

**STATE OF NEW HAMPSHIRE  
LIQUOR COMMISSION**

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





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### *To The Fiscal Committee Of The General Court:*

We have audited the financial statements of the New Hampshire Liquor Commission as of and for the fiscal year ended June 30, 2020 and have issued our report thereon dated December 18, 2020.

This management letter, a byproduct of the audit of the New Hampshire Liquor 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, beginning on page 10, provides a summary of the status of observations presented in the fiscal year 2019 and the fiscal year 2018 Liquor Commission management letters.

The New Hampshire Liquor Commission's fiscal year 2020 Comprehensive Annual Financial Report can be accessed online at:

[http://www.gencourt.state.nh.us/LBA/AuditReports/FinancialReports/pdf/Liquor\\_2020\\_CAFR.pdf](http://www.gencourt.state.nh.us/LBA/AuditReports/FinancialReports/pdf/Liquor_2020_CAFR.pdf)

*Office of Legislative Budget Assistant*

Office Of Legislative Budget Assistant

December 18, 2020

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

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\* No audit comments suggest legislative action may be required.

This report, and all other LBA-issued financial audit reports, can be accessed in its entirety on-line at: <http://www.gencourt.state.nh.us/LBA/AuditReports/FinancialReports.aspx>

**Abbreviations Used**

|         |  |
|---------|--|
| CFO     | Chief Financial Officer  |
| GASB    | Governmental Accounting Standards Board                                      |
| IT      | Information Technology   |
| MAPPER  | Current front and back office, point of sale information system              |
| NextGen | New point-of-sale, E-commerce, warehouses, and back office financial systems |
| NHFirst | New Hampshire state government accounting system                             |



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### **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 Liquor Commission (Commission) which comprise the Statement of Net Position as of June 30, 2020 and the Statements of Revenues, Expenses and Changes in Net Position and Cash Flows for the year then ended, and the related notes to the financial statements, which collectively comprise the Commission's basic financial statements, and have issued our report thereon dated December 18, 2020.

#### **Internal Control Over Financial Reporting**

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

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the following observations, we identified certain deficiencies in internal control that we consider to be a material weakness and significant deficiencies.

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and

corrected on a timely basis. We consider the 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. 6 to be significant deficiencies.

### **Compliance And Other Matters**

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

### **Liquor Commission's Responses To Findings**

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



Office Of Legislative Budget Assistant

December 18, 2020

**Internal Control Comments**  
**Material Weakness**

**Observation No. 1: Implement And Staff A Financial Accounting And Reporting Structure Appropriate For The Commission's Size And Complexity**

*Observation:*

Management letters issued from 2013 through 2018 reported a material weakness in the Commission's core financial accounting and reporting resources and recommended the Commission employ additional staff that have financial accounting and reporting expertise appropriate for the scope and complexity of the Commission's operations. The 2019 management letter reported a similar comment, however the level of severity of the control deficiency was reduced to a significant deficiency as a Comptroller was hired in May 2018 that strengthened the Commission's ability to prepare accurate and timely financial statements, and assist with the day to day financial operations. The Comptroller position became vacant again in April 2020 and remains unfilled as of the date of this report. The lack of continuity in this position along with the Commission's inability to fill other critical financial positions has weakened financial accounting and reporting controls to again necessitate the reporting of this control deficiency as a material weakness.

During fiscal year 2020, the Commission netted \$740 million in sales, operated 77 stores, and as of June 30, 2020 held \$89 million of products in inventory. The financial reporting of the Commission encompasses wholesale, retail, and government accounting practices. The following challenges within the Commission's financial accounting and reporting operations were noted during the course of the audit:

1. As of December 2020, the Commission had not adequately staffed its financial reporting section. This deficiency has led to the need for the Commission to obtain a Certified Public Accounting firm to assist in the review of the compilation of the Commission's fiscal-year 2020 financial statements, and additional tasks of incompatible duties being performed by Chief Financial Officer (CFO).
2. The Commission has not established comprehensive policies and procedures for all critical financial accounting and reporting activities including the use of the Multi-Ledger module of NHFirst. The Commission began using Multi-Ledger during fiscal year 2020 to record accounting transactions related to capital assets, debt balances, and certain accruals. Due to the lack of developed and documented policies and procedures for the recording of financial activity, the Due to Capital Fund account balance, as reported in the ledgers at June 30, 2020, had not been updated and required the manual addition of fiscal year 2019 entries to compute the correct balance as of June 30, 2020. While the Commission has made progress in the establishment of its policies and procedures, significant financial accounting and reporting activities performed by the CFO (and business office) remain unaddressed.



