



OFFICE OF THE STATE TREASURER  
LYNN FITCH  
TREASURER

February 12, 2013

Honorable Stacey Pickering  
State Auditor  
State of Mississippi  
8<sup>th</sup> Floor, Woolfolk Building  
Jackson, Mississippi 39201

Subject: Financial Audit Findings

Dear Mr. Pickering:

We have reviewed the financial audit findings in reference to our fiscal year 2012 audit. Listed below are our responses and plan for corrective action:

Audit Finding:	Investment Ratios Should be Maintained in Accordance with State Law
Response:	We do not concur with the audit finding. We fundamentally disagree with the application of the 50 percent limitation to certain Agency securities.
Corrective Action:	Under the conservatorship put in place on September 7, 2008 FNMA and FHLMC are being run by the Federal Housing Finance Agency. The US Treasury's actions on September 7 <sup>th</sup> included the institution of Preferred Stock Purchase Agreements, which are the foundation of the direct financial support of the US government to the agencies. The Treasury secretary's speech highlighted the additional security and clarity that these agreements provide to debt holders of FNMA and FHLMC. There were other steps that provided additional security to the debt holders through the provision of greater market stability, but the Purchase Agreements are, in our view, the most important and direct source of financial support. Because FNMA and FHLMC are congressionally chartered, only Congress can effect a permanent change in the status of the companies – either making them entirely public or entirely private. That is a matter that has yet to be

determined. Reform will likely occur in some form over the next couple of years, and we will see what ultimately becomes of FNMA and FHLMC. The point put forth by Treasury is that what we know today is that the debt is for all intents and purposes fully supported by the US government, and therefore the debt of FNMA and FHLMC held in the portfolio should not be included in the 50 percent calculation. There is not an explicit legal guarantee, and there will not be – partly because of the balance sheet effects on the US as a whole and partly because of the congressional charters of these companies, to say nothing of the precedent set by the US assuming a public/private entity's debt. The net result of the conservatorship is financial support of the companies, which includes support to pay its debt obligations and amounts to a guarantee from the federal government on the debt.

Treasury does not believe it is in the best interests of the taxpayers to liquidate FNMA and FHLMC holdings in favor of Treasuries to lower the allocation to Agencies due to the large losses in income to the portfolio that would result from such a rebalancing. The allocation to FNMA and FHLMC securities does not represent additional risk vis-à-vis Treasuries to the State or the taxpayers but does offer meaningfully higher yields. As FNMA and FHLMC holdings mature and/or are called, US Treasury holdings will be added to the portfolio as market rates and pricing are compelling compared to prevailing market rates of securities of similar maturities.

Audit Finding: Perform comparisons between the Transmittal Sheet BFC Total and the Daily Cash Receipt Register

Response: We concur with this finding.

Corrective Action: The verification of the BFC total per the Transmittal sheet to the Daily Cash Receipt Register total was performed visually from April 2012 through August 9. At that time, we initiated the physical placement of a tick mark to provide evidence of review on the report and an explanation of any differences.

Audit Findings: Review employee approval levels in the Statewide Automated Accounting System

Response: We concur with this finding.

Corrective Action: The Office of the State Treasurer has evaluated the employee approval levels for cash receipts, disbursements and journal vouchers in the Statewide Automated Accounting System, and has taken corrective action to ensure that duties are adequately segregated. We have assigned responsibilities to ensure that no individual has the ability to initiate and approve a transaction. In addition,

the signers on the documents do not have the authority to initiate the transactions. These measures should mitigate our risks and ensure transactions are recorded properly and promptly.

Audit Finding: Strengthen controls over replacement of checks with forged endorsements

Response: We concur with this finding.

Corrective Action: Due to personnel changes, the responsibilities of this control were not delegated to new personnel. When this oversight was brought to our attention, we assigned personnel the authority to review and approve the issuance of the replacement check for forged checks. The review and approval will be evidenced by the authorized signature on the "Approval for Treasurer's Check Issuance" form.

Audit Finding: Strengthen controls over the issuance of checks for pay warrants

Response: We concur with this finding.

Corrective Action: We reviewed the instances in which there were no authorized signatures on the "Approved for Issuance of Check" line on the last page of the Daily Bank Reconciliation (DBR) and determined agency oversight. The person generating the DBR will ensure it is signed by the reviewer before giving it to the Cash Management and Investment Division. We have also taken steps to ensure adequate review of the DBR and comparison to the warrant reports from the banks with evidence thereof, before issuance of the checks.

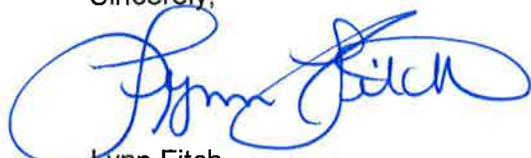
Audit Finding: Strengthen controls over electronic bank account access

Response: We concur with this finding.

Corrective Action: In early January 2012, we presented to each of the banks a new signature card and list of employees that were allowed access to the accounts. Although this particular bank was not specifically instructed to remove the name of the former employee, common banking practice calls for all parties to sign new cards, meaning all old signatures become obsolete. It is apparent to us that the bank realized this oversight when they responded to OSA's audit confirmation inquiry in July 2012. In the future, when signature cards are updated for employee resignations, we will send a letter with the signature card informing the banks of the names to be removed.

If you have any question, please call Laura Jackson, Deputy Treasurer at 359-3600.

Sincerely,

A handwritten signature in blue ink, appearing to read "Lynn Fitch". The signature is fluid and cursive, with a large initial "L" and a stylized "F".

Lynn Fitch  
State Treasurer