

**STATE OF NEW HAMPSHIRE
NEW HAMPSHIRE STATE PORT AUTHORITY
REPORT TO THE FISCAL COMMITTEE
JULY 14, 2000**

**STATE OF NEW HAMPSHIRE
NEW HAMPSHIRE STATE PORT AUTHORITY**

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This report can be accessed in its entirety on-line at www.state.nh.us/lba

To The Fiscal Committee Of The General Court:

We had intended to audit the accompanying financial statements of the New Hampshire State Port Authority as of and for the nine months ended March 31, 2000. We began audit fieldwork February 14, 2000.

Due to circumstances that became apparent early in audit fieldwork, as described in the accompanying observations and recommendations in this report, we determined that it was appropriate for our Office to withdraw from the audit of the financial statements and to bring a report of our findings to date to the Committee. This unprecedented course of action was taken as a result of our consideration of auditing standards and also in order to not further delay any appropriate action that may be undertaken to address what we considered to be serious problems in the Port Authority's operations. Our concern about the propriety of Port Authority activities noted during audit fieldwork caused us to meet with the New Hampshire Department of Justice in February and again in July, 2000 for both consultation purposes and to advise the Department of Justice of our concerns for possible fraudulent activity occurring at the Port Authority.

The report which follows includes an introductory section, providing background on the Port Authority's organization and operations; a comments section, including comments categorized as internal control, compliance, and management issues related to the Port Authority; other agency comments – comments on the relationship between the Port Authority and the Department of Administrative Services; and a financial section, including **unaudited** financial statements of the Port Authority.

It is important to emphasize that the accompanying financial statements have not been audited by us. The financial statements in this report are the representations of management and are included to provide the reader with some perspective on the extent of the Port Authority's financial operations. It is also important to note that the scope of work that we performed was less than what would have been performed had an audit been completed. While the number and nature of the observations included in this report indicated serious problems at the Port Authority, there is no assurance given that all significant problems that may exist at the Port Authority have been identified and included in this report.

Office Of Legislative Budget Assistant

Office Of Legislative Budget Assistant

July 14, 2000

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**STATE OF NEW HAMPSHIRE
NEW HAMPSHIRE STATE PORT AUTHORITY**

Organization

The New Hampshire State Port Authority, an agency of the State of New Hampshire, was established by RSA 271-A:1 to consist of and be governed by a board of eight members including the Mayor of the City of Portsmouth, the Commissioner of the New Hampshire Department of Resources and Economic Development, and six additional members appointed by the Governor with the advice and consent of the Council. The Governor and Council also appoint a director of the Port Authority who holds office for a five-year term. The director serves as the chief administrative officer of the Port Authority and performs such duties as the Authority may require. The Port Authority is authorized and empowered to appoint and compensate a chief harbor master and harbor masters at Hampton, Rye, New Castle, Portsmouth, Seabrook and Newington who enforce the directives of the Port Authority, such as the placement of moorings, the assignment of anchorage areas, and the movement of traffic. The Port Authority may appoint assistant harbor masters.

At March 31, 2000, the Port Authority employed a port operations manager, who also served as the interim port director, a chief harbor master, three office personnel, and five part-time harbor masters.

Responsibilities

The Port Authority is charged, along with the Department of Resources and Economic Development, with the responsibility to:

1. Plan for the maintenance and development of the ports, harbors, and navigable tidal rivers of the state to foster and stimulate commerce and the shipment of freight;
2. Aid in the development of salt water fisheries and associated industries;
3. Cooperate with any federal agencies or departments in planning the maintenance, development, and use of the state ports, harbors, and navigable tidal rivers; and
4. Plan, develop, maintain, use, and operate land transportation facilities within a 15 mile radius of the Port Authority headquarters in Portsmouth.

The Port Authority is authorized to contract with and secure the services of a port terminal operating firm, subject to the review and approval of Governor and Council; setting and collecting fees for mooring and slip permits and waiting lists for such permits; and installing and continually maintaining a uniform system for marking the intercoastal waters of the state including the ports, harbors, and navigable tidal rivers not presently marked by the U.S. Coast Guard. The Port Authority became responsible for non-recreational activities at the State-owned commercial fishing piers in Portsmouth, Rye Harbor, and Hampton Harbor by Chapter 55:6 of the Laws of 2000, effective June 16, 2000.

Responsibilities (Continued)

The Port Authority is also authorized to make application to the U.S. Secretary of Commerce for the purpose of establishing, operating, and maintaining foreign-trade zones in the state.

Funding

The Port Authority is funded by appropriations in the General, Special, and Capital Projects Funds. The fiscal year 2000 appropriations combined with supplemental warrants, balances forward, and transfers resulted in spending authority of \$608,692, \$299,141, and \$14,855,869 in the General, Special, and Capital Projects Funds, respectively, at March 31, 2000. Estimated unrestricted and restricted revenues combined with supplemental warrants and balances forward resulted in anticipated fiscal year 2000 revenues of \$578,015, \$164,780, and \$2,181,115 in the General, Special, and Capital Projects Funds, respectively, at March 31, 2000. The following table summarizes the financial activity of the Port Authority, as reported by the Port Authority in the General, Special, and Capital Projects Funds for the nine months ended March 31, 2000.

Summary Of Revenues And Expenditures Nine Months Ended March 31, 2000

	General Fund	Special Fund	Capital Projects Fund	Total
Unrestricted Revenues	\$ 240,001	\$ -0-	\$ -0-	\$ 240,001
Restricted Revenues	107,803	27,347	2,121,020	2,256,170
Total Revenues	<u>\$ 347,804</u>	<u>\$ 27,347</u>	<u>\$ 2,121,020</u>	<u>\$ 2,496,171</u>
Expenditures	<u>\$ 348,447</u>	<u>\$ 1,229</u>	<u>\$ 92,066</u>	<u>\$ 441,742</u>
Other Financing Sources	\$ -0-	\$ 132,708	\$ -0-	\$ 132,708
Other Financing Uses	<u>\$ -0-</u>	<u>\$ 214,500</u>	<u>\$ -0-</u>	<u>\$ 214,500</u>
Excess (Deficiency) Of Revenues And Other Financing Sources Over (Under) Expenditures And Other Financing Uses	<u>\$ (643)</u>	<u>\$ (55,674)</u>	<u>\$ 2,028,954</u>	<u>\$ 1,972,637</u>

The Port Authority also operates a Marketing Fund, an "off-State-books" trust fund, to promote activities at the Port's terminal. Through provisions in the Port Authority's contract with the port terminal operator (contract effective through July 2000), the port terminal operator provides a \$50,000 annual payment to the Marketing Fund.

A Port Authority Maintenance Fund, effective January 2000, also an "off-State-books" trust fund, is funded by a \$5,000 annual payment from a lessee of Port property. The Maintenance Fund is intended to be used to provide maintenance of the Port Authority facilities utilized by the lessee, which operates a transportation and sightseeing steamship company.

Funding (Continued)

RSA 271-A:21, effective July 1, 1999, established a Dredging Projects Fund (revised to Harbor Dredging and Pier Maintenance Fund, effective June 16, 2000). During the nine months ended March 31, 2000, there was no activity in this fund.

Prior Audit

The most recent prior financial and compliance audit of the New Hampshire State Port Authority was for the eighteen months ended December 31, 1985. The appendix to this report on page 61, contains a summary of the current status of the observations contained in the 1985 report. 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.

Internal Control Comments

Observation No. 1 - Lack Of Oversight By The Port Authority Board Has Allowed An Environment Conducive To Potential Abuse And Mismanagement

Observation:

The Port Authority Board (Board) has not met its responsibility for the management of the Port Authority's (Port) affairs and has allowed Port employees to manage the Port operations without effective oversight.

State statutes place the overall responsibility for the operation of the Port on the Board. RSA 271-A:1, I states "There shall be a New Hampshire state port authority, consisting of and governed by a board...." RSA 271-A:1, II provides that the Board "shall have the right to ... establish bylaws and regulations for the management of its affairs...." The Board's apparent lack of control awareness has allowed the Port employees to usurp the Board's authority over Port operations and has allowed the Port to operate without effective oversight.

For example, as discussed in the observations in this report, the Board did not require Port employees to adhere to Board Bylaws controlling expenditures, did not require its contracted terminal operator to comply with contract requirements, did not require a lessee to comply with contract requirements, did not recognize when these organizations were not in compliance, did not recognize when Port employees were not adhering to Board Bylaws, State policies and procedures, or common good business practice, and apparently was not aware of the Port's day-to-day activities for which it was responsible. Because the Board did not maintain effective oversight of Port operations, the Board was not aware that Port operations were not in compliance with Board expectations. Poor management oversight creates an environment where abuse and mismanagement can go undetected.

Recommendation:

The Board must reestablish its authority over Port operations. The Board must become more aware of and involved in the administrative operations of the Port. The Board must ensure that the Port employees are aware of and comply with Board Bylaws, administrative rules, State and federal policies and procedures, and general good business practice.

Port Authority Response:

While past Boards may have not been as vigilant as they could have been over the past 15 years, the present Board cannot evaluate all previous Boards that have managed the Port Authority affairs since the last audit in 1985.

Observation No. 1 - Lack Of Oversight By The Port Authority Board Has Allowed An Environment Conducive To Potential Abuse And Mismanagement (Continued)

Port Authority Response (Continued):

The present Board can report that in the past 16 months it has reestablished its authority over Port operations through the institution of many significant management oversight controls and measures. In fact, were it not for the Board's actions past practices would be continuing today.

By the later part of 1999, the Board had become dissatisfied with the past Executive Director's management/administration of the Port Authority and undertook measures to make fundamental changes in Port Operations as this audit subsequently concurred with. Between September 1999 and December 1999 the Board instituted a variety of management/administrative policies and procedures requiring the past Executive Director to:

- Provide the Board with written weekly reports on the Port's day-to-day operation.
- Involve the Board in administrative operations at the Port, including staff organization/changes, operating/capital budgets, current and past expense statements, cargos (type, tonnage, import/export), lease and operator contract requirement compliance, etc.
- Complete a Master Plan for the Market Street Marine Terminal.
- Hire qualified staff to administer the Commercial Fishing Program Revolving Loan Fund (RLF) and Port operations.

On December 15, 1999 the Authority's Executive Director since 1996 tendered his resignation with very short notice, and 18 months before the end of his appointment term. Few of the above directed Board policies and procedures had been progressed by the Past Director and none were completed.

On December 20, 1999 the Board temporarily reassigned duties/responsibilities of the Executive Director to the Port's Operations Manager in order to provide interim management and controls at the Port Authority; and initiated a nationwide Executive search for a new Port Director.

In January 2000, the Board requested an audit of the Authority be completed by the NH Office of the Legislative Budget Assistant (LBA) in part due to the general concerns stated above. The Board and current Authority staff have cooperated fully with the LBA auditors and welcome the opportunity to continue making necessary changes at the Port.

Even though the Board was dissatisfied with previous management and initiated a change in staff followed by a request for an audit, still the Board and current staff have been surprised and extremely disappointed with many of the audit observations. Over the past 6 months the Board and current staff have worked diligently and quickly to correct the problems.

Observation No. 1 - Lack Of Oversight By The Port Authority Board Has Allowed An Environment Conducive To Potential Abuse And Mismanagement (Continued)

Port Authority Response (Continued):

These efforts have included the following:

- Issuing Interim Administrative Policies and Procedures
- Increasing the number of Board subcommittees from 4 to 7
- Increasing the number of Board officers from 3 to 4
- Amending the Port Authority's By-laws to require regular audits
- Requiring formal monthly Port Operation Reports to be submitted (and accepted by vote) to the Board on a monthly basis.

It should be noted that the Board is comprised of eight (8) volunteers who are appointed to govern the NH Port Authority (NHPA) and provide policy guidance. With regards to management and administration, the Authority's enabling legislation (RSA 271-A) states that the Governor and Executive Council appointed Executive Director "...shall serve as chief administrative officer of the Port Authority..." as a full time State employee. The Authority's Executive Director receives much of his administrative and fiscal oversight from the NH Department of Administrative Services (DAS).

The Board and current Authority Staff remain committed to operating an effective Port Authority, but need the assistance of the NH DAS and sufficient staffing levels to avoid these problems from reoccurring in the future.