3. The Commission should develop a routine, streamlined process for the compilation of its financial statements. The preparation of the Statement of Cash Flows has historically been challenging for the Commission. During fiscal-year 2020, the initial draft of the Statement of Cash Flows contained \$5 million in classification errors that were eventually resolved.

*Recommendation:*

The Commission must mitigate the risk of inaccurate financial accounting and reporting created from its continued reliance on the performance of an individual employee by establishing a financial accounting and reporting structure committed to recruiting, developing, and retaining competent senior level financial management. We continue to recommend the establishment of a senior-level management unclassified position such as a Director of Finance responsible for heading the Commission's financial accounting and reporting activities.

The Commission should continue its efforts to establish written policies and procedures for all significant financial accounting and reporting activities, including high-level financial statement processes in order to support the responsibilities of key employees, and to provide for continuity of operations in the event of employee turnover.

The Commission should continue to develop a routine process that facilitates the annual compilation of its financial statements, including its Statement of Cash Flows. The process and experience of one year should be understood and incorporated into the financial reporting process of the following year.

*Auditee Response:*

Concur.

The Commission actively recruited for two Comptroller positions since July 2020, but despite numerous interviews with good candidates, was unable to find a candidate prepared to enter the state system. Recently, because of continued recruitment efforts, the Commission engaged a new Comptroller of Financial Reporting. The new Comptroller, who started with the Commission on February 26, 2021, is a CPA with extensive financial reporting experience. We will reassess our needs after the new Comptroller has an opportunity to come up to speed.

Now that the Commission has a new Comptroller in place, the focus will be on writing policies and procedures for all significant financial accounting and reporting activities and to continue to build the processes that facilitate the annual compilation of the financial statements.

## Significant Deficiencies

### **Observation No. 2: Seek Additional Resources To Fulfill Information Technology Needs**

#### *Observation:*

The Commission could benefit from hiring additional expert-level staffing to support its immediate and future information technology needs.

Beginning in fiscal year 2016 and continuing into fiscal year 2021, the Commission has been in the process of replacing a legacy information system that provides the base information technology support for the Commission's inventory, purchasing, sales, and other financial and operational activities with a new system, NextGen. The NextGen information technology system is intended to support essentially all aspects of the Commission's activities, including financial accounting and reporting. The vendor initially responsible for the implementation and deployment of the NextGen system was terminated in August 2019, forcing the Commission to begin the process of selecting a new vendor to complete the project, and further delaying the replacement of its legacy information system.

The implementation of the NextGen system has burdened not only financial and embedded informational technology staff, but also various other staff throughout the Commission with additional tasks resulting in overtime and time away from their regular job responsibilities and reportedly will continue to require additional staffing resources for training, deployment, and regular maintenance of the system.

The successful implementation of the NexGen system is dependent upon having a dedicated support staff that has the appropriate knowledge and expertise to deploy and maintain all aspects of the information system.

#### *Recommendation:*

The Commission should seek additional resources to fulfill its information technology needs including the remaining development, deployment, and maintenance of its NextGen information technology system to ensure a smooth transition from its legacy system. The Commission should ensure that the additional staff resources have the appropriate qualifications and experience to reduce the risks of further business interruptions.

#### *Auditee Response:*

Concur. The Commission has begun working with the Commissioner of Department of Information Technology including pursuing our option for resources under a state contract with Computer Aid, Inc.

### **Observation No. 3: Re-Establish A Formal Risk Assessment Process**

#### *Observation:*

The Commission has not maintained and updated its business-risk assessment process, previously established in fiscal year 2017. While tasks have been performed involving certain risk assessment components, such as a Procurement Card Industry (PCI) risk assessment questionnaire, and a recently developed Strategic Plan with identified risks, neither of these tasks were performed as part of a formal risk assessment process to evaluate risks to the Commission's financial accounting and reporting functions, information technology functions, and overall business operations.

Risk assessment is the process of identifying, assessing, and responding to risks related to the achievement of the entity's objectives, and is one of the five generally accepted components of internal control. A prerequisite to an effective risk assessment is the establishment and recognition of objectives and the identification of risks that may put achieving those objectives in jeopardy.

