



KPMG LLP
Two Financial Center
60 South Street
Boston, MA 02111

Independent Auditors' 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

The Fiscal Committee of the General Court
State of New Hampshire:

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 governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of New Hampshire (the State) as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the State's basic financial statements, and have issued our report thereon dated December 27, 2018. Our report includes an emphasis of matter paragraph regarding the State adopting the provisions of Governmental Accounting Standards Board (GASB) Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefit Plans Other Than Pensions*. Our report includes a reference to other auditors who audited the financial statements of the Liquor Commission, Lottery Commission, Business Finance Authority of the State of New Hampshire, Community Development Finance Authority, Pease Development Authority, Community College System of New Hampshire, New Hampshire Retirement System, New Hampshire Judicial Retirement Plan and the New Hampshire Public Deposit Investment Pool, as described in our report on the State's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors. The financial statements of the New Hampshire Public Deposit Investment Pool and the Business Finance Authority of the State of New Hampshire were not audited in accordance with *Government Auditing Standards*, and accordingly, this report does not include reporting on internal control over financial reporting or instances of reportable noncompliance associated with the New Hampshire Public Deposit Investment Pool and the Business Finance Authority of the State of New Hampshire.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the State'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 opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the State's internal control. Accordingly, we do not express an opinion on the effectiveness of the State's internal control.

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.



Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, 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*.

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 State'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 State's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

Boston, Massachusetts
December 27, 2018



STATE OF NEW HAMPSHIRE

Management Letter

For the Fiscal Year Ended June 30, 2018



KPMG LLP
Two Financial Center
60 South Street
Boston, MA 02111

April 1, 2019

Management of the Department of Administrative Services
Honorable Members of the Fiscal Committee of the General Court
State of New Hampshire
Concord, New Hampshire

Ladies and Gentlemen:

In planning and performing our audit of the financial statements of the State of New Hampshire (the State) as of and for the year ended June 30, 2018, in accordance with 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, we considered the State's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the State's internal control. Accordingly, we do not express an opinion on the effectiveness of the State'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 and/or significant deficiencies and therefore, material weaknesses and/or significant deficiencies may exist that were not identified. In accordance with *Government Auditing Standards*, we issued our report dated December 27, 2018 on our consideration of the State's internal control over financial reporting.

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. During our audit, we identified the deficiencies in internal control as summarized in the accompanying attachment.

The State's responses to our comments and recommendations are described in the accompanying attachment. The State's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the responses.

This purpose of this letter is solely to describe the deficiencies in internal control identified during our audit. Accordingly, this letter is not suitable for any other purpose.

Very truly yours,

KPMG LLP

**Observation 2018-1: Department of Administrative Services and Department of Treasury
Classification of Cash, Cash Equivalents and Investments**

Background

The Governmental Accounting Standards Board (GASB) has presentation and disclosure requirements for reporting monetary assets such as cash, cash equivalents, and investments.

The State' Comprehensive Annual Financial Report (CAFR) does not consistently categorize money market funds, a monetary asset, reported in its various governmental and proprietary funds. Money market fund assets in some funds are categorized as cash and cash equivalents while money market assets in others funds are classified as investments.

Observation

The State CAFR's presentation and disclosure of money market assets is inconsistent among funds.

Recommendation

We recommend that the Department of Administrative Services and Department of Treasury review the accounting treatment for cash, cash equivalents and investments. The State CAFR should report cash, cash equivalents and investments in the statements of financial position and the notes to the statements consistent with GASB requirements and in a manner that is accurate and consistent with the nature of the monetary asset.

Management Response

Treasury agrees with the recommendation and is planning to work with the Department of Administrative Services, Bureau of Accounts to understand and appropriately classify cash, cash equivalents and investments as presented in the CAFR.

**Observation 2018-2: Department of Environmental Services
State Revolving Fund - Unreconciled Variances**

Background

The State Revolving Fund (SRF), administrated by the Department of Environmental Services, is reported as a major enterprise fund in the State's CAFR. The SRF operates to provide loans to public water systems and local governments for wastewater treatment and safe drinking water systems. Funding for the SRF is obtained from the U.S. Environmental Protection Agency with matching funds provided by the General Fund, as well as from interest on outstanding loans. The State established the SRF as a separate enterprise fund in fiscal 2014 through a cash transfer from the General Fund.

