

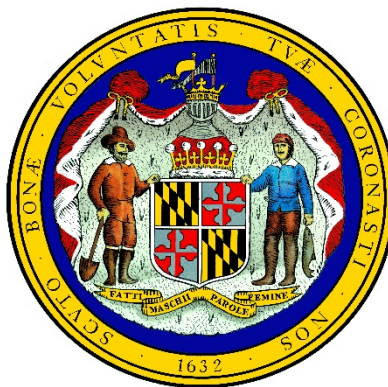
Audit Report

Comptroller of Maryland Revenue Administration Division

January 2024

Public Notice

In compliance with the requirements of the State Government Article Section 2-1224(i), of the Annotated Code of Maryland, the Office of Legislative Audits has redacted cybersecurity findings and related auditee responses from this public report.



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DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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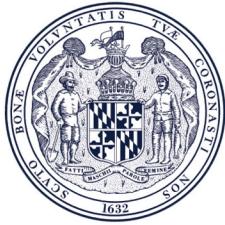
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Victoria L. Gruber
Executive Director

DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Gregory A. Hook, CPA
Legislative Auditor

January 22, 2024

Senator Clarence K. Lam, M.D., Senate Chair, Joint Audit and Evaluation Committee
Delegate Jared Solomon, 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 September 21, 2018 and ending September 30, 2021. 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 did not conduct all required reviews of tax overpayments that taxpayers chose to apply to the next tax year, which for two tax types not reviewed totaled approximately \$1.2 billion between December 2018 and July 2021; and although reviews were performed for a third tax type, they were not sufficiently comprehensive. Furthermore, RAD did not ensure that refund replacement checks issued, which totaled approximately \$29.5 million in calendar year 2021, were reviewed by supervisory personnel as required.

We also noted that RAD did not ensure that current records of deceased individuals, which are used to help ensure that fraudulent or otherwise improper tax returns and refunds are not processed, were regularly loaded into the COM's automated State of Maryland Tax (SMART) system, which RAD uses for processing returns and refunds. In addition, RAD had not determined the cost benefit of expanding the use of its current individual taxpayer data analytics vendor to help identify corporate and business tax fraud.

We also noted a lack of control over certain checks received. Finally, our audit also disclosed certain cybersecurity-related findings. However, in accordance with the State Government Article, Section 2-1224(i) of the Annotated Code of Maryland, we have redacted the findings from this audit report. Specifically,

State law requires the Office of Legislative Audits to redact cybersecurity findings in a manner consistent with auditing best practices before the report is made available to the public. The term “cybersecurity” is defined in the State Finance and Procurement Article, Section 3.5-301(b), and using our professional judgment we have determined that the redacted findings fall under the referenced definition. The specifics of the cybersecurity findings were previously communicated to those parties responsible for acting on our recommendations.

Our audit also included a review to determine the status of the six findings contained in our preceding audit report on RAD. For the non-cybersecurity-related findings we determined that RAD satisfactorily addressed three of those five findings. The remaining two 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 agreement to our findings and related recommendations and while there are other aspects of the response which will require further clarification, we do not anticipate that these will require the Joint Audit and Evaluation Committee’s attention to resolve. Additionally, in accordance with our policy, we have edited COM’s response to remove vendor names or products. Finally, consistent with State law, we have redacted the elements of COM’s response related to the cybersecurity audit findings.

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, flowing style.

Gregory A. Hook, CPA
Legislative Auditor

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* Denotes item repeated in full or part from preceding audit report

Background Information

Agency Responsibilities

The primary responsibilities of the Comptroller of Maryland's (COM) 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 also administers certain laws and regulations pertaining to the dispensing and content of motor fuel and collects excise taxes for motor fuel, alcoholic beverages, and tobacco.¹

Our office conducts separate fiscal compliance audits of other COM units. A listing of the most recent fiscal compliance audits of COM units performed during the current audit cycle can be found in Exhibit 1 of this report.

Financial Activities

According to RAD's records, significant taxes collected (sources greater than \$100 million annually) for fiscal years 2019, 2020, and 2021, are listed in Figure 1. According to the State's records, during fiscal year 2022, RAD's expenditures totaled approximately \$60.7 million (See Figure 2).

¹ Previously, RAD also administered laws and regulations pertaining to the manufacture, storage, transportations, sale, and distribution of alcoholic beverages and tobacco. However, effective January 1, 2021 all such functions were to be performed by the newly established independent Alcohol and Tobacco Commission. Effective May 3, 2023, Chapter 255, Laws of Maryland 2023 renamed the Alcohol and Tobacco Commission as the Alcohol, Tobacco, and Cannabis Commission.

