STATE OF NEW HAMPSHIRE
LIQUOR COMMISSION

MANAGEMENT LETTER
FOR THE FISCAL YEAR ENDED JUNE 30, 2014

To The Fiscal Committee Of The General Court:

We have audited the financial statements of the New Hampshire Liquor Commission as of and for the fiscal year ended June 30, 2014 and have issued our report thereon dated December 30, 2014.

This management letter, a byproduct of the audit of the New Hampshire Liquor Commission for the fiscal year ended June 30, 2014, contains our auditor's report on internal control over financial reporting and on compliance and other matters and related audit findings. The appendix, on page 19 of the management letter, provides a summary of the status of observations presented in the fiscal year 2013 management letter of the Liquor Commission.

The New Hampshire Liquor Commission's fiscal year 2014 Annual Financial Report can be accessed online at:

http://www.gencourt.state.nh.us/LBA/AuditReports/FinancialReports/pdf/Liquor_2014_CAFR.pdf

Office of Legislative Budget Assistant

Office Of Legislative Budget Assistant

December 30, 2014

STATE OF NEW HAMPSHIRE
LIQUOR COMMISSION
2014 MANAGEMENT LETTER

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* Audit comments suggest legislative action may be required.

This report can be accessed in its entirety on-line at:
http://www.gencourt.state.nh.us/LBA/AuditReports/financialreports.aspx

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 statements of the New Hampshire Liquor Commission (Commission) which comprise the Statement of Net Position as of June 30, 2014 and the Statements of Revenues, Expenses and Changes in Net Position and Cash Flows for the year then ended, and the related notes to the financial statements and have issued our report thereon dated December 30, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Commission'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 statements, but not for the purpose of expressing an opinion on the effectiveness of the Commission's internal control. Accordingly, we do not express an opinion on the effectiveness of the Commission's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph 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. However, as described in the following observations, we identified certain deficiencies in internal control that we consider to be a material weakness and significant deficiencies.

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 a 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. We consider the deficiency described in observation No. 1 to be a material weakness.

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. We consider the deficiencies described in Observations No. 2 through No. 7 to be significant deficiencies.

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the Commission's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, rules, regulations, contracts, and grant agreements, 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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in Observations No. 8 through No. 11.

Liquor Commission's Responses To Findings

The Commission's responses to the findings identified in our audit are included with each reported finding. The Commission's responses were not subjected to the auditing procedures applied in the audit of the financial statements 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 results of that testing, and not to provide an opinion on the effectiveness of the Commission'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 Liquor Commission'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

December 30, 2014

Internal Control Comments
Material Weakness

Observation No. 1: Strengthen Core Financial Accounting And Reporting Resources

Observation:

The financial accounting and reporting control environment in place at the Commission during and subsequent to fiscal year 2014 exhibited weaknesses that impacted the Commission's ability to account for and report financial activity in compliance with accounting principles generally accepted in the United States of America (GAAP).

A primary component of an entity's overall control system is its control environment. An entity's control environment includes, among other things, its organizational structure and its assignment of authority and responsibility. The control environment has a pervasive influence on the way an entity's business activities are structured and controlled. Weaknesses in the Commission's control environment during fiscal year 2014, especially limitations in the Commission's support structure for financial accounting and reporting, were evidenced by the Commission's difficulty in preparing timely financial reporting, including preparing GAAP financial statements within the 90 day timeframe provided in statute.

During fiscal year 2014, the Commission's financial accounting and reporting expertise was centered in two key employee positions. A new employee filled the senior position in September 2013 and the other position became vacant in February 2014 and remained unfilled until October 2014. The lack of continuity in these positions created situations where the Commission found it difficult to explain and support certain accounting transactions and recorded balances. While auditors did not find it necessary to propose any material adjustments during the fiscal year 2014 audit, the audit was delayed by the Commission's difficulties in explaining and supporting certain of its accounting records including estimates for accruals of payables and receivables, accounting for the effect of certain prior year journal entries, supporting purchases of inventory, and ensuring that information systems were sufficiently secured and data was available to support financial transactions.

A similar comment was included in the fiscal year 2013 management letter.

Recommendation:

The Commission should strengthen its core financial accounting and reporting resources.

- The Commission should ensure its key financial accounting and reporting personnel have sufficient training and resources to allow them to adequately perform their responsibilities. When necessary and appropriate, the Commission's financial accounting and reporting staff should reach out for assistance to other personnel within the State with more subject matter expertise or training.

