

Audit Report

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**Department of Labor, Licensing and Regulation**

**Division of Racing**

July 2008

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**OFFICE OF LEGISLATIVE AUDITS**  
**DEPARTMENT OF LEGISLATIVE SERVICES**  
**MARYLAND GENERAL ASSEMBLY**

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Karl S. Aro  
Executive Director

DEPARTMENT OF LEGISLATIVE SERVICES  
OFFICE OF LEGISLATIVE AUDITS  
MARYLAND GENERAL ASSEMBLY

Bruce A. Myers, CPA  
Legislative Auditor

July 17, 2008

Senator Verna L. Jones, Co-Chair, Joint Audit Committee  
Delegate Steven J. DeBoy, Sr., Co-Chair, Joint Audit Committee  
Members of Joint Audit Committee  
Annapolis, Maryland

Ladies and Gentlemen:

We have audited the Division of Racing of the Department of Labor, Licensing and Regulation for the period beginning August 15, 2005 and ending February 3, 2008.

Our audit disclosed that the Division did not maintain proper control over cash receipts due to inadequate separation of duties and the lack of proper, independent deposit verifications. In addition, the Division did not ensure that wire transfers of taxes remitted by the racetracks were received timely.

Respectfully submitted,

Bruce A. Myers, CPA  
Legislative Auditor



## **Background Information**

### **Agency Responsibilities**

The Division of Racing is responsible for implementing the policies of the Maryland Racing Commission, which operates under the provisions of Title 11 of the Business Regulation Article of the Annotated Code of Maryland. The Commission, which consists of nine members who are appointed by the Governor, is responsible for regulating the conduct of racing and pari-mutuel wagering in the State. According to the State's records, the Division's operating expenditures during fiscal year 2007 were approximately \$6.6 million.

### **Status of Findings From Preceding Audit Report**

Our audit included a review to determine the status of the three findings from our preceding audit report dated February 10, 2006. We determined that the Division satisfactorily addressed two of these items. The remaining item is repeated in this report.

## **Findings and Recommendations**

### **Cash Receipts**

#### **Finding 1**

**Adequate controls were not established over cash receipts.**

#### **Analysis**

Adequate controls were not established over cash receipts. Specifically, the duties over cash receipts were not adequately separated since an employee responsible for opening the mail, logging receipts, and preparing receipts for deposit was also responsible for recording the payments in the Division's accounting records and for billing and recording accounts receivable related to laboratory fees. Furthermore, this employee was also responsible for verifying that the deposits of certain cash receipts were recorded on the State's accounting records (FMIS). During the period from July 2007 to February 2008, independent verifications were not performed to ensure that recorded collections were transferred to the Department of Labor, Licensing and Regulation – Office of Budget and Fiscal Services' general accounting office and were subsequently deposited. As a result of these conditions, there was no assurance that all amounts

received by the Division were deposited and recorded in the Division's and the State's accounting records.

The Comptroller of the Treasury's *Accounting Procedures Manual* requires that the duties of cash receipts handling be segregated from accounts receivable record keeping, billing and reconciliation functions, and that independent deposit verifications be performed. The Division's cash receipts for fiscal year 2007, which consisted primarily of receipts for betting taxes and unredeemed winning pari-mutuel tickets, totaled approximately \$5.1 million. These receipts also included approximately \$600,000 for laboratory fee reimbursements from racetracks for testing racehorses for the use of unauthorized drugs.

#### **Recommendation 1**

**We recommend that employees receiving and depositing cash receipts not have access to the related accounting records, and that an employee independent of the cash receipts functions verify that all collections have been deposited by comparing the initial record of collections with the validated bank deposit documentation. We also recommend that the Division ensure that employees responsible for maintaining the billing and accounts receivable records do not have access to the related cash receipts. We advised the Division how to accomplish the necessary separation of duties using existing personnel.**

#### **Finding 2**

**The Division did not always ensure that wagering taxes received via wire transfer from Maryland racetracks were transmitted timely.**

#### **Analysis**

Wire transfers of wagering taxes owed the State were not always transferred by the racetracks within three days after the running of a race, as required by State law, and the Division did not take appropriate action to ensure the timely collection of these funds. Our test disclosed that, for 61 of 62 days during fiscal years 2007 and 2008, taxes received totaling approximately \$105,000 were transferred, via wire transfer, from 1 to 11 days after the required transfer dates. A similar condition was commented upon in our preceding audit report. Although Chapter 22, Laws of Maryland 2008, effective July 1, 2008, extended the time for transfer of the taxes to seven days, many of the items we tested would still have exceeded the new seven-day limit.

