

**STATE OF NEW HAMPSHIRE
SWEEPSTAKES COMMISSION**

**MANAGEMENT LETTER
FOR THE YEAR ENDED JUNE 30, 2001**

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, 2001 and have issued our report thereon dated November 30, 2001.

This management letter, a product of the audit of the New Hampshire Sweepstakes Commission for the year ended June 30, 2001, 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 presented in the fiscal year 2000 management letter of the Sweepstakes Commission.

Sweepstakes 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. Sweepstakes received GFOA certification for its 2000 CAFR, and it is believed that this CAFR will also conform to the certificate of achievement program requirements. A copy of the Sweepstakes Commission's 2001 CAFR can be obtained from the New Hampshire Sweepstakes Commission, 14 Integra Drive, Concord, NH 03301.

Office Of Legislative Budget Assistant

November 30, 2001

**STATE OF NEW HAMPSHIRE
SWEEPSTAKES COMMISSION**

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This report can be accessed in its entirety on-line at www.gencourt.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 as of and for the year ended June 30, 2001 and have issued our report thereon dated November 30, 2001. We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the New Hampshire Sweepstakes Commission'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 that are required to be reported under *Government Auditing Standards*. However, we noted an immaterial instance of noncompliance which is described in observation No. 6 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 Sweepstakes' 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 through No. 5 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 none of the reportable conditions referred to above are material weaknesses.

This auditor's report on compliance and on internal control over financial reporting is intended solely for the information 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

November 30, 2001

Internal Control
Reportable Conditions

Observation No. 1 - A Formal Information Technology Policy And Procedures Manual Should Be Developed

Observation:

Sweepstakes operates with no formal information technology (IT) policy and procedures manual. A comprehensive IT policy has not been established with documented procedures to address system operations, including, but not limited to, logical access, physical access, security, and change management.

As of July 1, 2000, Sweepstakes entered into an on-line service contract with a new vendor. The new gaming system involves new software, hardware, and procedures for Sweepstakes and all its retailers. This gaming system controls and reports all lottery game activity.

Sweepstakes is highly dependent on its IT systems to operate, not only the day-to-day functioning of the lottery games but the processing of financial activity, administrative data, and Bingo/Lucky 7 licenses. The more dependent agencies become on their computer systems to operate, the more crucial it becomes to have those systems documented and proper controls established. An IT policy and procedures manual allows management to identify those areas deemed critical to its operations and put into writing what is expected of the users and administrators of the system. This way, basic weaknesses and any departures from the established process can be detected and corrected in a timely manner.

Recommendation:

Sweepstakes management has the responsibility for instituting and monitoring an IT policy sufficient to protect the agency's resources and integrity. It is imperative that an IT policy and procedures manual be created to document and address critical aspects of its IT systems. The manual should be examined and updated periodically for systems and technological changes and communicated to all users.

Auditee Response:

We concur. The New Hampshire Sweepstakes Commission has operated under IT security requirements of the Multi-State Lottery (MUSL) Association, in addition to those requirements already in place, the New Hampshire Sweepstakes Commission will review IT security policies and manuals adopted by other state lotteries, and incorporate them into a New Hampshire Sweepstakes Commission "IT Manual of Procedures and Policies"(ITMPP).

Observation No. 2 - Disaster Recovery Plan Should Be Updated And Tested Periodically

Observation:

Sweepstakes' disaster recovery plan is outdated. The plan was last updated as of July 2, 1998, and does not encompass any new systems or changes to existing systems. An effective plan should allow continuity of future lottery operations with no or minimal interruptions in the event of an unforeseen future event or occurrence.

The purpose of a disaster recovery plan is to document plans and procedures in the event of a disaster, including disaster recovery strategies, essential resources, and procedures necessary to implement a recovery process. The lack of a plan would significantly lengthen Sweepstakes' recovery time, should a disaster or systems failure occur. It is important for Sweepstakes to maintain an effective plan, including regular testing of the plan, to minimize recovery time in the event of a disaster or systems failure.

