



PERFORMANCE AUDIT REPORT

**Reviewing Operations of the State Treasurer's Office
Fiscal Year 2003**

**A Report to the Legislative Post Audit Committee
By the Joint Venture of Allen Gibbs & Houlik and
Berberich Trahan & Co., audit firms under contract with the
Legislative Division of Post Audit
State of Kansas
December 2003**

Legislative Post Audit Committee

Legislative Division of Post Audit

THE LEGISLATIVE POST Audit Committee and its audit agency, the Legislative Division of Post Audit, are the audit arm of Kansas government. The programs and activities of State government now cost about \$9 billion a year. As legislators and administrators try increasingly to allocate tax dollars effectively and make government work more efficiently, they need information to evaluate the work of governmental agencies. The audit work performed by Legislative Post Audit helps provide that information.

We conduct our audit work in accordance with applicable government auditing standards set forth by the U.S. General Accounting Office. These standards pertain to the auditor's professional qualifications, the quality of the audit work, and the characteristics of professional and meaningful reports. The standards also have been endorsed by the American Institute of Certified Public Accountants and adopted by the Legislative Post Audit Committee.

The Legislative Post Audit Committee is a bipartisan committee comprising five senators and five representatives. Of the Senate members, three are appointed by the President of the Senate and two are appointed by the Senate Minority Leader. Of the Representatives, three are appointed by the Speaker of the House and two are appointed by the Minority Leader.

Audits are performed at the direction of the Legislative Post Audit Committee. Legisla-

tors or committees should make their requests for performance audits through the Chairman or any other member of the Committee. Copies of all completed performance audits are available from the Division's office.

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Representative John Edmonds, Chair
Representative Tom Burroughs
Representative Bill McCreary
Representative Frank Miller
Representative Dan Thimesch

Senator Derek Schmidt, Vice-Chair
Senator Bill Bunten
Senator Anthony Hensley
Senator Dave Kerr
Senator Chris Steineger

LEGISLATIVE DIVISION OF POST AUDIT

800 SW Jackson
Suite 1200
Topeka, Kansas 66612-2212
Telephone (785) 296-3792
FAX (785) 296-4482
E-mail: LPA@lpa.state.ks.us
Website:
<http://kslegislature.org/postaudit>
Barbara J. Hinton, Legislative Post Auditor

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LEGISLATURE OF KANSAS
LEGISLATIVE DIVISION OF POST AUDIT

800 SOUTHWEST JACKSON STREET, SUITE 1200
TOPEKA, KANSAS 66612-2212
TELEPHONE (785) 296-3792
FAX (785) 296-4482
E-MAIL: lpa@lpa.state.ks.us

December 12, 2003

To: Members, Legislative Post Audit Committee

Representative John Edmonds, Chair	Senator Derek Schmidt, Vice-Chair
Representative Tom Burroughs	Senator Bill Bunten
Representative Bill McCreary	Senator Anthony Hensley
Representative Frank Miller	Senator Dave Kerr
Representative Dan Thimesch	Senator Chris Steineger

This report contains the findings, conclusions, and recommendations from the completed performance audit, *Reviewing Operations of the State Treasurer's Office*. This audit was conducted by the joint venture of Allen Gibbs & Houlik and Berberich Trahan & Co., audit firms under contract with the Legislative Division of Post Audit.

The report includes a recommendation to finalize and implement revised unclaimed property procedures. We would be happy to discuss this recommendation or any other items in the report with any legislative committees, individual legislators, or other State officials.

A handwritten signature in black ink that reads "Barbara J. Hinton". The signature is written in a cursive, flowing style.

Barbara J. Hinton
Legislative Post Auditor

EXECUTIVE SUMMARY

LEGISLATIVE DIVISION OF POST AUDIT

Reviewing the Operations of the State Treasurer's Office

As part of its responsibilities, the State Treasurer's Office does the following: page 1

- deposits receipts it collects in State bank accounts as applicable
- ensures that moneys in those bank accounts are collateralized as required by State law
- ensures that cash flow needs of State agencies for moneys in the State Treasury are met
- redeems State warrants presented for redemption
- maintains adequate custodial accountability for moneys in the State Treasury
- administers the State's unclaimed property program
- serves as fiscal agent for certain public bonds
- distributes local taxes and State aid moneys to cities and counties as required by State law
- administers the Agrigultural Production Loan Deposit Program and other linked deposit programs
- administers the Kansas Postsecondary Education Savings Program

The audit reviewed each of the above areas of responsibility, and found no major deficiencies. The audit also made a recommendations to finalize and implement revised unclaimed property procedures.

