

Audit Report

**Comptroller of Maryland
Revenue Administration Division**

June 2020



OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Victoria L. Gruber
Executive Director

Gregory A. Hook, CPA
Legislative Auditor

June 1, 2020

Senator Clarence K. Lam, M.D., Senate Chair, Joint Audit and Evaluation Committee
Delegate Carol L. Krimm, House Chair, Joint Audit and Evaluation Committee
Members of Joint Audit and Evaluation Committee
Annapolis, Maryland

Ladies and Gentlemen:

We have conducted a fiscal compliance audit of the Comptroller of Maryland (COM) – Revenue Administration Division (RAD) for the period beginning July 1, 2015 and ending September 20, 2018. RAD is primarily responsible for receiving and depositing various tax remittances, processing tax returns, maintaining taxpayer records, distributing taxes in accordance with State laws, issuing income tax refunds, and providing assistance to taxpayers.

Our audit disclosed that RAD had not established effective procedures for ensuring that all financial adjustments to taxpayer accounts, in particular, adjustments that reduced taxpayer liabilities, were subject to supervisory or managerial review. This condition was noted in two units that processed adjustments to reduce taxpayer liabilities by \$2.5 billion in fiscal year 2018. Similarly, we found that tax overpayments, which taxpayers chose to either apply to the next tax year or receive as a refund, were not being reviewed for propriety as required.

We also noted that sufficient controls had not been established over cash receipts at RAD's Annapolis location and Baltimore cash office. For example, several employees at RAD's Annapolis location who processed cash receipts, also had the capability to record critical financial adjustments in taxpayer accounts, such as to reduce a tax liability. Finally, our audit also disclosed certain deficiencies relating to information systems security.

Our audit also included a review to determine the status of the eight findings contained in our preceding audit report on RAD, and one finding contained in our

preceding audit report on COM – Compliance Division dated April 10, 2017 relating to cash receipts functions that subsequently were transferred to RAD. We determined that RAD satisfactorily addressed six of these nine findings. The remaining three findings are repeated in this report.

COM's response to this audit, on behalf of RAD, is included as an appendix to this report. We reviewed the response and noted general agreement to our findings and related recommendations, and while there are other aspects of COM's response which will require further clarification, we do not anticipate that these will require the Joint Audit and Evaluation Committee's attention to resolve.

We wish to acknowledge the cooperation extended to us during the audit by RAD. We also wish to acknowledge COM's and RAD's willingness to address the audit issues and implement appropriate corrective actions.

Respectfully submitted,

A handwritten signature in black ink that reads "Gregory A. Hook". The signature is written in a cursive style with a large, prominent initial "G".

Gregory A. Hook, CPA
Legislative Auditor

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Background Information

Agency Responsibilities

The primary responsibilities of the Comptroller of Maryland's Revenue Administration Division (RAD) include receiving and depositing various tax remittances, processing tax returns, maintaining taxpayer records, distributing taxes in accordance with applicable State laws, issuing income tax refunds, and providing assistance to taxpayers. RAD uses the Comptroller of Maryland's automated State of Maryland Tax (SMART) system to record and process tax return information and issue refunds for individual income taxes, as well as for other taxes, such as corporate income taxes, employer withholding taxes, and sales and use taxes. RAD also administers laws and regulations pertaining to the manufacture, storage, transportation, sale, and distribution of alcoholic beverages, tobacco, and motor fuel, and collects the related excise taxes. According to RAD's records, the significant taxes collected (sources greater than \$100 million annually) for fiscal years 2016, 2017, and 2018, are listed in Table 1.

Table 1
Selected Tax Collections and Distributions
Applicable to Fiscal Years 2016 – 2018
(sources greater than \$100 million annually)

