

**STATE OF NEW HAMPSHIRE  
DEPARTMENT OF TRANSPORTATION  
BUREAU OF MECHANICAL SERVICES  
FUEL DISTRIBUTION SECTION**

**FINANCIAL AND COMPLIANCE  
AUDIT REPORT  
FOR THE YEAR ENDED  
JUNE 30, 2001**



**STATE OF NEW HAMPSHIRE  
DEPARTMENT OF TRANSPORTATION  
BUREAU OF MECHANICAL SERVICES  
FUEL DISTRIBUTION SECTION**

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**STATE OF NEW HAMPSHIRE  
DEPARTMENT OF TRANSPORTATION  
BUREAU OF MECHANICAL SERVICES  
FUEL DISTRIBUTION SECTION**

**Reporting Entity And Scope**

The reporting entity and scope of this audit and audit report is the Fuel Distribution Section of the New Hampshire Department of Transportation, Bureau of Mechanical Services, for the year ended June 30, 2001. During this period, the Fuel Distribution Section operated 96 fueling sites providing credit sales of motor fuel to state, local, and federal government organizations and certain nonprofit agencies.

**Organization**

The Fuel Distribution Section is part of the organization of the Department of Transportation, Bureau of Mechanical Services. The Fuel Distribution Section is under the direction of an engineering technician V, who reports to the Bureau administrator. The Bureau administrator reports to the director of the Division of Operations, who reports to the commissioner of the Department.

At June 30, 2001, the Fuel Distribution Section employed four permanent full-time employees. A fifth full-time employee's time was allocated between the Fuel Distribution Section and other Bureau responsibilities.

The Section's main office is located on Stickney Avenue in Concord. The main offices of the Department are located in the John O. Morton Building on Hazen Drive in Concord.

**Responsibilities**

The primary responsibility of the Fuel Distribution Section is the operation of 96 motor fueling sites located throughout the state. During fiscal year 2001, the Section sold approximately 4.6 million gallons of diesel fuel and gasoline to 793 billable customers. The operation of the Fuel Distribution Section is intended to increase efficiencies for governmental fuel purchases allowing customers to purchase fuel at near wholesale costs and avoid state and federal fuel tax refund processing while promoting environmental controls of government fuel storage and distribution by centralizing operations at regional sites. The fuel inventory maintained by the Section is also intended to provide the State with a strategic fuel reserve.

**Funding**

The financial activity of the Fuel Distribution Section is accounted for in the Highway Fund of the State of New Hampshire. A summary of the Section's fiscal year 2001 revenues and expenditures are shown graphically on page 3.

The financial activity related to the purchase and sale of motor fuel is accounted for in a revolving fund in the State's accounting system. Funds from the sale of fuel, which is priced at a ten-cent per gallon markup over cost, are intended to cover operating costs and the purchase of additional inventory for sale. The purchase and sale of motor fuel is not budgeted or subject to appropriations however, certain administrative costs of the Fuel Distribution Section are subject to budget and appropriations. The fiscal year 2001 appropriations combined with supplemental warrants, balances forward, and transfers resulted in spending authority of \$506,284 in the Highway Fund. Estimated restricted revenue combined with supplemental warrants and balances forward resulted in anticipated fiscal year 2001 revenues of \$398,439 in the Highway Fund. The following table summarizes the financial activity of the Section in the Highway Fund for the year ended June 30, 2001.

**Summary Of Revenues And Expenditures**

**Fiscal Year Ended June 30, 2001**

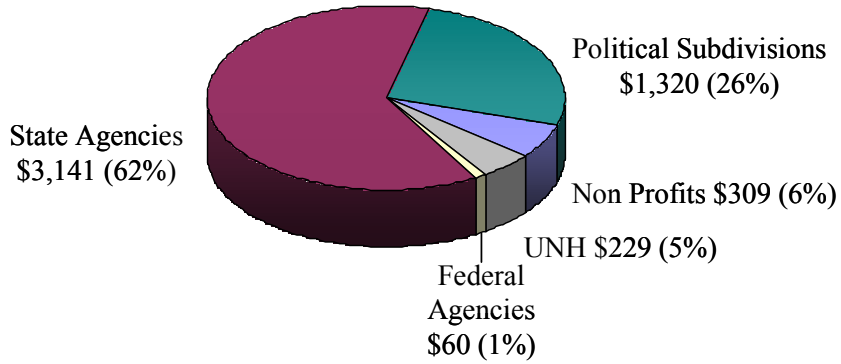
(expressed in thousands)

	<b>Highway Fund</b>
<b>Revenue</b>	
Sale Of Fuel	\$ 5,059
<b>Total Revenues</b>	<b>\$ 5,059</b>
<b>Expenditures</b>	
Purchase Of Fuel	\$ 4,551
Salaries And Benefits	226
Other	135
<b>Total Expenditures</b>	<b>\$ 4,912</b>
<b>Excess (Deficiency) Of Revenues Over (Under) Expenditures</b>	<b>\$ 147</b>

**Prior Audit**

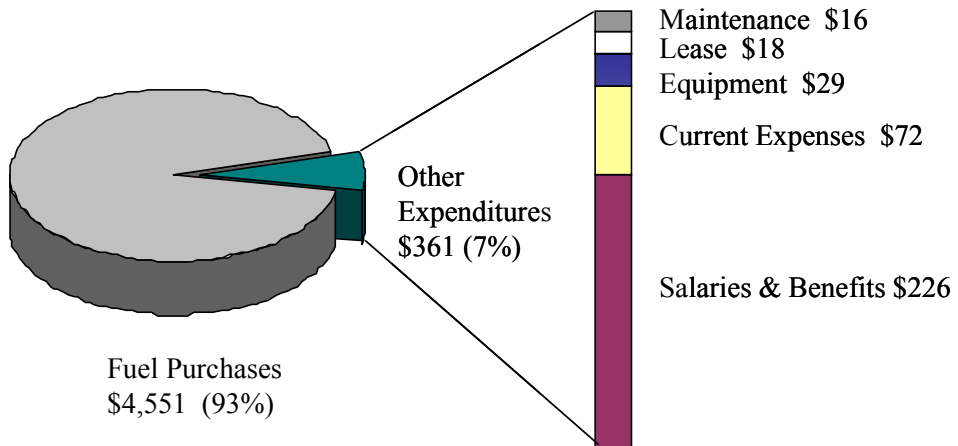
The most recent prior financial and compliance audit covering the operations of the Fuel Distribution Section was the audit of the Department of Transportation for the year ended June 30, 1994. The appendix to this report on page 39, contains a summary of the current status of the observation contained in that prior report that relates to the Department's Fuel Distribution Section operations. Copies of the prior audit report can be obtained from the Office of Legislative Budget Assistant, Audit Division, 107 North Main Street, State House Room 102, Concord, NH 03301-4906.

FUEL DISTRIBUTION SECTION  
 FISCAL YEAR 2001  
 FUEL SALES BY CUSTOMER  
 (Amounts Expressed In Thousands)



TOTAL FUEL SALES \$5,059

FUEL DISTRIBUTION SECTION  
 FISCAL YEAR 2001  
 EXPENDITURES BY TYPE  
 (Amounts Expressed In Thousands)



TOTAL EXPENDITURES \$4,912

## **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 Fuel Distribution Section of the New Hampshire Department of Transportation, Bureau of Mechanical Services, for the year ended June 30, 2001. 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 Fuel Distribution Section and tested the Section's compliance with certain provisions of applicable State laws and administrative rules. Major accounts or areas subject to our examination included, but were not limited to, the following:

- Revenues and appropriations,
- Expenditures and encumbrances,
- Inventory, and
- Real property and equipment.

Our reports on compliance and on internal control over financial reporting, and on management issues, the related observations and recommendations, our independent auditor's report, and the financial statement of the Fuel Distribution Section of the Department of Transportation, Bureau of Mechanical Services, are contained in the report that follows.



