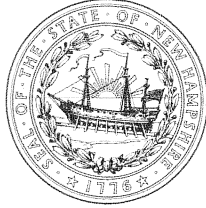


**STATE OF NEW HAMPSHIRE
TURNPIKE SYSTEM**

**MANAGEMENT LETTER
FOR THE FISCAL YEAR ENDED JUNE 30, 2011**



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To The Fiscal Committee Of The General Court:

We have audited the financial statements of the New Hampshire Turnpike System as of and for the fiscal year ended June 30, 2011 and have issued our report thereon dated December 29, 2011.

This management letter, a byproduct of the audit of the New Hampshire Turnpike System for the fiscal year ended June 30, 2011, contains our auditor's report on internal control over financial reporting and on compliance and other matters and related audit findings. The appendix, included as an attachment to the management letter, provides a summary of the status of observations presented in the fiscal year 2010 management letter of the Turnpike System.

The New Hampshire Turnpike System Comprehensive Annual Financial Report (CAFR) can be accessed online at:

http://www.gencourt.state.nh.us/LBA/AuditReports/FinancialReports/pdf/Turnpike_2011_CAFR.pdf.

Office of Legislative Budget Assistant
Office Of Legislative Budget Assistant

December 29, 2011

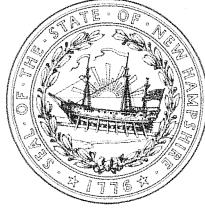
**STATE OF NEW HAMPSHIRE
TURNPIKE SYSTEM
2011 MANAGEMENT LETTER**

TABLE OF CONTENTS

	<u>PAGE</u>
Letter Of Transmittal	i
Auditor’s Report On Internal Control Over Financial Reporting And On Compliance And Other Matters	1
 <i>Internal Control Comments *</i>	
<i>Material Weakness</i>	
1. Efforts To Improve Financial Accounting And Reporting Processes Should Continue	3
 <i>Significant Deficiencies</i>	
2. Controls Over Open Road Tolling Transactions Should Be Established	7
3. Lane Audit Controls Should Be Improved	10
4. Automated Open Road Tolling Data Transfer Error Alert Should Be Implemented	12
5. Risk Assessment And Response Plans Should Be Established For Open Road Tolling System	13
6. Controls Over Accounting For Replaced, Sold, Or Unserviceable Capital Assets Should Be Improved.....	14
7. Controls Over Monthly Revenue Reconciliations Should Be Improved.....	16
8. Effective Monitoring Controls Over Account Reconciliations Should Be Established	17
9. Payments Should Be Based On Services Received, Not Budgeted Amounts	18
 <i>State Compliance Comments</i>	
10. Accounts Should Be Utilized As Provided In General Bond Resolution Requirements...	20
11. Transponder Inventory Fund Should Not Exceed Statutory Limit.....	21
 APPENDIX - Current Status Of Prior Audit Findings	 23

* 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>.



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Auditor's Report On Internal Control Over Financial Reporting And On Compliance And Other Matters

To The Fiscal Committee Of The General Court:

We have audited the financial statements of the New Hampshire Turnpike System (Turnpikes) as of and for the fiscal year ended June 30, 2011, and have issued our report thereon dated December 29, 2011. We conducted our audit 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.

Internal Control Over Financial Reporting

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying audit comments, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be 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 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 deficiency described in Observation No. 1 to be a material weakness.

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. 2 through No. 9 to be significant deficiencies.

Compliance And Other Matters

As part of obtaining reasonable assurance about whether Turnpikes' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, rules, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*. However, we noted immaterial instances of noncompliance which are described in Observations No. 10 and No. 11.

Turnpikes' written response to the observations in this report have not been subject to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the management of the New Hampshire Turnpike System, others within Turnpikes, and the Fiscal Committee of the General Court, and is not intended to be used by anyone other than these specified parties.

Office of Legislative Budget Assistant

Office Of Legislative Budget Assistant

December 29, 2011

Internal Control Comments
Material Weakness

Observation No. 1: Efforts To Improve Financial Accounting And Reporting Processes Should Continue

Observation:

Improvements were evident in the New Hampshire Turnpike System's (Turnpikes) financial accounting and reporting processes during fiscal year 2011. However, during the course of the audit instances were noted where Turnpikes needs to continue its efforts to address weaknesses in its financial transaction processing and reporting.

1. As described more fully in Observation No. 9, Turnpikes paid certain expenses such as law enforcement, indirect costs, and maintenance costs based upon budgeted amounts versus actual costs incurred or calculated amounts due.
2. Turnpikes records Federal Highway Administration (FHWA) and State Highway Fund contributions towards Turnpikes' construction projects and other costs as capital contributions.
 - a. Turnpikes was unable to provide system-generated reports such as NHFirst reports or FHWA reports to adequately support the \$28.4 million balance reported as federal capital contributions through June 30, 2010. In addition, a review of FHWA project reports and Turnpikes' calculations of contributions for two projects indicated Turnpikes understated fiscal year 2011 capital contributions by approximately \$696,000.
 - b. Turnpikes reported an amortization expense for capital contributions in its detail accounting records. When asked, Turnpikes could not fully explain the appropriateness of the amortization or support the amount of the amortization expense recorded.
 - c. Turnpikes overstated capital contributions by \$3.4 million because the capital contributions related to the transfer of a bridge from the Highway System to Turnpikes during fiscal year 2011 were recorded at cost versus depreciated cost.
3. Turnpikes continues to be challenged in accounting for and reporting capital assets. Much of Turnpikes' reporting of capital assets during fiscal year 2011 relied upon manual preparation and updates to data on spreadsheets that are subject to error and loss of data integrity and support. For example, as noted in Observation No. 6, Turnpikes does not have controls in place to ensure capital assets are appropriately removed from the financial records when they are replaced by newer assets. In a limited review requested by the auditors, Turnpikes identified four replaced assets recorded at \$7.5 million in Turnpikes infrastructure asset accounts with associated accumulated depreciation of \$7.2 million that remained in Turnpikes reported balances even though the assets did not exist at June 30, 2011. Projecting the results of its review, Turnpikes estimated that there was an additional \$2.6 million in previously replaced capital assets still on the books at June 30, 2011.

