



STATE OF ILLINOIS
**OFFICE OF THE
 AUDITOR GENERAL**

Frank J. Mautino, Auditor General

SUMMARY REPORT DIGEST

STATE OF ILLINOIS

Statewide Financial Statement Audit
 For the Year Ended June 30, 2017

Release Date: March 22, 2018

FINDINGS THIS AUDIT: 5	New	Repeat	Total	AGING SCHEDULE OF REPEATED FINDINGS			
				Repeated Since	Category 1	Category 2	Category 3
Category 1:	0	3	3	2010	17-05		
Category 2:	0	0	0	2009			17-03, 17-04
Category 3:	<u>0</u>	<u>2</u>	<u>2</u>	2007	17-01		
TOTAL	0	5	5	2002	17-02		
FINDINGS LAST AUDIT: 5							

INTRODUCTION

The Office of the State Comptroller prepares the State of Illinois' Comprehensive Annual Financial Report (CAFR). The CAFR is the State's official annual report which provides the readers with the financial position of the State as of June 30, 2017, and results of operations during the fiscal year.

The financial section of the CAFR includes the Independent Auditors' Report on the basic financial statements, management discussion and analysis, the basic financial statements, required supplementary information, and individual fund statements and schedules.

AUDITOR'S OPINION

The financial statements of the State of Illinois are fairly presented in all material respects.

The financial statements at June 30, 2017, reflect the following:

- The net position of governmental activities continued to deteriorate and the deficit increased by \$10.1 billion from June 30, 2016 to June 30, 2017. Overall, the net position of governmental activities is reported as a deficit of \$141.7 billion. (Exhibit 1)
- The General Fund deficit increased by \$5 billion from June 30, 2016 to June 30, 2017. The General Fund deficit is \$14.6 billion. (Exhibit 2)

Over time, increases and decreases in net position measure whether the State's financial position is improving or deteriorating. A comparison of the State's financial position to other states is contained in Exhibit 3.

- Category 1:** Findings that are **material weaknesses** in internal control and/or a **qualification** on compliance with State laws and regulations (material noncompliance).
- Category 2:** Findings that are **significant deficiencies** in internal control and **noncompliance** with State laws and regulations.
- Category 3:** Findings that have **no internal control issues but are in noncompliance** with State laws and regulations.

**REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE**

In accordance with *Government Auditing Standards*, a report on our consideration of the State of Illinois' internal control over financial reporting and our tests of its compliance is also issued as part of our financial statement audit. This report is a separate document and is summarized in this document. Our report noted that the State's decentralized internal control system is not adequate. We also reported significant financial reporting deficiencies at several State agencies.

