Internal Audit Plan
Fiscal Year 2014
Texas Racing Commission

Monday N. Rufus, P.C.
Certified Public Accountants and Consultants

Table of Contents

	Page
Transmittal Letter	2
Purpose	3
Background Information	3
Internal Audit Methodology	8
Internal Audit Plan	11
Reporting	11
Appendix A: Organizational Chart	12
Appendix B: Risk Assessment	13

MONDAY N. RUFUS, P.C.
Certified Public Accountants & Consultants

Member: American Institute of Certified Public Accountants

October 17, 2013

Commissioners of the
Texas Racing Commission
Austin, Texas

Dear Commissioners:

As required by the Internal Auditing Act (Texas Government Code, Section 2102.008), we have prepared the audit plan for Fiscal Year 2014.

We prepared a risk assessment to determine the areas in the Texas Racing Commission that should be considered for audit. Based on that risk assessment, our audit plan for Fiscal Year 2014 is shown below:

• Licensing Applications and Registrations	100
• FY 2014 Risk Assessment & Audit Plan	20
• FY 2015 Risk Assessment & Audit Plan	20
Total Hours	**140**

Your approval of the audit plan is required. I would like to discuss this plan with you at the Commission meeting on December 10, 2013.

Sincerely,

Monday N. Rufus, MBA, CISA, CPA
Audit Director
Monday N. Rufus, P.C.,CPAs

I. Purpose

The Purpose of this internal audit plan is to document the development, risk assessment, scope of assignments, and implementation timetable for fiscal year 2014 internal audit activities. This document will serve as a primary tool to carry out internal audit responsibilities in an efficient manner and prioritize the audit areas based on risk assessments agreed to by the Commissioners of the Texas Racing Commission (Agency). Due to the nature, scope and timing of audit procedures contemplated here, planning for specific aspects of the audits is a continuing process. Accordingly, the plan will be revised as necessary and reviewed at least annually.

This plan has been prepared to meet planning guidelines as required by both generally accepted auditing standards and the standards for the Professional Practice of Internal Auditing as determined by the Institute of Internal Auditors, Inc.

II. Background Information

The Texas Racing Commission regulates all aspects of pari-mutuel horse and greyhound racing through licensing, on-site monitoring, and enforcement. Statute and rule require the Commission to:

- License racetracks that offer racing and the people directly involved with pari-mutuel wagering who work at the racetracks or own race animals.
- Allocate race dates, supervise the conduct of all races, monitor the health and safety of the race animals, and conduct drug tests to ensure the animals race without prohibited substances.
- Oversee all pari-mutuel wagering activity, approve simulcasts, test the totalisator systems (complex computer systems that tally and calculate pari-mutuel wagers), and ensure the proper allocation and distribution of revenue generated by pari-mutuel wagering.
- Administer the Texas-Bred Incentive Program, which provides economic incentives to support a health and vigorous breeding industry in the state.

The Racing Act allows pari-mutuel wagering on horse and greyhound racing and provides for the strict regulation and control of pari-mutuel wagering in connection with that racing.

Principal responsibilities of the Commission are to:

1. Adopt rules and regulations for conducting racing involving wagering;
2. Administer and enforce all laws, rules, and regulations affecting horse racing, greyhound racing, and pari-mutuel wagering;
3. Adjudicate disciplinary matters arising from the enforcement of those laws and regulations dealing with horse racing and greyhound racing and pari-mutuel wagering; and
4. Regulate and supervise each racing meeting conducted in the state of Texas, the operations of racetracks, and the participants in a race meeting.

Extensive rulemaking authority is granted to the Commission throughout the Racing Act. The rulemaking authority vested in the Texas Racing Commission is authorized for administration and enforcement purposes.
The Racing Commission consists of seven members appointed by the governor with the advice and consent of the Senate to serve overlapping six year terms. Five members must represent the general public and have general knowledge of business or agribusiness. At least one of those appointed members may be a veterinarian, and being licensed as a veterinarian satisfies the requirement that the person have general knowledge of business or agribusiness. One member must have special knowledge or experience related to horse racing and one member must have special knowledge or experience related to greyhound racing. In addition to the appointed members, there are two ex-officio members, the Chair of the Public Safety Commission and the Comptroller of Public Accounts. The Governor appoints the chair and the members elect the vice-chair.