- The Commission should also establish comprehensive and documented policies and procedures for all critical financial accounting and reporting activities in order to support the responsibilities of key employees, and to provide for a continuity of operations upon employee turnover. All financial transactions should be sufficiently supported and documented to allow for an understanding of the transactions, both for the current accounting and reporting periods and possible accounting and reporting effects on future periods.

Auditee Response:

We concur. During fiscal year 2014, the Commission experienced vacancies in two key financial positions. The senior position (Financial Reporting Administrator II) was vacant in August and September 2013. The other position (Administrator III) became vacant in February 2014, and the position remained unfilled until October 2014. These positions provided the majority of the Commission's financial structure and direction, as well as ensured the control environment was documented. Difficulties ensued as a result of the lack of documentation of how data was previously collected and organized.

The Commission recently requested the authority to hire a Financial Analyst to further augment the Finance Section.

The Finance Section has undertaken a desk-audit project to document each employee's function and to create a succession plan in the event key employees leave the Commission.

The Commission will continue to strengthen its financial accounting and reporting procedures and resources.

Significant Deficiencies

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

Observation:

The Commission does not have a well-developed risk assessment process or formal disaster recovery and business continuity plans in place to plan for and respond to disruptions to its operations, including disruptions to the Commission's main computer system and to the operations of its prime vendors and service providers. The increase in operational risk posed by the lack of a well-developed risk assessment process and disaster recovery and business continuity plans was also noted in the fiscal year 2013 management letter.

Risk assessment is the process by which an organization reviews and responds to its exposure to risks, generally through the implementation of controls to limit the frequency and impact of risk events. Disaster recovery and business continuity plans, while related, do not serve the same purpose. A business continuity plan describes an organization's roadmap for continuing operations under adverse conditions, including situations where an organization faces an unanticipated vulnerability. A disaster recovery plan describes procedures and assigns responsibilities for reacting to and recovering from a natural or other disaster such as the loss of a critical asset.

The Commission faces a number of significant risks in its current operating environment. For example, the Commission relies on a legacy information system which regularly requires support from a part-time, retired Commission employee. The Commission operates 77 sales locations that require secure information and communication systems, including internet access, seven days a week for sales recording, inventory ordering, and credit card processing. The Commission relies on one key vendor for keeping essentially all of its goods in stock for immediate transport to the stores. The failure of any one of these or a number of other processes could have a significant effect on the Commission's ability to successfully operate.

Recommendation:

The Commission should institute a well-designed risk assessment process and business continuity and disaster recovery plans to assist the Commission in addressing and responding to its operational and financial risks.

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

The Commission should establish disaster recovery and continuity of operations plans that address any identified significant risks to the Commission's operations. The Commission should work with its information technology, product, warehouse, and other key vendors to understand how the risks to those entities may affect the Commission's risk to continued operations. The Commission should document plans of action to address and respond to those risks, including disasters that may arise from those risks.

Once plans are established, the Commission will need to train its employees on how to execute the plans and periodically review the plans for continued applicability.

Auditee Response:

We concur. The Liquor Commission has a Continuity of Operations Plan (COOP) plan in draft and is in the process of updating and finalizing that plan. The Commission expects to complete its COOP by September 2015.

The Commission completed a Facility Risk and Vulnerability Assessment study in July 2010. This assessment will be updated and expanded as part of our effort to complete our COOP.

We expect the final version of our COOP to address disaster recovery.

Observation No. 3: Identify And Respond To Financial Transaction Risk

Observation:

Weaknesses in the Commission's processing of certain sales and refund transactions combined with the lack of effective mitigating controls increased the risk of errors or frauds occurring in those transactions which would not be detected and corrected in a timely manner.

The Commission reported it was not fully aware of the extent of this financial activity, nor the ineffective controls over the financial activity, processed through the central business office account during fiscal year 2014.

Recommendation:

As part of its risk assessment process discussed in Observation No. 2, the Commission should perform a thorough review of its financial accounting processes to ensure that it has a complete understanding of its risk exposure in its current operations, including limitations in any current controls intended to mitigate that risk.

The Commission should establish effective controls over all significant financial transactions. Employees should not have authority or ability to process financial transactions without a suitably designed review and approval control for the appropriateness and accuracy of the transactions.