Recommendations page 12

Agency Response page 13

This audit was conducted by the joint venture of Allen Gibbs & Houlik and Berberich Trahan & Co., audit firms under contract with the Legislative Division of Post Audit. If you need any additional information about the audit's findings, please contact Randy Tongier at the Division's offices. Our address is: Legislative Division of Post Audit, 800 SW Jackson Street, Suite 1200, Topeka, Kansas 66612. You also may call us at (785) 296-3792, or contact us via the Internet at LPA@lpa.state.ks.us.



ALLEN, GIBBS & HOULIK, L.C.



Berberich Trahan & Co., P.A.

Certified Public Accountants & Consultants

Certified Public Accountants

Epic Center • 301 N. Main, Suite 1700
Wichita, Kansas 67202-4868
(316) 267-7231 • FAX (316) 267-0339
www.aghlc.com

3630 SW Burlingame Road
Topeka, KS 66611-2050

Telephone 785 234 3427
Toll Free 1 800 530 5526
Facsimile 785 233 1768
E-mail cpa@cpakansas.com

November 14, 2003

Legislative Post Audit Committee Members:

The performance audit report on Reviewing the Operations of the State Treasurer's Office for the year ended June 30, 2003 is enclosed. This work was performed in accordance with *Government Auditing Standards* for performance audits.

Please do not hesitate to contact the undersigned if you have any questions.

Allen, Gibbs & Houlik, L.C.

Berberich Trahan & Co., P.A.

PERFORMANCE AUDIT REPORT

REVIEWING THE OPERATIONS OF THE
STATE TREASURER'S OFFICE

FOR THE YEAR ENDED JUNE 30, 2003

PERFORMANCE AUDIT REPORT

Reviewing the Operations of the
State Treasurer's Office

For the Year Ended June 30, 2003

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Reviewing the Operations of the State Treasurer's Office

Introduction

The State Treasurer is one of six state officials elected every four years. The Treasurer is responsible for the timely receipt and deposit of all receipts and revenues into the State treasury. The 1992 Legislature gave the Treasurer authority to establish a Municipal Investment Pool to enhance investment options for Kansas Municipalities. The State Treasurer has established a director of the following operations:

- Administrative Services (currently the Unclaimed Property Director)
- Bond Services
- Cash Management
- College Savings Plan
- Information Technical Services
- Unclaimed Property

The State Treasurer was designated as the fiscal agent for the State of Kansas in 1908. The Municipal Bond Services program currently operates under the provisions of Chapter 10 of the Kansas Statutes. The registration of the issuance of municipal bonds was originally performed by the State Auditor, but these duties were transferred to the State Treasurer in 1975 when the office of State Auditor was abolished. The enactment in 1982 of PL 97-428, the Tax Equity and Fiscal Responsibility Act, required municipal obligations issued after June 30, 1983 be issued in registered form in order for the interest on these obligations to qualify for exemption from federal income tax. The 1983 Legislature then enacted Senate Bill 265, which made major changes to the State's bond laws in order to permit Kansas municipalities to issue their bonds in the required registered form; this legislation contained provisions which were codified in Kansas Statutes Annotated (K.S.A.) 10-260 et seq., the Kansas Bond Registration Law. As a consequence of this legislation, the State Treasurer has become a registrar and transfer agent for those registered form municipal bonds which designate the Treasurer as paying agent.

The Cash Management Services program is charged with receipt and deposit responsibilities, as well as those relating to payment of warrants. The requirement that the State Treasurer maintain an accurate account of the receipts and disbursements of the Treasury is contained in K.S.A. 75-603, first enacted in 1879, while K.S.A. 75-604, enacted in 1923, entrusts the State Treasurer with the possession of all public moneys paid to the State Treasury and permits the Treasurer to deposit moneys in Kansas banks designated as State depositories. The State Moneys Law (K.S.A. 75-4201 et seq.), enacted in 1967, regulates the designation of banks that receive State accounts, the pledging of securities by these banks, and the rate of interest to be paid on deposits of State moneys. The 1985 session of the Legislature passed House Bill 2122 which increased the pledge requirements for banks on State accounts from 70% to 100% of market value on all funds not covered by the Federal Deposit Insurance Corporation. Senate Bill 480, 1992-session, substantially changed the types and terms of allowable investments. It also authorized the Treasurer to offer a Municipal Investment Pool for the benefit of all Kansas taxing units.

The Director of Accounts and Reports is required by K.S.A. 75-3732, enacted in 1953, to pay the State's obligations by issuing warrants drawn on the State Treasurer and to remit to the Treasurer a duplicate copy of the Director's record of all warrants issued. K.S.A. 75-607 and 75-608, originally enacted in 1879, require respectively that the Treasurer return paid warrants to the Director and Accounts and Reports and that the State Treasurer prepare an annual report.

