STATE OF CONNECTICUT

AUDITORS' REPORT
DEPARTMENT OF BANKING
FOR THE FISCAL YEARS ENDED JUNE 30, 2001 AND 2002

AUDITORS OF PUBLIC ACCOUNTS
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June 9, 2004

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We have made an examination of the financial records of the Department of Banking for the fiscal years ended June 30, 2001 and 2002. This report consists of the Comments, Condition of Records, Recommendations and Certification that follow.

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

COMMENTS

FOREWORD:

The Department of Banking operates under the provisions of Title 36a, Chapters 664 through 669 and Title 36b, Chapters 672 to 672c of the Connecticut General Statutes. The Department functions as a regulatory agency responsible for the supervision, licensing and regulation of financial institutions and organizations within the State. Included among such institutions are State chartered banks and credit unions, small loan and second mortgage companies, sales finance companies, collection agencies, security brokers, salesmen and investment counselors. Among the Department's other responsibilities are the administration and enforcement of Connecticut's Truth-in-Lending Law, other consumer credit laws and the Connecticut Uniform Securities Act.

John P. Burke served as Banking Commissioner during the audited period.

RÉSUMÉ OF OPERATIONS:

Banking Fund:

The Banking Fund (#1103) operates under Section 36a-65 of the Connecticut General Statutes. All assessments and other fees received from entities subject to the supervision of the Banking Commissioner are deposited in this special revenue fund. The expenditures of the Department of Banking are to be made pursuant to appropriation by the General Assembly and are charged to the Banking Fund.

Banking Fund receipts are summarized below, with amounts for the 1999-2000 fiscal year presented for comparative purposes.

	1999-2000	**2000-2001**	**2001-2002**
Receipt Type:			
Bank and credit union assessments	$1,053,751	$ 591,819	$ -
Registration of securities	4,731,349	4,717,035	4,233,304
Broker/dealer & investment advisor registration	8,273,460	9,122,150	8,371,850
Other application, license and examination fees	1,945,078	1,865,947	2,118,253
Penalties for failure to register	469,400	184,100	343,100
All other revenue	76,538	78,528	83,258
Total Banking Fund Receipts	**$16,549,576**	**$16,559,579**	**$15,149,765**

Subsection (a) of Section 36a-65 of the General Statutes gives the Commissioner discretion in the amount to assess banks and credit unions. These assessments are based on the funding needs of the Department and were imposed during the 1999-2000 and the 2000-2001 fiscal years, but were not imposed during the 2001-2002 fiscal year because the Commissioner determined that the Department had sufficient funds to meet its operational needs for that period.

Banking Fund expenditures are summarized below, with amounts for the 1999-2000 fiscal year presented for comparative purposes.

	1999-2000	**2000-2001**	**2001-2002**
Expenditure Type:			
Personal services and fringe benefits	$10,704,374	$11,005,023	$11,296,444
Contractual services	1,626,536	1,685,033	1,734,081
Commodities	78,656	60,646	39,920
Revenue refunds	58,497	70,878	64,044
Sundry charges, excluding fringe benefits	(69,549)	183,294	407,599
Equipment	108,988	171,279	1,278
Total Banking Fund Expenditures	**$12,507,502**	**$13,176,153**	**$13,543,366**

Personal services and fringe benefits increased at a moderate rate during the audited period. The fringe benefit cost recovery rate decreased from 41.28 percent in fiscal year 2000 to 39.26 percent in fiscal year 2001, and increased to 42.29 percent in fiscal year 2002. The State

Comptroller establishes the fringe benefit cost recovery rate annually. While filled positions decreased slightly from 130 at June 30, 2000 to 125 at June 30, 2002, there were cost of living increases, which account for the moderate increases in personnel costs.

Our analysis of contractual services expenditures indicated relatively modest increases in each of the fiscal years audited. However, there were some major changes in a few categories. Expenditures for “rents and storage” decreased significantly from the 1999-2000 fiscal year through the 2001-2002 fiscal year. This decrease resulted from the Department reducing its reliance on outside storage facilities to store records by utilizing State facilities. The “rents-nonreportable” category of expenditures increased as a result of the Department’s increase in rent for office space. Expenditures for “outside consulting services” increased approximately $70,000 and $78,000 for each of the audited fiscal years, respectively. These increases resulted from increased legal and accounting services, as well as assistance from the Attorney General’s Office. Expenditures for “EDP software license” increased by about $33,000 in the 2000-2001 fiscal year, but decreased by about $52,000 in the 2001-2002 fiscal year. The increase was due to the need to purchase licenses for additional software for the hardware purchases during the 2000-2001 fiscal year. There was a subsequent decrease, as there were no EDP hardware purchases in the 2001-2002 fiscal year.