Auditee Response:

We concur. A multi-step review to document all financial accounting processes is underway. Initially, all transaction types will be reviewed to ensure duties are segregated. Where possible, the recording, custody, reporting and reconciling of such items will be performed by a different employee. Another step is to document all accounting practices. The Commission expects to hire an internal auditor to review all high-risk transaction items; including reviewing the processing of credit card and refund transactions.

Observation No. 4: Modify Controls To Address System And Process Changes

Observation:

Certain of the Liquor Commission's key purchasing and inventory controls were not operating during a significant portion of fiscal year 2014, due in part to system and process changes necessitated by the Commission's change in its warehouse vendor. While the Commission timely recognized the loss of the controls, it was unable to effectively and quickly build suitable controls into the new systems.

1) From November 2013 through March 2014, the Commission did not reconcile inventory purchases between the daily shipping orders received from the warehouser to the daily purchasing orders created by the Liquor Inventory Distribution System (LIDS). This reconciliation control is intended to ensure the Commission receives all of the products it purchases.

   During April 2014, the Commission implemented an information system reconciliation control that matches the data received from the vendor to the purchase information in LIDS. The Commission investigates discrepancies identified by the system control.

2) During the Spring of 2014, the Commission undertook a reconciliation of Commission-owned inventory transferred from the prior warehouse to the new warehouse. The reconciliation was performed over a two-month period by a part-time retired Commission employee, who had high-level access authorities to the inventory system and data. The Commission reported that the reconciliation resulted in relatively minimal adjustments to the Commission's inventory records. There was no documentation that Commission management reviewed or verified any of the adjustments resulting from the reconciliation.

3) The Commission's quarter-end physical inventory conducted at its 77 retail stores is a key inventory control. The Commission did not post the adjustments identified by the January 2014 inventory counts, reportedly due to concerns that the accuracy of the inventory counts and records were negatively affected by the effects of transition in warehouse vendors. The Commission did post adjustments identified by the April 2014 inventory counts at the stores; however, no adjustments were posted related to state-owned product held at the warehouse as the reconciliation control noted in item two above was being initiated.

Recommendation:

As part of an effective risk assessment process, management should review and modify key controls as needed prior to any significant vendor transition, system implementation, or other potential system disruption to ensure new processes will include the necessary safeguards for a controlled transition. Short-term compensating controls may need to be performed by mid and high-level management to ensure that employees with appropriate experience and skill quickly identify and respond to unexpected events that often occur during a transition. All adjustments made to financial records, including inventory, should be reviewed and approved by a knowledgeable person at a proper level of management who is otherwise independent of the transaction.

Auditee Response:

We concur. A process was not in place to properly reconcile (on a timely basis) inventory received by the Commission at the time of the warehouse changeover. The Commission needed to change reconciliation procedures as that process was different from reconciliation processes in place with the previous warehouse contractor. The Commission had to develop and implement an alternative plan to verify inventory received at the stores against inventory shipping records from the warehouse. This process was automated in March 2014.

The Commission conducted a wall to wall inventory with our new warehouse contractor in January 2014. This inventory was required to obtain a baseline of all inventory received at the new warehouse and identify any lingering problems resulting from the transition. Subsequent to completing the fiscal year 2014 financial statements, the Commission worked with the Inventory Control Manager at the new warehouse to resolve outstanding inventory issues. Ultimately, it was determined that unresolved inventory differences were less than $13,000.

Observation No. 5: Document Information System Controls

Observation:

The Commission has not established documented policies and procedures for its information system backup and recovery process. While the Commission reports information system backups are performed on a daily and weekly basis, the Commission also reports there are no documented policies and procedures describing this activity.

Backup and recovery controls are critical information technology controls intended to provide reasonable assurance that the Liquor Commission can recover from the loss or destruction of its information system hardware, software, or data. Backup and recovery controls describe how data and applications are copied, stored, and made available to replace damaged systems.

The difficulties experienced by the Commission in retrieving data for the audit related to the purchasing and shipping of inventory for specific fiscal year 2014 dates identified lapses in the Commission's data backup processes.

Not having documented backup and recovery policies and procedures increases the risk that a full and efficient recovery from a breakdown in the information system may prove difficult or impossible.

