STATE OF NEW HAMPSHIRE
DEPARTMENT OF REVENUE ADMINISTRATION

FINANCIAL AUDIT REPORT
FOR THE FISCAL YEAR ENDED
JUNE 30, 2014

STATE OF NEW HAMPSHIRE
DEPARTMENT OF REVENUE ADMINISTRATION

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* Audit comment suggests legislative action may be required.

Supplementary Information

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STATE OF NEW HAMPSHIRE
DEPARTMENT OF REVENUE ADMINISTRATION

Reporting Entity And Scope

The reporting entity and scope of this audit and audit report is the New Hampshire Department of Revenue Administration for the fiscal year ended June 30, 2014.

The following report describes the financial activity of the Department of Revenue Administration, as it existed during the period under audit. Unless otherwise indicated, reference to the Department or DRA refers to the Department of Revenue Administration.

Organization

The Department was reorganized under the terms of RSA 21-J, effective July 1, 1985. The Department is under the executive direction of a Commissioner who is appointed by the Governor, with the consent of the Executive Council (Council), to a four-year term. In addition, the Commissioner is authorized to nominate an Assistant Commissioner and Division Directors of Document Processing, Municipal and Property, Collections, and Audits, subject to confirmation by the Governor and Council. Embedded personnel from the Department of Information Technology support the Department's automated information systems.

The Department is organized into five functional areas: the Administration Unit, the Document Processing Division, the Municipal and Property Division, the Collection Division, and the Audit Division. At June 30, 2014, the Department employed 111 classified and 27 unclassified employees.

Responsibilities

The Department of Revenue Administration is responsible for overseeing the collection of State taxes, providing the Governor and Council with information for public policy decisions, and establishing a uniform system of financial reports and accounting for the State's political subdivisions.

The responsibilities of the Department's five functional areas are summarized below:

Administration Unit: performs administrative functions necessary to support Department operations including accounting, purchasing, adjudicative and administrative hearings, tax policy and legislative analysis, fleet and facility maintenance, human resources, and project management.

Document Processing Division: receives, processes, stores, and retrieves all tax documents, return payments, and electronic transactions filed with the Department.

Municipal and Property Division: assures fairness, equity and proportionality in the assessment and collection of property taxes and the administration of municipal finances in the state by establishing tax rates, providing technical assistance and education to municipal officials, monitoring revaluations, reviewing assessment practices, equalizing local assessed valuation, appraising public utility and railroad property, and administering timber and gravel taxation.

Collections Division: ensures taxpayer compliance with the tax laws of New Hampshire by fairly and effectively recovering overdue taxes through the uniform application of state laws, rules, and policies.

Audit Division: promotes voluntary taxpayer compliance with New Hampshire's tax laws through fair, impartial, and efficient selection and review of taxpayers' returns; taxpayer education; and discovery of non-filers. The Central Tax Services Unit of the Division handles taxpayer inquiries and account maintenance.

Funding

The financial activity of the Department of Revenue Administration is accounted for in the General, Capital Projects, and Education Trust Funds of the State of New Hampshire. A summary of the Department's revenues and expenditures for the fiscal year ended June 30, 2014 is shown in the following schedule.

Summary Of Revenues And Expenditures
Fiscal Year Ended June 30, 2014

	General Fund	**Capital Projects Fund**	**Education Trust Fund**	**Total Governmental Funds**
Revenues				
Unrestricted Revenues	$ 941,371,065	$ -0-	$ 734,716,969	$ 1,676,088,034
Restricted Revenues	219,438,183	-0-	-0-	219,438,183
Total Revenues	1,160,809,248	-0-	734,716,969	1,895,526,217
Total Expenditures	14,401,531	552,024	2,021,902	16,975,457
Excess (Deficiency) Of Revenues Over (Under) Expenditures	**$ 1,146,407,717**	**$ (552,024)**	**$ 732,695,067**	**$ 1,878,550,760**

Prior Audits

The most recent prior financial audit of the Department of Revenue Administration was for the fiscal year ended June 30, 2008, and the most recent prior performance audit of the Department was dated July 2013. The appendices to this report on pages 37 and 39 contain a summary of the current status of the observations contained in those reports. The prior audit reports can be accessed on-line at:

http://www.gencourt.state.nh.us/LBA/AuditReports/financialreports.aspx
http://www.gencourt.state.nh.us/LBA/AuditReports/performancereports.aspx

Audit Objectives And Scope

The primary objective of our audit is to express an opinion on the fairness of the presentation of the financial statement of the Department of Revenue Administration for the fiscal year ended June 30, 2014. As part of obtaining reasonable assurance about whether the financial statement is free of material misstatement, we considered the effectiveness of the internal controls in place at the Department of Revenue Administration and tested the Department’s compliance with certain provisions of applicable State laws, rules, and contracts. Major accounts or areas subject to our examination included, but were not limited to, the following:

- Revenues
- Expenditures

Our report on internal control over financial reporting and on compliance and other matters, the related observations and recommendations, our independent auditor's report, and the financial statement of the Department of Revenue Administration are contained in the report that follows.

Independent Auditor's Report On Internal Control Over Financial Reporting And On Compliance And Other Matters Based On An Audit Of Financial Statements Performed In Accordance With *Government Auditing Standards*

To The Fiscal Committee Of The General Court:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statement of the New Hampshire Department of Revenue Administration (Department) which comprises the Statement of Revenues and Expenditures - Governmental Funds for the fiscal year ended June 30, 2014, and the related notes to the financial statement and have issued our report thereon dated April 24, 2015, which was qualified as the financial statement does not constitute a complete financial presentation of the Department in the Governmental Funds.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statement, we considered the Department's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statement, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control that we consider to be significant deficiencies. We consider the deficiencies described in Observations No. 1 through No. 7 to be significant deficiencies.

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the Department's financial statement is free of material misstatement, we performed tests of its compliance with certain provisions of laws, rules, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed one instance of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which is described in Observation No. 8.

Department's Responses To Findings

The Department's responses to the findings identified in our audit are included with each reported finding. The Department's responses were not subjected to the auditing procedures applied in the audit of the financial statement and, accordingly, we express no opinion on them.

Purpose Of This Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Office of Legislative Budget Assistant

Office Of Legislative Budget Assistant

April 24, 2015

Internal Control Comments
Significant Deficiencies

Observation No. 1: Establish Formal Risk Assessment Policies And Procedures

Observation:

The Department does not have formal risk assessment policies and procedures or described processes in place for recognizing and responding to risks potentially affecting the Department's operations. While the Department takes steps to address identified risks, the Department does not have a formal documented process for specifically and actively reviewing for and considering financial and other risks facing Department operations. A similar finding was noted in our 2008 financial audit report of the Department and our July 2013 performance audit report.

The purpose of an entity's risk assessment efforts is to identify, analyze, and where appropriate, respond to risks and thereby manage risks that could affect the entity's ability to reach its objectives. An effective and documented risk assessment process should be a core element of management's controls.

Recommendation:

The Department should establish a formal risk assessment process. The Department should regularly review its financial and operational activities for indicators of risk exposure, and establish and monitor controls that appropriately address those risks. The Department should involve employees with particular areas of expertise and knowledge of Department operations in the review to ensure that details of operations that may not be obvious to management are appropriately considered.

Auditee Response:

The Department concurs. In 2013, the Commissioner established a policy and procedure committee, which reviews existing policies and procedures and creates new policies and procedures for significant business processes. The committee has undertaken a review of over 50 policies since its inception. The Department's staff is required to review and sign policies annually. The Department has training on its policies. Further, the Commissioner reviews each newly-enacted policy during his monthly Department meeting on the first Friday of each month. In addition, the Department's internal audit function is active as other responsibilities that were temporarily assigned to the Internal Auditor have been transferred to other employees with the Department, allowing the Internal Auditor time to conduct planned internal audits. The Department's policies help identify and prevent risk. However, the Department has been formalizing a risk assessment plan, which it expects to finalize soon.

Observation No. 2: Establish Disaster Recovery And Business Continuity Plans

Observation:

The Department did not have updated disaster recovery or business continuity plans in place during fiscal year 2014. The lack of effective plans increases the risk that the Department will not react timely and efficiently to foreseeable disruptions to its operations.

