



# Ohio Lottery Commission

## Video Lottery Terminal (VLT) Audit

---

**Audit Period: August 2013 through February 2014**

### Results Summary:

Objective	Conclusion
Issuance and maintenance of employee licenses	Well-Controlled with Improvement Needed
Monitoring the issuance and redemption of promotional credits	Improvement Needed
Jackpot intercept reviews	Well-Controlled with Improvement Needed

Report number: 2014-LOT-01

Issuance date: June 25, 2014

---



## Executive Summary

### Background

The Ohio Lottery Commission (LOT) began regulating VLTs at Ohio horse racetracks in FY 2012. Four racinos are currently open and LOT plans to have all seven racinos operational by FY 2015. Nearly \$3.9 billion was bet at racinos on a total of 7,091 VLTs available to patrons as of the end of April 2014 (YTD figures). Net VLT revenue remaining after payouts to customers was over \$333 million, with \$111 million of that distributed to LOT. Gross proceeds from VLTs are shared by the lottery sales agents (the racinos) (66.5%), and the Ohio Lottery Commission (33.5%). Of \$350 million in one-time licensing fees to be paid by the owners of the horse racetracks for the privilege of operating VLTs, LOT is to receive the remaining \$225 million in FYs 2014-2015. LOT also collects an additional 0.5% of VLT net revenue to support responsible gambling programs (as authorized by H.B. 386 of the 129th General Assembly).

During the audit, OIA identified opportunities for LOT to strengthen internal controls and improve business operations. This audit conforms to the *International Standards for the Professional Practice of Internal Auditing*. OIA would like to thank LOT staff and management for their cooperation and time in support of this audit.

This report is solely intended for the information and use of agency management and the State Audit Committee. It is not intended for anyone other than these specified parties.

### Scope and Objectives

OIA staff was engaged to perform an assurance audit related to the controls over VLT operations at Scioto Downs and Belterra Park during the period of August 2013 through February 2014. This work was completed between March 2014 and June 2014. The scope of this audit was limited to the areas of licensing, promotional credit, and jackpot intercept. The following detailed audit objectives included:

- Evaluate the design and effectiveness of controls over employee license issuance and maintenance.
- Evaluate the design and effectiveness of controls over the issuance and redemption of promotional credits.
- Evaluate the design and effectiveness of controls over jackpot intercept reviews.

## Detailed Observations and Recommendations

The Observations and Recommendations include only those risks which were deemed high or moderate. Low risk observations were discussed with individual agency management and are



not part of this report. However, the low risk observations were considered as part of the audit objective conclusions.

## Observation 1 – Document Annual Audit Plan and Risk Assessment

The Committee Of Sponsoring Organizations' (COSO) internal control framework asserts that an essential component of internal control systems include effective monitoring of control activities which employ a risk-based approach. Utilizing a risk-based approach can also align limited personnel and resources to specific areas of concern and determine the nature, timing, and extent of procedures to be performed.

The VLT management group does not adequately document the approach used to select which areas will be reviewed each year for the different racinos. Some audit steps are documented as low risk in the work program, but do not include adequate justification in relation to organization objectives. In addition, due to schedule and personnel demands warranted by the opening of new racinos in 2013 and 2014, limited procedures were performed at racinos already in operation. A comprehensive annual plan of VLT management oversight was not available for review.

Failure to consistently implement a risk-based approach to determine the extent of monitoring of racinos may result in high-risk processes not being adequately monitored to provide reasonable assurance that racinos are operating within statutory requirements. It also may result in an inefficient use of resources used to conduct monitoring of low-risk processes. Furthermore, the lack of a documented annual audit plan increases the risk that the appropriate level of monitoring is not conducted at all facilities within Commission oversight.

### Recommendation

Consider developing and documenting a formal risk assessment process each year to assist in determining which areas represent a higher risk and priority for review. Documentation of a risk assessment can also be used as a tool in future years to identify areas not reviewed recently which can increase their risk rating. A risk assessment may include:

- Developing standardized risk profiles for each of the audit program areas currently utilized by VLT management;
- Developing weighted risk factors (i.e. materiality, frequency, audit results) that can be used as a basis to quantify risk;
- Identifying stakeholders effected by the risk and evaluate the potential impact;

Formally document the results of the annual risk assessment and consider periodically



evaluating the plan to determine whether the risks identified in previous years remain pertinent or require updating for other risk areas.

In addition, consider the development of an annual audit plan based upon the outcome of the risk assessment. The annual audit plan can provide direction to staff on where to focus time and resources, as well as serve as an accountability measure to the Commission that what was planned was accomplished. A documented audit plan will also help in future years planning to indicate the areas covered in a previous audit. Management should also formally report on the execution of the plan, comparing planned monitoring procedures to completed procedures, and determine if risks were sufficiently mitigated.

**Management Response**

The VLT regulators perform an assessment at each facility based upon historical results and risk; however, we agree that the process can be more appropriately documented. The agency has developed a fiscal 2015 review calendar (June 2014) and will work to create a corresponding annual plan. The regulators did complete a fiscal 2013 annual report documenting reviews, licensing, and other regulatory facts. The fiscal 2014 report will be expanded to include audit items (August 2014). Documentation of risk assessment and formal audit plan will be developed in fiscal year 2015 and implemented in fiscal year 2016.

Risk*	Remediation Owner	Estimated Completion Date
<b>Moderate</b>	Assistant Director, VLT Management	May 2015

Due to the limited nature of our audit, we have not fully assessed the cost-benefit relationship of implementing the observations and recommendations suggested above. However, these observations reflect our continuing desire to assist your department in achieving improvements in internal controls, compliance, and operational efficiencies.

\* Refer to Appendix A for classification of audit observations.



## Appendix A – Classification of Conclusions and Observations

### Classification of Audit Objective Conclusions

Conclusion	Description of Factors
<b>Well-Controlled</b>	The processes are appropriately designed and/or are operating effectively to manage risks. Control issues may exist, but are minor.
<b>Well-Controlled with Improvement Needed</b>	The processes have design or operating effectiveness deficiencies but do not compromise achievement of important control objectives.
<b>Improvement Needed</b>	Weaknesses are present that compromise achievement of one or more control objectives but do not prevent the process from achieving its overall purpose. While important weaknesses exist, their impact is not widespread.
<b>Major Improvement Needed</b>	Weaknesses are present that could potentially compromise achievement of its overall purpose. The impact of weaknesses on management of risks is widespread due to the number or nature of the weaknesses.

### Classification of Audit Observations

Rating	Description of Factors	Reporting Level
<b>Low</b>	Observation poses relatively minor exposure to an agency under review. Represents a process improvement opportunity.	Agency Management; State Audit Committee (Not reported)
<b>Moderate</b>	Observation has moderate impact to the agency. Exposure may be significant to unit within an agency, but not to the agency as a whole. Compensating controls may exist but are not operating as designed. Requires near-term agency attention.	Agency Management and State Audit Committee
<b>High</b>	Observation has broad (state or agency wide) impact and possible or existing material exposure requiring immediate agency attention and remediation.	Agency Management and State Audit Committee