

STATE OF CONNECTICUT

**AUDITORS' REPORT
STATE TREASURER - DEPARTMENTAL OPERATIONS
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2004**

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

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March 24, 2006

**AUDITORS' REPORT
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We have made an examination of the financial records of the Office of the State Treasurer (State Treasurer, or Treasury) as they pertain to the Agency's departmental operations for the fiscal years ended June 30, 2003 and 2004. This report on that examination consists of the Comments, Recommendations and Certification that follow. We also issued separate audit reports covering the State Treasurer - State Financial Operations and the Investment Advisory Council for the June 30, 2003 and 2004 fiscal years.

This audit has been limited to assessing the State Treasurer's compliance with certain provisions of financial 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, 2004, 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.

New Legislation:

Public Act 03-1 of the June Special Session of the 2003 General Assembly, Sections 66 to 84, reduced the dormancy period for most unclaimed property from five to three years. The dormancy period for safe deposit boxes was reduced from ten to five years. Section 69, subsection (c), was added to include demutualization amounts from insurance companies to escheat to the State if unpaid after three years. These Sections were effective August 16, 2003

Public Act 04-216, Section 53, subsection (d), of the February 2004 Regular Session, allows the Treasurer to liquidate unclaimed property (stocks) upon receipt. Sections 56 to 63 allowed for securitization of future unclaimed property revenues, however, no action was taken to do so during our current audit period. These Sections were effective May 6, 2004.

RÉSUMÉ OF OPERATIONS:

Presentation of Revenue and Expenditure Comparisons:

Public Act 04-2 of the May Special Session of the 2004 General Assembly authorized the establishment of a special revenue fund to account for grants and restricted accounts that were formerly accounted for in the State's General Fund. Starting in the 2003-2004 fiscal year, revenues and expenditures that were formerly accounted for in the General Fund's restricted accounts have been reclassified into the special revenue fund known as the Grants and Restricted Accounts Fund.

Department Revenues:

Departmental revenues were mainly from the Second Injury and Compensation Assurance Fund (SIF), Workers' Compensation Administration Fund (WCA), Grants and Restricted Accounts Fund and the General Fund. SIF's revenues consisted mainly of assessments levied against self-insured employers and companies writing workers' compensation or employers' liability insurance and totaled \$88,712,928 and \$93,965,092 for the 2002-2003 and 2003-2004 fiscal years, respectively. WCA Fund assessment receipts totaled \$21,383,555 for the 2002-2003 fiscal year and \$17,918,436 for the 2003-2004 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's and Grants and Restricted Accounts Fund's revenues, a large percentage of which consisted of restricted account and special revenue fund transfer receipts to cover Combined Investment Funds' and Second Injury Fund's charges, and Unclaimed Property Division's receipts, amounted to \$163,056,005 and \$251,706,556 for the 2002-2003 and 2003-2004 fiscal years, respectively. A summary of the General Fund's and Grants and Restricted Accounts Fund's revenue is presented below:

	<u>2002-2003</u>	<u>2003-2004</u>
Unclaimed property's receipts	\$67,608,435	\$ 99,922,381
Restricted account transfers	92,537,889	-
Special Revenue Fund's transfers	-	146,045,744
All other receipts	<u>2,909,681</u>	<u>5,738,431</u>
Total General Fund's and Grants and Restricted Accounts Fund's Revenue	<u>\$163,056,005</u>	<u>\$251,706,556</u>

Department Expenditures:

Civil List expenditures for operations of the Treasury for the 2002-2003 and 2003-2004 fiscal years, 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:

	<u>2002-2003</u>	<u>2003-2004</u>
Net Expenditures by Fund:		
General-Budgeted	\$ 3,067,389	\$ 3,263,926
General-Restricted	72,177,469	-
General-Non-Functional	9,441,860	10,862,104
Capital Projects	574,696	31,263
Special Revenue	13,393	71,824,201
Enterprise	251	-
Fiduciary	887,846	-
Net Expenditures	<u>\$86,162,904</u>	<u>\$85,981,494</u>

The General Fund's 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 during the 2002-2003 fiscal year. Such expenditures were accounted for as part of the Special Revenue Funds during the 2003-2004 fiscal year. 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:

	<u>2002-2003</u>	<u>2003-2004</u>
Net Expenditures by Major Object:		
Personal services	\$11,079,440	\$11,083,947
Contractual services	61,158,836	60,121,619
Commodities	102,026	148,280
Sundry charges	3,445,196	3,750,572
Equipment	47,700	14,973
Unclaimed property	9,441,860	10,862,104
Expenditures by Agency Funds	887,846	-
Net Expenditures	<u>\$86,162,904</u>	<u>\$ 85,981,495</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 2002-2003 and 2003-2004 fiscal years were paid from the following sources:

	<u>2002-2003</u>	<u>2003-2004</u>
General Fund:		
Budgeted Accounts	\$2,779,973	\$2,923,590
Restricted Accounts:		
Pension Fund Management	1,549,913	-
Second Injury Fund	4,588,847	-
Unclaimed Property	1,530,572	-
Short-Term Investment Fund	527,510	-
Special Assessment Fund	60,952	-
Grants and Restricted Accounts Fund:		
Pension Fund Management	-	1,600,795
Second Injury Fund	-	4,439,509
Unclaimed Property	-	1,562,475
Short-Term Investment Fund	-	557,578
Other Civil List Funds	41,673	-
Totals	<u>\$11,079,440</u>	<u>\$ 11,083,947</u>

Total personal services expenditures increased by approximately 4.2 percent in the 2002-2003 fiscal year and stayed relatively constant for the 2003-2004 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>2003</u>	<u>June 30,</u> <u>2004</u>
Full-time Permanent:		
General Fund:		
Budgeted Accounts	41	44
Restricted Accounts	102	-
Grants and Restricted Accounts Fund	-	101
Other Funds	4	4
Totals	<u>147</u>	<u>149</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 \$2,800,000 and \$4,500,000 for the 2002-2003 and 2003-2004 fiscal years, respectively. 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 other 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 2002-

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2003 and 2003-2004 fiscal years follows:

	<u>2002-2003</u>	<u>2003-2004</u>
Financial institutions	\$11,435,269	\$49,332,658
Business corporations	19,683,966	41,678,929
Insurance companies	8,844,598	6,144,911
Securities liquidated	21,118,557	1,413,120
Governmental and public agencies	2,046,605	3,469,330
Dividends on securities held	866,459	709,614
Interest penalty assessments	330,220	236,608
Reciprocal exchange with other States	803,483	927,228
Miscellaneous	5,279,277	510,789
Totals	<u>\$70,408,434</u>	<u>\$ 104,423,187</u>

Public Act 03-01 of the June 30, 2003 Special Session, reduced the dormancy periods for many different types of property from five to three years, which resulted in large increases from the prior fiscal year.