The purpose of a disaster recovery plan is to document plans and procedures in the event of a disaster, including disaster recovery strategies, essential resources, and procedures necessary to implement a recovery process. The purpose of a business continuity plan is to document plans and procedures in the event of a significant change in the way a business conducts its daily business functions. Effective disaster recovery and business continuity planning is essential to minimize business interruptions in the event of a disrupting incident, and relies heavily upon an organization's risk assessment activities.

The Department reported it was redrafting and formalizing a continuity of operations plan, which it believes will serve as both a disaster recovery and business continuity plan.

A similar finding was noted in our 2008 financial audit report of the Department.

Recommendation:

The Department should complete the updating of its disaster recovery and business continuity plans. Plans should be distributed to employees with plan roles and responsibilities, and those employees should be appropriately trained. The Department should regularly test the plans to ensure the plans remain relevant and effective, and employees are practiced in implementing the plans.

Auditee Response:

The Department concurs. The Department has a Continuity of Operations Plan (COOP) and has been consistently updating it over the years. In 2013, the employee managing the COOP left the Department's employment and, therefore, the Department reassigned these duties. The new employee assigned to managing the COOP has performed an extensive review and determined areas of improvement that require additions, modifications, and enhancements. The Department is actively working with the Homeland Security and Emergency Management Division of the Department of Safety as part of the overall State initiative to address COOPs for all state agencies. The Department's current updates have been in accordance with the State-established standards. DoIT is actively working on the COOP with the Department and in developing the environment and testing schedules. The Department's improvement to its COOP, which will finalize its formal disaster recovery plan, will be completed by June 30, 2015.

Observation No. 3: Obtain And Evaluate Understanding Of Relevant Controls At Service Provider

Observation:

The Department has not obtained reports regarding the design and operation of controls over tax return filing and tax receipt collection services provided by a primary service organization. The absence of a documented understanding and assessment of relevant controls and weaknesses in the service organization's processing of tax returns increases the risk the Department would not be in a position to detect and correct frauds and errors that may occur in the service organization's processing of the tax returns and receipts on behalf of the Department.

Substantially all Meals and Rooms and Car Rentals and some Business and Interest and Dividends Tax returns and receipts are filed by taxpayers using an e-file (online) or telefile (telephonic) tax reporting system operated by the service organization. The Department estimates that during fiscal year 2014, taxpayers reported $449 million on tax forms processed through the service organization's e-file and telefile system.

On July 2, 2014, the Department requested the service organization to arrange for a SOC 1 report **(**service organization control report prepared pursuant to the AICPA's Statement on Standards for Attestation Engagements (SSAE) No. 16, *Reporting on Controls at a Service Organization***)** to describe the controls at the service organization which are relevant to the Department's internal control over financial reporting. The receipt and consideration of a SOC 1 report is generally necessary to allow an entity to have reasonable assurance that appropriate controls are in place at a service organization processing significant financial activity on behalf of that entity.

A similar finding was noted in our 2008 financial audit report of the Department.

Recommendation:

The Department should regularly obtain and evaluate SOC 1 reports for the service organizations that process significant financial activity on its behalf. Management should consider the contents of the reports to determine if controls at the service organizations are adequate and that all complementary controls required at the Department to support the service organization's operations are in place. The Department should address and follow up on any errors or concerns noted in the reports that affect the Department's operations and controls to ensure the controls are, and remain, effective.

Auditee Response:

The Department concurs. The Department has taken steps to ensure controls are in place at its service provider, First Data Government Solutions (FDGS). Prior to this audit, the Department requested that the Department of Information Technology (DoIT) contact FDGS to explain the SSAE 16 requirement. The contract with FDGS allows tax return and payment filing through the Department's webfile/telefile system and is negotiated by DoIT on behalf of the Department. DoIT has reported to the Department that FDGS is SSAE 16 compliant. The Department has requested that DoIT obtain the control status reports or SOC 1 reports, which DoIT confirms has been done. Upon receipt, the SOC 1 reports will be reviewed by the Department to ensure effective controls. In addition, the webfile/telefile service contract is in the process of being re-bid. The Department will work with DoIT to make sure that future service provider vendors are SSAE 16 compliant and issue SOC 1 reports to the Department for review.

Observation No. 4: Planning For Acquisition Of New Tax Information System Should Continue

Observation:

The Department continues to report that limitations in its Tax Management Information System (TIMS) present substantial risks to the completeness, reliability, security, and safeguarding of taxpayer data maintained by the Department.

The Department developed TIMS in the early 1990's to integrate and automate the collection and processing of tax information. TIMS was originally developed with the assistance of outside consultants but, since implementation, the system has been further developed and maintained by staff. TIMS, as it currently operates, is comprised of several major subsystems. All divisions of the Department, with the exception of the Municipal and Property Division, use TIMS daily to manage and warehouse taxpayer and other information for the Business Profits, Business Enterprise, Interest and Dividends, and Meals and Rooms and Car Rentals taxes. The Department processed over $1.7 billion dollars in tax revenue in TIMS during fiscal year 2014.

In October 2014, the Department initiated a process to document the current limitations of TIMS and the potential benefits to the State of replacing TIMS with a modern tax information system. As part of that process, the Department established a committee to document Department-wide concerns with TIMS, including its archaic programming language, lack of efficient processing and extraction of information, and inefficient communication capabilities with taxpayers. The committee summarized its concerns into the six categories of technology, core application, financial, reporting and other outputs, collections, and audit. In each of the categories, the Department reports concerns with the current TIMS or opportunities where a more modern information system would serve the State and taxpayers more efficiently.

A similar finding was noted in our prior 2008 financial audit report of the Department.

Recommendation:

The Department should continue to build its case for implementing a new tax information system that would be more adaptable to the Department's and State's needs and more efficient for taxpayer interaction.

The Department and State should ensure that a replacement system has been fully designed, vetted, and acquired before the limitations in TIMS become too much of a burden on the operations of the Department.

Auditee Response:

The Department concurs. In preparation for the acquisition of a new Tax Information Management System (TIMS), the Department posted a Request for Information (RFI) and received many submissions for review. Next, the Department intends to post a Request for Proposal (RFP) seeking professional services to assist in drafting its business requirements for a new TIMS and to determine the level of funding needed for the project. The Department plans to request funding for a new TIMS as part of the 2017 capital budget process.

Observation No. 5: Review Accounts Payable Practices

Observation:

A lack of policies and procedures for accruing accounts payable at June 30, 2014 contributed to the Department not reporting certain expenditures in the correct fiscal year.

The Department's 2014 fiscal year-end accrual of accounts payable for the Low Income Property Tax Relief Program included payments made on claims during the first 45 days of the new fiscal year. The Department used a 70 day accrual period in the prior fiscal year for these payments. The use of inconsistent fiscal year 2013 and 2014 accrual periods contributed to a net understatement of fiscal year 2014 expenditures from the Education Trust Fund of approximately $67,000. The Department was unable to explain the different accrual periods used in fiscal year 2013 versus fiscal year 2014.

Testing of six capital projects fund expenditures revealed an instance where the Department did not follow the Department of Administrative Services' *Annual Closing Review* accounts payable policy and two instances where the lack of a split invoice policy resulted in overstatements of fiscal year 2014 expenditures.

- One invoice totaling $95,388, covering the period June 1 through June 30, 2013, was charged to fiscal year 2014 in error, resulting in a $95,388 overstatement of fiscal year 2014 expenditures.
- One invoice totaling $264,387, covering the period April 1 through July 21, 2014, was charged entirely to fiscal year 2014, resulting in a $50,234 overstatement to fiscal year 2014 expenditures for the portion of the invoice attributable to fiscal year 2015.
- One invoice totaling $22,790, covering the period June 19 through July 31, 2013, was charged entirely to fiscal year 2014, resulting in a $6,381 overstatement to fiscal year 2014 expenditures for the portion of the invoice attributable to fiscal year 2013.

The *Annual Closing Review* includes policies and procedures for the accrual of unrecorded liabilities (recording of accounts payable). The policies and procedures generally direct agencies to identify and code expenditure transactions that should be accrued as accounts payable of the prior period.