	Fiscal Year		
	2016	2017	2018
(dollars stated in millions)			
Gross income taxes collected	<u>\$17,703</u>	<u>\$18,401</u>	<u>\$19,208</u>
Less:			
Refunds	2,811	2,967	2,937
Administrative expenses	17	14	17
Total refunds and expenses	<u>2,828</u>	<u>2,981</u>	<u>2,954</u>
Balance available for distribution	<u>\$14,875</u>	<u>\$15,420</u>	<u>\$16,254</u>
Distribution of remaining balance:			
To State's General Fund	\$9,392	\$9,862	\$10,328
To Local Subdivisions Reserve Fund	5,228	5,351	5,713
To other Funds as provided by State Law (including the Transportation Trust Fund)	255	207	213
Total distributions	<u>\$14,875</u>	<u>\$15,420</u>	<u>\$16,254</u>
Gross sales and use tax collections which are primarily credited to the State's General Fund	<u>\$4,537</u>	<u>\$4,633</u>	<u>\$4,728</u>
Gross motor fuel tax collections which are primarily credited to the Transportation Trust Fund	<u>\$1,085</u>	<u>\$1,128</u>	<u>\$1,126</u>
Gross tobacco tax collections which are primarily credited to the State's General Fund	<u>\$396</u>	<u>\$387</u>	<u>\$373</u>
Gross estate tax collections which are primarily credited to the State's General Fund	<u>\$227</u>	<u>\$190</u>	<u>\$170</u>

Source: RAD Records

Note: Distributions shown relate to the stated fiscal year, but were not necessarily distributed in that year.

Status of Findings From Preceding Audit Reports

Our audit included a review to determine the status of the eight findings contained in our preceding audit report on RAD dated September 16, 2016, and one finding related to cash receipts functions, from our preceding Comptroller of Maryland – Compliance Division report, dated April 10, 2017, that subsequently had been transferred to RAD. As disclosed in the following table, we determined that RAD satisfactorily addressed six of these nine findings. The remaining three findings are repeated in this report.

Table 2
Status of Preceding Findings

Preceding Finding	Finding Description	Implementation Status
Revenue Administration Division		
Finding 1	RAD had not determined the underlying cause(s) for erroneous subdivision codes recorded in SMART for numerous taxpayers in one county, which resulted in \$8.7 million in local income taxes being incorrectly distributed.	Not repeated
Finding 2	RAD lacked sufficient policies and procedures to ensure that all subdivision codes assigned to taxpayers in SMART were proper.	Not repeated
Finding 3	Required documentation was not always on file to support out-of-state tax credits claimed on paper tax returns filed by individual taxpayers.	Not repeated
Finding 4	Significant financial adjustments to corporate taxpayer accounts were not always independently reviewed as required.	Not repeated
Finding 5	Controls were not in place to ensure adjustments to critical taxpayer account information were properly reviewed, and supporting documentation was not always on file.	Not repeated
Finding 6	Certain critical database security and audit events were either not logged or not reviewed for propriety.	Repeated (Current Finding 6)
Finding 7	RAD had not established sufficient controls over remotely deposited checks, and employees with access to collections had the capability to adjust taxpayer accounts.	Repeated (Current Finding 4)
Finding 8	RAD lacked documentation that replacement refund checks were independently reviewed as required.	Not repeated
Compliance Division		
Finding 3	Controls in the cash office were not sufficient to ensure collections were properly accounted for and deposited.	Repeated (Current Finding 5)

Findings and Recommendations

Adjustments to Taxpayer Accounts

Finding 1

An effective process was not in place to ensure that significant financial adjustments made to taxpayer accounts in two units were subject to supervisory or managerial review.

Analysis

The Revenue Administration Division (RAD) did not have an effective process to ensure significant financial adjustments and corrections (collectively “financial adjustments”) made to taxpayer accounts in the Comptroller’s automated State of Maryland Tax (SMART) system were subject to supervisory or managerial review. According to RAD’s records, financial adjustments processed by RAD’s units reduced taxpayer liabilities by a total of \$2.6 billion during the period from July 2015 through September 2018. We found deficiencies with two units that collectively processed approximately \$2.5 billion of these adjustments.

One RAD unit we reviewed did not have formal procedures for supervisory review of significant financial adjustments processed by unit employees. Unit personnel were responsible for reviewing and resolving tax returns that were suspended from processing for various reasons, such as tax return scanning errors or mathematical accuracy errors. Although supervisors in this unit used system output reports of suspended returns to selectively review error corrections processed by unit personnel, this process was ineffective as the output reports did not identify whether each error correction resulted in a financial adjustment and did not identify the value of any financial adjustment. Consequently, unit supervisors were not in a position to identify significant financial adjustments for review. Our test of 12 financial adjustments processed by this unit, each exceeding \$100,000, disclosed that there was no documented supervisory review for any of these adjustments, which collectively reduced taxpayer liabilities recorded in the system by \$371.9 million. According to RAD’s records, during the period from July 2015 through September 2018, this unit processed adjustments that reduced taxpayers’ liabilities recorded in the system by approximately \$900 million.