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

	<u>2002-2003</u>	<u>2003-2004</u>
Salaries and fringe benefits	\$2,144,697	\$2,295,637
Data processing and hardware	779,771	1,020,881
All other	113,144	236,078
Totals	<u>\$3,037,612</u>	<u>\$3,552,596</u>

In addition, \$865,958 and \$8,168,755 in fees were netted against unclaimed property receipts during the 2002-2003 and 2003-2004 fiscal years, respectively. Such fees consisted of fees for participation in out-of-state audits, brokerage fees for the sale of securities and other percentage-based fee relationships. Fiscal year 2003-2004 fees include \$6,907,921 associated with the receipt of cash and securities from the demutualization of insurance companies. 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, 2003</u>	<u>June 30, 2004</u>
Stocks and bonds	\$27,228,349	\$93,320,395
Mutual funds	7,340,330	10,951,926
Totals	<u>\$ 34,568,679</u>	<u>\$ 104,272,321</u>

The demutualization of several insurance companies and the related unclaimed stock from these transactions caused the increase in the market value of the stock portfolio. Mutual funds increased because of the reduction in the dormancy period.

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 \$9,441,860 and \$10,862,104 for the 2002-2003 and 2003-2004 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 Reports on the State Treasurer – State Financial Operations for the fiscal years ended June 30, 2003 and June 30, 2004.

PERFORMANCE REVIEW OF THE UNCLAIMED PROPERTY DIVISION:

Overview:

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 State Treasurer's Unclaimed Property Division (Division). Our objective was to determine whether the Treasury was complying with its statutory responsibilities to safeguard unclaimed property, make property owners' names public, and return the property to its rightful owners. We reviewed the Treasury's responsibility for the program as it relates to:

- Section 3-62g of the General Statutes, which requires the Treasurer to assume custody of unclaimed property and be responsible for all claims to owners.
- Section 3-66a of the General Statutes, which requires the Treasurer to publish the names of (previously unpublished) unclaimed property owners at least once every two years.
- Section 3-67a, subsection (c), of the General Statutes, which requires that when stocks are received, the Treasurer shall credit to the owners' accounts any dividends, interest or other increments realized or accruing on the property at or before liquidation.
- Section 3-70a, subsection (b), of the General Statutes, which specifies that the Treasurer shall consider each claim within ninety days after it is filed.

Background:

Prior to the fiscal year ended June 30, 2003, cash receipts of the Unclaimed Property Division of the State Treasury approximated between \$35 and \$40 million annually. Approximately 25 to 29 percent of these amounts were returned to property owners and the excess was remitted to the General Fund. The cash receipts for the fiscal years ended June 30, 2003 and 2004, increased substantially to \$71 and \$113 million, respectively. The large increases were due to changes in legislation that reduced the dormancy period for many types of abandoned property from five to three years. Generally, payouts of cash (not including the value of any stock) to rightful owners were between \$9.5 and \$11 million each year for the past five years. The Treasury has received almost as much money in the two fiscal years ended June 30, 2003 and 2004 combined (\$184 million), as it had in the previous five years since July 1, 1997 combined (\$194 million). With the increased receipts and the related demands to return more money to owners, the Division is clearly struggling to maintain its normal operations of assuming, accounting for, and repaying unclaimed property. We discovered considerable backlogs associated with both the posting of property to the Division's database, and returning property to owners of stock claims.

The Division has also been selling its inventory of stocks and forwarding the proceeds to the General Fund. Unfortunately, the stocks were sold before the Treasury properly updated owners' accounts for the stocks, splits, dividends, spin-offs, mergers, or other corporate actions for which the owners are entitled. Because the database was not completely updated with this information in a timely manner, additional attention is constantly required to verify the information to process

claims. This process appears to have resulted in slowed operations, very large backlogs and noncompliance with Section 3-67a, subsection (c), of the General Statutes, which requires that owners' accounts be updated before the stock is sold. As of June 30, 2005, the Division continues to have difficulties maintaining its daily tasks of taking in property and remitting it back to the rightful owners.

History of Accounting for Corporate Actions for Stocks:

Prior to 1998, the Treasury used a manual system to account for stock certificates and the related corporate actions such as dividends and stock splits. At that time, only owners' names and original shares were posted to the database, and the manual log sheets were used to account for the corporate actions attributable to each claim. This process, although not automated, was sufficient to process stock claims efficiently and effectively. In 1998, the Treasury sold off large amounts of stocks, while retaining others. The Treasury did not update its system in a timely manner to reflect what was sold and the database still reflected the original shares of stock escheated to the State. In our audit report for the fiscal year ended June 30, 1998, we recommended that, "Transactions and proceeds from the December 1998 stock sale should be reconciled to Treasury records, and the proceeds applicable to each owner should be identified."

About the same time, the Treasury began electronically uploading into its database the dividends, splits, mergers and other corporate actions for each stock. Because the system was not properly updated, the subsequent, automated postings for corporate actions were posted incorrectly to those owners' original shares, even if their shares had been sold. As the years passed, the posting errors multiplied as electronic uploads of corporate actions continued to post inaccurate information to the database. After mentioning this issue in three prior audit reports for the fiscal years ended June 30, 1998, 1999, and 2000, we summarized our concerns about the lack of attention this issue generated within the Treasury in our report for the fiscal year ended June 30, 2000:

"Treasury Officials stated in our prior audit report that additional staff would be assigned to work on updating the system and they projected it would take one year (until March 2001) to complete. Nearly three years have passed since the sale of securities in 1998 . . . yet only 50 percent of the project is complete. During our audit we noted that actual hours devoted to the project had decreased substantially and original timeframes were not met. Clearly, the State Treasury has not placed the appropriate emphasis on this project as needed to effectively, efficiently, and accurately return unclaimed property to their rightful owners."

This situation was made worse when the Treasury had two additional massive sales of stock, which were accounted for in substantially the same manner. As a result, the computerized database does not contain accurate information necessary to process stock claims. Instead, stock claims are calculated manually, which takes an inordinate amount of time (one claim was documented to take 83.5 hours to research and pay), and inevitably leads to frequent errors. This may explain why older, more complex stock claims are not processed sooner and backlogs continue in both holder reporting and claims processing areas.

Unresolved Prior Audit Recommendations:

Our prior audit reports for the periods ended June 30, 1998, 1999, 2000, 2001, and 2002 have included a total of 26 recommendations, many repeated from previous years' audits, which highlight areas needing improvement in the Division. This report includes 12 recommendations regarding the Division's operations and the following issues continue to be the basis for many of our concerns:

- Substantial amounts of cash, stocks, and other property have been collected by the Treasury but not posted to the database of owners' names. As of June 30, 2004, 4,417 holder reports representing owners' names associated with \$76,281,886 in cash and 4,073,045 shares of stock, estimated to be worth \$74,781,100, were not loaded to the database. Some of these amounts were received by the Treasury in 1999, yet owners still may not be aware that the Treasury is holding their unclaimed property as the database has not been updated to reflect all the property that was taken in. If the names are not included on the database, they are not published.
- Owners' names are not always published accordingly. In December 2004, the Treasury published the "Big List," a newspaper insert of owners' names received over approximately two years. The Big List did not include owners' names representing some \$5,039,031 in cash and 564,777 shares of stocks that should have been published in accordance with Section 3-66a. The failure to load owners' names on the database after collecting their property is a significant issue that should warrant immediate attention.
- Owners' property records are not always maintained on a current basis. The Treasury has failed to maintain current and accurate accounting records for all the owners' property in accordance with Section 3-67a, subsection (c). The database is not completely updated to accurately reflect stocks, dividends, stock splits, merger transactions, cash-in-lieu of shares and other corporate actions that owners of unclaimed property are rightfully entitled to.
- Claims are not always paid accurately. Because the database cannot be relied upon for accurate accounting of owners' property, the Division continues to process claims for stock by a very labor-intensive process through a complicated review of the stock's working file, dividend logs, and the proceeds from any sales of stocks. These calculations are not always accurate and our reports detail numerous errors we found during the course of our audit.
- Stock claims are frequently delayed and owners have waited multiple years for the Treasury to return their property. Most claims for stock are delayed well beyond the 90-day consideration period set forth in Section 3-70a, subsection (b), of the General Statutes. As of March 31, 2005, we counted a backlog of 714 stock claims, many with multiple-year delays and some claims dated back to 1999. It appears the Treasury cannot easily determine whether the owners' stocks were sold or retained due to the absence of updated and reconciled computer and accounting records.

