A Report
to the
Montana
Legislature

Financial-Compliance Audit

Department of Revenue

For the Two Fiscal Years Ended June 30, 2014

October 2014

Legislative Audit
Division

14-14

Legislative Audit Committee

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Financial-compliance audits are conducted by the Legislative Audit Division to determine whether an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States Government Accountability Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) licenses.

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October 2014

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit report on the Department of Revenue (department) for the two fiscal years ended June 30, 2014.

During the course of the audit we analyzed the financial schedules contained in this report, reviewed the financial records, and tested compliance with selected state laws and regulations. The work resulted in four recommendations related to compliance with state laws regarding coal gross proceeds and contractor's gross receipts taxes, access to the department's tax system, and charging fees commensurate with costs in the department's internal service fund.

This report also includes the department's financial schedules. The financial schedule presentation is intended to provide the legislative body with information necessary for decision-making purposes; it is not intended to conform to the financial reporting requirements established in generally accepted accounting principles (GAAP). The financial schedule presentation has not changed, however audit reporting standards have changed. Auditing standards require us to clearly communicate that the financial schedule presentation is not intended to, and does not, conform to GAAP reporting requirements. The Independent Auditor's Report on page A-1 contains language to this effect in the section titled "Adverse Opinions on U.S. Generally Accepted Accounting Principles." This section does not imply the amounts presented on the department's financial schedules are not fairly stated. Page A-1 also communicates the extent to which the user can rely on the information contained in the financial schedules in the section titled "Unmodified Opinions on Regulatory Basis of Accounting."

The department's written response to the audit recommendations is included in the audit report on page B-1. We thank the director and his staff for their cooperation and assistance throughout the audit.

Respectfully submitted,

/s/ Tori Hunthausen

Tori Hunthausen, CPA
Legislative Auditor

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Appointed and Administrative Officials

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Ed Caplis, Director, Tax Policy and Research

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Montana Legislative Audit Division

Financial-Compliance Audit
Department of Revenue
For the Two Fiscal Years Ended June 30, 2014

October 2014 | 14-14 | Report Summary

The Montana Department of Revenue administers state tax laws, enforcing regulations for more than 30 state taxes and fees. During the audit period, the department collected approximately $1.9 billion in taxes in each fiscal year. Of this, over $216 million was distributed to local governments in fiscal year 2013, and $228 million in fiscal year 2014.

Context

In addition to tax administration, the Department of Revenue (department) oversees liquor distribution and licensing operations in the state and administers the one-stop licensing program and bad debt collections on behalf of state agencies. The department also manages unclaimed property, returning property to its rightful owners.

Results

The department administers the coal gross proceeds and contractor's gross receipts taxes. Both of these tax types are prescribed in law. Our audit determined interest and penalties are not assessed as required by state law on contractor's gross receipts. We also noted the form prescribed to report coal gross proceeds is not detailed enough to demonstrate the state received its required allocation.

The taxes collected by the department are primarily administered through the use of a computer system referred to as GenTax. Our audit procedures determined that access to GenTax was not restricted as required by department policy.

Finally, the internal service fund used to administer the bad debt collection program charged fees that generated revenue collections greater than the program's expenditures. This resulted in excess fund equity balance in both fiscal years 2013 and 2014.

Recommendation Concurrence	
Concur	4
Partially Concur	0
Do Not Concur	0
Source: Agency audit response included in final report.	

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Chapter I – Introduction

Introduction

We performed a financial-compliance audit of the Department of Revenue (department) for the two fiscal years ended June 30, 2014. The objectives of our audit were to:

1. Determine whether the department's financial schedules fairly present the financial position and results of its operations for each of the fiscal years ended June 30, 2014, and 2013.
2. Obtain an understanding of the department's control systems to the extent necessary to support our audit of the department's financial schedules and, if appropriate, make recommendations for improvements in management and internal controls of the department.
3. Determine whether the department complied with selected state laws and regulations during the audit period.
4. Determine the implementation status of prior audit recommendations.

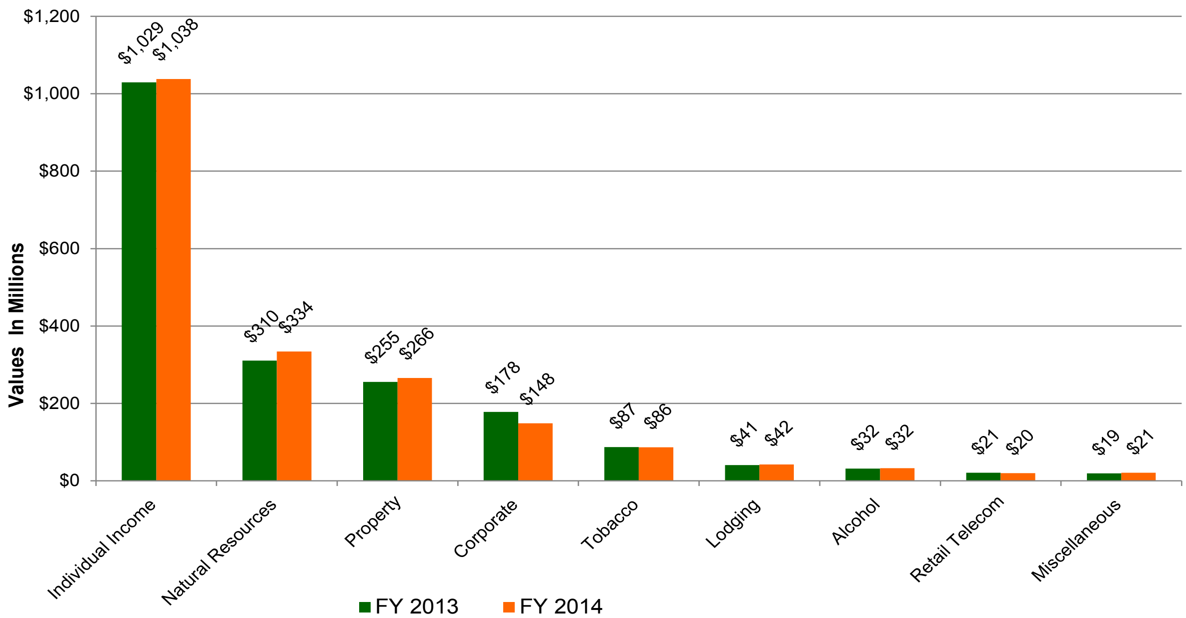
To address objectives #1 and #2, we focused our audit effort primarily on tax revenues, distributions to local governments, and liquor and coal tax activities. This included understanding the department's internal control policies and procedures, performing analytical procedures, and reviewing accounting transactions. We addressed objective #3 by reviewing and testing compliance with over 150 state laws.

As required by §17-8-101(6), MCA, we analyzed the fees and charges for services and the fund equity of the department's internal service fund, which is used to provide bad debt collection services to state agencies. Our review noted fees are not commensurate with costs during the audit period. See Recommendation #4 starting on page 8 for our complete analysis.

Department Organization and Functions

The department is responsible for the administration of state tax laws and enforcing regulations for numerous state taxes and fees. Revenues collected by the department include, but are not limited to, individual income, corporate income, natural resource, lodging facility use, accommodation, property, alcohol and tobacco taxes. Department tax revenues are recorded primarily in the General, State Special Revenue, and Permanent Funds. Figure 1 on page 2 shows the total taxes collected by the department in fiscal years 2013 and 2014 by type. Additionally, the department regulates the sale and distribution of alcoholic beverages in the state; associated revenue collections are recorded in the Enterprise Fund.

