

**STATE OF NEW HAMPSHIRE**

**STATE TREASURY**

**PROGRESS REPORT ON AUDIT FINDINGS  
PURSUANT TO EXECUTIVE ORDER 2014-03**

**SEPTEMBER 21, 2018**



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

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**Observation No. 1***Improve Compliance With Federal Treasury-State Agreement*

The audit report identified that 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:**

Efforts to ensure ongoing compliance with the federal Cash Management requirement continue. State Treasury, as the New Hampshire Agency responsible for representing the State in the U.S. Treasury-State Agreement, oversees coordination of the federal cash management requirements included in the TSA and provides the necessary support to Grant Administrators directly responsible for the management and compliance of federal programs. State Treasury also remains in contact with the Federal Grants and Cost Allocation Administrator within the Comptroller's Office, who coordinates and manages all aspects of federal program activity.

With the purpose of improving communications between State Treasury and State Agencies, in 2015 Treasury began publishing the yearly TSA documents on the State's Intranet site "*Sunspot*". The TSA contains relevant compliance information such as allowed funding techniques, clearance patterns, and other significant components of the federal Cash Management requirement pertaining to major federal programs. Therefore, this observation, as it pertains to State Treasury, remains resolved.

**Observation No. 2***Review And Improve Controls Over Information Technology Systems*

The audit report noted that 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:**

1. Following the audit, State Treasury implemented an Agency-wide policy to review, monitor, and update all system accesses at least once every year. Treasury also performed a complete inventory of systems and third-party web-based applications and sites routinely accessed by Treasury employees to ensure Treasury's and state-wide IT policies are being followed. In addition, through Treasury's risk assessment process, Treasury continues to evaluate all aspects of online banking access/functionality and has recently implemented several fraud-prevention procedures to further mitigate the risk associated with online banking system access. Lastly, Treasury retired a legacy debt management system and replaced it with a commercial off-the-shelf application software. This application contains embedded authentication and other system controls not previously available in the legacy system.
2. 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 encrypts the accounts payable files upon creation in NHFirst and automates the retrieval and decryption process by MHC, the application utilized for transferring the payment files to the banking applications used by financial institutions.
3. All data backups are maintained off-site. Treasury has implemented Virtual Servers supported by DoIT that include data backup and restore capabilities. The backup cycle is *incremental* – Monday through Saturday, *full back up* – Sunday, and *monthly* – last business day in a month. The backups are retained for 18 months. Hosted Microsoft Exchange databases are backed up daily by a third-party vendor.
4. State Treasury updates its Continuity of Operations Plan (“COOP”) at least once per year and submits a copy of its COOP update to Homeland Security and Emergency Management (HSEM) to remain off-site and assist the State in the development of the State's Continuity of Government Plan. As part of Treasury's ongoing testing program, on August 15, 2018, Treasury management temporarily relocated to the Public Utilities Commission, Treasury's *Primary Alternate Location* identified in the COOP, to perform continuity of operations tests, training, and exercises as prescribed in State Treasury's COOP.

Ongoing monitoring of controls in place will continue. This observation remains resolved.

***Observation No. 3***

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

This observation stated that “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 mitigated the vulnerability causing the errors prior to the audit report issuance on March 21, 2014. This observation remains resolved.

***Observation No. 4***

***Maintain Accurate Information On All State-Guaranteed Debt***

This observation indicated that 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 identify and properly disclose in its comprehensive annual financial report (“CAFR”) dated June 30, 2014, the full measure of contingent obligations resulting from guarantees extended to quasi-government entities, 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, and 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 that 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 issuance of new General Obligation Bonds, undergo many iterations before they are finalized, as they reflect actual (bondable) and projected capital expenditures on authorized capital appropriations. Once finalized, the project list is included in the Bond Closing Documents of each bond issuance.

During the timetable for the required expenditure of bond proceeds, general funded projects that do not spend as much or as quickly as anticipated must 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 bondable expenditure activity as possible for 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. The allocation of bond proceeds and the establishment of debt service schedules for projects funded with non-general funds (“other funds”) are also based on agency budgets, which are typically enacted one or two years prior to a bond issuance. When agencies are developing their budgets, they typically consult with Treasury to request one or more estimated amortization schedules based on different assumptions in order to determine how much to budget for debt service payments. This exercise assists in the allocation of bond proceeds and total debt assigned to State agencies and programs.

During the last two years, Treasury has had the opportunity to evaluate a module within NH First with the goal of more easily identifying and compiling bondable and projected capital expenditures prior to a bond issue in an automated and integrated manner. Unfortunately, this NHFirst module has not been able to provide the benefits initially anticipated, therefore spreadsheets continue to be the best tool for tracking and compiling capital expenditures. Treasury will continue to explore other software applications that could automate and improve the current manual process. Treasury believes this observation remains resolved.

***Observation No. 6***

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

The audit report noted 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 of the omission by the auditors. 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. Review of information and inventory of accounts is now performed annually. This observation remains resolved.

