STATE OF NEW HAMPSHIRE
STATE REVOLVING FUND

MANAGEMENT LETTER
FOR THE FISCAL YEAR ENDED JUNE 30, 2015

To The Fiscal Committee Of The General Court:

We have audited the financial statements of the New Hampshire State Revolving Fund as of and for the fiscal year ended June 30, 2015 and have issued our report thereon dated January 15, 2016.

This management letter, a byproduct of the audit of the State Revolving Fund (SRF) for the fiscal year ended June 30, 2015, contains our auditor's report on internal control over financial reporting and on compliance and other matters and related audit findings.

Also included in this management letter are the audit comments generated as a result of the fiscal year 2015 Single Audit procedures applied to the federal/State Clean Water and Drinking Water SRF programs. These comments are presented as they are reported in the State of New Hampshire's Single Audit report for the fiscal year ended June 30, 2015.

There is no status of prior audit findings appendix included with this report, as this was our first audit of the State Revolving Fund as a State enterprise fund.

The State Revolving Fund's fiscal year 2015 Annual Financial Report can be accessed online at:

http://www.gencourt.state.nh.us/LBA/AuditReports/FinancialReports/pdf/SRF_2015_FinRpt.pdf

Office of Legislative Budget Assistant

Office Of Legislative Budget Assistant

January 15, 2016

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STATE OF NEW HAMPSHIRE
STATE REVOLVING FUND
2015 MANAGEMENT LETTER

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* No audit 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 State Revolving Fund (SRF) which comprise the Statement of Net Position as of June 30, 2015 and the Statements of Revenues, Expenses, and Changes in Net Position and Cash Flows for the year then ended, and the related notes to the financial statements and have issued our report thereon dated January 15, 2016. Our report includes an emphasis-of-matter paragraph noting the SRF's adoption of Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting and Financial Reporting For Pensions,* as amended by GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date,* in the fiscal year ended June 30, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the SRF'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 SRF's internal control. Accordingly, we do not express an opinion on the effectiveness of the SRF's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph 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. However, as described in the following observations, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

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. We consider the deficiencies described in observations No. 1 through No. 4 to be material weaknesses.

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. We consider the deficiencies described in Observations No. 5 through No. 16 to be significant deficiencies.

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the SRF's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, rules, regulations, contracts, and grant agreements, 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.*

State Revolving Fund's Responses To Findings

The SRF's responses to the findings identified in our audit are included with each reported finding. The SRF'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 SRF'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 SRF's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Office of Legislative Budget Assistant

Office Of Legislative Budget Assistant

January 15, 2016

Internal Control Comments
Material Weaknesses

Observation No. 1: Establish Policies And Procedures To Support All Significant Operational And Financial Accounting And Reporting Activities

Observation:

The Department of Environmental Services (Department or DES) and State Revolving Fund (SRF) do not have documented policies and procedures covering significant aspects of the SRF operations. While the Department reports it has documented some task-specific processes, such as guidelines for processing a loan disbursement and entering a loan into the SRF's Project Manager accounting system, the Department does not have documented policies and procedures in place for significant areas of the SRF's operational and financial accounting and reporting activities, including:

- Accounting for and reporting the SRF as a State enterprise fund,
- Reconciling SRF data in Department accounting records to the same in the State accounting records,
- Accounting for and reporting debt,
- Accounting for project commitments and project costs,
- Capitalizing loan interest,
- Determining eligibility and accounting for principal forgiveness,
- Accounting for federal grant awards, set asides, and the state match,
- Providing loan amortization options for borrowers, and
- Estimating short-term receivables.

The Department acknowledged its documented policies and procedures for the SRF program were not complete during fiscal year 2015, and reported the accounting office was in the process of updating and formally documenting policies and procedures. However, the Department did not provide auditors with copies of documented policies and procedures of any significant nature related to the administration of the SRF.

The absence of effective policies and procedures detailing and controlling significant SRF operating and accounting activities results in a situation where compliance with management's intentions and directions for the program is dependent upon the knowledge and experience of the current employees. Without reasonably comprehensive policies and procedures in place, turnover in key SRF program staff positions could cause significant disruption to the SRF's financial operations.

Recommendation:

Management of the SRF should establish policies and procedures to support all significant operational and financial accounting and reporting activities. Coordination with the Department of Administrative Services, the State Treasury, and other parties should occur to ensure policies and procedures are complete, appropriate, and consistent with related State policies and procedures. Regular training, including cross training, should occur so the SRF can operate in a controlled and efficient environment and manner, even when there is turnover in key employee positions.

Employees performing nonroutine transactions should be encouraged to regularly reference the policies and procedures documentation to ensure they are performing their responsibilities as intended, and that the policies and procedures remain current and relevant to their duties.

Auditee Response:

Concur.

The SRF Program is now in the process of developing written policies and procedures. The SRF Program was unable to devote time to this effort this past fiscal year due to key accounting vacancies within the SRF Program. The SRF program has three key accounting positions and the two most senior positions were vacant for the majority of fiscal year 2015. The SRF Program, in operating with the above mentioned staff shortages, made a conscious decision to make financial reporting a priority. Developing policies and procedures was delayed as a result of our efforts to get the financial statements done in a timely manner. Now that the key positions have been filled, the SRF program has begun establishing current policies and procedures and will also continue to have staff cross trained.

Observation No. 2: Establish Policies And Procedures For Timely Posting Of Financial Transactions

Observation:

The SRF does not have policies and procedures to ensure that transactions are posted to the Project Manager general ledger in a timely manner and that an appropriate audit trail is created and maintained for all transactions that are recorded in the Project Manager information system.

The SRF's method of recording certain financial accounting transactions in the Project Manager system during fiscal year 2015 did not provide timely financial reporting for management decisions and other purposes, distorted the historical accounting record, and increased the risk that the historical record of transactions would be lost or considered unreliable.

During fiscal year 2015, the SRF posted the majority of its financial transactions to the Project Manager system in three batches in: August 2014, May 2015, and June 2015. Transactions should be posted as soon as practical, generally daily. Transactions that were recorded but held unposted in a pending status did not update account balances and could be changed without leaving an audit trail.

- For example, during fiscal year 2015, the SRF recorded transactions in the Project Manager system to revise the recorded funding sources of certain, previously issued loan disbursements. In recording the adjustments, the SRF effectively deleted the original entries and recorded the correcting entries using the prior date of record. Recording the entries in this manner, in essence, recorded the correcting entries as if they were the original transactions, effectively erasing the original entries and audit trail from the record.

The accounting record in all critical accounting systems should be posted timely to provide complete and reliable financial reporting. An accounting system that is not current and that allows the accounting record to be altered without establishing a complete audit trail is at an increased risk of not being reliable for management's use in understanding the results of operations, current balances, cash flows, and investment opportunities and is at an increased risk of being used to perpetrate or obscure errors or frauds.

Recommendation:

The SRF should establish policies and procedures for recording transactions in the Project Manager system, including adjusting and other correcting entries, that ensures transactions are posted timely and a complete historical accounting record is preserved.

Auditee Response:

Concur.

As a result of the SRF Program's staffing shortages during most of fiscal year 2015, monthly journal entry transactions were posted as timely as possible, and all data were entered into the Project Manager database daily in order to maintain accurate loan balances. The SRF Program will ensure that its written policies and procedures include timelines for the posting of all types of transactions. The SRF Program will also develop monthly trial balances.

