

STATE OF CONNECTICUT

**AUDITORS' REPORT
STATE TREASURER - DEPARTMENTAL OPERATIONS
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

**AUDITORS OF PUBLIC ACCOUNTS
KEVIN P. JOHNSTON ♦ ROBERT G. JAEKLE**

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October 2, 2003

**AUDITORS' REPORT
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FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

We have made an examination of the financial records of the State Treasurer as they pertain to the Agency's departmental operations for the fiscal year ended June 30, 2002. This report on that examination consists of the Comments, Recommendations and Certification which follow. We also issued separate audit reports covering the State Treasurer - State Financial Operations and the Investment Advisory Council for the June 30, 2002 fiscal year.

This audit has been limited to assessing the State Treasurer's compliance with certain provisions of financial related laws, regulations and contracts, and evaluating the State Treasurer's internal control structure policies and procedures established to ensure such compliance. Financial statement presentation and auditing are done on a Statewide Single Audit basis to include all State agencies, including the State Treasurer.

COMMENTS

FOREWORD:

The State Treasurer operates primarily under the provisions of Article Fourth of the State Constitution and Title 3, Chapter 32 of the General Statutes. The Treasury Department is organized into several divisions and performs a number of functions. This report is concerned with the departmental operations of the Treasury Department and includes our review of the Business Office, Personnel, Informational Services, and the Unclaimed Property Division. Our review of financial operations of the State Treasurer that have Statewide impact has been issued under separate cover to include the Pension Funds Management Division, the Debt Management Division, the Cash Management Division, the Connecticut Higher Education Trust, and the Second Injury Fund. A separate report on the Investment Advisory Council has also been issued. A listing of officers and officials and a description of the major functions of the divisions covered in this report follows.

Officers and Officials:

The officers and officials of the Treasury Department as of June 30, 2002, were as follows:

State Treasurer: *

Denise L. Nappier

Deputy Treasurer:

Howard G. Rifkin

Assistant Deputy Treasurer:

Linda Hershman

Chief Investment Officer:

Susan B. Sweeney

Assistant Treasurer, Cash Management:

Lawrence A. Wilson

Assistant Treasurer, Policy:

Meredith A. Miller

Assistant Treasurer, Second Injury Fund:

Alberta Mendenhall

Assistant Treasurer, Unclaimed Property:

Madelyn Colon

Assistant Treasurer, Debt Management:

Catherine Boone

* As used in ensuing comments of this report, the term "Treasurer" refers to the State Treasurer.

RÉSUMÉ OF OPERATIONS:

Department Revenues:

Departmental revenues consisted mainly of Second Injury and Compensation Assurance Fund (SIF), Workers' Compensation Administration Fund (WCA), and General Fund revenue. SIF revenues consisted mainly of assessments levied against self-insured employers and companies writing workers' compensation or employers' liability insurance and totaled \$107,132,005 for the 2001-2002 fiscal year. WCA Fund assessment receipts totaled \$20,350,611 for the 2001-2002 fiscal year. More detailed information concerning the SIF and WCA is included in our Auditors' Report on the State Treasurer – State Financial Operations. The General Fund revenues, a large percentage of which consisted of restricted account transfer receipts to cover Combined Investment Funds' and Second Injury Fund's charges, and Unclaimed Property Division receipts, amounted to \$160,995,313 for the 2001-2002 fiscal year and \$155,575,926 for the 2000-2001 fiscal year.

A summary of General Fund revenue is presented below.

	<u>2001-2002</u>	<u>2000-2001</u>
Unclaimed property receipts	\$31,160,363	\$36,120,942
Restricted account transfers	128,480,907	117,794,263
All other receipts	<u>1,354,044</u>	<u>1,660,721</u>
Total General Fund Revenue	<u>\$160,995,314</u>	<u>\$155,575,926</u>

Department Expenditures:

Civil List expenditures for operations of the Treasury Department for 2001-2002, excluding expenditures classified as "debt service paid" and "workers' compensation awards" which are included in the separate audit report on State financial operations, are presented below, along with the prior year's expenditures:

	<u>2001-2002</u>	<u>2000-2001</u>
Net Expenditures by Fund:		
General-Budgeted	\$3,201,851	\$3,377,581
General-Restricted	78,146,913	63,116,456
General-Non-Functional	10,117,462	9,838,935
Capital Projects	781,950	62,249
Special Revenue	16,844	9,605
Enterprise	(3,134)	11,510
Fiduciary	<u>623,970</u>	<u>808,345</u>
Net Expenditures	<u>\$92,885,856</u>	<u>\$77,224,681</u>

General Fund restricted accounts were the major funding source for the Treasurer's Pension Funds Management Division, Second Injury Fund, Bond Issue Costs, and a Bank Compensation Account. Operating expenditures of the Unclaimed Property Division and a Special Assessment account are also charged to General Fund Restricted accounts. General Fund Non-Functional expenditures were for reimbursements of unclaimed property.