4. Turnpikes made two material audit adjustments to the fiscal year 2011 Statement of Cash Flows to correct errors made in its preparation of the statement.
 - a. One audit adjustment increased both the “Purchases of Investments” and “Sales of Investments” line items by \$6.9 million. The audit adjustment corrected an error made by Turnpikes in calculating the fiscal year 2011 account activity.
 - b. One audit adjustment decreased both the “Acquisition and Construction of Capital Assets” and the “Capital Contributions” lines on the Statement of Cash Flows by approximately \$17 million. During fiscal year 2011, Turnpikes determined a significant bridge infrastructure asset had erroneously been recorded as a Department of Transportation asset and not a Turnpike asset in 2001. Turnpikes properly corrected the recording of the asset during fiscal year 2011 by transferring the asset onto Turnpikes’ books as a capital contribution. However, as no cash flows resulted from the addition of the asset to inventory, Turnpikes should not have reflected the transaction on the Statement of Cash Flows.

5. Turnpikes made a significant audit adjustment to the fiscal year 2011 Statement of Revenues, Expenses, and Changes in Net Assets (Statement) to correct an error made by Turnpikes in its initial preparation of the Statement. Turnpikes initially reported the monies related to federal interest subsidies for Build America Bonds as reductions of expenses instead of revenues on Turnpikes’ fiscal year 2011 Statement. While a similar transaction was accurately reported in fiscal year 2010, and a supervisory review during fiscal year 2011 reportedly was in place, the error in Turnpikes’ initial reporting of fiscal year 2011 bond subsidies resulted in understatements of revenues and interest expense of approximately \$3.1 million.

Recommendation:

Turnpikes should continue in its efforts to improve its financial accounting and reporting processes. This should include a thorough review of all accounting entries by a second knowledgeable employee. In making and reviewing financial accounting entries, Turnpikes should consider the nature of transactions when determining how the transactions should be included in the accounting records and reported in the financial statements.

While a number of the financial accounting and reporting challenges facing Turnpikes are compounded by insufficient capital asset accounting systems (which likely will only be satisfactorily resolved with the implementation of an appropriate fixed asset accounting system), Turnpikes needs to strengthen its financial accounting and reporting through improved policies and procedures. Better policies and procedures could improve consistency in accounting and reporting financial activity and result in better trained and informed employees.

Auditee Response:

Turnpikes concurs.

Improvements to the New Hampshire Turnpike System's (Turnpikes) financial accounting and reporting processes have indeed occurred. Financial accounting and reporting highlights for the year include and are certainly not limited to the following:

- Implementation of automated financials,
- Establishment of the General Reserve Account,
- Successful interpretation and implementation of new GASB Statements,
- Creation of new general ledger accounts as needed,
- Implemented monthly (timely) interest posting on investments,
- Approved reclassification of position to assume Fixed Asset development, and
- Provide support and assistance in successful refunding of revenue bonds realizing cash savings of \$5.4 million.

Staff awareness and attention to detail continue to improve as evidenced by Department of Transportation (Department) staff that researched, discovered, and reported a misclassified asset of \$17 million originating in 2001.

Accounts payable, a past issue, is now reviewed and processed through October to ensure all payables are properly captured. The Department has also employed scanning to its accounts payable process.

Specific to the auditor's comments:

1. Over-payment of certain expenses for billable services to the Turnpike Fund (both internal and other agency) will be better communicated to both staff and other agencies to perform year-end adjustments as necessary to reflect actual experience versus budgeted.
2. a. The Department developed its support for the reported \$28.4 million balance for reported federal contributions from its internal data warehouse reports. A review of the internal data warehouse report to the FHWA/FMIS federal report for two projects suggested a difference of \$696 thousand in reporting for federal contributions. As a result of this difference, the Department in the future will utilize the federal FHWA/FMIS report in federal contribution calculations.
b. The Department will research why certain amortized amounts are recorded to Capital Contributions (as has been practiced in prior years). Once decided, policy will be written and practiced.
c. The result of the methodology and treatment employed by the Department on this transaction was to overstate capital contributions and depreciation expense by \$3.4 million (as indicated by the auditors) but had no net effect to Net Capital Assets as presented on the Statement of Net Assets. The Department agrees with this finding and in the future will closely review these and other unusual transactions for financial implications.
3. The recording and reporting of capital assets has been an issue for a number of years because of the use of manually prepared spreadsheets subject to error and loss of integrity as the auditors indicate and management agrees. To this end, Department staff did perform an

additional review that identified assets recorded at \$7.5 million that should not have been recorded to infrastructure assets. Combined with accumulated depreciation of \$7.2 million, the net impact to Net Capital Assets as presented on the Statement of Net Assets was \$300 thousand. This amount was deemed immaterial by management to the total reported June 30 infrastructure amount of \$713 million.

