

**State of Arizona  
Office  
of the  
Auditor General**

**PERFORMANCE AUDIT**

**DEPARTMENT  
OF  
TRANSPORTATION**

**MOTOR VEHICLE  
DIVISION'S  
REVENUE FUNCTIONS**

**Report to the Arizona Legislature  
By Douglas R. Norton  
Auditor General  
February 1997  
Report No. 97-4**



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February 14, 1997

Members of the Arizona Legislature

The Honorable Fife Symington, Governor

Mr. Larry S. Bonine, Director  
Arizona Department of Transportation

Transmitted herewith is a report of the Auditor General, A Performance Audit of the Arizona Department of Transportation, Motor Vehicle Division's revenue function. This report is in response to a May 30, 1995, resolution of the Joint Legislative Audit Committee. The performance audit was conducted as part of the Sunset review set forth in A.R.S. §§41-2951 through 41-2957.

This is the first in a series of reports to be issued on the Department of Transportation. This report found that the Motor Vehicle Division needs to improve its collection and handling of fees and taxes collected from the general public and the motor carrier industry. Hundreds of millions of dollars handled by MVD offices issuing drivers' licenses and vehicle registrations are not adequately safeguarded, creating the potential for loss or theft. Motor carriers' ability to bypass the ports of entry is estimated to result in a potential revenue loss of from \$24 million to \$45 million annually. Additional revenue is lost by MVD's failure to ensure motor carriers file tax returns and post bonds as required by law. Finally, MVD has lacked basic information needed to manage the collection of millions of dollars in delinquent taxes.

My staff and I will be pleased to discuss or clarify items in the report.

This report will be released to the public on February 17, 1997.

Sincerely,

Douglas R. Norton  
Auditor General

# SUMMARY

The Office of the Auditor General has conducted a performance audit of the Department of Transportation pursuant to a May 30, 1995, resolution of the Joint Legislative Audit Committee. This audit focuses on the Motor Vehicle Division's revenue functions. This audit was conducted as part of the Sunset review set forth in Arizona Revised Statutes (A.R.S.) §§41-2951 through 41-2957 and is the first of four audits of the Department.

The Arizona Department of Transportation is charged with collecting and allocating fee and tax revenues for the Highway User Revenue Fund (HURF). The Fund has many sources of revenue, including gasoline taxes, use (diesel) fuel taxes, motor carrier taxes, vehicle license taxes, registration fees, and other fees. In fiscal year 1995-96, HURF's total revenues were nearly \$860 million.

## **MVD Needs To Better Protect Cash and Valuables in Its Field Offices (See pages 7 through 12)**

In fiscal year 1995-96, MVD field offices processed over \$400 million in various motor vehicle taxes and fees, yet poor cash-handling and inventory procedures leave these monies vulnerable to loss or theft. A review of 10 of 72 field offices across the State revealed that, overall, cash controls are lacking from the time a clerk receives customer fees to the time the day's total revenue is deposited at the bank. Cash drawers were not locked, excess cash was not secured, a large number of employees had unnecessary access to the safe, and employees that had access to cash also performed the cash deposit function. Similar control weaknesses were identified regarding the license plate and tab inventory. For example, field office employees not responsible for issuing license plates or tabs had unnecessary access to this inventory. Moreover, in some offices, clerks in charge of issuing license plates and tabs were not assigned a specific set of these items. Therefore, if the items are lost or stolen, they are not traceable back to the employee responsible for the items.

The lack of adequate procedures to safeguard cash and inventory can result in loss or theft. For example, a janitor was found attempting to sell tabs for \$25 apiece after taking them from an office he cleaned. Similarly, a cash deposit of over \$4,000 was missing from a field office because it had not been secured in the safe after being counted.

Several improvements to adequately safeguard cash and inventory are relatively simple to implement. MVD needs to update its policies and procedures to cover such areas as cash handling, inventory, and deposits. In addition, it needs to ensure that field office employees are adequately trained and supervised. Currently, MVD provides minimal cash-handling training, including a 10-minute video discussing the consequences of stealing money. Finally, the Department's internal audit unit can assist in ensuring the adequacy of internal controls by conducting more field office audits.

### **MVD Should Strengthen Enforcement of Taxes on Motor Carriers (See pages 13 through 16)**

Taxes imposed on commercial motor carriers account for approximately \$200 million of the revenues generated for the HURF. Motor carrier taxes are generally based on vehicle miles traveled in Arizona, and MVD operates 22 ports of entry established along the State's borders to monitor motor carrier travel. Port officers check motor carriers to verify tax credentials and that tax accounts are current. However, motor carriers can easily bypass the ports by traveling on routes that do not have established ports, or traveling through the State during hours when the ports are not open. Moreover, motor carriers traveling primarily within the State are even more likely to go unchecked, since MVD places little emphasis on intrastate enforcement. In 1995-96, MVD checked only 1,681 trucks traveling through the State's interior, as compared to over 5.4 million trucks traveling through the ports.

With an enforcement system susceptible to avoidance, MVD risks losing substantial revenue for the HURF. Although motor carrier tax evasion is difficult to identify, a recent study by JHK & Associates estimated the potential revenue lost in calendar year 1994 to be between \$24 million and \$45 million. To better enforce taxes on motor carriers, MVD should increase the use of mobile enforcement crews along Arizona's highways. These crews would extend enforcement efforts to trucks that bypass the ports or travel only within the State by establishing port operations at temporary roadside locations throughout the State.

### **MVD Needs To Ensure Taxpayers File Reports and Post Adequate Tax Bonds (See pages 17 through 20)**

MVD should strengthen its oversight of taxpayer accounts to ensure the State recovers the correct amount of tax revenue due. Although motor carrier companies are required to pay taxes based on the reported amount of fuel used and miles traveled on Arizona roads, the Division fails to ensure tax reports are filed. Subsequently, taxpayers can accumulate large

amounts of unpaid taxes before the Division becomes aware the carrier has not filed returns.

MVD also needs to ensure taxpayers are adequately bonded to protect the State from lost revenue due to taxpayer default. MVD cannot currently determine if bonds posted by motor carriers are adequate because the computer program designed to monitor bonds incorrectly calculates the bond requirement, and the records used to calculate the required bond amount may be inaccurate.

### **MVD Should Continue Recent Efforts To Enhance Its Collection of Delinquent Taxes (See pages 21 through 24)**

Throughout our entire audit, MVD was unable to determine how successful it was in collecting the \$39 million in delinquent tax revenues due to the State or how effective the collections methods it employed were. Specifically, the unit lacked basic management information to answer such questions as:

- How much money did the unit collect?
- How much money did individual staff collect?
- How much of the delinquent revenue could still be collected?
- What actions have been taken to collect on delinquent accounts?

However, under the direction of a new supervisor, MVD has recently increased its emphasis on the collection of delinquent revenue by starting to record basic management information and revising a number of its collections procedures. For example, it has prioritized its collections efforts by targeting high-dollar delinquent accounts and has assigned collectors responsibility for specific accounts. Yet, MVD still needs to revise its policies and procedures, establish performance measures and monitor the revenue collection function on a regular basis.

### **Other Pertinent Information (See pages 25 through 29)**

During the audit, other pertinent information was also collected regarding the various computer systems used in the revenue collection function and the status of the Enterprise

Project, which is intended to consolidate several of the existing computer information systems. Despite MVD already spending most of the \$28 million appropriated for the project, it is still not operational. In addition, information was obtained regarding the use of electronic transponders at the ports of entry and aboard motor carriers that could enable the ports to process traffic more efficiently.

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# INTRODUCTION AND BACKGROUND

The Office of the Auditor General has conducted a performance audit of the Department of Transportation pursuant to a May 30, 1995, resolution of the Joint Legislative Audit Committee. This audit focuses on the Motor Vehicle Division's revenue functions. This audit was conducted as part of the Sunset review set forth in Arizona Revised Statutes (A.R.S.) §§41-2951 through 41-2957 and is the first of four audits of the Department.

## The Department Collects Highway User Revenues

The Arizona Department of Transportation (ADOT) collects and allocates fee and tax revenues due from highway users. Once collected, these monies are deposited with the State Treasurer in the Highway User Revenue Fund (HURF). By statute, the Fund can be used only for the costs associated with public highways or streets, such as right-of-way acquisition, construction, repair, and maintenance. In fiscal year 1995-96, total revenues for HURF totaled nearly \$860 million. As illustrated in Figure 1 (see page 2), the Fund has many sources of revenue, including:

- **Gasoline tax** 18 cents per-gallon tax placed on each gallon of gasoline sold in the State.
- **Use fuel taxes** 18 cents per-gallon tax placed on diesel fuel used in the State. In addition, an 8 cents per-gallon surcharge is levied on each gallon of diesel fuel used by a vehicle weighing over 26,000 pounds.
- **Motor carrier tax** placed on each mile driven in the State by a commercial motor carrier. The amount of the tax varies based on the number of miles traveled in Arizona and vehicle weight.
- **Vehicle license tax** based on the vehicle's assessed value and paid upon registration.
- **Registration fee** \$8 fee per registered passenger vehicle, collected at the time of registration.
- **Other fees** \$4 fee to title a vehicle, driver's license fees, and other fees.