An analysis of departmental expenditures categorized by object is as follows:

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	<u>2001-2002</u>	<u>2000-2001</u>
Net Expenditures by Major Object:		
Personal services	\$10,628,107	\$10,127,517
Contractual services	67,971,420	53,353,637
Commodities	103,917	107,525
Sundry charges	3,358,068	2,918,657
Equipment	82,912	70,065
Unclaimed property	10,117,462	9,838,935
Expenditures by Agency Funds & Other	<u>623,970</u>	<u>808,345</u>
Net Expenditures	<u>\$92,885,856</u>	<u>\$ 77,224,681</u>

Contractual and personal services are the major expenditures of the Treasury, other than debt service cost. The most significant cost item in contractual services is the payments of the investment advisor performance fees by the Pension Fund Management Division (PFMD). Payment processing procedures made pursuant to these contracts were reviewed as part of this audit. Returns of unclaimed property remained relatively constant between fiscal years.

Personal services expenditures in the 2001-2002 and 2000-2001 fiscal years were paid from the following sources:

	<u>2001-2002</u>	<u>2000-2001</u>
General Fund:		
Budgeted Accounts	\$2,869,876	\$2,970,332
Restricted Accounts:		
Pension Fund Management	1,103,712	1,032,455
Second Injury Fund	4,566,533	4,176,925
Unclaimed Property	1,495,788	1,365,770
Short-Term Investment Fund	486,598	480,039
Special Assessment Fund	63,655	62,450
Other Civil List Funds	<u>41,945</u>	<u>39,546</u>
Totals	<u>\$10,628,107</u>	<u>\$ 10,127,517</u>

Total personal services expenditures increased by approximately 4.9 percent in the 2001-2002 fiscal year. Increased expenditures for annual salary increments and collective bargaining increases accounted for nearly all of the increase.

Treasury employment statistics for two years follow:

	<u>June 30,</u>	
	<u>2002</u>	<u>2001</u>
Full-time Permanent:		
General Fund:		
Budgeted Accounts	43	46
Restricted Accounts	105	105
Other Funds	<u>6</u>	<u>6</u>
Totals	<u>154</u>	<u>157</u>
Unclaimed Funds:		

The administration and disposition of property held by banking and other organizations for the

benefit of owners who cannot be located is provided for in Sections 3-56a to 3-74a of the General Statutes. The Statutes provide for all escheat receipts to be deposited into the General Fund with the exception of periodic transfers to a restricted unclaimed property account within the General Fund. The restricted account funds are used to pay unclaimed property's administrative costs. These transfers totaled \$3,200,000 for the 2001-2002 fiscal year. The receipts, presented below, show revenues prior to their reallocation to adjust for these transfers.

Unclaimed property includes unclaimed bank accounts and insurance policies and claims. It further consists of unclaimed wages and customer overpayments held by business associations and various court deposits. A comparison of unclaimed property receipts of the escheats revenue accounts for the 2001-2002 and 2000-2001 fiscal years follows:

	<u>2001-2002</u>	<u>2000-2001</u>
Financial institutions	\$11,417,298	\$10,214,502
Business corporations	10,182,099	12,026,482
Insurance companies	7,530,563	10,243,121
Securities tendered	261,560	1,010,844
Governmental and public agencies	1,886,622	3,174,113
Dividends on securities held	892,774	771,776
Interest penalty assessments	405,937	725,742
Reciprocal exchange with other States	318,977	812,583
Miscellaneous	1,464,532	541,784
Totals	<u>\$34,360,362</u>	<u>\$ 39,520,947</u>

Unclaimed Property administrative expenses as reported in the Treasurer's Annual report are as follows:

	<u>2001-2002</u>	<u>2000-2001</u>
Salaries and fringe benefits	\$2,112,937	\$1,900,906
Data processing and hardware	640,557	883,587
All other	286,749	313,763
Totals	<u>\$3,040,243</u>	<u>\$3,098,256</u>

In addition, during the 2001-2002 fiscal year, \$1,049,491 in fees was netted against unclaimed property receipts. Such fees consisted of fees for participation in out-of-state audits and other percentage based fee relationships. These receipts and fees are not recorded on the books of the State Comptroller, but are reported in the Treasurer's Annual Report.

The Unclaimed Property Division also receives abandoned stocks, bonds and mutual funds as authorized under Section 3-56a and Section 3-56b of the General Statutes.

According to the Treasurer's Annual Report, the estimated market values were as follows:

	<u>June 30, 2002</u>	<u>June 30, 2001</u>
Stocks and bonds	\$49,405,062	\$53,362,736

Mutual funds	<u>11,363,341</u>	<u>13,373,611</u>
Totals	<u>\$ 60,768,403</u>	<u>\$ 66,736,347</u>

Section 3-69a of the General Statutes states, in part, that unclaimed property claims allowed shall be paid from the unappropriated resources of the General Fund. Unclaimed property cash disbursements were \$10,117,462 and \$9,838,935 for the 2001-2002 and 2000-2001 fiscal years, respectively.

Second Injury and Compensation Assurance Fund:

The operations of this fund are provided for by various statutes of the Workers' Compensation Act, Chapter 568, of the General Statutes (notably Sections 31-310 and 31-349 through 31-355a). This Act provides protection for employees suffering occupational injuries or diseases and establishes criteria determining whether benefits due employees are to be paid by the employers (or their insurance carrier) or out of the Second Injury Fund (SIF). The Treasurer is the custodian of the SIF. Per Section 31-349e of the General Statutes, there is an advisory board to advise the custodian of the SIF on matters concerning administration, operation, claim handling and finances of the fund.

