STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
STACEY E. PICKERING
AUDITOR

March 20, 2015

Financial Audit Management Report

Honorable Lynn Fitch, State Treasurer
Office of the State Treasurer
P.O. Box 138
Jackson, MS 39205

Dear Ms. Fitch:

Enclosed for your review are the financial audit findings for the Office of the State Treasurer for the Fiscal Year 2014. In these findings, the Auditor's Office recommends the Office of the State Treasurer:

1. Maintain investment ratios in accordance with state law;
2. Strengthen controls over review of taxes receivable classifications;
3. Strengthen controls over arbitrage calculations; and
4. Review employee approval levels in the statewide automated accounting system.

Please review the recommendations and submit a plan to implement them by April 6, 2015. The enclosed findings contain more information about our recommendations.

During future engagements, we may review the findings in this management report to ensure procedures have been initiated to address these findings.

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the Office of the State Treasurer's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Office of the State Treasurer's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. However, this report is a matter of public record and its distribution is not limited.

I hope you find our recommendations enable the Office of the State Treasurer to carry out its mission more efficiently. I appreciate the cooperation and courtesy extended by the officials and employees of the Office of the State Treasurer throughout the audit. If you have any questions or need more information, please contact me.

Sincerely,

Patrick Dendy, CPA
Director, Department of Audit
Enclosures

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FINANCIAL AUDIT MANAGEMENT REPORT

The Office of the State Auditor has completed its audit of selected accounts included on the financial statements of the Office of the State Treasurer for the year ended June 30, 2014. These financial statements are consolidated into the State of Mississippi's *Comprehensive Annual Financial Report*. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. The Office of the State Auditor's staff members participating in this engagement included Amy Buller, CPA, Donna Parmegiani, CPA, Camden Baird, CPA, Kyle Goldman, CPA, Elaina Smith, and Kelly Holtsinger.

Our procedures and tests cannot and do not provide absolute assurance that all state legal requirements have been met. In accordance with Section 7-7-211, Miss. Code Ann. (1972), the Office of the State Auditor, when deemed necessary, may conduct additional procedures and tests of transactions for this or other fiscal years to ensure compliance with legal requirements.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Office of the State Treasurer's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion of the effectiveness of the Office of the State Treasurer's internal control. Accordingly, we do not express an opinion on the effectiveness of the Office of the State Treasury's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify a deficiency in internal control, listed in this letter as item 14-01 that we consider to be a significant deficiency.

In addition, we noted certain control deficiencies involving internal control that require the attention of management. These matters are listed under the heading **OTHER CONTROL DEFICIENCIES** as items 14-02 and 14-03.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether selected accounts included on the financial statements of the Office of the State Treasurer are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance

with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion.

The results of our tests disclosed an instance of noncompliance or other matter that is required to be reported under *Government Auditing Standards*. This matter is identified in this letter as item 2014-004.

Finding Number **Finding and Recommendation**

MATERIAL NONCOMPLIANCE

2014-004 Investment Ratios Should Be Maintained in Accordance with State Law

Finding:

Section 27-105-33, Miss. Code Ann. (1972) establishes guidelines for use in the maintenance of the State's investment pool portfolio. The law also states that at no time shall funds invested in United States Government agency, United States Government instrumentality, or United States Government sponsored enterprise obligations exceed 50 percent of all monies invested with maturities 30 days or longer. Testwork at the Office of the State Treasurer revealed the total of United States Government agency, instrumentality, and government sponsored enterprise obligations exceeded 50 percent of total investments for 12 of the 12 dates selected for testwork (one per month). The actual investment percentages for dates tested ranged from approximately 77 to 84 percent, resulting in investments in U.S. Government agency, instrumentality, and government sponsored enterprise obligations of approximately $697 million to approximately $938 million in excess of statutory limits. Failure to maintain investment ratios in the State's investment pool portfolio within the required percentages resulted in violation of state law.

