

**STATE OF NEW HAMPSHIRE
BANKING DEPARTMENT
(EXCLUDING THE PUBLIC DEPOSIT INVESTMENT POOL)**

**FINANCIAL AND COMPLIANCE
AUDIT REPORT
FOR THE NINE MONTHS ENDED MARCH 31, 2002**

**STATE OF NEW HAMPSHIRE
BANKING DEPARTMENT**

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This report can be accessed in its entirety on-line at www.gencourt.state.nh.us/lba.

**STATE OF NEW HAMPSHIRE
BANKING DEPARTMENT**

Reporting Entity And Scope

The reporting entity and scope of this audit and audit report is the revenues, expenditures, and fixed assets reported by the New Hampshire Banking Department (the Department), excluding the New Hampshire Public Deposit Investment Pool (PDIP) for the nine months ended March 31, 2002. Pursuant to RSA 383:22, the bank commissioner established the PDIP for the purpose of investing the funds of the State and other governmental entities. The PDIP operates under contract with a private investment advisor and receives an independent audit annually.

Organization

The New Hampshire Banking Department, established pursuant to RSA 383, is a regulatory State agency. The Department is under the direction of a commissioner and deputy commissioner, both appointed by Governor and Council to six year terms. The Department employs 25 full-time and two part-time employees. The Department is comprised of two divisions, Banking and Consumer Credit.

Responsibilities

The Banking Division is responsible for the supervision and examination of the 60 State-chartered banks, credit unions, and other similar depository institutions. State statute requires that the Department conduct an examination of the condition and management of each institution, with certain exceptions, at least once every 18 months. Joint examinations are performed by the Department and federal regulatory agencies on certain institutions annually. During the nine months ended March 31, 2002, the Banking Division performed 18 examinations. The Division is comprised of a chief bank examiner and 13 examiners.

The Consumer Credit Division is responsible for the licensing and examination of 2,083 non-depository licensees, such as first or second mortgage companies, retail sellers of motor vehicles, sales finance companies, and other small loan companies. During the nine months ended March 31, 2002, the Division processed approximately 1,900 license applications and renewals. It also performed 23 examinations of non-depository institutions. The Division is comprised of an administrator of industry regulation and licensing, a consumer credit administrator, and five examiners.

Funding

The Department is self-supporting, operating initially from General Fund appropriations, and subsequently recovering these funds through licenses, examination fees, and year-end assessments. Assessments are levied on depository and non-depository institutions in accordance with RSA 383:11.

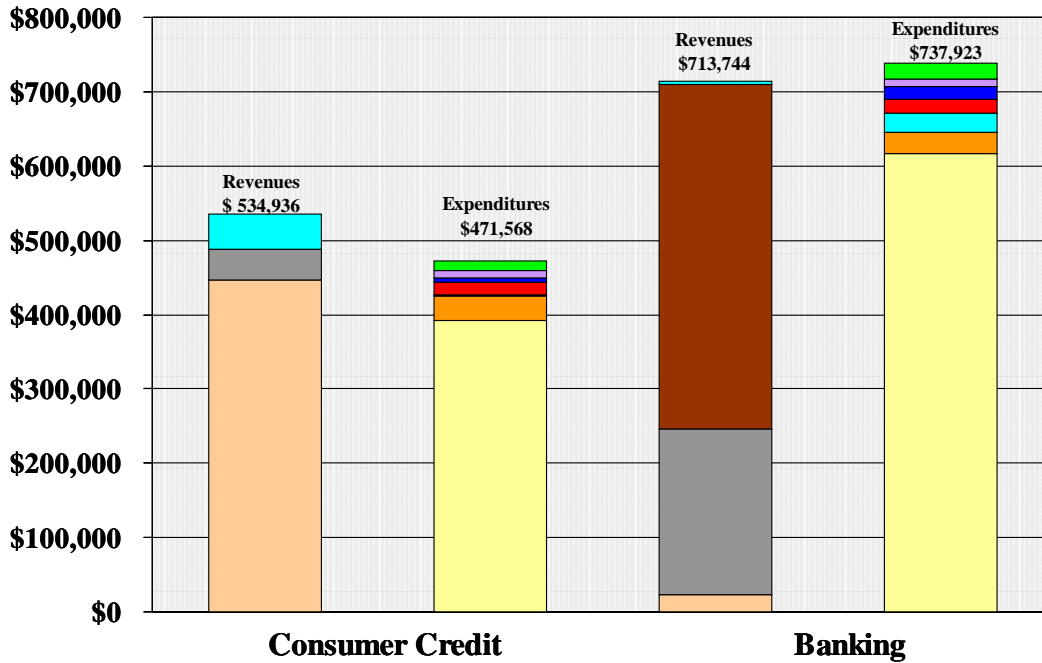
The fiscal year 2002 appropriations combined with supplemental warrants, balances forward, and transfers resulted in a spending authority of \$2,304,224 in the General Fund. Estimated restricted revenue combined with supplemental warrants, balances forward, and transfers resulted in anticipated fiscal year 2002 restricted revenue of \$1,912,971 in the General Fund. The actual financial activity of the Department is summarized below. Revenues and expenditures by division are shown graphically on the next page.

Summary of Revenues And Expenditures For The Nine Months Ended March 31, 2002	
Total Revenues	<u>General Fund</u> \$ 1,248,680
Total Expenditures	<u>1,209,491</u>
Excess Revenues Over Expenditures	<u>\$ 39,189</u>

Prior Audit

The most recent prior financial and compliance audit of the Department was for the fiscal year ended June 30, 1995, and the six months ended December 31, 1995. The appendix to this report on page 39, contains a summary of the current status of the observations contained in that prior 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.

**Banking Department
Revenues And Expenditures By Division
For The Nine Months Ended March 31, 2002**



		Consumer	
Revenues		Credit	Banking
[Orange]	Licenses	\$ 446,150	\$ 23,400
[Grey]	Examinations	41,236	222,939
[Brown]	Assessments	-0-	463,033
[Cyan]	Other	47,550	4,372
	Total	<u>\$ 534,936</u>	<u>\$ 713,744</u>

		Consumer	
Expenditures		Credit	Banking
[Yellow]	Salaries And Benefits	\$ 392,507	\$ 616,174
[Orange]	Rents And Leases	32,347	28,889
[Cyan]	Travel	1,822	25,861
[Red]	Current Expenses	16,791	18,276
[Blue]	Equipment	5,387	17,200
[Purple]	Indirect Cost	11,000	11,000
[Green]	Other	11,714	20,523
	Total	<u>\$ 471,568</u>	<u>\$ 737,923</u>

Audit Objectives And Scope

The primary objective of our audit is to express an opinion on the fairness of the presentation of the financial statement of the Banking Department for the nine months ended March 31, 2002. As part of obtaining reasonable assurance about whether the financial statement is free of material misstatement, we considered the effectiveness of the internal controls in place at the Department and tested the Department's compliance with certain provisions of applicable State laws, rules, regulations, and contracts. Major accounts or areas subject to our examination included, but were not limited to, the following:

- Revenues and appropriations,
- Expenditures, and
- State compliance.