Recommendation:

The Commission, with guidance from the Department of Information Technology, should establish formal, written policies and procedures describing how its information system applications and data is to be backed up and how that backup can be restored to replace lost or damaged information and information systems. The policies and procedures should be routinely followed and periodically tested to ensure they remain current and comprehensive and can be reasonably relied upon to provide security to the information system applications and data.

Auditee Response:

We concur. Not having documented backup and recovery policies and procedures increases the risk for an incomplete and inefficient recovery. The difficulties with retrieving the back-ups noted above were documented and a corrective action plan was put in place.

The Commission will continue to assist the Department of Information Technology in identifying systems that need backup procedures; when those systems shall receive a backup; the requirement for retrieval of a backup; the review period for a backup policy and the Commission representatives that can authorize a backup or retrieval of data.

Observation No. 6: Improve Controls Over Store Payroll

Observation:

Weaknesses in the Commission's payroll process for part-time store employees identified in the fiscal year 2013 audit continued during fiscal year 2014, increasing the risk that the pay for these employees may not accurately reflect hours worked.

Store managers are responsible for keying part-time employees' hours into the State's payroll system. While there is no review and approval control for the hours keyed by the managers, employees are expected to sign a hardcopy of the timecard to demonstrate agreement with the hours worked. The Commission's *Store Operations Manual* states, "Payroll signature sheets **will be signed** by all employees for every payroll period". As originally identified in the fiscal year 2013 management letter, this control is not operating as designed.

Auditors tested a random sample of 22 fiscal year 2014 payroll transactions involving store employees below a Store Manager Level. In five of the tested transactions (23%), a signed timesheet was not available to support the hours worked. The Commission gave the following reasons for the missing or unsigned timesheets:

- the prior manager is no longer at the selected store,

- there was an oversight that has now been discussed with the manager, and
- signature sheets were thrown away when the store moved to its new location.

In addition to the five missing or unsigned timesheets, the following was noted:

- an employee signed the timesheet for only one week of the two-week pay period and
- a supervisor had the employees initial the work schedule instead of the timesheet. In this instance, the tested employee's scheduled hours did not agree with the paid hours.

In its response to the fiscal year 2013 management letter comment, the Commission reported that its planned implementation of biometric time clocks would resolve this weakness. The Commission had not implemented its biometric time clock solution as of December 30, 2014.

Recommendation:

The Commission should improve its controls over part-time pay for its store employees. Pending the implementation of its planned biometric time-clock system, the Commission should reinforce store manager compliance with its policy for store employees to sign timesheets.

Auditee Response:

We do not concur. The Liquor Commission is doing the best it can regarding store payroll given the time and resources currently required to process payroll under NH First/Lawson. This is a case where there was not adequate research of the specific needs of our agency regarding payroll systems before the Lawson Payroll module was implemented statewide. The uniqueness of our decentralized operations and significant store payroll requirements was never acknowledged. Currently, our store managers spend approximately 8 to 10 plus hours per week tracking and entering payroll information for their respective part-time store employees. With our larger retail stores, this involves payroll entries for up to 71 part-time employees. Additionally, store managers spend additional time several times a week coordinating with payroll staff at our headquarters regarding payroll issues.

The Commission is currently testing a biometric clock system that, if successful, will be installed in all 77 retail stores. This new system will allow part-timers to "clock in", thus eliminating the requirement for store managers to physically enter their hours into a timecard. The payroll data will then be uploaded to the Lawson payroll module in order for payroll to be processed.

Assuming this test is successful, the Commission expects these biometric clocks to be installed in all stores by June 30, 2015.

Observation No. 7: Determine Compliance With Federal Wage And Hour Regulations

Observation:

The State reported that, as a result of converting to a new consolidated payroll system, which among other actions required consideration of the Affordable Care Act changes which became effective in January 2015, it has become aware of certain compliance concerns with Federal wage and hour regulations associated with the State's and the Liquor Commission's payroll processing procedures.

As a result, subsequent to the end of fiscal year 2014, the State reported it intended to revise its employer classification from multiple employers, where each agency was considered a separate employer, to a single employer, where the State was considered the single employer of all State employees. Prior to the January 2015 change, each agency of the State was considered a separate employer for the wage and benefit determinations affecting its employees.

