

STATE OF NEW HAMPSHIRE

STATE TREASURY

PROGRESS REPORT ON AUDIT FINDINGS

PURSUANT TO EXECUTIVE ORDER 2014-03

MARCH 21, 2015

**State of New Hampshire Treasury
Progress Report on Audit Findings
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Observation No. 1

Improve Compliance With Federal Treasury-State Agreement

The audit report indicated Treasury had not monitored the State's operation of the Federal Treasury-State Agreement ("TSA") for drawing federal funds to ensure State agencies are in compliance with its provisions. The audit report also stated the State's recent (2013) Single Audits of federal programs identified a number of concerns with State agencies' drawing of federal program funds. Concerns included certain Agency practices for drawing federal program funds did not align with provisions in the TSA, the TSA does not necessarily treat the State's interests fairly, and the State accounting system's cash management routine was not in agreement with controlling provisions of the TSA.

Current Status:

State Treasury understands it is the Agency authorized to represent the State in the Federal Treasury-State Agreement. However, efforts have not been sufficient to coordinate all federal programs and the provisions relative to the Cash Management Improvement Act of 1990. Upon recognition of the federal grant activity and funding levels, it was determined that greater central resources were needed. As a result, the Department of Administrative Services created the Federal Grants and Cost Allocation Administrator ("Administrator") position in 2014 to coordinate all aspects of the federal program activity. Since then, the State Treasury has received increased support from this Administrator and this collaboration with State Treasury has made it possible to amend the previously approved fiscal year 2014 TSA, which was retroactive, effective July 1, 2014. The purpose of the amendment was to immediately align the cash management practices carried out by State agencies with the provisions of the TSA.

State Treasury expects to collaborate with the Administrator to establish an agreed-upon plan that would define roles and responsibilities going forward and ensure compliance with the cash management requirements, in particular as it relates to the TSA. Completion of this plan is targeted for June 30, 2015.

Observation No. 2

Review And Improve Controls Over Information Technology Systems

The audit report noted Information Technology ("IT") controls could be improved to lessen risk and improve the security and reliability of Treasury's information systems.

Issues noted were as follows:

1. Access permissions to certain Treasury key information systems as well as templates and permissions granted in banking applications were not routinely reviewed,
2. Security concern identified by Treasury had not been timely addressed by other responsible agencies (Financial Data Management ("FDM") and Department of Information Technology ("DoIT")) since the implementation of NHFirst in 2009,
3. Backups and recovery controls were in need of improvement.

Current Status:

State Treasury is actively reviewing and updating user permissions granted to State Treasury and other State department employees for the use of key information systems and banking products. Furthermore, many old and unused banking templates have been deleted from the main banking platforms. Management of banking tools and security controls, as established by banking partners, has been difficult to manage and monitor, and the risks associated with it are regularly evaluated by Treasury management. Treasury recognizes that there is more that can be done to respond to the identified risks and expects to have a plan in place by June 30, 2015.

State Treasury initiated discussions with FDM and DoIT requesting efforts to find a solution for the security concern identified by State Treasury in 2009. FDM and DoIT have committed to implement a solution which is currently on schedule to be implemented by the end of March 2015.

All data backups are now maintained both locally and offsite. State Treasury has implemented virtual servers maintained by DoIT that have included new data backup and restore capabilities. State Treasury performs two types of external backups, a Disk-to-Disk backup and a directory synchronization to a different virtual server located at DoIT.

State Treasury's procedures include routine updates of certain Treasury disaster recovery and business continuity components. In addition, State Treasury utilized certain cash operations procedural contingencies, which are part of the current business continuity plan, in January of 2015 when the State closed its operations due to a weather-related event. However, State Treasury recognizes that the Disaster and Business Continuity Plan needs to be updated and that tests need to be performed on a more routine basis. Treasury is currently re-evaluating how to proceed with this important planning mechanism and the corresponding documentation. State Treasury expects to have more optimal measures in place by June 30, 2015.

Observation No. 3

Ensure Policies And Procedures For Posting Inter-Agency Transactions Are Appropriate For Treasury's Purpose

This observation stated "Treasury's error in posting two inter-agency transactions during fiscal year 2013 resulted in Treasury understating both revenues and expenditures by \$2.1 million.

The audit identified that Treasury posted the receipt of reimbursements for two debt service payments as negative expenditures instead of revenues. These two posting errors resulted in expenditures and revenues both being understated. Treasury corrected the errors prior to the preparation of the June 30, 2013 financial statements."