Conclusion:

Although the Unclaimed Property Division within the State Treasurer’s Office strives to meet its statutory responsibilities under the General Statutes, the Division is constantly struggling to maintain daily operations and meet statutory responsibilities. The Division is not realizing the benefits from the efficiencies of automated processes and resources could be better placed to more efficiently and effectively upload the correct data into the system on a timely basis, which would lessen the delays in claims processing. Consequently, the Treasury does not always meet its statutory responsibilities under the General Statutes to account for, publish, and return property to its rightful owners in a timely manner.

Performance Audit – Elimination of Backlogs:

Criteria: Sections 3-62g, 3-66a, 3-67a, subsection (c), and 3-70a, subsection (b), of the General Statutes, require the Treasury to receive, account for, publish and repay property amounts on behalf of, or to, owners of unclaimed property. There is a 90-day consideration period for claims.

Condition: The Division has two substantial backlogs that require immediate attention. First, as of June 30, 2004, owners’ names associated with \$76,281,886 in cash and 4,073,045 shares of stock, worth an estimated \$74,781,100, were not loaded to the database. Generally, owners of this property are unaware that the Treasury is holding their funds because the database of owners’ names has not been updated upon receipt of the abandoned property as required by Section 3-67a of the General Statutes. The owners’ database must be updated to reflect the property held by the State for the names to eventually be published. Cash proceeds from this property have been forwarded to the General Fund.

Second, if owners do attempt to claim their property based on escheated shares of stock from the Treasury, they face multiple-year delays, and their property repaid may not be accurate. As of March 31, 2005, we counted 714 backlogged stock claims, many with multiple-year delays, and some even date back to 1999. During our current audit, we noted that 7 of 20 stock claims tested were paid inaccurately and none of these claims were paid within the 90-day consideration period. Additional recommendations based on our current audit work are presented later in this report.

Cause: Management’s failure to address significant issues that were presented in our five prior audit reports has contributed to this condition.

Effect: Unclaimed property records are not maintained properly, owners’ names do not always get published and stock claims are unreasonably delayed.

Recommendation: The Treasurer’s Unclaimed Property Division should comply with Sections 3-62g, 3-66a, 3-67a, subsection (c), and 3-70a, subsection (b), of the General Statutes, and resolve the backlogs related to updating property to

the database and repaying stock claims. (See Recommendation 1.)

Agency Response: “The Unclaimed Property Division (UCP) has initiated a process to eliminate the backlog of holder reports (in fact this was initiated before the draft audit report was received) with regular reports to the Deputy Treasurer.

Additional resources have been identified and some staff redeployed to finalize the Corporate Action Project, prepare stocks and mutual fund holdings for sale after loading to the owner data base, and address the backlog in servicing claims. In addition, our claims processing vendor is implementing an updated owner database system, which is currently being used in approximately 35 states. This system, developed by an individual with over thirty years experience in the unclaimed property field will provide UCP with much better technology to support the full range of activities in the Division. A project management team and conversion process for migrating to this system is being put in place.”

Performance Audit – Sell Stock When Received:

Criteria: Section 3-68a of the General Statutes allows the Treasurer to sell unclaimed stock certificates at the Treasurer’s discretion. Selling stock certificates as they escheat to the State would provide more immediate benefits to the General Fund and would simplify the process of updating owners’ records.

Condition: The Treasury’s practice is to sell unclaimed stocks in massive quantities, approximately once each year, and not as the stocks escheat to the State. Our reports have detailed the problems associated with this practice. They include failure to maintain current and accurate accounting records for all owners’ property, failure to reconcile and update the database on a timely basis, failure to always return the accurate amount of unclaimed property to owners, and failure to process all claims without significant delays.

Cause: Since the database was not consistently and completely updated in the past, current postings of corporate action information are not always accurate.

Effect: The Treasury incurs a significant administrative burden when it holds stock certificates in its inventory and does not sell them when received. This process has an effect on all aspects of the Division, including making inaccurate payments to owners and unreasonable, multiple-year delays in the processing of claims. Also, until the stock is sold for cash, the General Fund does not receive any benefits of the escheated stocks.

Recommendation: The Treasurer’s Unclaimed Property Division should consider selling stocks as they escheat to the State and immediately forward the cash proceeds to the General Fund. (See Recommendation 2.)

Agency Response: “UCP has conducted an annual sale of unclaimed securities since the law was changed in 2003. The inventory of mutual fund securities was liquidated in calendar year 2005 and stock certificates will be sold after owners’ records are updated. The frequency of future stock sales as recommended by the auditors is undergoing review.”

CONDITION OF RECORDS

The following findings resulted from our current review of the Office of the State Treasurer's Departmental Operations.

Late Deposit 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 that revenues received by the Unclaimed Property Division were not deposited within 24 hours. Receipts totaling \$19,959 were deposited and accounted for one day late.
- Cause:* The Treasury reported an employee did not follow established procedures.
- 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 Unclaimed Property Division should deposit funds in accordance with Section 4-32 of the General Statutes. (See Recommendation 3.)
- Agency Response:* "UCP believes it has adequate procedures for timely deposit of all receipts. However on October 28, 2003, a late deposit was reported by UCP to the Auditors. The late deposit occurred as a result of an error by a new employee. Checks totaling \$19,959 were not deposited within twenty-four hours of receipt. The new employee had been on the job less than two weeks and has received additional instruction on deposit procedures."

Delayed Collection Proceedings of Receivable Amounts:

- Criteria:* Section 3-66c of the General Statutes generally requires that whenever there may be unclaimed property escheatable to the State, the Treasurer shall make a demand for these amounts or request the Attorney General to institute proceedings, and shall take appropriate action to recover such funds or property. Sound business practice requires that adequate attempts be made at collecting outstanding receivables.
- Condition:* It does not appear that adequate attempts were made to collect outstanding receivables. As of June 30, 2004, the State was owed \$185,677 from two holders of unclaimed property, yet the Unclaimed Property Division contacted each of the holders only once in 2,308 and 923 days, respectively.
- Subsequent to our request, one holder was contacted via fax. Also, it appears that sufficient efforts have not been made to collect or account for other claimants who were overpaid \$22,487.