In 1992, K.S.A. 75-628 charged the State Treasurer with the responsibility of reviewing and making recommendations for efficient handling of cash and cash equivalents for the State. In that regard, education and assistance in cash management practices, consideration of the operating needs of State agencies, and government wide efficiencies are principles which are to be addressed.

The 1999 Legislature passed K.S.A. 75-640 through 75-648 which authorized the Treasurer to implement and administer a qualified tuition savings plan as defined in Internal Revenue Code, Section 529. The language in the bill was broad enough to allow the Treasurer many decisions in designing the program. In fiscal year 2000, the Treasurer hired a program manager, adopted rules and regulations and developed a marketing plan. The implementation date for the program was July 1, 2000.

The Disposition of Unclaimed Property Act (K.S.A. 58-3934 et seq.), enacted in 1979, designates the State Treasurer to administer functions established by the Act. Amendments to the Act in 1983 broadened the definition of abandoned property to which the Act applies. Senate Bill 326 enacted by the 1989 Legislature shortened the holding period for unclaimed property from seven to five years on most property and allowed aggregate reporting of amounts up to \$ 25. The 1994 Legislature enacted Senate Bill 393 which repealed several of the Statutes relating to unclaimed property and enacted a more recent version of the model Uniform Unclaimed Property Act. The legislation recognized new financial instruments developed since the 1954 Uniform Code was adopted. In 1996, House Bill 2643 amended the Act to raise the aggregate dollar amount to \$ 100, defined when a financial institution must presume a demand account to be abandoned, and allowed additional flexibility in the advertisement of owner names.

Objective and Scope of Work

K.S.A. 46-1106(a) requires a written audit report on the financial management practices of the State Treasurer's Office (STO). The following report addresses ten specific questions and includes a summary of each area and our conclusions and recommendations regarding those questions.

The audit work was performed in accordance with *Government Auditing Standards* for performance audits.

Did the Treasurer's Office properly deposit the receipts that it collected in State bank accounts?

The primary activity of the receipt depository process is handled by cashier's cage personnel. All receipts are accounted for through the cage. This includes cash and check receipt vouchers as well as ACH and wire transfers. Checks for certain large agencies, such as the Department of Revenue, are encoded prior to submission to the cage. The remainder of items are encoded by the Cashier.

On a daily basis, the cashier accounts for and deposits all funds received into the State bank accounts. The daily cash receipts are summarized and posted to the daily cash sheet. The daily cash sheet provides a summary of daily receipt and disbursement activity, the total bank balances and the daily analysis of investments, receivables and other items.

Wire transfers out and between the bank accounts held by the State Treasurer's Office are entered into the accounting system by the cashier. The transfers are reviewed by the Director of Cash Management, the Accounting Specialist, or the Assistant State Treasurer. The original documentation of the transfer is received, amounts are checked and the funds then transferred in accordance with current statutory authority.

On a daily basis the State Treasurer's Office completes the daily cash sheet which acts as the daily deposit form. This form is signed by the Cashier, who has been duly authorized by the Treasurer, and filed with the Director of Accounts and Reports in accordance with K.S.A. 75-4203.

No exceptions were noted.

Did the Treasurer's Office ensure that moneys in State bank accounts were collateralized as required by State law?

All State bank accounts are collateralized at all times. When a financial institution requests funds from the STO, the institution is issued a resolution form and a security agreement form. These forms must be filled out completely and signed before any funds are released. After the requested amount has been determined, the financial institution is required to go through a third party to obtain sufficient collateral for the funds. After the required collateral has been obtained, all supporting documentation including a custodial agreement signed by the custodial bank is forwarded to the Securities Custodian. The Custodian verifies that the collateral is sufficient to cover the requested funds and notifies Pooled Money Investment Board (PMIB) to authorize the release of the funds. All collateral support information is filed and maintained by the Securities Custodian.

At the end of each month, the Custodian runs exception reports to determine whether any accounts, other than the operating, clearing or benefit accounts, are deficient. In cases of deficiency, the Custodian immediately informs the undercollateralized bank and additional collateral is pledged.

The operating, clearing and benefit accounts are not included in the analysis because of the nature of the activity in the accounts. The operating account is established by contract. The contract specifies that the bank:

“. . . has executed a Security Agreement in favor of the Kansas State Treasurer and/or Pooled Money Investment Board granting a security interest in any collateral pledged to secure the deposit of public funds, directly or indirectly . . .”

The contract is supported by the bank's procedure manual stating the “depository bank shall pledge securities that have a market value equal to at least 100% of the amount of the total deposits of public funds in depository bank . . .” In addition, a cashier analyzes the account balance at mid-day since additional cleared deposits may increase the balance in the account. Near the close of each month, the balance may exceed the standard collateralization level thereby requiring that additional collateralization be pledged. Normally the bank pledges additional collateral, but if not, the Cashier notifies the Vault Custodian to secure additional collateral.