Observation

The Department of Environmental Services utilizes a sub-financial reporting system, Loan and Grants Tracking System (LGTS), to record detailed activity related to the SRF and on a monthly basis reconciles the LGTS activity to the State's general ledger, NH First. The LGTS system is used for financial statement reporting purposes in the CAFR. At June 30, 2018, the two systems did not agree. The Department of Environmental Services staff reported the cause of the differences is unknown; however, the differences have existed for several years.

Recommendation

We recommend the Department of Environmental Services work with the Department of Administrative Services to investigate the root cause of the differences and to adjust the accounting records as necessary.

Management Response

The Department of Environmental Services will continue to work with the Department of Administrative Services to resolve this NH First issue.

Observation 2018-3: Department of Revenue Administration
Tax Abatement – Economic Revitalization Zone Tax Credit

Background

The State of New Hampshire provides incentives for businesses to engage in job creation in certain economic revitalization zones. RSA 162-N, Economic Revitalization Zone Tax Credits, defines and establishes the requirements related to these business tax credits. RSA 162-N:5 places certain limits on the total credit a taxpayer may claim, specifically, "the maximum credit which may be utilized by a taxpayer in any calendar year shall not exceed \$40,000." During fiscal year 2018, 51 taxpayers reported credits under this program.

Observation

During our testwork over these credits, we identified three instances where taxpayers claimed, and were given credit for, more than the maximum allowable credit of \$40,000. The three instances included credits of \$43,372, \$49,379 and \$72,646, for total excess credits of \$45,397.

Recommendation

We recommend the Department of Revenue Administration review its tax forms and directions to ensure that taxpayers are prompted to claim no more than the maximum allowable credit under statute. Additionally, we recommend that the Department of Revenue Administration review its monitoring procedures to determine if these instances of taxpayer noncompliance would have been detected through existing processes and controls; and to implement any needed enhancements to current procedures to detect such non-compliance.

Management Response

The Department agrees with the recommendation.

In pertinent part, RSA 162-N:5 reads "the maximum credit which may be utilized by a taxpayer in any calendar year shall not exceed \$40,000." The three taxpayers who claimed a credit in excess of \$40,000 are not in compliance with RSA 162-N:5. The Business tax is a self-reporting tax, meaning the taxpayer compiles the return to the best of their knowledge and in compliance with relevant law and submits it to the Department. Once the return is received and processed, potential errors maybe found on the return through both standard reviews and formal audit selection. When the Department identifies an error on a return with respect to a credit or any other item required by law to be reported, the return will be referred to the audit division. The Department operates under a statute of limitations which gives the Department 3 years from the due date of the return or the date of actual filing (whichever is later), to identify and correct any errors on the taxpayer's return. The taxpayer also may amend their return in that 3 year period to correct any errors.

The Department agrees to look at adding more information on the DP-160 form and instructions to address the \$40,000 maximum credit for the ERZTC. The Department has evaluated programming the form to disallow entry of an amount greater than \$40,000 and has determined that is not doable. Form changes have already been implemented for Tax Year 2019, which means that changes to the DP-160 form and instructions will not take effect until Tax Year 2020. As a result, the same issues may arise for the next couple of fiscal years and may continue to arise if the taxpayer does not follow the directions on the form.

The Department also agrees to review its taxpayer compliance process to determine whether those procedures are sufficient to detect instances of taxpayer noncompliance and to enhance those procedures if it is determined to be necessary.

Observation 2018-4: Department of Employment Security

**Unemployment Compensation Trust Fund - Contributions Receivable Reserve
Analysis**

Background

The Department of Employment Security's Unemployment Compensation Trust Fund (UCTF) is reported as a major enterprise fund in the State's CAFR. The UCTF receives contributions from employers and provides benefits to eligible unemployed workers. Through the normal conduct of operations, the UCTF is owed amounts from both employers, for contributions due, as well as from participants, for any benefit overpayments.

Generally accepted accounting principles require the State present its UCTF receivables at net realizable value, or the amount it expects to receive. Arriving at an estimate of net realizable value requires a robust analysis of the facts and circumstances including historical evidence of collectability.

At June 30, 2018 the UCTF reported a net receivable of \$16.9 million which was comprised of the following components (amounts in thousands):

	<u>Amount due</u>	<u>Allowance</u>	<u>Net receivable</u>
Due from:			
Employers	\$ 20,710	(4,901)	15,809
Benefits overpayments	30,174	(29,402)	772
Federal programs	13	—	13
Other states	354	—	354
Receivables, net	<u>\$ 51,251</u>	<u>(34,303)</u>	<u>16,948</u>

Rather than performing a robust analysis of the collectability of its receivables, the Department of Employment Security simply reserves the accounts that are 12 months or older, and maintains a policy of not writing off receivables.

