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F I S C A L I M P A C T R E P O R T

SPONSOR Muñoz **ORIGINAL DATE** 2/25/15 **LAST UPDATED** 3/8/15 **HB**

SHORT TITLE Daily Reconciling of Certain State Accounts **SB** 543/aSFC

ANALYST Malone/Griego

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY15	FY16	FY17	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total		Minimal	Minimal	Minimal	Recurring	DFA Operating
		Minimal	Minimal	Minimal	Recurring	STO Operating

(Parenthesis ( ) Indicate Expenditure Decreases)

Related to SJR 11, which proposes amending the Constitution of New Mexico to require daily cash reconciliation.

SOURCES OF INFORMATION
LFC Files

Responses Received From
Department of Finance and Administration (DFA)
State Treasurer's Office (STO)
Office of the State Auditor (OSA)
Department of Information Technology (DoIT)

SUMMARY

Synopsis of SFC Amendment

The Senate Finance Committee amendment to Senate Bill 543 requires monthly, rather than daily, reconciliation. Monthly reconciliation is what is currently required by statute and generally accepted at industry best practice.

By eliminating the requirement for daily reconciliation, much of the fiscal impact noted under the synopsis of the original bill is no longer pertinent (tables have been updated to reflect this). In fact, the remaining requirements ought to be achievable with current funding levels and HB 2, theGeneral Appopriation Act, includes an additional 6 FTE for the Financial Control Division, a special appropriation to fully fund the second phase of cash reconciliation for SHARE (about $4 million), and a special appropriation to fund the implementation of software to develop the state comprehensive annual financial report (CAFR), Hyperion (about $2 million). There may be some minimal operating budget impact at DFA and STO related to the quarterly reporting requirement of the bill.

Synopsis of Original Bill

Senate Bill 543 creates new statutory language requiring the State Treasurer and the Financial Control Division (FCD) of DFA to reconcile cash accounts daily and report at least quarterly to the governor and the Legislature on the state of the state budget. The bill requires four distinct forms of reconciliation, which are:

1. STO is required to reconcile the daily bank action to the state's register
2. FCD is required to reconcile the register to the general journal
3. FCD is required to reconcile the general journal to the general ledger (SHARE), and
4. STO is required to reconcile balances between the investment banker and the fiscal agent banker.

The quarterly report prepared by the State Treasurer and the director of FCD on the state of the state must include details of each agency's budget, note of cash reconciling items that have not been cleared, the number of errors during the quarter, documentation of state reserve accounts, and a comparison of the state budget to the latest economic forecast.

Additionally, SB 543 amends several sections of NMSA 1978 to require third-party payers to conform to the uniform statewide accounting system network and accounting methods and procedures.

FISCAL IMPLICATIONS

Daily reconciliation of all cash accounts will require increased resources at STO and DFA.

According to DFA, if the current banking structure is kept at 172 fiscal agent bank accounts, the department estimates it would require approximately 57 additional FTE in FCD. This does not include the current Cash Control staff of four or the additional request for six FTE for FCD made for FY16 (which is supported in the HAFC-adopted budget recommendation). The additional 57 FTE would be needed to perform the daily reconciliations and to track communications with agencies. Additionally, DFA estimates the Help Desk would need an additional two FTE to reconcile the various SHARE modules to the SHARE general ledger and work with DoIT to resolve system issues in a shorter timeframe. Finally, the department projects that the Budget Control Group would need one FTE to coordinate between all of the Financial Control Divisions, agencies and STO to create the quarterly report. The department estimates the costs of these FTE as follows:

- 57 (FTE) x $65,000.00 (average salary) = $ 3,705,000.00 x 30% benefits = $1,111,500.00 + $3,705,000.00 = $4,816,500 FCD FTE
- 2 (FTE) x $48,960.00 (average salary) = $ 97,920.00 x 30% benefits = $29,376.00 + $97,920.00 = $127,296.00 DFA Helpdesk FTE
- 1 (FTE) x $65,000.00 (average salary) = $65,000.00 x 30% benefits = $19,500.00 + $65,000.00 = $84,500.00 Budget Division FTE
- Total impact would be over $5 million annually

STO predicts the most critical fiscal implication of the bill would be the need for a new system at STO to allow adequate tracking of bank activity, but does not have an estimate of the cost of such a system at this time. The office notes that in order to accomplish an independent reconciliation of the bank activity and bank balances to the activity and balances recorded within the SHARE System by the various agencies by agency and fund, STO would require a separate, independent system into which daily bank activity will be uploaded by business unit (agency) and fund.