4. a. The Department agrees with the recommendation regarding the reporting of the purchases and sales of investments offered by the auditors and will change its calculation in the future.
 - b. The Department made this adjustment regarding the transfer of the \$17 million bridge infrastructure asset to the 2011 financials and considers this observation resolved.
5. The Department made this adjustment regarding the reporting of interest subsidies for Build America Bonds to the 2011 financials and considers this observation resolved.

The Department will continue its efforts to improve its financial transaction processing and reporting. The Department continues to transit from a system of manually prepared subsidiary ledgers and spreadsheets to automated accounting systems. As automation continues (including fixed assets), staff and management will be able to prepare and interpret meaningful data and financials in a timely manner. Significant improvements have occurred as a result of the automation of certain accounting and financial processes, cash reconciliation, and improvement in overall general business practices. As these and other improvements continue, current business practices and processes too will continue to evolve and written policies and procedures will be developed and practiced. The Department continues to partner and seek the assistance and cooperation of the Comptroller's office, Financial Data Management, and State Treasury.

Significant Deficiencies

Observation No. 2: Controls Over Open Road Tolling Transactions Should Be Established

Observation:

Weaknesses exist in Turnpikes' operation of its open road tolling (ORT) system that should be addressed in a timely manner.

Turnpikes relies upon a number of information systems to determine, accumulate, and report operational and financial activity related to its open road tolling. ORT information is accumulated from the ORT system, which determines and reports vehicle types and counts; TRMI (The Revenue Markets Inc.) system, which accumulates and reports vehicle types and counts; ACS (Affiliated Computer Services), which accumulates and reports tolls collected; and the State accounting system, NHFirst, which reports Turnpikes' toll system revenues. Turnpikes performs reconciliations to ensure information from the relevant parts of the ORT system is completely and consistently accumulated and reported.

1. Even though the ORT system has been in service since June 2010, the ORT system has not been determined to have met operational acceptance testing requirements. Turnpikes reports certain technical problems have prevented Turnpikes from being able to test the accuracy of the data accumulated from the ORT system. The original completion date for operational acceptance testing was July 15, 2010. The vendor and Turnpikes set a revised deliverables schedule on May 13, 2011, which set October 20, 2011 as a revised date for completing the ORT project. That end date was also missed by the vendor. The ORT project had significant deliverables, including acceptance testing for the ORT system, outstanding at December 29, 2011.

Turnpikes reported other missing or incomplete ORT project deliverables at December 29, 2011 included finalized operations manuals, including the Disaster Recovery Plan discussed in Observation No. 5, staff training, and final system acceptance.

2. During audit planning, auditors requested data to review the results of the operational acceptance testing that had been completed. At that point, Turnpikes reported that all but six hours of night-time observation had been completed. Turnpikes could not provide documentation and data supporting all of the testing it presumed had been completed. Turnpikes reported the vendor was responsible for maintaining testing documents and the vendor could not locate documentation supporting the results of the testing done to date. The only testing support that Turnpikes could provide represented certain transactions which Turnpikes had specifically reviewed with the vendor.
3. Turnpikes reported that as of December 29, 2011 it had not formally accepted the ORT system due to the vendor's outstanding contract deliverables. Turnpikes also reported that because it had not formally accepted the ORT system, a formal change control system for the ORT system had not been implemented. Given that as of December 29, 2011 Turnpikes had

used and relied upon the ORT system to meet significant toll revenue collection responsibilities for approximately 18 months without having a formal change control process in place, Turnpikes accepted a significant risk that it may not have been made aware of all ORT system changes made by the vendor and that changes made to the ORT system may not be as understood and envisioned by Turnpike management.

4. During fiscal year 2011, Turnpikes did not perform lane audits (a comparison of observed transactions to those captured by the toll system) for transactions captured by the ORT system. Turnpikes did perform lane audits for other electronic toll transactions.

The weaknesses noted above increase the risk that Turnpikes' ORT system may not be capturing, accumulating, and reporting toll transactions accurately as Turnpikes expects and intends.

Recommendation:

Turnpikes should immediately implement appropriate controls to reasonably ensure the ORT system accurately captures, accumulates, and reports toll transactions.

1. Turnpikes should continue to work with the vendor to complete operational acceptance testing as soon as possible. Turnpikes should work with the ORT vendor to resolve the remaining outstanding contract deliverables.
2. Turnpikes should take steps to ensure records of all system-critical testing are maintained. Control procedures should be established to ensure responsible employees are aware of and comply with appropriate documentation control requirements.
3. Turnpikes should establish and maintain reasonable controls over the system, including ensuring that changes made to the system by the vendor have been reviewed, approved, tested, and accepted by responsible Turnpike officials.
4. Turnpikes should establish regular and ongoing reviews of the ORT such as standard lane audits to reasonably ensure that the ORT system is operating as intended and capturing, accumulating, and reporting toll transactions as expected and intended.

Auditee Response:

Turnpikes concurs.

The ORT system was placed into revenue service on June 17, 2010, but only after extensive Factory Acceptance Testing of the ORT system, an On-site First Installation Test and commissioning, and a temporary opening on Memorial Day 2010 validated the functional requirements of the system. All testing and system validation steps leading up to the completed opening were observed and approved by Turnpikes, HNTB (Turnpikes' consultant), and Telvent.