Our reports on compliance and on internal control over financial reporting, and on management issues, the related observations and recommendations, our independent auditor's report, and the financial statement of the Banking Department are contained in the report that follows.

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

To The Fiscal Committee Of The General Court:

We have audited the accompanying Statement of Revenues and Expenditures – Budget and Actual – General Fund of the New Hampshire Banking Department, for the nine months ended March 31, 2002, and have issued our report thereon dated August 16, 2002, which was qualified with respect to the lack of presentation of the financial position of the Department in the General Fund. We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Banking Department's financial statement is free of material misstatement, we performed tests of its compliance with certain provisions of laws, rules, regulations, and contracts, 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 that are required to be reported under *Government Auditing Standards*. However, we noted certain immaterial instances of noncompliance which are described in Observations No. 8 through No. 11 of this report.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Banking Department's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statement and not to provide assurance 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 Department's ability

to record, process, summarize, and report financial data consistent with the assertions of management in the financial statement. Reportable conditions are described in Observations No. 1 through No. 7 of this report.

A material weakness is a 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 in amounts that would be material in relation to the financial statement 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 noted above is a material weakness.

This auditor's report on compliance and on internal control over financial reporting is intended solely for the information and use of the management of the Banking Department 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

August 16, 2002

Internal Control Comments
Reportable Conditions

Observation No. 1 - Segregation Of Duties Control Procedures Need To Be Established

Observation:

The Banking Department lacks the personnel to effectively segregate duties in its business office. The business office is comprised of the business administrator and two part-time employees, whose primary responsibilities include answering the telephone and processing cash receipts. Essentially, the business administrator assumes all responsibility over the accounting for revenue, expenditures, and fixed assets. A similar observation was noted in our 1995 audit of the Department.

The business administrator is responsible for handling all aspects of recording revenue and accounts receivable transactions, including preparing invoices, posting billings to the Department's database, reconciling such records to the paid invoices, and inputting revenue information into the State accounting system (NHIFS). She is also occasionally responsible for signing A-17s (Cash Receipts) and handling cash and checks.

The business administrator is responsible for all aspects of the expenditure process, including ordering, receiving and verifying purchases, and processing payments through NHIFS. Additionally, the business administrator enters all employee leave time earned and taken into the State payroll system, with no subsequent periodic review of her leave balances by supervisory personnel.

The business administrator is responsible for the custody of equipment items and conducts the annual physical inventory. Moreover, she has access to the equipment listing when performing the physical inventory and only records items that are identified with a control card. She does not record items that appear to meet the equipment threshold but are missing a control tag or identification.

Sound internal control procedures dictate that no one individual should be in a position to commit, either intentionally or unintentionally, errors or irregularities and also be responsible for the detection of those errors. In general, there are three incompatible duties that must be segregated for proper internal control: (1) authorization, (2) custody of assets, and (3) recording or reporting of transactions.

Recommendation:

While we recognize that the Banking Department has limited resources in its business office, it should strive to segregate duties of transaction authorization, custody of assets, and recording or reporting of transactions.

Auditee Response:

We concur. We have implemented a temporary system of segregation of duties to address this observation. In addition, we have a request in with the Division of Personnel to add an additional position for the business office (Accounting Technician) to fully address this issue as well as other issues identified in this audit.

Observation No. 2 - Formal Policy For Accounts Receivable Should Be Developed And Collection Procedures Should Be Improved

Observation:

The Department does not have formal policies and procedures governing the review and collection of its accounts receivable. Also, procedures for collecting amounts outstanding should be improved.

Formal, well-established accounts receivable policies and procedures allow an entity to better control and increase the efficiency and timeliness of collecting amounts due. Standard procedures include the preparation and supervisory review of monthly aging accounts receivable reports. This procedure is generally regarded as necessary for effectively monitoring balances outstanding. Additionally, documentation should be maintained with written supervisory approval for any amounts deemed uncollectible.

The Department's business administrator is responsible for billing, recording, reviewing, and collecting amounts due. According to the business administrator, outstanding balances are reviewed approximately three times a year and are not periodically reviewed by upper management. Accounts that are written off are not supported by written documentation containing supervisory approval or the reason for eliminating the account. Additionally, the billing system used by the Department does not allow a second invoice to be produced until 60 days after the first invoice was generated, or 30 days after the original invoice is due.

We noted on the following page various accounts that, had formal policies and procedures been in place, the timeliness and probability of collections may have been improved.

Timeliness of Collecting Amounts Due

Institution	Bill Type	Invoice	Date	# Of Days	
		Date	Collected	Late	Amount Due
1	Assessment	09/24/01	01/15/02	53	\$ 83,616.80
2	Assessment	09/24/01	01/18/02	56	47,478.95
3	Examination	01/18/02	05/13/02	85	8,736.00
4	Fine	02/01/02	-	166*	6,925.00
5	Examination	06/06/01	05/22/02	320	2,688.00
6	Examination	06/19/01	11/20/01	124	2,352.00
7	Examination	06/06/01	10/23/01	109	1,680.00
8	Examination	06/15/01	09/12/01	59	1,118.88
9	Fine	02/07/02	-	160*	900.00
10	Fine	02/25/02	-	142*	475.00
11	Fine	02/25/02	-	142*	450.00
12	Fine	02/12/02	-	155*	250.00
13	Assessment	09/24/01	12/20/01	27	64.93

* - indicates the amount was still outstanding as of August 16, 2002 (end of audit fieldwork).

Recommendation:

The Department should develop formal policies and procedures for the recording, reviewing, collecting, and writing off of accounts receivable. The policy should contain, but not be limited to, procedures to properly segregate responsibilities and functions of those employees involved in the collection process, periodic supervisory reviews, timely follow-up of outstanding amounts, collection procedures, and write-off procedures. The Department should include as part of these procedures the preparation of aging and other appropriate schedules for supervisory review. Additionally, the billing system should be modified to allow the generation of a second past due invoice as needed.

While it should be understood that formal policies and procedures do not guarantee the collection of amounts due it will increase the likelihood of receiving payment for those amounts in a timely manner.

Auditee Response:

We concur. We will develop and implement a policy that addresses the entire accounts receivable process. The billing system was modified during the audit to generate an invoice for all unpaid invoices at 30, 60, and 90 days after the initial invoice is sent. At the 120 day mark administrative proceedings are started.

Observation No. 3 - Monthly Revenue Reconciliations Should Be Performed

Observation:

The Department does not have a policy in place requiring the preparation and supervisory review of a monthly revenue reconciliation. Without the preparation of a monthly revenue reconciliation, the Department runs the risk that revenues may be incorrectly recorded or not recorded at all.

Revenue received is entered into a Department database, then into the State accounting system (NHIFS). The Department does not reconcile the revenue posted to its database to NHIFS, nor does it review revenue posted to NHIFS for accuracy. During revenue testing we noted several instances where revenue was incorrectly posted to accounts in NHIFS and was not detected by the Department. Specifically, we noted where \$25,561 of examination fees were posted as assessment and license revenue in NHIFS.