Financial adjustments processed by the second unit we reviewed were not always reviewed by managerial personnel in accordance with RAD’s established formal procedures. This unit is responsible for processing financial adjustments to taxpayer accounts when, for example, the taxpayer provides previously missing critical documentation that requires an adjustment. RAD’s written procedures for

this unit require managerial review of all adjustments greater than \$250,000, and a supervisory review of selected adjustments below that amount. Our test of 16 financial adjustments processed by this unit, each exceeding \$250,000, which in total reduced taxpayer liabilities by \$388.5 million, disclosed that there was no documentation of the required managerial review for 5 of these adjustments totaling \$123.5 million. According to RAD's records, during the period from July 2015 through September 2018, this unit processed adjustments that reduced taxpayers' liabilities recorded in the system by \$1.6 billion.

Recommendation 1

We recommend that RAD

- a. implement formal written procedures for effectively identifying and reviewing the propriety of significant financial adjustments in all units that process adjustments to taxpayer accounts;**
- b. ensure that significant financial adjustments are reviewed in accordance with established written procedures, and that these reviews are documented; and**
- c. review for propriety the aforementioned 17 adjustments tested that lacked documented supervisory or managerial review.**

Taxpayer Declaration Credits

Finding 2

Declaration credits, representing tax overpayments that taxpayers chose to apply to the next tax year, were not always reviewed for propriety as required.

Analysis

Approximately \$214.4 million in declaration credits, which are tax overpayments that taxpayers chose to apply to the subsequent tax year rather than receive as a tax refund, were not reviewed for propriety by RAD personnel as required. Although RAD's formal procedures require all declaration credits exceeding an established dollar threshold to be reviewed for propriety, RAD personnel reviewed only 284 (\$27.7 million) of the 2,829 (\$242.1 million) credits processed during the period between December 2016 and August 2018 that exceeded the specified dollar threshold. These reviews, that ensure the credits processed are valid, are to include an examination of required taxpayer supporting documentation, which would typically include documentation of a taxpayer's withholdings.

Recommendation 2

We recommend that RAD ensure that taxpayer declaration credits are reviewed in accordance with its established procedures, including those credits processed during the audit period exceeding the established dollar threshold.

Taxpayer Refunds

Finding 3

RAD did not comply with its established review procedures to ensure the propriety of significant individual taxpayer refunds.

Analysis

The process used by RAD employees to conduct required reviews of significant individual taxpayer refunds was not in accordance with established procedures and was not effective to ensure their propriety. Specifically, these reviews of individual taxpayer refunds did not include an examination of certain critical supporting documentation (tax withholdings), as required. According to RAD's records, during March, June, September, and December of 2018 there were 4,169 significant refunds totaling \$90.8 million that required a review for propriety.

RAD management confirmed with us that they did not ensure tax withholdings claimed on the tax returns reviewed agreed with supporting documentation prior to approving the tax refunds, as required. Rather, RAD personnel simply agreed the tax withholding amounts on the tax returns with SMART, which displayed uploaded tax return information. According to RAD's written procedures, withholdings must be verified to supporting documentation prior to the issuance of significant refunds (defined as exceeding a predetermined dollar amount). Our review of 20 significant refunds issued during the period from July 2015 through September 2018, totaling \$37.1 million, disclosed that the refunds appeared to be appropriate based on supporting documentation.

Recommendation 3

We recommend that RAD conduct reviews of individual taxpayer refunds and supporting documentation in accordance with its established written procedures, including refunds issued during our audit period.

Cash Receipts

Background

RAD processed the vast majority of its taxpayer mail-in receipts at its primary location in Annapolis. In addition, RAD operated a cash office in Baltimore, effective February 2014, when the responsibility for the cash office was transferred by the Comptroller of Maryland from its Compliance Division. The Baltimore cash office primarily processed post-return collections that were received either through the mail or as walk-in receipts. Accordingly, our RAD audit included an examination of the operations of the Baltimore cash office. According to RAD's records, cash receipt collections received at the Annapolis office and the Baltimore cash office totaled approximately \$4.3 billion and \$60.4 million, respectively, during fiscal year 2018.

Finding 4

RAD had not established sufficient controls over checks for income tax payments received in the mail at its Annapolis location, as several employees were assigned incompatible functions, and certain documentation used to account for batches of checks processed was not retained.