In accordance with the contract, subsequent to the successful completion of the On-site Installation test, Operational testing was initiated in the fall of 2010. The testing involved the

collection of streaming video, which was reviewed for vehicle passage and matched with reported data from the ORT system. Both vehicle detection and vehicle classification were confirmed. The AVI reader (E-ZPass) subsystem component of the ORT was also independently sampled, matched with reported tag data, and confirmed. All violations were reviewed for proper image capture, with multiple images confirmed to be available for violator transactions. All file transfers of the collected data were confirmed to be completely transferred to other NHDOT service providers for final processing. Based on initial estimates of the aforementioned data, the performance metrics, defined by the Contract, were measured to exceed requirements. The review and analysis of the collected data, verified by streaming video review, was completed jointly by Turnpikes, HNTB, and Telvent, and all parties were in agreement with the stated results and performance of the ORT system.

In order to fully complete the Operational testing, one hour samples during nighttime operation were also to be collected. However, it was determined that the video surveillance system was insufficient to allow close inspection of vehicle classification characteristics, namely axle count and specifically the presence of dual tires during certain nighttime hours at traveling speeds of approximately 70 miles per hour in a narrow field of view under low light levels. This has resulted in a delay in the completion of the operational testing. Telvent has identified an acceptable solution and is planning to complete the nighttime testing April 1, 2012, as well as schedule the remainder of test sampling and arrange for the same joint review that was conducted during earlier testing.

During the delay to completion of the Operational Acceptance Testing, the system has been continually monitored by its own automated systems (Nagios and ROMS), Telvent, and by Turnpike staff. During this time, additional random test sampling (logged vehicle passages), testing prior to preventative maintenance closure re-openings, and internal NHDOT audits of the system have all returned results that are consistent with the findings of all prior testing and the initial portion of the Operational Acceptance Testing as operating without issue and above Contract performance requirements.

Turnpikes is committed to work with Telvent to fully complete and document the operational testing, as well as resolve the outstanding contract deliverables. With that said, Turnpikes has not paid for the outstanding deliverable items nor has paid the toll system maintenance expense for fiscal year 2011 due to these unresolved elements.

Turnpikes does have a formal change control process in place for the entire toll system, including the ORT system. A formal change control process also exists as an element of the ORT contract with the vendor. The formal change control process for the ORT system had not been triggered due to the system technically being in the “design and implementation” phase prior to the ORT system’s formal acceptance. Under direction and prior approval of Turnpikes, only one minor change (i.e. business rule affecting ORT software) has been made to the ORT lane controller logic since the ORT opened through the present day. No other changes have been made with the exception of modifications to reports. Once the ORT system is formally accepted (anticipated July 2012), the formal change process will be followed.

Turnpikes has initiated regular and ongoing audit reviews of the ORT lanes and system as part of a larger standard audit lane process for the entire toll system that was implemented in fiscal year 2012.

Observation No. 3: Lane Audit Controls Should Be Improved

Observation:

Based upon a review of one of the quarterly lane audits performed by Turnpikes, it appears the control intended by this activity was not in place and operating as intended by management.

1. Auditors reviewed the June 2011 quarterly lane audit performed by Turnpikes staff and noted the following errors which indicate the control was not operating as intended by management:
 - Two instances were noted where transaction information (transponder number) recorded by Turnpikes staff appeared to be inaccurately recorded on the respective auditors' test sheet. While these were likely transposition errors, the errors should have been noticed and corrected when the staff traced the transaction information into the toll system (The Revenue Markets Inc. or TRMI) reports, as required by the lane auditing procedures.
 - One instance was noted where Turnpikes staff mixed information from two separate transactions into one line item, making it unclear if the selected transaction was ever tested. Again, the error should have been noticed had the staff traced the transaction information into the TRMI reports, as required by the lane audit testing procedures.
 - Four instances were noted where the times "observed" by Turnpikes staff did not match the times reported in the TRMI report. These variances were not investigated by Turnpikes staff, reportedly because the transactions went through within a few seconds of the times noted. The unexpected difference in recorded transaction times was not identified as an indicator of a potential system problem.
 - Five additional mismatch transactions were noted in the June 2011 audits that were not identified by Turnpikes lane audit staff. Had the transactions been traced to the TRMI report, these mismatches should have been noted on the test sheet.
 - One noted transaction, appearing to be a "violation" type transaction, was not identified by Turnpikes lane audit staff. Had the transaction been traced to the TRMI report, the violation transaction should have been noted and identified on the test sheet.
 - One transaction was noted which Turnpikes staff failed to identify as an "away" transaction or a transaction where the transponder was from another state. As the out-of-state status of the transponder was not identified by the Turnpikes lane auditor, data was never requested to determine if toll revenue associated with the selected transaction was ultimately collected from the other state. Had the transaction been traced to the TRMI report, the away status of this transaction should have been noticed.
 - Quarterly audit results did not include required narrative reports to management.
2. In reviewing all of Turnpikes' fiscal year 2011 lane audit results, it was noted that 51 of the 400 transactions (13%) tested by Turnpikes were identified as "mismatch" transactions.

“Mismatch” transactions occur when the vehicle class detected by the toll lane sensors does not match the vehicle class indicated by the vehicle’s transponder. Turnpikes reported that its policy is to charge the transponder account the higher vehicle class and toll rate when a mismatch is detected. The relatively large proportion (13%) of mismatch transactions detected by the lane audits may indicate an underlying problem with Turnpikes’ toll software and or equipment supporting the collection of electronic tolls.

Turnpikes stated the relatively large number of mismatches during this period was due in part to issues initially recognized in 2008 that resulted in a toll system software change, which apparently resulted in only a partial fix. When fiscal year 2011 lane audits indicated problems similar to those noted in 2008, Turnpikes’ toll lane equipment vendor investigated and discovered the 2008 corrective software change fixed only one of four error message types. It was also recognized that part of the toll monitoring system known as “MOMS” was not performing correctly, as it was not issuing system alerts when parts of the auto-scan system were not working.