Figure 1
Selected Tax Collections and Distributions
Applicable to Fiscal Years 2019 – 2021
(sources greater than \$100 million annually)

	Fiscal Year (dollars stated in millions)		
	<u>2019</u>	<u>2020</u>	<u>2021</u>
Gross income taxes collected	<u>\$20,504</u>	<u>\$21,430</u>	<u>\$23,994</u>
Less:			
Refunds	2,786	2,843	2,941
Administrative expenses	<u>21</u>	<u>24</u>	<u>27</u>
Total refunds and expenses	<u>2,807</u>	<u>2,867</u>	<u>2,968</u>
Balance available for distribution	<u>\$17,697</u>	<u>\$18,563</u>	<u>\$21,026</u>
Distribution of remaining balance:			
To State's General Fund	\$11,105	\$11,751	\$13,167
To Local Subdivisions Reserve Fund	6,123	6,539	7,480
To other Funds as provided by State Law (including the Transportation Trust Fund)	<u>469</u>	<u>273</u>	<u>379</u>
Total distributions	<u>\$17,697</u>	<u>\$18,563</u>	<u>\$21,026</u>
Gross sales and use tax collections which are primarily credited to the State's General Fund	<u>\$4,902</u>	<u>\$4,969</u>	<u>\$5,471</u>
Gross motor fuel tax collections which are primarily credited to the Transportation Trust Fund	<u>\$1,182</u>	<u>\$1,122</u>	<u>\$1,061</u>
Gross tobacco tax collections which are primarily credited to the State's General Fund	<u>\$357</u>	<u>\$363</u>	<u>\$388</u>
Gross estate tax collections which are primarily credited to the State's General Fund	<u>\$138</u>	<u>\$150</u>	<u>\$192</u>

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

Figure 2
RAD Positions, Expenditures, and Funding Sources

Full Time Equivalent Positions as of June 30, 2022		
	Positions	Percent
Filled	341	90.4%
Vacant	36	9.6%
Total	377	
Fiscal Year 2022 Expenditures		
	Expenditures	Percent
Salaries, Wages and Fringe Benefits	\$ 31,292,852	51.5%
Technical and Special Fees	1,083,886	1.8%
Operating Expenses	28,327,318	46.7%
Total	\$ 60,704,056	
Fiscal Year 2022 Funding Sources		
	Funding	Percent
General Fund	\$ 33,516,298	55.2%
Special Fund	14,172,833	23.3%
Reimbursable Fund	13,014,925	21.5%
Total	\$ 60,704,056	

Source: State financial and personnel records

System Implementation

RAD has historically used COM's automated State of Maryland Tax (SMART) system to record and process tax return information and issue refunds for corporate and individual income taxes, as well as for other taxes, such as employer withholding taxes, and sales and use taxes. In fiscal year 2018, with the assistance of the Maryland Department of Information Technology, COM's Office of the Comptroller initiated a competitive procurement for an information technology modernization project to replace SMART. In December 2018, the Board of Public Works approved a ten-year contract, with one additional five-year option and a cumulative value of approximately \$159.7 million, with a primary vendor² to implement the Revenue Premier Enterprise system, referred to as COMPASS. In addition to replacing the current functionality of SMART,

² Other vendors are associated with the project to perform specific tasks such as oversight and consulting, the "primary vendor" is responsible for system design.

COMPASS is intended to improve automation of business processes and best practices, create a taxpayer interface to allow for more timely and direct communication, and provide additional fraud detection capabilities for RAD. COMPASS will be implemented in three phases or Releases, with all Releases anticipated to be completed by July 2024 (See Exhibit 2). RAD transitioned to COMPASS for alcohol taxes and corporate taxes in July 2020 and February 2021, respectively, as Release 1 of the implementation. During calendar year 2021 revenues processed in COMPASS for the aforementioned two tax types totaled approximately \$2.4 billion. As of May 2022, the vendor had been paid \$51.8 million.

Pass-Through Entity (PTE) Credit Processing Delays

Subsequent to completion of our fieldwork, we received an allegation through our fraud, waste, and abuse hotline of taxpayers experiencing extensive delays in receiving refunds claimed on personal income tax returns that included a PTE credit. State law provides that a member of a PTE, such as a partner in a partnership, may claim a credit on their personal income tax return for taxes paid by the PTE attributable to the member's share of the PTE's taxable income.

Accompanying the aforementioned allegation was a September 19, 2023 letter to tax professionals from the Office of the Comptroller acknowledging challenges in processing returns claiming the PTE credit, attributing delays to the complexity of returns filed, lack of staff, and outdated technology. The letter outlined the steps being taken and the progress being made to address these challenges and delays, as well steps that tax professionals can take to help expedite return processing.