The *Annual Closing Review* is silent with respect to coding portions of invoices that cross two fiscal years as accounts payable. Some State agencies have developed split invoice policies and procedures to charge expenditures to the proper fiscal year, but these split invoice policies and procedures were not incorporated into the *Annual Closing Review* for fiscal year 2014 and were not employed by the Department.

Recommendation:

The Department should review with the Department of Administrative Services the appropriate accounts payable policies and procedures that should be employed to report accounts payable at the end of each fiscal year. This review should consider whether the adoption of a split invoice policy would better ensure Department expenditures are reported in the proper fiscal year.

Auditee Response:

The Department concurs with the need to refine its review of accounts payable for invoicing related to capital project services spanning more than one fiscal year. The Department will review bills it receives that pertain to services being paid to vendors during such time periods to avoid overstatements in one fiscal year.

Department of Administrative Services' Response:

We concur. The Department of Administrative Services will work with the Department of Revenue Administration and other state agencies to clarify the appropriate policies and procedures around the reporting of year-end accounts payable. We will contemplate including a specific split invoice policy within our *Annual Closing Review*.

Observation No. 6: Monitor Compliance With Filing Of Statements Of Financial Interests

Observation:

The Department has not routinely monitored members of administratively-attached boards of the Department for compliance with RSA 15-A requirements for filing statements of financial interests. Of the attached board members who were required to file a statement of financial interests with the Secretary of State by January 17, 2014, we noted the following issues of noncompliance:

- Three of 14 members of the Current Use Advisory Board did not file timely.
- Four of 14 members of the Current Use Advisory Board did not file.
- Seven of 13 members of the Assessing Standards Board did not file.

The Department and the State relies upon the Current Use Advisory Board and Assessing Standards Board for property tax-related matters.

Pursuant to RSA 15-A:6, "No person required to file a statement of financial interest pursuant to RSA 15-A:3, I, shall be eligible to serve in his or her appointed capacity prior to filing a statement in accordance with this section."

Pursuant to RSA 15-A:7, "Any person who knowingly fails to comply with the provisions of this chapter or knowingly files a false statement shall be guilty of a misdemeanor."

Non-compliance with RSA 15-A increases the risk that potential conflicts of interest may not be properly disclosed. Additionally, the validity of decisions in which noncompliant board members participate may be called into question.

All Department employees required to file Statements of Financial Interests had statements on file during fiscal year 2014.

A similar finding was noted in our 2008 financial audit report of the Department.

Recommendation:

Although it is each individual's responsibility to file, the Department should monitor the filing status of its attached board members to promote compliance with the statute and reduce the risk, if any, that the Department's decision making authority may be subject to challenge for noncompliance with the statute.

Auditee Response:

The Department concurs. RSA 15-A requires certain State officials to file a complete Statement of Financial Interests. The observation finds that members of the Department's administratively-attached boards have not timely filed. The Department will take steps to annually notify the board members of its administratively-attached boards of the requirements set forth in RSA 15-A.

Observation No. 7: Facilitate Compliance With Municipal Reporting Statute

Observation:

Each of the three municipalities reviewed for timely submission of annual reports submitted late reports. Each of the three reports were submitted approximately five months after the statutorily mandated due date of April 1, 2013. The Department reported the annual reports due by April 1, 2014 were submitted three months late.

RSA 21-J:34 requires each city and town to file reports in order to compute and establish the property tax rate for each city and town. RSA 21-J:34, V, requires "a financial report for each city, town, school district, village district, or county shall be filed showing the summary of receipts and expenditures, according to uniform classifications, during the preceding fiscal year, and a balance sheet showing assets and liabilities at the close of the year." The report for the municipalities is called the Financial Report of the Town or City Budget (MS-5). Pursuant to RSA 21-J:34, V, the reports (Financial Report of the Town or City Budget (MS-5)) are required to be submitted by April 1 if the municipality keeps its accounts on a calendar year basis or by September 1 if the municipality keeps it accounts on a fiscal year basis. The three towns reviewed in the audit test were calendar-year towns.

The Department reports the untimely availability of the MS-5 reports generally results from municipal audits not being completed in time to submit the MS-5 reports by the statutory due dates. The Department also reports the untimely submission of annual municipal financial reports can delay the Department's setting of municipal property tax rates.

A similar finding was noted in our 2008 financial audit report of the Department.

Recommendation:

The Department should take additional steps to assist the municipalities to file timely annual financial reports. If the Department deems compliance with the requirements of RSA 21-J:34, V, to be unfeasible or unenforceable, the Department should seek to have the statutes appropriately amended.

Auditee Response:

The Department concurs. The Department's policy is to not set a tax rate until all statutory report filing requirements are met. The Department works with each local government to make sure all statutorily-required reports are submitted on time. The Department consistently monitors the financial filings of the cities and towns in order to set tax rates. Some of the documents that are used in setting the tax rates (warrants, minutes, appropriations forms, budget forms, and official ballots) are due within 20 days of the voting session of the annual meeting. The financial reports are due April 1 for the calendar year municipalities, and September 1 for optional fiscal year municipalities. The revised revenue estimates and property valuations are also due September 1. The Department's Municipal Services Bureau is informed, by the city or town, of any late reporting. With the financial reports, most of these are prepared by independent CPA auditors, and are frequently late due to the CPA's schedules for performing the field work. The Department stays in contact with both the municipalities and the CPAs during the Spring and Summer months to ensure that all documents are in prior to tax rate setting in the Fall.

The Department has no authority to compel local governments to timely file their annual filing requirements with the Department. In fact, a penalty provision, RSA 21-J:36 was repealed in Chapter Law 182 of the 2007 legislative session, where the Department is no longer authorized to impose a failure to file penalty on local governments that did not meet their statutory filing requirements. Instead, the Department is required to "compute and establish the tax rate of each town, city, or unincorporated place." See RSA 21-J:35. There is no statutory mechanism to authorize the Department to compel the timely filing of annual financial reports from the local governments.

A computerized tracking system has been developed to generate automatic notices to the municipalities of their noncompliant status. This new system will enable better tracking and faster follow-up on delinquent filers, including formal notification, and will begin processing the annual financial reports for the first time this fall after spending the past year training local officials on the system.

State Compliance Comment

Observation No. 8: Adopt Required Administrative Rules

Observation:

The Department has not adopted, or kept current, administrative rules required by the following statutes.

Statute	Description of Administrative Rule	Status
RSA 75:1-a, IX	Residential Property Subject to Housing Covenant Under the Low-Income Housing Tax Credit Program	Not Adopted
RSA 78:11	Tobacco Tax Metering Machines	Not Adopted
RSA 79-E:12	Community Revitalization Tax Relief Incentive	Not Adopted
RSA 84-D:4	Intermediate Care Facility Quality Assessment	Not Adopted
RSA 541-A:16, I	Organizational Rules; Filing Required	Rev 100 – Not Current

The Department reports that certain of the rules required in statute are not necessary because RSA 21-J:13-a exempts the Commissioner from "adopting, as rules pursuant to RSA 541-A, the requirements on all forms." It is unclear that the administrative rules required by RSA 79-E:12 and RSA 84-D:4 are limited to the "requirements on all forms".

Administrative rules are intended to communicate policies, procedures, and practices to persons both inside and outside an organization to promote understanding and compliance with the application of the authorizing statutes. The lack of required rules decreases transparency in Department operations and increases the risk the Department's operations could be challenged.

A similar finding was noted in our 2008 financial audit report of the Department.

Recommendation:

The Department should adopt, and keep current, statutorily-required administrative rules.

If the Department determines that rules are not necessary, it should pursue a timely change in statute to eliminate the requirement for the rules.

Auditee Response:

The Department concurs.

<u>RSA 75:1-a, IX</u>
RSA 75:1-a, IX provides that the Commissioner "shall adopt rules… concerning how capitalization rates shall be established, including a process for receiving public input prior to such establishment." The Department presently holds a public hearing prior to establishing the

capitalization rate, which is noticed on our website. The established rates are then posted on our website. However, this process is not presently addressed in rules. Accordingly, the appropriate addition shall be made to the Department's administrative rules.