Comments regarding the financial operations of this fund are included under separate cover in our Report on the State Treasurer – State Financial Operations for the fiscal year ended June 30, 2002.

PERFORMANCE REVIEWS:

In accordance with Section 2-90 of the General Statutes, audits conducted by the Auditors of Public Accounts may include an examination of performance in order to determine an agency's effectiveness in achieving expressed legislative purposes. We have conducted such a review of the practice of publishing escheated property that falls under the minimum required to be published by Section 3-66a of the General Statutes. Pursuant to that section, the Treasurer must publish all property having a value of fifty dollars or more that was presumed abandoned. Such property shall be published at least once in a general circulation newspaper and may be made accessible electronically by means of the World Wide Web (WWW). In addition to the publication of statutorily required property, in fiscal year 2000-2001, the Office of the Treasurer began publishing escheated property on the World Wide Web that is less than fifty dollars but at least ten dollars.

Our review found in fiscal year 2001-2002, 16,684 claims were processed, an increase of 17.8 percent over fiscal year 2000-2001 totals. Total claims paid, in dollars, increased by only 2.8 percent, to \$10,117,462 over fiscal year 2000-2001 totals. We analyzed these 16,684 claims and found that 2,101 of them were for cash claims under \$50. We calculated that the total amount returned to property owners for these claims was \$58,360.

As can be seen from the above, the number of claims processed has increased significantly as a result of publishing claims under \$50 on the World Wide Web. This has taxed the claims processing system and has consumed limited resources that could be used to process more substantial claims.

The Treasurer has informed us that certain operational steps have been taken by the division to improve overall claims-processing productivity and more efficient utilization of staff resources, including plans to implement scanning technology.

In conclusion, if the Office of the Treasurer publishes claims under \$50 on the World Wide Web, then it should also continue its work to achieve greater operational efficiencies designed to compensate for the increased workload as a result of publishing those claims.

The following resulted from our review of the Second Injury Fund Investigations Unit in our prior auditors' report:

Pursuant to Section 31-349a of the General Statutes, Special Investigators in the Second Injury Fund (SIF) investigate indications of claim fraud and employers' compliance with the law that mandates workers' compensation insurance coverage. Section 31-288 subsection (c) of the General Statutes states that whenever an investigator finds that an employer is not in compliance with the workers' compensation insurance requirements, such investigator shall issue a citation requiring such employer to appear at a hearing before the Workers' Compensation Commission (WCC). The WCC can assign the Special Investigators to examine insurance coverage and penalties for noncompliance can total \$55,000. The number of actual SIF claims that require investigation have been decreasing because the Second Injury Fund was closed to most second injury claims for injuries occurring on or after July 1, 1995, in accordance with Public Act 95-277. According to the State Treasurer's Annual Report, the number of open active SIF claims has dropped from 5,700 to 2,737 since 1995. Some investigations are conducted by outside vendors on contract with the State Treasurer's Office.

There are six Special Investigators in SIF who are assigned to specific WCC districts throughout the State. The average caseload is about 30 open cases per investigator. Special Investigators are assigned cases by both the SIF and the Workers' Compensation Commissioners. We estimated that 57 percent of the Special Investigators' caseload consists of uninsured employers' cases from the WCC; however, all of the costs of operating the Investigations Unit are paid with SIF resources.

Our review indicated that Special Investigators in the SIF appear to be meeting the statutory mandate of Section 31-349a to investigate SIF claims and employers' compliance. Because the WCC also receives programmatic benefits from the efforts of the Special Investigators in the SIF, we believe that some portion of this cost should be allocated to the WCC, and charged to the Workers Compensation Fund.

We recommended in the prior auditors' report that consideration should be given to placing the Treasurer's Second Injury Fund's Investigations Unit under the direct control of the WCC, and the costs of operating the Investigations Unit should be allocated between the Second Injury Fund and the Workers Compensation Commission. The Office of the Treasurer did not support the part of the recommendation dealing with re-assigning the Investigations Unit and noted that jurisdiction over the investigators was transferred to the WCC in 1993, and back to the Treasurer's Office in 1995 under Public Act 95-277. The Office of the Treasurer cites this as evidence that the intent of the legislation was to ensure proper supervisory oversight of the investigators by transferring them back to the SIF. While we still believe that the Investigations Unit should be under the control of the

WCC, we are not repeating this part of the recommendation.

The Office of the Treasurer did indicate in the prior audit report, however, that it would evaluate the other part of the audit recommendation that concerned the allocation of the costs of operating the Investigations Unit between the SIF and the WCC. Our follow-up of this area found that an evaluation was informally conducted and concluded that the matter needed to be taken up with the Workers Compensation Commission. Accordingly, we are repeating the part of the recommendation pertaining to the allocation of Investigations Unit costs between the SIF and the WCC. We note that if the Second Injury Fund's Investigations Unit is not transferred to the WCC, allocation of the expenses becomes much more important.