Analysis

Controls were not sufficient over checks received in the mail at RAD's Annapolis location for the payment of income taxes. Specifically, a number of employees with access to collections could also adjust taxpayer accounts, and certain critical check processing documentation was not retained. Most checks received by RAD for income tax payments are received through the mail. According to RAD's records, mail collections totaled approximately \$4.3 billion during fiscal year 2018, of which \$3.5 billion was for income tax payments.

- Fifteen employees with access to mail collections, of which 12 were responsible for processing the collections, also had the capability to record critical financial adjustments to taxpayer accounts in SMART, such as to reduce a tax liability. Although RAD had a process for the supervisory review of these financial adjustments, only selected transactions were subject to supervisory review and, as previously mentioned (Finding 1), these reviews for certain transactions were not adequate. According to RAD's records, 2 of these 12 employees actually processed adjustments to taxpayer accounts during our audit period and those adjustments totaled approximately \$422 million. A similar condition was commented upon in our preceding audit report.

- RAD did not retain critical documentation used to provide accountability and control over batches of tax returns and checks received in the mail prior to their initial recordation via scanning into RAD's imaging system. While the processed documents and checks were scanned into RAD's imaging system, the batch control sheets were not included in the scanned documents; furthermore, these batch control sheets were destroyed 90 days after the documents and checks were scanned.

The batch control sheets are uniquely numbered and provide documentation of the number and type of tax returns within each batch and whether the batch included associated check receipts. The batched documents and checks were transferred among personnel within several RAD units for processing and the batch control sheets were initialed by each RAD employee until final scanning. Accordingly, the batch control sheets provided a record of the transfer of the documents and checks among RAD personnel and assurance that the collections remained intact until recordation through scanning. In addition, as each scanned tax return is associated with the batch control number in RAD's records, the batch control sheet provided a future reference if needed for taxpayer inquiries.

The Comptroller of Maryland's *Accounting Procedures Manual* requires the establishment of sufficient internal controls over collections, including adequate separation of cash receipt processing duties. Finally, the State Government Article of the Annotated Code of Maryland, Section 10-615 requires State agencies, including RAD, to retain critical documentation relating to their financial operations or collection of State taxes until required and authorized audits have been completed.

Recommendation 4

We recommend that RAD

- a. ensure that employees who have access to collections do not have the capability to record critical adjustments to taxpayer accounts in SMART (repeat), and**
- b. retain copies of batch control sheets to provide accountability and control over tax returns and collections prior to recordation.**

Finding 5

Controls over collections received in the Baltimore cash office were not sufficient to ensure that those collections were properly accounted for and deposited.

Analysis

Controls over collections received in the Baltimore cash office were not sufficient and, as a result, errors or other discrepancies could occur without timely detection.

- Nine RAD employees who worked in the cash office and had access to collections as part of their job duties, also had the capability to record adjustments in taxpayer accounts. Two types of reports of adjustments processed by these individuals were generated each day for required independent supervisory review and approval; however, we noted that the reports were not being consistently retained and reviewed. During our audit period, these nine employees processed adjustments to reduce taxpayer liabilities by \$9.4 million.

Specifically, we requested to review 132 reports for the period from April 2018 to July 2018. For 85 reports, RAD personnel advised us that the reports had not been retained; accordingly, there is a lack of assurance that the adjustments processed on these days had been reviewed as required. In addition, for 17 reports with adjustments, there was no documentation of supervisory review. These 17 reports included adjustments that reduced taxpayer liabilities by \$125,726 and collections recorded in taxpayer accounts by \$32,205. All of these adjustments were made by employees with cash handling responsibilities.

- Adequate verifications were not performed to ensure that all collections received by the Baltimore cash office were deposited with the bank. Although employees at RAD's Annapolis office reconciled the report of remotely deposited checks to the final acceptance by the bank, this reconciliation would not provide assurance that all collections received by the Baltimore cash office were deposited. A similar condition was commented upon in our two preceding audit reports on the Compliance Division.

The Comptroller of Maryland's *Accounting Procedures Manual* requires the establishment of sufficient internal controls over collections, including adequate separation of cash receipt processing duties and independent verification of collections to deposit.