No exceptions were noted.

Did the Treasurer's Office have a good way to ensure that cash flow needs of State agencies for moneys in the State Treasury were met?

The 1992 Legislature enacted changes to the law that applies to the investment of State moneys, known as the State Moneys Law. The new law authorized additional investment personnel to implement and continuously generate cash forecasting information to maximize interest earnings. Two forecasting procedures are performed.

The first is a daily forecast. A daily cash flow analysis is provided to maintain the amount of funds in the operating account to clear all obligations and to allow for investment of idle funds on a daily basis. A current cash position analysis is prepared each morning to determine the amount of money available for investment that day.

The second forecast is long-term and provides data for 15-24 months of daily receipts and disbursements. The forecast also provides assistance in computing investment portfolio maturity information. The Assistant State Treasurer prepares the forecasts based on historical data and constantly changing legislative actions. This forecast is concerned with the overall picture of the total pool, which includes cash available in State funds, special revenue funds, federal funds, certain trust funds, capital projects fund, and enterprise, intra governmental and clearing funds. The performance measure for the forecast is the Pooled Money Investment Board's feedback on whether or not the information is accurate for investing.

No exceptions were noted.

Did the Treasurer's Office properly redeem State warrants presented for redemption?

On a daily basis, warrants are presented to the Federal Reserve Bank (FRB), which acts as a clearinghouse for the STO. There are currently two types of presentation: Direct Presentation (a small group of banks present warrants directly to the Fed) and FRB (all other banks' warrants go through the Federal Reserve System). Each day these warrants are read and split into two files: Direct and Federal Reserve. The files are downloaded by the Vault Custodian through a direct connection to the FRB (called the “fed line”). The data is reformatted, saved on a disk and then transferred to the STO network payment system. The system compares each paid warrant to the outstanding warrant record in the STO system. A totals summary report is printed and given to a cashier who then verifies that the totals from the report correspond to the totals obtained from the “fed line”.

The System generates a "Warrant Exception Report". All exceptions are investigated and cleared. The Federal Reserve keeps images of checks on-line for a specific amount of time. These images can be accessed by the STO to aid in following up on the exception items. If older check images are needed, the images can be accessed upon request.

Separate spreadsheets are prepared for each type of outstanding exception for each account. As each of the exceptions are cleared, they are marked as such. A copy of the spreadsheet is sent to the Cashier, who enters them as cash items on the daily cash reconciliation. This process provides accountability as exceptions are resolved.

The warrant payment system is well designed to safeguard against payments of forgeries and altered warrants. All presented warrants are compared with the disbursement records. The system properly redeems warrants as presented for redemption.

Did the Treasurer's Office maintain adequate custodial accountability for moneys in the State Treasury?

The vault is responsible for two major areas of custodianship: Adequacy of collateral on all STO deposits, and safeguarding of other assets of the STO.

Adequacy of Collateral

Approximately every other day, the Securities Custodian runs an "undercollateralized bank exception report," which highlights any bank which is close to its collateralized limit. This is a special report generated from a software program (VAULT). The market value of pledged collateral is compared to total bank balances including accrued interest for each bank. For each undercollateralized bank, the Securities Custodian calls the bank and notifies them that they must increase their pledge. When the pledge is made, the custodial (safekeeping) bank faxes a notice to the Securities Custodian and an entry is posted to the pending collateral in VAULT. The collateral remains pending until the safekeeping receipt and submission forms are received. All collateral is priced monthly using electronic communications with a national pricing service.

Safeguarding of Other Assets

When certificates of deposit (CD) and other securities are bought by STO and other agencies, a deposit slip is filled out and delivered to the Securities Custodian along with the appropriate documentation (safekeeping receipt, CD, etc.). The Securities Custodian maintains a file of deposit slips. The related asset is kept in the vault. When an agency sells an instrument or the instrument matures, the agency fills out a withdrawal form. After it has been determined that the requested security will not adversely affect collateralization agreements the withdrawal form is signed. The Securities Custodian records the carryforward balance, the deposit or withdrawal, and the new balance on the control sheet. A perpetual inventory system has been developed which currently tracks all safekeeping inventory.

No exception were noted.

Did the Treasurer's Office properly handle unclaimed property in accordance with the requirements of State law?

The Unclaimed Property Division seeks to return various forms of unclaimed property to the rightful owners or heirs. Unclaimed property is property that is presumed abandoned if it is unclaimed by the apparent owner during the time set forth in K.S.A. 58-3935 for the particular type of property. All property that meets the statutory requirements for presumption of abandonment must be reported and remitted to the State Treasurer. The State Treasurer, upon taking possession of the abandoned personal property, becomes the custodian in perpetuity, preserving the right of the original owners or heirs to claim the property.

