

**STATE OF NEW HAMPSHIRE
SWEEPSTAKES COMMISSION**

**MANAGEMENT LETTER
FOR THE YEAR ENDED
JUNE 30, 1999**

To The Fiscal Committee Of The General Court:

We have audited the financial statements of the New Hampshire Sweepstakes Commission, a department of the State of New Hampshire, as of and for the year ended June 30, 1999 and have issued our report thereon dated November 24, 1999.

This management letter, a product of the audit of the New Hampshire Sweepstakes Commission for the year ended June 30, 1999, contains an auditor's report on compliance and on internal control over financial reporting and an auditor's report on management issues. The appendix, included as an attachment to the management letter, provides a summary of the status of observations that were previously reported in the *Management Letter For The Year Ended June 30, 1998*.

The Commission is again submitting its comprehensive annual financial report (CAFR) to the Government Finance Officers Association (GFOA) for consideration for the GFOA's Certificate of Achievement for Excellence in Financial Reporting. A certificate of achievement is a prestigious national award for CAFRs that are prepared in accordance with program standards. The program standards are intended to promote easily readable and understandable financial reports that demonstrate financial accountability and comparability. The Commission received GFOA certification on its 1998 CAFR, and it is believed that this CAFR will conform to the certificate of achievement program requirements. A copy of the New Hampshire Sweepstakes Commission's 1999 CAFR can be obtained from the New Hampshire Sweepstakes Commission, 14 Integra Drive, Concord, NH 03301.

Office of Legislative Budget Assistant
Office Of Legislative Budget Assistant

November 24, 1999

**STATE OF NEW HAMPSHIRE
SWEEPSTAKES COMMISSION**

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

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

To The Fiscal Committee Of The General Court:

We have audited the financial statements of the New Hampshire Sweepstakes Commission, a department of the State of New Hampshire, as of and for the year ended June 30, 1999, and have issued our report thereon dated November 24, 1999. We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the New Hampshire Sweepstakes Commission's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*. However, we noted a certain immaterial instance of noncompliance that is described in observation No. 3 of this report.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the New Hampshire Sweepstakes Commission's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Commission's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable conditions are described in observations No. 1 and No. 2 of this report.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that neither of the reportable conditions referred to above is a material weakness.

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

Office of Legislative Budget Assistant
Office Of Legislative Budget Assistant

November 24, 1999

Internal Control Comments

Observation No. 1 – Inadequate Monitoring Of Advertising Contract

Observation:

The Sweepstakes Commission does not have adequate policies and procedures in place to monitor its advertising contract to determine that advertising costs are reasonable and within project estimates.

The Commission is engaged in a two-year \$3.3 million advertising contract; half of which is budgeted for fiscal year 1999 and half for fiscal year 2000. The advertising firm receives 15 percent of the total contracted amount in the form of a retainer fee. Radio, television, and print advertising is arranged through the advertising firm, for which the firm bills the Commission periodically. The retainer fee is billed in equal monthly installments.

We noted the following issues during our testing of advertising expenditures for fiscal year 1999:

- A. A \$55,000 invoice for an estimate of pre-production work lacked proper supporting documentation; nonetheless, the invoice was approved for payment by management. This invoice, billed in fiscal year 2000 and charged to the fiscal year 1999 budget, equaled the amount remaining in the fiscal year 1999 budget. It was subsequently determined that the \$55,000 estimate was approximately \$51,000 over the actual charges incurred in fiscal year 1999. The Commission did eventually receive credit for this charge, after it was questioned by the LBA audit team.
- B. The current contract does not contain a comprehensive definition of what is covered by the retainer fee. We noted two bills, one for \$22,500 for concept development work and the above noted bill of \$55,000 for pre-production work that may be covered by the \$20,625 monthly retainer fee. It is unclear what services are covered under the retainer fee.
- C. Non-retainer fee items did not receive Commissioners' approval in advance of incurring the expenditure as specified in the contract agreement. By not having written Commissioners' approval, services undertaken by the advertising firm could potentially be in conflict with Commission interests.

Observation No. 1 – Inadequate Monitoring Of Advertising Contract (Continued)

Recommendation:

We recommend the Commission improve its procedures over the monitoring of its advertising contract to include the following:

- A. As it is good internal control practice and required by the contract agreement, all invoices should be accompanied by proper supporting documentation prior to being approved by management for payment. Management should also ensure that advertising expenditures are recorded in the proper accounting periods.
- B. The Commission, in its contract with the advertising firm, should develop a comprehensive definition of “retainer fees” and what is covered by the monthly fee. The Commission may also want to consider abolishing retainer fees from future advertising contract agreements and pay for all services as incurred.
- C. Non-retainer fee items should receive written approval of the Commissioners in advance of incurring the expenditure in accordance with the contract agreement. Additionally, projects should be monitored to determine that the costs are reasonable and within expectations.