When we attempted to reconcile revenue from the Department database to NHIFS, we noted numerous posting errors where license revenue was posted in the database as examination revenue, license fees were posted to the wrong type of license (i.e. second mortgage fees posted as retail sellers fees) and application revenue was posted as zero dollar transactions in the database.

Good internal control procedures dictate a formal reconciliation should be performed at least monthly for both revenues and expenditures.

Recommendation:

While we recognize that the Department has limited resources in its business office, it should develop and implement a policy requiring the preparation and supervisory review of a monthly revenue reconciliation.

Auditee Response:

We concur. We will develop and implement a policy that addresses the items outlined in this observation within six months.

Observation No. 4 - Initial Controls Over Cash Receipts Should Be Enhanced

Observation:

The Department does not utilize full control over its initial recording of cash receipts. The computer generated form A-15 (Record of Cash Receipt) is used to record the initial receipt of cash at the Department. The A-15 serves as the supporting documentation used by the supervisor when approving the A-17 (Cash Receipt form), used to record revenue in the State accounting system (NHIFS).

The Department does not utilize the control provided by having two copies of the A-15 as both signed copies, along with the cash and checks, are sent to the employee who prepares the A-17. This allows the possibility that the A-15 could be altered without detection. As a function of supervisory approval, an independent copy of the A-15 should be compared with the A-17. This observation was also noted in our 1995 audit of the Department.

Recommendation:

The two signed copies of the A-15 should be separated after initial preparation with one copy forwarded to the preparer of the A-17 and the second copy forwarded to the supervisor for review and comparison with amounts reported on the A-17. In this way, the control provided by having two copies of the A-15 can be utilized.

Auditee Response:

We concur. This process was implemented during the audit. As noted in number one, an additional support position would significantly improve this procedure.

Observation No. 5 - Cost Allocation Methods Should Be Improved

Observation:

The Department has not developed appropriate methods to accurately allocate shared expenses and as a result incorrectly allocated costs between its two divisions, Banking and Consumer Credit.

The Department incurred approximately \$1.2 million in expenditures during the nine months ended March 31, 2002. Department expenditures are allocated between divisions, which are funded by depository (i.e. banks) and non-depository (i.e. consumer credit) financial institutions, respectively. Because the cost of operating each division is borne by the institutions it regulates, misallocations of costs results in either the banks or consumer credit companies assuming a disproportionate share of costs.

The Department has not developed appropriate methods to accurately allocate shared expenses such as salaries and benefits, rent, telephone, and other indirect costs. We noted the following instances where costs were inaccurately allocated between the divisions.

- The Department arbitrarily allocated the building rent between the Banking and the Consumer Credit Divisions. The allocation was not based on any rational basis such as square footage occupied by division.
- Computer components, totaling \$2,198, for the Banking Division operations were charged to the Consumer Credit Division.

- The Department allocates costs for salaries and benefits based upon the allocation of employee positions in the budget. As the Department has many employees who perform work for both divisions the current practice does not accurately allocate the cost of these employees. Payroll costs by division could not be determined as the Department does not have a mechanism for tracking and accurately allocating all employees' time. See Observation No. 6 for further discussion on the lack of an effective timekeeping system.

Improper allocation of expenditures between divisions results in disproportionate shares of the Department expenditures being charged to the institutions. In addition, management may have difficulty budgeting expenditures in the future, as the true cost of its expenditure categories is currently unknown.

Recommendation:

The Department should establish procedures to improve its accounting for expenditures. The Department should review the allocation of expenditures shared by the two divisions to determine a fair and equitable cost allocation method for each class of expenditures, so that institutions will be charged the correct portion of the assessment. To improve its allocation of salaries and benefits the Department should maintain a timekeeping system that allows the accumulation of time worked by employee by division. Salary and benefit costs for those employees who work for both divisions should be allocated based upon time worked for each division.

Auditee Response:

We concur. A process will be developed that identifies which costs should be allocated and establish guidelines for distributing those costs to the two PAU's within the department.

Observation No. 6 - An Effective Timekeeping System Should Be Utilized

Observation:

The Department does not have an effective timekeeping system in place to accumulate employees' time worked by task, job, and division. This increases the risk of not detecting and correcting errors in payroll in a timely manner. In addition, the Department's lack of an effective timekeeping system prevents the Department from developing a useful method of allocating salary and benefit costs for divisional assessment billings as discussed in Observation No. 5.

In our testing we noted that while examiners prepare time cards for hours worked on an examination, most employees are not required to record their time worked or leave taken. Specifically we noted:

- Part-time employees do not complete timesheets, nor is their time worked reviewed or approved by their supervisor. Part-time employees' hours are noted on a calendar, which is then used by the business administrator to enter information into the Government Human Resource System

(GHRS). Per the business administrator, this current system causes confusion, as there are times when the calendar information is inaccurate.

- Examiners working in the Consumer Credit Division prepare timecards which are used for preparing examination billings. However, time worked on other tasks is not documented, therefore the Department is unable to monitor effective use of their time or to confirm that leave taken or compensatory time earned has been properly recorded in GHRS.
- Leave time taken and compensatory time earned by employees is input into GHRS by the business administrator based upon receipt of an approved leave slip or an approved compensatory time earned report, respectively. There is no verification that leave information recorded into GHRS is accurate and complete. Many times the business administrator receives leave information several weeks after the pay period has ended and payroll was processed.

The Department's timekeeping procedures do not provide sufficient information on the activity of its employees to assist management in determining effective and efficient allocation of time worked by task for each division. As mentioned in Observation No. 5, the Department bases its assessment billings to depository (banks) and non-depository (consumer credit) institutions upon net operating costs for the respective divisions, therefore any misallocation of costs results in either the banks or consumer credit companies assuming a disproportionate share of costs.

In addition, the Department lacks sufficient information for monitoring and performing analyses of employees time. A timekeeping system would allow for the generation of reports to assist management in monitoring time worked, tasks performed, and leave earned or taken by employee or job.

Recommendation:

The Department should institute a timekeeping system that allows for the accumulation of employees' time worked by task, job, and division. The timekeeping system should allow for the generation of various reports to provide management with timely and useful information. Information should be accumulated as a method of allocating payroll and salary costs for each division. In order for the timekeeping system to provide accurate and useful information, all Department employees should prepare timesheets. Leave taken and earned listed on employees' timesheets should be reconciled to approved leave applications and approved compensatory time earned reports.

Auditee Response:

We concur. During the audit we implemented a time keeping system. The system generates management reports to assist in tracking the issues identified in the observation.

Observation No. 7 - A Formal Information Security Policy And Disaster Recovery Plan Should Be Developed

Observation:

The Department has not formally developed or established a disaster recovery plan to ensure continuity of operations should operations be interrupted due to an unforeseen future event or occurrence nor has the Department developed a formal information security policy. Good internal control policies dictate that there should be a current formal written information security policy.

