

North Dakota  
Racing Commission  
BISMARCK, NORTH DAKOTA

**Audit Report**

For the Biennium Ended  
June 30, 2013

ROBERT R. PETERSON  
STATE AUDITOR

Office of the State Auditor  
Division of State Audit

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## *Transmittal Letter*

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March 26, 2014

The Honorable Jack Dalrymple, Governor  
Members of the North Dakota Legislative Assembly  
Mr. Gunner LaCour, Director of Racing

We are pleased to submit this audit of the North Dakota Racing Commission for the biennium ended June 30, 2013. This audit resulted from the statutory responsibility of the State Auditor to audit or review each state agency once every two years. The same statute gives the State Auditor the responsibility to determine the contents of these audits.

In determining the contents of the audits of state agencies, the primary consideration was to determine how we could best serve the citizens of the state of North Dakota. Naturally we determined financial accountability should play an important part of these audits. Additionally, operational accountability is addressed whenever possible to increase efficiency and effectiveness of state government.

The in-charge auditor for this audit was Jacqueline Castleberry. Cindi Pedersen, CPA, was the audit manager. Inquiries or comments relating to this audit may be directed to the audit manager by calling (701) 328-2241. We wish to express our appreciation to Director LaCour and his staff for the courtesy, cooperation, and assistance they provided to us during this audit.

Respectfully submitted,

A handwritten signature in cursive script that reads "Bob Peterson".

Robert R. Peterson  
State Auditor

# *Executive Summary*

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## *Introduction*

The North Dakota Racing Commission is the regulatory body in charge of regulating live and simulcast racing in North Dakota and administers three special funds for the benefit of the horse racing industry in North Dakota. The Breeders' Fund was established to financially reward breeders or owners of North Dakota bred horses. The Purse Fund was established to supplement and improve purses offered at racetracks within the state. The Racing Promotion Fund was established to assist in improving and upgrading racetracks in the state, promoting horse racing in the state, and developing new racetracks in the state as necessary. The Commission is made up of five members appointed by the Governor and the office staff consists of a Director of Racing and an Administrative Assistant.

The Legislative Audit and Fiscal Review Committee (LAFRC) requests certain items be addressed by auditors performing audits of state agencies. Those items and the Office of the State Auditor's responses are noted below.

## *Responses to LAFRC Audit Questions*

### *1. What type of opinion was issued on the financial statements?*

Financial statements were not prepared by the North Dakota Racing Commission in accordance with generally accepted accounting principles so an opinion is not applicable. The agency's transactions were tested and included in the state's basic financial statements on which an unqualified opinion was issued.

### *2. Was there compliance with statutes, laws, rules, and regulations under which the agency was created and is functioning?*

Yes.

### *3. Was internal control adequate and functioning effectively?*

Yes.

### *4. Were there any indications of lack of efficiency in financial operations and management of the agency?*

Other than our work addressing "Breeders' Fund Registry Cost Savings" (page 11), there were no indications of a lack of efficiency in financial operations and management of the North Dakota Racing Commission.

### *5. Has action been taken on findings and recommendations included in prior audit reports?*

There were no recommendations included in the prior audit report.

6. *Was a management letter issued? If so, provide a summary below, including any recommendations and the management responses.*

Yes, a management letter was issued and is included on page 14 of this report, along with management's response.

### **LAFRC Audit Communications**

7. *Identify any significant changes in accounting policies, any management conflicts of interest, any contingent liabilities, or any significant unusual transactions.*

There were no significant changes in accounting policies, no management conflicts of interest were noted, no contingent liabilities were identified or significant unusual transactions.

8. *Identify any significant accounting estimates, the process used by management to formulate the accounting estimates, and the basis for the auditor's conclusions regarding the reasonableness of those estimates.*

The North Dakota Racing Commission's financial statements do not include any significant accounting estimates.

9. *Identify any significant audit adjustments.*

Significant audit adjustments were not necessary.

10. *Identify any disagreements with management, whether or not resolved to the auditor's satisfaction relating to a financial accounting, reporting, or auditing matter that could be significant to the financial statements.*

None.

11. *Identify any serious difficulties encountered in performing the audit.*

None.

12. *Identify any major issues discussed with management prior to retention.*

This is not applicable for audits conducted by the Office of the State Auditor.