Observation No. 3: Establish Policies And Procedures For The Regular Reconciliation Of Information Systems

Observation:

As of June 30, 2015, the SRF had not fully reconciled the Project Manager accounting and information system to similar information contained in the State's accounting system, NHFirst, since the SRF was designated as a separate enterprise fund at the start of fiscal year 2014. The SRF uses Project Manager as its primary system to account for and report the SRF loan program, including generating and supporting SRF financial statements and reporting SRF program activity to the federal grantor agency. While NHFirst also accounts for much of the financial information contained in Project Manager, NHFirst does not contain certain loan balance and related non-cash financial information accounted for in Project Manager.

An effective reconciliation process would likely have allowed the SRF to timely detect and correct a significant reported cash balance misstatement at June 30, 2014 and June 30, 2015.

Auditors proposed, and the SRF recorded, a correcting adjustment to the June 30, 2015 financial statements (see Observation No. 4).

Reconciliation of financial information in parallel systems is a primary control to ensure that systems report consistent information to reduce the risk of inaccurate and incomplete recording of transactions. The failure to perform reconciliations of critical information systems presents a material risk of erroneous information not being detected and corrected in a timely manner.

Recommendation:

The SRF should establish policies and procedures for the regular reconciliation of the common data in its Project Manager and NHFirst information systems. The results of the reconciliations, including the resolution of any identified differences, should be reviewed and approved timely by a supervisor knowledgeable of the information in the systems.

Auditee Response:

Concur.

The SRF Program is working with the Department of Administrative Services to be given access to the NHFirst general ledger module in order to be able to see Company 18 [State Revolving Fund] balances in NHFirst, which will allow the SRF Program to perform the recommended reconciliation.

Observation No. 4: Establish Policies And Procedures To Account For And Report State Match Transactions

Observation:

The SRF did not establish effective policies and procedures to account for and report bond proceeds intended to match federal grant revenue during fiscal years 2014 and 2015.

In December of fiscal year 2014, the State issued $18,965,000 of general obligation bonds to finance the State match to federal program funds drawn for certain Clean Water and Drinking Water project loans. The bond proceeds were reported as a cash balance in the SRF’s fiscal year 2014 financial statements. Prior to the bond issue, the State match was funded by State General Fund appropriations.

During fiscal years 2014 and 2015, the SRF paid the State match from Capital Project Fund appropriations but did not charge the bond proceed cash account for the disbursements. As a result, the SRF’s bond proceed cash account did not reimburse the State’s Capital Project Fund account for the disbursed State match amounts. To correct the reported funding source for fiscal year 2014 and 2015 State match amounts, auditors proposed, and the SRF recorded, a material audit adjustment to the June 30, 2015 financial statements.

The fact that the SRF did not recognize that its bond proceed cash balance did not reflect a significant reduction for its matches to drawn federal funds indicates a lack of understanding and monitoring of the intended accounting for the transactions.

While other State entities including the State Treasury and the Department of Administrative Services also should have recognized that the SRF was not properly accounting for the bond transactions, the responsibility for establishing appropriate policies and procedures to account for and report the transactions rests with the SRF.

Recommendation:

The SRF should establish policies and procedures to account for and report State match transactions funded from bond proceeds. The policies and procedures should include appropriate control activities, information sharing, and monitoring controls to reasonably ensure that the transactions will be accounted for and reported in accordance with management's intentions and State appropriations.

The SRF should coordinate its policies and procedures with the Department of Administrative Services and the State Treasury to ensure that those policies and procedures align with and support the State's policies and procedures for recording and reporting similar financial activity.

Auditee Response:

Concur.

DES has worked diligently with the Department of Administrative Services and the State Treasury to ensure that cash transfers within the NH Banking system have been completed for the State match portion. The bond proceeds have been completely spent and the entire amount of the bond proceeds have been transferred to the appropriate bank accounts. There will be a fiscal year 2017 bond issue and the SRF Program will have applicable written policies and procedures in place prior to that time.

Significant Deficiencies

Observation No. 5: Establish Policies And Procedures For A Formal Bank Reconciliation Process

Observation:

The SRF's bank balance to cash account reconciliation process was neither complete nor timely during fiscal year 2015.

The SRF holds cash balances in nine separate bank accounts. During fiscal year 2015, the SRF maintained separate federal clearing accounts, loan repayment accounts, and short-term investment accounts for both the Clean Water and Drinking Water program activity. Both Clean Water and Drinking Water management fees are deposited into a pooled State Treasury account and commingled with cash from other State agencies. The SRF uses this account primarily to fund administrative costs. The cash balance in the State Revolving Fund at June 30, 2015 was $257.9 million.

During fiscal year 2015, the State Treasury was responsible for the reconciliation of the bank statements to the NHFirst general ledger cash accounts and the SRF was responsible for reconciling the bank statements to the Project Manager cash accounts.

We noted the following weaknesses in the SRF cash account reconciliations.

1. The SRF did not reconcile the pooled management fee bank account to Project Manager during fiscal year 2015, in part because the SRF did not have access to sufficient bank account information to identify its financial activity in the account. The SRF reported its book balance in the management fee account at June 30, 2015 was $10.8 million.

2. The SRF reports it did not document its reconciliation of investment account activity or balances recorded in Project Manager to the bank, because of the relatively low level of activity in the accounts. In addition to monthly investment income postings, the investment accounts also included a $50 million short-term investment transaction with the State Treasury and semi-annual debt service payments totaling $2.6 million for fiscal year 2015. The combined balance in the investment accounts at June 30, 2015 was $174.5 million.

3. Project Manager cash account reconciliations have carried relatively small ($502 to $52,682) unresolved reconciling items for a period of years, including book balances that don't agree to the Project Manager trial balance. The SRF reports that it is aware of the unresolved differences, however it has not had the time to research and resolve the differences.

4. Bank balance to Project Manager cash account reconciliations were not performed monthly during fiscal year 2015. The reconciliations for the months of July through November 2014 were performed in December 2014, reconciliations for the months of December 2014 through May 2015 were performed in June 2015, and the reconciliation for the month of June

2015 was performed in July 2015. Untimely bank reconciliations can delay the detection and correction of errors.

5. The SRF has not established policies and procedures for a formal bank reconciliation process that includes full documentation of reconciliations by both the preparer of the reconciliation and a reviewer and approver of the reconciliation. The absence of a documentation of the performance and acceptance of the reconciliation control procedure increases the risk that the control will not be performed as designed.

Recommendation:

The SRF should establish policies and procedures for a formal bank reconciliation process that includes full documentation of reconciliations by both the preparer of the reconciliation and a reviewer and approver of the reconciliation. All cash and investment accounts should be reconciled at least monthly. The SRF should request copies of the State Treasury's monthly reconciliations of the bank balances to NHFirst balances to inform and supplement the SRF reconciliations. The SRF should consider restructuring its cash accounts in the Project Manager system to better align with its bank accounts to make the reconciliations and review of those accounts more efficient.

The SRF should request the State Treasury to establish a separate bank account for management fees. A separate bank account will allow for a reconciliation of the entire SRF cash bank balance to the Project Manager cash accounts and improve the reliability of the financial statements.

Auditee Response:

Concur.

The SRF Program reconciled receipts and disbursements between Project Manager and NHFirst for the management fee accounts. Because the pooled account is a statewide bank account and funds from all agencies are credited there, only the State Treasury can perform this reconciliation and the SRF Program has relied on the Treasury Department's reconciliation. The SRF Program has worked with the State Treasury to establish separate bank accounts for management fees and will perform a cash reconciliation of every SRF cash bank balance with the Project Manager cash accounts now that these new accounts are operational.

The SRF Program will develop written policies and procedures for this process, which will include documenting the preparation and review of reconciliations.