The purpose of a disaster recovery plan is to document plans and procedures in the event of a disaster, including disaster recovery strategies, essential resources, and procedures necessary to implement a recovery process. The lack of a plan significantly lengthens the Department's recovery time, increases recovery costs, and increases the risk that vital information may never be recovered. It is important for the Department to maintain and regularly test its plan in order to minimize recovery time in the event of a disaster or systems failure.

By not having a formal information security policy in place, department employees may not know what is required of them concerning the protection/security of department information and computer assets. By not implementing and reviewing user access levels, the department runs the risk that individuals may enter unauthorized or fraudulent transactions or adjustments. Personnel may also accidentally or intentionally alter or delete important data.

We noted an example where the Department's current procedures do not effectively address recovery and/or security in the event of a computer system failure. The Department performs a backup of its computer system each night and the information technology manager takes the previous day's backup tape home. The backup tape is returned to the Department every morning and reused. This presents two problems as the tape could be lost while in the possession of the information technology manager and there is no off-site storage since the tape is brought back to the office. If a disaster were to happen at the office during the day, the Department is left without any backups of its systems.

Recommendation:

The Department should develop and maintain a disaster recovery plan for all important aspects of its operations. At least one backup tape should be kept off-site and adequately protected. The disaster recovery plan should include a program of regular testing of key provisions of the plan. The testing program should include employee training in the operations of the plan and critique of the plan's effectiveness.

The Banking Department should also develop, implement, and frequently review a formal information security policy.

Auditee Response:

We concur. We established a Disaster Recovery Committee comprised of senior staff to develop a disaster recovery plan. This is in the framework stages and is anticipated to be completed within six

months. In addition, attempts will be made to work within the State system in identifying disaster recovery techniques and processes that will enhance our ability to react to disasters.

We will develop an information security policy within six months.

State Compliance Comments

Observation No. 8 - Department Statutes Should Be Reviewed For Relevancy

Observation:

The Department has not performed a thorough review of its statutes to determine whether current laws are relevant or require amendment. The Department does not fully comply with certain statutes, rather, it applies the law the way it believes the law was intended. We have noted three examples of this below.

- The Department is not performing the calculation of the annual assessment in accordance with the language written in statute, RSA 383:11. The Department performs an annual assessment calculation as it believes the statute had intended to recover the deficit of the Department's operations. The law provides for the bank commissioner to annually collect from the institutions the total amount appropriated for the Department less revenue collected for examinations. The Department bases the calculation of the assessment on actual expenses less all revenue received.
- RSA 384:16-c provides for the Department to calculate and set a 6-month interest rate for escrow accounts to be paid by New Hampshire institutions. The law specifies that the minimum rate shall be one percent below the mean interest rate paid by New Hampshire chartered banks on regular passbook savings accounts. The Department obtains from the banks the interest rates for passbook and statement savings, and total deposit balances for the respective savings accounts. Many banks no longer offer passbook savings accounts. The escrow interest rate is calculated based upon passbook and statement savings interest rates using a weighted average allocation from total deposits. The law does not mention statement savings, or a weighted average method of calculation.
- RSA 384:43 requires that certain financial institutions direct their auditors to submit a copy of the audit engagement letter to the Department. The Department does not enforce this statute. In our review we noted that of nine financial institutions checked, only two submitted the engagement letter. According to Department personnel, the Department used to approve the institutions' audit firm, therefore the engagement letter was required to be submitted. Currently, there is no statute that requires institutions to seek the approval from the Department for its audit firm.

According to Department personnel, there are other various laws in the current statutes that are applicable to the institutions supervised by the Department that should be amended or repealed.

Recommendation:

The Department should thoroughly review its current statutes to determine whether laws are still relevant, or if amendments are needed. The Department should periodically perform a review of its statutes to ensure the laws remain current with changes in the banking industry and that the language in the statutes is appropriate to fulfill the Department's goals of keeping the citizens of New Hampshire well protected against fraud and abuse.

Auditee Response:

We concur. We are in the process of reviewing all the applicable laws and rules that govern the department's activities. Some proposed changes will be presented to the Legislature in the 2003 Session.

Observation No. 9 - The Number Of Examinations Of Consumer Credit Institutions Needs To Be Increased

Observation:

The Department is not fully meeting its statutory mandate of examining the condition and management of all institutions it supervises. RSA 383:9 requires the Department to examine the institutions it regulates at least once every 18 months.

The Department's two divisions, Banking and Consumer Credit, perform examinations. The Banking Division performs examinations of depository institutions; banks, credit unions and trust companies. The Consumer Credit Division performs examinations of non-depository institutions; mortgage companies, small loan companies, retail sellers, sales finance companies, etc.

Consumer Credit Division

As of December 31, 2001 there were 2,083 non-depository licensees with the Banking Department. During the nine months ended March 31, 2002, only 23 non-depository licensees were examined by the Consumer Credit Division. Over the last five years, there have been 9,600 licenses issued and only 379 exams performed.

**Consumer Credit Division Licenses Issued And Examinations Performed
During Fiscal Years 1997-2001**

<u>License Type</u>	<u># Of Licenses Issued From 1997 - 2001</u>	<u># of Exams Performed During 1997 - 2001</u>
First Mortgage Co.	3,868	245
Second Mortgage Co.	2,309	58
Retail Sellers	2,143	4
Sales Finance Co.	876	17
Small Loan Co.	216	55
Mortgage Servicers	183	-0-
Debt Adjuster	<u>5</u>	<u>-0-</u>
Totals	<u>9,600</u>	<u>379</u>

Based on discussions with the Department, the present statutory requirements are too stringent for the staff level employed to perform examinations of all institutions regulated by the Consumer Credit Division. During the nine months ended March 31, 2002, the Department had five examiners in the Consumer Credit Division. One examiner works full-time in the office processing license applications and the other examiners work in the office six months of the year processing applications. This means

that there are only six months of the year where four examiners are performing examinations. Consumer credit institutions are more transient than banks and as a result are considered riskier in terms of potential harm to the consumer, therefore, it is imperative that the Department establish tighter monitoring over these institutions.

Banking Division

There are currently 60 institutions subject to examination by the Department's Banking Division. While the institutions examined by the Banking Division receive significantly more attention than those examined by Consumer Credit, the Department is not fully in compliance with RSA 383:9 with regards to examining depository institutions. RSA 383:9 requires that institutions be examined every 18 months, with certain exceptions. The Department may waive an exam for a highly rated institution and may replace a State exam for one done by a federal bank examining agency.

We selected ten institutions to determine if the Department met the examination requirement and considered the eligibility for waivers. Seven institutions either did not have a sufficient number of examinations performed or the examinations were performed late. The Department is not in full compliance with RSA 383:9 nor does it maintain documentation to support waived examinations.

Recommendation:

The Department should determine the amount of examinations that are reasonable and economically feasible to promote the safety and soundness of those institutions it regulates. Once the Department has made this determination, it should work with the legislature for the possible approval of more staff and/or change in legislation as needed. The Department should also monitor its compliance with meeting the number of examination requirements and document its reasons for waiving an examination.

Auditee Response:

We concur.