13. *Identify any management consultations with other accountants about auditing and accounting matters.*

None.

14. *Identify any high-risk information technology systems critical to operations based on the auditor's overall assessment of the importance of the system to the agency and its mission, or whether any exceptions identified in the six audit report questions to be addressed by the auditors are directly related to the operations of an information technology system.*

ConnectND Finance and Human Resource Management System (HRMS) are high-risk information technology systems critical to the North Dakota Racing Commission.

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

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## ***Audit Objectives***

The objectives of this audit of the North Dakota Racing Commission for the biennium ended June 30, 2013 were to provide reliable, audited financial statements and to answer the following questions:

1. What are the highest risk areas of the North Dakota Racing Commission's operations and is internal control adequate in these areas?
2. What are the significant and high-risk areas of legislative intent applicable to the North Dakota Racing Commission and are they in compliance with these laws?
3. Are there areas of the North Dakota Racing Commission's operations where we can help to improve efficiency or effectiveness?

## ***Audit Scope***

This audit of the North Dakota Racing Commission is for the biennium ended June 30, 2013. We conducted this performance audit 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 the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The North Dakota Racing Commission's sole location is its Bismarck office which was included in the audit scope.

## ***Audit Methodology***

To meet the objectives outlined above, we:

- Prepared financial statements from the legal balances on the state's accounting system tested as part of this audit and the audit of the state's Comprehensive Annual Financial Report and developed a discussion and analysis of the financial statements.
- Performed detailed analytical procedures including computer-assisted auditing techniques. These procedures were used to identify high-risk transactions and potential problem areas for additional testing.
- Tested internal control and compliance with laws and regulations which included selecting representative samples to determine if controls were operating effectively and to determine if laws were being followed consistently. Non-statistical sampling was used and the results were projected to the population. Where applicable, populations were stratified to ensure that particular groups within a population were adequately represented in the sample, and to improve efficiency by gaining greater control on the composition of the sample.

- Interviewed appropriate agency personnel.
- Queried the ConnectND (PeopleSoft) system. Significant evidence was obtained from ConnectND.
- Observed North Dakota Racing Commission's processes and procedures.

In aggregate there were no significant limitations or uncertainties related to our overall assessment of the sufficiency and appropriateness of audit evidence.



## ***Discussion and Analysis***

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The accompanying financial statements have been prepared to present the North Dakota Racing Commission's revenues and expenditures on the legal (budget) basis. The accompanying financial statements are not intended to be presented in accordance with generally accepted accounting principles (GAAP).

For the biennium ended June 30, 2013, operations of the North Dakota Racing Commission were primarily supported by racing tax and unclaimed ticket and breakage revenue collected on pari-mutual wagering. This is supplemented by appropriations from the state's general fund.

### ***Financial Summary***

Revenue consisted primarily of racing taxes and unclaimed tickets and breakage revenue, as well as license and registration fees. Other revenue during the audited period included interest and reimbursements from services providers for the simulcast auditor. Total revenues were \$750,752 for the year ended June 30, 2013, as compared to \$643,891 for the year ended June 30, 2012. The increase in total revenue for the audited period reflects primarily the increase in racing tax. All other revenues remained fairly constant.

Total expenditures for the North Dakota Racing Commission were \$732,527 for the year ended June 30, 2013, as compared to \$615,783 for the prior year. The increase in total expenditures for the audit period reflects primarily the increase in purse supplements and breeder award payments. All other expenditures remained fairly constant.

### ***Fund Balance Summary***

The cash balances in the North Dakota Racing Commission's Breeders' Fund and Racing Promotion Fund have stabilized, with slight increases noted since the prior biennium; whereas the Purse Fund continues to decline. The decline in the Purse Fund appears to be directly related to the increase in grants given from this fund and the decrease in unclaimed tickets and breakage revenue. 2009 North Dakota Session Law, Chapter 455, directs that all unclaimed tickets and breakage revenue is allocated amongst the three funds. Fifty percent is deposited into the Purse Fund, thirty percent into the Breeders' Fund, and twenty percent into the Racing Promotion Fund.