STATE OFFICIALS

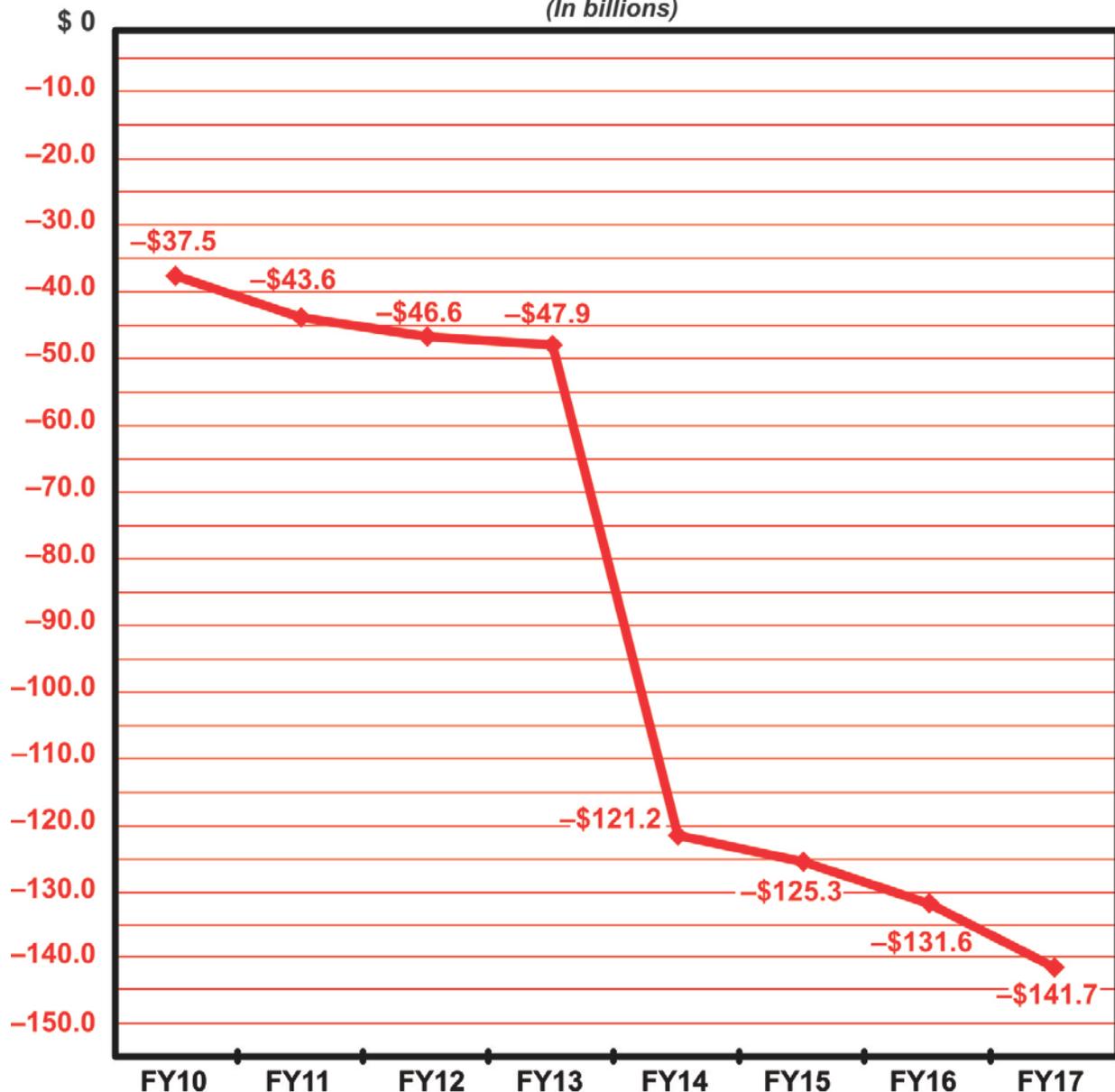
As of June 30, 2017

Governor	Bruce Rauner
Comptroller	Susana A. Mendoza
Speaker of the House	Michael J. Madigan
President of the Senate	John J. Cullerton
House Republican Leader	Jim Durkin
Senate Republican Leader	William E. Brady

FINANCIAL ANALYSIS OF THE STATE

The net position of the State's governmental activities declined \$10.092 billion. The following condensed financial information was derived from the government-wide Statement of Net Position and reflects the State's governmental activities financial position as of June 30 for Fiscal Years 2010 through 2017.

EXHIBIT 1 STATE OF ILLINOIS DEFICITS FOR NET POSITION OF GOVERNMENTAL ACTIVITIES FY10-FY17 (In billions)



Source: State of Illinois' Comprehensive Annual Financial Report (2017)
Numbers reflect restatements.

The deficits reflected in Exhibit 1 are presented on an accrual basis and represent the excess of total liabilities and deferred inflows of resources over total assets and deferred outflows of resources at a given point in time. These deficits represent the deferral of current and prior year costs to future periods.

GENERAL FUND

Many programs are accounted for in the General Fund. The GAAP basis financial position of the General Fund deficit increased at June 30, 2017, from June 30, 2016. The fund balance deficit in the State's General Fund increased by \$5.020 billion on a GAAP basis. The June 30, 2017, deficit was \$14.6 billion. Exhibit 2 reflects the General Fund deficit for Fiscal Years 2010 through 2017.

