

Oklahoma Tax Commission - Basic Financial Statements and Independent Auditor's Report

JULY 1, 2006 THROUGH JUNE 30, 2007



FINANCIAL STATEMENT AUDIT



Jeff A. McMahan

Oklahoma State Auditor
& Inspector

**OKLAHOMA TAX COMMISSION
FINANCIAL STATEMENTS AND
INDEPENDENT AUDITOR'S REPORTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2007**

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STATE OF OKLAHOMA
OFFICE OF THE AUDITOR AND INSPECTOR

JEFF A. McMAHAN
State Auditor and Inspector

February 29, 2008

TO THE HONORABLE BRAD HENRY
GOVERNOR OF THE STATE OF OKLAHOMA

Transmitted herewith is our report on the Oklahoma Tax Commission financial statements for the fiscal year ended June 30, 2007. The audit was conducted in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, issued by the Comptroller General of the United States.

We wish to take this opportunity to express our appreciation for the assistance and cooperation extended to our office during the course of the audit.

The Office of the State Auditor and Inspector is committed to serving the public interest by providing independent oversight and issuing reports that serve as a management tool to the state to ensure a government which is accountable to the people of the State of Oklahoma.

Sincerely,

A handwritten signature in black ink that reads "Michelle R. Day". The signature is written in a cursive style.

Michelle R. Day, Esq.
Deputy State Auditor and Inspector

**OKLAHOMA TAX COMMISSION
FINANCIAL STATEMENTS AND
INDEPENDENT AUDITOR'S REPORTS
FOR THE YEAR ENDED JUNE 30, 2007**

Table of Contents

	Page
Management's Discussion and Analysis	1
Report of the State Auditor and Inspector	6
Basic Financial Statements	
<i>Government-Wide Financial Statements:</i>	
Statement of Net Assets	8
Statement of Activities	9
<i>Fund Financial Statements:</i>	
Balance Sheet – Governmental Funds and Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Assets	10
Statement of Revenues, Expenditures, and Changes in Fund Balances – Governmental Funds and Reconciliation of the Change in Fund Balances of Governmental Funds to the Statement of Activities.....	11
Statement of Net Assets – Fiduciary Funds.....	12
Notes to Basic Financial Statements.....	13
Required Supplementary Information	23
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters.....	26

Management's Discussion and Analysis

As management of the Oklahoma Tax Commission, we offer readers of the Agency's financial statements this overview and analysis of the financial activities for the fiscal year ended June 30, 2007.

FINANCIAL HIGHLIGHTS

- Total net assets of the Agency decreased 2% to (\$10.3) million during the fiscal year ending June 30, 2007. The primary reason for the decline was a deficit in the Ad Valorem Reimbursement Fund. Reimbursements from the fund exceeded cash resources available at June 30, 2007. This fund is a pass-through to counties and schools and is not used for the general operations of the Agency.
- The Agency program revenues for the fiscal year increased 8.5% or \$2.2 million over the prior year while expenses increased \$10.8 million or 8.6%. The increase in program revenues is primarily attributable to an increase in revolving fund collections during Fiscal Year 2007.
- The assets of fiduciary funds, which represent taxes held in trust for distribution to state and local governments and others, totaled \$1.2 billion at June 30, 2007.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of three parts – management's discussion and analysis (this section), the basic financial statements, and required supplementary information. The basic financial statements include two kinds of statements that present different views of the Agency.

The first two statements are government-wide financial statements that provide both long-term and short-term information about the Agency's overall financial status.

The remaining statements are fund financial statements that focus on individual parts of the Agency, reporting the Agency's operations in more detail than the government-wide statements.

- The governmental statements tell how the general government services were financed in the short term as well as what remains for future spending.
- Fiduciary fund statements provide information about the financial relationships in which the agency acts solely as trustee or agent for the benefit of others, to whom the resources in question belong.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of required supplementary information that further explains and supports the information in the financial statements.

Government-wide Statements

The government-wide statements report information about the Agency as a whole using accounting methods similar to those used by private-sector companies. The statement of net assets includes all of the Agency's assets and liabilities. All of the current year's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two government-wide statements report the Agency's net assets and how they have changed. Net assets -- the difference between the Agency's assets and liabilities -- is one way to measure the Agency's financial health, or position.

- Over time, increases or decreases in the Agency's net assets are an indicator of whether its financial health is improving or deteriorating, respectively.
- To assess the overall health of the Agency you need to consider additional non-financial factors such as changes in administrative requirements added by legislation and changes in state and local tax rates and the overall tax base.

The government-wide financial statements of the Agency consist of only one category:

- Governmental activities -- All of the basic activities are included here, such as the general administration, taxpayer services, tax return processing, audit and compliance.

Fund Financial Statements

The fund financial statements provide more detailed information about the Agency's most significant funds -- not the Agency as a whole. Funds are accounting devices that the Agency uses to keep track of specific sources of funding and spending for particular purposes.

All funds are required by State law. The Agency has two kinds of funds:

- Governmental funds -- Most of the Agency's basic services are included in governmental funds, which focus on (1) how cash and other financial assets that can readily be converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the Agency's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, we provide additional information at the bottom of the governmental funds statement that explains the relationship (or differences) between them.
- Fiduciary funds -- The Agency is the trustee, or fiduciary, for taxes levied by local governments and the majority of all state taxes levied for funding the essential services and infrastructure of the State Government of Oklahoma. The Agency is responsible for ensuring that the assets reported in these funds are apportioned or distributed as provided by law. All of the Agency's fiduciary activities are reported in a separate statement of fiduciary net assets. We exclude these activities from the Agency's government-wide financial statements because the Agency cannot use these assets to finance its operations.

