STATE OF NEW HAMPSHIRE
STATE TREASURY

FINANCIAL AND COMPLIANCE
AUDIT REPORT
FOR THE FISCAL YEAR ENDED
JUNE 30, 2005

STATE OF NEW HAMPSHIRE
STATE TREASURY

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STATE OF NEW HAMPSHIRE
STATE TREASURY

Reporting Entity And Scope

The reporting entity of this audit and audit report is the New Hampshire State Treasury (State Treasury or Treasury) as of and for the fiscal year ended June 30, 2005, excluding the custody and escheat of unclaimed and abandoned property pursuant to RSA 471-C.

Organization

The Treasury operates under the executive direction of the State Treasurer, a constitutional officer elected biennially by a joint ballot of the Senate and House of Representatives. Assisting, and appointed by the Treasurer, is a chief deputy treasurer, a deputy treasurer, and two assistant treasurers, all of whom are unclassified State employees. The Treasury also employed 17 classified employees at June 30, 2005.

Responsibilities

The Treasury's primary responsibility as provided in RSAs 6, 6-A, 6-B, 6-C, and 11, is the management of the State's cash, investments, debt, and trust funds, as detailed below. The Treasury is also responsible for the abandoned property program as provided in RSA 471-C.

Cash Management

The Treasurer serves as custodian over the State's receipt of funds and is responsible for the payment of all State operating expenses. RSA 6:7 establishes the State's policy for depositing public monies. Part 2, Article 56 of the New Hampshire State Constitution requires all payments made from the Treasury, except debt obligations, to be authorized by warrant under the hand of the Governor, with the advice and consent of the Executive Council.

Investment Management

The Treasury is responsible for maximizing the return on State funds while considering cash flows and liquidity requirements. The Treasury invests funds, above those necessary to meet operating expenses, in instruments set forth in RSA 6:8, including:

- Obligations of the U.S. government;
- All types of savings accounts; and
- Certificates of deposit of State or federally chartered banking institutions within New Hampshire.

Debt Management

The Treasury is responsible for developing long-term debt plans, tracking the status of the State's debt, and making debt service payments on all State bonds and notes.

In accordance with RSA 6:13, the Treasury is authorized to borrow on the State's credit, under the direction of the Governor and Council, such sums as may be necessary when it is anticipated that there will not be sufficient general funds to meet current obligations. The total of this temporary borrowing for the General Fund may not exceed $200 million. There were no temporary borrowings outstanding at June 30, 2005.

Bonds may be issued, when authorized by the Governor and Council, for specified projects or purposes. Bonds are not issued after every statutory authorization. Instead, the Treasury monitors the status of capital projects and then issues bonds to cover several authorizations. Except for revenue bonds, such borrowing usually constitutes general obligation debt of the State. The total balance of general obligation bonds issued for governmental activities outstanding at June 30, 2005 was approximately $690.2 million.

Fiduciary Funds

In accordance with RSA 11:1, all trust funds left to and accepted by the State shall be in the custody of the State Treasurer. The Treasury holds these funds as agency funds for other State government units and invests the funds as directed by those government units.

Funding

The financial activity of the Treasury is accounted for in the Governmental and Fiduciary Funds of the State. A summary of the Treasury's General Fund and Capital Projects Fund revenues and expenditures for the fiscal year ended June 30, 2005 is shown in the following schedule.

Summary Of Revenues And Expenditures
Fiscal Year Ended June 30, 2005

	General Fund	Capital Projects Fund	Total Governmental Funds
Total Revenues	$ 7,209,713	$ -0-	$ 7,209,713
Total Expenditures	$ 196,057,492	$ 3,525,884	$ 199,583,376
Excess (Deficiency) Of Revenues Over (Under) Expenditures	$ (188,847,779)	$ (3,525,884)	$ (192,373,663)

Prior Audit

The most recent prior financial and compliance audit of the Treasury was for the fiscal year ended June 30, 2002. The appendix to this report on page 61 contains a summary of the current status of the observations contained in that report. Copies of the prior audit report can be obtained from the Office of Legislative Budget Assistant, Audit Division, 107 North Main Street, State House Room 102, Concord, NH 03301-4906.

Audit Objectives And Scope

The primary objective of our audit is to express an opinion on the fairness of the presentation of the financial statements of the Treasury for the fiscal year ended June 30, 2005. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we considered the effectiveness of the internal controls in place at the Treasury and tested the Treasury's compliance with certain provisions of applicable State laws, rules, and contracts. Major accounts or areas subject to our examination included, but were not limited to, the following:

- Revenues,
- Expenditures,
- Cash and investments,
- Long-term debt,
- Contingent liabilities, and
- Fiduciary Funds

Our report on internal control over financial reporting and on compliance and other matters, our report on management issues, the related observations and recommendations, our independent auditor's report, and the financial statements of the Treasury are contained in the report that follows.

Auditor's Report On Internal Control Over Financial Reporting And On Compliance And Other Matters

To The Fiscal Committee Of The General Court:

We have audited the accompanying financial statements of the governmental activities and each fund of the New Hampshire State Treasury as of and for the fiscal year ended June 30, 2005, as listed in the table of contents and have issued our report thereon dated February 27, 2006, which was qualified with respect to the lack of presentation of the financial position of the Treasury in the government-wide and governmental fund financial statements. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Treasury's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Treasury's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in Observations No. 1 through No. 16 of this report.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that none of the reportable conditions described above is a material weakness.

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the Treasury's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, rules, 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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*. However, we noted certain matters which are described in Observations No. 17 through No. 19 of this report.

We noted certain other management issues, which are described in Observations No. 20 and No. 21, which we reported to management of the Treasury in a separate letter dated February 27, 2006.

This auditor's report on internal control over financial reporting and on compliance and other matters is intended solely for the information and use of the management of the Treasury and the Fiscal Committee of the General Court and is not intended to be and should not be used by anyone other than these specified parties.

Office Of Legislative Budget Assistant
Office Of Legislative Budget Assistant

February 27, 2006

Internal Control Comments
Reportable Conditions

Observation No. 1: Business Continuity Plan Should Be Established

Observation:

The Treasury does not have a documented disaster recovery and business continuity plan.

The objectives of a Treasury disaster recovery and business continuity plan would be to minimize financial loss to the State; to continue to serve its customers and financial market partners; and to mitigate the negative effects disruptions can have on the State's and the Treasury's strategic plans, reputation, operations, liquidity, credit quality, and ability to remain in compliance with applicable laws and regulations.

A disaster recovery and business continuity plan documents the strategies, essential resources, and plans and procedures necessary to implement a recovery from an unplanned business interruption. A well-designed disaster recovery and business continuity plan is essential to mitigate losses and allow for the continuity of operations with minimal interruptions, should an unplanned future event or occurrence make continued operation using the Treasury's headquarters or systems, or the systems of its critical business partners, problematic. Plans should be tested regularly to provide reasonable confidence of the continuity of operations in the event of a disaster.

Recommendation:

The Treasury should establish a business continuity plan.

Once a plan is established, the Treasury will need to regularly test the plan to ensure that it remains viable to the Treasury's operations and that the Treasury employees remain trained in the application of the plan.

Auditee Response:

We concur in part. The Treasury Business Continuity Plan (Plan) is currently being developed and a significant number of deliverables have already been completed and their related actions implemented. These deliverables include:

1. Comprehensive development work plan.
2. Plan policy, objectives, scope and plan assumptions.
3. Assessment of all potential business interruptions.
4. Analysis of the impacts of potential business interruption events.
5. Proactive and reactive strategies to both mitigate and respond to business interruptions with several key strategies already implemented.
6. Detailed Treasury business functions and processes have been identified and documented.
7. Assessment and analysis requirements of business functions and processes have been defined and are being applied.

Since Treasury is a relatively small agency with a heavy reliance on other agencies for shared infrastructure and facilities (i.e. physical plant, central information technology (IT) and communications services), and has limited resources available, certain Plan strategies have been defined but are dependent on other agencies or will need to be phased in as resources permit. For example:

1. Certain IT-related strategies have already been implemented while others will be implemented in FY 2007, or as financial resources become available (see Observation No. 2).
2. Certain staff training-related strategies are dependent on the availability of scheduled classes provided by the Bureau of Education and Training in FY 2007.
3. Certain other strategies that have been evaluated will not be implemented until such time as the business impacts of the Enterprise Resource Planning system (ERP) are better understood by Treasury.

Other strategies, typical of a business continuity plan, are outside the scope of the Treasury's Plan due to its dependence on other agencies to provide those services. Examples of this dependence are the first response and emergency management, recovery of a crisis or disaster event, the disaster recovery planning for centralized IT and communications processing, and physical security of Treasury staff and the office environment.

The Treasury believes that a robust Business Continuity Plan is a continual "work in progress" and must be continually revised in light of changing business conditions and business processes. Treasury intends, therefore, not only to continue to complete and roll-out the currently planned deliverables, as identified in the development work plan, but will need to continually re-evaluate deliverables of the work plan that have already been completed.

Observation No. 2: Controls Over Information Technology Systems Should Be Improved

Observation:

Weaknesses exist in the Treasury's information technology (IT) operations that place the Treasury's IT systems at risk.

1. There is no off-site storage of the backup copies of the Treasury IT system,
2. Comprehensive system documentation does not exist outside of the system,
3. Physical access to all of the Treasury's IT systems is not adequately restricted,
4. Change controls for changes to employee access to the systems are informal. Employee access levels are not regularly reviewed for continued appropriateness.

Weak IT controls increase the risk that unplanned events could seriously disrupt Treasury and State operations.

Recommendation:

The Treasury, as part of its business continuity planning efforts discussed in Observation No. 1, should improve its controls over its IT systems.

1. System backup tapes should be stored offsite. System backup tapes should also be regularly restored to ensure that the backups remain a useable control.
2. System documentation should be improved. Printed documentation should be maintained of significant systems and functions. Copies of the documentation should be maintained offsite to be available even if the Treasury offices are inaccessible.
3. Physical access to all critical aspects of the Treasury's IT systems should be limited to authorized employees. Only employees with job responsibilities for the maintenance and operation of the systems should have physical access to the systems.
4. Change controls over the assignment of employee access to the Treasury's IT systems should be formalized and include a regular management review of employee access. Employees' right to use the Treasury systems and information should be restricted to the access required for current job responsibilities.

Auditee Response:

1. *Concur in Part.* Options for data tape storage do not exist in the State in the form of a standard contract through either the Department of Administrative Services (DAS) or the Office of Information Technology (OIT) with any internal or 3rd parties to offer data tape storage services. If we are to fully address this observation we will need to establish a contract with a 3rd party vendor for these services. We have identified this as an issue, which will need to be addressed within our business continuity plan (see Observation No. 1). We are now actively seeking options for offsite data storage, and if the budget allows will implement a solution to this issue in State fiscal year 2007.
2. *Concur.* In general we have begun to take overall steps today to improve documentation of systems and processes that Treasury IT performs or maintains. These systems and processes will change as Enterprise Resource Planning (ERP) implementation progresses. Offsite documentation options have been identified and will be incorporated into our business continuity plan (see Observation No. 1). Treasury considers its steps to address this issue to be a "work in progress" and cannot offer a firm date by which this will be resolved due to the relatively small size of the Agency and its limited financial resources.
3. *Concur in part*. During the recent period of major renovations to Treasury's office space in the State House Annex, the server cabinet, in which computer hardware was stored under lock and key, has been moved from Treasury's location on the first floor of the State House Annex to the basement of the same building into a shared access computer room. This area provides additional physical security but does not allow for us to monitor the access to this room as closely as we could when it was on the first floor, since this room is shared with personnel from OIT and the Department of Administrative Services. The server cabinet remains under lock and key, therefore physical access is and was restricted with regard to this cabinet. In addition, there are, of course, specific password protected login codes, which allows only identified Treasury employees access to the hardware. Treasury does not believe that the server's "physical" access is at risk of compromise. While there could be more improvements to physical security we are confident that the system security features are strong enough to outweigh the cost associated with the minor incremental benefit of investing in those physical security improvements.
4. *Concur in part.* Treasury has now put in place a more formal process for requesting changes to any system that allows us to track these changes as well as who has requested them through a web based online Request\Helpdesk system. This new system has been implemented and is in use today. Changes around access in the banking systems are now all

requested to information technology staff through the Treasurer or Chief Deputy Treasurer. There will also be a process established for the management reports to review access permissions for the web banking applications.

Observation No. 3: Investment Accounts Should Be Reconciled Monthly

Observation:

The Treasury does not perform formal reconciliations between its records of investment account balances and activities maintained in its internal banking system (TROLS) and similar information contained on the monthly account statements from the financial institutions holding the investments. While some of the Treasury investment accounts are certificates of deposits and other investment devices with little or no monthly activity, some of the investment accounts may have daily transfer activity. Accounts with relatively large amounts of activity are generally more prone to undetected error or fraud.

Monthly reconciliations between a department's records and a financial institution's records are an essential control to detect errors and/or frauds in the department's or financial institution's records in a timely manner. These reconciliations should be reviewed and approved by management to ensure that reconciliations are done correctly and timely. The controls at the financial institutions should not be relied upon in lieu of Treasury controls.