Recommendation 5

We recommend that RAD

- a. ensure that all reports of adjustments processed by employees in the Baltimore cash office are reviewed by supervisory personnel as required, and that documentation of these reviews is retained; and**
- b. ensure that an employee independent of the cash receipts functions verifies that all collections initially recorded in the cash office were deposited (repeat).**

Information Systems Security and Control

Background

RAD supports information systems processing for several key tax systems. The most significant tax systems supported include the systems for the individual and corporate income taxes and the sales and use taxes in the State of Maryland Tax (SMART) system. RAD's centralized automated support for these systems includes processing tax remittances, tax returns, and tax refunds. The automated applications for these systems operate on the Comptroller of Maryland (COM) – Information Technology Division's (ITD) mainframe computer, with security software used as the primary means to protect the applications and related tax data.

Additionally, the SMART system interfaces with RAD's iFile, bFile, and Bill Pay systems. The COM – Information Technology Division operates these Internet based systems that allow individuals to file individual income tax returns (iFile), businesses to file returns for employer withholding taxes and sales and use taxes (bFile), and individuals and businesses to pay taxes (Bill Pay). The iFile, bFile, and Bill Pay systems are three-tiered, consisting of a website tier, an application software tier, and the back-end database tier. The physical servers supporting these systems reside in ITD's Annapolis Data Center computer room.

Finding 6

Security and audit events for several critical databases were either not logged or not reviewed for propriety.

Analysis

For three critical systems, database security and audit events were either not logged or not reviewed for propriety.

- Logging was not enabled for seven user accounts which had the capability to process direct changes to one system's critical database tables. Also, a

security system software report listed instances when direct changes were made to critical database tables such as those involving certain tax information, however, associated detail reporting of related specific change activity did not exist for use, to confirm that the direct changes made to critical tables were proper. A similar condition was commented upon in our two preceding audit reports concerning detailed change reports control weaknesses.

- One system's database security reports of grants and revokes of users' privileges and the assignment of changes to a userid were not reviewed for propriety. A similar condition was commented upon in our preceding audit report.
- Two systems' database security and audit events such as adding and configuring roles of system users and turning off the audit function were not logged even though the capability to perform such logging existed. A similar condition was commented upon in our two preceding audit reports.

These conditions could result in unauthorized or inappropriate activities (affecting the integrity of the production databases' information) going undetected by management.

The State of Maryland *Information Technology Security Manual* requires that information systems must generate audit records for all security-relevant events, and procedures must be developed to routinely (for example real time or weekly) review audit records for indications of inappropriate activities and report findings to appropriate officials for prompt resolution.

Detailed sensitive aspects of this finding were omitted from this report, however the related detailed information was previously shared with RAD for purposes of implementing the following recommendations.

Recommendation 6

We recommend that RAD implement appropriate database monitoring controls over the aforementioned critical tax systems. Specifically, we recommend that RAD

- a. ensure that logging is enabled for all user accounts granted database table level change capabilities;**
- b. ensure that reviews of the propriety of the critical security system software reports include a review of recently developed detail change reports (repeat);**
- c. log all critical database security and audit events (repeat); and**

- d. review all significant database security reports for propriety on a timely basis, document these reviews and retain the reviews for future reference.**

Audit Scope, Objectives, and Methodology

We have conducted a fiscal compliance audit of the Comptroller of Maryland (COM) – Revenue Administration Division (RAD) for the period beginning July 1, 2015 and ending September 20, 2018. The audit was conducted in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

As prescribed by the State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine RAD’s financial transactions, records, and internal control, and to evaluate its compliance with applicable State laws, rules, and regulations.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of significance and risk. The areas addressed by the audit included the processing, evaluating, verifying, and recording of tax data as reported by taxpayers and other parties; the collection of tax receipts; and the distribution of tax refunds. We also determined the status of the findings contained in our preceding audit report on RAD and one finding in our preceding audit report on COM – Compliance Division.

Our audit did not include certain support services provided to RAD by COM – Office of the Comptroller. These support services (such as processing of invoices, maintenance of accounting records, human resources, related fiscal functions, and payroll processing prior to January 1, 2018) are included within the scope of our audits of the Office of the Comptroller. In addition, our audit did not include certain support services provided to RAD by COM – Central Payroll Bureau, effective January 1, 2018. These support services (payroll processing) are included within the scope of our audits of the Central Payroll Bureau since that date. Furthermore, our audit did not include certain support services provided to RAD by COM – Information Technology Division related to the procurement and monitoring of information technology equipment and services and the operation of the Annapolis Data Center. The operation of the Annapolis Data Center includes the development and maintenance of RAD applications and maintenance of the operating system and security software environment. These support services are included in the scope of our audits of the Information Technology Division.