FINANCIAL ANALYSIS OF THE AGENCY AS A WHOLE

Net assets

The Agency's combined net assets decreased between fiscal years 2006 and 2007 to (\$10.3) million. Table A-1 illustrates the changes between the two years in more detail.

TABLE A-1
Oklahoma Tax Commission's Net Assets
(in millions of dollars)

	<u>Governmental Activities</u>		<u>Percentage Change</u>
	<u>2006</u>	<u>2007</u>	<u>2006 - 2007</u>
Current and other assets	\$40.5	\$8.3	(79.5)%
Capital assets	<u>2.4</u>	<u>3.8</u>	58.3%
Total assets	42.9	12.1	(71.8)%
Long-term liabilities	3.2	3.4	6.2%
Other liabilities	<u>49.8</u>	<u>18.9</u>	(62.0)%
Total liabilities	53.0	22.3	(57.9)%
Net assets			
Invested in capital assets	2.4	3.8	58.3%
Unrestricted	<u>(12.5)</u>	<u>(14.1)</u>	(12.8)%
Total net assets	<u>(10.1)</u>	<u>(10.3)</u>	(2.0)%

Net assets of the Agency's governmental activities decreased 2% to (\$10.3) million. Unrestricted net assets showed a \$1.6 million decrease during the year due to constitutionally required reimbursements to counties from the Ad Valorem Reimbursement Fund as specified in 74 O.S. 2001, Section 194. Obligations for these reimbursements exceeded available funding at year-end.

Statement of Activities

The Agency's program revenues for the fiscal year ending June 30, 2007 increased 8.5% or \$2.2 million over the prior year while expenses increased \$10.8 million or 8.6%. The increase in program revenues is primarily attributable to an increase in retention from city and county sales tax collections.

See Table A-2 below.

TABLE A-2
Comparison of Revenues and Expenses
(in millions of dollars)

	<u>2006</u>	<u>2007</u>	<u>Percentage Change 2006 - 2007</u>
Program Revenues:			
Charges for Services	\$ 25.3	\$ 28.1	11.1%
Grants	.7	.1	(85.7)%
General Revenues:			
Taxes	31.3	34.1	8.9%
Fees	4.8	5.1	6.3%
Other	<u>.2</u>	<u>.1</u>	(50.0)%
Total Revenues	\$ 62.3	\$ 67.5	8.3%
State Appropriations	45.6	47.7	4.6%
Transfers In	11.7	20.6	76.1%
Expenses:			
General Government	(124.8)	(135.5)	8.6%
Depreciation	<u>(.4)</u>	<u>(.5)</u>	25.0%
Total Expenses	(125.2)	(136.0)	8.6%
Change in Net Assets	(5.6)	(.2)	(96.4)%

Fiduciary Fund Statements

The Agency, acting on statutory authority and contractual agreements, collects taxes, licenses and fees, which are distributed to state and local governments and private entities. At June 30, 2007 the Agency maintained as a fiduciary \$1.2 billion in total assets for others. Of that amount \$3 million was due to taxpayers for refunds and the balance is due to state entities, local government subdivisions and private entities.

BUDGET INFORMATION

Budget versus Actual Variances

Budgeted charges to appropriations for the fiscal year exceeded actual totals by \$275,144 while actual resources available were lower than budgeted resources by \$17,684,598 resulting in a negative overall variance of \$17,409,454. The primary reason for the overall negative variance was because actual expected deposits from collection agency fees were significantly lower than budgeted reimbursements and available funds were less than actual reimbursements to counties and schools from the Ad Valorem Reimbursement Fund. A variance of \$36.6 million occurred between the original and final budget of the Ad Valorem Reimbursement Fund. The increase resulted from additional funds made available by the legislature in the last quarter of fiscal year 2007 and the use of deposits to the fund subsequent to year-end.

Next Year's Budget

The Agency budget for Fiscal Year 2008 was developed with available appropriations and estimated income from tax collections and fees associated with operating activities. The original budget totaled \$101.3 million, down \$36.3 million from the final budget of \$137.6 million for Fiscal Year 2007. The decrease in budget between Fiscal Years 2007 and 2008 consists primarily of a reduction in the amount available for reimbursements from the Ad Valorem Reimbursement Fund.

Of the \$101.3 million total budget, \$76.1 is designated as General Fund, representing expenditures necessary for the performance of the Agency's statutory functions, and auditing, collection and legal activities. The remaining \$25.2 million consists of \$19.7 million for the Ad Valorem Reimbursement Fund, \$5.3 million for the Waste Tire Indemnity Fund and \$200,000 for the Film Enhancement Rebate Fund.

CONTACTING THE AGENCY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and the executive and legislative branches with a general overview of the Agency's finances and to demonstrate the Agency's accountability for the money it receives. If you have questions about this report or need additional information, contact the Oklahoma Tax Commission Comptroller's Office at 2501 North Lincoln, Oklahoma City, OK 73194.



STATE OF OKLAHOMA
OFFICE OF THE AUDITOR AND INSPECTOR

JEFF A. McMAHAN
State Auditor and Inspector

INDEPENDENT AUDITOR'S REPORT

**TO THE COMMISSIONERS OF THE
OKLAHOMA TAX COMMISSION**

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Oklahoma Tax Commission (OTC), as of and for the year ended June 30, 2007, which collectively comprise OTC's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the OTC's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the OTC's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the OTC, as of June 30, 2007, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 12, 2008, on our consideration of the OTC's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our

testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis on pages 1 through 5 and budgetary comparison information on pages 23 through 25 are not a required part of the basic financial statements, but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

A handwritten signature in black ink that reads "Michelle R. Day". The signature is written in a cursive style with a large initial "M".

