MINUTES OF THE MEETING OF THE
AUDIT SUBCOMMITTEE OF THE LEGISLATIVE COMMISSION
Legislative Building
401 South Carson Street, Room 4100
May 21, 2007

This is the first meeting of 2007.

A meeting of the Audit Subcommittee of the Legislative Commission (NRS 218.6823) was called to order by Assemblywoman Sheila Leslie, Chair, at 3:04 p.m., Monday, May 21, 2007, in room 3143 of the Legislative Building, Carson City, Nevada, with a simultaneous video conference to room 4401 of the Grant Sawyer State Office Building, 555 East Washington Avenue, Las Vegas, Nevada.

AUDIT SUBCOMMITTEE MEMBERS PRESENT:

Assemblywoman Sheila Leslie, Chair
Assemblyman John Marvel, Vice-Chair
Assemblyman Morse Arberry Jr.
Senator Bob Coffin
Senator Dean A. Rhoads

LEGISLATIVE COUNSEL BUREAU STAFF PRESENT:

Paul Townsend, Legislative Auditor
Stephen Wood, Chief Deputy Legislative Auditor
Donna Wynott, Office Manager
Daniel Crossman, Deputy Legislative Auditor
Rick Neil, Audit Supervisor

The roll was taken. A quorum was present.

Item 1—Approval of minutes of the meeting held on December 14, 2006

Chair Leslie called for a motion.

> ASSEMBLYMAN ARBERRY MOVED TO APPROVE THE AUDIT SUBCOMMITTEE MINUTES OF DECEMBER 14, 2006. THE MOTION WAS SECONDED BY ASSEMBLYMAN MARVEL AND CARRIED UNANIMOUSLY.

Item 2—Presentation of audit report (NRS 218.823)

A. Office of the State Treasurer, Nevada College Savings Program

Paul Townsend, Legislative Auditor, introduced Steve Wood, Chief Deputy Legislative Auditor; Rick Neil, Audit Supervisor; and Daniel Crossman, Deputy Legislative Auditor and in-charge auditor on this audit. He explained the Nevada College Savings Program had achieved extraordinary success in helping families to save for college. The Program was created in 2001 and had experienced tremendous growth. As of December 31, 2006, there were over 320,000 accounts with total assets of $3.2 billion. Mr. Townsend added almost every state had a college savings plan and Nevada ranked as the seventh largest plan in the country. Mr. Townsend stated it was important to note that participant investments that make up this $3.2 billion were handled by large national firms. Auditors found that the participants' investments were properly handled and accounted for. Mr. Townsend noted the issues within the report addressed the handling and accounting of fees that were due to the state. He stated Mr. Daniel Crossman would begin the presentation of the audit.

Mr. Crossman began the presentation with background information. The Legislature established the Nevada College Savings Program and Nevada College Savings Trust Fund, in 2001, through Assembly Bill 554. The Program's mission was to increase the number of families who save for higher education expenses, thus allowing more students to go to college. He explained the Program was administered by the Office of the State Treasurer and the Board of Trustees of the College Savings Plans of Nevada, and qualified as a section 529 plan under the U.S. Code.

As of December 31, 2006, the State's program consisted of $3.3 billion in assets, which included 1.4% in investments by Nevada residents. Exhibit 1 demonstrated the current structure of the Program including the current contracted Program Manager, Upromise, and the four available investment plans. The next exhibit detailed the values of the assets held in each of the four plans as of December 31, 2006. Mr. Crossman noted that Nevada's program was the seventh largest in the country based on total assets.

Mr. Crossman stated audit objectives were to determine whether the financial activities of the Nevada College Savings Trust Fund were properly accounted for, and whether the operations of the Program had been conducted in accordance with applicable laws, regulations, and contractual obligations.

Findings and recommendations of the report found participants' money in the Program was properly handled and accounted for. However, money earned by the State was not. More than $6 million of state funds were held outside the state's system and used to pay program expenses resulting in authorized expenditure limits being exceeded. Additionally, the Trust had not been properly or fully accounted for in the State's accounting system. Finally, statutory and other requirements for contracting services were not always followed.

Mr. Crossman explained that of the $11.2 million in funding available to the state since the Program's inception, more than $6 million was not deposited in the State Treasury. Pursuant to instructions from officials in the Treasurer's Office, the Program Manager held a portion of the State's funds rather than remit them for deposit in the State Treasury. It was determined that $2.6 million of funds held by the Program Manager were used to pay administrative and marketing expenses outside of the state's system. Furthermore, more than $3.4 million was paid directly to the Plan Advisor from state funds held by the Program Manager.

Another report exhibit detailed the sources of program funds by fiscal year which totaled $11.26 million and included program fees of over $8.8 million; marketing and administrative support of over $2.1 million; and other funding sources earned by the state of over $250,000. The next exhibit detailed the total deposits made in the State's Accounting System over the same period which totaled $5.2 million.

Mr. Crossman explained another exhibit showed the $6 million in Program funds that were not deposited in the State's Accounting System, and were outlined by fiscal year. He pointed out that financial administration laws, the State Budget Act, and statutes governing the Program required funds be deposited and disbursed through the State Treasury.

Mr. Crossman explained that some State funds were held and disbursed by the initial Program Manager, Strong Capital Management, at the direction of officials in the Treasurer's Office. Of the $1.4 million in marketing and administrative support the State received under the contract with the Program Manager (Strong), only $590,000 was deposited in the State Treasury. Another exhibit detailed the disposition of the $1.4 million in marketing and administrative support from Strong Capital Management. Mr. Crossman highlighted some of the larger categories including Plan Advisor expenses of $200,000, advertising and marketing expenses of over $200,000, and legal expenses of $380,000.

Mr. Crossman reported that, at the direction of officials in the Treasurer's Office, state funds earned from the Vanguard plan were held by the Program Manager (Upromise) beginning in March 2003 until December 2006. During this period, a total of $3.2 million of state funds earned under the Vanguard plan were held by the Program Manager, of which $1.1 million was paid to the Plan Advisor and $1.2 million was used to pay Program expenses outside of the State's system at the direction of officials in the State Treasurer's Office. He pointed out that the Treasurer's Office staff did not maintain an adequate record of the amounts held by the Program Manager. Mr. Crossman explained on several occasions, staff had to ask the Program Manager how much state money was being held.

The audit report identified other examples where Program funds earned by the state were not deposited into the State Treasury and were used to pay Program expenses. Two examples included $298,580 in state fees earned from the USAA plan which were, at the direction of the officials in the State Treasurer's Office, sent to the law firm representing the Program. The second example related to $900,000 in marketing and administrative support payments from the Program Manager. Of this amount, only $200,000 was deposited in the State Treasury.

Chair Leslie asked for a potential reason why anyone would not have recorded these funds through the State budget system. She could not understand how this could have happened.

Mr. Townsend replied in the course of the audit there were several reasons given for this happening. In the report, one of these reasons was referenced to a specific statute. He explained the laws related to the savings programs plan provided for certain monies to be held outside the Trust Fund. However, even though they were supposed to be held outside of the Trust Fund, they were still required to be accounted for within the Treasury. Another reason provided by the former Treasurer was that in a contract agreement with the Program Manager they felt these advertising funds were supposed to be paid by the Program Manager. Mr. Townsend noted there had been a couple of reasons given, however, auditors had not been able to reconcile these and did not agree with them.

