STATE OF CONNECTICUT

AUDITORS' REPORT
STATE INSURANCE AND RISK MANAGEMENT BOARD
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2004

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

TABLE OF CONTENTS

November 30, 2005

AUDITORS' REPORT
STATE INSURANCE AND RISK MANAGEMENT BOARD
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 AND 2004

We have examined the financial records of the State Insurance and Risk Management Board (the Board) for the fiscal years ended June 30, 2003 and 2004. This report on that examination consists of the Comments, Recommendations, and Certification that follow.

Financial statements pertaining to the operations and activities of the Board for the fiscal years ended June 30, 2003 and 2004 are presented and audited on a Statewide Single Audit basis to include all State agencies and funds. This audit has been limited to assessing the Board's compliance with certain provisions of financial related laws, regulations and contracts, and evaluating the Board's internal control structure policies and procedures established to ensure such compliance.

COMMENTS

FOREWORD:

The Board operates under the provisions of Section 4-20 and Sections 4a-19 through 4a-21 of the General Statutes that place it under the Office of the State Comptroller for administrative purposes only.

The Board's primary responsibility is to decide the method by which the State is to insure itself against losses through the purchase of insurance. The Board’s principal duties include establishment of specifications for the purchase of such insurance, determination of deductible limits to be included in State insurance programs, determination of the feasibility, wherever appropriate, of the State's acting as a self-insurer, designation of the agent of record and negotiation of the agent's compensation, selection of companies from which insurance coverage is to be obtained, and the solicitation of bids for each such contract for insurance coverage through the agent of record. The Board may also develop and implement risk management and loss prevention programs.

The Board has adopted procedures for requesting bids on insurance contracts. For insurance policies with premiums anticipated to be equal to or greater than $50,000, the agent of record must seek formal written bids from the available insurance carriers. For insurance policies with premiums anticipated to be less than $50,000, the agent of record must contact at least three insurance carriers and seek oral bids based on policy specifications. Bid and award sheets prepared by the agent are forwarded to the Board for its review. Insurance policies requiring written bids are awarded after a formal vote by the Board. Insurance policies requiring oral bids are awarded by the agent to the low bidder unless other considerations are present. These latter awards are reviewed by the Board after payment.

All receipts concerning the State's insurance program, such as loss claims and returned premiums, are handled by the State Comptroller's Office as provided in Sections 4-20 and 4a-20 of the General Statutes.

Members of the Board:

In accordance with Section 4a-19 of the General Statutes, the Board’s 11 members are appointed by and serve terms concurrently with that of the Governor or until a successor is appointed. Four of the appointees must be public members and seven must be qualified in the area of insurance by training and experience. The State Comptroller, who may appoint a designee, serves as an ex-officio voting member of the Board. Except for reimbursements for necessary expenses, members of the Board serve without compensation for the performance of their duties. The members of the Board as of June 30, 2004, were as follows:

David M. Landsberg, Chairman	John H. Howard
Joseph G. Lynch, Vice Chairman	Pamela J. Kedderis
David W. Clark, Jr	Marjorie F. B. Lemmon
Cynthia L. DiSano	Robert J. McLucas
Robert B. Gyle, III	M. Alice Sherman
Robert L. Hill	Nancy Wyman, State Comptroller, ex-officio

RÉSUMÉ OF OPERATIONS:

Department Operations:

The Board’s General Fund receipts totaled $552,928 and $763,734 for the fiscal years ended June 30, 2003 and 2004, respectively, compared to $481,881 for the fiscal year ended June 30, 2002. These receipts consisted primarily of checks from colleges and universities (that are not on the State Comptroller’s accounting system) for the cost of insurance policy premiums. In addition, reimbursements of current year insurance payments were recovered from other State agencies by expenditure transfers. These transfers amounted to $2,123,633 and $2,539,751 for the fiscal years ended June 30, 2003 and 2004, respectively, compared to $1,572,172 for the fiscal year ended June 30, 2002. These reimbursements were mainly for Department of Administrative Services, Fleet Operations and Department of Transportation related insurance coverage. The increase in transfers is caused mainly by an increase in premiums.