To accomplish our audit objectives, our audit procedures included inquiries of appropriate personnel, inspections of documents and records, observations of RAD's operations, and tests of transactions. Generally, transactions were selected for testing based on auditor judgment, which primarily considers risk. Unless otherwise specifically indicated, neither statistical nor non-statistical audit sampling was used to select the transactions tested. Therefore, the results of the tests cannot be used to project those results to the entire population from which the test items were selected.

We also performed various data extracts of pertinent information from the Comptroller's SMART system for the purpose of testing certain areas, such as tax credits and refunds. We performed various tests of the relevant data and determined that the data were sufficiently reliable for the purposes the data were used during the audit. Finally, we performed other auditing procedures that we considered necessary to achieve our audit objectives. The reliability of data used in this report for background or informational purposes was not assessed.

RAD's management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records; effectiveness and efficiency of operations, including safeguarding of assets; and compliance with applicable laws, rules, and regulations are achieved. As provided in *Government Auditing Standards*, there are five components of internal control: control environment, risk assessment, control activities, information and communication, and monitoring. Each of the five components, when significant to the audit objectives, and as applicable to RAD, were considered by us during the course of this audit.

Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

This report includes findings relating to conditions that we consider to be significant deficiencies in the design or operation of internal control that could adversely affect RAD's ability to maintain reliable financial records, operate effectively and efficiently and/or comply with applicable laws, rules, and

regulations. Our report also includes findings regarding significant instances of noncompliance with applicable laws, rules, or regulations. Other less significant findings were communicated to RAD that did not warrant inclusion in this report. Aspects of certain findings contained in this report address issues of a sensitive nature, and we have omitted that detailed information from this report. However, for the purposes of implementing the related recommendations that information was previously shared with RAD.

The response from COM, on behalf of RAD, to our findings and recommendations is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise COM regarding the results of our review of its response.

APPENDIX



Peter Franchot
Comptroller

May 18, 2020

Mr. Gregory Hook, CPA
Legislative Auditor
Office of Legislative Audits
301 West Preston Street, Room 1202
Baltimore, MD 21201

Dear Mr. Hook:

Enclosed, please find the Revenue Administration Division's (RAD) response to the legislative audit conducted between July 1, 2015 – September 20, 2018.

I want to take this opportunity to thank the Office of Legislative Audits (OLA) for your diligent review of RAD's performance. I am pleased that no occurrences of improper, inaccurate or mistaken allocations were identified in the audit. I take exceeding pride in the work of the RAD and the dedication and professionalism of our outstanding employees.

As you are aware, RAD remains a national leader in efforts to process returns, disburse refunds, and protect taxpayers from tax fraud and identity theft through investments in both personnel and technology. I commend both Maryland General Assembly for their continued partnership in these efforts, and to OLA for identifying opportunities for procedural improvements.

I take the audit findings and recommendations very seriously and pledge to dedicate my full attention and efforts to implement corrections and utilize this opportunity for growth. It is noteworthy that this very thorough and comprehensive audit found no occurrences of inaccurate and inappropriate disbursements of taxpayer dollars. I believe this is testament to the proven policies and procedures that my agency has established and executed over many years.

As always, I appreciate and welcome the audit findings and recommendations from OLA, and look forward to implementing the suggested solutions accordingly.

Sincerely,

A handwritten signature in black ink that reads "Peter Franchot". The signature is written in a cursive, flowing style.

Peter Franchot
Comptroller

**Comptroller of Maryland
Revenue Administration Division**

Agency Response Form

Adjustments to Taxpayer Accounts

Finding 1
An effective process was not in place to ensure that significant financial adjustments made to taxpayer accounts in two units were subject to supervisory or managerial review.

We recommend that RAD

- a. implement formal written procedures for effectively identifying and reviewing the propriety of significant financial adjustments in all units that process adjustments to taxpayer accounts;
- b. ensure that significant financial adjustments are reviewed in accordance with established written procedures, and that these reviews are documented; and
- c. review for propriety the aforementioned 17 adjustments tested that lacked documented supervisory or managerial review.