## **Auditor's Report On Compliance And On Internal Control Over Financial Reporting**

*To The Fiscal Committee Of The General Court:*

We have audited the accompanying Statement of Revenues and Expenditures – Budget and Actual – Highway Fund of the Fuel Distribution Section of the New Hampshire Department of Transportation, Bureau of Mechanical Services, for the year ended June 30, 2001, and have issued our qualified report thereon dated October 19, 2001, which was qualified with respect to the lack of presentation of the financial position of the Fuel Distribution Section in the Highway Fund and with respect to the accounting for general fixed assets. Except as discussed in the previous sentence, we conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

### Compliance

As part of obtaining reasonable assurance about whether the Fuel Distribution Section's financial statement is free of material misstatement, we performed tests of its compliance with certain provisions of laws and rules, 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 no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

## Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Fuel Distribution Section's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statement and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Fuel Distribution Section's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statement. Reportable conditions are described in observations No. 1 through No. 14 of this report.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statement being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider Observation No. 1 to be a material weakness.

This auditor's report on compliance and on internal control over financial reporting is intended solely for the information and use of the management of the Department of Transportation and the Fiscal Committee of the General Court and is not intended to be and should not be used by anyone other than these specified parties.

*Office Of Legislative Budget Assistant*  
Office Of Legislative Budget Assistant

October 19, 2001

**Internal Control Comments**  
**Material Weakness**

**Observation No. 1 - Fixed Asset Management System Should Be Established**

*Observation:*

Neither the Fuel Distribution Section nor the Department maintain inventory controls over the property and equipment utilized by the Section at its fueling sites. Costs associated with the property and equipment at the fueling sites (e.g. asset costs, maintenance and repair costs) are unknown, hindering the Section's and Department's informed decision making and planning processes over the operations of the sites.

The State's Fixed Assets Policies and Procedures Manual (dated August 14, 1996) requires each agency to have a fixed assets inventory system to record its equipment and state-owned real property (i.e., land, land improvements, buildings, building improvements, construction in progress, and infrastructure). The purpose of a fixed assets inventory system is to provide documentation, control, and accountability for fixed assets; to ensure all fixed assets are recorded; and to gather information for financial reporting and asset management purposes.

The Section operates 96 fueling sites located across New Hampshire. Assets at each site range from one to multiple fuel pumps, tanks, tank monitoring equipment, sheds, buildings, etc. The Department estimates that the original cost of the equipment and improvements made to operate the fueling sites was approximately \$2.6 million. Neither the Section nor the Department has maintained records in a manner that would allow efficient determination of the actual cost paid to purchase the equipment and improvements or what specific equipment and improvements are located at each site. Because there is no central inventory of equipment and improvement information for the fuel sites, the Section and Department do not have information necessary to properly report the cost of its fixed assets, plan for maintenance and replacement of the assets, and truly understand and control the operations of the fueling sites.

*Recommendation:*

The Section, in conjunction with the Department, should develop a fixed asset management system that could provide the information required for the efficient documentation, control, accountability, and reporting of the assets for financial reporting and asset management purposes.

*Auditee Response:*

We concur with the recommendation and as stated on several occasions in our responses to this audit report, the Division of Operations is pursuing an asset management system, which will include the fuel sites and track construction, repair and maintenance costs accordingly.

## Other Reportable Conditions

### **Observation No. 2 - Review Of Fuel Usage Should Be Performed**

#### *Observation:*

The Fuel Distribution Section does not utilize information in its automated fueling system database to review for possible misuse of fuel by its customers, including other State agencies. Fueling data such as gallons pumped, vehicle tank capacity, and fueling frequency are not reviewed for unusual transactions.

Each customer vehicle is assigned a fuel-use card and information related to the vehicle, including vehicle type, fuel type, tank capacity, etc., is captured in the Section's customer database. Each customer fueling is charged to both an operator card and a vehicle card. Fueling records include operator, vehicle, time and place of fueling, type of fuel, and number of gallons of fuel pumped.

During audit testing we noted a number of fueling transactions that appeared unusual as the gallons of fuel recorded as pumped were in excess of vehicles' tank capacities. Follow-ups with customers provided the various scenarios that resulted in these unusual transactions. According to Section personnel who contacted the customers, these unusual transactions included customers combining several separate fuelings of the same vehicle at non-automated fuel sites in one recorded transaction and customers filling large capacity fuel transfer tanks and charging the fueling to the card of a vehicle with a much smaller tank. Each of these practices is in contravention of the Fuel Distribution's fueling policies. And while no fraud was detected in the transactions that were reviewed with the Section, fraudulent transactions could be reflected in the fueling records in this manner.

According to the Section, the monitoring of customer purchases of fuel has not been considered part of the Section's responsibilities. The Section relies upon the customers to monitor proper usage of the fuel. The Section's stated primary focus has been to ensure that customers pay for fuel pumped.

#### *Recommendation:*

The Fuel Distribution Section should increase its fuel-use monitoring procedures. Fuelings in excess of vehicle tank capacities, or of fuel types that are inconsistent with vehicle information in the customer database, should be identified and flagged on the invoices to notify the Section and its customers of possible misuse of vehicle cards or other violation of fueling policies. These fuel-use monitoring procedures should be performed both as a fraud detection activity and as a review to identify customers who may need additional training or assistance in Section policies and procedures. Identifying this exception data to the customers will aid in making the customers more effective participants in ensuring that employees responsible for performing and recording fueling transactions are trained and compliant with Section policies and that vehicle information in the Section's database is current.

*Auditee Response:*

We concur with this recommendation.

The Fuel Distribution System provides its customers with a monthly fuel use statement, identifying the operator, vehicle, time of transaction, site location, fuel type and gallons pumped. Because even our fully automated sites are not “on line” for instant validation of data in the central database in Concord, much of this information that the system is capable of providing such as validating tank size and mileage ranges cannot be utilized to control the pumping of fuel.

We will consult with the software manufacturer to determine the possibility of modifying existing invoices to include identification of possible fueling discrepancies.

**Observation No. 3 - Procedures For Determining Eligibility For Tax-Free Fueling Privileges Should Be Reviewed And Formalized**

*Observation:*

The Fuel Distribution Section has not established formal criteria for determining who is eligible to use Section fuel sites and whether fuel taxes should be collected from eligible users. As a result, the Fuel Distribution Section may be inadvertently providing ineligible entities exemptions from the federal fuel excise tax and state road toll tax by allowing them to purchase tax-free fuel at Section sites.

RSA 228:24-a authorizes the Department of Transportation to sell motor fuels to departments and institutions of the state, political subdivisions of the state, and agencies of the federal government. The general policy used by the Fuel Distribution Section in implementing this statute is that if a vehicle is operated by a department or institution of the state, political subdivision of the state, agency of the federal government, or has a permanent license plate issued subject to RSA 261:92, the vehicle is eligible for service at a Fuel Distribution Section site. RSA 261:92 allows the director of the Division of Motor Vehicles to issue permanent plates to vehicles owned and driven by the federal government, the state, or any county, city, town, regional planning commission, school district, volunteer fire department, eligible nonprofit corporation operating transportation under contract with the department of transportation for the public or elderly or disabled persons, or public or private educational institutions used for the purpose of student driver training.

RSA 260:32 provides that the State road tolls [motor fuel tax collected by fuel distributors and remitted to the State] do not apply to fuel sales to the United States, its agencies or instrumentalities...and bulk sales to the state or any city, town, county, school district, or village district. RSA 260:47 provides that refunds are available to the state, its agencies, or any city, town, county, school district, or village district which uses the motor fuel in its own vehicles. In addition, refunds are available generally for off-road use of motor fuel as well as certain other uses.

IRS regulations provide for exemption from the federal fuel excise tax for state and local governments, school buses, qualified intercity or local buses, nonprofit educational organizations, etc. The IRS regulations do not provide for exemptions from the federal fuel excise tax to federal agencies and organizations.

A review of the Section's customer list yielded 10 customers that appeared to be neither state agencies, political subdivisions, nor otherwise clearly meet State or IRS eligibility criteria. The eligibility for two other customers, who held contracts with the Department of Transportation during a portion of the fiscal year, appeared to end at the completion of the contract period partway through fiscal 2001. However, they were allowed to continue to purchase tax-free fuel at the Section's sites after their eligibility had apparently ended.