Consumer Credit Division

We are in the process of conducting an analysis on the staffing needed to effectively supervise the entities regulated by the division. We will seek legislation that provides us with the resources to ensure compliance with the State statutes we are charged with enforcing.

Banking Division

We will remain diligent in monitoring the financial institutions under the division's supervision. A process for documenting waived examinations has been implemented.

Observation No. 10 - The Department Should Revise Its Assessment Methodology And Timing Of Collections

Observation:

The Department is not calculating the annual assessment in accordance with RSA 383:11 and therefore is not in compliance with the provisions of the statute. The Department should consider changing the timing of its assessment billings from after year-end to the beginning of the fiscal year.

RSA 383:11 stipulates that “The bank commissioner shall, each fiscal year, charge and collect from the institutions....he is required to examine.....the **total amount appropriated** [emphasis added] for the bank commissioner’s department.” The statute also states that the cost of examinations shall be deducted from total appropriations in determining the assessment amount. The statute further states, “Any excess collected in any fiscal year under the provisions of this section shall be used to reduce the sum required to be collected in the next succeeding fiscal year.”

The Department bases its annual assessment on actual expenditures plus encumbrances, less all revenues, including examinations, licenses, fines, and other fees. RSA 383:11 is silent as to how licenses, fines, and other fees are to be factored into the assessment calculation.

Technically, the Department is not in compliance with RSA 383:11 in that it did not charge and collect from depository institutions the total amount appropriated less examination revenues. It would appear, however, that using actual expenditures instead of appropriated amounts less prior year excess, would, over the course of time, equal out.

In revising its assessment calculation methodology, the Department should also consider revising the timing of its billings. Currently, the Department bills institutions in one fiscal year for the actual cost of operating the department in the previous fiscal year. RSA 383:11 is silent as to when assessment billings are to be made. In reviewing the billing practices of other self-supporting State agencies, (i.e. Public Utilities Commission, Insurance Commission, Department of Labor - Workers Compensation Division), these agencies bill at the beginning of the fiscal year, based on appropriations with adjustment for any over or under billings from the previous year. These agencies’ statutes specify that billings will occur at the start of the fiscal year.

In this manner, the institutions being regulated are truly providing the funding for the operations of the agencies rather than reimbursing the State for costs incurred, upwards of one year in arrears as is the current situation with the Department. The fiscal year 2001 assessment billing for the Department was sent out to institutions in September 2001.

Recommendation:

The Department should seek legislation to clarify the method of calculating its annual assessment as required by RSA 383:11. In seeking statutory amendment, the Department should give consideration to requiring that assessments be billed at the start of the fiscal year rather than in the following year and that all revenues generated be taken into consideration when determining the amount of the assessment.

Auditee Response:

We concur in part. We will seek legislation to address some of the issues identified in the observation.

However, to change the timing of the assessment billing would be burdensome to the institutions regulated by the department. If the change was made the department would assess the institutions under the current method and then, in short order, assess again under the proposed method. It would be difficult at best to explain to the entities that they are not paying twice for the same services. This could also have an adverse impact on some of the smaller institutions as the annual assessment is an accrued for expense and any unanticipated expense could affect the financial condition of the institution.

Observation No. 11 - Administrative Rules Should Be Adopted As Required By Statute

Observation:

The Banking Department has not adopted administrative rules for all statutes that require it do so pursuant to RSA 541-A.

The Department is required by several statutes to adopt administrative rules. In our review of the Department's statutes and administrative rules, we noted that some of the Department's rules have expired and other rules have yet to be adopted. The following is a summary of expired and unadopted rules noted during testing. With the exception of RSA 389-A:5 II, these same rules were noted in our 1995 audit as being either expired or unadopted.

RSA	RSA Description	Admin Rule	Status
361-A:2 VI	Licensing of Sales Finance Companies and Retail Sellers	BAN 1000	Expired
383:9 II	Duties of Commissioner	BAN 1103	Expired
386:1-b	Savings Banks, associations, and trust companies	BAN 1400 BAN 1410 BAN 1420 BAN 1430	Expired Expired Expired Expired
386-A:4 II	Petition for incorporation of a savings bank	BAN 1440	Expired
398-A:13 I	Second Mortgage Companies	BAN 2602	Expired
386-B:12	Reorganization of mutual savings banks into mutual holding companies	--	Not Adopted

RSA	RSA Description	Admin Rule	Status
389-A:5 II	Conversion between banks and loan associations	--	Not Adopted
399-A:26	Regulation of Small Loan Companies	--	Not Adopted

Recommendation:

The Banking Department should work with the Joint Legislative Committee on Administrative Rules to adopt the required rules. Additionally, the Department should establish procedures to ensure that administrative rules are adopted or readopted in a timely manner.

Auditee Response:

We concur. Ban 1000 rules, which were conditionally approved by the Joint Legislative Committee on Administrative Rules (JLCAR) on October 17, 2002, became effective on October 31, 2002. In addition, several other sections of the rules are in draft form and will be presented to JLCAR within six months. Lastly, we will introduce legislation changing the rulemaking provisions of RSA 386-B: 12 and RSA 389-A:5, II from mandatory to permissive status.

Auditor's Report On Management Issues

To The Fiscal Committee Of The General Court:

We have audited the accompanying Statement of Revenues and Expenditures – Budget and Actual – General Fund of the New Hampshire Banking Department for the nine months ended March 31, 2002, and have issued our report thereon dated August 16, 2002, which was qualified with respect to the lack of presentation of the financial position of the Department in the General Fund.

We conducted our audit in accordance with auditing standards generally accepted in the United States 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 statement is free of material misstatement.

In planning and performing our audit of the financial statement of the New Hampshire Banking Department for the nine months ended March 31, 2002, we noted certain issues related to the operation of the Department that merit management consideration but do not meet the definition of a reportable condition as defined by the American Institute of Certified Public Accountants, and were not issues of noncompliance with laws, rules, regulations, or contracts.

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. 12 through No. 14 of this report.

This auditor's report on management issues is intended solely for the information and use of the management of the Banking Department 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

August 16, 2002

Management Issues Comments

Observation No. 12 - Procedures For The Identification Of Unlicensed Institutions And Providing Public Awareness Should Be Improved

Observation:

The Department's procedures to identify unlicensed institutions are weak. The Department does not actively search for unlicensed institutions. Currently the Department identifies unlicensed institutions (primarily consumer credit institutions) by one of three ways; either an employee sees a new business sign in their travels, the Department receives a consumer complaint, or the public informs the Department of an unlicensed institution. As we noted in Observation No. 9, consumer credit institutions are more transient than banks and as a result are considered riskier in terms of potential harm to consumers, therefore it is imperative that the Department establish tighter monitoring over these institutions.

If an institution fails to renew its license or does not fully complete the application process, the Department does not follow-up with the institution to determine the reason the institution did not renew or continue with their application process. By performing a follow-up the Department may discover that an institution is operating without the required license.

We selected 29 license numbers where the license was not current, had expired or had been withdrawn, and performed limited inquiry to determine whether the entity was in business and was required to be licensed. We noted that one institution's application was withdrawn because the application was not complete and was returned to the entity. However, the entity was still in business and operating without a license.