Auditor's Addendum:

The controls over the Port's operations have been less than effective for a number of years. (We noted a 1996 payment for two tires and an oil change for an employee's personal vehicle.) While the Board's requests for certain reporting from the prior port director in the fall of 1999 may evidence an increase in Board management oversight during this period of time, it is not clear that the Board understood the significance of the management problems at the Port. The LBA auditors, on several occasions during a January meeting and during phone calls when the Board's request for an audit was discussed, directly asked Board representatives and the interim port director whether the Board had any specific concerns over the operations of the Port, especially considering the recent changes in personnel at the Port. The Board's representative stated that the Board did not have any specific concerns related to the Port's operations or to the performance of current or former Port employees beyond the risk related to having "off-State-books" checking accounts at the Port.

While the LBA supports the Board's intentions to move forward with appropriate actions to reinforce controls, the episode reveals a basic requirement for the volunteer leadership of an agency. If you accept the responsibility to sit on the governing board of an agency, you need to be sufficiently involved to understand the day-to-day activities that affect the financial viability of that agency. Failure to do so encourages problems that may prevent you from accomplishing the laudable goals set for your organization.

Observation No. 2 - Inadequate Segregation Of Duties Over The Processing Of Expenditures In The Port Authority Office And Lack Of Alternative/Mitigating Procedures

Observation:

Port Authority (Port) expenditures were not effectively controlled during and prior to the intended audit period.

Port management's apparent lack of control awareness, including failure to establish and enforce an effective segregation of duties over expenditures and failure to enforce adherence to Port Board Bylaws requiring submission of significant expenditures for Board approval, has resulted in an environment where errors or frauds in expenditure processing may go undetected. The Port has not established effective mitigating or countervailing controls to offset the risk of undetected errors or frauds that may occur as a result of this lack of segregation of duties over expenditure processing. Compounding the seriousness of the lack of segregation of duties is the lack of expertise and training in State accounting policies and procedures provided to the Port employee responsible for processing expenditures. Due to this lack of training/expertise, inappropriate expenditure transactions have been processed - including duplicate payments, questionable expenditures, and improper account allocations - that have not been detected by Port or Department of Administrative Services personnel.

The Port's management is responsible for establishing controls (policies and procedures) to provide reasonable assurance that its objectives are achieved. Segregation of duties is a primary control activity used to detect errors or frauds that may occur. The fundamental purpose of properly segregating duties is to protect the integrity of the accounting and administrative systems by ensuring that no one employee is in a position to both commit, either intentionally or unintentionally, errors or frauds and is also responsible for the detection of those errors or frauds. Management did not meet this responsibility.

Recommendation:

The Port should immediately take steps to ensure that its accounting personnel receive appropriate training in State controls (policies and procedures) so that they can become effective components of the Port's and the State's control system.

The Port should increase controls over its expenditure process. Where possible, duties should be sufficiently segregated to provide reasonable assurance that errors or frauds occurring would be detected and corrected in a timely manner in the normal course of business. If the Port determines that there are not sufficient suitably trained employees available in its business office to provide for adequate segregation of duties, the Port should implement appropriate mitigating controls that could include management's review of supporting transaction reports and other documentation reporting expenditure activity.

The Port Board should require compliance with its Bylaws. If the Bylaws do not address the current needs of the Port, the Bylaws should be revised as appropriate and not ignored.

Observation No. 2 - Inadequate Segregation Of Duties Over The Processing Of Expenditures In The Port Authority Office And Lack Of Alternative/Mitigating Procedures (Continued)

Port Authority Response:

We concur. The previous administration set the practices that were observed. The present administration actively participated in the audit and made corrections in operating procedures that are compliant with State procedures. The Port Authority asked for the audit to assure compliance with regulations and by-laws. Additionally, new administrative procedures have been initiated that require financial reporting be provided to the Board for review at the regular Board meetings. The Board has also revised its bylaws to address these concerns and requires strict compliance with these bylaws.

Observation No. 3 - The Port Authority Has Made Numerous Payments For Personal Items And Other Expenditures That Do Not Appear To Have Furthered State And Port Operations

Observation:

The Port Authority (Port) has historically made purchases that appear questionable with regards to whether the purchases furthered the State's and the Port's operations.

Port resources, including State appropriations, should be husbanded and expended only to further State and Port operations. However, Port management's apparent lack of control awareness of the Port expenditures has allowed State and Port resources to be squandered on questionable expenditures. Port and State resources have been used inefficiently at best and possibly fraudulently. For example:

1. As further discussed in Observation No. 4, on July 12, 1999 the Port purchased a \$3,400 snowplow which was mounted on the prior port director's private vehicle. This plow was purchased ostensibly to plow snow at the Port, even though the Port had no snowplowing responsibilities. This expenditure was made from the Port's Marketing Trust Fund. (The plow was subsequently removed from this private vehicle.)
2. On July 26, 1999, the Port paid \$200 for three additional cutting edges ostensibly for the snowplow mentioned above. Even if the Port had snowplowing responsibilities, the need for three additional cutting edges for this plow would be questioned as a single cutting edge generally lasts more than one season, even if the plow is used commercially. This expenditure was made from the Port's State appropriation accounts.
3. On July 13, 1999, the Port paid \$40 for a convertible top for a Jeep vehicle. While the Port does not own a Jeep vehicle, two Port employees at the time reportedly did own such vehicles. This expenditure was made from the Port's State appropriation accounts.

Observation No. 3 - The Port Authority Has Made Numerous Payments For Personal Items And Other Expenditures That Do Not Appear To Have Furthered State And Port Operations (Continued)

Observation (Continued):

4. On July 15, 1999, the Port paid \$212 for a battery and repairs to a 1987 Ford pick-up truck. This truck appears to be the same truck, owned by the prior port director, on which the snowplow was mounted. This expenditure was made from the Port's State appropriation accounts.
5. On July 15, 1999, the Port paid \$80 for a tire. This tire is not on either of the Port's vehicles, nor does it appear to ever have been. This expenditure was made from the Port's State appropriation accounts.
6. On July 19, 1999, the Port paid \$50 for two watches, \$36 for a pair of neoprene shorts, \$82 for a wet suit, \$38 for a shirt, \$13 for shorts, and \$10 for sunscreen. There is no evidence at the Port that these items furthered the operations of the State or Port. This expenditure was made from the Port's State appropriation accounts.
7. During fiscal year 1999, the Port paid \$550 for prepaid car wash coupons. During fiscal year 1998, the Port paid \$780 for prepaid car wash coupons. During most of this period, the Port owned two vehicles and leased a third vehicle. These expenditures were paid from the Port's State appropriation accounts.
8. On January 10, 1998, the Port paid \$354 for six Portsmouth afghan blankets. There is no evidence at the Port that these items furthered the operation of the State or Port. This expenditure was paid from the Port's State appropriation accounts.
9. During July 1999, the Port paid \$800 for a lawnmower, string trimmer, brush trimmer, leaf blower, and other yard maintenance products. This expenditure was paid from the Port's State appropriation accounts. Based on discussions with a Port employee, this equipment may not have consistently remained on-site at the Port. It is unclear that the purchase of this equipment could be considered an efficient and effective use of Port resources as there is only minimal lawn/plantings at the Port and the contracted port terminal operator was responsible for maintenance of the Port grounds.
10. During the first six months of fiscal year 2000, the Port paid \$1,100 for clothing at an embroidery and printware store and \$1,800 for clothing and accessories at a uniform store.
 - Included in a September 7, 1999 purchase at the printwear store were two Blass polo shirts at \$30 each, two windshirts with logo at \$45 each, and eight other shirts with logos costing \$28 to \$30 each. Included in an October 1999 purchase at the printware store were eleven Berber fleece vests at \$42 each, one windshirt at \$42, one jacket at \$65, and three fleece articles at \$40 each.

Observation No. 3 - The Port Authority Has Made Numerous Payments For Personal Items And Other Expenditures That Do Not Appear To Have Furthered State And Port Operations (Continued)

Observation (Continued):

- Included in an October 1999 purchase at the uniform store was a \$125 flashlight (which is not at the Port), two belts at \$16 each, two jackets at \$60 each, a \$44 shirt, and two \$35 pairs of pants. Included in December 1999 purchases at the uniform store were two pair of foul-weather pants at \$55 each, four jackets at \$69 each, six insulated bib coveralls at \$58 each, three shirts at \$12 each, one belt at \$16, and one pair of boots at \$75.

During fiscal year 1999, the Port expended \$3,300 for clothing, footwear, and accessories. During fiscal year 1998, the Port expended \$7,700 for these purposes.

These expenditures were made from the Port's State appropriation accounts. Per discussions with members of the Port Authority Board, employees were not authorized to purchase clothing or uniforms with Port funds.

Recommendation:

The Port needs to contact and work with the Department of Justice to determine whether these questionable Port expenditures indicate fraudulent activity on the part of current or former Port employees.

As noted in other observations and recommendations, the Port must immediately establish controls over its operations. Port management must establish a control environment in the Port organization and communicate to employees through both policies and procedures and example that controls are important to achieving the Port's goals and objectives. Management must lead by example creating a "tone at the top" that sets the standard for the organization. Controls should not be regarded as "red tape" that can be "cut through" as needed to "get the job done."

Port Authority Response:

We concur. At the recommendation of the Office of the Legislative Budget Assistant, the present administration has contacted the Department of Justice to determine whether these questionable Port expenditures indicate fraudulent activity on the part of current or former Port employees. Furthermore, the current administration has established policies and procedures on expenditures to insure that all expenditures are utilized for the goals and objectives of the Port Authority (refer to response to Observation No. 2).

The following response is from the Interim Director based on personal knowledge or from interviews with Port employees.

Observation No. 3 - The Port Authority Has Made Numerous Payments For Personal Items And Other Expenditures That Do Not Appear To Have Furthered State And Port Operations (Continued)

Port Authority Response (Continued):

1. The Chief Harbor Master reported that the prior Director purchased the snowplow in anticipation of an early departure of the terminal operator. By contract, the terminal operator was responsible for snow plowing. The plow was placed on the prior Director's personal vehicle to "save wear and tear on the Port's truck."
2. Same as above.
3. The Chief Harbor Master reported that this purchase was an attempt to install a sunscreen on a patrol boat. The unused item is at the Port office.
4. Current Port employees have no knowledge of this purchase.
5. Current Port employees have no knowledge of this purchase.
6. Current Port employees have no knowledge of this purchase. Inspection of the sales receipts show that the receipts were signed by the prior Port Director.
7. The Chief Harbor Master reported that the car wash coupons were for Port vehicles and were authorized by the prior Port Director.
8. The Interim Director believes that the previous Director bought these blankets to exchange as gifts while on trade missions.
9. The HMS BOUNTY visited the Port in July. At that time the Port staff cleared the weeds along the bank and parking lot using the referenced equipment. The Interim Director (then operations manager) was not aware that the equipment was the property of the Port. It was his impression that the items in question were the property of the director. Previously, the Interim Director had stated that he had never seen the equipment. However, if this equipment was purchased in the middle of July 1999, the Interim Director (operations manager) was subject to a lay-off from August 15, 1999 until the middle of November and may not have seen the equipment. Other employees report that the equipment consistently remained at the Port.
10. The Interim Director has no knowledge of items purchased between August 1, 1999 and November 15, 1999 as that was the period of his (operations manager) lay-off. During the Interim Director's/Operations Manager's employment, since 1995, he personally received approximately; 4 sport shirts with the Port authority logo, 2 sweat shirts with the Port Authority logo, 1 fleece pull-over and 1 fleece vest with the Port Authority logo, 1 windbreaker with Port Authority logo, 2 neck ties with Port Authority logo, 1 duffel bag with the Port Authority logo, and various ball caps and t-shirts with the Port Authority logo. During this same period the Interim Director/Operations Manager personally purchased with his own funds, 6 sport shirts (\$24.00 each) and 1 jacket (\$85.00) with the Port Authority logo. All work clothing including foul weather gear, boots and steel toe boots, were personally purchased. The Interim Director has requested and received personal inventory reports from Port employees.

While attending the Seatrade Cruise Ship Convention, the Port Authority booth was equipped with canvas bags, hats, coffee cups and t-shirts with the Port Authority logo. These were promotional items for cruise ship executives.

Observation No. 3 - The Port Authority Has Made Numerous Payments For Personal Items And Other Expenditures That Do Not Appear To Have Furthered State And Port Operations (Continued)

Port Authority Response (Continued):

The present administration has not allowed any purchases at the uniform, embroidery or the boot stores. A policy for personnel uniforms is being developed.