EXHIBIT 2
STATE OF ILLINOIS
GENERAL FUND DEFICITS
FY10-FY17
(In billions)

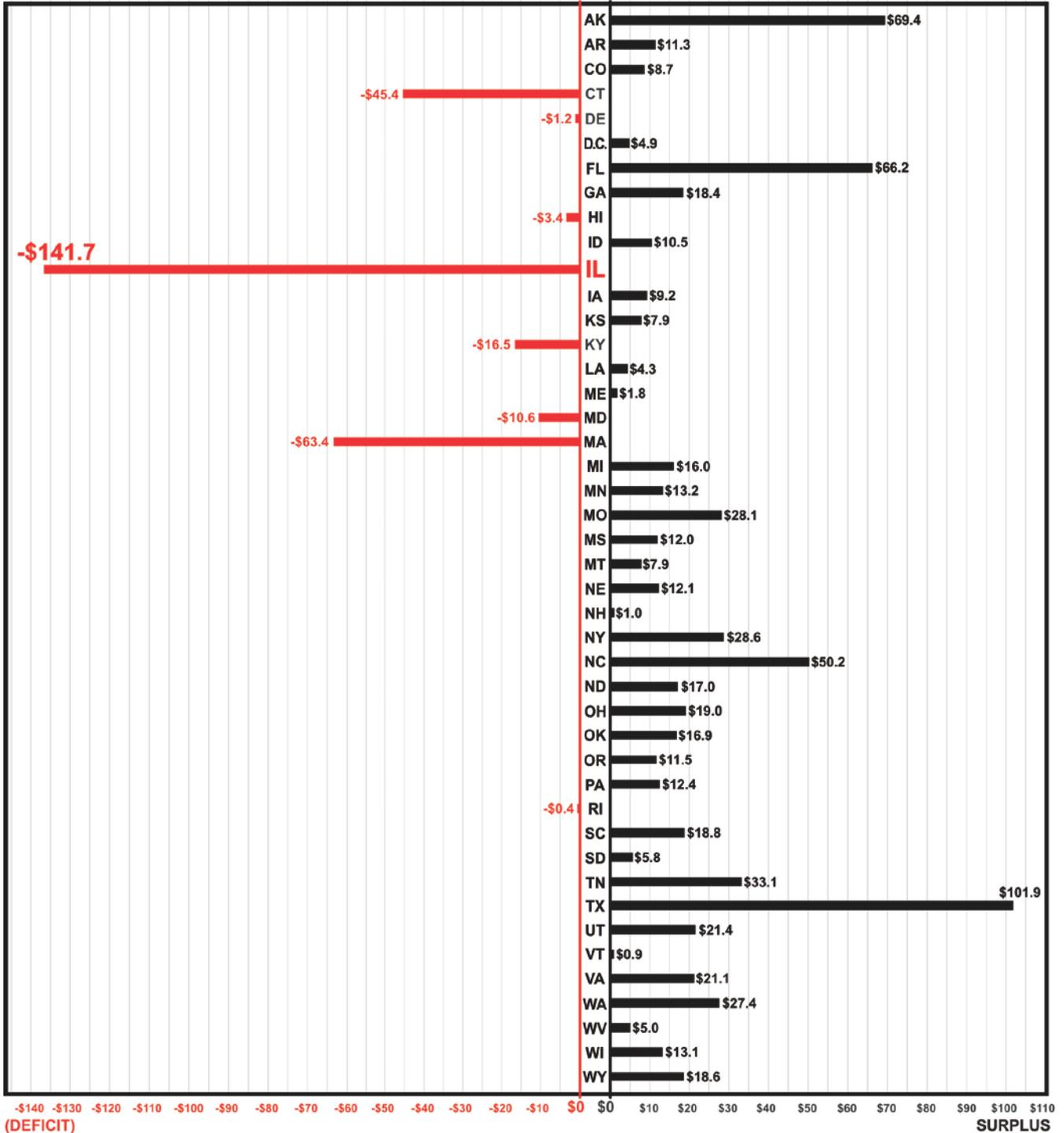


Source: State of Illinois' Comprehensive Annual Financial Report (2017)
Numbers reflect restatements.

STATE COMPARISON

Exhibit 3 provides an analysis of State's governmental activities net position at June 30, 2017, compared to other States.

EXHIBIT 3
STATE COMPARISON OF NET POSITION OF GOVERNMENTAL ACTIVITIES
FOR FY17
(In billions)



Source: Compiled by Illinois Auditor General's Office from Comprehensive Annual Financial Reports (CAFR) for each state, excluding Alabama, Arizona, California, Indiana, Nevada, New Jersey, and New Mexico, which were not available at March 15, 2018.