Michelle R. Day, Esq.
Deputy State Auditor and Inspector

February 12, 2008

OKLAHOMA TAX COMMISSION
STATEMENT OF NET ASSETS
JUNE 30, 2007

	<u>Governmental Activities</u>
ASSETS	
Current Assets:	
Cash	\$1,827,055
Investments	50,349
Accounts receivable	6,513
Taxes & fees receivable	6,233,954
Inventory	137,078
Total Current Assets	<u>8,254,949</u>
Noncurrent Assets:	
Capital assets (Net of accumulated depreciation)	<u>3,776,245</u>
Total Noncurrent Assets	<u>3,776,245</u>
TOTAL ASSETS	<u><u>\$12,031,194</u></u>
 LIABILITIES	
Current Liabilities:	
Accounts Payable	\$18,686,841
Deferred Revenue	39
Accrued Payroll	91,215
Compensated Absences	164,187
Total Current Liabilities	<u>18,942,282</u>
Noncurrent Liabilities:	
Compensated Absences	<u>3,425,404</u>
Total Noncurrent Liabilities	<u>3,425,404</u>
TOTAL LIABILITIES	<u><u>22,367,686</u></u>
 NET ASSETS	
Invested in Capital Assets	3,776,245
Unrestricted (deficit)	<u>(14,112,737)</u>
TOTAL NET ASSETS	<u><u>(\$10,336,492)</u></u>

The notes to the financial statements are an integral part of this statement.

OKLAHOMA TAX COMMISSION
STATEMENT OF ACTIVITIES
JUNE 30, 2007

Functions/Programs	Expenses	Program Revenues		Net (Expense) Revenue and Changes in Net Assets
		Charges For Services	Operating Grants and Contributions	
Governmental Activities				
General Government	\$135,429,794	\$28,087,138	\$33,084	(\$107,309,572)
Depreciation Expense	521,683			(521,683)
Total Governmental Activities	135,951,477	28,087,138	33,084	(107,831,255)
General Revenues:				
Taxes:				
Personal and Corporate Income				34,084,411
Fees:				
Waste Tire				5,147,450
Other				32,036
State Appropriations				47,711,604
Transfers In				20,600,000
Total Revenues				107,575,501
Change in Net Assets				(255,754)
Net Assets - beginning				(10,081,819)
Prior Year Adjustment				1,081
Net Assets - ending				(\$10,336,492)

The notes to the financial statements are an integral part of this statement.

**OKLAHOMA TAX COMMISSION
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2007**

	General Fund	Waste Tire Indemnity Fund	Ad Valorem Reimbursement Fund	Total Governmental Funds
ASSETS				
Cash	\$1,799,890		\$27,165	\$1,827,055
Investments		\$50,349		50,349
Accounts receivable			6,513	6,513
Taxes and fees receivable	1,221,173	19,923	4,992,858	6,233,954
Inventory	137,078			137,078
TOTAL ASSETS	\$3,158,141	\$70,272	\$5,026,536	\$8,254,949
LIABILITIES				
Accounts Payable	\$2,092,968	\$473,648	\$16,120,225	\$18,686,841
Deferred Revenue	39			39
Accrued Payroll	91,215			91,215
Compensated Absences	24,466			24,466
TOTAL LIABILITIES	2,208,688	473,648	16,120,225	18,802,561
FUND BALANCES				
Reserved for Encumbrances	25,137			25,137
Reserved for Inventory	137,078			137,078
Unreserved	787,238	(403,376)	(11,093,689)	(10,709,827)
TOTAL FUND BALANCES	949,453	(403,376)	(11,093,689)	(10,547,612)
TOTAL LIABILITIES AND FUND BALANCES	\$3,158,141	\$70,272	\$5,026,536	\$8,254,949

**Reconciliation of the Governmental Funds Balance Sheet to the
Statement of Net Assets
June 30, 2007**

Total Fund Balances - Governmental Funds	(\$10,547,612)
Amounts reported for governmental activities in the statement of net assets are different because:	
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds: These consist of:	
Furniture and Equipment	12,349,074
Accumulated Depreciation	(8,572,830)
Some liabilities are not due and payable in the current period and therefore are not reported in the funds. Those liabilities consist of:	(3,565,124)
Compensated Absences	(3,565,124)
Net Assets of Governmental Activities	<u>\$10,336,492</u>

The notes to the financial statements are an integral part of this statement.

OKLAHOMA TAX COMMISSION
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
June 30, 2007

	General	Waste Tire Indemnity Fund	Ad Valorem Reimbursement Fund	Total Governmental Funds
Revenues				
Taxes	\$24,335,663		\$34,084,411	\$58,420,074
Licenses Permits and Fees	3,681,730	\$5,147,450		8,829,180
Federal Revenue	33,084			33,084
Other	69,745	4,871	27,165	101,781
Total Revenues	<u>28,120,222</u>	<u>5,152,321</u>	<u>34,111,576</u>	<u>67,384,119</u>
Expenditures				
Current:				
Salaries and Benefits	51,538,770			51,538,770
Professional Services	7,404,922			7,404,922
Inter-Agency Personal Services	58,846			58,846
Travel	827,211			827,211
Miscellaneous Administrative	5,498,733			5,498,733
Rent of Buildings and Equipment	3,274,325			3,274,325
Maintenance	3,497,506			3,497,506
Supplies	3,082,007			3,082,007
Waste Tire Payments		5,222,802		5,222,802
Building Renovation	55,139			55,139
Payments to Local Governments	356,740		52,733,717	53,090,457
Other Expenditures	201,303			201,303
Capital Outlay:				
Equipment	3,360,639			3,360,639
Total Expenditures	<u>79,156,141</u>	<u>5,222,802</u>	<u>52,733,717</u>	<u>137,112,660</u>
Revenues Over (Under) Expenditures	<u>(51,035,919)</u>	<u>(70,481)</u>	<u>(18,622,141)</u>	<u>(69,728,541)</u>
Other Financing Sources (Uses)				
State Appropriations	47,711,604			47,711,604
Transfers In	1,800,000		18,800,000	20,600,000
Total Other Financing Sources (Uses)	<u>49,511,604</u>	<u>0</u>	<u>18,800,000</u>	<u>68,311,604</u>
Net Change in Fund Balances	(1,524,315)	(70,481)	177,859	(1,416,937)
Fund Balance - Beginning of Year	2,473,768	(332,895)	(11,271,548)	(9,130,675)
Fund Balance - End of Year	<u>\$949,453</u>	<u>(\$403,376)</u>	<u>(\$11,093,689)</u>	<u>(\$10,547,612)</u>

