

Performance Audit Report

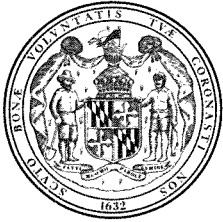
**Video Lottery Operations Revenue
Small, Minority, and Women-Owned Businesses Account**

October 2012



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

October 16, 2012

Senator James C. Rosapepe, Co-Chair, Joint Audit Committee
Delegate Guy J. Guzzone, Co-Chair, Joint Audit Committee
Members of Joint Audit Committee
Annapolis, Maryland

Ladies and Gentlemen:

Section 9-1A-35 of the State Government Article of the Annotated Code of Maryland requires the Office of Legislative Audits each fiscal year to audit and evaluate the use of the funds by eligible fund managers who receive grants from the Board of Public Works (BPW) to provide investment capital and loans to small, minority, and women-owned businesses in the State. The grants are to be made from the Small, Minority, and Women-Owned Businesses Account which is funded by 1.5 percent of video lottery terminal proceeds. BPW is to ensure that the fund managers allocate at least 50 percent of the funds to small, minority, and women-owned businesses in the jurisdictions and communities surrounding video lottery facilities.

We conducted an audit of the Account and noted that, as of June 30, 2012, no grants had been made from the Account to fund managers. Accordingly, we recommend that BPW ensure that a grant process for using Account funds is carried out, and grants are awarded to eligible fund managers to accomplish the purpose of the Account. On August 22, 2012, subsequent to our fieldwork, BPW entered into a Memorandum of Understanding with the Department of Business and Economic Development (DBED) for DBED to manage the grants program on BPW's behalf.

We determined that proper accountability had been established over the Account, which had a balance at June 30, 2012 totaling \$2,606,388. Receipts into the Account have totaled \$4,473,388 for fiscal years 2011 and 2012, and one transfer from the Account of \$1,867,000 was made in June 2012 to the Education Trust Fund as specified by law.

We wish to acknowledge the cooperation extended to us during the course of this audit by BPW.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Tom J. Barnickel III". The signature is written in a cursive style with a large, stylized initial "T".

Thomas J. Barnickel III, CPA
Acting Legislative Auditor

Background Information

Small, Minority, and Women-Owned Businesses Account

During the 2007 special session, the General Assembly enacted legislation to license video lottery terminal (VLT) gaming in Maryland contingent on the legislation being ratified by the voters of the State. In the November 2008 general election, the voters of Maryland ratified a constitutional amendment authorizing VLTs in the State. As a result of the ratification of the constitutional amendment, the Small, Minority, and Women-Owned Businesses Account (Account) was established; the legislation creating the Account was similarly enacted during the 2007 special session. State Law generally requires that 1.5 percent of VLT proceeds be paid into the Account, which is a special, nonlapsing fund administered by the Comptroller of Maryland under the authority of the Board of Public Works (BPW). State Law specifies that the Account is to be used by the BPW to make grants to eligible fund managers to provide investment capital and loans to small, minority, and women-owned businesses in the State, of which at least 50 percent must be allocated to such businesses in the jurisdictions and communities surrounding a video lottery facility. BPW is responsible for ensuring that the fund managers allocate the funds in accordance with the State law.

Video Lottery Facility Licenses and Operations

Licenses have been awarded to operate VLT casinos in Cecil, Worcester, Anne Arundel, and Allegany Counties and Baltimore City. The casinos in Cecil, Worcester, and Anne Arundel Counties began VLT gaming operations on September 27, 2010, January 4, 2011, and June 6, 2012, respectively. VLT gaming operations have not begun in Allegany County and Baltimore City.

Audit Scope, Objectives, and Methodology

Scope and Objectives

Section 9-1A-35 of the State Government Article of the Annotated Code of Maryland requires the Office of Legislative Audits each fiscal year to audit and evaluate the utilization of the funds that are allocated to small, minority, and women-owned businesses by eligible fund managers who received grants from

the BPW. As part of the audit, we also determined that the appropriate amounts were paid into the Account, disbursements or transfers from the Account were properly authorized, and proper accountability was established over the Account.

Our audit was performed 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.

Methodology

To accomplish our objectives, we interviewed employees of the BPW and the Department of Business and Economic Development (DBED), which as of August 22, 2012, was designated by the BPW to manage the grant program authorized by State law. We also reviewed the records maintained by the Comptroller for the Account, including the one transfer from the Account to the Education Trust Fund. Finally, we verified that the amounts transferred into the Account during fiscal years 2011 and 2012 were proper based on the total VLT revenue reflected in the records of the State Lottery Agency. As of June 30, 2012, no grants to any fund managers had been made from the Account.