FINDINGS, CONCLUSIONS, AND
RECOMMENDATIONS

INADEQUATE FINANCIAL REPORTING PROCESS

The State of Illinois' current financial reporting process does not allow the State to prepare a complete and accurate Comprehensive Annual Financial Report (CAFR) in a timely manner. Reporting issues at various individual agencies caused delays in finalizing the financial statements. The lack of timely financial reporting limits effective oversight of State finances and may adversely affect the State's bond rating.

Financial reporting problems continue

Accurate and timely financial reporting problems continue to exist even though the auditors have: 1) continuously reported numerous findings on the internal controls (material weaknesses and significant deficiencies), 2) commented on the inadequacy of the financial reporting process of the State, and 3) regularly proposed adjustments to financial statements year after year. These findings have been directed primarily towards major State agencies under the organizational structure of the Office of the Governor and towards the Office of the State Comptroller.

Financial reporting problems not resolved

The Office of the State Comptroller has made significant changes to the system used to compile financial information; however, the State has not solved all the problems to effectively remediate these financial reporting weaknesses. The process is overly dependent on the post audit program even though the Office of the Auditor General has repeatedly informed State agency officials that the post audit function is **not** a substitute for appropriate internal controls at State agencies.

Financial reporting process dependent on post audits

Only 16% of the 263 different financial reporting systems compliant with GAAP

The State has a highly decentralized financial reporting process. During an Office of the Auditor General's management audit (released in 2011), it was reported that 88 of 90 primary units of government had 263 different financial reporting systems that are used by primary government agencies and only 16 percent of these financial reporting systems are compliant with Generally Accepted Accounting Principles (GAAP), which drastically increases the amount of time spent by the agencies during the year-end GAAP conversion process. In addition, 53 percent of the financial reporting systems are not interrelated, which, consequently, requires manual intervention to convert data. This process is time consuming and increases the likelihood of errors.

53% of the 263 different financial reporting systems not interrelated

Annual financial reporting to the Office of the State Comptroller requires the State's agencies to prepare a series of financial reporting forms (SCO forms) designed by the Office of the State Comptroller, which are utilized to prepare the CAFR. Although these SCO forms are subject to review by the Office of the State Comptroller's financial reporting staff

Financial reporting process still lacks sufficient internal controls

during the CAFR preparation process and there are minimum qualifications for all new GAAP Coordinators who oversee the preparation of the SCO Forms, the current process still lacks sufficient internal controls at individual agencies. (Finding 1, pages 7-9)

We recommended the Office of the Governor and the Office of the State Comptroller continue to work together to resolve the State's inability to produce timely and accurate Generally Accepted Accounting Principles basis financial information.

Governor's Office agreed with auditors

The Governor's Office agreed with our recommendation and stated that the Governor's Office and the Office of the State Comptroller will continue to work together to address the core issues of the State's inability to produce timely and accurate GAAP basis financial information. Both offices are in the midst of a multi-year implementation of an Enterprise Resource Planning (ERP) system to develop an integrated enterprise-wide application system for financials, which is an aspect of the Governor's Executive Order that created the Illinois Department of Innovation and Technology to transform Illinois' IT system to be more responsive to State employees and taxpayers. An operational ERP system will improve the State's control environment and processes to produce accurate financial statements in a timely manner.

Comptroller's Office agreed with auditors

The Comptroller's Office agreed with our recommendation and stated that the State still faces several road blocks in the timely completion of the CAFR. The General Assembly enacted P.A. 97-0691, which extended lapse period from August 31 to December 31 for fiscal year 2013 and future fiscal years for medical assistance payments of the Department of Healthcare and Family Services. As a result of the extension, the preparation and completion of critical financial schedules will continue to be delayed. In addition, during fiscal year 2016 and 2017, the State operated without a complete budget. P.A. 100-0021, which provided for a significant portion of the fiscal year 2017 appropriations, was not signed into law until July 6, 2017, further delaying the financial reporting process. More importantly, the CAFR completion continues to be delayed because of financial reporting issues identified during individual State agency financial and compliance audits. The CAFR cannot be finalized until these issues are resolved at the individual State agency reporting level. The Office will continue to work with the Governor's Office, the Auditor General's Office and agency GAAP coordinators to improve the timeliness, quality, and processing of financial reporting for the State.