Observation No. 6: Establish A Formal Risk Assessment Process

Observation:

The Department and SRF program reported they did not have a formal risk assessment process in place during the fiscal year ended June 30, 2015. According to the Department, while there was no formal written risk assessment process in place, issues affecting the operation of the Department and SRF, including identified risks, were regularly considered.

The lack of formal policies and procedures for actively reviewing for and considering risk places the Department and SRF program in a largely reactive mode where it responds to disruptive events as they may occur.

The purpose of an entity's risk assessment efforts is to identify, analyze, and where appropriate, respond to risks and thereby manage risks that could affect the entity's ability to reach its objectives. An effective and documented risk assessment process should be a core element of management's controls.

Recommendation:

The Department and SRF program should establish a formal risk assessment process supported by policies and procedures for recognizing, evaluating, and responding to risks that could affect their ability to reach their objectives.

The Department and SRF program should regularly review their financial and operational activities for indicators of risk exposure, and establish and monitor controls that appropriately address those risks. Department employees with particular areas of expertise and knowledge of Department and SRF program operations should participate in the review to ensure that details of operations that may not be obvious to management are appropriately considered.

Auditee Response:

Concur.

DES and the SRF Program will work to establish a formal risk assessment process, including written policies and procedures for conducting risk assessments, and will conduct a risk assessment pursuant to those policies and procedures.

Observation No. 7: Continue With Rewrite Of Continuity Of Operations Plan

Observation:

In April 2015, the Department communicated that its continuity of operations plan (COOP), a combined COOP and disaster recovery plan, was undergoing a major rewrite during the audit period, as requested by the New Hampshire Homeland Security and Emergency Response

Group. According to a further, January 4, 2016, communication, no updates had been made to the plan since April 2015.

A business continuity plan describes an organization's roadmap for continuing operations under adverse conditions, including situations where an organization faces an unanticipated vulnerability.

A disaster recovery plan describes procedures and assigns responsibilities for reacting to and recovering from a natural or other disaster such as the loss of a critical asset.

The plans can be combined into one comprehensive document if the objectives of each are suitably addressed.

Recommendation:

The Department should continue with the rewrite of their COOP/Disaster Recovery Plan to ensure the plan addresses the objectives of both a continuity of operations and a disaster recovery plan, and the plan is suitable for its purpose.

The Department should regularly review and compare the provisions in the plan with their current financial and operational activities to ensure the plan adequately addresses their objectives and remains current.

All significant aspects of the plan should be periodically tested to ensure that the plan remains relevant and Department employees with particular areas of expertise and responsibilities critical to the success of the plan are knowledgeable of and trained in its application.

Auditee Response:

Concur.

The existing COOP is operational and working well. The COOP identifies the SRF Program as a mission critical function if there is an event that triggers the COOP. The SRF Program staff maintain "go kits" to ensure that they will have access to all essential materials during a COOP event, and their contact information is regularly updated within the COOP. DES, at the request of the Division of Homeland Security and Emergency Management (HSEM) is currently updating the COOP to conform with a new template provided by HSEM. The substantive content of the DES COOP will remain largely unchanged through this process, as it already adequately addresses all key needs identified by HSEM and DES. This update is anticipated to be completed within calendar year 2016.

Observation No. 8: Establish Policies And Procedures For Investment Of Excess SRF Funds

Observation:

The SRF did not have policies and procedures for managing its investment of excess SRF funds during fiscal year 2015. The SRF did not have internal policies and procedures for actively monitoring and projecting cash flow needs and investable balances and could not demonstrate that it had current, executed investment guidelines with the State Treasury covering its investment of excess SRF funds. Pursuant to a memorandum of agreement with the State Treasury dated May 2011, investment guidelines were to be developed by Treasury and reviewed with and approved by the Department of Environmental Services periodically to determine appropriate investments for excess SRF funds. The lack of current and vetted guidelines increases the risk that the State Treasury's investment activity will not meet the SRF needs, and risk and return profile.

Federal program regulations direct that excess SRF program funds be invested in interest-earning devices. During fiscal year 2015, the SRF's excess funds were primarily held in bank demand deposit accounts. At June 30, 2015, approximately $159 million of SRF funds were deposited in demand deposit accounts earning 0.20% interest. Other amounts were invested in mutual fund money market accounts. During this period, the rate of return on those accounts, which often held balances of $15 million, was approximately 0.11%. According to the SRF, the State Treasury is responsible for managing the SRF bank accounts, and will periodically inquire as to the anticipated cash needs of the SRF and the available balance for investment purposes.

Recommendation:

The SRF should take increased responsibility for managing the investment of excess SRF funds to ensure an optimal return on the investment of its excess cash. The SRF should establish policies and procedures for actively monitoring and projecting cash flow needs and investable balances and ensure that it maintains current, comprehensive, and executed investment guidelines on file with the State Treasury covering its criteria for the investment of excess SRF funds.

Auditee Response:

Concur.

The SRF Program will develop written policies and procedures documenting the frequency and factors to be considered in its consultations with the State Treasury regarding investment of excess SRF Program Funds. By statute, all such investments are managed by the State Treasury, and the SRF Program does not anticipate managing such investments directly. The SRF Program will ensure that its Memorandum of Agreement with the State Treasury, including the associated agreed-upon investment guidelines, is kept up-to-date.

Observation No. 9: Reassign Incompatible Responsibilities

Observation:

A segregation of duties weakness exists in the SRF business office as one employee is responsible for a number of incompatible functions without suitable mitigating controls over the resulting risks.

During fiscal year 2015, one SRF employee was responsible for receiving and maintaining custody of checks received from borrowers, recording receipts and disbursements in the NHFirst and Project Manager information systems, and reconciling monthly receipts and disbursement activity recorded in those systems. In addition, this employee also was involved in setting up bank account transfer information for transferring loan disbursements to borrowers.

Placing incompatible responsibilities with one employee position without sufficient and appropriate mitigating controls presents a significant risk of error and fraud and also increases the risk of disrupted operations in the event of unscheduled employee turnover in this position.

Recommendation:

The SRF should review and reassign as practical the incompatible responsibilities currently assigned to this employee. For those incompatible responsibilities that remain, the SRF should design appropriate mitigating controls to lessen the risk that errors or frauds could occur and not be detected and corrected in a timely manner in the normal course of business.

The SRF should also ensure that the scope of responsibilities placed with this employee is adequately documented to allow for continuity of operations in the event of unscheduled employee turnover in this position.

Auditee Response:

Concur.

As a general matter, the SRF Program believes appropriate controls are in place, but it will review its work practices to reassign any incompatible responsibilities. Importantly, all reconciliations performed by the SRF business office personnel are reviewed by management. All receipt and disbursement activity is reviewed and approved by management on the day the activity occurs. It is again reviewed during the cash reconciliation process as well as the general ledger posting and reconciliation process.

The State Treasury is responsible for setting up bank account transfer information, for transferring loan disbursements to borrowers, and for managing all cash accounts for the Programs. DES is working with the State Treasury to see if additional control procedures would be appropriate.

Observation No. 10: Establish Appropriate Policies And Procedures For Determining And Reporting Accounts Receivable

Observation:

The SRF has not established policies and procedures for determining and reporting accounts receivable in its financial statements.

At June 30, 2015, the SRF reported approximately $4.6 million of current loan interest and management fee receivables and approximately $23.6 million of current and $346.5 million of noncurrent loans receivable. The SRF did not accrue federal grants receivable at June 30, 2015. The SRF reports accounts receivable anticipated to be collected within one year of the financial statement date as current and accounts receivable anticipated to be collected more than one year from the financial statement date as noncurrent, in accordance with the accrual basis of accounting.