Recommendation:

Sweepstakes should update and maintain its disaster recovery plan to address systems and technology changes. Sweepstakes should ensure that it has a thoroughly tested disaster recovery plan in place for all supporting systems and significant networks. A program of regular testing of key provisions should be part of the plan, including the testing of any other State agency's computer systems to be used as backup. The testing program should include critiques of the plan's effectiveness and the need for revisions to the plan and employee training in the operation of the plan. All employees should be trained in their roles and responsibilities relative to the emergency, disaster, and contingency plans.

Auditee Response:

We concur. The process of updating the disaster recovery plan is in process with an expected completion date by the end of the current fiscal year. The Y2K plan that was submitted to LBA in the Fall of 1999 is a viable plan. The agency will be testing the plan on an annual basis to gauge the adequacy and make changes as required to the disaster recovery plan.

Observation No. 3 - Review And Monitoring Of Instant Ticket Vendor Agreements Should Be Improved

Observation:

Sweepstakes has not thoroughly reviewed and monitored its agreements with its instant ticket vendor to understand the terms that were specified and agreed upon. As a result, transactions have taken place with this vendor that are not in Sweepstakes' best interest.

Sweepstakes prepaid \$50,000 during fiscal year 2001 for ten prize trips to Graceland for its “Elvis” instant ticket game even though the agreement with the vendor stipulated that the trips would be invoiced one-at-a-time as they were awarded. Per discussion with Sweepstakes, they were unaware of the one-at-a-time clause in the contract when payment was authorized for the \$50,000. The prize trips were not awarded until fiscal year 2002.

In addition, Sweepstakes has three unclaimed snowmobiles, costing \$25,995, from its “Chiller Thriller” instant ticket game that should be returned to the vendor. The “Chiller Thriller” instant tickets were sold in the fall/winter seasons of fiscal years 2000 and 2001. The agreement between the vendor and manufacturer states, “In the event that any snowmobiles are unclaimed, as defined by the Lottery’s regulations regarding unclaimed prizes, [manufacturer] will buy back said snowmobiles at the cost listed [in the contract].” Sweepstakes informed us that their intention is to transfer the snowmobiles to the Department Of Administrative Services to be sold as surplus property. Sweepstakes has not determined whether it has the legal right to return the snowmobiles to the instant ticket vendor for a full refund of the costs and related federal taxes. The \$25,995 cost includes \$5,283 in federal taxes prepaid by Sweepstakes on the winners behalf.

Sweepstakes has not required its vendor to adhere, nor has it adhered, to the terms of the above-mentioned agreements, and as a result, it incurred costs sooner than needed and risked losing thousands of dollars by not returning merchandise to the vendor for a full refund.

Recommendation:

Sweepstakes should thoroughly review its instant ticket agreements to gain a full understanding of all provisions and the responsibilities of the contracting parties. Sweepstakes should monitor and enforce compliance with all its vendor agreements to ensure decisions made are in Sweepstakes’ best interest. Any questions regarding contract provisions should be discussed with the Attorney General’s Office.

Auditee Response:

We concur. It is true the Commission paid for the Graceland trips upfront, however, there was no net effect to the game’s profits. The Commission will ask all managers responsible for the instant ticket program to more closely review contracts for proper enforcement. The Commission shall seek guidance from the Attorney General’s Office of the final disposition of the three snowmobiles.

Observation No. 4 - Provisions For Unclaimed MUSL Prizes Should Be Made In Determining Unclaimed Prize Liability

Observation:

Sweepstakes' current practice of recognizing the full liability of Multi-State Lottery Association (MUSL) prizes that are outstanding without consideration of those prizes that are unlikely to be claimed overstates the liability at June 30. MUSL on-line game prizes must be claimed within one year of the draw date or the prize is forfeited and recognized by Sweepstakes as profit. By not recognizing those prizes that are unlikely to be claimed Sweepstakes is overstating unclaimed prize liability and prize expenses and understating net income.

In lottery operations, there is normally a difference between the total amount of prizes won and the total amount of prizes actually paid because some winners never claim their prizes. In our fiscal year 2000 audit, we reported that Sweepstakes did not reduce its unclaimed prize liability account at year-end to reflect winning MUSL game tickets sold in New Hampshire that would not be claimed. Sweepstakes concurred with this observation, however, it did not develop an estimate to adjust the MUSL unclaimed prize liability of \$1.3 million reported in its fiscal year 2001 financial statements.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period.