- Cause:* There were issues that delayed the final determination of the amounts due from each of the holder companies, however, since the final receivable amount was established, the holders were each contacted only once over a total of nearly nine years, or 3,231 days. It is unclear why overpayments to claimants are not pursued for collection.
- Effect:* General Fund revenues suffer when all amounts owed are not collected.
- Recommendation:* The Unclaimed Property Division should follow-up on receivables in accordance with Section 3-66c of the General Statutes, and enhance efforts to collect longstanding receivable amounts. (See Recommendation 4.)
- Agency Response:* “UCP has been in contact with the State of New York regarding \$109,239 in funds that were incorrectly submitted by a holder to New York. Although discussions with New York began in 2002, New York has only recently agreed that the funds will be returned to Connecticut and payment is expected by December 2005. UCP is working to recover the funds as expeditiously as possible. UCP’s attempt to collect the remaining \$76,677 of penalties and receivables from the other holder has been unsuccessful. The Attorney General’s Office has been notified as required by Section 3-66c of the CGS and UCP will proceed to write-off the remaining receivable and other receivable overpayments.”

Unnecessary Expenditure of State Funds:

- Criteria:* Section 3-65a, subsection (b), of the General Statutes, requires that holders of unclaimed property pay or deliver such property to the Treasurer. The Treasury’s Unclaimed Property Division has the ability, in accordance with subsection (g), to send experienced State Accounts Examiners to review a company’s records to determine whether the company has complied with the State laws relating to unclaimed property. There should be no conflict of interest between the services a contractor provides for the State of Connecticut and its other clients.
- Condition:* We became aware of fees paid amounting to \$6,865,646 for the identification and collection of unclaimed property which we believe could have been avoided. The engagements were commissioned by the Treasury and the fees were paid pursuant to an existing contract between a vendor and the Treasurer’s Office. The contract allowed for a fee of 12 percent of the value of the net abandoned property paid or delivered to the Treasurer’s Office by a vendor assigned to identify and recover unclaimed property. The \$6,865,646 of fees was related to the collection of abandoned cash and securities related to the demutualization of insurance companies.

Our review disclosed that the insurance companies would have been

required to self-report the unclaimed property amounts by March 31, 2005. No fees are paid when companies self-report. Instead, the Division authorized the contractor to perform a preemptive audit and paid the contractor its full fee of 12 percent of the value of the funds escheated to the State. Our review disclosed that certain insurance companies involved were already reporting to the Division on a regular basis in which case the contractor should not have received its full 12 percent fee. The contract specifically states that net abandoned property paid or delivered to the vendor and subject to the 12 percent fee does not include the value of all abandoned property which otherwise would have been delivered pursuant to the reporting practices of the holder. The contract states that if the State elects to receive such property through the vendor, then the State shall pay a reduced fee of 6 percent.

The contract also states that the State may direct the vendor not to process records on behalf of the State for a particular holder, in which case no percentage fee would be paid. Since the Division employs staff for the purpose of performing compliance examinations of holders of abandoned property, the examination of all demutualized insurance companies could have been performed by State employees at a much lower cost than that paid to the contractor.

Further, we also discovered that the contractor authorized to perform these services by the State Treasury, also was performing business process outsourcing for at least one of the demutualized companies. It appears there is a conflict of interest in providing a type of services to the holder (insurance) company and then charging the State for the “recovery” of funds that the insurance company was already required to submit under State law.

Cause: Management of the Treasury made an administrative decision to have the contractor act as its agent to recover these funds in advance of the voluntary reporting date.

Effect: An unnecessary payment of \$6,865,646 was made to a vendor with an appearance of a conflict of interest.

Recommendation: The Unclaimed Property Division should allow companies to self-report their unclaimed property, seek to reclaim all or a portion of the \$6,865,646, and should exercise certain contractual provisions that could result in substantial savings to the State. (See Recommendation 5.)

Agency Response: “The Office of the Treasurer strongly disagrees with this finding.

Perceived conflict of interest:

The auditors assert that an apparent conflict of interest at ACS should have precluded the firm from performing an unclaimed property audit at MetLife. By way of background, an ACS affiliate, ACS Commercial Solution, Inc. (“CSI”), provides MetLife back office services in the area of Group Life Insurance and Dental Care involving mail processing, x-ray processing, imaging, data entry, stored image and retrieval, etc., for dental and eligible enrollment forms that have nothing to do with the ACS Unclaimed Property Clearinghouse group (UPCH). The two ACS groups are organized and operated as separate and distinct businesses that prohibit sharing of information, employees, management, and facilities designed to avoid such conflicts of interest.

Applicability of the lower percentage rate:

There is no legal basis for the application of the contract’s reduced fee structure. Under the terms of the agreement with ACS, a reduced fee is available under a specific set of facts, which did not exist under the demutualization program. Therefore, the contractual basis for paying a reduced fee is the State of Connecticut electing to assign collection of abandoned property to ACS from a company that is (1) domiciled in Connecticut or (2) has a prior history of reporting. The facts do not support the desire to pay a reduced fee. All of the entities holding demutualization property were formed well after the execution of the ACS contract. None of the demutualization holders audited by ACS for the benefit of Connecticut were domiciled in the State of Connecticut.

Allow for voluntary reporting:

Had the State not engaged ACS to collect this property early, as a result of enabling legislation being changed in 2003 to reduce the dormancy period from 5 to 3 years, it is estimated that it could have cost the state \$3.1 million in lost investment income assuming 100% of the assets collected by ACS would not have been remitted on a voluntary basis. ACS advised the Office of the Treasurer that holders would be extremely pressed for time to determine liability to each state and were not prepared to report the escheatment of unclaimed accounts as many records lacked correct addresses of which state has the priority claim to an account. The UCP internal auditors did not have the capacity or resources to handle examination of demutualization unclaimed property owed to Connecticut by these holders, the most significant in the history of the unclaimed property program. With this much property involved, and the risk of the property being reported to the incorrect state, it is our position that the decision to engage ACS to audit the demutualization companies before the voluntary deadline was appropriate and in the best financial interest of the state.”

Auditors' Concluding

Comments:

Regarding the perception of a conflict of interest due to the State's contractor (ACS) providing back office services to the same insurance company that they were engaged to review, the Unclaimed Property Division was unaware that this potential conflict existed until we brought it to their attention. It is our contention that a potential conflict of interest exists when a contractor that is paid by the State to review an insurance company's group life records for accuracy is being paid by that same insurance company to update those group life records. The Unclaimed Property Division should be more diligent in uncovering business relationships between its contractors and the holders of abandoned property before engaging a contractor to perform an examination.

Our comments pertaining to the applicability of the lower percentage rate result from our observation that one holder had been consistently reporting on an annual basis both prior to the business reorganization that resulted in the demutualization of the company and after the business reorganization. This company reorganized into a public stock company and did holder reporting for the two years following the reorganization, then ACS was contracted to perform a preemptive review of this insurance company's reporting prior to the third year of reporting. Since the company had a prior history of reporting for the two years following the reorganization, we concluded that the reduced rate should apply.