An effective risk assessment process is the foundation for the development and implementation of controls intended to identify and eliminate, mitigate, or otherwise manage identified risks. A formal and well-planned risk assessment process increases the likelihood that the appropriate balance between the costs and benefits of controls can be understood and become the basis for controls put into operation. As risks change over time due to changes in processes, information technology, and the environment, controls intended to mitigate risk may become inefficient and ineffective. Without an ongoing risk assessment process, the identification and response to risk often occurs in a reactive mode, after a risk had been realized and a loss incurred.

Periodic monitoring of the Commission's processes and activities using a risk-based mindset promotes effective planning and assists in resource allocation decision-making.

#### *Recommendation:*

The Commission should re-establish a formal and documented risk assessment process for recognizing, evaluating, and responding to risks that could affect its ability to achieve its financial accounting and reporting objectives. The process should include an information technology security risk assessment component to ensure the Commission's information systems are adequately protected. Risks identified should be analyzed to determine whether current internal controls mitigate risk to a level desired by management or whether actions are required in response to risks. Commission employees with particular areas of expertise should participate in the review to ensure details of operations that may not be obvious to management are appropriately considered.

#### *Auditee Response:*

Concur. The Commission is actively in the process of creating a formal Internal Audit and Compliance Unit to provide independent and objective evaluation of internal control processes and compliance-related matters. A priority of the Unit will be to develop and implement a process for conducting periodic risk assessments in collaboration with management and relevant staff to

identify and analyze risks that could affect the Commission’s ability to achieve expected outcomes and to ensure the controls in place appropriately mitigate those risks.

**Observation No. 4: Capitalized Costs Should Be Properly Evaluated For Impairment Under GASB Statement No. 42**

*Observation:*

As of the date of this report the Commission has not properly evaluated its capitalized software in progress for impairments.

As noted in Observation No. 2, beginning in fiscal year 2016 and continuing as of the date of this report, the Commission has been in the process of replacing its legacy information system with a new system, NextGen. On August 26, 2019, the Commission terminated its contract with the software vendor responsible for the development and implementation of its NextGen system resulting in the impairment of certain capitalized software in progress.

Governmental Accounting Standards Board (GASB) Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, Section 9, states, “Impairment is indicated when events or changes in circumstances suggest that the service utility of the capital asset may have significantly and unexpectedly declined.” GASB Statement No. 42, Section 16, further states “Impaired capital assets that will no longer be used by the government should be reported at the lower of carrying value or fair value.”

In June 2020, the Commission contracted with another vendor to continue with the development and implementation of the NextGen system. This newly contracted vendor should have sufficient knowledge and expertise to evaluate which capitalized software in progress costs are impaired, and to determine the appropriate reported value, in accordance with GASB Statement No. 42.

A similar comment was reported in the Commission’s fiscal year 2019 management letter which noted an assessment performed by the Commission had identified impaired asset costs totaling approximately \$970,000 of the \$11 million capitalized IT costs reported at June 30, 2019. No adjustment to reduce software in progress cost has yet been made as a result of the Commission’s assessment. The Commission reported it was waiting for the newly contracted vendor to provide an assessment of the NextGen System project development completed to date, and the transferability of those costs, prior to recording any potential impairment.

As of June 30, 2020, the Commission’s capitalized software in progress totaled \$14.5 million.

*Recommendation:*

The Commission should coordinate with the vendor to help determine what capitalized assets continue to have service utility in accordance with guidelines provided in GASB Statement No. 42. A formal evaluation should be completed to support the assessment of the capitalized assets, including support for the reduction in the carrying value of those assets determined to be impaired.

*Auditee Response:*

Concur. Effective June 24, 2020, the Commission entered into a contract with a new vendor to complete development and deploy the new Enterprise Resource Planning system. Throughout system development, the vendor is reviewing and testing work done by the previous vendor. The Commission is working with the vendor to identify and determine the value of any impaired capitalized assets.

**Observation No. 5: Liquor Stock Payables Reconciliation Control Should Be Improved**

*Observation:*

The Commission has not developed robust reconciliation procedures to ensure all of the accounts payable activity processed in Mapper, the internal information system, is accurately accounted for in NHFirst.