In fiscal year 2000, Powerball (the primary MUSL game played in New Hampshire) represented 98% of MUSL unclaimed prize liability. At June 30, 2000, Sweepstakes recognized a Powerball unclaimed prize liability of \$1.3 million. During fiscal year 2001, we noted approximately \$1.2 million of the June 30, 2000 Powerball prize liability was never claimed and subsequently expired.

Sweepstakes' new on-line game system has the capability of tracking purges (expired unclaimed prizes). By using the reports generated from the system to measure past purges and project future unclaimed expired prizes, Sweepstakes should be able to develop a reasonable estimate for the year-end adjustment. Typically, lower tier prizes (i.e. \$3, \$4, \$7 and \$10) make up the majority of the unclaimed prize liability. We also noted that if a lower tier prize has not been claimed within three months of the draw date, the probability that the prize will be claimed decreases significantly.

If Sweepstakes does not develop a reasonable estimate to adjust the liability, this issue could have a material effect on Sweepstakes' financial statements for fiscal year 2002. The Powerball unclaimed prize liability is expected to exceed \$2.2 million as a result of increased sales from a \$295 million Powerball jackpot prize won in August 2001.

Recommendation:

Sweepstakes should develop a reasonable accounting estimate of unclaimed MUSL prizes. The amount to adjust the prize liability should be determined after a review of the history of total prizes won, purged prizes, and the percentage of prizes not claimed for recent fiscal years. Based on the estimate, an adjustment to the MUSL unclaimed prize liability account should be made at year-end to more accurately reflect the unclaimed prize liability in the financial statements for the reporting year. Sweepstakes should also consult with other MUSL states with regards to the accounting for their unclaimed prize liabilities.

Auditee Response:

We concur. The Sweepstakes Commission has been reviewing the data in the current fiscal year and will be presented to Bureau of Financial Reporting for proper action.

Observation No. 5 - Revolving Fund Reconciliation Should Be Improved

Observation:

Sweepstakes reported balance in its revolving fund account at June 30, 2001 was overstated by \$232,000 as a result of its failure to identify and properly adjust for prize payment activity at year-end. Sweepstakes' revolving fund account is used for payment of lottery prizes. The revolving fund account balance is set at \$500,000 and is replenished weekly by transfers from Treasury.

In our fiscal year 2000 audit we noted that Sweepstakes monthly revolving fund account reconciliations consisted of reconciling the general ledger account balance to \$500,000 and then reconciling the reported bank balance to \$500,000. It was the LBA's recommendation that Sweepstakes directly reconcile the revolving fund general ledger activity to the bank statements.

Sweepstakes discussed its revolving fund account reconciliation procedures with the Department of Administrative Services, Bureau of Financial Reporting (BFR). Based on BFR's recommendation, Sweepstakes began, during fiscal year 2001, to maintain its revolving fund balance in the general ledger at \$500,000 posting no monthly activity to the account.

Consequently, when Sweepstakes performed its June 30, 2001 reconciliation, it identified \$232,000 as a reconciling item, however, it failed to record the \$232,000 as an outstanding expenditure, instead labeling it as a deposit-in-transit. At June 30, 2001, these prize payment checks had neither cleared the bank nor been requested from the Treasury account, which resulted in the payments not being deducted from either the revolving fund general ledger balance of \$500,000 or the Treasury account general ledger balance, thereby overstating cash and understating prize expense.

While communication and coordination between Sweepstakes and BFR are highly encouraged and recommended, Sweepstakes needs to understand the financial impact of changes like this on

its financial statements. By failing to post monthly activity to the general ledger account, Sweepstakes inadvertently allowed an overstatement of cash and an understatement of expenses to occur.

Recommendation:

Sweepstakes should post the revolving fund monthly activity to the respective general ledger account. Additionally, Sweepstakes should perform a direct reconciliation of the revolving fund general ledger balance to the bank statement. This will help ensure that errors or frauds related to this account are noted and resolved in a timely manner.

Auditee Response:

We concur. The Sweepstakes Commission will continue to account for transfers in and out of revolving fund as current. At year-end we will reconcile and record adjusting entries to reflect the correct balance.