The Commission appoints an Executive Director to supervise the agency's daily activities as a whole and manages the agency's two divisions and its information team. The Agency's operating budget is prepared and approved by the Commission on an annual basis, whereas the State legislative appropriation request is determined every two years. Both the budget and appropriations are reviewed and approved by the State Legislature.

The 82nd Legislature, Regular Session, passed House Bill 2271 which altered the Commission's method of finance eliminating outstanding uncashed winning tickets as a source of revenue. The Commission is now self-funded from fees assessed to racetracks and occupational licenses from the entities it regulates and is typically appropriated only General Revenue – Dedicated funds. Approximately 50% of the expenditures are passed through the Agency to the official breed registries for the Texas Bred Incentive Programs. Funds collected by the Agency are directly utilized for operations, and not passed on to the State.

The agency's structure consists of two divisions and an Executive group. The Executive group is headed by the Executive Director; a Racing Oversight Division is directed by a Deputy Director for Racing Oversight; and a Finance and Wagering Division is directed by a Deputy Director for Finance and Wagering Review.

A. Executive Group

i. **Executive Director -** The Executive Director supervises agency activities as a whole and manages the agency's two divisions and its information technology team. The Executive Director oversees development of agency operating policies and procedures and ensures that the agency's regulatory responsibilities are carried out. The Executive Director represents the agency before the Legislature and other governmental agencies and serves a primary role in external relations with industry stakeholders, regulators in other states, and a national regulatory association.

The Executive Director, with the assistance of the General Counsel's staff oversees coordination of the evaluation of racetrack license applications, the race date allocation process, and assesses administrative penalties against

racetrack licensees. The Executive Director's office is also responsible for other administrative functions including responding to public information and media requests.

ii. **General Counsel** – The General Counsel advises the Commissioners and staff on legal and regulatory enforcement issues affecting the agency. The General Counsel coordinates all aspects of Commission meetings and rulemaking proceedings and also represents the agency before the State Office of Administrative Hearings when prosecuting appeals from decisions made by the Board of Stewards/Judges and disciplinary cases initiated by the Executive Director.

iii. Department of Information Technology (IT)
The IT division develops and maintains the agency's network, database and Web site. This division recommends and supports all hardware and software necessary for the day-to-day activities of the Commission. The Commission's custom programs and database operate twenty-four hours a day, seven days a week, providing staff, licensees, the Department of Public Safety (DPS), the Texas A&M Veterinary Medical Diagnostic Laboratory and the general public with up-to-date information regarding all aspects of the Commission's regulatory programs.

B. Divisional Information

The Agency's staff is organized into two operating divisions which have specific duties and responsibilities in carrying out the overall mission of the Agency. The two operating divisions are the Racing Oversight Division and the Finance and Wagering Division.

i. **Racing Oversight Division** –This division is focused on enforcement and oversight of day-to-day racetrack operations. The members of this division make up the agency's presence at Texas tracks. The Deputy Director supervises personnel directly responsible for regulating the conduct of live racing and is responsible for the following teams: Licensing, Investigations, Stewards/Judges, and Veterinarians/Drug Testing.

- Licensing

  Staff in licensing issue occupational licenses to all people in positions that afford the person an opportunity to influence pari-mutuel wagering and to those who will likely have significant access to the restricted areas of a racetrack. Licensing staff at each racetrack help maintain the integrity of the industry by ensuring that all appropriate participants are licensed and in good standing.

To ensure that that all participants in racing are properly licensed, the Commission has more than fifty categories of occupational licenses. Stable and kennel area occupations – jockeys, owners, kennel owners, trainers and grooms – must secure licenses, as must racetrack employees.

- Investigations

  The investigators, who must be licensed peace officers, coordinate enforcement of the Commission's Rules and the Texas Racing Act.

  Investigations are conducted on animal drug positives, criminal histories returned on license applicants, illegal wagering, use and possession of contraband, drug abuse and narcotics trafficking, and other illicit activities that could affect the integrity of pari-mutuel racing.

  Drug testing of licensees suspected of using illegal drugs while performing their duties has become an important aspect of regulating the industry. If a licensee tests positive for an illegal controlled substance or alcohol, the licensee faces a suspension and must seek professional help.