Observation

The Department of Employment Security does not have a process for evaluating the net realizable UCTF receivable balance or the adequacy of the reserve over the gross receivable balance, nor has it performed any formal analysis to assess the reasonableness of the reserve.

Recommendation

We recommend that the Department of Employment Security perform a retrospective review over the reserve for uncollectible receivables estimate to help ensure that the methodology is still reasonable and to substantiate the assumptions used in the calculation.

Management Response

The Department of Employment Security will perform a retrospective review of our allowance for uncollectible receivables estimate to help ensure our methodology is reasonable and to substantiate the assumptions used in our calculation.

**Observation 2018-5: Department of Health and Human Services
New Heights - General Information Technology Controls**

Background

The State of New Hampshire Department of Health and Human Services uses the New Heights application for eligibility determinations for programs that are funded in part by Federal awards. As part of our audit, we tested the General Information Technology Controls (GITC) related to the New Heights application for the following domains: Access to Programs and Data; Change Management; Computer Operations; and Program Development.

Observation

The GITC testwork over the New Height application identified certain controls were not operating effectively for the period of July 1, 2017 - June 30, 2018, as noted below:

- A. Privileged access rights to the New Heights application and related infrastructure should be restricted to users based on current job function and responsibility. During our review, it was noted that 1 user account with privileged access rights to the backup scheduling tool was that of a terminated user account. With regards to the privileged user accounts for the backup scheduling tool, removal of access for the terminated employee in question was not performed timely upon notification of termination. When access rights for terminated employees are not disabled and/or removed in a timely manner, there is a risk that unauthorized users may obtain access to the New Height's application and related infrastructure. Inappropriate privileged access to the application and/or related infrastructure increases the risk that segregation of duties controls will be ineffective and that secure access to sensitive data may be compromised leading to an increased opportunity for error or fraud. The audit team obtained system-based evidence for the terminated user and determined the user account was not accessed after the user's termination date.
- B. When completing the monthly review of access to the datacenter, documentation supporting the performance of the review should be retained. During our review, we noted that for one month, management did not retain the documentation supporting the performance of the review. When access rights are not formally reviewed, there is an increased risk that unauthorized access to the datacenter which houses New Height's infrastructure may occur and not be detected timely. Management prepared and the audit team obtained and reviewed a retroactive review of datacenter access and noted that access was appropriate for the month with no changes requested.
- C. On at least an annual basis, management should complete a successful disaster recovery test. Should the test fail, the related issues should be investigated and resolved. During our review, it was noted that subsequent to an unsuccessful disaster recovery test, while issues were investigated and remediation plans were developed, the remediated plan was not tested during the period. When a disaster recovery test is performed with failed results, there is an increased risk that in the case of a disaster the data will not be able to be restored completely and accurately.
- D. Documentation supporting the monitoring of backup jobs for success or failure should be retained for at least a 12-month period. During our review, it was noted that management did not retain evidence supporting the monitoring of the backup jobs or retain the audit logs for more than 30 days. When backup jobs are not monitored for successful completion there is an increased risk that if backup jobs are not being completed successfully there could be a potential loss of data. Furthermore, the audit team obtained systematic evidence for 15 days within the final month of the audit period and noted that backup jobs appeared to have completed successfully.

Recommendation

The Department of Health and Human Services should:

- A. Reinforce policies and procedures to strengthen controls relative to privileged access to ensure only access to privileged accounts are appropriate.
- B. Reinforce policies and procedures to strengthen controls to validate users are appropriate to the datacenter and inappropriate access is removed in a timely manner.
- C. Perform procedures necessary to strengthen controls to validate the disaster recovery tested completed successfully.
- D. Perform procedures necessary to strengthen controls for monitoring backup job for successful completion.

Management Response

- A. The Department concurs in part. There was no inappropriate privileged access to the system. The user id in question was a secondary definition of the user id within a 3rd party product, but its definition does not constitute access to the product or system. This product uses RACF security to allow access to the system and to the product, and the user id in question was revoked from RACF so the user id could not be used. The definition within the scheduling product is merely the rights the user id has within the product once authenticated by the RACF mechanism.

The state will note this finding and update the procedures to ensure all definitions of inactive user id's are removed from all 3rd party product definitions

- B. The Department concurs. The access logs for the month in question were reviewed, but the review was not documented. Data Center management has implemented a process to document review that access has taken place by creating a log which contains the date the review occurred and by whom.
- C. The Department concurs. The state will be conducting another Disaster Recovery test in November in which the mitigation plans for the above mentioned documented issues will be tested and confirmed.
- D. The Department concurs. The current scheduling system does not have the capability of retaining history for a 12 month period. The state is in the process of implementing a new scheduling system that will allow for this 12 month history retention as well as automated notifications of success/failure of backup jobs via email or other means. This system should be completely operational within the next 12 months.