We also noted that the Department's outreach to the public is weak. The Department does not issue regular press releases or public awareness announcements about those institutions that continue to operate in violation of the State laws. Announcements similar to the type of notices published by the Liquor Commission may be helpful to consumers. Additionally, the Department should better educate the public of where and what type of consumer complaints should be made. There may be many citizens that are unaware of the Department and its responsibilities to the public.

Recommendation:

The Department should improve its procedures for identifying unlicensed institutions. The Department can improve this process by performing follow-ups with licensees who do not renew or withdraw their applications. In addition, the Department could improve its discovery of unlicensed businesses by better educating consumers. The Department should also improve its outreach to the public through expanded use of the media and the internet.

Auditee Response:

We concur. We will develop processes to address the issues identified in the observation.

Observation No. 13 – The Department Should Seek Legislation To Help Enforce Governing Statutes

Observation:

The Department does not have the ability to enforce compliance with certain State statutes governing the institutions it regulates. In addition, the laws are inconsistent in the treatment of institutions regulated by the Department.

- RSA 383:13 requires that all depository institutions submit to the Department quarterly reports within 30 days of the last business day of each quarter ending in, March, June, September, and December. The Department uses the December quarterly report to prepare its annual report submitted to Governor and Council. A fine of \$25 for each day the December quarterly report is late is required to be imposed. However, the law does not address that a fine be imposed for the late filing of the other quarterly reports. The Department uses the June quarterly reports to obtain each institution's net assets in preparation of the assessment bill for the Banking Division. Assessment bills are delayed for any institution's report not received timely, since all reports must be received in order to compute the amount due. Further, State law requires that the assessment billing be paid within 60 days of the notice, however, the law does not institute any kind of penalty when the assessment is paid late. We noted that two institution's assessments totaling \$131,096 (24% of total assessment) were not received until January 2002.
- Non-depository institutions (first and second mortgage companies, retail sellers, sales finance companies, etc.) that have lending practices involving the citizens of New Hampshire are generally required by law to obtain a license from the Department. Although there are laws requiring these non-depository institutions to be licensed, the Department does not have any mechanism to enforce compliance, except in the case of retail sellers and sales finance companies. RSA 361-A:11 provides that any retail seller or sales finance company operating without a license shall pay a fine of \$25 a day for each day the seller operated without a license. There is no fine penalty for first mortgage companies, second mortgage companies, mortgage servicers, small loan companies, and debt adjusters for operating without a license.
- The Department imposes a fine of \$50 a day, as set in State statute, on non-depository institutions for each day an acknowledgement or response to a consumer complaint is overdue. Consumer complaints are required to be acknowledged by an institution within 30 days after receipt of such complaint and responded to within 60 days. State statutes do not provide the inflicting of a fine for non-responses to consumer complaints by banks, credit unions, and fiduciary trusts. Therefore the law is inconsistent in its treatment amongst the institutions regulated by the Department.

Recommendation:

The Department should seek legislation to provide the mechanisms that will aid in the enforcement of its statutes and offer better consumer protection. The Department should penalize those institutions that are not in compliance with State law.

Auditee Response:

We concur. As part of our review of the laws and rules that govern the department's activities we will strive to identify and propose changes to laws and rules that, in our opinion, strengthen our ability to protect the consumers and strengthen the industries that we regulate.

Observation No. 14 –A Long-Term Strategic Plan Should Be Developed

Observation:

The Department has not formally developed or established a long-term strategic plan to identify goals and methods to measure progress towards those goals. As we have noted elsewhere in this report, the Department faces many issues including staffing needs, complying with statutory requirements, and ensuring public safety and confidence in the banking and consumer credit industries.

Traditionally, the Department has focused its efforts on banks, as they are the main repositories of peoples' money. Over time the number of banks has decreased, while the number of consumer credit institutions has grown, however, the Department has not kept pace with the changing dynamics of the institutions it regulates. It continues to focus its regulatory efforts on banks as can be seen by the number of examiners for each division; 13 examiners for 60 banks verses 5 examiners for 2,083 consumer credit licensees. During the last year the Department has seen a large change in its personnel, including a new commissioner, which presents the Department with an opportunity to reexamine old practices and conventions.

The Department lacks a formal plan for the important aspects of its continuing operations. The plan should include how to better meet the Department's mission (protecting the public interest); how to better educate consumers; how to improve the licensing process (are current fees recovering the costs of processing licenses); when to incorporate more efficient technologies; how to improve communication between itself, those it regulates and those it serves; and whether the Department has sufficient staff to fulfill its responsibilities. Decisions are currently made without the benefit of a formal planning document to assist management in making the decisions in a coordinated and concerted effort.

A written strategic plan could enhance the Department's overall ability to efficiently and effectively manage operations. Established goals help to ensure that operations are carried out as management intended. A written plan could assist Department management in measuring progress toward goals and to recognize and correct deviations from the plan before conditions become critical. The plan could also encourage management to look ahead to anticipate and avoid problems before they arise and affect operations.

Recommendation:

The Department should develop a written strategic plan which would include (1) the goals of the Department, (2) the means of how management intends to meet these goals, and (3) the methods to

measure progress toward goals. Monitoring progress toward the goals is essential; without it, a strategic plan has little value. The strategic plan should be periodically reviewed and updated to reflect changes in operating conditions.

Auditee Response:

We concur. We will endeavor to develop a business plan that address the issues identified in the observation.

Independent Auditor's Report

To The Fiscal Committee Of The General Court:

We have audited the accompanying Statement of Revenues and Expenditures – Budget and Actual – General Fund of the New Hampshire Banking Department for the nine months ended March 31, 2002. This financial statement is the responsibility of the Banking Department's management. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States 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 statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. 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 opinion.

As more fully discussed in Note 1, the financial statement referred to above is not intended to present the financial position of the Banking Department in the General Fund.

In our opinion, except for the matter discussed in the third paragraph, the financial statement referred to above presents fairly, in all material respects, certain financial activity of the Banking Department for the nine months ended March 31, 2002, in conformity with accounting principles generally accepted in the United States.

