

REPORT DIGEST

OFFICE OF THE TREASURER - STATE OF ILLINOIS FISCAL OFFICER RESPONSIBILITIES FINANCIAL AND COMPLIANCE AUDIT FOR THE YEAR ENDED JUNE 30, 1995

SYNOPSIS

The Treasurer's Office did not transfer \$46,154 of protested tax funds from the Protest Fund to the General Revenue Fund in a timely fashion as required by an Appellate Court ruling.

A specialist retained by the auditors to assist in their review of the Treasurer's financial statements valued the Treasurer's mortgage interest in the Springfield Renaissance at \$2.2 million as of June 30, 1994, and \$1.7 million as of June 30, 1995. The Treasurer's mortgage interest in the Collinsville Holiday Inn was valued at \$8.2 million at June 30, 1994, and \$8.9 million at June 30, 1995. Further, the Treasurer held certain additional collateral on each hotel valued cumulatively by the specialist at \$4 million and \$4.6 million, at June 30, 1994 and June 30, 1995, respectively. As of June 30, 1995, the total amount of the unpaid principal and interest on the loans was approximately \$19.9 million for the Springfield hotel and approximately \$20.7 million for the Collinsville hotel.

The specialist's mortgage valuations resulted in some changes in the Treasurer's financial statements. Last year, the value of the hotel mortgages was reduced, or "written down," by approximately \$5.7 million on the Treasurer's June 30, 1994, financial statements. That write down was based upon an independent appraisal obtained by the Treasurer. Because of the more recent valuation, the write down has been reduced from \$5.7 million to \$3.2 million. However, the specialist's mortgage valuations did not result in any changes to the Treasurer's June 30, 1995, financial statements.

PROTEST FUND

The Treasurer's Office did not transfer \$46,154 of protested tax funds from the Protest Fund to the General Revenue Fund as required by an Appellate Court ruling in a timely fashion.

During our test work of the Protest Fund, we noted one instance whereby the Treasurer received a favorable ruling from the Appellate Court for \$46,154 in protested tax funds. The ruling was made on April 27, 1995, and the Treasurer should have transferred the \$46,154 to the General Revenue Fund subsequent to the ruling; however, the transfer was not made until August 28, 1995.

The State Officers and Employees Money Act (30 ILCS 230/2a) requires that all protested tax funds be maintained in the Protest Fund until the protested tax case is resolved. The Treasurer shall either refund the protested taxes to the defendant or transfer the money to the appropriate fund based on the Court's ruling.

We recommended the Treasurer review the cost effectiveness of additional control procedures to ensure all resolved protest tax cases are properly accounted for on a timely basis. (Finding 1, page 10)

The Treasurer stated the office accepts the recommendation. Their response also indicated they believe current controls are adequate, assuming a high level of compliance by agency personnel. The Treasurer will attempt to heighten the sensitivity of agency personnel to their obligation to promptly review reports designed to ensure that all resolved protest tax cases are properly accounted for in a timely manner.

Mr. James Stapleton, Chief of Staff for the Office of the Treasurer provided the response to the finding on April 15, 1996.

ILLINOIS INSURED MORTGAGE PILOT PROGRAM TRUST

For the sole purpose of assisting in the audit of the Treasurer's financial statements, the Office of the Auditor General's Special Assistant Auditors obtained the expertise of a specialist, Coopers & Lybrand, L.L.P., to provide a valuation analysis at June 30, 1994, and June 30, 1995, of the Treasurer's mortgage positions and additional collateral relating to the Collinsville Holiday Inn and the Springfield Renaissance hotels. These hotel investments are part of the Treasurer's Illinois Insured Mortgage Pilot Program.

The specialist's valuation is provided for financial statement auditing purposes only. The work performed by the specialist, however, does not constitute an appraisal or an audit. The valuation relies on certain underlying assumptions that could be affected by unanticipated events and circumstances which may occur during the analysis period. Further, the valuation is based on historical and prospective financial information which was not independently verified or audited

as part of the valuation process. Therefore, the specialist notes that, in the event there is a sale of the mortgages, the proceeds may differ from the specialist's valuation due to the above factors, as well as additional considerations that may be taken into account by any given buyer and the seller.

