

**STATE OF NEW HAMPSHIRE
LOTTERY COMMISSION**

**MANAGEMENT LETTER
FOR THE FISCAL YEAR ENDED JUNE 30, 2020**



MICHAEL W. KANE, MPA
Legislative Budget Assistant
(603) 271-3161

State of New Hampshire

CHRISTOPHER M. SHEA, MPA
Deputy Legislative Budget Assistant
(603) 271-3161

OFFICE OF LEGISLATIVE BUDGET ASSISTANT
State House, Room 102
Concord, New Hampshire 03301

STEPHEN C. SMITH, CPA
Director, Audit Division
(603) 271-2785

To The Fiscal Committee Of The General Court:

We have audited the financial statements of the New Hampshire Lottery Commission (Lottery) as of and for the fiscal year ended June 30, 2020 and have issued our report thereon dated December 22, 2020.

This management letter, a byproduct of the audit of the New Hampshire Lottery Commission for the fiscal year ended June 30, 2020, contains our auditor's report on internal control over financial reporting and on compliance and other matters and related audit findings. The appendix to this letter, on page 10, provides a summary of the status of observations presented in the fiscal year 2019 and fiscal year 2018 Lottery Commission management letters.

The Lottery is again submitting its comprehensive annual financial report (CAFR) to the Government Finance Officers Association (GFOA) for consideration for the GFOA's Certificate of Achievement for Excellence in Financial Reporting. A certificate of achievement is a prestigious national award for CAFRs that are prepared in accordance with program standards. The program standards are intended to promote easily readable and understandable financial reports that demonstrate financial accountability and comparability. The Lottery received GFOA certification for its 2019 CAFR, and it is believed that the 2020 CAFR also conforms to the certificate of achievement program requirements. A copy of the Lottery's 2020 CAFR can be obtained from the New Hampshire Lottery Commission, 14 Integra Drive, Concord, NH 03301. The Lottery CAFR can also be accessed online at:

http://www.gencourt.state.nh.us/LBA/AuditReports/FinancialReports/pdf/Lottery_2020_CAFR.pdf

Office of Legislative Budget Assistant

Office Of Legislative Budget Assistant

December 22, 2020

**STATE OF NEW HAMPSHIRE
LOTTERY COMMISSION
2020 MANAGEMENT LETTER**

TABLE OF CONTENTS

	<u>PAGE</u>
Letter Of Transmittal.....	i
Independent Auditor’s Report On Internal Control Over Financial Reporting And On Compliance And Other Matters Based On An Audit Of Financial Statements Performed In Accordance With <i>Government Auditing Standards</i>	1
<i>Internal Control Comments *</i>	
<i>Significant Deficiencies</i>	
1. Lottery Should Continue To Develop The Division Of Sports Wagering And Strengthen Controls Over Mobile Sports Betting.....	3
2. Independent Service Auditor’s Report Over Mobile Sports Betting Activities Should Be Obtained And Reviewed	4
3. Building Access Controls Should Be Strengthened And Procurement Of A New Access Control System Should Continue	5
<i>Compliance Comments</i>	
<i>State Compliance</i>	
4. Statements of Financial Interests Should Be Filed As Required By Statute.....	7
APPENDIX - Current Status Of Prior Audit Findings	10

* No 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>

Abbreviations

ACS	Access Control System – controls and monitors facility access
CUEC	Complementary User Entity Controls – essential part of SOC audit report of controls required to be implemented by user entity (entity that utilizes a service organization)
ICS	Internal Control System – redundant games processing system
RFP	Request For Proposal
SOC	Service Organization Control audit report
UAT	User Acceptance Testing



MICHAEL W. KANE, MPA
Legislative Budget Assistant
(603) 271-3161

CHRISTOPHER M. SHEA, MPA
Deputy Legislative Budget Assistant
(603) 271-3161

State of New Hampshire

OFFICE OF LEGISLATIVE BUDGET ASSISTANT
State House, Room 102
Concord, New Hampshire 03301