We noted the following instances where the SRF was either not fully aware of the collectability of the accounts and balances included in its accruals or did not consider the need for reporting accounts receivable.

1. The SRF included $3.0 million of current loans receivable in the financial statements for loans that were in the disbursement phase and that, according to the usual repayment process, would not typically be collected in the current period (one year from the financial statement date). While recognizing a portion of this amount as current may be appropriate if based on an analysis of historical activity or other data, the SRF did not have support for its classification of the $3.0 million as current receivables.

2. The SRF incorrectly reported approximately $249,000 of loan interest and management fees collected prior to the financial statement date as accounts receivable at June 30, 2015.

3. The SRF did not accrue approximately $1.0 million of federal grant receivable on its June 30, 2015 financial statements even though the SRF recorded this federal receivable in the State's accounting system, NHFirst. The SRF reports federal revenues on its financial statements on the cash basis of accounting, contrary to generally accepted accounting principles which require reporting on the accrual basis of accounting for an enterprise fund such as the SRF.

The lack of policies and procedures for determining and reporting accounts receivable likely contributed to the difficulties experienced by the SRF in preparing its fiscal year 2015 financial statements.

Recommendation:

The SRF should establish appropriate policies and procedures for determining and reporting accounts receivable on its financial statements. The SRF should consider seeking assistance from the Department of Administrative Services, Bureau of Financial Reporting, if necessary to ensure that the policies and procedures establishing the basis of SRF's financial accounting and reporting are compliant with generally accepted accounting principles.

All accounting and financial reporting estimates prepared by the SRF, including determining and reporting accounts receivable, should be appropriately supported to ensure the estimates are reliable, consistent with program and financial policy and criteria, and accurately made.

Auditee Response:

Concur.

The SRF Program will establish written policies and procedures for determining and reporting accounts receivable, and for any estimates that are necessary for preparing the financial statements.

The SRF Program acknowledges that $243,000 of the $249,000 identified was incorrectly reported. The SRF Program will ensure that the interest and fee accrual worksheet is accurate and reviewed in the future.

With regard to the comment on the $3 million current vs. long term receivable classification, to date, during fiscal year 2016 at least $2.2 million of this amount has been received, thus providing substantial validation of the SRF Program's estimation methodology.

DES continues to work with DAS on all significant accounting policy decisions.

Observation No. 11: Institute Controls To Ensure Charge Rates Are Accurately Determined

Observation:

Audit testing identified instances where charge rates applied to some SRF program loans were not in full compliance with program administrative rules and loan agreements. The calculation and application of charge rates (loan interest and administrative fees) is described in the administrative rules for the SRF program and in the loan agreement documents.

Because of long-term loan repayment periods, errors made in the determination of charge rates can have an ongoing effect for up to a 30-year loan period. We noted the following issues in the SRF's setting of charge rates for Clean Water and Drinking Water loans.

<u>For loans closed during fiscal year 2015</u>:

1. Testing of charge rates applied to a sample of five Clean Water loans closed during fiscal year 2015 identified one loan (20%) where the charge rate was not the rate in effect at the execution date of the loan agreement, contrary to program administrative rules.

2. Testing of charge rates applied to a sample of seven Drinking Water loans closed during fiscal year 2015 identified two loans (29%) where the charge rate was not the rate in effect at the execution date of the loan agreements, contrary to program administrative rules.

<u>For loans closed prior to fiscal year 2015:</u>

1. The contracted supplemental loan agreement (SLA) charge rates for two out of a random sample of 22 loans (9%) in the Drinking Water program were not the charge rates the SRF used to invoice the borrowers. The two borrowers were overcharged approximately $25,000 and $2,000, respectively, during fiscal year 2015 and overcharged approximately $181,000 and $14,000, respectively, over the life-to-date of the loan as of June 30, 2015. A review of an additional sample of 20 loans revealed no similar errors.

2. Testing of charge rates applied to a random sample of 25 Clean Water loans identified 12 loans (48%) which had incorrect charge rates. For three of the loans (12%), the charge rate applied to the loans was derived from an incorrect market rate and for nine of the loans (36%) the charge rate applied to the loans was not the rate in effect at the execution date of the loan agreements, contrary to program administrative rules.

   A further review of the entire population of Clean Water loans in repayment status identified six additional loans that were based on an incorrect market rate.

3. Testing of charge rates applied to a random sample of 22 Drinking Water loans identified 15 loans (68%) which had incorrect charge rates. For one of the loans (4%), the charge rate was derived from an incorrect market rate and, for 14 of the loans (64%), the charge rate applied to the loan was not the rate in effect at the execution date of the loan agreements, contrary to program administrative rules.

   A further review of the entire population of Drinking Water loans in repayment status identified three additional loans that were based on an incorrect market rate.

Incorrect or misapplied charge rates result in borrowers paying incorrect amounts to the SRF.

Recommendation:

The SRF should review the cause of the above noted errors and institute controls to ensure charge rates as outlined in the SRF program administrative rules are accurately determined and consistently applied.

If the SRF determines the current program rules are not responsive to the programs, the SRF should act to implement appropriate rule changes. The SRF's policies and procedures for determining and applying charge rates should be clearly described in rule and supported by an appropriately designed review and approval function to promote accuracy and compliance with program rules and contractual understanding.

The SRF should review the above noted errors and correct, as appropriate, instances where borrowers are being overcharged. The SRF should review with legal counsel whether the SRF can correct the charge rates for ongoing loans in the event it determines it is also currently undercharging borrowers.

Auditee Response:

Partially concur.

For the two Drinking Water loans that were invoiced at a different charge rate than the contracted SLA rate, the SRF Program concurs and is currently working on a corrective action plan to appropriately credit the borrowers.

With regard to the question of whether the correct charge rate was used by the SRF Program, based on the auditor's interpretation of "execution date", we understand why the auditors have questioned what the appropriate rate to use is. Because different processes were used over time, the OLAs were dated at different times.

The SRF Program will work to update its administrative rules and to establish written policies and procedures to help ensure that such concerns do not arise in the future by more clearly articulating the process for review, acceptance and approval of the rates used in the loan agreements.

The SRF Program will also review with legal counsel the issues identified in Observation 11.

Observation No. 12: Implement Policies And Procedures To Ensure Access To The Project Manager System Is Appropriate Based On Employee Job Responsibilities

Observation:

A review of employee access authorities to the SRF Project Manager accounting and information system revealed that five out of 27 users reviewed (19%) had inappropriate or excessive access permissions, as further described below.

- One employee who had left Department employment on May 30, 2014 still had an active Project Manager system user ID as of the October 15, 2015 date of audit inquiry.
- The access permissions of two employees, who were temporarily granted increased permissions to the Project Manager system during a period of vacancies in the State Revolving Fund (SRF) accounting office, were not readjusted until the March 2016 time frame when the SRF accounting office was back at full staff.
- Two employees who had transferred to different positions within the Department and no longer work for the SRF programs retained project manager access to the SRF's Project Manager system. Users with project manager access can edit information in the project detail and project cost sections of the system.

Access controls should be designed to allow usage of data processing assets only in accordance with management's authorizations. Protection of these assets consists both of physical and logical access controls that prevent or detect unauthorized use, damage, loss, or modifications. Access to these resources should be limited to those individuals authorized to process or maintain a particular system. Access should be appropriate based on employees' job responsibilities, and incompatible functions should be appropriately segregated.