These system problems likely would have been detected sooner if Turnpikes performed a reasonable review and follow-up on quarterly lane audit results and employed a reasonable change protocol which could have properly scoped the system problem in 2008 and provided for a tested and accepted change that addressed the full scope of the problem at that time.

Recommendation:

Turnpikes should review its toll lane audit protocols to ensure its policies and procedures provide for an appropriate level of controls for that critical aspect of its operation. Once satisfied that the protocols are appropriate and adequately described in policy and procedure, Turnpikes should ensure responsible employees are appropriately trained to perform the audits including being able to identify and respond to potential problems identified through the review of the test transactions.

1. Lane audits should result in documented tests and summaries of results, including possible recommendations for actions to be taken. Turnpikes’ management should review the audit results and respond to recommendations for further actions.
2. Turnpikes should resolve the system issues that appear to be contributing to the high level of mismatched toll transactions. Turnpikes should reconsider the appropriateness of always charging the higher toll rate without consideration of the potential cause of the mismatch.

Auditee Response:

Turnpikes concurs.

Turnpikes has retrained the internal audit staff on the EZPass lane audits and implemented a check and sign-off process of this audit involving three Turnpike Staff members. Also in fiscal year 2012, Turnpikes has implemented a more elaborate audit process utilizing video which

involves a large sample size (2,000 to 5,000 transactions) and checking the accuracy of the Automatic Vehicle Identification (AVI), Automatic Vehicle Classification (AVC), and Imaging systems.

Turnpikes is aware of the class mismatch issue in the lanes and has approved a software fix to address this matter that was fully implemented on February 13, 2012. This fix had been thoroughly reviewed and verified by TRMI and Turnpike staff prior to the final implementation in the field. TRMI's existing contract ends June 30, 2012 and Turnpikes has issued a request for proposal (RFP) for a new enhanced Toll Collection System which will provide an upgrade to the existing lane software and hardware. In the interim, Customers who are inappropriately overcharged will be reimbursed by our EZPass Back Office vendor as requested following a review and approval by Turnpikes.

Observation No. 4: Automated Open Road Tolling Data Transfer Error Alert Should Be Implemented

Observation:

There is no automated control to ensure all transactions initially captured by the open road tolling (ORT) system are successfully transmitted to the TRMI (The Revenue Markets Inc.) system. TRMI accumulates and reports information related to the number of vehicles, by type, passing through the toll systems.

The ORT system transfers vehicle information to TRMI hourly. TRMI transfers toll information to the ACS Vector system daily. Upon transmitting a data file to TRMI, the ORT system also sends an automatic "check file", notifying TRMI of the transmission, including check data such as the total number of transactions. Once TRMI accepts the file transmission, an automatic acknowledgement or "ack" file is sent to report the receipt of the data. If for any reason an ORT file transfer is not completed, there is no automated system control to notify Turnpikes of the missing data transfer, unless a responsible Department of Information Technology (DoIT) or Turnpikes employee notices that an expected ack file is missing. Turnpikes reports that because it may be several hours before a missing ack file is noticed, the resolution of the error is delayed, potentially increasing the required effort for correction.

Recommendation:

Turnpikes should work with the ORT vendor to implement an automatic error alert to notify DoIT or Turnpikes if ORT to TRMI data transfers fail. The control should notify responsible DoIT or Turnpikes employees immediately if an expected data transfer does not occur as expected to minimize the risk of incomplete data in the ORT system and to make error correction more efficient.

Auditee Response:

Turnpikes concurs.

It should be noted that no transactions were lost during the one instance when data was temporarily stored on the ORT server and not transferred in accordance with standard hourly protocol. Since that time, both the ORT vendor and lane vendor continually manually verify these files have been properly transferred. Turnpikes also completes spot checks and monthly checks to ensure the files are properly transferred. The ORT vendor has investigated and designed an alarm message as recommended, which is expected to be implemented by March 1, 2012.

Observation No. 5: Risk Assessment And Response Plans Should Be Established For Open Road Tolling System

Observation:

Turnpikes does not have disaster recovery and business continuity plans or a formal risk assessment process for its open road tolling (ORT) system which became operational in June 2010. While the Department of Transportation has a general continuity of operations plan, the plan does not address risks specific to the ORT system and the transactions processed by the ORT system. At December 29, 2011, a disaster recovery plan was an outstanding ORT contract deliverable.

A disaster recovery plan is essential to allow continuity of operations with minimal or no interruptions in the event of a business disruption. A formal risk assessment process allows an entity to regularly identify risks (including business, disaster, and fraud risks) which may aid the entity in the formulation of effective disaster recovery and business continuity plans.

The purpose of a disaster recovery plan is to document plans and procedures in the event of a disaster, including disaster recovery strategies, essential resources, and procedures necessary to implement a recovery process. The purpose of a business continuity plan is to document plans and procedures in the event of a significant change in the way a business conducts its daily business functions.

Without a formal risk assessment process and responsive disaster recovery and business continuity plans, Turnpikes may be forced into a reactive, rather than proactive, approach when situations arise. Specifically, Turnpikes is at an increased risk that its ORT business functions, including ability to collect toll revenue, may be impacted by a foreseeable incident. Lack of effective planning may hamper Turnpikes' ability to respond effectively and timely to any ORT system failure that may occur.

Recommendation:

Turnpikes should establish disaster recovery and business continuity plans, and train its employees in the use of those plans.

Turnpikes should implement a formal risk assessment process for risks specific to the new ORT system.