<u>RSA 78:11</u>
RSA 78:11 provides that the Commissioner shall adopt rules relative to the use of metering machines in lieu of tobacco tax stamps. No rules have been promulgated because the regulated community does not use metering machines. Additionally, HB 550-FN was proposed this legislative session and includes the repeal of references to metering machines from RSA 78. HB 550-FN passed in the House and is pending before the Senate.

<u>RSA 79-E:12</u>
RSA 79-E:9 requires the Commissioner to prescribe and issue forms to the local assessing officials for their use in assessing taxes in response to a property owner's failure to adhere to a Community Revitalization Tax Relief Incentive covenant under RSA 79-E:1. The Commissioner has created Form PA-47, "Community Revitalization Tax Relief Incentive Penalty." Pursuant to RSA 21-J:13-a, the Commissioner is exempt from adopting Department forms in rules. RSA 79-E:12 provides that the Commissioner shall adopt rules relative to the procedures outlined in RSA 79-E:9. The procedures outlined in RSA 79-E:9 are sufficiently detailed for the administration of RSA 79-E:9. As such, the Commissioner will seek to eliminate the rulemaking requirement in RSA 79-E:14 during the 2016 legislative session.

<u>RSA 84-D:4</u>
RSA 84-D:4 requires the Commissioner to adopt rules regarding the Intermediate Care Facility (ICF) return form. The Commissioner has created the ICF return form, DP-158 "Intermediate Care Facility (ICF) Quality Assessment Return." Pursuant to RSA 21-J:13-a, the Commissioner is exempt from adopting Department forms in rules. Otherwise, the procedures outlined in RSA 84-D are sufficiently detailed for the administration of the statute. As such, the Commissioner will seek to eliminate the rulemaking requirement in RSA 84-D:4 during the 2016 legislative session.

<u>RSA 541-A:16, I</u>
RSA 541-A:16, I provides that each agency shall adopt rules describing the agency's organization. The appropriate updates will be made to the Department's organization rules, N.H. Administrative Rules Chapter 100.

Independent Auditor's Report

To The Fiscal Committee Of The General Court:

Report On The Financial Statement

We have audited the accompanying financial statement of the Department of Revenue Administration which comprises the Statement of Revenues and Expenditures - Governmental Funds, for the fiscal year ended June 30, 2014, and the related notes to the financial statement.

Management's Responsibility For The Financial Statement

Management is responsible for the preparation and fair presentation of this financial statement in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on this financial statement based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit opinion.

Basis For Qualified Opinion

As discussed in Note 1, the financial statement referred to above does not purport to and does not constitute a complete financial presentation of the Department of Revenue Administration in conformity with accounting principles generally accepted in the United States of America.

Qualified Opinion

In our opinion, except for the matter described in the Basis for Qualified Opinion paragraph, the financial statement referred to above presents fairly, in all material respects, the respective revenues and expenditures of the Department of Revenue Administration's portion of the State of New Hampshire's Governmental Funds for the fiscal year ended June 30, 2014 in accordance with accounting principles generally accepted in the United States of America.

Emphasis Of Matter

As discussed in Note 1, the financial statement referred to above reports certain financial activity of the Department of Revenue Administration. It does not purport to, and does not, present fairly the financial activity of the State of New Hampshire as of June 30, 2014 in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Management has omitted the management's discussion and analysis and the budgetary comparison information that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the financial statement is not affected by this missing information.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statement of the Department of Revenue Administration which comprises the Statement of Revenues and Expenditures - Governmental Funds, for the fiscal year ended June 30, 2014. The accompanying

Budget to Actual Schedule - General Fund, Budget to Actual Schedule - Education Trust Fund, and Schedule of Budget and Expenditures - Capital Projects Fund are presented for purposes of additional analysis and are not required parts of the basic financial statement.

The Budget to Actual Schedule - General Fund, Budget to Actual Schedule - Education Trust Fund, and Schedule of Budget and Expenditures - Capital Projects Fund are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statement. Such information has been subjected to the auditing procedures applied in the audit of the financial statement and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statement or to the financial statement itself, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Budget to Actual Schedule - General Fund, Budget to Actual Schedule - Education Trust Fund, and Schedule of Budget and Expenditures - Capital Projects Fund are fairly stated, in all material respects, in relation to the financial statement as a whole.

Other Reporting Required By *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated April 24, 2015 on our consideration of the Department of Revenue Administration's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Department of Revenue Administration's internal control over financial reporting and compliance.

Office of Legislative Budget Assistant

Office Of Legislative Budget Assistant

April 24, 2015

STATE OF NEW HAMPSHIRE
DEPARTMENT OF REVENUE ADMINISTRATION
STATEMENT OF REVENUES AND EXPENDITURES - GOVERNMENTAL FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2014

Revenues	General Fund	Capital Projects Fund	Education Trust Fund	Total Governmental Funds
Unrestricted Revenues				
Statewide Property Tax (Note 2)	$ -0-	$ -0-	$ 363,756,125	$ 363,756,125
Business Profits Tax	269,695,143	-0-	58,108,835	327,803,978
Meals and Rooms/Car Rentals Tax	254,726,036	-0-	7,649,613	262,375,649
Tobacco Tax	130,115,744	-0-	89,807,032	219,922,776
Business Enterprise Tax	72,879,023	-0-	146,194,321	219,073,344
Real Estate Transfer Tax	67,262,515	-0-	33,586,680	100,849,195
Interest And Dividends Tax	80,078,833	-0-	-0-	80,078,833
Communications Services Tax	59,403,396	-0-	-0-	59,403,396
Utility Property Tax	-0-	-0-	35,614,363	35,614,363
Electricity Consumption Tax	6,205,463	-0-	-0-	6,205,463
Nursing Facility Quality Assessment (Note 3)	513,022	-0-	-0-	513,022
Other Unrestricted Revenues	491,890	-0-	-0-	491,890
Total Unrestricted Revenues	**941,371,065**	**-0-**	**734,716,969**	**1,676,088,034**
Restricted Revenues				
Medicaid Enhancement Tax (Note 3)	180,457,706	-0-	-0-	180,457,706
Nursing Facility Quality Assessment (Note 3)	37,832,878	-0-	-0-	37,832,878
Other Restricted Revenues	1,147,599	-0-	-0-	1,147,599
Total Restricted Revenues	**219,438,183**	**-0-**	**-0-**	**219,438,183**
Total Revenues	**1,160,809,248**	**-0-**	**734,716,969**	**1,895,526,217**
Expenditures				
Salaries And Benefits	10,158,082	-0-	-0-	10,158,082
Property Tax Relief	-0-	-0-	2,021,902	2,021,902
Information Technology	2,220,769	552,024	-0-	2,772,793
Current Expenses	1,173,990	-0-	-0-	1,173,990
Maintenance Other Than Buildings And Grounds	410,478	-0-	-0-	410,478
Other Expenditures	438,212	-0-	-0-	438,212
Total Expenditures	**14,401,531**	**552,024**	**2,021,902**	**16,975,457**
Excess (Deficiency) Of Revenues Over (Under) Expenditures	**1,146,407,717**	**(552,024)**	**732,695,067**	**1,878,550,760**
Other Financing Sources (Uses)				
Transfer To Health And Human Services (Note 3)	(218,313,754)	-0-	-0-	(218,313,754)
Net Appropriations (Note 4)	13,253,932	552,024	2,021,902	15,827,858
Total Other Financing Sources (Uses)	**(205,059,822)**	**552,024**	**2,021,902**	**(202,485,896)**
Excess (Deficiency) Of Revenues And Other Financing Sources Over (Under) Expenditures And Other Financing Uses	**$ 941,347,895**	**$ -0-**	**$ 734,716,969**	**$ 1,676,064,864**

The accompanying notes are an integral part of this financial statement.

STATE OF NEW HAMPSHIRE
DEPARTMENT OF REVENUE ADMINISTRATION

NOTES TO THE FINANCIAL STATEMENT
FOR THE FISCAL YEAR ENDED JUNE 30, 2014

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statement of the New Hampshire Department of Revenue Administration (Department) has been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and as prescribed by the Governmental Accounting Standards Board (GASB), which is the primary standard-setting body for establishing governmental accounting and financial reporting principles.