Auditee Response:

- A. We concur. The Commission currently requires proper supporting documentation for all expenditures. The year-end invoice of \$55,000, referenced in the observation, was for pre-production work in connection with the fall 1999 ad campaign. It has long been the practice of the advertising firm, with approvals from the Commission, to begin work in April or May for a fall campaign. Developing concepts, hiring talent and pre-production occurs prior to June 30 to ensure successful production in September. The Commission allotted a portion of its fiscal year 1999 budget for such expenses. As the actual production did not occur until the beginning of fiscal year 2000, it would appear that the \$55,000 invoice was charged to the incorrect period. The Commission requested that the advertising firm credit the fiscal year 1999 budget and charge the fiscal year 2000 budget for this ad campaign until such time as an agreement can be reached on how to account for campaign work that spans two fiscal years.
- B. We concur in part. The advertising firm’s proposal to the Commission defines what services are included under the retainer fee arrangement such as copywriting, media planning/buying, standard public relations, etc. The two invoices referenced in the observation for concept development and pre-production were properly billed as those services are not included in the retainer fee. The Commission, in cooperation with the advertising firm, will develop a more comprehensive definition of retainer fee to be included in the contract.

Observation No. 1 – Inadequate Monitoring Of Advertising Contract (Continued)

Auditee Response (Continued):

- C. We concur. The contract language states the requirement of “Commission approval” for non-retainer fee items, however it is highly impractical and inefficient to bring every estimate before the Commission at their monthly meeting. Therefore, an amendment to the contract will be drafted to allow approvals to be granted by the Commission’s designee. It should be noted that currently, approval by the Marketing Director and/or the Executive Director is required prior to expenses being incurred.

Observation No. 2 – Unresolved Prior Audit Comment

Observation:

The Sweepstakes Commission and the Tri-State Lotto Commission have, in the past, received an audit comment from the LBA and from the outside auditors contracted to conduct a service center audit on the on-line vendor’s computer site in Augusta, Maine. The comment, repeated here again for fiscal year 1999, cites the Commission for not having reviewed or approved the disaster recovery plan put forth by the current on-line vendor.

An important part of an organization’s internal control is the development of a disaster recovery plan for its automated systems to ensure continuity of operations in the event of a disaster. Such plans should be tested, reviewed, and updated on a regular basis to determine that the recovery plan still adequately addresses the organization’s needs. Thus, the purpose of the audit comments from two different auditors.

As a part of the Commission’s fiscal year 1997 audit, a service center audit was performed on the on-line vendor’s Augusta, Maine computer site. The audit report contained an observation noting that the Sweepstakes and Tri-State Lotto Commissions had neither reviewed nor approved the existing disaster recovery plan. Furthermore, the observation disclosed that the existing recovery plan did not clearly address the estimated recovery time of critical operations and services that would be suspended under various disaster scenarios.

The status of this observation remains unresolved.

Recommendation:

As mentioned in the prior audits of the Commission, it should review and approve the disaster recovery plan in place for its applications. It should also ensure that a functional recovery plan is in place, in a timely manner, when a new on-line contract is entered into effective July 1, 2000.

Observation No. 2 – Unresolved Prior Audit Comment (Continued)

Auditee Response:

We concur. Since the first LBA finding in fiscal year 1998, the Commission repeatedly requested an adequate disaster recovery plan from its on-line vendor. After comments from the service center auditors and the LBA, as well as the growing concern over Y2K, the vendor finally complied and submitted a revised plan in December 1999. The plan was approved by the Tri-State Commission in December 1999 and was approved by the New Hampshire Sweepstakes Commission in February 2000.

The Commission is well aware of the importance of developing a disaster recovery plan to ensure continuity of operations. The Commission's own internal disaster recovery plan was adopted in 1997 and is reviewed and updated on an annual basis. The new on-line contract, effective July 1, 2000, requires the vendor to submit a disaster recovery plan to the Commission for approval prior to system implementation.

State Compliance Comment

Observation No. 3 – Merchandise Prizes Not Subject To Child Support Intercept

Observation:

In fiscal year 1999, the Commission began offering instant ticket games that give players a chance to win merchandise in lieu of cash prizes. The Commission has not been verifying whether winners of merchandise prizes are in arrearage for child support in accordance with the provisions of RSA 284:21-v.

RSA 284:21-v requires that the Commission verify with the Department of Health and Human Services whether winners, subject to federal W-2G reporting requirements, are in arrearage for child support. The Internal Revenue Service requires reporting of all winnings exceeding \$600 on a W-2G form. The Commission is responsible to withhold child support arrearages from the winnings and to make payment to the Department of Health and Human Services on the winner's behalf.