Reconciliation of the change in fund balances of governmental funds to the Statement of Activities
June 30, 2007

Net change in fund balances - total governmental funds	(\$1,416,937)
Amounts reported for governmental activities in the statement of activities are different because:	
Capital outlays are reported as expenditures in the governmental funds. However, in the statement of activities, the cost of capital assets is allocated over their estimated useful lives as depreciation expense.	1,347,126
Some items reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds. These consist of an increase in compensated absences.	(185,943)
Change in net assets of governmental activities	<u>(\$255,754)</u>

The notes to the financial statements are an integral part of this statement.

**OKLAHOMA TAX COMMISSION
STATEMENT OF FIDUCIARY NET ASSETS
AGENCY FUND
JUNE 30, 2007**

ASSETS	
Cash	\$612,886,820
Investments	309,344,778
Accounts receivable	1,284,563
Taxes receivable	256,366,276
TOTAL ASSETS	<u><u>\$1,179,882,437</u></u>
LIABILITIES	
Tax Refunds Payable	\$2,952,225
Due to State General Funds	916,372,399
Due to Enterprise Funds	3,585,718
Due to Pension Trust Funds	36,195,752
Due to Other Accounts	4,954,027
Due to Local Governments	197,961,056
Due to Others	16,126,500
Amount to be Apportioned	1,734,760
TOTAL LIABILITIES	<u><u>\$1,179,882,437</u></u>

The notes to the financial statements are an integral part of this statement.

OKLAHOMA TAX COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
INDEX

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

- A. Reporting Entity
- B. Basis of Presentation
- C. Measurement Focus and Basis of Accounting
- D. Assets, Liabilities and Equity
- E. Program Revenues

NOTE 2. PENSION PLAN

NOTE 3. DEPOSITS AND INVESTMENTS

- A. Deposits
- B. Investments

NOTE 4. CAPITAL ASSETS

NOTE 5. OPERATING LEASE COMMITMENTS

NOTE 6. DUE TO OTHER FUNDS

NOTE 7. RISK MANAGEMENT

NOTE 8. LONG-TERM OBLIGATIONS

NOTE 9. LITIGATION AND CONTINGENCIES

NOTE 10. NET ASSETS DEFICIT

**OKLAHOMA TAX COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2007**

1. Summary of Significant Accounting Policies

The Oklahoma Tax Commission complies with generally accepted accounting principles (GAAP). Generally accepted accounting principles include all relevant Governmental Accounting Standards Board (GASB) pronouncements. The accounting and reporting framework and the more significant accounting policies are discussed in subsequent sections of this Note.

A. Reporting Entity

The Oklahoma Tax Commission, as established under 68 O.S. § 101 et seq., is a part of the primary government of the State of Oklahoma. The Oklahoma Tax Commission is composed of three members appointed by the Governor with the advice and consent of the State Senate, for six year terms. No more than two members of the Tax Commission shall be, or shall have been in the previous six months, members of the same political party.

The Oklahoma Tax Commission shall appoint an administrator who serves at the pleasure of the Commission and who shall be the administrative officer of the Commission and manage the activities of the employees.

The Commission is a full-time working body which is responsible for the administration and enforcement of state tax laws, the collection of a majority of all state-levied taxes, fees, and licenses, and the subsequent apportionment and allocation of revenue designated for various state agencies and local units of government. In its quasi-judicial capacity, the Commission has the authority to subpoena witnesses and records, administer oaths, and render decisions appealable directly to the State Supreme Court.

The organizational make-up of the Oklahoma Tax Commission includes three separate departments. These departments include Taxpayer Services, Revenue Administration, and Support Services. The Taxpayer Services department includes Taxpayer Assistance, Communications, Central Processing, and Account Maintenance. The Revenue Administration department includes Tax Policy, Compliance, Motor Vehicle, and Ad Valorem. The Support Services department includes Human Resources, Information Technology, Legal, and Management Services.

COMMISSION MEMBERS

Thomas E. Kemp, Jr., Chairman
Term Expires January, 2013

Jerry Johnson, Vice Chairman
Term Expires January, 2009

Connie Irby, Secretary-Member
Term Expires January, 2011

ADMINISTRATOR

Tony Mastin, Administrator to the Commission

**OKLAHOMA TAX COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2007**

1. Summary of Significant Accounting Policies (cont...)

B. Basis of Presentation

Government-Wide Financial Statements:

The statement of net assets and statement of activities display information about the reporting government as a whole. They include all funds of the reporting entity except for fiduciary funds. The Agency is involved only in governmental activities. Governmental activities are generally financed through taxes, intergovernmental revenues and other non-exchange revenues.

