

LEGISLATIVE AUDIT COMMISSION



Review of
Department of Corrections
Correctional Industries
Two Years Ended June 30, 2012

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**REVIEW: 4411
DEPARTMENT OF CORRECTIONS
CORRECTIONAL INDUSTRIES
TWO YEARS ENDED JUNE 30, 2012**

FINDINGS/RECOMMENDATIONS - 13

**IMPLEMENTED - 11
ACCEPTED - 2**

**REPEATED RECOMMENDATIONS - 5
PRIOR AUDIT FINDINGS/RECOMMENDATIONS - 6**

This review summarizes the reports on the Department of Corrections, Correctional Industries (ICI), filed with the Legislative Audit Commission on February 28, 2013. The auditors performed a compliance examination for the two years ended June 30, 2012, and a financial audit for the one-year ended June 30, 2012. The auditors issued a qualified opinion on ICI's basic financial statements. Auditors were unable to obtain sufficient appropriate audit evidence supporting accounts receivable stated at \$10 million and revenues stated at \$50.7 million.

Correctional Industries operates as a productive enterprise employing prisoners from institutions under the jurisdiction of the Department of Corrections. ICI programs are supported by revenues derived from the sale of its products and services. Tax-supported institutions and non-profit organizations comprise the majority of the market. State law requires state agencies give the Department preference when procuring items manufactured by the ICI. The Director of the Department of Corrections during the audit period was Michael P. Randle (6/7/2009 to 9/18/10), Gladyse Taylor, Acting (9/19/10 to 5/1/11), and Salvador A. Godinez (effective 5/2/11 to present). The Chief Executive Officer of Correctional Industries during the audit period was Timothy Gleason (5/16/10 to 9/15/12) and Rich Mautino (9/16/12 to 11/30/12). Jen Aholt became Chief Executive Officer on December 1, 2012 and she continues to serve in that position. Previously she was a deputy director of projects at Public Safety Shared Services.

Following is the average number of employees (excluding inmates) in the Correctional Industries Division:

FY12 -129; FY11- 132; FY10 - 121.

Expenditures From Appropriations

The General Assembly appropriated \$51,002,200 from the Working Capital Revolving Fund to Correctional Industries for FY12. Appendix A summarizes the appropriations and expenditures for the period under review. Correctional Industries' operations are financed by sales of its products. All appropriations are made from the Working Capital Revolving

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Fund, which receives proceeds from the sale of products and services and rent from farm leases. Total expenditures for the Working Capital Revolving Fund increased from \$39,911,186 million in FY10 to \$44,097,251 in FY11, and \$48,895,538 in FY12. Expenditures increased primarily due to an increase in the cost of commodities and a rise in State contribution to the retirement system. Lapse period spending was approximately \$4.4 million, or 6.9%.

Working Capital Revolving Fund

Appendix B provides a statement of net assets and changes in net assets for the Working Capital Revolving Fund at June 30, 2012. The Working Capital Revolving Fund accounts for the activities of the Correctional Industries program. Operating income for the Fund for FY12 was \$891,000. However, the auditors issued a qualified opinion on ICI's basic financial statements. Auditors were unable to obtain sufficient appropriate audit evidence supporting accounts receivable stated at \$10,043,000 million and revenues stated at \$50,757,000 million.

Summary of Operations by Industry

Appendix C presents a summary of Correctional Industries' net income for each industry in FY08 and FY07. During FY12, Correctional Industries operated 28 separate industries, of which seven were found to be profitable and 21 experienced losses. During FY12, the following industries had the largest losses: Western Illinois Food Processing (-\$679,328), Vandalia Farm Milk Processing (-\$638,182), Graham furniture (-\$609,502), and Shawnee Metal Furniture (-\$609,108). The industry with the greatest profit was Dixon Optical (\$6,326,233).

Accounts Receivable

Accounts receivable as shown in Appendix D amounted to \$10,590,918 at June 30, 2012. A receivable of almost \$6.5 million is due from the Department of Corrections. Accounts receivable represent amounts due from sale of goods and services to State agencies, local governments, and others. Most receivables were current. Accounts over 180 days old totaled \$1.6 million. The Department considers all accounts fully collectible. As noted in Finding No. 1, the Department did not maintain adequate and accurate records related to customer accounts receivables.

Inventories and Property and Equipment

Inventories at June 30, 2012 are shown in Appendix E, and totaled \$6.7 million. Appendix F contains a summary of property and equipment. The sum of equipment and buildings at June 30, 2012 was \$26,969,001.