In addition, the Section sold fuel to several federal organizations as allowed by State statute yet did not collect federal fuel excise tax on the transactions as required by federal regulations. The Section has no procedures for collecting or remitting federal fuel excise taxes on fuel sales to nonexempt customers.

*Recommendation:*

The Fuel Distribution Section should review whether the criteria it uses to determine eligibility for tax-free fuel is in compliance with State and IRS regulations. The Section should consider seeking advice from the Department of Safety Road Toll Administration, the Internal Revenue Service, and legal counsel versed in tax law to assist in this review. Upon the completion of the eligibility criteria review, current customers should be compared to the criteria to ensure they remain eligible. The Section should document the basis for its eligibility determination of each customer. The Section should also consider what information/evidence it will require from entities pursuing fueling privileges for use in its eligibility determination. For those entities deemed eligible, the Section will need to determine what documentation it needs to have on file in order to substantiate its eligibility determinations and at what frequency the determinations should be reevaluated to ensure the entities' continued compliance with eligibility criteria.

*Auditee Response:*

We concur with the recommendation.

We will seek immediate assistance from all of the above sources, as well as the AG's office or Legislative Services to clarify the issue of eligibility of tax-free fuel through our system. From this determination or clarification, those not entitled to the fuel will be denied further access and a published list of eligibility requirements will be issued to prospective customers.

#### **Observation No. 4 - Price Markup On Fuel Cost Should Be Based On Analysis Of Actual Costs Of Operations**

*Observation:*

The sales price of fuel is based on a ten-cent per gallon mark-up over the cost of the fuel delivered to the fuel site. The ten-cent per gallon margin was arbitrarily set without determining actual costs of operations and whether the margin adequately covered those costs.

RSA 228:24-a authorizes an assessment of a fair and equitable charge with respect to the sale of motor fuel sufficient to defray all administrative, transportation, storage, amortization, and other costs incurred by the Department in administering the fuel program. While the cost for fuel and Section administrative costs are known and recorded in the State accounting system, not all of the costs of operations of the fuel program are recognized as such. For example, the Department of Transportation and the Fuel Distribution Section do not track nor consider for potential cost recovery the expenditures associated with the creation and maintenance of the 96 fuel sites, including the costs of the tanks, pumps, and associated equipment and site improvements, to ensure that the price of the fuel recovers all costs of operations. The Department estimates the original cost of the equipment and improvements at the fuel sites was approximately \$2.6 million.

Costs of operations need to be determined before a sales price can be established sufficient to defray the costs and provide sufficient margin to administer the fuel distribution program. Incomplete understanding of costs and arbitrarily set margins hinder effective planning and other decision-making activities related to changes and improvements in fuel distribution activities.

*Recommendation:*

The Department and the Section should establish a system to properly determine and periodically report the actual costs related to the operation of the fuel distribution program. Based on an understanding of what the current costs of the operations are and the costs related to planned changes to the operations, the Section should establish margins and sales prices that are fair and equitable and sufficient to cover the cost of operations. The margins should also be sufficient to recover the planned refurbishment and improvements to the Section's property and equipment necessitated by the operation of the program.

*Auditee Response:*

We concur with the recommendation.

With the implementation of the Asset Management System, soon to be purchased by the Department and mentioned in Observations Nos. 11 and 15, it is felt that costs for installation, repairs, maintenance, and planned replacement for each fuel site can be tracked and calculated into a verifiable markup amount. This amount will cover all aspects of RSA 228.

## **Observation No. 5 - Testing Program To Monitor Quality Of Fuel Purchases Should Be Implemented**

### *Observation:*

The Fuel Distribution Section is very conscious of the need to monitor the quantity of fuel it purchases. It is less proactive in efforts to monitor the quality of the fuel it purchases.

During the year ended June 30, 2001, the Section purchased approximately \$4.6 million of motor fuel. Per its contracts with fuel vendors, there are product specifications for fuels to be delivered to Section terminals. Regular and premium unleaded gasoline must meet minimum octane ratings and reformulated gasoline must be delivered to the Section's terminals in Merrimack, Strafford, Rockingham, and Hillsborough counties. Diesel fuels must be low sulfur and blended with kerosene, as opposed to other additives, in the winter season.

Vendor compliance with contractual product requirements and specifications is not monitored on an on-going basis. The Section tests the quality of the fuel it purchases only if suspicions about fuel quality arise due to fuel-related vehicle malfunctions being reported by customers.

The Section's contracts with its fuel vendors include provisions permitting the Section to require a vendor-furnished lab analysis of the fuel delivered to Section tanks. The Section has not regularly required vendors to provide fuel analyses, partly due to the Section not wanting to burden the vendors when there are no overt fuel quality problems.

Because there are cost differentials between fuels of different specifications, and the operating characteristics of vehicles may not be affected when using different qualities of fuel, there is significant risk that fuel product provided by vendors that does not meet contract specifications will not be detected based solely on complaints of vehicle malfunctions from Section customers.

### *Recommendation:*

The Fuel Distribution Section should monitor the quality of the fuel delivered by its vendors to ensure that the Section is receiving the quality of fuel it is paying for. While requiring the load certifications from the wholesale terminals is a first step in ensuring product quality, the Section should also develop and implement a regular testing program to prove the continued quality of the product it purchases.

### *Auditee Response:*

We concur in part with the recommendation.

We will demand bills of lading (documentation) from vendors.

We concur that there needs to be a system for monitoring motor fuel delivered by our vendors, but we do not have the ability to perform the tests, nor do we possess the resources to establish a remote program of testing. We feel the program should be a part of a statewide effort to monitor



fuel supplied to commercial stations as well. Years ago, the NH Department of Agriculture, Bureau of Weights and Measures, tried to establish a program of testing fuel as a consumer action. Unleaded fuel was to be tested for octane ratings and diesel was to be tested for Cetane rating (octane for diesel), sulphur content, and bacteria content. The cost to ship a sample of gasoline out of state (there were no known labs in-state) became prohibitive and their funding for the program ended. It is hoped that program will start up again.

We have approached the Bureau of Purchase & Property in the past with this problem in hopes they could help us verify what they had awarded contracts to deliver, but their only recommendation was to force the vendor to have random samples analyzed. This, we found quickly, was not in the State's best interest.

Again, we strongly believe that we are in need of verifying the product that is being delivered to us, but we do not have the ability to perform the tests, nor do we possess the resources to establish a remote program of testing.

We will explore the possibility of cooperative efforts with other state agencies with fuel purchasing responsibilities to develop a quality assurance plan. Perhaps future legislation may be introduced as a consumer bill to test the fuel we all purchase.

#### **Observation No. 6 - Fuel-Storage Integrity Evaluations Should Be Documented**

*Observation:*

The Fuel Distribution Section does not document its evaluation of the results of its monitoring of the integrity of its fuel-storage tanks and distribution systems, including its explanations for apparent fuel gains or losses in excess of the monthly maximum allowable variances.

N.H. Admin. Rule, Env-Wm 1401.11 requires the Section to complete monthly inventory monitoring reports for each of its fuel storage tanks. The reports provide information on the daily changes in fuel inventory levels caused by deliveries of fuel to the tank and fuel pumped out of the tank. In accordance with the administrative rule, the Section is required to notify the Department of Environmental Services (DES) within 24 hours if the monthly inventory monitoring report for a tank shows an unexplained gain or loss of fuel in excess of 1% of the total metered usage plus 130 gallons. This unexplained variance could signify a tank leak with environmental consequences.

