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Auditor of State

From: Auditor of State's Center for Audit Excellence
To: All IPA Firms
Subject: AOS State Region Memo over TOS – OPCS – 6/30/18
Date: October 1, 2018

The bi-annual report (memo) over the Office of the Ohio Treasurer of State (TOS) – Ohio Pooled Collateral System (OPCS) for the period of January 1, 2018 through June 30, 2018 (referred to in Ch. 2-9 of the 2018 OCS) from the Auditor of State (AOS) State Region is now available (attached).

Note: The memo for the period July 1, 2017 through December 31, 2017 was communicated on May 25, 2018 and can be accessed at:

<https://ohioauditor.gov/ipa/correspondence/May%202018/2018-05-25%20WEB%20State%20Region%20memo%20over%20TOS%20-%20OPCS.pdf>.

Below is the guidance we sent to AOS auditors relating to this memo. IPAs should determine the audit implications for their specific audits.

Auditors should review and include this memo in the working papers for audits where the auditee had significant deposits with financial institutions enrolled in the Ohio Pooled Collateral System (OPCS). To aide in consistency, auditors should understand the implications of the noted errors as follows:

- **Issue 1 summary:** The previous report had an error that indicated the OPCS did not have controls in place in order to allow the State Region to obtain sufficient assurance over the accuracy of the daily bank information. Similarly, this report alludes to the fact there are no confirmations of the bank balances done.
 - **Implication:** This process is set up and operational as of September 2018. However, since it was not operational or able to be relied upon for the audit period, auditors should perform their own comparisons. Auditors should compare bank balance information in the OPCS to available confirmations (and/or bank statement information) and investigate any discrepancies with the client, with CFAE, and if necessary with the Financial Institution and the TOS (administrator of OPCS).
- **Issue 2 summary:** No procedure was in place until May 2018 to monitor OAC 113-40-04(A)6g (Public moneys limited to 30% of total bank assets),
 - **Implication:** While there was no process in place prior to May 2018, one was in place as of May 2018. When implementing it, the TOS also re-evaluated all previous approvals for reduced collateral. No issues were found with this

requirement, and therefore auditors should not need to include any specific mention of it in local audits.

- **Issue 3 summary:** For 1.8% of the OPCS pools, collateral pledged was not in compliance with ORC 135.182(B).
 - **Implication:** 1.8% is not considered significant, so this issue does not broadly effect all. The financial institution that had the issue (Community Bank) promptly corrected the issue within 2 days, so this likely should not be considered a reportable issue on its own for entities that use this financial institution.

Questions related to the Ohio Pooled Collateral System can be directed to Jesse Carroll at JMCarroll@ohioauditor.gov.



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MEMORANDUM

TO: Bob Hinkle, Chief Deputy Auditor
FROM: Debbie Liddil, Chief Auditor, State Region
DATE: September 25, 2018
RE: Office of the Ohio Treasurer of State (TOS) – Ohio Pooled Collateral System (OPCS)

As requested by senior management, the State Region performed audit procedures over OPCS for the period of January 1, 2018 through June 30, 2018 to support local audits. The procedures and results of the work performed are summarized below:

1. Control Procedures: We completed a systems narrative and control procedures were tested over application approval, reduced collateral application, reduced collateral bank monitoring, collateral position, collateral compliance, and collateral sufficiency. The manual controls were tested (for implementation) by the TOS financial auditors and the automated controls were tested by our ISA group (RCEC and application controls).
2. Substantive Procedures:
Note: Procedures were performed over the collateral only. Confirmation of the deposit balances should be completed at the local level.
 - Collateral – As of June 30, 2018, 55 financial institutions (FI) were enrolled** in OPCS. We obtained the Pooled Collateral report, which included the collateral sufficiency analysis for the main pools of all 55 financial institutions in OPCS, and scanned the report to ensure all the pools were collateralized in accordance with their collateral floor.
 - We then selected a sample of 30 pledged securities out of 3,246 total pledged securities as of June 30, 2018 (note: we selected each security from a different FI) and tested to ensure:
 - A. The collateral was appropriately priced.
 - B. The securities pledged as collateral were eligible per ORC 135.182(E)
 - Perfected Security Interest – Perfecting of the security interest is established as part of the application process. AOS Legal reviewed TOS' legal opinion and agreed that the application and executed security agreement sufficiently addressed the perfecting of the security agreement.
 - Reduced Collateral Banks – As of June 30, 2018, 11 FIs were approved within OPCS to have a reduced collateral floor of 50%. We selected a sample of three reduced collateral FIs and tested to ensure:
 - A. The FI participated in OPCS for at least thirty days prior to implementing the reduced collateral floor per OAC 113-40-03(D)
 - B. All data elements of the SCALE checklist were completed prior to the approval of the reduced floor.

- C. The SCALE Composite and Component average score was 2.25 or less for the current and past five quarters per OAC 113-40-04(A)6.
- D. The SCALE Report met all the required variables for the average of the preceding five quarters per OAC 113-40-04(A)6.
- E. The FI was in good standing with government regulators with respect to their deposit business per OAC 113-40-04(A)6.
- F. The FI's public deposits did not exceed 30% of its total assets per OAC 113-40-04(A)6.

*** - The enrollment date and the go-live date are the same.*

3. Conclusion

We noted the following errors:

- The Office had planned procedures to confirm the deposit balance reported by the FI via negative confirmation by the public unit on a periodic basis. However, due to the very limited participation of the public units in OPCS as of the period end date, management postponed the confirmation until September 2018 (also identified in the 12/31/17 testing memo).
- Per OAC 113-40-04(A)6g, in order for financial institutions to be approved for a reduced collateral floor they must not have received or have on deposit at any one time public moneys in an aggregate amount in excess of thirty percent of its total assets. However, prior to May 2018, TOS did not have procedures in place to verify whether FIs were in compliance with this requirement.
- For one of 55 (1.8%) of the OPCS pools, the collateral pledged was not in compliance with ORC 135.182(B). The pledged collateral was 77% of uninsured deposits or 25% less than the required 102%. The financial institution (Community Bank) corrected the deficiency in two business days.

No other errors were identified during testing.