0299	**Tax Compliance and Administration 0384**	**Local Government Distributive 0515**	**Drycleaner Environmental Response 0548**	**Supplemental Low Income Energy Assistance 0550**	**Renewable Energy Resource 0564**	**School Infrastructure 0568**
REVENUES							
Federal operating grants	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Income taxes	-	9,783	921,502	-	-	-	-
Sales taxes	-	4,838	149,469	-	-	-	-
Motor fuel taxes	-	18	-	-	-	-	-
Public utility taxes, Net	-	2,201	-	-	91,129		96,893
Other taxes	13,581	8	-	534	-	-	60,000
License and fees	-	980	-	1,974	-	4,840	-
Other charges for services	-	-	-	-	-	-	-
Interest and other investment income	-	-	-	-	-	-	-
Other	-	253	-	-	-	-	-
Total revenues	13,581	18,081	1,070,971	2,508	91,129	4,840	156,893
EXPENDITURES							
General government	-	3,265	-	-	-	-	-
Health and social services	-	-	-	-	-	-	-
Environment and business regulation	-	-	-	-	-	-	-
Intergovernmental	-	-	1,065,346	-	-	-	-
Capital outlay	-	-	-	-	-	-	-
Total expenditures	-	3,265	1,065,346	-	-	-	-
Excess (deficiency) of revenues over (under) expenditures	13,581	14,816	5,625	2,508	91,129	4,840	156,893
OTHER SOURCES (USES) OF FINANCIAL RESOURCES							
Appropriations from State resources	-	-	-	-	-	-	-
Lapsed appropriations	-	-	-	-	-	-	-
Receipts collected and transmitted to State Treasury	(13,297)	-	-	(2,525)	(94,434)	(5,046)	(159,529)
Amount of SAMS transfers-in	-	-	-	-	-	-	-
Amount of SAMS transfers-out	-	-	-	-	-	-	-
Transfers-in	-	-	-	-	-	-	-
Transfers-out	-	-	(5,625)	-	-	-	-
Net other sources (uses) of financial resources	(13,297)	-	(5,625)	(2,525)	(94,434)	(5,046)	(159,529)
Net change in fund balances	284	14,816	-	(17)	(3,305)	(206)	(2,636)
Fund balances (deficits), July 1, 2010, as restated	205	792	-	144	8,049	502	1,430
FUND BALANCES (DEFICITS), JUNE 30, 2011	$ 489	$ 15,608	$ -	$ 127	$ 4,744	$ 296	$ (1,206)

(Continued)

State of Illinois
Department of Revenue

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

For the Year Ended June 30, 2011 (Expressed in Thousands)

	Special Revenue							
	International Tourism 0621	Personal Property Tax Replacement 0802	Dram Shop 0821	Senior Citizen Real Estate Deferred Tax 0930	Build Illinois 0960	Local Tourism 0969	Evidence Fund 1369	Total
REVENUES								
Federal operating grants	$ -	$ -	$ 41	$ -	$ -	$ -	$ -	$ 526
Income taxes	-	1,065,444	-	-	-	-	-	1,996,729
Sales taxes	-	-	-	-	406,227	-	-	2,580,692
Motor fuel taxes	-	-	-	-	-	-	-	1,299,397
Public utility taxes, Net	-	169,827	-	-	-	-	-	368,635
Other taxes	8,894	-	-	-	103,110	15,777	-	247,977
License and fees	-	-	6,328	-	-	-	-	38,453
Other charges for services	-	-	-	-	-	-	-	2
Interest and other investment income	-	411	-	1,151	-	-	-	3,709
Other	-	-	153	33,697	-	-	5	34,116
Total revenues	8,894	1,235,682	6,522	34,848	509,337	15,777	5	6,570,236
EXPENDITURES								
General government	-	23,164	89	-	-	-	5	95,232
Health and social services	-	-	-	-	-	-	-	120
Environment and business regulation	-	-	6,015	-	-	-	-	6,015
Intergovernmental	-	1,481,570	-	-	-	-	-	4,528,346
Capital outlay	-	1,856	15	-	-	-	-	2,839
Total expenditures	-	1,506,590	6,119	-	-	-	5	4,632,552
Excess (deficiency) of revenues over (under) expenditures	8,894	(270,908)	403	34,848	509,337	15,777	-	1,937,684
OTHER SOURCES (USES) OF FINANCIAL RESOURCES								
Appropriations from State resources	-	-	-	-	-	-	-	110,415
Lapsed appropriations	-	-	-	-	-	-	-	(45,677)
Receipts collected and transmitted to State Treasury	(8,706)	-	-	-	(503,865)	(15,441)	-	(2,158,598)
Amount of SAMS transfers-in	-	-	-	-	(37,800)	-	-	(37,800)
Amount of SAMS transfers-out	-	-	-	-	-	-	-	1,592
Transfers-in	-	111,582	-	-	37,800	-	-	149,382
Transfers-out	-	-	-	-	-	-	-	(45,021)
Net other sources (uses) of financial resources	(8,706)	111,582	-	-	(503,865)	(15,441)	-	(2,025,707)
Net change in fund balances	188	(159,326)	403	34,848	5,472	336	-	(88,023)
Fund balances (deficits), July 1, 2010, as restated	1,589	(226,359)	2,716	4,784	36,620	2,823	3	288,809
FUND BALANCES (DEFICITS), JUNE 30, 2011	$ 1,777	$ (385,685)	$ 3,119	$ 39,632	$ 42,092	$ 3,159	$ 3	$ 200,786

State of Illinois

Department of Revenue

Combining Statement of Fiduciary Net Assets - Agency Funds

June 30, 2011 (Expressed in Thousands)

	Agency					
	County Water Commission Tax 0084	Non-Home Rule Municipal ROT 0088	Home Rule Municipal Soft Drink ROT 0097	Home Rule Municipal ROT 0138	Home Rule County ROT 0139	Business District Retailers' Occupation Tax 0160
ASSETS						
Cash equity in State Treasury	$ 6,777	$ 21,467	$ 1,889	$ 119,416	$ 45,231	$ 1,751
Cash and cash equivalents	-	-	-	-	-	-
Securities lending collateral with State Treasurer	2,047	6,596	-	31,663	29,657	-
Taxes receivable, net	1,156	2,499	954	34,520	32,173	791
Other receivables, net	2	8	-	36	34	-
Due from other Department funds	-	-	-	-	-	-
Total assets	$ 9,982	$ 30,570	$ 2,843	$ 185,635	$ 107,095	$ 2,542
LIABILITIES						
Accounts payable and accrued liabilities	$ -	$ -	$ -	$ 1,710	$ -	$ -
Intergovernmental payables	7,935	23,974	2,843	152,262	77,438	2,542
Obligations under securities lending - State Treasurer	2,047	6,596	-	31,663	29,657	-
Other liabilities	-	-	-	-	-	-
Total liabilities	$ 9,982	$ 30,570	$ 2,843	$ 185,635	$ 107,095	$ 2,542

(Continued)

State of Illinois

Department of Revenue

Combining Statement of Fiduciary Net Assets - Agency Funds - Continued

June 30, 2011 (Expressed in Thousands)

	Agency					
	County Option Motor Fuel Tax 0190	**County Public Safety ROT 0219**	**Sports Facility Tax Trust 0229**	**Metropolitan Pier & Expo. Auth. Trust 0337**	**Illinois Tourism Tax 0452**	**School Facility Occupation Tax 498**
ASSETS						
Cash equity in State Treasury	$ 5,801	$ 15,878	$ -	$ 68,538	$ 2,345	$ 5,057
Cash and cash equivalents	-	-	-	-	-	-
Securities lending collateral with State Treasurer	1,726	-	-	23,071	-	-
Taxes receivable, net	2,956	2,351	51	11,193	1,965	1,369
Other receivables, net	2	-	-	26	-	-
Due from other Department funds	-	-	-	-	1,529	-
Total assets	$ 10,485	$ 18,229	$ 51	$ 102,828	$ 5,839	$ 6,426
LIABILITIES						
Accounts payable and accrued liabilities	$ 116	$ -	$ 50	$ -	$ 28	$ -
Intergovernmental payables	8,643	18,229	1	79,757	5,811	6,426
Obligations under securities lending - State Treasurer	1,726	-	-	23,071	-	-
Other liabilities	-	-	-	-	-	-
Total liabilities	$ 10,485	$ 18,229	$ 51	$ 102,828	$ 5,839	$ 6,426

(Continued)

State of Illinois
Department of Revenue

Combining Statement of Fiduciary Net Assets - Agency Funds - Continued

June 30, 2011 (Expressed in Thousands)

	Agency					
	Flood Prevention Occupation Tax 0558	**Tax Suspense Trust 0583**	**Metro East Park & Recreation 0717**	**Municipal Telecom 0719**	**RTA Sales Tax Trust 0812**	**Metro East Mass Transit District Tax 0841**
ASSETS						
Cash equity in State Treasury	$ 2,373	$ 45	$ 1,076	$ 22,151	$ 130,495	$ 6,745
Cash and cash equivalents	-	-	-	-	-	-
Securities lending collateral with State Treasurer	-	-	-	-	33,617	2,065
Taxes receivable, net	629	-	250	1,136	32,194	590
Other receivables, net	-	-	-	-	38	2
Due from other Department funds	-	-	-	54,234	28,426	-
Total assets	$ 3,002	$ 45	$ 1,326	$ 77,521	$ 224,770	$ 9,402
LIABILITIES						
Accounts payable and accrued liabilities	$ -	$ -	$ -	$ 6,150	$ -	$ -
Intergovernmental payables	3,002	-	1,326	71,371	191,153	7,337
Obligations under securities lending - State Treasurer	-	-	-	-	33,617	2,065
Other liabilities	-	45	-	-	-	-
Total liabilities	$ 3,002	$ 45	$ 1,326	$ 77,521	$ 224,770	$ 9,402

(Continued)

State of Illinois

Department of Revenue

Combining Statement of Fiduciary Net Assets - Agency Funds - Continued

June 30, 2011 (Expressed in Thousands)

	Agency				
	Municipal Automobile Renting Tax 0868	County Automobile Renting Tax 0869	Surety Bond 1151	Lottery Agent Security Deposit 1309	Total
ASSETS					
Cash equity in State Treasury	$ 1,363	$ 30	$ -	$ -	$ 458,428
Cash and cash equivalents	-	-	2,020	787	2,807
Securities lending collateral with State Treasurer	426	10	-	-	130,878
Taxes receivable, net	139	5	-	-	126,921
Other receivables, net	-	-	-	-	148
Due from other Department funds	-	-	-	-	84,189
Total assets	$ 1,928	$ 45	$ 2,020	$ 787	$ 803,371
LIABILITIES					
Accounts payable and accrued liabilities	$ -	$ -	$ -	$ -	$ 8,054
Intergovernmental payables	1,502	35	-	-	661,587
Obligations under securities lending - State Treasurer	426	10	-	-	130,878
Other liabilities	-	-	2,020	787	2,852
Total liabilities	$ 1,928	$ 45	$ 2,020	$ 787	$ 803,371

State of Illinois
Department of Revenue
Combining Statement of Changes in Assets and Liabilities - Agency Funds
For the Year Ended June 30, 2011 (Expressed in Thousands)