Recommendation:

The Treasury should perform formal monthly reconciliations between its internal record of investment account balances and financial activity with the monthly account statements from the financial institutions. The monthly reconciliations should be performed by an employee independent of other responsibilities with the investment accounts (performing, approving/authorizing and posting transactions), and should be reviewed and approved by management to ensure the reconciliations are complete, timely, and accurate.

Auditee Response:

Concur.

Observation No. 4: Coordination With Bureau Of Financial Reporting Should Be Improved

Observation:

Difficulties experienced in identifying, classifying, and reporting State cash and investment accounts at fiscal year end indicate the need for increased coordination of efforts between the Treasury and the Department of Administrative Services, Bureau of Financial Reporting (BFR).

The BFR relies upon the Treasury to provide information on the State's cash and investment accounts in order for the BFR to accurately report those accounts in the State's comprehensive annual financial report (CAFR). Annually, the Treasury provides the BFR with information necessary for this reporting. Complicating this process for fiscal year 2005 was a change in financial reporting standards, which revised the disclosure reporting for cash and investment accounts. The Treasury was required to capture and report new and additional information to BFR to allow the State to meet the new financial reporting standard. A lack of understanding and experience with the requirements of the new reporting standard appeared to cause additional problems with the Treasury's reporting, as inconsistencies were noted in the Treasury's and BFR's reporting of certain investment accounts.

Recommendation:

The Treasury should continue to work with the BFR to establish appropriate criteria and other relevant policies and procedures for proper identification and classification of State cash and investment information for State financial reporting purposes.

Auditee Response:

Concur. We have and will continue to work closely with the Department of Administrative Services, Bureau of Financial Reporting to make sure that the fiscal year end closing process is as efficient as possible.

Observation No. 5: Transactions Initiated By Service Providers Should Be Subject To Review

Observation:

The Treasury makes interest and principal payments on certain variable rate bonds without reviewing the invoice for accuracy.

The Treasury issued $5 million of variable rate bonds in 2001 to fund a State pension obligation. The bonds were private placement bonds sold to a single commercial bank. The Treasury makes interest payments on these bonds semiannually and principal payments annually. Because the bonds are variable rate bonds, the semiannual interest payment amount is periodically redetermined, based on an agreed-to formula. Each time a payment is due, the bondholder bank calculates the interest payment due and notifies the Treasury. Although the Treasury reportedly spot-checked the calculation when the bonds were first issued, during fiscal year 2005, the payments were not subject to a Treasury recalculation. The bank withdraws the payment from a Treasury account at the bank when due and the Treasury records the transaction in its books, when it is notified that the payment has been taken.

Relying on the bondholder to determine the amount that is owed, without reviewing the amount for accuracy, presents a risk that the Treasury could be charged inaccurate amounts without detecting the error.

Recommendation:

The Treasury should review all payments for accuracy. The Treasury should not accept service provider determinations of amounts owed without subjecting the amount to a reasonable review and approval control process. To be an effective control, all review and approval processes should be documented.

Auditee Response:

Concur. We do review invoices for accuracy prior to making payments. In this particular case, while we do not perform a detailed calculation we do check for the reasonableness of the interest payment, which is admittedly not represented by any person's initials on the documentation.

Observation No. 6: Contracts And Significant Service Provider Agreements Should Be Subject To Improved Controls

Observation:

The Treasury has not formalized its operating agreements with its bond counsel or provided a system to account for its operating agreements with the financial institutions it transacts business with.

The Treasury operates with the assistance of outside service providers including an investment advisor, bond counsel, and numerous banks. Some of these services are subject to formal contracts and others, such as banking services, are subject to documented agreements that outline conditions of services provided but are not considered by the Treasury to be contract documents requiring formal approvals.

- During fiscal year 2005, the Treasury paid $164,000 for bond counsel services without the benefit of a contract to explain and document the scope and other particulars of the services provided. The relationship between the Treasury and bond counsel is longstanding. It is unclear whether services provided by the bond counsel were ever subject to a contract.
- Financial institutions providing service to the Treasury, for the most part, do so without the benefit and controls provided by a formal contract document. The Treasury does establish documented agreements with some of its banks outlining specifics of the services to be provided by the banks. However, the Treasury does not maintain a central depository of the account agreements making it difficult for the Treasury to provide a complete listing of the agreements covering its accounts.

While it can be argued that formal contracts limit an organization's ability to actively manage and bargain the delivery of services from among several providers, contracts also provide controls including standards of performance and certainty of service price and availability.

Recommendation:

The Treasury should establish policies and procedures regarding its use of contracts and agreements to support purchased services. The policies and procedures should include guidance on determining when a service requires the control provided by approved contract documents and when a service is adequately supported by less-formal account agreements.

- The Treasury should evidence its significant business agreements with formal contracts. The contracts should detail the significant aspects of the agreements including performance requirements and other terms that form the basis for the services to be provided to the Treasury and Treasury's responsibility to the vendor.
- The Treasury should establish a system to centrally accumulate and archive account agreements to provide for their efficient management and to make referral to the account agreements efficient and a practical component of the Treasury's control system.

Auditee Response:

We concur. With the sole exception of Bond Counsel, all significant business services arrangements are covered by formal contracts which are periodically competitively bid through a formal Request-For-Proposal (RFP) process. An RFP for Bond Counsel services has been developed, reviewed by the Attorney General's office, and is expected to be sent out later in State fiscal year 2007.

With respect to arrangements with financial institutions (i.e. banks), Treasury does have agreements in place for certain critical and specialized services which focus on unique transaction processes and the timing of such transactions. As stated in the LBA observation, Treasury does not have an effective system for recording and organizing these agreements but has started to improve upon this weakness.

Observation No. 7: Segregation Of Duties Controls Should Be Implemented

Observation:

A number of important Treasury transactions are not subject to an effective review and approval control process as no one with the requisite knowledge documents an independent review and approval of these certain transactions.

- When a new bond is issued, the Chief Deputy Treasurer prepares debt-funding schedules, which include the funding source for each bonded project. A Treasury employee inputs the bond issue transaction from the debt funding schedules into the State's accounting system (NHIFS) debt subsystem and prints out the NHIFS Funding Source Status Report, which summarizes the information entered. The report is reviewed by the Chief Deputy Treasurer to ensure the transactions were input correctly, however the review is not documented. No knowledgeable Treasury employee reviews the accuracy of the debt funding schedules used as a source for the input.
- When a bond is refunded, the Chief Deputy Treasurer notes the required revisions on the paper copy of the original bond payment schedule and the changes are entered into the Debt Management System. The revised schedules are subsequently reviewed by the Chief Deputy Treasurer to ensure that all noted changes were entered correctly. No knowledgeable Treasury employee reviews the accuracy of the revisions made to the debt payment schedules used as the source for the input.

- Financial transactions related to the New Hampshire and Maine Interstate Bridge Authority are performed by the Chief Deputy Treasurer and are not subject to a documented review and approval process.
- The Treasurer prepares a zero-coupon bond schedule annually for use in the compilation of the debt maturity footnote of the State's comprehensive annual financial report (CAFR). The spreadsheet, developed by the Treasurer for this purpose, tracks future zero coupon bond principal and interest payments based on individual bond debt schedules derived from the Treasury's Debt Management System. Several discrepancies were noted in amounts reported on the schedule for fiscal year 2005. While the schedule agreed in total to supporting documentation, the breakdown of principal and interest by fund (i.e. General, Highway, and Self-Supporting) was incorrect.
  - Upon review, the Treasurer determined the discrepancies were a result of an incorrect formula used in the spreadsheet supporting the schedule, and one supporting debt schedule that was entered incorrectly. The spreadsheet has been used for several years and the error had not previously been detected.

While the Treasury reports that the transactions recorded by the Chief Deputy Treasurer and the Treasurer are subject to each other's review, the review is not a required procedure and there is no documentation maintained to indicate whether the review occurs.

Recommendation:

All significant Treasury transactions should be subject to an effective review and approval control process, including transactions prepared by the Treasury's management-level employees.

To be most effective, review and approval functions should be documented to evidence timely completion.

Auditee Response:

We concur in part. There are a number of controls currently in place for the procedures described in the observation. We have already and will continue to review more closely the existing controls to see if there are additional steps that can be taken to improve them.

Observation No. 8: Segregation Of Duties Over Certain Trust And Agency Funds Should Be Improved

Observation:

A lack of segregation of responsibilities exists in the Treasury's processing of certain trust and agency fund transactions.

One Treasury employee is primarily responsible for incompatible functions related to certain trust and agency funds maintained by the Treasury including: opening the mail, restrictively endorsing checks, record keeping, preparing individual fund statements and financial statements for each fund, purchasing and redeeming investments, and reconciling the investment account statements to respective Treasury records. The reconciliations prepared by the employee are not subject to a Treasury review and approval control to ensure the reconciliations are properly and timely performed.

The fundamental purpose of segregating functions is to protect the integrity of the system by ensuring that no one employee has such exclusive control to permit, intentionally or unintentionally, errors or irregularities to remain undetected. In general, there are three principal groups of incompatible duties that must be segregated for proper internal controls: 1) authorization; 2) custody of assets; and 3) recording of transactions. For example, those who handle cash should not have the authority to prepare checks, should not have access to accounting records, and should not be involved in reconciling transactions. (Source: State of N.H., Internal Controls Tool Kit, October 1995).

The lack of segregation of duties over certain trust and agency funds at the Treasury could allow errors, frauds, or other matters, intentional or unintentional, to occur and not be detected in a timely manner.

Recommendation:

The Treasury should segregate employee responsibilities over the incompatible trust and agency fund functions. For example:

- The initial receipt, recording, and endorsing of checks should be segregated from the account record keeping responsibilities,
- The reconciliation of the investment accounts should be segregated from the record keeping responsibilities, and
- The reconciliations should be reviewed and approved by someone independent of the reconciliation process.

Auditee Response:

We concur in part. There are a number of controls in place for the procedures described in the observation. We have already and will continue to review more closely the existing controls to see if there are additional steps that can be taken to improve them. One of the fundamental constraints of the current financial system is that there is no module or platform in which to maintain the records of trust and agency accounts. Our hope is that the new Enterprise Resource Planning system will allow for the capability to maintain this type of data and allow us to more formally address the observation beyond the controls we have in place today.

Observation No. 9: Communications Related To Contingent Debt Should Be Improved

Observation:

Lack of communication between the Treasury, local governments, and the New Hampshire Municipal Bond Bank has contributed to inaccurate Treasury information related to the State's liability for contingent debt.

Per RSA's 485-A:7, 195-C:2, 33:3-f, 481:19 and 149-M:31, the State can provide a guarantee for certain debt issued by municipalities and school districts to fund projects for purposes defined by the respective statutes. In the event the municipality or school district defaults on the bond obligations, the State becomes contingently liable for the debt. The statutes establish the State's total guarantee limit for each type of covered debt. It is important that the State is aware of how much debt is outstanding under each RSA so that the guarantee limit is not exceeded.

The Treasury's Contingent Liability Report is not periodically updated to reflect changes in municipal and school debt caused by refunding or other events after the initial issuance of the debt. Confirmation of contingent debt as part of the fiscal year 2005 audit revealed two debt issues that were listed as having State guarantees that actually had been refunded or advance funded prior to fiscal year 2005. These debt issues were inaccurately reported on the Treasury's Contingent Liability Report as having a State guarantee.

Recommendation:

The Treasury should improve its communications with the Municipal Bond Bank and the local governments to ensure that the Treasury becomes aware of changes to debt issues subject to the State's guarantee in a timely manner. The Treasury should periodically remind its partners in this process of the need to timely inform the Treasury of changes in debt issues covered by the State's guarantee and the Treasury should periodically confirm with its partners the amounts of guaranteed debt outstanding.

Auditee Response:

We concur in part. An increased volume and quality of communication with those entities described in the observation would be positive. On the other hand, as part of the audit process the Treasury specifically asked the LBA to conduct a 100% confirmation of all contingent debt, since we had a suspicion that there could be discrepancies between what we were recording for guaranteed debt and what municipalities might claim was their guarantee balances. We also asked the LBA to conduct this 100% confirmation of balances as part of the audit since it had been three (3) years since such a process was conducted. The result of the confirmation process was exactly as we had expected. There were, as described in the observation, a number of municipalities that had guaranteed debt which they had refinanced which effectively removed the state's guarantee and resulted in our overstating the exposure for guarantee programs.

Observation No. 10: Coordination Of Responsibilities For Account Maintenance Should Be Improved

Observation:

Although the Treasury's policy is to notify all financial institutions of changes to the list of authorized personnel, the Treasury did not notify the operator of the unclaimed property clearinghouse (Affiliated Computer Services or ACS) of an authorized employee that was no longer employed by the Treasury. While the clearinghouse had submitted annual employee authorization update requests to the Treasury, a lack of coordination between the Treasury and its Abandoned Property Division caused the Treasury to not recognize when it had failed to respond to the requests. The result was that the most current authorized signer information on file at ACS for the Treasury was dated February 2002 and contained the name of a prior Treasury employee.

In order for authorization controls to be effective, the Treasury must ensure that its business partners are provided with accurate and timely information.