STEPHEN C. SMITH, CPA
Director, Audit Division
(603) 271-2785

Independent Auditor's Report On Internal Control Over Financial Reporting And On Compliance And Other Matters Based On An Audit Of Financial Statements Performed In Accordance With *Government Auditing Standards*

To The Fiscal Committee Of The General Court:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the New Hampshire Lottery Commission (Lottery) which comprise the Statement of Net Position as of June 30, 2020 and the related Statements of Revenues, Expenses, and Changes in Net Position and Cash Flows for the fiscal year then ended, and the related notes to the financial statements, which collectively comprise the Lottery's basic financial statements, and have issued our report thereon dated December 22, 2020.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Lottery's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Lottery's internal control. Accordingly, we do not express an opinion on the effectiveness of the Lottery'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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. 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. We did identify certain deficiencies in internal control that we consider to be significant deficiencies. We consider the deficiencies described in Observations No. 1 through No. 3 to be significant deficiencies.

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the Lottery's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, rules, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance or other matter that is required to be reported under *Government Auditing Standards* and which is described in Observation No. 4.

Lottery Commission's Responses To Findings

The Lottery's responses to the findings identified in our audit are included with each reported finding. The Lottery's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose Of This Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Lottery'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 Lottery's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Office Of Legislative Budget Assistant

December 22, 2020

Internal Control Comments
Significant Deficiencies

Observation No. 1: Lottery Should Continue To Develop The Division Of Sports Wagering And Strengthen Controls Over Mobile Sports Betting

Observation:

Lottery had neither an established Division of Sports Wagering, nor an adequate internal control structure in place to accurately calculate and reconcile revenue prior to the launch of the mobile sports betting platform in December 2019.

RSA 287-I became effective on July 12, 2019, authorizing sports wagering activities to be offered within the State of New Hampshire, and further directing the Lottery to “create a division of sports wagering which will be responsible for ensuring compliance with the requirements of this chapter and any rules promulgated by the commission in accordance with the authorities granted under this chapter”.

In December of 2019, Lottery contracted with a third-party vendor to provide a mobile platform which allows players within the geographical borders of the State to place wagers on various professional, collegiate, and amateur sporting events. The vendor is responsible for providing the entirety of the mobile sports betting platform, including the managing of player accounts, wagers, etc. Without an established Division of Sports Wagering in place, responsibilities for the implementation and supervision of the mobile sports betting platform were distributed amongst existing Lottery staff, adding to their already considerable responsibilities.

Lottery’s contract with the vendor called for a weekly settlement of funds. However, over the first few weeks of operations, significant discrepancies were noted between Lottery’s expected amounts due, and the actual amounts remitted. During investigation into the variances, it was determined that Lottery had received overpayments in sports betting revenues amounting to \$879,000 during the period of January – February 2020. A coding error within the vendor’s system that incorrectly accounted for promotional wagers when calculating the portion of gross gaming revenue due to Lottery was the cause of the overpayment. The coding error was subsequently corrected, and a contract change order was executed to move from weekly to monthly settlements of funds to allow for a more effective reconciliation process.

While Lottery employees have documented the procedures required to reconcile mobile sports betting revenues, a formal management-approved policy and procedure has not been developed.

The Lottery hired a Director for the Division of Sports Wagering in August 2020, and as of the date of this report, continues in its development of the Division.

Recommendation:

Lottery should continue the development of its Division of Sports Wagering to ensure compliance with statute and administrative rule.

Lottery should take steps to develop and formally document policies and procedures for the major activities of the Division, including, but not limited to monthly reconciliations of mobile sports betting revenues, and its expansion into physical sports betting and existing retailer locations. Policies and procedures should include a monitoring control to ensure the documented processes continue to operate as intended and remain relevant; and should be approved by management and effectively communicated to responsible employees.

Auditee Response:

We concur.

