DEPARTMENT OF REVENUE
STATE OF LOUISIANA

FINANCIAL AUDIT SERVICES
MANAGEMENT LETTER
ISSUED NOVEMBER 30, 2016

LOUISIANA LEGISLATIVE AUDITOR
1600 NORTH THIRD STREET
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LEGISLATIVE AUDITOR
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Louisiana Legislative Auditor
Daryl G. Purpera, CPA, CFE

Louisiana Department of Revenue

November 2016 *Audit Control # 80160161*

Introduction

As a part of our audit of the state of Louisiana's Comprehensive Annual Financial Report (CAFR) and the Single Audit of the State of Louisiana for the year ended June 30, 2016, we performed procedures at the Louisiana Department of Revenue (LDR) to provide assurances on financial information that is significant to the state's CAFR, evaluate the effectiveness of LDR's internal controls over financial reporting and compliance, and determine whether LDR complied with applicable laws and regulations. In addition, we determined whether management has taken actions to correct findings reported in the prior year.

LDR is the state agency charged with the assessment, collection, administration, and enforcement of taxes, fees, licenses, penalties, and interest due to the state of Louisiana. The department's mission is to fairly and efficiently collect state tax revenues to fund public services; to regulate charitable gaming and the sale of alcoholic beverages and tobacco; and to support state agencies in the collection of overdue debts.

Results of Our Procedures

Follow-up on Prior-year Findings

Our auditors reviewed the status of the prior-year findings reported in a management letter dated December 23, 2015. We determined that management has resolved the prior-year findings related to Ineffective Controls over Certain Severance Tax Refunds and Inadequate Preparation of the Annual Fiscal Report, and partially resolved the finding on Inadequate Planning and Management of Information Technology Projects and Systems. The prior-year findings related to Inadequate Controls over LaCarte Card Purchases, Overpayment of Sales Tax Distributions to Local Government, and Inadequate Planning and Management of Information Technology Projects and Systems, as it relates to timely deposits, have not been resolved and are addressed again in this report.

Current-year Findings

Overpayment of Sales Tax Distributions to Local Government

LDR continued to overpay the Algiers Economic Development District No. 1 (District). The overpayment to the District since the beginning of its Cooperative Endeavor Agreement (Agreement) executed in 2004 is $7.3 million, including $494,454 in overpayments during fiscal year 2016. LDR did not concur with our prior-year finding and has not implemented any corrective action during fiscal year 2016, although the Agreement requires that LDR eliminate any shortage or overage by adjusting future distributions.

The Agreement between LDR and the District states that LDR shall distribute the calculated "Monthly Pledged State Increment" to the District every quarter, which is defined by the Agreement as the lesser of the "Monthly State Increment" (MSI) and the "Monthly Local Increment."

The MSI is equal to the excess of 1.25 cents of the state sales tax collections from taxpayers in the District over the monthly state base ($74,864, per the agreement). Rather than using the excess of 1.25 cents of the sales tax collections in its calculation, LDR used the total sales tax collections from the taxpayers in the District, which resulted in the overpayments.

LDR management should reevaluate the current distribution calculation and work on a plan to recoup past overpayments. Management concurred with the finding and stated, "The necessary steps to correct the issue and all future distributions to the ADD will be implemented during the current fiscal year." See Appendix A, pages 1-2.

Inadequate Controls over LaCarte Card Purchases

For the third consecutive year, LDR did not effectively implement or adequately monitor controls over LaCarte card purchases, resulting in unauthorized purchases, increased risk of errors and fraud, and noncompliance with state guidelines.

A review of 64 transactions from the third and fourth quarters of fiscal year 2016 for six LDR LaCarte cardholders, including one for the Louisiana Office of Alcohol and Tobacco Control (ATC), disclosed six exceptions – two Paypal purchases and four Amazon.com purchases. Expanded testing was performed on all LDR cardholders for the entire fiscal year to identify additional PayPal and Amazon.com purchases. Our testing disclosed the following combined exceptions:

- Forty-five transactions totaling $6,384, including 25 for the ATC cardholder, were for purchases through Amazon.com without evidence of pre-approval from the program administrator or documentation of Amazon.com being the sole source, as required by LDR policy.

- Five purchases totaling $1,804, including three for the ATC cardholder, were made using PayPal accounts, which are prohibited by LDR policy.