As will be repeated throughout the audit responses, the present administration has initiated procedures and has maintained compliance with state spending and purchasing procedures. Purchasing and inventory controls have been placed in effect. An inventory was initiated by the present administration, however, not all of the articles mentioned in the observation appear on the inventory.

Observation No. 4 - The Port Authority Has Failed To Maintain Adequate Accounting Records For Its Marketing Trust Fund

Observation:

There is a dearth of financial records available at the Port Authority (Port) to support whether the activity reported in the Marketing Trust Fund was in compliance with Port management's directions and assertions.

The Port operates the Marketing Trust Fund, an "off-State-books" trust fund, to promote activities at the Port's terminal. Through provisions in the Port Authority's contract with the port terminal operator (contract effective through July 2000), the port terminal operator provides a \$50,000 annual payment to the Marketing Fund.

The Port does not maintain or have a check register, financial statements, periodic accounting or reporting, account reconciliations, or other accounting records of the financial activity occurring in the Port's Marketing Trust Fund. The only records for the Fund available at the Port were bank statements, a very limited number of receipts and paid checks, and a spreadsheet prepared by a contractor that listed and broadly categorized payments from and deposits to the Fund. The spreadsheet was prepared during fiscal year 2000 and covered the period August 1997 through the current period. The bank statements and limited other documentation at the Port apparently were used as the source for this spreadsheet.

Port management is responsible for establishing controls (policies and procedures) to provide reasonable assurance that management's objectives are achieved. Controls must be maintained to provide evidence that existing documents, records, and processing steps in the financial reporting information system are sufficient to ensure that the Port's financial activity is accurately and completely reported in the financial statements of the Port. In addition, N.H. Admin. Rules, Adm 311.03 (a) (1) (expired) [State Manual of Procedures] states that "A complete record of other than state funds which are the responsibility of state officials serving in their official capacity shall be maintained."

Observation No. 4 - The Port Authority Has Failed To Maintain Adequate Accounting Records For Its Marketing Trust Fund (Continued)

Observation (Continued):

Port management's apparent lack of control awareness related to the operations of the Marketing Trust Fund allowed the following conditions to occur.

- During the two-year period of fiscal years 1998 and 1999, the prior port director was paid \$39,000 from the Marketing Trust Fund - ostensibly as reimbursements for travel and meals. There are only \$5,600 of receipts on file at the Port to document the reimbursement payments made to the prior director during this period. Documents included in the files include reimbursement for one leg of one trip at first-class airfare. Another receipt was for a \$725 meal for a group of people at a Portsmouth restaurant, including a \$100 bar tab. Other receipts raise a question of whether some travel expenses were reimbursed twice, once from the Marketing Fund and once from the Port's State appropriation accounts.

There is insufficient documentation at the Port to determine that the reimbursement payments made to the prior port director furthered the purpose of the Marketing Trust Fund and that these expenditures would be properly classified as Marketing Fund expenditures.

- During the two-year period of fiscal years 1998 and 1999, the Port leased a 1997 Ford Expedition sports utility vehicle (SUV) at a total cost of \$13,000. The cost of the lease, registration, and vehicle insurance was paid from the Marketing Trust Fund. According to the prior chairman of the Port Authority Board (Board), the vehicle was leased to transport visitors at the Port, the vehicle was not to be used for private purposes, and the vehicle was to remain at the Port after business hours. The chief harbor master and the Port's business manager were aware that the vehicle was leased by the Port. Other Port employees and the current chairman of the Board and the Commissioner of the Department of Resources and Economic Development, who is also a Board member, reported that they were unaware that the Port had leased the vehicle.

Current Port employees reported that they assumed the vehicle was a personal vehicle as the prior port director used the vehicle as such. There is no documentation at the Port to determine that the purchase of this lease furthered the purpose of the Marketing Trust Fund and that this expenditure would be properly classified as a Marketing Trust Fund expenditure.

- On July 12, 1999, the Port purchased a snowplow and had the snowplow mounted on the prior port director's personal pick-up truck. The \$3,400 cost of the snowplow was paid from the Marketing Trust Fund. The Port had no apparent need for a snowplow as a contractor hired by the port terminal operator plows the Port property. There is also no possible reason why a snowplow purchased with State funds should be mounted on an employee's personal vehicle.

Observation No. 4 - The Port Authority Has Failed To Maintain Adequate Accounting Records For Its Marketing Trust Fund (Continued)

Observation (Continued):

[The snowplow has since been taken off the prior port director's truck, mounted on the Port's State truck, removed from the Port's State truck, and given back to the vendor with no surplus value received by the Port.]

There is no documentation at the Port to determine that the purchase of this snowplow furthered the purpose of the Marketing Trust Fund and that this expenditure would be properly classified as a Marketing Fund expenditure.

The prior chairman of the Board indicated that, as a second signer on the Marketing Trust Fund, he had access to documentation supporting checks that he co-signed. It is unclear why this supporting documentation has not been maintained on file at the Port.

Recommendation:

The Board must reestablish its authority over Port operations. The Board must become more aware of and involved in the administrative operations of the Port including the operations of the Port's Marketing Trust Fund.

The Board should establish appropriate controls (policies and procedures) to account for the Marketing Trust Fund. Sufficient documentation should be maintained to evidence that the operations of the Fund are in compliance with the Boards' directions and assertions. Control processes including the preparation of periodic financial statements and reporting of financial activity to the Board would assist in ensuring that the Board is aware of the uses of the Fund. Documentation supporting all Fund transactions should be maintained in the accounting records of the Port.

While having transferred the custody of the Fund to the State's accounting system was a first step in gaining control over the Fund, the Board also needs to review and consider what are the proper uses of the Fund. Guidelines should be established to ensure that the Board's intent is communicated to the Port employees and that the use of the Fund is monitored for compliance with those guidelines.

Port Authority Response:

We concur. The present administration has no personal knowledge of how the account was handled as this was strictly controlled by the previous director. At a meeting on August 29, 2000 the prior Chairman of the Board indicated that as the second signer on the Marketing Trust Fund checks he had access to all invoices supporting checks that he signed. It is unknown why this supporting documentation has not been maintained on file at the Port. The present Chairman has requested the previous director to provide supporting documentation for reimbursements paid to the previous Director's VISA account.

Observation No. 4 - The Port Authority Has Failed To Maintain Adequate Accounting Records For Its Marketing Trust Fund (Continued)

Port Authority Response (Continued):

Furthermore, the Marketing Fund has been transferred into the State system and closed out at the bank and the Department of Administrative Services has been requested to reconcile the account.

The Board had previously established a policy regarding the use of the fund. This policy was re-stated at the October 4, 2000 Board meeting. The fund will be used exclusively for advertising and promotion of the Port and expenditures will be in compliance with the Port's by-laws and State rules and procedures. Accurate accounting will be reported in the detail register.

Observation No. 5 - The Port Authority Has Not Established Adequate Segregation Of Duties Over The Processing Of Expenditures From The Port Authority's Marketing Trust Fund

Observation:

The Port Authority (Port) management's apparent lack of control awareness of expenditures from its Marketing Trust Fund (Fund) allowed the financial activity in the Fund to be ineffectively controlled. This lack of controls promoted an environment where there was a significant potential for errors or frauds in Fund expenditure processing to go undetected.

During the period 1997 until the end of calendar year 1999, there was a near complete lack of segregation of duties over the Fund. According to current Port employees, the prior port director controlled all aspects of the Fund with the exception that the prior chairman of the Board was a second signer on all checks drawn on the Fund.

There were no mitigating or countervailing controls in operation to offset the significant risk of undetected errors or frauds that may occur as a result of the lack of segregation of duties over the expenditures in the Fund.

Port management is responsible for establishing controls (policies and procedures) to provide reasonable assurance that its objectives are achieved. Segregation of duties is a primary control activity used to detect errors or frauds that may occur. The fundamental purpose of properly segregating duties is to protect the integrity of the accounting and administrative systems by ensuring that no one employee is in a position to both commit, either intentionally or unintentionally, errors or frauds and is also responsible for the detection of those errors or frauds. Management did not meet this responsibility.

Observation No. 5 - The Port Authority Has Not Established Adequate Segregation Of Duties Over The Processing Of Expenditures From The Port Authority's Marketing Trust Fund (Continued)

Recommendation:

Port management should establish controls over the Marketing Trust Fund. Where possible, duties should be sufficiently segregated to provide reasonable assurance that errors or frauds occurring would be detected and corrected in the normal course of business and in a timely manner. If the Port determines that sufficient suitably trained employees are not available in its business office to provide for adequate segregation of duties, the Port should implement appropriate mitigating controls that could include the Board's review of supporting transaction reports and other documentation reporting expenditure activity.

Port Authority Response:

We concur. The Marketing Fund has been placed into the State accounting system thereby producing the layering effect. Expenditures are made according to Port policy and the revised by-laws of October 4, 2000. Additionally the Department of Administrative Services rules and State purchasing procedures are to be followed. All expenditures are pre-approved by the Director, within the guidelines, and reported on a monthly basis to the board (see response No. 2).

Observation No. 6 - The Port Authority Has Not Monitored And Enforced Its Contract Agreements With Regards To Revenues Paid To The Port

Observation:

The Port Authority (Port) has been ineffective in monitoring and enforcing the revenue and reporting conditions of the contract agreements with its port terminal operator and its lessee of property at the Port.

The Port is responsible for monitoring and enforcing its contract agreements including ensuring that it receives all revenues and associated reporting due in the proper accounting periods. The Port has been ineffective in this monitoring and enforcement effort as described in the following points because the responsibility for monitoring contract compliance was not established by the Port.

- The Port's contracted terminal operator has:
 1. not made dockage and wharfage payments to the Port since December 1998,
 2. not adhered to the contract provisions requiring the filing of tariff statements,
 3. waived/discounted dockage and wharfage fees without submitting the change in fee structure to the Port. (There is no provision in the contract for the waiving/discounting of fees),

Observation No. 6 - The Port Authority Has Not Monitored And Enforced Its Contract Agreements With Regards To Revenues Paid To The Port (Continued)

Observation (Continued):

4. not met activity reporting requirements of the contract making it impossible for the Port to determine the amounts of dockage and wharfage that are due the Port,
 5. not adhered to the contract provisions for the schedule of recovering costs for capital improvements, and
 6. been allowed to establish contracts for temporary storage at the Port (agreements with the U.S. Coast Guard and a local car dealership) even though it may have been more appropriate for the storage contracts to be with the Port. (Contracts were not stevedore related but were simply for storage.)
- The lessee of property at the Port has not adhered to contract provisions requiring monthly lease payments. Payments have been rescheduled without the Port Board's agreement to the change. Also, there has been no reconciliation of amounts due on the contracts. Delays in the collection of revenues increases the risk of failure of ultimate collection as well as negatively impacts the State's cash flow. At the July 14, 2000 end of fieldwork date, we found that the Port was unaware the lessee owed the Port approximately \$7,000 from prior contract years.

Recommendation:

The Port has to take responsibility for monitoring and enforcing compliance with its contracts. Lessees and other contracted parties must be required to adhere to contract provisions including payments of revenues and reporting activity. Lessees and other contracted parties must not be allowed to unilaterally change contract provisions. All changes to contract provisions should be approved in writing by all signatories to the contract.

The Port should fully understand all provisions of its contracts. The Port should ensure that it is proactive in its relationship with its lessees and other contracted parties and not simply reactionary.

Port Authority Response:

We concur. The present administration has developed a system of accounts receivable, which will assure oversight of revenues. Revenues due and revenues collected are reported to the Board at the regular meeting.

The present administration will make every attempt to assure timely collection of revenues.

Observation No. 7 - The Port Authority Has Allowed Inappropriate Unrecorded Transactions To Occur

Observation:

The Port Authority (Port) has entered into exchange transactions which are neither documented nor recorded in the Port's and State's accounting records. Unrecorded exchange transactions are inappropriate as they have a significant risk for fraud and abuse.

1. The Port has allowed current and prior Port employees no-fee mooring permits even though N.H. Admin Rules, Por 301.04 states that "(a) All vessels moored in New Hampshire tidal waters shall be assessed an annual fee...."
 - The prior port director was allowed a no-fee mooring permit during the period he served as port director and during the period he served as chief harbor master.
 - Three current part-time harbor masters are allowed no-fee mooring permits for their personal boats. According to the Port, these harbor masters have elected to use their personal boats while performing their harbor master duties.
 - A prior part-time harbor master is currently allowed a no-fee mooring permit. According to the Port, this no-fee permit is allowed because the individual occasionally performs diving services for the Port. (There is no documentation at the Port supporting that these services have been recently performed.)