- Stewards/Judges

  The division includes stewards at horse tracks and judges at greyhound tracks. The judges and stewards monitor the conduct of live races and enforce the Racing Act and the Commission's Rules of Racing. The stewards and judges have broad authority to resolve matters arising during a race meeting. They may redistribute purses, issue fines up to $5,000 and suspend licensees for up to one year.

- Veterinarians / Drug Testing

  The Chief Veterinarian oversees this division, supervising the veterinarians and test barn supervisors working at the racetracks.

  Employees in this division inspect all race animals before a competition to ensure they are sound to compete, inspect the stable and kennel areas for animal health and safety issues, and implement the Commission's race animal drug testing program.

  The Chief Veterinarian also serves as a liaison between the Commission and veterinary-related organizations and agencies, such as the Texas Animal Health Commission, the American

Association of Equine Practitioners, and the Texas Veterinary Medical Association.

ii. **Finance and Wagering Division –** This division is focused on protecting the interests of the wagering public and industry participants by assuring the proper collection and distribution of funds in accordance with the Racing act, providing reliable information on wagering, and responding to public inquiries about wagering. The division is responsible for agency finance and administrative functions to include budget, accounting, purchasing, personnel, human resources, travel coordination and related administrative functions.

The Deputy Director supervises the agency's pari-mutuel and compliance auditors and staff dedicated to accounting, purchasing, and human resources.

- Pari-mutuel Auditors

  The pari-mutuel auditors protect the interest of the wagering public and industry participants by assuring the proper collection and distribution of funds in accordance with the Act and providing reliable information on wagering. The auditors review, verify and report all live and simulcast wagering activity at the racetracks to ensure the public is paid the correct amount on each winning wager. On-site pari-mutuel auditors perform daily audits and verifications of handle, earned purse, paid purse, outs balances, deposit reports and requests for simulcast approval in compliance with the Interstate Horse Racing Act (IHA). The audit staff ensure the daily collection of the escrowed horse purse funds earned from interstate cross-species wagers placed at greyhound racetracks and the allocation of these funds to the various horse racetracks based on Commission-approved formulas.

- Compliance Auditor
  The compliance auditor deals primarily with issues related to the Texas-bred Incentive Program and computer testing. The Texas Racing Act provides purse supplements and monetary awards to breeders and owners of Texas-bred greyhound and horses to encourage agriculture and the horse and greyhound breeding industries. The agency collects this money and then allocates it to the various recognized breed registries based on formulas approved by the Commission. This program accounts for approximately 50 percent of the agency's appropriation. The compliance auditor works to ensure that funds are collected and allocated appropriately.

  The compliance auditor also tests the totalisator (tote) systems that racetracks use to process pari-mutuel wagers. The hardware, software, and related peripheral devices are all subject to testing and ongoing monitoring.

- Administration and Finance

  Staff members prepare the biennial Legislative Appropriations Request (LAR), the operating budget, the annual financial report, reports on performance measures, and other administrative reports. Staff members in this area are responsible for the agency's purchasing, personnel, human resources and travel coordination activities.

C. The Agency's General Appropriations Act authority for fiscal years 2014 and 2015 is as follows:

	2014	2015
License and Regulate Racetracks	$ 400,839	$400,839
Texas Bred Incentive Program	4,125,000	4,125,000
Supervise & Conduct Live Races	596,283	591,228
Monitor Occupational License Activities	270,601	271,136
Inspect & Provide Emergency Care	290,308	292,515
Administer Drug Tests	254,753	248,903
Occupational Licensing Program	562,587	562,587
TEXASONLINE	22,500	22,500
Monitor Wagering and Audit	321,110	321,110
Wagering Compliance Inspections	242,242	242,242
Central Administration	730,012	730,012
Information Resources	499,171	507,335
Supplemental Appropriation	635,637	635,637
Total	$ 8,951,043	$ 8,951,044

III. Internal Audit Plan Methodology

This section summarizes the methodology used in preparing the fiscal year 2014 internal audit plan. In order to understand the Agency and develop our risk assessment process, we reviewed the Agency's:

- Enabling Legislation
- Strategic plan

- Legislative appropriations request/operating budget
- Prior internal audit reports
- Reports from the State Auditor's Office
- Sunset Commission Report
- Other documents available to us

In planning internal audit procedures, financial, operational, as well as compliance issues are considered in determining processes/systems of interest. Functional areas that cross many divisions and the interaction between divisions are key criteria in the process of identifying areas of interest. Agency financial reports, planning documents, laws, rules, and regulations, in addition to soliciting input from management and commission members, were all considered in developing the list of areas of interest. Upon completion of this list, each area was subjected to our risk analysis process.