Figure 1
Taxes by Tax Type
Fiscal Years 2013 and 2014
(in millions)



Source: Compiled by the Legislative Audit Division from SABHRS records.

The department also distributes various tax revenues based on requirements in law. The two largest distributions relate to the local government's entitlement share revenue and oil and natural gas production taxes. The entitlement share is recorded in the Director's Office Program. The oil and natural gas production taxes distributions to counties and school districts are recorded in the Citizen Services & Resource Management Division Program.

For fiscal year 2013-14, the department employed a total of 684.78 full-time equivalent (FTE) employees. As a result of re-organization in November 2013, the department currently consists of the Director's Office administering four divisions instead of five divisions. The former Information Technology and Processing Division was eliminated and divided into an Information Technology Office under the direction of the Director's Office and an Information Management Bureau within the Citizens Services and Resource Management Division. Prior to re-organization, the Information and Technology Division was responsible for providing application development and support services, network services in the areas of data, desktop, information security, and help desk support. They were also responsible for processing tax returns and payments for the department and for state agency partners, and for managing department records. These responsibilities are now divided between the Technology Office and Information Management Bureau mentioned above.

<u>Director's Office</u> (85.48 FTE) provides overall department direction and management. It also supports the agency's director and is composed of the following ten work units:

- Legal Services
- Tax Policy and Research
- Human Resources
- Executive Office
- Office of Taxpayer Assistance
- Information Technology Office
- Enterprise Planning & Analysis Office
- Security Office
- Public Information Office
- Budget and Finance Office

<u>Business and Income Taxes Division</u> (139.45 FTE) administers and collects 38 Montana taxes and fees and some local government taxes, oversees tax audits and verifies compliance with Montana tax law for all state taxes, oversees state revenue collection activity, and completes appraisals and assessments of industrial and centrally assessed property.

<u>Citizen Services and Resource Management Division</u> (114.25 FTE) administers the accounting, purchasing, safety, security, and statewide facility functions. The division also administers the call center, forms design, eStop business licensing coordination, receipt and distribution of unclaimed property, collection of delinquent accounts and data and remittance processing operations. The division includes the Financial and Asset Management Bureau, the Citizen Services Bureau, the Collections Bureau and the Information Management Bureau.

<u>Liquor Control Division</u> (32.75 FTE) administers the state's Alcoholic Beverage Code, which governs the control, sale, and distribution of alcoholic beverages. The division includes licensing of businesses, manufacturers, wholesalers, warehouses, importers, and liquor representatives.

<u>Property Assessment Division</u> (312.35 FTE) is responsible for the valuation and assessment of residential, commercial, agricultural, forestland, and business equipment property throughout the state for property tax purposes. The division has a central office located in Helena and six regional offices. There is a local office in each county seat.

Advisory Councils, Boards, and Memberships

The department is a member of the Multistate Tax Commission, the Federation of Tax Administrators, the Western States Association of Tax Administrators, the National Alcohol and Beverage Control Association, and the National Association of Unclaimed Property Administrators. The department's advisory councils include:

Agricultural Land Valuation Advisory Council is created by §15-7-201(7), MCA, to advise the department concerning the valuation of agricultural property. This council must include a staff member from the Montana State University – Bozeman, College of Agriculture. This advisory council is not a policy making body and has no rule making authority.

The **Board of Review** established in §30-16-302, MCA, provides policy direction to the department in establishing and operating the one-stop business licensing program. The board is attached to the department for administrative purposes only and has separate rule making authority under §30-16-104, MCA.

Prior Audit Recommendations

The previous financial-compliance audit report of the department for the two fiscal years ended June 30, 2012, contained four recommendations. The department implemented three and partially implemented one. The partially implemented recommendation relates to the adoption of rules for three separate state laws. The department adopted rules for §15-30-2327(4), MCA, and §15-68-401(3), MCA, as required by statute.

The department has not adopted rules related to connoisseur's licenses as required by §16-4-901(5), MCA. During the 2013 Legislative Session, this law was amended, but the requirement to adopt rules was not removed, as the department believes the state law is sufficient and additional rules are not necessary for connoisseur's licenses.State law requires the completion of a department-provided application and sets the fee. While we make no further recommendation at this time, the law still requires the adoption of rules.

Chapter II – Findings and Recommendations

GenTax Access

The department granted access to the department's tax software contrary to department policy.

The Integrated Revenue Information System (IRIS), now referred to as GenTax, is a computer system implemented by the Department of Revenue (department) to maintain taxpayer records and process tax revenue for 38 different tax types.

During the audit, we reviewed access to the computer system by looking at all employees who were granted access during fiscal year 2014. Department policy requires employee access be granted via a computer access request form. Although the access request form requires security approval by both the Information Security Manager and Technology Security Manager, we noted access request forms for 9 of the 47 employees with hire dates in fiscal year 2014 were missing one or both of the security approvals.

Additionally, department policy states if the access request is for a temporary or contracted position, a termination date must be provided. We noted ten instances where a termination date was not provided for temporary employees, and one instance where a termination date was provided for a temporary employee, but access was not removed on or before the date provided.

Department staff stated these oversights were caused by the retirement of the department employees responsible for approving the forms. The department has implemented a ticketing system to assist in working access requests. In regards to the temporary employee access, department staff stated it is not always feasible to document a termination date since they do not always know up front when the temporary employment will end. Department staff intend to update the department policy to require a documented termination date only if known. Additionally, temporary staff are not granted remote access. According to department personnel, even if GenTax access was not terminated, physical access to the department has terminated and without remote access, accessing GenTax is not possible. If department staff are aware of the date to terminate physical access, this same date should be used to terminate GenTax access.

Unnecessary or unauthorized access to GenTax could lead to the potential misuse of data. Because GenTax contains federal tax information, federal guidelines apply as well. Federal guidelines state the department must require approval for requests to create accounts and remove information system accounts in accordance with department policy. By granting access without both required signatures and not documenting a termination date as required by department policy, the department risks noncompliance with federal guidelines as well.

Recommendation #1

We recommend the department comply with department policy by:

A. *Obtaining required approvals prior to granting access to GenTax.*

B. *Terminating temporary employee access when employment terminates.*

Coal Gross Proceeds Tax

Department procedures are not adequate to ensure the approximate $9 million in assessed coal gross proceeds tax are received.

State law requires the department assess a Coal Gross Proceeds tax at a flat rate of 5 percent of the value of coal produced. Annually, the department provides to each county in which a coal mine operates, the gross proceeds of the coal produced and the resulting assessed tax for each mine. The counties then bill the coal companies and collect the tax when due.

Once the counties collect the tax, they are required to remit the state's share per §15-23-703(3), MCA. The counties do this through a county collection report in a format provided by the department. This format does not include specific line items for reporting nonlevy taxes, such as the Coal Gross Proceeds Tax. Department personnel stated the county collection report previously contained a separate line, but counties did not use it so the line was removed when the collections went electronic.

Since the Coal Gross Proceeds Tax is co-mingled with the mill levy revenue on the county collection report and subsequently on the state's accounting records, the department has no way to clearly identify that the tax was remitted to the state for the correct amount. The amount of the state's share of Coal Gross Proceeds tax was approximately $9.1 million in fiscal year 2013 and $8.8 million in fiscal year 2014.

Recommendation #2

We recommend the department implement procedures to ensure nonlevy revenue, such as coal gross proceeds, is complete and accurate.

Contractor's Gross Receipts Tax

The department does not assess the required penalties and interest associated with delinquent Contractor's Gross Receipts Tax.