The Port also allows other State organizations no-fee mooring permits. (The Department of Fish and Game is issued one no-fee mooring permit and the University of New Hampshire is issued eight no-fee mooring permits.)

The policy of allowing no-fee mooring permits was reportedly established/expanded by the prior port director/chief harbor master. This policy is not in compliance with current administrative rules and there is no evidence that the Port Board ratified the policy.

2. Port employees reportedly have been encouraged to charge gas on the Port's account at a local gas station instead of filing for mileage reimbursement for the use of personal vehicles. This policy is contrary to State procedures for use of personal vehicles and has a significant potential for fraud and abuse.
3. During fiscal year 1998, the Port paid \$1,200 toward the slip rental cost for a part-time harbor master's personal boat, ostensibly as the boat was used by the part-time harbor master on Port-related business.

Observation No. 7 - The Port Authority Has Allowed Inappropriate Unrecorded Transactions To Occur (Continued)

Recommendation:

All Port transactions should be accurately and completely recorded in the Port's accounting system. Unrecorded transactions should not be allowed to occur.

All revenues due the Port should be collected. If the Port determines that it is appropriate to waive fees, the Port's administrative rules should be revised to allow the Port that option.

All State policies regarding reimbursements for personal vehicle use should be adhered to. Gasoline and other supplies should only be used in and for Port-owned vehicles.

The Port should not pay costs related to the use of personal vehicles or boats except as allowed by State policies and procedures.

Port Authority Response:

We concur based on the observation. The previous administration set the practices that were observed. The present administration will operate in compliance with all laws and rules and regulations. Furthermore the Port has investigated the issues reported and made the following corrections.

- A policy will be developed regarding non-revenue moorings,
- No gasoline purchases are being made for personal vehicles or vessels, and
- No slip fees are being paid for personal vessels.

Observation No. 8 - The Port Authority Has Not Established Effective Controls Over Its Revenue Collection

Observation:

The Port Authority (Port) has not established controls (policies and procedures) to ensure that all revenue due the Port is collected and deposited into the Port's accounts.

- As noted in Observation No. 6, the Port is essentially reactive in its collection of revenue. The Port has not established controls to anticipate the collection of revenue or pursue revenue that is not paid to the Port in a timely manner. In addition to the examples in Observation No.6, the Port also allowed a \$2.1 million accounts receivable from the federal government to remain uncollected for approximately three years, apparently due to the Port not filing the necessary paperwork to close out the project.

Observation No. 8 - The Port Authority Has Not Established Effective Controls Over Its Revenue Collection (Continued)

Observation (Continued):

- Due to the limited number of Port employees involved in the revenue process (2), each employee is able to process revenue singly in the event of the other employee's absence. There are no mitigating or countervailing controls in place at the Port to offset the risk of undetected errors or frauds that may occur as a result of this lack of segregation of duties over revenue processing. The fundamental purpose of properly segregating duties is to protect the integrity of the accounting and administrative systems by ensuring that no one employee is in a position to both commit, either intentionally or unintentionally, errors or frauds and also is responsible for the detection of those errors or frauds.

Port management is responsible for establishing controls (policies and procedures) to provide reasonable assurance that management's objectives are achieved. Management has not met that responsibility for Port revenues.

Recommendation:

The Port must establish controls over the collection of its revenues.

- The Port should become more proactive in its revenue collection process. The Port should understand the nature and schedule of the revenue that it collects and establish a process to ensure that the Port's revenue is collected completely and in a timely manner.
- Port management, where possible, should sufficiently segregate the revenue collection responsibilities of its employees to provide reasonable assurance that errors or frauds occurring in revenue processing would be detected and corrected in a timely manner and in the normal course of business. If the Port determines that there are not sufficient suitably trained employees available in its business office to provide for adequate segregation of duties, the Port should implement appropriate mitigating controls which could include management's review of supporting transaction reports and other documentation reporting revenue activity.

Port Authority Response:

We concur. The previous administration set the practices that were observed. As stated in our response to observation No. 6, a system of accounts receivable has been implemented, to ensure the timely collection of revenues. The present administration has initiated a segregated system for the collection and processing of revenues in the Port office. Included in this process, a listing of revenues is presented to the Board at the regular meeting for their review.

Observation No. 9 - The Port Authority Has Not Implemented State-Established And Appropriate Policies And Procedures To Safeguard State Equipment Assets

Observation:

The Port Authority (Port) management's apparent lack of control awareness of equipment issues has resulted in the Port not being certain that it has properly accounted for all of its equipment.

Port management is responsible for establishing and implementing controls (policies and procedures) for its equipment assets and for adhering to the State's equipment controls to provide reasonable assurance that management's objectives are achieved. The State's established controls include comprehensive inventories and periodic reporting of all equipment items costing \$100 or more and having an expected useful life of greater than one year.

The Port has not established equipment controls nor implemented State equipment controls. There is no comprehensive inventory (listing) of Port-owned equipment. Such a listing should include item control number, document reference number, cost, acquisition date, location, and equipment description. The Port has not tagged or specifically identified Port equipment items as State-owned. The Port has not submitted required monthly reporting of changes in equipment balances, or the required annual reporting of comprehensive inventory.

Examples of problems with the controls over the Port's equipment include the following.

- There is no way to determine what State equipment the Port is accountable for. For example, there are a number of boat motors in storage at the Port. At the time of inquiry there reportedly was also a boat motor at a repair shop. There are also a number of recently purchased motors attached to Port boats. However, there is no documentation available to establish the ownership of the motors and to determine that these are all of the boat motors the Port owns.
- Equipment purchased by the Port is known to be missing (for example a \$125 flashlight purchased in October 1999 and a \$140 tarp purchased in November 1999 are not at the Port).
- Port equipment has been loaned to local jurisdictions without appropriate approvals and documentation. One small Port boat with a new Port motor is painted as if it was the Town of Newfields' boat. Another small Port boat reportedly has been loaned to the Town of Exeter. (The current interim port director does not know whether this boat has a Port motor.)

Observation No. 9 - The Port Authority Has Not Implemented State-Established And Appropriate Policies And Procedures To Safeguard State Equipment Assets (Continued)

Recommendation:

The Port should immediately implement State policies and procedures (controls) over its equipment inventory. A complete physical inventory of equipment should be taken. All items of equipment should be specifically identified, tagged, and described on a comprehensive inventory listing. Original costs for the equipment items should be determined and included on the inventory list. Research should be performed to ensure that all Port equipment is accounted for. The results of the inventory should be reported to the Department of Administrative Services and should be updated monthly as changes in the equipment inventory occur. The inventory should be used by the Port to track and control the whereabouts and ownership of its equipment.

The Port may also want to establish additional controls specific to the operations of the Port.

Port Authority Response:

We concur. The present administration has initiated an inventory. Due to the lack of controls by the previous administration, a concise and accurate inventory is not obtainable at this time. However, to the best possible means, an inventory has been taken, assets have been labeled and registration numbers recorded. All purchases from that time forward will be inventoried and labeled. The monthly inventory report (P21) and the year ending inventory report (P16) for the fiscal year, have been/will be submitted in accordance with filing dates.

Observation No. 10 - The Port Authority Has Not Adequately Documented Payroll Expenditures For Part-Time Employees And Overtime Expenditures For Full-Time Employees

Observation:

The Port Authority (Port) management's apparent lack of control awareness of payroll issues has resulted in the situation where the propriety of part-time employee payroll and overtime payroll for full-time employees cannot be determined.

All financial transactions, including payroll expenditures, should be adequately documented to support that the purpose, amount, and propriety of the transactions are in compliance with management's assertions. However, payroll expenditures for part-time Port employees and overtime expenditures for full-time Port employees are not adequately documented.

Observation No. 10 - The Port Authority Has Not Adequately Documented Payroll Expenditures For Part-Time Employees And Overtime Expenditures For Full-Time Employees (Continued)

Observation (Continued):

- There is no activity reporting or timesheets for part-time harbor masters. Part-time harbor masters generally are paid for working 20 hours per week without regard to actual hours worked. According to the chief harbor master, “harbor masters are on the honor system” and generally work greater than 20 hours per week during the boating season and less than 20 hours per week in the off-season averaging 20 hours per week. As a result, the actual amounts paid the part-time harbor masters for a given payperiod do not necessarily reflect the actual hours worked by these employees during the relevant payperiod. The chief harbor master reports he is generally not aware when part-time harbor masters are working.

The work activities of the part-time harbor masters are also not documented. As well as not recording when the part-time harbor masters were working, there were no records maintained of what tasks the part-time harbor masters worked on. The lack of activity reporting by the part-time harbor masters hinders effective management review of their activities.

- Two Port employees accrued significant amounts of overtime in a regular pattern, often claiming the same amount of overtime hours each pay period. There was no documentation to support the necessity/propriety of the overtime paid to these employees. There were no activity reports or timesheets supporting the time worked. When asked, the employees could not provide reasonable descriptions of the activities requiring the overtime hours.

The necessity/propriety of the overtime payments cannot be established because there is no documentation available to determine the activities performed during these periods.

Recommendation:

The Port should immediately establish controls (policies and procedures) for part-time and overtime payroll. All part-time employees should submit activity reports/timesheets documenting hours worked. To be most useful, these reports should also indicate tasks worked on. All activity reports/timesheets should be reviewed and approved by an authorizing individual. Part-time employees should only be paid for the actual hours worked during the payroll reporting period.

All overtime for full-time employees should be approved in advance by an authorizing individual. All overtime should be supported by activity reports/timesheets.

Observation No. 10 - The Port Authority Has Not Adequately Documented Payroll Expenditures For Part-Time Employees And Overtime Expenditures For Full-Time Employees (Continued)

Recommendation (Continued):

The Port should consider requiring all full-time employees to submit regular activity reports/timesheets to support hours worked and to provide Port management with regular information on employee activities, workloads, etc.

Port Authority Response:

We concur. The present administration has initiated the use of time cards for the documentation of hours worked. Additionally, all overtime must be pre-approved except in the case of an emergency, and activity reports are required for overtime. Activity reports are also required by all part-time employees.

Observation No. 11 - The Port Authority Apparently Took Steps To Circumvent State Purchasing Rules In Order To Make Purchases Outside Of The State's Purchasing Control System

Observation:

The Port Authority (Port) apparently deliberately avoided State purchasing controls for some purchases.

Management's stewardship of assets is subject to numerous restrictions established by policy, regulation, law, or contract. It is not enough for management to demonstrate compliance with such restrictions after the fact. Rather management is responsible for establishing controls to ensure compliance with such requirements.

The following are examples where the Port appears to have intentionally avoided State purchasing controls. Port management's apparent lack of control awareness over expenditures may have contributed to the Port's improper and inefficient purchasing activities avoiding detection by the State's control processes.

1. State purchasing controls provide that personal service contracts in excess of \$2,500 require Governor and Council approval.
 - During fiscal year 1999, the Port entered into a \$7,200 personal service contract with a Port employee's spouse for the development of a computer database to track boat moorings. Five separate payments of \$1,440 were made on the contract totaling the \$7,200 contract amount. According to a Port employee, the payments were split by the Port to circumvent the \$2,500 State contract limit.

Observation No. 11 - The Port Authority Apparently Took Steps To Circumvent State Purchasing Rules In Order To Make Purchases Outside Of The State's Purchasing Control System (Continued)

Observation (Continued):

2. State purchasing controls provide that field purchase orders may be used for purchases of less than \$500. Purchases of greater than \$500 require purchase orders to be prepared in advance and submitted to the Department of Administrative Services' Bureau of Purchase and Property for State purchasing procedures, including selection of the most cost-effective vendors and other State purchasing controls. Agencies are not to split purchases of greater than \$500 over multiple field purchase orders.
 - The Port purchased \$620 of clothing on December 10, 1999 using two field purchase orders – one totaling \$345 and the other totaling \$275. Splitting the purchase over two field purchase orders allowed the Port to buy the clothing without subjecting the transaction to State purchasing controls.

Recommendation:

All Port expenditures should be subject to the State's control process. The Port should not circumvent the State's control processes for any reason.