Recommendation:

The Treasury should coordinate the responsibility for account maintenance, including the accounts of the Abandoned Property Division. Changes in the employee job responsibilities and employment status affecting authorization controls must be recognized and communicated in a timely manner for controls to remain effective.

Auditee Response:

Concur. An update authorization letter was prepared and delivered to ACS Unclaimed Property Clearinghouse to correct this oversight.

Observation No. 11: Accountability Controls Over Cash Drawers Should Be Improved

Observation:

The accountability controls over the cash drawer used by the Treasury's cashiers are weak.

Cash and checks received at the Treasury are processed by either one of two cashiers. Cash and checks received are recorded and then put into a cash drawer. The two cashiers share one unlocked cash drawer for the temporary accumulation of cash and checks prior to deposit. Because more than one employee uses the cash drawer, the source of any shortage or other error, fraud, or matter in the amounts accumulated may not be determinable.

The amounts accumulated in the cash drawer prior to deposit ranged from $1,000 to $4,000 during the month of June 2005, a representative month.

Recommendation:

The Treasury should review the current cash collection procedures to minimize the risk that employees may become vulnerable to improper assignment of responsibility for shortages or other error, fraud, or matter in the amounts accumulated. If possible, cashiers should be assigned their own locking cash drawer that can establish accountability over cash receipts and protect the employees and the Treasury from improper assignment of responsibility.

Auditee Response:

Concur. We are reviewing this process and will examine our options for addressing this issue.

Observation No. 12: Abandoned Property Procedures Should Be Updated To Reflect Change In Statute And Process

Observation:

The Treasury has not reviewed its administration of the State's abandoned property program to determine whether changes in the State's abandoned property statutes and procedures call for the updating of certain other abandoned property statutes and procedures.

1. A revision to the abandoned property statutes, effective during 1995, allows original owners to claim previously escheated abandoned property. This change in the abandoned property statute eliminates the court-based due-process prerequisite previously required to take property. As a result of the change, significant escheat-related expenses that were incurred for advertising, etc., under the prior court-based process are avoided. However, the Treasury has not reviewed its program to establish whether the Treasury's retention of the statutorily set 15% of the amount to be returned as a deduction for costs (RSA 471-C:30, II) continues to reflect the Treasury's costs to administer the program under the new procedures.
2. Per RSA 471-C:25, II, the Treasury is allowed to deduct any costs incurred in connection with the administration of the abandoned property laws from the amount available for escheat. Under the prior process, property was escheated 24 months after it was presumed abandoned. The majority of the expenses related to the escheatment occurred in the final year of escheatment and the expenses of that second fiscal year were recovered from the property prior to distribution to the counties. Under the new process, property is held 36 months prior to escheatment. The Treasury's expenses related to escheatment no longer occur primarily in the final year but are more or less proportional over the 36-month period the property is held. However, the Treasury continues to net its abandoned property expenses of the second fiscal year period prior to the distribution to the counties.
3. RSA 471-C:25, I directs the Treasury to return any money presumed abandoned that originated from the Highway or Fish and Game Funds to those respective funds. The Treasury has not established any process to identify abandoned property originating in the Highway and Fish and Game Funds.

Per the Treasury, the calculation used to determine the amount of abandoned property to be returned to the counties has been used for a number of years, and the county treasurers have never questioned the propriety of the amount returned to them.

Recommendation:

The Treasury should review its administration of the State's abandoned property program to determine whether changes in the State's abandoned property statutes and procedures call for the updating of certain other abandoned property statutes and procedures. For example, if the 15% cost recovery provided by statute is not supported by current Treasury operations, the Treasury should recommend the statute be revised to provide recovery of actual costs incurred. As administrator of the abandoned property program, the Treasury is responsible for periodically reviewing whether current statutes provide for the most efficient operation of the program and recommending, where appropriate, changes to statutes to improve the program's operations.

Auditee Response:

We concur in part. Treasury acknowledges the responsibility to periodically review RSA 471-C and other applicable statutory provisions in an effort to further the efficient operation of the program and, if deemed appropriate and feasible, suggest changes to such statutes to promote the program's consistency and efficiency, and does so.

With respect to the "numbered" sections of the observations:

1. We concur that a change in statute eliminated the procedure wherein Superior Court approval was required and that related expenses no longer result. Treasury's current escheatment practices and procedures afford full consideration to these and any other applicable statutory changes.
2. We concur Chapter 471-C: 25 allows for the deduction of "any costs incurred in connection with the administration of this chapter" as well as "costs incurred in the effectuation of RSA Chapter 471-C:30…". Treasury does in fact "net abandoned property expenses" from the applicable report year against the fiscal year two (2) years hence. This is consistent with the provisions of Chapter 471-C: 25 and 471-C:30, II.
3. We concur. Treasury will analyze the current uncashed State check process to determine the requirements necessary to comply with this section of the law.

Observation No. 13: Allocation Of Abandoned Property Costs Should Be Based On Cost Analysis

Observation:

The Treasury's allocations of Abandoned Property operating costs related to property reported by in-state holders and out-of-state holders do not appear to reflect the Treasury's actual costs of processing the two classes of abandoned property. The Treasury's current allocation procedures appear to over allocate program costs against the counties' share of the proceeds.

Per RSA 471-C:25, II, before making any deposit to the credit of the general fund or county treasurer as provided in paragraph I, the administrator may deduct any costs incurred in connection with the administration of this chapter. The Treasury's current cost allocation procedure deducts direct out-of-state account costs from the State's share of escheat proceeds and deducts all other costs, including general overhead costs, from the counties' share of the proceeds. The Treasury was unable to describe why it is appropriate to charge all abandoned property costs, other than the costs that are specifically identifiable as out-of-state processing costs, against the counties' share of the proceeds.

A similar comment was included in the fiscal year 1999 Treasury Department, Abandoned Property Division audit report.

Recommendation:

As noted in the 1999 report, the Treasury should develop and implement a reasonable method for allocating abandoned property costs to the State and counties that more accurately reflects the actual costs incurred by the Treasury in processing abandoned property reported by in-state and out-of-state holders. A more accurate allocation of costs, based on an analysis of costs of processing abandoned property of in-state and out-of-state holders, will result in a distribution of proceeds that better reflects the statutory requirements.

Auditee Response:

We concur in part. While the Treasury considers its current cost allocation procedure to be compliant with statute, we do believe that there are a couple of areas of the Abandoned and Unclaimed Property Law (RSA 471-C) such as this one that can lead to different conclusions or opinions about what specific business processes are required to implement the policy set forth by this law. We will consider over the next couple legislative sessions proposing legislation to clarify those sections.

Observation No. 14: Formal Risk Assessment Policies And Procedures Should Be Established

Observation:

The Treasury does not have formal risk assessment policies and procedures in place for recognizing and responding to risks potentially affecting its operations.

Management's assessment of and response to risks facing the organization is an integral component of internal control. The purpose of an entity's risk assessment efforts is to identify, analyze, and where appropriate respond to risks and thereby manage risks that could affect the entity's ability to reach its objectives. Effective risk assessment practices should be a core element of management's planning activities and should be an ongoing activity.

The Treasury does not have formal policies and procedures in place for periodically reviewing its operations for risks that could jeopardize its ability to continue to function as management intends. Currently, when risks are identified, the Treasury may respond with a change in procedure or other action, however, there are no formal policies and procedures to continuously review operations for risks. A lack of understanding of risks generally pushes an entity toward a reactive mode when significant risks are realized or occur. A reactive mode may compromise the efficiency and effectiveness of a response due to the lack of prior identification and understanding of the risks and ramifications.

An entity faces many risks. Risk can be defined as, the threat that an event or action will adversely affect an entity's ability to achieve its objectives. Risk can be classified in many ways. For example:

External risks - threats from broad factors external to the entity including changes in the political arena, statutes and rules, competition from other sources, and illegal activity external to but affecting the organization.

Operational risks - threats from ineffective or inefficient processes for acquiring and providing goods and services, as well as loss of physical, financial, or information assets.

Information risks - threats from the use of poor quality information for operational, financial, or strategic decision-making within the entity and providing misleading information to others.

A continuous review of Treasury processes and activities using a risk-based mindset would promote effective planning and assist in resource allocation decision-making. Risks identified should be analyzed to determine whether current internal controls mitigate risk to a level desired by management or whether other actions are required in response to the risk.

Recommendation:

The Treasury should formalize its risk assessment process. A formal risk assessment process is a necessary tool the Treasury needs to assist in the effective management of risks. Identifying risks significant to Treasury operations and strategies to mitigate those risks should enhance the effectiveness of the Treasury's planning and resource allocation processes and its control processes.

Auditee Response:

We concur in part. Treasury does not have a formal written risk assessment program but is continually assessing risk, primarily the State's financial risk, when evaluating such things as business systems, processes, new banking products and investment and liquidity activities. This assessment program is evidenced by written procedures, assignment of work to insure segregation of responsibilities and with documented investment programs and policies.

It is Treasury's understanding that Administrative Services will be developing a Risk Assessment policy and procedure and, once completed, Treasury will use it as a model to develop its own written policy/procedure.

Observation No. 15: Formal Fraud Risk Mitigation Efforts Should Be Developed And Implemented

Observation:

The Treasury has not established a formal fraud assessment, prevention, deterrence, and detection program and has not established a fraud reporting policy.

Fraud encompasses an array of irregularities and illegal acts characterized by intentional deception. Persons outside or inside the organization can perpetrate it for the benefit or to the detriment of the organization. Fraud runs the spectrum from minor employee theft and unproductive behavior to misappropriation of assets, fraudulent financial reporting, and intentional noncompliance with a law or rule to an undue benefit.

Management is responsible for assessing the risk of fraud and implementing measures to reduce the risks of fraud to an organization. Fraud assessment, prevention, deterrence, and detection are crucial to the controlled operations of an organization.

- Assessment is critical since risks can only be effectively managed if risks are identified.

- Prevention reduces opportunities. Preventative methods are typically part of the organization's internal control – tone at the top and control procedures.
- Deterrence consists of those actions taken to discourage the perpetration of fraud and limit the exposure if fraud does occur. The principal mechanism for deterring fraud is the establishment of effective internal controls. Management has the primary responsibility for establishing and maintaining controls.
- Detection consists of identifying indicators of fraud sufficient to warrant recommending an investigation. These indicators may arise as a result of controls established by management, tests conducted by management or staff, and other sources both within and outside the entity.

Management is responsible for assisting in the deterrence and detection of fraud by examining and evaluating the adequacy and effectiveness of controls, commensurate with the extent of the potential exposure/risk in the various segments of an entity's operations.

The attributes of an effective fraud reporting policy include:

- The policy is in writing;
- The reporting policy describes fraudulent activities and the actions required when fraud is suspected or detected;
- The policy is communicated to all employees; and
- Management obtains written assurance from each employee that the policy and related reporting mechanism is understood.

The effectiveness of a fraud reporting policy is enhanced when employees have a clear understanding of fraud indicators and what constitutes a fraudulent act. It is important that the reporting procedure is non-threatening for the reporter and provides for the reasonable protection of all parties.

Recommendation:

The Treasury should establish formal fraud risk mitigation policies and procedures and perform a fraud risk assessment to help limit the Treasury's exposure to fraud and to promote the timely detection of, and reaction to, fraud and fraud risks.

- The Treasury should establish formal fraud assessment, prevention, deterrence, and detection policies and procedures to help limit the Treasury's exposure to fraud and promote early detection of fraud that might occur. The Treasury should take measures to foster a high degree of control consciousness among its employees and ensure that its employees understand that adhering to controls is a primary concern of management.
- The Treasury should establish fraud reporting policies and procedures and provide its employees with fraud awareness training. The Treasury should take measures to ensure that the policies and procedures facilitate and encourage reporting and protects all parties involved.

Auditee Response:

We concur in part. Treasury does not have a formal written policy regarding fraud prevention, deterrence, detection, and reporting. It is Treasury's understanding, however, that Administrative Services is currently working with the Office of the Attorney General to establish a formal fraud prevention, deterrence and detection policy program. Once this policy is established, Treasury will use it as a model to address its own relevant areas of responsibility and risk.

Treasury does have both written and unwritten processes and procedures, internally and between Treasury and its banking partners, built around sound internal controls to prevent, deter and detect fraud from both external and internal sources. Examples of such procedures are:

1. Segregation of responsibilities within Treasury.
2. Dual Management signatures on disbursements.
3. Bank reconciliations performed by individuals with no receipt or disbursement responsibilities.
4. Use of "Positive Pay" services from banks to prevent payment of fraudulent checks.

Treasury management and staff continually operate within an environment of heightened awareness for the potential of fraud and continually question and evaluate internal control features within existing processes as evidenced by discussions at routine staff meetings, discussions between various Treasury managers and staff.

Treasury staff has clear expectations from the State Treasurer regarding fraud reporting and has not experienced any delays in the reporting of attempted fraudulent activities. The most recent attempted fraud occurred in April, 2006 when banks and certain private citizens began inquiring about suspicious checks. Treasury staff brought this matter to the immediate attention of senior Treasury management who then contacted the Attorney General's office to begin an immediate investigation. Additionally, when performing routine procedures, in place to detect fraud, staff does bring irregularities to the attention to management.