State law requires a Contractor's Gross Receipts (CGR) Tax of 1 percent of payments made to a prime contractor be withheld by the contracting entity and remitted to the state for any publicly funded project greater than $5,000. Prime contractors are also required to withhold the 1 percent CGR Tax from subsequent payments made to subcontractors and report these withholdings to the state. In most cases, the 1 percent CGR tax has already been withheld from the prime contractor so the reporting is required to reallocate the payment from the prime contractor's account in GenTax to the subcontractor's account. The CGR tax becomes delinquent if not paid within 30 days after a payment to a prime contractor is made. Likewise, if a prime contractor fails to file the allocation form for payments made to subcontractors within the required 30 days, it is also considered delinquent. State law requires assessing a 10 percent penalty and 12 percent interest for delinquent taxes. While state law allows the department to waive the penalty, there is no allowance for interest.

When the department identifies a person has failed to file the required statement, state law requires the department to send a letter and tax assessment stating the amount of delinquent tax, penalty and interest due, and advise that if payment is not made, a warrant for distraint may be filed by the department.

Our audit found the department is not assessing penalties and interest for untimely filings identified.

Department staff indicated several reasons for the noncompliance. The CGR is unlike any other tax or fee administered by the department, as there is no uniform period due date for payments to be remitted. The CGR receipts reside on a contractor's account within GenTax as a credit and remain as a credit on the account until the contractor either uses it to offset income taxes or requests a refund of personal property taxes. GenTax is not programmed to calculate penalties and interest on credits.

Department personnel further stated, in order to properly assess the penalty and interest for CGR, the department would have to review every payment, for every contractor, for every public project. The review would consist of annually requesting and analyzing the dates on 12,000 to 14,000 copies of checks and automatic funds transfers between public agencies, primary contractors and secondary contractors. The assessment of penalty and interest could only occur after the completion of an audit making it the only tax or fee that the department would audit strictly to apply penalty and interest. The department deems this to be cost prohibitive.

Although the amount of CGR penalties and interest the department fails to assess is not easily estimated, department staff have indicated contractors not filing the required allocation forms is a significant problem. Errors in the proper allocation of the CGR tax are usually found when a subcontractor files for a refund, but does not have an available credit balance in their GenTax account indicating the CGR tax remittances have not been allocated to the correct contractors. Department staff are then required to follow-up with the contracting entity, prime contractor, and any subcontractors in order to verify the proper allocation of the CGR tax remittance. The department should assess interest and penalties on these cases when identified which would hold the contractor's accountable to file the required allocation forms on time.

Recommendation #3

We recommend the department comply with state law by assessing Contractor's Gross Receipts Tax penalties and interest.

Internal Service Fund

The department charged fees in excess of its expenses for bad debt collections.

The department administers an internal service fund to provide bad debt collection services to state agencies. Bad debt collections primarily occur during the months of January through June when the department is able to offset the debts against requested tax refunds.

State policy allows for a 60-day working capital and §17-8-101(6), MCA, requires fees charged in internal service funds to be commensurate with the costs to operate the internal service fund. Due to the timing of the collections, primarily in January through April, our review noted at June 30, there is a large fund equity balance. At June 30, the fund typically has a six-month working capital since the fund equity is spent down from July through December when collections lag.

However, at June 30, 2014, the fund equity balance exceeded the total year's expenditures by $11,178. Table 1 illustrates the activity in the internal service fund for both years of the audit period.

Table 1

Fiscal Years 2013 and 2014 Internal Service Fund Activity

	FY13	FY14
Total Revenues	$213,202	$201,092
Total Expenditures	$178,983	$175,975
	June 30, 2013	June 30, 2014
Fund Equity	$162,045	$187,153

Source: Compiled by the Legislative Audit Division from Statewide Accounting Budgeting and Human Resource System.

Table 1 also shows revenues exceeded expenditures each year by an average of $30,000. The analysis indicates that fees were not commensurate with costs as required by state law and the ending fund equity balance is also not reasonable.

According to department personnel, the growth in fund equity was the result of employee turnover during the audit period and an automation of processes in December of 2013. The department postponed analyzing the fund until after the following fiscal year-end when the automation had been in place six months and they would have enough data to analyze. Based on their analysis, they plan to reduce the rate charged from 5 percent to 3.5 percent starting in September 2014. They anticipate this will reduce the fund equity balance to a reasonable level by June 30, 2015.

Recommendation #4

We recommend the department comply with state law and charge fees that are commensurate with costs.

Independent Auditor’s Report and Department Financial Schedules

LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor
Deborah F. Butler, Legal Counsel

Deputy Legislative Auditors:
Cindy Jorgenson
Angus Maciver

Independent Auditor's Report

The Legislative Audit Committee
of the Montana State Legislature:

Introduction

We have audited the accompanying Schedules of Changes in Fund Equity & Property Held in Trust, Schedules of Total Revenues & Transfers-In, and Schedules of Total Expenditures & Transfers-Out of the Department of Revenue for each of the fiscal years ended June 30, 2014, and 2013, and the related notes to the financial schedules.

Management's Responsibility for the Financial Schedules

Management is responsible for the preparation and fair presentation of these financial schedules in accordance with the regulatory format prescribed by the Legislative Audit Committee, based on the transactions posted to the state's accounting system without adjustment; this responsibility includes recording transactions in accordance with state accounting policy; and designing, implementing, and maintaining internal controls relevant to the preparation and fair presentation of the financial schedules that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial schedules based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial schedules. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial schedules, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the department's preparation and fair presentation of the financial schedules in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the department's internal control, and accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as the overall presentation of the financial schedules.

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We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Basis for Adverse Opinions on U.S. Generally Accepted Accounting Principles

As described in Note 1, the financial schedules are prepared from the transactions posted to the state's primary accounting system without adjustment, in the regulatory format prescribed by the Legislative Audit Committee. This is a basis of accounting other than accounting principles generally accepted in the United States of America. The financial schedules are not intended to, and do not, report assets, liabilities, and cash flows.

The effects on the financial schedules of the variances between the regulatory basis of accounting described in Note 1 and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

Adverse Opinions on U.S. Generally Accepted Accounting Principles

In our opinion, because of the significance of the matter discussed in the "Basis for Adverse Opinions on U.S. Generally Accepted Accounting Principles" paragraph, the financial schedules referred to above do not present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of the department as of June 30, 2014, and June 30, 2013, or changes in financial position or cash flows for the years then ended.

Unmodified Opinions on Regulatory Basis of Accounting

In our opinion, the Schedules of Changes in Fund Equity & Property Held in Trust, Schedules of Total Revenues & Transfers-In, and Schedules of Total Expenditures & Transfers-Out, present fairly, in all material respects, the results of operations and changes in fund equity and property held in trust of the Department of Revenue for each of the fiscal years ended June 30, 2014, and 2013, in conformity with the basis of accounting described in Note 1.

