

STATE OF CONNECTICUT



*AUDITORS' REPORT
DEPARTMENT OF BANKING
FOR THE FISCAL YEARS ENDED JUNE 30, 2012 and 2013*

AUDITORS OF PUBLIC ACCOUNTS
JOHN C. GERAGOSIAN ❖ ROBERT M. WARD

Table Of Contents

INTRODUCTION	1
COMMENTS	2
FOREWORD	2
New Legislation.....	3
RÉSUMÉ OF OPERATIONS.....	3
Receipts	3
Expenditures	4
Fund Balance	5
Staffing Levels.....	5
STATE AUDITORS' FINDINGS AND RECOMMENDATIONS.....	6
Property Control	6
RECOMMENDATIONS	8
CONCLUSION.....	9

STATE OF CONNECTICUT



AUDITORS OF PUBLIC ACCOUNTS

State Capitol
210 Capitol Avenue
Hartford, Connecticut 06106-1559

JOHN C. GERAGOSIAN

ROBERT M. WARD

October 1, 2015

AUDITORS' REPORT DEPARTMENT OF BANKING FOR THE FISCAL YEARS ENDED JUNE 30, 2012 and 2013

We have audited certain operations of the Department of Banking in fulfillment of our duties under Section 2-90 of the Connecticut General Statutes. The scope of our audit included, but was not necessarily limited to, the years ended June 30, 2012 and 2013. The objectives of our audit were to:

1. Evaluate the department's internal controls over significant management and financial functions;
2. Evaluate the department's compliance with policies and procedures internal to the department or promulgated by other state agencies, as well as certain legal provisions; and
3. Evaluate the economy and efficiency of certain management practices and operations, including certain financial transactions.

Our methodology included reviewing written policies and procedures, financial records, minutes of meetings, and other pertinent documents; interviewing various personnel of the department; and testing selected transactions. We obtained an understanding of internal controls that we deemed significant within the context of the audit objectives and assessed whether such controls have been properly designed and placed in operation. We tested certain of those controls to obtain evidence regarding the effectiveness of their design and operation. We also obtained an understanding of legal provisions that are significant within the context of the audit objectives, and we assessed the risk that illegal acts, including fraud, and violations of contracts, grant agreements, or other legal provisions could occur. Based on that risk assessment, we designed and performed procedures to provide reasonable assurance of detecting instances of noncompliance significant to those provisions.

We conducted our audit in accordance with the standards applicable to performance audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform our audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides such a basis.

The accompanying *Résumé of Operations* is presented for informational purposes. This information was obtained from the department's management and was not subjected to the procedures applied in our audit of the department. For the areas audited, we identified:

1. Deficiencies in internal controls;
2. Apparent noncompliance with legal provisions;
3. Need for improvement in management practices and procedures that we deemed to be reportable.

The State Auditors' Findings and Recommendations in the accompanying report presents any findings arising from our audit of the Department of Banking.

COMMENTS

FOREWORD

The Department of Banking operates under the provisions of Title 36a, Chapters 664 through 669 and Title 36b, Chapters 672 to 672c of the Connecticut General Statutes. The department functions as a regulatory agency responsible for the supervision, licensing and regulation of financial institutions and organizations within the state. Included among such institutions are state chartered banks and credit unions, mortgage lenders, brokers, consumer collection agencies, small loan companies, and check cashers. In addition, it has limited jurisdiction over landlord/tenant security deposit disputes. The department receives the majority of its revenues through the registration, supervision, and examination of the securities business within the state, including brokerage firms, investment banking houses, retail stockbrokers and investment advisors. The department administers and enforces Connecticut's Truth-in-Lending Law and Uniform Securities Act, among other consumer-credit laws.

Howard F. Pitkin was appointed Banking Commissioner on October 1, 2006, and served throughout the audited period. Jorge Perez was appointed commissioner in February of 2015 and continues to serve in that capacity.

New Legislation

Public Act 11-6, Section 134, effective July 1, 2011, stated that any fines, civil penalties, or restitution imposed by the banking commissioner or ordered by a court in accordance with Sections 36a-50, 36a-53 or 36a-57 of the General Statutes shall be deposited into the General Fund. These fines, penalties and other revenues were previously deposited into the Banking Fund.