	Balance at July 1, 2010	Additions	Deletions	Balance at June 30, 2011
County Water Commission Tax (0084)				
ASSETS				
Cash equity in State Treasury	$ 5,790	$ 28,665	$ 27,678	$ 6,777
Securities lending collateral with State Treasurer	2,732	22,101	22,786	2,047
Taxes receivable, net	1,914	27,870	28,628	1,156
Other receivables, net	6	33	37	2
Total assets	$ 10,442	$ 78,669	$ 79,129	$ 9,982
LIABILITIES				
Intergovernmental payables	$ 7,710	$ 27,903	$ 27,678	$ 7,935
Obligations under securities lending - State Treasurer	2,732	22,101	22,786	2,047
Total liabilities	$ 10,442	$ 50,004	$ 50,464	$ 9,982
Non-Home Rule Municipal ROT (0088)				
ASSETS				
Cash equity in State Treasury	$ 17,959	$ 94,845	$ 91,337	$ 21,467
Securities lending collateral with State Treasurer	4,989	51,026	49,419	6,596
Taxes receivable, net	4,910	92,348	94,759	2,499
Other receivables, net	11	83	86	8
Total assets	$ 27,869	$ 238,302	$ 235,601	$ 30,570
LIABILITIES				
Intergovernmental payables	$ 22,880	$ 92,431	$ 91,337	$ 23,974
Obligations under securities lending - State Treasurer	4,989	51,026	49,419	6,596
Total liabilities	$ 27,869	$ 143,457	$ 140,756	$ 30,570
Home Rule Municipal Soft Drink ROT (0097)				
ASSETS				
Cash equity in State Treasury	$ 1,770	$ 8,977	$ 8,858	$ 1,889
Taxes receivable, net	841	9,090	8,977	954
Total assets	$ 2,611	$ 18,067	$ 17,835	$ 2,843
LIABILITIES				
Intergovernmental payables	$ 2,611	$ 9,090	$ 8,858	$ 2,843
Total liabilities	$ 2,611	$ 9,090	$ 8,858	$ 2,843

(Continued)

State of Illinois
Department of Revenue
Combining Statement of Changes in Assets and Liabilities - Agency Funds - Continued
For the Year Ended June 30, 2011 (Expressed in Thousands)

	Balance at July 1, 2010	Additions	Deletions	Balance at June 30, 2011
Home Rule Municipal ROT (0138)				
ASSETS				
Cash equity in State Treasury	$ 97,050	$ 795,158	$ 772,792	$ 119,416
Securities lending collateral with State Treasurer	23,388	244,901	236,626	31,663
Taxes receivable, net	38,455	790,808	794,743	34,520
Other receivables, net	50	401	415	36
Total assets	$ 158,943	$ 1,831,268	$ 1,804,576	$ 185,635
LIABILITIES				
Accounts payable and accrued liabilities	$ 1,752	$ 977	$ 1,019	$ 1,710
Intergovernmental payables	133,803	790,232	771,773	152,262
Obligations under securities lending - State Treasurer	23,388	244,901	236,626	31,663
Total liabilities	$ 158,943	$ 1,036,110	$ 1,009,418	$ 185,635
Home Rule County ROT (0139)				
ASSETS				
Cash equity in State Treasury	$ 91,188	$ 494,927	$ 540,884	$ 45,231
Securities lending collateral with State Treasurer	21,746	251,777	243,866	29,657
Taxes receivable, net	26,036	557,321	551,184	32,173
Other receivables, net	47	342	355	34
Total assets	$ 139,017	$ 1,304,367	$ 1,336,289	$ 107,095
LIABILITIES				
Intergovernmental payables	$ 117,271	$ 557,663	$ 597,496	$ 77,438
Obligations under securities lending - State Treasurer	21,746	251,777	243,866	29,657
Total liabilities	$ 139,017	$ 809,440	$ 841,362	$ 107,095
Business District ROT (0160)				
ASSETS				
Cash equity in State Treasury	$ 1,477	$ 9,357	$ 9,083	$ 1,751
Taxes receivable, net	644	9,504	9,357	791
Total assets	$ 2,121	$ 18,861	$ 18,440	$ 2,542
LIABILITIES				
Intergovernmental payables	$ 2,121	$ 9,504	$ 9,083	$ 2,542
Total liabilities	$ 2,121	$ 9,504	$ 9,083	$ 2,542

(Continued)

Combining Statement of Changes in Assets and Liabilities - Agency Funds - Continued

For the Year Ended June 30, 2011 (Expressed in Thousands)

	Balance at July 1, 2010	Additions	Deletions	Balance at June 30, 2011
County Option Motor Fuel Tax (0190)				
ASSETS				
Cash equity in State Treasury	$ 5,519	$ 32,511	$ 32,229	$ 5,801
Securities lending collateral with State Treasurer	1,435	13,576	13,285	1,726
Taxes receivable, net	2,864	32,579	32,487	2,956
Other receivables, net	3	23	24	2
Total assets	$ 9,821	$ 78,689	$ 78,025	$ 10,485
LIABILITIES				
Accounts payable and accrued liabilities	$ 165	$ 615	$ 664	$ 116
Intergovernmental payables	8,221	31,987	31,565	8,643
Obligations under securities lending - State Treasurer	1,435	13,576	13,285	1,726
Total liabilities	$ 9,821	$ 46,178	$ 45,514	$ 10,485
County Public Safety ROT (0219)				
ASSETS				
Cash equity in State Treasury	$ 12,456	$ 85,893	$ 82,471	$ 15,878
Taxes receivable, net	4,308	83,936	85,893	2,351
Total assets	$ 16,764	$ 169,829	$ 168,364	$ 18,229
LIABILITIES				
Intergovernmental payables	$ 16,764	$ 83,936	$ 82,471	$ 18,229
Total liabilities	$ 16,764	$ 83,936	$ 82,471	$ 18,229
Sports Facility Tax Trust (0229)				
ASSETS				
Cash equity in State Treasury	$ 111	$ -	$ 111	$ -
Taxes receivable, net	90	-	39	51
Total assets	$ 201	$ -	$ 150	$ 51
LIABILITIES				
Accounts payable and accrued liabilities	$ 64	$ 193	$ 207	$ 50
Intergovernmental payables	137	14	150	1
Total liabilities	$ 201	$ 207	$ 357	$ 51

(Continued)

Combining Statement of Changes in Assets and Liabilities - Agency Funds - Continued

For the Year Ended June 30, 2011 (Expressed in Thousands)

	Balance at July 1, 2010	Additions	Deletions	Balance at June 30, 2011
Metro Pier & Exposition Authority Trust (0337)				
ASSETS				
Cash equity in State Treasury	$ 8,919	$ 110,588	$ 50,969	$ 68,538
Securities lending collateral with State Treasurer	2,633	87,113	66,675	23,071
Taxes receivable, net	12,487	109,155	110,449	11,193
Other receivables, net	6	161	141	26
Total assets	$ 24,045	$ 307,017	$ 228,234	$ 102,828
LIABILITIES				
Accounts payable and accrued liabilities	$ -	$ -	$ -	$ -
Intergovernmental payables	21,412	109,316	50,971	79,757
Obligations undersecurities lending - State Treasurer	2,633	87,113	66,675	23,071
Total liabilities	$ 24,045	$ 196,429	$ 117,646	$ 102,828
Illinois Tourism Tax (0452)				
ASSETS				
Cash equity in State Treasury	$ 2,205	$ 15,744	$ 15,604	$ 2,345
Taxes receivable, net	1,794	15,915	15,744	1,965
Due from other Department funds	-	1,529	-	1,529
Total assets	$ 3,999	$ 33,188	$ 31,348	$ 5,839
LIABILITIES				
Accounts payable and accrued liabilities	$ 32	$ 98	$ 102	$ 28
Intergovernmental payables	3,967	17,346	15,502	5,811
Total liabilities	$ 3,999	$ 17,444	$ 15,604	$ 5,839
School Facility Occupation Tax (498)				
ASSETS				
Cash equity in State Treasury	$ 394	$ 30,379	$ 25,716	$ 5,057
Taxes receivable, net	5,824	25,924	30,379	1,369
Total assets	$ 6,218	$ 56,303	$ 56,095	$ 6,426
LIABILITIES				
Intergovernmental payables	$ 6,218	$ 25,924	$ 25,716	$ 6,426
Total liabilities	$ 6,218	$ 25,924	$ 25,716	$ 6,426

(Continued)

State of Illinois

Department of Revenue

Combining Statement of Changes in Assets and Liabilities - Agency Funds - Continued

For the Year Ended June 30, 2011 (Expressed in Thousands)

	Balance at July 1, 2010	Additions	Deletions	Balance at June 30, 2011
Flood Prevention Occupation Tax (558)				
ASSETS				
Cash equity in State Treasury	$ 527	$ 12,920	$ 11,074	$ 2,373
Taxes receivable, net	2,297	11,253	12,921	629
Total assets	$ 2,824	$ 24,173	$ 23,995	$ 3,002
LIABILITIES				
Intergovernmental payables	$ 2,824	$ 11,253	$ 11,075	$ 3,002
Total liabilities	$ 2,824	$ 11,253	$ 11,075	$ 3,002
Tax Suspense Trust (0583)				
ASSETS				
Cash equity in State Treasury	$ 37	$ 8	$ -	$ 45
Total assets	$ 37	$ 8	$ -	$ 45
LIABILITIES				
Other liabilities	$ 37	$ 8	$ -	$ 45
Total liabilities	$ 37	$ 8	$ -	$ 45
Metro East Park and Recreation (0717)				
ASSETS				
Cash equity in State Treasury	$ 920	$ 4,490	$ 4,334	$ 1,076
Taxes receivable, net	253	4,487	4,490	250
Total assets	$ 1,173	$ 8,977	$ 8,824	$ 1,326
LIABILITIES				
Intergovernmental payables	$ 1,173	$ 4,487	$ 4,334	$ 1,326
Total liabilities	$ 1,173	$ 4,487	$ 4,334	$ 1,326
Municipal Telecommunications Fund (0719)				
ASSETS				
Cash equity in State Treasury	$ 37,515	$ 260,789	$ 276,153	$ 22,151
Taxes receivable, net	5,330	256,596	260,790	1,136
Due from other Department funds	31,413	22,821	-	54,234
Total assets	$ 74,258	$ 540,206	$ 536,943	$ 77,521
LIABILITIES				
Accounts payable and accrued liabilities	$ 4,089	$ 73,433	$ 71,372	$ 6,150
Intergovernmental payables	70,169	205,984	204,782	71,371
Total liabilities	$ 74,258	$ 279,417	$ 276,154	$ 77,521

(Continued)

Combining Statement of Changes in Assets and Liabilities - Agency Funds - Continued

For the Year Ended June 30, 2011 (Expressed in Thousands)

	Balance at July 1, 2010	Additions	Deletions	Balance at June 30, 2011
RTA Sales Tax Trust (0812)				
ASSETS				
Cash equity in State Treasury	$ 115,289	$ 1,042,273	$ 1,027,067	$ 130,495
Securities lending collateral with State Treasurer	26,308	293,002	285,693	33,617
Taxes receivable, net	40,194	920,088	928,088	32,194
Other receivables, net	56	460	478	38
Due from other Department funds	26,555	115,578	113,707	28,426
Total assets	$ 208,402	$ 2,371,401	$ 2,355,033	$ 224,770
LIABILITIES				
Intergovernmental payables	$ 182,094	$ 1,036,126	$ 1,027,067	$ 191,153
Obligations under securities lending - State Treasurer	26,308	293,002	285,693	33,617
Total liabilities	$ 208,402	$ 1,329,128	$ 1,312,760	$ 224,770
Metro East Mass Transit Dist. Tax (0841)				
ASSETS				
Cash equity in State Treasury	$ 6,019	$ 29,579	$ 28,853	$ 6,745
Securities lending collateral with State Treasurer	1,692	17,468	17,095	2,065
Taxes receivable, net	1,631	28,509	29,550	590
Other receivables, net	4	27	29	2
Total assets	$ 9,346	$ 75,583	$ 75,527	$ 9,402
LIABILITIES				
Intergovernmental payables	$ 7,654	$ 28,536	$ 28,853	$ 7,337
Obligations under securities lending - State Treasurer	1,692	17,468	17,095	2,065
Total liabilities	$ 9,346	$ 46,004	$ 45,948	$ 9,402
Tennessee Valley Authority Local Trust (0861)				
ASSETS				
Cash equity in State Treasury	$ 25	$ 298	$ 323	$ -
Total assets	$ 25	$ 298	$ 323	$ -
LIABILITIES				
Intergovernmental payables	$ 25	$ 298	$ 323	$ -
Total liabilities	$ 25	$ 298	$ 323	$ -

(Continued)

Combining Statement of Changes in Assets and Liabilities - Agency Funds - Continued

For the Year Ended June 30, 2011 (Expressed in Thousands)