The Section reviews the monthly reports for variances that exceed the maximum allowable variances and determines the reason for the excessive variance. Excessive variances are usually caused by data not being posted to the reports or by known physical conditions such as the tilt of a tank that can interfere with standard measuring techniques. There were no potential tank leaks detected/identified by the Section during the audit period based on its review of report variances. We reviewed a sample of 24 inventory-monitoring reports prepared by the Section. Six of the 24 reports included excessive variances as defined by the administrative rule. While there was no documentation of the explanation of these variances, the Section was able to explain the

circumstances causing the variances when asked. The Section's explanations were supported by information available at the Section and did not point to leaking tanks. While the Section was able to explain each variance and therefore did not need to report variances to the DES, the process of supporting that prior decision would have been more efficient if the explanation of the variance had been documented when the determination was originally made.

*Recommendation:*

The Section should document its review for and explanations of excessive fuel storage variances. The documentation should include the Section's explanation for the variances and support for the conclusions made as to whether variances that exceed the gallon criteria require reporting.

*Auditee Response:*

We concur with the recommendation.

The section will immediately begin proper documentation of the reviews of excessive fuel storage variances as recommended. We feel that lack of proper documentation, especially relative to fuel storage variances, would not be looked upon favorably by regulatory agencies.

These reports will be reviewed by the Assistant Administrator of Mechanical Services.

**Observation No. 7 - Continued Validity Of Fuel-Card Information Should Be Periodically Reestablished**

*Observation:*

The Fuel Distribution Section relies upon customers to inform the Section when operator or vehicle cards become obsolete due to changes in employee status or vehicle use.

Operator and vehicle cards are similar to credit cards and are used to obtain fuel at the Section's fueling sites. Essentially each authorized operator has an assigned card, as does each authorized vehicle. To obtain fuel at an automated site, the operator simply has to swipe both the operator and vehicle card through the card reader and pump the fuel. The Section's automated pump system registers the purchaser and the vehicle information for billing purposes. At June 30, 2001, there were 7,200 operator and 6,400 vehicle cards in use by Section customers.

Currently, the Section relies upon notification from its customers if issued cards are no longer in use. Obsolete cards could be the result of misplaced or lost cards, vehicles being disposed of, transferred or terminated employees, etc. While the Section reported that it confirmed the continued use of cards with customers a few years ago, it reported that it has not been able to repeat the confirmation procedures due to lack of resources. The effect of not terminating cards that are no longer needed is that cards that should be deactivated (i.e., fueling privileges ceased) may remain active and provide a platform for unauthorized taking of fuel.

*Recommendation:*

The Section should apply more control over the fuel cards it issues. The Section should periodically reestablish with its customers the validity of the fuel-card information to ensure fuel cards are being used by the operators and for the vehicles intended. The Section could use this confirmation opportunity to ensure that its operator and vehicle database information remains current and accurate.

*Auditee Response:*

We concur with the recommendation.

Though we realize that simply relying upon a customer to keep its own fuel card information up to date, no clear instructions have ever been issued to instruct an agency of the procedures involved when replacing vehicles. Initially, this information will be included in the customer handbook, to be developed in response to Observation No. 9. An expiration date on the card would be in order to correct this condition.

For existing accounts, a notice will be sent with a future billing, requesting updates to their vehicle cards and identifying a date that the card will expire if no response is forwarded.

It must be noted, however that any unauthorized usage of an old card, as mentioned in the observation, would certainly be reported by an agency when auditing their monthly invoice.

**Observation No. 8 - Fuel Site Operating Guides Should Be Emphasized**

*Observation:*

The Fuel Distribution Section is not maximizing the control, efficiency, and effectiveness in operations that are promoted through the use of a comprehensive and regularly updated fuel-site operating guide.

Good internal control practices support the periodic review of an organization's operating guide to help ensure the directions provided for operations remain relevant, effective, and meet the needs of the employees who use the manuals and also support management's goals.

Comprehensive and current operating guides provide assistance and guidance to employees and promote consistency in business activities according to management's plan, and can be especially helpful as a training tool.

The Section last reviewed its fuel-site operating guides approximately three years ago. The next review of the guides has not been scheduled. The managers of three of the eight fuel sites visited during the audit reported that they did not have copies of the fuel-site operating guides.

*Recommendation:*

Formal periodic reviews of operating guides should become an established practice of the Section to help ensure the guides are current and effective in communicating policies and procedures. The guides should provide policies and procedures that promote consistency in fuel-site activities and support management's goals.

Each fuel site location should have a guide for reference as needed. Consideration should be given to developing a formal mechanism for gathering feedback on the current guides and recommendations for changes from guide users.

*Auditee Response:*

We concur with the recommendation.

With the hiring of a temporary clerical position within FDS, we will begin the process of updating our Fuel Site Operating Guide, including site specific information as well as information also found in the Operator's Handbook discussed in Observation No. 9. Each site manager will receive an Operating Guide.

**Observation No. 9 - Customer Handbook Should Be Prepared**

*Observation:*

The Fuel Distribution Section has not developed comprehensive written policies for customers of the Section's fueling operations.

The Section verbally informs new customers of Section policies including procedures for using the pumps. The Section makes available to its customers a brochure that lists the locations of the automated fueling sites, steps to operate the pumps at the automated sites, and the telephone number of the Section where further assistance is available. However, the Section's information brochure is not a comprehensive customer-use and Section-policy document. For example, the brochure does not include procedures to follow at the manual sites including how to record a fueling transaction, guidelines on the allowable uses of the fuel, consequences for unauthorized taking of fuel, how to obtain additional fuel cards, action to take if fuel cards are lost or damaged, or information on billing.

Policies need to be effectively communicated to ensure that the controls intended by the policies are understood and consistently applied. While the current procedures of providing a brochure to customers and answering questions not covered by the brochure has allowed the Section to operate, this method of communicating policies to the customers of the Section is not as efficient and effective as a comprehensive handbook. Verbal notification of policies and procedures in response to customer questions may result in inconsistent or incomplete information being provided to different users. Also, customers may not be effectively informed of all of the opportunities available to users of the Section's fueling sites.

*Recommendation:*

The Section should develop and distribute a comprehensive customer handbook to help ensure that customers are provided with comprehensive and consistent information for utilizing and doing business with the Section. The handbook should include information describing procedures for using the fueling sites, the allowable uses of tax-exempt fuel, and the responsibility of customers to monitor their proper use of the fuel.

*Auditee Response:*

We concur with the recommendation.

We concur with the recommendation and will review and update our informational items. We will produce a handbook for utilizing manual fueling facilities as well as a manual for the automated sites. Information will include operation of the pumps, recording fuel dispensed data, and instructions for lost or damaged cards. We feel that the handbook should also include information from potential customers and a more formal process for application to use the system.

We can post guidelines on intended use of the fuel through RSA 228, and any violations could result in loss of fueling privileges.

We will begin work on these informational items immediately, in hopes of producing a final version by the Fall of 2002.

**Observation No. 10 - Standardization/Policies For Initiating Reorders Should Be Established**

*Observation:*

There are no formal Fuel Distribution Section policies and procedures for fuel site managers to consider when determining when and how much fuel to order.

Managers at the 96 fuel sites request fuel deliveries through the Section office in Concord. Fuel site managers base the quantity of fuel requested on current levels of fuel on hand, the expected future need for fuel, and the tank size. There are no policies and procedures to assist the site managers in determining the most efficient time to order, the most efficient quantities to order, and the most efficient target balance to maintain on hand. While no situations were noted during the audit where a disruption of fuel sales occurred due to problems ordering fuel, there were instances when too much fuel was ordered which required the vendor to deliver the excess to a second fuel site. There were no analyses performed to determine the efficiency of the ordering processes.

There are 132 tanks located at the Section's 96 fueling sites. The capacity of most of the tanks ranges from 3,000 to 10,000 gallons. During fiscal year 2001, approximately 4.6 million gallons of fuel were pumped from these sites.

*Recommendation:*

The Section should develop policies and procedures to assist the fuel site managers in ordering fuel deliveries. These policies and procedures should be based on analyses that consider efficient ordering and purchasing, as well as other goals of the fuel section such as maintaining a strategic reserve capacity. The results of these analyses and policies may indicate that standard reorder points, adjusted for expected usage, would provide more efficient ordering for the Section.

*Auditee Response:*

We concur with the recommendation.

