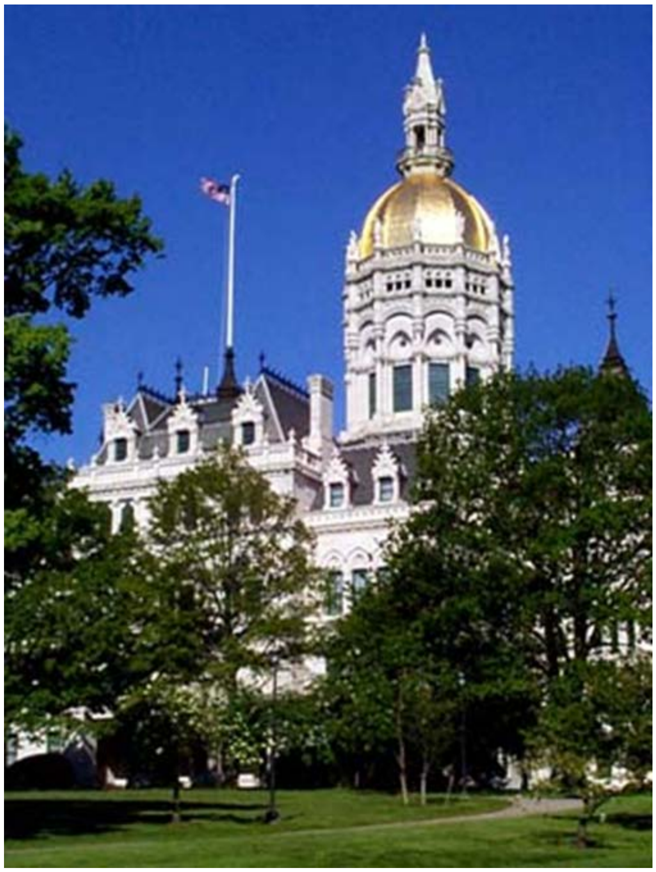
STATE OF CONNECTICUT



AUDITORS' REPORT
DEPARTMENT OF BANKING
FISCAL YEARS ENDED JUNE 30, 2018 AND 2019

AUDITORS OF PUBLIC ACCOUNTS
JOHN C. GERAGOSIAN ❖ CLARK J. CHAPIN

Table of Contents

July 14, 2021

EXECUTIVE SUMMARY

In accordance with the provisions of Section 2-90 of the Connecticut General Statutes, we have audited certain operations of the Department of Banking for the fiscal years ended June 30, 2018 and 2019. Our audit identified internal control deficiencies; instances of noncompliance with laws, regulations, and policies; and a need for improvement in practices and procedures that warrant the attention of management. The significant findings and recommendations are presented below:

Page 6	Our review disclosed that the receivables the department reported on its GAAP Form 2 and aging report did not agree. The Department of Banking should strengthen internal controls over the accounting and reporting of its accounts receivable balances. (Recommendation 1.)
Page 7	Our review of the department's Asset Management Report (CO-59) disclosed that the department understated the CO-59 balances by $130,036 and $79,368 for the 2017-2018 and 2018-2019 fiscal years, respectively. DOB submitted its 2019 CO-59 report 45 days late and did not record certain items in its inventory records. The Department of Banking should strengthen internal controls to ensure that amounts on its annual inventory report are accurate, complete, and reported in accordance with the State Property Control Manual. (See Recommendation 2.)
Page 8	Our review of the department's purchasing cards for the audit period disclosed several instances in which the department did not reconcile and/or approve purchasing card documentation. The Department of Banking should strengthen controls over purchasing card transactions by ensuring compliance with established purchasing card procedures. (See Recommendation 3.)
Page 9	Our review of 10 medical leaves of absence disclosed three instances in which the department did not have the required medical certificate on file. The Department of Banking should improve monitoring of medical leave to ensure employees provide medical certificates for any absence of more than five consecutive workdays as prescribed by the commissioner of Administrative Services. (See Recommendation 4.)
Page 10	Our review of 10 terminated employees disclosed that the department did not deactivate eight accounts until 299 to 683 days after termination. The Department of Banking should establish internal controls to ensure that it promptly deactivates employee access to the Core-CT system upon termination. (See Recommendation 5.)
Page 11	Our review of the Department of Banking's software inventory disclosed the inventory records did not contain the required information prescribed by the State Comptroller. The Department of Banking should comply with the Office of the Comptroller's software inventory policies and procedures. (See Recommendation 6.)