As required by the State of Louisiana's LaCarte Purchasing Card Policy, LDR has established policies documenting all internal procedures for cardholders, supervisors, and the program administrator. LDR's policies are written to ensure that the department complies with the state program guidelines. However, these policies are not being consistently enforced and are therefore not effectively implemented and monitored by LDR.

LDR management should ensure that the WORKS site is reviewed regularly by the Program Administrator to ensure all support and receipts are attached timely to each transaction, that all purchases are properly approved, and that all purchases are allowable per state and LDR LaCarte policies. In addition, management should consider decreased credit lines and/or card suspension for cardholders and supervisors who fail to follow program policies. Furthermore, management should monitor established controls to reduce the risk of error and fraud in the program. Management concurred with the finding and outlined the corrective actions implemented by the department (see Appendix A, pages 3-4).

Untimely Deposit of Tax Payments

For the second consecutive year, LDR's Revenue Processing Center has failed to deposit tax payments into the State Treasury in a timely manner. LDR's untimely deposit of state funds increases the risk of loss or misappropriation of funds due to error or fraud.

Of 489,746 checks received and processed through the Tax Express system between January 1, 2016, and June 30, 2016, 114,710 checks (23%) totaling $175,977,774 were deposited between 14 and 79 days after receipt, an average of 18 days after receipt. Per LDR management, the untimely deposits of tax payments were due to the volume of return filings and a 39% reduction in the number of employees processing the filings.

The Louisiana Constitution, Article VII, Section 9 (A) requires that all monies received by the state or by any state board, agency, or commission shall be deposited immediately upon receipt in the State Treasury. According to Louisiana Administrative Code, Title 4, Part XIII, "immediately" is defined as within 24 hours of receipt.

LDR management should ensure that all tax payments are processed and deposited timely in accordance with state law. Management indicated concurrence with the facts presented but attributed the delay during the period tested to the high volume of returns processed and the inability to hire temporary staff during high-volume months (see Appendix A, pages 5-6).

Inadequate Controls over Human Capital Management and Advantage Financial System Access

LDR did not adequately monitor access to the Human Capital Management (HCM) system and Advantage Financial System (AFS) during fiscal year 2016. As of June 30, 2016, three current LDR employees held inappropriate access in HCM, and one former LDR employee retained AFS access following termination. Inadequate monitoring of system access exposes the department to an increased risk of undetected errors or fraud and possible misappropriation of assets.

The agency inappropriately granted HCM timekeeper access to three new employees who have no timekeeper duties because they were placed in positions that previously functioned as timekeepers. Additionally, the agency failed to disable AFR access for an employee who had been terminated in March 2016. While LDR has a process in place to periodically review terminated employee access, the newly-appointed security administrator was not aware of the review process. The Division of Administration requires user agencies to establish procedures for the authorization of changes and adequately monitor access in the systems. Good internal control requires that LDR restrict access to those functions necessary for its employees' job duties, and ensure access is appropriate and based on business need.

LDR management should develop and implement a plan to ensure that proper and necessary system access is granted to employees and periodically reviewed to ensure a continued business need. As staffing changes are made throughout the department, procedures should be in place to provide timely notification of such changes to the security administrator. Management concurred with the finding and outlined a corrective action plan (see Appendix A, pages 7-8).

Comprehensive Annual Financial Report - State of Louisiana

As a part of our audit of the state of Louisiana's CAFR for the year ended June 30, 2016, we considered LDR's internal controls over financial reporting and examined evidence supporting certain account balances and classes of transactions as follows:

Revenues - Corporate income and franchise tax, individual income tax, sales tax, severance tax, and gasoline and special fuels tax
Receivables - Full accrual and modified accrual receivables on the revenues listed above
Note Disclosures - Refunds Payable and Judgments, Claims, and Similar Contingencies