The following finding resulted from our performance review of the Second Injury Fund Investigations Unit in the prior audit report.

The Costs of Workers' Compensation Fund Case Investigations performed by the Second Injury Fund's Investigations Unit should be reimbursed:

Criteria: Pursuant to Section 31-349a of the General Statutes, investigators in the State Treasurer's Second Injury Fund (SIF) investigate claims and employers' compliance with the law that mandates workers' compensation coverage. The Workers Compensation Commission (WCC) is statutorily responsible to ensure that employers carry out their legal responsibilities, among other issues pertaining to workers' compensation laws. Services provided by the Investigations Unit to satisfy requests made by other agencies to administer the program should be reimbursed, if applicable.

Condition: The Investigations Unit is located within the Office of the State Treasurer and received an estimated 57 percent of uninsured employers' caseload from the WCC in calendar year 2002, and the remainder from the SIF. Many of these cases are requests to verify whether an employer has insurance coverage or, in the case of an uninsured company, whether the employer has assets the State can claim. As the SIF is responsible to pay injured workers' benefits only after the Workers' Compensation Commissioner orders the Fund to pay, the investigators' work on these cases is more closely related to the operations of the WCC and not the SIF. We noted that for the fiscal year ended June 30, 2002, the SIF incurred \$677,861 of personal services and related expenses for investigations and the SIF did not request or receive reimbursement from the WCC for its share of case investigation costs.

Cause: Public Act 95-277 amended Section 31-349 of the General Statutes to close the SIF to most claims after July 1, 1995. This Act served to considerably reduce the Investigations Unit's caseload pertaining to SIF cases causing it to handle an increasing caseload directly from the WCC.

Effect: The costs of the Investigations Unit are not being reimbursed appropriately to the Second Injury Fund from the Workers Compensation Fund. This

overstates the expenditures of the Second Injury Fund, a General Fund operation, and understates the expenditures of the Workers' Compensation Fund, a Special Revenue Fund.

Recommendation: A formal review should be conducted to determine the amount of reimbursement due the Second Injury Fund for the amount of work done by the Investigations Unit on cases pertaining to the Workers' Compensation Commission. (See Recommendation 1.)

Agency Response: "The Second Injury Fund and the Workers' Compensation Commission along with the Attorney General's Office, all partners in the system, reviewed the Auditors of Public Accounts recommendation made in the prior year's audit report to allocate operating costs of the Second Injury Fund investigators between the Worker's Compensation Commission and the Fund. Following this initial study, the Second Injury Fund is conducting a more formal analysis of the time and expense incurred by the investigators performing requested investigations on behalf of the Worker's Compensation Commission.

When this information is obtained and reviewed, the analysis will be shared with the chairman of the Workers' Compensation Commission in order to identify the investigators' costs that should be charged to the Commission."

CONDITION OF RECORDS

Timeliness of Deposits in the Unclaimed Property Division:

- Criteria:* Section 4-32 of the General Statutes requires each State agency to deposit and account for revenues within 24 hours of receipt.
- Condition:* We were notified by Treasury officials of an incident when cash received by the Unclaimed Property Division was not deposited within 24 hours. The instance involved a receipt of \$1,752 that was deposited and accounted for one day late. The late deposit was reported to the Governor and other State Officials on August 8, 2002.
- Cause:* The Treasury reports that the employee forgot to check the secured cabinet for checks awaiting deposit.
- Effect:* Receipts were not deposited in a timely manner as required by Section 4-32 of the General Statutes. Delays in depositing compromise physical control over undeposited checks.
- Recommendation:* The Office of the State Treasurer's Unclaimed Property Division should deposit in accordance with Section 4-32 of the General Statutes. (See Recommendation 2.)
- Agency Response:* "As reported to the Governor's Office and the State Auditors on August 8, 2002, our Agency Audit Liaison investigated the matter immediately and concluded that processing procedures in place to ensure timely deposits were not followed. The employee responsible received counseling and re-training and we believe that existing procedures are adequate to prevent a reoccurrence of this situation."

Contract Management in the Unclaimed Property Division and Second Injury Fund:

- Criteria:* Good business practices require that all contracts should be closely monitored for cost containment and adherence to contractual terms.
- Condition:* In our review of administrative payments for the operation of the Unclaimed Property Division (UPD), we noted a contract for the provision of claims processing services that has resulted in significant "overage" payments for the second fiscal year in a row. The contract requires an annual base payment of \$365,000 with a provision for monthly charges for additional volume that exceed certain base volume figures. As of June 30, 2002 no invoices for monthly volume overages had been submitted. On July 9, 2002 the contractor submitted an invoice for "contract overage charges" for fiscal

year 2001-2002 in the amount of \$195,833.50. A payment of \$177,216 was made in January 2003 representing the contract overage charges, apparently in full payment of the amount owed.

In the Second Injury Fund a personal service agreement with a contractor “not to exceed \$459,600” was later amended for an additional \$145,010, an increase of 32 percent. Services provided under the agreement related to the implementation of operational and risk management information system improvements by the Second Injury Fund (SIF). However, after the original \$459,600 had been committed the contractor reported the project to be only about 80-90 percent complete. The additional funds were reportedly needed for payment for contracted work that was performed “out of scope”, or in excess of anticipated volume of hours, and for work performed unrelated to the objectives of the original agreement. This unrelated work involved the review of uninsured/bankrupt employer claims and the analysis of internal development of claims management.