We currently report location balances and average usage to determine reorder quantities and time our deliveries for optimum fuel drops, but instead of this information being forwarded to the site manager, it is provided for the administrator of the Fuel Section. He must consider many variables, such as past usage, special projects near a location requiring additional fuel supply, changes in equipment assignments and most importantly temperature and weather, before determining a reorder quantity. Formal guidelines will assist in this process.

**Observation No. 11 - Segregation Of Duties Over Equipment Controls Should Be Improved**

*Observation:*

The Fuel Distribution Section's equipment policies and procedures do not properly segregate responsibilities to promote controls and accuracy in reporting equipment transactions and balances.

There is a lack of segregation of duties over the incompatible responsibilities of equipment custody and the performance of the annual physical inventory of that equipment. Each Section employee is responsible for inventorying equipment in their custody and reporting it to the Section business office. While this procedure currently used by the Section is efficient, as the employee familiar with the equipment performs the inventory, it is not an effective control process, as the procedure does not allow for an independent observation of the existence and completeness of the inventory.

*Recommendation:*

The Section should strengthen its controls over its equipment by segregating the responsibilities for custody of equipment from the responsibilities for performing the annual inventory of the equipment.

*Auditee Response:*

We concur with the recommendation.

We will include Fuel Distribution Section upper management in the annual inventory audits.

We do feel, however, that controls will be strengthened with the implementation of the Division of Operation's Asset Management System mentioned in Observation No. 15.

**Observation No. 12 - Formal Policy For The Collection Of Accounts Receivable Should Be Established**

*Observation:*

The Fuel Distribution Section and the Department's Bureau of Finance and Contracts, which is responsible for collecting payments for fuel sales, have not established a formal policy for pursuing collections on delinquent customer accounts.

The Bureau of Finance and Contracts reviews past-due accounts on a monthly basis. If the customer has four or five outstanding invoices, the Bureau contacts the customer to request payment. If the customer does not respond, the Fuel Distribution Section manager is notified of the delinquent account. If payment is not forthcoming in a timeframe negotiated with the Section manager, the fuel cards are deactivated. According to the Section manager, customers usually respond promptly and make payment on past-due balances when the cancellation of fueling privileges is threatened.

The procedures currently used by the Bureau and Section for managing and collecting accounts receivable do not include the standard procedures of monthly preparation and review of formal agings of accounts receivable, charging fees on delinquent accounts, and including a payment due date on the invoices. These procedures are generally regarded as necessary for controlling accounts receivable and ensuring that amounts due are collected efficiently, customers are treated consistently and fairly, that customers know when payments are due and consequences of not being current in their accounts, and the Bureau's and Section's costs of collections and the costs of holding overdue accounts are recovered by fees charged to delinquent customers.

During fiscal year 2001, the Section sold approximately \$5 million of fuel to over 790 customers invoicing, on average, approximately \$416,000 per month. At June 30, 2001 the Section had approximately \$462,000 of accounts receivable outstanding. While the Section and Bureau have not experienced great difficulty in collecting accounts from customers, the process could be better controlled and made more efficient.

*Recommendation:*

The Section should work with the Bureau of Finance and Contracts to develop a collection policy that standardizes collection activities. The implementation of a collection policy should

enhance the efficiency of the current collection practices. Customers should be informed of their payment responsibilities and consequences for untimely payment. The policy should include provisions to increase the controls over amounts due including the monthly preparation and review of formal agings of accounts receivable and also provisions to notify customers of procedures that will be used by the Section and Bureau to collect accounts receivable, including charging interest, application of payments, and shutting off fueling privileges.

*Auditee Response:*

We concur with the recommendation.

Currently the Fuel Distribution Section relies upon existing collection procedures within the Department, whereby after a 3<sup>rd</sup> notice is sent to a customer for non-payment (usually 90-120 days by then), the case is turned over to the AG's office, where the case may or may not be acted upon, depending on the amount. In Fuel Distribution's case, however, fuel cards can be turned off and the matter should never reach the AG. It must be noted that Finance & Contracts has produced a 100% collection rate involving FDS funds.

Nevertheless, account collection procedures are already being reviewed as a Department wide initiative and a new system or policy is currently being developed. Due in part to this recommendation, the system will include those issues pertaining to the Fuel Distribution System. It is hoped that a draft of the policy will be available before the end of fiscal 2002.

**Observation No. 13 - Method Of Recording Recovery Of Operating Costs Should Be Changed To Prevent Overstatements Of Revenues And Expenditures**

*Observation:*

The method used by the Department's Bureau of Finance and Contracts on behalf of the Fuel Distribution Section to record the recovery of administrative operating costs overstates both revenues and expenditures of the Fuel Distribution Section.

All revenue from the sale of motor fuel is first recorded in the Section's clearing account in the State's accounting system (NHIFS). Expenditures from the clearing account are used primarily to purchase additional fuel for resale. Amounts are also transferred out of the clearing account and into the Section's administrative account to support the costs of administrative operations. The Bureau of Finance and Contracts records these transactions that fund the administrative costs as expenditures out of the clearing account and revenue into the administrative account. Recording transfers within organizations as revenues and expenditures overstates actual organization revenues and expenditures. During fiscal year 2001, the recording of these transfers to the administrative account in this manner overstated both revenue and expenditures by approximately \$340,000. Because the overstatements of revenues and expenditures net on the financial statements, there is no effect on the net operations of the Section.



*Recommendation:*

The Section should work with the Department's Bureau of Finance and Contracts to revise the methods used to record the funding to the administrative account. Recording the transactions as transfers instead of revenues and expenditures could be one method that would provide for the recognition of funding in the proper accounts without overstating revenues and expenditures.

*Auditee Response:*

We concur with the recommendation.

Finance & Contracts has met recently with Administrative Services regarding this issue and F&C assures us that they will work closely with Financial Reporting to resolve this issue and strengthen end of year reporting procedures.

**Observation No. 14 - More Emphasis Should Be Placed On Determining Accurate Year-End Accounts Receivable Amounts**

*Observation:*

Errors and oversights by the Department of Transportation's Bureau of Finance and Contracts resulted in misstatements of the Fuel Distribution Section's accounts receivable at both June 30, 2000 and June 30, 2001.

At June 30, 2000, apparently due to a Bureau oversight, \$119,000 due to the Section from fuel sales to the Department's Bureau of Mechanical Services was not included in the Section's accounts receivable. In addition to understating the June 30, 2000 accounts receivable, this oversight caused an understatement in fiscal year 2000 revenues and an overstatement in fiscal year 2001 revenues in the same \$119,000 amount.

Apparently due to an error in timing, the year-end accounts receivable report run by the Bureau had an effective date of July 9 instead of June 30, 2001. As a result, the payments received on accounts during the first nine days of July understated the June 30 accounts receivable by \$47,000. In addition to understating the June 30, 2001 accounts receivable, this error caused an understatement in fiscal year 2001 revenues and an overstatement of fiscal year 2002 revenues in the same \$47,000 amount.

Because the Bureau was not accurate in determining accounts receivable amounts, the Section's revenues reported in the State's accounting system and reports for fiscal year 2001 were overstated by \$72,000, the net of these two misstatements. While the amount of this overstatement is not material to the total financial activity of the Section, the fact that errors were made in both fiscal year 2000 and 2001 indicates that more emphasis should be placed on determining these amounts.

*Recommendation:*

The Bureau of Finance and Contracts should review its year-end accounts receivable procedures to ensure that accounts receivable and the related revenues are reported accurately and in the appropriate accounting period.

*Auditee Response:*

We concur with the recommendation.

As in Observation No. 13, Finance & Contracts is committed to working with Administrative Services to strengthen its year end accounting procedures. The incident noted in the observation, whereby a \$119,000 invoice to Mechanical Services was not included in fiscal 2000 revenues for the section was perceived as an oversight by F&C, but in actuality, it may have been a result of a decision within Mechanical Services to withhold the invoice until July 1 funding became available. Steps have been taken to prevent a reoccurrence.