Our audit was conducted for the purpose of forming an opinion on the financial statement referred to in the first paragraph. The accompanying schedule on page 37 is presented for the purpose of additional analysis and is not a required part of the financial statement of the Department. Such information has been subjected to the auditing procedures applied in our audit of the financial statement referred to in the first paragraph and, in our opinion, is fairly presented in all material respects in relation to the financial statement taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued a report dated August 16, 2002, on our consideration of the Banking Department's internal control over financial reporting and on our tests of its compliance with certain provisions of laws and rules, regulations, and contracts. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Office Of Legislative Budget Assistant
Office Of Legislative Budget Assistant

August 16, 2002

**STATE OF NEW HAMPSHIRE
BANKING DEPARTMENT**

**STATEMENT OF REVENUES AND EXPENDITURES
BUDGET AND ACTUAL – GENERAL FUND
FOR THE NINE MONTHS ENDED MARCH 31, 2002**

	<u>Budget</u>	<u>Actual</u>	<u>Favorable/ (Unfavorable) Variance</u>
<u>Revenues</u>			
Examinations	1,045,448	264,175	(781,273)
Licenses/Petitions	598,961	469,550	(129,411)
Assessments (Note 2)	163,798	463,033	299,235
Fines	81,046	47,550	(33,496)
Other	23,718	4,372	(19,346)
Total Revenues	<u>\$ 1,912,971</u>	<u>\$ 1,248,680</u>	<u>\$ (664,291)</u>
<u>Expenditures</u>			
Salaries And Benefits	\$ 1,941,620	\$ 1,008,681	\$ 932,939
Rents And Leases	84,200	61,236	22,964
Travel	79,800	27,683	52,117
Current Expenses	67,708	35,067	32,641
Equipment	42,694	22,587	20,107
Training	31,500	16,403	15,097
Indirect Cost	22,000	22,000	-0-
Other	34,702	15,834	18,868
Total Expenditures	<u>\$ 2,304,224</u>	<u>\$ 1,209,491</u>	<u>\$ 1,094,733</u>
Excess (Deficiency) Of Revenues Over (Under) Expenditures	<u>\$ (391,253)</u>	<u>\$ 39,189</u>	<u>\$ 430,442</u>

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

**STATE OF NEW HAMPSHIRE
BANKING DEPARTMENT**

**NOTES TO THE FINANCIAL STATEMENT
FOR THE NINE MONTHS ENDED MARCH 31, 2002**

NOTE 1 -- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statement of the New Hampshire Banking Department has been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

A. Financial Reporting Entity

The Department is an organization of the primary government of the State of New Hampshire. The accompanying financial statement reports certain financial activity of the Department, excluding the Public Deposit Investment Pool (PDIP). Pursuant to RSA 383:22, the bank commissioner established the PDIP for the purpose of investing the funds of the State and other governmental entities. The PDIP operates under contract with a private investment advisor and receives an independent audit annually. The financial activity of the Department is accounted for and reported in the General Fund 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 Department, as an organization of the primary government, accounts for only a portion of the General Fund and those assets, liabilities, and fund balances as reported in the CAFR that are attributable to the Department can not be determined. Accordingly, the accompanying financial statement is not intended to show the financial position of the Department in the General Fund and the change in the fund balance is not reported on the accompanying financial statement.

B. Basis Of Presentation - Fund Accounting

The State of New Hampshire and the Department use funds and account groups 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. An account group is a financial reporting device designed to provide accountability for certain assets and liabilities that are not recorded in the funds because they do not directly affect net expendable available financial resources.

Governmental Fund Type

General Fund

The General Fund accounts for all financial transactions not specifically accounted for in any other fund. By law, and with certain exceptions, all revenues of governmental funds are paid daily into the State Treasury.

Account Groups

General Fixed Assets

The General Fixed Assets Account Group is used to account for the fixed assets of the governmental funds. As of March 31, 2002, the Department had recorded in the General Fixed Assets Account Group the cost of general fixed assets based on available historical cost records. Donated fixed assets are recorded at fair market value at the time donated.

C. Measurement Focus And Basis Of Accounting

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds are accounted for using the flow of current financial resources measurement focus and reported on a modified accrual basis of accounting. Accordingly, the State of New Hampshire accounts for its financial transactions relating to the General Fund on the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recognized when measurable and available to finance operations of the fiscal period. "Measurable" means the amount of the transaction can be determined and "available" means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Expenditures are recognized in the period in which obligations are incurred as a result of the receipt of goods or services.

D. Budgetary Data

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 annual budgets 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 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 is prepared principally on a modified cash basis and adopted for the governmental and proprietary funds, with the exception of the Capital Projects Fund. The Capital Projects Fund budget represents appropriations for individual projects, which extend over several fiscal years. Fiduciary-type funds are not budgeted.

In addition to the enacted biennial operating budget, the Governor may submit to the Legislature supplemental budget requests necessary to meet expenditures during the current biennium. During the 2002 Legislative session, no significant supplemental budget requests affecting the Department were approved. 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. As shown on the Schedules of Budgetary Components – General Fund on page 37, the final budgeted amount includes the initial operating budget plus supplemental appropriation warrants, balances brought forward, and transfers.

Additional fiscal control procedures are maintained by both the Executive and Legislative Branches of government. 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 are legally defined as non-lapsing which means the balances are reported as reservation of fund balance. Capital Projects Fund unencumbered appropriations lapse in two years unless extended or designated as non-lapsing by law.

Variances - Favorable/(Unfavorable)

The variance column on the Combined Statement of Revenues and Expenditures - Budget And Actual - General Fund highlights differences between budget and actual revenues and expenditures. For revenues, these variances are caused by actual revenue exceeding budget generating a favorable variance or actual being less than budget generating an unfavorable variance. For expenditures, a favorable variance results from actual expenditures being less than the amount budgeted for the fiscal year. The favorable expenditure variances represent a combination of ending available balances and unliquidated encumbrances. Unfavorable expenditure variances represent actual expenditures for the reporting period exceeding the amounts budgeted for the fiscal year.

When statements are presented at an interim date, a date other than a June 30 fiscal year end, the variance reflects the difference between the budget period amount, twelve months in the case of the General Fund, and a partial year's actual revenue and expenditures. Thus, for the nine month financial statement dated March 31, 2002, unfavorable variances in General Fund revenues are expected to be collected in the twelve month period. Similarly, favorable expenditure variances are expected as nine months of expenditures are compared to amounts expected to be expended in the twelve month budget period.

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. Total encumbrances outstanding at March 31, 2002 were \$26,868.

E. Fixed Assets - General

General fixed assets are not capitalized in the funds used to acquire or construct them. Instead, capital acquisition and construction costs are reflected as expenditures in governmental funds, and the related assets are reported in the General Fixed Assets Account Group. For State Comprehensive Annual Financial Report reporting purposes, the State capitalizes equipment that costs \$10,000 or more and land, land improvements, buildings, building improvements, and construction in progress with costs of \$100,000 or greater. All purchased fixed assets are valued at historical cost and in some instances at estimated historical cost. Donated fixed assets are valued at their estimated fair market value on the date received. Interest costs incurred during construction are not capitalized. Public domain (“infrastructure”) general fixed assets consisting of roads, bridges, dams, curbs and gutters, streets and sidewalks, drainage systems, and lighting systems are not capitalized, as these assets are immovable and of value only to the State. Assets in the General Fixed Assets Account Group are not depreciated.

F. Interfund And Intrafund Transactions

The State accounts for interfund and intrafund transactions as described below:

Reimbursements - Various departments charge user fees for such services as centralized data processing, accounting and auditing, purchasing, personnel, and maintenance. In addition, the Department of Administrative Services charges rent to those departments that are housed in state-owned buildings. These fees and rent are not considered material and are recorded as revenue by the servicing department and as expenditures by the user department.