Recommendation:

We recommend the Office of the State Treasurer ensure the State's investment pool be maintained in accordance with Section 27-105-33 d. (iii), Miss. Code Ann. (1972). Agency personnel should periodically review the investment pool portfolio for compliance with state law and adjust the portfolio if required. This review should be documented as evidenced by the signature and date of the reviewer.

SIGNIFICANT DEFICIENCY

14-01 Controls Should Be Strengthened Over Review of Taxes Receivable Classifications

Finding:

In the GAAP reporting package prepared for fund 9171, each line item on the Untransferred Collections and Accounts Receivable schedule is manually assigned a receivable type. During our review of the GAAP reporting package for fund 9171, we noted that significant account 3769-40150 Motor Vehicle Ad Valorem Tax Reduction Sales Tax was classified as Other Tax Receivable (#12250) by Treasury; the account should have been classified as Sales Tax Receivable (#12200). The total amount misclassified was $13,118,079. An audit adjustment was proposed by the auditors and accepted by management to properly state the receivable accounts on the financial statements.

Good internal controls require that a supervisory review of the GAAP package be performed before submission. The misclassification resulted in an understatement of Sales Tax Receivable and an overstatement of Other Tax Receivable on the financial statements.

Recommendation:

We recommend the Office of the State Treasurer strengthen controls to ensure a review is performed of the classification of taxes receivable prior to GAAP package submission to ensure the classification of the tax types receivable is correct.

OTHER CONTROL FINDINGS

14-02 Controls Should Be Strengthened Over Arbitrage Calculations

Finding:

Per Internal Revenue Service (IRS) guidance on the instructions for form 8038-T (arbitrage rebates), issuers must pay arbitrage rebates in installments for computation dates that occur at least once every 5 years. Rebate payments are due within 60 days after each computation date. The final rebate payment for an issue is due within 60 days after the issue is discharged. During testwork on arbitrage at the Office of the State Treasurer, it was noted that the agency had not prepared an arbitrage calculation for three bond issues within the timeframe specified by the IRS. The agency did send information to a third party to prepare the calculation for the bond issues after notification by the auditor. The calculations revealed there was no arbitrage payment due. It was also noted that for one bond issue there was no indication of supervisory

review of the data sent to the third party for use in calculating arbitrage. Further, there was one bond issue where the data sent to the arbitrage attorney related to the bond arbitrage calculation did not agree to the supporting information. Failure to ensure arbitrage calculations are prepared, and rebates submitted, within the timeframe specified by the IRS could result penalties being charged and/or loss of tax exempt status for the bond issue. Failure to ensure a supervisory review for accuracy of the data sent for use in preparing the arbitrage calculation could result in an incorrect arbitrage calculation, and subsequently, incorrect information being filed with the IRS.

Recommendation:

We recommend that the Office of the State Treasurer strengthen controls to ensure all bonds are monitored for the timing of arbitrage calculations and rebate submissions, and that those calculations and rebate submissions occur timely, in accordance with the Internal Revenue Service regulations.

14-03 A Review Should Be Performed of Employee Approval Levels in the Statewide Automated Accounting System (SAAS)

Finding:

We performed testwork on the employee approval levels in the Statewide Automated Accounting System (SAAS) for all four quarters of State fiscal year 2014 at the Office of the State Treasurer. In the first three quarters, one employee had the ability to enter transactions and apply all levels of approval for disbursements (DISB security code), revenues (REV security code) and journal vouchers (J2 and JRVC security codes). In the first quarter, nine employees had the ability to enter and apply all levels of approval for revenues (REV security code). In the second and fourth quarters, eight employees had the ability to enter and apply all levels of approval for revenues (REV security code). In the third quarter, seven employees had the ability to enter and apply all levels of approval for revenues (REV security code).

Good internal controls require duties to be segregated so one individual does not have the ability to initiate, authorize and record a transaction. Failure to ensure segregation of duties could allow unauthorized or erroneous transactions to be recorded in SAAS and not be detected promptly.

Recommendation:

We recommend the Office of the State Treasurer review employee approval levels in the Statewide Automated Accounting System (SAAS)

to ensure duties are properly segregated and no one individual is assigned both input capability and all levels of agency approval.

End of Report