Number of Inmates Employed by Industry

Appendix G indicates the number of inmates employed by each industry for FY12 and FY11. During FY12, the average number of inmates working was 937.

Accountants' Findings and Recommendations

Condensed below are the 13 findings and recommendations included in the audit report. Five recommendations were repeated from prior audits. The following recommendations are classified on the basis of updated information provided by Ron Faith, Chief Internal Auditor, Department of Corrections, in a memo received on December 24, 2013 via electronic mail.

Accepted or Implemented

- 1. Work with customers to determine the accurate accounts receivable. In addition, ensure all invoices and payments are properly posted.**

Finding: The Illinois Department of Corrections—Correctional Industries (Department) did not ensure the information utilized to prepare financial statements and the Office of the Comptroller GAAP (Generally Accepted Accounting Principles) packages was accurate for the Working Capital Revolving Fund.

Auditors noted the Department did not maintain adequate and accurate records related to their customer accounts receivable. The Department reported in their financial statements \$10,042,850 in customer accounts receivable for the Working Capital Revolving Fund at June 30, 2012.

As part of standard audit procedures, auditors selected a sample of 40 customer accounts receivable and requested the customer to confirm the balance they owed at June 30, 2012. Of the 16 confirmations returned, the customer indicated they owed \$4,641,117, whereas the Department records stated they owed \$5,082,035, for an overstatement of \$440,918.

Upon discussion with management, it was determined the Department customer accounts receivable system contained payment posting errors. Management also stated they did not have all the supporting detail to ensure the posting of payments to the proper invoice.

Due to the noted differences in customer account balances and the payment posting errors within the accounts receivable system, the information related to accounts receivable and revenues included in the financial statements cannot be verified. As a result, the auditors issued a qualified opinion on the Department's financial statements.

Accepted or Implemented – continued

Updated Response: Implemented. Illinois Correctional Industries fiscal staff has implemented controls over accounts receivable and is taking the necessary steps to ensure receivable financial information is properly reflected in the financial statements.

2. Maintain adequate controls over accounts receivable to ensure:

- **Monthly statements are sent out,**
- **Reasonable efforts are put forth related to the billing and collection of accounts,**
- **Catch up billings are sent out, and**
- **Quarterly Summary of Accounts Receivable Reports are accurate and signed by an appropriate official.**

Finding: Correctional Industries (Department) did not maintain adequate internal controls over their accounts receivable. During a review of accounts receivable, auditors noted:

- The Department did not send out monthly statements to their customers.
- The Department did not take actions to bill and collect receivables within the fiscal year in which the debt was incurred. According to Department records, accounts receivable due over one year totaled \$1,344,677 at June 30, 2012.
- The Department did not issue catch up billings in the subsequent fiscal year for accounts with balances from the prior fiscal year.
- The Quarterly Summary of Accounts Receivable Reports (C-97) filed with the Office of the Comptroller for fiscal years 2011 and 2012 were not signed by management for seven of the eight filings.
- The Quarterly Summary of Accounts Receivable Reports (C-97) filed with the Office of the Comptroller for the period ended June 30, 2011 was amended three times.

Department Management stated that between 2006 and 2012 the payments were not always posted properly to the matching invoices. As a result the customers detailed statement became lengthy and was no longer sent. Management stated the majority of their receivables are from state agencies. The Department also noted the responsibility for reviewing the receivable aging trial balance is the task of the Chief Financial Officer which was not permanently filled during the engagement period.

Updated Response: Implemented. Illinois Correctional Industries fiscal staff has implemented controls over accounts receivable reconciliation by ensuring proper invoicing and collection of accounts is occurring and the Comptroller's Quarterly Summary of Accounts Receivable Report is accurate and approved by appropriate staff.

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3. Work with the Department of Central Management Services regarding the administration of the farm leases. In addition, ensure all information is accurately reflected in the financial statements.

Finding: Correctional Industries (Department) failed to pursue collections of past due amounts owed from farm leases.

The Department has entered into 12 leases totaling 3,619 acres with annual rent of \$601,578 for fiscal years 2011 and 2012. According to Department records, accounts receivable at June 30, 2012 related to farm leases was \$209,737.