A comparison of the June 30, 2020 Mapper and NHFirst balances of Liquor Stock Payables and Depletion Allowances (supplier rebates) identified a \$4 million understatement in NHFirst to each of these accounts. While the discrepancy resulted in a zero dollar net effect on the Commission's fiscal year 2020 financial statements, the discrepancy was not detected and corrected by the Commission's accounts payable reconciliation control procedures.

*Recommendation:*

The Commission should continue to develop formal policies and procedures for the performance of complete and accurate monthly reconciliations of all applicable Mapper activity to NHFirst. Periodic and timely reconciliations should be performed by someone knowledgeable of the activity, but independent of the recording and posting processes. The reconciliations should be reviewed and approved by management to ensure timely and accurate performance.

*Auditee Response:*

Concur. The understatements had a zero net effect within the two accounts that were carrying balances from 2015 and had not been previously identified. As a result of the recent years' reconciliations of the accounts, the inaccuracies were identified and corrected. We are in the process of finalizing the procedures for reconciling the accounts going forward.

**Observation No. 6: Procedures To Ensure Complete Reporting Of Capital Assets Should Be Strengthened**

*Observation:*

The Commission's lack of specific procedures to perform a thorough review of Liquor Fund expenses for items that should be capitalized resulted in an error of \$400,000 not being detected by the Commission.

The Commission charges capital asset purchases to both the Capital Projects Fund and Liquor Fund accounts. Capital assets consist of equipment, real property, construction in progress, and software in progress. According to the Department of Administrative Services, Annual Closing Review for Fiscal Year 2020, "Agencies are required to capitalize and depreciate all equipment with a stand-alone purchase value greater than or equal to \$10,000, all real property greater than \$100,000..."

During testing of expenses auditors detected that capital lease improvement costs that were incurred in the Liquor Fund and should have been capitalized were not resulting in an understatement of capital assets in the amount of \$400,000 and a corresponding overstatement of Administrative Expenses. This error could have been detected and corrected in a timely manner had the Commission performed an effective review of its accounts in the Liquor Fund that are used to purchase capital assets.

*Recommendation:*

The Commission should strengthen procedures to ensure that all charges, including those that are incurred in the Capital Projects Fund and Liquor Fund accounts are appropriately identified and reported as capital assets. The procedures should allow for the timely detection and correction of any errors identified.

*Auditee Response:*

Concur. The Commission has updated the fixed asset addition procedures to include quarterly reconciliations and added another level of review.

## APPENDIX

### Current Status Of Prior Audit Findings

The following is a summary of the status, as of December 18, 2020, of the observations contained in the New Hampshire Liquor 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](http://www.gencourt.state.nh.us/LBA/AuditReports/FinancialReports.aspx).

|                                  |   | <u>Status</u> |
|----------------------------------|---|---------------|
| <b>2019 Audit Comments</b>       |   |               |
| <b>Internal Control Comments</b> |   |               |
| <i>Significant Deficiencies</i>  |   |               |
| 2019-1                           | Implement And Staff A Financial Accounting And Reporting Structure Appropriate For The Commission’s Size And Complexity<br><i>Enhance financial accounting with additional staff having financial accounting and reporting expertise appropriate for the scope and complexity of operations, and establish comprehensive policies and procedures for critical financial activities and consider compiling and reporting a more complete set of periodic financial statements. (See Current Observation No. 1)</i> | ● ○           |
| 2019-2                           | Implement Independent Timely Monitoring Of Project Deliverables And Preventative Controls To Aid In Completion Of New Information System<br><i>Implement independent, timely monitoring of project deliverables and preventative controls to help ensure the successful completion of the NextGen IT projects.</i>  | ● ○           |
| 2019-3                           | Internal Audit Function Should Be Developed<br><i>Develop internal audit function and work towards the implementation of leading internal audit industry practices.</i>   | ● ○           |
| 2019-4                           | Controls Over Issuance Of Promotional Cards Should Be Improved<br><i>Develop automated controls within the point of sale system to limit the number and amount of promotional cards issued to retail customers according to total dollars spent on product purchases, and establish policies and procedures over the issuance and safeguards of promotional cards.</i>  | ● ●           |
| 2019-5                           | Reconciliation Procedures Should Be Developed And Improved<br><i>Develop formal policies and procedures over its reconciliation processes. Periodic and timely reconciliations should be performed for all significant accounts where activity is reported in separate systems, and be reviewed and approved by management.</i>   | ● ○           |
| 2019-6                           | Complete Account Activity Should Be Maintained In The State’s Accounting System<br><i>Coordinate with the Department of Administrative Services to obtain access to the Multi-Ledger module in NHFirst in order to properly</i>   | ● ○           |