Respectfully submitted,

/s/ Cindy Jorgenson

Cindy Jorgenson, CPA
Deputy Legislative Auditor
Helena, MT

September 3, 2014

DEPARTMENT OF REVENUE
SCHEDULE OF CHANGES IN FUND EQUITY & PROPERTY HELD IN TRUST
FOR THE FISCAL YEAR ENDED JUNE 30, 2014

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Debt Service Fund	Capital Projects Fund	Enterprise Fund	Internal Service Fund	Agency Fund	Private Purpose Trust Fund	Permanent Fund
FUND EQUITY: July 1, 2013	$ 5,241,461	$ 35,612,677	$ 33,721	$ 843,999	$ 1,532,696	$ 4,758,037	$ 162,045	$ 0	$ 3,483,422	$ 1,081,946,519
PROPERTY HELD IN TRUST: July 1, 2013								$ 115,123		
ADDITIONS										
Budgeted Revenues & Transfers-In	1,777,426,551	320,502,260	262,610		8,734,806	110,810,369	199,821			100,174,392
Nonbudgeted Revenues & Transfers-In	888,612	2,260,548		2,005,196		(327,208)			4,671,433	16,831,292
Prior Year Revenues & Transfers-In Adjustments	(2,096,649)	(279,311)	(33,971)	(93,577)	155,004	9,856	1,271			254,883
Direct Entries to Fund Equity	(1,613,106,472)	(209,918,250)		(2,017,243)	(8,615,027)	(1,192,535)				(1,079,041)
Additions to Property Held in Trust								5,904,833		
Total Additions	163,112,042	112,565,248	228,640	(105,624)	274,783	109,300,481	201,092	5,904,833	4,671,433	116,181,526
REDUCTIONS										
Budgeted Expenditures & Transfers-Out	169,743,110	111,584,615	262,360			108,944,717	164,403			
Nonbudgeted Expenditures & Transfers-Out	(48,238)	33,159				698,816	11,581		3,464,753	74,514,849
Prior Year Expenditures & Transfers-Out Adjustments	8,068	320,089				(52,194)			(1,372)	
Reductions in Property Held in Trust								5,425,217		
Total Reductions	169,702,940	111,937,863	262,360	0	0	109,591,339	175,985	5,425,217	3,463,381	74,514,849
FUND EQUITY: June 30, 2014	$ (1,349,437)	$ 36,240,062	$ 0	$ 738,375	$ 1,807,479	$ 4,467,179	$ 187,153	$ 0	$ 4,691,474	$ 1,123,613,195
PROPERTY HELD IN TRUST: June 30, 2014								$ 594,739		

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
Additional information is provided in the notes to the financial schedules beginning on page A-9.

DEPARTMENT OF REVENUE
SCHEDULE OF CHANGES IN FUND EQUITY & PROPERTY HELD IN TRUST
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Debt Service Fund	Capital Projects Fund	Enterprise Fund	Internal Service Fund	Agency Fund	Private Purpose Trust Fund	Permanent Fund
FUND EQUITY: July 1, 2012	$ (5,760,879)	$ 34,779,949	$ (728)	$ 818,469	$ 1,185,653	$ 4,443,515	$ 127,837	$ 0	$ 3,179,687	$ 1,075,485,281
PROPERTY HELD IN TRUST: July 1, 2012								$ 278,901		
ADDITIONS										
Budgeted Revenues & Transfers-In	1,775,766,718	306,106,159	349,143		8,625,515	106,554,148	215,076			103,167,707
Nonbudgeted Revenues & Transfers-In	1,586,102	668,905		2,305,881		(241,418)			4,036,181	(21,086,665)
Prior Year Revenues & Transfers-In Adjustments	2,809,114	1,643,041		6,926	111,951	9,636	(1,873)			(22,986)
Direct Entries to Fund Equity	(1,609,005,462)	(201,831,504)		(2,287,277)	(7,883,102)	(1,338,368)				(1,045,484)
Additions to Property Held in Trust								5,239,319		
Total Additions	171,156,472	106,586,601	349,143	25,530	854,365	104,983,999	213,203	5,239,319	4,036,181	81,012,572
REDUCTIONS										
Budgeted Expenditures & Transfers-Out	160,193,695	104,704,084	314,698		507,322	104,772,952	169,228			
Nonbudgeted Expenditures & Transfers-Out	(37,444)	16,091	(5)			(36,111)	9,766		3,739,403	74,551,334
Prior Year Expenditures & Transfers-Out Adjustments	(2,120)	1,033,697				(67,364)			(6,958)	
Reductions in Property Held in Trust								5,403,097		
Total Reductions	160,154,132	105,753,872	314,693	0	507,322	104,669,477	178,994	5,403,097	3,732,446	74,551,334
FUND EQUITY: June 30, 2013	$ 5,241,461	$ 35,612,677	$ 33,721	$ 843,999	$ 1,532,696	$ 4,758,037	$ 162,045	$ 0	$ 3,483,422	$ 1,081,946,519
PROPERTY HELD IN TRUST: June 30, 2013								$ 115,123		

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
Additional information is provided in the notes to the financial schedules beginning on page A-9.

DEPARTMENT OF REVENUE
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2014

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Debt Service Fund	Capital Projects Fund	Enterprise Fund	Internal Service Fund	Private Purpose Trust Fund	Permanent Fund	Total
TOTAL REVENUES & TRANSFERS-IN BY CLASS										
Licenses and Permits	$ 5,075,417	$ 32,322,947				$ 1,900,596				$ 39,298,960
Taxes	1,685,467,209	236,249,634	$ 45	$ 1,911,619	$ 8,889,810	25,128,671			$ 30,604,331	1,988,251,318
Charges for Services	3,637	14,690,718				2,335	$ 201,092			14,897,783
Investment Earnings	(2,648)							$ 5,356	58,001,189	58,003,896
Fines and Forfeits						100,999				100,999
Sale of Documents, Merchandise and Property						83,330,655				83,330,655
Grants, Contracts, and Donations	7,756,492	597,633						4,666,078		13,020,203
Transfers-in	52,207,422	29,888,698							28,655,047	110,751,167
Inception of Lease/Installment Contract	1,739									1,739
Federal Indirect Cost Recoveries	26,736									26,736
Miscellaneous	(415,041)	34,683				29,760				(350,598)
Federal	26,097,552	8,699,184	228,594							35,025,331
Total Revenues & Transfers-In	1,776,218,514	322,483,498	228,640	1,911,619	8,889,810	110,493,016	201,092	4,671,433	117,260,566	2,342,358,189
Less: Nonbudgeted Revenues & Transfers-In	888,612	2,260,548		2,005,196		(327,208)		4,671,433	16,831,292	26,329,874
Prior Year Revenues & Transfers-In Adjustments	(2,096,649)	(279,311)	(33,971)	(93,577)	155,004	9,856	1,271		254,883	(2,082,495)
Actual Budgeted Revenues & Transfers-In	1,777,426,551	320,502,260	262,610	0	8,734,806	110,810,369	199,821	0	100,174,392	2,318,110,810
Estimated Revenues & Transfers-In	1,768,560,241	344,664,778	252,612		8,757,000	109,614,700	184,640		103,255,000	2,335,288,971
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ 8,866,310	$ (24,162,518)	$ 9,998	$ 0	$ (22,194)	$ 1,195,669	$ 15,181	$ 0	$ (3,080,608)	$ (17,178,161)
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS										
Licenses and Permits	$ 220,436	$ 655,144				$ (717,304)				$ 158,276
Taxes	21,132,736	(18,962,010)			$ (22,194)	2,208,006			$ (216,061)	4,140,477
Charges for Services	(271,384)	(728,119)	$ (1)			(465)	$ 15,181			(984,787)
Investment Earnings	(2,863)	(2,690,000)							(1,419,594)	(4,112,457)
Fines and Forfeits						699				699
Capital Contributions	(77,000)									(77,000)
Sale of Documents, Merchandise and Property						(295,268)				(295,268)
Grants, Contracts, and Donations	3,991,092	(5,716)								3,985,376
Transfers-in	(4,009,420)	(1,361,767)							(1,444,953)	(6,816,140)
Federal Indirect Cost Recoveries	(18,330)									(18,330)
Miscellaneous	(8,889,812)	(1)								(8,889,813)
Federal	(3,209,145)	(1,070,049)	9,999							(4,269,195)
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ 8,866,310	$ (24,162,518)	$ 9,998	$ 0	$ (22,194)	$ 1,195,669	$ 15,181	$ 0	$ (3,080,608)	$ (17,178,161)

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Additional information is provided in the notes to the financial schedules beginning on page A-9.