Upon our inquiries, RAD advised us in October 2023 that the majority of the outstanding credits had been resolved. We attempted to obtain detailed documentation to support the number of returns with PTE credits received and the applicable tax returns not yet processed for calendar year 2021. However, RAD was unable to provide us with the requested information prior to the issuance of this report and as such, we were unable to determine the disposition of the PTE credits to determine the veracity and disposition of the allegation. Consequently, we will pursue the matter once the information is obtained and will disclose the results of our review at a later date.

Status of Findings From Preceding Audit Report

Our audit included a review to determine the status of the six findings contained in our preceding audit report dated June 1, 2020. As disclosed in Figure 3, for the non-cybersecurity-related findings, we determined that RAD satisfactorily addressed three of these five findings. The remaining two findings are repeated in this report.

Figure 3
Status of Preceding Findings

Preceding Finding	Finding Description	Implementation Status
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.	Not repeated
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.	Repeated (Current Finding 1)
Finding 3	RAD did not comply with its established review procedures to ensure the propriety of significant individual taxpayer refunds.	Not repeated
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.	Repeated (Current Finding 7)
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.	Not repeated
Finding 6	Security and audit events for several critical databases were either not logged or not reviewed for propriety.	Status Redacted ³

³ Specific information on the current status of this cybersecurity-related finding has been redacted from the publicly available report in accordance with State Government Article, Section 2-1224(i) of the Annotated Code of Maryland.

Findings and Recommendations

Taxpayer Refunds

Finding 1

The Revenue Administration Division (RAD) did not conduct all required reviews of declaration credits (tax overpayments that taxpayers chose to apply to the next tax year) and the reviews performed were not sufficiently comprehensive.

Analysis

Required reviews of declaration credits (which are tax overpayments that taxpayers chose to apply to the subsequent tax year rather than receive as a tax refund) were either not performed or were not sufficient to ensure that the credit was valid. RAD procedures require all declaration credits exceeding an established dollar threshold to be reviewed for propriety. However, our review disclosed that declaration credits for corporate and fiduciary tax returns, which totaled approximately \$1.2 billion between December 2018 and July 2021, were not reviewed, and credits for individual tax returns were not reviewed for tax year 2020.⁴

Furthermore, although declaration credits for individual tax returns were reviewed for tax years 2018 and 2019, the number of credits reviewed was less than the total required by RAD policy, and the reviews were not sufficiently comprehensive. Specifically, RAD only reviewed 221 credits totaling \$3.7 million of the 5,511 totaling \$513.2 million that should have been reviewed for tax years 2018 and 2019. In addition, the reviews that were conducted did not include an examination of required supporting documentation, such as taxpayer's withholdings from their W-2 forms. Rather, the review used uploaded taxpayer prepared return data already in SMART for verification purposes, which would not provide an independent verification of the data.

These reviews are meant to ensure that declaration credits processed are valid and are to include an examination of required taxpayer supporting documentation, which would typically include required documentation of a taxpayer's withholdings and credits. Comments regarding the lack of a sufficient number of reviews for individual tax returns were included in our preceding audit report. In its response to that report, the Comptroller of Maryland, on behalf of RAD, stated that effective June 2020, taxpayer declaration credits would be reviewed in accordance with established procedures and documentation of these reviews

⁴ The latest year in which reviews could have been performed as of the time of our audit.

would be retained. During our current audit RAD management advised that the aforementioned corrective actions were not fully implemented because staff was working on other activities.

Recommendation 1

We recommend that RAD

- a. conduct required reviews of declaration credits for individual (repeat), corporate, and fiduciary tax returns; and**
- b. ensure that the reviews include a review of critical supporting documentation, such as documentation of a taxpayer's withholdings.**

Finding 2

RAD did not ensure that refund replacement checks, which totaled \$29.5 million during calendar year 2021, were reviewed by supervisory personnel as required by its policy.

Analysis

Refund replacement checks processed in calendar year 2021 totaling \$29.5 million were not subjected to supervisory review as required by RAD's policy. Replacement checks are generated for several reasons, including when an original refund check is returned by a taxpayer due to an error, a taxpayer claims to have not received their refund check, or the taxpayer has passed away. RAD's policy requires that supervisors use weekly output reports of replacement checks to select refunds for review within 30 days of the report. RAD's policy also requires that on a monthly basis, management personnel ensure that the supervisory reviews were performed and verify that high dollar refunds were proper.

Our test of replacement checks issued in calendar year 2021 disclosed that, as of March 2022, no supervisory reviews had been performed for checks issued during 45 of the 52 weeks totaling approximately \$29.5 million, and the reviews of checks for the other 7 weeks totaling approximately \$3.3 million were performed between 1 and 9 months late. In addition, the required monthly management reviews were not performed. Upon our inquiry in April 2022, RAD began performing the missing calendar year 2021 supervisory and management reviews.