In addition, RSA 284:21-v requires that rules be adopted under RSA 541-A, relative to withholding prize money from lottery claimants having child support arrearages. The current rules do not address the treatment of merchandise prizes subject to child support intercept.

Recommendation:

We recommend that the Commission seek an opinion from the Attorney General's Office on the legality of its practices for handling merchandise prize claims that meet W-2G reporting requirements to ensure the Commission is in compliance with RSA 284:21-v.

It is evident that child support payments may not be withheld as easily from merchandise prizes as they are for cash prizes. Therefore, we further recommend that the Commission revise its administrative rules regarding child support intercepts based upon the Attorney General's Office opinion.

Auditee Response:

We concur. The Commission sought an opinion from the Attorney General's Office on the legality of not subjecting merchandise prize winners to child support intercept. Based on the opinion of the Attorney General's Office, the Commission is required to subject all winners, whether for cash or merchandise, to child support intercept. The Commission's administrative rules regarding child support intercept will be reviewed should we offer other merchandise prize games.

Auditor's Report On Management Issues

To The Fiscal Committee Of The General Court:

We have audited the financial statements of the New Hampshire Sweepstakes Commission as of and for the year ended June 30, 1999 and have issued our report thereon dated November 24, 1999. We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States.

In planning and performing our audit of the financial statements of the New Hampshire Sweepstakes Commission for the year ended June 30, 1999, we noted a certain issue related to the operation of the Commission that merits management consideration but does not meet the definition of a reportable condition as defined by the American Institute of Certified Public Accountants, and was not an issue of noncompliance with laws, rules, or regulations.

The issue that we believe is worthy of management consideration but does not meet the criteria of reportable internal control or compliance conditions is described in observation No. 4 of this report.

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

Office of Legislative Budget Assistant
Office Of Legislative Budget Assistant

November 24, 1999

Management Issues Comment

Observation No. 4 – Performance Measurement Considerations For Future Products

Observation:

As mentioned in observation No. 3, the Commission began offering instant ticket games in fiscal year 1999 that provided players a chance of winning merchandise prizes. Such prizes included Harley Davidson® motorcycles and Polaris® snowmobiles. Below we suggest analysis that the Commission should perform for future products to verify its goals have been achieved.

Instant ticket games are the single largest selling game for the Commission, accounting for approximately 60% of total sales for 1999. In an effort to expand markets and tap into new players, the Commission began offering merchandise games, beginning with the Harley Davidson® motorcycle ticket, where a player could win a motorcycle in a second chance drawing. The cost to use the Harley Davidson® name was \$153,700. While the Commission is to be commended for trying to expand its markets, it has not established performance measurements for this type of game to determine whether the game achieved the goal of expanded markets or new players.

It is unclear whether the merchandise games have opened up markets that were previously untapped. In answering that question and others, the Commission has the opportunity to perform post game surveys from the player information that was provided with the second chance drawing to win a Harley Davidson® motorcycle.

Finally, the Commission did not entertain bids when it entered into its commercial ventures with Harley Davidson® and Polaris®. If it had, it may have discovered that the competitors of Harley Davidson® and Polaris® were willing to offer more favorable terms on their merchandise and the use of their names.

Recommendation:

We recommend the Commission continue to seek out innovative ways of expanding the market. In so doing, it should consider establishing performance measurements at the inception of the process in order to determine whether its goals have been achieved. The Commission should work with its advertising firm to develop methods of capturing this information for future analysis. Further, we recommend that competing merchandisers be offered an opportunity to bid for participation in the instant ticket game sales promotions.

Observation No. 4 – Performance Measurement Considerations For Future Products (Continued)

Auditee Response:

We concur. As always, the Commission will continue to seek out innovative ways of expanding its player base. We acknowledge the LBA Audit Division's suggestion and will take it under advisement.

APPENDIX

Current Status Of Prior Audit Findings

The following is a summary of the status, as of November 24, 1999, of the observations contained in the management letter of the Sweepstakes Commission for the year ended June 30, 1998. A copy of the prior management letter can be obtained from the Office of Legislative Budget Assistant, Audit Division, 107 North Main Street, State House, Room 102, Concord, N.H. 03301.

	Status
 <i>State Compliance</i>	
1. Noncompliance With Certain State Statutes	● ● ●
2. Relocation Of Powerball Sign	● ● ●
 <i>Management Issues</i>	
3. Awarding Of Terminals For On-Line Agents	● ● ●
4. Year 2000 Compliance	● ● ●
5. Contracting With CPA Firm To Witness Lottery Drawings	● ● ●
6. Service Center Disaster Recovery Plan (See Current Observation No. 2)	0 0 0

Status Key

Fully resolved	● ● ●
Substantially resolved	● ● 0
Partially resolved	● 0 0
Unresolved	0 0 0

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