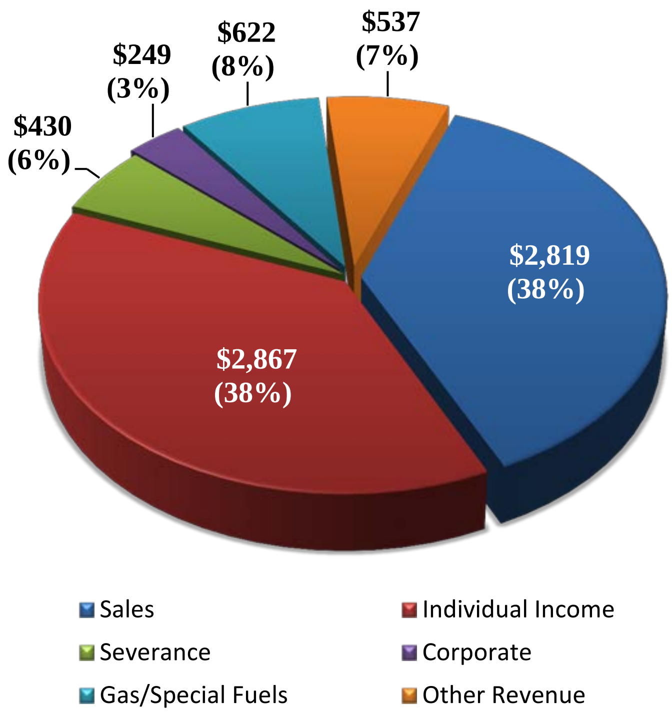
The account balances and classes of transactions tested, as adjusted, are materially correct.

Based on the results of these procedures on the CAFR, we reported four findings related to Overpayment of Sales Tax Distributions to Local Government, Inadequate Controls over LaCarte Card Purchases, Untimely Deposit of Tax Payments, and Inadequate Controls over Human Capital Management and Advantage Financial System Access (see Current-year Findings section).

Trend Analysis

We compared the most current and prior-year financial activity using LDR's annual fiscal reports and/or system-generated reports and obtained explanations from LDR management for any significant variances. We also prepared an analysis of fiscal year 2016 tax revenue collections. The majority of revenues collected by LDR, 93% of total tax revenues, is composed of Individual Income tax and major business taxes including Sales tax, Corporate Income and Franchise tax, Severance tax, and Fuel tax revenue.

Exhibit 1
Fiscal Year 2016 Collections, in millions
Total: $7,524



Source: Fiscal Year 2016 LDR Annual Fiscal Report

The recommendations in this letter represent, in our judgment, those most likely to bring about beneficial improvements to the operations of LDR. The nature of the recommendations, their implementation costs, and their potential impact on the operations of LDR should be considered in reaching decisions on courses of action.

Under Louisiana Revised Statute 24:513, this letter is a public document, and it has been distributed to appropriate public officials.

Respectfully submitted,

Daryl G. Purpera, CPA, CFE
Legislative Auditor

EMS:BQD:EFS:aa

LDR 2016

APPENDIX A: MANAGEMENT’S RESPONSES

State of Louisiana
Department of Revenue

JOHN BEL EDWARDS
Governor

KIMBERLY LEWIS ROBINSON
Secretary

November 18, 2016

Mr. Daryl G. Purpera, CPA, CFE
Louisiana Legislative Auditor
1600 N. 3rd Street
Baton Rouge, LA 70804

RE: Overpayment of Sales Tax Distributions to Local Government
Algiers Economic Development District No. 1 (ADD)

Dear Mr. Purpera:

The management team of the Department of Revenue ("LDR") understands the importance of having policies and procedures for the overall successful operations of an organization. This would include the distribution of state funds to third party stakeholders. The finding addressed below indicates that the agency overpaid the Algiers Economic Development District over $7.3 ($494,454 in FY 2016) million in sales tax distributions since its inception in 2004.

Previously the agency did not concur with the finding of the Legislative Auditor. Though made by the agency's previous administration, the basis of that decision was grounded in the agency's belief that the monthly state base calculation was correctly defined and that the auditor's report fails to set forth the methodology or analysis used by the auditor to establish the finding.

Notwithstanding last year's response and after the completion of this year's audit and a more detailed discussion was had with the Louisiana Legislative Auditor's (LLA) office on this matter, LDR has begun to take steps to work with the Algiers Development District to correct the issue raised by LLA. Also, it appears that from LDR's subsequent review of the TIF and its definition of the monthly state tax base that the calculation of the initial baseline in the cooperative endeavor agreement did create an issue. The necessary steps to correct the issue and all future distributions to the ADD will be implemented during the current fiscal year. In conclusion, the senior management team of the agency concurs with the finding.