In the interim, the state is manually verifying all nightly/weekly backup jobs for success/failure and manually taking action if any job fails.

Observation 2018-6: Department of Administrative Services

NH FIRST ERP System for the Financial Reporting, Time Reporting, and Human Resources/Payroll ERP System (ERP System) - General Information Technology Controls

Background

The State of New Hampshire uses the NH FIRST ERP System (ERP System) for the Financial Reporting, Time Reporting, and Human Resource/Payroll functions. As part of our audit, we tested the General Information Technology Controls (GITC) related to the ERP System for the following domains: Access to Programs and Data; Change Management; Computer Operations; Program Development.

Observation

The GITC testwork over the ERP System identified certain controls were not operating effectively for the period of July 1, 2017 - June 30, 2018, as noted below:

- A. During our review, we noted that access to the NH FIRST ERP application was not removed in a timely manner for 3 of the 8 samples, with a duration of time between the date of termination and the removal of access ranging from 6 to 9 days. The audit team compared the termination list for the audit period to the active user listing and noted no additional terminated users that were not removed in a timely manner. Furthermore, we examined system-based evidence to determine that none of the user accounts identified as exceptions were accessed subsequent to the individual's termination date.
- B. During our review, we noted that privileged access to the database layer and developer access was not removed in a timely manner for 5 users. Furthermore, the audit team examined system-based evidence to determine that none of the user accounts identified were accessed subsequent to the individual's termination date.
- C. When completing the monthly review of access to the datacenter, documentation supporting the performance of the review should be retained. During our review, we noted that for one month, management did not retain the documentation supporting the performance of the review. Management prepared and the audit team obtained and reviewed a retroactive review of datacenter access and noted that access was appropriate for the month with no changes requested.
- D. During our review, we noted that 2 quarterly reviews of system changes were not completed in a timely manner. Furthermore, the audit team obtained and examined a retroactive review of the changes and management noted all changes were appropriate.

Recommendation

Management responsible for the NH FIRST ERP application should establish and enforce policies and procedures to:

- A. Ensure that notification of termination for users of the NH FIRST ERP application occurs in a consistent and timely manner, resulting in timely removal of access rights (in excess of read-only), as well as the removal of all access rights upon reaching 90 days post- termination.
- B. Strengthen controls relative to privileged access to ensure only access to privileged accounts are appropriate.

- C. Strengthen controls to validate users are appropriate to the datacenter and inappropriate access is removed in a timely manner.
- D. Ensure that the quarterly review of changes is being performed in a timely manner.

Management Response

- A. Discussions regarding the implementation of additional system controls have revealed any additional controls would inherently be based on the state's payroll and timekeeping cycle of two weeks. These discussions have also indicated there would be significant resources needed to design, test, and implement additional system controls.

Management believes improving the flow of information and communication regarding both means of compliance and importance of compliance with statewide policies regarding the initiation of termination transactions in the NH FIRST ERP application between the Administrative Services Department, Division of Personnel and state agencies would effectively achieve similar results as additional system controls.

Accordingly, management will seek to improve compliance with statewide policies and procedures through enhanced communication with agencies with the goal of achieving a rate of compliance sufficient to reasonably ensure any future instances of non-compliance are minimal.

- B. Management will establish a process to ensure employee terminations and transfers are compared against privileged user access to the database layer accounts on a monthly basis.
- C. DoIT management will ensure that evidence of monthly reviews of access to the data center that are signed off by the appropriate parties is retained for proof of the reviews. The original signed copy will be retained by the Director of DoIT Operations.

DoIT reviews the access audit logs to the computer room weekly and reviews the users with access to the computer room monthly. When someone terminates or moves so that their access is no longer valid the Director of DoIT Operations is notified so that the Director may remove their access from the building and/or computer room. The Director of DoIT Operations monthly review also validates who has access to the computer room. Access Authorization forms to the building and/or computer room need to have the Director of DoIT Operations signature or the Deputy Commissioner's, if the Director of DoIT Operations is unavailable.

- D. Management will ensure quarterly NH FIRST change reports are produced and signed off by the appropriate parties in a timely manner. The original signed copy will be retained in Financial Data Management (FDM) and soft copies will be retained by FDM and provided to DoIT.