

STATE OF CONNECTICUT



*AUDITORS' REPORT
STATE TREASURER – DEPARTMENTAL OPERATIONS
FOR THE FISCAL YEARS ENDED JUNE 30, 2015 AND 2016*

AUDITORS OF PUBLIC ACCOUNTS
JOHN C. GERAGOSIAN ❖ ROBERT J. KANE

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JOHN C. GERAGOSIAN

State Capitol
210 Capitol Avenue
Hartford, Connecticut 06106-1559

ROBERT J. KANE

October 10, 2018

AUDITORS' REPORT STATE TREASURER - DEPARTMENTAL OPERATIONS FOR THE FISCAL YEARS ENDED JUNE 30, 2015 AND 2016

We have audited certain operations of the Office of the State Treasurer (Treasury) in fulfillment of our duties under Section 2-90 of the Connecticut General Statutes. The scope of our audit included, but was not necessarily limited to, the fiscal years ended June 30, 2015 and 2016. The objectives of our audit were to:

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

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

We conducted our audit in accordance with the standards applicable to performance audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United

States. Those standards require that we plan and perform our audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides such a basis.

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

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

The State Auditors' Findings and Recommendations in the accompanying report presents any findings arising from our audit of the Office of 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 is organized into several divisions and performs a number of functions. This report is concerned with the departmental operations of the Treasury and primarily includes our review of the Business Office, Personnel, Informational Services, and the Unclaimed Property Division. Our review of financial operations of the Treasury 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 listing of officers and officials with a description of the major functions of the divisions covered in this report follows.

Officers and Officials

The officers and officials of the Treasury as of June 30, 2016, were as follows:

Denise L. Nappier, State Treasurer
Lawrence Wilson, Deputy Treasurer, Assistant Treasurer Cash Management
Maria M. Greenslade, Asst. Deputy Treasurer, Second Injury and Unclaimed Property
Deborah Spalding, Chief Investment Officer
Mary Phil Guinan, Assistant Treasurer, Policy
Sarah Sanders, Assistant Treasurer, Debt Management

New Legislation

Public Act 15-5, effective July 1, 2015, amended Section 3-66a of the Connecticut General Statutes to allow the Treasury to post on its website unclaimed property with a value of \$50 or more that was not previously posted. This removed the requirement that the information be published in various newspapers around the state.

Public Act 15-80, effective October 1, 2015, required the State Treasurer to establish a federally qualified Achieving a Better Life Experience (ABLE) program and administer ABLE accounts. The program must help eligible individuals save private funds to pay for qualifying expenses related to a disability. The earnings from these accounts would generally be exempt from state, local, and federal taxes. Also, these funds would not be considered when determining an individual’s eligibility for assistance under federally funded assistance or benefit programs.

Public Act 16-113 made changes to Section 3-13a of the Connecticut General Statutes to include a principal investment officer with the existing positions of chief investment officer and deputy chief investment officer, as positions in which the State Treasurer can establish a salary range with consultation from the Investment Advisory Council. Under prior law, the Department of Administrative Services determined the compensation of principal investment officers, subject to the approval of the Office of Policy and Management.

RÉSUMÉ OF OPERATIONS

Department Revenues

Departmental revenues were primarily from the Second Injury and Compensation Assurance Fund (SIF), Workers’ Compensation Administration Fund (WCAF), Federal and Other Restricted Accounts Fund, and the General Fund. The Second Injury Fund’s revenues consisted mainly of assessments levied against self-insured employers and companies writing workers’ compensation or employers’ liability insurance, and totaled \$41,120,849 and \$40,447,957, for the fiscal years ended June 30, 2015 and 2016, respectively. WCAF assessment receipts totaled \$23,722,454 and \$25,054,344, for the fiscal years ended June 30, 2015 and 2016, respectively. Unclaimed property receipts increased during the fiscal year ended June 30, 2015, and then decreased for the year ended June 30, 2016. These amounts will fluctuate from year to year based on the type of escheats received as well as the value of the stock that is escheated. The changes in the Other Restricted Account represents deposit of funds associated with the operating expenses of the Pension Funds Management Division, Second Injury Fund, Unclaimed Property Division, Short-Term Investment Fund, and the Debt Management Division. These amounts will fluctuate from year to year based on activity.