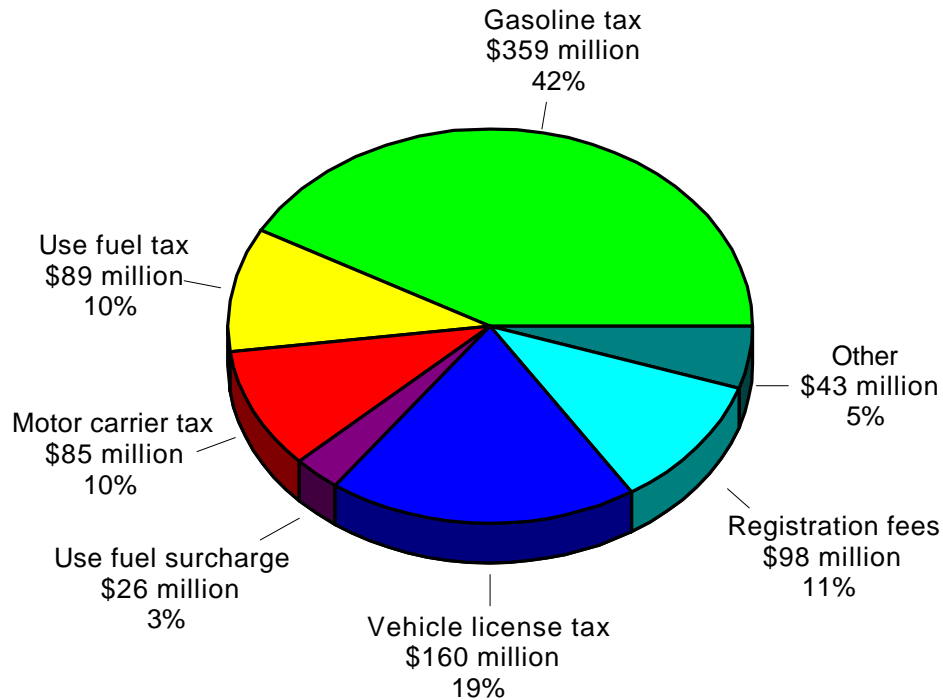
More detailed information on these taxes is presented in the Appendix (see pages a-I through a-iv.)

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**Figure 1**

**Arizona Department of Transportation  
Highway User Revenue Fund  
Amount and Percentage of Revenues by Source  
Year Ended June 30, 1996  
(Unaudited)**



Source: Auditor General staff analysis of data provided by the Arizona Department of Transportation Administrative Services Division.

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### **Motor Vehicle Division Performs the Department's Primary Revenue Collection Functions**

The Department places most of the responsibility for collecting highway user revenues with the Motor Vehicle Division (MVD). The following organizational units within MVD assist in collecting revenues:

- **Field offices** The Division's 72 field offices across the State employ almost 750 staff who collect registration fees, vehicle license tax revenue, and driver's license fees from the public.

- **Enforcement services** This unit operates the port-of-entry system and carries out special enforcement details. Approximately 170 port officers staff the 22 port-of-entry offices near the state borders to ensure that commercial vehicles entering the State are in compliance with Arizona tax laws and are carrying loads that are within the legal weight.
- **Motor carrier services** This unit establishes tax accounts for approximately 22,000 motor carriers that travel in and through the State. These carriers are required to report on a periodic basis the amount of taxes due, the amount of fuel used, and miles traveled. The unit maintains records on taxpayers by recording tax reports and updating taxpayer vehicle insurance information.
- **Collections unit** The collections unit collects past-due taxes from motor carriers. The unit has seven collectors who inform taxpayers of their delinquent taxes, arrange payment agreements when possible, and take more aggressive collection actions as needed to recover monies due to the State.

## **Audit Scope and Limitations**

This audit focused on the Division's various revenue-generating functions, specifically the adequacy of internal controls used in MVD offices to safeguard cash and inventory, the effectiveness of the Division's tax enforcement program, the Division's ability to monitor taxpayer compliance with reporting and bonding requirements, and its ability to collect delinquent tax revenue.

In two of the areas, our evaluation of the Division's revenue functions was significantly impaired by MVD's lack of information, poor recordkeeping, and computer system deficiencies. First, the collection unit's effectiveness in recovering past-due amounts from commercial taxpayers could not be evaluated because ADOT, until recently, did not track the amount of monies received from collections efforts. As a result, collector productivity also could not be determined or compared to other private or government collections functions. The effectiveness of collection methods employed to collect on individual accounts also could not be evaluated, since neither the computer records nor the physical files contained complete, accurate information on the efforts made to recover monies owed to the State.

Second, an evaluation of whether current bonding levels are sufficient to meet statutory requirements could not be made. The accuracy of the information available on the tax and revenue group automated tracking system (TARGATS) and the information in the physical files needed to make these determinations could not be verified. Therefore, the extent to which tax revenues are protected by bonds could not be determined.

## Methodology

To evaluate whether cash and inventory are adequately safeguarded, 10 of the 72 customer service offices were selected from around the State for review. These offices were chosen to represent a cross section of offices, based on location and staff size. Each of the 10 offices was visited during July 1996 to interview staff, observe office operations, and review office records.

To evaluate tax enforcement efforts, we interviewed enforcement staff, visited 6 of the 22 ports of entry, reviewed data on recent enforcement efforts, studied several ADOT consultants' reports, and surveyed other states.

Due to the scope limitations described earlier, the collection unit's effectiveness could not be evaluated. However, the current process by which collectors attempt to collect delinquent tax revenues was reviewed. Collectors were observed to determine what tools were used to collect amounts due. The unit's procedures were then compared against those considered effective by other state and private collection organizations.

This report presents findings and recommendations in four areas:

- The need to improve internal controls in customer service offices to ensure that cash, and license plate and tab inventories, are adequately safeguarded.
- The need to strengthen enforcement efforts to ensure that motor carriers within the State comply with tax laws.
- The need to ensure that taxpayers file tax reports and post sufficient tax bonds.
- The need to track information regarding delinquent revenues and to use several valuable collection techniques.

This report covers two issues similar to those addressed in prior performance audit reports:

A 1986 audit of the MVD Revenue Group (Auditor General Report 86-7) found that the Group could reduce the growth in the number of uncollectible tax accounts. The report noted over \$3 million in uncollectible accounts at that time and recommended that MVD monitor accounts to identify uncollectible accounts as soon as possible. Our current report notes that uncollectible accounts have grown to at least \$16 million; however, agency officials believe that the uncollectible amount is significantly higher. While MVD has recently initiated efforts to enhance its collection of delinquent

revenues, it still needs to revise its policies and procedures and establish performance measures for the collections unit (see Finding IV, pages 21 through 24).

The 1986 report on MVD Weight Enforcement (Auditor General Report 86-9) found that increased mobile enforcement was needed to monitor trucks that bypass the ports and those that travel only within the State. Similarly, this current audit found that increased mobile enforcement efforts are still needed to strengthen enforcement of taxes on motor carriers (see Finding II, pages 13 through 16).

This report also presents other pertinent information regarding the status of the Department's automation project and the technological upgrades for the ports of entry the Department is considering.

This audit was conducted in accordance with government auditing standards.

The Auditor General and staff express appreciation to the Director and the staff of the Department of Transportation and its Motor Vehicle Division for their cooperation and assistance throughout the audit.

## **FINDING I**

### **MVD NEEDS TO BETTER PROTECT CASH AND VALUABLES IN ITS FIELD OFFICES**

MVD can help prevent loss and theft of cash, and license plates and tabs, by instituting and enforcing an adequate system of internal controls in each office. Currently, poor cash-handling and inventory procedures leave millions of dollars in revenues that are received each year vulnerable to loss or theft. Office procedures that generally protect cash and valuable inventory are compromised by a lack of sufficient internal control policies, inadequate training, and computer system limitations. Therefore, MVD needs to develop adequate policies and procedures, emphasize employee training and field office oversight, and incorporate adequate control procedures into its computer systems. To ensure controls are in place, ADOT internal auditors should conduct more field office audits.

#### **Background**

In fiscal year 1995-96, MVD's 72 field offices processed over \$400 million in motor vehicle transactions. These transactions represent a significant source of revenue available to the State for highway construction and improvement. In addition to large amounts of cash collected from customers, offices maintain valuable license plate and vehicle tab inventories that are ultimately sold to the public.

Due to the high volume of transactions involving cash and valuable inventory, it is important that each office maintain adequate internal controls. Internal controls are field office policies and procedures designed to protect state revenues or assets against loss or theft. These policies set out specifically how cash transactions should be processed from the time money is received to the time it is deposited. Additionally, internal controls provide guidance regarding proper recording, distributing, and storing of assets. Without such controls, the possibility of MVD losing cash or valuable inventory to carelessness or fraud greatly increases.

#### **Poor Internal Controls Place Cash and Valuables at Risk of Loss or Theft**

While the fees and taxes collected at field offices comprise a significant amount of state highway revenue, weak internal controls leave these monies vulnerable to loss or theft. In

fact, poor cash-handling procedures have already resulted in losses of state monies. Furthermore, inadequate controls over valuable office inventories, such as license plates and vehicle tabs, increase the likelihood that these items could also be lost or stolen.

**Poor controls over cash handling result in losses**—Current cash-handling procedures in MVD field offices do not sufficiently guard against cash loss or theft. Cash controls are lacking from the time that a clerk receives customer fees to the time that the day's total revenue is deposited at the bank. Visits to ten MVD field offices revealed the following internal control weaknesses:

**Cash drawers not locked** In seven of the ten offices, cash drawers were unlocked when cashiers were away from their stations.

**Excess cash not secured** None of the offices had procedures limiting the amount of cash held in the cash registers during a shift. During the day, several thousand dollars can accumulate in a cash register. Such monies would be more secure in the office safe.

**Unnecessary access to safe** In three of the larger offices, more employees had easy access to the safe or safe combinations than was necessary. For example, in one office with more than ten employees, the safe was left open during working hours. Limiting access to cash would reduce the chances that someone not responsible for the money has the ability to take it from the safe.