One effect of the change in employer classification would appear to require the Commission to consider the total hours worked by its employees for all State agencies combined, when determining whether the hours worked for the Commission resulted in the employees exceeding the 40 hours of work per week threshold for the payment of overtime. The State reported this payroll change would go into effect early in calendar year 2015. Prior to this change in employer classification, the Commission only considered the hours worked for the Commission in determining employee overtime pay eligibility.

At the time of this report, an estimate of potential liability for the State related to its past payroll practices, if any, cannot be determined. The Commission also had not concluded what effect this change in practice would have on its current and future employee pay and work schedules. The State reported that during the latter part of calendar year 2014, the Commission employed approximately 22 individuals who also worked part or full-time for other State agencies.

Recommendation:

The Commission and State should ensure that proper processes are in place to assure compliance with Federal wage and hour regulations.

The Commission and State should consult with appropriate parties to determine whether any liability exists for past wage and benefit determinations and whether action is required at this time relative to its pre-conversion practices.

Auditee Response:

We concur. The Commission will continue to work with the Department of Administrative Services and the appropriate state agencies to ensure compliance with all requirements including Collective Bargaining Agreements, Federal and State laws, etc.

Department of Administrative Services Response:

We concur. The State continues to review the general Human Resources (HR) and Payroll internal controls and procedures to ensure compliance with all requirements. As the State has historically operated in a very decentralized manner, the Department of Administrative Services believes that the centralization of HR and Payroll will provide additional and important internal controls in this area in the future. The Department of Administrative Services now has a fully staffed Statewide Payroll Unit within the Division of Accounting Services which currently consists of three individuals as well as a new payroll auditor.

State Compliance Comments

Observation No. 8: Pay All Liquor Commission Expenses From The Liquor Commission Fund

Observation:

Certain expenses incident to the administration of the Commission during fiscal year 2014 were not paid from the Liquor Commission Fund established by RSA 176:16.

RSA 176:16, I, provides, "...the state treasurer shall credit all gross revenue derived by the commission from the sale of liquor, or from license fees, and interest received on such moneys, to a special fund, to be known as the liquor commission fund, from which the treasurer shall pay all expenses of the commission incident to the administration of this title."

RSA 176:16, II, provides, "Notwithstanding any provision of law … the general court shall retain budgeting authority and control over the liquor commission."

The State's operating budget for fiscal year 2014 did not budget retiree healthcare costs to the Liquor Commission. During fiscal year 2014, as in prior years, the Commission's retiree healthcare costs were paid by the State's General Fund.

As a result, the Liquor Commission financial statements do not reflect the Liquor Commission's complete cost of operation. The retiree health care costs incident to the administration of the Liquor Commission were paid by the General Fund and are not reflected in the fiscal year 2014 financial activity reported in the Liquor Commission Fund.

Recommendation:

In order to have a more complete and accurate accounting for, and reporting of, the Liquor Commission's net position and results of operation, all expenses incident to the administration of the Commission should be paid from, and recorded in, the Liquor Commission Fund.

Auditee Response:

We concur. The Commission was not instructed to establish an account for retiree pension benefit health insurance during the fiscal year 2014-2015 budget process and therefore did not incorporate this into its budget for fiscal years 2014 and 2015.

The Commission has established under the Store Operations budget a class 64 Retiree Pension Benefit Health Insurance for the fiscal year 2016- 2017 biennial budget. The amount budgeted was provided by the Department of Administrative Services.

Observation No. 9: Prepare Timely Year End Financial Statements

Observation:

Stand-alone Liquor Commission financial statements, consistent with generally accepted accounting principles (GAAP), were not available within 90 days after the close of fiscal year 2014, contrary to RSA 21-I:8, II(b).

Pursuant to RSA 21-I:8, II(b), separate, stand-alone GAAP financial statements that detail the financial condition and operation of the Liquor Commission shall be available no later than 90 days after the close of the fiscal year, unless the Governor and Council provide an extension of the period. GAAP financial statements for an entity such as the Liquor Commission include the statement of net position and statements of revenues, expenses, and changes in net position and cash flows, notes to the financial statements, and management discussion and analysis.

While the statement of net position and the statements of revenues, expenses, and changes in net position and cash flows were available and included in the State's September 30 draft comprehensive annual financial report, the notes to those statements, which are required for the Liquor Commission's stand-alone financial statements, were not made available to the auditors within the statutory time-frame. An incomplete draft of financial statement notes was provided to the auditors on October 10, 2014. The Commission did not make the management discussion and analysis section of the report available until December 4, 2014. The delay in the auditor's receipt of a full GAAP financial statement presentation hindered the efficient completion of the audit.