Please feel free to reach out to our agency for any additional information or clarification is required by your office.

Contributing to a better quality of life.
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Sincerely,

Kimberly Lewis Robinson
Secretary
Louisiana Department of Revenue

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Mr. Daryl G. Purpera, CPA, CFE
Louisiana Legislative Auditor
1600 N. 3rd St.
Baton Rouge, LA 70804

Re: Inadequate Controls over LaCarte Card Purchases

Dear Mr. Purpera:

The Louisiana Department of Revenue (LDR) recognizes the importance of having adequate controls in place over the LaCarte card program to prevent the occurrence of unauthorized purchases, errors, fraud and noncompliance with the program objectives and state guidelines. Notwithstanding the agency's general concurrence with the finding, the agency believes additional clarification of the facts surrounding this finding must be discussed.

It is being alleged that LDR did not effectively implement or adequately monitor controls over LaCarte card purchases. However, the allegations shared in the audit finding do not consider the following. During the previous audit, it was determined that LDR's program guidelines were more restrictive than the program guidelines issued by the Division of Administration ("DOA"). As a result, LDR's LaCarte Card Program Administrator ("Program Administrator") began working with other colleagues in the agency to update and re-implement LDR's internal Policy and Procedure Memorandum ("PPM") to more correctly align LDR's LaCarte card program guidelines with the state guidelines issued by the DOA. While the Louisiana Legislative Auditor (LLA) began its respective re-audit of the LaCarte card program prior to the policy being revision being completed, the updated PPM was implemented on October 18, 2016 and it has corrected the previous concerns of LLA and those discussed in this audit finding also.

Also, while the audit characterizes two of the reviewed purchases as Paypal purchases, a true description of the purchases should include the fact that the LDR employees made the purchases in accordance with the program purchase rules. When finalizing the purchases, the vendor and/or entity required the sale be finalized through the Paypal system. So, while the purchase of the item was authorized by LDR policy, the method of completing the transaction as dictated by the vendor created the issue.

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LDR, through the Program Administrator, has also implemented various corrective actions to address the LLAs' concerns regarding the agency's ability to monitor controls over LaCarte card purchases. The Program Administrator increased the frequency in which the WORKS site will be reviewed for documentation showing the approval of purchases and receipts evidencing the date, method and amount of various purchases. LDR and its Program Administrator have also reduced of the number of cardholders, segregated the types of transactions performed by specific cardholders, expressly outlined a list of prohibited purchases, implemented a more detailed back-up cardholder purchase procedure, and reduced cardholder purchase limits.

During the last audit cycle, LDR had eighteen (18) cardholders; that number has now been reduced to six (6). Additionally, one (1) of the six (6) cardholders is directly responsible for purchasing items that require specific detailed information to ensure proper approvals are in place. Of the 6 existing cardholders, one cardholder has been designated as a backup cardholder to make purchases in the absence of any cardholder. A list of prohibited purchases has been included in LDR's PPM to further alert all cardholders and agency personnel of items that cannot be purchased under the LaCarte card program. Lastly, each cardholder's purchase limit has been reduced.

LDR is committed to effectively implement and administer the necessary controls, procedures and guidelines of the LaCarte card program. The Program Administrator and the Undersecretary will be the responsible parties for ensuring that the LDR continues to do so in a timely manner. Please feel free to reach out to our agency if any additional information or clarification is needed.

Sincerely,

Kimberly Lewis Robinson
Secretary
Louisiana Department of Revenue

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November 18, 2016

Mr. Daryl G. Purpera, CPA, CFE
Louisiana Legislative Auditor
1600 N. 3rd Street
Baton Rouge, LA 70804

RE: Untimely Deposit of Tax Payments

Dear Mr. Purpera:

The management team of the Louisiana Department of Revenue (LDR) recognizes the importance of the timely depositing of paper remittances processed by the agency.

The management of LDR does not dispute the fact that these payments exceed the average of the processing time for paper checks for the fiscal year. However, management does not agree that this is a "repeat finding". The finding in the prior year was associated with "Inadequate Planning and Management of IT Projects and Systems". The finding from FY 16 just highlights the high volume of transactions that are processed by the Revenue Processing Center and the yearly fluctuation in volume during the income processing season.