**Poor deposit procedures** In seven out of ten offices, the clerk who handled cash transactions also prepared the bank deposit. In addition, in five of those offices, one employee consistently took the money to the bank every day. A single employee with consistent control over both the cash and the deposit increases the opportunity to alter deposit forms and abscond with the difference between what was deposited and what was actually received.

The types of internal control weaknesses observed in the field offices have, in fact, resulted in cash losses. ADOT's Office of Special Investigations, which handles theft or fraud cases, has documented several losses due to poor internal controls. The following cases exemplify the impact of poor cash-handling controls:

- Several times in 1993, two MVD employees collaborated to steal cash from daily deposits. These employees took the deposits home, altered deposit figures on the bank deposit slips, and stole the excess money. To cover up these thefts, the employees would use monies collected the next day to replace the monies stolen from the deposit. Since these same employees were frequently responsible for deposits, they could



continue this scheme undetected. This loss of \$11,634 could possibly have been avoided if the bank deposit function was rotated between all clerks in this office.

- On November 6, 1995, an MVD field office supervisor reported that the bag containing the previous day's cash deposit was missing. The deposit bag had been left on the supervisor's desk after an employee counted the money to be deposited. This loss of \$4,380 could have been prevented if the supervisor had ensured the bag was in the safe before closing the office.

*Poor controls over license plates and vehicle tabs also result in losses*—In addition to inadequate cash controls, poor inventory control procedures over license plates and tabs increase the likelihood of loss or theft. Customers obtain vehicle tabs and license plates at field offices as proof that vehicle registration taxes and fees have been paid. On newer cars, registration and taxes can amount to several hundred dollars; therefore, stolen plates or tabs that are placed on an unregistered vehicle represent significant revenue loss to MVD.

Despite the potential for revenue loss from the misuse of license plates and tabs, many offices maintain limited or no controls over office inventory. Specifically, the following weaknesses were identified:

- **Number of license plates and tabs on hand at office not recorded** Five of the nine offices that sell license plates and tabs do not maintain inventory records.<sup>1</sup> When physically counting this inventory, records listing the number of plates and tabs currently on hand in the office should be compared to the quantities listed on the original receiving reports to ensure that plates and tabs have not been lost, damaged, or stolen subsequent to delivery.
- **License plates and tabs not issued directly to clerks** In five of the nine offices, plates and tabs are not assigned in numerical order to the clerks responsible for selling the items, and supervisors in six offices are not notified when items are obtained from the storeroom. Recording plates and tabs issued to clerks accompanied with supervisory oversight ensures that lost or missing items are traceable to the employee in control or possession of those items.
- **Unnecessary access to stored plates and tabs** In five of the nine offices, employees who do not distribute plates and tabs have access to the plate and tab storeroom. Limiting access to unissued plates and tabs reduces the opportunity for someone not responsible for the items to take them from the storeroom.

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<sup>1</sup> Of the ten offices visited, one office exclusively distributed driver's licenses. Therefore, inventory controls that apply to license plates and tabs were relevant in only nine of the ten offices visited by auditors.

- **Tabs within reach of customers** In two of the nine offices, tabs were within the reach of customers at the counter, providing an opportunity for customers to take a tab without paying the appropriate registration fees and taxes.

While inventory losses have been difficult to document, several incidences of theft have occurred. For example, at one office, a janitor was attempting to sell tabs for \$25 each after taking them from the office he cleaned. Investigators noted that these tabs were taken from a desk that is supposed to be locked. In another case, 27 license plate tabs were stolen and sold to undercover police officers during a February 1996 Phoenix Police Department investigation. Given that tabs are not assigned to individual clerks by number, investigators were only able to trace the tabs to their originating department. They could not determine which employees were accountable for the tab series or how the suspects obtained the tabs.

### **MVD Should Take Several Steps To Ensure Field Offices Implement Proper Internal Controls**

To ensure cash and inventory are adequately safeguarded, MVD needs to improve internal controls in its field offices. First, it needs to ensure that effective internal control policies and procedures are in place and updated manuals are distributed to all field offices. Second, MVD needs to improve training and oversight to ensure procedures are consistently followed. Third, MVD needs to strengthen current computer system controls while also ensuring that it incorporates adequate safeguard mechanisms into future computer systems. Finally, MVD can use the assistance of ADOT's internal audit unit to ensure compliance with policies and procedures.

*MVD field offices need adequate policies*—In order to implement adequate internal controls, MVD needs to complete development of its policies and procedures. Currently, policies and procedures do not address important controls, and field office supervisors are generally unfamiliar with them. In fact, supervisors in six field offices stated they did not have a copy of the current manual and were unaware of standard internal control policies.

MVD recently began updating its fiscal policy manual, intending to include improved internal control procedures. While the manual's completion date has not been determined, MVD needs to ensure the following areas are addressed:

- **Cash-handling procedures** limiting safe combinations and keys to an essential number of employees as well as procedures limiting the amount of cash that may accumulate in a clerk's drawer during the day. Loss is less likely to occur when large cash amounts are secured in a safe until deposited.

- **Inventory procedures** ensuring employees are accountable for license plates and tabs as well as procedures requiring MVD offices to retain inventory records. Lost items would be traceable to the responsible employees, and a physical count of plates and tabs could be completed on a periodic basis.
- **Deposit procedures** requiring that the daily deposit be prepared by someone with no access to cash and that deposit duties are alternated between clerks. Segregation of these duties between two individuals helps prevent theft of the cash being deposited.

*Training and oversight needs to be increased*—Once MVD has revised its policies and procedures, it needs to ensure that all field office personnel are adequately trained in the proper application of all procedures. Currently, MVD does not emphasize protecting cash and inventory in its initial training classes. In four weeks of basic title and registration training and eight days of basic driver's license training, employees receive minimal cash-handling training, including a 10-minute video discussing the consequences of stealing money.

MVD also needs to ensure adequate field office oversight. Forty-nine of the 72 field offices do not have a full-time supervisor. Lack of proper oversight can result in losses. For example, ADOT's Office of Special Investigation identified one office that continually recorded cash shortages during a three-month period when the office was not supervised on a regular basis. A trained supervisor has since been assigned to the office and problems with missing money and cash shortages have decreased. Therefore, to ensure oversight is maintained, schedules should be developed to allow supervisors to regularly visit field offices for which they are responsible. During these visits, supervisors should monitor cash-handling and inventory procedures to ensure policies are followed.

*Computer system controls need to be improved*—Enhanced computer systems can also provide an added check to ensure proper transaction recording. Currently, the title and registration and driver's license computer systems are not linked to the system used to record and account for cash received. Because these systems do not communicate, a clerk could potentially update customer records on the system and steal the money received without entering the collected fees into the automated cash register. In fact, in one case, an MVD employee on at least 78 occasions collected fees from customers but did not put the money in the automated cash register, stealing over \$1,800. Moreover, the driver's license computer system currently fails to account for the number and price of driver's licenses sold in field offices; consequently, a supervisor would not know if all driver's license revenues were accounted for.

While the current computer systems contain serious limitations, there are some measures MVD can take to better account for revenues received from cash transactions. At a minimum, MVD should provide transaction receipts to all customers to help ensure that they are charged the proper amount. Furthermore, supervisors should monitor activity

reports produced by the automated cash register to ensure that transactions are performed correctly and properly accounted for. To address inventory controls, MVD has begun preliminary planning on an automated inventory tracking system that is intended to log various inventory items, such as tabs and plates, and identify the clerks responsible for their sale. This system should ensure tabs and plates can always be located by serial number, that inventory in office storerooms is recorded, that item quantities can be verified by physical counts, and that clerks are accountable for the items issued to them.

In the long term, MVD needs to link the driver's license and title and registration computer systems with the automated cash register function when developing a new automated system. This will allow both title and registration and driver's license fees to be properly charged to the customer. Furthermore, the total number and types of licenses issued can be recorded, thereby ensuring that license revenues are properly accounted for. MVD is currently developing a new automated system intended to link the two systems as well as perform the cash register function. While it had originally anticipated implementing this system in fiscal year 1995-96, the project has yet to be completed (see Other Pertinent Information, pages 25 through 29, for further information on the status of this project).

*ADOT internal auditors should conduct more field office audits*—Finally, ADOT internal auditors can also assist in ensuring the adequacy of internal controls by conducting more field office audits. The Agency's internal auditors, responsible for auditing all of ADOT's operational areas, have performed field office reviews in the past. In fact, in 1996, they conducted eight field office reviews as of September and found many of the same internal control problems we identified. However, only a limited number of these audits have been performed. Therefore, in light of existing control weaknesses, more audits are needed. Furthermore, internal auditors should conduct follow-up reviews to ensure that offices address their initial findings and recommendations.

## Recommendations

1. MVD should ensure that adequate policies and procedures are developed regarding all aspects of internal controls, particularly those related to cash-handling, inventory, and deposits.
2. MVD should emphasize internal control training of its employees and improve oversight of its field offices to ensure that procedures are being consistently followed.
3. MVD should enhance current computer system controls by providing transaction receipts, monitoring automated cash register activity reports, and continuing to enhance the automated inventory system.
4. MVD should link the driver's license and the title and registration systems with an automated cash register function when developing a new automated system.
5. ADOT internal auditors should conduct more field office visits to ensure offices are maintaining adequate levels of internal controls.