The cash balances in the North Dakota Racing Commission's funds for the biennium ended June 30, 2013 were as followed: Breeders' Fund \$789,161.41; Purse Fund 124,194.83; and Racing Promotion Fund \$117,565.16. The limited funds available in the Purse Funds have limited the North Dakota Racing Commission's ability to supplement purse prizes.

The Fund Balance Table in Appendix A, on page 13, shows the balances of the North Dakota Racing Commission's funds as of calendar years ended 2009 – 2013.

# *Financial Statements*

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## *Statement of Revenues and Expenditures*

	<u>June 30, 2013</u>	<u>June 30, 2012</u>
<b><u>Revenues and Other Sources:</u></b>		
Racing Taxes	\$505,513	\$406,295
Unclaimed Tickets and Breakage	166,634	184,639
Licenses and Registration	76,505	50,899
Miscellaneous Refunds	1,374	800
Interest on Investments	726	1,258
<b>Total Revenues and Other Sources</b>	<u>\$750,752</u>	<u>\$643,891</u>
<b><u>Expenditures and Other Uses:</u></b>		
Purse Supplements	\$231,000	\$157,000
Racing Promotion Grants	121,200	113,995
Breeder Award Payments	122,379	95,287
Salaries and Benefits	152,272	144,749
Fees – Professional Services	48,410	49,105
Travel	13,645	12,382
Miscellaneous Expenses	25,955	22,309
Operating Fees and Services	9,318	12,588
Rentals/Leases – Bldg/Land	8,348	8,368
<b>Total Expenditures and Other Uses</b>	<u>\$732,527</u>	<u>\$615,783</u>

## Statement of Appropriations

For The Biennium Ended June 30, 2013

<b>Expenditures by Line Item:</b>	<u>Original Appropriation</u>	<u>Adjustments</u>	<u>Final Appropriation</u>	<u>Expenditures</u>	<u>Unexpended Appropriation</u>
Racing Commission	\$ 447,501		\$ 447,501	\$ 421,268	\$ 26,233
<b>Totals</b>	<u>\$ 447,501</u>	<u>\$ 0</u>	<u>\$ 447,501</u>	<u>\$ 421,268</u>	<u>\$ 26,233</u>
<b>Expenditures by Source:</b>					
General Fund	\$ 317,501		\$ 317,501	\$ 317,500	\$ 1
Other Funds	130,000		130,000	103,768	26,232
<b>Totals</b>	<u>\$ 447,501</u>	<u>\$ 0</u>	<u>\$ 447,501</u>	<u>\$ 421,268</u>	<u>\$ 26,233</u>

### Expenditures Without Appropriations Of Specific Amounts:

The Breeders' Fund has a continuing appropriation authorized by North Dakota Century Code section 53-06.2-11 (\$255,393 of expenditures for this biennium).

The Purse Fund has a continuing appropriation authorized by North Dakota Century Code section 53-06.2-11 (\$388,000 of expenditures for this biennium).

The Racing Promotion Fund has a continuing appropriation authorized by North Dakota Century Code section 53-06.2-11 (\$283,648 of expenditures for this biennium).

## ***Internal Control***

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In our audit for the biennium ended June 30, 2013, we identified the following areas of the North Dakota Racing Commission's internal control as being the highest risk:

### ***Internal Controls Subjected to Testing:***

- Controls surrounding the processing of revenues.
- Controls surrounding the processing of payroll.
- Controls surrounding the processing of expenditures.
- Controls relating to compliance with legislative intent.
- Controls surrounding the ConnectND (PeopleSoft) system.

The criteria used to evaluate internal control is published in the publication *Internal Control – Integrated Framework* from the Committee of Sponsoring Organizations (COSO) of the Treadway Commission.

We gained an understanding of internal control surrounding these areas and concluded as to the adequacy of their design. We also tested the operating effectiveness of those controls we considered necessary based on our assessment of audit risk. We concluded internal control was adequate.

Auditors are required to report deficiencies in internal control that are significant within the context of the objectives of the audit. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect: (1) misstatements in financial or performance information; (2) violations of laws and regulations; or (3) impairments of effectiveness or efficiency of operations, on a timely basis. Considering both qualitative and quantitative factors, we did not identify any significant deficiencies in internal control. However, we noted other matters involving internal control that we have reported to management of the North Dakota Racing Commission in a management letter dated March 26, 2014.