During a review of the farm lease program, auditors noted:

- The Department of Central Management Services (CMS) is responsible for the collection of any delinquent accounts. However, the lease agreement states monthly payments are to be submitted to Illinois Correctional Industries for deposit into the Working Capital Revolving Fund.
- CMS sent out two notices for collection. Both tenants paid; however, one tenant did not make payment of interest totaling \$9,305. Additionally, the Department did not record the outstanding interest as an accounts receivable on their financial statements at June 30, 2012.
- The Department did not follow their internal procedures for accounts receivable, whereby monthly statements are required to be sent on all delinquent accounts. The Department relied upon the lease as the tenant's notification of amounts owed.
- The lease agreements states monthly finance charges of 1.5% (18% annually) are to be assessed. However, interest was not assessed on past due accounts, totaling approximately \$89,910. In addition, the Department did not record the outstanding interest as an account receivable on their financial statements at June 30, 2012.
- The farm lease accounts receivable at June 30, 2012 included \$209,737 which has been outstanding over one year, and 90% past due for more than five years. However, the Department had not reviewed the accounts for collectability and had not established an allowance for doubtful accounts.

Department Management stated, in prior years, the Department attempted to monitor and track farm leases. Upon a letter dated January 2, 2012 from the Department of Central Management Services Bureau of Property Management, it was determined that the Department Central Management Services has the role of administrator of these leases.

Updated Response: Implemented. Illinois Correctional Industries fiscal staff has implemented controls over farm leases and is taking the necessary steps to ensure farm lease financial information is properly reflected in the financial statements.

Accepted or Implemented – continued

4. Timely post expenditures to the Accounting Information System. Additionally, timely investigate all outstanding reconciling items.

Finding: Correctional Industries (Department) did not timely post expenditures to the Accounting Information System (AIS).

During a review of payroll expenditures, auditors noted the Department did not post the bi-monthly payroll expenditure to AIS until the next monthly Comptroller's report was received. The August 2012 reconciliation, completed on September 21, 2012, indicated reconciling items of \$366,613. Reconciling items dated back to January 2011.

Department Management stated due to competing priorities, they cannot ensure these transactions are posted in a timely manner. They are working with Department of Corrections to bring this function back to the responsibility of Illinois Correctional Industries.

Updated Response: Implemented. Illinois Correctional Industries fiscal staff has assumed responsibility for the timely posting of the bi-monthly payroll expenditures to the Accounting Information System (AIS), and is monitoring and investigating outstanding reconciling items.

5. Seek full reimbursement from a manager for improper payments. Additionally, submit salary reversals to the Office of the Comptroller within the time frame outlined in the SAMS Manual.

Finding: Correctional Industries (Department) inappropriately paid a Manager \$16,875. On July 1, 2011, the Department entered into an Interagency Agreement with the Department of Commerce & Economic Opportunity related to the assignment of a Manager to the Department. According to the Agreement, the Department of Commerce & Economic Opportunity would continue to pay the Manager and Correctional Industries would compensate the Department of Commerce & Economic Opportunity for such costs.

However, beginning in August 2011, the Department also began to pay the Manager. The Manager was paid by both the Department and the Department of Commerce & Economic Opportunity for the months of August, September and October 2011, totaling an overpayment of \$16,875 (\$5,625 per month).

In December 2011, the Department entered into an agreement with the Manager for repayment. The Manager left State employment in April 2012. As of June 30, 2012, the Manager still owed the Department \$5,639, and the department had not submitted salary reversals to the Office of the Comptroller salary reversals related to the erroneous overpayments.

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Department management stated the overpayment occurred when the Manager was processed in the Department's payroll system as a provisional exempt filing position. Department management which approved the provisional exempt filing was unaware this would allow payroll to begin from the Department. The Department's personnel who processed the provisional exempt filing position was not aware the Manager was being paid by the Department of Commerce & Economic Opportunity.

Response: Accepted. Management will monitor and ensure salary reversals are completed for improper payments made to the prior Manager.

Updated Response: Implemented. Illinois Correctional Industries is monitoring the involuntary withholding which was filed in April 2013. At the end of the audit \$5,639 was still owed. The amount outstanding now is \$306.82

6. Implement controls to ensure cash receipts and refunds are deposited in a timely manner in accordance with State statutes.

Finding: Correctional Industries (Department) did not deposit into the State treasury the gross amount of the money received on a timely basis as required by State law.

During testing of receipts and refunds for the fiscal year 2011 and 2012, auditors noted the following:

- Eight of 48 receipts totaling \$138,092 were not deposited timely. For FY11, one receipt for \$1,488 was deposited 21 days late. For FY12, seven receipts totaling \$136,604 were deposited 4 to 245 days late.
- Six of seven refunds totaling \$2,047 were not deposited timely. For FY11, five refunds totaling \$1,938 were deposited 2 to 30 days late. For FY12, one receipt for \$109 was deposited eight days late.