## **FINDING II**

### **MVD SHOULD STRENGTHEN ENFORCEMENT OF TAXES ON MOTOR CARRIERS**

MVD needs to strengthen enforcement of taxes on motor carriers to protect the State from tax evasion. Currently, MVD relies primarily on immobile ports of entry located on the State's perimeter to enforce tax laws. However, this method has proven to be susceptible to avoidance by taxpayers. Therefore, MVD should take steps to develop a stronger enforcement program within the State by increasing mobile enforcement efforts and targeting these efforts using ADOT highway traffic information.

#### **Background**

Taxes imposed on motor carriers represent about 20 percent of the revenues generated to fund highway construction, repair, and maintenance. In fiscal year 1995-96, these taxes totaled over \$200 million. Because motor carrier taxes are based on vehicle miles traveled in Arizona, it is critical to monitor motor carriers' travel. MVD primarily performs the monitoring function by stopping vehicles as they enter the State through the 22 ports of entry established along its border. While port personnel enforce vehicle weight and safety laws, they also aid in tax enforcement and collection efforts in several ways. First, port officers verify tax credentials to confirm that carriers have valid Arizona tax accounts and that taxes have been paid. If there is a delinquent amount outstanding on the carrier's tax account, port officers can prevent vehicles from entering the State. Second, port staff directly collect revenue from carriers without valid tax accounts who purchase permits allowing single trips into the State. In fact, the ports collected almost \$18 million in revenues in fiscal year 1995-96. Finally, as motor carriers pass through the ports, port personnel record the number of miles the driver will travel in Arizona for future use in auditing tax reports.

In addition to the ports, MVD occasionally places mobile enforcement crews at roadside locations within the State. Operating similar to ports, these crews extend enforcement efforts to trucks that do not cross the ports. The crews direct all truck traffic off the highway, guide the truck over a set of portable scales to be weighed, then conduct a safety inspection and check compliance with registration and tax laws. In fiscal year 1995-96, MVD conducted 19 mobile enforcement efforts in Arizona. During these efforts, 1,681 vehicles were checked, 44 permits were sold, and 108 citations were written.

## **Current Enforcement Efforts Easily Avoided**

Despite the importance of enforcing tax laws on motor carriers, MVD currently uses a method that is susceptible to avoidance and therefore can result in lost revenue for highway funding. Although MVD relies on ports of entry as its primary enforcement mechanism, the ports are unable to monitor all traffic into and out of the State and are easily avoided. Moreover, while the ports emphasize enforcement of interstate traffic, enforcement efforts within the State have been limited. As a result, motor carriers can avoid payment of taxes, potentially reducing revenues needed for highway funding.

*Ports system susceptible to avoidance*—Current enforcement of taxes on motor carriers is primarily limited to a port-of-entry system that vehicle drivers can easily avoid. MVD operates ports of entry on only 22 of the 33 paved roads that enter Arizona. Therefore, to bypass a port, drivers can simply choose to drive on routes that do not have ports. In fact, MVD staff at several ports visited pointed out there were nearby routes that truckers could quickly and easily use to avoid a port. They believe that drivers who are aware that they were violating weight, safety, or tax regulations can and do choose to bypass a port. A 1996 study, *Assessment of Arizona's Motor Carrier Enforcement Efforts* by JHK & Associates, confirmed the staff's observations, concluding that up to 20 percent of the trucks crossing on routes without ports may be violating regulations.

Even if drivers do not use a bypass route, they can drive through ports unchecked when the ports close, since only 9 of the 22 ports are open on a 24-hour basis. MVD officials noted that some drivers even pull off the highway to wait until a port closes before crossing the border. For example, drivers wanting to avoid the port of entry at Page were able to pass through it unchecked as early as 5:00 p.m. Although 24-hour operations for all its ports is not necessary, MVD officials indicated that they have identified at least two ports that need extended hours. In fact, one of those identified ports is the one located in Page.

*Enforcement within the State limited*—While interstate carriers can fairly easily avoid being checked for compliance with tax laws, motor carriers traveling primarily within the State are even more likely to go unchecked. According to 1995 ADOT estimates, 25 to 40 percent of all heavy vehicles travel only within the State, never crossing a border. However, MVD's mobile enforcement crews checked only 1,681 vehicles in fiscal year 1995-96 for tax and weight compliance. In contrast, port personnel checked over 5.4 million vehicles during that same year.

*Substantial revenue loss possible*—With an enforcement system open to avoidance, MVD risks losing substantial revenue for the Highway User Revenue Fund. Although difficult to identify, two studies have attempted to estimate the evasion rate in Arizona. Most recently, the JHK & Associates study estimated the potential revenue lost from motor carrier tax evasion in calendar year 1994 was between \$24 million and \$45 million, or 29

to 55 percent of revenues generated from the tax in that year. This study is consistent with the Highway Cost Allocation Study for 1988-92, which suggested an evasion rate of as much as 35 percent of total motor carrier tax revenue.

## **Stronger Mobile Enforcement Efforts Are Needed**

MVD needs to strengthen tax enforcement to ensure taxpayers not currently checked by the port system are adequately monitored. Specifically, it needs to enhance mobile enforcement capabilities within the State. To better target these mobile details, MVD should use highway traffic information from the Department's Intermodal Transportation Division.

*Increased mobile enforcement efforts can monitor more carrier traffic*—MVD should increase the use of mobile operations to enforce tax compliance on more carriers. Mobile enforcement crews would monitor carriers that are currently not checked at the ports, particularly carriers operating only within the State that never cross a port, and interstate carriers that avoid the ports. As mentioned earlier, MVD has made only limited efforts to place mobile enforcement crews within the State. MVD officials indicate this is because the Division does not have staff dedicated for these operations; thus, they can only be scheduled when enough port personnel are available to staff them. Therefore, the Division has operated only 24 crews in the last 3 years.

Recognizing the importance of enhanced enforcement, MVD has developed an enforcement plan to improve mobile enforcement. Currently, the mobile enforcement program consists of only two mobile ports. However, the scales and equipment staff use are outdated and unreliable. The MVD plan proposes purchasing equipment for six mobile units, which would include a truck and trailer containing computers, communications equipment, and new scales. However, JHK & Associates recently reviewed this plan as part of its 1996 study, and recommended that MVD begin with a prototype mobile unit as a pilot project and evaluate its effectiveness before expanding the program. Consequently, MVD was authorized \$80,000 to purchase a trailer for one unit.

MVD hopes to eventually provide consistent staffing for the mobile ports by employing technology upgrades for the ports of entry. These upgrades would potentially decrease port staff's workload and thus provide additional employees to conduct mobile enforcement operations on a regular basis (see Other Pertinent Information, pages 25 through 29).

*Mobile enforcement opportunities could be better targeted*—MVD could further improve mobile enforcement efforts by better targeting the placement of mobile details. When planning mobile details, MVD could use highway traffic information collected by the



Intermodal Transportation Division. Specifically, the Intermodal Transportation Division monitors vehicle traffic on state highways automatically through many traffic data collection sites imbedded in the roadway. These electronic monitors count the number of vehicles using the highway. Although this information is primarily used for highway planning purposes, MVD could also use it to help identify routes used to avoid ports and to assess travel inside the State's borders. Moreover, while this information would be most helpful for identifying potential mobile enforcement sites, MVD could also use it to determine which ports of entry should be considered for extended hours of operation.

## **Recommendations**

1. MVD should increase the use of mobile enforcement crews to better ensure motor carriers comply with the tax laws.
2. MVD should work in conjunction with the Department's Intermodal Transportation Division to obtain essential traffic data that can be used to better plan and deploy mobile enforcement units. In addition, this data can also be used to determine the need for extended hours of operation for ports of entry that currently are not open on a 24-hour basis.

## FINDING III

### MVD NEEDS TO ENSURE TAXPAYERS FILE REPORTS AND POST ADEQUATE TAX BONDS

By improving its oversight of taxpayer accounts, MVD can better ensure taxpayers correctly file returns and post proper tax bonds. MVD can reduce the risk of tax evasion by improving its ability to identify taxpayers who do not file tax returns. MVD can also better ensure the State is adequately protected from taxpayers who fail to pay their taxes by improving the way it monitors taxpayer bonds.

#### Background

Arizona law requires operators of motor vehicles over 26,000 pounds to pay taxes on fuel they use on Arizona roads (use fuel tax) and an additional tax based on the vehicle's weight and the distance traveled on state roads (motor carrier tax). In fiscal year 1995-96, these taxes brought in over \$200 million for the Highway User Revenue Fund (HURF). To pay these taxes, taxpayers must establish a tax account with MVD and post a bond as collateral in case they default on taxes due. Taxpayers then report and submit tax payments by filing a report monthly, quarterly, semiannually, or annually, depending on the amount of their liability. Currently, MVD has approximately 22,000 of these taxpayer accounts on record.

#### Checks on Tax Reports Should Be Implemented To Reduce Tax Evasion Risk

MVD can reduce the risk of tax evasion by monitoring taxpayer compliance with the State's tax reporting requirements. Although statutes require all taxpayers to file a return periodically, MVD risks losing revenue through tax evasion by not adequately monitoring who submits tax returns. To easily identify taxpayers who fail to file tax returns, MVD should review its tax account data and reinstate a process to identify non-reporting taxpayers.

*MVD fails to ensure all taxpayers file a report*—While MVD receives approximately \$200 million each year in motor carrier and use fuel taxes, there are additional tax revenues that

may be lost because MVD does not ensure all taxpayers file returns. Although it is difficult to identify the extent to which companies do not file tax reports, studies have shown that the rate of companies not paying taxes can potentially be quite high. For example, in a 1993 special project, ADOT revenue auditors reviewed records for 5,600 tax accounts and found that 36 percent of the taxpayers reviewed had not filed tax returns. MVD verified that many of those companies owed taxes to the State that had not been paid and mailed reminder notices to them. This project demonstrated that identifying and contacting taxpayers who fail to file reports can recover significant amounts of revenue, since it successfully recovered over \$2 million in unreported taxes that might not otherwise have been detected.