STATE OF CONNECTICUT

AUDITORS OF PUBLIC ACCOUNTS

JOHN C. GERAGOSIAN
State Capitol
210 Capitol Avenue
Hartford, Connecticut 06106-1559
CLARK J. CHAPIN

July 14, 2021

AUDITORS' REPORT
DEPARTMENT OF BANKING
FISCAL YEARS ENDED JUNE 30, 2018 and 2019

We have audited certain operations of the Department of Banking in fulfillment of our duties under Section 2-90 of the Connecticut General Statutes. The scope of our audit included, but was not necessarily limited to, the fiscal years ended June 30, 2018 and 2019. The objectives of our audit were to:

1. Evaluate the department's internal controls over significant management and financial functions;

2. Evaluate the department's compliance with policies and procedures internal to the department or promulgated by other state agencies, as well as certain legal provisions; and

3. Evaluate the effectiveness, 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, as well as certain external parties[1]; and testing selected transactions. Our testing was not designed to project to a population unless specifically stated. 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 this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the 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 a reasonable basis for our findings and conclusions based on our audit objectives.

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

1. Deficiencies in internal controls;

2. Apparent non-compliance with laws, regulations, contracts and grant agreements, policies, and procedures; and

3. A need for improvement in management practices and procedures that we deemed to be reportable.

The State Auditors' Findings and Recommendations section of this report presents findings arising from our audit of the Department of Banking.

COMMENTS

FOREWORD

The Department of Banking (DOB) primarily operates under the provisions of Title 36a, Chapters 664 through 669, Title 36b, Chapters 672 through 672c, and Section 47a-21 subsection (b), (d), (h), (i), and (j) of the Connecticut General Statutes. DOB functions as a regulatory agency responsible for the supervision, licensing, and regulation of financial institutions and organizations within the state. Among such institutions are state-chartered banks and state-chartered credit unions, suppliers of consumer credit such as mortgage lenders, brokers, consumer collection agencies, small loan companies, and check cashers. Also, DOB has jurisdiction over landlord/tenant security deposit conflicts. The department receives the majority of its revenues through the registration, supervision, and examination of the securities business within the state, including brokerage firms, investment banking houses, retail stockbrokers, and investment advisors. The department administers and enforces Connecticut's Truth-in-Lending Law and Uniform Securities Act, among other consumer-credit laws.

DOB transferred its human resource and affirmative action functions to the Department of Administrative Services (DAS) Small Agency Resource Team (SmART) in October 2018. In March 2019, DOB also transferred its payroll functions.

Jorge L. Perez was appointed Banking Commissioner effective March 13, 2015 and served in that capacity during the audited period.

Significant Legislation

Public Act 18-90, effective October 1, 2018, required the banking commissioner to adopt regulations requiring credit rating agencies to provide the commissioner with a dedicated point of contact so that the department may assist consumers following a data breach.

Public Act 18-173, effective October 1, 2018, made numerous changes to the banking statutes that generally expand the banking commissioner's authority and standardize various requirements across several license types. Principally, the bill: 1) extended many existing authorities over certain mortgage-related licensees to small loan lenders, mortgage servicers, student loan servicers, lead generators, and six other nonmortgage licenses; and 2) codified two of the banking commissioner's orders requiring various nonmortgage licensees to use the Nationwide Mortgage Licensing System and Registry for license applications, renewals, and other license related activities. The law already required this for mortgage-related licenses. The bill also established new requirements and modified existing requirements across mortgage and nonmortgage licenses types.

Public Act 18-117, effective October 1, 2018, expanded the authority of credit unions to engage in activities available to federal or out-of-state credit unions under state or federal law, without the commissioner's preapproval that prior law required. The act permits credit unions to engage in these activities if they give the commissioner prior written notice. The commissioner has 30 days after a credit union files its notice to disapprove of the activity if deemed inappropriate.