State Compliance

Observation No. 6 - Information Technology Plan Should Be Submitted Timely

Observation:

Sweepstakes does not have adequate procedures to ensure that it has a current and approved Information Technology Plan (ITP) on file with the Department of Administrative Services, Division Of Information Technology Management (DITM). All state agencies must have an approved ITP on file with DITM before spending funds totaling more than \$5,000 for information technology equipment, software, or services.

RSA 9:4-b requires each executive branch agency to prepare an ITP in accordance with the process established by the Director of DITM. The ITP process is intended to ensure that State agencies purchase computer systems that are compatible and are able to efficiently and effectively interchange information with other State systems. The ITP covering fiscal years 2002/2003 was due by October 1, 2001.

Sweepstakes' ITP for the 2000/2001 biennium was submitted 18 months late and due to unresolved issues, was never approved. Sweepstakes' 2002/2003 ITP was submitted to DITM in October 2001, returned to Sweepstakes in November 2001 for corrections, and finally approved on March 5, 2002.

Therefore, for over two years, Sweepstakes has run the risk of not being able to make any major technology purchases that may have been needed for its operations. As a result of not having an approved ITP, Sweepstakes was unable to update the Chief Accountant's computer or purchase a software package designed to monitor internet usage.

Recommendation:

Sweepstakes should develop procedures to ensure that its ITP is submitted to DITM in a timely manner. The plan should be submitted well in advance of the initial filing date to allow enough time for corrections and to ensure efficient continuation of Sweepstakes computer-based operations.

Auditee Response:

We concur. The Information Technology Plan was submitted in October of 2001. There were changes requested by the Division of Information Technology and these were corrected to their satisfaction. The Division of Information Technology did submit the plan to the Capital Budget Oversight Committee for the March 2002 meeting. Our plan was accepted with 12 other state agencies.

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, 2001 and have issued our report thereon dated November 30, 2001.

We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

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

Those issues that we believe are worthy of management consideration but do not meet the criteria of reportable conditions or noncompliance are described in observations No. 7 through No. 12 of this report.

This auditor's report on management issues is intended solely for the information 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

November 30, 2001

Management Issues

Observation No. 7 - GASB 34 Implementation Effort Should Be Coordinated With The Bureau Of Financial Reporting

Observation:

The Sweepstakes Commission should continue to coordinate its implementation of the Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments* with the Department of Administrative Services, Bureau of Financial Reporting (BFR) in order to establish a consistent basis of reporting on a statewide level.

There are various major reporting revisions and changes in accounting practices necessitated with the implementation of GASB 34, including report format revisions, fixed asset reporting, and reporting operations on a governmentwide basis as opposed to the traditional fund basis. The three areas where Sweepstakes should continue to work with BFR are addressed below.

- As part of the new reporting requirements, the State will now include fixed assets as part of the governmentwide balance sheet (previously governmental funds did not show fixed assets on the balance sheet but as part of a fixed asset account group). The State adopted a minimum threshold for reporting purposes of \$10,000 for equipment and \$100,000 for land and buildings. It has not required its enterprise fund agencies (i.e. Turnpikes, Liquor, and Sweepstakes) to use this threshold in their reporting. Sweepstakes currently maintains a \$100 capitalization threshold. Sweepstakes should coordinate with BFR the establishment of a common threshold.
- GASB 34 requires a comprehensive management discussion and analysis (MD&A). The MD&A will precede the financial statements and provide an analysis of the government's financial activities, including discussion of current year results in comparison to the prior year. This MD&A is similar to the letter of transmittal currently required by the Government Finance Officers Association (GFOA) as part of its certification program. Sweepstakes should work with BFR in development of its MD&A to provide consistency in presentation and analysis information. In order to avoid redundancy in this information, Sweepstakes should also seek guidance from GFOA as to what information will still be required in the letter of transmittal.
- Another component of GASB 34 is the presentation of new financial statements on a governmentwide basis and revisions to current report formats on a fund basis. Sweepstakes should work with BFR on the design and format of the new statements to provide consistency of presentation between itself, the other enterprise fund agencies, and the State's financial statements.

Recommendation:

Implementing the new GASB 34 standard requires significant planning. Sweepstakes should continue to coordinate with BFR to establish consistencies in reporting formats and accounting issues. Sweepstakes should discuss capitalization and depreciation of capital assets with BFR and consider increasing its capitalization threshold for equipment purchases.