A. Reporting Entity

The Department of Revenue Administration is an organization of the primary government of the State of New Hampshire. The accompanying financial statement reports certain financial activity of the Department.

The financial activity of the Department of Revenue Administration is accounted for and reported in the State’s General, Education Trust, and Capital Projects Funds in the State of New Hampshire’s Comprehensive Annual Financial Report (CAFR). Assets, liabilities, and fund balances are reported for the State as a whole and by fund in the CAFR. The Department of Revenue Administration, as a department of the primary government, accounts for only a part of the State’s financial activities and those assets, liabilities, and fund balances as reported in the CAFR that are attributable to the Department cannot be determined. Accordingly, the accompanying financial statement is not intended to show the fund balances, or changes in fund balances of the Department. Likewise, the State CAFR reports governmental activities for the State as a whole in the State’s government-wide financial statements. The Department accounts for only a part of the State’s governmental activities and the governmental activities related to the Department cannot be determined. Accordingly, the accompanying financial statement is not intended to show a governmental activities presentation of the Department’s financial activities. The accompanying financial statement is intended to show a fund presentation of the Department’s revenues and expenditures in the Governmental Funds.

B. Financial Statement Presentation

A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to report financial position and the results of operations, to demonstrate legal compliance, and to aid financial management by segregating transactions related to certain government functions or activities. The Department of Revenue Administration reports its financial activity in the funds described below.

Governmental Fund Types:

General Fund: The General Fund is the State's primary operating fund and accounts for all financial transactions not accounted for in any other fund. All revenues of governmental funds, other than certain designated revenues, are credited to the General Fund. Annual expenditures that are not allocated by law to other funds are charged to the General Fund.

Education Trust Fund: In fiscal year 2000, the Education Trust Fund was created in accordance with Chapter 17:41, Laws of 1999. The fund is non-lapsing and is used to distribute adequate education grants to school districts.

Capital Projects Fund: The Capital Projects Fund is used to account for certain capital improvement appropriations which are or will be primarily funded by the issuance of State bonds or notes, other than bonds and notes for highway or turnpike purposes, or by the application of certain federal matching grants.

Reporting Period

The accompanying Department of Revenue Administration financial statement is presented for the fiscal year ended June 30, 2014.

C. Measurement Focus and Basis of Accounting

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the State generally considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Receivables not expected to be collected within 60 days are offset by deferred inflows of resources. An exception to this policy is federal grant revenue, which generally is considered to be available if collection is expected within 12 months after year end. Taxes, grants, licenses, and fees associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period.

Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, expenditures related to debt service and other long-term obligations including compensated absences, other post-employment benefits, pollution remediation obligations, and claims and judgments are recorded only when payment is due.

D. Revenues And Expenditures

In the governmental fund financial statements, revenues are reported by source and expenditures are reported by function. For budgetary control purposes, revenues are further classified as either "unrestricted" (general purpose) or "restricted." Unrestricted revenues are credited directly to the appropriate fund balance upon recording in the State's accounting system. Pursuant to the State's operating budget, unrestricted or general purpose revenues collected by an agency are not used as a direct source of funding for agency operations but are available to fund any activity accounted for in the fund. The recording of unrestricted revenues has no effect on an agency's authorization to expend funds.

Restricted revenues are either by State law or by outside restriction (e.g. federal grants), available only for specified purposes and are credited to the agency's accounting unit to which the restricted revenue is budgeted upon recording in the State's accounting system. Restricted revenues recorded by an agency are direct sources of funding for budgeted agency operations (appropriations).

Unused restricted revenues at year end are either lapsed or generally recorded as a committed or assigned fund balance. When both unrestricted (general purpose) and restricted funds are available, it is the State's policy to use restricted revenues first.

Other Financing Sources (Uses) - these additions to and reductions from resources in governmental fund financial statements normally result from transfers from/to other funds and financing provided by bond proceeds and net appropriations. Transfers are reported when incurred as "Transfers In" by the receiving fund and as "Transfers Out" by the disbursing fund.

E. Receivables

In the governmental fund financial statement, receivables are for taxpayer-assessed revenues where the underlying exchange has occurred in the period ended June 30 or prior which are received by the Department of Revenue Administration within 60 days after period-end.

F. Encumbrances

Contracts and purchasing commitments are recorded as encumbrances when the contract or purchase order is executed. Upon receipt of goods or services, the encumbrance is liquidated and the expenditure and liability are recorded.

G. Budget Control And Reporting

General Budget Policies

The statutes of the State of New Hampshire require the Governor to submit a biennial budget to the Legislature for adoption. This budget, which includes a separate budget for each year of the biennium, consists of three parts: Part I is the Governor's program for meeting all expenditure needs and estimating revenues. There is no constitutional or statutory requirement that the Governor propose, or the Legislature adopt, a budget that does not resort to borrowing. Part II is a detailed breakdown of the budget at the department level for appropriations to meet the expenditure needs of the government. Part III consists of draft appropriation bills for the appropriations made in the proposed budget.

The operating budget for State agencies, including the Department, is prepared principally on a modified cash basis and adopted for the governmental funds, with the exception of the Capital Projects Fund and certain proprietary funds. The Capital Projects Fund budget represents individual projects that extend over several fiscal years. Since the Capital Projects Fund comprises appropriations for multi-year projects, it is not included in the budget and actual comparison schedule. Fiduciary funds are not budgeted.

In addition to the enacted biennial operating budget, State departments may submit to the Legislature and Governor and Council, as required, supplemental budget requests necessary to meet expenditures during the current biennium. Appropriation transfers can be made within a department with the appropriate approvals; therefore, the legal level of budgetary control is generally at the department level.

Both the Executive and Legislative Branches of government maintain additional fiscal control procedures. The Executive Branch, represented by the Commissioner of the Department of Administrative Services, is directed to continually monitor the State's financial operations, needs, and resources, and to maintain an integrated financial accounting system. The Legislative Branch, represented by the Joint Legislative Fiscal Committee, the Joint Legislative Capital Budget Overview Committee, and the Office of Legislative Budget Assistant, monitors compliance with the budget and the effectiveness of budgeted programs.

Unexpended balances of appropriations at year-end will generally lapse to assigned or unassigned fund balance and be available for future appropriations unless they have been encumbered or legally defined as non-lapsing, which means the balances are reported as restricted, committed, or assigned fund balance. The balance of unexpended encumbrances is brought forward into the next fiscal year. Capital Projects Fund unencumbered appropriations lapse in two years unless extended or designated as non-lapsing by law.

Contracts and purchasing commitments are recorded as encumbrances when the contract or purchase order is executed. Upon receipt of goods or services, the encumbrance is liquidated and the expenditure and liability are recorded. The Department's unliquidated encumbrance balance in the General and Capital Projects Funds at June 30, 2014 were $835,923 and $772,140, respectively.

Budget To Actual Schedules for the General And Education Trust Funds are included as supplemental information.

NOTE 2 - STATEWIDE PROPERTY TAX

The Commissioner of the Department of Revenue Administration is charged by RSA 76:8 to calculate the portion of the Statewide Education Tax to be raised by each municipality by multiplying the Uniform Education Property Tax rate by the municipality's tax base. The Commissioner issues a warrant to the selectmen or assessors of each municipality directing them to assess such sum and pay it to the municipality. The Department reports the total amount of Statewide Property Tax raised by the municipalities as unrestricted revenue.

NOTE 3 - TRANSFER TO DEPARTMENT OF HEALTH AND HUMAN SERVICES

During fiscal year 2014, the Department collected and processed $180,457,706 in Medicaid Enhancement Tax and $38,345,900 in Nursing Facility Quality Assessments. The revenue was collected as tax revenue by the Department and transferred to the Department of Health and Human Services for financial reporting in the Department of Health And Human Services' Medicaid Enhancement Fund and Nursing Facility Trust Fund accounts.

NOTE 4 - NET APPROPRIATIONS

Net appropriations reflects appropriations for expenditures in excess of restricted revenues. Net appropriations are made from fund balance of the respective Governmental Fund.