RÉSUMÉ OF OPERATIONS

Receipts and Expenditures

A comparison of revenues and expenditures for the fiscal years under review and the preceding year follows:

Receipts	Fiscal Year Ended June 30,		
	2017	2018	2019
General Fund	$126,091,841	$ 6,383,323	$ 6,427,848
Banking Fund	30,544,632	36,435,100	35,923,775
Restricted Fund	286,000	50,100	47,200
Total Receipts	**$156,913,455**	**$42,868,524**	**$42,398,823**

Department of Banking receipts by revenue category are summarized below for the fiscal years ended June 30, 2017, 2018, and 2019:

Receipts	Fiscal Year Ended June 30,		
	2017	2018	2019
Fees	$ 30,803,184	$35,152,034	$36,260,914
Fines	120,597,541	1,002,845	1,023,582
Licenses	5,135,427	5,282,675	4,894,350
Miscellaneous	377,303	1,430,970	219,977
Total Receipts	**$156,913,455**	**$42,868,524**	**$42,398,823**

Total receipts were primarily derived from the Banking Fund and the General Fund. Total receipts decreased in the 2017-2018 fiscal year by $144,044,931 and decreased by $469,700 in the 2018-2019 fiscal year. The decrease in revenues in the 2017-2018 fiscal year was due to a $120,000,000 settlement the department received from a financial institution during the 2016-2017 fiscal year. Total fees increased $4,348,850 in the 2017-2018 fiscal year and $1,108,880 in the 2018-2019 fiscal year. Public Act 17-2 of the June Special Session increased various broker-dealer and investment advisor fees. Generally, total fees vary from year to year. Total miscellaneous receipts increased in the 2017-2018 fiscal by $1,053,667 and decreased in the 2018-2019 fiscal year by $1,210,993 due to refunds of prior years' expenditures.

The department's total expenditures by fund and expenditure category for the fiscal years under review and the preceding year are as follows:

Expenditures	**Fiscal Year Ended June 30,**		
	2017	**2018**	**2019**
Banking Fund	$20,119,239	$20,337,241	$22,409,988
Restricted Fund	8,420	12,978	111,153
Total Expenditures by Fund	**$27,127,659**	**$20,350,219**	**$22,521,141**

Expenditures	**Fiscal Year Ended June 30,**		
	2017	**2018**	**2019**
Personal Services and Employee Benefits	$18,567,643	$17,824,110	$19,587,68
Employee Allowances & Travel	136,577	109,177	123,030
Contractual Services	212,003	333,999	309,446
Motor Vehicle Costs	172,304	174,827	152,806
Premises and Property	778,618	811,616	791,979
Information Technology	49,886	424,394	981,676
Communications	53,267	137,759	53,634
Purchase Commodities	70,499	68,505	79,270
Other Charges	86,862	291,192	441,615
Capital Outlays	-0-	174,640	-0-
Total Expenditures	**$20,127,659**	**$20,350,219**	**$22,521,141**

The department's expenditures increased by $222,560 during the fiscal year ended June 30, 2018 and $2,170,922 during the fiscal year ended June 30, 2019. The majority of the budgeted expenditures are personal services and employee benefits, premises and property expenses, and information technology and communications expenditures. The Personal Services and Employee Benefits expenditures decreased by $743,533 for fiscal year 2017-2018 and increased by $1,763,575 for fiscal year 2018-2019. This was due to changes in contributions to the State Employee Retirement System, salary increases and changes in medical insurance contributions. The Information Technology expenditures increased by $374,508 for fiscal year 2017-2018 and $557,282 for fiscal year 2018-2019, primarily due to the agency upgrading to a new e-License software system. Communications expenditures increased by $84,492 for fiscal year 2017-2018 and decreased by $84,125 for fiscal year 2018-2019 due to the installation of a new telephone system in the 2017-2018 fiscal year.

Fund Balance

The Banking Fund budgetary fund balances plus reserves for the fiscal years ended June 30, 2018 and 2019 were $3,326,196, and $3,048,035, respectively.

STATE AUDITORS' FINDINGS AND RECOMMENDATIONS

Our examination of the records of the Department of Banking disclosed the following six recommendations, of which one has been repeated from the previous audit.