Agency Response			
Analysis			
Please provide additional comments as deemed necessary.	RAD would like to distinguish that OLA included in the term “financial adjustments” instances where the business rules of our processing system have detected an error which will not allow the return to be processed. As such, these corrections are not strictly financial adjustments as no liability or refund is determined and established until all return errors are resolved.		
Recommendation 1a	Agree	Estimated Completion Date:	5/15/2020
Please provide details of corrective action or explain disagreement.	RAD agrees it will update and enhance its existing written procedures regarding supervisory review of corrections and adjustments to address review of significant financial corrections and adjustments in all RAD units whose staff correct and/or adjust suspended returns and taxpayer accounts.		
Recommendation 1b	Agree	Estimated Completion Date:	5/15/2020
Please provide details of corrective action or explain disagreement.	RAD will ensure that reports are generated to identify significant financial corrections and adjustments requiring supervisory review. RAD will also ensure that managers are monitoring compliance with the updated supervisory review procedures in all RAD units whose staff correct and/or adjust suspended returns and taxpayer accounts as part of our ongoing performance review and will ensure that documentation of the reviews is retained.		

**Comptroller of Maryland
Revenue Administration Division**

Agency Response Form

Recommendation 1c	Agree	Estimated Completion Date:	5/1/2020
Please provide details of corrective action or explain disagreement.	RAD has reviewed for propriety the 17 adjustments tested that lacked documented supervisory review and will retain the supporting documentation. No issues or improprieties were found in the review of these 17 items.		

Taxpayer Declaration Credits

<p>Finding 2 Declaration credits, representing tax overpayments that taxpayers chose to apply to the next tax year, were not always reviewed for propriety as required.</p>
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We recommend that RAD ensure that taxpayer declaration credits are reviewed in accordance with its established procedures, including those credits processed during the audit period exceeding the established dollar threshold.

Agency Response			
Analysis			
Please provide additional comments as deemed necessary.	As noted by OLA, reviews were conducted of declaration credits; however, documentation did not substantiate that all declaration credits exceeding an established dollar threshold were reviewed for propriety.		
Recommendation 2	Agree	Estimated Completion Date:	6/30/2020
Please provide details of corrective action or explain disagreement.	Taxpayer declaration credits will be reviewed in accordance with established procedures and documentation of these reviews will be retained. RAD will document the review of credits that exceeded the threshold during the audit period.		

**Comptroller of Maryland
Revenue Administration Division**

Agency Response Form

Taxpayer Refunds

Finding 3
RAD did not comply with its established review procedures to ensure the propriety of significant individual taxpayer refunds.

We recommend that RAD conduct reviews of individual taxpayer refunds and supporting documentation in accordance with its established written procedures, including refunds issued during our audit period.

Agency Response			
Analysis			
Please provide additional comments as deemed necessary.	As noted by the legislative auditors, RAD has established, written procedures for the review of significant individual taxpayer refunds. These reviews do include an examination of certain critical supporting documentation. The OLA review of 20 significant refunds issued totaling \$37.1 million did not disclose any impropriety and the refunds were considered appropriate based on supporting documentation.		
Recommendation 3	Agree	Estimated Completion Date:	Ongoing
Please provide details of corrective action or explain disagreement.	RAD will ensure that reviews of significant individual taxpayer refunds are performed in compliance with established and existing procedures and appropriate documentation retained.		

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Cash Receipts

Finding 4
RAD had not established sufficient controls over checks for income tax payments received in the mail at its Annapolis location, as several employees were assigned incompatible functions, and certain documentation used to account for batches of checks processed was not retained.

We recommend that RAD

- a. ensure that employees who have access to collections do not have the capability to record critical adjustments to taxpayer accounts in SMART (repeat), and**
- b. retain copies of batch control sheets to provide accountability and control over tax returns and collections prior to recordation.**

Agency Response			
Analysis			
Please provide additional comments as deemed necessary.	RAD wishes to note that in OLA’s comprehensive review on this issue, there was no evidence of impropriety or loss of revenue associated with this finding.		
Recommendation 4a	Agree	Estimated Completion Date:	Ongoing
Please provide details of corrective action or explain disagreement.	In concurrence with this recommendation, RAD will limit access where practical. It must be noted that in order to efficiently process tax forms during certain times, some employees with the ability to post critical adjustments to taxpayer accounts may be assigned temporary access to collections. During these limited times, the access to post critical adjustments will be restricted. In addition, RAD policy requires supervisory review of financial adjustments recorded in SMART which therefore limits the exposure to potential misappropriation and corresponding adjustment to a taxpayer’s account. Accordingly, we believe that these actions will ensure adequate control.		
Recommendation 4b	Agree	Estimated Completion Date:	12/31/2019
Please provide details of corrective action or explain disagreement.	RAD will retain copies of batch control sheets to provide accountability and control over tax returns and collections prior to recordation.		