NOTE 5 - EMPLOYEE BENEFIT PLANS

New Hampshire Retirement System

The New Hampshire Retirement System is the administrator of a cost-sharing multiple-employer Public Employee Retirement System (The Plan) established in 1967 by RSA 100-A:2 and is qualified as a tax-exempt organization under Sections 401(a) and 501(a) of the Internal Revenue Code. The Plan is a contributory defined-benefit plan providing service, disability, death, and vested retirement benefits to members and beneficiaries. The Plan covers substantially all full-time state employees, public school teachers and administrators, permanent firefighters, and police officers within the state of New Hampshire.

Full-time employees of political subdivisions, including counties, municipalities, and school districts, are also eligible to participate as a group if the governing body of the political subdivision has elected participation. The Plan is divided into two membership groups. Group I consists of State and local employees and teachers. Group II consists of firefighters and police officers. All assets are in a single trust and are available to pay retirement benefits to its members and beneficiaries.

Group I members at age 60 (age 65 for members beginning service on or after July 1, 2011) qualify for a normal service retirement allowance based on years of creditable service and average final compensation (AFC). The yearly pension amount is 1/60 (1.67%) of average final compensation multiplied by years of creditable service (1/66 of AFC times creditable service for members beginning service on or after July 1, 2011). AFC is defined as the average of the three highest salary years for members vested as of January 1, 2012 and five years for members not vested as of January 1, 2012. At age 65, the yearly pension amount is recalculated at 1/66 (1.5%) of AFC multiplied by years of creditable service.

Members in service with 10 or more years creditable service who are between age 50 and 60 or members in service with at least 20 or more years of service, whose combination of age and service is 70 or more, are entitled to a retirement allowance with appropriate graduated reduction based on years of creditable service.

Group II members who are age 60, or members who are at least age 45 with a minimum of 20 years of creditable service (age 50 with a minimum of 25 years of creditable service or age 60 for members beginning service on or after July 1, 2011) can receive a retirement allowance at a rate of 2.5% of AFC for each year of service not to exceed 40 years (2% of AFC times creditable service up to 42.5 years for members beginning service on or after July 1, 2011). A member who began service on or after July 1, 2011 shall not receive a service retirement allowance until attaining age 52.5, but may receive a reduced allowance after age 50 if the member has at least 25 years of creditable service. However, the allowance will be reduced by ¼ of one percent for each month prior to age 52.5 that the member receives the allowance.

Group II members hired prior to July 1, 2011 who have non-vested status as of January 1, 2012 are subject to graduated transition provisions for years of service required for regular service retirement, the minimum age for service retirement, and the multiplier used to calculate the retirement annuity, which shall be applicable on January 1, 2012.

Members of both groups may qualify for vested deferred allowances, disability allowances, and death benefit allowances subject to meeting various eligibility requirements. Benefits are based on AFC or earnable compensation, service, or both.

All covered Department employees are members of Group I.

Pursuant to RSA 100-A:52, RSA 100-A:52-a and RSA 100-A:52-b, the New Hampshire Retirement System also provides a postretirement medical premium subsidy for Group I employees and teachers and Group II police officers and firefighters.

The New Hampshire Retirement System issues publicly available financial reports that can be obtained by writing to them at 54 Regional Drive, Concord, NH 03301-8507 or from their web site at http://www.nhrs.org.

Funding Policy

The Plan is financed by contributions from the members, the State and local employers, and investment earnings. During the fiscal year ended June 30, 2014, by statute, Group I members contributed 7.0% of gross earnings. Employer contributions required to cover that amount of cost not met by the members' contributions are determined by a biennial actuarial valuation by the system's actuary using the entry age normal funding method and are expressed as a percentage of gross payroll. The State funds 100% of the employer cost for all of the Department's employees enrolled in the Plan.

The Department's normal contribution rate was 10.51% of the covered payroll for the fiscal year ended June 30, 2014. The Department's normal contributions for that period were $664,293.

Other Postemployment Benefits

In addition to providing pension benefits, RSA 21-I:30 specifies that the State provide certain health care benefits for retired employees and their spouses. These benefits include group hospitalization, hospital medical care, surgical care, and other medical care. Substantially all of the State's employees who were hired on or before June 30, 2003 and have 10 years of service, may become eligible for these benefits if they reach normal retirement age while working for the State and receive their pensions on a periodic basis rather than a lump sum. During fiscal year 2004, legislation was passed that requires State Group I employees hired on or after July 1, 2003 to have 20 years of State service in order to qualify for health benefits. During fiscal year 2011, legislation was passed that requires Group II employees to have 20 years of State service to qualify for retiree health benefits. Additionally, during fiscal year 2012, legislation was passed requiring Group I employees hired after July 1, 2011 to have 25 years of State service and increased the normal retirement age for Group I and Group II employees hired after July 1, 2011. These and similar benefits for active employees and retirees are authorized by RSA 21-I:30 and provided through the Employee and Retiree Benefit Risk Management Fund, a single-employer group health plan (Plan), which is the State's self-insurance internal service fund implemented in October 2003 for active State employees and retirees. The Plan funds the cost of medical claims by charging actuarially developed working rates to State agencies for participating employees, retirees, and eligible spouses. An additional major source of funding for retiree benefits is from the New Hampshire Retirement System's medical premium subsidy program for Group I and Group II employees.

The Department's Medical Subsidy normal contribution rate during the fiscal year ended June 30, 2014 was 1.62% of the covered payroll for its Group I employees. The Department's contributions for the Medical Subsidy for the fiscal year ended June 30, 2014 were $102,393.

The State Legislature currently plans to only partially fund (on a pay-as-you-go basis) the annual required contribution (ARC), an actuarially determined rate in accordance with the parameters of Governmental Accounting Standards Board (GASB) Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years.

The State's long-term cost of retirement health care and Other Post-Employment Benefits (OPEB) are determined actuarial on a state-wide basis as required under GASB 45. The most recent actuarial valuation was performed as of December 31, 2012. Disclosure of the annual OPEB cost, funding status, net OPEB obligation components of cost and other information concerning the plan are provided in the State of New Hampshire Comprehensive Annual Financial Report.

NOTE 6 - LITIGATION

Catholic Medical Center (CMC), et al. v. Department of Revenue Administration

Catholic Medical Center ("CMC"), Exeter Hospital ("Exeter"), Northeast Rehabilitation Hospital ("Northeast Rehab") and St. Joseph's Hospital ("St. Joseph's") filed three separate lawsuits challenging the constitutionality, both facially and as applied, of RSA 84-A, the Medicaid Enhancement Tax ("MET"). The hospitals claim the MET tax is unconstitutional under both state and federal law because: (1) it taxes hospitals for net patient services revenue (NPSR) but does not tax other medical entities for the same revenue; and (2) there is an alleged different rate of taxation assessed between the hospitals and rehabilitation hospitals. Each hospital seeks full reimbursement of the tax it paid in fiscal year 2011. These respective amounts are: CMC - $12,521,429; Exeter - $10,269,562; Northeast Rehab - $1,480,632; and St. Joseph's - $8,693,811. The parties to the CMC litigation settled the 2011 claims and agreed that the remainder of the case would be only for fiscal year 2014 and beyond. The amount at issue for fiscal year 2014 is approximately $200 million. The Northeast Rehab case is still separate but the parties in that case have also agreed to an agreed stipulation of facts and will litigate the case through cross-motions for summary judgment. After the parties filed cross motions for summary judgment, on February 7, 2014, the trial court in the Northeast Rehab case found a portion of the tax (revenue from outpatient hospital services) to be unconstitutional. It implicitly found the State's taxation of inpatient treatment to be constitutional. Finally, the trial court held that the MET did not constitute a double tax of for-profit hospitals. Both parties appealed this decision. On April 8, 2014, the trial court in the CMC case found the entire tax (inpatient and outpatient hospital services) unconstitutional.

The State entered into a global settlement with 25 hospitals including CMC, Exeter and Northeast Rehab. Litigation with these three hospitals will be stayed pending federal approval of changes to the State's distribution of DSH [disproportionate share hospital] payments. Dismissal of the litigation will not occur until after the settlement is implemented, which may take several years.

