



KPMG LLP
99 High Street
Boston, MA 02110-2371

Telephone 617 988 1000
Fax 617 507 8321
Internet www.us.kpmg.com

December 7, 2007

Lottery Commissioners
New Hampshire Lottery Commission
Concord, New Hampshire

Ladies and Gentlemen:

We have audited the financial statements of the New Hampshire Lottery Commission (the Commission), for the year ended June 30, 2007, and have issued our report thereon dated December 7, 2007. In planning and performing our audit of the financial statements of the New Hampshire Lottery Commission, we considered internal control as a basis for designing our auditing procedures 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 Commission's internal control. Accordingly, we do not express an opinion on the effectiveness of the Commission's internal control.

During our audit we noted certain matters involving internal control and other operational matters that are presented for your consideration. These comments and recommendations, all of which have been discussed with the appropriate members of management, are intended to improve internal control or result in other operating efficiencies and are summarized as follows:

Audit performed in Accordance with Statement of Auditing Standard No. 70 (SAS 70)

During our audit, we noted that only a SAS 70 type I report was performed on Scientific Games, a third party that performs transaction processing services for the Lottery. A SAS 70 type I report only includes a test of the design of the controls, not also whether the controls were operating effectively. Additionally, from our review of this SAS 70 report, we noted that certain controls that we would have expected to be included were not. These include:

- Controls related to making changes to Games Management System (GMS) production jobs, such that access capabilities to update, modify and delete job schedules should be limited to IT Operations personnel with job scheduling responsibilities and is segregated from the development function.
- Controls related to ensuring that network and application data is backed up on a regular basis.
- Controls to ensure that backup and restoration are periodically tested and deficiencies are addressed within a reasonable time frame, as well as ensuring back up tapes are rotated off-site.

We recommend the Lottery have a SAS 70 type II report performed for fiscal 2008 and annually thereafter to ensure that the controls designed are operating effectively. The Lottery should consider ensuring the controls noted above are included in the review.



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Management Response:

The Lottery has requested and Scientific Games has agreed to have a SAS 70 Type II audit performed for the remaining years of the contracts (2008, 2009, 2010). The controls noted above will be forwarded to the vendor for action. Due to the contract expiring on June 30, 2010 a SAS 70 will be done as of March 31, 2010. Further discussions with the auditors concerning this date will be ongoing.

Information Technology Review of Platinum General Ledger

We performed a review of IT General Controls including access to programs and data, program changes, program development and computer operations around the Platinum General Ledger system. We identified a few controls not being performed. Specifically, these controls are that backup tapes are not periodically tested and files are being restored on an ad-hoc basis only, and there are no formalized policies and procedures in place addressing backup and restoration activities.

We recommend that the Lottery formalize procedures related to testing backup files to ensure files are properly and completely backed up, and restored.

Management Response:

The Lottery has restored data from the backup tapes without any problems in the past. Due to the lack of a test system at the Lottery we will work with the Office of Information Technology in setting up procedures for testing the backup data. OIT will also be consulted to develop formalized policies and procedures for backup and restoration activities.

Monthly Reconciliation of the Fidelity Cash Account

The Commission does not perform monthly cash reconciliations for the Fidelity investment account (Cash in Treasury) in its entirety.

We recommend that the Commission perform monthly reconciliation of the Fidelity investment account. This reconciliation will help to ensure that cash and revenue reported is proper.

Management Response:

This Fidelity account is a Treasurer's account and accordingly we do not have access to this account to do a reconciliation. In accordance with the Lottery's response to a similar observation for FY 03, the Lottery does match and reconcile all cash activities from the account to the state's monthly cash reports.

Online Games Subscription Reports

The Commission is not able to produce a report as of a particular date which shows the total liability (deferred revenue) broken down by the remaining draws for each subscription.



We recommend the Commission develop a report that shows the total liability by subscription, with details of subscription effective date, draws purchased, and remaining draws. This report will help to validate the deferred revenue balance at year end.

Management Response:

A request has been made of the online vendor to design and produce a report that will address this request.

Recording “Replay” Program

We noted that the financial statements of the Commission, did not originally record the financial statement impact of the Replay Program.

We recommend the Commission develop a process to record the financial statement impact of prizes donated to the Replay Program in exchange for promotional consideration. This process will help ensure all contributed prizes are properly safeguarded. Additionally we recommend that the Commission work with the Department of Administrative Services to properly account for any new program in its financial statements prior to submitting them for audit.

Management Response:

We did hold discussions with Administrative Services during Fiscal Year 2007 concerning this new program. We decided to interface with the auditors on this issue prior to the completion of the entry. The accounting entry was recorded for June, 2007, we believe that all parties are in agreement with the entry that was made.

Agent Licensing

- 1 The Commission evaluates the business records of prospective agents prior to licensure and assigns a credit rating from excellent to bad. Each credit rating imposes progressively stricter requirements of the agent, thereby mitigating most collection risk of poor agents. We observed several instances agents assigned “cautious” or “bad” credit ratings that subsequently had electronic fund transfer (EFT) sweeps returned due to insufficient funds.

We recommend the Commission re-evaluate the agent application criteria and consider not granting licenses to applicants with “bad” or “cautious” credit scores. This will help reduce chances that funds will not be collected.

- 2 Although prospective agents attest to their prior criminal background via a check box on the application and consent to investigations into the criminal background, the Commission does not conduct standard criminal background checks.

The Commission should work with appropriate New Hampshire authorities (e.g. Attorney General) to develop a process to ensure that a standard criminal background check is performed for prospective agents prior to licensure.