The Board's General Fund budget provides for personnel costs and various general State insurance policies. Additionally, a Special Transportation Fund appropriation is used, primarily for highway liability insurance costs. Certain insurance costs are paid by the Board and reimbursed by the State agencies that benefit from the coverage. Such reimbursements are made by charging non-General Fund accounts of those State Agencies. A comparative summary of expenditures for the Board follows:

	June 30,	
	2003	**2004**
Personal Services	$ 210,162	$ 215,074
Capital Expenditures	1,771	5,272
Other:		
Insurance	14,855,476	15,582,430
Professional Fees	303,900	288,750
Claim Administrator Fees	295,658	486,176
Operating costs	9,545	28,915
Totals	15,676,512	16,606,617
Less Reimbursements:		
Current Year Payments		
Expenditure transfers	2,123,633	2,538,176
Receipts	497,215	709,168
Prior Year Payments		33,617
Total Reimbursements	2,620,848	3,280,961
Net Expenditures	**$ 13,055,664**	**$13,325,656**
Fund Categories:		
General Fund	10,651,712	11,731,718
Special Transportation	2,402,181	1,588,666
Capital Equipment/Purchase Fund	1,771	5,272
Totals	**$ 13,055,664**	**$13,325,656**

Insurance payments increased by $3,948,146 in 2003 and by $726,954 in 2004. The increases noted in 2003 and 2004 were primarily the result of overall increases in insurance premiums since September 11, 2001, and new property coverage including the Rentschler Field Stadium. The majority of payments made fell into four major categories of insurance as follows:

	2003		
	Premiums	**Deductible Payments**	**Totals**
Fire and extended coverage	$4,110,767	$ -	$4,110,767
General Liability	1,915,646	1,893,527	3,809,173
Auto Fleet	709,915	4,965,448	5,675,363
Bus Fleet	345,600	151,630	497,230
All Others	762,943	-	762,943
Total	$7,844,871	$ 7,010,605	$14,855,476

	2004		
	Premiums	**Deductible Payments**	**Totals**
Fire and extended coverage	$4,260,328	$ -	$4,260,328
General Liability	2,654,965	764,645	3,419,610
Auto Fleet	906,026	5,249,897	6,155,923
Bus Fleet	532,875	218,258	751,133
All Others	995,436	-	995,436
Total	$9,349,630	$ 6,232,800	$15,582,430

Deductible payments represent liability claims against the State within the deductible limits of the various policies. Such claims were processed by two third-party claims administrators that were remunerated on a fee-per-claim basis by the Board totaling $295,658 and $486,176 for the fiscal years ended June 30, 2003 and 2004, respectively, compared to $479,470 for the fiscal year ended June 30, 2002. These fluctuations reflect a number of factors including the per-claim rates, claims activity, and the deductible levels.

Insurance Recoveries:

As noted in the "Foreword" section of this report, State insurance recoveries are handled by the State Comptroller's Office. The processing of such recoveries is reviewed by our audit of that Office. In addition, as noted above in "Department Operations" the Board collected receipts for various premium reimbursements. The following table presents both the recoveries recorded by the Comptroller and total insurance program receipts, exclusive of expenditure transfers to other State agencies, of $2,123,633 in 2003 and $2,538,176 in 2004.

	June 30,	
	2003	**2004**
Fire and Extended Coverage	$145,404	$ -
All Others	14,318	118,486
Total Recoveries	159,722	118,486
Other receipts	552,928	761,500
Total Receipts	**$712,650**	**$879,986**

Fire and Extended Coverage Insurance:

Fire and extended coverage insurance was provided for on a blanket property policy. A seven-year tabulation of ESRC (estimated replacement cost of the State's inventory of personal and real property) as of June 30, and the premiums paid and damages recovered on blanket fire policies during the State Financial year ending June 30, follows:

Fiscal Year	Premiums Paid	Recoveries	ESRC at June 30,
1997-1998	$1,055,000	$266,977	$5,607,178,248
1998-1999	1,085,028	364,676	6,027,931,121
1999-2000	1,224,673	30,256	6,461,231,119
2000-2001	1,286,698	577,897	6,984,210,526
2001-2002	2,222,685	150,924	8,322,222,222
2002-2003	3,588,767	145,404	8,398,611,611
2003-2004	4,161,084	-	9,478,822,102

As of June 30, 2004, the blanket fire policy provides replacement coverage of $9,478,822,102 (less the deductible provisions) on all State-owned buildings and contents. The premiums paid on the blanket fire policy purchased during the 2004 fiscal year were at the rate of $.04 per hundred dollars of coverage.