Fund Financial Statements:

Fund financial statements of the reporting entity are organized into funds each of which is considered to be separate accounting entities. Each fund is accounted for by providing a separate set of self-balancing accounts which constitute its assets, liabilities, fund equity, revenues, and expenditure/expenses. Funds are organized into categories: governmental and fiduciary. An emphasis is placed on major funds within the governmental category. A fund is considered major if it is the primary operating fund of the Agency or meets the following criteria:

1. Total assets, liabilities, revenues, or expenditures/expenses of that individual governmental fund are at least 10 percent of the corresponding total for all funds of that category or type, and
2. Total assets, liabilities, revenues, or expenditures/expenses of the individual governmental fund are at least 5 percent of the corresponding total for all governmental funds combined.

The funds of the financial reporting entity are described below:

Governmental Funds

General Fund

The General Fund is the primary operating fund of the Agency and is always classified as a major fund. It is used to account for all activities except those legally or administratively required to be accounted for in other funds.

Special Revenue Funds

Special revenue funds are used to account for the proceeds of specific revenue sources that are legally or administratively restricted to expenditures for certain purposes.

**OKLAHOMA TAX COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2007**

1. Summary of Significant Accounting Policies (cont...)

In the fund financial statements all governmental funds are accounted for using a current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (e.g., revenues and other financing sources) and decreases (e.g., expenditures and other financing uses) in net current assets.

Basis of Accounting

In the government-wide Statement of Net Assets and Statement of Activities governmental activities are presented using the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset used. Revenues, expenses, assets and liabilities resulting from exchange transactions are recognized when the exchange takes place.

In the fund financial statements, all governmental funds are maintained and reported on the modified accrual basis of accounting while agency funds are presented using the accrual basis of accounting. Under the modified accrual basis of accounting, revenues and related current assets are recognized when measurable and available to finance operations during the year or liquidate liabilities existing at the end of the year; expenditures and liabilities are recognized when obligations are incurred as a result of receipt of goods and services. Revenues are recognized as available when collected within 60 days of year-end. Modifications to the accrual basis of accounting include:

- Employees' vested annual leave is recorded as expenditures when utilized. The amount of accumulated annual leave unpaid at June 30, 2007, has been reported in the Statement of Net Assets.
- Executory purchase orders and contracts are recorded as a reservation of fund balance.

D. Assets, Liabilities, and Equity

Inventories

Inventories are valued at cost. The flow assumption used to determine cost is weighted average. The costs of inventories for the Oklahoma Tax Commission are recorded as expenditures when purchased. Reported inventories are equally offset by a fund balance reserve, which indicates that it does not constitute available spendable resources even though it is a component of total assets.

Capital Assets

The Department of Central Services (formerly the Office of Public Affairs), in accordance with 74 O.S. 2001, § 110.1 of the Oklahoma Statutes has primary responsibility to maintain control of all

**OKLAHOMA TAX COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2007**

1. Summary of Significant Accounting Policies (cont...)

property and equipment owned by the State of Oklahoma with a cost in excess of \$500. The Department of Central Services has delegated to each of the various state agencies the responsibility to maintain the accounting records for property and equipment purchased and used by each agency. Capital assets held by the Oklahoma Tax Commission and reflected in the accompanying financial statements are stated at original cost or estimated cost as determined from available records maintained by the Commission net of accumulated depreciation. Assets valued by estimate represent less than one percent of total capitalized assets. The asset values were based on equipment fair market values at the time of acquisition.

Additional capital asset disclosures are presented in Note 4.

Compensated Absences

Employees earn annual vacation at the average rate of 10 hours per month for up to 5 years service and may accumulate to a maximum of 240 hours. Employees earn an average of 12 hours per month for 5 to 10 years, an average of 13.33 hours per month for 10 to 20 years, and an average of 16.67 hours per month for over 20 years of service. Annual leave for employees over 5 years service may accumulate to a maximum of 480 hours. All accrued annual leave is payable upon layoff, resignation, retirement, or death.

The general fund records expenditures when the employee is paid for annual leave, and the cost of accumulated annual leave is recorded in the statement of net assets. Payments for employee vested annual leave for the year-ended June 30, 2007, were made in the amount of \$181,054. Total amount outstanding at June 30, 2007, is \$3,589,591 of which \$3,425,404 is recorded as a long-term liability.

Reserve for Encumbrances

The reserve for encumbrances represents executed but unperformed purchase orders. In the accompanying governmental fund balance sheet, encumbrances are recorded as a reserve of fund balance if expected to be presented for payment by November 15 following the end of the fiscal year.

E. Program Revenues

In the Statement of Activities, revenues are derived directly from governmental activities and reported as program revenue.

The agency has the following types of program revenues in the governmental activities:

Charges for Services	Statutorily the Agency is authorized to retain a percentage or fee associated with certain tax collections such as sales and use taxes, levied by local governments and collected through a contractual agreement by the Agency. These types of revenues are specifically related to the government activity program.
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**OKLAHOMA TAX COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2007**

1. Summary of Significant Accounting Policies (cont...)

Operating Grants
and Contributions

The Agency participates in a federal grant program for the purpose of reimbursing direct expenses relating to motor fuel audits for tax evasion identification and compliance. These revenues are specifically attributed to the governmental activity.

2. Pension Plan

Plan Description. Substantially all of the Oklahoma Tax Commission full-time state employees participate in the Oklahoma Public Employees Retirement Plan (the Plan), a division of the Oklahoma Public Employees Retirement System (OPERS), a multiple-employer cost-sharing defined benefit public employee retirement system. The official text governing the operation of the system, contributions, and the payment of benefits is found in Title 74, O.S. 2001, § 901, et. seq. OPERS issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. This report can be obtained by writing to OPERS, PO Box 53007, Oklahoma City, Oklahoma 73105 or by calling 1-800-733-9008.