Failing to periodically review and monitor employee access to the Project Manager system increases the risk that unauthorized changes will be made to the system that will not be detected and corrected timely by management.

Recommendation:

The SRF should implement policies and procedures to ensure access to the Project Manager system is appropriate based on the employee's job responsibilities. Access should be periodically reviewed to ensure that access levels continue to remain appropriate, and that only current SRF employees maintain access.

Auditee Response:

Concur.

The SRF will ensure that its written policies and procedures include a periodic review of the appropriateness of staff access to and their access levels within the Project Manager system.

Observation No. 13: Draw Federal Funds At The Earliest Date Allowed

Observation:

The SRF's drawing of federal administrative funds continues to be problematic as the guidelines (policies and procedures) for the draws remain unclear, and the SRF did not consistently draw the administrative funds in accordance with its interpretation of the guidelines. The SRF's untimely drawing of administrative funds was also a comment in the 2013 and 2014 Single Audit Reports.

In accordance with the Treasury State Agreement (TSA) required by the federal Cash Management Improvement Act of 1990 (CMIA), the SRF administrative draws are to occur on a quarterly basis so that the period of expenses to be reimbursed is also a quarter, and "the state shall request funds for each fiscal quarter, such that they are deposited on the median day of the quarter… This funding technique is interest neutral." The CMIA is intended to ensure greater efficiency, effectiveness, and equity in the exchange of funds between the federal government and the states.

During fiscal year 2015, while the SRF interpreted the TSA to provide for a draw of federal administrative funds on the median day of the following quarter, the SRF drew administrative funds 60 to 90 days after that date. The plain reading of the TSA would require these funds to be drawn the median day of the current quarter, 90 days earlier than the date understood by the SRF, and 105 to 135 days earlier than the funds were drawn during fiscal year 2015.

Recommendation:

The SRF should draw federal funds at the earliest date allowed by the federal program or regulations.

The SRF should review the TSA with the State Treasury and the federal agencies to ensure that a correct understanding exists of the TSA conditions and that the TSA conditions appropriately serve and protect the State's interests by allowing the drawing of federal funds as close as possible to when the underlying disbursements are made. The SRF should ensure that it establishes policies and procedures that appropriately implement the TSA when drawing federal funds.

Auditee Response:

Concur.

Funds for fiscal year 2016 are being drawn quarterly in accordance with the existing TSA. DES is working with State Treasury to modify the TSA to allow the Department to draw funds for administrative expenses more frequently than quarterly. It should be noted that loan funds are drawn upon disbursement.

Observation No. 14: Establish Policies And Procedures To Encourage Timely Repayments

Observation:

The SRF did not aggressively pursue timely collection of loan repayments from borrowers during fiscal year 2015. While the SRF reported it re-invoiced delinquent payers, it did not apply late payment fees to delinquent Drinking Water program loans or default delinquent Clean Water program loans. We noted the following with regard to late payments received from borrowers during fiscal year 2015.

1. 82 of the 160 (51%) Clean Water program loan repayments processed during fiscal year 2015 were received from one to 234 days after the invoice due date. Fifteen of the 160 (9%) loan repayments, totaling $14,223,302, were received more than 30 days after the invoice due date.

2. 281 of the 670 (42%) Drinking Water program loan repayments processed during fiscal year 2015 were received from one to 275 days after the invoice due date. Twenty-eight of the 670 (4%) loan repayments, totaling $353,887, were received more than 30 days after the invoice due date.

Drinking Water loan agreements include provisions such as, “the Maker agrees to pay a late charge of five percent (5%) of the amount of any payment due under this Note that is not paid within seven (7) days of its due date.” The Clean Water loan agreements do not have similar language but do state, “upon default in the prompt and full payment of any installment of principal or interest on this Loan Agreement, the entire unpaid principal hereof and interest thereon to the date of payment shall immediately become due and payable upon the demand of the State of New Hampshire.”

According to the SRF, late payment fees are not charged and defaults are not issued, as the SRF “prefers to work with the borrowers to resolve late payments.”

While the SRF reports that it has historically collected all loan repayments due and has not had to pursue collections through litigation or other extraordinary means, untimely collections of loan repayments and abeyance of late fees negatively impacts the cash flows and balances of the loan programs.

Recommendation:

The SRF should establish policies and procedures encouraging borrowers to make timely repayments on outstanding loans. The SRF should consider charging late payment fees when allowed by rule and contract.

The SRF should review its internal communication of late payment information to ensure both the program management and the business office are made aware of loans that become delinquent so that they can take appropriate and timely action.

Auditee Response:

Partially concur.

The SRF Program will establish written policies and procedures regarding its collection practices. As a general matter, the SRF Program expects and encourages borrowers to make timely repayments on outstanding loans. The SRF Program actively monitors loan repayments to ensure that all repayments are collected. In addition, there are now regular communications between program management and the business office regarding loan balances and payments. Throughout the history of the SRF Program, there has never been a default on a SRF loan. The SRF Program takes seriously its responsibility to work collaboratively with its customers, most of which are municipalities and other governmental entities, to help them cost effectively provide essential drinking water and wastewater services to their residents and customers. Because the SRF Program is a governmental program that serves other governments, many of which are very small communities or water systems and may not be able to obtain water project financing from any other source, and may for cash flow purposes be heavily dependent on timely receipt of payments from their customers, the parties must work very closely together. For these and other reasons, the SRF Program would not be comfortable adopting a written policy that would require the SRF Program to routinely charge late fees if repayments are not timely. While there may be very limited circumstances under which charging late fees could be appropriate, this would not be a standard practice for the SRF Program. Rather, the written policies and procedures will document a set of approaches that emphasize the current practices of staying in close communication with borrowers, recognizing that most borrowers make timely payments.

Borrowers that are late in making payments are contacted and closely tracked, and this practice has always resulted in their accounts being brought up to current.

Observation No. 15: Principal Forgiveness Should Be Recorded In Accordance With SLAs And Be Subject To Review And Approval

Observation:

There are no formal, policies and procedures to ensure loan repayment schedules are accurately recorded in the SRF Project Manager system and to ensure principal forgiveness is consistently recorded in the Project Manager system in accordance with the provisions of the supplemental loan agreements (SLAs).

Outstanding loan balance and repayment information is determined at the end of a project's construction period and is documented in the SLA. The SLA identifies a loan balance outstanding, representing the amount borrowed under the original loan agreement (OLA) and any unpaid interest that accrued during the OLA period; any grant of principal forgiveness, and when the amount forgiven is recognized; the interest rate to be applied to the loan; and the repayment schedule for the outstanding principal and interest.

1. According to the SRF, a borrower's eligibility for principal forgiveness is initially determined at the time of the OLA, but the amount of forgiveness is not guaranteed until the eligibility is finally determined at the time of the SLA. Principal forgiveness is finalized as a percentage applied to the total disbursed amount in the SLA and a repayment schedule, recognizing the principal forgiveness, is attached in the exhibits to the SLA.

    - In one out of seven Clean Water program loans tested (14%), $2.0 million of principal forgiveness was awarded to a municipality, even though the borrower paid off the loan prior to the execution of a SLA. There was no documentation provided to evidence SRF management agreed to granting of principal forgiveness prior to a SLA, even though this was contrary to the SRF's regular stated practice.

2. According to the SRF, there are no formal, written review or approval controls in place to ensure the loan repayment schedules input into the Project Manager system are in accordance with the SLA. Loan terms are communicated by the Program Managers to the business office for input into the Project Manager system. There is no subsequent documented review of the repayment schedule to confirm the accuracy of the data provided or the accuracy of its entry into the Project Manager system. This places an undue reliance on the Project Manager system for compliance with the SLA repayment provisions.