Public Act 12-96, Section 4, effective October 1, 2012, broadened the banking commissioner’s investigatory powers by allowing the commissioner to require or permit any person under the department’s jurisdiction to testify, produce a record, file a statement in writing, or under oath. Section 5, effective October 1, 2012, allows the commissioner to order restitution or disgorgement for banking law violations without a court order.

Public Act 13-135, Section 14, effective June 18, 2013, gave the commissioner authority to increase collateral requirements in the event of an increased risk to public deposits before the factors that would automatically trigger an increase in collateral come into effect.

RÉSUMÉ OF OPERATIONS

Receipts

Receipts of the Department of Banking are summarized below by fund for the fiscal years ended June 30, 2011, 2012 and 2013:

	<u>2010-2011</u>	<u>2011-2012</u>	<u>2012-2013</u>
General Fund	\$ -0-	\$ 1,178,551	\$ 6,593,741
Banking Fund	40,916,068	31,551,683	26,157,810
Restricted Fund	6,000	741,465	490,000
Total Receipts by Fund	<u>\$ 40,922,068</u>	<u>\$ 33,471,699</u>	<u>\$ 33,241,551</u>

Receipts of the Department of Banking are summarized below by revenue category for the fiscal years ended June 30, 2011, 2012, and 2013:

	<u>2010-2011</u>	<u>2011-2012</u>	<u>2012-2013</u>
Fees	\$ 27,810,159	\$ 27,855,576	\$ 28,059,692
Fines	10,272,927	1,178,551	1,583,528
Licenses	2,638,445	3,695,460	3,107,450
Miscellaneous	200,537	742,112	490,881
Total Receipts by Category	<u>\$ 40,922,068</u>	<u>\$ 33,471,699</u>	<u>\$ 33,241,551</u>

Total receipts decreased by 18 percent and by one percent during the fiscal years ended June 30, 2012 and 2013, respectively. Revenues from fines decreased for fiscal year 2011-2012 due to a large increase in fines realized in the prior fiscal year. Fines in subsequent years were not as large. Public Act 11-6 required certain receipts previously deposited to the Banking Fund to be deposited to the General Fund effective at the commencement of the fiscal year ended June 30, 2012.

Expenditures

The expenses of the Department of Banking are made pursuant to appropriations by the General Assembly. Expenditures for the fiscal years ended June 30, 2011, 2012, and 2013, totaled \$18,635,514, \$18,750,715 and \$18,172,814, respectively. Most expenses were charged to the Banking Fund. Those expenditures charged to the Grants and Restricted Accounts Fund were for investor education programs. A summary of expenditures by fund is presented below:

	<u>2010-2011</u>	<u>2011-2012</u>	<u>2012-2013</u>
Banking Fund	\$ 18,619,261	\$ 18,449,686	\$ 17,880,903
Restricted Fund	16,253	301,029	291,911
Total Expenditures by Fund	<u>\$ 18,635,514</u>	<u>\$ 18,750,715</u>	<u>\$ 18,172,814</u>

A summary of expenditures for the Department of Banking by expenditure category is presented below:

	<u>2010-2011</u>	<u>2011-2012</u>	<u>2012-2013</u>
Total Personal Services	\$ 16,064,665	\$ 16,268,375	\$ 16,190,197
Employee Allowances & Travel	294,881	316,173	243,078
Contractual Services	237,527	466,068	502,594
Motor Vehicle Costs	11,677	19,537	74,684
Premises and Property	738,421	734,159	745,579
Information Technology	216,852	101,582	103,783
Purchased Commodities	15,353	16,102	23,507
Other Charges	1,039,567	726,727	215,207
Capital Outlays-Equipment	16,571	101,990	74,185
Total Expenditures	<u>\$ 18,635,514</u>	<u>\$ 18,750,715</u>	<u>\$ 18,172,814</u>

Expenditures increased one percent and decreased three percent during the fiscal years ended June 30, 2012 and 2013, respectively. Increases in personal services and contractual services in fiscal year 2011-2012 were partially offset by decreases in information technology and overhead charges for centralized state services, as determined by the Office of the State Comptroller and included in other charges above. Decreases in fiscal year 2012-2013 were mainly attributable to

further reduction in overhead charges for centralized state services. Personal services comprised about 87 and 89 percent of the department's total expenditures in the respective audited years.