	Balance at July 1, 2010	Additions	Deletions	Balance at June 30, 2011
Municipal Automobile Renting Tax (0868)				
ASSETS				
Cash equity in State Treasury	$ 1,180	$ 5,639	$ 5,456	$ 1,363
Securities lending collateral with State Treasurer	331	3,688	3,593	426
Taxes receivable, net	544	5,228	5,633	139
Other receivables, net	1	5	6	-
Total assets	$ 2,056	$ 14,560	$ 14,688	$ 1,928
LIABILITIES				
Intergovernmental payables	$ 1,725	$ 5,233	$ 5,456	$ 1,502
Obligations under securities lending - State Treasurer	331	3,688	3,593	426
Total liabilities	$ 2,056	$ 8,921	$ 9,049	$ 1,928
County Automobile Renting Tax (0869)				
ASSETS				
Cash equity in State Treasury	$ 20	$ 168	$ 158	$ 30
Securities lending collateral with State Treasurer	2	48	40	10
Taxes receivable, net	5	168	168	5
Total assets	$ 27	$ 384	$ 366	$ 45
LIABILITIES				
Intergovernmental payables	$ 25	$ 168	$ 158	35
Obligations under securities lending - State Treasurer	2	48	40	10
Total liabilities	$ 27	$ 216	$ 198	$ 45
Surety Bond (1151)				
ASSETS				
Cash and cash equivalents	$ 1,352	$ 940	$ 272	$ 2,020
Total assets	$ 1,352	$ 940	$ 272	$ 2,020
LIABILITIES				
Other liabilities	$ 1,352	$ 940	$ 272	$ 2,020
Total liabilities	$ 1,352	$ 940	$ 272	$ 2,020

(Continued)

Combining Statement of Changes in Assets and Liabilities - Agency Funds - Continued

For the Year Ended June 30, 2011 (Expressed in Thousands)

	Balance at July 1, 2010	Additions	Deletions	Balance at June 30, 2011
Lottery Agent Security Deposit (1309)				
ASSETS				
Cash and cash equivalents	$ 937	$ 263	$ 413	$ 787
Total assets	$ 937	$ 263	$ 413	$ 787
LIABILITIES				
Other liabilities	$ 937	$ 263	$ 413	$ 787
Total liabilities	$ 937	$ 263	$ 413	$ 787
Total - All Agency Funds				
ASSETS				
Cash equity in State Treasury	$ 406,370	$ 3,063,208	$ 3,011,150	$ 458,428
Cash and cash equivalents	2,289	1,203	685	2,807
Securities lending collateral with State Treasurer	85,256	984,700	939,078	130,878
Taxes receivable, net	150,421	2,980,779	3,004,279	126,921
Other receivables, net	184	1,535	1,571	148
Due from other Department funds	57,968	139,928	113,707	84,189
Total assets	$ 702,488	$ 7,171,353	$ 7,070,470	$ 803,371
LIABILITIES				
Accounts payable and accrued liabilities	$ 6,102	$ 75,316	$ 73,364	$ 8,054
Intergovernmental payables	608,804	3,047,431	2,994,648	661,587
Obligations under securities lending - State Treasurer	85,256	984,700	939,078	130,878
Other liabilities	2,326	1,211	685	2,852
Total liabilities	$ 702,488	$ 4,108,658	$ 4,007,775	$ 803,371

McGladrey

Independent Auditors' 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 William G. Holland
Auditor General
State of Illinois

As Special Assistant Auditors for the Auditor General, we have audited the financial statements of the governmental activities, the business-type activities, the major fund, and the aggregate remaining fund information of the State of Illinois, Department of Revenue (Department), as of and for the year ended June 30, 2011, which collectively comprise the Department's basic financial statements and have issued our report thereon dated May 30, 2012. Our report was modified to include emphasis of a matter paragraphs regarding the adoption of the reporting and disclosure requirements of Governmental Accounting Standards Board Statement No. 54, and to describe significant fund balance deficits. 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.

Internal Control Over Financial Reporting

Management of the Department is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Department's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, and not for the purpose of expressing our opinions on the effectiveness of the Department's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However as described in the accompanying schedule of findings, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

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 Department's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in findings 11-1 and 11-2 in the accompanying schedule of findings to be material weaknesses.

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. We consider the following deficiencies described in findings 11-3, 11-4, 11-5, 11-6, 11-7, 11-8, 11-9, 11-10, 11-11 and 11-12 in the accompanying schedule of findings to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department's financial statements are free of 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 11-7 and 11-9.

We noted certain matters that we reported to management of the Department in a separate letter dated May 30, 2012.

The State of Illinois, Department of Revenue's responses to the findings identified in our audit are described in the accompanying schedule of findings. We did not audit the Department's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, State of Illinois, Department of Revenue management and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

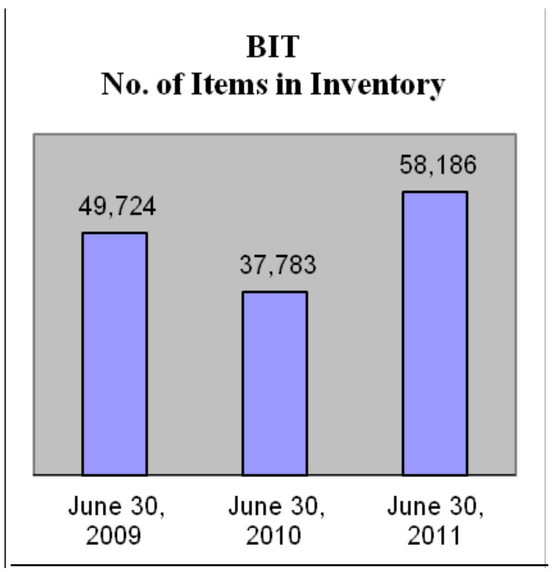
McGladrey LLP

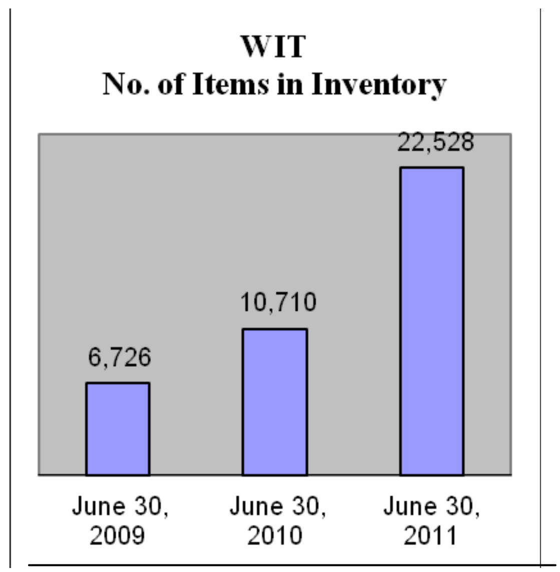
Schaumburg, Illinois
May 30, 2012

11-1 <u>Finding</u> (Increased Levels of Unprocessed Taxpayer Information)

During testing, auditors noted the Department has experienced a significant increase in the inventory of Business Income Tax (BIT) and Withholding Income Tax (WIT) taxpayer information to be processed and finalized.

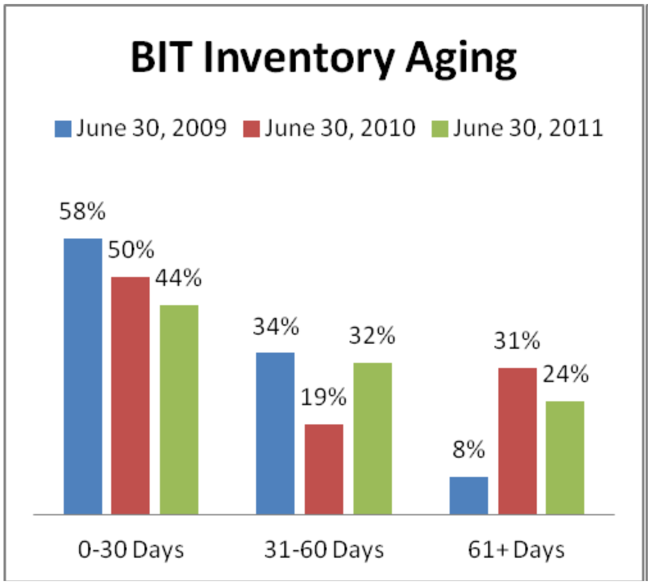
Taxpayer information to be processed and finalized consists of returns that are data entered but need further manual review and taxpayer correspondence that has been received but yet to be processed. Because of the statutory filing dates of the various required tax returns, the Department will always have a certain level of taxpayer information that is in inventory awaiting processing. With increased levels of taxpayer information at year-end, the final disposition (i.e. payment due to the Department (account receivable), payment due to the taxpayer (refund), or no balance) of this unworked taxpayer information cannot be determined, which increases the need for the Department to rely more on the use of estimates in their financial statement preparation process as opposed to actual finalized information. Auditors noted the inventory of taxpayer information to be processed and finalized at June 30, 2011 had increased significantly from the prior year as noted in the following charts:

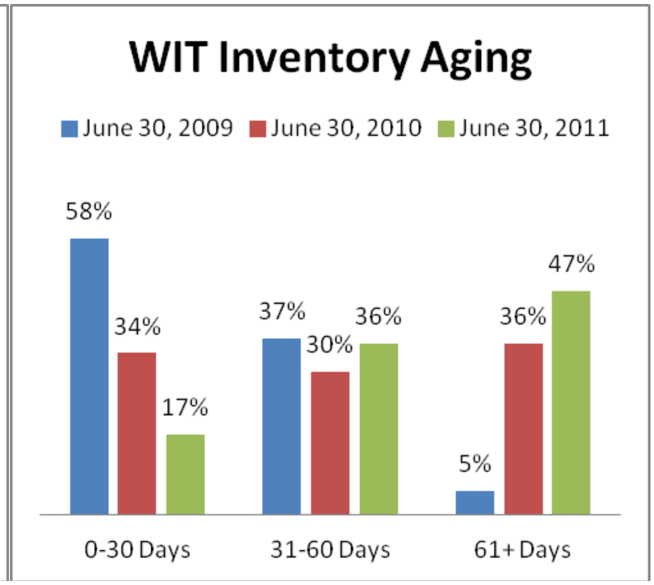




In addition to the significant increases in the taxpayer information to be processed and finalized, auditors also noted taxpayer information was taking longer to be completed. Auditors found the length of time BIT and WIT taxpayer information had been in various inventories increased, particularly for the information that had been in inventory 31 days and longer as noted in the following charts:

11-1 Finding (Increased Levels of Unprocessed Taxpayer Information) (Continued)





One segment of the Department's inventory consists of original tax returns to be processed and finalized. When taxpayer information is entered into the Department's tax processing system (GenTax), certain returns are automatically flagged by GenTax that require additional manual processing to finalize, which creates this category of inventory. These flags are attached for various reasons including mathematical errors, missing tax forms, etc. This segment has increased significantly over the past few years and is predominantly business income tax returns.

It is the Department's policy to exclude the indicated balances due on these returns from the financial statements, because the true balances are unknown until the returns are manually worked by the Department's tax specialists.

At June 30, 2011, the Department identified $4.7 billion of items related to taxpayer information to be processed and finalized (representing 68,862 returns). Although it is generally agreed the vast majority of the $4.7 billion is invalid and will be reduced upon the tax information being finalized, there is no reasonable methodology or process for estimating the valid receivable amount of these partially processed returns. The number and amount of these returns has been increasing steadily, as follows:

Year Ended	No. of Original Returns to be Processed and Finalized (All Tax Types)	GenTax Value of Original Returns to be Processed and Finalized (Billions)
June 30, 2009	41,517	$0.1
June 30, 2010	55,766	$0.2
June 30, 2011	68,862	$4.7

11-1 Finding (Increased Levels of Unprocessed Taxpayer Information) (Continued)

In accordance with Generally Accepted Accounting Principles (GAAP) and as noted in GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, governments should recognize assets from derived tax revenue transactions in the period when the exchange transaction on which the tax is imposed occurs (this occurs as individuals and corporations earn income) or when the resources are received, whichever comes first. There is no provision in the standard to delay recognition of these types of transactions until the accounts are fully processed. However, recognition of nonexchange transactions in the financial statements is not required if the transactions are not measurable (reasonably estimable) or are not probable of collection. Transactions that are not recognizable because they are not measurable should be disclosed.