Revenues were virtually unchanged from the 1999-2000 fiscal year to the 2000-2001 fiscal year and decreased by approximately 8.5 percent during the 2001-2002 fiscal year. However, accompanied by relatively moderate increases in expenditures, the fund balance of the Banking Fund (#1103) increased as presented below:

Year Ended	Fund Balance
June 30, 2000	$19,056,747
June 30, 2001	22,440,173
June 30, 2002	24,046,572

CONDITION OF RECORDS

Generally, the financial records of the Department of Banking were maintained in a satisfactory manner. However, we noted two areas where improvement is possible, as described in the following findings.

Missing Inventory:

Criteria: Pursuant to Section 4-33a of the Connecticut General Statutes the Office of the Comptroller and the Auditors of Public Accounts shall be promptly notified of any illegal, irregular or unsafe handling or breakdowns in safekeeping of any resources of the State. The Office of the State Comptroller's Property Control Manual establishes that "equipment that is deemed lost, missing or unaccountable… must be accounted for."

Condition: The Department could not locate four out of 20 inventory items randomly selected from the Department's inventory records to be traced to their physical locations. Additionally, one other item could not initially be located, but was later determined to have been entered onto the inventory records under two different inventory tag numbers.

Effect: The Department has property listed on its inventory record that is physically unaccounted for in the amount of $922. The Department also has a $3,755 item on its inventory record with a property tag number different from the actual tag number on the item.

Cause: Unknown.

Recommendation: The Department should adhere to the Office of the State Comptroller's Property Control Manual and make every effort to locate missing property. If unsuccessful, it should consider notifying the proper law enforcement authorities and file Lost/Stolen Property reports with the Office of the State Comptroller and the Auditors of Public Accounts to promptly inform them pursuant to Section 4-33a of the Connecticut General Statutes. (See Recommendation 1.)

Agency Response: "Diligent efforts have been made to locate all missing items specific in the inventory sample. Items not located have been identified and lost/stolen property reports have been prepared and filed with the Office of the Comptroller, the State Police, and the Auditors of Public Accounts. Procedural guidelines are now in place to assure that this practice becomes a standard agency operating measure."

Timely Submittal of Employee Vouchers After Travel:

Criteria: The State Accounting Manual states that the custodian of the Petty Cash Fund must obtain a statement, signed by the recipient of a petty cash advance, acknowledging that within five working days after return from travel the employee will submit a completed Form CO-17XP, Employee Voucher, with the required documentation, to the agency Business Office.

The Business Office date stamps Employee Vouchers upon receipt as a means of identifying the receipt dates of the documents.

Condition: Of the ten out-of-state travel transactions tested, seven did not have the Department's Business Office date stamp upon them. Three, out of the seven transactions that did not have date stamps, involved travel advances from the Petty Cash Fund.

Effect: The date that seven of the Employee Vouchers were submitted to the Business Office could not be determined. Three of the seven involved petty cash advances, and it could not be determined if they were submitted in a timely manner. Therefore, the Petty Cash Fund may have to carry a larger balance than would be necessary if replenishments were submitted in a timely manner.

Cause: The internal control procedure established by the Department's Business Office to date stamp Employee Vouchers upon receipt in the Business Office is not being complied with.

Recommendation: The Department should adhere to its procedures of date stamping all Employee Vouchers upon receipt to ensure that it is conforming to the timely submission of these vouchers as required by the State Accounting Manual. (See Recommendation 2.)

Agency Response: "All Employee Vouchers will be date stamped by the appropriate department head prior to being submitted to the business office. We will take steps to notify department heads and their liaisons as to the procedure that should now be followed. We believe this step will create a stronger internal control that will help assure that expenses related to petty cash advances are reported within the time constraints specified in the State Accounting Manual."

Other Matters:

In a letter dated March 15, 2004, we wrote to the Governor and other State Officials on a reportable condition that did not result in a finding.

Our review found that the Department of Public Works exercised a lease expansion option on May 24, 2002, for the Department of Banking to move into the G. Fox building. This option was exercised with all of the required approvals; however, the option was exercised before any funds had been appropriated to cover the approximately $3,100,000 in up-front tenant improvements that were required. The State was not able to pay for these improvements without the proper funding in place and so the project was put on hold and the Department of Banking did not move into the building. It was determined by the Office of the Attorney General that even though the Department did not move into the building it was still obligated, under the lease expansion option to make payments to the landlord effective September 22, 2002, at the rate of $65,000 per month in base rent and $13,950 per month for 93 parking spaces, for a monthly total of $78,950. The Department of Public Works has made payments totaling $1,286,885, which represents the rent for office space and 93 parking spaces, for the period from September 22, 2002 through January 31, 2004. Pursuant to Public Act 03-6 (June 30, 2003 Special Session) the Department of Banking is required to reimburse the Department of Public Works for these amounts.