Current Status:

State Treasury corrected the errors and the weakness causing the errors prior to the audit report issuance on March 21, 2014. This observation remains fully resolved.

Observation No. 4***Maintain Accurate Information On All State-Guaranteed Debt***

This observation indicated Treasury did not have policies and procedures for maintaining accurate information regarding the State's contingent liabilities related to certain mortgage loans issued with State guarantees.

Current Status:

The State Treasury completed the necessary procedures to implement Statement No. 70 of the Governmental Accounting Standard Board (GASB) relative to *Accounting and Financial Reporting for Nonexchange Financial Guarantees* for the fiscal year ended June 30, 2014. As a result of this implementation, the State was able to determine and properly disclose in its comprehensive annual financial report ("CAFR") dated June 30, 2014, the likelihood of making payments in relation to guarantees extended to other governments, as well as other pertinent information relative to its extended guarantees. State Treasury has also updated its year-end procedures to ensure accurate information is reported each year relative to the State's contingent liabilities, in particular, information on bonds and loans issued with State guarantees. As a result, this observation is considered resolved.

Observation No. 5***Finalize Capital Projects Lists Timely***

The audit report indicated Treasury had not finalized the capital projects list supporting its November 2012 bond issue as of March 5, 2014. The capital projects list identifies the capital projects supported by the bond issue and is used in Treasury's allocation of bond proceeds, liabilities, and debt service charges. The incomplete nature of the capital projects list at June 30, 2013 may have contributed to the need for Treasury to make several corrections to draft debt disclosures prepared for the State's comprehensive annual financial report, subsequent to auditor inquiry about amounts presented. Documentation made available to the auditors did not fully support the debt service allocated to certain State agencies responsible for paying a portion of debt service at June 30, 2013.

Current Status:

Capital Project lists undergo many iterations before they are finalized, as they always reflect in part the reimbursement of existing project expenditures and in part future projections of capital expenditures on authorized but unissued capital appropriations. During the timetable for deployment of bond proceeds, projects that do not spend as much as anticipated have to be replaced in whole or in part with projects that spend more quickly than expected. This reallocation process is manual and thus very time consuming. For this reason, Treasury strives to include as much actual expenditure activity as possible on each bond issue before "finalizing" the list for budgeting purposes as well as determining individual debt service schedules based on funding sources that are then consolidated into the entire issue.

State Treasury agrees that maintaining accurate and meaningful capital project activity reports using spreadsheets has been challenging and believes that with the implementation of the new functionality within NHFirst (Activities Module), this process will be significantly improved. State Treasury continues to collaborate with the Department of Administrative Services and is now in the implementation phase of the Capital Projects functionality. Treasury believes once the implementation of this functionality occurs, certain functions currently performed manually will become automated, making the process more efficient. Furthermore, the reporting ability of this functionality will provide accurate and timely information for its users, as well as historical and auditable information. The Capital Projects functionality is on schedule to be in production by June 30, 2015.

Observation No. 6

Notify Financial Institutions Timely Of Changes In Individuals Authorized To Initiate Transactions

The audit report indicated that Treasury did not timely update its list of authorized signers at one financial institution with which it maintained 52 State investment accounts during, and subsequent to, fiscal year 2013.

Current Status:

Treasury updated the list of authorized signers as soon as it was notified by the auditors of the omission. Since being notified of the weakness, Treasury updated procedures, completed an exhaustive inventory of all accounts, and followed up with banking and investment partners to ensure such changes were implemented. Treasury believes this observation remains fully resolved.

Observation No. 7

Improve Segregation Of Duties For Trust And Agency Funds

The audit reported the financial accounting duties for Treasury's trust and agency funds were not fully segregated during most of the fiscal year ended June 30, 2013.

Current Status:

Treasury has been aware of the risks associated with trust and agency fund activity and, accordingly, has tried to mitigate those risks with other internal controls. Treasury continues to review its trust and agency fund responsibilities to determine whether these functions could be further segregated or if additional controls could be applied to ensure those risks are further reduced or eliminated. State Treasury has also initiated preliminary discussions with the Comptroller's office relative to accounting for the trust and agency accounts in the State's accounting system, NHFirst, which has inherent system controls; however, the two agencies have not had an opportunity to fully explore this issue. State Treasury will continue to pursue this initiative and expects to have a plan for implementation by June 30, 2015.

Observation No. 8

Improve Record-Keeping For Trust And Agency Accounts

The audit reported during fiscal year 2013 Treasury primarily used spreadsheets to account for the financial activity in the 49 trust and agency funds for which it is custodian. The financial activity of certain trust and agency funds is also budgeted and accounted for in the State's accounting system (NHFirst).