The need for a well-considered risk assessment process and disaster recovery and business continuity plans will become even more important as Turnpikes expands its use of ORT plazas, increasing business risks associated with those operations.

Auditee Response:

Turnpikes concurs.

A draft Disaster Recovery Plan for Turnpikes' review was received on February 10, 2012 with the plan expected to be reviewed and finalized by April 2012.

The Disaster Recovery Plan will include risks associated with the ORT system and preventive measures to mitigate said risk. The plan goals will include the following key elements:

- Minimize interruption to normal operations,
- Limit extent of disruption and damage,
- Minimize the economic impact of an interruption,
- Establish alternative means in advance of an interruption,
- Train personnel on emergency procedures, and
- Provide for smooth and rapid restoration of service.

Observation No. 6: Controls Over Accounting For Replaced, Sold, Or Unserviceable Capital Assets Should Be Improved

Observation:

Turnpikes does not have adequate policies and procedures in place to ensure compliance with its policy regarding the removal of capital assets that are replaced, sold, or otherwise are of no service to Turnpikes.

Turnpikes has a policy stating that when older capital assets are replaced, they should be removed from their respective capital asset listings; however, Turnpikes has not established adequate policies and procedures to ensure Turnpikes business office employees become aware of, and properly account for, capital assets that are replaced, sold, or otherwise are of no service to Turnpikes. As a result, certain capital assets have remained on Turnpikes' capital asset listings and in Turnpikes' reported capital asset balances subsequent to the assets being replaced.

Auditors requested Turnpikes review its capital asset listings for assets that remained on the listings even though they likely had been replaced. In answering this information request, Turnpikes focused on bridges as assets that would be most susceptible to this type of error.

Through its review of likely replaced bridges, Turnpikes identified four infrastructure assets totaling \$7.5 million, with an associated \$7.2 million of accumulated depreciation, that likely no longer exist. These assets are included on Turnpikes' June 30, 2011, Statement of Net Assets.

Recommendation:

Turnpikes should establish policies and procedures to ensure compliance with its policy regarding the removal of capital assets that are replaced, sold, or otherwise are of no service to Turnpikes. These policies and procedures should promote the capture and communication of relevant financial information between Turnpikes employees knowledgeable of construction, operations, and accounting and financial reporting activities to reasonably ensure that information related to changes in those activities, including changes affecting Turnpikes' financial reporting, is timely and effectively captured, communicated, understood, and where appropriate, reflected in the accounting records and financial reporting of Turnpikes.

Turnpikes should continue with its review of fixed assets to determine, recognize, and appropriately adjust the financial records for assets that have been replaced, sold, or otherwise are of no service to Turnpikes. This review should include all asset types including buildings, roadways, interchanges, as well as bridges.

Auditee Response:

Turnpikes concurs.

The Department has policies and procedures in place regarding the removal of capital assets and agrees that effective compliance of this policy needs to be better communicated to both program staff and Finance. The current process in the project "paper trail" makes it difficult for staff members of Finance to ascertain clearly, what part of the project is replaced, maintained, or enhanced for capital recognition purposes. To address this and other issues, the Department has a plan in place to address the recording of Fixed Assets and have in place by June 30, 2012, an automated fixed assets module. This module will replace the current accounting practice of manually preparing spreadsheets that are subject to error. To this end, Department staff did perform an extra review that identified assets recorded at \$7.5 million that should not have been recorded to infrastructure assets as indicated by the auditors. However, combined with accumulated depreciation of \$7.2 million, the net impact to Net Capital Assets as presented on the Statement of Net Assets was \$300 thousand. This amount was deemed immaterial by management to the reported June 30 infrastructure amount of \$713 million.

Observation No. 7: Controls Over Monthly Revenue Reconciliations Should Be Improved

Observation:

Turnpikes has not established a review and approval control over its monthly revenue reconciliation process. While Turnpikes has policies and procedures addressing the performance of monthly revenue reconciliations, the results of the reconciliations are not reviewed and approved by anyone other than the preparer.

A Turnpikes employee prepares a monthly revenue reconciliation that compares revenues reported as collected by the toll systems to amounts deposited into Turnpikes' bank accounts. The preparer of the reconciliation reports the use of an acceptable difference threshold of a plus or minus of three percent. If the difference between revenue reported as collected and revenue deposited is less than the acceptable difference, the cause of the variance likely will not be reviewed further. According to the employee who prepares the reconciliation, the unwritten policy requires differences greater than the acceptable variance amount to be researched and resolved. The completed reconciliations are filed by the employee who prepares them, with no review or approval control applied by another Turnpikes employee.

Recommendation:

Turnpikes should establish a review and approval control over its monthly revenue reconciliation process. Also, Turnpikes should consider all significant differences identified during the monthly revenue reconciliations and should investigate variances that exceed set thresholds or otherwise appear unusual. Evidence of the considerations, explanations, and resolution of significant variances should accompany each reconciliation. Turnpikes should monitor the reconciliation process to ensure that reconciliations are occurring as intended and significant differences are identified and resolved.

Auditee Response:

Turnpikes concurs.

Turnpikes agrees the Revenue Reconciliation from Toll Collection System (TRMI) and EZPass (ACS) Reports to the State accounting system (NHFirst) should be prepared by one person but reviewed and approved by someone else. Turnpikes has begun this process for fiscal year 2012. The Business Manager will be preparing the reconciliation and the Financial Manager will be reviewing, approving and signing off on it.

The reconciliation is a complex process. The primary ACS report reflects E-ZPass revenue by collection date. Turnpikes records revenue when it is posted to a NH customer's account or when it is received from other agencies through the reciprocity process. These timing differences are recognized, documented and reviewed for reasonableness. An important step in the monthly reconciliation has always been to verify that the correct amount of revenue posted or received has been entered into the correct NHFirst account. Any errors are documented and corrected promptly.