- In three out of 10 Drinking Water program loans tested (30%), the principal forgiveness amount shown on the Project Manager repayment schedule did not agree to the SLA. The differences between the Project Manager repayment schedule and the SLA ranged from a $133 understatement to a $2,092 overstatement of the amount forgiven according to the SLA. The SRF indicated the cause of the differences is often due to system complications when large amounts of principal forgiveness are awarded.
- The Project Manager system does not revise all components of the loan repayment schedule (principal, interest, management fees, principal forgiveness, and carrying value of the loan) when a borrower makes unscheduled additional principal payments. For example, while prepayments of principal amounts can shorten the life of the loan, the Project Manager system does not revise the amortization of loan forgiveness, resulting in a delayed recognition of loan forgiveness, an overcharge of loan interest and management fees, and likely requiring a manual adjustment of the principal forgiveness balance at the termination of the loan.

Recommendation:

The SRF should review, evaluate, and document its current practices to determine and record loan repayment schedules to improve initial and continued compliance with the loan agreements. The practices should be consistently applied to all loans.

The SRF should establish a review and approval process over the repayment schedules to better assure compliance with loan agreements. The review should be performed subsequent to the execution of the SLA to confirm compliance with SLA conditions and be documented. All revisions to repayment schedules should be reviewed and approved.

The SRF should determine whether the reporting from the Project Manager system can be revised to update all components of a loan repayment schedule, including principal forgiveness, when unscheduled additional principal payments are received from a borrower.

The SRF should prepare an SLA or other loan closing document for all loan projects that reach the completion stage or whose conditions otherwise are no longer covered by OLA provisions. The DES exposes itself to increased risks of disagreements with, and challenges from, borrowers when loans agreements are not fully documented.

Auditee Response:

Concur.

The SRF program will develop written policies and procedures to better document loan closures. The SRF Program will also work with the vendor to see if upgrades to Project Manager can be made to better handle the amortization of loan forgiveness.

It should be noted that a SLA for projects that pay their loan balance off in full prior to loan closure is not necessary. Every loan is covered by OLA provisions until an SLA takes the place of an OLA. The SRF Program will modify the process to require that documentation be placed in the file indicating the agreement of the recipient and the SRF Program to close out the project, and this will be reflected in the written policies and procedures.

Observation No. 16: Implement Policies And Procedures To Record Revenue In The Audit Fund Set-Aside Account

Observation:

The SRF did not contribute required amounts into the audit fund set-aside account during fiscal year 2015.

Pursuant to RSA 124:16, *Funds Set Aside* - Every state department, board, institution, commission or agency which receives federal funds shall set aside an amount equal to the rate approved in the statewide indirect cost plan of the funds received. The amount set aside shall be used to pay for financial and compliance audits as required by the federal government or by state statute.

Pursuant to the *Statewide Indirect Cost Allocation Plan* (excerpt) **-** The federal financial participation (FFP) for each federal financial assistance program administered by state agencies is one-tenth of one percent (.001) of all funds or items of value received from the federal government, including federal financial assistance programs under the American Recovery and Reinvestment Act of 2009 (ARRA) administered by state agencies. The FFP shall be one-tenth of one percent of the funds or items of value received without regard to match ratios or state financial participation.

The SRF received approximately $47 million in federal funds during fiscal year 2015, which would require approximately $47,000 to be deposited into the State's audit fund set-aside account. The SRF recorded $3,000 in the set aside account during fiscal year 2015, approximately $44,000 less than the amount required by statute and the *Statewide Indirect Cost Allocation Plan*.

Recommendation:

The SRF should implement policies and procedures to ensure that the appropriate amount of revenue is recorded in the audit fund set-aside account, as required by RSA 124:16, and the *Statewide Indirect Cost Allocation Plan*.

Auditee Response:

Concur.

The SRF Program will develop written policies and procedures that will ensure that the appropriate amount of revenue is remitted to the audit fund set-aside account.

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Federal Single Audit Comments

The following are federal compliance comments developed by Legislative Budget Assistant auditors in performing fiscal year 2015 Single Audit procedures for the federal Clean Water State Revolving Fund and Drinking Water State Revolving Fund programs operated by the Department of Environmental Services (DES). These comments are presented in the format suggested by federal Single Audit guidance. The comments are included in the management letter to report auditor communications related to the operation of the SRF program during fiscal year 2015.

Single Audit Comment No. 1: Noncompliance With Applicable Funding Technique Over Administrative Costs In The Treasury-State Agreement

U.S. Environmental Protection Agency	***Finding: 2015-041***
N.H. Department of Environmental Services	
CFDA #66.468 Capitalization Grants for Drinking Water State Revolving Funds (DWSRF)	
Grant Year and Award:	
2012 ***FS991150-12***	
2013 ***FS991150-13***	
2014 ***FS991150-14***	

Finding: Noncompliance with applicable funding technique over administrative costs in the Treasury-State Agreement

Criteria:

U.S. Department of Treasury (Treasury) regulations at 31 CFR part 205, which implement the Cash Management Improvement Act of 1990 (CMIA), as amended (Pub. L. No. 101-453; USC 6501 et seq.), require State recipients to enter into agreements that prescribe specific methods of drawing down Federal funds (funding techniques) for selected large programs. Annually, the State of New Hampshire negotiates the Treasury-State Agreement (TSA) with the Treasury which details the funding techniques to be used for the drawdown of federal funds and the terms for the transfer of financial assistance funds between the Federal government and the State of New Hampshire.

Administrative Costs:

In the TSA for the period July 1, 2014 – June 30, 2015, the funding technique agreed upon was the Cost Allocation Plan - Quarterly. This technique states that the State shall request funds for each fiscal quarter, such that they are deposited on the median day of the quarter. The amount of the request shall be based on the actual allocation of costs for that quarter.

Condition:

The DWSRF program did not comply with the applicable funding technique specified in the TSA for administrative costs. During fiscal year 2015, DWSRF drawdown requests were performed for April 2014 expenditures in July 2014, for May and June of 2014 expenditures in August 2014, and, for the remaining months during the fiscal year, the drawdowns were performed quarterly. A similar finding was noted in the prior single audit report.

Cause:

For the administrative costs of the DWSRF, the Department of Environmental Services (DES) did not perform the administrative draws in accordance with the TSA.

Effect:

DES was not in compliance with the funding technique specified in the TSA.
Questioned Costs:

None

Recommendation:

DES should review the TSA prior to requesting funds, to ensure the approved clearance patterns for administrative costs are met. DES should establish procedures to ensure drawdowns are performed quarterly, as prescribed in the TSA.

Auditee Corrective Action Plan:

DES concurs. The DWSRF set-aside funds for FY2016 are being drawn quarterly in accordance with the existing TSA. DES is working with Treasury to modify the 2016 TSA to allow for more flexibility with drawdowns (as needed but no less than quarterly).

