

**MEMORANDUM**

Date: July 1, 2011

To: Members of the Legislative Audit Committee

From: Dianne E. Ray, CPA, State Auditor

Re: CollegeInvest, College Savings Plans Performance Evaluation Status Report

Attached is a summary status report of the progress made by CollegeInvest in implementing recommendations from the College Savings Plans Performance Evaluation presented to the Legislative Audit Committee in October 2010. Out of a total of 16 recommendations (each subpart counted separately), 11 have been implemented, 3 have been partially implemented, and 2 have not been implemented.



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AUDIT RECOMMENDATION STATUS REPORT

AUDIT NAME: College Savings Plans

AUDIT NUMBER: 2056

DEPARTMENT/AGENCY/ENTITY: CollegeInvest

DATE: October 2010

SUMMARY INFORMATION

Please complete the table below with summary information for all audit recommendations. **For multi-part recommendations, list each part of the recommendation SEPARATELY.** (For example, if Recommendation 1 has three parts, list each part separately in the table.)

Recommendation Number <i>(e.g., 1a, 1b, 2, etc.)</i>	Agency's Response <i>(i.e., agree, partially agree, disagree)</i>	Original Implementation Date <i>(as listed in the audit report)</i>	Implementation Status <i>(Implemented, Implemented and Ongoing, Partially Implemented, Not Implemented, or No Longer Applicable)</i> Please refer to the attached sheet for definitions of each implementation status option.	Revised Implementation Date <i>(Complete only if agency is revising the original implementation date.)</i>
1a	Agree	December 2010	Partially Implemented	June 2011
1b	Agree	Ongoing	Implemented and Ongoing	
2a	Agree	December 2010	Implemented and Ongoing	
2b	Agree	December 2010	Partially Implemented	June 2011
3	Disagree	N/A	Not Implemented – see audit report response	
4	Agree	November 2010	Implemented	
5a	Agree	September 2010	Implemented	
5b	Agree	January 2011	Implemented and Ongoing	
6a	Agree	November 2010	Implemented	
6b	Agree	November 2010	Not Implemented	June 2011
6c	Agree	November 2010	Implemented and Ongoing	

Recommendation Number <i>(e.g., 1a, 1b, 2, etc.)</i>	Agency's Response <i>(i.e., agree, partially agree, disagree)</i>	Original Implementation Date <i>(as listed in the audit report)</i>	Implementation Status <i>(Implemented, Implemented and Ongoing, Partially Implemented, Not Implemented, or No Longer Applicable)</i> Please refer to the attached sheet for definitions of each implementation status option.	Revised Implementation Date <i>(Complete only if agency is revising the original implementation date.)</i>
6d	Agree	November 2010	Implemented and Ongoing	
6e	Agree	November 2010	Implemented and Ongoing	
6f	Agree	November 2010	Partially Implemented – see audit report response	
6g	Agree	November 2010	Implemented and Ongoing	
6h	Agree	November 2010	Implemented	

DETAIL OF IMPLEMENTATION STATUS

Recommendation #: 1

Agency Addressed: CollegeInvest

Recommendation Text in Audit Report:

CollegeInvest should strengthen its fiduciary oversight of its college savings plans by:

- a. Defining in the Stable Value Plus investment policy statement what factors should be considered when monitoring the financial health of the Stable Value Plus investment provider and hiring an investment consultant to annually monitor the provider's financial health and to complete an annual, independent review of the provider.
- b. Continuing to evaluate revisions to its investment approaches for Scholars Choice and Direct Portfolio to allow the addition of actively or passively managed mutual funds to either plan if the funds can help the plans achieve investment objectives.