Cause: In the Unclaimed Property Division, the lack of administrative oversight contributed to vendor contractual noncompliance with respect to the provision for monthly overage billings.

In the Second Injury Fund it appears the contract was not written to keep it within the contracted amount for the type and volume of services expressly agreed to in the original agreement.

Effect: For the Unclaimed Property Division, the budgetary process has been compromised, as expenditures of the 2001-2002 fiscal year must be charged to the 2002-2003 fiscal year’s appropriation.

For the Second Injury Fund contract an additional \$145,010 was expended for contract services that were originally stated “not to exceed \$459,600”. Of this amount \$86,000 was expended to complete the project and \$59,010 was expended for services rendered that were “out-of- scope”.

Recommendation: The Treasurer’s Office should improve its contract monitoring procedures. In the Unclaimed Property Division, vendor adherence to contractual terms should be enforced and in Second Injury Fund, stricter monitoring should be employed to keep contracts within the original cost and scope of services. (See Recommendation 3.)

Agency Response: “As covered by contract, the Unclaimed Property Division instructed the claims processing vendor to submit monthly, invoices for overage charges, rather than waiting until the end of the fiscal year. After reviewing and reconciling overage charges, Unclaimed Property now submits the invoice to the Business Office for payment by the end of the month in which it is received. In addition, a new vendor contract for claims processing services is

being negotiated that will eliminate all overage payments.

The Agency concurs with the Auditors regarding keeping contracts within the original cost and scope of services. Although the Second Injury Fund vendor contract reviewed by the auditors was completed in 2002, the Fund had obtained Office of Policy and Management and Attorney General's Office approval for an additional \$86,000 over the estimate in the original contract for additional hours that could not have been foreseen to complete the review of operations and the risk management information system.

In addition, the Fund had also obtained Office of Policy and Management and Attorney General's Office approval to add an incremental \$59,010 to the contract to review uninsured/bankrupt employer claims because of problems identified by the Auditors. Supplementing the existing contract with the incremental added expenses was more cost effective than issuing a new contract given that the entire project was nearly finished."

Duplicate payment made in Unclaimed Property Division:

Criteria: Internal controls should be in place to prevent duplicate payments from being made.

Condition: Our review of expenditures made under this unclaimed property claims processing contract revealed that payment for the June 2001 monthly fee was made twice. The Office of the Treasurer did not discover this overpayment until we informed them in December 2002 after reviewing the payments made. This overpayment was reported to the Governor and other State Officials on February 11, 2003.

Cause: It appears a lack of proper internal controls over this contract expenditure contributed to this condition.

Effect: The Office of the Treasurer expended \$30,416.67 more than was necessary under the contract period and must recoup this amount from the contractor. Additional administrative costs have been incurred by processing an unnecessary expenditure and the State has lost the use of these funds and any earnings on them for the duration of the non-collection of the overpayment.

Recommendation: The Office of the Treasurer should review and strengthen internal controls in order to prevent another occurrence of duplicate payments. (See Recommendation 4.)

Agency Response: "The Treasury Business Office and Unclaimed Property Division have re-enforced vendor payment processing procedures and the vendor overpayment has been recovered. Unclaimed Property has also created a vendor control sheet to log ACS invoices upon receipt and to record the payment when made

by the Business Office. In addition, the staffs of the Business Office and Unclaimed Property have been reminded to continue to follow the internal control procedures, and to formally follow-up timely on any discrepancies.”

Holder Reporting and Publishing of Property Owner’s Names:

Criteria: Section 3-62g of the General Statutes requires the Treasurer to assume custody of money or other property and be responsible for all claims to unclaimed property owners. Items that escheat to the State annually include cash, stock, and items held in safe deposit boxes. Safe deposit box contents are physically retrieved by Treasury staff members from the banks, all other property is sent by holders. Property owner information is stored in a database, which is used for claims processing and the source for Statewide publication. Section 3-66a of the General Statutes requires the Treasurer to publish the names of unclaimed property owners at least once every two years.

Condition: Our review disclosed property in the custody of the Unclaimed Property Division that was not loaded to the database of owners’ names. We also found that property reported abandoned was not recovered by the Unclaimed Property Division. As a result these names can not be published and it is more difficult for claimants to recover their property. The property not loaded as of December 31, 2002 includes:

- 474 holder reports representing \$9,889,711 of unclaimed cash and 318,309 shares of unclaimed stock. Of these, 98 holder reports could not be loaded due to incomplete reporting by the holder. The number of actual owners that this property represents could not readily be determined.
- Thirty four banks and six hospitals reporting property for the calendar years 1998, 1999, 2000, and 2001 continue to hold the contents of approximately 1,597 safe deposit boxes that have not yet been collected by the Treasury staff. Although savings bonds were retrieved in previous years, they were not loaded to the system as abandoned property due to owners.
- 329 owner names representing \$54,480 of proceeds from the sale of safe deposit box items auctioned October 2001.