Allowing the demutualized insurance companies to report their abandoned policies voluntarily prior to contracting for an examination would have resulted in a lower fee for the State. We were informed that the majority of demutualized insurance company policy records were clearly identified as to State of domicile. If the companies were first allowed to voluntarily report on the abandoned insurance policies that had complete addresses then these would not have been subject to the contractor's 12 percent fee. After the voluntary reporting had been completed, the contractor could have been engaged to review the remaining records and determine the State of domicile for the policies with incomplete addresses. Under this scenario the State would only pay the contractor's 12 percent fee for the difficult-to-identify policies. In our conversations with the contractor's representative, it was stated to us that approximately 67 percent of the demutualized insurance company's policy records contained clearly decipherable addresses. Had the holders not reported the remaining 33 percent accurately, they would have been subject to a 15 percent statutory penalty on the amounts not remitted to the State on a timely basis. This penalty would have been sufficient to cover the cost of the examination and provide the State with 3 percent of additional income.

The examination of demutualized insurance companies was conducted under an existing contract between the Unclaimed Property Division and ACS which included the maintenance of unclaimed stock and mutual fund

inventory as well as various holder examinations. Given the special conditions surrounding the examination of demutualized insurance companies, the Unclaimed Property Division should have executed a separate contract for this engagement and negotiated a fee more appropriate to the circumstances.

Holder Reporting Manual and “Big List” Publication:

Criteria: Section 2-90 requires us to report any irregular or unsafe handling or expenditure of State funds or any breakdown in the safekeeping of any resources of the State. Each year (usually prior to March 31st) the Treasury has Holder Reporting Manuals (Manuals) printed and mailed to approximately 3,500 holders of unclaimed property. The Manual helps to explain how and when holders are to remit unclaimed property to the State. Also, the Treasury contracts with a printer to publish the “Big List” of unclaimed property owners. The correct list should be presented to the printer to avoid any additional costs associated with corrections after the first proof is generated.

Condition: The Treasurer’s Office paid \$4,557 to have 3,500 58-page Manuals printed, but the Treasury never mailed them to the intended recipients. The reporting deadline (for holders to report their unclaimed property to the State) passed prior to getting the Manuals back from the printer. Instead, a letter was mailed to remind holders of their reporting responsibilities and inform them that the Manual was available online. Separately, the Treasury supplied the incorrect data file to the printer for the “Big List.” The State was charged an additional \$400 because a new file was supplied after the first proof was generated.

Cause: Treasury’s management placed the order too late for the publication deadline to be met and an employee’s error caused the wrong data file to be sent to the printer.

Effect: The Treasury incurred unnecessary expenses totaling \$4,957.

Recommendation: The Unclaimed Property Division should verify the file to be published for the “Big List,” not make unnecessary expenditures, and should publish only an online Holder Reporting Manual to reduce State expenditures in the future. (See Recommendation 6.)

Agency Response: “The 2004 holder-reporting manual distributed to holders and holder representatives was delayed until April 2005 in order to include legislative changes requiring banks to report and safe keep the contents of safe deposit boxes. However, the manual was available in its entirety on the Treasurer’s official Internet web page on February 4, 2005, several weeks before the March 31 reporting deadline and has been published online since 2001. 1,070 copies of the 3,500 printed copies were distributed to holders and

professional business organizations under a targeted outreach program and 1,900 printed copies have been distributed representing 54% of the total printed. The remaining copies of the manual will be distributed throughout the year at holder outreach events as well as UCP presentations. In addition, a second mailing of manuals occurs in the fall of each year to business groups, libraries and chambers of commerce depending on the number of manuals available. As noted by the Auditors, an error in the first proof of the “Big List” publication was discovered that resulted in an additional \$400 fee to correct the data file with the Hartford Courant.”

Auditors’ Concluding

Comments:

If the manual was available (online) in advance, as stated in the Treasurer’s response, it would seem its final print publication would not be delayed for any reason; we were told that constant editing caused the order to be placed late, incurring \$4,557 of unnecessary expenditures. We reiterate that the publication has not been used for its intended purpose.

Publication of Owners of Savings Bonds and Auctions of Safe Deposit Box Contents:

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. Section 3-66a of the General Statutes requires the Treasurer to publish the names of (previously unpublished) property owners at least once every two years.

Under Section 3-68a, subsection (a), of the Connecticut General Statutes, safe deposit box contents delivered to the Treasurer shall be sold at the Treasurer’s discretion with the cash proceeds deposited into the General Fund in accordance with Section 3-69a of the General Statutes. Proper internal controls over inventory items would help to ensure that items are appropriately safeguarded. Effective August 16, 2003, institutions that were holding safe deposit box items were required to sell such property and escheat the cash proceeds to the Treasury.

Condition:

In our prior audits, we disclosed that savings bonds were retrieved by the Treasury, but owners’ names have not yet been published in accordance with Section 3-66a of the General Statutes. We were informed that only the United States Treasury can determine whether the savings bonds hold any value as some (presumably lost) bonds may have been reissued by the United States Treasury. In the State Treasurer’s Holder Reporting Manual, it states that found savings bonds can be mailed to the United States Treasury. Despite this, the State Treasury has not yet forwarded its inventory of savings bonds with a face value of \$159,435 to the United States Treasury.

The State Treasury has been holding the contents of 124 safe deposit boxes

that were collected during the fiscal years ended June 30, 2001, 2002, and 2003. These owners' names have not yet been published as an auction needs to be held to determine the value of the property. Although the law allows the property to be sold at the Treasurer's discretion, some property has been stored at the Treasury for five years without owners' names being published. Effective August 16, 2003, future unclaimed safe deposit box items will not be delivered to the Treasury (but sold by the institution with the cash forwarded to the State), so older items held at the Treasury should be sold without further delay so owners' names can be published and the proceeds deposited into the General Fund.

During our audit we also discovered that the contents of 52 safe deposit boxes have not yet been added to the safe deposit box inventory list. We also found that items listed on the inventory (13 half dollars) could not be found and other items found (foreign and old coins, wooden nickel, federal reserve note, and 11 Indian Head nickels) were not posted to the inventory listing. In addition, our prior audit for the fiscal year ended June 30, 2002 disclosed that thirty four banks and six hospitals reported abandoned property in 1,653 safe deposit boxes for the calendar years 1998, 1999, 2000 and 2001, but the property was not retrieved by the Treasury as required during that time. Although the law now requires the holders to auction the property and escheat the cash proceeds to the State, it does not appear the Division has followed up on the status of these boxes to ensure all amounts were auctioned, with the proceeds forwarded to the State.

Cause: According to Treasury Officials, they are waiting to participate in a national initiative to forward the remaining inventory of savings bonds to the United States Treasury. It appears this initiative is delaying the final placement of the bonds. Concerning the safe deposit box auctions, Treasury appears to have placed greater emphasis on other issues.

Effect: Publication of names is delayed and the General Fund does not receive the benefits of items recovered from safe deposit boxes until sold.

Recommendation: The Unclaimed Property Division needs to improve its handling of the inventories of savings bonds and safe deposit box contents and ensure that owners' names associated with such property are made public. (See Recommendation 7.)