Contact Person:

Sarah Pillsbury, Administrator, Drinking Water Ground Water Bureau

Anticipated Completion Date:

June 30, 2016

Single Audit Comment No. 2: Lack Of Appropriate System Access Permissions Controls

U.S. Environmental Protection Agency		***Finding: 2015-042***
N.H. Department of Environmental Services		
CFDA #66.458 Capitalization Grants for Clean Water State Revolving Funds (CWSRF)		
CFDA #66.468 Capitalization Grants for Drinking Water State Revolving Funds (DWSRF)		
Grant Year and Award:		
2010	***FS991150-10 (DWSRF)***	
2011	***CS330001-11 (CWSRF),***	***FS991150-11 (DWSRF)***
2012	***CS330001-12 (CWSRF),***	***FS991150-12 (DWSRF)***
2013	***CS330001-13 (CWSRF),***	***FS991150-13 (DWSRF)***
2014	***CS330001-14 (CWSRF),***	***FS991150-14 (DWSRF)***

Finding: Lack of appropriate system access permissions controls

Criteria:

OMB Circular A-133, Subpart C – Auditees**,** §___.300 (b) states that the auditee shall "maintain internal control over Federal Programs that provides reasonable assurance that the auditee is managing Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its Federal programs."

Information system access controls should be designed to allow usage of data processing assets only in accordance with management's authorizations. Protection of these assets consists both of physical and logical access controls that prevent or detect unauthorized use, damage, loss, or modifications. Access to these resources should be limited to those individuals authorized to process or maintain a particular system. Access should be appropriate based on employees' job responsibilities, and incompatible functions should be appropriately segregated.

Condition:

Access permissions to the DES' Project Manager system are not appropriately limited.

The Department of Environmental Services (DES) Project Manager system is a Microsoft Access-based software application designed to manage the financial and technical aspects of water quality projects that the State is helping to finance. The software was designed specifically for the CWSRF and DWSRF programs. The Project Manager system has built-in security that verifies a user each time they open the program. This security system is based on defined user roles within the program. Security roles limit users to performing certain functions. The system administrator is responsible for establishing both the user accounts and the assigned security roles within the system.

Both CWSRF and DWSRF program staff, as well as select DES accounting office staff, have access to the Project Manager system. The system does not restrict access by program (CWSRF or DWSRF). A review of DES personnel who have access to the Project Manager system, and their related access levels, revealed that five out of 27, or 19%, of users had inappropriate or excessive access permissions, as further described below.

- One employee who had left Department employment on May 30, 2014 still had an active Project Manager system user ID as of the October 15, 2015 date of audit inquiry.
- The access permissions of two employees, who were temporarily granted increased permissions to the Project Manager system during a period of vacancies in the State Revolving Fund (SRF) accounting office, were not readjusted until 10 months after the May 2015 time frame when the SRF accounting office was back at full staff.
- Two employees who no longer work for the CWSRF/DWSRF programs, and had transferred to different positions within the DES, still maintained access to the Project Manager system.

Cause:

It appears that management does not periodically review Project Manager system access levels.

Effect:

Failing to periodically review and monitor employee access to the Project Manager system increases the risk that unauthorized changes will be made to the Project Manager system that will not be detected and corrected by management in a timely manner.

Questioned Costs:

None

Recommendation:

DES should implement policies and procedures to ensure access to the Project Manager system is appropriate based on the employee’s job responsibilities. Access should be periodically reviewed to ensure that access levels continue to remain appropriate, and that only current CWSRF/DSWRF employees and appropriate accounting office personnel maintain access to the system.

Questioned Costs:

None

Clean Water and Drinking Water:

Auditee Corrective Action Plan:

DES concurs with the recommendation and agrees to update its procedures to review access levels to the Project Manager system more timely.

Contact Person:

Tracy Wood, Administrator, Wastewater Engineering Bureau – Clean Water
Sarah Pillsbury, Administrator, Drinking Water Ground Water Bureau

Anticipated Completion Date:

December 31, 2016

Single Audit Comment No. 3: Noncompliance With Annual And Final Federal Financial Reports (FFR) SF-425

U.S. Environmental Protection Agency ***Finding: 2015-043***
N.H. Department of Environmental Services

CFDA #66.458 Capitalization Grants for Clean Water State Revolving Funds (CWSRF)
CFDA #66.468 Capitalization Grants for Drinking Water State Revolving Funds (DWSRF)

Grant Year and Award:

2010	***FS991150-10 (DWSRF)***	
2011	***CS330001-11 (CWSRF),***	***FS991150-11 (DWSRF)***
2012	***CS330001-12 (CWSRF),***	***FS991150-12 (DWSRF)***
2013	***CS330001-13 (CWSRF),***	***FS991150-13 (DWSRF)***
2014	***CS330001-14 (CWSRF),***	***FS991150-14 (DWSRF)***

Finding: Noncompliance with annual and final Federal Financial Reports (FFR) SF-425

Criteria:

40 CFR 31.41 (b) and 40 CFR 31.50 (b) are existing requirements that mandate EPA recipients submit annual and final Federal Financial Reports (FFR's) SF-425 to the EPA. Annual FFRs are due no later than 90 calendar days following the end of the reporting year. Final FFRS are due within 90 days after the expiration or termination of the grant.

Condition:

The Department of Environmental Services (DES) did not complete annual FFR SF-425s for two grants open for the Clean Water State Revolving Fund (CWSRF) program, and for four grants open for the Drinking Water State Revolving Fund (DWSRF).

Additionally, the DES did not file final FFR SF-425s within 90 days of expiration or termination of the grant, for two CWSRF grant awards and two DWSRF grant awards which were required during SFY 2015.

A similar finding was noted in the prior single audit report.

Cause:

DES reports that the required FFRs were not filed due to lack of available staffing in the accounting office.

Effect:

The DES is not in compliance with federal reporting requirements 40 CFR 31.41 (b) and 40 CFR 31.50 (b).

Questioned Costs:

None.

Recommendation:

The DES should make it a priority to file timely annual FFR's for any grant open during the fiscal year, and file final FFRs, as required.

Clean Water and Drinking Water:

Auditee Corrective Action Plan:

DES concurs. DES will make it a priority to have staff available in order to file timely annual and final FFRs.

Contact Persons:

Tracy Wood, Administrator, Wastewater Engineering Bureau
Sarah Pillsbury, Administrator, Drinking Water Ground Water Bureau

Anticipated Completion Date:

September 30, 2016

Single Audit Comment No. 4: Noncompliance With Requirements Over Period Of Performance For The DWSRF Program

U.S. Environmental Protection Agency	***Finding: 2015-044***
N.H. Department of Environmental Services	
CFDA #66.468 Capitalization Grants for Drinking Water State Revolving Funds (DWSRF)	
Grant Year and Award:	
2010 FS991150-10	

Finding: Noncompliance with requirements over Period of Performance for the DWSRF Program

Criteria:

Payments to the line of credit (LOC) from a particular grant will begin in the quarter in which the grant is awarded and will end no later than the earlier of eight quarters after the capitalization grant is awarded or twelve quarters after advices or allowances are issued to the regions (40 CFR § 35.3155 (c) and 40 CFR §35.3560 (b)).

Condition:

State Revolving Fund grants cover ten year periods, but to control the flow of funds to the State, the EPA sets payment schedules within each grant. During our testing of the period of performance requirement for the DWSRF, we noted that the period of performance for the Federal payment schedules of two grants ended during SFY 2015. For the grant award payment schedule that ended July 1, 2014, there were 4 federal draws totaling $573,167 processed after the grant's payment schedule end date. These draws did not occur within the applicable payment schedule end date as required but should have been drawn against the next open payment schedule.

Cause:

Ineffective internal controls over ensuring the period of performance requirements were met.

Effect:

DES was not in compliance with period of performance requirements for fiscal year 2015.

Questioned Costs:

None.

Recommendation:

DES should establish controls, including written policies and procedures, related to period of performance requirements to ensure draws are drawn within a grant's period of performance.

Auditee Corrective Action Plan:

DES concurs. The Department will review each grant payment schedule more frequently to ensure all draws are performed within the allowable period of performance for each grant.

