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A Follow-up Audit Report on

**Workforce Management,  
Procurement, and Lotto Texas  
Activities at the Texas Lottery  
Commission**

February 2008  
Report No. 08-022



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***Workforce Management, Procurement, and***  
***Lotto Texas Activities at the Texas***  
***Lottery Commission***

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## ***Overall Conclusion***

The Texas Lottery Commission (Agency) has fully or substantially implemented the majority of prior State Auditor's Office recommendations regarding workforce management, procurement, and Lotto Texas activities. Specifically, of the 34 high-risk recommendations selected for follow-up audit work:

- The Agency has fully implemented 11 of 13 (85 percent) recommendations for workforce management.
- The Agency has fully or substantially implemented 10 of 12 (83 percent) recommendations for procurement.
- The Agency has fully implemented 8 of 9 (89 percent) recommendations for Lotto Texas activities.

While the Agency has made progress in implementing most of the prior audit recommendations, it should continue its efforts to strengthen workforce management and procurement activities. For example:

- Although the Agency has a process for addressing formal complaints made through its Human Resources Division, it does not have a process to address informal employee complaints made to its ombudsman, managers or division directors, and internal audit. It also does not ensure that it communicates complaint resolutions to all interested parties. In addition, the Agency lacks formal policies and procedures for the ombudsman position it created in 2006. Additionally, the Agency's ombudsman does not have a formal role in the employee complaint process.
- Results of an Agency-wide survey the State Auditor's Office conducted in 2007 indicate that Agency staff believe that some key aspects of employee relations have improved significantly since the State Auditor's Office conducted a similar

### **Background Information**

Auditors determined the implementation status for 34 high-risk recommendations that the State Auditor's Office made in the following reports:

- *An Audit Report on Workforce Management at the Texas Lottery Commission* (State Auditor's Office Report No. 06-047, July 2006).

At the time auditors completed follow-up work, that report had been released for 18 months; auditors followed up on 13 of the 24 recommendations in that report.

- *An Audit Report on Procurement at the Texas Lottery Commission* (State Auditor's Office Report No. 06-062, August 2006).

At the time auditors completed follow-up work, that report had been released for 17 months; auditors followed up on 12 of the 22 recommendations in that report.

- *An Audit Report on Lotto Texas Activities at the Texas Lottery Commission* (State Auditor's Office Report No. 06-046, July 2006).

At the time auditors completed follow-up work, that report had been released for 18 months; auditors followed up on 9 of the 18 recommendations in that report.

See Appendix 3 for the Agency's self-reported status of recommendations not selected for follow-up audit work.

survey in February 2006. For example, in 2007, 70 percent of employees agreed that they were treated with respect and dignity, compared with 55 percent in 2006. At the same time, responses and employee comments indicate that employees continue to have concerns about key aspects of the work environment, including a fear of retaliation. In 2007, 44 percent of employees agreed that they will not be retaliated against if they raise issues or concerns; in 2006, 38 percent of employees agreed with that statement.

- Weaknesses in the Agency's policies and procedures for negotiating contracts increase the risk that the most favorable terms and conditions may not be obtained. In addition, the Agency should address weaknesses that remain in its monitoring of the primary lottery operator. A third-party reviewer contracts with the primary lottery operator, rather than directly with the Agency, to monitor the primary lottery operator's contract compliance. Therefore, the third-party reviewer may appear to lack independence from the primary lottery operator. This may impair the third-party reviewer's ability to ensure that it conducts its reviews in the best interests of the Agency.

## ***Key Recommendations***

The Agency should:

- Develop guidelines for informal complaints made to the Agency's ombudsman, internal auditors, or supervisors. The Agency's processes for addressing informal complaints should assist supervisors in identifying issues that require follow-up beyond the informal complaint process. Additionally, for complaints made to the Agency's ombudsman or internal auditor, or for complaints that require additional follow-up beyond informal management resolution, these guidelines should provide a defined process to ensure appropriate initiation, investigation, documentation, resolution, and communication of the final resolution of all complaints to all parties involved, as well as timeframes for each of these stages.
- Finalize its policies and procedures for the ombudsman position and obtain approval of those policies and procedures from executive management and the Commission.
- Evaluate how the ombudsman position can best address the concerns of employees and, if necessary, revise the ombudsman's duties so that the ombudsman has a formal role in ensuring the success of the employee complaint process.
- Contract directly with a third-party reviewer to monitor its primary lottery operator's compliance with contract terms and requirements. The Agency may choose to continue to rely on the third-party reviewer's reports until the current contract is expired, but the Agency should take additional steps to verify the accuracy and completeness of these reports. The Agency may also consider

contracting directly with the current third-party reviewer until such time as it can conduct a competitive procurement process to avoid an interruption in service.