## **Auditor's Report On Management Issues**

*To The Fiscal Committee Of The General Court:*

We have audited the accompanying Statement of Revenues and Expenditures – Budget and Actual – Highway Fund of the Fuel Distribution Section of the New Hampshire Department of Transportation, Bureau of Mechanical Services, for the year ended June 30, 2001 and have issued our qualified report thereon dated October 19, 2001 which was qualified with respect to the lack of presentation of the financial position of the Fuel Distribution Section in the Highway Fund and with respect to the accounting for general fixed assets.

Except as discussed in the previous paragraph, we conducted our audit in accordance with auditing standards generally accepted in the United States 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 of material misstatement.

In planning and performing our audit of the financial statement of the Fuel Distribution Section for the year ended June 30, 2001, we noted certain issues related to the operation of the Fuel Distribution Section that merit management consideration but do not meet the definition of a reportable condition as defined by the American Institute of Certified Public Accountants, and were not issues of noncompliance with laws or rules.

Those issues that we believe are worthy of management consideration but do not meet the criteria of reportable conditions or noncompliance are included in Observations No. 15 and No. 16 of this report.

This auditor's report on management issues is intended solely for the information of the management of the Department of Transportation and the Fiscal Committee of the General Court and is not intended to be and should not be used by anyone other than these specified parties.

*Office Of Legislative Budget Assistant*  
Office Of Legislative Budget Assistant

October 19, 2001

## Management Issues Comments

### **Observation No. 15 - Long-Term Business Plan Should Be Developed**

#### *Observation:*

The Fuel Distribution Section has not formally developed or established a long-term business plan to identify goals and methods to measure progress toward those goals. Section operations are generally run on a day-to-day basis with little formal planning.

The Section does not have a formal plan for important aspects of its continuing operations including goals and resources needed to reach those goals. Decisions such as the replacement of existing tanks and pump equipment as they age; establishing the criteria for determining when and where to expand fueling sites and automate existing sites; how and when to incorporate new more efficient technologies; developing fuel reserve strategies; and at what point it may become more efficient for the Section to purchase fuel directly from the terminals, are currently made without the benefit of any formal Section planning document to assist in making the decisions in a coordinated and concerted effort.

A written business plan could enhance the Section's overall ability to efficiently and effectively manage operations. Established goals help to ensure operations are carried out as management intended. A written plan could assist Section management in measuring progress toward goals and to recognize and correct deviations from the plan before conditions become critical. The plan could also encourage management to look ahead to anticipate and avoid problems before they arise and affect operations.

#### *Recommendation:*

The Section in conjunction with the Department's planners should develop a written business plan. The business plan should include the goals of the Section, how management intends to meet those goals, and methods to measure progress toward the goals. Monitoring progress toward goals is essential; without it, a business plan has little value. The business plan should be periodically reviewed and updated to reflect changing operating conditions. Potential areas to consider in developing the Section's business plan include but are not limited to: 1) determining the timing of tank and pump equipment replacements, 2) determining the location of fuel sites, 3) determining whether to increase the number of automated fuel sites, 4) the use of new technologies, 5) the development of a fuel reserve strategy, and 6) contracting for fuel delivery services versus the development of an in-house delivery function.

#### *Auditee Response:*

We concur with the recommendation.

The Department of Transportation's Division of Operations is presently pursuing a computerized Asset Management System and will soon become a request for proposal. Though Fuel

Distribution Section's parent bureau (Bureau of Mechanical Services) cannot utilize the asset management system as a fleet tool, the Fuel Distribution System will use it to account for its site locations and site makeup, allowing management to develop replacement strategies where none exist now.

Item #2 of the recommendation (determining location of fuel sites) is an ongoing process and revolves around D.O.T. Patrol locations. Item #4 (the use of new technologies) is also an ongoing process, whereby newer tank monitoring systems are being budgeted for and installed to further reduce the reliance of Division personnel to monitor and report site activity. The remaining recommendations for developing a fuel reserve strategy and contracting for fuel delivery versus an in-house delivery are either being addressed or have been addressed.

The development of a fuel reserve strategy is being studied in the Department's emergency response plan and the delivery of fuel by in-house personnel has been studied and found not to be feasible, given the investment, regulations and risks involved.

#### **Observation No. 16 - Policy Of Setting Separate Fuel Prices For Each Location Should Be Reviewed**

##### *Observation:*

The fuel pricing policy used by the Fuel Distribution Section is labor intensive, as it establishes separate prices for fuel at each of the Section's 96 fuel sites.

The current pricing methodology sets the pump price at the cost of fuel delivered to the tank plus a ten-cent per gallon markup intended to cover Section costs. Under the Section's current method, prices are subject to change upon each delivery of fuel. This methodology requires the Section to perform separate price calculations and update the price information in the billing system for pumps at each of the 96 fuel sites. While some sites may go months between deliveries and resulting price changes, some of the Section's busier sites may have several deliveries in a week. Because of time constraints/unapplied or unavailable resources, there is typically a lag between the date of fuel delivery and the date of the related price change. It is not unusual for a subsequent delivery to occur before the new price is calculated and a price change is applied to the affected pump.

During our testing of the timing of price changes, we reviewed a sample of 10 deliveries to fuel sites and noted an average of 15 business days passed before the related price change was made. We noted at one site two subsequent deliveries were received and at another site one subsequent delivery was received prior to the price change related to the initial delivery having been made.

It is important to note fuel prices generally change relatively slowly and the effect of missing one or even two price changes may not be significant to the revenues collected. The Section's current pricing policy attempts to establish a level of price precision that may not be worth the necessary effort to maintain and, given the available resources, the Section may not be able to consistently achieve.

*Recommendation:*

The Section should review its current pricing method to determine whether it is as efficient and effective as intended and needed. The Section should explore whether using average costs to establish a single sales price for all pumps providing similar product may be more efficient than determining and setting individual prices at each pump without sacrificing appropriate management information on cost of product, etc. Using an average cost periodically determined based on market/commodity price, with an average delivery cost plus markup, would allow more efficient price changes and consistent pricing to all fuel customers that more closely tracks current market prices.

*Auditee Response:*

We concur with the recommendation.

We will seek assistance from Finance and Contracts in reviewing current pricing methods.

While the above process of determining actual fuel costs at each facility can be time consuming and often there are instances where one or maybe two fuel deliveries may take place before a price can be determined, we believe that we are following best management practices as they relate to system averaging of inventory.

## **Independent Auditor's Report**

*To The Fiscal Committee Of The General Court:*

We have audited the accompanying Statement of Revenues and Expenditures – Budget and Actual – Highway Fund of the Fuel Distribution Section of the New Hampshire Department of Transportation, Bureau of Mechanical Services, for the year ended June 30, 2001. This financial statement is the responsibility of the Department's management. Our responsibility is to express an opinion on this financial statement based on our audit.

Except as discussed in the fourth paragraph, we conducted our audit in accordance with auditing standards generally accepted in the United States 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 statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As more fully discussed in Note 1, the financial statement referred to above is not intended to present the financial position of the Fuel Distribution Section of the Department of Transportation in the Highway Fund.

As more fully described in Note 2, the Fuel Distribution Section does not have complete financial records to support the amounts included in the General Fixed Asset Account Group. Accordingly, we were unable to examine sufficient evidential matter to support such amounts.

In our opinion, except for the effect of such adjustments, if any, as might have been determined to be necessary had our audit not been limited in scope as discussed in the fourth paragraph and the matter discussed in the third paragraph, the financial statement referred to in the first paragraph presents fairly, in all material respects, certain financial activity of the Department's Fuel Distribution Section for the year ended June 30, 2001, in conformity with accounting principles generally accepted in the United States.

Our audit was conducted for the purpose of forming an opinion on the financial statement referred to in the first paragraph. The accompanying schedule on page 37 is presented for the purpose of additional analysis and is not a required part of the financial statement of the Fuel Distribution Section. Such information has been subjected to the auditing procedures applied in our audit of the financial statement referred to in the first paragraph and, in our opinion, is fairly presented in all material respects in relation to the financial statement taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 19, 2001 on our consideration of the Fuel Distribution Section's internal control over financial reporting and on our tests of its compliance with certain provisions of laws and rules.