Current Status:

As stated above, Treasury will pursue discussions with the Comptroller's office regarding the possibility of transferring the books and records of the trust and agency accounts to NHFirst.

State Treasury performs this function through the use of spreadsheets, and using NHFirst for this function would eliminate duplication of records and the potential risks associated with recording accounting transactions in spreadsheets. State Treasury expects to have a plan for implementation by June 30, 2015.

Observation No. 9

Maintain Listing Of Authorized Initiators Of Trust And Agency Account Transactions

The audit report noted that Treasury's controls over the initiation of trust and agency account transactions did not include ensuring the individuals requesting the transactions have the proper authority to direct the receipt or expenditure of funds within the accounts.

Current Status:

In the fall of 2014, State Treasury compiled a list of individuals who are authorized to direct routine transactions. In addition, State Treasury updated its procedures relative to its biennial update of Custodial Account Agreements ("Agreement") maintained with all the Trust and Account Administrators by adding information relative to individuals who are authorized to conduct trust and agency financial transactions. State Treasury believes this observation is now fully resolved.

Observation No. 10

Determine The Ownership And Disposition Of Account Balances

The audit report indicated that three trust and agency accounts maintained by the Treasurer require review to determine the purpose and ownership of certain balances in those accounts.

Current Status:

Recent conversations have taken place between State Treasury and the State agency that has historically benefited from the Laconia State School trust funds regarding the use of this trust fund

money. Since the Laconia State School is no longer in existence, State Treasury has requested that this State Agency obtain guidance from the Attorney General's office as to the proper disposition, ownership, and new purpose of the funds. An update is expected by the end of March 2015. State Treasury is not currently fulfilling any requests until there is clarity regarding the appropriate use of these funds.

State Treasury has begun investigating the current status of the Crown Paper Workers Compensation fund to determine the ownership and disposition of the funds. More work needs to be done before any decision is made relative to this fund.

State Treasury has been actively reviewing the Financial Responsibility accounts and has returned funds to the individuals as indicated by RSA 264:5. The issue of interest earned and maintained in the money market account still needs to be addressed. State Treasury is requesting guidance from the Attorney General's office to properly determine the ownership and potential distribution of the interest.

Resolution is now targeted for September 30, 2015.

Observation No. 11

Review Trust And Agency Financial Information In State CAFR For Proper Presentation

The audit reported Treasury had not established policies and procedures to periodically review the trust and agency financial information included in the State's CAFR to ensure that the trust and agency financial information of the accounts in the Treasury's custody is properly presented.

Current Status:

As noted previously, Treasury's procedure is to review, in collaboration with Administrative Services, the nature and authority of any new accounts assigned to State Treasury for its custody in order to determine how the funds should be reported in the CAFR. In addition, beginning in the fall of 2014, State Treasury incorporated into its year-end procedures a review and reconciliation between the trust and agency account reports included in the Unaudited CAFR and the State Treasury's records to ensure that they are accurate and maintained in accordance with established criteria, as well as consistent with prior years. State Treasury believes this observation is fully resolved.

Observation No. 12

File Report Of Information Required By Statute

The audit reported Treasury did not file certain statutorily-required reports during the fiscal year ended June 30, 2013.

Current Status:

State Treasury has now filed its second, third, and fourth quarter (calendar year 2014) Quarterly Cash and Investments Balance Reports with the Governor and Executive Council, Commissioner of Administrative Services, and the Joint Fiscal Committee pursuant to RSA 6-B:2,VII. State Treasury has established a procedure to file the quarterly reports timely going forward.

After the auditors brought the issue to State Treasury's attention, Treasury forwarded its 2013 annual report to the Director of Charitable Trusts. Accordingly, State Treasury also sent its fiscal year 2014 annual report to the Department of Justice by October 1, 2014 as required by RSA 11:5-b,II. This observation is fully resolved.

Observation No. 13

Create And Operate Accounts As Established And Described By Statute

The audit indicated Treasury did not utilize certain statutorily-established accounts during fiscal year 2013.

Current Status:

State Treasury made an effort to amend RSA 261:97-b (conservation number plate trust fund) and RSA 227-M:7-a (the land and community heritage investment program administrative fund) during the 2015 legislative session. However, State Treasury targeted statutory amendments through the improper legislative committee and will now seek a sponsor from the House Ways and Means prior to the 2016 legislative session. Observation should be resolved by December of 2016.