Chair Leslie added it was illegal. She asked how the state's money would not be in the State Treasury.

Mr. Townsend stated the statutes required that all money be deposited in the State Treasury, a fact confirmed by the Legislative Counsel in a legal opinion that was included in the report.

Assemblyman Marvel asked if all the money had been tracked.

Mr. Crossman replied yes, of the Program revenues identified, auditors were able to account for all of the money spent on program expenses.

Assemblyman Marvel asked for additional information about the tracking of the money and if all of the money had been accounted for.

Mr. Crossman replied yes the money had been tracked to the source of where the funds went.

Chair Leslie asked when auditors stated the money was tracked to the source had the auditors reviewed backup documents which noted how the money was expended.

Mr. Crossman answered yes, based on the records available to the auditors.

Chair Leslie asked who directed these funds that were not in the State Treasury. She referred to emails from the State Treasurer's Office notifying Program officials of the State Treasurer's Office advising the Program Manager not to transmit any future fees to the state. And later in the report emails from the State Treasurer to the Program Manager told them how to spend the money. She asked for an explanation of this section of the report.

Mr. Crossman stated in those two examples the emails were provided by a senior deputy treasurer within the Treasurer's Office.

Chair Leslie asked if it was correct that the State Treasurer's Office was directing the Program Manager how to spend the money.

Mr. Crossman stated that was correct.

Chair Leslie asked if the State Treasurer's Office was using that excuse for why the money was not state money. She was confused about who was telling whom to spend money for what.

Mr. Crossman clarified that auditors looked at the expenditure of the funds held outside of the system. He stated auditors found significant support showing that, at the direction of officials within the State Treasurer's Office, funds held outside the system were asked to be expended on various expenses, whether marketing or legal expenses and they were specific about what funds were to be used and where they were to go.

Chair Leslie interpreted that the State Treasurer's Office was telling Upromise how to spend the state's money on marketing and legal fees.

Mr. Crossman stated that was correct.

Chair Leslie asked for questions from the Committee.

Senator Coffin stated the audit indicated all the money spent was accounted for. He asked of the money disbursed or held by vendors or others outside of the state system had records been reviewed to see how the money was spent. The audit outlined the amounts given to Upromise, Vanguard, legal firms, and marketing and advertising firms. Senator Coffin asked if it was documented how the money was spent by these entities.

Mr. Crossman answered auditors obtained invoices which identified the services provided and the funds used to pay the invoices.

Senator Coffin asked where the information was located in the report.

Mr. Crossman answered the report did not identify each individual invoice. He added, the information was included in the audit work.

Senator Coffin commented that auditors identified what the money was spent for but asked if they were sure the monies were spent as intended.

Mr. Townsend commented about the appendices located in the back of the report. He explained legal billings were categorized by type of charge and hours on the legal billings. He noted advertising invoices and billing records generally indicated what was represented on the invoices. Mr. Townsend added contractor records were not audited as the audit analysis only included the information on the actual invoices.

Senator Coffin stated the audit covered one statute (NRS 353) where policy was not followed in the report. He asked if there were other statutes involved in the audit.

Mr. Townsend answered yes there was a statute where money was required to be deposited in the state system and the audit found this was not done. He added the auditors would elaborate on other examples as the report was presented.

Mr. Crossman continued the presentation. He explained an exhibit showed the disposition of the State earned program fees.

Senator Coffin asked for a more detailed explanation of the exhibit.

Mr. Crossman stated the exhibit was an example of how the State program fees flowed. He further explained the diagram for the Committee. Mr. Crossman stated the next exhibit detailed the disposition of the other funding sources received by the Program. Similarly he explained the diagram for the Committee.

Mr. Crossman stated Steve Wood, Chief Deputy Legislative Auditor, would continue the presentation with the next section of the report.

Mr. Steve Wood, Chief Deputy Legislative Auditor, stated the next section of the report discussed expenses paid outside of the State system, and the effect that had on the Program's budget. Mr. Wood explained during the 5½-year period the Program had been in operation, the Legislature had authorized total expenditures of $1.6 million. He added, more than $7 million of Program expenses had been incurred during that time. Because most of these expenses were paid outside of the State system, the budgetary controls normally associated with State expenditures had been bypassed. As a result, expenses had exceeded the legislatively approved budget each year the Program had been in operation. It was determined that more than $6 million was paid for Program expenses from funds held outside the State Treasury.

Mr. Wood explained the report outlined where these expenses were paid. He reported Plan advisory services totaled $3.4 million, legal services amounted to nearly $1 million, marketing and advertising services were $1.5 million, and, other expenses totaled $45,000, for a total of $6 million spent outside the state accounting system. If the State Treasurer's Office had processed these transactions through the state system, revisions to the Program's budget would have been required. Pursuant to the provisions of the State Budget Act, these revisions would have required approval from the Legislature's Interim Finance Committee. Mr. Wood explained if revisions to the budget had been approved in accordance with statutory provisions, the State Treasurer's Office would have had budgetary authority to process these expenditures through the state system. However, since approval was not requested, the expenses bypassed the budget established by the Legislature.

Mr. Wood explained an exhibit which outlined Program expenditures recorded in the Administrative Budget Account for each year of operation.

Chair Leslie recognized Senator Coffin.

Senator Coffin asked if Mr. Wood was referring to the same statute, NRS 353, as in previous testimony.

Mr. Wood stated yes that was a part of the State Budget Act. He further explained the provisions required that all funds be spent in accordance with the Legislative Budget.

Chair Leslie stated the first violation was that the money was not run through the State Treasury and the second violation was that the expenditures also were not run through the State Treasury.

Mr. Wood stated that was correct. He added the money also was not run through the State Budget System as specified by the Legislature.

Chair Leslie stated the Legislature had no control or knowledge of any of the $6 million noted in the report.

Mr. Wood stated that was correct.

Mr. Wood continued the presentation. He stated the total expenditures charged against the budget authorized by the Legislature amounted to just over $1 million. An exhibit in the report showed the Program expenses paid outside the State System in addition to those recorded in the Program's Budget Account. The exhibit also showed total expenses of more than $7 million since the Program began.

The total budgeted expenditures authorized by the Legislature since the Program began in 2001, amounted to $1.6 million. Since expenses incurred totaled more than $7 million, Legislature approved budgets were exceeded by more than $5 million. Another exhibit showed the Program expenses paid in excess of the Legislature approved budget for each year of operation.

At the Board of Trustees meeting in November 2006, the Board approved a contract amendment with the Program Manager which restructured the economics of the Program. The report discussed details of this amendment and the effect on the fee structure for future payments.

Senator Coffin asked why the Board agreed to discontinue receiving asset based fees and instead to receive annual payments indexed to inflation.

Mr. Wood answered the parties agreed that the State would no longer receive an asset based fee on the Vanguard or the Upromise plans. They agreed to accept a one-time payment from Upromise and annual payments from the Vanguard plan of $1.5 million. They felt this change was needed to keep Nevada's program competitive with other states.

Senator Coffin clarified that the Treasurer's Office changed its position. He asked if this change was better for the state.

Mr. Wood asked if Senator Coffin was asking if the amendment was good for the state.

Senator Coffin stated that was correct.

Mr. Wood answered it would depend on what would happen in the future. He added it was too early to report whether the state would be better or worse under this scenario. Mr. Wood stated the auditors reviewed other states that received a flat fixed fee and Nevada was competitive.