***Observation No. 7***

*Improve Segregation Of Duties For Trust And Agency Funds*

The audit reported that 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 strengthened procedures in order to mitigate some of the risks identified in the audit observations. For example, as noted in the response to observation No. 9, Treasury implemented procedures to ensure that only authorized individuals have the ability to direct Treasury's actions while in custody of trusts and custodial accounts. Another example is that all of the records prepared by the Senior Treasury Analyst are now reviewed and reconciled by other staff within Treasury, in addition to the oversight provided by the respective trustees and fund administrators. However, Treasury believes the administration of these accounts will improve once the accounting of trust and custodial account transactions, currently maintained off-books via spreadsheets, is migrated to NHFirst. Reference response to Observation No. 8 below. This observation remains partially resolved.

<p><b><i>Observation No. 8</i></b> <i>Improve Record-Keeping For Trust And Agency Accounts</i></p>
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The audit reported that 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 NHFirst.

**Current Status:**

Treasury has custody of over 40 trust and custodial accounts and is responsible for maintaining related accounting records. Trust and custodial accounting records have been maintained off-books via spreadsheets and Treasury seeks to automate this process in the near future by migrating the accounting records from spreadsheets to NHFirst, the State's general ledger system, which is administered by the Comptroller's Office. Multiple benefits would be realized if trust and custodial accounting records were transferred to NHFirst: stronger internal controls over financial reporting of trust and custodial accounts, duplication of records and multiple data-entry would be eliminated, risks associated with recording accounting transactions in spreadsheets could be mitigated, etc.

Treasury has received initial guidance from the Comptroller's Office, however, also impacting this observation is the recent issuance of GASB statement No. 84, Fiduciary Activities, which clarifies the accounting and reporting treatment of fiduciary funds. This pronouncement may change the way in which certain trust and custodial accounts will be reported in the CAFR. Therefore, in collaboration with the Comptroller's Office, Treasury will need to perform a thorough evaluation of each trust and custodial account in order to comply with GASB requirements. Consequently, this effort will also facilitate the future migration of these accounts to NHFirst.

This observation remains unresolved.



***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 that the individuals requesting the transactions have the proper authority to direct the receipt or expenditure of funds within the accounts.

**Current Status:**

As a result of the audit in 2013, Treasury updated its procedures over trust and custodial accounts; periodic reviews are now being conducted. In the fall of 2014, Treasury compiled a list of individuals who are authorized to direct routine transactions on behalf of the Trust and Account Administrators. In addition, as part of its biennial review, Custodial Account Agreements were updated to identify the individuals who are authorized to conduct financial transactions on behalf of the Trust and Account Administrators. This observation remains 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:**

- On July 5, 2017, the Division of Community Based Care Services ("DCBCS"), as administrator of the Laconia State School Trust Funds, filed a petition for Cy Pres seeking court approval to direct the funds from the trust to a charitable purpose that would fulfill, as closely as possible, the general charitable intent of the donors. On March 9, 2018, the 6<sup>th</sup> Circuit Court Judge approved the Cy Pres petition to allow the use of trust funds for the benefit of "former residents" of the Laconia State School, such that when no former residents are living and there is any trust corpus remaining, the funds could be used to benefit individuals receiving services from the State's developmental services system.

DCBCS has developed procedures in accordance with the court judgement and will begin submitting distribution requests to State Treasury. Now that the purpose of the trust has been redefined, Treasury will resume disbursing funds to eligible payees in accordance with the new procedures and court-approved judgment.

- After performing extensive research, Treasury has received final guidance from NH Department of Labor ("NH DOL") legal counsel directing that the Crown Paper Workers Compensation fund must remain open until all potential claims have been received or until potential claimants no longer exist. Therefore, Treasury has instituted a procedure by which annual confirmation is obtained from NH DOL indicating whether or not the account should remain open.

- Treasury received final guidance from the Attorney General’s Office directing that the interest earned on Financial Responsibility funds, which are monies held in a custodial capacity, belong to Treasury and thus should be credited to the general fund. Treasury began transferring interest earned to the general fund in 2016 and has done so annually each June.

This observation is now resolved.

<p><b><i>Observation No. 11</i></b> <i>Review Trust And Agency Financial Information In State CAFR For Proper Presentation</i></p>
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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 follows a comprehensive process to not only determine the proper reporting of Trust and Custodial account information reported in the State’s financial statements, but to determine how the accounts should be administered. Treasury begins tracking proposed legislation as soon as bills are introduced. Once it is determined State Treasury will be involved in the administration of new accounts, Treasury performs an initial evaluation of whether the account will be considered a Dedicated Account, Trust, or Custodial account. If accounts are assigned to Treasury by other means, Treasury performs a similar evaluation, in collaboration with other State Agencies (i.e. Administrative Services, Attorney General, etc.), in order to determine how the funds should be administered and ultimately reported in the CAFR. Beginning in the fall of 2014, Treasury incorporated into its year-end procedures a review and reconciliation procedure between Trust and Custodial (Agency) account information included in the unaudited CAFR and Treasury’s records to ensure that financial transactions are being reported accurately, in accordance with established criteria, and consistent with prior years. This observation remains resolved.

<p><b><i>Observation No. 12</i></b> <i>File Report Of Information Required By Statute</i></p>
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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 Legislative 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:**

[Chapter 61, Laws of 2016](#), legislation requested by the State Treasurer, amended 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. This observation is fully resolved.