Our fieldwork was completed during the period from March through July 2012. A copy of the draft report was provided to the BPW. The BPW's response to our findings and recommendations is included as an appendix to this report. As prescribed in State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise the BPW regarding the results of our review of its response.

Conclusions

We concluded that proper accountability had been established over the Account. Specifically, as of June 30, 2012, the Account had been funded as required by law and the one transfer from the Account to another State fund was made in accordance with law. No Account funds had yet been disbursed to fund managers to provide investment capital and loans to small, minority, and women-owned businesses in the State.

Since inception through June 30, 2012, the Small, Minority, and Women-Owned Businesses Account has been properly credited with 1.5 percent of VLT proceeds as specified by law. The Account began receiving funds during fiscal year 2011 when the first VLT facility began gaming operations.

A transfer of \$1,867,000 from the Account to the Education Trust Fund was made on June 1, 2012. This transfer was authorized by the enactment of Chapter 1, Laws of Maryland, 2012 Special Session 1 (Budget Reconciliation and Financing Act of 2012).

A summary of Account activity through June 30, 2012, according to the Comptroller's accounting records, is presented below.

Summary of Account Activity Fiscal Years 2011 and 2012	
Receipts	
Fiscal Year 2011	\$1,546,992
Fiscal Year 2012	<u>2,926,396</u>
Total Receipts	4,473,388
Transfer to the Education Trust Fund – June 1, 2012	<u>(1,867,000)</u>
Account Balance – June 30, 2012	<u>\$2,606,388</u>

Findings and Recommendations

Grant Awards

Finding 1

As of June 30, 2012, the Board of Public Works (BPW) had not made any grants to fund managers from the Account.

Analysis

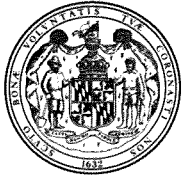
As of June 30, 2012, the BPW had not made any grants to eligible fund managers from the Account. State law specifies that BPW shall use the Account to make grants to eligible fund managers (entities with significant financial or investment experience) to provide investment capital and loans to small, minority, and women-owned businesses in the State. The law also requires that BPW ensure that eligible fund managers allocate at least 50 percent of the funds to small, minority, and women-owned businesses in jurisdictions and communities surrounding a video lottery facility and set the maximum amount of grant money that each eligible fund manager may use to pay expenses for administrative, actuarial, legal, and technical services.

We were advised by BPW staff that the Department of Business and Economic Development (DBED), at the instruction of the Governor, was in the process of preparing a proposal for BPW to designate DBED as the administering agency for the grant program. BPW staff also advised us that no grants would be made from the Account until BPW has approved a plan from DBED. On August 22, 2012, subsequent to our field work, the BPW entered into a Memorandum of Understanding (MOU) with DBED to have DBED manage the grants program on BPW's behalf.

Recommendation 1

We recommend that BPW

- a. ensure that the MOU grant process for using Account funds is carried out as intended,**
- b. award grants to fund managers to accomplish the purpose of the Account, and**
- c. ensure fund managers comply with the related law and applicable grant terms.**



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Board of Public Works

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APPENDIX

Martin O'Malley
Governor

Nancy K. Kopp
Treasurer

Peter Franchot
Comptroller

Sheila C. McDonald
Executive Secretary

October 12, 2012

Mr. Thomas J. Barnickel, CPA
Acting Legislative Auditor
301 West Preston Street, Room 1202
Baltimore, Maryland 21201

Dear Mr. Barnickel:

Our response to the audit report on the *Video Lottery Operations Revenue – Small, Minority, and Women-Owned Businesses Account* for fiscal years 2011 and 2012 is as follows.

Audit Finding: As of June 30, 2012, the Board of Public Works had not made any grants to fund managers from the Account.

Recommendation: We recommend that the Board of Public Works:

- a. ensure that the MOU grant process for using Account funds is carried out as intended;
- b. award grants to fund managers to accomplish the purpose of the Account; and
- c. ensure fund managers comply with the related law and applicable grant terms.

Our Response: The Board of Public Works agrees with the audit finding and the recommendation. As noted in the audit report, on August 22, 2012, the Board delegated to the Department of Business and Economic Development the authority to procure fund managers and designated DBED to administer the program as the Board's agent. Currently, DBED is engaged in a competitive process to procure fund managers. Based on the procurement, DBED will recommend proposed awards to the Board for approval. Through its approval process, the Board will make sure that the selections are of fund managers who will accomplish the Account's purpose. Once fund managers are in place, the Board – through DBED – will likewise ensure that the fund managers comply with State law.

Sincerely,

Sheila McDonald

cc: The Honorable Martin O'Malley
The Honorable Nancy K. Kopp
The Honorable Peter Franchot

AUDIT TEAM

Stephen C. Pease, CPA
Audit Manager

Terry S. Gibson
Senior Auditor