During the period under review the provisions of the blanket fire policy required the State to bear a $250,000 deductible per occurrence.

Flood, earthquake, loss of rents and business income, valuable paper and records coverage was also provided. Insurance on flood and earthquake risks provides coverage of $100,000,000 for each peril per insured location with a $1,000,000 per occurrence deductible and a policy period limit of $100,000,000. Rental value insurance on dormitories at State schools and universities provides coverage of $1,000,000 per occurrence subject to the appropriate deductible for the peril that causes the loss. Loss-of-income insurance on business income at Bradley International Airport provides a policy period limit of $61,636,000 in coverage subject to a 30 day deductible. Valuable papers and records coverage of $25,000,000 and coverage of $5,000,000 on property in transit were provided.

Auto physical damage coverage is provided under a separate policy. This policy provides comprehensive and collision coverage to State vehicles valued at $100,000 or more and any leased vehicles per the contractual agreement. The maximum limit is $400,000 per any one vehicle, subject to a $50,000 deductible.

General Liability:

General liability insurance costs were as follows:

	June 30, 2003	June 30, 2004
Premiums	$1,915,647	$2,654,965
Deductible payments	1,893,626	764,645
Totals	$3,809,173	$3,419,610

Major insurance policies in this category include highway liability coverage and the excess combined coverage for fleet, highway, and buses. Other policies included insurance for lawyers' professional liability for public defenders.

As noted under the caption "Department Operations," deductible payments represent liability claims against the State within the deductible limits of the various policies.

Fleet Insurance:

Fleet (automobile) insurance costs were as follows:

	June 30, 2003	June 30, 2004
Premiums	$ 709,915	$ 906,026
Deductible payments	4,965,448	5,249,897
Totals	$5,675,363	$6,155,923

Total fleet insurance increased by $480,560 during the 2004 fiscal year when compared with the previous fiscal year. This reflects an increase in premiums of $196,111 and claims settled totaling $284,449.

The fleet insurance policy also provided coverage that included excess insurance for privately-owned vehicles used on State business. Primary coverage for such vehicles was provided by policies carried by their owners in accordance with State travel regulations. As noted in the "General Liability" section, additional liability coverage was provided by the excess policies covering fleet, highway, and buses.

Bus Insurance:

Bus insurance costs were as follows:

	June 30, 2003	June 30, 2004
Premiums	$ 345,600	$ 532,875
Deductible payments	151,630	218,258
Totals	$ 497,230	$ 751,133

Property and Liability insurance was provided for Connecticut Transit, a State-owned bus system. Payments were also made for coverage on buses leased by the State to various transit districts and contractual operators providing public bus service. As noted in the "General Liability" section, additional liability coverage was provided by the excess combined policies covering fleet, highway, and buses.

All Others:

Other insurance coverage included surety bonding of various State officers and employees pursuant to Section 4-20 of the General Statutes, comprehensive crime policies covering State employees, work-related accident and medical coverage for volunteer workers at State institutions, members of the State's armed forces, instructors of applicants for hunting licenses, and various types of coverage on State property such as aircraft and watercraft.

The comprehensive crime policies in effect during the audited period covered public employee dishonesty up to $1,000,000 per loss with a $100,000 deductible. Other limits and deductibles applied to such defined areas of coverage as forgery or alteration, and robbery and safe burglary. By the terms of endorsements to the policy, employees include students at State schools handling State property or funds, persons serving without pay on Boards and commissions, and persons employed by an employment contractor (temporary help services) while subject to and performing services for the State.