	<u>Fiscal Year Ended June 30,</u>		
	<u>2014</u>	<u>2015</u>	<u>2016</u>
Federal and Other Restricted Accounts Fund	\$ 235,051,080	\$ 299,284,816	\$ 268,807,813
General Fund - All other Receipts	30,176,005	36,183,907	39,192,352
General Fund – Unclaimed Property	87,050,009	128,605,748	100,097,186
Total Revenues	<u>\$ 352,277,094</u>	<u>\$ 464,074,471</u>	<u>\$ 408,097,351</u>

Section 3-69a of the General Statutes calls for a portion of escheat revenues to be allocated to the Citizens' Election Fund. Transfer amounts are determined based on the prior year amount, adjusted by the changes in the consumer price index. The transfers to the Citizens' Election Fund totaled \$11,281,219 and \$11,349,203 for the fiscal years ended June 30, 2015 and 2016, respectively. Since its inception, transfers to the Citizens' Election Fund have totaled \$160,024,275. The State Elections Enforcement Commission administers this fund, which grants public financing to the campaigns of participating candidates for state office. Prior to the Citizens' Election Fund, all unclaimed property funds were deposited into the General Fund. The amounts for the Citizens' Election Fund as well as administrative expenses for the Unclaimed Property Program were deducted from the General Fund – Unclaimed Property amounts noted above. Although amounts are distributed to various funds, the full value of escheated property is always available to be claimed by the rightful owner. The Treasury also receives non-cash (unclaimed) property, including shares of stocks and mutual funds. The noncash property is not reflected in the General Fund cash receipts until it is sold. As of June 30, 2015 and 2016, the Treasury estimated the market value of unclaimed securities to be \$534,458 and \$3,773,812, respectively.

Department Expenditures

General Fund expenditures of the Treasury for the fiscal years ended June 30, 2014, 2015, and 2016, are summarized below:

	<u>Fiscal Year Ended June 30,</u>		
	<u>2014</u>	<u>2015</u>	<u>2016</u>
Debt Service	\$ 1,645,589,711	\$ 1,690,022,326	\$ 1,967,360,338
Unclaimed Property Returned to Owners	63,776,421	61,100,129	57,572,275
Purchased & Contractual Services	637,407	1,722,234	440,856
Personal Services & Employee Benefits	3,133,301	3,122,049	3,060,211
Information Technology	20,072	18,690	16,866
Premises & Property Expenses	22,179	15,748	20,547
Employee Expenses, Allowances & Fees	8,421	4,120	8,324
Purchased Commodities	17,747	13,560	11,495
Motor Vehicle Costs	8,265	6,193	9,301
Capital Outlays - Equipment	-	-	-
Net Expenditures	<u>\$ 1,713,213,524</u>	<u>\$ 1,756,025,049</u>	<u>\$ 2,028,500,213</u>

Debt service expenditures can vary significantly from year to year based on the amount of bonds issued. Unclaimed property returned to owners also varies, as it depends on several factors, including volume of claims and the performance of the stock market, as a significant amount of claims represent escheated stock that is sold by the Treasury upon receipt.

Federal and Other Restricted Accounts Fund expenditures of the Treasury for the fiscal years ended June 30, 2014, 2015, and 2016, are summarized below:

	<u>Fiscal Year Ended June 30,</u>		
	<u>2014</u>	<u>2015</u>	<u>2016</u>
Debt Service	\$ 76,701,720	\$ 151,548,687	\$ 143,149,354
Purchased & Contractual Services	106,435,702	103,630,274	97,621,197
Personal Services & Employee Benefits	16,779,840	16,975,749	17,582,303
Information Technology	273,535	469,307	434,496
Premises & Property Expenses	42,993	46,697	49,961
Employee Expenses, Allowances & Fees	31,230	25,716	27,384
Purchased Commodities	47,179	48,084	78,968
Motor Vehicle Costs	35,587	29,137	30,396
Capital Outlays - Equipment	11,804	-	34,495
Other Expenditures	500,800	6,400,000	2,013,358
Net Expenditures	<u>\$ 200,860,390</u>	<u>\$ 279,173,651</u>	<u>\$ 261,021,912</u>

Special Revenue Funds were the major funding source for the State 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 paid from the Special Revenue Fund. Contractual and personal services are the major expenditures of the Treasury other than debt service costs. The most significant items included in contractual services are the payments of investment advisor fees by the Pension Funds Management Division.

In addition to the General Fund and Federal and Other Restricted Accounts Fund expenditures, there were expenditures from the Transportation Fund and the Clean Water Fund. Total expenditures from these funds for the fiscal years ended June 30, 2015 and 2016, were \$464,522,274 and \$498,436,245, respectively. The majority of these amounts, \$459,736,393 and \$493,549,682, were related to debt service payments for transportation bonds.