Port Authority Response:

We concur. The present administration has no knowledge of these past practices, however the present administration is following the spending guidelines of the Port Authority's by-laws and all State purchasing and personal services requirements.

It is reported by the Port employee whose spouse developed the data base (a new employee at the time) that the prior Director had expressed a desire for a new system and when told that the spouse could develop that system, the prior Director hired the spouse and asked for incremental billing.

Observation No. 12 - The Port Authority Has Not Adequately Controlled The RLF Loan Program Bank Account

Observation:

The financial activity in the Port Authority's (Port) account at the bank administering the Port's Revolving Loan Fund (RLF) loan program has not been subject to appropriate review and control by the Port. (See page 36 for a description of the RLF program.)

The bank administering the RLF loan program has established a bank account in the Port's name to temporarily hold loan funds. This account has not been submitted for approval by the Governor and Council, the prior port director is still listed on the account,

Observation No. 12 - The Port Authority Has Not Adequately Controlled The RLF Loan Program Bank Account (Continued)

Observation (Continued):

the Port has not consistently received periodic statements for review of the activity in the account, and there is no documentation indicating whether the Port has ever performed a reconciliation of the activity in the account.

N.H. Admin. Rules, Adm 311.03 (a) (2) (expired) [State Manual of Procedures] requires that when other than State funds are held in accounts not under the control of the State Treasurer, the Governor and Council shall approve the bank of deposit.

Good business practice requires that bank account documentation is kept current and that activity statements are obtained, reviewed, and reconciled for accuracy to ensure that all activity in the account reported by the bank has been properly authorized by management.

The Port's lack of a proper review of the activity in this account apparently was due to the Port management's lack of awareness of State controls (policies and procedures) and general good business practices.

Recommendation:

The Port should immediately take steps to more closely review the financial activity in the RLF loan program bank account. Controls should be established to ensure that the account documentation remains current, including the names and signatures of authorizing individuals at the Port and that the activity in the account is properly, timely, and consistently reported to the Port. The Port should periodically reconcile the account to ensure that all activity in the account is accurate and authorized. The Port should also submit the account to the Governor and Council for approval as required by the State Manual of Procedures.

Port Authority Response:

We concur. The present administration had no knowledge of the account. The present administration has closed the account and transferred the funds to the state system. Reconciliation of that account by Administrative Services has been requested.

State Compliance Comments

Observation No. 13 - The Port Authority's Revolving Loan Fund Board Has Not Been Properly Established Or Created

Observation:

The Port Authority (Port) has created the Revolving Loan Fund (RLF) Board as an advisory-type board without having the RLF Board established by law or submitting the creation of the RLF Board to the Governor for approval under the provisions of RSA 21-G:11. The failure to properly create the RLF Board was apparently due to the Port's lack of awareness of State policies and procedures. (See page 36 for a description of the RLF program.)

The Port created the RLF Board to assist in administering the RLF program. Generally, boards must be established by law, however RSA 21-G:11, I allows the head of an executive branch department to create advisory committees with the approval of the Governor. RSA 21-G:11, II provides that the department must report the committee to the Secretary of State and RSA 21-G:11, III provides that the Governor shall appoint the members of each advisory committee.

Because the Port RLF Board was not properly established or created, the RLF Board may not have proper legal standing and therefore actions taken by the RLF Board may be subject to dispute.

Recommendation:

The Port should review its operations to determine the necessity for the continuation of its RLF Board. If it determines that the RLF Board continues to serve an important function, the Port should request that the RLF Board be established by statute or created by RSA 21-G:11. If the Port Authority selects the RSA 21-G:11 process, it should be aware that RSA 21-G:11, VII provides only a three-year life for committees created by this section after July 1, 1995.

Port Authority Response:

We concur. The Revolving Loan Fund Board has been dissolved and the need for an advisory group will be reviewed.

Observation No. 14 - The Port Authority Has Not Submitted Required Annual Trust Fund Financial Statements

Observation:

The Port Authority (Port) historically has not reported the financial activity in its Marketing Trust Fund to the Department of Administrative Services for review and inclusion in the State's annual financial report. As a result, the Department of Administrative Services has not been provided an opportunity to review the annual activity in the Marketing Trust Fund and the financial activity in the Marketing Trust Fund has not been included in the State's annual financial report.

Reporting of trust funds held by State officials is required by N.H. Admin. Rules, Adm 311.03 (a) (4) (expired) [State Manual of Procedures] which states that "A yearly submission of a detailed operating statement of each [trust] fund shall be submitted not later than September 1."

The Port's apparent lack of awareness of State policies and procedures apparently led to the Port not being in compliance with this administrative rule.

Recommendation:

The Port should comply with the above-cited administrative rule and submit a detailed operating statement for its Marketing Trust Fund to the Department of Administrative Services for its review and inclusion in the State's annual financial report.

Port Authority Response:

We concur. The funds have been placed into the State appropriation system thereby eliminating the necessity for the report. A reconciliation of the account by Administrative Services has been requested.

Observation No. 15 - The Port Authority Did Not Submit Its Purchase Of A Computer Database Program To DITM For Its Review

Observation:

The Port Authority (Port) purchased a \$7,200 computer database program during fiscal year 1999 without first submitting the purchase to the State's Division of Information Technology Management (DITM) for review and approval. Per RSA 21-I:11, XI, data processing hardware, software, etc., costing \$5,000 or more must be submitted to DITM for approval, prior to purchase, to ensure the purchase meets the State's information technology standards.

The Port's purchase of this mooring database program was not submitted to DITM for review apparently due to the Port's lack of control awareness of State policies and procedures.

Observation No. 15 - The Port Authority Did Not Submit Its Purchase Of A Computer Database Program To DITM For Its Review (Continued)

Recommendation:

The Port should submit all data processing purchases that meet the statute's guidelines to DITM, as required by the above-cited statute.

Port Authority Response:

We concur. The present administration is aware of the DITM and will follow all guidelines.

Observation No. 16 - The Port Authority Has Not Requested Governor And Council Approval To Accept The Gift Of A Boat

Observation:

The Port Authority (Port) has accepted and is using a boat donated by the prior port director without submitting the gift of the boat to Governor and Council for their acceptance.

According to RSA 4:8, all gifts or other expenditures by third parties in support of State operation, unless otherwise authorized by statute, should be placed before the Governor for acceptance. Generally, the authority to accept gifts on behalf of the State pursuant to RSA 4:8 has been delegated by the Governor to the Governor and Executive Council.

The Port apparently was unaware of the requirement and accepted the gift of the boat on behalf of the State without authority to do so.

Recommendation:

The Port should submit a request to Governor and Council to accept the gift of the boat and to allow the Port to use the boat in its operations.

Port Authority Response:

We concur. The present administration has returned the boat to the original owner. Future gifts will require Governor and Council approval.

Observation No. 17 - The Port Authority Has Not Filed Capital Budget Status Reports

Observation:

The Port Authority (Port) historically has not submitted the capital budget status reports that are required by RSA 17-J:4.

RSA 17-J:4 requires each State agency with capital budget projects to submit a status report every 60 days to the Capital Budget Overview Committee.

The reports apparently were not submitted due to the Port's lack of awareness of State policies and procedures.

Recommendation:

The Port should implement procedures necessary to ensure timely submission of capital budget project status reports in accordance with RSA 17-J:4.

Port Authority Response:

We concur. The present administration is aware of the required report, (which was filed October 31, 2000) and will comply.

Observation No. 18 - The Port Authority Has Not Consistently Filed Annual Dredging Projects Status Reports

Observation:

According to Port Authority (Port) personnel, no annual dredging reports have been submitted since the fiscal year 1998 report was filed.

RSA 271-A:20, IV requires the Port to submit an annual report to the Senate President, the Speaker of the House, and the Governor on the status of current dredging projects and the projection of future dredging projects and costs.

The fiscal year 1999 report was not submitted and as of July 14, 2000 the fiscal year 2000 report has not been prepared, apparently due to the Port's lack of awareness of the statute's requirements.

Recommendation:

The Port should implement procedures necessary to ensure timely submission of the annual dredging projects status report required by RSA 271-A:20, IV.

Observation No. 18 - The Port Authority Has Not Consistently Filed Annual Dredging Projects Status Reports (Continued)

Port Authority Response:

We concur. RSA 271-A:8, sets the duties of the Chief Harbor Master which shall include but not be limited to “Overseeing the dredge management program”. The present administration has required the Chief Harbor Master file the annual dredge report to the Board for approval for submission.

It should be noted that when Dredge Management duties were delegated to the Port Authority by the Legislature in 1994, associated funding was not included. The Board has consistently directed the past Executive Director to request funding for these efforts in the Ports budget. To date no such funding has been made.

Federal Compliance Comments

The Port Authority (Port) operates the Fishing Industry Loan Program, which is funded from a U.S. Department of Commerce, Economic Development Administration grant (Federal Catalog of Domestic Assistance No. 11.307) with matching funds provided by a local bank.

The purpose of the loan program, commonly referred to as the Revolving Loan Fund (RLF), is to assist the fishing industry in sustaining itself within the new, more restrictive federal fishing regulations and to maintain compliance with the U.S. Coast Guard fishing vessel safety regulations. The program was expanded to refocus traditional fishing activities away from the seriously depleted stocks by encouraging fishermen to seek alternative species, engage in aquaculture, and explore alternative non-fishing employment options through conversion or diversification. The RLF program loans borrowers up to \$100,000. Twenty-five percent of each RLF loan is secured by the local bank, at New York prime plus 2% floating, and the remaining seventy-five percent of each loan is secured with the Port through the RLF at a 5% fixed interest rate. The loan term does not exceed the economic life of the project and cannot exceed 25 years.

Observation No. 19 - The Port Authority Has Issued RLF Loans To RLF Board Members And Other Related Parties

Observation:

The Port Authority (Port) has issued Revolving Loan Fund (RLF) loans to RLF Board members and to parties related to the RLF Board and Port, contrary to the RLF program federal terms and conditions.

Section D.16 of the Department of Commerce, Economic Development Administration (EDA) Standard Terms and Conditions for the Revolving Loan Fund specifies that no Port or RLF Board members or parties related to members of these Boards or Port employees are eligible to receive RLF loans. If any of these ineligible parties receive any benefits resulting from the use or loan of grant funds, as opposed to a direct loan, that benefit must first be disclosed and documented as being inconsequential by the Port. Former Board members and/or officers are ineligible to apply for or receive loans or grant funds for a period of one year from the date of termination of his/her services.

- Seven RLF loans have been made to active RLF Board members or to prior RLF Board members during the one-year exclusion period. Three RLF loans have been made to relatives of Port employees or RLF Board members. There was at least one RLF loan made to an individual who had a business arrangement with an RLF Board member. RLF loans were made to two co-ops. Several RLF Board members were members of these co-ops. Since the inception of the Port's RLF program, approximately \$1.3 million of RLF loans have been issued. At least \$430,000 of those loans have been made to apparently ineligible borrowers.

Observation No. 19 - The Port Authority Has Issued RLF Loans To RLF Board Members And Other Related Parties (Continued)

Observation (Continued):

As recorded in the March 25, 1997 RLF Board minutes, the RLF Board “felt that the R.L.F. Board of Directors should be eligible for loans as long as there was a proper procedure.” Proper procedure generally took the form of the Board member who was not independent of the loan withdrawing from discussions on the merits of the loan and from voting on the approval of the loan.

There is no documentation at the Port indicating that the Port requested or was granted a waiver from the Standard Terms and Conditions prohibiting loans to related parties. In a letter dated May 19, 2000, the interim port director requested clarification from the EDA on the Port’s practices of allowing RLF Board members to be eligible for loans if the subject Board member withdrew from discussing and voting on the loan. In an undated response to this letter, the EDA stated that “According to EDA’s RLF Standard Terms and Conditions, section D.16.(a), Conflict of Interest, loans made to advisory board members would constitute a conflict of interest.”

Recommendation:

The Port should establish controls (policies and procedures) over the issuance of RLF loans to ensure that all loans comply with all EDA terms and conditions, including conflict of interest provisions.

The Port should contact the EDA to determine what action is required with respect to these related-party loans.

In the future, the Port should request formal clarifications of, and waivers from, the EDA terms and conditions prior to taking any actions that may not be in compliance with the program’s terms and conditions.