It must be said, however, that the manner in which NHFirst “summarizes” multiple transactions makes the reconciliation process even more cumbersome.

At the end of the fiscal year, all of the reports are rerun on the same date and a final reconciliation is done. The reports could be rerun on a monthly basis, but it would involve rerunning one to twelve months of reports each time. Three percent has been deemed an acceptable variance for interim months. The year end reconciliation was forwarded to Finance and Contracts in August 2011 for their review and approval in the closing process.

The final Fiscal Year 2011 variances were:

- Cash Revenue: \$8.99 less than \$44,624,032.42 reported by TRMI,
- E-ZPass Revenue: \$135.11 more than \$72,172,929.12 reported by ACS, and
- E-ZPass Prepaid Toll: \$59,462.41 less than \$7,953,504 reported by ACS (less than 1%).

The reconciliation of Prepaid Tolls has determined that the variance is not due to deposits of account replenishments, which are reconciled monthly. The amount transferred from prepaid tolls to the E-ZPass revenue accounts was also verified as correct. The difference is attributed to timing of reciprocity payments or timing of settlements by credit card deposits.

ACS is now in the process of upgrading its reports, which will be available for use in fiscal year 2013. Turnpikes is involved with the conversion and has identified the reconciliation as an area that needs improvement. In the meantime, Turnpikes will look at the process again to see if there are additional reports available to reduce the variance.

Observation No. 8: Effective Monitoring Controls Over Account Reconciliations Should Be Established

Observation:

A \$560,000 overstatement of Turnpikes’ cash first noted on a December 2009 State Treasury bank reconciliation was not corrected until November 2011, subsequent to an auditor inquiry.

In a combined June 30, 2011 reconciliation of Turnpikes’ System Escrow and Debt Service Accounts, State Treasury reported a book balance of \$560,000 in accounts that were closed in November 2010. The \$560,000 balance was carried as a reconciling item on monthly account reconciliations from December 2009 until the error was corrected in November 2011. Upon research, State Treasury determined certain transactions which should have been posted as reductions to the book cash balance and increases in bond interest expense on the State’s books in December 2009 were not recorded.

Turnpikes reported it was unaware of the difference until notified by the auditors. The book balances were adjusted and the reconciling item was cleared in November 2011, subsequent to the auditor’s inquiry.

Recommendation:

Turnpikes should establish more effective monitoring controls over Turnpikes account reconciliations performed by the State Treasury. Turnpikes should review all cash and other reconciliations of Turnpikes accounts performed on its behalf by State Treasury to ensure that all recognized differences are resolved timely.

Auditee Response:

Turnpikes concurs.

Treasury and Turnpikes have worked collaboratively to establish more effective monitoring controls over Turnpikes account reconciliations performed by the State Treasury and a procedure was approved and adopted. The Department considers this observation resolved.

State Treasury Response:

Treasury concurs and believes this observation is fully resolved. Treasury and Turnpikes meet regularly and have worked very closely developing procedures mutually agreed upon. All Turnpikes related account reconciliations are now performed timely by Treasury and are forwarded to the Department of Transportation upon completion.

Observation No. 9: Payments Should Be Based On Services Received, Not Budgeted Amounts

Observation:

During fiscal year 2011, Turnpikes made payments for certain services provided by other State organizations based on budgeted amounts and not the costs of services received.

- Turnpikes overpaid the Department of Safety approximately \$700,000 for traffic enforcement on the Turnpike System. This payment error resulted from Turnpikes paying the budgeted amount instead of the actual costs of the services received. Upon the auditor's inquiry regarding the paid amount, Turnpikes recovered its overpayment.
- Turnpikes underpaid the Department of Transportation approximately \$327,000 for indirect costs. This payment error resulted from Turnpikes paying the budgeted amount instead of the amount determined by applying the indirect cost rate. Turnpikes did not correct its underpayment.
- Upon the auditor's inquiry into the above-mentioned payment errors, Turnpikes reviewed similar transactions. In its review, Turnpikes determined it had overpaid the Department of Transportation by approximately \$132,000 for sign, traffic, and bridge maintenance costs. This payment error also resulted from Turnpikes paying the budgeted amount instead of the actual cost of services received. Turnpikes recovered the overpayment. In reviewing the supporting documentation related to the error and error correction, auditors noted an

additional overpayment error of approximately \$68,000 which had not been detected and corrected by Turnpikes.

Recommendation:

Turnpikes should establish policies and procedures for making payments for services received from other governmental organizations.

Turnpikes should coordinate with those other governmental organizations to ensure costs of services are accurately determined and recorded in the accounts and accounting records used by Turnpikes to make payments for those services.

Auditee Response:

Turnpikes concurs.

For fiscal year 2011, Turnpike Funds as a budgeting source to other agencies was for the first time, recorded at the gross legislative approved appropriation level and not at the expenditure level as performed in prior years. A follow-up lapse adjustment from budget to actual did not occur at year-end. The Department will communicate with the Department of Administrative Services, Bureau of Accounts, in the future to ensure this is performed.

Additionally, the Department computes an internal indirect cost calculation initially based on budgeted amounts. The Department will perform a true-up to actual at year-end.

