

STATE OF CONNECTICUT



*AUDITORS' REPORT
STATE TREASURER – DEPARTMENTAL OPERATIONS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2018*

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

Table of Contents

EXECUTIVE SUMMARY	i
INTRODUCTION	1
COMMENTS	2
FOREWORD	2
Officers and Officials	2
Significant Legislation.....	3
RÉSUMÉ OF OPERATIONS.....	3
Department Revenues.....	3
Department Expenditures	4
Unclaimed Property Division	5
STATE AUDITORS' FINDINGS AND RECOMMENDATIONS.....	7
Deficiencies in Contracting Processes.....	7
Statutory Reporting Requirements	9
Annual Report of the State Treasurer	10
RECOMMENDATIONS	12
Status of Prior Audit Recommendations:	12
Current Audit Recommendations:.....	13
ACKNOWLEDGMENTS	14
CONCLUSION.....	15

June 2, 2020
EXECUTIVE SUMMARY

In accordance with the provisions of Section 2-90 of the Connecticut General Statutes, we have audited certain operations of the Office of the State Treasurer. The objectives of this review were to evaluate the department's internal controls; compliance with policies and procedures, as well as certain legal provisions; and management practices and operations for the fiscal years ended June 30, 2017 and 2018.

The key findings and recommendations are presented below:

Page 7	Our review of contracts found that contracts were executed after the start date and services were rendered prior to the execution of contracts. In addition, the Treasury did not follow OPM procurement standards. 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. Additionally, the office should adhere to the procurement standards set forth in the Connecticut General Statutes and established by the Office of Policy and Management. (Recommendation 1.)
Page 8	The Office of the State Treasurer did not submit the required report on the firefighters' cancer relief account as required by section 7-313k of the General Statutes. The Office of the State Treasurer should comply with the reporting requirements of Section 7-313k of the General Statutes or seek a legislative change to repeal the statute or amend it to reflect the current practice. (Recommendation 2.)
Page 9	The Office of the State Treasurer did not adhere to its internal schedule for the preparation of the annual report. The Office of the State Treasurer should institute procedures to ensure that the annual report is prepared and reviewed in a timely manner. (Recommendation 3.)

STATE OF CONNECTICUT



AUDITORS OF PUBLIC ACCOUNTS

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JOHN C. GERAGOSIAN

ROBERT J. KANE

June 2, 2020

AUDITORS' REPORT

INTRODUCTION

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 years ended June 30, 2017 and 2018. 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 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, 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 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 noncompliance with policies and procedures or legal provisions; and
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 focused primarily on the departmental operations of the Treasury and includes our review of the Business Office, Human Resources, Information Technology, the Unclaimed Property Division, and the Connecticut Higher Education Trust. Our review of financial operations of the Treasury that have statewide impact has been issued under separate cover and includes the Pension Funds Management Division, the Debt Management Division, the Cash Management Division, and the Second Injury Fund.

Officers and Officials

The officers and officials of the Treasury as of June 30, 2018, 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
Laurie Martin, Chief Investment Officer
Christine Shaw, Assistant Treasurer, Policy
Christopher Martin, Assistant Treasurer, Debt Management

On January 9, 2019, Shawn T. Wooden was sworn in as State Treasurer.

Significant Legislation

Public Act 16-10, effective February 1, 2017, required the State Treasurer to submit a status report on the firefighters cancer relief account not later than January 1, 2018, and annually thereafter, to the joint standing committee of the General Assembly on matters relating to public safety. The report must include information on the balance of the account, participation in the program and demographic information of recipients.

Public Act 17-2, section 712(f)(2), of the June 2017 Special Session, effective October 31, 2017, required the State Treasurer to provide the Governor with a list of the allocated but unissued bonds not later than January 1, 2018, and January first annually thereafter.

RÉSUMÉ OF OPERATIONS

Department Revenues

Departmental revenues include amounts from Federal and Other Restricted Accounts Fund, and the General Fund, which includes unclaimed property receipts. The changes in the Other Restricted Account represents deposit of funds associated with the operating expenses of the Pension Funds Management Division, Short-Term Investment Fund, and the Debt Management Division. For fiscal year ended June 30, 2018, the Debt Management Division had a significant decrease in bond issuance premiums received. These amounts fluctuate from year to year based on activity. Unclaimed property receipts fluctuate from year to year based on the type of escheats received, as well as the value of the stock that is escheated.