DEPARTMENT OF REVENUE
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Debt Service Fund	Capital Projects Fund	Enterprise Fund	Internal Service Fund	Private Purpose Trust Fund	Permanent Fund	Total
TOTAL REVENUES & TRANSFERS-IN BY CLASS										
Licenses and Permits	$ 4,922,808	$ 31,410,243				$ 2,095,641				$ 38,428,691
Taxes	1,683,991,760	223,602,880		$ 2,312,807	$ 8,737,467	24,172,472			$ 29,846,001	1,972,663,387
Charges for Services	5,293	14,538,635				2,879	$ 213,203			14,760,010
Investment Earnings	(15,051)							$ 8,008	22,416,308	22,409,266
Fines and Forfeits						100,396				100,396
Capital Contributions	(77,000)									(77,000)
Sale of Documents, Merchandise and Property						79,929,371				79,929,371
Grants, Contracts, and Donations	4,348,768	593,420						4,028,172		8,970,360
Transfers-in	53,500,279	27,253,506							29,795,746	110,549,531
Inception of Lease/Installment Contract	16,943									16,943
Federal Indirect Cost Recoveries	34,573									34,573
Miscellaneous	447,596	24,100				21,608				493,304
Federal	32,985,965	10,995,322	$ 349,143							44,330,429
Total Revenues & Transfers-In	1,780,161,933	308,418,105	349,143	2,312,807	8,737,467	106,322,367	213,203	4,036,181	82,058,055	2,292,609,261
Less: Nonbudgeted Revenues & Transfers-In	1,586,102	668,905		2,305,881		(241,418)		4,036,181	(21,086,665)	(12,731,015)
Prior Year Revenues & Transfers-In Adjustments	2,809,114	1,643,041		6,926	111,951	9,636	(1,873)		(22,986)	4,555,810
Actual Budgeted Revenues & Transfers-In	1,775,766,718	306,106,159	349,143	0	8,625,515	106,554,148	215,076	0	103,167,707	2,300,784,465
Estimated Revenues & Transfers-In	1,544,106,828	316,730,766	271,219		8,140,000	112,070,405	150,000		100,578,775	2,082,047,993
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ 231,659,890	$ (10,624,607)	$ 77,924	$ 0	$ 485,515	$ (5,516,257)	$ 65,076	$ 0	$ 2,588,932	$ 218,736,472
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS										
Licenses and Permits	$ 159,020	$ (2,117,005)				$ (212,184)				$ (2,170,169)
Taxes	237,889,064	(4,358,601)			$ 485,515	195,836			$ 1,738,036	235,949,850
Charges for Services	(269,800)	(1,775,627)	$ (1)			(1,002)	$ 65,076			(1,981,354)
Investment Earnings	(15,400)	(1)							764,272	748,871
Fines and Forfeits						(81,004)				(81,004)
Sale of Documents, Merchandise and Property						(5,417,903)				(5,417,903)
Grants, Contracts, and Donations	583,368	(16,521)								566,846
Transfers-in	(5,973,310)	(2,642,943)							86,623	(8,529,631)
Federal Indirect Cost Recoveries	(18,330)									(18,330)
Miscellaneous	(2,454,000)	(300,000)								(2,754,000)
Federal	1,759,278	586,093	77,925							2,423,296
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ 231,659,890	$ (10,624,607)	$ 77,924	$ 0	$ 485,515	$ (5,516,257)	$ 65,076	$ 0	$ 2,588,932	$ 218,736,472

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
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DEPARTMENT OF REVENUE
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
FOR THE FISCAL YEAR ENDED JUNE 30, 2014

	Business & Income Taxes Division	Citizen Services & Resource Management Division	Director's Office	Information Management & Technology Division	Liquor Control Division	Property Assessment Division	Total
PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT							
Personal Services							
Salaries	$ 6,361,006	$ 3,849,839	$ 5,077,531		$ 1,386,188	$ 11,776,281	$ 28,450,844
Employee Benefits	2,296,080	1,512,444	1,578,069		525,137	4,691,576	10,603,308
Personal Services-Other		633			288		921
Total	8,657,086	5,362,916	6,655,600		1,911,613	16,467,857	39,055,073
Operating Expenses							
Other Services	495,134	829,062	2,270,366	$ (49,276)	102,941	856,769	4,504,996
Supplies & Materials	140,050	155,194	654,202		122,061	465,650	1,537,157
Communications	198,948	1,022,297	182,453	98	50,380	522,956	1,977,131
Travel	216,016	26,860	102,865		24,967	192,233	562,940
Rent	218,573	745,840	205,195		913	1,660,427	2,830,949
Utilities		548			55,479		56,026
Repair & Maintenance	11,386	47,653	4,102,053		67,229	78,795	4,307,117
Other Expenses	230,357	131,166	215,854		294,617	34,294	906,287
Goods Purchased For Resale					70,633,009		70,633,009
Total	1,510,465	2,958,619	7,732,989	(49,179)	71,351,595	3,811,124	87,315,613
Equipment & Intangible Assets							
Equipment			277,639		122,445		400,084
Total			277,639		122,445		400,084
Capital Outlay							
Other Improvements			175,000				175,000
Total			175,000				175,000
Local Assistance							
From State Sources		110,415,715	118,433,471				228,849,186
Total		110,415,715	118,433,471				228,849,186
From Other Sources							
Distrib from Priv Purp Trusts		3,463,381					3,463,381
Total		3,463,381					3,463,381
Transfers-out							
Fund transfers					35,691,023	74,514,849	110,205,873
Total					35,691,023	74,514,849	110,205,873
Debt Service							
Loans					11,617		11,617
Capital Leases						125	125
Installment Purchases						6,259	6,259
Total					11,617	6,384	18,001
Other Post Employment Benefits							
Other Post Employment Benefits		11,118			155,389		166,507
Total		11,118			155,389		166,507
Total Expenditures & Transfers-Out	$ 10,167,551	$ 122,211,749	$ 133,274,699	$ (49,179)	$ 109,243,682	$ 94,800,215	$ 469,648,718
EXPENDITURES & TRANSFERS-OUT BY FUND							
General Fund	$ 9,242,361	$ 7,811,817	$ 132,402,042	$ 98		$ 20,246,624	$ 169,702,940
State Special Revenue Fund	663,830	110,723,596	478,023		$ 33,671	38,742	111,937,863
Federal Special Revenue Fund	261,360		1,000				262,360
Enterprise Fund		36,970	393,634	(49,276)	109,210,011		109,591,339
Internal Service Fund		175,985					175,985
Private Purpose Trust Fund		3,463,381					3,463,381
Permanent Fund						74,514,849	74,514,849
Total Expenditures & Transfers-Out	10,167,551	122,211,749	133,274,699	(49,179)	109,243,682	94,800,215	469,648,718
Less: Nonbudgeted Expenditures & Transfers-Out	(11,308)	3,468,697	(8,789)		732,487	74,493,833	78,674,921
Prior Year Expenditures & Transfers-Out Adjustments	(118)	317,617	8,732	(49,179)	(2,918)	457	274,592
Actual Budgeted Expenditures & Transfers-Out	10,178,978	118,425,434	133,274,755	0	108,514,113	20,305,925	390,699,205
Budget Authority	10,298,690	126,368,066	133,506,712		126,680,495	20,317,196	417,171,159
Unspent Budget Authority	$ 119,712	$ 7,942,632	$ 231,957	$ 0	$ 18,166,382	$ 11,271	$ 26,471,954
UNSPENT BUDGET AUTHORITY BY FUND							
General Fund	$ 12,870	$ 5,840	$ 210,953			$ 6,540	$ 236,202
State Special Revenue Fund	3,750	7,910,127	21,004			4,731	7,939,612
Federal Special Revenue Fund	103,093						103,093
Enterprise Fund					$ 18,166,382		18,166,382
Internal Service Fund		26,665		$			26,665
Unspent Budget Authority	$ 119,712	$ 7,942,632	$ 231,957	$ 0	$ 18,166,382	$ 11,271	$ 26,471,954