Recommendation 2

We recommend that RAD ensure that all supervisory and management reviews of replacement refund checks are performed as required, including those noted above.

Data Matches

Finding 3

RAD did not ensure that current death records were obtained and loaded into the Comptroller of Maryland's automated State of Maryland Tax (SMART) system, resulting in potential improper tax returns and refunds going undetected.

Analysis

RAD lacked assurance that monthly death records used to help identify improper tax returns and refunds had been obtained and loaded into SMART, and our review disclosed five months in 2020 for which this data was not obtained. RAD obtained national death records from the National Technical Information Service on a monthly basis and uploaded them into SMART to help identify potentially fraudulent or otherwise improper tax returns and refunds. Although RAD policy required supervisory personnel to verify that the monthly death records were received and uploaded, we found there was no documentation supporting that the verifications were performed during the audit period. For at least five months we determined that the verifications were not performed, which contributed to the five months of missing records remaining undetected.

Specifically, we noted that the death records from May 2020 through September 2020 had not been obtained and uploaded into SMART. RAD was not aware that the records were not obtained and uploaded (evidencing the lack of a verification) until we brought the matter to its attention in September 2022. The failure to obtain the death records is significant because during tax year 2021, the death matches resulted in tax returns claiming refunds of approximately \$18.4 million being suspended for further investigation.

Recommendation 3

We recommend that RAD

- a. ensure that required supervisory reviews of monthly data uploads are performed and documented, and**
- b. obtain the missing death records and match the data to tax returns and refunds claimed since May 2020 to identify potentially improper returns and claims.**

Data Analytics for Fraud Detection

Finding 4 (Policy Issue)

RAD did not determine the cost benefit of expanding the use of its existing individual taxpayer data analytics vendor to help identify corporate and business tax fraud.

Analysis

RAD did not determine the cost benefit of using its data analytics vendor to help identify fraud beyond individual tax returns such as corporate and business returns. RAD contracted with a vendor to assist with fraud detection using complex algorithms based on historical fraudulent return information and continual machine learning of individual tax returns deemed fraudulent. Individual tax returns with high indicators of fraud based on these analytics are reviewed by RAD for propriety. During calendar year 2021, the contractor identified approximately 78,000 individual tax returns warranting further investigation, of which 6,499 associated with \$13.2 million in refunds were determined by RAD to be potentially fraudulent.

Our review disclosed that RAD did not consider using the vendor for other types of returns such as corporate, business, pass-through entities, and employer withholding tax; although we confirmed that the vendor provides such services to other states. During fiscal year 2021, State tax revenues related to these tax sources totaled approximately \$18.1 billion. RAD management advised us that they did not use the vendor for these returns because it would cost more, but could not provide us with a cost benefit analysis to support its decision. Given the results the vendor has had with individual returns, we believe RAD should determine the cost benefit of using data analytics for other tax returns.

Recommendation 4

We recommend that RAD determine the cost benefit of expanding its current use of its data analytics for other types of tax returns.

SMART

We determined that Finding 5 related to “cybersecurity”, as defined by the State Finance and Procurement Article, Section 3.5-301(b) of the Annotated Code of Maryland, and therefore is subject to redaction from the publicly available audit report in accordance with the State Government Article 2-1224(i). Consequently, the specifics of the following finding, including the analysis, related recommendation(s), along with COM’s responses, have been redacted from this report copy.

Finding 5
Redacted cybersecurity-related finding.

COMPASS

We determined that Finding 6 related to “cybersecurity”, as defined by the State Finance and Procurement Article, Section 3.5-301(b) of the Annotated Code of Maryland, and therefore is subject to redaction from the publicly available audit report in accordance with the State Government Article 2-1224(i). Consequently, the specifics of the following finding, including the analysis, related recommendation(s), along with COM’s responses, have been redacted from this report copy.

Finding 6
Redacted cybersecurity-related finding.

Cash Receipts

Finding 7
RAD had not established sufficient controls over checks for tax payments received in the mail at its Annapolis location, as certain documentation used to account for batches of checks processed was not retained prior to May 2021.

Analysis

Critical documentation used to maintain accountability and control over checks received by RAD through the mail at its Annapolis location, which constituted most of the tax payments received by RAD, were either not retained prior to May 2021 or were not reviewed for propriety. Consequently, there was an increased

risk that checks could be misappropriated without detection. According to RAD's records, Annapolis mail collections totaled approximately \$5.6 billion during fiscal year 2021, which accounted for the majority of payments received by RAD.