*Office Of Legislative Budget Assistant*  
Office Of Legislative Budget Assistant

October 19, 2001



**STATE OF NEW HAMPSHIRE  
DEPARTMENT OF TRANSPORTATION  
BUREAU OF MECHANICAL SERVICES  
FUEL DISTRIBUTION SECTION**

**STATEMENT OF REVENUES AND EXPENDITURES  
BUDGET AND ACTUAL – HIGHWAY FUND  
FOR THE YEAR ENDED JUNE 30, 2001**

	<u>Highway Fund</u>		<b>Favorable/ (Unfavorable) Variance</b>
	<b>Budget</b>	<b>Actual</b>	
<u>Restricted Revenues</u>			
Sale Of Fuel	\$ 398,439	\$ 5,058,827	\$ 4,660,388
<b>Total Restricted Revenues</b>	<b>\$ 398,439</b>	<b>\$ 5,058,827</b>	<b>\$ 4,660,388</b>
<u>Expenditures</u>			
Purchase Of Fuel	\$ 101,695	\$ 4,551,210	\$ (4,449,515)
Salaries And Benefits	229,914	226,385	3,529
Current Expenses	76,252	72,140	4,112
Equipment	30,000	28,532	1,468
Lease Of State Owned Equipment	17,949	17,849	100
Maintenance	50,000	16,151	33,849
Miscellaneous	474	209	265
<b>Total Expenditures</b>	<b>\$ 506,284</b>	<b>\$ 4,912,476</b>	<b>\$ (4,406,192)</b>
<b>Excess (Deficiency) Of Revenues Over (Under) Expenditures</b>	<b>\$ (107,845)</b>	<b>\$ 146,351</b>	<b>\$ 254,196</b>

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

**STATE OF NEW HAMPSHIRE  
DEPARTMENT OF TRANSPORTATION  
BUREAU OF MECHANICAL SERVICES  
FUEL DISTRIBUTION SECTION**

**NOTES TO THE FINANCIAL STATEMENT  
FOR THE YEAR ENDED JUNE 30, 2001**

**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The financial statement of the Fuel Distribution Section of the New Hampshire Department of Transportation, Bureau of Mechanical Services, has been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

**A. Financial Reporting Entity**

The Department of Transportation is an organization of the primary government of the State of New Hampshire. The accompanying financial statement reports certain financial activity of the Fuel Distribution Section of the Bureau of Mechanical Services of the Department of Transportation.

The financial activity of the Fuel Distribution Section is accounted for and reported in the Highway Fund in the State of New Hampshire's Comprehensive Annual Financial Report (CAFR). Assets, liabilities, and fund balances are reported by fund for the State as a whole in the CAFR. The Fuel Distribution Section, as an organization of the primary government, accounts for only a small portion of the Highway Fund and those assets, liabilities and fund balance as reported in the CAFR that are attributable to the Fuel Distribution Section cannot be determined. Accordingly, the accompanying financial statement is not intended to show the financial position of the Fuel Distribution Section in the Highway Fund and the change in this fund balance is not reported on the accompanying financial statement.

**B. Basis Of Presentation - Fund Accounting**

The State of New Hampshire and the Fuel Distribution Section use funds and account groups to report on their financial position and the results of their operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

A fund is a separate accounting entity with a self-balancing set of accounts. An account group is a financial reporting device designed to provide accountability for certain assets and liabilities that are not recorded in the funds because they do not directly affect net expendable available financial resources.

## *Governmental Fund Types*

### General Fund

The General Fund accounts for all financial transactions not specifically accounted for in any other fund.

### Special Revenue Funds

The Highway Fund, one of the State's Special Revenue Funds, is used to account for specific revenue sources that are legally restricted to expenditures for specific purposes.

## *Account Groups*

### General Fixed Assets (Unaudited)

The General Fixed Asset Account Group is used to account for the fixed assets of the governmental funds. As of June 30, 2001, the Fuel Distribution Section had recorded in the General Fixed Assets Account Group the cost of general fixed assets based on available historical cost records. Donated fixed assets are recorded at fair market value at the time donated.

## **C. Measurement Focus And Basis Of Accounting**

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds are accounted for using the flow of current financial resources measurement focus and reported on a modified accrual basis of accounting. Accordingly, the State of New Hampshire accounts for its financial transactions relating to the Highway Fund on the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recognized when measurable and available to finance operations of the fiscal period. "Measurable" means the amount of the transaction can be determined and "available" means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Expenditures are recognized in the period in which obligations are incurred as a result of the receipt of goods or services, except that interest on long-term debt is recognized as an expenditure as it becomes payable.

## **D. Budgetary Data**

### *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 governmental and proprietary fund types with the exception of the Capital Projects Fund. The Capital Projects Fund budget represents appropriations for individual projects, which extend over several fiscal years. Fiduciary-type funds are not budgeted.

In addition to the enacted biennial operating budget, the Governor may submit to the Legislature supplemental budget requests necessary to meet expenditures during the current biennium. During the 2001 Legislative session, no significant supplemental budget requests affecting the Section were approved. Appropriation transfers can be made within a department without the approval of the Legislature; therefore, the legal level of budgetary control is at the department level. As shown on the Schedule of Budgetary Components – Highway Fund on page 37, the final budgeted amount includes the initial operating budget plus supplemental appropriation warrants, balances brought forward, and transfers.

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 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 lapse to undesignated fund balance and be available for future appropriations unless they have been encumbered or are legally defined as non-lapsing accounts. Capital Projects Fund unencumbered appropriations lapse in two years from the date appropriated unless extended or designated as non-lapsing by law.

#### *Variances - Favorable/(Unfavorable)*

The variance column on the Statement Of Revenues and Expenditures - Budget And Actual - Highway Fund highlights differences between budget and actual revenues and expenditures. For revenues, these variances are caused by actual revenue exceeding budget generating a favorable variance or actual being less than budget generating an unfavorable variance. For expenditures, a favorable variance results from actual expenditures being less than the amount budgeted for the fiscal year. The favorable expenditure variances represent a combination of ending available balances and unliquidated encumbrances. Unfavorable expenditure variances represent actual expenditures for the reporting period exceeding the amounts budgeted for the fiscal year.

The unfavorable expenditure variance on the Statement of Revenues and Expenditures - Budget and Actual - Highway Fund reflects the Fuel Distribution Section using a revolving fund to report motor fuel sales and purchases. Revenues and expenditures are not budgeted in a revolving fund. Expenditures are limited by the offsetting revenues into the fund.

### *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. The Fuel Distributions Section's unliquidated encumbrance balance at June 30, 2001 was \$47,332 in the Highway Fund.

### **E. Inventories**

Inventories for materials and supplies are determined by physical count. Inventories in the governmental funds are stated at average cost.

Governmental fund inventories are recorded under the purchase method. Reported inventory balances in the governmental funds are offset by a fund balance reserve that indicates they do not constitute "available expendable resources" even though they are part of net current assets.

### **F. Fixed Assets - General (Unaudited)**

General fixed assets are not capitalized in the funds used to acquire or construct them. Instead, capital acquisition and construction costs are reflected as expenditures in governmental funds, and the related assets are reported in the General Fixed Assets Account Group. For State Comprehensive Annual Financial Report reporting purposes, the State capitalizes equipment that costs \$10,000 or more and land, land improvements, building, building improvements, and construction in progress with costs of \$100,000 or greater. All purchased fixed assets are valued at historical cost and in some instances at estimated historical cost. Donated fixed assets are valued at their estimated fair market value on the date received. Interest costs incurred during construction are not capitalized. Public domain ("infrastructure") general fixed assets consisting of roads, bridges, dams, curbs and gutters, streets and sidewalks, drainage systems, and lighting systems are not capitalized, as these assets are immovable and of value only to the State. Assets in the General Fixed Assets Account Group are not depreciated.