The Unclaimed Property Division is divided into two sections: Holder Services and Owner Services. Holders of unclaimed property are required to submit unclaimed property and an "Unclaimed Property Holder Report" form annually per K.S.A. 58-3950. The property is received by Holder Services. When safe deposit box contents are remitted to Holder Services, an inventory is taken and the contents are secured in the vault. In accordance with K.S.A. 58-3955, tangible property must be sold within three years after receipt of the property unless, in the judgment of the State Treasurer, the probable cost of sale exceeds the value of the property. If a claim is received after the property has been sold, the owners receive the proceeds from the sale.

When the unclaimed property is money, the funds are posted by a Holder Services employee to the Unclaimed Property System. All funds received by the Unclaimed Property Division are deposited in the State's General Fund in accordance with K.S.A. 58-3956. Transfers are made from the General Fund to the Unclaimed Property Fund account as needed in order to pay claims. There are also fund transfers to the Unclaimed Property Expense account, which is used to pay all expenses and salaries of the Unclaimed Property Division.

The Unclaimed Property Division reconciles the daily cash receipts and disbursements activity to the STARS system. Currently, however, there is no reconciliation of the Unclaimed Property Division's cash balance to the total cash balance in the State's General Fund per the STARS system, due to the inability of the STARS system to track balances in sub accounts. The State Treasurer's Office believes that it is not practical to establish a reconciled balance in the State's General Fund, because of the difficulty involved in developing a balance for activity that extends back more than twenty years and was under various levels of accountability.

After all receipts are posted, the Owner Services section assumes responsibility for locating all possible owners and/or heirs. Owner Services uses various methods to locate owners, including, but not limited to, social security number matches, address matches, the State Treasurer's Office website, and local network television events.

When potential owners believe they have unclaimed property held by the State Treasurer, they notify Owner Services. A claim form is sent to the potential owner. This procedure can also be done directly over the Internet. After the completed form is returned, Owner Services reviews it for possible payment. If all the information is accurate, the claim is paid. All claims greater than \$ 1,500 require dual approval. If there are any uncertainties, a letter is sent stating that additional information is required. If there is no response within two years, the claim becomes inactive and the unclaimed property is once again available to be claimed by the original owners and/or heirs.

The procedures for the receipt and processing of safe deposit boxes states that inventory of safe deposit box should be securely and neatly packaged in a new package or container. The outside of the container should be labeled with the property number, date received, owner's name, and initials of the inventory team. Currently, the procedure of writing the owner's name on the outside of the package is not being followed. During fiscal year 2003, the State Treasurer's Office was in the process of revising the procedure to eliminate writing the owner's name on the outside of the package as the computer system tracks this information. We recommend that review and potential revision of this procedure continue to be developed and finalized as soon as possible.

Did the Treasurer's Office properly handle its fiscal agency responsibility?

The STO fiscal agency maintains responsibility as the fiscal agency and paying agent for bond issues for municipalities and state issued bonds. All bonds except for Industrial Revenue Bonds must be registered with the STO. A unique registration number is assigned to each bond issue. For 80 - 90 percent of the municipal bonds issued, the STO becomes the paying agent. Currently, the STO is the paying agent for over 2,100 active issues.

For new bond issues the STO reviews certain key aspects of the bond, such as the name of the municipality, the series of bonds, date, amount, number, maturity, purpose, and name and address of the bondholder to ensure proper registration. A CUSIP number is ordered by the bond underwriter and assigned to each bond issue. The Attorney General reviews the bond transcript to ensure that all legal requirements have been met. The bond printer provides bond stock to the STO. These are inventoried and reviewed for accuracy and completeness and held in the vault until issuance. Upon closing, the bond is issued to the purchaser or Depository Trust Corporation (holder for purchaser). The STO collects a registration and/or certification fee in accordance with the State statute.

The STO is also responsible for collecting the funds needed to pay bondholders. Approximately 30 - 45 days before the due date, a notice is sent to the municipalities stating that a bond payment is due. The municipality informs the STO of the payment process they plan to follow, i.e., check, wire, ACH, date of payment, etc. State statute requires that payments be received by the STO within 20 days of its due date. If payments are not received 20 days prior to its due date, the STO sends a second notice of payment due. (During our examination, we noted several instances in which the municipality submitted payment to the STO less than 20 days prior to its due date. However, the payment was always received by the due date and therefore, the payments to bondholders were never late.) Once the payment is received, a deposit is made and the transaction is posted to the system. A daily reconciliation is performed on the deposits and system entries.