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DEPARTMENT OF REVENUE
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

	Business & Income Taxes Division	Citizan Services & Resource Management Division	Director's Office	Information Managment & Technology Division	Liquor Control Division	Property Assessment Division	Total
PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT							
Personal Services							
Salaries	$ 6,224,005	$ 2,062,526	$ 3,109,202	$ 3,472,098	$ 1,291,437	$ 10,981,402	$ 27,140,669
Employee Benefits	2,145,983	772,301	916,689	1,212,990	466,979	4,218,074	9,733,016
Personal Services-Other		43			11,818		11,861
Total	8,369,988	2,834,869	4,025,891	4,685,088	1,770,233	15,199,476	36,885,546
Operating Expenses							
Other Services	333,634	354,378	1,059,603	2,429,555	75,204	695,552	4,947,925
Supplies & Materials	133,797	83,133	177,495	326,576	105,720	408,001	1,234,722
Communications	224,667	194,224	77,796	982,218	54,102	551,291	2,084,297
Travel	210,227	18,609	69,269	17,730	22,050	79,074	416,958
Rent	249,713	78,303	136,235	734,955	102	1,841,805	3,041,112
Utilities		1,027			50,076		51,103
Repair & Maintenance	19,094	5,868	22,534	3,033,918	52,863	58,439	3,192,716
Other Expenses	209,450	106,745	57,999	86,179	(58,141)	20,065	422,296
Goods Purchased For Resale					67,340,983		67,340,983
Total	1,380,582	842,287	1,600,930	7,611,131	67,642,957	3,654,226	82,732,112
Equipment & Intangible Assets							
Equipment		(19,254)		516,012	(5,670)		491,087
Capital leases - equipment						12,666	12,666
Total		(19,254)		516,012	(5,670)	12,666	503,754
Local Assistance							
From State Sources		104,368,833	112,151,427				216,520,260
Total		104,368,833	112,151,427				216,520,260
From Other Sources							
Distrib from Priv Purp Trusts		3,723,322					3,723,322
Total		3,723,322					3,723,322
Transfers-out							
Fund transfers			1,691		34,755,707	74,560,458	109,317,855
Total			1,691		34,755,707	74,560,458	109,317,855
Debt Service							
Loans					17,377		17,377
Capital Leases						2,188	2,188
Installment Purchases						15,293	15,293
Total					17,377	17,481	34,858
Other Post Employment Benefits							
Other Post Employment Benefits		9,866			134,696		144,562
Total		9,866			134,696		144,562
Total Expenditures & Transfers-Out	$ 9,750,570	$ 111,759,923	$ 117,779,939	$ 12,812,231	$ 104,315,299	$ 93,444,307	$ 449,862,269
EXPENDITURES & TRANSFERS-OUT BY FUND							
General Fund	$ 8,785,115	$ 3,258,347	$ 117,538,014	$ 11,737,052		$ 18,835,604	$ 160,154,132
State Special Revenue Fund	650,762	104,556,045	107,572	374,804	$ 16,444	48,245	105,753,872
Federal Special Revenue Fund	314,693						314,693
Capital Projects Fund				507,322			507,322
Enterprise Fund		43,215	134,353	193,053	104,298,856		104,669,477
Internal Service Fund		178,994					178,994
Private Purpose Trust Fund		3,723,322				9,123	3,732,446
Permanent Fund						74,551,334	74,551,334
Total Expenditures & Transfers-Out	9,750,570	111,759,923	117,779,939	12,812,231	104,315,299	93,444,307	449,862,269
Less: Nonbudgeted Expenditures & Transfers-Out	(8,359)	3,737,249	(3,544)	(5,463)	(19,667)	74,542,819	78,243,035
Prior Year Expenditures & Transfers-Out Adjustments	5,682	1,021,501	(29,789)		(67,364)	27,226	957,256
Actual Budgeted Expenditures & Transfers-Out	9,753,247	107,001,173	117,813,273	12,817,694	104,402,331	18,874,262	370,661,979
Budget Authority	9,810,505	151,526,035	118,177,985	12,832,938	132,340,916	18,913,517	443,601,896
Unspent Budget Authority	$ 57,258	$ 44,524,862	$ 364,712	$ 15,244	$ 27,938,585	$ 39,255	$ 72,939,917
UNSPENT BUDGET AUTHORITY BY FUND							
General Fund	$ 9,854	$ 10,386	$ 363,677	$ 15,244		$ 23,472	$ 422,633
State Special Revenue Fund	17,929	44,504,913	35			15,783	44,538,660
Federal Special Revenue Fund	29,475		1,000				30,475
Enterprise Fund					$ 27,938,585		27,938,585
Internal Service Fund		9,564					9,564
Unspent Budget Authority	$ 57,258	$ 44,524,862	$ 364,712	$ 15,244	$ 27,938,585	$ 39,255	$ 72,939,917

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
Additional information is provided in the notes to the financial schedules beginning on page A-9.

Department of Revenue
Notes to the Financial Schedules
For the Two Fiscal Years Ended June 30, 2014

1. Summary of Significant Accounting Policies

Basis of Accounting

The department uses the modified accrual basis of accounting, as defined by state accounting policy, for its Governmental fund category (General, State Special Revenue, Federal Special Revenue, Capital Projects, Debt Service, and Permanent). In applying the modified accrual basis, the department records:

- Revenues when it receives cash or when receipts are realizable, measurable, earned, and available to pay current period liabilities.
- Expenditures for valid obligations when the department incurs the related liability and it is measurable, with the exception of the cost of employees' annual and sick leave. State accounting policy requires the department to record the cost of employees' annual and sick leave when used or paid.

The department uses accrual basis accounting for its Proprietary (Enterprise and Internal Service) and Fiduciary (Private-Purpose Trust and Agency) fund categories. Under the accrual basis, as defined by state accounting policy, the department records revenues in the accounting period when realizable, measurable, and earned, and records expenses in the period incurred when measurable.

Expenditures and expenses may include: entire budgeted service contracts even though the department receives the services in a subsequent fiscal year; goods ordered with a purchase order before fiscal year-end, but not received as of fiscal year-end; and equipment ordered with a purchase order before fiscal year-end.

Basis of Presentation

The financial schedule format was adopted by the Legislative Audit Committee. The financial schedules are prepared from the transactions posted to the state's accounting system without adjustment.

The department uses the following funds:

Governmental Fund Category

- **General Fund** – to account for all financial resources except those required to be accounted for in another fund. The department records various tax receipts in the General Fund. The primary expenditures in the General Fund include department payroll costs and distribution of the General Fund entitlement share payments to cities and counties.