Contact Person:

Sarah Pillsbury, Administrator, Drinking Water Ground Water Bureau

Anticipated Completion Date:

June 30, 2016

Single Audit Comment No. 5: Noncompliance And Control Failure Over Monitoring Of Subrecipient Audits

U.S. Environmental Protection Agency ***Finding: 2015-045***
N.H. Department of Environmental Services

CFDA #66.458 Capitalization Grants for Clean Water State Revolving Funds (CWSRF)
CFDA #66.468 Capitalization Grants for Drinking Water State Revolving Funds (DWSRF)

Grant Year and Award:

2010	***FS991150-10 (DWSRF)***	
2011	***CS330001-11 (CWSRF),***	***FS991150-11 (DWSRF)***
2012	***CS330001-12 (CWSRF),***	***FS991150-12 (DWSRF)***
2013	***CS330001-13 (CWSRF),***	***FS991150-13 (DWSRF)***
2014	***CS330001-14 (CWSRF),***	***FS991150-14 (DWSRF)***

Finding: Noncompliance and control failure over monitoring of subrecipient audits

Criteria:

In accordance with OMB Circular A-133, Subpart D, §___.400 (d)(4)&(5), pass-through entities shall ensure that subrecipients expending $500,000 or more in Federal awards during the subrecipient's fiscal year for fiscal years ending after December 31, 2003 have met the audit requirements of OMB Circular A-133.

The DWSRF and CWSRF, as pass-through entities, are required to ensure the audit requirements of OMB Circular A-133 for the fiscal year are met and issue a management decision on audit findings within six months after receipt of the subrecipient's audit report and ensure that the subrecipient takes appropriate and timely corrective action.

Condition:

The DWSRF and CWSRF programs are responsible for monitoring subrecipients to ensure recipients expending federal subawards who meet the audit requirements are being audited and performing necessary follow ups on audit findings. We noted that the control designed to monitor subrecipient audit reports was not implemented and operating during fiscal year 2015.

Cause:

The Department of Environmental Services (DES) reports the cause is due to lack of available staff to perform the designed controls.

Effect:

DES was not in compliance with subrecipient monitoring requirements for fiscal year 2015, as subrecipient audit reports were not reviewed or followed up on.

Questioned Costs:

None

Recommendation:

DES should maintain necessary staff levels to conduct ordinary business and review controls to ensure they are designed, implemented, and operating effectively. Controls designed and implemented effectively will help to ensure compliance with the federal subrecipient monitoring requirements.

Clean Water and Drinking Water:

Auditee Corrective Action Plan:

DES concurs. There were two full time SRF accounting positions vacant during the fiscal year and now that the positions are fully staffed the monitoring procedures are being applied.

Contact Person:

Tracy Wood, Administrator, Wastewater Engineering Bureau
Sarah Pillsbury, Administrator, Drinking Water Ground Water Bureau

Anticipated Completion Date:

June 30, 2016

Single Audit Comment No. 6: Noncompliance With Setting Of Principal And Interest Repayment Due Dates

U.S. Environmental Protection Agency		***Finding: 2015-046***
N.H. Department of Environmental Services		
CFDA #66.458 Capitalization Grants for Clean Water State Revolving Funds (CWSRF)		
CFDA #66.468 Capitalization Grants for Drinking Water State Revolving Funds (DWSRF)		
Grant Year and Award:		
2010	***FS991150-10 (DWSRF)***	
2011	***CS330001-11 (CWSRF),***	***FS991150-11 (DWSRF)***
2012	***CS330001-12 (CWSRF),***	***FS991150-12 (DWSRF)***
2013	***CS330001-13 (CWSRF),***	***FS991150-13 (DWSRF)***
2014	***CS330001-14 (CWSRF),***	***FS991150-14 (DWSRF)***

Finding: Noncompliance with setting of principal and interest repayment due dates

Criteria:

An assistance recipient can be awarded a loan only if an assistance recipient begins annual repayment of principal and interest no later than one year after project completion. A project is completed when operations are initiated or are capable of being initiated (40 CFR § 35.3525 (a)(1)(i)) and 40 CFR § 35.3120 (a)(1)(ii)).

Condition:

<u>DWSRF</u>
Loan agreements between the DWSRF and the assistance recipient dictate the agreed upon project completion date and the first principal and interest repayment due date. During testing of Deposits to DWSRF, we noted that, for 2 of 25 sample selections tested, the DWSRF had set the first repayment due dates of principal and interest to be repaid more than one year after project completion, ranging from 275 to 366 days after one year from project completion. In both instances, although an earlier payment was received from the borrower, the loan agreement with the borrower did not require the first principal and interest repayment to be paid within one year, contrary to federal regulations.

During expanded testing of the compliance requirement, we noted that, for 2 of 7 sample selections tested, the DWSRF also set the first repayment due dates of principal and interest to be repaid more than one year after project completion. In one instance, the DWSRF program was untimely with a Supplemental Loan Agreement which caused the DWSRF program to extend the principal and interest due date 31 days beyond one year of project completion. In the other instance, due to the improper amortization of the repayment schedule, the DWSRF program did not require a payment that included both principal and interest until 7 years after project completion.

During expanded testing, we also noted that, for 1 of 7 sample selections tested, the DWSRF set the first repayment due date of principal and interest one year from project completion but, due to a typographical error with the construction completion date in the loan agreement, it appeared as if the payment was not due within one year. The DWSRF control to review loan agreements failed to ensure the accuracy of the construction completion date and, as a result, the loan agreement was agreed to and signed by all parties without detection of what appeared to be a noncompliance issue.

<u>CWSRF</u>
During testing of CWSRF loan repayments, we noted that, for 3 of 25 sample selections tested, the CWSRF set the first repayment due dates of principal and interest to be repaid more than one year after project completion, ranging from 3 to 60 days after one year from project completion. During our expanded testing of the compliance requirement for 5 additional sample selections, we noted no additional noncompliance errors.

Cause:

Ineffective internal control over the review and approval of loan agreements and repayment schedules.

Effect:

DES was not in compliance with requirements due to ineffective internal controls over the DWSRF and CWSRF special tests and provisions requirements.

Questioned Costs:

None.

Recommendation:

DES should establish written policies and procedures, including documented review and approval controls, over loan repayments to ensure that the federal compliance requirements are met. The DWSRF and CWSRF programs should develop procedures to document an agreed upon construction completion date between the program and the assistance recipients prior to the completion of loan agreements. The programs should increase efficiency in the timeliness of processing Supplemental Loan Agreements to better facilitate billing of loan recipients prior to the one year requirement.

Clean Water:

Auditee Corrective Action Plan:

DES concurs. DES will revise existing controls and procedures related to repayment to ensure that the related compliance requirements are met. It should be noted that the three identified loans had initial payment due dates ranging between 10-19 years ago.

Contact Person:

Tracy Wood, Administrator, Wastewater Engineering Bureau

Anticipated Completion Date:

December 31, 2016

Drinking Water:

Auditee Corrective Action Plan:

DES concurs. DES will revise existing controls and procedures related to repayment to ensure that the related compliance requirements are met. It should be noted that procedures have already been implemented to improve compliance including multiple staff review of all loan documents, monthly meetings with project managers to track project status, project tracking spreadsheets, final disbursement and close out checklists, and the development of cash flow projections that are updated no less than quarterly.

Contact Person:

Sarah Pillsbury, Administrator, Drinking Water Ground Water Bureau

Anticipated Completion Date:

December 31, 2016

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