Observation No. 16: Accounting And Reporting Treatment Of The Community Conservation Endowment Fund Should Be Reviewed

Observation:

The Treasury as well as the Department of Administrative Services (DAS) is unclear on the accounting treatment and reporting of the State's Community Conservation Endowment Fund.

Neither the Treasury nor DAS was able to sufficiently define the nature, ownership, and purpose of the Community Conservation Endowment Fund to establish whether the fund is a private-purpose, agency, permanent fund, or other governmental fund type of the State. While deposits have been made to the account, as of June 30, 2005, no expenditures have been made from the account.

The Community Conservation Endowment Fund was classified and reported as an agency fund of the State for the fiscal year ended June 30, 2005. The reported balance in the fund was

$685,050. Based upon discussions with the Treasury and DAS, it is unclear whether the money in this fund supports State programs and activities, which would suggest a fund classification of a governmental fund, or if the fund is held by the State in purely custodial capacity, which would suggest an agency fund classification.

Recommendation:

The Treasury should work with DAS to determine the appropriate accounting and reporting treatment for the Community Conservation Endowment Fund. Once determined, the Treasury should establish policies and procedures for processing account activity including controls over the account appropriate for the classification of the fund.

Auditee Response:

Concur. Treasury will work with DAS to determine the appropriate accounting and reporting treatment for the Community Conservation Endowment Fund.

State Compliance Comments

Observation No. 17: Land and Community Heritage Investment Program Administrative Fund Should Be Created

Observation:

As of June 30, 2005, the Treasury had not established the Land and Community Heritage Investment Program (LCHIP) administrative fund within the office of the Treasury. The Treasury has allowed the N.H. Land and Community Heritage Investment Authority to establish the administrative account outside the office and authority of the Treasury.

RSA 227-M:7-a establishes in the office of the State Treasurer the LCHIP administrative fund into which the Treasurer shall credit any revenue generated pursuant to RSA 261:97-b, I-a and, for the biennium ending June 30, 2007, interest income generated on appropriations made to the LCHIP investment program trust fund.

During fiscal year 2005, the Treasurer transferred the revenue and interest that otherwise would have been deposited to the administrative fund to an administrative checking account held by the N.H. Land and Community Heritage Investment Authority.

Recommendation:

The Treasury should create the LCHIP administrative fund as established by statute. If the Treasury determines that the Treasury and State would be better served if the account continued to be held and administered by the N.H. Land and Community Heritage Authority, The Treasury should seek to have the statute amended as appropriate to provide for that account structure.

Auditee Response:

Concur in part. Treasury will review the existing procedures for making payments to the Land and Community Heritage Authority. As of today, the Authority receives "Moose Plate Revenue" pursuant to RSA 261:97-b, I-a and " interest generated on appropriations" made for LCHIP from the state's general fund. Both these revenue sources are paid to the Authority without being credited to the administrative fund established in RSA 227-M:7-a. Treasury's review of the current process will be to investigate whether there is an effective way to meet the requirement of using the administrative fund while keeping the process as efficient as possible.

Observation No. 18: Clear Language Of Statute Should Be Applied

Observation:

The Treasury distributes abandoned property payments to the General Fund and to the counties based on a fiscal year-end rather than a calendar-year end, as provided in statute. While the Treasury considers that it is complying with the intent of the legislation, it is not complying with the clear language of the statute. This was also a comment in the prior fiscal year 2002 audit of the Treasury.

According to RSA 471-C:30, "Within **36 months after the close of the calendar year** [emphasis added] in which any property presumed abandoned under this chapter is paid or delivered to the administrator, if no claim for the property has been made and established by any person, not including another state, entitled to the property, the administrator shall pay or deliver all such property to the appropriate county treasurer as required under RSA 471-C:31, subject to the state deduction under paragraph II."

Based on a reading of the clear language in the statute, calendar year 2001 abandoned property should have been paid to the counties and General Fund 36 months after the close of the calendar year, or December 31, 2004. However, the 2001 calendar year escheatment occurred six months later on June 27, 2005 in the amount of $2,711,352 to the General Fund and $609,336 to counties.

Recommendation:

The Treasury should comply with the clear language of the statute and make the required abandoned property payments within the 36-month period outlined in the statute. If the Treasury wants to continue making payments using the fiscal year end, it should request the statute be amended to provide for the different payment date.

Auditee Response:

We concur in part. Although existing procedures, as applied, may result in a timing difference with a strict reading of the statutory provisions, there is no noteworthy impact to the general fund or the appropriate county treasurers.

Treasury has processes in place to effectively comply with escheatment provisions of RSA 471-C in a timely manner.

RSA 471-C: 30, I states: "Within 36 months after the close of the calendar year in which any property presumed abandoned under this chapter **is paid or delivered** to the administrator, if no claim for the property has been made and established by any person, not including another state, entitled to the property, the administrator shall pay or deliver all such property to the appropriate county treasurer as required under RSA 471-C:31, subject to the state deduction under paragraph II." **(Emphasis added).**

The Abandoned Property Division receives delivery of properties, not only on or about the statutory deadlines of November 1st and May 1st, but also at varying times throughout the remainder of the year. As the result of the ongoing delivery and receipt of properties the "Report Year", which is the basis of the escheatment process, has been adapted to coincide with the state's fiscal year. Therefore, properties presumed abandoned and delivered are from two (2) different calendar years.

Under current processes the tasks necessary to comply with all escheatment provisions of RSA 471-C are completed and funds are paid or delivered before the June 30th close of each fiscal year.

Treasury believes the current processes are compliant with the legislative intent and the spirit of the applicable law. If there were any impact resulting from timeliness of the payment and/or the availability for use of the funds it would be de minimis.

Federal Compliance Comment

Observation No. 19: Check-Payment Clearance Patterns Should Be Established

Observation:

The Treasury, at June 30, 2005, was not in compliance with Section 7.9 of the federal/State Cash Management Improvement Act (CMIA). As of June 30, 2005, the Treasury had not timely recertified its check-payment clearance patterns, an action required at least every five years by the CMIA.

The Treasury and the U.S. Department of Treasury, Financial Management Service (FMS), enter into a federal treasury-State Agreement (TSA) each State fiscal year in accordance with the Cash Management Improvement Act of 1990, as amended. This agreement defines the terms for the transfer of funds between the Federal government and the State with the objective of minimizing the time between an expenditure occurring and the availability of federal funds to the State to support that expenditure.

Sections 7.1 and 7.9 of the TSA requires the Treasury to develop check-payment clearance patterns and to periodically recertify that the clearance pattern developed by the State accurately corresponds to the clearance activity of the programs to which it is applied. In the TSA, the State agrees to recertify its clearance patterns at least every five years.

The Treasury, as of June 30, 2005, had not developed relevant check-payment clearance patterns for all covered programs. As patterns had not been previously developed, they also had not been recertified, as required by the TSA.

Recommendation:

The Treasury should develop relevant check-payment clearance patterns for expenditures of all CMIA covered programs.

The Treasury, in accordance with the CMIA, should notify the FMS of the Treasury's lack of compliance with the TSA and the Treasury's intended corrective action plan to come into compliance with the TSA.

Auditee Response:

Concur. Treasury has contacted FMS to discuss the update of the check clearance patterns.

Auditor's Report On Management Issues

To The Fiscal Committee Of The General Court:

We have audited the accompanying financial statements of the governmental activities and each fund of the New Hampshire State Treasury as of and for the fiscal year ended June 30, 2005 as listed in the table of contents, and have issued our report thereon dated February 27, 2006, which was qualified with respect to the lack of presentation of the financial position of the Treasury in the government-wide and governmental fund financial statements.

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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

In planning and performing our audit of the financial statements of the Treasury as of and for the fiscal year ended June 30, 2005, we noted issues related to the operation of the Treasury that merit management consideration but do not meet the definition of reportable conditions as defined by the American Institute of Certified Public Accountants, and were not issues of noncompliance with laws, rules, regulations, contracts and grant agreements.

Those issues that we believe are worthy of management consideration but do not meet the criteria of reportable conditions or noncompliance are included in Observations No. 20 and No. 21 of this report.

This auditor's report on management issues is intended solely for the information of the management of the Treasury and the Fiscal Committee of the General Court and is not intended to be and should not be used by anyone other than these specified parties.

Office Of Legislative Budget Assistant
Office Of Legislative Budget Assistant

February 27, 2006

Management Issues Comments

Observation No. 20: Bank Service Fees Could Be Reported Separately From Interest Income

Observation:

The Treasury reports interest income earned on the State's operating account bank accounts net of bank service fees charged for financial activity processed through those accounts. By netting the fees against interest income, the Treasury did not clearly report approximately $682,000 of service fees charged to the State's accounts and understated interest income by the same amount during the fiscal year ended June 30, 2005.

While RSA 6:7-a allows the State Treasurer to pay for the cost of bank services, security transaction fees, and investment management fees from income generated by the Treasury Department, by netting the costs of maintaining the State's operating accounts against interest income, the actual costs incurred in operating the accounts may not be readily apparent and may not receive the attention they warrant.

Recommendation:

The Treasury should consider reporting bank service fees separately from interest income for the State's operating accounts. If the Treasury determines that reporting these accounts gross and not net is appropriate, the Treasury should work with the Department of Administrative Services to establish the most efficient and effective method to account for and report the information.

Auditee Response:

Concur. Treasury will consider reporting bank service fees separately from interest income.

Observation No. 21: Current Status Of Foreign Escheated Estates Account Should Be Reviewed

Observation:

The necessity for the continuation of the Foreign Escheated Estates Account is not clear.

At June 30, 2005, the balance in the Foreign Escheated Estates Account was $222,768. The account has been relatively inactive for a number of years with the only activity in the account being the periodic posting of interest.

Per RSA 561:12-a, the probate courts could defer delivery of an estate to a legatee, etc., when there was a question whether a legatee who lived outside the United States would have the benefit, use, or control of property due him. The provision for the deferral of delivery of property was often used when the legatee, etc., lived in a communist controlled country, generally behind the "iron curtain". The probate courts would order such property converted into available funds and paid to the Treasury to be invested and held subject to further order of the probate court. The Treasury maintains these funds in the Foreign Escheated Estates Trust Fund Account.

This comment was also noted in our audit reports of the Treasury for the years ended June 30, 1999 and 2002. The Treasury's response to the 1999 audit comment was that it would propose changes to RSA 561:12-a in the next [2000] legislative session. The Treasury response to the comment in the 2002 report was that it would contact the various Probate Courts that ordered the Treasury to hold the funds to clarify the status of those funds. Apparently, the Treasury did not act on either response.

Recommendation:

Treasury should contact the appropriate probate courts to clarify the status of the funds and determine whether action could be taken to return the funds to an owner.

Auditee Response:

We concur in part. Treasury is in full compliance with the clear language of the statute which governs foreign escheated estates (RSA 561:12-a) and holds and invests these funds as custodian, as ordered by the Probate Court. The continuation of this account is necessary until such time as the Probate Court orders the release of all funds in the account and the statute is repealed or modified in such a way as to prevent new money from future estates being added to the account.

Treasury has performed a thorough analysis of the account to determine the detailed transaction history and potential ownership of the funds. The funds originated from only 11 estates and were deposited in the account at various times from 1956 through 1989 at the order of Probate Courts of four New Hampshire counties. The amounts of the original deposits from these estates range from less than $1,000 to $45,000. The Probate Courts have ordered the release of funds to heirs three times since the inception of the account, the latest of which was in 2000.

Treasury has also performed an historical review of federal law and practices regarding Presidential powers and economic sanctions leading up to and likely triggering the creation of the New Hampshire statute and has continued this review to the current day. This analysis and historical review has been provided to the Probate Court for review and recommendations. In the opinion of the Probate Court, a change in the statute is not necessary nor is there any need to change any existing process or procedures. Treasury is, however, considering contacting, if possible, the attorney-of-record for one or more of the largest estates to determine if they are worth pursuing. Depending on the outcome of those discussions, Treasury may or may not take additional action.

Independent Auditor's Report

To The Fiscal Committee Of The General Court:

We have audited the accompanying financial statements of the governmental activities and each fund of the New Hampshire State Treasury as of and for the fiscal year ended June 30, 2005, as listed in the table of contents. These financial statements are the responsibility of the Treasury's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 1, the financial statements referred to above are not intended to present the financial position of the Treasury in the government-wide or fund financial statements.

As discussed in Note 1, the financial statements of the New Hampshire State Treasury are intended to present certain financial activity of only that portion of the governmental activities of the State that is attributable to the transactions of the Treasury. They do not purport to, and do not, present fairly the financial position of the State of New Hampshire as of June 30, 2005 and the changes in its financial position for the fiscal year ended June 30, 2005 in conformity with accounting principles generally accepted in the United States of America.

In our opinion, except for the matter referred to in the third paragraph, the financial statements referred to above present fairly, in all material respects, certain financial activity of the governmental activities and each fund of the Treasury for the fiscal year ended June 30, 2005, in conformity with accounting principles generally accepted in the United States of America.

The Treasury has not presented the management's discussion and analysis that the Government Accounting Standards Board has deemed necessary to supplement, although not required to be part of, the basic financial statements.