While the statute requiring the preparation of stand-alone financial statements within 90 days of fiscal year-end was new for fiscal year 2014, the practice of preparing stand-alone financial reports was not new. The Liquor Commission has regularly prepared annual financial reports and has prepared comprehensive annual financial reports in the recent years it has been separately audited.

Recommendation:

The Commission should comply with RSA 21-I:8, II(b) and prepare timely stand-alone GAAP financial statements.

The Commission should review its fiscal year 2014 experience in preparing these financial statements to determine how it can revise its processes to become timely in financial reporting. In order to improve its ability to meet the statutory time requirement, the Commission will need to address a number of the comments noted elsewhere in this report, including strengthening its financial accounting and reporting policies and procedures, ensuring that it has appropriate financial accounting and reporting expertise with appropriate training and support to provide continuity in the event of key employee turnover, and that it receives appropriate and timely assistance, when necessary, from the Department of Administrative Services, Division of Accounting Services, as provided in RSA 21-I:8, II(b).

Auditee Response:

We concur. The Commission will make every effort to complete its financial statements within the prescribed time dictated by law.

Department of Administrative Services Response:

We concur. As a result of employee turnover at the Liquor Commission and lack of dedicated resources needed to complete the full set of financial statements by September 30, 2014, the best and most complete information was provided to the auditors as soon as possible. The Department of Administrative Services provided the best assistance and support that it could provide to the Commission during this time; however, the Department of Administrative Services also experienced turnover during this period of time and additionally had to spend a significant amount of time assisting with the development and audit of the Employee Benefit Fund financial statements which were required for the first time in fiscal year 2014 per SB 222 [RSA 21-I:8, II(c)]. The Department of Administrative Services has already been working with the Liquor Commission in planning for the preparation of the fiscal year 2015 financial statements and we will work with the Commission to meet the requirements in fiscal year 2015.

Observation No. 10: Prepare Statutorily Required Store Plan

Observation:

The Commission, as of June 30, 2014, had not adopted a statutorily-required written store plan. This observation was also noted during our fiscal year 1998, 2006, and 2013 financial audits and the 2009 performance audit of the Commission.

Pursuant to RSA 177:3, "The state liquor commission shall develop and maintain a formal written store plan for its retail liquor stores. This plan shall establish goals and policies related to the number, size, and staffing patterns of state operated retail liquor stores to ensure the efficient and effective operation of the state store system. The plan shall be reviewed and revised as necessary and shall include, but not be limited to, policies related to:

I. The operational definition of a marginal store, identification of such stores, and specific plans to consolidate or otherwise improve the profitability of such stores.
II. The optimum size, location, and staffing pattern of stores to maximize their profitability. This shall include a plan to increase use of part-time employees to reduce store personnel costs and a formula for determining appropriate rental payments for leased stores.
III. Plans for the expansion of the existing store system where such expansion is justified."

In its response to the 2013 management letter comment, the Commission reported that a store plan should be completed by the end of September 2014.

Recommendation:

The Commission should adopt a formal written store plan in compliance with RSA 177:3. Once adopted, the Commission should monitor compliance with the plan and periodically review and revise the plan as appropriate.

If the Commission does not believe a store plan for its retail stores is appropriate, it should seek to have the statute amended accordingly.

Auditee Response:

We concur. The Liquor Commission does have a current Retail Store Plan, dated September 2014. The Plan has been made available for review by the auditors.

Observation No. 11: Adopt Required Administrative Rules

Observation:

As of June 30, 2014, the Commission had not adopted administrative rules required by RSA 178:27-a, VI, and RSA 178:28, I and V, and RSA 126-K:5, II, and had not re-adopted administrative rules required by RSA 178:22.

- Pursuant to Per RSA 178:27-a, VI, *Alcohol Consultant*, "Alcohol consultants shall register each educational event with the liquor commission-division of enforcement and licensing. The commission shall adopt rules, pursuant to RSA 541-A, relative to:

  (a) The registration procedures and required information to ensure that consumers are over 21 years of age.

  (b) The signature form or other identification procedures to be used by an alcohol consultant to ensure compliance with RSA 179:5 [Prohibited Sales] and 178:27 [Direct Shippers]."

