

**STATE OF NEW HAMPSHIRE
LOTTERY COMMISSION**

**MANAGEMENT LETTER
FOR THE FISCAL YEAR ENDED JUNE 30, 2018**

To The Fiscal Committee Of The General Court:

We have audited the financial statements of the New Hampshire Lottery Commission (Lottery) as of and for the fiscal year ended June 30, 2018 and have issued our report thereon dated December 19, 2018.

This management letter, a byproduct of the audit of the New Hampshire Lottery Commission for the fiscal year ended June 30, 2018, contains our auditor's report on internal control over financial reporting and on compliance and other matters and related audit findings. The appendix to this letter, on page 7, provides a summary of the status of observations presented in the fiscal year 2017 and fiscal year 2016 Lottery Commission management letters.

The Lottery 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 Lottery received GFOA certification for its 2017 CAFR, and it is believed that the 2018 CAFR also conforms to the certificate of achievement program requirements. A copy of the Lottery's 2018 CAFR can be obtained from the New Hampshire Lottery Commission, 14 Integra Drive, Concord, NH 03301. The Lottery CAFR can also be accessed online at:

http://www.gencourt.state.nh.us/LBA/AuditReports/FinancialReports/pdf/Lottery_2018_CAFR.pdf

Office of Legislative Budget Assistant

Office Of Legislative Budget Assistant

December 19, 2018

**STATE OF NEW HAMPSHIRE
LOTTERY COMMISSION
2018 MANAGEMENT LETTER**

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* No comments suggest legislative action may be required.

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

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

To The Fiscal Committee Of The General Court:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the New Hampshire Lottery Commission (Lottery) which comprise the Statement of Net Position as of June 30, 2018 and the related Statements of Revenues, Expenses, and Changes in Net Position and Cash Flows for the fiscal year then ended, and the related notes to the financial statements, which collectively comprise the Lottery's basic financial statements, and have issued our report thereon dated December 19, 2018, which includes an emphasis-of-matter paragraph noting the Lottery's adoption of Governmental Accounting Standards Board (GASB) Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* and GASB Statement No. 85, *Omnibus 2017*.

Internal Control Over Financial Reporting

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

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control that we consider to be significant deficiencies. We consider the deficiencies described in Observations No. 1 through No. 3 to be significant deficiencies.

Compliance And Other Matters

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

Lottery Commission's Responses To Findings

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

Purpose Of This Report

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


Office Of Legislative Budget Assistant

December 19, 2018

Internal Control Comments
Significant Deficiencies

Observation No. 1: Strengthen Contract Monitoring Controls

Observation:

The Lottery has not established sufficiently independent contract monitoring controls to ensure that its advertising contract is operating as intended.

Auditor review of fiscal year 2018 advertising expenses noted that approximately \$5,000 of expenses the contractor/vendor charged the Lottery was supported by documentation of payments made by the contractor to a Lottery employee. Review of the documentation supporting the contractor's invoice revealed that, at the end of fiscal year 2018, a Lottery employee submitted work-related expenses accumulated over the course of the fiscal year to the contractor for reimbursement. The contractor paid the employee directly and subsequently invoiced the Lottery for the amount paid to the Lottery's employee.

The documentation supporting the employee's reimbursement request was largely a collection of food service, grocery, and other store receipts with pencil notes and circled amounts. Some receipts appeared to reference meetings. There was no evidence that the purchases were reviewed and approved for reimbursement by any Lottery employee. There also was no evidence that the expenses claimed by the employee for reimbursement were valid advertising contract expenses eligible to be claimed by the advertising contractor.

Allowing a contractor to make payments directly to an agency employee raises a number of concerns about the entity's controls and its ability to recognize and respond to the related significant operational risks. The increased risk resulting from this type of transaction is especially concerning when the employee receiving payment from the vendor is one of the primary agency employees responsible for monitoring the performance of the contractor.

Recommendation:

The Lottery should strengthen its contract monitoring controls, including controls to more closely monitor expenses claimed by its contractors, to ensure that only valid Lottery contract-related expenses are paid by the contractor and submitted for Lottery reimbursement.

The Lottery should strengthen its controls over general expenses by ensuring that Lottery employees submit timely claims for reimbursement of business expenses and that all employee claims for reimbursement are subject to Lottery and State review and approval controls prior to payment.

The Lottery should immediately direct its contractor not to make any payments directly to Lottery employees. All valid Lottery employee expenses should be paid directly by the Lottery.

The Lottery's advertising contract should not be used by the Lottery to fund expenses of other Lottery operations.

Auditee Response:

We concur.

The Lottery has implemented a contract review team that will meet monthly. Management has notified employees of acceptable reimbursable items and how they must be submitted through the State process and include a sign off from either the Executive Director, Deputy Director, or Chief Financial Officer. Further, we advised the Advertising vendor to not make payments directly to employees.

Observation No. 2: Review Use Of Keno Proceeds

Observation:

It is not clear that the provisions of RSA 284:47 that direct a portion of the proceeds of the Keno lottery game to be paid to the Department of Health and Human Services (DHHS) are in compliance with the State Constitution.

RSA 284:47 Operation of Keno Games, II. states "... (a) One percent [of Keno proceeds] shall be paid to the department of health and human services to support research, prevention, intervention, and treatment services for problem gamblers."

Part 2, Article 6-b of the State Constitution states: "All moneys received from a state-run lottery and all the interest received on such moneys shall, after deducting the necessary costs of administration, be appropriated and used exclusively for the school districts of the state. Such moneys shall be used exclusively for the purpose of state aid to education and shall not be transferred or diverted to any other purpose."