Valuation Analysis

In valuing the Treasurer's position in the mortgages, the specialist used a traditional Discounted Cash Flow (DCF) analysis. Valuations derived using the DCF methodology depend, in part, upon the discount and capitalization rates used in performing the analysis. In its report, the specialist recognizes a range of possible discount and capitalization rates based upon differing assumptions. Variations in valuations will be obtained depending upon the selection of discount and capitalization rates within the range. However, the specialist asserts that the most likely outcome is at the mid-point of the ranges.

Utilizing the mid-points, the specialist determined that the mortgage value for the Springfield hotel was approximately \$2.2 million as of June 30, 1994, and approximately \$1.7 million as of June 30, 1995. Likewise at mid-point, the mortgage value for the Collinsville hotel was approximately \$8.2 million as of June 30, 1994, and approximately \$8.9 million as of June 30, 1995.

In addition to the mortgages, the Treasurer also holds additional collateral on the hotel loans. The Collinsville loan is secured by letters of credit and personal guarantees, while the Springfield loan is secured by a surety bond. Similar to the underlying mortgages, the value of the additional collateral is affected by such factors as timing, risk and collectability. As with the mortgages, the report contains a range of possible valuations of the additional collateral; however, as with the mortgages, the specialist believes the most likely outcome is at the mid-point of the ranges. At mid-point, the Collinsville letters of credit were valued at approximately \$2.0 million at June 30, 1994, and approximately \$2.3 million at June 30, 1995. Also at mid-point, the Springfield surety bond was valued at approximately \$2.0 million at June 30, 1994, and approximately \$2.3 million at June 30, 1995. No value was assigned to the Collinsville personal guarantees, which have a maximum amount of \$1.5 million, because current information was not readily available.

Summary Of Valuation Conclusions

The following table summarizes the value conclusions. As discussed earlier, the final value conclusions used by the Treasurer for financial statement reporting were the mid-point of the ranges displayed in the tables.

SUMMARY OF VALUATION

Springfield Renaissance Hotel	June 30, 1994			June 30, 1995		
	<u>Low</u>	<u>Mid</u>	<u>High</u>	<u>Low</u>	<u>Mid</u>	<u>High</u>
Mortgage Loan Valuation	\$2,028,000	\$2,170,000	\$2,334,000	\$1,535,000	\$1,670,000	\$1,827,000
Surety Bond Valuation	<u>1,871,000</u>	<u>1,995,000</u>	<u>2,128,000</u>	<u>2,215,000</u>	<u>2,340,000</u>	<u>2,471,000</u>
Total	<u>\$3,899,000</u>	<u>\$4,165,000</u>	<u>\$4,462,000</u>	<u>\$3,750,000</u>	<u>\$4,010,000</u>	<u>\$4,298,000</u>

Collinsville Holiday Inn	June 30, 1994			June 30, 1995		
	<u>Low</u>	<u>Mid</u>	<u>High</u>	<u>Low</u>	<u>Mid</u>	<u>High</u>
Mortgage Loan Valuation	\$7,380,000	\$8,178,000	\$9,113,000	\$7,999,000	\$8,850,000	\$9,842,000
Letters of Credit Valuation	1,999,000	2,044,000	2,090,000	2,255,000	2,295,000	2,335,000
Personal Guarantee (no value assigned due to lack of information)	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total	<u>\$9,379,000</u>	<u>\$10,222,000</u>	<u>\$11,203,000</u>	<u>\$10,254,000</u>	<u>\$11,145,000</u>	<u>\$12,177,000</u>

Springfield & Collinsville Combined	June 30, 1994			June 30, 1995		
	<u>Low</u>	<u>Mid</u>	<u>High</u>	<u>Low</u>	<u>Mid</u>	<u>High</u>
Mortgage Loan Valuation	\$9,408,000	\$10,348,000	\$11,447,000	\$9,534,000	\$10,520,000	\$11,669,000
Surety Bond Valuation	1,871,000	1,995,000	2,128,000	2,215,000	2,340,000	2,471,000
Letters of Credit Valuation	1,999,000	2,044,000	2,090,000	2,255,000	2,295,000	2,335,000
Personal Guarantee (no value assigned due to lack of information)	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total	<u>\$13,278,000</u>	<u>\$14,387,000</u>	<u>\$15,665,000</u>	<u>\$14,004,000</u>	<u>\$15,155,000</u>	<u>\$16,475,000</u>

Further details supporting these conclusions are contained in an "Executive Summary" which is appended to this Report Digest.