Funding Policy. The contribution rates for each member category of the Plan are established by and can be amended by the Oklahoma Legislature and are based on an actuarial calculation, which is performed to determine the adequacy of contribution rates. Active members for fiscal year 2007 made a 3.5% contribution on wages. State agencies contributed 12.5% of active members' monthly salaries for fiscal year 2007. Contributions from the agency for fiscal years 2005, 2006 and 2007 totaled \$3,227,425, \$3,852,157 and \$4,522,193, respectively, equal to the established required contributions for each year.

- 2.1.1 **Other Post-Employment Benefits (OPEB).** In addition to the pension benefits described in Note 2, the State provides post-retirement health care benefits to retirees. The Oklahoma Public Employees Retirement System (OPERS) by which the Oklahoma Tax Commission employees are covered, provides \$105 per month for all retirants who elect coverage at time of retirement. There is no OPEB obligation information available specific to the Oklahoma Tax Commission.

3. Deposits and Investments

At June 30, 2007, all cash and investments under the control of the State Treasurer were collateralized in accordance with 62 O.S. 2001, § 72.1, titled, "Security For Public Deposits Act."

A. Deposits

As of June 30, 2007, the bank balances of deposits are fully insured or collateralized with securities held by the State's agent in the State's name.

**OKLAHOMA TAX COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2007**

3. Deposits and Investments (cont...)

B. Investments

The State Treasurer maintains two investment portfolios. The Treasurer's Portfolio, which is used to manage the investments of all State monies that are under the control of the Treasurer where earnings accrue to the general fund of the State, and the State Agency Portfolio, for the investment of a limited number of state agencies specifically authorized by statute to direct the activities of certain funds and accounts where the earnings accrue to those funds and accounts. Ancillary to the Treasurer's Portfolio is an internal investment pool, OK INVEST, for all state funds and agencies that are considered part of the State of Oklahoma. All cash balances held through the State Treasurer for the Primary Government, Component Units and Fiduciary Funds earn a return through the OK INVEST pool program.

State Treasurer Investment Policy Diversification Limits

<u>Investment Type</u>	<u>Percentage of Total Invested</u>	<u>Percentage of Total by Issuer</u>	<u>Maturity Limit</u>	<u>Rating</u>
U.S. Government Agency Securities	54.0%	35.0%	3 Years	AAA
Tri-party Repurchase Agreements	16.0%	15.0%	1 Day	A-1
Money Market Mutual Funds	6.0%	15.0%	1 Day	AAA
Certificates of Deposit (Collateralized)	7.0%	\$35 Million*	365 Days	N/A
US Treasury Notes (Full Faith and Credit)	17.0%		5 Years	N/A

* No More Than \$35 Million per Financial Institution

Investments for governmental and fiduciary funds at June 30, 2007, by investment type, are listed below:

	<u>Carrying Amount</u>	<u>Reported Amount/ Fair Value</u>
Repurchase Agreements:		
<u>Governmental Funds</u>	\$ 50,349	\$ 50,349
<u>Fiduciary (Agency) Fund</u>	\$309,344,778	\$309,344,778

Investment securities are exposed to custodial credit risk if they are uninsured, not registered in the name of the State, or counterparty or the counterparty's trust department but not in the State's name. All investments held by the State Treasurer are insured, registered, or held in the name of the State Treasurer.

**OKLAHOMA TAX COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2007**

4. Capital Assets

In accordance with guidelines established by the Office of State Finance, capital assets reflected in the accompanying financial statements are those with a cost in excess of \$25,000. Expenditures for capital assets are recorded as period costs when the assets are recorded in the governmental funds. A provision for depreciation has been recorded in the governmental activities of the Statement of Net Assets and Statement of Activities. The depreciation method used for capital assets is straight-line with half-year convention. Capital asset activity for the year ended June 30, 2007, was as follows:

Governmental Activities:

	<u>Equipment</u>	<u>Accumulated Depreciation</u>	<u>Capital Assets - Net</u>
Beginning Balance	\$ 11,575,931	(\$ 9,147,894)	\$ 2,428,037
Increases	1,930,824	(520,602)	1,410,222
Decreases	<u>(1,157,681)</u>	<u>1,095,667</u>	<u>(62,014)</u>
Ending Balance	\$ 12,349,074	(\$ 8,572,829)	\$ 3,776,245

5. Operating Lease Commitments

The Oklahoma Tax Commission has commitments to lease certain buildings and equipment. For FY2007, lease expenditures were \$2,067,966. Future minimum rental commitments for operating leases as of June 30, 2007, are as follows:

2008	\$ 2,100,000
2009	2,163,000
2010	2,228,000
2011	2,295,000
2012	<u>2,364,000</u>
Total Future Minimum Lease Payments	\$11,150,000

6. Due To Other Funds

Amounts due to other funds are presented in the Fiduciary Fund. To the extent that transactions between funds had not been executed at June 30, 2007, the balances are included.

7. Risk Management

The Risk Management Division of the Department of Central Services is empowered by the authority of 74 O.S. 2001, § 85.34 et seq. The Division is responsible for the acquisition and administration of all insurance purchased by the State or administration of any self-insurance plans and programs adopted for use by the State or for certain organizations and bodies outside of state government, at the sole expense of such organization and bodies.

The state Risk Management Division is authorized to settle claims of the State and shall govern the dispensation and/or settlement of claims against a political subdivision. In no event shall self-insurance coverage provided to the State, an agency or other covered entity exceed the limitations on the maximum

**OKLAHOMA TAX COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2006**

7. Risk Management (cont...)

dollar amount of liability specified by the Oklahoma Governmental Tort Claims Act, as provided by 51 O.S. 2001, § 154. The Risk Management Division oversees the collection of liability claims owed to the State incurred as the result of a loss through the wrongful or negligent act of a private person or other entity.