Further, the Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires State agencies establish and maintain a system, or systems, of internal fiscal and administrative controls to provide assurance that revenues 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.

Department management stated the increase in taxpayer information to be processed and finalized was due to less staff available to process returns and other assigned tasks required of the processing staff such as performing "tests" of GenTax updates and revisions including the implementation of new tax laws.

Due to the increasing backlog of taxpayer information to be processed and finalized, the Department is not able to accurately measure and report associated receivables, deferred revenue, and tax revenue in the financial statements within the proper fiscal year. Additionally, due to increased demands and less staff in general for processing taxpayer information, the backlog has the potential to continue to increase over time.

Failure to process and finalize the taxpayer information and determine the final disposition to taxpayers in a timely fashion increases the risk the Department will be unable to recover the full amount owed and delays the recognition of receivables, deferred revenue, and tax revenue in the financial statements. (Finding Code No. 11-1)

RECOMMENDATION

We recommend the Department seek sufficient resources to process taxpayer information in a timely manner to ensure taxpayer records and financial statement information reflect appropriate information and expedite the ability of the Department to collect all taxes due to the State.

DEPARTMENT RESPONSE

We agree with the auditors that Business Income Tax (BIT) inventories should be worked in a timely manner and will seek additional resources to resolve this issue. Headcount vacancies due to retirements and funding issues have delayed the hiring process within the Department. The Business Income Tax Unit operated 20 to 30 percent below approved headcount during FY11. The State's constrained fiscal environment has made it a challenge for the Department to maintain sufficient resources to operate effectively, and we have re-assigned and consolidated operations of staff to key units to mitigate the risks to the State.

June 30, 2011 Headcount	Separations since June 30, 2011	Hires since June 30, 2011	March 31, 2012 Headcount	Reduction in workforce
1,771	**194**	**53**	**1,630**	**8%net reduction**

11-2 Finding (Fund Balance Deficit Exceeding $1.6 Billion)

The Department of Revenue (Department) has a $1.64 billion deficit in the General Fund's fund balance as of June 30, 2011. This deficit is primarily due to the State failing to allocate sufficient income tax receipts to the Income Tax Refund Fund, which is a subaccount of the General Fund reported by the Department.

The Income Tax Refund Fund (Fund 278) was established by the State Finance Act (30 ILCS 105/5.249) and the Illinois Income Tax Act (Act) (35 ILCS 5/901(c)) to receive a percentage of individual, estate, and trust (collectively, "individual") and corporate income tax collections. From these cash receipts, the Department is authorized, pursuant to a continuing appropriation, to refund requested income tax overpayments to individual and corporate taxpayers up to the amount of cash available in Fund 278.

Under the present system created by the Act, the percentage of income tax receipts deposited into Fund 278 each year is established by one of two methods:

1) the General Assembly passes and the Governor signs into law an exact percentage for the Department to deposit into Fund 278 during the next fiscal year ("Rate per Statute"); or,

2) the Department's Director calculates the annual deposit percentage for the Department to deposit into Fund 278 during the next fiscal year ("Rate as Certified") using a statutory formula and certifies this amount to the State Comptroller by June 30 of the fiscal year preceding the fiscal year in which the rate is to be effective. The statutory formula is based upon:
    a. refunds approved for payment in the preceding fiscal year (AR);
    b. plus, approved, but unpaid, refunds at the end of the preceding fiscal year (UR);
    c. less, amounts transferred into Fund 278 from the Tobacco Settlement Fund (TS);
    d. divided by income tax collections during the preceding fiscal year (C).

$$\frac{AR + UR - TS}{C}$$

Essentially, the purpose of this formula is to determine the portion of total income tax collections ultimately refunded back to taxpayers, so adequate cash can be reserved for paying refunds as receipts are collected from taxpayers. In the event the Department is unable to pay refunds in a timely manner (generally, within 90 days of the Department's receipt of a return) as determined under the Uniform Penalty and Interest Act (35 ILCS 735/3-2), the Department must add interest to the taxpayer's refund.

The Department's Director is only required to calculate the "Rate as Certified" by June 30th each year only if State law has not been modified to establish the "Rate per Statute" prior to June 30th.

11-2 Finding (Fund Balance Deficit Exceeding $1.6 Billion) (Continued)

A comparison of the "Rates per Statute" and the "Rate as Certified" since FY02 is as follows below:

	Individual		Corporate		Fund 278
State Fiscal Year	Rate per Statute	Rate as Certified	Rate per Statute	Rate as Certified	Fund Balance(Deficit) (in thousands)
2002	7.60%	7.60%	23.00%	23.00%	$ (1,091,619)
2003	8.00%	8.00%	27.00%	27.00%	(1,308,642)
2004	11.70%	11.70%	32.00%	32.00%	(745,086)
2005	10.00%	11.20%	24.00%	36.80%	(530,317)
2006	9.75%	*	20.00%	*	(622,628)
2007	9.75%	*	17.50%	*	(731,784)
2008	7.75%	*	15.50%	*	(854,829)
2009	9.75%	9.62%	17.50%	8.75%	(949,386)
2010	9.75%	11.99%	17.50%	17.14%	(1,380,161)
2011	8.75%	14.60%	17.50%	26.00%	(1,503,610)
2012	8.75%	10.63%	17.50%	24.59%	Not Available

Note: In the table above, the "Rate per Statute" was enacted into law prior to June 30th for FY06, FY07, and FY08. As such, the Department did not prepare the "Rate as Certified"

From the table, the amounts deposited into Fund 278 from FY02 through FY04 were based upon the "Rate as Certified", and the deficit within Fund 278 was reduced over those years. Since then, the General Assembly has annually passed legislation which the Governor signed into law specifying the "Rate per Statute" for deposits of income tax receipts into Fund 278. Since this change, the deficit within Fund 278 has been gradually increasing. The underfunding of Fund 278 – as indicated by the corresponding increasing deficit – is a major contributing factor to the significant deficit that has accumulated within the General Fund through June 30, 2011.

As a result of the significant deficit within Fund 278, which has grown rapidly since FY09, the auditors inquired with Department management regarding their plans for reducing or eliminating the deficit. In FY09, FY10, and FY11, the Department's plans to reduce the deficit were stated in the financial statements as follows: "The fund deficit in the General Fund (Refund Fund) will be eliminated through the collection and allocation of future State revenues to the Department."

Despite the Department's plan to reduce the deficit through future revenues, the percentage of receipts to be deposited into Fund 278 from individual income tax receipts decreased by 10.26% from 9.75% in FY10 to 8.75% in FY11 and corporate income tax receipts remained stable at 17.5%. Further, the percentage rates for cash receipts to be deposited into Fund 278 during FY12 will remain at the FY11 rates.

In accordance with sound financial management practices, the State should ensure an adequate amount of cash for refunding income tax overpayments is reserved and maintained in Fund 278. As these financial resources (tax overpayments) are not revenues of the State on an accrual basis, every effort should be made to estimate the amount of cash necessary to pay all refunds due, deposit that amount into Fund 278, and timely pay refunds requested by taxpayers.

Department management stated they have fulfilled their statutory obligations by both calculating the "Rate as Certified" when necessary and depositing the appropriate percentage of income tax receipts into Fund 278 pursuant to State law.

11-2 Finding (Fund Balance Deficit Exceeding $1.6 Billion) (Continued)

As of June 30, 2011, the Department's financial statements reported the Department owes the taxpayers of the State of Illinois approximately $1.67 billion in income tax refunds payable. For any refunds paid late, the Department is incurring additional interest costs. Without a significant increase in deposits into Fund 278, the liability to taxpayers – and the fund deficit – will continue to increase. (Finding Code No. 11-2, 10-1)

RECOMMENDATION

We recommend the Department work with the Governor and the General Assembly to increase the percentage of income tax receipts deposited into Fund 278.

DEPARTMENT RESPONSE

The Department agrees that taxpayers should be paid income tax refunds as quickly as possible.

However, raising the Refund Fund percentages requires legislative action that has not occurred. It should be noted that the $1.64 billion Fund deficit is based on accrual accounting and most of this amount relates to tax returns not yet filed, some not due for over a year.

At June 30, 2011, outstanding refunds approved for payment, but in fact not paid due to the lack of funds equaled $645.5 million. The equivalent figure at June 30, 2012 will be substantially less.

11-3 Finding (Service Organization Internal Control Reports Not Obtained)

The Department of Revenue (Department) did not obtain Service Organization Internal Control Reports containing independent reviews of externally controlled service providers used to data enter tax returns.

The Department uses three external service providers to provide data entry services for many sales tax and business, individual and withholding income tax returns. The Department did not obtain Service Organization Internal Control Reports from any of these service providers. Of the total returns processed by the Department, 71% of the volume is processed by these three external service providers.

It is essential to obtain and review an independent review, Service Organization Internal Control Report, of each service provider's tax processing systems environment. Independent reviews provide a method of evaluating the systems in place at each service provider and helps the Department develop internal control processes that would complement those at the service providers.

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.

Department management stated they continuously monitor the data entered returns from the vendors in the same manner as returns that go through data entry internally in the Department.

Without having obtained and reviewed the Service Organization Internal Control Reports, the Department does not have assurance the external service providers' internal controls are adequate to ensure the taxpayer account balances and revenue recorded from such returns are accurate and reliable. (Finding Code No. 11-3, 10-6, 09-13)

RECOMMENDATION

We recommend the Department obtain and adequately review copies of the independent reviews (Service Organization Internal Control Reports) for data entry services provided by all third-party service providers (Providers) on an annual basis. User controls delineated in these reports should be implemented and monitored by the Department. For those Providers that do not have a Service Organization Internal Control Report performed, the Department should perform sufficient procedures to obtain satisfaction that internal controls are adequate for safeguarding assets and accounting information, and that controls are operating effectively. Any procedures performed should be fully documented by the Department including exceptions noted, the disposition of exceptions, conclusions reached and corrective action taken by the vendor. This information should be maintained for review by the external auditors.

DEPARTMENT RESPONSE

The Department agrees on the need to ensure the adequacy of controls over data entry services provides by third-party providers. It should be noted that the Department has in place a systematic review process of data entry done internally and by external vendors, this process has detected and prevented problems.

The Department had planned to contract for independent review services during FY 2011 but was unable to do so because of budget constraints. Instead it was determined that Internal Audit would perform reviews of the data entry vendors starting in FY2012 as part of the Two-Year Audit Plan to get appropriate coverage for these contracted services. Internal audit is also in the process of reviewing the Department's procedures for oversight of the data entry vendors.

11-4 <u>Finding</u> (Reconciliations of Hotel Operators' Occupation Tax Allocations Not Performed)

The Department of Revenue (Department) does not perform a reconciliation of estimated deposit allocations to actual return information for all funds receiving Hotel Operators' Occupation Tax (HOOT) collections.

During FY11, the Department processed a total of $278,799,844 in HOOT collections. Based on their testing, the auditors concluded there were no material misallocations of HOOT receipts to the various funds in FY11. Even though the auditors did not identify any material misallocations, the lack of a formalized reconciliation between the estimated deposits and actual return information can lead to undetected misallocations of HOOT collections among:

- **State Funds**, including the General Revenue Fund, the Build Illinois Fund, the Local Tourism Fund, and the International Tourism Fund; and,
- **Fiduciary Funds**, including the Sports Facilities Tax Trust Fund, the Metropolitan Pier and Exposition Authority Trust Fund, and the Illinois Tourism Tax Fund and not detect and correct it in a timely fashion.

The Hotel Operators' Occupation Tax Act (35 ILCS 145/6) specifies an allocation methodology for the disposition of State HOOT tax collections into various funds.

The Illinois Sports Facilities Authority Act (70 ILCS 3205/19), the Metropolitan Pier and Exposition Authority Act (70 ILCS 210/13(c)), and the Municipal Code (65 ILCS 5/8-3-13) require all taxes, penalties, and interest collected pursuant to each respective imposed tax be deposited into the Sports Facilities Tax Trust Fund, the Metropolitan Pier and Exposition Authority Trust Fund, and the Illinois Tourism Tax Fund, respectively.

The Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires State agencies to establish and maintain a system of fiscal and administrative controls to 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.

Department personnel stated they are working on developing a reconciliation methodology for HOOT receipts.

Failure to reconcile deposit allocations of HOOT collections with actual return data can lead to undetected errors among funds within the State Treasury. (Finding Code No. 11-4, 10-7)

<u>RECOMMENDATION</u>

We recommend the Department develop a receipt reconciliation methodology – considering the impact of cash deposits, audit payments, credit memoranda, and refunds – to adjust estimated deposits to actual return data to ensure the accuracy of deposits into the State Treasury. Further, we recommend the Department evaluate the funds receiving HOOT allocations for any prior period adjustments.

<u>DEPARTMENT RESPONSE</u>

Although the issues identified are immaterial to the financial statements and the funds, the Department agrees that a reconciliation methodology to adjust estimated deposits to actual HOOT return data should be performed. A monthly reconciliation methodology for all HOOT fund balances considering cash deposits, audit payments, credit memoranda, and refunds is currently being developed, and adjustments will be made for FY2012.

11-5 Finding (Weaknesses in the Processes over Sales and Use Tax Fund Allocations)

The auditors noted weaknesses in the Department of Revenue's controls over the fund allocation process for sales and use taxes (ROT).

The Department of Revenue (Department) is mandated by various State laws to collect and allocate ROT receipts to various State and local government funds based upon amounts or percentages designated by State statute. During FY11, the Department deposited approximately $12 billion in ROT receipts into the State Treasury. As cash is collected daily, the Department allocates 98% of receipts to various State and local government funds based upon a biannual estimate. For the remaining 2% of receipts, the Department sets aside these collections (2% reserve) in order to have sufficient funds to "true-up" the various local government funds once the ROT returns are perfected and the correct/final local government allocations are known. This process is necessary due to a delay of typically two months to both "perfect" (process and approve) the ROT returns and present vouchers to the State Comptroller for distribution of ROT collections from the date a return is received by the Department.

Each month, the Department distributes ROT collections to local governments based upon data from batches of taxpayer information "perfected" during the previous month. These batches include new returns, cash receipts from previously perfected returns (collections on accounts receivable), taxpayer audits finalized by the Department, and other miscellaneous items. These perfected batches consist predominately, but not exclusively, of ROT receipts and returns received by the Department two months ago. ROT amounts for batches not perfected are not distributed to the local governments until after the perfection process, regardless of when the cash was collected by the Department. As such, there are always differences between cash collected in the month prior to the measurement period when compared to the perfected returns.

The monthly cash information associated with the perfected returns is used by the Department to determine the amount of ROT receipts to distribute to local governments. This distribution is compared to the 98% deposits made in the second preceding month. Any shortage is allocated from the 2% reserve, which the Department set aside for this purpose. Any overage is retained in the local government fund and is added to the next month's receipt collections for consideration as part of the "true-up" process in the subsequent month. Any amounts remaining after this "true-up" are then allocated to the various State funds.

At the conclusion of this process, the Department has deposited and recorded all cash receipts received during the second preceding month; however, the "true-up" process does not ensure an adequate amount of cash receipts are retained in each local government fund for cash receipts associated with returns awaiting "perfection" by the Department.

Further, for financial reporting purposes, the Department reports each fund's cash balance in the Department's financial statements based upon the results of the process described above at June 30; however, these balances may not be individually representative of cash for "unperfected" returns.
Due to this limitation, the auditors noted the following weaknesses:

- For local government funds showing a cash overage during the "true-up" process, the cash overage retained within the fund does not reflect an estimation by the Department for unperfected cash receipts due to that local government fund.

- While the local government funds showing a cash shortage during the "true-up" process receive additional deposits from the 2% reserve, the ending cash overage of $0.00 does not reflect an estimation by the Department for unperfected cash receipts due to that local government fund.

11-5 Finding (Weaknesses in the Processes over Sales and Use Tax Fund Allocations) (Continued)

- The deposit of the remaining cash from the 2% reserve after performing the "true-up" process into State ROT funds does not reflect an estimation by the Department for cash receipts due to the State for unperfected cash receipts due to the State funds.

At the conclusion of each month, the cash balance for ROT receipts deposited into each local government fund and the State's ROT funds as a whole should reflect:

a) the total amount of 98% daily deposits paid into the fund during the previous month and current month;
b) interest deposited by the State Treasurer during the current month; and,
c) the total amount of cash receipts estimated by the Department to reflect unperfected ROT batches due to the fund collected during any month preceding the previous month.

In addition, the auditors noted other issues involving ROT allocations reported in Finding 11-10.

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

The Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires the Department establish and maintain a system, or systems, of fiscal and administrative controls to provide assurance "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."

Department personnel stated they lack the appropriate system capabilities to accurately allocate cash receipts into the proper local government and State funds when initially received until returns are "perfected".

Failure to develop a process to allocate unperfected ROT receipts into various State and local government funds within the State Treasury leads to preparing financial reports without considering all information available to the Department and limits the State Treasurer's ability to accurately deposit interest receipts to local government funds. (Finding Code No. 11-5, 10-8)

RECOMMENDATION

We recommend the Department review the current ROT cash allocation process and develop a process to account for unperfected cash receipts due to various State and local government funds.

11-5 Finding (Weaknesses in the Processes over Sales and Use Tax Fund Allocations) (Continued)

DEPARTMENT RESPONSE

The Department is reviewing their estimation methodologies to determine if there are areas where improvements can be made in future preliminary receipt allocations.

The Department deposits all cash receipts into the various funds based upon percentages determined from averages of perfected receipts over the prior two years. Because the Department acknowledges that without significant investments into system upgrades, it lacks the appropriate system capabilities to allow for precisely allocating the receipts when initially received, using historical averages and the monthly true-up process is the Department's internal work-around process. It is important to note that this longstanding methodology has resulted in accurate distributions to local governments as returns are perfected and the needed cash being available in all funds to support these distributions.

The Department will research the feasibility and cost/benefit of further enhancements to GenTax, a rewrite of the current Consolidated Accounting System, and development of a general ledger system for reconciling detail return information with deposit information.

11-6 Finding (Weaknesses in Processing and Taxpayer Information)

The Department of Revenue (Department) has not completely implemented controls and safeguards over processing taxpayer information. During FY11, the Department processed approximately 8.2 million tax receipt documents throughout its facilities.

The Department receives and uses federal tax information (FTI) to verify information contained on various State tax returns; therefore, under the Internal Revenue Service's definition of comingling, the information on the Department's tax processing system (GenTax) related to Business Income Tax (BIT) and Individual Income Tax (IIT) is considered FTI and should be handled as such. FTI includes any return, Revenue Agent's Report, transcript, or any information received on diskette and/or any other electronic transmission of data received from the Internal Revenue Service (IRS). This includes all of the IRS extract files received by the Department. Any detailed information printed or copied or used in any manner, including screen prints and/or detailed reports, with specific taxpayer information from GenTax that includes BIT and/or IIT information should be handled as FTI.

During testing, the auditors noted the Department had made improvements related to internal controls and physical safeguards to protect taxpayer receipts and taxpayer information. However, the auditors still noted areas where there were weaknesses. Weaknesses were specifically noted in the following areas:

- Temporary employees hired throughout the year and full time employees are allowed to possess cell phones and other personal devices while processing taxpayer information.

- The Department has not implemented sufficient physical safeguards during non-business hours to control access to the tax processing areas throughout the Department from contractors, vendors and other State employees utilized by the Department.

- Auditors noted taxpayer files were stored on open shelving units throughout the Department. This information is not secure from potential unauthorized access.

The Department is responsible for ensuring the confidentiality of tax information within its possession. The Department maintains data that is covered by both State and Federal requirements. The State's disclosure statutes are within the Retailers' Occupation Tax Act (35 ILCS 120/11) and the Illinois Income Tax Act (35 ILCS 5/917). The Internal Revenue Code (26 U.S. Code §6103(a)) requires returns and return information shall be confidential and no State officer or employee shall disclose return information for unofficial purposes. Further, the Code defines "return information" as "a taxpayer's identity, the nature, source, or amount of his income, payments, receipts, deductions, exemptions, credits, assets, liabilities, net worth, tax liability, tax withheld, deficiencies, overassessments, or tax payments…". To address data received from the IRS, the Department developed a definition of what information is considered FTI, which was approved by the Project Manager of the IRS Office of Safeguards. In addition, the Department is required to ensure all tax information is protected in accordance with the Internal Revenue Service's Publication 1075, *Tax Information Security Guidelines for Federal, State, and Local Agencies, Safeguards for Protecting Federal Tax Returns and Return Information.*

State statute and IRS Publication 1075 require the Department ensure it safeguard federal tax information from unauthorized disclosure. Specifically, section 4.1 of IRS Publication 1075 states, "Security may be provided for a document, an item, or an area in a number of ways. These include, but are not limited to, locked containers of various types, vaults, locked rooms, locked rooms that have reinforced perimeters, locked buildings, guards, [and] electronic security systems."

11-6 Finding (Weaknesses in Processing and Taxpayer Information) (Continued)

The Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires State agencies to establish a system of fiscal and administrative controls to provide assurance that "funds, property, and other assets and resources are safeguarded against waste, loss, unauthorized use, and misappropriation."

Department officials stated they have made significant improvements over the area of receipt processing and protection of taxpayer records. Further, Department officials stated this is a continuing effort and they are continually making improvements as recommendations from their Security Consultant are completed and funding is available to enact the recommendations.

The Department has the responsibility to ensure only authorized individuals have access to taxpayer information and taxpayer payments. Failure to establish adequate security controls could result in taxpayer identity theft or unintended use and the misappropriation of taxpayer payments. (Finding Code No. 11-6, 10-9)

RECOMMENDATION

We recommend the Department ensure taxpayer information is adequately protected during both business and non-business hours from potential unauthorized access as mandated by State statute and IRS Publication 1075.

DEPARTMENT RESPONSE

The Department agrees and considers the safeguarding of confidential taxpayer information to be a core function of the Department, and has taken strides to assure this information remains secure. As new threats to security emerge, the effort to make improvements evolves to meet them. We receive recommendations from our own internal reviews, third-party Security Consultants and the IRS. Implementing recommendations will continue to be done as funding is available. It should be noted, that no State meets all the requirements of Publication 1075. The IRS expects to see continuous improvements and IDOR has ongoing discussions with the IRS to ensure that we are meeting their expectations regarding safeguarding matters.

In regards to the first bullet point, the Department instituted a new policy on November 7, 2011 that restricts the use of cell phones, cameras, PDAs, and any other video equipment within the Account Processing, Information Technology, Collections, Audit and Taxpayer Services areas of the Department

The Department requires all employees and contractors to complete annual safeguard training that has been approved by the IRS. As part of that training, employees are advised to review Publication 19, Keeping Tax Information Confidential. This training and publication are provided to all new employees as part of orientation.

11-7 Finding (Inadequate Control over Illinois Sports Facilities Authority Funds)

The Department of Revenue (Department) did not exercise adequate control over the Illinois Sports Facilities Fund or the Sports Facilities Tax Trust Fund.

During testing, auditors noted the Department did not deposit the entire statutorily required “Advance Amount” into the Illinois Sports Facilities Fund from the State’s share of Hotel Operators’ Occupation Tax receipts. During FY11, the Department deposited $33,100,000; however, the Department should have deposited $36,270,000. The Hotel Operators’ Occupation Tax Act (35 ILCS 145/6) requires the Department to deposit the annual “Advance Amount” from FY02 through FY32 pursuant to a statutory formula from the State’s share of Hotel Operators’ Occupation Tax.

In addition, the auditors tested the Illinois Sports Facilities Fund’s cash balance at June 30, 2011, and identified approximately $5 million that should have been transferred to the General Revenue Fund. The State Finance Act (30 ILCS 105/8.25-4) requires a transfer for all amounts remaining within the “advance account” of the Illinois Sports Facilities Fund on June 30 to the General Revenue Fund.