Department management stated that in all but one instance, the Department processed the checks on the same day they were received. Once the deposits are moved to the D2 status, which involves Shared Services, the process is out of their control.

Updated Response: Implemented. Illinois Correctional Industries fiscal staff has reminded staff and implemented controls over receipts and refunds to ensure processing is done timely and accurately.

7. Include the occupancy costs for the manufacturing facilities in accordance with the Product Costing Manual and generally accepted accounting principles. (Repeated-2006)

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Accepted or Implemented – continued

Finding: Correctional Industries (Department) did not include any occupancy costs for the production facilities they use at the Correctional Centers (Centers) in their computation of the manufacturing cost of its products.

The Department has 19 facilities for manufacturing its products at various Correctional Centers. The Correctional Centers have not historically charged the Department for occupancy of these production facilities. As such, the Department does not include any amount for these costs in their computation of product cost.

The Department's Policy, Pricing Products, states a pricing committee will develop a price for each product based on information provided on a quote sheet which reflects the manufacturing costs and current selling price of each product.

Department management stated the Department is a statutorily created program that operates within the Illinois Department of Corrections, which has never provided a breakdown of occupancy costs, nor have the rates been factored into the annual spending authority for the Department. Accordingly, it is important to note the Department's spending authority is approved by the Director of the Illinois Department of Corrections and included within the Department's budget.

Updated Response: Implemented. Illinois Correctional Industries has established a lease agreement with IDOC.

8. Obtain and maintain employee authorizations for medical insurance deductions and supporting documentation for all payroll deductions in accordance with the State Records Act and Administrative Directive. (Repeated-2010)

Finding: Certain Correctional Industries (Department) records were destroyed and were not available to the auditors.

During a review of the employees' payroll files, the Department could not provide:

- 17 of 25 employees medical insurance deduction authorizations,
- 15 of 23 employees union dues deduction authorizations, and
- 13 of 22 employees various other deductions authorizations.

The Department management stated the medical authorization forms were destroyed in a flood of the basement with storage for Central Office on May 26, 2010. Per management, the union and deduction cards often do not get transferred from other facilities within the Department when an employee transfers work locations. The Department had an average of 129 employees at June 30, 2012.

Updated Response: Accepted and partially implemented. Illinois Correctional Industries is working with payroll section, which has reviewed all payroll files, and is

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currently obtaining employee documents that are missing in order to support payroll deductions.

- 9. Comply with the Administrative Code and the collective bargaining agreement in regards to utilizing employees for temporary assignments. Also, establish a monitoring system to identify the time served by employees in temporary positions and send notification to upper management in advance of completion of the period to allow for alternative plans to be made before the time limit is exceeded. (Repeated-1998)**

Finding: Correctional Industries (Department) utilized employees on temporary assignments for periods beyond the permitted time limit.

During the two-year period ended June 30, 2012, the Department had 23 temporary employee assignments, of which testing indicated eight of the assignments exceeded the allowable time limit, without the proper agreement allowing the extensions. The assignments ranged from one to 30 months over the allowable limit.

Department management stated the extensions of the temporary assignments were due to staffing limitations.

Updated Response: Implemented. Illinois Correctional Industries staff, in response to a new temporary assignment process that has resulted due to the settlement agreement between IDOC Labor Relations and the Union, is preparing a monthly, updated listing of ICI employees on temporary assignment. IDOC Labor Relations is meeting monthly with the union to discuss that listing.

- 10. Comply with the statute and develop procedures to prevent committed persons from entering any personally identifiable information.**

Finding: Correctional Industries (Department) failed to prevent a committed person from accessing and entering personally identifiable information in computer systems.

Auditors reviewed job descriptions for 71 inmate positions at 18 Department locations and found 12 positions allowed inmates to process inmate payroll or Medicaid billings, and 10 positions allowed inmates to process vouchers using computers. For the 12 inmate payroll processing positions, one reported having access to inmate social security numbers. Additionally, no formal procedures or policies were in place to describe personally identifiable information.

Department management stated they relied upon the Administrative Directive (01.05.110) which allows offenders to use hardware and software for Correctional Industries work assignments if it is limited to a stand-alone or closed system network. The Directive does not mention or describe personally identifiable information.

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Accepted or Implemented – concluded

Updated Response: Implemented. Illinois Correctional Industries management rectified the situation and direction was given that inmates must not have this level of access.