  The Commission adopted relevant administrative rules on December 10, 2014.

- Pursuant to RSA 178:28 *Discount and Credit on Sales to Licensees, "*Pursuant to RSA 541-A and in furtherance of the objectives of this chapter and title, the commission shall adopt rules providing for the following:

  I. When fixing the price for sale of liquor and wine to on-premises licensees, the commission may allow discounts at percentages to be determined by the commission from the regular retail price on case lot orders F.O.B. the warehouse or commission direct delivery system. No discount determined by the commissioner under this paragraph shall be less than 10 percent.

  V. A schedule of hours and procedures by which fortified wines and table wines may be purchased at the discount price for resale by holders of off-premises retail licenses at percentages of discount to be determined by the commission. Discounts for holders of

> off-premises retail licenses with annual wine purchases under $350,000 shall be no less than 15 percent less than the regular retail price in the liquor stores and 20 percent less than the regular price F.O.B. at the warehouse."

The Commission has not adopted administrative rules required by this statute.

- RSA 126-K:5, II, *Distribution of Free Samples* requires the Commission to adopt rules pursuant to RSA 541-A, concerning the distribution of free samples of tobacco products, e-cigarettes, or liquid nicotine to prevent their distribution to minors. The Commission has not adopted administrative rules required by this statute.

- Administrative rules adopted pursuant to RSA 178:22, *On-Premises Cocktail Lounge Licenses*, expired October 21, 2013. The Commission readopted relevant administrative rules on July 24, 2014.

The Commission's authority to regulate certain activities may be subject to challenge if statutorily required rules are not in effect.

Recommendation:

The Commission should adopt statutorily required administrative rules.

If the Commission determines that statutorily required administrative rules are not necessary for its efficient and effective operations, the Commission should seek to have the applicable statutes appropriately amended.

Auditee Response:

We concur.

Regarding RSA 178:27-a, VI, *Alcohol Consultant,* no action is required at this time as new rules were adopted.

The Commission intends to request a change to RSA 178:28 *Discount and Credit on Sales to Licensees,* as the Commission does not want the amount of the discount to be placed in an Administrative Rule as this would not allow the Commission flexibility to change the discount amounts as necessary to optimize profits without going through a lengthy rule making process every time. This would considerably delay our ability to act expeditiously.

Regarding RSA 126-K:5, II, *Distribution of Free Samples,* the Commission will immediately initiate the process to research and develop administrative rules regarding this RSA.

Regarding RSA 178:22, *On-Premises Cocktail Lounge Licenses*, no action is required at this time as these rules were readopted.

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APPENDIX

Current Status Of Prior Audit Findings

The following is a summary of the status, as of December 30, 2014, of the observations contained in the financial audit of the New Hampshire Liquor Commission for the fiscal year ended June 30, 2013. That report can be accessed at, and printed from, the Office of Legislative Budget Assistant website:
www.gencourt.state.nh.us/LBA/AuditReports/FinancialReports/pdf/Liquor_Management_Letter_2013.pdf

	Status		
Internal Control Comments			
Material Weakness			
1. Strengthen Core Financial Accounting And Reporting Resources *(See Current Observation No. 1)*	●	○	○
Significant Deficiencies			
2. Develop And Implement Comprehensive Risk Assessment Process And Business Continuity And Disaster Recovery Plans *(See Current Observation No. 2)*	●	○	○
3. Establish Fraud Policies	●	●	●
4. Document Controls Over Changes In Product Costs	●	●	●
5. Enforce And Monitor Compliance With Cash Handling Control Policies	●	●	●
6. Enforce And Monitor Controls Over Voided Sales Transactions	●	●	●
7. Review And Revise Controls Over License And Permit Revenues	●	●	●
8. Improve Accountability Controls Over License And Permit Revenues	●	○	○
9. Enforce And Monitor Compliance With Store Operations Manual *(See Current Observation No. 6)*	●	○	○
10. Align Inventory Computer Application With Intended Workflow	●	●	●
State Compliance Comments			
11. Prepare Store Plan *(See Current Observation No. 10)*	●	○	○
12. Adopt Required Rules *(See Current Observation No. 11)*	●	●	○

Status Key				**Count**
Fully Resolved	●	●	●	6
Substantially Resolved	●	●	○	1
Partially Resolved	●	○	○	5
Unresolved	○	○	○	0

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