PROGRAM EVALUATION:

Section 2-90 of the General Statutes authorizes the Auditors of Public Accounts to conduct a program evaluation as part of their routine audits of public and quasi-public agencies. In this engagement, we selected the Board's risk management and loss prevention program for examination. The objective of this review was to determine if the program was being run in an effective manner consistent with State laws.

As a result of the above review, we are presenting the following finding and recommendation for consideration by the Board.

Controls over Risk Management and Loss Prevention Programs:

Criteria: Section 4a-20 of the General Statutes states that the "board may develop and implement risk management and loss prevention programs related to insurance plans established pursuant to the provisions of sections 4a-19 to 4a-21, inclusive."

Condition: The Board has only implemented one risk management and loss prevention program during the audit period. When the National Highway Safety Administration warned users of 15-passenger vans of the increased risk of rollovers and fatalities, the Board assessed this risk and developed a program to overhaul 78 vehicles' suspensions. During June 2004, the Board paid approximately $15,300 for equipment and arranged for the Department of

Administrative Services to overhaul the vehicles' suspensions. The Board had not determined how many of the vans had been overhauled until our audit asked for this information. They determined that by August 2005 only one-half of the equipment had been installed. The Board has not developed policies and procedures for monitoring the program and has not established criteria for assessing the program's success.

Effect: The Board does not know whether its risk management and loss prevention program has been effective.

Cause: The Board has not established a system or criteria for monitoring the program.

Recommendation: The Board should develop a system to monitor its risk management and loss prevention programs that includes establishing criteria for evaluating a program's success. It should monitor the current program and evaluate its effectiveness. (See Recommendation 1.)

Agency Response: "The Board with cooperation from DAS Fleet Operations will develop a system to monitor its risk management and loss prevention program for the installation of the Roadmaster System to the 15 passenger vans."

CONDITION OF RECORDS

Our audit of the Board's records revealed the following matters of concern requiring disclosure and Board attention.

Ethics Filings and Gift Affidavits:

Criteria: Governor Rell's Executive Order Number 1, Section 6 requires that by July 31, 2004, "all state employees and public officials who have responsibility for the review, award, or monitoring of state contracts must file a statement of financial interest with the State Ethics Commission" in accordance with Section 1-83 of the General Statutes.

Section 1-79, subsection (k), of the General Statutes defines a public official as including any person appointed to the Executive Branch by the Governor. Ethics Opinion No. 2000-21 also concludes that Board members are public officials.

Section 4a-19 of the General Statutes, establishes the 11-member State Insurance Risk Management Board that is appointed by the Governor. Section 4a-20 establishes the Board's authority to select the agent(s) of record, negotiate either a commission or fee for the agent(s) of record, select insurers, retain consulting firms, and negotiate consultant's fees.

Section 1-83, subsection (a), of the General Statutes requires specific individuals and those required by the Governor to file a Statement of Financial Interest with the Ethics Commission. It also requires the Board to develop and implement an Ethics Statement as it relates to their mission. Subsection (b) of this Section outlines the specific types of information required in the Statement of Financial Interest that is intended to disclose individuals' apparent conflicts of interest regarding their official duties.

Section 4-251 of the General Statutes, effective June 1, 2004, requires individuals and organizations that either are seeking a large contract or are contracting with the State to disclose gifts made to any public officials or State employees involved with the contract during the preceding two-years. It also requires public officials and employees of the State, authorized to execute large contracts, to disclose gifts they receive from contractors.

Condition: We noted that the Board did not fully comply with ethics and gift affidavit requirements.

Statement of Financial Interest: The Board's members have not been designated by the Governor or the Ethics Commission as needing to file these Statements. Based on the statutory definition of a "public official," and the member's authority to obligate the State, these individuals should file a Statement of Financial Interest in accordance with the Governor's Executive Order No. 1.

Ethics Statement: The Board has not developed an Ethics Statement.

Gift Affidavits: We were told that since June 1, 2004, only one insurer has been required to submit a gift affidavit. Affidavits have not been obtained from the Agent of Record who is responsible for obligating the State for purchases of insurance policies costing under $50,000 and for recommending insurers for larger policies. Also, the vendor providing management of self-insured claims was paid fees and claim reimbursements totaling approximately $6,875,800 and $6,717,100 during the fiscal years ending June 30, 2003 and 2004, respectively, but was not required to submit the affidavit.