	<u>Fiscal Year Ended June 30,</u>		
	<u>2016</u>	<u>2017</u>	<u>2018</u>
Federal and Other Restricted Accounts Fund	\$ 268,702,516	\$ 287,668,077	\$ 177,329,235
General Fund - All other Receipts	39,192,352	45,355,497	66,034,899
General Fund – Unclaimed Property	100,097,186	106,262,465	127,088,405
Total Revenues	<u>\$ 407,992,054</u>	<u>\$ 439,286,039</u>	<u>\$ 370,452,539</u>

Section 3-69a of the General Statutes provides for the allocation of a portion of escheat revenues 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 \$11,428,647 and \$11,634,363 for the fiscal years ended June 30, 2017 and 2018, respectively. Since its inception, transfers to the Citizens’ Election Fund totaled \$183,087,285. 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 can always 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, 2017 and 2018, the Treasury estimated the market value of unclaimed securities to be \$4,208,673 and \$3,906,687, respectively.

The Treasury also receives revenue for the Second Injury Fund and the Workers' Compensation Administration Fund (WCAF). The Second Injury Fund's revenues consisted primarily of assessments levied against self-insured employers and companies writing workers' compensation or employers' liability insurance, and totaled \$37,046,906 and \$36,762,940, for the fiscal years ended June 30, 2017 and 2018, respectively. WCAF assessment receipts totaled \$23,898,254 and \$18,095,352, for the fiscal years ended June 30, 2017 and 2018, respectively.

Department Expenditures

General Fund expenditures of the Treasury for the fiscal years ended June 30, 2016, 2017, and 2018, are summarized below:

	<u>Fiscal Year Ended June 30,</u>		
	<u>2016</u>	<u>2017</u>	<u>2018</u>
Debt Service	\$ 1,967,360,338	\$ 2,057,604,392	\$ 2,300,756,828
Unclaimed Property Returned to Owners	57,572,275	41,108,111	58,212,157
Purchased & Contractual Services	440,856	648,559	846,160
Personal Services & Employee Benefits	3,060,211	2,862,558	2,671,652
Information Technology	16,866	16,624	15,453
Premises & Property Expenses	20,547	17,773	20,763
Employee Expenses, Allowances & Fees	8,324	8,333	(109)
Purchased Commodities	11,495	18,806	5,903
Motor Vehicle Costs	9,301	11,909	11,055
Capital Outlays - Equipment	-	25	5,058
Net Expenditures	<u>\$ 2,028,500,213</u>	<u>\$ 2,102,297,090</u>	<u>\$ 2,362,544,920</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 stocks that are sold by the Treasury upon receipt.

Federal and Other Restricted Accounts Fund expenditures of the Treasury for the fiscal years ended June 30, 2016, 2017, and 2018, are summarized below:

	<u>Fiscal Year Ended June 30,</u>		
	<u>2016</u>	<u>2017</u>	<u>2018</u>
Debt Service	\$ 143,149,354	\$ 172,356,300	\$ 91,293,903
Purchased & Contractual Services	97,621,197	93,709,642	99,874,146
Personal Services & Employee Benefits	17,582,303	17,090,768	16,365,810
Information Technology	434,496	319,121	218,914
Premises & Property Expenses	50,304	43,527	47,999
Employee Expenses, Allowances & Fees	27,384	20,212	29,020
Purchased Commodities	78,968	42,386	61,584
Motor Vehicle Costs	30,396	27,904	28,185
Capital Outlays - Equipment	34,495	1,038	55,535
Other Expenditures	2,013,358	1,810,976	1,673,356
Net Expenditures	<u>\$ 261,022,255</u>	<u>\$ 285,421,874</u>	<u>\$ 209,648,452</u>

The Federal and Other Restricted Accounts Fund expenditures include operating expenses for the State Treasurer’s Pension Funds Management Division and the Unclaimed Property Division. 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, the Capital Equipment Purchases Fund, and the operational expenses of the Connecticut Higher Education Trust and the Clean Water Fund. Total expenditures from these funds for the fiscal years ended June 30, 2017 and 2018, were \$549,655,825 and \$578,952,221, respectively. The majority of these amounts, \$542,981,635 and \$574,810,394, were related to debt service payments for transportation bonds.

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 \$6,135,219 and \$5,491,178 for the fiscal years ended June 30, 2017 and 2018, 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, 2016, 2017, and 2018, is as follows:

	<u>Fiscal Year Ended June 30,</u>		
	<u>2016</u>	<u>2017</u>	<u>2018</u>
Corporations	\$ 38,368,606	\$ 39,778,153	\$ 50,862,536
Financial Institutions	26,666,525	32,091,552	24,144,558
Insurance Companies	21,810,296	23,065,068	14,340,442
Governmental and Public Agencies	5,683,123	4,008,597	4,053,394
Dividends on Securites Held	106,664	117,225	175,227
Reciprocal Exchange with Other States	1,088,868	1,079,326	1,092,781
Miscellaneous	3,738	15,104	3,172
Securities Tendered	86,007	86,244	18,392
Securities Liquidated	17,632,827	28,946,243	44,034,620
Totals	<u>\$ 111,446,654</u>	<u>\$ 129,187,512</u>	<u>\$ 138,725,122</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>2016</u>	<u>2017</u>	<u>2018</u>
Claim Payments	\$ 57,568,310	\$ 41,105,448	\$ 58,182,884
Transfers to Citizens Election Fund	11,349,203	11,428,647	11,634,363
Salaries and Fringe Benefits	3,786,288	3,692,758	3,584,769
Data Processing and Hardware	1,837,988	2,329,983	1,770,305
All Other	68,760	112,478	136,104
Totals	<u>\$ 74,610,549</u>	<u>\$ 58,669,314</u>	<u>\$ 75,308,425</u>