Senator Coffin clarified that was with the new contract.

Mr. Wood agreed.

Chair Leslie asked Mr. Wood about the members of the Board of Trustees.

Mr. Wood answered the State Treasurer was the Chair. Other members included the Director of the Department of Administration; the Chancellor of the University System which at the present time was a designee of the Chancellor; and two Governor appointees.

Chair Leslie clarified that the State Treasurer served as the Chairman of the Board. She asked Mr. Wood to continue the report presentation.

Mr. Wood continued with information about the contract amendment. Mr. Wood clarified that November 2006 was when the Board of Trustees approved the amendment and December 28, 2006, was the date the Board of Examiners approved the amendment, which was also the effective date of the change.

Mr. Wood stated this amendment contained language indicating all future money payable to the State would be paid to the Board for deposit into the State System. It further indicated that no funds would be expended by the Program Manager on behalf of the Board for marketing or administration, except funds authorized in the State Budget. Prior to the November 2006 meeting, Board minutes did not reflect any discussion of how the Program Manager was to handle the retention or remittance of Program fees earned by the State. Furthermore, information presented to the Board and minutes of Board meetings contained no indication that the Board had ever been informed of how the marketing and administrative support payments were being handled.

Chair Leslie recognized Assemblyman Marvel.

Assemblyman Marvel asked if the auditors had interviewed any of the Board members.

Mr. Wood answered yes.

Assemblyman Marvel asked if the Board members were aware of what was going on.

Mr. Wood stated no, the Board members interviewed were not aware of the money being held outside of the state system.

Chair Leslie asked if the Board had placed their trust in the Chairman of the Board and not reviewed meeting minutes. She was surprised with the high level of people on the Board that this could happen.

Mr. Wood stated auditor work indicated there were areas where the Board did not receive information. A number of the areas were discussed in the report. He stated this included information provided by contractors; information provided by staff; financial information; audit reports; and marketing budgets that were not presented to the Board.

Senator Rhoads asked if the state lost interest due to money being in the wrong hands.

Mr. Wood replied auditors calculated the money held in the Vanguard account and determined $38,000 was lost in interest as a result of the money being held by the Program Manager in a non-interest bearing account.

Chair Leslie asked Mr. Wood to continue the report presentation.

Mr. Wood stated the next area of the report discussed the failure to use the Trust Fund to account for the Program's financial activity. He explained the recordkeeping for participant money was performed by the Program Manager and by the investment firms holding the underlying Trust assets. Although participant money was handled properly, it was not accounted for in the Nevada College Savings Trust Fund, as required by state law. In addition, the portion of the administrative activity that was recorded in the state system was accounted for in the State General Fund, not the Trust Fund as required by statute.

Mr. Wood continued, when the Legislature created the Program in 2001, it created a trust fund to be administered by the State Treasurer. NRS 353B.340 and 350 required that the Trust Fund be used to account for the Program's financial transactions. The statutes also established the following accounts within the Fund: the Program Account for the receipt, investment, and disbursement of participant money; the Administrative Account for the deposit and disbursement of money to administer and market the Program; and the Endowment Account for the deposit of other Trust Fund money.

Mr. Wood noted the only account established in the state system was the Administrative Account. The Program account had not been established in the State's Accounting System to account for participant money. Furthermore, the Endowment Account had never been established. Therefore, despite the framework established by the Legislature to account for Program activity in the Trust Fund, it had not been used.

Instead, the financial activity of the Program had been accounted for as separate units by various parties involved with the Program. This fragmented approach did not provide the level of accountability needed by the State Treasurer to properly administer the Trust Fund or by the Board to properly oversee the financial activities of the Program.

Chair Leslie asked exactly whose responsibility was it to have caught these errors. She stated it was certainly the Board of Trustees' responsibility and the State Treasurer's responsibility to set up the accounts as the law required. She asked if the Legislative fiscal staff should have noticed that the accounts did not exist. She expressed concern that the statute was clear on how these accounts were supposed to be used; yet two of three accounts were never established.

Mr. Wood responded the program was operating because the administrative account was being budgeted so there was a mechanism to fund the administrative activities of the account. The Program account would not be one that would be budgeted. So the budget staff would not necessarily see that one. He stated in the endowment account the Board or the Treasurer's Office had not elected to use it. He stated one of the audit recommendations was to use and set up those accounts.

Chair Leslie asked Mr. Wood to continue the report presentation.

Mr. Wood stated $5.2 million of the $11.2 million in state revenues and just over $1 million of the $7 million in Program expenses had been recorded in the State's Accounting System. Furthermore, each plan in the Program was accounted for and reported on separately outside of the State System; but, this information was not aggregated for a complete financial reporting of the Trust activity. Financial information such as Program and management fees paid from participant accounts, investment earnings on Trust assets, and Trust account balances were not aggregated for presentation in a financial statement. For instance, Trust assets totaled nearly $3.3 billion as of the end of 2006; however, this information was not presented for financial statement reporting purposes.

Chair Leslie recognized Assemblyman Marvel.

Assemblyman Marvel asked where this was reported.

Mr. Wood replied in regard to the Trust assets the four individual plans prepared financial statements but they were all individual. They consisted of the Vanguard piece, a Upromise piece, a USAA piece, and a Columbia piece. They were not aggregated and the statements did not include the detail needed to properly manage the Program.

Assemblyman Marvel asked if the auditors had accounted for all of the money.

Mr. Wood assured the Committee that the Program account (participant money) was all accounted for. The auditors had reviewed the audited statements and were able to tie those into the account activity. He added what was missing was the consolidated view of those as well as the $6 million that was not processed through the State system.

Chair Leslie stated that was a very important point that the Committee would want to make sure the public understood that the participant money was safe, was handled properly, and was properly accounted for. She noted it was just the money that the state was earning which was not properly tracked. Basically, the Treasurer's Office was not using the basic accounting framework. Chair Leslie stated it sounded so simple. She was amazed since the State Treasurer's Office was where one would expect a very high quality accounting system to be in place. Sloppy comes to mind as an adjective. Chair Leslie asked it this was what the Committee was looking at here.

Mr. Wood agreed. He added expectations were that the state would have an accounting system that relied on principles to identify, record, classify, summarize, and report the financial transactions of an entity. Mr. Wood noted it was mandated by state law that agencies follow the statutes which was not the case at the Treasurer's Office.

Chair Leslie stated these mandates were ignored.

Chair Leslie recognized Senator Coffin.

Senator Coffin noted the report included the state accounting procedures law. He asked if these laws had also been breached.

Mr. Wood stated that was correct. He added the fund was not used which was a violation of NRS 353.305, as well as 353B (340 and 350).

Chair Leslie asked Mr. Wood to continue the presentation.

Mr. Wood stated the State Treasurer's Office had not prepared financial statements for the Trust Fund since the Program began. Furthermore, the Board of Trustees had not received periodic financial statements or other reports showing the combined financial activity of the Trust. With financial statements, Program officials could demonstrate accountability for the Trust's financial activities. The Board, the Legislature, and other stakeholders would have had complete financial information needed to properly oversee and evaluate Program operations.

Recommendations were made that the State Treasurer's Office should record all Program transactions through the State's Accounting System in the Nevada College Savings Trust Fund or other accounts budgeted by the Legislature. In addition, the Office should prepare annual financial statements for presentation to the Board of Trustees.