Our review disclosed that RAD did not retain batch control sheets 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. A similar condition was commented upon in our preceding audit report. In response to that report, RAD stated that batch control sheets would be retained starting in January 2020, but RAD did not begin retaining the documents until May 2021. Furthermore, even when batch control sheets were retained, subsequent adjustments to the control sheets were made without explanation. Our review of 42 batch control sheets maintained from July 2021 through September 2021 disclosed that 17 batches had a total of 282 adjustments, such as the removal of checks, without any explanation or support.

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 provide a record of the transfer of the documents and checks among RAD personnel and provide assurance that the collections remained intact until recordation into SMART occurs via the scanning of the checks. In addition, as each scanned tax return is associated with the batch control number in RAD's records, the batch control sheet provides a future reference if needed for taxpayer inquiries.

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 7

We recommend that RAD

- a. retain copies of batch control sheets to provide accountability and control over tax returns and collections prior to recordation (repeat), and**
- b. retain support for any adjustments made to batch control sheets.**

Information Systems Security and Control

We determined that the Information Systems Security and Control section, including Findings 8 and 9 related to “cybersecurity”, as defined by the State Finance and Procurement Article, Section 3.5-301(b) of the Annotated Code of Maryland, and therefore are subject to redaction from the publicly available audit report in accordance with the State Government Article 2-1224(i). Consequently, the specifics of the following findings, including the analysis, related recommendations, along with COM’s responses, have been redacted from this report copy.

Finding 8
Redacted cybersecurity-related finding.

Finding 9
Redacted cybersecurity-related finding.

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 September 21, 2018 and ending September 30, 2021. 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; the issuance of tax refunds; and information technology systems. We also determined the status of the findings contained in our preceding audit report.

Our audit did not include certain support services provided to RAD by COM – Office of the Comptroller. These support services (such as procurement, processing of invoices, maintenance of accounting records, human resources, and related fiscal functions) are included within the scope of our audit of the Office of the Comptroller. In addition, our audit did not include certain support services provided to RAD by COM – Central Payroll Bureau. These support services (payroll processing) are included within the scope of our audit of the Central Payroll Bureau. Furthermore, our audit did not include certain support services provided to RAD by COM – Information Technology Division related to the 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 audit of the Information Technology Division.

Our assessment of internal controls was based on agency procedures and controls in place at the time of our fieldwork. Our tests of transactions and other auditing

procedures were generally focused on the transactions occurring during our audit period of September 21, 2018 to September 30, 2021, but may include transactions before or after this period as we considered necessary to achieve our audit objectives.

To accomplish our audit objectives, our audit procedures included inquiries of appropriate personnel, inspections of documents and records, tests of transactions, and to the extent practicable, observations of RAD's operations. Generally, transactions were selected for testing based on auditor judgment, which primarily considers risk, the timing or dollar amount of the transaction, or the significance of the transaction to the area of operation reviewed. As a matter of course, we do not normally use sampling in our tests, so unless otherwise specifically indicated, neither statistical nor non-statistical audit sampling was used to select the transactions tested. Therefore, unless sampling is specifically indicated in a finding, the results from any tests conducted or disclosed by us cannot be used to project those results to the entire population from which the test items were selected.

We performed various data extracts of pertinent information from the State's Financial Management Information System (such as revenue data). The extracts are performed as part of ongoing internal processes established by the Office of Legislative Audits and were subject to various tests to determine data reliability. We determined that the data extracted from this source were sufficiently reliable for the purposes the data were used during this audit. We also extracted data from RAD's systems for the purpose of testing certain areas, such as refund activity. 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. Finally, this report includes a finding, which is identified as a "Policy Issue". Such findings represent significant operational or financial-related issues for which formal criteria may not necessarily exist, and for which management has significant discretion in addressing, but the recommendation represents prudent and or practical actions, which we believe should be implemented by the agency to improve outcomes. Other less significant findings were communicated to RAD that did not warrant inclusion in this report.

State Government Article Section 2-1224(i) requires that we redact in a manner consistent with auditing best practices any cybersecurity findings before a report is made available to the public. This results in the issuance of two different versions of an audit report that contains cybersecurity findings – a redacted version for the public and an unredacted version for government officials responsible for acting on our audit recommendations.