### **G. Interfund And Intrafund Transactions**

The State accounts for interfund and intrafund transactions as described below:

Reimbursements - Various departments charge user fees for such services as centralized data processing, accounting and auditing, purchasing, personnel, and maintenance. In addition, the Department of Administrative Services charges rent to those departments that are housed in state-owned buildings. These fees and rent are not considered material and are recorded as revenue by the servicing department and as expenditures by the user department.

### **NOTE 2 - GENERAL FIXED ASSETS ACCOUNT GROUP (UNAUDITED)**

The following is a summary of changes in the General Fixed Asset Account Group during the year ended June 30, 2001. As well as reporting general fixed assets as defined by the State for financial reporting purposes, the Fuel Distribution Section also reports equipment using the

criteria required by the State Manual of Procedure, that being equipment with a historical cost of \$100 or more and useful life of greater than one year.

Fixed assets at the fuel sites may include land and land improvements, buildings and building improvements, and equipment. Fixed assets at the main office include equipment. The General Fixed Assets Account Group was not audited due to the absence of complete financial records to support the amounts included in the account group.

<b>General Fixed Assets</b> (expressed in thousands)	<b>Balance</b> <b>July 1, 2000</b>	<b>Additions</b>	<b>Deletions</b>	<b>Balance</b> <b>June 30, 2001</b>
Fixed Assets - Fuel Sites	\$ 2,600	\$ -0-	\$ -0-	\$ 2,600
Fixed Assets - Main Office	71	2	-0-	73
<b>Total General Fixed Assets</b>	<b>\$ 2,671</b>	<b>\$ 2</b>	<b>\$ -0-</b>	<b>\$ 2,673</b>

### NOTE 3 - MOTOR FUEL INVENTORY

The following is a summary of the Fuel Distribution Section's motor fuel inventory activity during the year ended June 30, 2001. Inventories are determined by physical observation and valued using weighted-average cost. The motor fuel inventory is recorded under the purchase method; inventories are recorded as expenditures on acquisition.

<b>Motor Fuel Inventory</b> (expressed in thousands)	<b>Balance</b> <b>July 1, 2000</b>	<b>Purchases</b>	<b>Issues</b>	<b>Balance</b> <b>June 30, 2001</b>
Motor Fuel Inventory	<u>\$ 339</u>	<u>\$ 4,551</u>	<u>\$ 4,522</u>	<u>\$ 368</u>

### NOTE 4 - EMPLOYEE BENEFIT PLANS

#### *New Hampshire Retirement System*

The Section, as an organization of the State government, participates in the New Hampshire Retirement System (Plan). 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 employees of the Section. The Plan qualifies as a tax-exempt organization under Sections 401 (a) and 501 (a) of the Internal Revenue Code. RSA 100-A established the Plan and the contribution requirements. The Plan, which is a cost-sharing, multiple-employer Public Employees Retirement System (PERS), 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 all members.

Group I members at age 60 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 AFC, multiplied by years of creditable service. AFC is defined as the average of the

three highest salary years. 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 ten or more years of creditable service who are between ages 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 at least 20 years of creditable service can receive a retirement allowance at a rate of 2.5% of AFC for each year of creditable service, not to exceed 40 years.

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.

Pursuant to RSA 100-A:50, the New Hampshire Retirement System also provides a postretirement medical premium subsidy for Group I employees of political subdivisions and teachers and Group II police officers and firefighters.

A special account has been established by RSA 100-A:16, II(h) for additional benefits. The account is credited with all the earnings of the assets in the account plus the earnings of the remaining assets of the Plan in excess of the assumed rate of return plus  $\frac{1}{2}$  of 1 percent.

The New Hampshire Retirement System issues a publicly available financial report that may be obtained by writing to them at 4 Chenell Drive, Concord, NH 03301-8509 or from their web site at <http://webster.state.nh.us/retirement>.

The Plan is financed by contributions from the members, the State and local employers, and investment earnings. In fiscal year 2001, Group I and II members were required to contribute 5% and 9.3%, respectively, 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 open group aggregate funding method and are expressed as a percentage of gross payroll. The State's share represents 100% of the employer cost for all of the Section's employees enrolled in the Plan.

The Section's payments for normal contribution costs for the year ended June 30, 2001 amounted to 3.94% of the covered payroll for its Group I employees. The Section's normal contributions for the year ended June 30, 2001 were \$6,644, an amount equal to the required employer contribution for the period.

#### *Post-employment Health Care Benefits*

In addition to providing pension benefits, RSA 21-I:30 specifies that the State provide certain health care insurance benefits for retired employees. These benefits include group hospitalization, hospital medical care, and surgical care. Substantially all of the State's employees 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.

These and similar benefits for active employees are authorized by RSA 21-I:30 and are provided through an insurance company whose premium is based on the benefits paid during the year. The State recognizes the cost of providing these benefits by paying the entire annual insurance premium.

During the year ended June 30, 2001, the State paid for the full cost of health insurance premiums for the retired employees and spouses on a pay-as-you-go basis. The cost of the health insurance for Section employees and spouses is a budgeted amount and is paid from an appropriation made to the administrative organization of the New Hampshire Retirement System. Accordingly, the cost of health insurance benefits for retired Section employees and spouses is not included in the Section's financial statement.



**STATE OF NEW HAMPSHIRE  
DEPARTMENT OF TRANSPORTATION  
BUREAU OF MECHANICAL SERVICES  
FUEL DISTRIBUTION SECTION**

**SCHEDULE OF BUDGETARY COMPONENTS  
HIGHWAY FUND  
FOR THE YEAR ENDED JUNE 30, 2001**

	<b>Operating Budget</b>	<b>Supplemental Appropriation Warrants</b>	<b>Balances Brought Forward</b>	<b>Net Transfers In/(Out)</b>	<b>Budget</b>
<b><u>Restricted Revenues</u></b>					
Sale Of Fuel	\$ 356,672	\$ 12,516	\$ 29,251	\$ -0-	\$ 398,439
<b>Total Restricted Revenues</b>	<b><u>\$ 356,672</u></b>	<b><u>\$ 12,516</u></b>	<b><u>\$ 29,251</u></b>	<b><u>\$ -0-</u></b>	<b><u>\$ 398,439</u></b>
<b><u>Expenditures</u></b>					
Purchase Of Fuel	\$ -0-	\$ -0-	\$ 101,695	\$ -0-	\$ 101,695
Salaries And Benefits	211,248	18,666	-0-	-0-	229,914
Current Expenses	72,001	-0-	4,251	-0-	76,252
Equipment	30,000	-0-	-0-	-0-	30,000
Lease Of State Owned Equipment	17,949	-0-	-0-	-0-	17,949
Maintenance	25,000	-0-	25,000	-0-	50,000
Miscellaneous	474	-0-	-0-	-0-	474
<b>Total Expenditures</b>	<b><u>\$ 356,672</u></b>	<b><u>\$ 18,666</u></b>	<b><u>\$ 130,946</u></b>	<b><u>\$ -0-</u></b>	<b><u>\$ 506,284</u></b>
<b>Excess (Deficiency) Of Revenues</b>					
Over (Under) Expenditures	<b><u>\$ -0-</u></b>	<b><u>\$ (6,150)</u></b>	<b><u>\$ (101,695)</u></b>	<b><u>\$ -0-</u></b>	<b><u>\$ (107,845)</u></b>

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## APPENDIX

### CURRENT STATUS OF PRIOR AUDIT FINDINGS

The following is a summary, as of October 19, 2001 of the status of the observation related to the Fuel Distribution Section contained in the audit report of the Department of Transportation for the year ended June 30, 1994. A copy of the prior report can be obtained from the Office of Legislative Budget Assistant, Audit Division, 107 North Main Street, State House Room 102, Concord, NH 03301-4906.

	<b>Status</b>
<b>Internal Control Structure</b>	
<i>Reportable Condition</i>	
Consumable Inventory: Motor Fuel	● ● ●

#### Status Key

Fully Resolved	●	●	●
Substantially Resolved	●	●	○
Partially Resolved	●	○	○
Unresolved	○	○	○

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