Mr. Wood stated if there are no questions he would turn the presentation over to Rick Neil who supervised the audit.

Chair Leslie clarified the recommendations covering the report up to this point were plain and obvious.

Mr. Rick Neil, Audit Supervisor, continued the report presentation with findings related to contracts. Since inception of the Program, a law firm had been paid nearly $985,000 for services to the Program. Payments for legal services were not always in compliance with statutory and other requirements. Findings related to legal services were discussed as follows.

The Board of Trustees had not signed or approved any of the contracts for legal services provided to the Program. In addition, the Board had never been a party to any of the contracts, as required by NRS 353B. Although the Board of Trustees did not have a written contract for legal services, it designated a firm as outside counsel for the Program at a meeting in July 2001. At that meeting, a Board member asked whether the Chairman was going to enter into a contract with the law firm or utilize an existing contract. The Chairman indicated the Treasurer's Office existing contract for bond counsel services would probably be amended and brought to a future Board of Examiners meeting for approval. However, this contract was never amended and the Board of Trustees did not sign or approve contracts for legal services provided in subsequent years.

Mr. Neil continued the second finding related to legal services and the composite hourly rate paid during the term of the contract ended June 30, 2002, which was about $428. He stated this was significantly higher than the $225 specified in the contract. As a result the law firm was paid nearly $96,000 in excess of the contract rate.

Senator Coffin asked how long the state had paid the wrong amount.

Mr. Neil stated since the Program started in July 2001 through June 2002, which was a one year period.

Senator Coffin clarified the legal fees were paid in excess of $96,000 of the contract rate. He asked if there was a justification given why the Treasurer's Office was paying the excess hourly amount versus the contract rate.

Mr. Neil answered no, there was no explanation.

Chair Leslie stated that the Board of Trustees never saw that amendment and did not sign the contract.

Mr. Neil stated that was correct.

Chair Leslie stated "sloppy" came to mind again. She added the Treasurer's Office just received the invoice and paid it.

Mr. Neil stated that was correct.

Chair Leslie recognized Assemblyman Marvel.

Assemblyman Marvel asked if all of the invoices were found.

Mr. Neil stated yes.

Mr. Neil stated the third finding was related to legal services billings provided by the law firm that were not submitted to the Treasurer's Office in a timely basis. The average time covered by billings was over 1 year. Two billings submitted in fiscal year 2006 each covered 21 months. State administrative policies, which were incorporated into the contract, require monthly billings. Without monthly billings, it would be difficult for agency personnel to effectively review the appropriateness of charges.

Chair Leslie asked if there were only two invoices for the 21 months.

Mr. Neil stated for the $985,000 noted in the report there were six invoices. Auditors highlighted two of the invoices in 2006.

Chair Leslie clarified that each of the two invoices covered time periods of 21 months. She agreed that no one would remember details about billed hours for almost two years.

Mr. Neil agreed. The bills were detailed and would be difficult if that much time had passed to recall whether or what service had been provided.

Chair Leslie stated it was an obvious violation of the State Administrative policies.

Mr. Neil stated that was correct.

Chair Leslie asked Mr. Neil to continue the report presentation.

Mr. Neil discussed concerns over contractual payments to the Program's Plan Advisor. Auditors identified payments of about $500,000 which were not properly supported or did not adhere to the terms of the contract. First, the contractor was paid $200,000 for initial program development services, including $141,000 for reimbursement of out-of-pocket expenses. Although the contractor submitted an invoice, it lacked detail to support the out-of-pocket expenses.

Chair Leslie asked for clarification that the contractor was paid $200,000 and that $141,000 of the $200,000 was for reimbursement of expenses. She asked for clarification that the state did not have appropriate documentation to know what the expenses were for.

Mr. Neil stated that was correct.

Chair Leslie exclaimed, "We paid it any way." She asked about the kinds of expenses that could have been incurred.

Mr. Neil stated the information was noted in the report.

Chair Leslie asked if a consulting fee was an out-of-pocket expense.

Mr. Neil stated that was the way the fee was characterized in the information provided by the Plan administrator.

Chair Leslie asked if that was a typical out-of-pocket expense that Mr. Neil would see as an auditor.

Mr. Neil replied it was surprising to the audit staff.

Chair Leslie stated some of the other expenses such as FedEx shipping could be an out-of-pocket expense. She asked if the expense was a consulting fee to someone else.

Mr. Neil replied the question was put to Program officials and they were unsure as to what or who it was for.

Chair Leslie stated when one sees a round number like that, she wondered about $80,000 as an out-of-pocket consulting fee expense. She was amazed that an invoice such as this would be paid. Chair Leslie asked Mr. Neil to continue the presentation.

Mr. Neil stated although the contractor submitted an invoice that lacked details to support the out-of-pocket expenses, the Treasurer's Office officials indicated no other documentation or details were provided to support the expenses, which included legal fees, consulting fees, and travel costs.

The second contract issue related to the Plan Advisor. Treasurer's Office officials directed payments totaling $300,000 to the Plan Advisor that were not in accordance with contract terms. The Plan Advisor received $200,000 in October 2005 and $100,000 in December 2006. These two payments represented one-third of the marketing and administrative support funds payable to the State under its contract with the Program Manager. However, the state's contract with the Plan Advisor entitled them to receive one-third of asset-based or account-based fees, not funds received for marketing and administrative support. Therefore, the state was not contractually obligated to make these payments to the Plan Advisor.

Chair Leslie asked Mr. Neil to remind the Committee who the Plan Advisor was.

Mr. Neil stated the Plan Advisor was GIF, a limited liability company from the state of Georgia.

Chair Leslie asked if the Treasurer's Office had overpaid GIF.

Mr. Neil stated that was correct. Auditors understood that GIF, from reading the amendment that provided for these payments to go to the state, that there was a misunderstanding as to the nature of the fees. From the legal opinion received and included in the report, it was clear that these funds qualified under NRS 353B.360 and the funds that were received under the statute did not qualify for reimbursement to the Plan Advisor.

Chair Leslie asked if there was any way to get the money back.

Mr. Neil believed the current State Treasurer was discussing that with the Plan Advisor.

Mr. Neil stated the next contract area discussed related to the contracts for marketing services. The Treasurer's Office contract with a marketing firm was not evaluated or approved by the Board of Trustees, as required by state law. Although the Board never evaluated the proposals, documentation indicated staff had evaluated them. Auditors noted two instances where amendments extending the marketing contract for additional years were either not approved by the Board of Trustees or were approved after the amendment became effective.

The Treasurer's Office made payments to the marketing firm in excess of the maximum allowed under the contract for Fiscal Years 2005 and 2006. An exhibit in the report provided details on the amounts paid to the marketing firm compared to the contract maximums. It showed that payments exceeded the maximums by about $1.3 million in the last two fiscal years.

Chair Leslie asked for further details about the amounts in each fiscal year.

Mr. Neil explained in Fiscal Years 2005 and 2006 the combined amount that exceeded the contract maximums was $1.3 million for the two years. That was $450,000 in 2005 and $878,000 in 2006.

Chair Leslie asked if someone with our accounting system should have caught the errors. She added members of IFC and agencies were remanded constantly for overspending. She asked how the overspending was not discovered.