The State Finance and Procurement Article, Section 3.5-301(b), states that cybersecurity is defined as "processes or capabilities wherein systems, communications, and information are protected and defended against damage, unauthorized use or modification, and exploitation." Based on that definition, and in our professional judgment, we concluded that certain findings in this report fall under that definition. Consequently, for the publicly available audit report all specifics as to the nature of cybersecurity findings and required corrective actions have been redacted. We have determined that such aforementioned practices, and government auditing standards, support the redaction of this information from the public audit report. The specifics of these cybersecurity findings have been

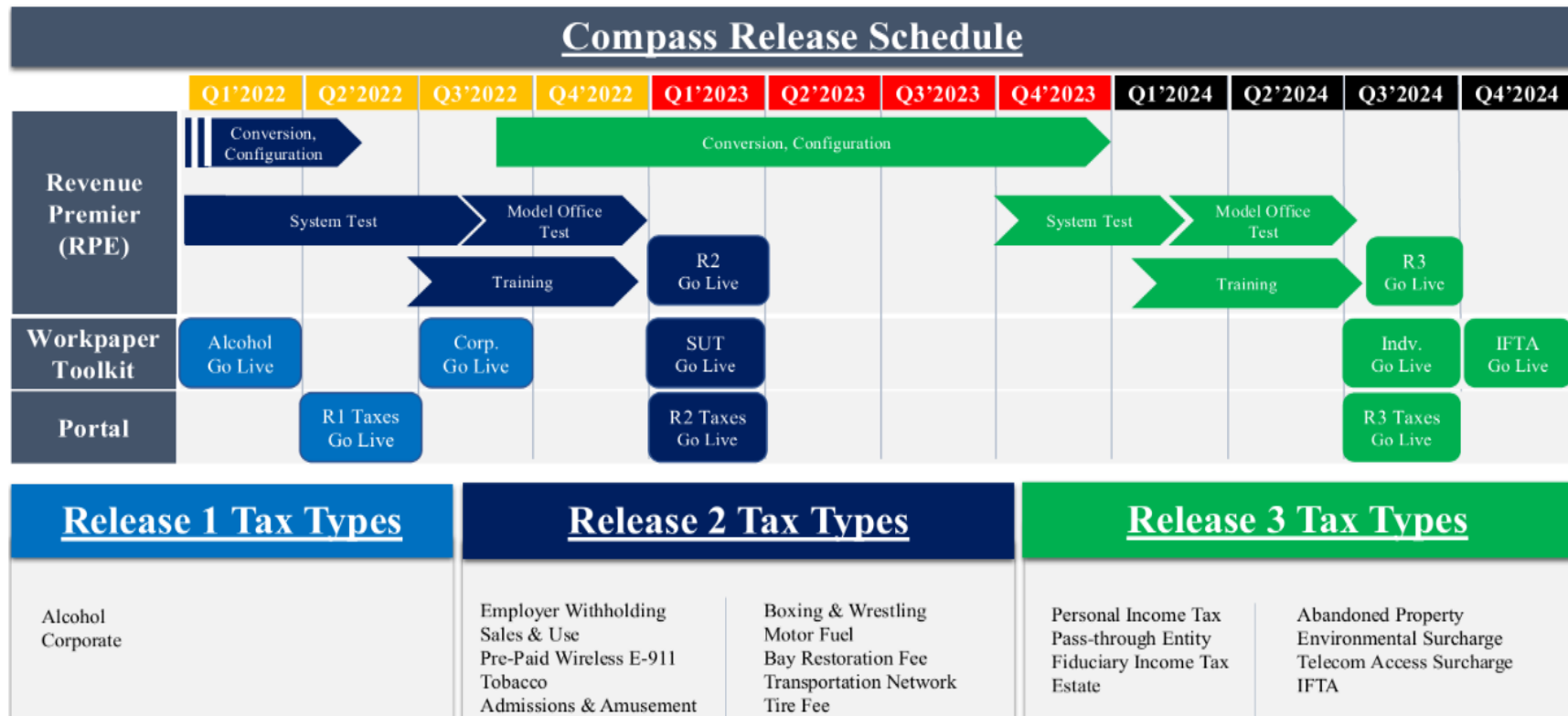
communicated to RAD and those parties responsible for acting on our recommendations in an unredacted audit report.

The response from COM, on behalf of RAD, to our findings and recommendations is included as an appendix to this report. Depending on the version of the audit report, responses to any cybersecurity findings may be redacted in accordance with State law. 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.

Exhibit 1
Listing of Most Recent Office of Legislative Audits
Fiscal Compliance Audits of Comptroller of Maryland Divisions
As of October 2023