STATE AUDITORS' FINDINGS AND RECOMMENDATIONS

Our examination of the records of the Office of the State Treasurer's departmental operations disclosed the following 3 findings and recommendations, one of which has been repeated from the previous audit:

Deficiencies in Contracting Processes

Background:

A state agency entering into a personal service agreement (PSA) or purchase of service (POS) contract must adhere to the procurement standards set forth in the General Statutes and in policies set forth by the Secretary of the Office of Policy and Management (OPM).

A competitive procurement is the purchase or acquisition of services by a state agency through an open and fair process, where all responsible sources have an equal opportunity to pursue, and possibly be selected for, a contract to provide the agency with the desired services. A solicitation document called a request for proposal (RFP) is used to communicate information about the services an agency wishes to procure.

When an agency solicits and negotiates with only one potential contractor, the acquisition method is considered a sole source procurement.

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.

Sections 4-215 and 4-216 of the General Statutes requires state agencies to conduct an RFP process to select a contractor when the anticipated cost or term of a future contract exceeds \$20,000 or one year. OPM procurement standards require that all participants involved in the RFP process must sign an ethics and confidentiality agreement prior to the start of the process.

Section 4-216 (b) of the General Statutes provides that each personal service agreement having a cost of more than \$50,000 or a term of more than one year shall be based on competitive negotiation or competitive quotations, unless the state agency purchasing the personal services is granted a waiver from OPM. The OPM procurement standards require that an agency must apply for approval from OPM before selecting a contractor for sole source procurement.

<i>Condition:</i>	<p>Our review of the procurement process for 15 contracts executed during the audited period revealed the following issues:</p> <ul style="list-style-type: none">• Six contracts were executed between 5 and 25 days after the service start date. In addition, contractors began providing services on two of those contracts prior to execution. Expenses incurred during that period were \$31,410.• Treasury did not have a procedure in place to have employees involved in the RFP process sign an ethics and confidentiality agreement prior to the start of the RFP process.• The Treasury executed a \$400,000 sole source contract with a starting date that was 14 days prior to receiving OPM approval to waive the RFP process.
<i>Context:</i>	<p>Treasury entered into 39 new contracts during the audited period.</p>
<i>Effect:</i>	<p>Unforeseen liabilities may be incurred if work starts on a project before all of the key terms have been agreed to and the contract has been fully executed.</p>
<i>Cause:</i>	<p>Employees responsible for processing contractual agreements failed to execute the contracts before the commencement date.</p>
<i>Prior Audit Finding:</i>	<p>This finding has been previously reported in the last two audit reports covering the fiscal years ended 2013 to 2016.</p>
<i>Recommendation:</i>	<p>The Office of the State Treasurer should strengthen internal controls over its contracting process. (See Recommendation 1.)</p>
<i>Agency Response:</i>	<p>“We agree with the Auditors’ recommendation. This finding occurred under the prior administration. As also noted in the previous audit response, Treasury personnel have been instructed not to allow costs to incur prior to the execution of a contract.</p> <p>Treasury has since implemented a procedure to have employees involved in the RFP process sign an Ethics and Confidentiality Agreement prior to the start of the RFP process. Additionally, we have updated our procedures to adhere to the procurement standards established by the Office of Policy and Management.”</p>

Statutory Reporting Requirements

- Criteria:* Sound internal controls suggest that a department should have a centralized mechanism in place to monitor compliance with various statutory and regulatory reporting requirements. Agencies should continuously evaluate their reporting requirements and propose legislation when such requirements become obsolete.
- Section 7-313k of the General Statutes provides that the State Treasurer, in consultation with the Connecticut State Firefighters Association, must submit a report to the joint standing committee of the General Assembly having cognizance of matters relating to public safety on the status of the firefighters' cancer relief account by January 1, 2018, and annually thereafter.
- Condition:* The Office of the State Treasurer did not submit the report on the firefighters' cancer relief account as required by Section 7-313k of the General Statutes.
- Effect:* The Office of the State Treasurer did not comply with Section 7-313k of the General Statutes.
- Cause:* The Office of the State Treasurer regarded the reporting requirement as unnecessary because funding was not available. Since there was no activity for the Firefighters Cancer Relief Fund, the Treasury did not complete the report.
- Prior Audit Finding:* This finding has not been previously reported.
- Recommendation:* The Office of the State Treasurer should comply with the reporting requirements of Section 7-313k of the General Statutes or seek a legislative change to repeal the statute or amend it to reflect the current practice. (See Recommendation 2.)
- Agency Response:* "We agree with the Auditors' recommendation. There was no activity for the Firefighters Cancer Relief Fund, which is why the report was not completed. Going forward, we will report no activity until we either seek a legislative change to either repeal or otherwise amend the current language to reflect the current practice."