Effect: The Ethics Commission may not be aware of the existence of conflicts of interest regarding the Board's procurement of contractors for insurance, the Agent of Record, and self-insured claims payments and fees that totaled approximately $15,500,000 and $16,400,000 during the fiscal years ending June 30, 2003 and 2004, respectively. The Board has not developed a formal ethics policy. The Board has not verified whether contractors have made gifts relating to its large contracts.

Cause: The Governor delegated the responsibility for determining who should file Statements of Financial Interest to the Ethics Commission and the Directors of each agency. According to the Ethics Commission they never contacted the Board to determine who should file. The Board did not realize it needed to develop an ethics statement. The requirements for gift affidavits are new and the Board did not consider them relevant to their operations.

Recommendation: Board members should be designated to file Statements of Financial Interest and should resolve this matter with the Governor's Office and the Office of State Ethics. They should develop an Ethics Statement and gift affidavits should be obtained in compliance with Section 4-251 of the General Statutes. (See Recommendation 2.)

Agency Response: "For administrative purposes only, the Board reports to the Office of the State Comptroller. A letter was sent to the Comptroller in accordance with the Governor's Executive Order 1. The Board members were not designated to file a Statement of Financial Interest. There are three people on the Board who are designated to file a Statement of Financial Interest. The Board will develop an Ethics Statement. Gift affidavits will be obtained from vendors with a contract value of $500,000 or greater."

Auditor's Concluding Comments: The State Comptroller, simply by virtue of the Department's "Administrative Purposes Only" role, may not be responsible for designating that the Board's members file Statements of Financial Interest. Rather, the State's Ethics Commission or the Governor's Office should determine and establish who has this responsibility. Also, we were told that the Board's members who did file the statements were not designated to file based on their role with the Board. They include the Comptroller, Deputy Comptroller (the Comptroller's designee,) and an employee of the Connecticut State University. The remaining 10 members of the Board should also be required to file the Statement.

Contingent Commissions Earned by the Board's Agent of Record:

Background: Contingent commissions are agreements made between insurance brokers and insurers that provide the broker with additional opportunities for commissions based on specific goals that may vary by insurer or by line of coverage. The State of Connecticut's Attorney General, among others, is investigating insurance bidding practices and contingent commission arrangements. As part of this broad investigation they subpoenaed records from the State's Agent of Record. As a result, the Board has required the Agent of Record to disclose the competitive nature of its bids and the contingent commissions they received relating to the State's insurance policies.

Criteria: Based on the Board's contract with its Agent of Record, insurance premiums paid by the Board should be net of "any type of commissions normally included in premium quotations." Also, the Agent is required to "reduce its overall fee" for commissions that "must be included in a premium charge" due to situations of law or insurance practice. This would include contingent commissions.

Section 4a-21 of the General Statutes requires the Board to report its activities to the Governor annually. This report should include "a breakdown of the actual commissions or fees paid" to their Agent of Record.

Condition: The State's Agent of Record did not reduce its fee for contingent commissions it received from insurers as required by the Board's contract. The Agent's response to the Board's request disclosed that during the 2002, 2003, and 2004 fiscal years, it had contingent commission arrangements with three of the State's insurers. The Agent did not report its commissions from prior periods and estimated that they will receive approximately $8,900 for the period July 2003 to July 2004. The Board paid the Agent $303,900 and $288,750 during fiscal years ending June 30, 2003 and 2004, respectively. The Board did not verify whether contingent commissions were paid to its Agent during prior periods.

The Board has interpreted the reporting requirement to include only the amount they disbursed to the Agent and not any contingent commissions paid by insurers. Also, since the Board was not aware of the amount of contingent commissions it could not include them in the report.

Effect: The Board may have overpaid approximately $8,900 to its Agent of Record for fees during the period July 2003 to July 2004. We could not determine the amount of overpayment occurring in previous fiscal years. The Board may not have fully complied with the reporting requirements.