Accounts Receivable – GAAP Form #2 Reporting

Criteria:	The State Accounting Manual, Management of Receivables Section 2.0, requires that accounts receivable records be maintained in an accurate and complete manner. The records must indicate how long the debt has been outstanding. Section 4.3 requires each agency to report its fiscal year-end receivables transactions and balances (GAAP Form 2) to the Office of the State Comptroller, Budget & Financial Analysis Division.
Condition:	Our review disclosed that the receivables the department reported on its GAAP Form 2 and aging report did not agree. In addition, the department overstated receivables by $1,403,800 on its aging report and $921,365 on its GAAP Form 2 as of June 30, 2019. We also noted receivables listed on the aging report were not listed on the GAAP forms and vice versa. We were unable to determine the accuracy of either report.
Context:	The Department of Banking reported accounts receivable balances of $5,975,818 and $4,264,161 as of June 30, 2018 and 2019, respectively.
Effect:	The department did not accurately report its account receivables to the Office of the Comptroller.
Cause:	The Department of Banking does not have procedures in place to adequately identify and record account receivables.
Prior Audit Finding	This finding has been previously reported in the last 2 audit reports covering the fiscal years ended 2014 to 2017.
Recommendation:	The Department of Banking should strengthen internal controls over the accounting and reporting of its accounts receivable balances. (See Recommendation 1.)
Agency Response:	"The department agrees with this audit finding. Although the former FAM1/Business Office Manager assured the Commissioner of the Department of Banking that a thorough review of the procedures for accounting and reporting of accounts receivable balances had been conducted and all procedural errors were corrected, there were still findings for this audit period. In May 2019 DOB hired a new FAM1/Business Office

Manager who conducted a review of the process being used to account for and report on its accounts receivable balances. Additional training has been provided to the appropriate staff and changes have been implemented to ensure the proper completion of the GAAP Form #2 going forward."

Asset Management - CO-59 GAAP Reporting Form

Criteria: Section 4-36 of the General Statutes requires that state agencies establish and maintain an inventory system as prescribed by the Office of the State Comptroller. Agencies are required to transmit an annual Asset Management Report (CO-59) to the Office of the State Comptroller, which provides a detailed inventory of all real or personal property owned by the state in the custody of an agency. The Property Control Manual requires each agency head, at their discretion, to maintain a list of "controllable" assets with a value of less than five thousand dollars. Assets having a value of five thousand dollars or more should be capitalized and recorded in the agency's property control records.

The Property Control Manual requires agencies to safeguard assets and account for them appropriately. Assets costing five thousand dollars or more should be capitalized and recorded in the agency's property control records. Assets costing less than $5,000 should be reviewed and reported correctly in the agency's controllable listing.

Condition: Our review of the Department of Banking's property control system revealed the following:

- DOB understated its 2018 and 2019 CO-59 reports by $130,036 and $79,368, respectively.
- DOB submitted its 2019 CO-59 report 45 days late.
- DOB purchased a $12,978 audio-visual system and a $5,710 workstation in the fiscal year ended 2018. The department did not record these items in its inventory records.

Context: The CO-59 ending balance was $335,716 for the 2017-2018 fiscal year and $208,348 for the 2018-2019 fiscal year

Effect: The department's inventory and amounts reported on the annual inventory reports (Form CO-59) were incomplete and inaccurate.

Cause: The department has not made a sufficient effort to maintain accurate inventory records in accordance with the State of Connecticut Property Control Manual.

Prior Audit Finding This finding has not been previously reported.

Recommendation: The Department of Banking should strengthen internal controls to ensure that amounts on its annual inventory report are accurate, complete, and reported in accordance with the State Property Control Manual. (See Recommendation 2.)

Agency Response: "The department agrees with this finding. The CO-59 GAAP Reporting form and the manner in which it was previously being completed has been reviewed. The Office of the State Comptroller has been consulted as well, to confirm any questions the Business Office had on elements of the reporting. With the guidance from OSC, the Business Office has revised its process in this area to be in complete compliance with OSC. The new Business Office Manager will once again review with staff the process on the proper coding and inventorying of Capital purchases to ensure full compliance with the State Property Control Manual. This review will ensure that all capitalized purchases will be added to the department's inventory in the future. All of these changes have strengthened DOB internal controls in the reporting of annual inventory and CO-59 GAAP reporting and will ensure that the report is submitted on time going forward."

Expenditures – Purchasing Cards

Criteria: The State Comptroller, in conjunction with the Department of Administrative Services, issued the State of Connecticut's Agency Purchasing Card Coordinator Manual, which sets forth the state guidelines and procedures on the use of purchasing cards (P-cards) by state agencies. In addition, the Department of Banking's policy requires P-card holders to review and reconcile their statements to the purchasing card logs within 3 to 4 business days of receipt. The reconciled statements are then reviewed and approved by division directors or supervisors.