Auditee Response:

We concur. The Sweepstakes Commission has and will coordinate with Bureau of Financial Reporting concerning this important subject. The Bureau of Financial Reporting does believe that we are in a good position for GASB 34 implementation due to the fact that we have produced a Comprehensive Annual Financial Report for the last four years.

Observation No. 8 - Sweepstakes Employees Should Be Prohibited From Playing Lottery Games

Observation:

Sweepstakes employees are allowed to participate in lottery games offered by Sweepstakes. This practice, however, is not consistent with general lottery industry practice, and is specifically disallowed by the Tri-State Lotto Commission and Multi-State Lottery Association (MUSL), both of which Sweepstakes is a member. Employees of the two joint lottery ventures are not allowed to participate in their organization's Tri-State or MUSL lottery games.

RSA 287-F:8, under the Tri-State Lotto Compact, states that no ticket shall be sold to and no prize shall be paid to any member, officer, or employee of the Tri-State Lotto Commission or their household members. This regulation also prohibits Sweepstakes' internal control system and drawing employees who work as Tri-State Lotto employees from participating in any Tri-State lottery games.

Rule 33 in the MUSL Rules defines ineligible players and specifies that a game ticket issued by MUSL or any of its Party Lotteries shall not be purchased by nor a prize won by a MUSL employee, officer, director or immediate family member residing in the same household.

To be consistent with its above member affiliations, general industry practice, and to preserve the integrity of the New Hampshire Sweepstakes Commission in appearance as well as in fact, Sweepstakes should prohibit its employees from participating in games that Sweepstakes sells or regulates. This will eliminate the appearance of impropriety in the event that a Sweepstakes employee should win a substantial lottery game prize.

Recommendation:

Sweepstakes should institute an internal policy to prohibit its employees from participating in any games for which it sells tickets or regulates. Sweepstakes should also seek legislation to establish this policy in law.

Auditee Response:

We concur. The Sweepstakes Commission will adopt an internal policy prohibiting employees from participating in any games for which the Sweepstakes Commission sells tickets or regulates. This would include Bingo and Lucky 7 games in the State of New Hampshire. We will review the request for legislation to establish this policy in law.

Observation No. 9 - Tri-State Wind-Up Provisions Should Be Formally Established

Observation:

Wind-up (i.e. dissolution) provisions have not been established for the Tri-State Lotto Commission organization. Additionally, the Tri-State contingency fund has not been reviewed to determine if the amount of the fund maintained remains suitable.

In our fiscal year 2000 audit we noted that the Tri-State Lotto Commission members had not established “wind-up” provisions for the organization. While the Tri-State Lotto Compact declares that a member state (New Hampshire, Maine and Vermont) may withdraw from the organization without rendering the compact invalid, the compact does not address how a member state may withdraw and the rights of a member state to any allocation of the retained earnings of the Tri-State Commission. Establishing policies and procedures in advance of actual events lessens potential conflicts and enables party states to know their rights and obligations should the status of the compact change. To date, Sweepstakes has not initiated discussion with the other member states on this issue.

The Tri-State Lotto Commission maintains a \$5 million contingency fund to be used in the event of an unforeseen judgment ordering the Tri-State Lotto Commission to pay a jackpot or large prize, or for any other unexpected occasion. The \$5 million contingency fund was set based upon average jackpots and has not been reviewed since it was established over a decade ago.

Recommendation:

Sweepstakes should initiate discussion with the other Tri-State Lotto Commission members to develop “wind-up” policies and procedures in the event that party states choose to withdraw from or ultimately dissolve the Tri-State Lotto Compact. Additionally, Sweepstakes should review with the Tri-State Lotto Commission the balance maintained in the contingency fund to determine if the \$5 million balance remains appropriate.

Auditee Response:

We concur. The Tri-State Commission will be asked to formalize a “wind-up” policy and review the \$5 million contingency fund to determine if this is an appropriate balance in this account.

Observation No. 10 - Liquor Commission Incentive Payment Policy Should Be Revised

Observation:

Sweepstakes’ practice of paying incentive checks directly to Liquor Commission employees is inconsistent with how it pays all other retailers who sell winning tickets.