The above-reflected mortgage valuations resulted in some changes in the Treasurer's financial statements. Last year, the value of the hotel mortgages was reduced, or "written down," by approximately \$5.7 million on the Treasurer's June 30, 1994, financial statements. That write down was based upon an independent appraisal obtained by the Treasurer. Because of the more recent valuation, the write down has been reduced from \$5.7 million to \$3.2 million. (See pages 24 and 35 of the Audit Report.)

For the period ended June 30, 1995, however, the Treasurer concluded that no further write-down of the hotel mortgage investments was necessary because the valuations at this date were higher than the amounts already recorded on the Treasurer's books at year end. Generally accepted accounting principles do not permit adjusting book values of impaired assets upward except to correct an error in a prior period. In the Treasurer's June 30, 1995, financial statements, the

Springfield and Collinsville hotel mortgages are recorded at approximately \$1.7 million and \$7.3 million, respectively. At that same date, the specialists valued the mortgages at approximately \$1.7 million and \$8.9 million, respectively. (See page 35 of the Audit Report.)

As of June 30, 1995, the total amount of the unpaid principal and interest on the loans was approximately \$19.9 million for the Springfield hotel and approximately \$20.7 million for the Collinsville hotel. (See page 33 of the Audit Report.)

AUDITORS' OPINION

Our auditors state the June 30, 1995 financial statements present fairly, in all material respects, the assets, liabilities and accountabilities and the statement of investment income of the Office of the Treasurer.

 WILLIAM G. HOLLAND, Auditor General
 WGH:BLB:pp

SUMMARY OF AUDIT FINDINGS

Number of This Audit Prior Audit
 Findings 12
 Repeated Audit Findings 01
 Prior Recommendations Implemented
 or Not Repeated 22

SPECIAL ASSISTANT AUDITORS

Geo. S. Olive & Co. LLC were our Special Assistant Auditors for this audit.

SPECIALIST USED BY SPECIAL ASSISTANT AUDITORS

Coopers & Lybrand L.L.P. was the specialist used by our Special Assistant Auditors.

**OFFICE OF THE TREASURER - STATE OF ILLINOIS
 FISCAL OFFICER RESPONSIBILITIES
 FINANCIAL AND COMPLIANCE AUDIT
 FOR THE YEAR ENDED JUNE 30, 1995**

<u>ASSETS, LIABILITIES AND ACCOUNTABILITIES</u>	<u>JUNE 30, 1995</u>	<u>JUNE 30, 1994</u>
<u>Assets</u>		
Cash	\$ 6,599,466	\$ 32,643,415
Revenue - Producing Deposits and Investments, At Cost (which approximates market)	4,178,080,565	3,769,402,939

Other Assets	177,486,503	257,052,821
Due from Multi-Purpose Bond Funds	0	2,576,200
Amount of Future General Revenues Obligated for Debt Service	<u>7,831,241,956</u>	<u>7,303,788,716</u>
TOTAL ASSETS	<u>\$12,193,408,490</u>	<u>\$11,365,464,091</u>
<u>Liabilities and Accountabilities</u>		
Liabilities for Balances on Deposit	\$ 4,054,807,905	\$ 3,798,331,314
Arbitrage Rebate Tax Payable	0	2,576,200
General Obligation Indebtedness	8,124,302,780	7,550,374,173
Accountabilities	<u>14,297,805</u>	<u>14,182,404</u>
TOTAL LIABILITIES AND ACCOUNTABILITIES	<u>\$12,193,408,490</u>	<u>\$11,365,464,091</u>
FINANCIAL HIGHLIGHTS	YEAR ENDED JUNE 30, 1995	YEAR ENDED JUNE 30, 1994
Investment Income	\$ 222,519,195	\$ 129,319,174
Average Yield on Time Deposits	5.14%	3.48%
Average Yield on Short-Term Investments	4.89%	3.04%
Write-down of Illinois Insured Mortgage Pilot Program	\$ 0	\$ 3,334,305
STATE TREASURER		
During Audit Period:Honorable Patrick Quinn (July 1, 1994 to January 8, 1995) and Honorable Judy Baar Topinka (January 9, 1995 to June 30, 1995) Currently: Honorable Judy Baar Topinka		