## ***Summary of Management's Response***

The Agency agreed with the recommendations in this report.

## ***Summary of Objective, Scope, and Methodology***

The audit objective was to determine whether the Agency has made progress in implementing recommendations to correct deficiencies identified in the following reports:

- *An Audit Report on Procurement at the Texas Lottery Commission* (State Auditor's Office Report No. 06-062, August 2006).
- *An Audit Report on Workforce Management at the Texas Lottery Commission* (State Auditor's Office Report No. 06-047, July 2006).
- *An Audit Report on Lotto Texas Activities at the Texas Lottery Commission* (State Auditor's Office Report No. 06-046, July 2006).

The scope of this audit originally included reviewing the Agency's implementation of high-risk audit recommendations concerning workforce management, procurement, and Lotto Texas activities during the period from September 1, 2006, through August 31, 2007. At the request of the Chairman of the Commission, the State Auditor's Office also conducted an Agency-wide employee survey and compared the results of that survey with a prior survey the State Auditor's Office conducted in February 2006.

The audit methodology consisted of identifying high-risk recommendations from three recent State Auditor's Office audits and collecting information to determine the implementation status of those recommendations.

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# Detailed Results

Chapter 1

## ***The Agency Has Fully Implemented the Majority of High-risk Recommendations Regarding Workforce Management, But It Should Continue Efforts to Strengthen Employee Relations Practices***

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The Texas Lottery Commission (Agency) has made progress in implementing high-risk recommendations to address deficiencies identified in *An Audit Report on Workforce Management at the Texas Lottery Commission* (State Auditor's Office Report No. 06-047, July 2006). Of the 13 recommendations auditors reviewed, 11 were fully implemented. Table 1 on the next page summarizes the implementation status of each of the recommendations auditors reviewed. For the Agency's self-reported status of recommendations not selected for follow-up audit work, see Appendix 3.

However, the Agency should continue to strengthen certain employee relations practices:

- The Agency should enhance its processes for addressing employee complaints to include complaints made informally to its ombudsman, managers or division directors, and internal auditor. Additionally, the Agency should ensure that it communicates complaint resolutions to all involved parties and implements a timeline for review of and response to appeals made to the executive director.

### Definitions of Implementation Status

- **Fully Implemented:** Successful development and use of a process, system, or policy to implement a prior recommendation.
- **Substantially Implemented:** Successful development but inconsistent use of a process, system, or policy to implement a prior recommendation.
- **Incomplete/Ongoing:** Ongoing development of a process, system, or policy to address a prior recommendation.
- **Not Implemented:** Lack of a formal process, system, or policy to address a prior recommendation.

- The Agency should clarify the role, reporting relationship, and responsibilities of its ombudsman and formalize these items in approved policies and procedures.
- The Agency should continue to address employee concerns identified in staff and management responses to the State Auditor's Office 2006 and 2007 employee surveys and the Survey of Organizational Excellence conducted by the University of Texas at Austin.

