

STATE OF NEW HAMPSHIRE

STATE TREASURY

PROGRESS REPORT ON AUDIT FINDINGS

PURSUANT TO EXECUTIVE ORDER 2014-03

SEPTEMBER 21, 2015

**State of New Hampshire Treasury
Progress Report on Audit Findings
Summary**

No.	Page	Observation Description	Status
1	1	Improve Compliance With Federal Treasury-State Agreement	Partially Resolved
2	1	Review And Improve Controls Over Information Technology Systems	Partially Resolved
3	2	Ensure Policies And Procedures For Posting Inter-Agency Transactions Are Appropriate For Treasury's Purpose	Resolved
4	3	Maintain Accurate Information On All State-Guaranteed Debt	Resolved
5	3	Finalize Capital Projects Lists Timely	Substantially Resolved
6	4	Notify Financial Institutions Timely Of Changes In Individuals Authorized To Initiate Transactions	Resolved
7	4	Improve Segregation Of Duties For Trust And Agency Funds	Partially Resolved
8	5	Improve Record-Keeping For Trust And Agency Accounts	Unresolved
9	5	Maintain Listing Of Authorized Initiators Of Trust And Agency Account Transactions	Resolved
10	6	Determine The Ownership And Disposition Of Account Balances	Partially Resolved
11	6	Review Trust And Agency Financial Information In State CAFR For Proper Presentation	Resolved
12	7	File Report Of Information Required By Statute	Resolved
13	7	Create And Operate Accounts As Established And Described By Statute	Partially Resolved

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:

In 2014, the Department of Administrative Services - Comptroller's office created the position of Federal Grants and Cost Allocation Administrator ("Administrator") to coordinate all aspects of federal program activity. Since then, the Administrator and Chief Deputy Treasurer have worked together to remediate some of the audit findings identified in recent Single Audits and have identified roles and responsibilities as it relates to the Cash Management requirement. Treasury being the Agency authorized to represent the State in the Federal Treasury-State Agreement, and with collaboration from the Administrator, obtained approval from U.S. Treasury to submit a revised TSA that corrected inconsistencies with State agencies' practices causing non-compliance in prior years' audits. As result, New Hampshire avoided several non-compliance findings in the area of Cash Management during the fiscal year 2014 federal Single Audit. Furthermore, Treasury continues to explore better ways to communicate with State agencies and is looking into to the possibility of posting relevant documents, including the TSA, on the State's Intranet site. State agencies would then have the ability to access information such as the funding techniques, clearance patterns, and other important information assigned to the grants they administer.

The work in this area is ongoing and unfortunately the Administrator position has been vacant for several months. In order for the State to reach full compliance, it would require ongoing collaboration among the Comptroller's Office, Treasury, and the State agencies responsible for administering the federal programs. Treasury expects to finalize documentation regarding roles and responsibilities already defined and continue with the actions already achieved until a person is again assigned to the Administrator role. Observation is deemed partially resolved.

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:

Treasury has performed a very thorough review of its procedures for granting banking access to Treasury and non-Treasury employees and has identified, and changed when possible, areas of improvement. Treasury has also reviewed and updated templates within banking applications, ensuring that routine banking transactions are performed in a more controlled and efficient manner. Treasury has also reviewed all assigned roles and permissions of all Treasury systems in production and continues to make modifications based on best practices. Treasury will continue its work in this area and will develop policies and procedures that will ensure proper role assignment and monitoring based on established procedures. Treasury should have this issue resolved by March 31, 2016.

FDM and DoIT, in consultation with Treasury, implemented a solution to remediate a security concern identified by Treasury in 2009 and the financial audit in 2013. The solution essentially encrypts the accounts payable files upon creation in NHFirst and it automates the retrieval and decryption process by MHC, the application utilized for transferring the payment files to the banking applications used by our banking partners. With this implementation, Treasury believes the risks previously identified have been mitigated, and therefore, this component of the audit observation is considered resolved.

All data backups are now maintained both locally and offsite. Treasury has implemented virtual servers maintained by DoIT that include new data backup and restore capabilities. Treasury performs two types of external backups, a Disk-to-Disk backup and a directory synchronization to a different virtual server located at DoIT. This component of the audit observation is considered resolved.

Treasury began updating its Continuity of Operations Plan (COOP) in April of 2015. Business functions within Treasury had the opportunity to re-evaluate essential functions and records of each operation. Treasury is currently in the process of compiling the updates and it is planning on testing certain elements of the COOP during the September-October timeframe. Treasury understands this is an ongoing effort; however, it intends to have a new updated COOP document by the end of October of 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:

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 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. 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. This observation remains 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 which support the yearly issuance of new General Obligation Bonds undergo many iterations before they are finalized, as they reflect actual and projected capital expenditures on authorized 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 is a manual process and may transpire over a period of 18 months due to bond proceed arbitrage rebate rules established in the Internal Revenue Code. For this reason, Treasury strives to include as much actual expenditure activity as possible from 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.