During our testing of 25 holder reports we found that one report was loaded to the system twice. The holder reported \$679,864 to the Treasury and the amount reflected on the system was \$1,359,727. Therefore, owners listed on the report were shown to have double the amount of property. There was one claim that was filed for the incorrect amount pending processing however it was not paid upon the discovery of this condition. Procedures for verifying

amounts loaded to the system were not followed.

Cause: The cause for the holder reports not being loaded and the safe deposit boxes not recovered was not determined. Procedures established by the Division were not followed, resulting in the loading error.

Effect: Publication of names was delayed due to the failure to load reports and recover safe deposit boxes timely. Safe deposit boxes not collected compromise controls over unclaimed assets. Internal control procedures not followed by the holder-reporting unit could lead to potential payment errors.

Recommendation: The Office of the State Treasurer's Unclaimed Property Division should comply with Section 3-62g of the General Statutes and their own internal procedures to appropriately collect and manage all unclaimed property including the contents of safe deposit boxes. The Treasury should also comply with the publication requirements of Section 3-66a of the General Statutes by loading abandoned property in a timely manner. (See Recommendation 5.)

Agency Response: "The Unclaimed Property Division has resumed safe deposit box pick-ups and has loaded onto its database all of the contents from the safe deposit boxes that were auctioned in 1998. The proceeds of the 2001 auctioned property will be loaded onto the system by the end of this fiscal year on June 30, 2003, following the reconciliation of the auctioned property to the holder report.

In addition, the 2003 General Assembly is presently reviewing legislative changes proposed by the Treasurer requiring holders of personal property to sell such property in the future and remit the proceeds to the Treasurer.

The Unclaimed Property Division will also load onto its database all holder reports except where holders have been unable to identify owner's names, and where holder reports do not agree with the cash or stock certificates received. New procedures were drafted and the staff was instructed on how to handle transfers to the database for this type of incomplete information, if received in the future."

Claims Processing in the Unclaimed Property Division:

Criteria: Section 3-70a, subsection (b) specifies that the Treasurer shall consider each claim within ninety days after it is filed. The Unclaimed Property Division has established procedures for the prevention of duplicate payments. The process of "check posting" which is the recording of the paid information on the original holder report will document that payment has been made and prevent duplicate payment. Internal control procedures should be followed.

Condition: Our audit revealed that 11 of 25 stock claims tested were paid between 154 and 602 days with an average of 302 days. There is also a large number of stock claims that are waiting to be processed. As of our first inquiry on November 1, 2002 approximately 574 stock claims outstanding required processing. Upon revisiting this condition we found that 513 stock claims remained outstanding as of January 31, 2003. We also found that 22 of 45 claims disbursed did not have check posting, an internal control procedure used by the Division to prevent duplicate payments. We were told approximately 600 stock claims paid during fiscal years 2002 and 2003 have not been check posted. We randomly reviewed 10 stock only and mutual fund claims and discovered that 5 of 10 that were not check posted were also not posted in the system as having been paid.

Cause: The Division's efforts to process a higher volume of cash claims appears to have caused an administrative burden that has led to a backlog in the processing of stock claims. The Division cites a lack of personnel resources as the reason for the delay in check posting.

Effect: Claimants are not receiving their unclaimed property in a reasonable amount of time. Internal controls are weakened by the lack of check posting, increasing the risk of overpayment.

Recommendation: The Unclaimed Property Division should comply with Section 3-70a, subsection (b) of the General Statutes. The Unclaimed Property Division should follow internal control procedures designed to prevent overpayments. (See Recommendation 6.)

Agency Response: "The Unclaimed Property Division has set as a priority the internal control procedure of "check-posting" which records paid information onto the original holder reports in order to prevent duplicate payments. Two staff members have been assigned full time, and two staff members part time, in order to complete by September 1, 2003, the "check-posting" project backlog.

Also, with the recent liquidation of approximately 50% of the eligible securities stock inventory, which will reduce the number of stock claims to be processed in the future, the Unclaimed Property Division should be able to return stock claims in a reasonable amount of time per Section 3-70a subsection (b) of the General Statutes. Instead, these claims will be processed as cash only claims which is typically a shorter processing procedure than processing stock claims."

RECOMMENDATIONS

Status of Prior Audit Recommendations:

Our prior audit examination resulted in eight recommendations. The following is a summary of those recommendations and the action taken by the State Treasury.