State Compliance Comments

Observation No. 10: Accounts Should Be Utilized As Provided In General Bond Resolution Requirements

Observation:

During fiscal year 2011, Turnpikes was not in full compliance with certain requirements in the General Bond Resolution related to the transfer of funds between required accounts. The General Bond Resolution (GBR) adopted in 1987 by the Governor and Council authorized the issuance of Turnpike System revenue bonds and describes the structure, accounting, and a number of other requirements for the bonds. The GBR has been amended and supplemented several times since 1987. Article III of the GBR requires the State to have certain accounts and to apply Turnpike revenues in a certain order or priority, after payment of operating expenses, to protect bondholders.

- Pursuant to section 3.3 of the GBR, the State is to pay from the Revenue Account to the Debt Service Account, no later than the 20th of each month, an amount necessary to adequately fund the upcoming principal and interest payments. Four of 12 monthly transfers from the Revenue Account to the Debt Service Account during fiscal year 2011 were not made timely, contrary to section 3.3 of the GBR.
- Pursuant to section 3.7 of the GBR, the State is to maintain a General Reserve Account into which excess funds in the Revenue Account, after paying operating expenses and deposits required by Article III of the GBR, are to be transferred by the 20th of each month. Amounts in the Reserve Account are to be used for the payment of renewal and replacement costs, payment of general obligation bonds, payments to the construction account, as well as for other purposes stated in the GBR. However, prior to May 2011, the State did not utilize a General Reserve Account consistent with the GBR or transfer excess funds from the Revenue Account to the General Reserve Account. Turnpikes' renewal and replacement and other costs were paid directly from the Revenue Account. Because the required transfers were not made, the working capital limit in the Revenue Account of 25% of budgeted operating expenses, noted in section 3.2 of the GBR, was exceeded during the period July 2010 through April 2011.

Recommendation:

Turnpikes should continue to work with State Treasury to establish policies and procedures that promote compliance with the GBR requirements for maintaining and operating Turnpikes accounts to record Turnpikes toll revenue.

Transfers among Turnpikes' accounts should occur as required by the GBR.

Payments should be made from the accounts specified in the GBR.

Auditee Response:

Turnpikes concurs.

The Department concurs that all requirements of the GBR should be met and it continues to work closely with the State Treasury to implement policies and procedures. The Department and Treasury meet regularly to address covenant compliance issues. These meetings are very productive in identifying and understanding covenant requirements and much improvement has occurred over the past year. This effort will continue to ensure covenant requirements are successfully addressed.

State Treasury Response:

Treasury concurs.

Treasury has and continues to work closely with the Turnpike System to implement policies and procedures to ensure compliance. In so doing, Turnpike and Treasury have put in place many controls and documented procedures. Treasury and Turnpike meet on a monthly basis and, in November of 2010, Treasury transitioned to a new trustee and paying agent to handle receipt and accounting for debt service payments.

The amount to be transferred monthly from the Revenue Account to the General Reserve Account will no longer be made net of renewal and replacement costs, as is currently the practice done for administrative ease. In order to strictly comply with the GBR, a gross amount will be transferred to the General Reserve Account and a second transfer will be made out of the General Reserve Account to cover the cost of renewal and replacement for the month. It is expected full compliance will be attained when the monthly transfers are made by March 20, 2012.

Observation No. 11: Transponder Inventory Fund Should Not Exceed Statutory Limit

Observation:

The balance in Turnpikes' transponder inventory fund at June 30, 2011 exceeded the \$1,000,000 fund limit in statute.

RSA 228:24-d states, "There is hereby established an electronic toll collection transponder inventory fund not to exceed \$1,000,000..." While not explicitly stated in the statute, amounts in excess of the statutory limit would presumably lapse to the Turnpikes' fund balance.

At June 30, 2011, the balance in Turnpikes' transponder inventory fund exceeded the \$1,000,000 maximum set in statute by approximately \$110,000. The balance of the fund at June 30, 2011 was comprised of a \$627,000 available balance in the State's accounting system (NHFirst) plus approximately \$483,000 of transponders in inventory.

According to Turnpikes, it considers the balance in the fund to be the available balance in NHFirst. It does not include the cost of transponders in inventory in determining the balance in the transponder inventory fund.

Recommendation:

Turnpikes should limit the transponder inventory fund to the statutory fund limit. Excess amounts in the fund should be lapsed to Turnpikes' fund balance.

Auditee Response:

Turnpikes concurs.

Turnpikes will transfer any excess to Turnpike fund balance if the account exceeds the statutory limit and considers this observation resolved.

APPENDIX

Current Status Of Prior Audit Findings

The following is a summary of the status, as of December 29, 2011, of the observations contained in the New Hampshire Turnpike System Management Letter for the fiscal year ended June 30, 2010. That report can be accessed at, and printed from, the Office of Legislative Budget Assistant website: http://www.gencourt.state.nh.us/LBA/AuditReports/ContractedAudits/Turnpike_SystemML_2010.pdf.

	<u>Status</u>		
<i>Internal Control Comments</i>			
<i>Material Weaknesses</i>			
1. Financial Accounting and Reporting (<i>See Current Observation No. 1</i>)	●	○	○
2. Cash Reconciliations (<i>See Current Observation No. 8</i>)	●	●	○
<i>Internal Control Comments</i>			
<i>Significant Deficiencies</i>			
3. Journal Entry Approval	●	●	●
4. Debt Covenant Compliance (<i>See Current Observation No. 10</i>)	●	●	○
5. Toll Reconciliations	●	●	●
6. Review and Transfer of Completed Projects	●	●	●

<u>Status Key</u>	●	●	●	<u>Count</u>
Fully Resolved	●	●	●	3
Substantially Resolved	●	●	○	2
Partially Resolved	●	○	○	1
Unresolved	○	○	○	0

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