FINANCIAL REPORTING WEAKNESSES

The State of Illinois did not have adequate controls to assess the risk that information reported by individual agencies of the primary government would not be fairly stated and compliant

12 of 25 agencies with 36 internal control findings over financial reporting

with generally accepted accounting principles (GAAP). The Office of the Auditor General performed audits at 25 agencies of the primary government, including five pension systems and the Illinois State Board of Investment. During these audits, we noted at 12 agencies there were a total of 25 material weaknesses and 11 significant deficiencies related to the internal controls over the financial reporting process.

Specifically, some of the more significant issues noted the following:

- The Department of Human Services and the Department of Healthcare and Family Services lacked controls over the Integrated Eligibility System.
- The Department of Healthcare and Family Services failed to implement adequate fiscal-related monitoring controls over Managed Care Organization contracts.
- The Office of the Treasurer, College Savings Program did not have an adequate process to identify and eliminate intra-fund activity within its financial statements.

Internal control deficiencies extend financial reporting timelines

Material weaknesses and significant deficiencies further extend financial reporting timelines since additional measurements and reporting are required. Completion or substantial completion of these audits is necessary in order for the Auditor General to issue an opinion on the State's basic financial statements.

Material misstatements identified

In addition to the deficiencies noted above, material misstatements were identified by the auditors at four agencies. The adjustments/reclassifications ranged from \$2.2 million to \$3.6 billion. (Finding 2, pages 10-14)

We recommended the State continue its efforts to improve internal control procedures in order to assess the risk of material misstatements to the financial statements and to identify such misstatements during the financial statement preparation process. The internal control procedures should include a formal evaluation of prior problems and implementation of procedures to reduce the risk of these problems reoccurring.

Governor's Office agreed with auditors

The Governor's Office agreed with our recommendation and stated that the Governor's Office will work with the Office of the State Comptroller to continue efforts to improve internal control procedures to reduce the likelihood of material misstatements to the financial statements. Both offices are in the midst of a multi-year implementation of an Enterprise Resource Planning (ERP) system to develop an integrated enterprise-wide application system for financials, which is an aspect of the Governor's Executive Order that created the Illinois Department of Innovation and Technology to transform Illinois' IT system to be more responsive to State

employees and taxpayers. An operational ERP system will improve the State's control environment and processes to assess the risk of material misstatements to the financial statements and to identify such misstatements during the financial statement preparation process.

Comptroller's Office agreed with auditors

The Comptroller's Office agreed with our recommendation and stated that the Office will continue to assist the Governor's Office in their efforts to increase the quality of GAAP packages by providing enhanced training and technical assistance to State agencies.

INSUFFICIENT CONTROLS OVER FINANCES

Insufficient controls over the State's finances

The State of Illinois did not have sufficient controls over its finances. This condition increases the risk that liabilities will not be properly recorded. Further, this condition increases risk and diminishes the oversight and authority of the budgeting and appropriation process.

\$10.876 billion of approved payments on hand at June 30, 2017

We noted during our audit of the State's financial statements that the State had transactions, totaling \$10.876 billion, on hand at June 30, 2017, that had been approved for payment by the State, but remained unpaid at year end due to the State's cash flow difficulties. Of this amount, approximately \$7.435 billion was owed to external parties, the remaining balance was related to intra-governmental transactions and statutorily mandated transfers. Due to the State not being able to pay external vendors in a timely manner, the State paid approximately \$226.381 million in interest payments during Fiscal Year 2017, and the State has paid (on a cash basis) an additional \$579.761 million during Fiscal Year 2018 as of March 15, 2018. (Finding 5, pages 19-20)

\$806.142 million paid in interest payments

We recommended the Governor work with the General Assembly to improve the State's control over its finances in a manner that eliminates significant payment delays and unnecessary interest payments to State vendors.

Governor's Office agreed with auditors

The Governor's Office agreed with our recommendation and stated that the Governor's Office will work with the General Assembly, the Office of the State Comptroller and the Office of the State Treasurer to improve the State's control over finances to eliminate significant payment delays and unnecessary interest payments to State vendors.

OTHER FINDINGS

The remaining findings included two noncompliance issues. We will review the State's progress towards the implementation of our recommendations in our next audit.

This financial audit was conducted by staff of the Office of the Auditor General.

SIGNED ORIGINAL ON FILE

JANE CLARK
Division Director

This report is transmitted in accordance with Section 3-14 of the Illinois State Auditing Act.

SIGNED ORIGINAL ON FILE

FRANK J. MAUTINO
Auditor General

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