Annual Report of the State Treasurer

- Background:* Each year the Office of the State Treasurer produces an annual report as required by Section 3-37(a) of the Connecticut General Statutes. This sizeable report provides financial information for the Connecticut Retirement Plans and Trust Funds, the Short-Term Investment Fund, the Second Injury Fund, The Connecticut Higher Education Trust, Civil and Non-Civil List Trust Funds, debt outstanding as well as many other areas of Treasury operations. It also includes performance data, statistical data and narrative information. Certain sections of the report must be audited and the Treasury must submit the report to the Governor by December 31st each year. In order to meet this date, management sets completion deadlines for each section of the report, as well as for the compiled, comprehensive draft. This occurs in conjunction with the auditors, as part of the terms of the audit engagement, to ensure that the report is compiled, reviewed, and audited in a timely manner.
- Criteria:* Sound business practice suggests that adequate time is provided for the review of report drafts so that management can efficiently detect and correct errors.
- Condition:* Our review of the annual report for fiscal year 2019 disclosed that the office did not complete 9 of 13 sections within its internal deadlines. The office completed those sections 6 to 95 days late (average of 44 days late).
- The agency provided us a report that included almost 200 clerical errors. Those included missing pages, missing paragraphs, missing amounts from financial statements that were correct in the divisional drafts, and incorrect headings. It took several revisions to correct the key identified errors, pushing back the date that the Treasury provided the auditors with the final report.
- Effect:* Although the Treasury submitted the report to the Governor on time, there is an increased risk of undetected errors when adequate time is not provided to review draft reports. There is an inefficient use of state resources when Treasury staff must spend time reviewing numerous revisions to verify that errors were corrected and check for new errors. The Treasury placed undue pressure on the auditors when it did not provide drafts in accordance with agreed-upon deadlines.
- Cause:* Treasury management did not adequately monitor the progress of the report, enforce deadlines, or communicate with the vendors and divisions in a timely manner. The office sent the report to a graphic designer for formatting too late for management to have sufficient time to review it before providing it to the auditors. In addition, the office

did not have a process in place to redline revisions and changes for ease of review.

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

Recommendation: The Office of the State Treasurer should institute procedures to ensure that the annual report is prepared and reviewed in a timely manner. (See Recommendation 3.)

Agency Response: “We concur with the Auditors’ recommendation. We are reviewing and will revise, as necessary, our process and procedures to ensure that the annual report is prepared, reviewed, and submitted in a timely manner going forward.”

RECOMMENDATIONS

Status of Prior Audit Recommendations:

Our prior audit report on the Office of the State Treasurer's Departmental Operations contained 2 recommendations. One has been implemented or otherwise resolved and one has been repeated or restated with modifications during the current audit.

- 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. **This recommendation is being repeated. (See Recommendation 1.)**
- The Office of the State Treasurer should comply with the Department of Administrative Services guidelines for telecommuting when establishing telecommuting agreements. **This recommendation has been resolved.**

Current Audit Recommendations:

- 1. The Office of the State Treasurer should strengthen internal controls over its contracting process.**

Comment:

Our review of contracts found that contracts were executed after the start date and services were rendered prior to the execution of contracts. In addition, the Treasury did not follow OPM procurement standards.

- 2. The Office of the State Treasurer should comply with the reporting requirements of Section 7-313k of the General Statutes or seek a legislative change to repeal the statute or amend it to reflect the current practice.**

Comment:

The Office of the State Treasurer did not submit the required report on the firefighters' cancer relief account as required by section 7-313k of the General Statutes.

- 3. The Office of the State Treasurer should institute procedures to ensure that the annual report is prepared and reviewed in a timely manner.**

Comment:

The Office of the State Treasurer did not adhere to its internal schedule for the completion of the annual report. The late preparation did not provide the agency with adequate time to properly review the report prior to submitting it to the auditors.

ACKNOWLEDGMENTS

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

Jaimie Hubeny
Thomas Caruso
David Tarallo

CONCLUSION

In conclusion, we wish to express our appreciation for the courtesies and cooperation 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