St. Joseph's did not agree to the settlement, and is the only remaining active litigant in the MET litigation challenging the constitutionality of the 2011 MET statute. The State has filed a motion arguing that the trial court's decision is now moot in light of statutory changes to MET effective June 30, 2014. On September 15, 2014, the court issued an order temporarily staying the proceedings for six months pending CMS's [Centers for Medicare and Medicaid Services] review of the amended State plan. CMS has approved the State's plan, and the State has requested that CMC and Exeter withdraw from the litigation. Once the stay is lifted, the litigation will proceed against St. Joseph's, at which time the issue of mootness will be addressed. It is not possible to predict the outcome of this case at this time.

St. Joseph Hospital v. DRA

St. Joseph Hospital has filed a lawsuit challenging the constitutionality, both facially and as applied, of RSA 84-A, the Medicaid Enhancement Tax ("MET"). The hospital claims the MET tax is unconstitutional under both state and federal law because: (1) it taxes hospitals for net patient services revenue (NPSR) but does not tax other medical entities for the allegedly same revenue; (2) it exempts rehabilitation hospitals from paying the tax despite the fact that they allegedly earn an identical revenue stream; and (3) retroactive application of amendments made to RSA 84-A in 2014 allegedly constitute unconstitutional retrospective taxation. St. Joseph Hospital seeks full reimbursement of the tax it paid in fiscal year 2014, which amounts to $9,376,356.

Eby v. State (formerly Leighton, et al. v. State of New Hampshire)

This is a class action filed in Merrimack County Superior Court against the State of New Hampshire challenging the constitutionality of the gambling winnings tax, RSA 77:39 (Supp. 2010) (repealed 2011). The State settled one plaintiff's claim (Leighton) in the amount of $260,300. Regarding the other plaintiffs, the State prevailed on summary judgment in the trial court.

Petitioners appealed and on June 13, 2014 the New Hampshire Supreme Court issued an opinion affirming the decision of the trial court. The petitioners' motion for reconsideration was denied, and the matter is now closed.

State v. Priceline, Inc. et al.

State v. Priceline is a tax case that could result in the recovery of past Meals and Rooms Tax alleged to be owed to the State. The case is in the discovery phase of litigation, with cross-motions for summary judgment expected later this year. A ruling on those motions is possible before the end of the calendar year 2015, but not certain. If the State prevails, Priceline would likely appeal. A ruling on the appeal would not be likely until calendar year 2016. This case uses contingency fee lawyers so there is no cost to the State of New Hampshire.

STATE OF NEW HAMPSHIRE
DEPARTMENT OF REVENUE ADMINISTRATION
BUDGET TO ACTUAL SCHEDULE - GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2014

Revenues	Fiscal Year 2014 Budget	Actual	Variance Favorable/ (Unfavorable)
Unrestricted Revenues			
Business Profits Tax	$ 276,010,000	$ 269,695,143	$ (6,314,857)
Meals and Rooms/Car Rentals Tax	242,400,000	254,726,036	12,326,036
Tobacco Tax	127,000,000	130,115,744	3,115,744
Interest And Dividends Tax	96,100,000	80,078,833	(16,021,167)
Business Enterprise Tax	73,600,000	72,879,023	(720,977)
Medicaid Enhancement Tax (Note 2)	72,200,000	-0-	(72,200,000)
Real Estate Transfer Tax	63,575,000	67,262,515	3,687,515
Communications Services Tax	62,500,000	59,403,396	(3,096,604)
Electricity Consumption Tax	6,000,000	6,205,463	205,463
Nursing Facility Quality Assessment (Note 2)	-0-	513,022	513,022
Other Unrestricted Revenues	-0-	491,890	491,890
Total Unrestricted Revenues	**1,019,385,000**	**941,371,065**	**(78,013,935)**
Restricted Revenues			
Medicaid Enhancement Tax (Note 2)	112,600,000	180,457,706	67,857,706
Nursing Facility Quality Assessment (Note 2)	36,597,325	37,832,878	1,235,553
Other Restricted Revenues	887,706	1,147,599	259,893
Total Restricted Revenues	**150,085,031**	**219,438,183**	**69,353,152**
Total Revenues	**1,169,470,031**	**1,160,809,248**	**(8,660,783)**
Expenditures			
Salaries And Benefits	11,536,517	10,158,082	1,378,435
Information Technology	2,553,219	2,220,769	332,450
Current Expenses	1,469,116	1,173,990	295,126
Maintenance Other Than Buildings And Grounds	729,000	410,478	318,522
Other Expenditures	582,135	438,212	143,923
Total Expenditures	**16,869,987**	**14,401,531**	**2,468,456**
Excess (Deficiency) Of Revenues Over (Under) Expenditures	**1,152,600,044**	**1,146,407,717**	**(6,192,327)**
Other Financing Sources (Uses)			
Transfer To Health And Human Services (Note 2)	(221,397,325)	(218,313,754)	3,083,571
Net Appropriations (Note 3)	15,982,281	13,253,932	(2,728,349)
Total Other Financing Sources (Uses)	**(205,415,044)**	**(205,059,822)**	**355,222**
Excess (Deficiency) Of Revenues And Other Financing Sources Over (Under) Expenditures And Other Financing Uses	**$ 947,185,000**	**$ 941,347,895**	**$ (5,837,105)**

The accompanying notes are an integral part of this schedule.

STATE OF NEW HAMPSHIRE
DEPARTMENT OF REVENUE ADMINISTRATION
BUDGET TO ACTUAL SCHEDULE - EDUCATION TRUST FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2014

Revenues	Fiscal Year 2014 Budget	Actual	Variance Favorable/ (Unfavorable)
Unrestricted Revenues			
Statewide Property Tax	$ 363,600,000	$ 363,756,125	$ 156,125
Business Enterprise Tax	149,440,000	146,194,321	(3,245,679)
Tobacco Tax	74,600,000	89,807,032	15,207,032
Business Profits Tax	58,550,000	58,108,835	(441,165)
Utility Property Tax	34,500,000	35,614,363	1,114,363
Real Estate Transfer Tax	31,325,000	33,586,680	2,261,680
Meals And Rooms/Car Rentals Tax	7,800,000	7,649,613	(150,387)
Total Unrestricted Revenues	**719,815,000**	**734,716,969**	**14,901,969**
Total Revenues	**719,815,000**	**734,716,969**	**14,901,969**
Expenditures			
Property Tax Relief (Note 4)	2,900,000	2,021,902	878,098
Total Expenditures	**2,900,000**	**2,021,902**	**878,098**
Excess (Deficiency) Of Revenues Over (Under) Expenditures	**716,915,000**	**732,695,067**	**15,780,067**
Other Financing Sources (Uses)			
Net Appropriations (Note 3)	2,900,000	2,021,902	(878,098)
Total Other Financing Sources (Uses)	**2,900,000**	**2,021,902**	**(878,098)**
Excess (Deficiency) Of Revenues And Other Financing Sources Over (Under) Expenditures And Other Financing Uses	**$ 719,815,000**	**$ 734,716,969**	**$ 14,901,969**

The accompanying notes are an integral part of this schedule.

Notes To The Budget To Actual Schedule - General And Education Trust Funds
For The Fiscal Year Ended June 30, 2014

Note 1 - General Budget Policies

The statutes of the State of New Hampshire require the Governor to submit a biennial budget to the Legislature for adoption. This budget, which includes annual budgets for each year of the biennium, consists of three parts: Part I is the Governor's program for meeting all expenditure needs as well as estimating revenues to be received. There is no constitutional or statutory requirement that the Governor propose, or the Legislature adopt, a budget that does not resort to borrowing. Part II is a detailed breakdown of the budget at the department level for appropriations to meet the expenditure needs of the government. Part III consists of draft appropriation bills for the appropriations made in the proposed budget.

The operating budget is prepared principally on a modified cash basis and adopted for the General Fund and other governmental funds, with the exception of the Capital Projects Fund.

The New Hampshire biennial budget is composed of the initial operating budget, supplemented by additional appropriations. These additional appropriations and estimated revenues from various sources are authorized by Governor and Council action, annual session laws, and existing statutes which require appropriations under certain circumstances.

The budget, as reported in the Budget To Actual Schedules, reports the initial operating budget for fiscal year 2014 as passed by the Legislature in Chapter 143, Laws of 2013.