Mr. Neil explained the amount of expenditures that went through the state's accounting system fell within the contract maximum. He added the amounts paid from the state funds held by the Program Manager pushed the payments over the contract maximums.

Chair Leslie stated the Treasurer's Office was spending within the state budget and the other fund was spending funds that were not known about. The combination of these two funds put the spending over the contract amounts. She asked about whether the contractor had "checks and balances" to prevent this overspending.

Mr. Neil stated the marketing firm often did not have written contracts with their clients. In this case there was a contract but he was not so sure in their environment that contracts were a standard practice and that a contract might have meant less to them.

Chair Leslie stated as long as the contractor was getting paid for the work they were doing they would not be concerned about whether it was approved state money or state money outside the state budget system that the Program Manager was sending.

Chair Leslie returned to Assemblyman Marvel's point that the invoices showed that marketing actually was being performed and there was no hint of fraudulent activity. The state was paying for and exceeding the contracts with the money that was being held outside the state system, that the Legislature was not aware.

Mr. Neil stated that was correct.

Chair Leslie recognized Senator Coffin.

Senator Coffin asked if some of the money was used to pay for work done in 2004. Senator Coffin noted the jump in 2005 from 2004 was half a million dollars. He asked if the invoices indicated the dates of work performed.

Mr. Neil answered the auditors had reviewed the invoices which indicated the dates of work performed. He noted it was impossible to make a connection between the payments and the invoices. Mr. Neil explained normally the invoice would come in and payment would be made. However, the payments were coming in from the Program Manager, for example, as an even number, such as $400,000, and did not connect to a particular invoice.

Senator Coffin asked about the payments coming in as even numbers.

Mr. Neil replied some payments came in even numbered amounts and some did not.

Chair Leslie noted in the audit report that state officials involved with the Program at the time thought that payments from the Program Manager to the marketing firm were the Program Manager's funds, not state funds. She stated auditors found that was not the case because there were emails from the State Treasurer's Office telling them how to spend the money. She asked if that was a contradiction.

Mr. Neil replied it was perfectly clear in communications from the Treasurer's Office to the Program Manager regarding the source of the funds that were to be sent to the contractors, either the legal firm or the marketing firm. The Program Manager, followed direction from the State Treasurer's officials regarding what to pay. The confirmations from the Program Manager were clear that they were to take money from the state funds they were holding and expend them as directed.

Chair Leslie asked if the Program Manager had other marketing requirements and if they were the same kind of marketing efforts they would utilize for other types of savings plans.

Mr. Neil stated that was correct. The Program Manager had indicated they utilized different marketing firms for their marketing commitments with the exception, he thought, of one instance when they used the same marketing firm the state was using.

Chair Leslie recognized Senator Coffin.

Senator Coffin asked if the marketing was done nationally or was the marketing through the firm in the state of Nevada.

Mr. Neil replied auditors understood the marketing was done in state. The invoices were not very detailed so it was difficult to tell. The invoices indicated if the services were for TV or radio or print but did not always indicate the audience they were trying to hit.

Chair Leslie asked Mr. Neil to continue the presentation.

Mr. Neil stated the final area was related to contracts for the College Savings Program which included various provisions requiring contractors to provide information to assist the Board in fulfilling its oversight role. However, officials in the Treasurer's Office did not provide adequate oversight of contractors to ensure key information was provided to the Board. This included audited financial statements for each of the four plans that made up the Trust. Mr. Neil reported other key information was not provided. Auditors noted other information not regularly provided to the Board included reports on investment performance, reports on performance measures related to customer service, as well as proposed marketing plans and budgets from the Program Manager. He added all of the above named items were required under the contracts with the Program Manager. Officials in the Treasurer's Office did not have any documentation to show they received this information. Nor did the auditors see evidence that this information was presented to the Board. The Program Manager had indicated the information was available upon request of the Board or state officials.

Chair Leslie recognized Assemblyman Marvel.

Assemblyman Marvel asked who had this information.

Mr. Neil replied Upromise, the Program Manager, said they could get this information. In some cases they actually passed the information to auditors and in other cases they could have compiled the information if requested. He added, it would be the Program Manager who would have that information.

Assemblyman Marvel asked if the Program Manager had the information.

Mr. Neil replied yes for most of the information that was in the contract.

Chair Leslie stated the point was that it was never requested.

Mr. Neil replied the information was never requested by personnel in the State Treasurer's Office. The Program Manager felt the information could be requested if needed.

Assemblyman Marvel asked if the auditors had reviewed the information.

Mr. Neil replied yes.

Chair Leslie recognized Senator Coffin.

Senator Coffin asked Mr. Neil to identify who the Program Manager was.

Mr. Neil replied the Program Manager was Upromise and the Plan Advisor was GIF.

Mr. Neil stated recommendations were made to improve compliance with contracts for legal, marketing, and plan advisory services.

Chair Leslie called for Committee questions on this portion of the audit presentation and audit recommendations.

Chair Leslie stated the recommendations were straight forward. It was amazing to her that an agency would have to be told to require contractors for professional services to submit bills monthly, but the report noted outstanding invoices from 21 months out. Chair Leslie called for Committee questions then asked Mr. Neil to continue the presentation.

Mr. Neil began presenting the last chapter of the report. Auditors noted the Treasurer's Office had not established accounting or internal control procedures to guide staff in carrying out their responsibilities for the Nevada College Savings Program. The lack of written control procedures contributed to many of the problems found during the audit. Although the Treasurer's Office had developed policies and procedures for other activities performed by the Office, it had not developed procedures related to the College Savings Program. These policies and procedures would help the Treasurer's Office officials and staff to better safeguard and account for Program resources.

Recommendations were made in regard to this finding.

Chair Leslie recognized Senator Coffin.

Senator Coffin asked if the procedures had since been established.

Mr. Neil replied the information presented was current as of a few weeks ago. That would have been the last time auditors would have asked for the information.

Senator Coffin asked if the Treasurer's Office was working on this.

Mr. Neil replied the current Treasurer understood the need for implementation of the procedures.

Mr. Neil continued stating a number of appendices were included in the report that provided additional information relevant to the audit. These appendices included details on the audit procedures performed to reach the audit conclusions; information on the size of each state's college savings program; details on the amount of assets and accounts in each of the four plans in the Nevada College Savings Program, as well as the amounts held by Nevadans; and the Legislative Counsel's Legal Opinion on various questions auditors asked related to the Program. Also included in the report was the agency's response to the audit report which indicated they accepted all of the recommendations.

Chair Leslie stated the Legislative Counsel's Legal Opinion was that the State Treasurer's Office must use the state budget system and the state accounting system. She stated there were no special rules set up for the Nevada College Savings Program. She asked Mr. Neil if this statement represented the information presented in the Opinion.

Mr. Neil stated that was a fair representation of the Opinion.

Chair Leslie stated the State Treasurer's Office must follow the state budget act, state accounting procedures law, and the state administrative policies, just like everybody else.

Chair Leslie recognized Senator Rhoads.

Senator Rhoads asked if the Attorney General should have been advised about and been more involved in following the process of the State Treasurer.

Mr. Townsend answered there was a deputy attorney general that worked with the Board. They also had the outside counsel.

Chair Leslie recognized it was a good question. She wondered if someone should have been aware of the problems. She added this was the state's money.

Mr. Neil indicated the agency accepted all of the recommendations.

Chair Leslie asked if the response to the audit recommendations was from the current State Treasurer.