The following Agency processes/systems have been considered during the development of the areas of interest list:

- Cash receipts and fee processing
- Cash disbursements
- Travel
- Payroll & Personnel Processes
- Reporting – Key Performance Measures
- Budgeting and Reporting
- Licensing application and registrations
- Complaints/Investigation process
- Pari-mutuel Auditing Process
- EDP Wagering Reviews/Audits
- Business Continuity/Disaster Recovery
- Information Systems - Security
- Information Technology System Development
- Drug testing
- Inspection Program
- Racing Administration
- Texas Bred Incentive Program – Associations
- Texas Bred Incentive Program – Policies and Procedures
- Equine Research
- Historically Underutilized Businesses (HUB)
- Fixed Asset Management

There are numerous other areas that may be identified during the process of performing internal audit procedures during the year. Continuing input from both the Commissioners and management will be essential in identifying additional or new areas of risk that should be considered in the future.

Our risk assessment was performed through the consideration of various factors, including:

1. Exposure Level (Adverse impact of errors within the process/unit)
2. Complexity of unit (Volatility of activities)
3. Materiality (Financial and Non Financial Impact)
4. Results of last audit (Positive, Some Findings, Negative)
5. Extent of other coverage or oversight (More coverage, Some coverage, No coverage)
6. Quality of internal controls/adherence to laws (Excellent, Good, & Poor controls)
7. Changes in systems and processes (More changes, Some changes, No changes)
8. Normal audit interval (Audited in last 1 year, 2-4 years, >4 years or Never)

All of the above factors were considered in assessing risk and were taken into consideration for each process/system as to their impact on the Agency. Once each area of interest was evaluated, it was assigned a risk factor of high, moderate or low. The following is the result of our risk assessment process.

<u>Processes Identified as High Overall Risk</u>
Licensing Applications and Registrations
Drug Testing
Reporting – Key Performance Measures

<u>Processes Identified as Moderate Overall Risk</u>
Information Systems – Security
Business Continuity/Disaster Recovery
Inspection Program
Texas Bred Incentive Program – Associations
Racing Administration
Budgeting and Reporting
Texas Bred Program – TxRC's Policies and Procedures
Cash Disbursements (excluding travel)
Pari-mutuel Auditing Process
Payroll & Personnel Processes
EDP Wagering Reviews/Audits
Cash Receipts and Fee Processing
Travel
Information Technology System Development

<u>Processes Identified as Low Overall Risk</u>
Complaints/Investigation Process
Equine Research
Historically Underutilized Businesses (HUB)
Fixed Asset Management

IV. Internal Audit Plan

The internal audit plan is designed to provide a review of all areas considered risky. Although the plan is structured in this manner, it should not prevent the review of areas on a more frequent basis, in the case of future restructuring or development of new processes/systems. Also, special reviews might be added in the future as requested by the Commissioners or when deemed necessary by the internal audit function after performance of in-depth review of the specific divisions/systems and approval by the Commission.

Internal audit activities will be primarily concerned with documenting, testing and evaluating each division or system's internal control policies and procedures and the quality of performance in carrying them out. This will include reporting conditions and suggestions to management and evaluating management's response and plans for corrective actions. Opportunities for improved efficiency identified as a result of performing internal activities will be communicated to management and the Commissioners as part of the reporting process.