While the Lottery reports that providing funds to help problem gamblers benefits the Lottery, as it helps provide a more favorable image of the Lottery, the Lottery could not demonstrate how DHHS' support of research, prevention, intervention, and treatment services for problem gamblers are a "necessary cost of administration" of the Lottery in accordance with Part 2, Article 6-b of the State Constitution.

Recommendation:

The Lottery should review with legal counsel whether the use of Keno lottery proceeds required by RSA 284:47 is in compliance with Part 2, Article 6-b of the State Constitution. If, upon review, the Lottery determines that a conflict exists, the Lottery should request an appropriate statutory revision.

Auditee Response:

We concur.

The question of whether part of the proceeds of Keno revenue, being dedicated to DHHS for responsible gaming, constituted a “necessary cost[s] of administration” of the Lottery was deliberated on during the hearing process of Keno legislative enactment at the House Ways and Means Committee and was ultimately deemed to be such. That being stated, the Lottery will seek an opinion as to this question of conflict of laws.

Observation No. 3: Complete The Development And Implementation Of The Games Of Chance Information System

Observation:

The Lottery’s Games of Chance information system failed during fiscal year 2018, requiring the Lottery to establish alternative procedures to track Games of Chance transactions. The Lottery’s Games of Chance information system included information on Games of Chance assessments and badge and license revenues totaling approximately \$2.3 million during fiscal year 2018. Lottery reported that the failure of the information system contributed to the Lottery not reconciling certain Games of Chance revenues during the second half of fiscal year 2018.

Lottery reports that while an information technology contractor is developing a new Games of Chance information system in coordination with a project to be used by other State agencies, employee turnover at the contractor and changing project requirements outside of Lottery’s control have resulted in the project being delayed.

Timely and accurate information is critical to secure agency operations. The absence of adequate information systems increases the risk that an agency may not become aware of, and react timely to, changes affecting operations.

Recommendation:

The Lottery should continue to monitor the completion and implementation of its Games of Chance information system to ensure the Lottery has the information, systems, and controls needed to securely manage its operations, including appropriate reconciliations.

Auditee Response:

We concur.

The Games of Chance Information System is a Department of Information Technology (DoIT) contracted project. As the project proceeded, delays were encountered beyond the control of the Lottery. As a result, the Lottery has been taking a more active role in the contract process by

attending bi-weekly meetings with the vendor and DoIT. The Lottery is continuing to use alternative means of recording data for Games of Chance until the new database is in place.

APPENDIX

Current Status Of Fiscal Years 2017 And 2016 Audit Findings

The following is a summary of the status, as of December 19, 2018, of the observations contained in the New Hampshire Lottery Commission Management Letters for the fiscal years ended June 30, 2017 and 2016. Those reports can be accessed at, and printed from, the Office of Legislative Budget Assistant website: www.gencourt.state.nh.us/LBA/AuditReports/FinancialReports.aspx.

		<u>Status</u>	
2017 Audit Comments			
Internal Control Comments			
Significant Deficiencies			
2017-1	Monitor Performance Of Reconciliation Controls <i>Review and reestablish, as necessary, reconciliation monitoring controls</i>	●	○
2017-2	Improve Game Draw Controls <i>Establish policies and procedures to ensure the draw process is sufficiently designed, and performed in a manner to maintain the reputation of the games (dropped game balls)</i>	●	●
2017-3	Mitigate ICS System Risks <i>Address the risk resulting from the lack of independence in its current internal control system</i>	○	○
2016 Audit Comments			
Internal Control Comments			
Significant Deficiencies			
2016-1	Expand Scope Of Service Auditor's Report <i>Request gaming-system service provider to expand the scope of its annual services auditor's report to include the identification and testing of controls that ensure the security and integrity of the Lottery's Fast Play games</i>	●	●
2016-2	Lottery Funds On Deposit With Treasury Should Be Credited With Interest <i>Request the State Treasury to comply with State statute and credit the Lottery Fund with interest earned on the Lottery's balances on deposit at the State Treasury</i>	●	○
2016-3	Improve Operation Of Controls To Ensure Ineligible Players Are Not Awarded Prizes <i>Review documented policies and procedures for prize claim payments to ensure they are complete and sufficiently detailed to provide the intended control</i>	●	●

2016-4	Improve Due Care Over Game Draw Activities <i>Improve controls, and level of due care, over the performance of all game draw activities (dropped game balls) (See Observation 2017 2)</i>	●	●
2016-5	Review Employer/Employee Status Of Workers Performing Tri-State Duties <i>Request the Department of Justice to again review whether the Tri-State Lottery and the New Hampshire Lottery should continue to be considered separate employers</i>	●	●
2016-6	Review Communication Controls <i>Design and implement controls that address the need for all levels of employees to be observant for anomalies in operations that potentially represent irregularities or other risks</i>	●	●
2016-7	Establish Controls Over Unclaimed Wager Revenue <i>Design and perform reasonable control activities to test the completeness and accuracy of unclaimed ticket revenue</i>	●	●
2016-8	Implement Controls For Timely Submission Of Distributor Fees <i>Establish policies and procedures to prompt Lucky 7 game distributors to comply with RSA 287-E:22 and submit Lucky 7 fees timely</i>	●	○
2016-9	Perform Lucky 7 Game Controls <i>Update policies and procedures and forms to include coverage of "electronic" tickets in reconciliations (See Observation 2017 1)</i>	●	○
2016-10	Accrue Accounts Receivable As Appropriate <i>Report all financial activity on the appropriate full-accrual basis</i>	●	●

State Compliance Comment

2016-11	Adopt Administrative Rules As Required By Statute <i>Adopt administrative rules as required by statute</i>	●	●
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Status Key

Count

Fully Resolved	●	●	9
Remediation In Process (Action beyond meeting and discussion)	●	○	4
Unresolved	○	○	1