Mr. Neil replied that was correct. He stated that concluded his presentation and offered to answer questions from the Committee.

Chair Leslie called for questions from the Committee.

Chair Leslie called for a recess.

Chair Leslie called the meeting back to order at 4:21:00 p.m. She asked State Treasurer Kate Marshall to come forward to testify. Chair Leslie stated the report included a copy of the Treasurer's response to the audit recommendations which were all accepted by the Office of the State Treasurer. She stated the Committee would hear her testimony.

Ms. Kate Marshall, State Treasurer, stated for the record that the time period covered by the audit was prior to when she became the State Treasurer. Ms. Marshall had initially noted discrepancies which the Office had begun to correct. Some recommendations were delayed due to the lack of historical information in the Treasurer's Office. She was waiting to review information gathered by the auditors from the vendors that had interacted with the Treasurer's Office. Ms. Marshall was now beginning to implement the recommendations. She stated for example, recommendation number one, early on when discrepancies were noted, she had called the Program Manager and explained that going forward all state fees would have to come directly to the State Treasury to be deposited into an appropriate account.

Ms. Marshall continued, with respect to recommendation number two, it was also correct that when she initially discovered discrepancies she had directed her staff to ensure that expenditures were properly processed and reconciled against legislative authority.

Ms. Marshall noted she was setting up the various accounts and working with the State Controller's Office. She stated as Chairman of the College Savings Plan Board, she would be scheduling a meeting following the Committee meeting this date. She had informed the Program Manager and Vanguard that they would need to be present at that meeting. She added Vanguard was the largest plan that the Program Manager supervised. They would be asked to present to the Board that participant's money, the money that people invested for their children's college, was safe and secure. She emphasized that nothing had been mishandled or processed inappropriately with respect to the participant accounts.

Ms. Marshall had reviewed the current Upromise contract and asked them to comply with the contract and to present to the Board their marketing plan and their financial statements for all the programs and provide the status on what was happening with those programs, as required by the contract.

Ms. Marshall noted the Treasurer's Office accepted all of the recommendations.

Chair Leslie stated there was no reason to go through the recommendations as they were all straight forward. She stated the important point was that this important program needed to get back on track and monies needed to be accounted for so it was obvious how they were being spent.

Chair Leslie recognized Assemblyman Marvel.

Assemblyman Marvel asked Mr. Townsend for information about a follow-up report.

Mr. Townsend replied the 60-day plan of corrective action would be due August 15, 2007. The plan would be due in the Legislative Auditor's office and would address how the Treasurer intended to implement the recommendations. Six months after that date on February 15, 2008, a six-month report would be prepared by the Treasurer and submitted to Mr. Townsend's office. The report would be presented to the next meeting of the Audit Subcommittee. He added there would be a public hearing to review the six-month report at that point.

Assemblyman Marvel wanted to be assured that the same procedure was being followed as for other agencies.

Chair Leslie concurred this was an audit just like any audit done and the agency would be required to provide the regular six-month report. Chair Leslie asked in this case to see the minutes of the Board of Trustees meeting. She understood the Treasurer would be providing the audit to the Board members and inviting the Audit staff to present the audit to the Board.

Ms. Marshall replied yes, she requested the Chair's permission to ask the auditors to present the report to the College Savings Board.

Chair Leslie agreed with the request. She noted the audit had been requested by the Chair of the Senate Finance Committee and the Chair of the Assemblyman Ways and Means Committee. She stated on behalf of the Legislature she asked that the Audit staff present the report findings to the Board of Trustees. She stated the Board was aware that they must be held accountable to follow all the rules.

Chair Leslie recognized Senator Coffin.

Senator Coffin stated the current Treasurer was in a unique position having come into the Office following the occurrence of events reported in the audit report. He noted Ms. Marshall's opening statement included remarks regarding a lack of historical evidence upon taking office. He asked Ms. Marshall to explain this statement.

Ms. Marshall replied the report stated the auditors had to make inquiries with various sources to obtain information which was because the Treasurer's Office did not have the information when she arrived. She added the auditors had to go to the vendors to determine what had happened with the state fees that were earned under the College Savings Plan. She was able to recognize there were accounting discrepancies and that the budget account did not fully explain or show the money that the state had earned over the period that was covered by the audit. She did not have the information available to know how much money was completely earned and where that money was spent. She now was aware of that information from the audit and could establish the accounts the auditors identified in the audit.

Senator Coffin stated that someone might not have maintained good records. He recalled stories about the shredding of documents and computer programs migrating out of the office. He stated it was not known if the records existed.

Ms. Marshall was aware of statements made by people who were in the Office prior to her tenure in regard to documents being shredded and computer files being discarded or erased. She had no knowledge of that happening because she was not there. She had referred that information to the Attorney General for investigation of whether there was any fact to those statements.

Senator Coffin asked Chair Leslie if the Committee should make inquiries about this information.

Chair Leslie stated she wanted to bring the Committee back to the audit and what they were charged with at the Audit Subcommittee. She wanted to narrow the information presented just to the audit. Chair Leslie stated her understanding from speaking with Mr. Townsend was that the audit and all of the background information would be forwarded to the Attorney General as part of the investigation. The Treasurer would have the benefit of the work that the auditors had done. She wanted to share the findings and let her take advantage of all the work done by the auditors. She emphasized the Attorney General would investigate. Chair Leslie noted that was separate from the Audit Subcommittee's scope.

Chair Leslie called for additional questions from the Committee. She stated the State Treasurer accepted all of the recommendations. The Committee would receive a progress report on the implementation of the recommendations. Chair Leslie stated all were anxious for the Trust Fund to be set up properly. She emphasized that the public's money was not at risk and had been accounted for properly. Chair Leslie stated the Committee wanted to know how the money had been spent. She added the fund was doing quite well.

Ms. Marshall agreed. She added that Nevada had a premier program. The Vanguard Plan was a very good plan.

Chair Leslie stated the Committee was very concerned about the state's share of the earnings which was the basis for the audit. She stated the state wanted those funds accounted for properly to know how they were being spent.

Chair Leslie recognized Senator Coffin.

Senator Coffin stated the Legislature and the Committee became aware of this problem due to Ms. Marshall bringing it to their attention. He recalled that Ms. Marshall found that some money was not deposited in the State Treasury. He stated Ms. Marshall initiated the new procedures to ensure that could not happen again. He appreciated that Ms. Marshall had uncovered this violation of law. Senator Coffin noted the Legislature treated all violations of state law with seriousness, especially when it included money.

Ms. Marshall stated with respect to any violations she would refer the audit to the Attorney General for review and analysis. She added with respect to the state earned fees, the Committee might be aware that the College Savings Plan had a debt to the General Fund. That debt was a little more than $4 million with a balance of a little more than $3 million still owing. She believed the current Legislature asked that the debt be paid off.

Chair Leslie added perhaps the debt could have been paid off already had the $6 million come back to the state. She stated that was what had initiated the audit. The budget in this area was held off in closing to see if there were monies that could be expected that would repay the General Fund. She added this would free up General Fund monies for the State's other needs. Chair Leslie thanked Ms. Marshall for her cooperation and attitude in regard to the audit. She looked forward to receiving the six-month report.

Chair Leslie called for public testimony.