- **State Special Revenue Fund** – to account for proceeds of specific revenue sources (other than private-purpose trusts or major capital projects) that are legally restricted to expenditures for specific state program purposes. Department State Special Revenue Funds include various earmarked tax accounts.
- **Federal Special Revenue Fund** – to account for activities funded from federal revenue sources. Department Federal Special Revenue Funds relate to the Federal Mineral Royalty Audit Program.
- **Debt Service Fund** – to account for accumulated resources for the payment of principal and interest on general long-term obligation debt. The department deposits coal, metal mine, and resource indemnity taxes into this fund type.
- **Capital Projects Fund** – to account for financial resources used for the acquisition or construction of major capital facilities, other than those financed by proprietary funds or trust funds. Coal severance tax and cigarette tax revenues collected by the department in support of the state Long Range Building Program are accounted for in capital project funds.
- **Permanent Fund** – to account for financial resources that are permanently restricted to the extent that only earnings, and not principal, may be used for purposes that support the government's programs. The department uses this fund to account for its activity in the Permanent Coal Trust Fund; the Cultural Trust Fund; the Coal Severance Tax Income and Bond Funds; the Resource Indemnity Trust and Income Funds; the Treasure State Endowment, Income Regional Water System, and Regional Water Income Funds; and the Big Sky Economic Development Funds.

Proprietary Fund Category

- **Internal Service Fund** – to account for the financing of goods or services provided by one department or agency to other departments or agencies of state government or to other governmental entities on a cost-reimbursement basis. The department's Internal Service Fund accounts for bad debt collection activity.
- **Enterprise Fund** – to account for operations (a) financed and operated in a manner similar to private business enterprises, where the Legislature intends that the department finance or recover costs primarily through user charges; (b) where the Legislature has decided that periodic determination of revenues earned, expenses incurred or net income is appropriate; (c) where the activity is financed solely by a pledge of the net revenues from fees and charges of the activity; or (d) when laws or regulations require that the activities' cost of providing services, including capital costs, be recovered with fees and charges rather than with taxes or similar revenues. The department's Enterprise Fund accounts for the Liquor Control Division's administration of the alcoholic beverage code.

Fiduciary Fund Category

- **Private-Purpose Trust Fund** – to account for activity of any trust arrangement not properly reported in a pension fund or an investment trust fund where the principal and income benefit individuals, private organizations, or other governments. Department Private-Purpose Trust Funds are used to account for unclaimed property, escheated property, and unlocated mineral owner interests.
- **Agency Fund** – to account for resources held by the state in a custodial capacity. Agency funds may be used on a limited basis for internal (to the State) clearing account activity, but these must have a zero balance at fiscal year-end. Property Held in Trust, accounts 2504A and 2504B, have a balance at fiscal year-end because bad debts captured during the offset process must be held in a custodial manner for thirty days for debtor notification and appeal. The department agency funds are used as clearing accounts to facilitate the distribution of receipts from the administration of the eStop licensing program, the county collection reports, bad debt collections, dishonored checks, treasury deposit and bank corrections, Automated Clearing House (ACH) collections and reversals, and account receivable activity.

2. General Fund Equity Balance

The department has authority to pay obligations from the statewide General Fund within its appropriation limits. The department's total assets placed in the fund exceed outstanding liabilities, resulting in a positive ending General Fund balance for the fiscal year ended June 30, 2013. This balance reflects the results of the activity of the department and not the fund equity balance of the statewide General Fund.

The negative fund balance in the General Fund for the fiscal year ended June 30, 2014, does not indicate overspent appropriation authority. The department has authority to pay obligations from the statewide General Fund within its appropriation limits. The department expends cash or other assets from the statewide fund when it pays General Fund obligations. The department's outstanding liabilities exceed the assets it placed in the fund, resulting in negative ending General Fund balance.

3. Direct Entries to Fund Equity

Direct entries to fund equity in the General, State Special Revenue, Debt Service, Capital Projects, Enterprise, and Permanent funds include entries generated by SABHRS to reflect the flow of resources within individual funds shared by separate agencies. The General Fund also includes adjustments for Insure Montana Tax Credits for previous periods that occurred at least two fiscal years prior.

4. Revenues Over (Under) Estimate

The Schedule of Total Revenues & Transfers-In for the fiscal year ended June 30, 2013, reports revenues over estimate by $231,659,890 in the General Fund and under estimate by $10,624,607 in the State Special Revenue Fund. In addition, the Schedule of Total Revenues & Transfers-In for the fiscal year ended June 30, 2014, reports revenues under estimate in by $24,162,518 in the State Special Revenue Fund. These are explained below:

- **General Fund** – Overall, for the fiscal year ended June 30, 2013, individual income tax collections were more than House Joint Resolution (HJ) 2 estimates by $188 million because the assumptions underlying the HJ2 estimates did not match actual experience. In addition, actual revenues collected for property tax (95 mills) were $4.3 million less than estimated, and corporation license tax revenues collected were $50 million more than estimated. A portion of the difference in corporation license tax revenues is due to a one-time only event: The conversion from a c-corp to another business structure that would be taxed as a disregarded entity. The IRS imposed certain rules forcing recognition of taxable income which flowed through to the state level. This event was not foreseeable and, consequently, not picked up in the forecast.
- **State Special Revenue Fund** – Revenues in the state special revenue fund were less than estimated for the fiscal year 2013, because hospital utilization fees collected were $1.9 million less than estimated. In addition, the Schedule of Revenue & Transfers-In includes a $3.1 million revenue estimate in a nonbudgeted transfer account for the Big Sky Economic Development Fund. Revenue transfers to this fund are not included in budgeted revenue collections on the schedule. Finally, natural resource tax revenue collections were $5.5 million less than estimated; the result of the HJ2 assumption that natural gas production would be 68 per million cubic feet (MMCF) with a contract sales price of $3.5 per MMCF when actual production was 57 MMCF with a contract sales price of $3.3 per MMCF and an overestimate of the combined oil and gas revenue distributed to the counties.

  Revenues in the state special revenue fund were less than estimated for the fiscal year ending June 30, 2014, because the Schedule of Revenue & Transfers-In includes a $3.1 million revenue estimate in a nonbudgeted transfer account for the Big Sky Economic Development Fund and a $2.7 million revenue estimate in an investment earnings account in the Montana Oil and Gas Tax Clearing Fund. In addition, during the 2012 budget preparation, a $9.5 million revenue estimate was established in Guarantee Fund. However, during the 2013 Legislative session, legislation was passed to redirect revenue to a different fund. The initial revenue estimate was not removed. A similar situation occurred in the Oil and Gas Natural Resource Fund (formerly Oil, Natural Gas and Coal Fund) which was split and revenue estimates were prepared for the split. A $3.1 million coal revenue estimate was initially established in this fund, but redirected to the Coal Board Fund. However, the original revenue estimate was not removed. Finally, the fiscal year 2014 revenue estimate for metal mines was $1.6 more than actual collections.

Since actual collections were 25 percent less than estimated, no revenue was reclassified to the Hard Rock Mining Reclamation Debt Service Fund, but a revenue estimate of $1.58 million was established in this fund.

5. Nonbudgeted Expenditures and Transfers-out

Nonbudgeted Expenditures and Transfers-Out in the permanent fund, on the Schedule of Changes in Fund Equity & Property Held in Trust, is approximately $74.5 million for both fiscal years 2013 and 2014. This amount is also reflected on the Schedule of Total Expenditures & Transfers-Out and is related to the coal tax transfers required by state law. These include transfers from the Coal Tax Bond Fund, distributions of investment earnings on the Treasure State Endowment Funds, Big Sky Economic Development Fund, Resource Indemnity Trust Fund and the coal tax trust funds.

6. Unspent Budget Authority

The Schedule of Total Expenditures & Transfers-out for fiscal year 2013 reports unspent budget authority under the Citizen Services and Resource Management Division of $44,524,862 in the State Special Revenue Fund and $27,938,585 under the Liquor Control Division in the Enterprise Fund.