The Budget to Actual (Non-GAAP Budgetary Basis) Schedule on page 57 is not a required part of the financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consist principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards,* we have also issued a report dated February 27, 2006, on our consideration of the Treasury's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, rules, regulations, contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Office Of Legislative Budget Assistant
Office Of Legislative Budget Assistant

February 27, 2006

STATE OF NEW HAMPSHIRE
STATE TREASURY

STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

Functions/Programs	Expenses	Program Revenues Charges For Services	Net (Expenses) Revenues And Changes In Net Assets
Governmental Activities:			
General Government	$ 120,699,064	$ 123,736	$ (120,575,328)
Interest Expense	26,307,423	-0-	(26,307,423)
Total Governmental Activities	**$147,006,487**	**$ 123,736**	**(146,882,751)**
General Revenues:			
General Fund Appropriations - Net			154,451,801
Interest Income			2,394,064
Abandoned Property			4,056,836
Pease Development Authority - Interest Income			587,070
Other			228,434
Total General Revenues			**161,718,205**
Change In Net Assets			**$ 14,835,454**

The accompanying notes are an integral part of this financial statement.

STATE OF NEW HAMPSHIRE
STATE TREASURY

STATEMENT OF REVENUES AND EXPENDITURES
GOVERNMENTAL FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

	General Fund	Capital Projects Fund	Total Governmental Funds
Revenues			
Abandoned Property	$ 4,056,836	$ -0-	$ 4,056,836
Interest Income	2,394,064	-0-	2,394,064
Pease Development Authority - Interest	587,070	-0-	587,070
Other	171,743	-0-	171,743
Total Revenues	**7,209,713**	**-0-**	**7,209,713**
Expenditures			
Debt Service	78,884,312	-0-	78,884,312
Judicial Retirement	42,800,000	-0-	42,800,000
Rooms And Meals Tax Distribution	42,686,666	-0-	42,686,666
Revenue Sharing	25,216,057	-0-	25,216,057
Administration Costs	3,610,917	-0-	3,610,917
Land Conservation Funds (LCHIP)	2,830,864	-0-	2,830,864
N.H. Housing Finance Authority	-0-	2,500,000	2,500,000
Cost Of Issuing Bonds	28,676	946,924	975,600
Intrastate Energy Pipeline Facility	-0-	78,960	78,960
Total Expenditures	**196,057,492**	**3,525,884**	**199,583,376**
Excess (Deficiency) Of Revenues Over (Under) Expenditures	**(188,847,779)**	**(3,525,884)**	**(192,373,663)**
Other Financing Sources (Uses)			
Net Appropriations	151,048,521	3,403,280	154,451,801
Bond Proceeds/Premium	42,857,823	122,604	42,980,427
Total Other Financing Sources (Uses)	**193,906,344**	**3,525,884**	**197,432,228**
Excess (Deficiency) Of Revenues And Other Financing Sources Over (Under) Expenditures And Other Financing Uses	**$ 5,058,565**	**$ -0-**	**$ 5,058,565**

The accompanying notes are an integral part of this financial statement.

STATE OF NEW HAMPSHIRE
STATE TREASURY

RECONCILIATION OF THE STATEMENT OF REVENUES AND EXPENDITURES - GOVERNMENTAL FUNDS - TO THE STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

Excess (Deficiency) Of Revenues And Other Sources Over (Under) Expenditures And Other Uses		**$ 5,058,565**
Amounts Reported For Governmental Activities In The Statement Of Activities Are Different Because (See Note 1-C):		
Bond Proceeds Provide Current Financial Resources To Governmental Funds, But Issuing Debt Increases Long-Term Liabilities In The Statement Of Net Assets. Repayment Of Bond Principal Is An Expenditure In The Governmental Funds, But The Repayment Reduces Long-Term Liabilities In The Statement Of Net Assets And Therefore Is Not Recognized As An Expense In The Statement Of Activities.		
Bond Proceeds - Judicial Retirement	(42,800,000)	
Repayment Of Bond Principal And Interest	58,592,221	
Accretion Of Bonds Payable	(6,015,332)	9,776,889
Change In Net Assets Of Governmental Activities		**$ 14,835,454**

The accompanying notes are an integral part of this financial statement.

STATE OF NEW HAMPSHIRE
STATE TREASURY

STATEMENT OF FIDUCIARY NET ASSETS
JUNE 30, 2005

	Agency Funds
Assets:	
Cash And Cash Equivalents	$ 10,662,220
Investments, At Fair Value	362,000,303
Total Assets	**$ 372,662,523**
Liabilities:	
Custodial Funds Payable	$ 372,662,523
Total Liabilities	**$ 372,662,523**

The accompanying notes are an integral part of this financial statement.

STATE OF NEW HAMPSHIRE
STATE TREASURY

COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
AGENCY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

	Balance July 1, 2004	Additions	Deletions	Balance June 30, 2005
Nuclear Decommissioning Fund				
Assets:				
Investments	$ 301,285,073	$ 27,469,477	$ 1,768,339	$ 326,986,211
Liabilities:				
Custodial Funds Payable	$ 301,285,073	$ 27,469,477	$ 1,768,339	$ 326,986,211
Seabrook Escrow Accounts				
Assets:				
Cash And Cash Equivalents	$ -0-	$ 2,494,583	$ 700	$ 2,493,883
Liabilities:				
Custodial Funds Payable	$ -0-	$ 2,494,583	$ 700	$ 2,493,883
College Savings Plan Trust				
Assets:				
Investments	$ 7,968,500	$ 7,210,206	$ 261,001	$ 14,917,705
Liabilities:				
Custodial Funds Payable	$ 7,968,500	$ 7,210,206	$ 261,001	$ 14,917,705
Special Fund For Second Injuries				
Assets:				
Cash And Cash Equivalents	$ 5,663,123	$ 9,349,351	$ 7,955,909	$ 7,056,565
Liabilities:				
Custodial Funds Payable	$ 5,663,123	$ 9,349,351	$ 7,955,909	$ 7,056,565
N.H. Hospital Trust Funds				
Assets:				
Investments	$ 5,400,092	$ 445,132	$ 371,050	$ 5,474,174
Liabilities:				
Custodial Funds Payable	$ 5,400,092	$ 445,132	$ 371,050	$ 5,474,174

(continued)

The accompanying notes are an integral part of this financial statement.

STATE OF NEW HAMPSHIRE
STATE TREASURY

COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
AGENCY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

	Balance July 1, 2004	Additions	Deletions	Balance June 30, 2005
Connecticut Lake Headquarters Endowments				
Assets:				
Investments	$ -0-	$ 3,543,674	$ -0-	$ 3,543,674
Liabilities:				
Custodial Funds Payable	$ -0-	$ 3,543,674	$ -0-	$ 3,543,674
Maine - N.H. Interstate Bridge Authority				
Assets:				
Investments	$ 3,422,424	$ 180,008	$ 765,000	$ 2,837,432
Liabilities:				
Custodial Funds Payable	$ 3,422,424	$ 180,008	$ 765,000	$ 2,837,432
Land Conservation Endowment				
Assets:				
Investments	$ 2,415,133	$ 92,464	$ 113,271	$ 2,394,326
Liabilities:				
Custodial Funds Payable	$ 2,415,133	$ 92,464	$ 113,271	$ 2,394,326
Ben Thompson Trust Fund				
Assets:				
Investments	$ 1,369,525	$ 127,542	$ 46,598	$ 1,450,469
Liabilities:				
Custodial Funds Payable	$ 1,369,525	$ 127,542	$ 46,598	$ 1,450,469
Fish And Game Lifetime License				
Assets:				
Investments	$ 1,434,415	$ 179,673	$ 174,930	$ 1,439,158
Liabilities:				
Custodial Funds Payable	$ 1,434,415	$ 179,673	$ 174,930	$ 1,439,158

(continued)

The accompanying notes are an integral part of this financial statement.

STATE OF NEW HAMPSHIRE
STATE TREASURY

COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
AGENCY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

	Balance July 1, 2004	Additions	Deletions	Balance June 30, 2005
Miscellaneous Agency Funds				
Assets:				
Cash And Cash Equivalents	$ 2,686,092	$ 2,571,888	$ 4,146,208	$ 1,111,772
Investments	2,474,033	590,612	107,491	2,957,154
Total Assets	$ 5,160,125	$ 3,162,500	$ 4,253,699	$ 4,068,926
Liabilities:				
Custodial Funds Payable	$ 5,160,125	$ 3,162,500	$ 4,253,699	$ 4,068,926
Total - Agency Funds				
Assets:				
Cash And Cash Equivalents	$ 8,349,215	$ 14,415,822	$ 12,102,817	$ 10,662,220
Investments	325,769,195	39,838,788	3,607,680	362,000,303
Total Assets	$ 334,118,410	$ 54,254,610	$ 15,710,497	$ 372,662,523
Liabilities:				
Custodial Funds Payable	$ 334,118,410	$ 54,254,610	$ 15,710,497	$ 372,662,523

The accompanying notes are an integral part of this financial statement.

STATE OF NEW HAMPSHIRE
STATE TREASURY

NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements of the New Hampshire State Treasury (Treasury) have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and as prescribed by the Governmental Accounting Standards Board (GASB), which is the primary standard-setting body for establishing governmental accounting and financial reporting principles.

A. Financial Reporting Entity

The Treasury is an organization of the primary government of the State of New Hampshire. The accompanying financial statements report the financial activity of the Treasury.

The financial activity of the Treasury is accounted for and reported in the State's General and Capital Projects Funds in the State of New Hampshire's Comprehensive Annual Financial Report (CAFR). Assets, liabilities, and fund balances are reported by fund for the State as a whole in the CAFR. The Treasury, as a department of the primary government, accounts for only a small portion of the General and Capital Projects Funds and those assets, liabilities, and fund balances as reported in the CAFR that are attributable to the Treasury cannot be determined. Accordingly, the accompanying financial statements are not intended to show the financial position or change in fund balances of the Treasury in the General and Capital Projects Funds.

B. Government-Wide And Fund Financial Statements

Government-Wide Financial Statements

The Statement of Activities reports information on the financial activities of the Treasury. As none of the Treasury's activities are business-type, the activities reported in the Statement are all governmental. Business-type activities rely significantly on fees and charges for support. Governmental activities are normally supported through taxes and intergovernmental revenues.

The Statement of Activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include: 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not meeting the definition of program revenues, including resources that are dedicated internally, are reported as general revenues. Certain indirect costs are included in program expenses reported for individual functions.

Fund Financial Statements

Separate financial statements are provided for governmental funds and fiduciary funds, even though the latter are excluded from the government-wide financial statement. The General and Capital Projects Funds are reported as a separate column in the fund financial statement.

C. Measurement Focus And Basis Of Accounting

The government-wide and fiduciary fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay the liabilities of the current period. For this purpose, the State generally considers non-grant revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, expenditures related to debt service, compensated absences, and claims and judgments are recorded only when payment is due.

D. Financial Statement Presentation

The State of New Hampshire and the Treasury use funds to report on their financial position and the results of their operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts. The Treasury reports its financial activity in the funds described below:

<u>Governmental Fund Types:</u>

General Fund: The General Fund accounts for all financial transactions not specifically accounted for in any other fund. All revenues of governmental funds, other than certain designated revenues, are credited to the General Fund. Annual expenditures that are not allocated by law to other funds are charged to the General Fund.

Capital Projects Fund: The Capital Projects Fund is used to account for certain capital improvement appropriations, which are or will be primarily funded by the issuance of State bonds or notes, other than bonds and notes for highway or turnpike purposes, or by the application of certain federal matching grants.

<u>Fiduciary Fund Type:</u>

Agency Funds: The Agency Funds report assets and liabilities for deposits and investments entrusted to the Treasury as an agent for others.

E. Cash Equivalents And Investments

Cash equivalents represent short-term investments with original maturities less than three months from the date acquired by the Treasury. Investments are reported at fair value.

F. Receivables

Receivables in the government-wide financial statement represents amounts due to the Treasury at June 30, recorded as revenue, which will be collected sometime in the future and consist primarily of accrued interest. In the governmental fund financial statements, receivables are primarily for accruals that are received by the Treasury within 60 days after year-end.

G. Capital Assets

Capital assets, which include property, plant, equipment and infrastructure assets, are reported by the State in its CAFR in its government-wide financial statements. Such assets, whether purchased or constructed, are recorded at historical cost or estimated historical cost. Donated capital assets are recorded at estimated fair value at the date of donation. The Treasury's capital assets are reported in Note 3.

Equipment is capitalized when the cost of the individual items exceeds $10,000 and all other capital assets are capitalized when the cost of individual items or project exceeds $100,000. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. Depreciation expense is recognized in the government-wide financial statements. Capital assets are depreciated using the straight-line method over the following useful lives:

Equipment	5 years
Computer Software	5 years
Building Improvements	20 years
Buildings	40 years
Infrastructure	50 years

H. Compensated Absences

All full-time State employees in classified service earn annual and sick leave. At the end of each fiscal year, additional leave (bonus days) may be awarded based on the amount of sick leave taken during the year. Accrued compensatory time, earned for overtime worked, must be taken within one year.