Further, as part of the auditors’ testing, it was determined certain amounts reported for the Illinois Sports Facilities Fund in the Department’s financial statements did not agree with amounts computed by the auditors. Based on auditor computations, the Department reported amounts in the Illinois Sports Facilities Fund for both assets and liabilities which were understated by approximately $5.9 million. These amounts were deemed immaterial and did not require the Department to make any adjustment to their financial statements.

During testing, auditors also noted distribution errors of receipt collections from the Hotel Operators’ Occupation Tax imposed by the Illinois Sports Facilities Authority (ISFA) that are deposited into the Sports Facilities Tax Trust Fund. The Department performed a review of the transactions recorded in the Sports Facilities Tax Trust Fund and determined the following:

- During FY10, the Department did not distribute the 4% administrative fee or repayment of the Advance Amount in August 2009 from the Illinois Sports Facilities Fund to the General Revenue Fund. As a result of this error, the Sports Facilities Tax Trust Fund owed the General Revenue Fund $1,788,726 for unpaid FY10 reimbursements at June 30, 2011. The Illinois Sports Facilities Authority Act (70 ILCS 3205/19) requires the Department to retain 4% of receipts as an administrative fee for deposit into the General Revenue Fund and to repay the General Revenue Fund for the Advance Amount pursuant to a statutory formula.

- During FY11, the receipts into the Sports Facilities Tax Trust Fund from the Hotel Operators’ Occupation Tax imposed by the ISFA were insufficient to repay the General Revenue Fund for the Advance Amount paid to the ISFA from the Illinois Sports Facilities Fund as required by the Illinois Sports Facilities Authority Act (70 ILCS 3205/19). As a result of this deficiency, the Department was required to reduce the City of Chicago’s share of State income tax receipt disbursements from the Local Government Distributive Fund by $185,009 to repay the General Revenue Fund for the shortage. Per requirements set forth in statute, the computation and determination of any amounts to be reimbursed from the City of Chicago should have been performed by August 2011. The Department submitted documentation for the reimbursement for the deficiency in December 2011 to the Office of the State Comptroller.

11-7 Finding (Inadequate Control over Illinois Sports Facilities Authority Funds) (Continued)

The Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires the Department establish and maintain a system, or systems, of fiscal and administrative controls to provide assurance "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."

Department personnel stated that staff has worked with the ISFA for years to ensure that the Department deposited the advance payment based on the certified amount and then required repayment to the General Revenue Fund throughout the fiscal year until the advance payment was satisfied. The Department received confirmation from the ISFA's Chief Financial Officer documenting their agreement with the Department's process and handling of the advance payments. Although the Department received a confirmation from the ISFA, the auditors believe the Department is obligated to comply with statutory requirements regarding deposits.

Failure to administer the Illinois Sports Facilities Fund and Sports Facilities Tax Trust Fund in accordance with statute led to deposit and distribution errors, impacting the Department's ability to prepare accurate financial statements and provide accurate financial information to the ISFA and City of Chicago. (Finding Code No. 11-7, 10-11)

RECOMMENDATION

We recommend the Department implement controls to ensure the Department's deposit and distribution activity from the Illinois Sports Facilities Fund and Sports Facilities Tax Trust Fund are performed accurately in accordance with State law.

DEPARTMENT RESPONSE

The Department believes that it has implemented the law as it was intended and as all parties agreed it should be implemented. We will continue to work with the General Assembly and the Illinois Sports Facility Authority to clarify the language of this statute. In addition, the process over the Illinois Sports Facilities Authority Fund and Sports Facilities Tax Trust Fund has been automated into the GenTax system during FY2012. This should help eliminate manual errors that have occurred in the past.

The bullet points noted in the finding were items corrected by the Department.

11-8 Finding (Exceptions in Income Tax Refunds Payable Balances at Year-End)

Some of the Department of Revenue's (Department) income tax refunds payable accounts included in the Department's payable calculation at June 30, 2011 contained inaccurate balances.

- A sample of 21 Individual Income Tax (IIT) accounts, with refunds payable totaling $402,390, were selected to test the accuracy and existence of the Department's June 30, 2011 payable information. The results of the testing noted eight accounts, totaling $267,361 (66%), in which the taxpayer had requested all or a portion of the refund be designated as a credit carry-forward to the next tax year. Amounts designated to be a credit carry-forward to the next tax year should be reported as deferred revenue as opposed to a refund payable. Based on the auditor's results, the Department conducted a review of the IIT accounts which had refunds payable at June 30, 2011 to determine the extent of the overstatement. The Department determined refunds payable, as it relates to IIT, was overstated by $6,702,916. The Department recorded an adjustment to the June 30, 2011 financial statements. Department management stated there were unpaid IIT refunds at year-end due to lack of funds available in the Income Tax Refund Fund to pay all refunds. GenTax does not adjust for the amount of credit carry-forwards from refunds payable until the refund release process is run. The refund release process was run on July 14, 2011 when there were adequate funds to pay the outstanding IIT refunds.

- A sample of 30 Business Income Tax accounts, with refunds payable totaling $77,967,2767, were selected to test the accuracy and existence of the Department's June 30, 2011 payable information. The results of the testing identified one account, totaling $2,586,308 (3%), in which the taxpayer had requested a portion of the refund be designated as a credit carry-forward to the next tax year. Upon further analysis of the exception identified in regard to the population of similar files, it was determined Refunds Payable was overstated by $5.6 million, and deferred revenue would then be understated.

In accordance with Governmental Accounting Standards Board (GASB) Statement No. 33, Paragraph 16, *Accounting and Financial Reporting for Nonexchange Transactions*, governments should recognize assets from derived tax revenue transactions in periods when the exchange transaction on with the tax is imposed occurs or when the resources are received, whichever, occurs first. Resources received in advance should be reported as deferred revenues (liabilities) until the period of the exchange.

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 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.

Department personnel stated GenTax does not adjust for the amount of credit carry-forwards from refunds payable until the refund process is ran. Due to cash shortages in the Income Tax Refund Fund at June 30, 2011, the Department did not run the refund process until cash was available to pay the outstanding refunds on July 14, 2011.

Based on the above exceptions the initial financial information provided by the Department resulted in refund liabilities being overstated and deferred revenue being understated at fiscal year-end. (Finding Code No. 11-8)

11-8 Finding (Exceptions in Income Tax Refunds Payable Balances at Year-End) (Continued)

RECOMMENDATION

We recommend the Department improve controls to ensure refunds payable are properly accounted for in the Department's financial statements.

DEPARTMENT RESPONSE

The Department accepts that improvements can be made and will take measures to ensure proper financial information is reported at year-end. However, we respectfully disagree with the materiality of the finding. The Department maintains adequate controls over refunds payable and our internal controls would have detected any financially material issues. The root cause of this issue was the lack of funds available at year-end in the Income Tax Refund Fund to pay all refunds. (see 11-2)

The issues noted by the auditors totaled $12.3 million out of a reported Refunds Payable of $1.67 billion at June 30, 2011 (i.e. our estimate of refunds payable was 99.3% accurate). In addition, these issues reflect just a classification difference between liability accounts in the financial statements, since deferred revenues and refunds payable are both liabilities of the State.

11-9 Finding (Noncompliance with Provisions of the Illinois Income Tax Act and State Revenue Sharing Act)

The Department of Revenue (Department) did not comply with provisions of the State Revenue Sharing Act and the Illinois Income Tax Act, as both of these Acts were impacted by the passage of Public Act 096-1496, the *Taxpayer Accountability and Budget Stabilization Act*.

During FY11, the General Assembly passed and the Governor signed Public Act 096-1496, which increased the State income tax rates on individuals, trusts, estates, and corporations and contained amendatory provisions to update existing State law.

During testing, the auditors noted the following:

- The Illinois Income Tax Act (35 ILCS 5/901(c)) was not amended by Public Act 096-1496 to authorize deposits of a portion of income tax receipts by the Department into the Income Tax Refund Fund. From February 2011 through June 2011, the Department deposited approximately $820 million into the Income Tax Refund Fund from income tax collections, with an unknown portion of these receipts representing taxes collected from the new tax rates.

Department management stated they believed they followed the intent of the General Assembly and this was an oversight in Public Act 096- 1496. Department management stated this issue is on their list of technical changes that need to be made to the Illinois Income Tax Act so that it clearly reflects the intent of the General Assembly.

- Prior to Public Act 096-1496, the Illinois Income Tax Act (35 ILCS 5/901(b)) and the State Revenue Sharing Act (30 ILCS 115/1) were harmonious statutes directing the Department to transfer 10% of the prior month's income tax receipts deposited into both the General Revenue Fund and Education Assistance Fund from the General Revenue Fund to the Local Government Distributive Fund. Public Act 096-1496 amended the Illinois Income Tax Act to change the transfer percentage to 6.86% for receipts from corporate tax collections and 6% for receipts from individual, estate, and trust collections; however, the State Revenue Sharing Act was not amended. From a review of the statutes, it does not appear a supremacy clause or other language directs which statute controls in this situation or a method exists to reconcile or harmonize the conflicting language. From February 2011 through June 2011, the Department would have approximately transferred an additional $282 million to the Local Government Distributive Fund had the Department followed the mandated allocation set forth in the State Revenue Sharing Act.

Department management indicated Public Act 096-1496 created a conflict between statutes and it was their opinion the most recent act of the General Assembly overrules older Acts with which it conflicts; therefore, they made deposits following the new law.

Further, the auditors noted the Department's receipt deposit codes and receipt processing system do not provide sufficient information for the Department to allocate receipts among the various State funds or calculate statutory transfers pursuant to State law. During testing, the auditors identified the following:

11-9 <u>Finding</u> (Noncompliance with Provisions of the Illinois Income Tax Act and State Revenue Sharing Act) (Continued)

- The auditors noted the Department's methodology for calculating the transfer from the General Revenue Fund to the Local Government Distributive Fund requires the Department's receipt source codes within the State Comptroller's Statewide Accounting Management System (SAMS) to contain sufficient detail to facilitate the proper transfer calculation. In reviewing the Department's receipt codes, the auditors noted the Department splits income tax receipts between account codes for individual income tax receipts and for corporate income tax receipts. Upon discussion with Department personnel, it was determined the deposits for estates, trusts, and certain individual income taxes are coded as corporate income tax receipts and transferred at 6.86%; however, the Illinois Income Tax Act transfer calculation includes estates, trusts, and individual income taxes under the 6% transfer calculation for individual income tax receipts. After this was brought to the Department's attention by the auditors, the Department determined the transfers from the General Revenue Fund to the Local Government Distributive Fund may be overstated by as much as $195,713.

- In addition to the receipt coding issue affecting transfers, the Illinois Income Tax Act (35 ILCS 5/901(c)) specifies deposits into the Income Tax Refund Fund between corporate receipts and individual income tax receipts, including receipts from estates and trusts. After notification from the auditors, the Department determined the deposits into the Income Tax Refund Fund during FY11 may be overstated by as much as $12.6 million, the General Revenue Fund may be understated by as much as $11.7 million, and the Education Assistance Fund may be understated by as much as $917,000.

Department management stated that these fund allocation issues occurred due to how these tax documents are processed through the systems.

The Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires the Department establish and maintain a system, or systems, of internal fiscal and administrative controls to provide assurance that resources are used in compliance with applicable law and 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. Further, SAMS, Procedure 25.20.30, requires the Department submit the Chart of Accounts Maintenance and Inquiry Form (Form C-45) to the Office of the State Comptroller to request additions or deletions to the State's Chart of Accounts.

Failure to identify and seek appropriate remedies for inconsistent or outdated State laws results in the Department performing functions not specifically directed by the General Assembly and could subject the State to legal risks. Further, failure to have a receipt processing system and sufficient receipt deposit codes resulted in inaccurate fund deposits, incorrect statutory transfers, and reduces the reliability of Statewide financial reporting. (Finding Code No. 11-9)

11-9 Finding (Noncompliance with Provisions of the Illinois Income Tax Act and State Revenue Sharing Act) (Continued)

RECOMMENDATION

We recommend the Department:

- improve their process of reviewing State tax laws, rules, and regulations to identify statutory inconsistencies and seek appropriate legislative remedy;
- implement systems and controls to capture sufficient information to properly allocate tax receipts among State funds and calculate statutory transfers; and,
- work with the Office of the State Comptroller to review and update the Department's receipt codes to ensure the receipt code information reported by the State Comptroller is accurate and fairly presented regarding the type of receipt collected by the Department.