However, without a regular system in place to identify non-filers such as those in the project described above, taxpayers can accumulate large amounts of unpaid taxes before MVD recognizes that returns have not been filed. For example:

- In 1994 and early 1995, a company failed to file a tax return for three consecutive quarters. The company then declared bankruptcy in March 1995. It was not until seven months later that a collector discovered the company had failed to file reports and assessed over \$27,000 in taxes and penalties. As of August 1996, this debt is still outstanding.
- Another company operated nearly a year and a half before MVD detected that it had failed to file tax reports. In all, the company failed to file three quarterly reports between 1993 and 1994. After a request for these reports went unanswered, MVD assessed the company over \$5,000 in penalties and back taxes. As of August 1996, these taxes had not been paid.

The only time MVD checks to determine whether a taxpayer has reported properly is when it audits a taxpayer, reconciles an account balance, or a collector reviews the account.

***MVD needs to review taxpayer files and identify non-filers***—To ensure it receives revenue when due, MVD should take steps to identify non-reporting taxpayers. In order to do this, MVD must first improve its computer records. Specifically, MVD needs to delete inactive accounts (i.e., those taxpayers who have gone out of business or no longer operate in the State) from its Tax and Revenue Group Automated Tracking System (TARGATS) records. Currently, TARGATS maintains information on both active and inactive accounts. This makes it difficult for MVD to identify only those taxpayers who are currently operating and should be filing tax returns. Once the inactive accounts are removed from TARGATS, MVD should regularly identify non-filers and automatically send notices reminding them to file.

## **MVD Needs To Ensure Adequate Tax Bonds Are Posted**

In addition to better tax report monitoring, MVD needs to ensure taxpayers are adequately bonded to protect the State against non-payment. While state law requires taxpayers to post a bond to guarantee payment of their taxes, MVD lacks an accurate system to review these bonds to ensure they meet state requirements. MVD can enhance its protection of state revenue by correcting inaccurate taxpayer information and computer programs.

*MVD does not ensure the State is adequately protected against tax default*—Despite the statutory requirement for taxpayer bonding, MVD does not know if the bonds posted by taxpayers adequately protect the State from lost revenue due to taxpayer default. Specifically, statutes require that all taxpayers with use fuel or motor carrier tax licenses post bonds based on their estimated tax liability and how frequently they file. For example, MVD requires that taxpayers who file quarterly maintain a bond equal to five times their average monthly tax liability. These bonds are similar to insurance policies; a taxpayer pays a premium, approximately \$50 to \$75 for a \$1,000 bond, each year. If taxpayers fail to pay their taxes, MVD has the authority to seize as much of that bond as it needs to cover the tax due to the State. This allows MVD to collect a significant amount of delinquent taxes. For example, in fiscal year 1992-93, the collections unit recovered over \$1 million from taxpayer bonds. Further, because it is difficult to seize assets from taxpayers based out of state, bonds are an efficient tool for recovering unpaid taxes from the approximately 18,000 motor carrier taxpayers based outside Arizona.

However, MVD does not regularly review these bonds to ensure they are adequate to cover taxpayer debt. Initially, when taxpayers apply for a tax account, MVD's rules require taxpayers to post a bond based on their estimated tax liability. Yet, according to a study by JHK & Associates, in practice, MVD allows new applicants to merely purchase the legal minimum bond of \$500. MVD does not update this initial bond unless it audits the taxpayer (only 10 percent of all tax accounts are audited), or if the taxpayer is delinquent in paying taxes. Further, MVD does not routinely examine all accounts to see if the initial estimate was correct, or to identify taxpayers who have increased their tax liability and require an increased bond amount.

*MVD must correct inaccurate records and its computer program to improve bond management*—In order for MVD to determine if taxpayer bonds are sufficient, it must keep accurate records of these bonds. However, MVD's bond records may not be complete or accurate. Specifically, when reviewing physical files, auditors did not always find the original copies of the current bond sent in by taxpayers. In addition, errors in TARGATS' computer records were identified, including several instances where the bond amount listed in the computer record did not match the bond document in the physical files. These inconsistencies make it extremely difficult for MVD to ensure taxpayer bonds meet the

legal requirements. Therefore, to ensure MVD's bond records are accurate, MVD should verify computer records of each taxpayer's bond to the bond document maintained in the physical file. In some instances, MVD may need to contact taxpayers to verify information.

Once MVD obtains accurate data, it should revise TARGATS to accurately calculate bond amounts needed. Although MVD has a computer program that determines needed bond amounts based on companies' estimated tax liability, the program uses a different formula than the one specified by MVD's rules, and MVD discontinued using this program after operating it only once.

The needed corrections to the computer program are relatively simple. MVD programming staff estimates it would take 45 hours of programming time to correct the formula. Once the corrections are made, MVD can then regularly operate the computer program and calculate the bond amount needed.

## **Recommendations**

1. MVD should remove inactive accounts from the TARGATS computer system, thus allowing MVD to focus on obtaining returns and tax payments from active taxpayers.
2. MVD should regularly identify taxpayers who have not filed returns and mail reminder notices at the end of each reporting period.
3. To ensure the State is adequately protected from taxpayer default, MVD should:
  - Compare bond information maintained in physical files and the TARGATS computer files and correct any inconsistencies;
  - Revise its computer program to calculate the minimum required bond amounts according to the Division's administrative rules; and
  - Use the program regularly to calculate the required taxpayer bonds and inform taxpayers of the new bond amount.

## **FINDING IV**

### **MVD SHOULD CONTINUE RECENT EFFORTS TO ENHANCE ITS COLLECTION OF DELINQUENT TAXES**

MVD recently implemented a number of collection procedures that should allow it to assess the performance of its collections unit. Throughout much of our audit, MVD failed to maintain basic management information for its collections unit, prohibiting our ability to measure the unit's overall performance. However, late in the audit, the collections unit implemented a new database to record management information and implemented a number of collection procedures to enhance its revenue collection function. MVD still needs to revise its policies and procedures to incorporate these changes and needs to establish performance measures for the unit.

#### **Background**

MVD's collections unit collects past due motor carrier, use fuel, and other commercial vehicle-related tax debts. As of January, 1997, delinquent tax debts of more than \$39 million were due to the State. The collections unit employs five collectors and one support staff who process delinquent notices, negotiate payment agreements, answer calls from taxpayers, and file bond claims, bankruptcy claims, liens, and levies. The unit relies on physical files and the Tax and Revenue Group Automated Tracking System (TARGATS) to maintain and update taxpayer account information.

#### **Until Recently, Overall Performance of MVD's Collection Unit Not Measurable**

Throughout most of the audit, MVD was unable to determine how successful it was in collecting the substantial amount of delinquent tax revenues due to the State, or how effective the collections methods it employed were. Specifically, MVD failed to maintain basic management information or keep accurate records of its accounts. For example, while MVD could report the total amount of revenues received in any given year, it could not distinguish between revenue received from taxpayers in compliance with reporting requirements and delinquent taxpayers referred to the collections unit. Moreover, MVD could not evaluate its collections techniques because it did not retain complete, accurate

collections records. Collectors used their own coding systems to track collection actions, which resulted in an inconsistent and confusing system to classify tax debt. Furthermore, once taxpayers paid their debt, the TARGATS computer deleted information on actions taken to resolve the debt. Without these records, MVD could not consider the effectiveness of the methods used to pursue debt.

Lacking adequate records and consistent methods for tracking collections efforts, MVD could not answer a number of questions regarding its collections unit, such as:

- *How much money did the unit collect?*
- *How much money did individual staff collect?*
- *How much of the delinquent revenue could still be collected?*
- *What actions have been taken to collect on delinquent accounts?*
- *What actions have been taken to successfully resolve tax debts?*

## **Recent Efforts Underway To Enhance Collections Unit**

Under the direction of a new collections supervisor, MVD recently increased its emphasis on the collection of delinquent revenue. Specifically, the collections unit began recording basic management information, such as the total amount of revenue collected by the unit as a whole as well as by individual collector. In addition, the unit instituted a number of collections procedures, including:

- **Setting priorities for its collections efforts** While MVD previously did not regularly target high-dollar delinquent accounts or accounts that have been delinquent for a long period of time, it now has established a priority system for its collections efforts. Specifically, collectors have begun to concentrate on delinquent accounts of \$1,000 or more.
- **Assigning collectors responsibility for specific accounts** In the past, MVD's collectors were assigned specific tasks, such as filing bond claims or making and maintaining payment agreements with accountholders, rather than being responsible for a set of accounts. Without full responsibility for specific accounts, collectors tended to rely more on automated letters to remind taxpayers of their delinquent debt rather than contacting them by telephone. Now, each collector has a specific list of accounts for which they are responsible for resolving from the time the account is identified as

delinquent until the debt is resolved. Since collectors have full responsibility to resolve delinquent accounts, they are making greater use of phone collections to set up payment agreements and resolve debts in a timely manner.

- **Addressing the timeliness of its bond claims** Historically, MVD had not focused on filing bond claims against taxpayers that had an outstanding delinquent debt. The collections unit has recently dedicated one of its employees to concentrate on initiating tax bond filings in a more timely manner. In addition, the unit has compiled a list of accounts that are eligible for bond recovery and is tracking the amount collected from these efforts.
- **Improving its resolution of old debt** The collections unit is in the process of establishing policies and procedures to initiate a process to resolve old debt. In 1992, the Legislature granted MVD the authority to purge accounts from its records after referring them to the Attorney General's Office for possible civil action. To date, the unit has identified nearly \$16 million in outstanding debt that has been determined uncollectible and thus, appropriate for referral to the Attorney General's Office.