- The cost of operating the Office of the Treasurer's Second Injury Fund Investigations Unit should be allocated between the Second Injury Fund and the Workers' Compensation Commission. Consideration should be given to placing the unit under direct control of the Commission. This recommendation was not implemented and has been repeated in revised form as Recommendation 1.
- Investigators in the Second Injury Fund Investigation unit should be provided with the tools needed to perform their duties efficiently and effectively. This recommendation was implemented.
- The Office of the State Treasurer's Unclaimed Property Division should promptly deposit in accordance with Section 4-32 of the General Statutes. Another instance of late deposit was reported to us and thus this recommendation has been repeated as Recommendation 2.
- The Office of the State Treasurer's Unclaimed Property Division should comply with Section 3-57a of the General Statutes and their own procedures to appropriately collect and manage all unclaimed property and comply with the publication requirements of Section 3-66a of the General Statutes and consider cost effectiveness when using other means to publish unclaimed property. This recommendation was not implemented and has been repeated in revised form as Recommendation 5.
- The Office of the State Treasurer's Unclaimed Property Division should pre-audit complex stock claims before the claims are paid, and recover any overpayments and compensate claimants who were underpaid. This recommendation was implemented.
- The Office of the State Treasurer's Unclaimed Property Division should improve controls over the maintenance and reconciliation of escheated stock inventory and provide each employee with a procedures manual. This recommendation was implemented.
- The Office of the State Treasurer's Unclaimed Property Division should develop policies and procedures to determine the most efficient and effective way to manage the sale of the securities inventory, and take appropriate action to transfer proceeds to the General Fund. This recommendation was implemented.
- The Treasurer's Office should improve contract management procedures, and properly allocate costs and comply with Sections 4-98 and 4-215 of the General Statutes regarding management of contracts paid for with State funds. We found new conditions with respect to contract management and thus this recommendation has been repeated in revised form as Recommendation 3.

Current Audit Recommendations:

The following recommendations resulted from our current review.

- 1. A formal review should be conducted to determine the amount of reimbursement due the Second Injury Fund for the amount of work done by the Investigations Unit on cases pertaining to the Workers' Compensation Commission.**

Comments:

The Investigations Unit is located within the Office of the State Treasurer and received an estimated 57 percent of uninsured employers' caseload from the WCC in calendar year 2002, and the remainder from the SIF. Many of these cases are requests to verify whether an employer has insurance coverage or, in the case of an uninsured company, whether the employer has assets the State can claim. As the SIF is responsible to pay injured workers' benefits only after the Workers' Compensation Commissioner orders the Fund to pay, the investigators' work on these cases is more closely related to the operations of the WCC and not the SIF. We noted that for the fiscal year ended June 30, 2002, the SIF incurred \$677,861 of personal services and related expenses for investigations and the SIF did not request or receive reimbursement from the WCC for its share of case investigation costs.

- 2. The Office of the State Treasurer's Unclaimed Property Division should deposit in accordance with Section 4-32 of the General Statutes.**

Comments:

We were notified by Treasury officials of an incident when cash received by the Unclaimed Property Division was not deposited within 24 hours. The instance involved a receipt of \$1,752 that was deposited and accounted for one day late. The late deposit was reported to the Governor and other State Officials on August 8, 2002.

- 3. The Treasurer's Office should improve its contract monitoring procedures. In the Unclaimed Property Division, vendor adherence to contractual terms should be enforced and in the Second Injury Fund, stricter monitoring should be employed to keep contracts within the original cost and scope of services.**

Comments:

In our review of administrative payments for the operation of the Unclaimed Property Division (UPD), we noted a contract for the provision of claims processing services that has resulted in significant unanticipated "overage" payments for the second fiscal year in a row. The contract requires an annual base payment of \$365,000 with a provision for charges for additional volume that exceeds certain base volume figures. As of June 30, 2002 no amount for volume overages had been paid. On July 9, 2002 the contractor submitted an invoice for "contract overage charges" for the fiscal year 2001-2002 in the amount of \$195,833.50. A payment of \$177,216 was made in January 2003 representing the contract overage charges, apparently in full and final payment of amounts owed.

In the Second Injury Fund a personal service agreement with a contractor “not to exceed \$459,600” was later amended for an additional \$145,010, an increase of 32 percent. Services provided under the agreement related to the implementation of operational and risk management information system improvements by the Second Injury Fund (SIF). However, after the original \$459,600 had been expended the contractor reported the project to be only about 80 to 90 percent complete. The additional funds were reportedly needed for payment for contracted work that was performed “out of scope”, or in excess of anticipated volume of hours, and for work performed unrelated to the objectives of the original agreement. This unrelated work involved the review of uninsured/bankrupt employer claims and the analysis of internal development of claims management.

4. The Office of the Treasurer should review and strengthen internal controls in order to prevent another occurrence of duplicate payments.

Comments:

Our review of expenditures made under an unclaimed property claims processing contract revealed that payment for the June 2001 monthly fee was made twice. The Office of the Treasurer did not discover this overpayment until we informed them in December 2002 after reviewing the payments made. This overpayment was reported to the Governor and other State Officials on February 11, 2003.

5. The Office of the State Treasurer’s Unclaimed Property Division should comply with Section 3-62g of the General Statutes and their own internal procedures to appropriately collect and manage all unclaimed property including the contents of safe deposit boxes. The Treasury should also comply with the publication requirements of Section 3-66a of the General Statutes by loading holder reports in a timely manner.

Comments:

Our review disclosed property in the custody of the Unclaimed Property Division that was not loaded to the database of owners’ names. As a result these names can not be published and it is more difficult for claimants to recovery their property. The reports not loaded are from calendar years 1998, 1999, 2000 and 2001.

During our testing of 25 holder reports we found that one report was loaded to the system twice. The holder reported \$679,864 to the Treasury and the amount reflected on the system was \$1,359,727. Therefore, owners listed on the report were shown to have double the amount of property. There was one claim that was filed for the incorrect amount pending processing however it was not paid upon the discovery of this condition. Procedures for verifying amounts loaded to the system were not followed.