Personal services expenditures were paid from the following sources:

	<u>Fiscal Year Ended June 30,</u>		
	<u>2014</u>	<u>2015</u>	<u>2016</u>
General Fund:			
Budgeted Accounts	\$ 3,133,301	\$ 3,122,049	\$ 3,060,211
Federal and Other Restricted Accounts Funds			
Second Injury Fund	6,083,205	6,206,167	6,476,881
Pension Funds Management Division	6,421,638	6,440,941	6,578,975
Unclaimed Property	2,977,698	2,991,270	3,155,614
Short-Term Investment Fund	1,297,299	1,337,371	1,370,833
Totals	<u>\$ 19,913,141</u>	<u>\$ 20,097,798</u>	<u>\$ 20,642,514</u>

Total personal services expenditures increased by 0.9% and 2.7% in the fiscal years ended June 30, 2015 and 2016, respectively. Wages remained somewhat constant and positions filled during the period were steady.

Unclaimed Property Division

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 cash receipts to be deposited into the General Fund with the exception of periodic transfers to the Citizens' Election Fund and a restricted unclaimed property account within the General Fund. The restricted account funds are used to pay the Unclaimed Property Division's administrative costs. These administrative costs totaled \$6,313,539 and \$5,693,036 for the fiscal years ended June 30, 2015 and 2016, respectively.

Unclaimed property includes unclaimed bank accounts, insurance policies, stock, customer overpayments held by businesses, and various court deposits. A comparison of unclaimed property receipts as presented in the State Treasurer's Annual Report for the fiscal years ended June 30, 2014, 2015, and 2016, is as follows:

	<u>Fiscal Year Ended June 30,</u>		
	<u>2014</u>	<u>2015</u>	<u>2016</u>
Corporations	\$ 31,395,616	\$ 39,346,724	\$ 38,368,606
Financial Institutions	19,418,814	22,198,137	26,666,525
Insurance Companies	24,900,486	36,551,915	21,810,296
Governmental and Public Agencies	2,856,444	3,893,901	5,683,123
Dividends on Securities Held	35,991	92,177	106,664
Reciprocal Exchange with Other States	3,185,516	3,636,006	1,088,868
Miscellaneous	131,343	114,091	3,738
Securities Tendered	27,367	8,624	86,007
Securities Liquidated	21,227,122	41,815,320	17,632,827
Totals	<u>\$ 103,178,699</u>	<u>\$ 147,656,895</u>	<u>\$ 111,446,654</u>

The Unclaimed Property Division's claim payments made in cash, transfers to the Citizens' Election Fund to support the State Elections Enforcement Commission, and administrative expenses as reported in the State Treasurer's Annual Report are as follows:

	<u>Fiscal Year Ended June 30,</u>		
	<u>2014</u>	<u>2015</u>	<u>2016</u>
Claim Payments	\$ 63,772,440	\$ 61,090,933	\$ 57,568,310
Transfers to Citizens Election Fund	11,081,918	11,281,219	11,349,203
Salaries and Fringe Benefits	3,542,003	3,539,983	3,786,288
Data Processing and Hardware	1,522,819	2,696,640	1,837,988
All Other	338,740	76,916	68,760
Totals	<u>\$ 80,257,920</u>	<u>\$ 78,685,691</u>	<u>\$ 74,610,549</u>

STATE AUDITORS' FINDINGS AND RECOMMENDATIONS

The following recommendations resulted from our current review of the Office of the State Treasurer's departmental operations:

Contract Management

Criteria: Good business practices dictate that contractors should not be authorized to begin work prior to the execution of a contract. Signed, formal, written agreements establishing rights and responsibilities safeguard all parties involved.

Condition: Our review of 10 contracts revealed that 7 were executed between 8 and 255 days after the service start date. In addition, contractors began providing services on 2 of those contracts prior to execution. Expenses incurred during that period were \$37,859.

Effect: Unforeseen liabilities may be incurred if work is started on a project before all of the key terms have been agreed to and the contract has been signed.

Cause: Employees responsible for processing contractual agreements failed to execute the contracts before the commencement date.

Recommendation: The Office of the State Treasurer should fully execute contracts prior to the starting date of the agreement and not authorize contractors to begin work before contracts are executed. (See Recommendation 1.)

Agency Response: "We concur with the Auditors' recommendation. While start dates listed on contracts do not necessarily represent when work actually begins, Treasury personnel have been instructed to not allow costs to be incurred prior to the execution of a contract.

Although this recommendation is identified as a repeated recommendation, we note that the contracts cited in this report were executed before the release of the previous audit report in December 2015, and before corrective actions could be implemented in response to that report."

Telecommuting Agreement

Criteria:

In accordance with Section 5-248i of the General Statutes, the Commissioner of Administrative Services shall develop and implement guidelines authorizing telecommuting and work-at-home programs for state employees. Department of Administrative Services General Letter 32 establishes compliance requirements for telecommuting and includes the following:

- The employee must not be in a job classification that requires leading or supervising staff.
- The telecommuting schedule must be defined for the employee.
- The agency shall not approve any telecommuting schedule that results in an employee out of the official work site more than 50% of the work week.
- Any changes to the schedule must be preapproved in writing by the agency.
- Timekeepers will record the number of hours each employee spends telecommuting by entering a specific code on the timesheet.