Mr. Brian Krolicki, Lieutenant Governor and former State Treasurer, stated he was present at the meeting in the capacity as the former State Treasurer and former Chairman of the College Saving Board. He appreciated the opportunity to speak during public comment. He stated that he was at a disadvantage because he had not been able to review the audit report prior to the meeting that day. Mr. Krolicki expressed appreciation to Mr. Townsend and the Audit staff. He emphasized it was a tremendous disadvantage to come here and not have the ability over weeks of time as the treasurer, certainly the two months that the auditors have been working, so he was not sure what things might be missing. He heard certain comments that beg the question, did you ask the question on this or that. Or were there contracts, there were legal questions, where was the Attorney General's Office, etc. He offered to answer questions following the meeting. Mr. Krolicki appreciated the audit recommendations and thought the State Treasurer made a wise decision and would accept the recommendations in the audit where possible.

Mr. Krolicki wanted to dwell on the good news. He noted all the money had been accounted for. That had been said several times. He stated this was a marvelous program with over $3.2 billion invested. There were, he believed, 300,000 young children around the country and in Nevada that were invested to save for college. He stated Nevada had the fasting growing program in the country. There were about $100 million in assets coming into the Program on a monthly basis. He noted Nevada's program was the seventh largest in size despite having a very tardy start into the college savings program and environment. He asked the Committee to remember that all of the monies, not only the invested monies on behalf of the families, but the fees had been accounted for. And while there were processes that may not have been adhered to by those involved, completely or to the satisfaction of the Legislative Auditor, the audit did not state the payments for services were inappropriate. In fact some of the vendors did a phenomenal job helping us grow this program. He reminded the Committee that no funding was provided in the General Fund for this program. It had become a revenue maker and was an important part of the tools for the pre-paid tuition program to make sure it remains solvent and fully funded. He added it was a funded liability. Mr. Krolicki stated again this had been balanced to the penny. He stressed that point needed to be very clear.

Mr. Krolicki stated there were questions Senator Coffin had asked about documents perhaps not being available or perhaps even misused. He stated in a meeting with Mr. Townsend, that Mr. Townsend indicated at the time that he had found what he needed and there was no indication in any way that any records or contracts or anything like that had been mishandled.

Chair Leslie stated he was more than welcome to speak under public comment but asked him to refrain from directing any of his comments to any particular person.

Mr. Krolicki understood the request. He stated he would leave that question dangling but in his recollection the question was answered that all records and documents had been located and that was how the auditors were able to do such a job that they did. He thought those allegations were off the table.

Mr. Krolicki stated what we have left is really a tough audit that discussed the administration and accounting matters related to this program. He noted that was what audits were designed to do. That was the process and he welcomed it. As State Treasurer, and Chief Deputy Treasurer for 16 years he had had his fair share of audits over the years. But this was the first time where substantive recommendations had been found.

Mr. Krolicki wanted to be clear that this was an extraordinary program. There was nothing else like it. These monies were not part of the state rhythm of finance. These are monies held in a mutual fund company, primarily Vanguard and some of the other partners. Mr. Krolicki stated many people had made a series of decisions over many years that got the Office to the point where they were today.

He stated, "I take full responsibility for what we have in front of us. I am the administrator. I have lots of folks working with me, advising me, legally, professionally, financially. But I know where the buck stops and I'll take that responsibility. But again, we should not lose focus that this a phenomenally successful program that is reconciled to the penny."

Mr. Krolicki stated the regulations that covered these programs were truly profound and intimidating. And the Municipal Securities Rule Making Board, the SEC, the national regulators that are involved in these programs are at the cutting edge.

Mr. Krolicki emphasized that the College Savings Board and the Treasurer's Office followed all legal, accounting, and professional financial advice provided to the Office from the Controller's Office, and the Treasurer's Office attorneys, which included some of the most senior deputy attorney general's in the state. He added the Office also had private sector legal and financial advisors. Mr. Krolicki stated the Office adhered to the instructions provided to the Office and emphasized Office actions were approved and directed by the Purchasing Division and the Department of Administration.

Mr. Krolicki noted these individuals would recognize processes if they were different. He stated the Office had a senior deputy treasurer who was a 29-year highly seasoned state employee, was a certified public manager, and a certified contract compliance manager, who was directly responsible for these programs. The Attorney General, the Secretary of State, and the Governor were participating as the Board of Examiners. Mr. Krolicki repeated the Office followed all the legal, accounting, and professional advice provided. He knew of no instance that these processes or any requirement were deliberately ignored.

Mr. Krolicki spoke about the recommendations in the report requiring College Savings Board approval. Some of these things could have been so easily handled. Part of his frustration was hearing these things in that the remedy was pretty simple which was to just put it on the agenda and make it happen. And again those things he trusted that the new Chairman would ensure that all of those actions were followed but again he believed they did a substantial amount of those and those cures were easy and again he thought they had adhered to many of those.

Mr. Krolicki stated the most substantive issue entailed with these findings was the fact that we have and he believed the auditors had evidence of lawful contracts that were generated in the Executive Branch. He stated the problem was that they conflict with the findings of the Legislative Auditor. From his standpoint a lawful contract was entered into and approved by the Board of Examiners. It was also asked why money was moved, how people were paid, and how vendors were taken care of. He stated it was per contract. He stated what he had was essentially two separate legal controls and he was following the advice he had received. In discussions with the auditors, one of the things we had a conversation about was the accounting system and that the Treasurer's Office had actually established a trust fund as the auditors were now recommending in the audit to do again. He explained it was a private purpose trust fund in 2001. In 2002 the State Controller's Office determined there was no need for this trust fund. The trust fund's elimination was determined by an accountant in the Controller's Office and the Office just made it happen. So essentially what occurred was the trust fund architecture was eliminated. So the accounting framework was done almost in entirety with this private company and it became a revenue source under the contracts to the state and those revenues were what came into the budget 1092 account that was spoken about today. And that was adhered to to the dime and to the law.

Chair Leslie interjected she did not want to get into too detailed questioning because it was public comment. She noted this was an extraordinary situation so she would allow a little bit of it.

Chair Leslie recognized Assemblyman Marvel.

Assemblyman Marvel asked about the rationale for the Controller taking the trust fund out of the state's system.

Mr. Krolicki replied there was no clear definition and he believed that was still the case, from the Governmental Accounting Standards Board on how to account for these programs. He believed there was discretion and he interpreted the decision was made by the Controller's Office that it was not necessary to account for as a private purpose trust fund. It did not fit into the CAFR. He stated with all due respect to the finding, he noted there were 300,000 participants and over $3 billion. He was unsure how much of that one would actually want to bring into the CAFR, if that was the situation. He added, that was the decision that was made.

Chair Leslie interjected she understood he had only received the audit today and noted it was clear that only the Audit Subcommittee members had received the final audit prior to being presented to the Audit Subcommittee. She stated even the current State Treasurer had not received the final audit before the meeting. Chair Leslie suggested if Mr. Krolicki would like to submit written testimony to the Audit Subcommittee they would be happy to take it. She stated at this point going forward the Committee was focusing on the recommendations. She asked if there were any of the audit recommendations that he would not accept. She noted all of the recommendations seemed straight forward.

Mr. Krolicki stated again he had not had the opportunity to review the audit.

Chair Leslie stated the recommendations were not that difficult.

Mr. Krolicki stated the recommendations seemed fair if implementable.

Chair Leslie recognized Senator Coffin.