Agency's Original Response (*i.e., Agree, Partially Agree, Disagree*): Agree

Agency's Written Response in Audit Report:

- a. The financial health of our plan manager for Stable Value Plus is critical. We will revise our Investment Policy Statement and review the provider annually as recommended.
- b. A report by the United States Department of Treasury on Section 529 programs (which the auditors discuss later in the report) recommends that states provide a plan invested in index funds and notes, "Index funds . . . are well suited to investors who do not wish to spend time acquiring information and evaluating the investment philosophy and track records of the various actively managed funds that are offered." The Direct Portfolio Plan is offered to investors who are not required to use an advisor or broker and have a wide variety of investment knowledge and sophistication. The plan is structured using index funds to provide conservative and diverse investment options while reducing volatility and complexity. We also believe that costs matter and adding actively managed funds will increase the cost of the plan and result in a complex and a less transparent fee structure. Vanguard was engaged to manage the plan, as they are a leader in low-cost index funds. We will continue to evaluate our options and the plan managers we utilize.

Agency's Current Comments on Implementation Status of Recommendation:

- a) CollegeInvest's financial advisor has agreed to perform an annual review of the Stable Value Plus provider under the current contract. The review will be performed in June of each year. The investment policy statement will be revised in conjunction with the June provider review.
- b) Already a part of the annual review process which occurs in June of each year.

Recommendation #: 2

Agency Addressed: CollegeInvest

Original Recommendation in Audit Report:

CollegeInvest should minimize the administrative fees it collects on its college savings plans by:

- a. Recommending action to the CollegeInvest Board every year that administrative fees exceed expenses, in compliance with its administrative fees policy.
- b. Revising its administrative fees policy to establish an excess administrative fee balance threshold that would trigger a reduction in fees on an annual basis.

Agency's Response (*i.e., agree, partially agree, disagree*): Agree

Agency's Written Response in Audit Report:

The CollegeInvest Board discussed the excess fee situation in 2008 and 2009 and felt there were extenuating circumstances necessitating the carryover of the fee balance due to the significant equity market disruptions and the uncertainty of the future value of the assets in the plans. The Board concluded that retention of the excess fees was necessary to ensure the stability of program management. However, assets values stabilized and withdrawals from the plan remained consistent with prior years such that fee revenues did not drop as significantly as feared, and in fact continued to exceed expenses. As a result, the Board took action in 2010 to reduce fees to zero. The Board will continue to evaluate the fee level every year and take appropriate action. In addition, the fee policy will be revised to require a fee reduction if excess fees exceed a set threshold on an annual basis.

Agency's Comments on Implementation Status of Recommendation:

- a) Done in conjunction with the annual budget process. The review and related fee recommendations will be presented to the Board for approval in June of each year.
- b) The Board discussed several options for setting a trigger threshold for reducing fees. Currently, no fees are being charged. Further analysis was required and the final decision was deferred to June 2011 to be made in conjunction with the decision regarding reestablishing an administrative fee.

Recommendation #: 3

Agency Addressed: Department of Higher Education

Original Recommendation in Audit Report:

The Department of Higher Education should enhance the options for individuals to invest in Section 529 programs by:

- a. Analyzing the effects of allowing Colorado residents to receive a state income tax deduction for making contributions to any Section 529 program nationwide. Consideration should be given to ways to make the extension of the deduction revenue-neutral by limiting the amount of the deduction that an individual may claim.
- b. Determining, based on the analysis in part “a,” whether it will work with the General Assembly on revising statute to allow state income tax deductions for contributions made to any Section 529 program nationwide.

Agency’s Response (*i.e., agree, partially agree, disagree*): Disagree

Agency’s Written Response in Audit Report:

One of the main objectives of the CollegeInvest Section 529 program is to encourage Colorado residents to save for college. A primary incentive for Colorado residents to save for college is the unlimited Colorado tax deduction. Broadening the tax deduction to any 529 college savings plan would have a negative impact on statewide tax revenues during a time of precipitously declining state budgets and higher education funds.

The only way to mitigate the negative impact to statewide tax revenues would be through capping or limiting the tax deductions afforded to Colorado residents. The impact of this would be to discourage residents from maximizing savings for college which runs counter to the primary objective and goal of saving for college.

The recommendation is based on the possibility that a Colorado resident could earn a better return or that the current tax policy leads to less competition and higher fees. We believe that the known detrimental impact of reducing statewide tax revenues or capping deductions far outweighs the unknown potential benefit of greater performance or lower fees.

Lastly, the Department does not believe it should devote its limited resources to conduct such an analysis in the midst of the fiscal challenges facing higher education.