## **MVD Should Establish Procedures and Performance Measures**

MVD should continue its efforts by completing its planned revision to policies and procedures, establishing performance measures, and subsequently monitoring the revenue collection function on a regular basis.

- **Policies and procedures** To help ensure that delinquent accounts are collected effectively, MVD should update its written collections procedures and ensure that these procedures are followed. As it has recently implemented several basic collections techniques, such as prioritizing accounts and filing bond claims, the collections unit should ensure its policy manual contains guidelines for its collectors in these areas. Additionally, it should continue its development of a procedure to periodically identify and refer all uncollectible accounts to the Attorney General.
- **Performance measures** Now that the collections unit is maintaining and recording management information, it needs to develop and formalize performance measures to ensure an adequate basis for evaluating all aspects of the collections function. Such performance measures should describe the goals which the collections unit and its collectors hope to achieve through its collection function. For example, it could set a goal of increasing revenue collected by a certain percent every month or quarter. Likewise, it could set a goal for its collectors to make a certain number of telephone attempts each day.



- **Monitoring** Once it has established performance measures, MVD should begin monitoring the collection unit's performance on a regular basis to assess its effectiveness in collecting delinquent revenue. Specifically, MVD should compile revenue collection information for the unit overall as well as by individual collector and compare it against its established performance measures. In addition, it should review collectors' files to ensure appropriate and timely collections techniques are employed.

## **Recommendations**

1. MVD should establish a formal mechanism to guide collectors in the revenue collection function by:
  - Completing its revision of the collections unit's policies and procedures manual, and
  - Completing and formalizing performance measures
2. MVD should monitor the collection unit's performance on a regular basis by:
  - Ensuring that collectors follow the policies and procedures to collect delinquent revenues,
  - Compiling revenue collection information and comparing it against established performance measures, and
  - Reviewing collectors' files to ensure appropriate and timely use of collections techniques.

## OTHER PERTINENT INFORMATION

During the audit, other pertinent information was obtained regarding the various computer systems used in the revenue collection function and the current status of the Enterprise Project, which is intended to consolidate several of the existing computer systems. In addition, we obtained information regarding new technologies that could enhance port-of-entry operations in the future.

### Revenue Collection Systems and the Enterprise Computer Project

The computer systems currently used to process tax and fee revenues do not communicate and cannot share information. In addition, the systems individually have weaknesses that compromise MVD's ability to efficiently process revenues. To address these issues, the Department launched the Enterprise Project. However, this system is not operational, despite MVD spending most of the \$28 million appropriated for its development.

*Multiple computer systems not connected*—Currently, MVD uses three separate computer systems to process vehicle tax and fee revenues. These systems, which were all implemented 10 or more years ago, perform separate functions:

- **The title and registration system** was developed in 1971 to record customer vehicle and registration information.
- **The driver's license system** was developed in 1978 to record and track licensed drivers in Arizona.
- **The tax and revenue group automated tracking system (TARGATS)** was developed in 1986 to manage motor carrier tax account information including tax returns, audit actions, and account reports, and to track the activities of trucks at ports of entry.

Because these driver's license and title and registration systems are separate, information about a customer or vehicle in one system may be missing or contradicted in the other systems. For example, a driver's address may be current in the title and registration database, but incorrect in the driver's license records.

In addition to these systems not sharing historical data, severe weaknesses exist in each system that prevent each component from effectively collecting and recording revenue information. For example, as described in Finding I (see pages 7 through 12), the driver's license database is incapable of recording the fees collected as a license is issued. This impacts MVD's ability to determine how many licenses are issued on a daily basis and how much revenue should be collected. In addition, it is difficult for MVD to obtain complete data or management reports from the TARGATS system because it is written in an outdated and cumbersome programming language.

*New system planned to consolidate existing systems*—Recognizing the existing systems' limitations, ADOT sought to consolidate them in 1989, proposing to integrate the title and registration and driver's license databases into a single system. The linkage of these systems promised several benefits, such as better enforcement of motor vehicle laws, enhanced public service, and operational improvements. With better vehicle registration enforcement, ADOT projected a possible \$22 million increase in annual revenues when the project was completed.

ADOT planned to complete the project using a combination of Department staff and contractors, and had completed some initial research and planning in the project's early stages. In July 1991, ADOT hired a consultant, CACI, to assist in developing the project.

To fund the project, ADOT received \$28.2 million in appropriations over seven fiscal years. In fiscal year 1989-90, the Legislature appropriated \$8.8 million over 4 years to connect the title and registration and driver's license databases. In fiscal year 1993-94, the scope of the project was expanded to redesign and integrate both of the databases and TARGATS. To accomplish this, ADOT was appropriated an additional \$19.4 million over 3 years.

*Progress to date*—Although originally projected to be completed in fiscal year 1996, the Enterprise Project is not yet finished. However, ADOT spent over \$26 million almost all of the specific appropriations for the project. Most of the monies have been spent on payments to contractors (\$12.3 million), hardware purchases (\$8.2 million), software purchases (\$1.2 million), and ADOT personnel working on the project (\$4.5 million). In addition to the appropriations specifically authorized for the project, ADOT spent over \$6 million from other funding sources, mainly to upgrade the Department's mainframe to support Enterprise.<sup>1</sup>

To date, few of the project's objectives have been successfully completed. As noted earlier, the project objectives were to redesign and integrate the driver's license and title and registration systems and upgrade the TARGATS system. The status of work in these major areas as of October 1996 is noted below:

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<sup>1</sup> Expenditure information was compiled by ADOT internal auditors and has not been audited.

- **Title and registration** CACI was scheduled to deliver the redesigned title and registration system in September 1995. While CACI did not deliver a complete system, it did some work that included design of the database and software applications. However, the system CACI began designing will likely not be used. A consultant ADOT hired in early 1996 to evaluate CACI's work found that the database and application design is seriously flawed and inadequate to meet ADOT's needs. The consultant noted that repairing this system would require extraordinary effort and that the system would be unlikely to perform as planned.
- **Driver's license** Little work has been done on the driver's license system; however, the planned conversion to a digital driver's license system, including bar codes, was completed in July 1995. The bar codes were intended to instantly access customer data on the title and registration and driver's license systems when scanned by a clerk. However, the bar code system is currently not being used, although over \$900,000 has been spent to purchase bar code readers.
- **Cash accounting functions** A cash accounting function, similar to a cash register, was completed in February 1995. This program was meant to work with the driver's license and title and registration systems to assist clerks in collecting and recording cash revenue at MVD field offices. While MVD attempted to implement this function in several offices, it has been discontinued because the program was slow and often made accounting errors.
- **TARGATS** The redesign of this system was removed from the project with no work having been performed.

Currently, work on the project has stalled. In September 1995, a contract dispute with CACI occurred and ADOT attempted to negotiate with CACI to complete the project. However, these negotiations reached a stalemate and CACI ceased work on the project in November 1995. At this point, both parties are pursuing legal action.

*Future direction of Enterprise*—Due to the litigation between ADOT and CACI, ADOT has been pursuing other alternatives to enhance the existing systems with MVD. Specifically, in an effort to increase revenue, improve MVD customer service and reduce workload, MVD has continued to use available resources within the Department to implement Enterprise-like process improvements. There are currently 10 special projects already completed or underway that have improved current systems. For example, MVD has implemented biennial registration, which allows certain customers to register their vehicle for a two-year period. According to MVD officials, this special project is anticipated to improve customer service by reducing the number of interactions between the customer and MVD. Another project currently underway is to provide alternate payment methods for customers such as the use of credit and debit cards at MVD offices, which is expected to improve customer

service while at the same time reducing the problem with receiving bad checks. As it continues to implement these types of special projects, MVD officials indicate that they will continue to search for and evaluate other Enterprise-like systems in other states. It is not known at this time, however, when ADOT will proceed with the next phase in its attempt to consolidate existing systems or to what extent this effort will be similar to or different from the original Enterprise system.

## **Emerging Technologies Could Impact Future Port Operations**

MVD has been exploring the use of emerging technology to enhance its motor carrier enforcement operations at the ports of entry. Specifically, MVD has become a member of a multi-state organization that is developing technology capable of remotely exchanging information between trucks and ports that would eliminate the need for trucks to stop at ports. Basically, a transponder aboard trucks would signal the port transponder, thus identifying the vehicle and the carrier. The port computer would then determine whether or not to allow the vehicle to proceed and signal the driver accordingly. To be cleared, carriers must meet several criteria, including having valid registration and a current tax account. In addition, weigh-in-motion technology could be used to check that the truck is carrying a legal weight load before clearing the port.

These types of technologies are designed to process traffic more efficiently by limiting the number of trucks port staff process manually, which allows staff to focus on carriers with problem accounts and vehicles. The system would also benefit the trucking industry by eliminating delays truckers can experience when stopped at the ports.

Several other states have already committed to testing this electronic clearance technology in an attempt to streamline the port-of-entry process. For example:

- Kentucky is leading the Advantage I-75 Project that will place electronic clearance equipment along Interstate 75, which runs from Florida through five other states and into Canada. Since the system has been operating on I-75 for less than one year, the state is just now in the process of evaluating the success of the project and is considering expanding the use of electronic clearance equipment in the state.
- Utah, Oregon, and Idaho have coordinated a combined electronic clearance pilot project along Interstate 84. This project, scheduled for completion in 1997, is planned to clear trucks to travel from Portland to Salt Lake City without being stopped at ports.
- Oregon has developed the Green Light Project, a plan to establish 21 electronic clearance sites by 1997, eventually allowing the state to automatically clear 3 million

vehicles per year. The expected benefits of the project include reducing delays for trucks at the ports, reducing paperwork, and reducing regulatory costs.

