

NEW YORK STATE LOTTERY

Report to Management,
March 31, 1982 Audit

New York State Lottery
Swan Street Building
Empire State Plaza
Albany, New York 12223

November 29, 1982

Dear Sirs:

We are pleased to submit to you our Report to Management containing our observations and recommendations concerning internal controls and other matters resulting from our audit of the New York State Lottery's 1982 financial statements. During our audit, no material weaknesses in internal accounting control came to our attention.

Our report consists of a series of comments arranged by department as listed in the accompanying table of contents and within each department in order of relative importance. Our principal recommendations are summarized in Section 1 immediately following the table of contents. These recommendations are not the result of a special study and do not purport to be other than our observations incidental to our audit and are based on our knowledge at that time.

This report is subject to the limitations and definitions stated in the Appendix and should be read in that context. It is intended solely for the use of management of the Lottery and the State of New York and should not be used for any other purpose.

We will be pleased to discuss these recommendations with you further and to assist you in implementing them.

Yours very truly,

Deloitte Haskins & Sells

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Appendix

Note - Observations followed by an asterisk (*) are similar to observations made in our 1981 Report. To the extent that we have been informed that management is in the process of implementing certain recommendations included in our 1981 report, such recommendations have not been repeated herein.

1. Summary of Principal Recommendations

Funds Management

- 2A. Consider performing a cost/benefit study to determine the cost effectiveness of the Lottery investing in higher yielding investment instruments which allow frequent deposits and withdrawals.

Production

- 3A. Require each department receiving instant game tickets to maintain a log.

Validation

- 4A. . Enforce procedures to properly cancel winning tickets.
- . Expand current sampling procedures for redeemed tickets.
- . Adhere to established procedures regarding follow-up on balances due from distributors as they become delinquent.
- 4B. . Require dual participation in the opening of mail containing Lotto subscription checks.
- . Deposit subscription amounts on a daily basis.

Regional Accounting

- 5A. Assure that regional staff personnel are educated in the purpose, use and proper preparation of the house book log.

2. Funds Management

A. Maintenance of Savings Accounts

Observation:

- . The Lottery maintains four savings accounts which earn interest at the rate of 5.25%

Recommendation:

- . Consideration should be given to performing a cost/benefit study to determine the cost effectiveness of the Lottery investing in higher yielding investment instruments which allow frequent deposits and withdrawals.

B. Written Procedures for Distributor Limits and Receivable Write-offs

Observations:

- . We noted that the policy manual lacks guidelines for distributor consignment limits and the write-off of receivable balances. We observed that:
 - .. several distributor/vendor balances were written off during the year with the oral approval of the administrative director, and
 - .. personnel appeared uncertain of distributor consignment limits.

Recommendation:

- . Include in the policy manual procedures for:
 - .. authorizing changes in distributor consignment limits (which procedure, we understand, has been implemented recently), and
 - .. authorizing write-offs of distributor/vendor balances.

C. Proper Approval of General Journal Entries*

Observation:

- . General journal entries prepared and posted by Funds Management Department personnel are not always approved by department supervisors.

Recommendation:

- . We suggest that all general journal entries be approved by appropriate personnel and that such approval be evidenced by the initial or signature of the approving person.

D. Approval of Special Promotion Vouchers

Observation:

- . We noted in two cases the number of signatures required to approve special promotion vouchers was not evident. (A similar observation was made by the Internal Auditor, who issued a recommendation to resolve this matter. Such recommendation was not implemented by Funds Management.)

Recommendations:

- . All special promotion vouchers should be properly signed and then checked for proper approval before they are filed by Funds Management personnel.
- . Establish procedures to implement recommendations set forth by the Internal Audit Department. Each internal audit report should be responded to by management, explaining whether the recommendations were implemented and if not, why not.

3. Production

A. Accountability of Instant Game Tickets

Observations:

- . There are no procedures to monitor tickets issued by the Production Department to various Lottery Central personnel. Since these tickets are not distributed to the regions, and although they represent a small percentage of tickets issued, they are not accounted for in the monthly "Pepperoni" reporting package like other tickets used for similar purposes by the regions (promotions, tests, ticket exchanges, etc.).
- . Material Consignment Manifests used to document tickets issued to Lottery Central personnel are not signed by the personnel authorized to receive them.

Recommendations:

- . Require each department receiving instant game tickets to maintain a log. Information recorded should include the number of tickets received from the Production Department, the number of tickets used, and the balance on hand. At the close of each game this log, along with any tickets on hand, should be returned to the Production Department. A copy also should be returned directly to Funds Management to be included in the monthly "Pepperoni" reporting package.

- . Material Consignment Manifests should only be delivered to, and signed by, personnel authorized to receive instant game tickets.

4. Validation

A. Accountability for Redeemed Instant Game Tickets by the Validation Department

Observations:

- . Winning instant game tickets are received by the Validation Department uncanceled (perforated, stamped or mutilated) and incomplete as to winners' signatures and vendor number.
- . In our testing of redeemed ticket envelopes, we noted the contents listed on the face of eight envelopes did not agree to the contents within the envelope. In addition, we noted that two forged instant game tickets were enclosed in the envelopes.
- ✓ Procedures to monitor the collection of redeemed ticket adjustments prepared by the Validation Department and recorded by the regions are not being followed.