The New Hampshire Lottery Commission successfully launched the mobile sports betting program six months earlier than planned and prior to the hiring of the director of sports betting. At the time of launch, the Lottery Commission had procedures in place relating to the mobile sports betting program, including the reconciliation of the weekly settlement of funds. Within the first several weeks, we discovered that our vendor did not complete their reconciliation until the end of the month which resulted in inaccurate weekly payments to the Lottery Commission. That issue was resolved with a contract change order and updated procedures. As noted, the Lottery Commission has hired a director of sports betting and has established policies and procedures for both mobile and retail sports wagering activities.

Observation No. 2: Independent Service Auditor's Report Over Mobile Sports Betting Activities Should Be Obtained And Reviewed

Observation:

Lottery did not receive a service auditor's report on the controls in place for its mobile sports betting activities, which began operations in late December 2019.

Lottery contracted with a vendor to provide its mobile sports betting platform, which went live on December 30, 2019. The initial Request For Proposal included a requirement for the vendor's annual provision of a Service Organization Control (SOC) 1, Type 2 report.

Management is responsible for establishing and maintaining a system of internal control for both internal operations, and contracted operations. When management intends to rely on a service organization's internal controls, its responsibilities extend to understanding the design and operating effectiveness of those controls in place at the service organization. Such understanding is often accomplished by obtaining and reviewing a SOC report known as a SOC 1 Type 2 report and ensuring that the required complementary user entity controls (CUECs) noted within the report are in place at the user entity.

The vendor did provide the Lottery with a report evidencing an ISO 27001 certification (an international standard that sets specifications for a best practice approach to design and certify an Information Security Management System) which it believed to be sufficient to ensure confidentiality and security of mobile sports betting transactions. However, the ISO 27001 certification does not report on the operating effectiveness of internal controls over financial reporting, and therefore does not allow the Lottery to rely upon it to gain comfort over the completeness and accuracy of financial transactions processed by the mobile sports betting system.

Lottery reports that at its request, the vendor has indicated they will obtain and provide a SOC 1 Type 2 report to Lottery for fiscal year 2021.

Recommendation:

Lottery should consider a contract change order with the vendor to require the annual provision of a SOC 1 Type 2 report and its submission to Lottery for review.

Lottery should implement policies and procedures to review and assess risks associated with outsourced services, including when SOC 1 Type 2 reports should be written into contracts and ensuring, when applicable, relevant CUECs identified by a third party are in place and operating effectively.

Auditee Response:

We concur.

The vendor has agreed to provide the SOC 1 Type 2 report annually.

Observation No. 3: Building Access Controls Should Be Strengthened And Procurement Of A New Access Control System Should Continue

Observation:

Lottery's monthly and quarterly reviews of draw room access logs were ineffective; and failed to detect system-wide lapses in recording access. Additionally, Lottery is unable to ascertain the reason behind the lapses, as the Access Control System (ACS) software is no longer supported by the vendor.

Lottery monitors draw room access to ensure the integrity of the draw equipment and balls used for Tri-State Lottery games drawings, and to verify that no unauthorized access occurred. Lottery reports that management reviews draw room access logs on a monthly and quarterly basis. Neither of the reviews completed for the month or quarter ended March 31, 2020 were successful in detecting two instances during which the ACS failed to record entry information.

Auditor review of draw room access logs created by the ACS for the month of March 2020 detected two instances where the ACS did not properly log employee entrance to the building and other

secured areas within the building for an extended period of time. Management reported that, while building access was not properly logged during these times, building security itself did not appear to have been disrupted and a review of logs provided by the building's Intrusion Detection System (alarm system) revealed no apparent inappropriate security access.

During fiscal year 2020, Lottery had been in the process of procuring a new access control system, which was ultimately delayed due to the COVID-19 pandemic. Lottery reports it will move forward with issuing a Request For Proposal (RFP) for a new security system.

Recommendation:

Lottery should continue to take steps to procure and implement a new access control system.