With the implementation of the Capital Projects application, a new functionality within the NHFirst - Activities Module, this process will be significantly enhanced as certain components of the process are now automated, allowing for more accurate and timely reporting of current and historical information. Treasury will have the opportunity to verify the benefits of this application during the next scheduled bond issuance. This observation is deemed substantially resolved.

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 communicated with banking and investment partners to ensure such changes were implemented. 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 segregated trust and agency account responsibilities as much as possible and has enhanced procedures mitigating some of the risks identified in the audit observations. For example, as explained in the response to observation No. 9, Treasury implemented procedures to

ensure only authorized individuals have the ability to direct Treasury's actions while in custody of trusts and custodial accounts. Another example is all the records prepared by the Senior Treasury Analyst are reviewed and reconciled by other staff within Treasury, as well as the oversight provided by the respective trustees and fund administrators. However, Treasury continues to believe the administration of these accounts will improve when the accounting of trust and custodial account transactions, currently maintained off-books via spreadsheets, is migrated to the State's accounting system (NHFirst). As a result, on April 20, 2015, Treasury revisited the topic of migrating these accounts to NHFirst and had a meeting with the State Comptroller to discuss it. The results of the meeting indicated it is possible to migrate all the accounting to NHFirst; unfortunately, this project is on hold until resources become available in the Comptroller's office.

Treasury will continue to pursue this initiative and renew discussions with the Comptroller's office on a periodic basis. Treasury expects to have a plan for implementation by March 31, 2016. This observation remains partially resolved.

<p><i>Observation No. 8</i> <i>Improve Record-Keeping For Trust And Agency Accounts</i></p>

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 serves as 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 continue discussions with the Comptroller's office regarding the possibility of transferring the books and records of the trust and agency accounts to NHFirst.

Treasury presently administers this function through the use of spreadsheets, and using NHFirst for this function would eliminate duplication of records and potential risks associated with recording accounting transactions in spreadsheets. Treasury expects to have a plan for implementation by March 31, 2016. This observation remains unresolved.

<p><i>Observation No. 9</i> <i>Maintain Listing Of Authorized Initiators Of Trust And Agency Account Transactions</i></p>

The audit report noted that Treasury's controls over the initiation of trust and agency account transactions did not include ensuring that 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, Treasury compiled a list of individuals who are authorized to direct routine transactions. In addition, 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. This observation remains 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:

Treasury continues to have conversations with the State agency that has historically benefited from the Laconia State School trust funds regarding the use of the trust fund money. Since the Laconia State School is no longer in existence, Treasury is awaiting final guidance provided by the Attorney General’s Office as to the proper use of these funds. Treasury is not currently fulfilling any requests until there is clarity of the purpose and ownership of these funds.

After performing extensive research, Treasury has received final guidance from NH Department of Labor (“NH DOL”) legal counsel indicating that the Crown Paper Workers Compensation fund has to remain open until all potential claims have been received or until potential claimants no longer exist. As a result, Treasury has instituted a procedure where annual confirmation will be obtained from NH DOL indicating whether or not the account should remain open. This portion of the observation is deemed resolved.

Treasury received final guidance from the Attorney General’s Office indicating that the interest earned on Financial Responsibility funds, which are monies held in a custodial capacity, belong to Treasury and thus should be deposited in the general fund. Treasury is still validating records maintained with those retained by the Division of Motor Vehicles to ensure an accurate amount is remitted to the general fund. This portion of the observation is deemed substantially resolved and final resolution is anticipated by March of 2016.

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:

Treasury’s procedure is to review, in collaboration with Administrative Services, the nature and authority of any new accounts assigned to Treasury for its custody in order to determine how the funds should be reported in the CAFR. Beginning in the fall of 2014, Treasury incorporated into

its year-end procedures a review and reconciliation between the trust and agency account reports included in the unaudited CAFR and Treasury's records to ensure they are accurately reported and in accordance with the established criteria, as well as consistent with prior years. This observation remains 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:

Treasury continues to file timely 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.

Treasury continues to file its Annual Report in accordance with the requirements of RSA 11:5-b,II. This observation remains 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:

Treasury has arranged for a sponsor from the House Ways and Means Committee to file legislation in the 2016 legislative session to amend the statutes referred to in the audit observation: RSA 261:97-b, relative to the administration of the Conservation Number Plate Trust fund and RSA 227-M:7-a, relative to the administration of the Land and Community Heritage Investment Program Administrative fund. Treasury anticipates these statutory changes will occur before July of 2016.

This observation remains partially resolved.