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Finding 5
Controls over collections received in the Baltimore cash office were not sufficient to ensure that those collections were properly accounted for and deposited.

We recommend that RAD

- a. ensure that all reports of adjustments processed by employees in the Baltimore cash office are reviewed by supervisory personnel as required, and that documentation of these reviews is retained; and
- b. ensure that an employee independent of the cash receipts functions verifies that all collections initially recorded in the cash office were deposited (repeat).

Agency Response			
Analysis			
Please provide additional comments as deemed necessary.	RAD wishes to note that in the comprehensive review on this issue by OLA, there was no evidence of impropriety or loss of revenue associated with this finding. The nature of a branch office includes being able to provide full and complete service to taxpayers and tax preparers to ensure compliance with the tax laws of the State of Maryland as applicable to the Comptroller's Office. This included employees being able to adjust taxpayer accounts in order to resolve issues. However, we have now modified taxpayer services by completely removing employee adjustment capability.		
Recommendation 5a	Agree	Estimated Completion Date:	2/1/2020
Please provide details of corrective action or explain disagreement.	Adjustment capabilities have been removed from all employees in the Baltimore Branch Office as well as in all other Branch offices effective 02/01/2020		
Recommendation 5b	Agree	Estimated Completion Date:	2/1/2020
Please provide details of corrective action or explain disagreement.	The branch office staff is reconciling both the total number of checks received and the total dollar amounts of each batch of checks (by reconciling the "daily transmittal report" with the "batch status report"); this ensures that the total amounts were successfully transmitted to the Annapolis deposit unit for final processing for deposit. Both the payment processing assistant manager and the branch office manager verify the reconciliation of each payment transmittal batch.		

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Agency Response Form

Information Systems Security and Control

Finding 6
Security and audit events for several critical databases were either not logged or not reviewed for propriety.

We recommend that RAD implement appropriate database monitoring controls over the aforementioned critical tax systems. Specifically, we recommend that RAD

- a. ensure that logging is enabled for all user accounts granted database table level change capabilities;
- b. ensure that reviews of the propriety of the critical security system software reports include a review of recently developed detail change reports (repeat);
- c. log all critical database security and audit events (repeat); and
- d. review all significant database security reports for propriety on a timely basis, document these reviews and retain the reviews for future reference.

Agency Response			
Analysis			
Please provide additional comments as deemed necessary.	<p>The Comptroller takes pride in the agency’s strong commitment to ensuring that its databases and networks are secure, which was reinforced by the fact that OLA found no security breaches within the agency’s IT system. Our IT division continues to prioritize the modernization of our network of firewalls, security appliances, intrusion detection and prevention programs, and Internet access control procedures. Protecting taxpayer data and combatting taxpayer identity fraud are two major goals for the agency. As such, the agency is committed to ensuring that its IT systems are compliant with all federal and state requirements and continues to audit and manage risks associated with threats to its core systems and processes.</p> <p>We agree with the overall finding and have completed implementation of processes to respond to all four recommendations.</p>		
Recommendation 6a	Agree	Estimated Completion Date:	4/20/2020
Please provide details of corrective action or explain disagreement.	Logging of all user accounts is active and has always been the default of our database systems.		

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Recommendation 6b	Agree	Estimated Completion Date:	4/20/2020
Please provide details of corrective action or explain disagreement.	Reviews of legacy reports were being performed on a daily basis prior to the audit and will continue; reviews of a new detailed report on table changes are now performed on a daily basis as well.		
Recommendation 6c	Agree	Estimated Completion Date:	4/20/2020
Please provide details of corrective action or explain disagreement.	Logging of all security and audit events is active and has always been the default of our database systems.		
Recommendation 6d	Agree	Estimated Completion Date:	4/20/2020
Please provide details of corrective action or explain disagreement.	All reviews of prior security reports and the newly established one are performed on a daily basis. The review is documented daily and scanned for retention.		

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