Agency Response: "UCP is participating with NAUPA/NAST and the U.S. Treasury to collectively advance Federal legislation that will address informing owners of unclaimed savings bonds. UCP plans to transfer all U.S. Savings Bonds to the U.S. Treasury in fiscal year 2006. The safe deposit box contents inventoried from the previous years appear to be of minimal value. However UCP is planning one final auction of all remaining safe deposit box contents by the end of fiscal year 2006. The 34 banks and 6 hospitals that were holding safe deposit box contents not previously collected by

UCP between 1998 and 2001 were instructed to include the property in their auctions when the law was changed in 2003. With respect to the other audit comments regarding the thirteen half dollars erroneously listed on the auction inventory sheet, they were deposited on January 14, 2003 and a claim was filed for them. Eleven Indian head nickels should have been listed on the auction inventory instead of eleven half dollars, and the correction to the auction inventory report has been made.”

Claims Processing Deficiencies 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 (Division) has established procedures that should prevent duplicate payments. The Division records the original request for return of the shares, and the paid information on the holder report to document that the payment has been requested and/or paid. Internal control procedures should be followed to prevent duplicate payments.

Condition: Our review of 25 claims paid by the Division, together with the Treasury’s disclosure of payment errors, found that:

- One owner was issued twice the number of shares than the owner was entitled to receive. The Treasury returned 120 shares of stock in error. These 120 shares were valued at \$3,000 on June 17, 2005.
- Another claim was processed twice for \$28.
- Seven of 25 claims we tested were underpaid for small amounts of dividends. These seven owners are due a total of \$229.

We also discovered during our review that key controls (established to prevent overpayments) were not always followed:

- Three of 25 holder reports were not properly posted to reflect a claim had been made against the property.
- 18 holder reports of 25 were not posted to show the claim was paid.
- Three claims were not updated to reflect paid status in the computerized database.
- Two claims had dividends recorded in the database that were not property of that owner.

Twenty of the 25 claims tested were processed well beyond the 90-day consideration period, with an average waiting period of 334 days, and the longest claim having an 823-day processing period.

We also noted a significant backlog of 714 claims to be processed, with some dating back to 1999. This backlog is more fully explained in the Performance Review section of this report.

Cause: A decision to publish claims under \$50 on the Internet, a change in the

dormancy period from five to three years, and demutualization claims have caused the claims processing staff to be extremely taxed. These heavy demands may have contributed to the overall deficiencies in this area.

Effect: Claimants are not receiving the full value of their property in a reasonable amount of time and poor adherence to established internal controls increases the risk that overpayments could occur.

Recommendation: The Unclaimed Property Division should comply with Section 3-70a, subsection (b), of the General Statutes, should follow internal control procedures designed to prevent overpayments and should recover overpayments. (See Recommendation 8.)

Agency Response: “UCP’s procedures to prevent overpayments will be reviewed and strengthened if necessary and overpayments will be recovered. The Office of the Treasurer recognizes that more progress and attention in the processing of stock claims and resolving the Corporate Action Project and backlog associated with claims processing is required as noted in our response under the Performance Audit section of the audit report.”

Holder Processing Deficiencies in the Unclaimed Property Division:

Criteria: Section 3-62g of the General Statutes requires the Treasurer to assume custody of property and be responsible for all claims to unclaimed property owners. Items that escheat to the State include cash, stock, and safe deposit box proceeds. Property owner information is stored in a database, which is used for claims processing and is the source for the Statewide publication. Section 3-66a of the General Statutes requires the Treasurer to publish the names of unclaimed property owners (that have not previously been published) at least once every two years. Section 3-67a, subsection (c), requires that certain owners’ records be updated accordingly.

Condition: Our review disclosed property in the custody of the Unclaimed Property Division that was not loaded into the database of owners’ names. Generally, property must be loaded into the database for it to be included in a future publication. Property not loaded as of June 30, 2004 includes an estimated \$151,062,986 in cash and securities. This backlog is further explained in the Performance Review section of this report.

Of the holder reports tested during our current audit, we found numerous errors:

- One holder report was not included in the “Big List” publication.

- 900 shares that were never received were loaded into the database.
- A holder report was not adjusted to reflect that 660 shares were not received by the Treasury. The database reflected the correct number of shares.
- Of our sample of 25, the Treasury did not load three holder reports totaling \$30,245 into the system as of June 2, 2005.
- One report was not available for our review.

Cause: Other issues appear to have taken greater priority.

Effect: Generally, if proper care is not taken to appropriately assume and account for unclaimed property, owners of property will not be served, claims will be delayed, and there may be an increased risk of loss.

Recommendation: In accordance with Sections 3-62g and 3-66a of the General Statutes, the Unclaimed Property Division should act responsibly to assume, account for, and publish unclaimed property. (See Recommendation 9.)

Agency Response: “Standard procedures in place to manage the holder reporting function will be reviewed in order to improve controls and minimize, if not eliminate future errors. UCP has initiated a process to eliminate the backlog of holder reports, with regular reports to the Deputy Treasurer, as noted in our response under the Performance Audit section of the audit report.”

Failure to Maintain Owners’ Accounts on a Current Basis:

Criteria: Section 3-67a, subsection (c), of the General Statutes requires that, “Whenever any property other than money is paid or delivered to the Treasurer..., the Treasurer upon receipt shall credit to the owner’s account any dividends, interest or other increments realized or accruing on the property at or before liquidation or conversion thereof into money.” Before the Treasurer sold massive quantities of stock, the Treasurer was responsible to update all owners’ records for corporate actions.

Condition: Stock holdings were sold during the audited period as well as prior periods, before owners’ records were completely updated in the database of owners’ names at the Treasury. The Treasury maintains a list of all the companies’ stocks that are not updated within the database of owners’ names. According to this list, there were 75 companies relating to a prior period sale whose escheated amount does not reconcile to Treasury accounting records. The failure to maintain owners’ records on a current basis causes increased work when a valid stock claim is presented for payment, which contributes to the backlog of stock claims. This is a significant backlog which is further explained in the Performance Review section of this report.

Cause: There has been a lack of management oversight concerning this issue.

Effect: Owners' records are not reflected accurately in the database and claims are delayed for unreasonable periods of time.

Recommendation: In accordance with Sections 3-67a, subsection (c), of the General Statutes, the Unclaimed Property Division should credit the appropriate amounts to owners' records and update its database to a current status. (See Recommendation 10.)

Agency Response: "As noted in the Performance Audit section of this report, the Office of the Treasurer recognizes that more progress and attention in the processing of stock claims and resolving the Corporate Action Project and backlog associated with claims processing is required. The Office of the Treasurer plans a full management and operations study of the Unclaimed Property Division that will include a review of all systems and processes currently in place, and the working relationship between UCP and our outside audit/custody services vendor.

Lack of Work-at-Home Agreements:

Criteria: In accordance with Section 5-248i of the General Statutes, employees may be authorized to participate in a telecommuting or work-at-home agreement with the approval of the appointing authority and with the approval of the Commissioner of Administrative Services. The agreement should be temporary, for a period not to exceed six months, and may be extended as necessary.

Condition: During the course of our audit, we noted that three Treasury employees were allowed to work at home without having signed telecommuting agreements on file.

Cause: Lack of administrative oversight may have contributed to this issue.

Effect: Ambiguities about issues such as the at-home work location and the agreed upon hours of work could result in conflicts regarding workers' compensation coverage and other aspects of the work relationship.