Once funds are collected from the municipalities, STO initiates the payment to the bondholders. An individual from STO posts the transaction to the bonds/coupons, determines the amount needed for payment, and begins the warrant issuance process. A supervisor completes this process by using the End of Day Processing activities. The individual at the disbursement desk reviews the bond and warrant for the propriety of the amount, bondholder and date.

The STO also handles transfers of bond ownership. The old bonds, which must be notarized, are collected from the bondholder. New bonds are retrieved from the vault and are reprinted for the new bondholder. The Treasurer signs the bonds and they are forwarded to the new bondholder. The old bonds are canceled and retained by the STO.

Municipalities are required by Statute to submit a report on its annual indebtedness to the STO by July 15th every year. Most municipalities cannot meet this deadline, therefore, the STO gives them until November to submit their annual indebtedness report so it can be posted on the web-site by January of the following year.

Did the Treasurer's Office properly distribute local taxes and State aid moneys to cities and counties as required by State law?

The Treasurer's Office distributes tax collections and aid money to cities and counties. For those calculations made by the Department of Revenue (DOR) a memo is submitted to the STO by DOR authorizing the total amount and a payment voucher. The warrant department transfers the data from DOR and prints a report showing the amount to be paid to each city/county. The warrant information is then processed to the Division of Accounts and Reports for distribution in a similar fashion to other state warrants. Approximately 40% of the local units utilize ACH as their distribution method.

For the remaining distributions not calculated by the Department of Revenue, the Treasurer and the Department of Administration provide the support for the calculation defining the distributions. The warrant preparation and distribution is handled as previously described. The following table outlines the taxes and local aid distributions.

Distributions Description	Statutory Distribution Dates	State Treasurer's Distributions Dates	Distributed to Whom	Who Calculates Distribution Amount
<u>Local Ad Valorem Tax Reduction (LAVTR)</u> – FY 2003 distribution statutorily set at \$26,246,722 on each distribution date. State sales tax distribution based 65% on population and 35% on tangible valuation – also considering a base year amount.	January 15* and July 15	Same as statute	Counties	Department of Administration and State Treasurer's Office
<u>County and City Revenue Sharing</u> – FY 2003 distribution statutorily set at \$16,740,646 on each distribution date. State sales tax distribution to the counties are based 65% on population and 35% on tangible valuation. The funds allocated to the county are then allocated based on ½ remaining at the county and ½ are allocated to the cities in the county based on population.	July 15 and December 10*	Same as statute	Counties and cities	Department of Administration and State Treasurer's Office
<u>Local Alcoholic Liquor</u> – Collections of the liquor private club tax. Distributed to the locality in which the club resides. Cities with a population of (1) more than 6,000 will receive 70% and (2) 6,000 or less will receive 46 2/3% of the total collected from the respective localities. The county receives (1) 70% of the total funds collected outside the corporate limits of any city, and (2) 23 1/3% of the amount collected within a city with a population of 6,000 or less.	March 15, June 15, September 15 and December 15	Same as statute	Counties and cities	Department of Revenue
<u>Special City and County Highways Distributions</u> – Collections of the state's motor fuel gallonage tax plus certain demand transfers from the SGF. Factors of calculations include avg. miles of travel; total miles of road; registration fees collected.	January 15, April 15, July 15 and October 15	Shortly after statute date	Counties and cities	Department of Administration and State Treasurer's Office
<u>Highway Equalization Distribution</u> - \$ 2.5 million collected from State's motor fuel gallonage tax is distributed to counties either to make up a deficit or on the regular calculation method.	April 15	April 18	Counties	State Treasurer's Office
<u>Rental Motor Vehicle Excise Tax</u> – Excise tax collections distributed to counties where transaction took place.	June 30 and November 30	Same as statute	Counties	Department of Revenue
<u>Transient Guest Tax</u> – Guest tax collections distributed to localities where the transaction took place.	January 30, April 30, July 30 and October 30	Same as statute	Counties and cities	Department of Revenue
<u>Local Retail Sales and Compensating Use Tax</u> – Collections have historically been distributed monthly since the funds are truly local moneys. Funds are distributed according to Dept. of Revenue instructions.	At least quarterly	Monthly	Counties and cities	Department of Revenue

*These distributions were not made during the year ending June 30, 2003 due to legislative action.

<u>Tax Increment Financing Revenue Replacement</u> – Method for cities with redevelopment districts established prior to July 1, 1996 to recoup any reduction of ad valorem taxes imposed on those districts due to legislative changes in the school finance formula. Once a year each city with an affected district certifies to the Director of Accounts & Reports an amount equal to the amount of tax reduction. Subsequently, the Director of Accounts & Reports certifies these amounts to the Treasurer who then pays each city its certified amount prior to April 15.	April 15	March 30	Cities	Department of Administration
<u>Racing Admissions Aid</u> – Taxes are imposed for: (1) 10% of (a) the amount received from charges for admissions, excluding any amount paid for retailers sales tax; and (b) the value of free or complimentary admissions, computed as if regular & usual rates were charged; and (2) Racetrack sites exempt from local and ad valorem property taxes must collect \$0.20 on each admission and remit those funds to the racing commission.	Quarterly	Same as statute	Counties and cities	Racing Commission

Did the Treasurer's Office properly administer the Agricultural Production Loan Deposit Program and other linked deposit programs as required by State law?