STO receives reports of all money from any source in the agency's custody on a monthly basis. There are approximately 374 bank accounts that are reported to STO monthly. The requirement that they report daily would greatly increase the workload at STO and the office estimates needing two additional FTE at a total cost of $186 thousand annually.

SIGNIFICANT ISSUES

1. Accurate and timely cash reconciliation, which the state has lacked since the implementation of SHARE in 2007, is key to ensuring financial accountability and has important implications for the state. DFA has booked a $101 million contingent liability against the state's operating reserve fund to account for historical cash variances between SHARE and the bank (although the department is uncertain if that sum is large enough and acknowledges that shortfalls could be much greater) and has taken steps to remediate cash control processes on a go-forward basis since 2013. See attachment 1 for detailed background on the state's cash control problems and remediation efforts.

2. The requirement contained in this bill for the State Treasurer to reconcile the daily bank action to the state's register has been occurring since the completion of DFA's first cash control remediation project in 2013. STO's response to this legislation notes that the office would need a new system to track bank activity in order to perform daily reconciliation, but there is already a cash management module built into SHARE that offers this functionality and is what the office currently uses to complete this daily reconciliation.

3. The requirement for FCD to reconcile the register to the general journal and then the general journal to the general ledger on a daily basis is slightly redundant and overly frequent. Standard accounting practices dictate monthly reconciliation of the general ledger to bank statements, referring back to the general journal and register to resolve variances identified in the monthly reconciliation. Furthermore, daily reconciliation is untenable. While there is merit to reconciling more frequently than every month (current practice), daily reconciliation would likely prove to be uninformative because so many transactions in each agency fund would be in-transit. Perhaps a bi-weekly reconciliation would be more practical and informative.

4. Requiring STO to reconcile the balances between the investment banker and the fiscal agent banker is a very good idea in order to maintain control of cash moving between these two entities. Currently, the monthly cash reconciliation performed at FCD does not include any bonds, and tracking of cash movement between the fiscal agent and investment accounts at STO is unknown. Requiring that bonds are included in reconciliation is a good practice.

5. Quarterly reporting to the governor and the Legislature would offer greater oversight of cash control in the state. Furthermore, it presents the regular opportunity to revisit business process, evaluate what practices are working and which are creating problems,

and adjust accordingly such that persisting cash control problems are identified and corrective action can be taken.

6. Finally, requiring third-party payers to conform to the uniform statewide accounting system network and accounting methods and procedures is important for creating financial transparency and accountability, as these transactions account for the vast majority of warrants issued by the State. Cash Remediation Phase II, which is scheduled to begin at the end of February 2015, will address this issue and integrate third-party payers into Share.

PERFORMANCE IMPLICATIONS

Addressing the state's cash control issues could help DFA prepare the state Comprehensive Annual Financial Report (CAFR) in a timely manner and facilitate the external auditing process.

ADMINISTRATIVE IMPLICATIONS

Both DFA and STO would have substantial new administrative duties as a result of this resolution.

RELATIONSHIP

Relates to SJR 11, which also dictates daily reconciliation

TECHNICAL ISSUES

The state fiscal agent bank produces official statements on a monthly basis. The daily transactions that are provided to the State are not guaranteed to include all transactions, the monthly statements are the official record of the activities at the fiscal agent bank. The fiscal agent bank's detailed checks report, which is a critical part of the current monthly reconciliation process, is provided on a monthly basis. The disbursement bank accounts cannot be reconciled without this report.

OTHER SUBSTANTIVE ISSUES

OSA supports the objective of addressing cash reconciliation problems, resolving historical discrepancies between the book and bank, and implementing appropriate accounting practices.

ALTERNATIVES

Currently the Cash Remediation Phase II project is not 100% funded. Both the executive and the legislative budget recommendations for FY15 include approximately $4 million dollars of funding for Cash Remediation Phase II. The Cash Control Bureau recommends that the funding be provided.

Additionally, the executive budget recommendation for FY15 includes a request for six additional FTE for FCD. The changes that will be implemented during the Cash Remediation Phase II project will require six additional FTE to perform the daily activities that will be necessary after the completion of the project. The HAFC passed budget bill includes funding for these FTE.

Consider the possibility of requiring reconciliation on a less frequent basis, perhaps bi-weekly, in order to maximize the benefits from such reconciliation.

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