Deposit time for this period of the fiscal year always increase due to the volume of payments received. In addition, due to budget reductions the agency was unable to hire the yearly temporary staff to provide additional manpower for the increased volume. The agency would like to point out that the Legislative Auditor has chosen the period of time when 70% of all the paper remittances are processed by the agency. Approximately 98% of the 114K transactions selected by the auditor were received in the months of April and May. It should be noted that the average deposit times for that period of time was 7.93 days, well below the 18 day average of the sample. The average deposit times for FY16 was 4.49 days well below the 18 day average sited by the auditor.

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Prior to the time frame noted by the auditor of January through May, the average processing time for the deposits was 2.7 days.

If you further analyze the sample of transactions selected, 70% of the transactions were processed at the average of 18 days noted by the auditors and 95% are processed within 21 days. The transactions with higher processing times are the minority and not a true representation of the performance of the agency or the staff assigned to perform the duties of processing these payments.

This type of variation in processing time is to be expected with volume fluctuation and occurs every year. While this can be minimized, it cannot be 100% eliminated unless 100% electronic payment policies are enacted.

Please feel free to reach out to our agency for any additional information or clarification is required by your office.

Sincerely,

Kimberly Lewis Robinson
Secretary

State of Louisiana
Department of Revenue

JOHN BEL EDWARDS
Governor

KIMBERLY LEWIS ROBINSON
Secretary

November 18, 2016

Mr. Daryl G. Purpera, CPA, CFE
Louisiana Legislative Auditor
1600 N. 3rd Street
Baton Rouge, LA 70804

RE: Inadequate Controls over Human Capital Management and Advantage Financial System Access

Dear Mr. Purpera:

The management team of the Department of Revenue understands the importance of internal controls over operations. This would include the supervising and monitoring of access to all computer systems necessary for the agency to perform its core mission.

While the agency concurs with the findings of the auditors, the recommendation of the auditor suggests that the agency does not have a process in place to review access rights to these systems. Over the last fiscal year there have been fourteen (14) changes to the ISIS system related to the agency. Only one (1) instance of an employee not having access rights removed after termination was noted. Going forward, the agency will require the director of the Budget and Financial Services Division to review the personnel action report in addition to the ISIS administrator. The division will enhance controls by instituting a formal written monthly review and signoff procedure. This will add a written signoff/acknowledgement document that will be retained in the division for a period of two (2) fiscal years to the already existing procedure. In addition, the agency will require the Human Resource Director to perform an independent quarterly review to ensure that only those with timekeeper duties have access to the Human Capital Management system.

The senior management team of the agency feels that these additional requirements will serve as an additional check on the access to these key systems and strengthen the internal controls in the agency.

Please feel free to reach out to our agency for any additional information or clarification is required by your office.

Sincerely,

Kimberly Lewis Robinson
Secretary

APPENDIX B: SCOPE AND METHODOLOGY

We performed certain procedures at the Department of Revenue (LDR) for the period from July 1, 2015, through June 30, 2016, to provide assurances on financial information significant to the state of Louisiana's Comprehensive Annual Financial Report (CAFR) and to evaluate relevant systems of internal control in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States. The procedures included inquiry, observation, and review of policies and procedures, and a review of relevant laws and regulations. Our procedures, summarized below, are a part of the audit of the CAFR and the Single Audit of the State of Louisiana (Single Audit) for the year ended June 30, 2016.

- We evaluated LDR's operations and system of internal controls through inquiry, observation, and review of its policies and procedures, including a review of the laws and regulations applicable to LDR.

- Based on the documentation of LDR's controls and our understanding of related laws and regulations, we performed procedures to provide assurances on certain LDR account balances and classes of transactions to support the opinions on the CAFR.

- We compared the most current and prior-year financial activity using LDR's annual fiscal reports and/or system-generated reports to identify trends and obtained explanations from LDR management for significant variances.

The purpose of this report is solely to describe the scope of our work at LDR and not to provide an opinion on the effectiveness of LDR's internal control over financial reporting or on compliance. Accordingly, this report is not intended to be, and should not be, used for any other purposes.

We did not audit or review LDR's Annual Fiscal Report, and accordingly, we do not express an opinion on that report. LDR's accounts are an integral part of the state of Louisiana's CAFR, upon which the Louisiana Legislative Auditor expresses opinions.