The Agricultural Production Loan Deposit Program was authorized by House Bill 2527 during the 2000 Legislative Session and began July 1, 2000. The purpose of the program is to provide money to lenders at less than market rates that will be loaned to farmers to fund their operating expenses. The program has a pool of \$ 55 million to draw from and funds will be provided on a first come, first serve basis. The maximum loan per borrower is \$ 250,000 with a term of up to eight years at a rate that is 2% less than the current market rate through April 16, 2003 (as determined by PMIB). On April 17, the Legislature passed House Bill 2055. This bill amends K.S.A. 75-4272.1(c) and sets the maximum loan rate to borrowers at 4% until June 30, 2003, when the maximum loan rate will be 4% greater than the interest rate on the agricultural production loan deposit with the State Treasurer. Until July 1, 2003, the change affects only new loans. Any current outstanding loans still fall under the old rules.

A Certification of Compliance by Lending Institution must be completed by each lending institution who wishes to participate in the program. The certification states that the lender has performed the following: (1) received written certification from each of the borrowers evidencing the borrowers' eligibility for this program, (2) approved the loan package submitted by each of the borrowers based on its internal guidelines of creditworthiness, (3) ensured that no other agricultural production loan is outstanding to any of the borrowers, and (4) once approved, the lender will fund the loan to each approved eligible agricultural borrower.

The Agricultural Borrower's Certification of Eligibility (as defined above) must be completed by each borrower and submitted to the lending institution upon application. The borrower certifies the following: (1) the borrower is an entity that is involved in farming, (2) the borrower has a debt-to-asset ratio of 40 percent or greater, (3) the borrower does not have another loan outstanding under this program, and (4) the loan will be used exclusively for operating expenses involved in farming.

A loan package (consisting of both certifications noted above) is submitted to the STO by the lending institution. The STO reviews the loan package and approves it for future funding. If funds are available, the STO certifies the amounts and terms with the PMIB. PMIB posts applicable interest rates on its website on a daily basis. STO refers to these rates when administering a new loan. Upon approval and funding availability, PMIB places a deposit in the amount certified by the Treasurer with the eligible lending institution. On an annual basis, STO confirms the loans outstanding with each lending institution.

Interest rates change every July 1 and January 1 and are reported to the eligible lending institutions. Interest payments are due twice a year (the first banking day following June 30 and December 31). Per State statute, STO and PMIB must give the lending institutions 14 days notice of interest payments that are due before they can electronically withdraw the money from the lending institutions. The June 30, 2003 and December 31, 2002 payments were received in a timely manner.

State statute requires a re-certification of lending institutions and borrowers biennially. Re-certifications were performed in January 2003. The STO reported on this program as part of their annual report to the State Legislature.

Did the Treasurer's Office properly administer the Kansas Postsecondary Education Savings Program as required by State and Federal law?

The Kansas Postsecondary Education Savings Program was created by the 1999 Legislature and was implemented July 1, 2000. This program permits individuals and organizations to contribute to education savings accounts to pay postsecondary education expenses for individuals they designate or for themselves. The program allows tax advantages under both Kansas and federal law. The STO administers the program and American Century Investments (ACI) of Kansas City is the program manager. ACI is responsible for individual education savings accounts and ensuring that all aspects of the program comply with the Internal Revenue Code Section 529, as amended, applicable to qualified state tuition programs.

During 1999, the STO sent out request for proposals for investment managers to manage the funds collected for this program. The request went nationwide and only eight companies responded. Through various meetings, a committee narrowed the companies to three and requested additional information from them. After further review, the STO chose American Century Investments to manage the investments for this Program.

When an individual is interested in participating in this program, an enrollment kit is mailed to them by ACI or by the Program's administrative office. Once the enrollment kit is completed, it is mailed directly back to ACI, who then establishes an account for the participant (account owner). Account owners receive quarterly statements from ACI and a 1099 at year-end.

The Program Director receives weekly reports from ACI regarding the number of account owners and the dollar value of total investments by Kansas and out-of-state account owners compared to total. In addition, the Program Director receives monthly and semi-annual reports, which include the same information plus various statistics on the account owners such as age range, household income, etc.

