

REPORT DIGEST

**OFFICE OF THE TREASURER - STATE OF ILLINOIS
FISCAL OFFICER RESPONSIBILITIES
FINANCIAL AND COMPLIANCE AUDIT
FOR THE YEAR ENDED JUNE 30, 1993**

{Financial information is summarized on the reverse page.}

FINDINGS, CONCLUSIONS, AND RECOMMENDATIONS

NEED TO UPGRADE COMPUTER PROGRAM USED TO ALLOCATE INVESTMENT INCOME

The Treasurer's computer program, which allocates approximately \$3 million of pooled investment income to participating funds each month, is outdated and inflexible resulting in erroneous calculations and increased personnel time to process and interpret allocations.

The computer program used to compute individual fund earnings has not been updated in recent years to reflect the changes in the Treasurer's investment portfolio. At the time the current program was developed, the Treasurer's investment portfolio was comprised almost entirely of time deposits. With the decline in the interest rates in the past few years, the Treasurer, in an effort to increase investment income, has begun investing in U.S. Treasury notes and Federal Farm Credit bonds. Such investments require monthly accrual of income, amortization of premiums and accretion of discounts, which cannot be performed by the current system, resulting in cumbersome manual computations and overrides.

Our audit procedures relating to investment income identified certain manual errors of accrued interest income for the pool.

We recommended that Treasurer personnel purchase or design a replacement for the existing computer program. A system which accurately allocates the pooled investment income and calculates accrued interest income would reduce the number of manual errors and the amount of effort required. (Finding 1, pages 11 & 12)

The Treasurer stated the office accepts the recommendation and noted that a redesign of the existing computer program to allocate investment income within the Treasurer's portfolio has not been completed. Further, the Treasurer's office has been able to implement a short-term solution we previously recommended by adding an adjustment line to the current program. The new computer program is scheduled for full implementation during the fourth quarter of FY 1994.

NEED TO DETERMINE AND RECORD ARBITRAGE REBATE TAX LIABILITY

The Treasurer's office did not record the liability for the arbitrage rebate tax due to the Internal Revenue Service for State of Illinois General Obligation College Savings Bonds Series of October 1988. Additionally, the Treasurer's office has not made a determination as to possible arbitrage liability resulting from bonds issued between 1988 and 1993.

At the time of the October 1988 bond issue, Federal tax law required bond proceeds to be spent within six months. If the proceeds were not spent within this period, the interest earnings on the unexpended bond proceeds must either be limited to the rate paid the bondholders or any excess earnings (considered arbitrage) must be rebated to the federal government.

In October, 1992 the law firm engaged to calculate the arbitrage rebate tax provided the

Treasurer's office with the total amount of arbitrage rebate tax due on the October 1988 College Savings Bonds. The amount due on November 1, 1992, was \$3,595,900. However, no liability was recorded on the Treasurer's records nor has any adjustment been made for interest that continues to accrue at the effective rate of the bonds. Interest accruing on this bond issue between November 1, and June 30, 1993, according to our calculations, approximated \$164,100. Additionally, the Treasurer's office has not determined if additional liability has accrued for other bond issues.

We recommended that Treasurer personnel record the liability related to arbitrage rebate tax currently due and payable on the October 1988 bond issue. Further, Treasurer personnel should determine if other bond issues are subject to arbitrage and calculate and record any estimated liability. (Finding 3, pages 13 & 14)

The Treasurer stated the office accepts the recommendation and has recorded the liability for the 1988 College Savings Bond Issue on the general ledger. Further, the office has initiated contact with arbitrage service providers to determine the extent of potential liability on other outstanding bond issues.

OTHER FINDING

The remaining finding is of lesser significance and is being given appropriate attention by the Office of the State Treasurer. We will review progress towards the implementation of recommendations in our next audit.

Mr. James A. Stapleton, the Treasurer's Chief Fiscal Officer, provided the responses to our recommendations.

OTHER MATTERS

As of June 30, 1993, the Treasurer recorded an additional \$8.9 million provision for the write-down of four investment loan balances in the Illinois Insured Mortgage Pilot Program based on the most recent independent appraisals. The provision is presented in the financial statements as a reduction of investment income earned. The write-down of the investment is not considered forgiveness of the obligations and collection efforts will continue for the entire loan balance. The hotel investment loans are considered to be nonperforming assets at June 30, 1993. (Note D, pages 33 - 37)

SUBSEQUENT EVENTS

The workout agreement entered into by the Cary Space Center, one of the commercial properties in the Illinois Insured Mortgage Pilot Program Trust, required the borrower to cure delinquencies and take steps to sell the collateral by July, 1993. After the borrower failed to comply with this and certain other provisions of the workout agreement, the deed in lieu of foreclosure was delivered and recorded on August 3, 1993. The property is now on the market for sale. At June 30, 1993, the amount due the trustee was \$1,650,000.

Subsequent to June 30, 1993, the State issued \$175,000,000 of general obligation bonds which mature annually from 1994 through 2018 with interest rates ranging from 4.4% to 5.5%. (Note J, page 47)

AUDITORS' OPINION

Our auditors state the June 30, 1993 financial statements present fairly, in all material respects, the assets, liabilities and accountabilities of the Office of the Treasurer.

WILLIAM G. HOLLAND, Auditor General

WGH:BLB:jr

SUMMARY OF AUDIT FINDINGS

Number of This Audit Prior Audit

Findings 33

Repeated Findings 10

Prior Recommendations Implemented
or Not Repeated 23

SPECIAL ASSISTANT AUDITORS

Kerber, Eck & Braeckel were our special assistant auditors for this audit.

**OFFICE OF THE TREASURER - STATE OF ILLINOIS
FISCAL OFFICER RESPONSIBILITIES
FINANCIAL AND COMPLIANCE AUDIT
FOR THE YEAR ENDED JUNE 30, 1993**

<u>ASSETS, LIABILITIES AND ACCOUNTABILITIES</u>	<u>JUNE 30, 1993</u>	<u>JUNE 30, 1992</u>
<u>Assets</u>		
Cash	\$ 98,834,570	\$ 58,324,664
Revenue - Producing Deposits and Investments, At Cost (which approximates market)	3,274,531,762	3,276,199,117
Other Assets	132,086,368	190,270,982
Due from Multi-Purpose Bond Funds	3,760,000	0
Amount of Future General Revenues Obligated for Debt Service	<u>7,047,030,115</u>	<u>6,938,099,215</u>
TOTAL ASSETS	<u>\$10,555,242,815</u>	<u>\$10,462,893,978</u>
<u>Liabilities and Accountabilities</u>		
Liabilities for Balances on Deposit	\$ 3,281,341,176	\$ 3,159,144,093
Arbitrage Rebate Tax Payable	3,760,000	0
General Obligation Indebtedness	7,267,165,415	7,298,583,766
Accountabilities	<u>2,976,224</u>	<u>5,166,119</u>
TOTAL LIABILITIES AND ACCOUNTABILITIES	<u>\$10,555,242,815</u>	<u>\$10,462,893,978</u>
FINANCIAL HIGHLIGHTS	<u>YEAR ENDED JUNE 30, 1993</u>	<u>YEAR ENDED JUNE 30, 1992</u>
Investment Income	\$ 107,160,331	\$ 139,170,395
Average Yield on Time Deposits	3.36%	4.94%
Average Yield on Short-Term Investments	3.38%	4.15%
Write-down of Illinois Insured Mortgage Pilot Program	\$ 8,928,256	\$ 2,000,000
STATE TREASURER		
Honorable Patrick Quinn State House, Room 219 Springfield, Illinois 62706		