Condition: Our review of the department's purchasing cards included the examination of transactions processed on 10 individual cardholder statements during the audited period. Our review noted the following:

- Three instances in which the purchasing card statement was not approved by the supervisor.
- One instance in which the purchasing card log was not approved by the supervisor.
- Two instances in which the purchasing card statements were not reconciled by the agency.
- One instance in which the purchasing card log was verified by the individual making the purchase.

Context: During the audited period, 24 purchasing card billing months totaled $267,102. We reviewed five billing months totaling $82,142.

Effect: The department did not comply with purchasing card policies and procedures. Without proper approvals, the risk of unauthorized use increases.

Cause: The individual cardholders did not follow established procedures.

Prior Audit Finding This finding has not been previously reported.

Recommendation: The Department of Banking should strengthen controls over purchasing card transactions by ensuring compliance with established purchasing card procedures. (See Recommendation 3.)

Agency Response: "The department agrees with this audit finding. The Department of Banking has conducted a thorough review of its procedures for purchasing card transactions and the State of Connecticut Purchasing Card Program Agency Purchasing Card Coordinator Manual. Steps have been taken to ensure that all P-card statements and logs will be completed properly and signed by all appropriate parties. Steps have also been taken to ensure that established procedures are complied with consistently. All of these changes have strengthened DOB's internal controls over purchasing card transactions."

Absence of Medical Certificates on File

Criteria: Section 5-247-11 of the Regulations of Connecticut State Agencies provides that an acceptable medical certificate, which must be on the form prescribed by the commissioner of Administrative Services and signed by a licensed physician or other practitioner whose method of healing is recognized by the state, will be required of an employee by his appointing authority to substantiate a request for sick leave for any period of absence consisting of more than five consecutive working days.

The Department of Administrative Services recommends that state employees absent for health reasons use the Employee Medical Certificate (P-33A).

The Department of Banking's policy states employees should report an absence due to illness or injury to their supervisors as soon as possible. Employees should submit a required medical certificate for an absence of more than 5 consecutive workdays to the Human Resources Unit. Various collective bargaining agreements specify the same policy.

Condition: We reviewed 10 medical leaves of absence and found that in three instances, the department did not have the required P-33A Employee Medical Certificate form on file.

Context: During the audit period, 18 employees were on medical leave for more than 5 consecutive days with a total of 249 days. We reviewed 10 employees on medical leave with a total of 178 days.

Effect: The department increases the risk that employees may abuse their use of sick leave when the department does not obtain required medical certificates.

Cause: The department did not adequately monitor employees for compliance with medical certificate requirements.

Prior Audit Finding: This finding has not been previously reported.

Recommendation: The Department of Banking should improve monitoring of medical leave to ensure employees provide medical certificates for any absence of more than five consecutive workdays as prescribed by the commissioner of Administrative Services. (See Recommendation 4.)

Agency Response: "The department agrees with this audit finding. During the period of this audit, the Department of Banking went through a transition from the internal handling of Human Resource and Payroll functions to joining the DAS SMART Unit for management of all Human Resources and Payroll related duties. Effective 8/28/20 a centralized HR Benefits and Leaves Unit took over the handling of medical leaves and will ensure full compliance with all regulations and record keeping procedures as prescribed by the Commissioner of Administrative Services."

Core-CT Security - Access to Core-CT for Terminated Employees

Criteria: The Core-CT Security Liaison Guide states that upon the notice of an employee's termination, retirement, or transfer to another department or agency, the agency's security liaison should request immediate deactivation of a functional employee's access to Core-CT. The agency should deactivate non-functional employees' access to Core-CT when their final check has been issued.

Condition: At the time of our review, the department had not deactivated five of the ten terminated employees' Core-CT accounts we examined. They remained active 299 to 683 days after termination.

Effect: There is an increased risk of unauthorized access to the Core-CT system and possible manipulation of data.

Cause: The department does not have appropriate controls in place to ensure that it deactivates employees' Core-CT access immediately upon termination.

The department does not manually lock out accounts when employees receive their last paycheck but waits for the automated Core-CT process.

Prior Audit Finding This finding has not been previously reported.

Recommendation: The Department of Banking should establish internal controls to ensure that it promptly deactivates employee access to the Core-CT system upon termination. (See Recommendation 5.)