Account owners must pay an annual fee of \$ 10, which is deducted from the account and retained by ACI. ACI also charges a management fee of 1% of portfolio value. The STO is reimbursed quarterly by ACI for administrative costs, which is in accordance with the management agreement. During fiscal year 2003, the STO billed ACI the amount budgeted for administrative costs and these fees were deposited into a fee fund account.

In accordance with State statute, the STO elected to have the program audited this year. The audit was conducted by PricewaterhouseCoopers, LLP and an unqualified opinion was issued on August 15, 2003. As part of its audit, PricewaterhouseCoopers, LLP tested ACI's compliance with the State statutes regarding the procedures for establishing and maintaining accounts for the account owners. No major deficiencies were noted. The STO did not elect to perform its own separate examination of ACI and the program since it was audited in the current year.

On August 5, 2003, the Interim Program Director and the STO presented an annual update to the Kansas Legislature.

Summary

Our observation of the efforts of the STO is that the employees are experienced, dedicated and responsive to the mission of that office.

Recommendations

1. During fiscal year 2003, the State Treasurer's Office was in the process of revising unclaimed property procedures. However, these updated procedures had not yet been finalized. We recommend the policy be finalized and implemented.



STATE OF KANSAS

Lynn Jenkins, CPA

TREASURER

900 SW JACKSON ST. SUITE 201
TOPEKA, KANSAS 66612-1235

TELEPHONE
(785) 296-3171

November 17, 2003

Karen Keehn
Berberich Trahan & Co., P.A.
Certified Public Accountants
3630 SW Burlingame Road
Topeka KS 66611-2050

RE: Performance Audit Report

Dear Ms. Keehn:

Thank you for the opportunity to respond to the recommendation you made as a result of the recently completed performance audit.

The following is your recommendation and our response:

1. During fiscal year 2003, the State Treasurer's office was in the process of revising unclaimed property procedures. However, these updated procedures had not yet been finalized. We recommend the policy be finalized and implemented.

The policy will be finalized and implemented by January 1, 2004.

It is a pleasure working with you and your staff. We appreciated the open discussion we were able to have with you and your staff throughout the process.

Sincerely,

A handwritten signature in cursive script that reads "Lynn Jenkins".

State Treasurer Lynn Jenkins

**Legislative Division of Post Audit
Performance Audit Reports on
Financial Management
Issued In Recent Years**

03PA15	Firefighters Relief Fund: Reviewing the Use of Fire Insurance Premium Taxes Distributed to Local Firefighters Relief Associations (100-hour audit)	April 2003
03PA22	General Fund Cash Balance: Reviewing the Projected Fiscal Year 2003 Ending Cash Balance for the State's General Fund (100-hour audit)	April 2003
03PA13	Financing Local Governments: Determining How to Avoid Future Problems Caused by State Revenue Shortfalls (100-hour Audit)	February 2003
03PA12	Reviewing the Projections Presented by the Kansas Public Employees Retirement System Regarding the Need for a Long-Term Funding Plan	February 2003
03PA23	Reviewing the Operations of the State Treasurer's Office	December 2002
03PA08	Reviewing the Operations of the Pooled Money Investment Board	December 2002
02PA10	School District Budgets: Determining Ways to Structure the Budget Document to Make It Understandable and Allow for Meaningful Comparisons	March 2002
02PA12	Reviewing the Operations of the State Treasurer's Office, FY2001	January 2002
02PA11	Reviewing the Operations of the Pooled Money Investment Board, FY2001	January 2002
01PA02	State-Held-Lands: Reviewing the Management and Use of Those Lands in Kansas	December 2000
01PA09	Reviewing the Operations of the State Treasurers's Office	December 2000
01PA10	Reviewing the Operations of the Pooled Money Investment Board	December 2000
00PA09	Reviewing the Operations of the State Treasurer's Office-Fiscal year 1999	February 2000
00PA10	Reviewing the Operations of the Pooled Money Investment Board-Fiscal Year 1999	February 2000
98PA49	Reviewing Financial Transactions of the Board of Cosmetology (100-hour audit)	May 1998
98PA47	Reviewing the Kansas Development Finance Authority's Selection of Bond Counsel and Costs of Issuing Bonds	May 1998
97PA59	Reviewing the Attorney General's Expenditures for Water Rights Litigation and Procedures for Selecting Attorneys	October 1997
97PA49	Reviewing the Department of Social and Rehabilitation Services' Efforts to Privatize Government Services (100-hour audit)	March 1997
97PA46	Reviewing the Operations of the Kansas Highway Patrol Motor Vehicle Program	December 1996
96PA38	Reviewing State Contracting for Consultants and Other Professional and Technical Services	April 1996
95PA52	Examining Contract Oversight by the Department of Social and Rehabilitation Services	July 1995
95PA59	Reviewing Certain Investment Transactions of the Municipal Investment Pool	June 1995