Budgetary control is at the department level. In accordance with RSA 9:16-a, notwithstanding any other provision of law, every department is authorized to transfer funds within and among all program appropriation units within said department, provided any transfer of $75,000 or more shall require prior approval of the Joint Legislative Fiscal Committee and the Governor and Council. Additional fiscal control procedures are maintained by both the Executive and Legislative Branches of government. The Executive Branch, represented by the Commissioner of the Department of Administrative Services, is directed to continually monitor the State's financial system. The Legislative Branch, represented by the Joint Legislative Fiscal Committee, the Joint Legislative Capital Budget Overview Committee, and the Office of Legislative Budget Assistant, monitors compliance with the budget and the effectiveness of budgeted programs.

Unexpended balances of appropriations at year end will lapse to fund balance and be available for future appropriations unless they have been encumbered or are legally defined as non-lapsing accounts.

Variances - Favorable/(Unfavorable)

The variance column on the Budget To Actual Schedules highlight differences between the original 12-month operating budget and the Department of Revenue Administration's actual revenues and expenditures for the fiscal year ended June 30, 2014. Actual revenues exceeding budget or actual expenditures being less than budget generate a favorable variance. Actual revenues being less than budget or actual expenditures exceeding budget cause an unfavorable variance.

Note 2 - Transfer To Department Of Health And Human Services

During fiscal year 2014, the Department collected and processed $180,457,706 in Medicaid Enhancement Tax and $38,345,900 in Nursing Facility Quality Assessments. That revenue was collected as tax revenue by the Department and transferred to the Department of Health and Human Services for financial reporting in the Department of Health and Human Services' Medicaid Enhancement Fund and Nursing Facility Trust Fund accounts. There is no budget for these accounts at the Department of Revenue Administration. The amounts reported as original Budget on the accompanying Budget to Actual Schedule are the amounts budgeted for these accounts at the Department of Health and Human Services. Pursuant to Chapter 144:47, Laws 2013, none of the Medicaid Enhancement Tax receipts collected during fiscal year 2014 were recorded as unrestricted revenue since these revenues were needed to support medical provider payments.

Note 3 - Net Appropriations

Net appropriations reflect appropriations for expenditures in excess of restricted revenue. Net appropriations are made from the fund balance of the General Fund.

Note 4 - Property Tax Relief

During fiscal year 2014, the Department expended $2,021,902 in rebates for the Enhanced Education Property Tax Relief. Property Tax Relief payments are budgeted in the Department of Education accounts. The amount reported as original Budget on the accompanying Budget to Actual Schedule is the amount budgeted for this account at the Department of Education.

STATE OF NEW HAMPSHIRE
DEPARTMENT OF REVENUE ADMINISTRATION
SCHEDULE OF BUDGET AND EXPENDITURES
CAPITAL PROJECTS FUND

			(Unaudited)		
			Expenditures		Unexpended
		Fiscal Year	Prior Fiscal		Budget
Chapter Law, Program	**Budget**	**2014**	**Years**	**Total**	**June 30, 2014**
Chapter 145:1, XI, A, Laws of 2009					
Tax System 2010	$ 7,000,000	$ 552,024	$ 5,787,827	$ 6,339,851	$ 660,149
Total Expenditures	**$ 7,000,000**	**$ 552,024**	**$ 5,787,827**	**$ 6,339,851**	**$ 660,149**

The accompanying notes are an integral part of this schedule.

Note To The Schedule Of Budget And Expenditures - Capital Projects Fund
For The Fiscal Year Ended June 30, 2014

Note - Capital Budget

Prior to May 2004, capital projects appropriations lapsed at the end of the biennium unless extended into the subsequent capital budget. Chapter 138, Laws of 2004 changed the two-year capital budget by establishing a six-year capital budget and amending sections of RSA 9. RSA 9:18 provides that all unexpended portions of capital appropriations made by the six-year capital budget are to lapse at the end of six-years from the date the appropriation took effect. However, legislative practice has been to continue extending the lapse dates for all approved projects through the subsequent biennium.

Obligations incurred by contract are recorded as encumbrances when the contract is executed. Upon satisfactory fulfillment of the contracted services, the encumbrance is liquidated and the expenditure and liability are recorded. For capital projects that have been allowed to legislatively lapse, expenditures will be recorded in the following fiscal period to the extent contractual obligations were entered into prior to the project’s lapse date.

The lapse date for the 2010 Tax System project was extended through June 30, 2015 during the 2011 and 2013 legislative sessions.

Unexpended Budget For The Budget To Actual Schedule - Capital Projects Fund

The Schedule Of Budget And Expenditures – Capital Projects Fund shows unexpended funds at June 30, 2014 of $660,149 *(unaudited)* out of the $7 million budgeted for the project.

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APPENDIX A

CURRENT STATUS OF PRIOR FINANCIAL AUDIT FINDINGS

The following is a summary of the status, as of April 24, 2015, of the observations contained in the fiscal year 2008 financial audit report of the Department of Revenue Administration. That report can be accessed at, and printed from, the Office of Legislative Budget Assistant website at: www.gencourt.state.nh.us/LBA/AuditReports/financialreports.aspx

	Status		
Internal Control Comments			
Significant Deficiencies			
1. Formal Risk Assessment Process Should Be Established *(See Current Observation No. 1 and No. 2)*	●	○	○
2. Planning For Acquisition Of New Tax Information System Should Be Formalized *(See Current Observation No. 4)*	●	●	○
3. Process For Determining And Reporting Taxes Receivable And Associated Revenues Should Be Reviewed	●	●	●
4. Tax Overpayments Held By The Department Should Be Reported As Deferred Revenue	●	●	●
5. Understanding Of Relevant Controls At Service Providers Should Be Documented *(See Current Observation No. 3)*	●	●	○
6. Collection Of Flood Control Contributions From Other States Should Be Pursued	●	●	●
7. Reconciliation Controls Should Be Monitored	●	●	●
8. Additional Training For Reviewing And Approving Tax Relief Payments Should Be Considered	●	●	●
9. Leave Accounting Controls Should Be Strengthened	●	●	●
10. Procedures Should Be Established To Remind Board Members Of Statement Of Financial Interests Filing Requirements *(See Current Observation No. 6)*	●	●	○
11. Compliance With Municipal Reporting Statute Should Be Encouraged *(See Current Observation No. 7)*	●	○	○
Compliance Comment			
12. Administrative Rules Should Be Current *(See Current Observation No. 8)*	●	●	○

Status Key				**Count**
Fully Resolved	●	●	●	6
Substantially Resolved	●	●	○	4
Partially Resolved	●	○	○	2
Unresolved	○	○	○	0

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APPENDIX B

CURRENT STATUS OF PRIOR PERFORMANCE AUDIT FINDINGS

The following is a summary of the status, as of April 24, 2015, of the observations contained in the July 2013 performance audit report, *Department of Revenue Administration: Collection of Delinquent Taxes*. That report can be accessed at, and printed from, the Office of Legislative Budget Assistant website at:
www.gencourt.state.nh.us/LBA/AuditReports/performancereports.aspx

		Status	
Administration			
1. Improve Abatement Management	●	●	●
2. Promulgate Administrative Rules For Payment Agreements	●	●	●
3. Adopt Administrative Rules For Liens	●	●	●
4. Technical Assistance Manual Should Be Authoritative	●	●	●
5. Improve Records Management	●	●	●
6. Strengthen Information Technology Control Environment *(See Current Observation No. 2*)	●	○	○
7. Improve Risk Management *(See Current Observation No. 1 and No. 3)*	●	○	○
Operations			
8. Ensure Timely Handling Of Collection Cases	●	●	●
9. Adopt Administrative Rules For Settlement Agreements And Offers–In-Compromise	●	●	●
10. Need To Publicize Payment Options	●	●	●
11. Identify Training Needs And Develop An Appropriate Employee Training Program	●	●	●
12. Improve Interdivisional Communication	●	●	●
13. Discontinue Practice Of Requiring Delinquent Meals And Rentals Operators To Provide Bank Account Security Information	●	●	●

Status Key				**Count**
Fully Resolved	●	●	●	11
Substantially Resolved	●	●	○	0
Partially Resolved	●	○	○	2
Unresolved	○	○	○	0

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