The unspent budget authority in the Citizen Services and Resource Management Division is created due to fiscal year 2013 revenue collected or accrued and distributed to local governments being less than estimated. Fiscal year 2013 combined oil and natural gas production tax estimates were created based on higher natural gas prices and production than were realized. In addition, distributions of bentonite taxes received to Carbon and Carter counties for fiscal year 2013 were less than estimated.

The Liquor Control Division receives language appropriations for funds necessary to maintain adequate inventories; pay freight charges; and transfer profits, taxes, and liquor licensing revenues to the appropriate accounts. In fiscal year 2013, the appropriation was not to exceed $132 million. The department purchased inventory and distributed profits and taxes based upon the volume of sales and did not spend up to the total appropriation authority. The language appropriation for the transfer of licensing revenues also includes appropriation authority for both the Department of Revenue and the Department of Justice to administer liquor licensing. By law, the transfer of the licensing revenue is net of the appropriation authority for the Department of Revenue and the Department of Justice and deferred revenues. Likewise, for fiscal year 2014, transfers were made based upon the volume of sales which were less than the language appropriation granted by approximately $18.2.

7. Prior Year Revenues

On the Schedule of Changes in Fund Equity & Property Held in Trust and the Schedule of Total Revenues & Transfers-In for fiscal year 2013 and 2014, the department recorded transactions that total $2,809,114 and $(2,096,649), respectively, in the General Fund and $1,643,041 in fiscal year 2013 in the State Special Revenue Fund as explained below:

- **General Fund –** The majority of this activity includes the difference between reversing estimated revenues accrued in the prior year versus reclassifying current year actual revenue collections as prior year revenues plus the reversal of accounts receivable revenues accrued in the prior year at fiscal year-end.
- **State Special Revenue Fund** - The majority of the transactions recorded as prior year revenue in the State Special Revenue Fund represents the difference between the reversal of estimated revenues accrued in the prior year versus current year actual revenue collections reclassified as prior year revenue.

8. Program Change

On the Schedule of Expenditures & Transfers-Out for fiscal year 2013, the expenditures and transfers out related to the Information Management and the Information Technology bureaus were recorded under the Information Management and Technology Division. In fiscal year 2014, the department reorganized from five divisions to four with these bureaus being moved under the Citizen Services and Resource Management Division and the Director's Office, respectively. Their related expenditures and transfers out are recorded under these divisions' headings for fiscal year 2014.

The department reorganization is due to the department aligning the functions of the Information Management Bureau with like services administered by the Citizen Services and Resource Management Division to create efficiencies and to put the responsibilities of the Information Technology Bureau under the Director's Office because it provides department-wide services which are better aligned under the umbrella of the Director's Office.

9. Subsequent Event

The department finalized two protested property tax settlements in June 2014; both with Cellco Partnership for Verizon and Alltel. While the settlements were finalized in fiscal year 2014, the refunds to Cellco and the reclassification of the state's share from protested property taxes to regular property taxes did not occur until July 2014, fiscal year 2015. The Verizon settlement resulted in a $1,640,342 refund including $2,964 in interest to Cellco and a total of $2,707,363 released to regular property taxes for the state's share. The Alltel settlement resulted in a $136,666 refund including $336 in interest to Cellco and a total of $407,098 released to regular property taxes for the state's share.

10. Financial Schedules

The financial schedules for the two fiscal years ended June 30, 2014, do not foot or cross-foot due to rounding. However, the rounding issue is immaterial and the department considers the schedules an accurate representation of the financial activity reported in SABHRS by the department.

DEPARTMENT OF REVENUE

DEPARTMENT RESPONSE

Montana Department of Revenue

Mike Kadas
Director

Steve Bullock
Governor

October 22, 2014

Tori Hunthausen, Legislative Auditor
Legislative Audit Division
Room 160, State Capitol
P O Box 201705
Helena, MT 59620-1705

Dear Ms. Hunthausen:

Thank you for the opportunity to respond to the Financial Compliance Audit Report recently completed for the two fiscal years ended June 30, 2014. This audit report includes four recommendations all of with which the department concurs. Our response to the recommendations is as follows:

Recommendation #1:

We recommend the Department of Revenue comply with department policy by:

A. Obtaining required approvals prior to granting access to GenTax.
B. Terminating temporary employee access when employment terminates.

Concur. In the nine instances where request forms were not approved, access was initially approved and granted by the Technology Security Officer. Although the access request form was not subsequently approved by both the Technology Security Officer and the Information Security Officer, the dual approval process was achieved by the manager requesting the access be granted and the Technology Security Officer approving and granting as requested. In the ten instances regarding the cease access date for temporary employees, it is not always known when that date will occur at the time the request for access is initially made. The department is currently revising its policy to include a cease access date at the time the access is requested if it is known.

The department is working on the implementation of a new procedure/policy where dual approval is required, with the first approval being the manager requesting the access and the second being a member of the Security Office approving that request. To ensure the second approval of the Security Office, a service manager tool has been implemented, along with continued use of a security office email box to work access requests as they are received. Although the one instance of a temporary employee's access did not terminate on the date documented, it is highly unlikely the security of the department's system would be compromised because temporary employees are not granted remote access. To gain access to the department's computers, they would have to access the department's work area; and they would be unable to do so because their physical access to the department would have been terminated when their employee access badge was cancelled.

Since these issues have been raised, the cases identified have all been rectified and procedures have been modified to ensure access is properly administered following department policy. The implementation of a new security office has included the use of a ticketing system to address computer access; plus a review of active network accounts as compared to Human Resource employee records.

Recommendation #2:

We recommend the Department of Revenue implement procedures to ensure non-levy revenue, such as coal gross proceeds, is complete and accurate.

Concur. The department will evaluate how it currently processes non-levy revenue and implement procedures to ensure non-levy revenue submitted to the department by Montana counties is distinguishable from other property tax revenue. This will entail making modifications to the county collection report which will require local governments to modify how they remit revenue to the department. While the authority to ensure counties are properly computing and remitting revenue to the state lies with the Department of Administration Local Government Services (LGS), the department intends to work with LGS to come to an equitable solution with all 56 counties.

Recommendation #3:

We recommend the Department of Revenue comply with state law by assessing Contractor's Gross Receipts Tax penalties and interest.

Concur. The department will begin assessing penalty and interest for the submission of untimely Contractor Gross Receipts Tax returns. The department is currently reviewing the most cost effective way to implement this recommendation. The department anticipates that this review will be complete by the end of December 2014 with the implementation of assessing penalty and interest beginning January 1, 2015.

Recommendation #4:

We recommend the Department of Revenue comply with state law and charge fees that are commensurate with costs.

Concur. The department is in the process of lowering the internal service fund rate from 5 percent to 3.5 percent in order to reduce the cash balance and ending fund equity to a level to meet the timing of when revenues are received and expenses are incurred. It is necessary to maintain a nine month working capital balance to pay expenses as they are incurred as the majority of commission revenue is not collected until the income tax filing season each year, some six to nine months after the start of the fiscal year.

While the department has been monitoring the activity in the internal service fund, the decision to adjust the rate was delayed until fiscal year end 2014 because the effects of the following circumstances on revenue and expenses could not be readily determined. The circumstances that weighed into this decision were the collections unit was not fully staffed in fiscal year 2013 and the department was engaged in a project to automate many of the manual collections processes. Now that the unit is fully staffed and the project to implement system changes has been completed, the department is able to reduce the rate with more confidence in what effect the reduction will have on cash flow.

Thank you for allowing us to respond to the financial compliance audit report and the opportunity to discuss the issues with you and your staff during the exit conference. I would also like to thank your staff who conducted the audit for their professionalism and their fairness in working through the issues that were raised.

Sincerely,

Mike Kadas, Director