Senator Coffin stated Mr. Krolicki had indicated that he had followed all of the professional advice from the Attorney General, the Controller, and others indicated, but the auditors found that he had violated at least three statutes while he was in office. He asked if Mr. Krolicki agreed or disagreed that this had happened.

Mr. Krolicki stated, "What I know is that I pursued these programs from an engineering standpoint to build, again what I believe is now one of the finest programs in this country under the advice and guidance that I received from the Attorney General's Office."

Mr. Krolicki emphasized some of the most senior people were advising the Treasurer's Office. He stated attorneys and national bond lawyers were assisting. These were municipal securities. Mr. Krolicki stated the Treasurer's Office had the advice, the people in the Office, the Department of Administration, and the Purchasing Division. He emphasized that advice and instruction the Office received to move forward with the Program was adhered to, to his knowledge, every single one. So he heard what the testimony had been today. From his standpoint he had a lawful contract that was entered into to make certain things happen, to make certain payments.

Senator Coffin stated he was not quite finished. He asked Mr. Krolicki about advertising marketing expenditures. He noted in 2003, $300,000 was spent; in 2004, $140,000 was spent; in 2005, $635,000 was spent; and in 2006, $1,063,000 was spent. He asked why the change and why the amount was so much over the contract maximum.

Mr. Krolicki stated this was an important part of all of this dialogue. He stated, "I believe all of the contracts adhered to the intent of the law and really to the direction of this committee. The marketing piece is a problem. You may recall that two months ago when I saw some of this information for the first time that how some of the fees were removed that there was an indication that perhaps the monies earned for the state were the monies used for some of the marketing. That was not supposed to be the case beyond that $185,000 authorized in the 1092 Budget Account."

He stated Mr. Townsend and his team essentially had certified that. He noted he would be asking the Attorney General to take the letter that was sent to the current State Treasurer and act upon it because there was a contract from 2002 with Upromise that clearly suggested that there was an obligation by this contract with Upromise that they would actually spend in that first year $700,000 for in-state marketing purposes and $500,000 every year thereafter. He stated he was referring to millions of dollars.

He explained the Office believed they were not using state monies but believed they were contractor's monies being used. He added that was why the numbers seemed so far out of the approved budget.

Mr. Krolicki stated Rose Glenn, the marketing company, had done a splendid job. He stated their billing records and billing accounts included two billing accounts for this program. He stated one account was with the State Treasurer's Office and the other account was with the College Savings Board which showed that the numbers did not go beyond the $185,000 a year. The contractor had a separate billing account for Upromise which was booked separately. He explained they were under the impression that these were the monies being used. Mr. Krolicki noted the program had grown and the monies had been spent over a period of time. He stated there had always been marketing. He explained the first advertisement was in 1999 when he had done an advertisement with Senator Bryan on the pre-paid college tuition program. He stated this had always been a significant part of what had been done.

Mr. Krolicki noted the fiscal year cramps up the money in a way that makes it look larger, but on a calendar year basis, which was the contract with Upromise, the billing records from Rose Glenn actually showed outside of that State Treasurer portion of the College Savings Board, about $500,000 a year from Upromise. Again he stated from the Office's vantage point from the information reviewed it looked like they were complying. He reiterated he thought there are contractual contentions regularly in the world, this was perhaps one of them. He stated he would urge the Attorney General to review this and if there was remedy to be had they should do so. If there was remedy with any of these contracts, and again I am not sure what back up was supplied, and I would have been delighted to work to try to secure some of these things with the vendors but he believed they performed their jobs and billed in good faith. The Office responded to those billings as per contract and required under law. Mr. Krolicki added the Office built something extraordinary and they cannot lose site of that.

Chair Leslie asked Mr. Krolicki if that concluded his remarks.

Mr. Krolicki asked the Chair for permission to touch on a couple of things that were said in the hearing. He stated the monies in the Program always stayed within the Program. So when it was suggested that these revenues could go to fund education, etc. that was not accurate. He stated the statutes were very clear that any revenues derived in these programs stay within these education programs, including the Millennium Scholarship. He stated it was very important that all of these monies were utilized in supporting these programs.

Mr. Krolicki stated Senator Coffin had asked about the contract amendment late last year. He noted it had been evolving over the year. He stated it was a very competitive business. In fact the great competitor for Vanguard was Fidelity which had a new arrangement with the state of California for their 529 College Savings Plan. He explained that put the pricing pressure on all others to drive down costs. Those changes were done for those reasons. He stated the program had to give up part of this resource. It had to be cheaper and that was why we made those changes. Vanguard also had several other states under contract with fixed fee arrangements. They could have migrated elsewhere. He indicated the Office received a very good deal.

Mr. Krolicki stated, "The interest that was perhaps not earned by the state because it was sitting in a non-interest bearing account. If that's the case, I would submit that our vendors were largely working on contingency. There were no fees to compensate them in the early parts of these programs. And we were quite fortunate they didn't bill us for, you know, invoices that hadn't been paid in a timely basis. So, and I think we got great favor out of how they did bill us and having the flexibility that they did."

Mr. Krolicki stated in terms of documents all of the monies were accounted for, to the penny. That was the most important thing. He added in terms of handling the actual money, the accounting system worked. He stated the accounting was done. Not necessarily in the state accounting system because of the nature of this mutual fund and the complexity and decisions made by many people, including the Controller's Office in how to handle these transactions.

Mr. Krolicki stated in terms of the handling and the transition for this program, the current senior deputy treasurer, he believed, was still working with this program so the continuity and institutional memory was there. Mr. Krolicki stated the Office was left impeccably and with all the records necessary to do their job.

Mr. Krolicki thanked Chair Leslie and the members of the Committee for hearing this audit. He offered to work with auditors on any follow-up to provide or to help to secure any of this information. He again emphasized that the program needed to continue to be a thriving program. Mr. Krolicki hoped Treasurer Marshall had the opportunity to be the Chairman of the largest college savings fund in this country.

Chair Leslie thanked Mr. Krolicki for his remarks. She called for questions from the Committee.

Chair Leslie called for a motion.

> ASSEMBLYMAN ARBERRY MOVED TO ACCEPT THE REPORT ON THE OFFICE OF THE STATE TREASURER, NEVADA COLLEGE SAVINGS PROGRAM. THE MOTION WAS SECONDED BY ASSEMBLYMAN MARVEL AND CARRIED UNANIMOUSLY.

Item 4—Public Comment.

Chair Leslie asked for public comment. There were none.

Chair Leslie stated this would be her last meeting as the Chair. She thanked the members of the Audit Subcommittee for all the support. She expressed the desire to continue serving on the Subcommittee.

Mr. Townsend stated once the new Legislative Commission was appointed, the Chair of the Commission would appoint the new Subcommittee and the next meeting would be held in the fall of 2007.

Chair Leslie thanked Mr. Townsend and all the members of the Audit staff on behalf of the Committee. She realized the audit was initiated a few months ago. She stated the Subcommittee always valued the Audit staff professionalism and the wonderful work done.

Chair Leslie noted there were no further comments. The meeting was adjourned at 5:00 P.M.

Respectfully submitted,

Donna Wynott, Audit Secretary

Senator Dean A. Rhoads
Chair of the Audit Subcommittee
of the Legislative Commission

Paul V. Townsend, Legislative Auditor
and Secretary to the Audit Subcommittee
of the Legislative Commission