Port Authority Response:

We concur. Prior to the March 25, 1997 RLF board meeting, the Fishing Program Administrator called EDA to discuss the unique aspects of the New Hampshire commercial fishing industry. The target group of the EDA grant was the Northeast Multi-Species Fishery. Although there are approximately 350 commercial fishermen in New Hampshire, there are approximately only 40 multi-species (groundfish) fishermen. The EDA Revolving Loan Fund Guidelines call for an advisory group made up of industry representatives. To get industry involvement with total exclusion would be impossible. EDA advised the Port to initiate a procedure such as abstention from discussion and voting, to avoid any appearance of a conflict. This is documented in the minutes of the RLF meetings however, a written waiver was not issued by EDA.

The Port has contacted EDA and with the submission of the semi-annual, a copy of this audit report will be included. A review by the EDA compliance division will occur.

Observation No. 19 - The Port Authority Has Issued RLF Loans To RLF Board Members And Other Related Parties (Continued)

Port Authority Response (Continued):

The RLF Advisory Board has been dissolved until this issue is resolved.

Observation No. 20 - The Port Authority Drew Federal Grant Funds Early

Observation:

The Port Authority (Port) requested disbursement of all federal Economic Development Administration (EDA) grant funds prior to utilizing program income.

Section E.05 of the Department of Commerce, EDA Standard Terms and Conditions for the Revolving Loan Fund (RLF) specifies that program income, "...must be used by the Recipient [Port] (1) prior to requesting a disbursement of EDA grant funds, or (2) concurrently with the proceeds of such a disbursement."

The Port did not expend the non-current RLF program income until the EDA grant funds were completely disbursed. Had the program income been used in the proper time frame, the Port may not have met the deadlines for the use of the program funds. Also, because the Port held program income on-hand while it drew down the federal funds, the Port had excess amounts of program funds on deposit.

The Port's failure to properly manage program cash resulted from an apparent misunderstanding on the part of the RLF Board. The RLF Board's incorrect belief that program income could not be used until all of the grant money was spent is documented in the minutes of the RLF Board including the minutes of the November 24, 1998 RLF Board meeting.

Recommendation:

The Port should review its departure from the RLF terms and conditions with the EDA to determine what if any action the EDA requires in response to that departure.

Port Authority Response:

We concur. Although an apparent misunderstanding of the disbursement procedure occurred, the total disbursement of EDA funds and the program income was completed before the 5-year disbursement deadline. Therefore, at the present time it is a non-issue.

Prior to this audit, the Port depended on the US Department of Commerce, Economic Development Administration for review of reports. Based on the fact that the EDA never notified the Port that there might be inconsistencies in the operation of the RLF it was assumed that the RLF operation was consistent with EDA rules.

Observation No. 21 - The Port Authority Does Not Document That The RLF Program Does Not Substitute For Private Sector Financing

Observation:

The Revolving Loan Fund (RLF) files do not contain sufficient evidence to document that the Port Authority's (Port) RLF loans do not substitute for private or public sector financing.

Section 18 of the Department of Commerce, Economic Development Administration (EDA) Standard Terms and Conditions and Additional Terms dated July 28, 1994 for the RLF specifies that "...no loans made through the RLF element of this project will serve as a substitute for private sector or public sector financing available on terms and conditions which would permit the completion and/or the successful operation or accomplishment of the activities to be financed."

Per Section IV. B. 3 of the RLF Grants Administrative Manual dated December 1998, "[t]he grant recipient [Port] is responsible for determining that each borrower meets this requirement [credit otherwise unavailable] and for documenting the basis for its determination in the loan write-up.... The grant recipient is also responsible for obtaining *supplemental evidence*, as appropriate, to support the need for RLF financing. This **may** include the following:

- a. a commitment letter from a participating bank stating the loan terms, the maximum amount to be extended by the bank, and the need for the RLF's participation; and/or
- b. bank rejection letter(s), if obtainable, listing the proposed loan terms."

The Port does not require either of these documents to be on file or otherwise document compliance with this term and condition of the RLF grant. It is not clear or documented that RLF loans are being issued to applicants who would be unable to obtain financing from other sources.

The RLF Board has expressed concern, as recorded in its minutes and in its correspondence with the bank administering the loans and the EDA, that applicants that fit the criteria for the program and need access to funds are turned down due to their inability to secure a matching loan with the bank administering the loans, yet applicants that do not need the RLF assistance to secure loans are approved.

Recommendation:

The Port should reconfirm with the EDA that the financing agreement as currently operated by the Port and the administering bank provides the types of loan assistance required by the RLF program. The Port should review with the EDA whether the Port's program could be revised to better target the funds to the population needing the assistance.

Observation No. 21 - The Port Authority Does Not Document That The RLF Program Does Not Substitute For Private Sector Financing (Continued)

Port Authority Response:

We do not concur. The EDA, Revolving Loan Fund, Administrative Manual states in section IV. Revolving Loan Fund Restrictions, B., 3, Credit Otherwise Available, a. “a commitment letter from a participating bank stating the loan terms, the maximum amount to be extended by the bank, and the need for the RLF’s participation”. The Port has partnered with Citizens Bank NH (private sector financing) to provide matching (75/25) funding for the RLF loans. The commitment letter from the bank, which is issued before the commitment letter from the Port, specifically states “subject to approval of funding by the NH Port Authority Revolving Loan Fund.” The RLF does not substitute for private sector funds but promotes the use of private sector funds.

A letter requesting clarification has been sent to EDA.

Observation No. 22 - The Port Authority Does Not Monitor RLF Borrower Compliance With The Davis-Bacon Act

Observation:

The Port Authority (Port) does not monitor or follow-up on Revolving Loan Fund (RLF) loans involving construction that exceeds \$2,000 to determine borrower compliance with the Davis-Bacon Act. While the Port’s RLF program loan questionnaire inquires whether construction exceeding the \$2,000 limit will result from the loan, the loan documents do not include stipulations that the borrower is required to comply with the Davis-Bacon Act and the Port does not monitor for compliance with the Davis-Bacon Act.

Section D.13 of the Department of Commerce, Economic Development Administration (EDA) Standard Terms and Conditions dated December 1998 for the Revolving Loan Fund (RLF) specifies that, “[t]he Recipient [Port] shall require borrowers to comply with the Davis-Bacon Act, as amended ... when construction is financed in whole or in part by the RLF and when any related construction contract exceeds \$2,000.” The Davis-Bacon Act provides for the payment of prevailing wages in construction contracts.

Examples of RLF loans issued by the Port which would appear subject to the Davis-Bacon Act included loans where proceeds were to be used for construction activities on boats, and in one instance, construction activities on a pier.

The Port was apparently unaware of its responsibilities with respect to federal RLF terms and conditions related to the Davis-Bacon Act and as a result there is no assurance that borrowers that used loan proceeds to finance construction costing in excess of \$2,000 were aware of and complied with the Davis-Bacon Act.

Observation No. 22 - The Port Authority Does Not Monitor RLF Borrower Compliance With The Davis-Bacon Act (Continued)

Recommendation:

The Port should implement procedures to ensure that RLF borrowers with loans intended to be used for construction activities are aware of and comply with the Davis-Bacon Act. Procedures should include adding appropriate disclosures in the loan documents and also setting up monitoring procedures within the Port to ensure that applicable loans are in compliance.

Port Authority Response:

We concur. The present administration has incorporated the requirement into loan documents.

Observation No. 23 - The Port Authority Has Not Been Consistent In Accurately And Completely Reporting EDA Program Activity

Observation:

The Port Authority (Port) has not consistently followed the Economic Adjustment Program Revolving Loan Fund (RLF) Grants Administrative Manual for reporting RLF financial activity to the Economic Development Administration (EDA).

The RLF Administrative Manual describes the compliance, reporting, grant record keeping, and other administrative requirements and procedures that apply to the RLF grants funded by the EDA.

The following are examples where the Port has not been in compliance with RLF Administrative Manual requirements and the Port has not provided the EDA with accurate and complete information regarding the Port's operation of the RLF program.

- The Port did not include an annual Plan Certification with its 1999 annual report. According to the annual report form, included in the Grants Administrative Manual, when the certification does not accompany the report, a reference to when the certification will be filed is to be included with the report. This reference was also not included with the 1999 report. No documentation evidencing that the 1999 certification has been filed could be located at the Port.
- Based upon copies of reports on file at the Port, the Port has not consistently filed Federal Cash Transaction Reports (SF272) and Financial Status Reports (SF269).
- Not all amounts reported on the Requests for Advance or Reimbursements (SF270) are supported by the Port's accounting records. For example, no program income was ever reported, even though the Port has collected program income. The effect of not accurately reporting program income was to draw federal funds early. Some columns on

Observation No. 23 - The Port Authority Has Not Been Consistent In Accurately And Completely Reporting EDA Program Activity (Continued)

Observation (Continued):

SF 270s filed by the Port were not clerically accurate, some totals do not agree to Port accounting records, and in the SF 270 submitted April 1999, the three elements of the program were not broken out but were submitted combined in a single total column.

The Port's apparent lack of awareness with respect to federal RLF Administrative Manual policies and procedures and clerical-type errors contributed to the Port's lack of complete and accurate reporting.

Recommendation:

The Port should establish controls (policies and procedures) over the record keeping and reporting process of its RLF program. Concurrently, the Port should work with the EDA to determine the current status of reports due from the Port and measures that should be taken to correct previously filed information and to submit required information not previously filed.

Port Authority Response:

We concur. Prior to this audit, the Port depended on the US Department of Commerce, Economic Development Administration for review of reports. Based on the fact that the EDA never notified the Port that there might be inconsistencies in the reporting and that the EDA reimbursed the Port based on those reports, it was assumed that all reports were complete and correct.

The Port requested the audit to insure that the operation of the Port was compliant with State and federal regulations and good business practices. Isolation of duties by the previous administration contributed to this deficiency. The fishing program administrator (now operations manager) was not totally involved in the filing of financial reports. The previous Administrative Assistant handled the financial reports. When that person left, the operations manager assumed the duties. Lack of consistent and concise record keeping of the prior reports and the previous administrative assistant's filing system contributed to this deficiency. The Port will review the reports and take note of this observation with regards to future projects.

Observation No 24 - The Port Authority Does Not Review RLF Program Borrowers For Suspension Or Debarment Status

Observation:

The Port Authority (Port) does not have procedures for determining whether or not an applicant for a Revolving Loan Fund (RLF) loan has been suspended or debarred from receiving certain types of federal financial assistance and benefits. The Port neither requires borrowers to submit a certification nor does it check the U.S. General Services Administration (GSA) list of excluded parties prior to approving borrowers for RLF loans.

RLF program borrowers must not be suspended or debarred from participating in the federal program. The Port may rely upon a certification from the borrower unless the Port knows that a certification is erroneous. The Port may also check for suspended and debarred individuals listed in the *List of Parties Excluded From Federal Nonprocurement Programs*, issued by the GSA. Requirements related to suspension and debarment are contained in the federal agencies' codification of the government debarment and suspension common rule which implements Executive Order 12549 and 12689, Debarment and Suspension, and the terms of the award.

The Port's apparent lack of awareness of federal RLF regulations caused this noncompliance situation.

Recommendation:

The Port should establish policies and procedures to ensure that RLF loans are not issued to borrowers who are suspended or debarred from the loan program.

Port Authority Response:

We concur. The present administration has included a statement of debarment or suspension status, on the required RLF "Compliance Disclosure Form."

Management Issues Comments

Observation No. 25 - The Port Authority Does Not Have A Plan In Place For The Operation Of The Port Terminal After The Expiration Of The Current Contract

Observation:

The Port Authority (Port) has not adequately planned for operation of the port terminal after the expiration of its contract with the current port terminal operator. By not properly anticipating the termination of the contract and establishing a formal and documented plan for the operation of the port terminal, the Port has deviated from standard and sound management practices.

The contract for the port terminal operator expires on July 31, 2000 and the Port has not made provisions for replacement of the port terminal operator. It is not clear whether the Port has the authority in statute to operate in place of a port terminal operator, including setting fees and making expenditures for hiring stevedores and the rental of necessary equipment to perform the port terminal operator functions.

Per RSA 271-A:3, IV the Port is “authorized and empowered to contract with and secure the services of a port terminal operating firm, subject to approval of governor and council, for the purpose of having such firm operate a part or all of the facilities of the authority, including piers, wharves, warehouses...with such operating firm having the exclusive right to operate the business of a port terminal operator and stevedore, including but not limited to the handling of cargo, the collection of fees from wharfage and dockage and other marine terminal operations....”