Name of Audit		Areas Covered	Most Recent Report Date
1	Central Payroll Bureau	<ul style="list-style-type: none"> • Management of the State payroll system • Non-budgeted funds maintained for payroll deductions • Critical information systems • Support services to other units of the Comptroller for processing payroll timekeeping records 	10/05/23
2	Information Technology Division (Fiscal Operations)	<ul style="list-style-type: none"> • Procurement • Equipment • Support services to other units of the Comptroller for monitoring information technology related services and maintaining information technology equipment inventory records 	02/02/22
3	Field Enforcement Bureau	<ul style="list-style-type: none"> • Confiscated Property • Business licenses • Routine Inspections 	09/07/21
4	Compliance Division	<ul style="list-style-type: none"> • Investigations, collection of delinquent taxes, and other taxpayer compliance activities related to individual income taxes • Audits and investigations, collection of delinquent taxes, and other taxpayer compliance activities related to business taxes • Identification, collection, and distribution of unclaimed property 	12/18/20
5	General Accounting Division	<ul style="list-style-type: none"> • State agency vendor payment processing • Vendor table maintenance • State agency working funds • Corporate purchasing card program 	11/09/20
6	Information Technology Division – Annapolis Data Center Operations	<ul style="list-style-type: none"> • Maintenance and monitoring of mainframe operating system, various security functions, and critical databases 	07/27/20
7	Office of the Comptroller Bureau of Revenue Estimates	<ul style="list-style-type: none"> • Capital grants monitoring • Procurement and disbursements • Corporate Purchasing cards • Support services to other divisions of the Comptroller, such as processing invoices, maintenance of accounting records, human resources, and related fiscal functions 	08/29/19

Exhibit 2 Compass Release Schedule





COMPTROLLER of MARYLAND

Brooke E. Lierman
Comptroller

Andrew Schaufele
Chief Deputy Comptroller

January 12, 2024

Mr. Gregory A. Hook, CPA, Legislative Auditor
300 West Preston Street
Room 1202
Baltimore, Maryland 21201

Dear Mr. Hook:

Enclosed is the Comptroller's response to your report on the Revenue Administration Division for the period beginning September 21, 2018 and ending September 30, 2021.

We have carefully reviewed each finding, and we believe that our responses fully address each recommendation contained in the report. Should you need additional information or clarification, please contact David Hildebrand, Director, Office of Risk Management by email at dhildebr@marylandtaxes.gov or by telephone at 410-260-7768.

The Comptroller appreciates your objective appraisal of our operations and your recommendations for continuous improvement and commends your auditors for their professionalism and thorough review.

Sincerely,

Andrew M. Schaufele

Chief Deputy Comptroller

Robert R. Scheerer

Director, Revenue Administration Division

Cc: Honorable Brooke Elizabeth Lierman, Comptroller



**Comptroller of Maryland
Revenue Administration Division**

Agency Response Form

Taxpayer Refunds

Finding 1

The Revenue Administration Division (RAD) did not conduct all required reviews of declaration credits (tax overpayments that taxpayers chose to apply to the next tax year) and the reviews performed were not sufficiently comprehensive.

We recommend that RAD

- a. conduct required reviews of declaration credits for individual (repeat), corporate, and fiduciary tax returns; and**
- b. ensure that the reviews include a review of critical supporting documentation, such as documentation of a taxpayer's withholdings.**

Agency Response			
Analysis			
Please provide additional comments as deemed necessary.	Point of clarification, the terminology is “over credit” not a declaration credit		
Recommendation 1a	Agree	Estimated Completion Date:	01/2024
Please provide details of corrective action or explain disagreement.	RAD will conduct the reviews in accordance with procedures established that utilizes a query from the Data Warehouse		
Recommendation 1b	Agree	Estimated Completion Date:	07/2022
Please provide details of corrective action or explain disagreement.	RAD will continue to rely on W-2 information loaded into the system when businesses submit their annual MW-508 reconciliation each year. We perform a cursory review of this process to verify accuracy		

**Comptroller of Maryland
Revenue Administration Division**

Agency Response Form

Finding 2

RAD did not ensure that refund replacement checks, which totaled \$29.5 million during calendar year 2021, were reviewed by supervisory personnel as required by its policy.

We recommend that RAD ensure that all supervisory and management reviews of replacement refund checks are performed as required, including those noted above.

Agency Response			
Analysis			
Please provide additional comments as deemed necessary.			
Recommendation 2	Agree	Estimated Completion Date:	06/30/22
Please provide details of corrective action or explain disagreement.	All reviews will be completed on refund replacement checks per procedures. Calendar year review of 2021 items was completed in June 2022.		

**Comptroller of Maryland
Revenue Administration Division**

Agency Response Form

Data Matches

Finding 3

RAD did not ensure that current death records were obtained and loaded into the Comptroller of Maryland's automated State of Maryland Tax (SMART) system, resulting in potential improper tax returns and refunds going undetected.