Recommendation: The Treasurer's Office should comply with Section 5-248i of the General Statutes and have signed agreements approved by the Commissioner of Administrative Services for all employees that are working at home. (See Recommendation 11.)

Agency Response: “All supervisory staff have been reminded that the Treasury Office Personnel unit has to process an employee’s request to work at home before being granted. Due to one employee’s existing medical requirement, a supervisor in error permitted work at home from the office since a previous medical work at home request related to the same medical condition had previously been approved by DAS. This supervisor has been reminded that DAS policy requires each work at home request to be properly submitted and approved by DAS. The Personnel unit will develop an internal process to ensure timely submittal and approval of work-at-home agreements.”

Auditors’ Concluding

Comments: The State’s Telecommunicating Agreement clearly states the agreement is temporary, for a period not to exceed six months, and may be extended as necessary with the appropriate written approvals. We could find no exceptions to these requirements, regardless of health. Although one employee had returned to work by the time our audit commenced, Treasury Officials allowed two employees to continue to work at home without approved telecommuting agreements. At our request, those employees were asked to report to the Treasury until approved agreements were in place.

Failure to Monitor Employees’ Excessive Absenteeism:

Criteria: The Treasurer’s policy regarding excessive absenteeism is intended to prompt closer scrutiny by supervisory personnel to ensure that abuse of leave time is not occurring. The policy provides for certain administrative or disciplinary action where excessive absenteeism is considered the result of abuse of sick or other leave.

Condition: The Treasurer’s Office failed to adequately monitor employees with patterns of usage that suggest excessive absenteeism. In our sample of an additional 20 employees, we found that the policy was not enforced for nearly half of the employees whose sick time usage could be considered excessive in accordance with the policy.

Cause: Lack of administrative oversight may have contributed to this issue.

Effect: Failure to adequately monitor employees’ use of sick time could result in abuse going undetected.

Recommendation: The Treasury should comply with its policy regarding administrative or disciplinary action when excessive absenteeism is considered the result of abuse of sick or other leave. (See Recommendation 12.)

Agency Response: “The Treasurer’s Office has updated and reissued its policy regarding excessive absenteeism. The original agency policy gave latitude to managers and supervisors in determining whether or not there was an

absenteeism abuse issue based on their supervisory experience and direct knowledge of individual situations. However, the policy was more restrictive than the policy issued by DAS to other State agencies. The new policy as reissued provides general criteria all agency supervisory personnel must be aware of in assessing whether or not abuse of leave time is occurring. We respectfully disagree with the number of alleged instances of excessive absenteeism as cited by the auditors. The reports formerly used for the quarterly attendance review were unavailable with initial implementation of Core-CT in 2003. As of February 2005, an automated reporting quarterly attendance module has become available on the Core-CT system. During the period between 2003 and 2005 agency attendance was monitored in other ways and absenteeism issues were addressed accordingly.”

Auditors’ Concluding

Comments: The Treasury’s procedures required the Human Resource Administrator to submit a quarterly Excessive Absenteeism Report to the Treasurer; however, we were told that this had not been done and that excessive absenteeism had not been monitored since October 2003. Based upon our review, absenteeism issues were not addressed accordingly and, if there were alternative methods to monitor excessive absenteeism, the Treasury failed to provide those documents to us.

Work Schedules Contrary to Established Guidelines:

Criteria: Section 5-238 of the General Statutes and the State Manager’s Guide, state that the required work hours for managers is 40 hours per week.

Condition: During our audit, we discovered that six nonbargaining unit employees’ work schedules did not reflect the standard, 40 hours per week. Three employees’ work schedules documented work hours to reflect 35 to 37 ½ hours per week, and the others did not document the number of hours to be worked; yet, they were all paid based upon a 40-hour week. After we notified the Treasury of the discrepancies, some employees changed their documented work schedules to reflect a standard 40-hour week. Our review of the card-key entrance records indicated that certain employees were coming in later than their specified work schedules.

Cause: Lack of administrative control and supervisory oversight may have contributed to this issue.

Effect: Employees whose work schedules do not reflect the required minimum may not be entitled to their full salary.

Recommendation: The Treasurer’s Office should establish and enforce a policy documenting the standard work schedule for each employee and should verify employees

are working their approved schedules to ensure the State gets the full value for wages paid to employees. (See Recommendation 13.)

Agency Response: “All work schedules have been reviewed to ensure compliance with applicable statute, regulation, collective bargaining agreement and Treasury Office policy. While every employee working in the agency has an established work schedule, some individual work schedules are modified when necessary to accommodate certain business or personal needs that arise requiring earlier or later start and ending times. Treasury employees are required to keep their immediate supervisors informed of their schedule and any short-term modification. Long-term/permanent schedule changes are reviewed and approved by the personnel officer (for collective bargaining positions) and by the Deputy Treasurer/Chief of Staff (for managerial and unclassified appointees.)”

*Auditors’ Concluding
Comments:*

We asked for the work schedules that the Treasury indicated it now has on file. For several employees, the schedules detailed work arrival times but not departure times. We do not consider these valid work schedules.

RECOMMENDATIONS

Status of Prior Audit Recommendations:

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

- 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. This issue has been studied by the Second Injury Fund Division and implementation of a reimbursement by the Workers' Compensation Commission is not forthcoming. We are not repeating this recommendation.
- The Office of the State Treasurer's Unclaimed Property Division should 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 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. Our current review of contract payments indicated an instance in which all contract provisions were not adhered to. We have restated this recommendation as Recommendation 5.
- The Office of the Treasurer should review and strengthen internal controls in order to prevent another occurrence of duplicate payments. Our current review disclosed instances of duplicate payments. This recommendation has been restated as Recommendation 8.
- The Office of the State Treasurer's Unclaimed Property Division should comply with Section 3-62g of the General Statutes and its 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. This recommendation is repeated as Recommendation 9.
- 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. This recommendation has been restated to reflect current conditions and is presented as Recommendation 8.

Current Audit Recommendations:

The following recommendations resulted from our current review.

- 1. The Treasurer's Unclaimed Property Division should comply with Sections 3-62g, 3-66a, 3-67a, subsection (c), and 3-70a, subsection (b), of the General Statutes and resolve the backlogs related to updating property to the database and repaying stock claims.**

Comments:

As of June 30, 2004, owners' names representing an estimated \$151,062,986 in cash and stock have not been posted to the database of owners' names. None of these owners would be able to claim their property as the Treasury has not posted the property to its database. Owners attempting to claim stocks (or the cash proceeds) that were posted to the database face very long delays, well beyond the 90-day consideration period set forth in the General Statutes. We found that certain owners have been waiting years for their property to be returned to them. As of March 31, 2005, we counted a backlog of 714 stock claims, many with multi-year delays, and some that date back to 1999.

- 2. The Treasurer's Unclaimed Property Division should consider selling stocks as they escheat to the State and immediately forward the cash proceeds to the General Fund.**

Comments:

Approximately once each year, the Treasury's practice is to sell unclaimed stocks in massive quantities prior to updating owners' records and not as the stocks escheat to the State. Our audit reports have detailed the problems associated with this practice. They include failure to maintain current and accurate accounting records for all owners' property, failure to reconcile and update the database on a timely basis and, either not returning the accurate amount of unclaimed property or incurring significant delays in the processing of stock claims.