Cause: We could not determine why the Agent did not previously disclose its contingent commissions. The Board did not verify whether its Agent was earning contingent commissions.

Recommendation: The Board should recover all contingent commissions earned by the Agent of Record on the State's business and should develop procedures to verify such contingent commissions periodically. The Board should seek the Attorney General's clarification of the reporting requirement to determine if it is intended to include commissions paid by insurers. (See Recommendation 3.)

Agency Response: "Contingent commissions are agreements (not client-specific) made between insurance brokers and insurers, providing the broker with additional opportunities for revenue. Contingent commissions were not paid by the Board to the Agent of Record. The Board will seek the Attorney General's opinion of the reporting requirement to determine if it is intended to include contingent commissions paid by insurers."

Auditor's Concluding Comments: While we agree that the Board did not directly pay contingent commissions to the Agent of Record, the State may have incurred the costs indirectly through its payment of premiums. We were informed that the intent of the agreement with the Agent of Record was to limit their compensation from the State's business. The "all-inclusive" language in the Board's contract with the Agent of Record supports this assertion by effectively limiting the amount of compensation the Agent may receive from the State's account. Also, Section 4a-20 of the General Statutes requires that "any refund, dividend or other payment from any insurance company in connection with insurance for the state shall be returned to the Comptroller for deposit in the General Fund." Contingent commissions, if directly attributable to policies held by the State, appear to be covered by this provision. The Agent of Record has indicated that it has received contingent commission income in the past and estimates that it will receive approximately $8,900 in "contingent commission income derived from the State of Connecticut account." This income is in addition to the amount established by the contract and should be offset against the Board's contractual General Fund payments.

Contractor Monitoring and Payment:

Criteria: Effective internal controls include reviewing invoices to ensure that billed amounts agree with contractual rates prior to making payments and to ensure that duplicate payments are not made.

Statement on Auditing Standard Number 70 (SAS 70) requires that audit reports on the processes of outside service organizations that process, execute, and record transactions be obtained periodically.

Condition: We noted that the Board contracted with an outside service organization to process self-insured claims. They did not verify the specific charges on the vendor's invoices that totaled $6,875,800 and $6,717,100 during the 2003 and 2004 fiscal years, respectively. The Board did consider the reasonableness of total claims at its meetings. We were unable to readily determine whether individual charges on the vendor's invoice were appropriate because the Board does not monitor small claims or their related invoices.

The Board did not review the contractor's SAS 70 report until we requested a copy.

Effect:	If overcharges or poor case management occurred, the Board would not be aware of it.
Cause:	The claims management invoices are very lengthy and therefore the Board did not review detailed billings. The Board was not aware that audits of outside service organizations' processes were available.
Recommendation:	The Board should improve its contractor monitoring and payment processes by periodically reviewing audit reports on the processes of outside service organizations and by reviewing invoices to prevent overpayments. (See Recommendation 4.)
Agency Response:	"The Board will review the Third Party Administrator's SAS 70 report on an annual basis. The Board will enhance their contractor review and payment process to verify the appropriateness of invoices."

RECOMMENDATIONS

Status of Prior Audit Recommendations:

One recommendation was presented in our prior report that will not be repeated by the current audit. The status of the recommendation is presented below.

- Controls should be put in place to ensure detailed compliance with statutory reporting requirements. We noted improvements regarding the Board's compliance with statutory reporting requirements during the audit period and will not repeat this recommendation. However, Recommendation 3 does include a reporting component that requires clarification by the Attorney General's Office.

Current Audit Recommendation:

1. **The Board should develop a system to monitor its risk management and loss prevention programs that includes establishing criteria for evaluating a program's success. It should monitor the current program and evaluate its effectiveness.**

   Comment:

   The Board did not establish policies and procedures for monitoring its risk management and loss prevention program. Only one-half of the stabilizer shocks the Board purchased for the State's 15-passenger vans were installed over one year after they were purchased.