Agency Response: "The department agrees with this audit finding. During the period of this audit, DOB went through a transition from the internal handling of Human Resource and Payroll functions to joining the DAS SMART Unit for management of all Human Resources and Payroll related duties. DOB now has a process in place where once a DOB Supervisor/Manager is notified of an employee retirement or resignation they must notify our HR Representative in the DAS SMART Unit. The HR Representative will confirm the date when the DOB employee should have their CORE-CT assess rights "locked-out" and notifies the DOB CORE-CT Liaison to do so. The CORE-CT Liaison also now keeps an Excel document listing the date that the CORE-CT access lock-out was requested by HR and completed."

Information and Technology – Software Inventory

Criteria: Chapter 7 of the State of Connecticut Property Control Manual requires state agencies to establish a software inventory to track and control all software media and licenses. Agencies must annually produce a software inventory report and have an inventory record for all licensed, owned, and agency-developed software. The manual requires state agencies to perform physical inventories of their software libraries at the end of each fiscal year and compare them to the annual software inventory report. Agencies should retain the comparison of the physical inventory for audit purposes.

The Copyright Act, United States Code - Title 17, protects software. The Office of the State Comptroller requires all agencies to comply with all provisions of the law. The agency may use the inventory/library source documentation to verify it complies with the Copyright Act, United States Code - Title 17. The state is responsible for ensuring compliance with software manufacturers' licensing requirements.

Condition: The department maintained a software inventory for the fiscal years ended June 30, 2018 and 2019. However, the department's software inventory did not comply with the requirements prescribed by the State Comptroller.

Effect: The lack of proper accountability increases the risk that software may be lost, stolen, or improperly used. The state may also be at a higher risk of litigation from software companies for violating licensing and copyright agreements.

Cause: There appears to be a lack of management oversight.

Prior Audit Finding: This finding has not been previously reported.

Recommendation: The Department of Banking should comply with the Office of the State Comptroller's software policies and procedures. (See Recommendation 6.)

Agency Response: "The department agrees with this audit finding. The Department of Banking has revised its software inventory listing to be in direct compliance with the method outlined in Chapter 7 of the State of Connecticut Property Control Manual. As software is purchased all pertinent information will be gathered concerning that software and added to the listing."

RECOMMENDATIONS

Status of Prior Audit Recommendations:

Our prior audit report on the Department of Banking contained one recommendation, which has been repeated during the current audit.

- The Department of Banking should improve internal control over receivables and identify, record, and report receivables as required by the State Comptroller. **Our current audit disclosed this condition has not been resolved and will be repeated. (See Recommendation 1.)**

Current Audit Recommendations:

1. **The Department of Banking should strengthen internal controls over the accounting and reporting of its accounts receivable balances.**

   Comment:

   Our review disclosed that the receivables the department reported on its GAAP Form 2 and aging report did not agree.

2. **The Department of Banking should strengthen internal controls to ensure that amounts on its annual inventory report are accurate, complete, and reported in accordance with the State Property Control Manual.**

   Comments:

   Our review of the department's Asset Management Report (CO-59) for the audit period disclosed that the department understated the CO-59 balances by $130,036 and $79,368 for the 2017-2018 and 2018-2019 fiscal years, respectively. DOB submitted its 2019 CO-59 report 45 days late and did not record certain items in its inventory records.

3. **The Department of Banking should strengthen controls over purchasing card transactions by ensuring compliance with established purchasing card procedures.**

   Comments:

   Our review of purchasing cards disclosed several instances in which the department did not reconcile and/or approve purchasing card documentation.

4. **The Department of Banking should improve monitoring of medical leave to ensure employees provide medical certificates for any absence of more than five consecutive workdays as prescribed by the commissioner of Administrative Services.**

   Comments:

   Our review of 10 medical leaves of absence disclosed three instances in which the department did not have the required medical certificate on file.

5. **The Department of Banking should establish internal controls to ensure that it promptly deactivates employee access to the Core-CT system upon termination.**

   Comments:

   Our review of 10 terminated employees disclosed that the department did not deactivate eight accounts until 299 to 683 days after termination.

6. **The Department of Banking should comply with the Office of the State Comptroller's software policies and procedures.**

   Comments:

   The department's software inventory did not comply with the requirements prescribed by the State Comptroller.

ACKNOWLEDGMENTS

The Auditors of Public Accounts 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.

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

Sophia Chen
Jennifer Courbin
Kathrien E. Williams
Benjamin Viccari

Kathrien E. Williams
Kathrien E. Williams
Principal Auditor

Approved:

John C. Geragosian
State Auditor

Clark J. Chapin
Clark J. Chapin
State Auditor