11. Comply with statutory requirements for timely filing and content of the annual report.

Finding: Correctional Industries (Department) did not prepare and timely file its annual report in accordance with the Unified Code of Corrections.

During testing auditors noted the 2011 Annual Report was submitted to the General Assembly three days late. Additionally, the Annual Report did not contain information about the actual total receipts by purchaser, the average length of time between the receipt of orders and delivery, and the average length of time between delivery and receipt of payment. The 2011 Annual Report listed the required filing date and factors for the report, which included each of these, even though the information was omitted.

Department management stated an employee of the Department informed them the report was delivered on the due date; however, they do not have documentation of the delivery date. Secondly, the Department was not aware of the omission of information until October 28, 2011 and could not receive accurate information in time as to not delay report filing.

Updated Response: Implemented. Illinois Correctional Industries have submitted their complete annual reports in a timely manner.

12. Maintain accurate property control records, and review and approve all Comptroller property reports, and properly tag equipment in accordance with SAMS procedures. (Repeated-2008)

Finding: Correctional Industries (Department) did not comply with property control procedures. During testing auditors noted:

- The capital lease valued at \$60,000 was not listed on property control records, but was properly capitalized on the Department's financial statements.
- One of eight quarterly Agency Reports of State Property (C-15) filed with the Comptroller was filed timely, but was not approved by personnel of the Department.
- Four of 146 items of equipment tested valued at \$6,733 did not have a property control tag affixed.

Department management stated they followed the Administrative Directive for the property to be recorded in the property control system when title has passed. The Department's contract accounting firm signed the C-15 and stated they were told to do so by a previous

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employee of the Department. Additionally, the Department stated two tags had fallen off, one was waiting to be tagged, and one was on a donated asset valued at less than \$100 which they understood did not need a tag.

Updated Response: Accepted and partially implemented. Illinois Correctional Industries is in the process of ensuring capital leases are stated correctly on property control reports and that Agency Reports of State Property (C-15) are filed complete and timely.

13. Strengthen internal controls over reporting of inventory to ensure inventory is valued at the lower of cost or market in accordance with the SAMS Manual. (Repeated-2010)

Finding: Correctional Industries (Department) inventory was not properly valued at June 30, 2011.

Testing of the Department's finished goods inventory of \$2,117,173 at June 30, 2011 disclosed an overstatement of \$44,119 (2%). The discrepancy was attributable to 83 items which were not valued at the lower of cost or market.

Department management stated the errors resulted from clerical errors. The majority of the error (\$34,091) was attributable to one item which had a decimal error in the software program that has now been corrected. Management noted that lower of cost or market formulas were put into place on January 1, 2012.

Updated Response: Implemented. Illinois Correctional Industries fiscal staff has reminded shops of the importance of following inventory process and procedure to verify that all production inventory is properly valued.

Emergency Purchases

The Illinois Procurement Code (30 ILCS 500/) states, "It is declared to be the policy of the State that the principles of competitive bidding and economical procurement practices shall be applicable to all purchases and contracts...." The law also recognizes that there will be emergency situations when it will be impossible to conduct bidding. It provides a general exemption when there exists a threat to public health or public safety, or when immediate expenditure is necessary for repairs to State property in order to protect against further loss of or damage to State Property, to prevent or minimize serious disruption in critical State services that affect health, safety, or collection of substantial State revenues, or to ensure the integrity of State records; provided, however that the term of the emergency purchase shall not exceed 90 days. A contract may be extended beyond 90 days if the chief procurement officer determines additional time is necessary and that the contract scope and duration are limited to the emergency. Prior to the execution of the extension, the chief procurement officer must hold a public hearing and

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provide written justification for all emergency contracts. Members of the public may present testimony.

Notice of all emergency procurement shall be provided to the Procurement Policy Board and published in the online electronic Bulletin no later than 3 business days after the contract is awarded. Notice of intent to extend an emergency contract shall be provided to the Procurement Policy Board and published in the online electronic Bulletin at least 14 days before the public hearing.

A chief procurement officer making such emergency purchases is required to file an affidavit with the Procurement Policy Board and the Auditor General. The affidavit is to set forth the circumstance requiring the emergency purchase. The Legislative Audit Commission receives quarterly reports of all emergency purchases from the Office of the Auditor General. The Legislative Audit Commission is directed to review the purchases and to comment on abuses of the exemption.

During FY11 and FY12, Correctional Industries filed 28 affidavits for emergency purchases totaling \$3,492,484.86 for the following items:

- \$3,405,971.86 for commodities; and
- \$86,513.00 for equipment repairs.