Arizona has previously been involved in testing such technology. The State was part of a project that began in 1984 and included a 3-year demonstration project through 5 states, including Arizona, California, New Mexico, Washington, and Texas. During the project period, 33 electronic clearance sites were installed on 2 interstates. In Arizona, 6 sites were developed using transponders and weigh-in-motion scales at the ports to electronically clear trucks. Overall, the project was considered successful; however, little federal funding was available to expand beyond the pilot. Moreover, the transponder technology used in the pilot project is now outdated and the sites are not currently operational, but the weigh-in-motion equipment installed as part of the project is still used by port staff to weigh trucks entering the port. Updated transponder technology is planned for implementation at 4 sites in Arizona, 2 on Interstate 10 and 2 on Interstate 40.

## **Agency Response**



# ARIZONA DEPARTMENT OF TRANSPORTATION

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FIFE SYMINGTON  
Governor

LARRY S. BONINE  
Director

February 11, 1997

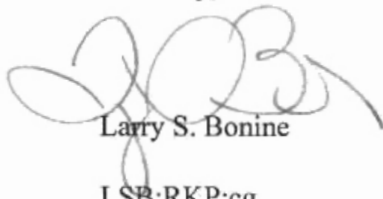
Mr. Douglas Norton  
Auditor General, State of Arizona  
2910 N. 44th Street, #410  
Phoenix, AZ 85018

Dear Mr. Norton:

Attached is the Arizona Department of Transportation's response to the performance audit recently conducted with the ADOT Motor Vehicle Division. Your staff has been most patient and courteous with us during the course of this audit and we appreciate their efforts.

Although we may not fully agree on every point, the performance audit and recommendations have been extremely helpful to improve the effectiveness of the Division's operations.

Sincerely,



Larry S. Bonine

LSB:RKP:cg

Enclosure

cc: Russell Pearce, Motor Vehicle Division



# ARIZONA DEPARTMENT OF TRANSPORTATION

## RESPONSE TO THE REPORT OF THE AUDITOR GENERAL

February 11, 1997

The Arizona Department of Transportation has received and reviewed the Auditor General's performance audit of the Department's revenue functions within its Motor Vehicle Division. The following response addresses, individually, the findings and recommendations contained in the report.

### **Finding One: MVD Needs to Better Protect Cash and Valuables in its Field Offices**

1. *MVD should ensure that adequate policies and procedures are developed regarding all aspects of internal controls, particularly those related to cash-handling, inventory, and deposits.*

ADOT agrees and accepts this recommendation.

The Division has begun a team effort to develop a revised set of cash control policies and procedures designed to mesh the separate sets of rules now being followed. That effort continues, with completion expected by the end of fiscal year 1997.

Specific procedures recommended which will be included in the policy/procedure document include:

- Limiting safe combinations/keys to an essential number of employees only.
  - Limiting the amount of cash that may accumulate in a clerk's drawer during the day.
  - Ensuring that employees are accountable for license plates and tabs assigned to them, with periodic physical counts.
  - Ensuring that plate and tab inventory records are retained.
  - Requiring that daily deposits are prepared by someone with no access to cash, alternating deposit duties between employees (this will be implemented where feasible; we have nine one and two-person facilities in the state where this would not be possible).
2. *MVD should emphasize internal control training of its employees and improve oversight of its field offices to ensure that procedures are being consistently followed.*

ADOT agrees and accepts this recommendation.

Plans are in place to establish a formal Training Academy, which we anticipate implementing during 1997. At that time, we will be returning all field personnel to the classrooms for in-service training. Proper cash handling procedures will certainly be addressed in these sessions, and a new emphasis on cash handling will become standard for new employee training as well.

Following is a list of actions to be taken to implement the recommendations contained in the Auditor General's report:

- New training modules are being developed, including a separate module for cash handling instruction. This will ensure standard procedures across the board.
  - Department employees experienced in the Division's processes will be utilized in the development of these new cash handling procedures to ensure we achieve an acceptable business standard. These employees will be asked to review proposed policy changes and offer recommendations to establish quality guidelines.
  - Follow-up audits will be conducted by Training Academy personnel to ensure students, once returned to the field, are utilizing the skills and standards taught in our training classes.
  - With increased training staff, we will be able to ensure a more timely training of our newly hired employees.
  - We are looking into the possibility of requiring background checks for incumbents being considered for positions involving routine handling of cash.
  - In-service training and refresher courses will also become a Division standard in the new Training Academy.
  - Supervisors will be required to monitor cash handling and inventory procedures during each office visit.
3. *MVD should enhance current computer system controls by providing transaction receipts, monitoring automated cash register activity reports, and continuing to enhance the automated inventory system.*

ADOT agrees and accepts this recommendation.

- We are continuing to research alternative methods of providing receipts to all customers.
- The revised policy/procedures manual will address the requirement that supervisors should monitor activity reports produced by the automated cash register to ensure that transactions are performed correctly and accounted for.
- The planned automated inventory tracking system will accommodate these specific recommendations – that tabs and plates can always be located by serial number; that inventory in office storerooms is recorded; that item quantities can be verified by physical counts; and that clerks are accountable for the items issued to them.

4. *MVD should link the driver's license and the title and registration systems with an automated cash register function when developing a new automated system.*

ADOT agrees and accepts this recommendation.

We are searching for suitable systems which may be developed by other government entities or possible "shrink-wrapped" solutions proposed by industry. The recommended three-way linkage will be a mandate for any new system considered.

5. *ADOT internal auditors should conduct more field office visits to ensure offices are maintaining adequate levels of internal controls.*

ADOT agrees and accepts this recommendation.

Audit and Analysis conducted various audits of MVD offices in the past. During the period of 1991-1995, Audit and Analysis did not expend significant resources auditing MVD operations because of the changes being made and those contemplated. MVD and ASD, however, reviewed MVD field operations for compliance with existing operating procedures.

Since July 1, 1996, Audit and Analysis has conducted nine audits of MVD field operations; during the remainder of fiscal year 1997, 19 audits are planned. In the future, continuous audit resources will be committed to MVD field operations.

### **Finding Two: MVD Should Strengthen Enforcement of Taxes on Motor Carriers**

1. *MVD should increase the use of mobile enforcement crews to better ensure motor carriers comply with the tax laws.*

ADOT agrees and accepts this recommendation.

Enforcement efforts put forth by Arizona's ports of entry and by mobile enforcement units are listed as part of the overall State plan. While the focus is on the ways that MVD could strengthen its enforcement of taxes on motor carriers, it is important to note that, in terms of weight/size enforcement endeavors, MVD is guided by federal standards.

MVD primarily operated only fixed ports until 1995. At that time, a more intense enforcement effort began which was based on tax evasion concerns, better compliance with the Federal Highway Administration (FHWA) weight/size reporting criteria, safeguarding the State's highways, and minimizing the risks to other motorists who might be exposed to unsafe trucks. Accordingly, MVD re-acquired some Department of Public Safety (DPS) portable scale equipment and began a systematic plan to support its fixed ports with mobile scale units which would be used both to enforce motor carrier laws and to collect requisite taxes when appropriate.

- An intergovernmental agreement has been signed between MVD and DPS to establish a joint Motor Carrier Enforcement Task Force. While the exact mission and scope of the task force is still being defined, a main priority will be to place a more aggressive emphasis on all types of motor carrier violations, both on the state's interstate and intrastate highway systems. A main priority of MVD will be directed at curbing tax evasion opportunities by non-compliant commercial vehicle operators.
  - MVD has already acquired portions of its special enforcement mobile unit, SPRINT Port, which will allow officers, as well as DPS staff, to target specific vulnerable locations to ensure that Arizona's motor carrier safety and tax laws are adhered to.
2. *MVD should work in conjunction with the Department's Intermodal Transportation Division to obtain essential traffic data that can be used to better plan and deploy mobile enforcement units. In addition, this data can also be used to determine the need for extended hours of operation for ports of entry that currently are not open on a 24-hour basis.*

ADOT agrees and accepts this recommendation.

The Division agrees that mobile enforcement efforts should utilize the modern technological advantages that are available within the ADOT structure. We will work closely with ADOT's Technical Information Resources (TIR) unit and the Intermodal Traffic Counter units to monitor selected state highways for illegal truck operations and commercial vehicle traffic trends.

- Electronic intelligence gathering equipment (roadway classifiers) has already been utilized for these purposes in conjunction with the Intermodal Transportation Division. Both permanent and semi-permanent roadway monitoring sites have been installed or are projected for future implementation.
- Five new data collection sites have been added this past year for traffic flow information on fixed port bypass routes. These sites will provide information such as the weight, speed and axle configurations on commercial traffic over Arizona's highways.

**Finding III: MVD Needs to Ensure Taxpayers File Reports and Post Adequate Tax Bonds**

1. *MVD should remove inactive accounts from the TARGATS computer system, thus allowing MVD to focus on obtaining returns and tax payments from active taxpayers.*

ADOT agrees and accepts this recommendation. Closed accounts over four years old will be removed from the system.

2. *MVD should regularly identify taxpayers who have not filed returns and mail reminder notices at the end of each reporting period.*

ADOT agrees and accepts this recommendation.