The Risk Management Division is also charged with the responsibility to immediately notify the Attorney General of any claims against the State presented to the Risk Management Division.

8. Long-Term Obligations

Long-term obligations at June 30, 2007, and changes for the fiscal year are as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
<u>Governmental Activities</u>				
Compensated Absences	\$3,218,905	\$206,499	\$ 0	\$3,425,404

9. Litigation and Contingencies

The Oklahoma Tax Commission is party to numerous lawsuits of which the outcome is uncertain. There are numerous lawsuits pending before the Oklahoma Tax Commission that, in the aggregate, could have a material effect on the Commission's financial statements. However, the outcome at this time is uncertain. Additionally, there are numerous tax assessments under taxpayer protest that could have a material effect on the Commission's financial statements. It is reasonably possible that these assessments could result in gains to the state. However, an estimate of such gains cannot be made.

10. Net Assets Deficit

Total net assets on the Statement of Net Assets are stated at a negative balance at June 30, 2007. Due to the constitutional requirement to fully fund reimbursements to counties from the Ad Valorem Reimbursement Fund as specified in 62 O.S. 2001, § 193, obligations exceeded available funding at year end. \$16,120,225 in unpaid claims was paid from funds available during the subsequent fiscal year. The Ad Valorem Reimbursement Fund is a pass through and not used for the general operations of the agency.

REQUIRED SUPPLEMENTARY INFORMATION
OKLAHOMA TAX COMMISSION
BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
FOR THE YEAR ENDED JUNE 30, 2007

	Budgeted Amounts		Actual Amounts (Budgetary Basis) (See Note A)	Variance with Final Budget - Positive (Negative)
	Original	Final		
Budgetary Fund Balance, July 1	\$1,027,965	\$1,027,965	\$1,027,965	\$0
Resources (inflows)				
Taxes	22,323,000	24,983,000	24,707,258	(275,742)
Other Revenues	4,689,000	4,689,000	3,746,937	(942,063)
Transfers In	0	1,800,000	1,800,000	0
State Appropriations	47,711,604	47,711,604	47,711,604	0
Amount Available for Appropriation	75,751,569	80,211,569	78,993,764	(1,217,805)
Charges to Appropriations (outflows)				
Salaries and Benefits	51,332,429	51,410,253	51,538,770	(128,517)
Professional Services	6,839,650	7,164,650	7,404,922	(240,272)
Inter-Agency Personal Services	120,000	120,000	58,846	61,154
Travel	815,500	930,500	827,211	103,289
Miscellaneous Administrative	4,938,000	5,113,000	5,498,733	(385,733)
Rent of Buildings and Equipment	3,866,291	4,153,467	3,274,325	879,142
Maintenance	1,984,160	2,424,160	3,497,506	(1,073,346)
Supplies	2,465,000	3,105,000	3,082,007	22,993
Equipment	1,808,470	4,008,470	3,360,639	647,831
Buildings - Renovation	150,000	150,000	55,139	94,861
Other Expenditures	38,000	38,000	201,303	(163,303)
Payments to Local Governments	366,104	566,104	356,740	209,364
Total Charges to Appropriations	74,723,604	79,183,604	79,156,141	27,463
Budgetary Fund Balance - June 30	\$1,027,965	\$1,027,965	(\$162,377)	(\$1,190,342)

BUDGETARY COMPARISON SCHEDULE - WASTE TIRE INDEMNITY FUND
FOR THE YEAR ENDED JUNE 30, 2007

	Budgeted Amounts		Actual Amounts (Budgetary Basis) (See Note A)	Variance with Final Budget - Positive (Negative)
	Original	Final		
Budgetary Fund Balance, July 1	(\$366,380)	(\$366,380)	(\$366,380)	\$0
Resources (inflows)				
Tire Fees	4,900,000	5,300,000	5,161,012	(138,988)
Other Revenues	4,200	4,200	4,871	671
Amount Available for Appropriation	4,537,820	4,937,820	4,799,503	(138,317)
Charges to Appropriations (outflows)				
Waste Tire Reimbursements	4,904,200	5,304,200	5,222,802	81,398
Other Expenditures	0	0	0	0
Transfers to Other Funds	0	0	0	0
Total Charges to Appropriations	4,904,200	5,304,200	5,222,802	81,398
Budgetary Fund Balance - June 30	(\$366,380)	(\$366,380)	(\$423,299)	(\$56,919)

BUDGETARY COMPARISON SCHEDULE - AD VALOREM REIMBURSEMENT FUND
FOR THE YEAR ENDED JUNE 30, 2007

	Budgeted Amounts		Actual Amounts (Budgetary Basis) (See Note A)	Variance with Final Budget - Positive (Negative)
	Original	Final		
Budgetary Fund Balance, July 1	(\$16,307,662)	(\$16,307,662)	(\$16,307,662)	\$0
Resources (inflows)				
Taxes	32,663,000	50,476,795	34,121,154	(16,355,641)
Transfers In	0	18,800,000	18,800,000	0
Other Revenue	0	0	27,165	27,165
Amount Available for Appropriation	16,355,338	52,969,133	36,640,657	(16,328,476)
Charges to Appropriations (outflows)				
County Reimbursements	16,286,205	52,900,000	52,733,717	166,283
Transfers to Other Funds	0	0	0	0
Total Charges to Appropriations	16,286,205	52,900,000	52,733,717	166,283
Budgetary Fund Balance - June 30	\$69,133	\$69,133	(\$16,093,060)	(\$16,162,193)

See independent auditor's report.