- 3. The Unclaimed Property Division should deposit funds 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. Receipts totaling \$19,959 were deposited and accounted for one day late.

- 4. The Unclaimed Property Division should follow-up on receivables in accordance with**

Section 3-66c and should enhance efforts to collect longstanding receivable amounts.

Comments:

It does not appear that adequate attempts were made at collecting or accounting for outstanding receivables. Two holders owe the State \$185,677, yet backup documentation showed the Division only contacted each of the holders once in 2,308 and 923 days, respectively. Several receivables from claimants who were overpaid by \$22,487 were also not sufficiently addressed.

- 5. The Unclaimed Property Division should allow companies to self-report their unclaimed property, seek to reclaim all or a portion of the \$6,865,646, and should exercise certain contractual provisions that could result in substantial savings to the State.**

Comments:

In our review of the Unclaimed Property Division (Division), we became aware of fees paid amounting to \$6,865,646 for the identification and collection of unclaimed property, which we feel could have been avoided. The engagements were commissioned by the Treasury and the fees were paid pursuant to an existing contract between a vendor and the Treasurer's Office. Since the Division employs staff for the purpose of performing compliance examinations of holders of abandoned property, the examination could have been performed by State employees at a much lower cost than that paid to the contractor.

Further, we also discovered that the contractor authorized to perform these services by the Treasury also was performing business process outsourcing for at least one of the companies being examined. This business arrangement represents a potential conflict of interest in providing a type of services to the holder company and then charging the State for the "recovery" of funds that the same company apparently was required to process under existing State statutes.

- 6. The Unclaimed Property Division should verify the file to be published for the "Big List," not make unnecessary expenditures, and should publish only an online Holder Reporting Manual to reduce State expenditures in the future.**

Comments:

The Treasurer paid \$4,557 to have 3,500 58-page Manuals printed, but the Treasury never mailed the manuals to the intended holders because the order was placed too late for the printer to supply the Manuals. Future publications of this Manual should be limited to an online publication. Separately, the Treasury paid an extra \$400 to another printer because they submitted a new "Big List" file after the first proof had been generated by the printer.

- 7. The Unclaimed Property Division needs to improve its handling of the inventories of savings bonds and safe deposit box contents and ensure that owners' names associated**

with such property are made public.

Comments:

The Treasury has been holding its inventory of savings bonds and the contents of 124 recovered safe deposit boxes for years without publishing owners' names. Institutions had also reported to the Treasury that the contents of some 1,653 safe deposit boxes were abandoned. Although it was the Treasury's responsibility to retrieve these items soon after they were reported (between 1998 and 2002), the Treasury had not done so. New legislation was passed that now requires the institutions to sell such items and forward the cash proceeds to the State, however, the Treasury has not verified that the proceeds from the sale of the 1,653 boxes were forwarded as required.

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

Comments:

Our review of property returned by the Unclaimed Property Division found that key controls were not adhered to, overpayments and underpayments were made and all stock claims were processed well beyond the 90-day consideration period.

- 9. In accordance with Sections 3-62g and 3-66a of the General Statutes, the Unclaimed Property Division should act responsibly to assume, account for, and publish unclaimed property.**

Comments:

Aside from our Performance Review, which included our concerns about the estimated \$151,062,986 of property not loaded into the database, our review of current property escheatments during our audit period disclosed several processing errors. One holder report was not included in the "Big List" publication, shares that were never received were loaded into the database, holder reports did not reflect the correct number of shares received, and one report was not available for our review.

- 10. In accordance with Section 3-67a, subsection (c), of the General Statutes, the Unclaimed Property Division should credit appropriate amounts to owners' records and update its database to a current status.**

Comments:

Failure to update the database to a current status causes claims for shares of stock to be delayed unnecessarily and the risk for loss to increase.

- 11. The Treasury should comply with Section 5-248i of the General Statutes and have signed agreements approved by the Commissioner of Administrative Services for all employees**

that are working at home.

Comments:

During our audit, we noted three employees were allowed to work at home without having approved telecommuting agreements.

- 12. The Treasury should comply with its policy regarding administrative or disciplinary action where excessive absenteeism is considered the result of abuse of sick or other leave time.**

Comments:

The Treasurer's policy regarding excessive absenteeism provides for certain administrative or disciplinary action when excessive absenteeism is considered the result of abuse of sick or other leave. The Treasurer's Office failed to adequately address employees whose patterns of usage may suggest excessive absenteeism.

- 13. The Treasurer's Office should establish and enforce a policy documenting the standard work schedule for each employee and should verify employees are working their approved schedules to ensure the State gets the full value for wages paid to employees.**

Comments:

We found documented work schedules that did not conform to the required standards. When we inquired how the documented work schedules were considered acceptable, we received several different responses that attempted to provide an explanation, such as employees were working at home (but had no telecommuting agreements), or were working through their lunch (which is not allowed), or finally, that the times listed on the work schedule form were simply "typographical errors." None of this information was verifiable. We noted that card-key entrance records were inconsistent with the documented work schedules in that employees were arriving later than their scheduled work times. We were unable to determine the times employees departed from work. Failure to adequately monitor employees' work schedules may result in payments for services that employees had not worked.

INDEPENDENT AUDITORS' CERTIFICATION

As required by Section 2-90 of the General Statutes we have audited the books and accounts of the Office of the State Treasurer for the fiscal years ended June 30, 2003 and 2004. This audit was primarily limited to performing tests of the Agency's compliance with certain provisions of laws, regulations, contracts and grants, 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, contracts and grants 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 Office of the State Treasurer for the fiscal years ended June 30, 2003 and 2004, is included as a part of our Statewide Single Audit of the State of Connecticut for those fiscal years.

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 Office of the State Treasurer complied in all material or significant respects with the provisions of certain laws, regulations, contracts and grants to obtain a sufficient understanding of the internal controls 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, contracts and grants applicable to the Office of the State Treasurer is the responsibility of the Office of the State Treasurer's management.

As part of obtaining reasonable assurance about whether the Agency complied with laws, regulations, contracts and grants, 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 years ended June 30, 2003 and 2004, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants. 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 Office of the State Treasurer is responsible for establishing and maintaining effective internal controls over its financial operations, safeguarding of assets, and compliance with the requirements of laws, regulations, contracts and grants 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 Office of the State Treasurer's financial operations, safeguarding of assets, and compliance with certain provisions of laws, regulations, contracts, and grants, and not to provide assurance on the internal control over those control objectives.

However, we noted certain matters involving the internal controls 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 controls 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, contracts and grants. We believe the following findings represent reportable conditions: the Unclaimed Property Division should allow companies to self-report their property, exercise certain contractual provisions that could result in savings to the State and consider potential conflicts of interest in the future; the Unclaimed Property Division should update all owners' records to a current status, and improve procedures to collect, manage, publish, account for and repay all unclaimed property; and the Treasury should monitor employees' attendance and work schedules more closely.

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 controls over the Agency's financial operations and over compliance would not necessarily disclose all matters in the internal controls 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.

Maura F. Pardo
Principal Auditor

Approved:

Kevin P. Johnston
Auditor of Public Accounts

Robert G. Jaekle
Auditor of Public Accounts