## *Compliance With Legislative Intent*

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In our audit for the biennium ended June 30, 2013, we identified and tested the North Dakota Racing Commission's compliance with legislative intent for the following areas we determined to be significant and of higher risk of noncompliance:

- Collection and depositing of the proper amounts for taxes on pari-mutuel racing (North Dakota Century Code 53-06.2-11).
- Compliance with the limit of racing promotion funds used for operating expenses (North Dakota Century Code 53-06.2-11)
- Proper use of the following legally restricted funds:
  - Breeders' Fund
  - Purse Fund
  - Racing Promotion Fund
- Proper use of the State Treasurer (State Constitution, Article X, Section 12)
- Compliance with appropriations (2011 North Dakota Session Laws Chapter 52)
- Adequate blanket bond coverage of employees (NDCC section 26.1-21-08).
- Compliance with annual inventory of fixed assets.
- Compliance with payroll-related laws including statutory salaries for applicable elected and appointed positions, and certification of payroll.

The criteria used to evaluate legislative intent are the laws as published in the *North Dakota Century Code* and the *North Dakota Session Laws*.

*Government Auditing Standards* require auditors to report all instances of fraud and illegal acts unless they are inconsequential within the context of the audit objectives. Further, auditors are required to report significant violations of provisions of contracts or grant agreements, and significant abuse that has occurred or is likely to have occurred.

The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*. Thus, we concluded there was compliance with the legislative intent identified above.

## *Operations*

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Our audit of the North Dakota Racing Commission identified the following area of potential improvement to operations:

- Is the contract for administrative services of the Breeders' Fund as required by NDCC 53-06.2-04.1 the proper use of the Breeders' Fund monies?

### ***Breeders' Fund Registry Cost Savings (Finding 14-1)***

#### **Condition:**

It may be more cost effective for the Horse Racing Commission (Commission) to maintain and administer the North Dakota-bred horse registry themselves. However, North Dakota Century Code (NDCC) section 53-06.2-04.1 requires the Commission to contract with a private person (Contractor) to maintain the registry which is used to determine qualification for breeders' fund awards or purse supplements.

The Contractor's rate during the 2011-2013 biennium was \$25 per hour but increased dramatically to \$65 per hour for the 2013-2015 biennium. Per review of the Commission's meeting minutes, errors made by the Contractor caused the Commission to expend staff time to make corrections and to disburse an additional \$23,250 from the Breeder's Fund beyond what it would have disbursed had the errors not been made by the Contractor.

#### **Criteria:**

NDCC 53-06.2-04.1 states through a competitive bidding process, the Commission shall award the contract to the lowest responsible bidder. The cost of the contract must be paid from the Breeders' Fund.

#### **Cause:**

Due to the Commission only receiving one bid, they were forced to accept the bid at a significantly increased hourly rate.

#### **Effect or Potential Effect:**

The Contractor was paid approximately \$51,000 during the audit period and the 160% increase in the hourly rate will result in substantial future payments. Additionally, the errors made by the Contractor during calendar years 2011 through 2013 resulted in the Commission spending numerous hours making corrections as well as additional costs to the Breeder's Fund.

#### **Operational Improvement:**

We recommend the North Dakota Racing Commission determine if it is cost effective to administer the Breeders' Fund themselves. If so, the Commission should consider proposing changes to NDCC section 53-06.2-04.1 which requires the Commission to contract those services with a private person.

**North Dakota Racing Commission Response:**

*The Commission is in full agreement with the State Auditor's findings and recommendations.*

*More specifically, the Commission has been frustrated by an inability to effectively control the Breeder's Fund for which it is responsible. The Commission by necessity relies on the accuracy of the Contracted Entity as it would otherwise incur significant costs in reviewing all calculations and awards. However, this problem has been compounded by the lack of available outside entities that have sufficient expertise to effectively administer the fund. This has ultimately led to a drastic increase in cost to the Breeder's Fund and numerous errors in its administration, imposing significant costs on both the Commission and the horsemen of North Dakota.*