NOTE 2 – ASSESSMENTS

RSA 383:11 provides that the Banking Department collect from the institutions it regulates an annual assessment to cover the cost of operating the Department. Separate assessments are calculated for the Banking and Consumer Credit Divisions. The assessment is calculated as the balance of remaining costs not already recovered through examination and license fees. Any excess revenue collected in any fiscal year is used to reduce the sum required to be collected in the next succeeding fiscal year. Currently, the Consumer Credit Division is in a surplus position as examination and license fees more than cover the cost of operating the Division.

NOTE 3 – GENERAL FIXED ASSETS ACCOUNT GROUP

The following is a summary of fixed assets balances and activity for the nine months ended March 31, 2002 reported by the Department. As well as reporting general fixed assets as defined by the State for financial reporting purposes, the Department also reports equipment using the criteria required by the State Manual of Procedure, that being equipment with a historical cost of \$100 or more and useful life of greater than one year.

	<u>Balance</u> <u>July 1, 2001</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance</u> <u>March 31, 2002</u>
Equipment With Original Cost Of \$10,000 Or Greater	\$ 107,494	\$ -0-	\$ -0-	\$ 107,494
Equipment With Original Cost Between \$100 And \$10,000	<u>275,422</u>	<u>21,715</u>	<u>(11,301)</u>	<u>285,836</u>
Total General Fixed Assets And Other Equipment	<u>\$ 382,916</u>	<u>\$ 21,715</u>	<u>\$ (11,301)</u>	<u>\$ 393,330</u>

NOTE 4 – EMPLOYEE BENEFIT PLANS

New Hampshire Retirement System

The Banking Department, as an organization of the State government, participates in the New Hampshire Retirement System (Plan). The Plan is a contributory defined-benefit plan providing service, disability, death, and vested retirement benefits to members and beneficiaries. The Plan covers substantially all full-time employees of the Department. 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.

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.

Pursuant to RSA 100-A:50, the New Hampshire Retirement System also provides a postretirement medical premium subsidy for Group I employees of political subdivisions and teachers and Group II police officers and firefighters. A special account has been established by RSA 100-A:16, II(h) for additional benefits. The account is credited with all the earnings of the assets in the account plus the earnings of the remaining assets of the plan in excess of the assumed rate of return plus ½ of 1 percent.

The New Hampshire Retirement System issues a publicly available financial report that may be obtained by writing to them at 4 Chenell Drive, Concord, N.H. 03301-8509 or from their web site at <http://webster.state.nh.us/retirement>.

The Plan is financed by contributions from the members, the State and local employers, and investment earnings. During the nine months ended March 31, 2002, Group I and II members were required to contribute 5% and 9.3%, respectively, of gross earnings. Employer contributions required to cover that amount of cost not met by the members' contributions are determined by a biennial actuarial valuation by the system's actuary using the open group aggregate funding method and are expressed as a percentage of gross payroll. The State's share represents 100% of the employer cost for all of the Department's employees enrolled in the Plan.

The Department's payments for normal contribution costs for the nine months ended March 31, 2002, amounted to 3.94% of the covered payroll for its Group I employees. The Department's normal contributions for the nine months ended March 31, 2002, were \$29,324, an amount equal to the required employer contribution for the period.

Post-employment Health Care Benefits

In addition to providing pension benefits, RSA 21-I:30 specifies that the State provide certain health care insurance benefits for retired employees. These benefits include group hospitalization, hospital medical care, and surgical care. Substantially all of the State's employees 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. These and similar benefits for active employees are authorized by RSA 21-I:30 and are provided through an insurance company whose premium is based on the benefits paid during the year. The State recognizes the cost of providing these benefits by paying the entire annual insurance premium.

During the nine months ended March 31, 2002, the State paid for the full cost of health insurance premiums for the retired employees and spouses on a pay-as-you-go basis. The cost of the health insurance for Department employees and spouses is a budgeted amount and is paid from an appropriation made to the administrative organization of the New Hampshire Retirement System. The

Department reimburses the New Hampshire Retirement System for its share of post-employment health care benefits. The amount reimbursed for the nine months ended March 31, 2002, totaled \$49,623.

**STATE OF NEW HAMPSHIRE
BANKING DEPARTMENT**

**SCHEDULE OF BUDGETARY COMPONENTS
GENERAL FUND
FOR THE NINE MONTHS ENDED MARCH 31, 2002**

	<u>Operating Budget</u>	<u>Supplemental Appropriation Warrants</u>	<u>Balances Brought Forward</u>	<u>Net Transfers In/(Out)</u>	<u>Budget</u>
<u>Revenues</u>					
Examinations	1,027,000	18,448	-0-	-0-	1,045,448
Licenses/Petitions	586,500	12,461	-0-	-0-	598,961
Assessments	515,305	15,120	(384,627)	18,000	163,798
Fines	80,000	1,046	-0-	-0-	81,046
Other	3,050	20,668	-0-	-0-	23,718
Total Revenues	<u>\$ 2,211,855</u>	<u>\$ 67,743</u>	<u>\$ (384,627)</u>	<u>\$ 18,000</u>	<u>\$ 1,912,971</u>
<u>Expenditures</u>					
Salaries And Benefits	\$ 1,867,877	\$ 67,743	\$ -0-	\$ 6,000	\$ 1,941,620
Rents And Leases	84,200	-0-	-0-	-0-	84,200
Travel	88,800	-0-	-0-	(9,000)	79,800
Current Expenses	65,150	-0-	558	2,000	67,708
Equipment	36,626	-0-	6,068	-0-	42,694
Training	31,500	-0-	-0-	-0-	31,500
Indirect Cost	22,000	-0-	-0-	-0-	22,000
Other	15,702	-0-	-0-	19,000	34,702
Total Expenditures	<u>\$ 2,211,855</u>	<u>\$ 67,743</u>	<u>\$ 6,626</u>	<u>\$ 18,000</u>	<u>\$ 2,304,224</u>
<u>Excess (Deficiency) Of Revenues</u>					
Over (Under) Expenditures	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ (391,253)</u>	<u>\$ -0-</u>	<u>\$ (391,253)</u>

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APPENDIX

CURRENT STATUS OF PRIOR AUDIT FINDINGS

The following is a summary of the status of the observations contained in the audit report of the Banking Department for the year ended June 30, 1995 and the six months ended December 31, 1995. 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.

	<u>Status</u>
Internal Control Structure	
1. Handling And Reporting Of Receipts (<i>See Current Observation No. 4</i>)	● ○ ○
2. Segregation Of Duties (<i>See Current Observation No. 1</i>)	○ ○ ○
3. Timeliness Of Assessment Billing	● ● ○
4. Thorough File Review	● ● ●
5. Accounts Receivable – Understatement Of Bank Examination Fees	● ● ●
State Compliance	
6. Expired/Unadopted Administrative Rules (<i>See Current Observation No. 11</i>)	○ ○ ○
7. Failure Of Board Members To File Statements Of Financial Interests	● ● ●
Management Issue	
8. Disposition Of Expendable Trust Fund Account	● ● ●

Status Key

Fully Resolved	●	●	●
Substantially Resolved	●	●	○
Partially Resolved	●	○	○
Unresolved	○	○	○

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