Lottery should review its current procedures for monitoring employee access to the draw room to determine why the March 2020 and third quarter reviews of draw room entries failed to recognize the ACS's lapses in logging of employee access. Once an understanding has been obtained, Lottery should revise its current process to ensure that it includes procedures to determine that the access logs under review are complete. The revised procedures should be formally documented in a policy approved by management.

Additionally, the Lottery should further consider whether to expand its review to include access to all secured areas within the building, rather than limiting its review of access logs to only the draw room.

Auditee Response:

We concur.

An access control RFP was released in January of 2021 with the expectation that work will take place in April-May of 2021. The issues identified with respect to the draw room access review were a result of technical failures or limitations with the legacy system. The Lottery Commission plans on reviewing its' access control policies and procedures based on technical capabilities and reporting once the new system is installed.

Compliance Comments
State Compliance

Observation No. 4: Statements Of Financial Interests Should Be Filed As Required By Statute

Observation:

Three of five individuals assigned to the Council for Responsible Gambling (Council), which is administratively attached to the Lottery, did not have statements of financial interests on file with the Secretary of State for fiscal-year 2020, as required by RSA 15-A. Additionally, one Council member, filed the required statement ten months late.

Members of the Council for Responsible Gambling are required filers under RSA 15-A:3, I (c) as they represent individuals appointed by the Governor and Council to an equivalent state entity that is regulatory, advisory, or administrative in nature.

Statements of financial interests are due annually by the third Friday in January, or within 14 days of assuming office or appointment. For calendar year 2020, statements of financial interests were required to be filed with the Secretary of State no later than January 17, 2020.

Members of the Council for Responsible Gambling were appointed during September and October 2019, and therefore should have completed their initial filing no later than October 16, 2019; and for calendar year 2020 filings no later than January 17, 2020.

During review of statement of financial interest filings, the following was noted:

- None of the five appointed Council members filed statements of financial interests within 14 days of their initial appointment in September or October 2019.
- As of December 2020, three of the five Council members did not have calendar year 2020 statements of financial interests on file with the Secretary of State.
- One Council member submitted the statement of financial interests in November 2020, ten months late.

Lottery's Executive Director, as well as all Lottery Commissioners filed statements of financial interests in a timely manner.

Recommendation:

The Council should establish procedures to ensure all administratively attached Council members submit statements of financial interests by the required filing deadline in accordance with RSA 15-A:3, I (c). As part of these procedures, Lottery should consider sending annual reminders to Council members to remind them of the filing requirements.

Auditee Response:

We concur.

Pursuant to RSA 21-G:10 – An Administratively Attached Agency must “(a) Exercise its powers, duties, functions and responsibilities independently of the department and without approval or control of the department.” Accordingly, while the Lottery Commission agrees to remind the Council for Responsible Gambling of its’ obligations and facilitate collection of the required statements of financial interests, we do not have authority to compel compliance from an administratively attached agency.

Council for Responsible Gambling’s Response:

We concur.

The Council for Responsible Gambling was sworn into their positions for the first time on November 23, 2019. The Chairman of the Council, Maura McCann, collected and filed statements of financial interests for all five members as a single submission before the January 2020 deadline. We only learned at the time of the audit that the Secretary of State only marked two of these statements as having been received. In order to avoid this issue in the future, the Council will clearly indicate by cover letter that the filing is for multiple individuals and will confirm with the Secretary of State that these have been received.

THIS PAGE INTENTIONALLY LEFT BLANK

APPENDIX

Current Status Of Fiscal Years 2019 And 2018 Audit Findings

The following is a summary of the status, as of December 22, 2020, of the observations contained in the New Hampshire Lottery Commission Management Letters for the fiscal years ended June 30, 2019 and 2018. Those reports can be accessed at, and printed from, the Office of Legislative Budget Assistant website: www.gencourt.state.nh.us/LBA/AuditReports/FinancialReports.aspx.