|         |   |   |   |
|---------|---|---|---|
|         | <i>record and account for all financial activities. (See Current Observation No. 1)</i>   |   |   |
| 2019-7  | Capitalized Costs Should Be Properly Evaluated For Impairment Under GASB 42<br><i>Determine what capitalized assets continue to have utility in accordance with guidelines provided in GASB 42. A formal evaluation should be completed to support the assessment of the capitalized assets, including support for the reduction in the carrying value of those assets determined to be impaired. (See Current Observation No. 4)</i>   | ● | ○ |
| 2019-8  | Non-GAAP Inventory Adjustment Should Be Discontinued<br><i>Implement policies and procedures to ensure inventory is valued in accordance with the provisions of GASB Statement No. 62.</i>  | ● | ● |
| 2019-9  | Centralize Cash Receipt Procedures<br><i>Centralize the cash receipt process to eliminate the handling of cash, checks, and credit card payments at multiple locations within headquarters.</i>   | ● | ○ |
| 2019-10 | Develop And Provide An Electronic Beer Tax Filing System<br><i>Continue efforts to develop and implement an electronic beer tax filing system as part of the NextGen IT project.</i>  | ● | ○ |
|         | <b>Compliance Comments</b>  |   |   |
| 2019-11 | Adopt Administrative Rules Required By Statute<br><i>Adopt administrative rules required by statute. If the required rules are not necessary, request an appropriate revision to the statute.</i>   | ● | ○ |
| 2019-12 | Impose Late or Nonpayment Requirements<br><i>Impose the late and nonpayment requirements identified in Administrative Rule Liq 904. If the requirements of Liq 904 are not practical seek an appropriate revision to the rule.</i>  | ● | ○ |
|         | <b>2018 Audit Comments</b>  |   |   |
|         | <b>Internal Control Comments</b>  |   |   |
|         | <b>Material Weakness</b>  |   |   |
| 2018-1  | Implement And Staff A Financial Accounting And Reporting Structure Appropriate For The Commission's Size And Complexity<br><i>Enhance financial accounting staff with additional staff having financial accounting and reporting expertise appropriate for the scope and complexity of operations, establish comprehensive and documented policies and procedures for all critical financial activities, and consider compiling and reporting a more complete set of periodic interim financial statements. (See Current Observation No. 1)</i> | ● | ○ |
|         | <b>Significant Deficiencies</b>   |   |   |
| 2018-2  | Review And Expand Accounts Payable Policies And Procedures<br><i>Ensure direction provided to staff promotes the accurate accrual of liabilities in accordance with State and Commission policy, and the proper basis of accounting.</i>  | ● | ● |



|                            |  |   |   |
|----------------------------|--|---|---|
| 2018-3                     | Establish Objectives And Policies And Procedures For Gift And Promotional Card Programs<br><i>Design and document objectives for gift and promotional card programs and establish policies and procedures for meeting its objectives and controlling and recording the related activity in alignment with its objectives. Review assumption data to determine if it is reflective of the redemption patterns for sold and issued cards.</i>                  | ● | ● |
| 2018-4                     | Review Information System User Access Controls<br><i>Review the user access controls of the information systems, including the automated timeclock system, and ensure that policies and procedures are appropriately designed and in operation to meet management's objectives for the systems' and security needs; and ensure that information controls are sufficient to allow timely notification to responsible parties of new and terminated users.</i> | ● | ● |
| <b>Compliance Comments</b> |  |   |   |
| 2018-5                     | Prepare And Submit Action Plans Required By Executive Order #2014-03<br><i>Prepare and submit action plans required by Executive Order #2014-03 to address audit findings included in the Commission's management letters.</i>   | ● | ● |
| 2018-6                     | Adopt Administrative Rules Required By Statute<br><i>Adopt administrative rules required by statute unless the Commission determines the required rules are not necessary for the operation of the Commission, then request an appropriate revision to the statute.</i>  | ● | ○ |

**Status Key**

|   | ● | ○ | <b><u>Count</u></b> |
|---|---|---|---------------------|
| Fully Resolved  | ● | ● | 6                   |
| Remediation In Process (action beyond meeting and discussion) | ● | ○ | 12                  |
| Unresolved  | ○ | ○ | 0                   |