Proposed legislation (HB 2171) would eliminate the use fuel and motor carrier licensing requirement, thus ensuring more time spent on missing reports and current reporting requirements. Missing reports are now identified annually. In the event the proposed legislation is not implemented, the Division's intentions are to do so quarterly.

3. *To ensure the State is adequately protected from taxpayer default, MVD should:*
  - *compare bond information maintained in physical files and the TARGATS computer files and correct any inconsistencies;*
  - *revise its computer program to calculate the minimum required bond amounts according to the Division's administrative rules; and*
  - *use the program regularly to calculate the required taxpayer bonds and inform taxpayers of the new bond amount.*

ADOT agrees and accepts this recommendation.

Proposed legislation (HB 2171) would eliminate bonding requirements. In the event the proposed legislation is not implemented, the Division's intentions are to check bond information at the time of renewal and through monthly reports and audits. The computer program will be rewritten as recommended, and bond amounts will be reviewed at the time of renewal or when reports are submitted. Taxpayers will be notified when an increase in bond amount is warranted and given 60 days to comply; those who fail to comply will be referred to the collections unit.

#### **Finding IV: MVD Should Continue Recent Efforts to Enhance its Collection of Delinquent Taxes**

1. *MVD should establish a formal mechanism to guide collectors in the revenue collection function by:*
  - *completing its revision of the collections unit's policies and procedures manual, and*
  - *completing and formalizing performance measures.*

ADOT agrees and accepts this recommendation.

Desk procedures are being written in the collections unit to address areas where no previous policies existed (e.g., settlements, write-offs). The collections unit is working on revisions to existing procedures resulting from a process/measurement improvement effort.

2. *MVD should monitor the collection unit's performance on a regular basis by:*

- *ensuring that collectors follow the policies and procedures to collect delinquent revenues,*
- *compiling revenue collection information and comparing it against established performance measures, and*
- *reviewing collectors' files to ensure appropriate and timely use of collections techniques.*

ADOT agrees and accepts this recommendation.

- Random selection of delinquent accounts will be reviewed to ensure proper guidelines are being followed.
- Established measurements are being compared against current monthly collection statistics.
- All collectors' reports are now entered into a data base and reviewed on a monthly basis to ensure proper use of collection techniques.

### **Other Pertinent Information**

Included in the Auditor General's report is information on "Revenue Collection Systems and the Enterprise Computer Project." In addition to the information in the report, the Department also provides the following:

- The Enterprise Project included a significant effort to analyze and improve MVD business processes. Significant benefits were derived from this effort which are presently being realized. For example, the extended driver license and allocated car rental program have generated significant revenue for the Highway User Revenue Fund.
- The project is presently in a "stand-down" status because (1) of the legal dispute with the contractor, CACI, and (2) the "Year 2000" problem dominates the information technology market creating a poor environment for system development projects at this time. The Department continues to explore and evaluate alternatives to achieving its ultimate goal of combining Driver License and Title & Registration information into one data base. As part of this effort, the Department will continue to monitor the progress of other states which are presently developing similar type systems.

The Department will continue to assess its options in light of its legal position, availability of new technology and development of similar systems in other states to provide an efficient and effective replacement of the existing Driver License and Title & Registration system.

# APPENDIX

## MAJOR SOURCES OF HIGHWAY USER REVENUES

### Overview

Highway financing in Arizona is comprised of a variety of taxes and fees relating to motor vehicles of all types. The major sources of revenue include gasoline and diesel fuel taxes, motor carrier taxes, vehicle license taxes, and registration fees. The majority of HURF revenues, 55 percent, are generated from fuel taxes, including both gasoline and diesel fuels. Vehicle license taxes account for 19 percent, registration fees account for 11 percent, and motor carrier taxes contribute 10 percent of total HURF revenues.

### Major Sources of Revenue

Information on the amount of revenue generated, tax rates, point of collection, and administration methods and evasion rates (where available) are presented below for each tax type:

#### Motor Vehicle Fuel (Gasoline) Tax

Revenue Generated: \$359 million in fiscal year 1995-96

Tax Rate: 18 cents per gallon

Point of Collection: Collected from the distributor.

Tax Administration: Gasoline taxes are considered easy to administer and enforce by ADOT staff because there are a small number of taxpayers (i.e., 196 distributors) to monitor.

Risk of Evasion: Gasoline taxes represent a low evasion risk because most of the gasoline is shipped into the State by pipelines that ADOT can easily monitor. Nationally, the Federal Highway Administration estimates evasion of this tax to be 3 to 7 percent.

#### Use (Diesel) Fuel Tax

Revenue Generated: \$89 million in fiscal year 1995-96

Tax Rate: 18 cents per gallon for all diesel fuel burning vehicles, except agricultural and highway construction vehicles, which are exempt from the tax.

**Point of Collection:** Collected from the distributor before the fuel is delivered to the vendor. The fuel users ultimately pay the tax at the pump to the gasoline vendors, such as truck stops and service stations.

**Tax Administration:** MVD is responsible for licensing, monitoring, and auditing the 196 distributors and 252 fuel vendors currently operating in the State to ensure proper collection of the tax.

**Risk of Evasion:** The risk of an individual motor carrier evading this tax is low, since the tax is included in the price at the pump. ADOT has not studied the risk of evasion by fuel vendors.

**(Diesel) Fuel Surcharge**

**Revenue Generated:** \$26 million in fiscal year 1995-96

**Tax Rate:** 8 cents per-gallon surcharge for each gallon of fuel used in the State by vehicles weighing over 26,000 pounds. The surcharge is in addition to the 18 cent per-gallon tax paid on the purchase of use fuel at the pump.

**Point of Collection:** Paid by the individual motor carriers by self-report to MVD. Periodically, the carriers report the gallons of fuel burned while traveling in Arizona and submit the amount due to MVD. For example, a carrier may report that its vehicles burned 1,000 gallons of use fuel in the State and remit the \$80 due (1,000 x .08) to the State.

**Tax Administration:** The tax is administered in two ways depending on the State in which the motor carrier bases its business. First, MVD licenses, monitors, and audits the 6,000 motor carriers based in Arizona who report taxes owed directly to Arizona. Second, MVD also receives revenue from out-of-state carriers who report to their home state, but owe taxes to Arizona for fuel used in the State. These carriers report and submit taxes due under the International Fuel Tax Agreement (IFTA), which allows carriers to report to their base state, which then distributes the revenues due to Arizona's MVD.

**Risk of Evasion:** Since this tax is self-reported by the motor carrier, it has a higher risk of evasion. A 1996 consultant's report estimated the rate of tax evasion for 1994 to be about 15 to 19 percent of total revenues for this tax.

**Motor Carrier (Weight Distance) Tax**

**Revenue Generated:** \$85 million in fiscal year 1995-96

**Tax Rate:** The calculation of this tax is fairly complex, since it is based both on the weight of the vehicle and the number of miles traveled in Arizona. The tax applies to vehicles that weigh in



Point of Collection:	excess of 12,000 pounds. For vehicles weighing between 12,000 and 26,000 pounds, the tax ranges from \$64 to \$119 per year, depending on vehicle weight. For vehicles weighing over 26,000 pounds, the tax rate is between 1 cent and 6 cents per mile traveled in the State based on vehicle weight. By statute, the motor carrier tax rate can be adjusted each year.
Tax Administration:	Tax is collected from the motor carrier when reporting number of miles driven in Arizona for the reporting period. Depending on their tax liability, carriers report monthly, quarterly, semi-annually, or annually. The lower the tax liability, the less frequently the carrier must report.
Risk of Evasion:	MVD is responsible for establishing, monitoring, and auditing the 22,000 motor carrier tax accounts. The weight distance tax is considered the hardest transportation tax to administer, due to its complex calculation and the large number of tax accounts to monitor. In fact, Arizona is one of only six states that administers a weight distance tax. Many other states rely primarily on fuel taxes to fund highway needs.
	The motor carrier tax is considered to be the easiest to evade because the tax liability is self-reported by the carriers. According to a 1996 consultant's study, the estimated rate of evasion could be as high as 35 percent.

**Vehicle License Tax (VLT):**

Revenue Generated:	\$160 million in fiscal year 1995-96. This is the amount HURF receives, which is only 31.5 percent of the total revenues generated by the VLT. The remaining monies are distributed to the State General Fund for general and educational purposes, and to the counties and local governments.
Tax Rate:	\$4 per \$100 of the assessed value for all vehicles.
Point of Collection:	Tax is collected directly from owners, generally through MVD offices.
Tax Administration:	MVD collects the VLT from the vehicle owner at the time the vehicle is initially registered and upon each registration renewal.
Risk of Evasion:	According to ADOT estimates, the evasion rate for the VLT is about 5 percent.

**Registration Fee:**

Revenue Generated:	\$98 million in fiscal year 1995-96
Tax Rate:	\$8 per year to register most vehicles, \$9 per year for motorcycles, and a graduated amount, based on weight, to register

Point of Collection:	vehicles weighing over 12,000 pounds, up to \$1,070 to register those over 26,000 pounds. Tax is collected directly from the vehicle owner upon registration, mostly through MVD offices.
Tax Administration:	MVD collects the fee when vehicle owners apply for Arizona license plates. In addition, MVD sends renewal notices to the owners of Arizona's 3 million registered vehicles, and provides a validator tab for the owner to place on the license plate as proof of renewal. In most cases, the fee is collected annually; however, recent legislation allows MVD to register some vehicles every two years.
Risk of Evasion:	The risk of evasion appears to be low. The rate of evasion appears to be similar to the VLT, since the VLT is collected at the time of registration.