DEPARTMENT RESPONSE

The Department is seeking legislative changes to the Illinois Income Tax Act (35 ILCS 5/901(c)) to authorize deposits of a portion of income tax receipts into the Income Tax Refund Fund and to the State Revenue Sharing Act (30 ILCS 115/1) to reflect the new percentages established by Public Act 096-1496 amending the Illinois Income Tax Act (35 ILCS 5/901(b)). The corrective language has been written and the Department is working to get the legislation enacted.

The Department is developing strategies to distinguish corporate from non-corporate tax collections associated with trust and estate returns in order to more accurately calculate transfers and deposits of these particular tax receipts. The Department agrees that, due to the inability to identify the exact breakdown between corporate and non-corporate tax receipts during the second half of FY11, there may have been overstatement/understatement to various state funds no greater than the amount described in the finding.

11-10. Finding (Weaknesses in Controls over the Deposit of Sales and Use Tax Receipts)

The Department of Revenue (Department) has weaknesses in the Department's internal control structure over the deposit, allocation, and distribution of receipts from sales and use taxes (ROT). The auditors identified errors within the Department's "true-up" calculations (see Finding 11-5 for more information), noncompliance with State laws in managing certain local government funds, and noncompliance with State laws regarding the allocation of State ROT receipts.

The auditors noted the following weaknesses within the Department's internal control structure over ROT deposits:

- The Department's receipt allocation process is a manual paper process involving data amassed from several sources with complex calculations on multiple spreadsheets. The auditors noted numerous errors during a review of this process.
- The Department lacks sufficient communication between the Department's various areas responsible for a component of the ROT tax deposit and allocation process. We noted some areas are reliant on records from the Office of the State Comptroller, while parts of the data needed to perform their functions are located in two different divisions within the Department. In addition, it does not appear the Department is fully utilizing the capabilities of GenTax to report processed tax collections by ROT type (i.e. schools, flood, public safety, et cetera). This situation has caused additional work and creates additional risk of error as Department employees perform calculations to reach a number generated by another area of the Department.
- The Department had not developed an internal control structure designed to identify and correct errors within a timely manner. We noted one unsupported fund transfer – totaling $1,086 – noted as "to allow the 10% RTA Use Tax warrant to be released." By performing this transfer, the Department did not take the opportunity to review why the cash balance in the fund was insufficient to support expenditures of shared revenue payments from the fund to correct the Department's records.

The Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires the Department establish and maintain a system, or systems, of fiscal and administrative controls to provide assurance "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."

During testing of the ROT "true-up" calculations process, the auditors noted situations where – in part due to the issues noted above – the Department did not properly account for fund transfers, interest deposits from the State Treasurer, lapse period payments, missing expenditure data, and uncorrected prior year errors noted in previous examinations. The net effect of these errors, by fund, is displayed in the following chart:

11-10. Finding (Weaknesses in Controls over the Deposit of Sales and Use Tax Receipts) (Continued)

Local Government Fund Name	Fund Number	Over(Under) Net Cash
County Water Commission	084	$ 6,981
Non-Home Rule Municipal	088	21,194
Home Rule Municipal Soft Drink	097	(9,211)
Home Rule Municipal	138	103,178
Home Rule County	139	75,526
Business District	160	(23)
State and Local Sales Tax Reform	186	(7,468,354)
Local Government Tax	189	(528,109)
County Option Motor Fuel Tax	190	5,877
Metropolitian Pier and Exposition Authority Trust	337	576,447
Tax Compliance and Administration Fund (School Facility)	384	(1,461)
Tax Compliance and Administration Fund (Flood)	384	(36,685)
Regional Transportation Authority	812	8,858,070
Metro-East Mass Transit District	841	7,207
	Net Overstatement:	$ 1,610,637

Under the Department's current ROT allocation process, $1,138,277 of the net overstatement could have been deposited into the General Revenue Fund, $379,426 could have been deposited into the Special Account for the Common School Fund, $88,585 could have been deposited into the Build Illinois Fund, and $4,349 could have been deposited into the Illinois Tax Increment Fund.

The auditors noted noncompliance in the Department's administration of local government ROT funds, as noted below:

- During testing of distributions from the County Option Motor Fuel Tax Fund (Fund 190), the auditors noted distributions to county governments were for 98% of current perfected returns processed during the previous month, with the remaining 2% reserved in the fund for the Department's expenditures.

  The Counties Code (55 ILCS 5/5-1035.1) requires the Department to distribute 100% of perfected returns processed during the previous month, less the amount expended during the second preceding month pursuant to an appropriation from the General Assembly. The Department is prohibited from expending more than 2% of the receipts deposited into the County Option Motor Fuel Tax Fund during the preceding year in the current year.

- During testing of distributions from the Home Rule Municipal Retailers' Occupation Tax Fund (Fund 138), the auditors noted distributions to municipal governments were not reduced by an administration fee equal to the appropriated expenditures from Fund 138 during the second preceding month.

  The Illinois Municipal Code (65 ILCS 5/8-11-6) requires the Department to distribute 100% of perfected returns processed during the previous month, less the amount expended during the second preceding month pursuant to an appropriation from the General Assembly. The appropriation is limited to 2% of the estimated receipts for the Home Rule Municipal Retailers' Occupation Tax Fund during the fiscal year.

11-10. Finding (Weaknesses in Controls over the Deposit of Sales and Use Tax Receipts) (Continued)

During a review of ROT receipt deposits, the auditors noted the following errors in the allocation of State ROT receipts into various State funds:

- While the Department estimated 80% of receipts from the sale of candy, soft drinks, grooming, and hygiene products during FY11 would be $52.52 million, the Department only deposited $52 million into the Capital Projects Fund (Fund 694).
- The Department treated receipts paid into the McCormick Place Expansion Project Fund as a reduction in receipts from the General Revenue Fund, rather than splitting the reduction between the General Revenue Fund and Special Account for the Common School Fund. As a result, the Department should have deposited an additional $7.3 million into the General Revenue Fund, with a corresponding reduction in receipts for the Special Account for the Common School Fund.
- The Department does not have a system in place to split remaining receipts from the Use Tax Act and Retailers' Occupation Tax Act and receipts from the Service Use Tax Act and Service Occupation Tax Act. As a result, the Department is unable to properly allocate receipts between the General Revenue Fund and Special Account for the Common School Fund.

The Use Tax Act (35 ILCS 105/9), Service Use Tax Act (35 ILCS 110/9), Service Occupation Tax Act (35 ILCS 115/9), and the Retailers' Occupation Tax Act (35 ILCS 120/3) require the Department allocate State ROT receipts pursuant to the following methodology:

- Net Revenues Realized from State Sales Tax Collections
  - Department's Estimation of Increased Tax Receipts from the Tax Increase on Soda, Candy, and Grooming Products to the Capital Projects Fund
    - Less: 5.55% of the Total Remaining Receipts to the Build Illinois Fund
  - 0.27% of Net Revenues Realized to the Illinois Tax Increment Fund
  - Specified Monthly Installment (determined by the State Treasurer), up to a yearly maximum of $139 million, to the McCormick Place Expansion Project Fund

- For Receipts Remaining after the Previous Allocations
  - For Receipts from the Use Tax Act and Retailers' Occupation Tax Act
    - 25% to the Special Account for the Common School Fund
    - 75% to the General Revenue Fund
  - For Receipts from the Service Use Tax Act and Service Occupation Tax Act
    - 100% to the General Revenue Fund

Department personnel wrote they developed the manual methodology because the Department "does not have an electronic receipt processing system capable of automatically calculating and allocating fund deposits. Inherent in any manual process, some human errors do occur and were detected by the auditors."

Failure to exercise adequate control over the deposit and allocation of receipts from sales and use taxes is noncompliance with State law, resulted in deposit errors in the State Treasury, and reduces the reliability of Statewide financial information. (Finding Code No. 11-10)

RECOMMENDATION

We recommend the Department implement controls to ensure the deposit, allocation, and distribution of receipts from sales and use taxes are performed accurately in accordance with State law. In addition, the Department should implement a process to review the individual fund cash balances to determine the fund cash balances are reasonable.

11-10. Finding (Weaknesses in Controls over the Deposit of Sales and Use Tax Receipts) (Continued)

DEPARTMENT RESPONSE

The Department does not have an electronic receipt processing system that can automatically calculate and allocate deposits to funds upon initial receipt for all form types collected for 73 different taxes using over a hundred different calculations for fund splits into 94 different funds. The Department has developed heavily manual deposit estimation and true up process that accounts for the necessary fund allocations and deposits after the returns are processed and perfected, until the State can invest in a general ledger and receipt processing system. This longstanding methodology has resulted in accurate payments to locals and no material adjustments to funds.

The Department will research the feasibility and cost/benefit of further enhancements to GenTax, a rewrite of the current Consolidated Accounting System, and development of a general ledger system for reconciling detail return information with deposit information.

11-11 Finding (Year-end Cash Balances Not Properly Recorded)

The Department of Revenue (Department) misstated cash during the year-end reporting process.

During testing of the cash balances recorded in the Office of the State Comptroller's GAAP reporting packages, the auditors noted the following:

- The amounts the Department allocated from each tax unit to the GAAP reporting packages did not agree with the balances reported on the bank reconciliations for the same tax units. In total, the Department maintains 19 tax units, for which 13 (68%) contained discrepancies in the amount allocated to the funds per the GAAP packages versus the amounts allocated in the bank reconciliations. In aggregate, the errors led to an overstatement of $4.7 million in cash on the GAAP packages. This amount was deemed immaterial and did not require the Department to make any adjustment to their financial statements.
- The Department did not properly record $7.1 million of cash from remittance clearing accounts, leading to cash being understated as of June 30, 2011. The Department maintains 10 remittance clearing accounts in 8 remittance clearing tax units totaling approximately $39.2 million at year end. In the current year, the Department did not record $7.1 million (18%) in the GAAP reporting packages. This amount was deemed immaterial and did not require the Department to make any adjustment to their financial statements.

In accordance with generally accepted accounting principles (GAAP), all assets, liabilities, revenues, and expenses should be accurately measured and recorded. Also, 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, which 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.

Department personnel stated the majority of the cash over(under)statements were included in suspense clearing accounts at June 30, 2011 pending final deposit to the appropriate tax units and were not included in the GAAP reporting packages as they were not deemed material. The majority of the cash over(under)statements were the result of consistently applying a procedure that picks up certain receipts for a few days in July each year.

Inaccurate Office of the State Comptroller GAAP reporting packages result in inaccuracies in the Department's financial statements as well as the State's Comprehensive Annual Financial Report (CAFR).

By failing to properly and accurately record all cash amounts, the Department has misstated its cash balance in the Office of the State Comptroller's GAAP reporting packages, Department financial statements and the Statewide CAFR. (Finding Code No. 11-11)

RECOMMENDATION

We recommend the Department implement procedures to ensure the amount allocated from each tax unit to the GAAP reporting packages agrees with the balances reported on the bank reconciliations for the same tax units.

11-11 Finding (Year-end Cash Balances Not Properly Recorded) (Continued)

DEPARTMENT RESPONSE

The Department agrees that it's GAAP reporting packages were 99.8 percent accurate at June 30, 2011 regarding cash equity (i.e. a net $2.4 million of the total $1.3 billion in total cash equity in State Treasury reported by the Department was not reported in the GAAP reporting packages). We respectfully disagree with the materiality of the finding.

The Department regularly receives electronic deposits of funds with invalid, incomplete, or missing tax unit information requiring follow up with financial institutions and taxpayers to determine the correct clearing account of deposit. These funds are deposited into a suspense clearing account until the appropriate tax unit is determined. This process is normally completed within a business day or two, and the amounts are then moved to the appropriate clearing account from the suspense clearing account.