The Port apparently has not wanted to act on contracting a new port terminal operator until it has hired a new port director and has further considered the options presented in the Port’s master plan document.

Recommendation:

The Port should immediately plan for the operation of the port terminal after the expiration of the current port terminal operator contract. If the Port does not anticipate immediately contracting with a terminal operator and plans to operate the terminal either on a short-term or long-term basis itself, it should research and determine its authority relative to the direct operation of the port terminal including setting of fees and making relevant expenditures.

The plan for the operation of the Port terminal should be documented and subject to Board ratification.

Observation No. 25 - The Port Authority Does Not Have A Plan In Place For The Operation Of The Port Terminal After The Expiration Of The Current Contract (Continued)

Port Authority Response:

We do not concur. The past and present administration had planned for the operation of the terminal in the absence of a terminal operator. During fiscal year 1999, it appeared doubtful to the administration that the terminal operator would honor the remaining term of the contract. In the event that the terminal operator prematurely ceased operating, the administration planned for the operation until a new operator was contracted. This event did not occur.

During fiscal year 2000, the terminal operator announced that they would not be requesting an extension or renewal of their contract. The Port planned to develop and issue a "Request For Proposal" (RFP) for a new terminal operator. At the end of December 1999, the Port Director resigned. With the absence of a Chief Administrative Officer, the Board withheld issuing an RFP until a new director could be appointed. Due to the unforeseen length of time in appointing a new director, the Port has been operating the terminal.

The sub-committee of the Port charged with the development of an RFP met to discuss the options (April 10, 2000) and reported to the Board (April 12, 2000) that until a director is appointed, the terminal should be operated as a public access facility. The present operation of the port is based on the following.

- The permissive language of the statute allows, but does not require, a terminal operator,
- The anticipated volume of activity,
- The availability of equipment and labor,
- The expertise of the Port's Operations Manager to oversee the facility, and
- The past practice of the "Terminal Tariff" relative to fees to be charged.

Cargo and passengers are moving through the facility, as before, the only difference being that a single contracted operator providing equipment and services is not available. Instead, multiple operators, on a cargo specific basis, handle the cargo with their own, rented or sub-contracted equipment. The Port Authority does not make expenditures for hiring longshoremen (stevedores). The local longshoremen have an agreement with a pay agent. Port users make payment for labor, directly to the pay agent. The pay agent disperses those funds to the individual laborers while making deductions for taxes, retirement, health insurance, etc. The pay agent also holds the workman's compensation insurance for the longshoreman.

The Port Authority does not rent equipment. Port users will rent, hire or provide their own equipment when handling cargo. The Port Authority requires proof of insurance and certification of equipment where available.

Observation No. 25 - The Port Authority Does Not Have A Plan In Place For The Operation Of The Port Terminal After The Expiration Of The Current Contract (Continued)

Port Authority Response (Continued):

The Port Authority, based on the previously established terminal tariff, now collects 100% of wharfage and dockage. The terms of the expired "Terminal Operators Agreement" only returned 20% of wharfage and dockage to the state.

Port users are charged for services provided such as water, use of the dumpster and electricity. In many cases the port user will contract directly with a contractor for waste removal.

Observation No. 26 - The Port Authority Does Not Have Clear Authority To Establish Rules Necessary For The Operation Of The State's Commercial Piers

Observation:

The Port Authority (Port) does not have clear authority to establish rules necessary for the commercial operations of the State piers transferred to its responsibility by Chapter 55:8 of the Laws of 2000.

Chapter 55:8 of the Laws of 2000 transfers the commercial fish piers in Portsmouth (transfer to be completed by August 15, 2000) and Rye and Hampton Harbors (transfers to be completed by June 30, 2001) from the Department of Resources and Economic Development to the Port Authority. Upon the transfers, the Port "shall have responsibility for and jurisdiction over each such pier and shall assume control of the management, operation, and maintenance of each respective pier."

Recommendation:

The Port should immediately request clarification from the Department of Justice of the Port's authority to establish rules for the operations of the piers transferred to its responsibility by Chapter 55:8 of the Laws of 2000.

The Port should also request legislation to provide clear statutory authority for the Port to establish rules relative to the operation of these piers.

Port Authority Response:

We concur. Upon passage of the legislation, which transferred the commercial fish pier in Portsmouth, dialogue was initiated with the Department of Justice and the Department of Administrative Services, Business Administration and Administrative Rules and the Legislature. It appears that the legislation may not have given the requisite authority to the Port Authority for the management of the pier. However, that authority may be

Observation No. 26 - The Port Authority Does Not Have Clear Authority To Establish Rules Necessary For The Operation Of The State's Commercial Piers (Continued)

Port Authority Response (Continued):

implied. The present administration has requested an opinion from the Attorney General regarding this matter. Furthermore, the Port may request a revision of the statute granting rule making authority to include "all provisions of the section (271-A)."

Comments For Other Agencies - Department Of Administrative Services

The following comments were developed as a result of the fieldwork performed at the Port Authority (Port). These comments address situations that were not directly under the control of the management of the Port but which affect Port operations. The Department of Administrative Services' responses are included with the comments.

Observation No. 27 - The Department Of Administrative Services' Oversight Of Port Authority Operations Should Be Improved

Observation:

The Department of Administrative Services (Department) has not fulfilled all of its responsibility to the State with regards to its oversight of the operations of the Port Authority (Port). Port operations that varied from State policies and procedures were not detected and corrected by the Department and became institutionalized at the Port.

The Department is responsible for maintaining fiscal control procedures over State executive branch agencies. The Department is directed to continually monitor the State's financial operations, needs, and resources, and to maintain an integrated financial accounting system. Examples of the Department's responsibilities include the following statutory cites.

- The Department's Budget Unit, per RSA 21-I:6, VI shall: "[c]onsult with the respective executive heads of state departments, agencies, boards and commissions, relative to the establishment, supervision, and maintenance of uniform and effective business records, business practices, and business management, and provide the necessary direction to insure that all manual of procedure requirements are complied with."
- The Department's Division of Accounting Services, per RSA 21-I:8, I (c) is responsible for: "Preauditing claims to be presented for the issuance of warrants and certifying to the governor and council that such are just and proper claims against the state and within appropriations provided by statute."
- The Department's Division of Accounting Services, per RSA 21-I:8, I (d) is responsible for: "Preparing appropriate warrants and schedules of pre-audited manifests supporting the same, for consideration and execution by the governor, with the advice and consent of the council."

It appears that despite indicators of control problems at the Port over the past several years, the Department did not recognize or take note of the indicators and failed to provide the assistance required by the Port. For example, a \$2.1 million account receivable due from the federal government remained uncollected from the completion of the construction of a pier in 1996 until reimbursement was made in September 1999. Additional indicators included numerous invoices submitted for payments that appear unusual and questionable on their face such as: a December 1998 invoice for \$550 of prepaid car washes; a January

Observation No. 27 - The Department Of Administrative Services' Oversight Of Port Authority Operations Should Be Improved (Continued)

Observation (Continued):

1998 invoice for \$340 of footwear; payments for wrist watches, neoprene shorts, a \$500 gas grill, suntan oil, and items of clothing; payments to normal vendors charged to the temporary personnel expenditure class line; payments for the repair of vehicles – when the Port did not own any vehicles; payments for the repair of boats – when the Port did not own any boats; payments on \$1,800 and \$2,400 invoices for unspecified boat repairs and services for the Port's current boats; invoices for gasoline pumped into cars with nongovernmental license plates; failure to recognize the risks associated with the Port's part-time employees not filing time sheets or otherwise accounting for hours worked even though the Department had to undertake a project at the Port to correct for prior part-time payroll problems; failure on the part of the Port to submit trust fund operating statements; and failure on the part of the Port to submit reasonable equipment inventory reports.

Recommendation:

The Department should become more proactively involved in the oversight of the financial operations of the State agencies for which it is responsible.

The Department should review the methods it uses to provide guidance and direction to the agencies for which it is responsible, including the adequacy of its expired manual of procedures (last issued in 1984). The Department should also review the need for continued training of agency staff in the State's policies and procedures regarding business records, practices, and management.

The Department should recognize through the review of documents provided by State agencies such as the Port (and required documents not supplied by the agencies) the nature of the agencies' operations. Department personnel responsible for the review of invoices supporting payment vouchers should be suitably knowledgeable of the agencies' operations to be able to recognize questionable expenditures. Department personnel responsible for the receipt of periodic agency reporting should question when agencies do not submit reasonable reports. Department personnel responsible for providing accounting policy and procedures guidance to the agencies should recognize when the policies are not being adhered to and take action to bring agencies into compliance with State policies.

Department Of Administrative Services Response:

The Department of Administrative Services (DAS) fully understands its responsibilities relative to the oversight of all state agency operations, including those of the Port Authority, and makes every attempt possible to ensure that adequate control systems are in place to fulfill these responsibilities. While we agree that the apparent level of non-compliance with policies and procedures cited in this observation is significant, we believe that this situation is clearly the exception rather than the rule. This fact is evidenced by the lack of similar findings in other agency audit reports issued by the LBA.

Observation No. 27 - The Department Of Administrative Services' Oversight Of Port Authority Operations Should Be Improved (Continued)

Department Of Administrative Services Response (Continued):

DAS has initiated a review of each of the "indicators" noted in the observation, and we will take the steps necessary to enhance the control structure and to minimize control risk. Our comments pertaining specifically to the recommendations follow.

Oversight of the Financial Operations of the Port Authority

DAS believes that it has been proactive in its oversight responsibility of the financial operations at the Port Authority. However, as mentioned above, to the extent that our review of the noted indicators concludes that there is a need for improvements in the control structure at either the Port Authority or within DAS, we will pursue those improvements.

Review of Methods of Providing Guidance and Direction to State Agencies

DAS is continually reviewing the methodologies it uses to provide guidance and direction to state agencies to ensure that such guidance is responsive to agency needs. Specifically, with respect to the manual of procedures, DAS has recently been successful in obtaining legislation (Chapter 288, NH Laws of 2000, effective July 1, 2000) that will allow the department to update the manual in a more timely and continuous manner. Our goal is to reissue the manual, in its entirety, before the end of fiscal year 2001. From the revision's issue date forward, the manual will be maintained as a "living document" that will be continuously reviewed to ensure that it reflects up to date policy guidance. Although the manual has not been "reissued" since 1984, this fact should not be construed as a failure by the Department to recognize its responsibility for providing guidance and direction to state agencies. There are numerous other forms that this guidance takes, including sessions to review annual closing procedures, written communications to all agencies relative to such issues as service contracting, purchasing, or travel procedures, and the development of an administrative handbook which has been utilized in formal class training provided through the Division of Personnel.

DAS does agree that its efforts relative to "hands on" training of agency staff can be enhanced. We also recognize that training needs vary from agency to agency and we are committed to ensuring that available training materials and sessions are responsive to those needs, regardless of an agency's size or the complexity of its operations. We are developing various initiatives that are designed to increase the availability of training to agency personnel, as well as examining ways that DAS personnel can provide more assistance and oversight through on-site agency visitations.

Observation No. 27 - The Department Of Administrative Services' Oversight Of Port Authority Operations Should Be Improved (Continued)

Department Of Administrative Services Response (Continued):

Document/Policy Review

Knowledge of Agency Operations - The Bureau of Accounting's Agency Records Auditors have, on average, approximately one minute to spend on each payment voucher that crosses their desks to be approved. While they must be, and are, well versed in general state guidelines for determining allowable expenditures, they have not been asked to make judgments as to whether or not an expenditure is necessary or appropriate for the individual agency's operations. In order to process the approximately 26,000 payment vouchers that cross the agency auditors' (staff of 4½ auditors which due to budget reductions has been reduced from 6 auditors) desks each month, their "pre-audit" review must be succinct and directed at determining that overall state procedure is being followed.

The Bureau has implemented a number of pre and post-audit reviews through the use of technologies which are aimed at tracking trends pertaining to agency errors or problems in an effort to determine where the areas of risk associated with payment voucher processing are the most prevalent. However, to accomplish a more detailed review of all transactions submitted for processing, the legislature must allow the Department to return staffing to pre-budget reduction levels.

Collection of Required Agency Reports - DAS concurs that agencies should be contacted when not responding to required report submissions and, to the extent this department is aware of any agency's need to file any such reports, we make every attempt to ensure that reports are obtained on a timely basis. However, completeness of these reports is the primary responsibility of the agency. We attempt to determine the reasonableness of all report submissions by analyzing trends within and among all agencies, and we make every effort possible to understand the operations of an agency as a basis for drawing conclusions on reasonableness.