2. **Board members should be designated to file Statements of Financial Interest and should resolve this matter with the Governor's Office and the Office of State Ethics. They should develop an Ethics Statement and gift affidavits should be obtained in compliance with Section 4-251 of the General Statutes.**

   Comment:

   Board members are public officials but have not been designated by the Governor to file Statements of Financial Interest. The Board has not developed an ethics statement and has not required gift affidavits for all of its large contracts.

3. **The Board should recover all contingent commissions earned by the Agent of Record on the State's business and should develop procedures to verify such contingent commissions periodically. The Board should seek the Attorney General's clarification of the reporting requirement to determine if it is intended to include commissions paid by insurers.**

   Comment:

   The Board's Agent of Record reported that it earned contingent commissions during the audit period but we noted that the Agent's fee was not reduced for such commissions in compliance with the Board's contract and their report to the Governor did not disclose these commissions.

4. **The Board should improve its contractor monitoring and payment processes by periodically reviewing audit reports on the processes of outside service organizations and by reviewing invoices to prevent overpayments.**

   Comment:

   The Board did not thoroughly review the invoices of its service contractor responsible for managing and paying self-insured claims. The Board did not monitor this service contractor's claims management by obtaining and reviewing the contractor's Statement on Auditing Standard Number 70 (SAS 70) report.

INDEPENDENT AUDITORS' CERTIFICATION

As required by Section 2-90 of the General Statutes we have audited the books and accounts of the State Insurance and Risk Management Board for the fiscal years ended June 30, 2003 and 2004. This audit was primarily limited to performing tests of the Board's compliance with certain provisions of laws, regulations, contracts and grants and to understanding and evaluating the effectiveness of the Board's internal control policies and procedures for ensuring that (1) the provisions of certain laws, regulations, contracts and grants applicable to the Board are complied with, (2) the financial transactions of the Board are properly recorded, processed, summarized and reported on consistent with management's authorization, and (3) the assets of the Board are safeguarded against loss or unauthorized use. The financial statement audits of the State Insurance and Risk Management Board, for the fiscal years ended June 30, 2003 and 2004, are included as a part of our Statewide Single Audits 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 State Insurance and Risk Management Board complied in all material or significant respects with the provisions of certain laws, regulations, contracts and grants 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, contracts and grants applicable to the State Insurance and Risk Management Board is the responsibility of the State Insurance and Risk Management Board's management.

As part of obtaining reasonable assurance about whether the Board 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 Board'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 State Insurance and Risk Management Board is responsible for establishing and maintaining effective internal control over its financial operations, safeguarding of assets, and compliance with the requirements of laws, regulations, contracts and grants applicable to the Board. In planning and performing our audit, we considered the Board's internal control over its financial operations, safeguarding of assets, and compliance with requirements that could have a material or significant effect on the Board's financial operations in order to determine our auditing procedures for the purpose of evaluating the State Insurance and Risk Management Board's financial operations, safeguarding of assets, and compliance with certain provisions of laws, regulations and contracts, and not to provide assurance on the internal control over those control objectives.

However, we noted certain matters involving the internal control over the Agency's financial operations, safeguarding of assets, and/or compliance that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control over the Agency's financial operations, safeguarding of assets, and/or compliance that, in our judgment, could adversely affect the Agency's ability to properly record, process, summarize and report financial data consistent with management's authorization, safeguard assets, and/or comply with certain provisions of laws, regulations, contracts and grants. We believe the following findings represent reportable conditions: the absence of ethics filings and gift affidavits; failure to report contingent commissions earned by the Board's Agent of Record; and contractor monitoring and payment.

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, contracts and grants or the requirements to safeguard assets that would be material in relation to the Agency's financial operations or noncompliance which could result in significant unauthorized, illegal, irregular or unsafe transactions to the Agency being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over the Agency's financial operations and over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material or significant weaknesses. However, we believe that the reportable conditions described above are material or significant weaknesses.

We also noted other matters involving internal control over the Agency's financial operations and over compliance, which are described in the accompanying "Program Evaluation" 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 assistance and courtesies extended to our representatives by the personnel of the State Insurance and Risk Management Board during the course of this examination.

Ramona Weingart
Associate Auditor

Approved:

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