RSA 284:21-s authorizes Sweepstakes to pay to retailers, as an inducement, cash incentives not to exceed 1% of the prize awarded or a maximum of \$30,000 for Powerball prizes or \$15,000 for other prizes, for selling a winning jackpot or high tier prize ticket. Incentives are only paid on prizes of \$10,000 or greater. Incentives are awarded for the following games: Powerball, Megabucks, Rolldown, and WinCash. With the exception of the Liquor Commission, incentive checks are issued directly to the licensed retail owner or corporate office of the store that sold the winning ticket. Any further distribution of incentive checks to employees is determined by the retail owner or corporate office who assumes all tax and income reporting requirement responsibilities.

In our fiscal year 2000 audit, we questioned the propriety of paying incentives to Liquor Commission employees and recommended that Sweepstakes seek legal advice on this issue. Sweepstakes sought legal advice from the Attorney General’s Office and it was their opinion that paying incentives to Liquor Commission employees was legal. While we no longer question the legality of paying incentives to Liquor Commission employees, we do question the method of payment. When Sweepstakes pays Liquor Commission employees directly for their proportional share of any incentives, Sweepstakes assumes the tax and income reporting responsibility rather than the Liquor Commission. When we questioned Sweepstakes on this issue, it conceded that if any other retailer were to make the same request (i.e. to pay employees directly), Sweepstakes would not accommodate the request.

We recognize that the incentive checks (\$2,200 and \$8,454 was paid to Liquor employees in fiscal years 2001 and 2000, respectively) are not significant amounts, however, the practice of paying Liquor Commission employees directly is inconsistent with how Sweepstakes pays all other retailers. Sweepstakes has no justification for this except that it has been a longstanding practice.

Recommendation:

Sweepstakes should review its policy of paying incentive checks directly to Liquor Commission employees and consider, at a minimum, changing its policy to one of paying the Liquor Commission directly, thus allowing the Liquor Commission the option and responsibility of paying its employees

or not. The division of the incentive check should be performed at the owner/administration level and not by Sweepstakes.

Auditee Response:

We concur. The Sweepstakes Commission will communicate to the Liquor Commission this position taken by the Office of Legislative Budget Assistant. The incentive check will be paid directly to the Liquor Commission and they will be responsible for paying the employees.

Observation No. 11 - Excess Funds Should Be Transferred From Powerball Unreserved Prize Fund

Observation:

Sweepstakes has excess funds in its Powerball Unreserved prize fund held by the Multi-State Lottery Association (MUSL). The excess funds should be transferred to Sweepstakes' Treasury account for use as working capital.

MUSL maintains a Powerball Reserve fund balance of \$77 million which acts as a contingency reserve to protect MUSL from unforeseen liabilities. The interest earned on the Reserve fund is credited to the Powerball Unreserved prize fund which is apportioned to each of the 22 member states. Sweepstakes' portion of the Unreserved prize fund equaled \$432,441 at June 30, 2001.

During fiscal year 2001, \$265,064 of interest earnings was credited to Sweepstakes' portion of the Unreserved prize fund. During fiscal year 2001, expenditures of \$231,302 were made from the Unreserved prize fund for Sweepstakes' portion of MUSL operating expenses, winning ticket incentive payments to lottery agents, and costs for the "Instant Powerball" television game show. Expenditures made from the Unreserved prize fund are at the discretion of the Sweepstakes executive director.

Sweepstakes' portion of interest earnings has been more than sufficient to pay for Sweepstakes' share of MUSL operating expenses. For this reason Sweepstakes' balance in the Unreserved prize fund continues to grow. Sweepstakes annually recognizes the interest income and expenses on its financial statements with the net amount due recorded as an accounts receivable. By failing to transfer the funds, Sweepstakes is, in effect, shortchanging itself working capital, as the net income from MUSL earnings is included in the annual transfers from the Sweepstakes Fund to the Education Trust Fund.

Recommendation:

Sweepstakes should transfer its excess Powerball Unreserved prize fund balance, held by MUSL, to Sweepstakes' Treasury account. Transferring the excess funds will allow Sweepstakes to recognize the "cash" and reduce the "accounts receivable" on its financial statements, as well as having the cash available for use as working capital.