The Treasury's compensated absences liability represents the total liability for the cumulative balance of employees' annual, bonus, compensatory, and sick leave based on the years of service rendered along with the Treasury's share of social security and retirement contributions. The current portion of the leave liability is calculated based on the characteristics of the type of leave and on LIFO (last in first out) basis, which assumes employees use their most recent earned leave first. The accrued liability for annual leave does not exceed the maximum cumulative balance allowed which ranges from 32 to 50 days based on years of service. The accrual for sick leave is made to the extent it's probable that the benefits will result in termination payments rather than be taken as absences due to illness. The liability for compensated absences is recorded in the government-wide financial statement.

In the governmental fund financial statement, liabilities for compensated absences are accrued when they are "due and payable" and recorded in the fund only for employee resignations and retirements that occur before year-end and were paid out after year-end.

I. Encumbrances

Contracts and purchasing commitments are recorded as encumbrances when the contract or purchase order is executed. Upon receipt of goods or services, the encumbrance is liquidated and the expenditure and liability are recorded.

J. Bond Discounts, Premiums, And Issuance Costs

In the government-wide financial statement, bond discounts / premiums and issuance costs are deferred and amortized over the term of the bonds using the straight-line method. Bond issue costs are reported as deferred charges.

In the fund financial statement, governmental fund types recognize bond discounts, premiums, and issuance costs in the period the bond proceeds are received. The face amount of the debt issued is reported as other financing sources. Premiums received on debt issuance are reported as other financing sources while discounts are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds, are reported as expenditures.

K. Revenues And Expenditures/Expenses

In the government-wide Statement of Activities, revenues and expenses are listed by activity type (governmental or business-type). Additionally, revenues are classified between program and general revenues. The Treasury's program revenues consist of charges for services provided. In general, resources not dedicated to a program, as well as resources that are internally dedicated, are reported as general revenues rather than program revenues. The general revenues reported on the Treasury's Statement of Activities include net appropriations and unrestricted revenues. These unrestricted revenues are collected by the Treasury but are not dedicated for use by the Treasury.

In the governmental fund financial statement, revenues and expenditures are reported by source. For budgetary control purposes, revenues are further classified as either "general purpose" or "restricted". General-purpose revenues are available to fund any activity accounted for in the fund. Restricted revenues are, either by State law or by outside restriction, available for only specified purposes. When both general purpose and restricted funds are available for use, it is the State's policy to use restricted resources first.

In the governmental fund financial statement, expenditures are reported by category: "Debt Service", "Rooms And Meals Tax Distribution", "Revenue Sharing", "Administration Costs", etc. Administration costs include such items as salary and benefits, current expenses, and equipment. Debt service includes both interest and principal outlays related to bonds. Capital outlay includes expenditures for real property, infrastructure (e.g. highways), or equipment.

Other Financing Sources – these additions to governmental resources in the fund financial statements result from financing provided by net appropriations and bond proceeds.

L. Interfund And Intra-Agency Transactions

As a general rule, the effect of interfund and intra-agency activity is eliminated from the government-wide statements, with the exception of activities between funds that are reported in different functional categories of governmental activities. Elimination of these activities would distort the direct costs and program revenues for the functions concerned.

M. Budget Control And Reporting

General Budget Policies

The statutes of the State of New Hampshire require the Governor to submit a biennial budget to the Legislature for adoption. This budget, which includes a separate budget for each year of the biennium, consists of three parts: Part I is the Governor's program for meeting all expenditure needs and estimating revenues. There is no constitutional or statutory requirement that the Governor propose, or that the Legislature adopt, a budget that does not resort to borrowing. Part II is a detailed breakdown of the budget at the department level for appropriations to meet the expenditure needs of the government. Part III consists of draft appropriation bills for the appropriations made in the proposed budget.

The operating budget for State agencies, including the Treasury, is prepared principally on a modified cash basis and adopted for the governmental and proprietary fund types with the exception of the Capital Projects Fund. The Capital Projects Fund budget represents individual projects that extend over several fiscal years. Since the Capital Projects Fund comprises appropriations for multi-year projects, it is not included in the budget and actual comparison schedule. Fiduciary funds are not budgeted.

In addition to the enacted biennial operating budget, the Governor may submit to the Legislature supplemental budget requests to meet expenditures during the current biennium. Appropriation transfers can be made within a department without the approval of the Legislature; therefore, the legal level of budgetary control is at the department level.

Both the Executive and Legislative Branches of government maintain additional fiscal control procedures. The Executive Branch, represented by the Commissioner of the Department of Administrative Services, is directed to continually monitor the State's financial operations, needs, and resources, and to maintain an integrated financial accounting system. The Legislative Branch, represented by the Joint Legislative Fiscal Committee, the Joint Legislative Capital Budget Overview Committee, and the Office of Legislative Budget Assistant, monitors compliance with the budget and the effectiveness of budgeted programs.

Unexpended balances of appropriations at year-end will lapse to undesignated fund balance and be available for future appropriations unless they have been encumbered or legally defined as non-lapsing, which means the balances are reported as reservation of fund balance. The balance of unexpended encumbrances is brought forward into the next fiscal year. Capital Projects Fund unencumbered appropriations lapse in two years unless extended or designated as non-lapsing by law.

Contracts and purchasing commitments are recorded as encumbrances when the contract or purchase order is executed. Upon receipt of goods or services, the encumbrance is liquidated and the expenditure and liability are recorded. The Treasury's General Fund unliquidated encumbrance balance at June 30, 2005 was $188,200.

A Budget To Actual (Non-GAAP Budgetary Basis) Schedule - General Fund is included as required supplemental information.

NOTE 2 - CASH, CASH EQUIVALENTS, AND INVESTMENTS

GASB Statement No. 40, *Deposit and Investment Risk Disclosures - an amendment of GASB Statement No. 3* was implemented for the fiscal year ended June 30, 2005. As a result, the disclosures related to deposit and investment risks were changed.

The State pools cash investments except for separate cash and investment accounts maintained in accordance with legal restrictions.

Deposits:

The following statutory requirements and Treasury policies have been adopted to minimize the risk associated with deposits.

RSA 6:7 establishes the policy the Treasurer must adhere to when depositing public monies. Operating funds are invested per investment policies that further define appropriate investment choices and constraints as they apply to those investment types.

Custodial Credit Risk: The custodial risk for deposits is the risk that in the event of a bank failure, the state's deposits may not be recovered.

Custodial credit risk is managed in a variety of ways. Although State law does not require deposits to be collateralized, the Treasurer does utilize such arrangements where prudent and/or cost effective. All banks, where the State has deposits and/or active accounts, are monitored as to their financial health through the services of Veribanc, Inc., a bank rating firm. In addition, ongoing reviews with officials of depository institutions are used to allow for frequent monitoring of custodial credit risk.

All depositories used by the State must be approved at least annually by the Governor and Executive Council. All commercial paper must be from issuers having an A1/P1 rating or better and an AA- or better long-term debt rating from one or more of the nationally recognized rating agencies. Certificates of deposits must be with State or federally chartered banking institutions with a branch in New Hampshire. The institution must have the highest rating as measured by Veribanc, Inc.

Whereas all payments made to the State are to be in U.S. dollars, foreign currency risk is essentially nonexistent on State deposits.

As of June 30, 2005, the state's bank balances were exposed to custodial credit risk as follows:

Deposit Credit Risk
June 30, 2005 (Amounts In Thousands)

	Governmental And Business Type			Fiduciary		
Type	**Insured**	**Collateralized And Held In State's Name**	**Uncollateralized**	**Insured**	**Collateralized And Held In State's Name**	**Uncollateralized**
Demand Deposits	$ 300	$ 35,621	$ 57,747	$ 1,377	$ 1,695	$ 2,173
Money Markets	-0-	30,314	176,573	86	-0-	19,983
Savings Accounts	100	-0-	267	1,515	3,528	-0-
Certificates Of Deposit	-0-	-0-	25,109	68	32	-0-
Totals	**$ 400**	**$ 65,935**	**$ 259,696**	**$ 3,046**	**$ 5,255**	**$ 22,156**

Investments:

The Treasury has adopted policies to ensure reasonable rates of return on investments while minimizing risk factors. Approved investments are defined in statute (RSA 6:8, 387:6, 387:6-a, and 387:14). Additionally, investment guidelines exist for operating funds as well as trust and custodial funds. All investments will be denominated in U.S. dollars. As of June 30, 2005, the State had the following types of investments:

Fair Value Of Investments By Type
June 30, 2005 (Amounts In Thousands)

Investment Type	**Governmental And Business Types**	**Fiduciary**
Repurchase Agreements	$ 100,519	$ -0-
Stocks	23,558	-0-
Corporate Bonds	2,400	26,395
U.S. Treasury	10,701	33,497
U.S. Government Agencies	9,183	9,413
U.S. Government Investment Pools	-0-	329
Municipal Bonds	-0-	29,113
Equity Open Ended Mutual Funds	1,407	237,300
Fixed Income Open Ended Mutual Funds	10,878	2,148
Unemployment Compensation External Pool		
(Special Issue Bonds Guaranteed By U.S. Government)	262,233	-0-
N.H. Public Deposit Investment External Pool	127	243,211
Total	**$ 421,006**	**$ 581,406**

Repurchase Agreements:

Repurchase agreements must be executed through a New Hampshire or Massachusetts bank with assets in excess of $500 million and have either the strongest rating as measured by Veribanc, Inc. or a long term debt rating of AA- or better as rated by Standard and Poor's and Fitch or Aa3 or better as rated by Moody's. Repurchase agreements may also be executed through any of the primary government security dealers as designated by the Federal Reserve.

Custodial Credit Risk: The state's repurchase agreements are all with banking institutions and therefore subject to custodial credit risk. The custodial credit risk is the risk that in the event of a bank failure, the state's deposits might not be recovered.

Interest Rate Risk: The Term Repurchase Agreements are also subject to interest rate risk. Interest rate risk is the risk that changes in interest rates will adversely affect the value of the State's investments. The State measures its interest rate risk by using a weighted average maturity method (WAM). The state's WAM is dollar weighted in terms of years.

As of June 30, 2005 the state's bank balances were exposed to custodial credit risk and interest rate risk as follows.

Investment Risk Exposure
June 30, 2005 (Amount In Thousands)

	Governmental And Business Types	
	Custodial Credit Risk	**Interest Rate Risk**
Investment Type	**Collateralized And Held In The State's Name**	**WAM**
Overnight Repurchase Agreements	$ 91,215	n/a
Term Repurchase Agreements	22,000	0.24
Total	**$ 113,215**	

Stocks:

The State does not have a formal policy relative to operating funds and mitigation of concentration credit risk. Although not issuer specific, individual investment guidelines for trust and custodial funds include overall asset allocation limits that are consistent with sound investment principles and practices.

Concentration Risk: The risk of loss attributed to the magnitude of the State's investment in a single issuer. As of June 30, 2005, the State's total stock investment is $23.6 million. The top ten issuers are noted below:

Governmental And Business Types
Top 10 Stock Investments
June 30, 2005 (Amounts In Thousands)

	Governmental Type				
Name / Issuer	**General Fund***	**Permanent Funds**	**Business Type**	**Total**	**% of Total**
Capital One Finl Corp	$ 394	$ -0-	$ -0-	$ 394	1.67%
General Electric Co	184	-0-	-0-	184	0.78%
Metlife Inc (1)	12,776	66	-0-	12,842	54.52%
Prudential Finl Inc	180	-0-	-0-	180	0.76%
Public Storage Inc	200	-0-	-0-	200	0.85%
TD Banknorth Inc	706	-0-	-0-	706	3.00%
Toronto Dominion Bk Ontario	507	-0-	-0-	507	2.15%
US Bancorp Del	202	-0-	-0-	202	0.86%
Verizon Communications	247	-0-	-0-	247	1.05%
Vodafone Grp	565	-0-	-0-	565	2.40%

* Abandoned Property Account
(1)The state holds Metlife Inc. securities as a result of shares forwarded to the State related to abandoned property.

Custodial Risk: The custodial risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investments that are in the possession of an outside party. All of the State's stocks are uninsured, registered in the State's name, and held by the custodian. Custodial credit quality with respect to investments is mitigated primarily through selection criteria aimed at investing only with high quality institutions where default is extremely unlikely.

Equity Mutual Funds and External Investment Pool:
As of June 30, 2005 the State had $238.7 million invested in open ended equity mutual funds and $243.3 million in an external investment pool.

New Hampshire Public Deposit Investment Pool (NHPDIP):
The NHPDIP was established in accordance with RSA 383:22-24, for the purpose of investing funds of the State of New Hampshire, funds under the custody of all governmental units, pooled risk management programs established pursuant to RSA 5-B, agencies, authorities, commissions, boards, political subdivisions, and other public units within, or instrumentalities of the State of New Hampshire. In accordance with GAAP, the external portion of the NHPDIP is reported as an investment trust fund in the Fiduciary Funds of the State's comprehensive annual financial report using the economic resources measurement focus and accrual basis of accounting. During fiscal year 2005, the State did not have any operating investments in the pool. However, the New Hampshire Hospital Permanent Trust Fund had $0.1 million invested in the pool. NHPDIP audited financial statements can be obtained by contacting NHPDIP at 497 Belknap Mountain Road, Gilford, NH 03249.