We recommend that RAD

- a. ensure that required supervisory reviews of monthly data uploads are performed and documented, and**
- b. obtain the missing death records and match the data to tax returns and refunds claimed since May 2020 to identify potentially improper returns and claims.**

Agency Response			
Analysis			
Please provide additional comments as deemed necessary.			
Recommendation 3a	Agree	Estimated Completion Date:	05/23/2023
Please provide details of corrective action or explain disagreement.	Monthly uploads are now confirmed and documented by RAD's Project Management Office as an additional step in the procedure.		
Recommendation 3b	Agree	Estimated Completion Date:	01/2024
Please provide details of corrective action or explain disagreement.	The Death Master File is uploaded monthly currently. We submitted a request to obtain a cumulative file but have yet to receive a response. Should we receive a response we will determine if there is a benefit to retroactively match the missing uploads from May 2020 through September 2020.		

**Comptroller of Maryland
Revenue Administration Division**

Agency Response Form

Data Analytics for Fraud Detection

Finding 4 (Policy Issue)

RAD did not determine the cost benefit of expanding the use of its existing individual taxpayer data analytics vendor to help identify corporate and business tax fraud.

We recommend that RAD determine the cost benefit of expanding its current use of its data analytics for other types of tax returns.

Agency Response			
Analysis			
Please provide additional comments as deemed necessary.			
Recommendation 4	Agree	Estimated Completion Date:	06/2024
Please provide details of corrective action or explain disagreement.	The Comptroller of Maryland is recognized nationally as the pioneer of implementing the fraud model for personal income tax and is intent on identifying and preventing fraud across all tax types. We will work with the outside vendor to determine cost and approach, an expansion of the existing fraud detection system will require additional funding. It is important to note that, due to the strength of bad actors, additional funding goes beyond the development and implementation of the algorithm. Our best-in-call income tax model is still only correct 50% of the time, that means that staff must be available to adjudicate algorithm results, answer phone calls, process documentation and correspondence validating identity, and hear appeals. We strongly implore the State to support this initiative, but we also have to ensure that the total cost for implementation is provided.		

**Comptroller of Maryland
Revenue Administration Division**

Agency Response Form

SMART

The Office of Legislative Audits (OLA) has determined that Finding 5 related to “cybersecurity”, as defined by the State Finance and Procurement Article, Section 3.5-301(b) of the Annotated Code of Maryland, and therefore is subject to redaction from the publicly available audit report in accordance with the State Government Article 2-1224(i). Although the specifics of the finding, including the analysis, related recommendation(s), along with COM’s responses, have been redacted from this report copy, COM’s responses indicated agreement with the finding and related recommendations.

<p>Finding 5 Redacted cybersecurity-related finding.</p>
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Agency Response has been redacted by OLA.

**Comptroller of Maryland
Revenue Administration Division**

Agency Response Form

COMPASS

OLA has determined that Finding 6 related to “cybersecurity”, as defined by the State Finance and Procurement Article, Section 3.5-301(b) of the Annotated Code of Maryland, and therefore is subject to redaction from the publicly available audit report in accordance with the State Government Article 2-1224(i). Although the specifics of the finding, including the analysis, related recommendation(s), along with COM’s responses, have been redacted from this report copy, COM’s responses indicated agreement with the finding and related recommendations.

Finding 6 Redacted cybersecurity-related finding.
--

Agency Response has been redacted by OLA.

**Comptroller of Maryland
Revenue Administration Division**

Agency Response Form

Cash Receipts

Finding 7

RAD had not established sufficient controls over checks for tax payments received in the mail at its Annapolis location, as certain documentation used to account for batches of checks processed was not retained prior to May 2021.

We recommend that RAD

- a. retain copies of batch control sheets to provide accountability and control over tax returns and collections prior to recordation (repeat), and**
- b. retain support for any adjustments made to batch control sheets.**

Agency Response			
Analysis			
Please provide additional comments as deemed necessary.			
Recommendation 7a	Agree	Estimated Completion Date:	01/01/2023
Please provide details of corrective action or explain disagreement.	Batch control sheets are retained in accordance with internal procedures		
Recommendation 7b	Agree	Estimated Completion Date:	01/01/2023
Please provide details of corrective action or explain disagreement.	Documentation is retained to support adjustments to batch control sheets in accordance with internal procedures.		

Comptroller of Maryland Revenue Administration Division

Agency Response Form

Information Systems Security and Control

OLA has determined that the Information Systems Security and Control section, including Findings 8 and 9 related to “cybersecurity”, as defined by the State Finance and Procurement Article, Section 3.5-301(b) of the Annotated Code of Maryland, and therefore are subject to redaction from the publicly available audit report in accordance with the State Government Article 2-1224(i). Although the specifics of the following findings, including the analysis, related recommendations, along with COM’s responses, have been redacted from this report copy, COM’s responses indicated agreement with the findings and related recommendations.

Finding 8
Redacted cybersecurity-related finding.

Agency Response has been redacted by OLA.

Finding 9
Redacted cybersecurity-related finding.

Agency Response has been redacted by OLA.

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