Auditee Response:

We concur. The Sweepstakes Commission will request the transfer of excess cash from the Powerball Unreserved Prize Fund.

Observation No. 12 - Prohibition On Future Employment Statute Should Be Updated

Observation:

The Sweepstakes Commission's statute on prohibition of employment of certain employees by ticket or on-line vendors is outdated. RSA 284:21-u was established in 1987 and, except for a gender-neutral amendment, has not been updated since. RSA 284:21-u states in part that, "No commissioner, executive director, assistant director, or games manager of the sweepstakes commission shall accept any employment, ... with any ticket or on-line vendor holding a valid contract with the commission ... until 2 years after such person shall become separated from the commission." In addition, RSA 284:21-u does not allow an on-line vendor holding a contract with Sweepstakes to employ any of the above mentioned positions until 2 years after such employee has separated from Sweepstakes.

Since 1987, the organizational structure of the commission has changed and other positions beyond the four listed in statute have risen to the level of key management positions within Sweepstakes. These include the Information Technology Manager and the Administrator III. During fiscal year 2001, Sweepstakes lost its Information Technology Manager to its new on-line system vendor.

To maintain its commitment to public integrity, so necessary for a public lottery system, Sweepstakes should take every opportunity to ensure that its operations are regarded as being above reproach. By allowing key management personnel to accept employment with a contracting vendor, Sweepstakes lends itself to possible appearances of conflict of interest and the potential appearance of impropriety between itself and its significant vendors.

Recommendation:

Sweepstakes should review RSA 284:21-u and consider seeking amendment to the statute to expand the employment prohibition to include the Information Technology Manager and the Administrator III.

Auditee Response:

We concur. The Sweepstakes Commission shall inquire of other state agencies' restrictions on employment and will review RSA 284:21-u for possible changes.

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APPENDIX

Current Status Of Prior Audit Findings

The following is a summary of the status, as of November 30, 2001 of the observations contained in the management letter of the Sweepstakes Commission for the year ended June 30, 2000. 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.

Internal Control	Status
<i>Reportable Conditions</i>	
1. Expenses Charged To The Tri-State Operations May Not Receive The Oversight And Control Reviews Appropriate For A State-Run Organization	● ● ●
2. Controls Over Sweepstakes Prize Payment Disbursement Process Should Be Improved	● ● ●
3. Proper Business Relationships Between Employees And Vendors Should Be Safeguarded	● ● ●
4. Sales Office Accountability Should Be Improved	● ● ●
5. Reconciliation Process For Cash Accounts Should Be Improved (<i>see current year observation No. 5</i>)	● ○ ○
6. Delinquent Agent Accounts Should Be Monitored More Closely	● ● ●
7. Responsibilities For Adjustments To The Accounting Records Should Be Segregated	● ● ●
8. Control Over Returned Prize Payment Checks Should Be Enhanced	● ● ●
9. Checks Should Be Restrictively Endorsed Upon Receipt	● ● ●
10. The Authority For The Payment Of Incentives To Agents Who Cash Pick3/Pick4 Winning Tickets Should Be Clarified	● ● ●
11. Bingo And Lucky 7 Reporting Compliance Should Be Reviewed	● ● ●
12. Responsibilities For Collecting Revenues From Delinquent Agents And Waiving Fees For Bounced Electronic Fund Transfers Should Be Segregated	● ● ●
13. Provisions For Unclaimed MUSL Game Prizes Should Be Made In Determining Unclaimed Prize Liability (<i>see current year observation No. 4</i>)	○ ○ ○

Compliance Comment

14. Current Information Technology Plan Should Be Filed (*see current year observation No. 6*) ● ○ ○

Management Issues

15. Sweepstakes Must Gain A Better Understanding Of Its Participation In Its Joint Lottery Ventures (*see current year observation No. 9*) ● ● ○
16. Employment Status Of Sweepstakes Employees Hired By The Tri-State Lotto Should Be Reviewed ● ● ●
17. Communication And Coordination Of Efforts With The Department Of Administrative Services, Bureau Of Financial Reporting Should Be Improved (*see current year observation No. 7*) ● ● ○
18. The Propriety Of Paying Bonuses To State Liquor Store Employees Should Be Reviewed (*see current year observation No. 10*) ● ● ○

Status Key

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