Custodial Risk: The custodial risk for investments is the risk that, in the event of the failure of the counterparty to a transaction a government will not be able to recover the value of investments that are in the possession of an outside party. Open ended equity mutual funds and external investment pools are not exposed to custodial credit risk because their existence is not evidenced by securities that exist in physical or book entry form.

Credit Risk: The risk that the issuer or other counterparty will not fulfill its obligations. Neither the equity mutual fund nor the NHPDIP are rated.

Debt Securities: The State invests in several types of debt securities, including corporate and municipal bonds, securities issued by the U.S. Treasury and government agencies, mutual funds, and investment pools.

Credit Risk: The risk that an issuer will not fulfill its obligations. The State invests in grade securities which are defined as those with a grade B or higher. Obligations of the U.S. Government or obligations explicitly guaranteed by the U.S. Government are not considered to have credit risk.

Interest Rate Risk: The risk that changes in interest rates will adversely affect the fair value of the State's investments. Interest rate risk is primarily measured and monitored by defining or limiting the maturity of any investment or weighted average maturity of a group of investments. Fixed income mutual funds that consist of shares of funds that hold diversified portfolios of fixed income securities are limited to those with average maturity not to exceed five years. Trust and custodial funds manage and monitor interest rate risk primarily through a weighted average maturity approach (WAM). The State's WAM is dollar-weighted in terms of years. The specific target or limits of such maturity and percentage allocations are tailored to meet the investment objective(s) and defined in the investment guidelines associated with those funds.

Custodial Credit Risk: The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of the investments that are in the possession of an outside party. Open ended mutual funds and external pools are not exposed to custodial credit risk because their existence is not evidenced by securities that exist in physical or book entry form. The State's selection criteria are aimed at investing only with high quality institutions where default is extremely unlikely.

The State's exposed risks at June 30, 2005 are noted below.

Exposed Investment Risk
June 30, 2005 (Amouts In Thousands)

	Governmental And Business Type			Fiduciary		
Investment Type	**Credit Risk**		**Interest Rate Risk**	**Credit Risk**		**Interest Rate Risk**
	Grade	Unrated	WAM	Grade	Unrated	WAM
Corporate Bonds	$ 2,400	$ -0-	3.47	$ 25,865	$ 530	7.70
U.S. Treasury	10,701	-0-	2.34	33,497	-0-	6.31
U.S. Government Agencies	9,183	-0-	2.73	9,413	-0-	5.41
U.S. Government Investment Pools	-0-	-0-	-	-0-	329	1.37
Municipal Bonds	-0-	-0-	-	29,113	-0-	12.00
Fixed Income Open Ended Mutual Funds	-0-	10,878	5.34	-0-	2,148	5.95
Unemployment Compensation Fund Pool (Special Issue Bonds Guaranteed by U.S. Government)	-0-	262,233	2.20	-0-	-0-	-0-

Concentration Risk: The risk of loss attributed to the magnitude of the State's investment in a single issuer. This risk is applicable to the State's investments in corporate bonds. The State does not have a formal policy relative to operating funds and mitigation of concentration of credit risk. Although not issuer specific, individual investment guidelines for trust and custodial funds include overall asset allocation limits that are consistent with sound investment principles and practices.

The State's top ten issuers at June 30, 2005 are as follows:

Investment Concentration Risk
Top 10 Corporate Bond Issuers
June 30, 2005 (Amounts In Thousands)

	Governmental And Business Types		
Name / Issuer	Fair Value		Percent Of Total
Aflac Inc	$	108	4.51%
Bear Stearns Cos Inc		151	6.30%
Boeing Cap Corp		210	8.75%
CitiGroup Inc		254	10.58%
Dow Chem Co		264	11.00%
FPL Group Cap Inc		111	4.62%
Goldman Sachs Group Inc		111	4.64%
Lehman Bros Hldgs Inc		114	4.75%
National City Bank Cleve		110	4.58%
SBC Communications Inc		108	4.52%
	Fiduciary		
Bank Of America Corp	$	612	2.32%
Chevrontexaco Cap Co		990	3.75%
Citigroup Inc		662	2.51%
Credit Suisse First Boston USA		556	2.11%
General Electric Credit Corp		1,117	4.23%
Gillette Co		988	3.74%
Goldman Sachs Group Inc		1,299	4.92%
Verizon Global Fdg Corp		933	3.54%
Viacom Inc		733	2.78%
Wal Mart Stores Inc		682	2.58%

NOTE 3 - CAPITAL ASSETS AND OTHER EQUIPMENT

The Treasury had no capital assets in fiscal year 2005. The State's Long-Term Assets Policy and Procedures Manual establishes the state's capitalization thresholds. Equipment is capitalized if the original cost is equal to or greater then $10,000. Computer software is capitalized if the cost is equal to or greater than $500,000. For accountability purposes, the State's policy requires departments to account for all long-term assets with a cost equal to or greater than $100 and a useful life of greater than one year. The Treasury's equipment for inventory purposes was as follows:

Inventoriable Equipment
Fiscal Year Ended June 30, 2005

Balance July 1, 2004	Additions	Deletions	Balance June 30, 2005
$ 266,839	$ 23,653	$ 33,395	$ 257,097

NOTE 4 - LONG TERM-DEBT

Bonds Authorized And Unissued: Bonds authorized and unissued amounted to $599.9 million at June 30, 2005. The proceeds of the bonds will be applied to the following funds when issued:

Bonds Authorized And Unissued
June 30, 2005 (Amounts In Thousands)

Capital Projects Fund	$ 128,280
Turnpike System	471,650
Total	**$ 599,930**

Turnpike System: The Legislature has established a 10-year highway construction and reconstruction plan for the Turnpike System to be funded from Turnpike revenues. This legislation also authorized the Governor and Executive Council to issue up to $1.01 billion of bonds to support this project. Through June 30, 2005, the State had issued $395 million of revenue bonds for this project.

Advance Refunding: The following is a summary of general obligation bonds and revenue bonds defeased by the primary government. The proceeds from each advance refunding issue were placed in an irrevocable trust to provide for all future debt service payments on the old bonds.

Accordingly, the trust account assets and the liability for the defeased bonds are not included in the State's financial statements:

Defeased Bonds
June 30, 2005 (Amounts In Thousands)

Date Of Advance Refunding	Amount Outstanding At June 30, 2005
Governmental Fund Types (General Obligation Bonds):	
December 11, 1998	$ 17,145
August 1, 2002	14,910
Subtotal	32,055
Turnpike System (Revenue Bonds):	
January 1991	27,000
Total	$ 59,055

Bond Issues: On December 10, 2004, the State issued $60 million of general obligation capital improvement bonds. The interest rates of these 20-year bonds will be variable per the provisions of their auction rate security (ARS) features. These ARS Bonds are different from past bond issues in that these bonds carry an interest rate that will change every seven days through an auction process specified in the terms of the bonds. A portion of the proceeds from this issue was used to pay off $50 million of bond anticipation notes that were outstanding at June 30, 2004.

On January 19, 2005, the State issued $15 million of general obligation capital improvement bonds. The interest rates on these serial bonds range from 3.0% to 4.25%, and the maturity dates range from 2006 through 2025.

Also on January 19, 2005, the State issued $42.8 million of taxable general obligation bonds to fund the unfunded accrued liability attributable to a newly established retirement plan for State judges pursuant to Chapter 311, Laws of 2003. The interest rates on these serial bonds range from 3.4% to 4.65%, and the maturity dates range from 2006 through 2015.

Changes In Long-Term Liabilities: The following is a summary of the changes in long-term liabilities for bonds and compensated absences during the fiscal year.

Changes In Long-Term Liabilities
Fiscal Year Ended June 30, 2005
(Amounts In Thousands)

Governmental Activities	Beginning Balance	Accretion	Increases	Decreases	Ending Balance	Current	Long-Term
General Obligation Bonds Payable	$ 634,130	$ 6,903	$ 117,800	$ 68,642	$ 690,191	$ 71,150	$ 619,041
Bond Anticipation Notes	50,000	-0-	-0-	50,000	-0-	-0-	-0-
Compensated Absences	83	-0-	58	57	84	23	61
Total Governmental	$ 684,213	$ 6,903	$ 117,858	$ 118,699	$ 690,275	$ 71,173	$ 619,102
Business-Type Activities							
Turnpike System							
General Obligation Bonds	$ 14,362	$ -0-	$ -0-	$ 3,567	$ 10,795	$ 3,682	$ 7,113
Revenue Bonds	305,857	-0-	-0-	11,083	294,774	10,900	283,874
Total Business-Type	$ 320,219	$ -0-	$ -0-	$ 14,650	$ 305,569	$ 14,582	$ 290,987

Bond Anticipation Notes: The State issues bond anticipation notes (BANs) in advance of issuing general obligation bonds. The proceeds are deposited into the capital fund to fund various capital outlay projects. At June 30, 2005, the State had no BANs outstanding.

Capital Appreciation Bonds: Six of the State's general obligation capital improvement bonds issued since November 1990 represent capital appreciation bonds (College Savings Bond Program) with interest being accrued and compounded semiannually. At June 30, 2005, the cumulative interest accretion since issuance for all six capital appreciation bonds is approximately $128.3 million. The interest is not paid until the bonds mature, at which time the expenditure will be recorded.

Debt Maturity: All bonds issued by the State, except for Turnpike revenue bonds, are general obligation bonds, which are backed by the full faith and credit of the State. Interest rates on these issues range from 2.0% to 7.2%. Debt service payments on “self-liquidating” debt are funded by reimbursements from component units for debt issued by the State on their behalf and through user fees and other revenues statutorily earmarked to fund debt service payments on specific projects. The anticipated source of repayment and annual maturities are as follows:

Debt Maturity
June 30, 2005 (Amounts In Thousands)

	SOURCE OF PRINCIPAL PAYMENTS						DEBT SERVICE		
	Governmental Activities				Business-Type Activities		TOTAL ALL FUNDS		
					Turnpike System				
Payable June 30,	General Fund	Highway Fund	Self Liquidating	Total	General Obligation	Revenue	Principal	Interest	Total
2006	$ 60,242	$ 4,941	$ 5,967	$ 71,150	$ 3,682	$ 10,900	$ 85,732	$ 39,947	$ 125,679
2007	56,832	4,937	5,913	67,682	2,644	11,835	82,161	37,151	119,312
2008	55,537	4,604	5,856	65,997	1,509	12,130	79,636	34,060	113,696
2009	55,962	4,622	5,893	66,477	1,474	13,010	80,961	31,212	112,173
2010	52,251	4,406	5,559	62,216	624	13,310	76,150	28,196	104,346
2011-2015	176,788	12,281	19,428	208,497	584	83,025	292,106	101,646	393,752
2016-2020	99,437	5,994	7,130	112,561	-0-	88,675	201,236	50,861	252,097
2021-2025	52,633	2,724	3,242	58,599	-0-	44,095	102,694	16,498	119,192
2026-2030	-0-	-0-	-0-	-0-	-0-	21,410	21,410	2,716	24,126
Subtotal	$ 609,682	$ 44,509	$ 58,988	$ 713,179	$ 10,517	$ 298,390	$ 1,022,086	$ 342,287	$ 1,364,373
Unamortized (Discount) / Premium	(13,584)	(2,746)	(1,381)	(17,711)	278	6,473	(10,960)	-0-	(10,960)
Unamortized Loss on Refunding	(5,277)	-0-	-0-	(5,277)	-0-	(10,089)	(15,366)	-0-	(15,366)
Totals	**$ 590,821**	**$ 41,763**	**$ 57,607**	**$ 690,191**	**$ 10,795**	**$ 294,774**	**$ 995,760**	**$ 342,287**	**$ 1,338,047**

NOTE 5 - EMPLOYEE BENEFIT PLANS

New Hampshire Retirement System

The Treasury, as an organization of the State government, participates in the New Hampshire Retirement System (Plan). The Plan is a contributory defined-benefit plan and covers substantially all full-time employees of the Treasury. The Plan qualifies as a tax-exempt organization under Sections 401 (a) and 501 (a) of the Internal Revenue Code. RSA 100-A established the Plan and the contribution requirements. The Plan, which is a cost-sharing, multiple-employer Public Employees Retirement System (PERS), is divided into two membership groups. Group I consists of State and local employees and teachers. Group II consists of firefighters and police officers. All assets are in a single trust and are available to pay retirement benefits to all members.

Group I members at age 60 qualify for a normal service retirement allowance based on years of creditable service and average final compensation (AFC). The yearly pension amount is 1/60 (1.67%) of AFC multiplied by years of creditable service. AFC is defined as the average of the three highest salary years. At age 65, the yearly pension amount is recalculated at 1/66 (1.5%) of AFC multiplied by years of creditable service. Members in service with ten or more years of creditable service who are between ages 50 and 60 or members in service with at least 20 or more years of service, whose combination of age and service is 70 or more, are entitled to a retirement allowance with appropriate graduated reduction based on years of creditable service.

Group II members who are age 60, or members who are at least age 45 with at least 20 years of creditable service can receive a retirement allowance at a rate of 2.5% of AFC for each year of creditable service, not to exceed 40 years.

All covered Treasury employees are members of Group I.

Members of both groups may qualify for vested deferred allowances, disability allowances, and death benefit allowances subject to meeting various eligibility requirements. Benefits are based on AFC or earnable compensation, service, or both.