Condition:

The Office of the State Treasurer entered into 1 telecommuting agreement during the audited period. The Treasury hired a former employee who no longer lived in the state, to a temporary position to perform the administrative function of preparing the Treasurer's Annual Report for publication. Due to an unreasonable commute, the office established a telecommuting agreement. The employee was hired as a Fiscal Administrative Manager, which, according to the job description, requires supervising a minimum of 3 staff. Examples of duties include, directing staff, managing activities and other supervisory duties. The position was a full-time position; however, the employee only averaged 3.7 hours per day and worked 45 days during the 3-month assignment. This position, as defined in the job description, would not appear eligible for telecommuting.

The employee began work on October 20, 2016. The agency entered into a telecommuting agreement with the employee on November 14, 2016. Based on observation and discussions with the agency, it appears that the employee was telecommuting prior to having an official agreement in place. The telecommuting

agreement did not have a defined schedule, established work hours, or the days the employee would be telecommuting, as required by the policy. The actual hours worked by the employee varied from day to day with no consistent pattern. In addition, timesheet records did not indicate the hours the employee was telecommuting, as required. All time was reported as regular time. Therefore, it cannot be determined which days the employee was present at the work site.

Effect: The Treasury established a telecommuting agreement that was not in compliance with the Department of Administrative Services telecommuting policy.

Cause: The Treasury has a statutory requirement to produce an annual report by December 31 each year. Management decided that hiring this employee and entering into this telecommuting agreement was the best way to meet that requirement.

Recommendation: The Office of the State Treasurer should comply with the Department of Administrative Services guidelines for telecommuting when establishing telecommuting agreements. (See Recommendation 2.)

Agency Response: “We concur with the Auditors’ recommendation. This was an urgent, one-off situation necessitated by the unexpected extended medical leave of our business manager. Our retired business manager, who lived in New York State, was available to help with business office and annual report development and production needs, on the condition that she split her time between working on-site and at her home. While we discussed the situation with the Auditors’ staff and filed the required telecommuting paperwork, evidently we did not meet every administrative requirement. We, however, believe that we were able to address critical needs in the most cost-efficient and timely manner with costs of less than \$9,700.”

RECOMMENDATIONS

Status of Prior Audit Recommendations:

Our prior audit examination resulted in four recommendations, of which one is being repeated in our current audit report. The following is a summary of those recommendations and the action taken by the Office of the State Treasurer.

- **The Office of the State Treasurer should rebid its banking service contracts periodically and should not authorize contractors to begin work before contracts are executed.** The Cash Management Division rebid its banking service contracts; therefore, that portion of the recommendation is not being repeated. However, several contracts we reviewed that were executed during the audited period were not fully executed prior to the starting date of the agreement and services were rendered during that time. This portion of the recommendation will be repeated. (See Recommendation 1.)
- **The Office of the State Treasurer should accurately report property amounts and be sure its property control records conform to the requirements set forth by the State Comptroller.** The Office of the State Treasurer has taken appropriate steps to address this recommendation. This recommendation will not be repeated.
- **The Office of the State Treasurer should implement procedures to improve internal controls over reconciling Core-CT records with Pension Fund Management Division records.** This recommendation will not be repeated.
- **The Office of the State Treasurer should update regulations related to certain divisions within the Treasury in the Regulations of State Agencies.** The Office of the State Treasurer published revised regulations. Therefore, this recommendation will not be repeated.

Current Audit Recommendations:

The following recommendations resulted from our current review.

1. **The Office of the State Treasurer should fully execute contracts prior to the starting date of the agreement and not authorize contractors to begin work before contracts are executed.**

Comments:

Contractors began working before contracts were fully executed.

2. **The Office of the State Treasurer should comply with the Department of Administrative Services guidelines for telecommuting when establishing telecommuting agreements.**

Comments:

One telecommuting agreement established by the Office of the State Treasurer violated several telecommuting requirements.

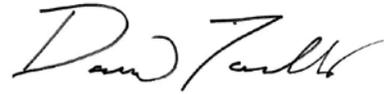
ACKNOWLEDGEMENT

The Auditors of Public Accounts would like to recognize the auditors who contributed to this report:

Taulant Baci
Edna L. Maldonado
David Tarallo

CONCLUSION

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



David Tarallo
Principal Auditor

Approved:



John C. Geragosian
State Auditor



Robert J. Kane
State Auditor