Agency's Comments on Implementation Status of Recommendation:

N/A

Recommendation #: 4

Agency Addressed: CollegeInvest

Original Recommendation in Audit Report:

CollegeInvest should ensure that contributions to the Stable Value Plus plan are deposited timely to MetLife, or to any subsequent manager of Stable Value Plus, by revising its policy so that Stable Value Plus deposits into participants' accounts occur within a reasonable time frame, not to exceed seven business days.

Agency's Response (*i.e., agree, partially agree, disagree*): Agree

Agency's Written Response in Audit Report:

Our procedures for depositing contributions to the Stable Value Plus program require weekly deposits of all funds received prior to each deposit. However, we will clarify our policy over deposits of contributions to state that amounts are to be deposited within seven business days of receipt of the monies.

Agency's Comments on Implementation Status of Recommendation:

The Policy was revised to require the deposit of monies received for Stable Value Plus to occur within seven business days.

Recommendation #: 5

Agency Addressed: CollegeInvest

Original Recommendation in Audit Report:

CollegeInvest should help ensure that account contributions and withdrawals meet applicable state and federal requirements by:

- a. Revising its Participation Agreement for both the Scholars Choice and Direct Portfolio plans to include a contributor certification regarding compliance with maximum account balance limits.
- b. Implementing a process for confirming that its third-party administrators file Form 1099-Q for all accounts in accordance with federal law.

Agency's Response (*i.e., agree, partially agree, disagree*): Agree

Agency's Written Response in Audit Report:

- a. CollegeInvest and our vendors have established strong controls over receipts of contributions. Any deposit to an account that causes it to exceed \$280,000 is immediately identified and the deposit is not allowed. We did add language to the Participation Agreements stating that the account owner represents they will not make a contribution in excess of the maximum account balance limits as of September 1, 2010.
- b. Vendors will be required to annually confirm the filing of all Form 1099-Qs.

Agency's Comments on Implementation Status of Recommendation:

- b.) All of the Vendors confirmed filing of all Form 1099-Qs for 2010.

Recommendation #: 6

Agency Addressed: CollegeInvest

Original Recommendation in Audit Report:

CollegeInvest should strengthen the controls over its information technology (IT) system by:

- a. Instituting a system development life-cycle and change management process covering system and software development and implementation.
- b. Creating strong passwords for access to its IT system at the Banner application and database levels.
- c. Routinely reviewing user access for appropriateness and ensuring that segregation of duties is maintained when granting user access.
- d. Documenting routine reviews of audit logs and employing intrusion detection software to determine if any anomalous events have occurred in the IT system.
- e. Formally monitoring data backup processes and following up on backup failures.
- f. Maintaining a fire suppression system in its IT data center, keeping its servers and other IT equipment in locked cabinets, testing its battery backup system, securing removable storage media, and changing the access code to its data center routinely.
- g. Testing its disaster recovery plan on a routine (e.g., annual) basis and implementing a formal process for monitoring backup activity.
- h. Ensuring that procedures for granting and disabling user access and training new employees on its policies and procedures are adequately documented.

Agency's Response (*i.e., agree, partially agree, disagree*): Agree

Agency's Written Response in Audit Report:

CollegeInvest performs regular audits of the information technology systems. The last audit was completed in May 2009 which identified all the issues noted in this recommendation. Implementation of all but two parts of the recommendations was completed in August 2010 as follows:

For part "b," the Banner system will be upgraded to allow for more complex passwords in November 2010.

Part "f" has been substantially implemented. However, the server cabinets we use no longer have replacement doors available and, therefore, we cannot implement this part of the recommendation until new server cabinets are acquired.

Agency's Comments on Implementation Status of Recommendation:

For part "b", we are in the process of upgrading Banner. Due to scope changes the implementation date has changed to May, 2011. It is anticipated that with the upgrade we will be able for fully implement the higher level of password protections.

For part "f", as noted in the response, we would need to acquire new server cabinets to implement this recommendation. There are no current plans to acquire new cabinets, but if new cabinets are required in the future, they will include doors.