Untimely transfer of funds to the State's bank account results in lost interest income and increases the potential for misappropriation of these cash assets. Wagering taxes collected by the Division during fiscal year 2007 totaled approximately \$1.7 million.

**Recommendation 2**

**We again recommend that the Division ensure that wire transfers of wagering taxes are transmitted in accordance with State law.**

## **Audit Scope, Objectives, and Methodology**

We have audited the Division of Racing of the Department of Labor, Licensing and Regulation for the period beginning August 15, 2005 and ending February 3, 2008. The audit was conducted in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

As prescribed by State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine the Division's financial transactions, records and internal control, and to evaluate its compliance with applicable State laws, rules, and regulations. We also determined the status of the findings included in our preceding audit report.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of materiality and risk. Our audit procedures included inquiries of appropriate personnel, inspections of documents and records, and observations of the Division's operations. We also tested transactions and performed other auditing procedures that we considered necessary to achieve our objectives. Data provided in this report for background or informational purposes were deemed reasonable, but were not independently verified.

Our audit did not include certain support services provided by the Department of Labor, Licensing and Regulation – Office of the Secretary. These support services (such as payroll, purchasing, data processing, maintenance of official accounting records, and related fiscal functions) are included within the scope of our audits of the Office of the Secretary.

The Division's management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records, effectiveness and efficiency of operations including safeguarding of assets, and compliance with applicable laws, rules, and regulations are achieved.

Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate. Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities that are functioning properly.

This report includes findings relating to conditions that we consider to be significant deficiencies in the design or operation of internal control that could adversely affect the Division's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. Our report also includes a finding regarding a significant instance of noncompliance with applicable laws, rules, or regulations. Other less significant findings were communicated to the Division that did not warrant inclusion in this report.

The Department of Labor, Licensing and Regulation – Office of the Secretary's response, on behalf of the Division, to our findings and recommendations is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise the Office of the Secretary regarding the results of our review of its response.

APPENDIX

**DLLR**

STATE OF MARYLAND

DEPARTMENT OF LABOR, LICENSING AND REGULATION

MARTIN O'MALLEY, Governor  
ANTHONY G. BROWN, Lt. Governor  
THOMAS E. PEREZ, Secretary

OFFICE OF THE SECRETARY

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July 7, 2008

Mr. Bruce A. Myers, CPA  
Legislative Auditor  
State of Maryland  
Office of Legislative Audits  
State Office Building, Room 1202  
301 West Preston Street  
Baltimore, Maryland 21201

Dear Mr. Myers:

Attached is a copy of the Department of Labor, Licensing and Regulation's reply to your letter dated June 20, 2008 regarding the audit of the Division of Racing for the period beginning August 15, 2005 and ending February 3, 2008.

**Recommendation 1 – Separation of Duties.**

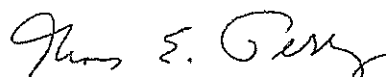
The Division of Racing will re-assign responsibilities regarding the handling of billing and cash receipts. The Division will also implement procedures to accomplish the necessary separation of duties using existing personnel as recommended by the Legislative Auditor.

**Recommendation 2 – Timely Submission of Collections.**

The Division will continue to monitor the timely submission of wagering taxes from licensees and request the Commission to take whatever action they deem appropriate when payments are not received within the seven days prescribed by the Business Regulation Article, §11-509 Annotated Code of Maryland.

If you have any questions regarding the Department's response, please contact me at 410-230-6020.

Sincerely,



Thomas E. Perez  
Secretary



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