- 3 Some EFT returns are caused by incorrect agent routing and transit information in either the Lottery's GMS Retailer database or the records of TD BankNorth.

The Commission should explore a process with TD BankNorth that would incorporate a prenote procedure to ensure that new agent bank accounts can be swept during the weekly EFT prior to initiating the first EFT for a new agent.

Management Response:

1. *We have been very successful using this credit rating process. During FY 07 we licensed 120 retailers with 8 retailers under this cautious credit rating. We only had one issue out of the 8 retailers which was immediately remedied.*
2. *The Commission will address this item with the Attorney General's Office, we do not have legal authority at this time to do a criminal background check on our retailers which total over 1,200 to date.*
3. *The Commission previously pre-noted all new bank accounts but discontinued the practice due to the one or two week delay receiving funds owed the Commission from the new accounts. The Commission will discuss a solution with the bank so that a timely procedure can be put in place for all new retailers prior to the first Electronic Fund Transfer (EFT) would be processed.*

Dedicated Trust Accounts

The Commission does not require agents to set up dedicated trust accounts for New Hampshire Lottery proceeds. Therefore, it has no ability to ensure that it receives notification automatically from TD BankNorth when agents switch banks, bank accounts or otherwise remove themselves from the EFT sweep system

The Commission should consider requiring agents to maintain dedicated trust accounts for Lottery proceeds and explore with TD BankNorth a method which will allow for automatic notification if agents switch bank accounts and move out of the EFT banking system.



Management Response:

Retailers could face additional bank charges for each dedicated trust account. The Commission is not aware of any problems as a result of the system currently in place. The Commission will discuss with the bank a solution to this issue. Currently we do not have any retailers with a dedicated trust account.

Insufficient Funds and Delinquent Agents

- 1 The current New Hampshire Lottery practice of allowing retailers two full business days to pay for NSF's – and only after a positive contact from the New Hampshire Lottery with the actual owner – is not consistent with best practices for managing agent NSF's.

The Commission should institute a more proactive application of agent sanctions for NSF's. The time period agents are allowed to make payments should be shortened to either the same business day or the next business day. The requirement that a positive agent contact occur before the Lottery should be eliminated. When NSF's are processed, the New Hampshire Lottery should send a message to the agent via the terminal instructing them to call the Lottery immediately because of a problem. Sanctions should then be applied within the defined time frame regardless of any positive Lottery contact with the actual agent owner.

- 2 Current agent sanctions are not uniformly applied. Specifically we observed that:
 - Agents who paid NSF's several weeks after being notified did not have their terminals disabled.
 - Agents who had four NSF's were not suspended.
 - An agent who had its terminal disabled for NSF non-payment was allowed to continue to sell instant tickets.

We recommend that the New Hampshire Lottery apply its NSF sanctions uniformly and in accordance with its policies.

- 3 In certain instances, delinquent agents are put on payment plans with unfavorable terms for the Commission.

The Commission should ensure payment plans follow Lottery policy (January 2007) that “payment plans should be arranged so that the entire amount due is paid within one year’s time.”

- 4 The current system used by Operations to monitor NSF's and delinquencies is manual, dependent upon periodic review of files and databases by one person.

We recommend that the New Hampshire Lottery explore methods to automate some of the monitoring procedures for NSF's and delinquent agents.



Management Response:

- 1. We will contact the retailers by terminal message and continue the telephone process currently in place. Many owners of the retailers' site may not be at that location and the message may not be received.*
- 2. We instituted new policies and procedures in January, 2007 to have a more uniform process and do believe this will solve this issue. There were two exceptions noted. One exception was reviewed by management and approved for a late payment due to extenuating circumstances. The second exception was related to a clerical error that was found in a weekly internal audit of the weekly electronic fund transfers which was corrected immediately.*
- 3. We are following the policy and procedure instituted in January, 2007 for collections from delinquent retailers. Payment plans are only acceptable if full payment is made within a one year period, if not we forward the information to the Attorney General's Office for collection process.*
- 4. We will explore an automated system for NSF using software tools we have access to or can be developed by the Commission or OIT.*

Instant Ticket Observations

The Games Management System (GMS) allows an agent to have two or more books of the same instant game activated at the same time.

The GMS should be configured so that when an agent activates more than one book of the same game, it aggregates the GLEPS of all cashing for that game for that agent. When the aggregated GLEPS is reached for the game, the oldest book (first activated) is autosettled. This will ensure that even if agents activate many books of the same game, they will not be able to avoid payment for NH Lottery sales.

Management Response:

- 1 Many of our retailers display more than one book of the same game in their dispensers; this particularly applies to the larger retailers.*
- 2 Many retailers have more than one set of dispensers and different shifts will sell from particular dispensers; this usually requires that more than one book of a particular game is offered for sale at the same time. This particularly applies to chain convenience stores and the State Liquor Stores.*
- 3 Over 200 retailers sell from vending machines in addition to counter dispensers and this, too, results in duplication of active books in a game.*
- 4 Our Sales Representatives visit all retailers in their territories on a regular basis (generally on a 3-week rotation) and are required to ensure that all sold books are settled.*



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Our audit procedures are designed primarily to enable us to form an opinion on the financial statements, and therefore may not bring to light all weaknesses in policies or procedures that may exist. We aim, however, to use our knowledge of the company's organization gained during our work to make comments and suggestions that we hope will be useful to you.

We would be pleased to discuss these comments and recommendations with you at any time.

We did not audit the Lottery Commission's responses included herein, and, accordingly, we express no opinion on them.

This communication is intended solely for the information and use of management, Lottery Commissioners, others within the organization, and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

KPMG LLP