Accounting Policy and Procedures Guidance - We believe that DAS personnel do a very capable job of advising agencies regarding adhering, or failing to adhere, to state policies and procedures and that immediate action is taken to correct deficiencies when appropriate. As mentioned above, we are looking at additional ways that the department may be more proactive in the way that it meets its statutory oversight responsibilities, but we believe a strong foundation already exists for doing so.

Establishment of an Internal Audit Function - RSA 21-I:7 establishes an internal audit unit, within the Department of Administrative Services, to assist the Commissioner by supplying analytical reports of examinations conducted of the Department's various divisions, bureaus, units, programs, and functions. Currently, this unit consists of one person whose efforts have been focused on reviewing agency responses to recommendations contained in financial and compliance audits, to ensure that commitments made to change policies or procedures are appropriately implemented.

Observation No. 27 - The Department Of Administrative Services' Oversight Of Port Authority Operations Should Be Improved (Continued)

Department Of Administrative Services Response (Continued):

The Department of Administrative Services believes that, to be successful in fulfilling its statutory obligations and to address the concerns raised in this observation, it must expand the focus of its internal audit function to include the review of external agency operations. Therefore, in our 2002-2003 biennial budget request, we have proposed the addition of three internal auditors whose responsibilities will be to review the operations and internal controls of smaller state agencies, and to assist or coordinate efforts with those agencies who may have their own internal audit function. Whereas the auditors have also recommended the establishment of a statewide effort directed at fraud deterrence and detection, the establishment of an internal audit staff will incorporate the necessary policies and procedures to address this concern as well.

Port Authority Response:

The Port Authority cannot comment on the performance of another department. However, the present administration of the Port Authority has proactively involved the Department of Administrative Services business agent in the daily financial operations.

It should be noted that the Port has a very small staff (4 full time and 6 part-time employees), all of which require specialized training in the fields of Marine Terminal Operations and Harbor Management. As such, the Authority is critically dependent on the NH Department of Administrative Services to provide administrative oversight and guidance.

Observation No. 28 - Formal Fraud Deterrence And Detection Program Should Be Established

Observation:

The State has no formal fraud deterrence and detection program.

Fraud encompasses an array of irregularities and illegal acts characterized by intentional deception. Persons outside or inside the organization can perpetrate it for the benefit or to the detriment of the organization.

Deterrence consists of those actions taken to discourage the perpetration of fraud and limit the exposure if fraud does occur. The principal mechanism for deterring fraud is the establishment of effective controls. Management has the primary responsibility for establishing and maintaining controls.

Observation No. 28 - Formal Fraud Deterrence And Detection Program Should Be Established (Continued)

Observation (Continued):

Detection consists of identifying indicators of fraud sufficient to warrant recommending an investigation. These indicators may arise as a result of controls established by management, tests conducted by internal auditors, and other sources both within and outside the entity.

The internal auditing arm of an entity is typically responsible for assisting in the deterrence and detection of fraud by examining and evaluating the adequacy and the effectiveness of controls, commensurate with the extent of the potential exposure/risk in the various segments of an entity's operations. In carrying out this responsibility, internal auditing should, for example, determine whether:

- The organizational environment fosters control consciousness;
- Realistic organizational goals and objectives are set;
- Written policies (e.g., code of conduct, fraud reporting policy) exist that describe prohibited activities and the action required whenever violations are discovered;
- Appropriate authorization policies for transactions are established and maintained;
- Policies, practices, procedures, reports, and other mechanisms are developed to monitor activities and safeguard assets, particularly in high-risk areas;
- Communication channels provide management with adequate and reliable information; and
- Recommendations need to be made for the establishment or enhancement of cost-effective controls to help deter fraud.

As noted above, the principal mechanism for deterring and detecting fraud is the establishment and operation of effective controls. An integral factor of an entity's control environment is the control consciousness of its people. Management is responsible for establishing controls and monitoring compliance, and is the primary influence on the degree of importance its employees attach to controls. High control consciousness at all levels of an entity is a significant factor in deterring fraud.

Recommendation:

The State should establish a formal fraud deterrence and detection program. Establishing a formal program should help limit the State's exposure to fraud and should promote timely detection.

Observation No. 28 - Formal Fraud Deterrence And Detection Program Should Be Established (Continued)

Recommendation (Continued):

The State should also take measures to foster a high degree of control consciousness among its employees and ensure that its employees understand that adhering to controls is a primary concern of management and takes priority over the speed of service.

While the State has established a system of controls over its operations, as indicated by the observations noted in this audit report, the State needs to do more in the area of fraud deterrence and detection. Management and employees must consider that allowing controls to be bypassed to expedite processes or “cutting red tape” generally comes with a cost of increased risk of errors and fraud. It is management’s responsibility to properly balance that risk.

Department Of Administrative Services Response:

The Department of Administrative Services (DAS) agrees with the recommendation and will examine its options with respect to establishing a system of fraud deterrence and detection.

In conjunction with the formulation of a formal fraud reporting policy as described in our response to observation number 29, DAS will investigate the need for adding to its internal audit capabilities as a primary way of addressing fraud deterrence and detection. While the Department currently employs one internal auditor, this person’s efforts are largely dedicated to a “post-auditing” process which involves ensuring that agencies are responsive to their proposed corrective actions as cited in LBA audit reports. Additionally, Business Supervisors within our Budget Office and Agency Records Auditors within our Bureau of Accounting do make periodic site visits to individual agencies, but these are generally directed at resolving identified problems.

As mentioned in our response to observation number 27, the DAS is proposing the addition of 3 internal auditors to address this issue, and to increase our capability to provide prudent oversight to all State agencies.

Observation No. 29 - Formal Fraud Reporting Policy Should Be Established

Observation:

The State has no formal fraud reporting policy. The lack of a written policy may delay the reporting of fraudulent activity.

The attributes of an effective fraud reporting policy include:

- The policy is in writing;
- The reporting policy describes fraudulent activities and the actions required when fraud is suspected or detected;
- The policy is communicated to all employees; and
- Management obtains written assurance from each employee that the policy and related reporting mechanism is understood.

The effectiveness of a fraud reporting policy is enhanced when employees have a clear understanding of fraud indicators and what constitutes a fraudulent act. It is important that the reporting procedure is non-threatening for the reporter and provides for the reasonable protection of all parties.

Recommendation:

The State should establish a formal fraud reporting policy and provide its employees with fraud awareness training. The State should take measures to ensure that the policy facilitates and encourages reporting and protects all parties involved.

Department Of Administrative Services Response:

The Department of Administrative Services (DAS) concurs with this recommendation and the Department will take the steps necessary to develop such a policy, communicate it to all employees, and ensure that the related reporting mechanism is well understood. DAS will coordinate this effort through consultation with the Justice Department to ensure that the proper safeguards, particularly as they relate to the reporting mechanism, are in place.

NOTE: THE FOLLOWING FINANCIAL STATEMENTS ARE UNAUDITED

**STATE OF NEW HAMPSHIRE
NEW HAMPSHIRE PORT AUTHORITY**

**COMBINED STATEMENT OF REVENUES AND EXPENDITURES
GENERAL, SPECIAL, AND CAPITAL PROJECTS FUNDS
NINE MONTHS ENDED MARCH 31, 2000**

	General Fund	Special Fund	Capital Projects Fund	Combined Total All Funds
Revenues				
<u>Unrestricted Revenue</u>				
Port Stevedore Contract	\$ 226,669	\$ -0-	\$ -0-	\$ 226,669
Facilities Lease	13,332	-0-	-0-	13,332
Miscellaneous	-0-	-0-	-0-	-0-
Total Unrestricted Revenues	\$ 240,001	\$ -0-	\$ -0-	\$ 240,001
<u>Restricted Revenues</u>				
Mooring And Waitlist Fees	\$ 88,183	\$ -0-	\$ -0-	\$ 88,183
Coastal Vessel Fund	19,185	-0-	-0-	19,185
Foreign Trade Zone Fees	435	-0-	-0-	435
Revolving Loan Program	-0-	26,026	-0-	26,026
Port Expansion Funds	-0-	-0-	2,121,020	2,121,020
Miscellaneous	-0-	1,321	-0-	1,321
Total Restricted Revenues	\$ 107,803	\$ 27,347	\$ 2,121,020	\$ 2,256,170
Total Revenues	\$ 347,804	\$ 27,347	\$ 2,121,020	\$ 2,496,171
Expenditures				
Salary And Benefits	\$ 225,592	\$ -0-	\$ -0-	\$ 225,592
Current Expenses	52,026	764	-0-	52,790
Mitigation Monitoring	35,610	-0-	-0-	35,610
Equipment	29,284	-0-	-0-	29,284
Payment In Lieu Of Taxes	-0-	-0-	-0-	-0-
Dredging Projects	-0-	-0-	92,066	92,066
Port Expansion	-0-	-0-	-0-	-0-
Other	5,935	465	-0-	6,400
Total Expenditures	\$ 348,447	\$ 1,229	\$ 92,066	\$ 441,742
Other Financing Sources				
Loan Principal Repayments	\$ -0-	\$ 132,708	\$ -0-	\$ 132,708
Other Financing Uses				
Loans Issued	\$ -0-	\$ 214,500	\$ -0-	\$ 214,500
Excess (Deficiency) Of Revenues And Other Financing Sources Over (Under) Expenditures And Other Financing Uses				
	\$ (643)	\$ (55,674)	\$ 2,028,954	\$ 1,972,637

**STATE OF NEW HAMPSHIRE
NEW HAMPSHIRE STATE PORT AUTHORITY**

**COMBINING BALANCE SHEET
EXPENDABLE TRUST FUNDS
MARKETING AND PORT MAINTENANCE FUNDS
AS OF MARCH 31, 2000**

	Marketing Fund	Port Maintenance Fund	Total Trust Funds
Assets			
Deposits	\$ 42,212	\$ -0-	\$ 42,212
Accounts Receivable	-0-	5,000	5,000
Total Assets	\$ 42,212	\$ 5,000	\$ 47,212
 Liabilities And Fund Balance			
Liabilities:			
Accounts Payable	\$ -0-	\$ -0-	\$ -0-
Fund Balance	\$ 42,212	\$ 5,000	\$ 47,212
Total Liabilities And Fund Balance	\$ 42,212	\$ 5,000	\$ 47,212

**STATE OF NEW HAMPSHIRE
NEW HAMPSHIRE STATE PORT AUTHORITY**

**COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCES
EXPENDABLE TRUST FUNDS
MARKETING AND PORT MAINTENANCE FUNDS
FOR THE NINE MONTHS ENDED MARCH 31, 2000**

	<u>Marketing Fund</u>	<u>Port Maintenance Fund</u>	<u>Total Trust Funds</u>
Revenues			
Contributions	\$ 50,000	\$ 5,000	\$ 55,000
Interest	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>
Total Revenues	\$ 50,000	\$ 5,000	\$ 55,000
Expenditures	<u>\$ 29,111</u>	<u>\$ -0-</u>	<u>\$ 29,111</u>
Excess Of Revenues Over Expenditures	\$ 20,889	\$ 5,000	\$ 25,889
Fund Balance July 1, 1999	<u>\$ 21,323</u>	<u>\$ -0-</u>	<u>\$ 21,323</u>
Fund Balance March 31, 2000	<u><u>\$ 42,212</u></u>	<u><u>\$ 5,000</u></u>	<u><u>\$ 47,212</u></u>

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APPENDIX

Current Status Of Prior Audit Findings

The following is a summary, as of July 14, 2000, of the status of the observations contained in the audit report of the New Hampshire State Port Authority for the eighteen months ended December 31, 1985. 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.

	Status
Internal Control Structure	
<i>Reportable Conditions</i>	
1. Controls Over Revenue (See Current Year Observation Nos. 6, 8, and 12)	● ○ ○
2. Equipment Records (See Current Year Observation No. 9)	○ ○ ○
State Compliance	
3. Obsolete Provision Of Statute Re: Stock And Trade Tax Exemption	● ● ●
Federal Compliance	
4. Incomplete Contract Provisions	● ● ●
5. Weak Federal Program Accounting (See Current Year Observation Nos. 19 Through 24)	○ ○ ○

Status Key

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

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