Recommendations:

- . Enforce procedures to properly complete and cancel winning tickets. Also, consideration should be given to adopting one uniform cancellation method.
- . Expand current sampling procedures for redeemed tickets.
- . Adhere to established procedures regarding follow-up on balances due from the distributors as they become delinquent. Further, we understand that procedures to include the preparation of a monthly log to accumulate balances due the Lottery, based upon errors discovered by the Validation Department, have been recently implemented. We recommend that Funds Management ascertain that subsequent adjustments to these balances have been appropriately reflected in the monthly "Pepperoni" reporting package.

- .. promotional tickets not yet distributed, and in certain instances undeposited receipts, were kept in a locked file cabinet in Region I which, we have been told, has been vandalized in the past.

Recommendations:

- . Assure that regional staff are educated in the purpose, use and proper preparation of the house book log. In addition, we recommend the following procedures be implemented:
 - .. internal audit should count house book log tickets as part of their regional audit procedures;
 - .. the house book log should account for the receipt of tickets from inventory as well as the disbursement of tickets for promotions as separate entries (which procedure, we understand, has been implemented recently);
 - .. enforce procedures to deliver promotional tickets directly to the appropriate persons and establish procedures for internal audit to confirm, on a test basis, the receipt of these tickets;
 - .. follow procedures to compare vouchers for authorized promotions to the regional house book, and
 - .. utilize the safe in Region I to store all tickets and receipts.

B. Preparation of Monthly "Pepperoni" Reporting Package

Observations:

- . We noted that a discrepancy between the number of instant game tickets sent by Region I to the Production Department and the number of instant game tickets received by them was not resolved on a timely basis. The tickets were reported incorrectly by Region I in the May 1981 monthly "Pepperoni" reporting package but were not corrected until the end of August 1981.
- . In one instance, we noted that the Regional Director's certification of the monthly "Pepperoni" reporting package did not include an indication as to the number of pages he was certifying.

Recommendations:

- . Discrepancies between the monthly "Pepperoni" reporting package and the records maintained by Lottery Central should be resolved during the monthly audit of the package by Funds Management. Any unresolved discrepancies should be followed up as part of the next month's audit procedures.
- . Regional Directors should ensure that their certification is complete.

C. Distributor Audit Reports

Observation:

- . Distributor audit reports are prepared monthly by regional personnel to reconcile each distributor's authorized regular consignment balance with the assets held by the distributor (tickets on hand, redeemed tickets, cash outstanding, promissory notes and claims). Any differences are required to be resolved by the regional director and communicated to Lottery Central. We noted several instances where the assets held by the distributor were less than his authorized regular consignment balance. These distributor audit reports were sent to Lottery Central with incomplete documentation explaining the differences and were not followed up in writing by Lottery Central employees.

Recommendation:

- . Require Lottery Central personnel to follow-up on the resolution of consignment balance differences on a timely basis. Any adjustments to consignment balances should be reported to Funds Management on a timely basis.

6. Administration

A. Unclaimed High Tier Lotto Prizes

Observation

- . The Lottery has changed its method for handling unclaimed high tier Lotto prizes. We noted that in three instances the Lottery purchased annuities for unclaimed high tier Lotto prizes, naming themselves as beneficiary.

Background:

- . In the past all unclaimed prizes in the Lottery's prize pending account were invested in a short-term investment pool by the New York State Department of Audit and Control.

Recommendation:

- . While we are unaware of the various investments approved by New York State for utilization by the Lottery, we recommend that the Lottery:
 - .. determine if these annuities are an appropriate investment, and
 - .. consider what course of action will be taken when the annuity payment is received and/or when the prize may be unclaimed for one year and thus payable to New York State.

REPORT LIMITATIONS AND DEFINITIONS

Purpose of the Study and Evaluation

We have examined the financial statements of the New York State Lottery (the "Lottery") for the year ended March 31, 1982 and have issued our report thereon dated July 9, 1982. We have not performed any substantive auditing procedures subsequent to that date; accordingly, this report is based on our knowledge as of that date and should be read with that understanding. As part of our examination, we made a study and evaluation of the Lottery's system of internal accounting control to the extent we considered necessary to evaluate the system as required by generally accepted auditing standards. The purpose of our study and evaluation was to determine the nature, timing and extent of the auditing procedures necessary for expressing an opinion on the Lottery's financial statements. Our study and evaluation was more limited than would be necessary to express an opinion on the system of internal accounting control taken as a whole and would not necessarily disclose all material weaknesses in the system. Accordingly, we do not express an opinion on the system of internal accounting control of the Lottery taken as a whole.

Management's Responsibility for, and the Objectives and Limitations of, Internal Accounting Control and the Definition of a Material Weakness

The following comments concerning management's responsibility for internal accounting control, the objectives of and the inherent limitations in a system of internal accounting control, and the definition of a material weakness are excerpts from Statements on Auditing Standards of the American Institute of Certified Public Accountants.

Management's Responsibility

The management of the Lottery is responsible for establishing and maintaining a system of internal accounting control. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures.

Objectives

The objectives of a system are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles.

Limitations

Because of inherent limitations in any system of internal accounting control, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of a system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the degree of compliance with the procedures may deteriorate.

Material Weakness

A material weakness for the auditor's purpose is a condition in which the specific control procedures, or the degree of compliance with them, do not, in the auditor's judgment, reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. These criteria may be broader than those that may be appropriate for evaluating weaknesses in accounting control for management or other purposes.