The above constitutes a breakdown in the safekeeping of the State's resources that resulted in the unnecessary expenditure of State funds totaling $1,286,885.

RECOMMENDATIONS

Status of Prior Audit Recommendations:

- We recommended that the Department should comply with Section 36a-14 of the General Statutes and submit the required annual reports to the Governor and the Banking Committee of the General Assembly. The Department has demonstrated compliance with the statute for the audited period.

Current Audit Recommendations:

1. **The Department should adhere to the Office of the State Comptroller's Property Control Manual and make every effort to locate missing property. If unsuccessful, it should notify the proper law enforcement authorities and file Lost/Stolen Property reports with the Office of the Comptroller and the Auditors of Public Accounts to promptly inform them pursuant to Section 4-33a of the Connecticut General Statutes.**

   Comment:

   The Department could not locate four out of 20 inventory items randomly selected from the Department's inventory records to be traced to their physical locations. Additionally, one other item could not initially be located and was later determined to have been entered onto the inventory records under two different inventory tag numbers.

2. **The Department should adhere to its procedures of date stamping all Employee Vouchers upon receipt to ensure that it is conforming to the timely submission of these vouchers, as required by the State Accounting Manual.**

   Comment:

   Of the ten out-of-state travel transactions tested, seven did not have the Department's Business Office date stamp upon the applicable Employee Vouchers. Three, out of the seven Employee Vouchers that did not have date stamps, involved travel advances from the Petty Cash Fund.

INDEPENDENT AUDITORS' CERTIFICATION

As required by Section 2-90 of the General Statutes we have audited the books and accounts of the Department of Banking for the fiscal years ended June 30, 2001 and 2002. This audit was primarily limited to performing tests of the Agency's compliance with certain provisions of laws, regulations and contracts, and to understanding and evaluating the effectiveness of the Agency's internal control policies and procedures for ensuring that (1) the provisions of certain laws, regulations and contracts applicable to the Agency are complied with, (2) the financial transactions of the Agency are properly recorded, processed, summarized and reported on consistent with management's authorization, and (3) the assets of the Agency are safeguarded against loss or unauthorized use. The financial statement audits of the Department of Banking for the fiscal years ended June 30, 2001 and 2002, are included as part of our Statewide Single Audits of the State of Connecticut for those fiscal years.

We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial-related audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Department of Banking complied in all material or significant respects with the provisions of certain laws, regulations and contracts and to obtain a sufficient understanding of the internal control to plan the audit and determine the nature, timing and extent of tests to be performed during the conduct of the audit.

Compliance:

Compliance with the requirements of laws, regulations and contracts applicable to the Department of Banking is the responsibility of the Agency's management.

As part of obtaining reasonable assurance about whether the Agency complied with laws, regulations and contracts, noncompliance with which could result in significant unauthorized, illegal, irregular or unsafe transactions or could have a direct and material effect on the results of the Agency's financial operations for the fiscal years ended June 30, 2001 and 2002, we performed tests of its compliance with certain provisions of laws, regulations and contracts. However, providing an opinion on compliance with these provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*. However, we noted certain immaterial or less than significant instances of noncompliance, which are described in the accompanying "Condition of Records" and "Recommendations" sections of this report.

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

The management of the Department of Banking is responsible for establishing and maintaining effective internal control over its financial operations, safeguarding of assets, and compliance with the requirements of laws, regulations and contracts applicable to the Agency. In planning and performing our audit, we considered the Agency's internal control over its financial operations, safeguarding of assets, and compliance with requirements that could have a material or significant effect on the Agency's financial operations in order to determine our auditing procedures for the purpose of evaluating the Department'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.

Our consideration of the internal control over the Agency's financial operations and over compliance would not necessarily disclose all matters in the internal control that might be material or significant weaknesses. 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 failure 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. We noted no matters involving internal control that we consider to be material or significant weaknesses.

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 courtesies and cooperation extended to our representatives by the personnel of the Department of Banking during the course of our examination.

Mark Dickerson
Associate Auditor

Approved:

Robert G. Jaekle	Kevin P. Johnston
Auditor of Public Accounts	Auditor of Public Accounts