		<u>Status</u>
2019 Audit Comments		
Internal Control Comments		
<i>Significant Deficiencies</i>		
2019-1	Expand Scope Of Service Auditor’s Report And Enhance Design Of Complementary User Entity Controls <i>Request the gaming system service provider require the iLottery platform vendor provide a SOC 1 Type 2 report annually, submit it for review, and implement policies and procedures to review and assess risks associated with outsourced services, including ensuring any relevant CUECs identified by a third party are in place and operating effectively</i>	● ●
2019-2	Contracts Amendments Should Be Submitted To Governor And Council For Approval <i>Implement adequate review and approval controls to ensure all contract amendments are executed in accordance with contract terms, and are submitted to Governor and Council for approval, as required by Manual Of Procedures Chapter 150 Section V.B.1</i>	● ●
2019-3	Interest Calculation For Lottery Funds On Deposit With State Treasury Should Be Supported <i>Request the State Treasury to provide supporting documentation for the annual calculation of net interest income allocated to the Lottery Fund to ensure the accuracy of the amount received</i>	● ○
Compliance Comments		
<i>State Compliance</i>		
2019-4	Review Authority For iLottery Incentive Payments <i>Seek clarification from legal counsel to determine if the current Retailer Incentive Policy for iLottery Sales is compliant with RSA 284:21-s</i>	● ●
2019-5	Seek Clarification Of Statute Requiring Percentage Of Breakage To Be Paid To State Treasury <i>Review with legal counsel whether depositing ¼ of breakage revenue with the State Treasury, for the use of the State as required by RSA 284:22, IV, is in compliance with Part 2, Article 6-b of the State Constitution and RSA 284:21-j</i>	● ○

Status

2018 Audit Comments

Internal Control Comments

Significant Deficiencies

2018-1	Strengthen Contract Monitoring Controls <i>Establish sufficiently independent contract monitoring controls to ensure that advertising contract is operating as intended</i>	●	●
2018-2	Review Use Of Keno Proceeds <i>Review with legal counsel whether the use of Keno lottery proceeds required by RSA 284:47 is in compliance with Part 2, Article 6-b of the State Constitution</i>	●	●
2018-3	Complete The Development And Implementation Of the Games of Chance Information System <i>Monitor the completion and implementation of Games of Chance information system to ensure the Lottery has the information systems, and controls needed to securely manage its operations</i>	●	●

Status Key

			<u>Count</u>
Fully Resolved	●	●	6
Remediation In Process (action beyond meeting and discussion)	●	○	2
Unresolved	○	○	0

Review Of Lottery Information Technology System General Controls Over ICS And Complementary User Entity Controls Within Gaming System Service Provider's Service Organization Control (SOC) Report

Status

2019 Internal Control Comments - Information Technology - Significant Deficiencies

I. ICS Application

A. Improve Procedures Over Data Center Access Listing Review

● ○

Establish a procedure to ensure a review of a complete and accurate listing of data center users is performed, in order to determine access is appropriately restricted based on job function and related responsibilities

B. Improve Monitoring Controls Over Server Backups

● ○

Design and implement control procedures to monitor the successful completion of backups, and to ensure failed backups are investigated, resolved, and re-run to successful completion

II. Gaming System Service Provider CUEC

A. Formally Document Management Approval Of User Acceptance Testing For System Changes

● ○

Formally document UAT (user acceptance testing) approvals in its change management process to ensure UAT is completed

B. Seek Clarification And Document Applicability Of LOTOS Access

○ ○

Work with the gaming system vendor to obtain a complete and accurate understanding of what the CUECs are, and how they relate to the control objectives. Once clarified, implement policies and procedures to ensure CUECs are suitably designed, effectively implemented, and sufficiently documented

Status Key

Count

Fully Resolved	●	●	0
Remediation In Process (action beyond meeting and discussion)	●	○	3
Unresolved	○	○	1

THIS PAGE INTENTIONALLY LEFT BLANK