Fund Balance

The Banking Fund budgetary fund balances plus reserve amounts for the fiscal years ended June 30, 2011, 2012 and 2013 were \$18,997,660, \$26,620,245 and \$27,350,239, respectively.

Staffing Levels

The department employed 112 individuals as of June 30, 2011 and 2012. The number of employees as of June 30, 2013 was 108, a decrease of three percent.

STATE AUDITORS' FINDINGS AND RECOMMENDATIONS

The following recommendation resulted from our current review of the Department of Banking:

Property Control

Criteria: Section 4-36 of the General Statutes requires each state agency to establish and keep an inventory account in the form prescribed by the State Comptroller, and to transmit to the Comptroller, a detailed annual inventory of all real property and capitalized personal property owned by the state and in the custody of the agency.

The State Property Control Manual requires state agencies to utilize the Core-CT system to record and control all property owned by and/or in the custody of the agency. In addition, all executive branch agencies must perform an annual physical inventory as of June 30th to ensure that property control records accurately reflect the inventory on hand and reported to the State Comptroller.

Section 4-36 of the General Statutes and the State Property Control Manual require agencies to maintain separate capital and controllable property listings. Capital property is personal property with a value greater than \$1,000 and a useful life greater than one year. Controllable property is personal property that does not meet the definition of capital property but requires identity and control, at the discretion of the agency head.

Conditions: A physical inspection of ten assets observed on the agency premises disclosed that five capital assets with a total value of \$23,243 had been wrongly removed from the inventory listing in Core-CT. Further review disclosed that, in an effort to correct inventory records in fiscal year 2011-2012, the department removed capital assets from its inventory listing with a total value of nearly \$759,000, including an unknown number of items that were still in the department's possession. The department's capital asset inventory prior to deletion of these items totaled approximately \$811,000.

During fiscal year 2012-2013, controllable property adjustments, totaling nearly \$76,800, were made to the department's controllable property inventory listing. However, the total value of those items was incorrectly included as deletions from the capital asset inventory on the annual inventory report, resulting in the further understatement of capital equipment inventory items.

- Effect:* Asset values reported to the State Comptroller were understated for the fiscal years ended June 30, 2012 and 2013. The amount of the understatement could not be determined without performing a complete physical inventory.
- Cause:* The department removed items from the inventory in Core-CT that were still in service.
- Recommendation:* The Department of Banking should improve internal controls to ensure that assets are properly recorded in Core-CT and accurately reported to the State Comptroller as prescribed by the State Property Control Manual. (See Recommendation 1.)
- Agency Response:* “We agree with this finding. An inventory of the agency’s capital assets will be taken and Core-CT will be adjusted to reflect the correct amount.”

RECOMMENDATIONS

Our prior report on the Department of Banking contained one recommendation. The previously noted recommendation has been implemented or otherwise resolved. As a result of our current examination, we have included one new recommendation.

Status of Prior Audit Recommendation:

- The Department of Banking's Financial Institutions Division should comply with Section 36a-428l subsection (e) to improve its internal controls over the calculation of foreign bank examinations, and recover or credit amounts as needed. The calculation of foreign bank examination costs was migrated from the financial institutions division to the business office during fiscal year 2012-2013. Our current review noted no similar exceptions in the calculation of foreign bank examination costs and as a result, this recommendation is not being repeated.

Current Audit Recommendation:

- 1. The Department of Banking should strengthen internal controls to ensure that assets are properly recorded in Core-CT and asset balances are accurately reported to the State Comptroller as prescribed by the State Property Control Manual.**

Comment:

Our current review noted that the department's capital asset listing was incomplete, resulting in inaccurate reporting of capital asset balances to the State Comptroller.

CONCLUSION

In conclusion, we wish to express our appreciation for the courtesies and cooperation extended to our representatives by the personnel of the Department of Banking during the course of this examination.



Douglas Stratoudakis
Associate Auditor

Approved:



John C. Geragosian
Auditor of Public Accounts



Robert M. Ward
Auditor of Public Accounts