*At the April 25, 2014 Commission meeting, authorization was provided to the Director to begin planning the appropriate corrective action. Specifically, the Director will draft and submit legislation which removes the language in NDCC 53-06.2-04.1 requiring the Commission to obtain Breeder's Fund administrative services from an outside entity. If the legislation is successful, the Commission has been exploring possible solutions such as the hiring of a half-time person for approximately half the current costs and/or the development of a Breeder's Fund database (one-time cost equal to or less than one year of services) which would significantly reduce the effort required to administer the fund allowing the Commission to rely on current personnel only.*

# Appendix A

## Fund Balance Table – Calendar Year Ended

	2009	2010	2011	2012	2013
<b><u>Breeders Fund:</u></b>					
Beginning Fund Balance	\$ 676,677	\$ 619,632	\$ 630,224	\$ 694,729	\$ 719,789
Revenue	62,681	110,987	176,534	157,355	155,984
Expenses	119,726	100,395	112,030	132,294	143,198
Ending Fund Balance	<u>\$ 619,632</u>	<u>\$ 630,224</u>	<u>\$ 694,729</u>	<u>\$ 719,789</u>	<u>\$ 732,576</u>
<b><u>Purse Fund:</u></b>					
Beginning Fund Balance	\$ 535,308	\$ 146,895	\$ 173,096	\$ 231,747	\$ 172,208
Revenue	66,127	149,201	238,651	186,461	168,603
Expenses	454,540	123,000	180,000	246,000	230,540
Ending Fund Balance	<u>\$ 146,895</u>	<u>\$ 173,096</u>	<u>\$ 231,747</u>	<u>\$ 172,208</u>	<u>\$ 110,271</u>
<b><u>Racing Promotion Fund:</u></b>					
Beginning Fund Balance	\$ 337,515	\$ 249,526	\$ 155,672	\$ 130,562	\$ 143,280
Revenue	225,335	122,635	143,735	166,171	263,906
Expenses	313,324	216,489	168,845	153,453	216,339
Ending Fund Balance	<u>\$ 249,526</u>	<u>\$ 155,672</u>	<u>\$ 130,562</u>	<u>\$ 143,280</u>	<u>\$ 190,847</u>
Total Funds	\$ 1,016,053	\$ 958,992	\$ 1,057,038	\$ 1,035,277	\$ 1,033,694



# ***Management Letter (Informal Recommendations)***

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March 26, 2014

Mr. Gunner LaCour  
Director of Racing  
North Dakota Racing Commission  
500 North 9<sup>th</sup> Street  
Bismarck, ND 58501-4509

Dear Mr. LaCour:

We have performed an audit of the North Dakota Racing Commission for the biennium ended June 30, 2013, and have issued a report thereon. As part of our audit, we gained an understanding of the North Dakota Racing Commission's internal control structure to the extent we considered necessary to achieve our audit objectives. We also performed tests of compliance as described in the same report.

Our audit procedures are designed primarily to enable us to report on our objectives including those related to internal control and compliance with laws and regulations and may not bring to light all weaknesses in systems and procedures or noncompliance with laws and regulations which may exist. We aim, however, to use our knowledge of your organization gained during our work to make comments and suggestions which we hope will be useful to you.

In connection with the audit, gaining an understanding of the internal control structure, and tests of compliance with laws and regulations referred to above, we noted certain conditions we did not consider reportable within the context of your audit report. These conditions relate to areas of general business practice or control issues that have no significant bearing on the administration of federal funds. We do, however, want to present our recommendations to you for your consideration and whatever follow-up action you consider appropriate. During the next audit we will determine if these recommendations have been implemented, and if not, we will reconsider their status.

The following present our informal recommendations.

## **INTERNAL CONTROL**

Informal Recommendation 14-1: We recommend the North Dakota Racing Commission strengthen controls surrounding their approval processes to ensure:

- The preparer of correcting entries is not also approving them.
- All Payroll Certifications are approved in a timely manner.
- Timesheets are approved by an individual with proper authority.

Informal Recommendation 14-2: We recommend the North Dakota Racing Commission strengthen controls to ensure proper support is received for all expenditures.

Management of the North Dakota Racing Commission agreed with these recommendations.

I encourage you to call myself or an audit manager at 328-2241 if you have any questions about the implementation of recommendations included in your audit report or this letter.

Sincerely,

A handwritten signature in cursive script that reads "Jacqueline Castleberry".

Jacqueline Castleberry  
Auditor in-charge

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