6. The Unclaimed Property Division should comply with Section 3-70a subsection (b) of the General Statutes. The Unclaimed Property Division should follow internal control procedures designed to prevent overpayments.

Comments:

Our audit revealed that 11 of 25 stock claims tested took between 154 and 602 days to pay with an average of 302 days. There are also a large amount of stock claims that are waiting to be processed. As of our first inquiry on November 1, 2002 there were approximately 574 stock claims outstanding in need of processing. Upon revisiting this condition we found that 513 stock claims remained outstanding as of January 31, 2003. We also found that 22 of 45 claims disbursed did not have proper check posting, an internal control procedure used by the division to prevent duplicate payments. We were told approximately 600 stock claims paid during fiscal years 2002 and 2003 have not been check posted. We randomly reviewed 10 stock only and mutual fund claims and discovered that 5 of 10 that were not check posted were also not posted as paid in the system, thus there is no record that those claims have been paid.

INDEPENDENT AUDITORS' CERTIFICATION

As required by Section 2-90 of the General Statutes we have audited the books and accounts of the State Treasurer for the fiscal year ended June 30, 2002. This audit was primarily limited to performing tests of the Agency's compliance with certain provisions of laws, regulations and contracts, and to understanding and evaluating the effectiveness of the Agency's internal control policies and procedures for ensuring that (1) the provisions of certain laws, regulations and contracts applicable to the Agency are complied with, (2) the financial transactions of the Agency are properly recorded, processed, summarized and reported on consistent with management's authorization, and (3) the assets of the Agency are safeguarded against loss or unauthorized use. The financial statement information related to the Departmental Operations of the State Treasurer for the fiscal year ended June 30, 2002, is included as a part of our Statewide Single Audit of the State of Connecticut for that fiscal year.

We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial-related 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 State Treasurer complied in all material or significant respects with the provisions of certain laws, regulations and contracts and to obtain a sufficient understanding of the internal control to plan the audit and determine the nature, timing and extent of tests to be performed during the conduct of the audit.

Compliance:

Compliance with the requirements of laws, regulations and contracts applicable to the State Treasurer's Office is the responsibility of the State Treasurer's Office management.

As part of obtaining reasonable assurance about whether the Agency complied with laws, regulations and contracts, noncompliance with which could result in significant unauthorized, illegal, irregular or unsafe transactions or could have a direct and material effect on the results of the Agency's financial operations for the fiscal year ended June 30, 2002, we performed tests of its compliance with certain provisions of laws, regulations and contracts. However, providing an opinion on compliance with these 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 that are required to be reported under *Government Auditing Standards*. However, we noted certain immaterial or less than significant instances of noncompliance, which are described in the accompanying "Condition of Records" and "Recommendations" sections of this report.

Internal Control over Financial Operations, Safeguarding of Assets and Compliance:

The management of the State Treasurer’s Office is responsible for establishing and maintaining effective internal control over its financial operations, safeguarding of assets, and compliance with the requirements of laws, regulations and contracts applicable to the Agency. In planning and performing our audit, we considered the Agency’s internal control over its financial operations, safeguarding of assets, and compliance with requirements that could have a material or significant effect on the Agency’s financial operations in order to determine our auditing procedures for the purpose of evaluating the State Treasurer’s financial operations, safeguarding of assets, and compliance with certain provisions of laws, regulations and contracts, and not to provide assurance on the internal control over those control objectives.

However, we noted certain matters involving the internal control over the Agency’s financial operations, safeguarding of assets, and/or compliance that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control over the Agency's financial operations, safeguarding of assets, and/or compliance that, in our judgment, could adversely affect the Agency's ability to properly record, process, summarize and report financial data consistent with management's authorization, safeguard assets, and/or comply with certain provisions of laws, regulations and contracts. We believe the following findings represent reportable conditions: the need to improved controls over contract payments in the Unclaimed Property Division to prevent duplicate payments; the need for procedures to collect and manage all unclaimed property; and controls deficiencies found in the processing of claims by the Unclaimed Property Division.

A material or significant weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with certain provisions of laws, regulations and contracts or the requirements to safeguard assets that would be material in relation to the Agency’s financial operations or noncompliance which could result in significant unauthorized, illegal, irregular or unsafe transactions to the Agency being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over the Agency’s financial operations and over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material or significant weaknesses. However, we believe that none of the reportable conditions described above is a material or significant weakness.

We also noted other matters involving internal control over the Agency’s financial operations and over compliance which are described in the accompanying “Condition of Records” and “Recommendations” sections of this report.

This report is intended for the information of the Governor, the State Comptroller, the Appropriations Committee of the General Assembly and the Legislative Committee on Program Review and Investigations. However, this report is a matter of public record and its distribution is not limited.

CONCLUSION

In conclusion, we wish to express our appreciation for the cooperation and courtesies extended to our representatives by the personnel of the State Treasurer's Office during the course of our examination.

Gary P. Kriscenski
Principal Auditor

Approved:

Kevin P. Johnston
Auditor of Public Accounts

Robert G. Jaekle
Auditor of Public Accounts