Internal Audit reviews for the fiscal year ending 2014 are planned for the following processes/systems:

Fiscal Year 2014

Licensing Applications and Registrations

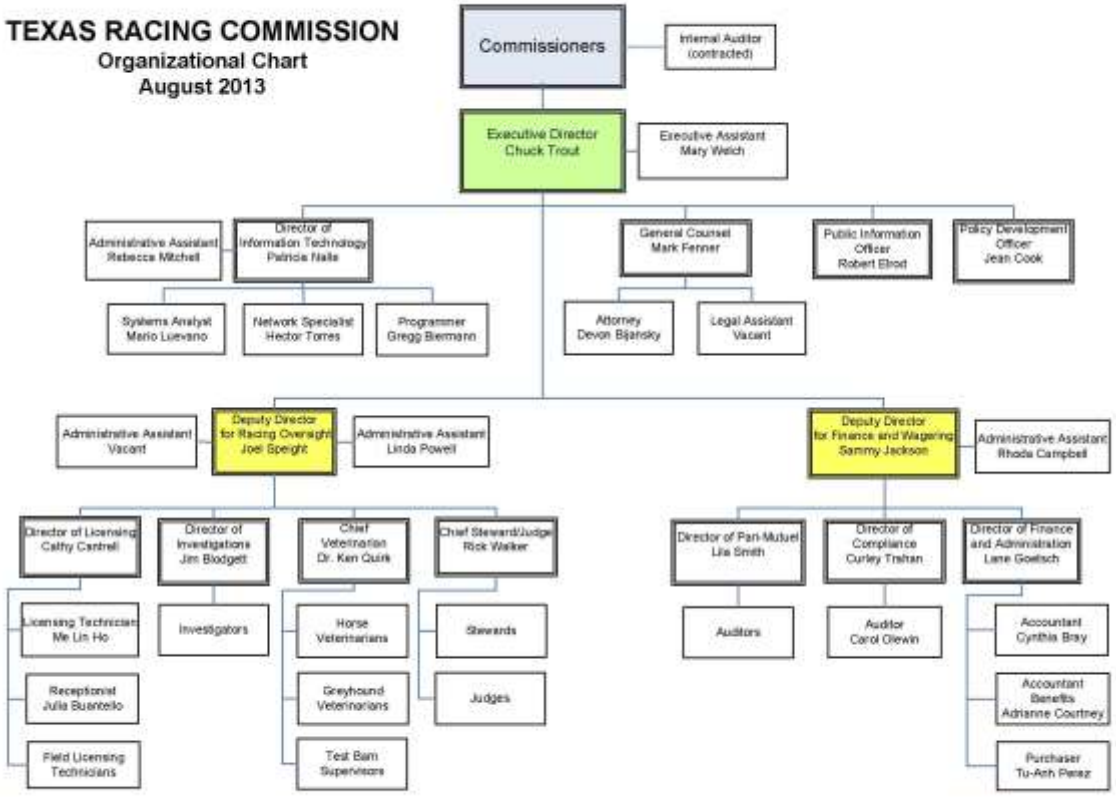
This audit will take place from December 2013 through August 2014 with final reporting occurring in September 2014. The above plan does not preclude the internal audit function from identifying and assessing risk relating to new divisions or systems added to the Agency.

These processes/systems were identified for review through risk assessment methodology. As discussed above, this methodology included personnel inquiries, identifying financial and non-financial risk, identifying interaction of divisions amongst each other, identifying rules and regulations various divisions must comply with and identifying the volume of transactions and personnel involved with each division.

V. Reporting

In compliance with the Texas Internal Auditing Act, the annual internal audit report will be filed with the Governor, the Legislative Budget Board, the Sunset Advisory Commission, the State Auditor, the Commissioners of the Agency, and the Agency's Executive Director by November 1, 2014. The annual internal audit report will be in the form specified by the State Auditor.

Appendix A: Organizational Chart



Appendix B: Risk Assessment

High = 38 and up
Med = 30-37
Low = less than 30

	Weighed Risk
Licensing Applications and Registrations	41
Drug Testing	41
Reporting – Key Performance Measures	39
Information Systems – Security	37
Business Continuity/Disaster Recovery	37
Inspection Program	37
Texas Bred Incentive Program – Associations	37
Racing Administration	37
Budgeting and Reporting	36
Texas Bred Program – TxRC's Policies and Procedures	36
Cash Disbursements (excluding travel)	35
Pari-mutuel Auditing Process	34
Payroll & Personnel Processes	34
EDP Wagering Reviews/Audits	33
Cash Receipts and Fee Processing	32
Travel	31
Information Technology System Development	30
Complaints/Investigation Process	29
Equine Research	28
Historically Underutilized Businesses (HUB)	25
Fixed Asset Management	25