The notes to the Required Supplementary Information are an integral part of this schedule

**REQUIRED SUPPLEMENTARY INFORMATION
BUDGETARY COMPARISON SCHEDULE
NOTES TO RSI**

Note A. Budgeting, Budgeting Control and Budgetary Reports

The State annual budget is prepared on the cash basis utilizing encumbrance accounting. Encumbrances represent executed but unperformed purchase orders. In the accompanying budgetary comparison schedules, encumbrances are recorded as expenditures for budgetary purposes if expected to be presented for payment by November 15 following the end of the fiscal year and as reservations of fund balance in the governmental funds balance sheet for GAAP purposes. Since the budgetary basis differs from generally accepted accounting principles, budget and actual amounts in the accompanying Budgetary Comparison Schedules - Budget and Actual (Non-GAAP Budgetary Basis) are presented on the budgetary basis.

The Governor prepares and submits to the Legislature at the beginning of each annual session a balanced budget based on budget requests prepared by the various state agencies. The General Fund, Waste Tire Indemnity Fund, Ad Valorem Reimbursement Fund and the Oklahoma Film Enhancement Fund (there was no activity in this fund for fiscal year 2007) are the only funds for which an annual budget is legally adopted. The Governor has the power to approve or veto each line item appropriation. Any other changes to the budget must be approved by the Legislature in a supplemental appropriation. All 2007 appropriation line items of the State were within their authorized spending level.

The legal level of budgetary control is maintained at the line item level (i.e. General Operations, Personal Services, Duties, etc.) identified in the appropriation acts. Budgets may be modified subject to statutory limits on transfers. The Director of the Office of State Finance can approve transfers between line items up to 25%. Agencies can obtain approval from the Contingency Review Board to transfer up to an additional 15%; however, all transfers are subject to review by the Joint Legislative Committee on Budget and Program Oversight to determine if the transfer tends to effectuate or subvert the intention and objectives of the Legislature.

Current policy allows agencies to use unexpended monies for one-time purchases or non-recurring expenditures in the next fiscal year. This policy provides an incentive for management to distribute resources efficiently; however, it is subject to annual approval by the Legislature. Unexpended balances not carried forward to the new fiscal year by November 15 may: 1) lapse to unrestricted balances and be available for future appropriation, 2) lapse to restricted balances and be available for future appropriations restricted for specific purposes as defined by statute, or 3) be non-fiscal, and may be spent from one to 30 months from the date of appropriation.

Note B. Excess of Expenditures Over Appropriations

Within the Waste Tire Indemnity Fund, expenditures exceeded the amount available for appropriations. Each month, funds are exhausted with reimbursement claims exceeding available cash on hand. June's reimbursement claims are received in July and paid from July resources.

Expenditures from the Ad Valorem Reimbursement Fund exceeded the amount available for appropriation due to inadequate funding for all claims submitted. Legislative appropriations and income tax receipts were used to fully fund claims subsequent to year-end.

See independent auditor's report.

REQUIRED SUPPLEMENTARY INFORMATION
BUDGETARY COMPARISON SCHEDULE
NOTES TO RSI

Note C - Explanation of Differences between Budgetary Inflows and Outflows and GAAP Revenues and Expenditures

	General Fund	Waste Tire Indemnity Fund	Ad Valorem Reimbursement Fund
	<u> </u>	<u> </u>	<u> </u>
Sources/inflows of resources			
Actual amounts (budgetary basis) "Resources (inflows)" from the budgetary comparison schedule	\$77,965,799	\$5,165,883	\$52,948,319
Differences - budget to GAAP:			
State appropriations are inflows of budgetary resources but are not revenues for financial reporting purposes.	(47,711,604)	0	0
Transfers from other funds are inflows of budgetary resources but are not revenues for financial reporting purposes.	(1,800,000)	0	(18,800,000)
Accrual adjustments for receivables are made for financial reporting purposes but not for the budgetary comparison.	<u>(333,973)</u>	<u>(13,562)</u>	<u>(36,743)</u>
Total revenues as reported on the statement of revenues, expenditures, and changes in fund balances - governmental funds	<u>\$28,120,222</u>	<u>\$5,152,321</u>	<u>\$34,111,576</u>
Uses/outflows of resources			
Actual amounts (budgetary basis) " total charges to appropriations" from the budgetary comparison schedule	\$79,156,141	\$5,222,802	\$52,733,717
Differences - budget to GAAP:			
Transfers to other funds are outflows of budgetary resources but are not expenditures for financial reporting purposes.	<u>0</u>	<u>0</u>	<u>0</u>
Total expenditures as reported on the statement of revenues, expenditures, and changes in fund balances - governmental funds	<u>\$79,156,141</u>	<u>\$5,222,802</u>	<u>\$52,733,717</u>

See independent auditor's report.



STATE OF OKLAHOMA
OFFICE OF THE AUDITOR AND INSPECTOR

JEFF A. McMAHAN
State Auditor and Inspector

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

**TO THE COMMISSIONERS OF THE
OKLAHOMA TAX COMMISSION**

We have audited the financial statements of the Oklahoma Tax Commission (OTC) as of and for the year ended June 30, 2007, and have issued our report thereon dated February 12, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Oklahoma Tax Commission's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Commission's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Commission's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is a more than remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Oklahoma Tax Commission's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the management of the Oklahoma Tax Commission and should not be used for any other purpose. This report is also a public document pursuant to the Oklahoma Open Records Act (51 O.S., § 24A.1 et seq.), and shall be open to any person for inspection and copying.



Michelle R. Day, Esq.
Deputy State Auditor and Inspector

February 12, 2008



**OFFICE OF THE STATE AUDITOR AND INSPECTOR
2300 N. LINCOLN BOULEVARD, ROOM 100
OKLAHOMA CITY, OK 73105-4896**

WWW.SAI.STATE.OK.US