The majority of the cash overstatements were the result of consistently applying a procedure to account for year-end cutoff of cash that picks up certain receipts for a few days in July each year and was not considered material to adjust.

The Department is developing a procedure to ensure such amounts are included in the GAAP reporting packages in the future.

11-12 Finding (Weaknesses in Internal Controls over Taxpayer Accounts)

The auditors noted weaknesses in the Department of Revenue's controls over taxpayer accounts.

During testing of the Department of Revenue's accounts receivable from income taxes, the auditors sampled 97 taxpayer accounts (from Business Income Tax, Individual Income Tax, and Withholding Income Tax), totaling $30.1 million. The accounts were selected from the Department of Revenue's accounts receivable data file for financial reporting. The auditors noted the following:

- Four taxpayer accounts tested (4%) were invalid, totaling $401,252, due to the Department of Revenue (Department) untimely processing taxpayer information, not identifying an uncollectable account, and posting tax payments to incorrect accounts.

GASB Statement No. 33, Paragraph 16, states governments should recognize assets from derived tax revenue transactions in periods when the exchange transaction on which the tax is imposed occurs or when the resources are received, whichever occurs first. In accordance with this guidance, the amount of any tax assessment and accrued penalties and interest should be recorded by the Department as a receivable, net of an allowance for uncollectable amounts. Further, there is no provision in the standard to delay recognition of these types of transactions until the accounts are fully processed.

- The Department incorrectly calculated tax due on three taxpayer accounts tested (3%), resulting in an overstatement of accounts receivable by $94,099. Specifically, these accounts – which had been audited by the Department – were incorrect on June 30, 2011 due to:
  - the Department calculating an estimated tax liability using 12 months of sales tax data for a six month tax period;
  - understating a taxpayer's bonus depreciation subtraction; and,
  - incorrectly calculating a taxpayer's apportionment factor.

Department Publication PIO-60, *Illinois Audit Information*, states the objective of an audit is to "determine whether the correct amount of tax has been reported and paid."

- The Department incorrectly calculated penalties and interest on ten taxpayer accounts tested (10%), resulting in an understatement of accounts receivable by $112,598. Specifically, interest and penalties were incorrect on June 30, 2011 due to:
  - calculations using an incorrect tax basis;
  - penalty not calculated through the Notice of Deficiency date;
  - interest being applied a day late;
  - interest not being applied back to the due date of the original return; and,
  - interest previously refunded to the taxpayer now due back to the Department not being properly recorded.

- The auditors noted the Department's tax processing system, GenTax, did not properly calculate interest and penalties on audits. During testing, it was noted the GenTax operates differently for audits than any other item that comes into the system. This requires a number of unique manual processes to be performed to have the system current and up to date for periods audited, specifically on complex audits. The Department's auditors maintained a spreadsheet to calculate interest and penalties on audits. However, upon placement of the audit information into GenTax, the interest and penalties were not manually updated to reflect the correct amount as GenTax is not programmed to calculate the interest and penalties on audits in an automated methodology.

11-12 Finding (Weaknesses in Internal Controls over Taxpayer Accounts) (Continued)

Department's Publication 103, *Penalties and Interest for Illinois Taxes*, states, "Interest will begin to accrue the day after the date the payment is due through the date you pay the tax." Additionally, the Illinois Income Tax Act (35 ILCS 5/804(f-g)) states that in order to calculate the penalty on estimated payments, withholdings from compensation and payments are to be reflected in the calculation.

The errors noted above and other errors only impacting financial reporting were projected to the entire billed income tax receivable populations, and the projected estimated overstatement for the populations as a whole are noted in the following chart. In addition, the Department projected an error rate based on their own review and made the adjustments noted in the chart below. The difference between the auditor's projection and the Department's adjustments were deemed immaterial and no adjustments were considered necessary to financial statements.

	Net Accounts Receivable			
	Business	Individual	Withholding	Total
Auditor's Projected Error	5,998,531	4,461,083	1,059,077	11,518,691
Department's Projected Error	4,953,308	4,414,645	639,279	10,007,232
Difference	1,045,223	46,438	419,798	1,511,459

Additionally, as part of performing their testing of income tax accounts receivable, the auditors noted internal control weaknesses in the processing of income taxes in the following areas:

- As part of the testing to substantiate reported accounts receivable balances, external auditors had to review documentation for balances determined through tax audits performed by Department auditors. In performing this testing, the external auditors, for some accounts, were provided tax audit documentation which was disorganized and incomplete. In addition, for one specific audit account, the Department could not provide audit documentation due to a Department auditor's hard drive crashing, which resulted in the loss of supporting audit information.

The Department's Audit Bureau should work towards implementing formalized documentation protocol and maintenance of tax audit information such that information is maintained in an organized format which should ensure completeness.

The State Records Act (5 ILCS 160/8) states "the head of each agency shall cause to be made and preserved records containing adequate and proper documentation of the organization, functions, policies, decisions, procedures, and essential transactions 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."

- The Department has not updated their form and GenTax is not programmed to process the payment provisions for withholding income tax within the Illinois Income Tax Act (35 ILCS 5/704A(c)). The Department currently does not require taxpayers to report payroll dates on the Form IL-941 and the GenTax system is not designed to apply payments and calculate or assess late payment penalties and interest upon taxpayers for failing to pay withholding income tax in a timely manner. The Department has not determined the financial impact of not implementing the payment provisions.

- GenTax is not programmed to automatically reassign monthly payment taxpayers to the semi-weekly payment schedule when the taxpayer's calendar year withholding exceeds $12,000.

11-12 Finding (Weaknesses in Internal Controls over Taxpayer Accounts) (Continued)

The Illinois Income Tax Act (35 ILCS 5/704A(c)) requires withholding income taxpayers to remit payments withheld by payroll period to the Department pursuant to statutorily mandated due dates. Further, the Act requires the Department assign a taxpayer to the semi-weekly payment schedule after their calendar year withholding exceeds $12,000.

- The Department's policy regarding the date to impose the Cost of Collection penalty does not comply with State law, resulting in the penalty being systemically imposed late onto taxpayer accounts.

The Uniform Penalty and Interest Act (35 ILCS 735/3-4.5) requires the Department assess the penalty on the 31st day following a notice and demand, a notice of additional tax due, or a request for the payment of a final liability issued by the Department.

Department personnel stated most of the errors noted by the auditors are the result of human errors due to entering data into the system and manual calculations being performed by Department personnel.

Exceptions in processing taxpayer accounts, system errors, and internal control deficiencies led to errors in calculating the proper amount of tax, penalties, and interest due from taxpayers in accordance with State laws, rules, and regulations. Further, the impact of these errors – when accumulated – could result in financial reporting errors. (Finding Code No. 11-12)

RECOMMENDATION

We recommend the Department:

- take action to improve the timeliness in processing taxpayer information to ensure the taxpayer's records and the Department's financial information is accurately reflected;
- improve controls to ensure tax, penalties, and interest are properly calculated and accurately reflected in the taxpayer's records and the Department's financial information;
- implement controls to ensure compliance with the Illinois Income Tax Act, the Uniform Penalty and Interest Act, and the State Records Act; and,
- implement controls in order to properly calculate interest and penalties on the Department's audited tax accounts once entered into GenTax.

DEPARTMENT RESPONSE

The Department agrees that it can improve its processes and take into consideration the issues noted by the auditors. Most of the errors noted by the auditors are the result of human errors due to entering data into the system and manual calculations being performed by Department personnel. These errors generally reflected a de minimis amount when compared to the matter in total. The Department continually strives for perfection, but a certain amount of errors will always be inherent in such a complex operating environment.

It should be noted that the review of the accounts in this testing by the auditors was selected from Department's year-end accounts receivable listing, which represents a small percentage of the total accounts processed by the Department. Moreover, these accounts are the most complex and are atypical of the normal taxpayer, as more assessments are issued for some sort of non-compliance with tax law on these accounts.

The effects of the errors noted by the auditors on Accounts Receivable balances for financial reporting purposes were minimal and reflected a difference of $1.5 million out of a reported Accounts Receivable amount of $1.3 billion (99.9% accurately reported).

11-12 Finding (Weaknesses in Internal Controls over Taxpayer Accounts) (Continued)

DEPARTMENT RESPONSE (Continued)

With respect to bullet point eight, we respectfully disagree with the auditor's interpretation of the statute and policies that the Department has in place. As stated, the auditors want the Department to assess penalty on the "31st day following a notice and demand". This is not effective or efficient tax compliance policy and is inherently inequitable to the taxpayers.

The Department has a stated policy that allows time for the mailing of payments to the Department.
The taxpayer is credited for timely payment as long as the bill item is post-marked by the 30th day. As an example, the taxpayer can mail the payment on the due date and it can take many days for the Department to receive the mail.

By following the interpretation of the auditors, as we understand it, the Department would be issuing thousands of erroneous assessments to taxpayers and then would have to correct such assessments when the payment is processed utilizing the post-mark date of the payment. This would be an enormous waste of State resources and increase the inventory levels of the Department, as these erroneous assessments would become work items.

A. Finding (Year-end Reporting Procedures for Receivables Not Followed)

During the prior audit period, the Department of Revenue (Department) did not follow its established procedures for determining the accuracy of its billed accounts receivable for financial reporting purposes. This led to the overstatement of balances initially reported in the GAAP packages for business income tax, individual income tax, withholding income tax and sales tax (BIT, IIT, WIT and ROT).

During the current audit period, the Department implemented updated procedures and improved controls to address the year-end reporting process of receivables. (Finding Code No. 10-2)

B. Finding (Year-end Accounting Estimate Not Prepared Accurately)

During the prior audit period, the Department of Revenue (Department) does not have sufficient procedures and controls in place to ensure that the amount reported for deferred revenue relating to income tax credit-carry forwards is determined based on all available information on hand.

During the current audit period, the Department implemented updated procedures and improved controls to address the year-end accounting estimate process for deferred revenue relating to income tax credit-carry forwards. (Finding Code No. 10-3)

C. Finding (Year-end Receivable Not Properly Allocated)

During the prior audit period, the Department of Revenue (Department) incorrectly allocated accrued taxes receivable for year-end financial reporting. A portion of the receivable pertaining to the Illinois Sports Facility's Fund (225) was recorded in error to the General Revenue Fund.

During the current audit period, the Department improved controls to address the year-end receivable allocation process related to reporting receivables in the Illinois Sports Facility's Fund (225). (Finding Code No. 10-4)

D. Finding (Certain Year-end Receivables Not Valid)

During the prior audit period, the Department of Revenue (Department) included invalid taxes receivable accounts in the Department's Sales Tax (ROT), Withholding Income Tax (WIT), Business Income Tax (BIT), and Individual Income Tax (IIT) accounts receivable calculation at June 30, 2010.

During the current audit period, the Department improved the process to better estimate a materially correct valid receivables at June 30, 2011; however, the auditors noted certain internal control deficiencies over income taxes receivable, which is reported in Finding 11-12. (Finding Code No. 10-5, 09-2, 08-2)

E. Finding (Noncompliance With the Public Utilities Revenue Act)

During the prior audit period, the Department of Revenue (Department) did not calculate and timely issue the invested capital tax on the distribution of electricity credit (tax credit), leading to an unrecorded $18.7 million liability in the Department's June 30, 2010 financial statements.

During the current audit period, the Department calculated and recorded the tax credit during the fiscal year. (Finding Code No. 10-10)

F. Finding (Inadequate Controls over Taxes Collected for Local Governments)

During the prior audit period, the Department of Revenue (Department) did not exercise adequate control over the deposit and allocation of locally-imposed School Facility Occupation Taxes (SFOT), Flood Prevention Occupation Taxes (FPOT), or Metro-East Mass Transit District fees.

During the current audit period, the auditors noted the Department processed SFOT and FPOT through the Department's normal ROT allocation process; however, the auditors noted control deficiencies within the Department's processes and procedures (see Finding 11-5 and Finding 11-10). Additionally, the auditors noted the Department reduced FY12 distributions to the Metro-East Mass Transit District to recover $71,02 in erroneous distributions from FY05 through FY11. (Finding Code No. 10-12, 09-10)