The Plan is financed by contributions from the members, the State and local employers, and investment earnings. During the fiscal year ended June 30, 2005, Group I and II members were required to contribute 5% and 9.3%, respectively, of gross earnings. The State funds 100% of the employer cost for all Treasury employees enrolled in the Plan. The annual contribution required to cover any normal cost beyond the employee contribution is determined every two years based on the Plan's actuary.

The Treasury's payments for normal contribution costs for the fiscal year ended June 30, 2005 amounted to 5.9% of the covered payroll for its Group I employees. The Treasury's normal contributions for the fiscal year ended June 30, 2005 were $45,740.

A special account was established by RSA 100-A:16, II (h) for additional benefits. The account is credited with all the earnings of the account assets in the account plus the earnings of the remaining assets of the plan in excess of the assumed rate of return plus 1/2 of 1 percent.

The New Hampshire Retirement System issues a publicly available financial report that may be obtained by writing to them at 54 Regional Drive, Concord, NH 03301or from their web site at http://www.nh.gov/retirement.

Health Insurance For Retired Employees

In addition to providing pension benefits, RSA 21-I:30 specifies that the State provide certain health care benefits for retired employees. These benefits include group hospitalization, hospital medical care, and surgical care. Substantially all of the State's employees who were hired on or before June 30, 2003 may become eligible for these benefits if they reach normal retirement age while working for the State and receive their pensions on a periodic basis rather than a lump sum. During fiscal year 2004, legislation was passed that requires State Group I employees hired on or after July 1, 2003 to have 20 years of State service in order to qualify for health insurance benefits. These and similar benefits for active employees are authorized by RSA 21-I:30 and are provided through the Employee Benefit Risk Management Fund, which is the State's self insurance fund implemented in October 2003 for active State employees and retirees. The State recognizes the cost of providing these benefits on a pay-as-you go basis by paying the actuarially determined contributions into the fund. The N.H. Retirement System's medical premium subsidy for certain Group I and Group II employees also contributes to the fund. The cost of the health benefits for the Treasury's retired employees and spouses is a budgeted amount paid from an appropriation made to the administrative organization of the N.H. Retirement System. Accordingly, the cost of health benefits for retired Treasury employees and spouses is not included in the Treasury's financial statements.

NOTE 6 - CONTINGENT AND LIMITED LIABILITIES

Contingent Liabilities: The State of New Hampshire is contingently liable, within statutory legal limits, for bonds sold by municipalities, school districts, and for first mortgages on industrial and recreational property that contain the guarantee of the State of New Hampshire. The following table shows the composition of the State's $127.8 million of contingent liabilities and the statutory limits as of June 30, 2005.

Contingent Liabilities
June 30, 2005 (Amounts In Thousands)

	RSA	Guarantee Limit		Remaining Capacity	June 30, 2005 Principal	June 30, 2005 Interest	June 30, 2005 Total	June 30, 2004 Total
Water Pollution Bonds	485-A:7	$ 175,000		$ 136,046	$ 31,439	$ 7,515	$ 38,954	$ 48,402
BFA - General Obligation	162-A:17	25,000	**		20,000	10,773	30,773	
BFA - Additional State Guarantee	162-I:9-b	50,000	**		29,473	240	29,713	
BFA - Unified Contingent Credit Limit	162-A:22	95,000	*	34,514	49,473	11,013	60,486	65,197
School Construction Bonds	195-C:2	95,000		67,204	19,705	8,091	27,796	33,164
Solid Waste Bonds	149-M:31	30,000		29,398	475	127	602	693
Super Fund Site Cleanup Bonds	33:3-f	50,000	*	50,000	-0-	-0-	-0-	-0-
Water Resources Council Bonds	481:19	5,000		5,000	-0-	-0-	-0-	-0-
Housing Finance Authority Child Care Loans	204-C:79	300		300	-0-	-0-	-0-	-0-
TOTALS		**$ 450,300**		**$ 322,462**	**$ 101,092**	**$ 26,746**	**$ 127,838**	**$ 147,456**

BFA-Business Finance Authority
*Plus Interest
**Plus interest (guarantee limit under this section is included in and also limited by RSA 162-A:22)

Limited Liabilities With The Pease Development Authority (PDA):
The State has statutory authority to guarantee bonds issued by the PDA, within certain limits, and advance money to the PDA, through both interest and non-interest bearing loans. In addition, RSA 12-G:17 authorizes the issuance of up to $250 million in bonds backed solely by the credit of the PDA. The following table highlights the legal limits of State guarantees and loans relative to the PDA as of June 30, 2005.

Pease Development Authority Loans
June 30, 2005 (Amounts In Thousands)

	(1) RSA 12-G:31	(2) RSA 12-G:34	(3) RSA 12-G:33	(4) RSA 12-G:35
Legal Limit	$ 50,000	$ 5,000	$ 35,000	$ 10,000
Debt Guaranteed By State				
Business Express Airlines *	10,000	-0-	-0-	-0-
Atlantic Coast Airlines	1,000	-0-	-0-	-0-
Amount Bonded By State And Loaned To PDA				
Operating Budget FY92 (V161)	2,800	-0-	-0-	-0-
Operating Budget FY93 (V161)	3,800	-0-	-0-	-0-
Operating Budget FY93 (V165)	1,000	-0-	-0-	-0-
Matching Grants Econ. Dev. (V165)	-0-	5,000		
Lonza (Celltech)	29,990	-0-	-0-	-0-
Remaining Capacity	$ 1,410	$ -0-	$ 35,000	$ 10,000

(1) RSA 12-G:31 - $50 million in bonds may be guaranteed by the State for airport projects or the State can make loans by issuing bonds.

(2) RSA 12-G:34 - $5 million in bonds may be issued and loaned to provide matching grants for FAA and EDA grants.
(3) RSA 12-G:33 - $35 million in bonds may be guaranteed by the State to develop a research district.
(4) RSA 12-G:35 - $10 million in bonds may be issued and loaned to provide matching to private grants for development of research district.

* Business Express Airlines - defaulted on loan, filed for bankruptcy protection under Chapter 11 in fiscal year 1997. State assumed payments on remaining balances, which were paid off and replaced with lower cost State debt.

The State loaned the PDA the proceeds from bond issues V161 ($6.6 million) and V165 ($6.0 million). Currently, the State pays the debt service payments for the bond issues and, when funds are available, PDA will repay the State. As of June 30, 2005, $2.4 million has been paid by the PDA to the State against these bonds. Total principal and interest due at maturity owed by PDA, for these two bonds, is $20.5 million.

Semiannually, the PDA makes payments to the State for the Lonza (Celltech) loans and the State pays the debt service payments. The amount outstanding as of June 30, 2005 relative to the Lonza (Celltech) loans is $25.5 million representing principal of $19.1 million and interest of $6.4 million).

NOTE 7 - SUBSEQUENT EVENTS

On December 6, 2005, the State issued $75 million of general obligation bonds. The interest rates on these serial bonds range from 4.0% to 5%, and the maturity dates range from 2007 through 2025.

STATE OF NEW HAMPSHIRE
STATE TREASURY
REQUIRED SUPPLEMENTARY INFORMATION

BUDGET TO ACTUAL (NON-GAAP BUDGETARY BASIS) SCHEDULE
GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

	Budgeted Amounts		Actual Amounts	Favorable/ (Unfavorable)
	Original	Final	(Budgetary Basis)	Variance- Final
Revenues				
Abandoned Property	$ 3,558,338	$ 3,983,338	$ 4,061,984	$ 78,646
Pease Repayment	1,718,644	1,718,644	1,718,644	-0-
Interest Income	500,000	500,000	1,712,135	1,212,135
Unique Plan Administrative Fees	393,000	393,000	267,391	(125,609)
Other	286,101	286,101	299,721	13,620
Total Revenues	6,456,083	6,881,083	8,059,875	1,178,792
Expenditures				
Debt Service	80,742,986	80,742,986	78,884,312	1,858,674
Judicial Retirement System	825	42,800,825	42,800,000	825
Rooms And Meals Tax Distribution	42,362,080	42,362,080	42,686,666	(324,586)
Revenue Sharing	25,216,057	25,216,057	25,216,057	-0-
Capital Outlays	6,358,056	6,358,056	2,830,864	3,527,192
Administration Costs	3,214,840	4,152,045	3,454,647	697,398
Total Expenditures	157,894,844	201,632,049	195,872,546	5,759,503
Other Financing Sources (Uses)				
Increase In Bonds Authorized	42,800,000	42,800,000	42,800,000	-0-
Excess (Deficiency) Of Revenues And Other Financing Sources (Uses) Over (Under) Expenditures	$ (108,638,761)	$ (151,950,966)	$ (145,012,671)	$ 6,938,295

The accompanying note is an integral part of this schedule.

Note To The Required Supplementary Information - Budgetary Reporting
Fiscal Year Ended June 30, 2005

The Treasury's biennial budget is prepared principally on a modified cash basis and adopted for governmental and proprietary funds. The "actual" results column of the Budget To Actual Schedule is presented on a "budgetary basis" to provide a meaningful comparison to budget.

The budget is composed of the initial operating budget, supplemented by additional appropriations. These additional appropriations and estimated revenues from various sources are authorized by Governor and Council action, annual session laws, and existing statutes which require appropriations under certain circumstances. For reporting purposes, the original budget is equal to the initial operating budget plus any balances brought forward, additional appropriations, and other legally authorized legislative and executive changes made before the beginning of the fiscal year. The final budgeted amount includes the original budget plus supplemental appropriation warrants and transfers made throughout the fiscal year.

The variance column on the Budget To Actual Schedule highlights differences between the final budget and actual revenue and expenditures. For revenue, a favorable variance is caused by actual revenue exceeding budget. For expenditures, a favorable variance results from actual expenditures being less than the amount budgeted for the fiscal year.

Budgetary vs GAAP Basis

Because the budget is prepared on a budgetary basis and not in accordance with generally accepted accounting principles (GAAP), there are differences in the revenue and expenditures amounts reported in the Statement of Revenues and Expenditures and the Budget To Actual Schedule. The major differences between the budgetary basis and the GAAP basis are:

1. Expenditures are recorded when cash is paid or committed (budgetary), rather than when the obligation is incurred (GAAP). In addition, revenue based on these accruals is adjusted on a GAAP basis only.
2. On a GAAP basis, major intra-agency transactions are eliminated in order to not double count revenues and expenditures reported in the Treasury's financial statements.

The following schedule reconciles the differences between budgetary accounting methods and the GAAP basis accounting principles for the fiscal year ended June 30, 2005.

RECONCILIATION OF BUDGETARY TO GAAP
FISCAL YEAR ENDED JUNE 30, 2005

Excess (Deficiency) Of Revenues Over (Under) Expenditures (Budgetary Basis)	**$ (187,812,671)**
Adjustments And Reclassifications:	
To Record The Net Effect Of Encumbrances	96,466
To Eliminate The Effect Of Receipt Of Loan Principal Repayment From Pease Development Authority	(1,131,574)
Net Adjustments	(1,035,108)
Excess (Deficiency) Of Revenues And Other Financing Sources Over (Under) Expenditures And Other Financing Uses (GAAP Basis)	**$ (188,847,779)**

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CURRENT STATUS OF PRIOR AUDIT FINDINGS

The following is a summary, as of February 27, 2006, of the current status of the observations and other issues and concerns contained in the audit report of the Treasury for the fiscal year ended June 30, 2002. A copy of the prior report can be obtained from the Office of Legislative Budget Assistant, Audit Division, 107 North Main Street, State House Room 102, Concord, NH 03301-4906. The prior report is also accessible on-line at www.gencourt.state.nh.us/lba.

	Status		
Internal Control Comments			
Reportable Conditions			
1. Revenue Sharing Payments Should Be Reviewed And Documented	●	●	●
2. Investment Transactions Should Be Subject To An Effective Review And Approval Procedure	●	●	●
3. Debt Management System Should Have The Capacity To Provide Complete Debt Accounting	●	○	○
4. Accounting For State-Guaranteed Debt Should Be Improved *(See Current Observation No. 9)*	●	○	○
5. Risk Categorization Of Cash And Investments Should Be Reviewed *(See Current Observation No. 4)*	●	○	○
6. Unique College Savings Plan Reimbursements Should Not Exceed Expenditures Incurred	●	●	●
7. The Rooms And Meals Distribution Should Be Adequately Reviewed	●	●	●
State Compliance Comment			
8. Abandoned Property Escheatment Proceeds Should Be Distributed Timely *(See Current Observation No. 18)*	○	○	○
Federal Compliance Comment			
9. Treasury-CMIA Federal Agreement Should Be Updated Timely *(See Current Observation No. 19)*	○	○	○
Management Issues Comments			
10. Current Status Of Foreign Escheated Estates Accounts Should Be Reviewed *(See Current Observation No. 21)*	○	○	○
11. Disaster Recovery And Business Continuity Plans Should Be Established *(See Current Observation No. 1)*	●	○	○

Status Key				Count
Fully Resolved	●	●	●	4
Substantially Resolved	●	●	○	0
Partially Resolved	●	○	○	4
Unresolved	○	○	○	3

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