Table 1

Status of Implementation of High-risk Audit Recommendations for Workforce Management			
Recommendation	Implementation Status	Auditor Comments	
1	The Agency should adopt an employee grievance policy to ensure consistency in how it addresses grievances. The policy should cover the initiation, documentation, investigation, and resolution of all employee grievances, as well as communication with all parties involved.	Incomplete/Ongoing	<p>While the Agency adopted procedures to address general complaints and grievances made to the Human Resources Department, those procedures do not include all complaints, such as those made to the ombudsman, to immediate supervisors, or to the internal auditor through EthicsPoint (the automated system the Agency uses to receive and respond to anonymous complaints from employees).</p> <p>For the majority of complaints auditors reviewed, the Agency did not communicate specific resolution to the employee. In addition, the appeal process for complaints and grievances lacks a timeline for review and response by the executive director.</p> <p>See Chapter 1-A of this report for additional discussion of the Agency's complaint processes.</p>
2	<p>The Agency should create an employee ombudsman position that reports directly to the executive director, with access to members of the Texas Lottery Commission. The position should meet the qualifications for an ombudsman set forth in the State Classification Plan. The ombudsman should be responsible for:</p> <p>Ensuring that the employee grievance policy is implemented.</p> <p>Facilitating a confidential and neutral process for resolving employment-related concerns in a fair and equitable manner.</p> <p>Meeting individually with employees to address issues before they become formal grievances.</p> <p>Facilitating ad hoc discussions with non-supervisory employees to give them an opportunity to provide the Commission and management with input on organizational and policy changes, including how to address issues raised in the State Auditor's Office survey and the Survey of Organizational Excellence.</p>	Incomplete/Ongoing	<p>The Agency created an ombudsman position that reports to the executive director and meets the requirements in the State Classification Plan. However, the Agency has not developed policies and procedures to govern the responsibilities of the ombudsman or formalized the ombudsman's reporting relationship. Specifically:</p> <ul style="list-style-type: none"> <li>▪ The ombudsman position is separate and apart from the Agency's employee complaint and grievance processes. The Human Resources Department, and not the ombudsman, is responsible for implementing those processes.</li> <li>▪ The ombudsman has not yet facilitated employee discussion groups regarding potential organizational or policy changes.</li> </ul> <p>See Chapter 1-B of this report for additional discussion of the Agency's ombudsman position.</p>
3	The Agency should develop, implement, and enforce Agency policies and procedures that provide guidance for management on counseling, disciplinary actions, and involuntary terminations. Information regarding best practices in these areas is available from sources such as the Society for Human Resource Management.	Fully Implemented	<p>The Agency has developed and implemented policies and procedures for addressing employee counseling, disciplinary actions, and involuntary terminations.</p> <p>However, auditors identified one instance in which Agency managers documented performance concerns regarding an employee but did not make a final disposition.</p>
4	The Agency should develop tools and training to assist supervisors and managers in selecting appropriate responses to unsatisfactory job performance.	Fully Implemented	<p>The Agency developed an annual supervisory training program for supervisors and managers that addressed managing performance issues and disciplinary actions. It provided this training to Agency supervisors in fiscal year 2007.</p>

**Status of Implementation of High-risk Audit Recommendations for Workforce Management**

Recommendation	Implementation Status	Auditor Comments
<p>5 The Agency should require supervisors and managers to document support for all disciplinary actions using standardized forms to ensure that the Agency can defend such actions and demonstrate compliance with state and federal employment laws.</p>	<p>Fully Implemented</p>	<p>The Agency revised its policies to require supervisors and managers to document support for disciplinary actions using standardized forms. For the six counseling and disciplinary actions that occurred in fiscal year 2007, the Agency complied with its established policies.</p> <p>The Agency can further assist managers in implementing its policies by developing procedures to clearly define which types of counseling require documentation. Providing additional guidance to managers and supervisors on what types of counseling, including verbal counseling, require documentation would improve the consistency of disciplinary documentation across the Agency.</p>
<p>6 The Agency should conduct its supervisory training program with sufficient regularity to ensure that all Agency supervisors are sufficiently prepared to facilitate the success of the employees they oversee. New supervisors should receive supervisory training as soon as practical after assuming supervisory responsibilities.</p>	<p>Fully Implemented</p>	<p>The Agency developed an annual supervisory training program and offered it in fiscal year 2007. The Agency requires supervisors to attend courses offered through this program within 90 days of becoming a supervisor and every two years thereafter. However, the training program does not identify course topics that all supervisors should be required to attend.</p> <p>Auditors tested the training records for seven supervisors and managers and determined that all of them had attended some supervisory training.</p>
<p>7 The Agency should enhance its supervisory training program to include training that addresses the issues raised in this report.</p>	<p>Fully Implemented</p>	<p>The Agency's annual supervisory training program includes topics such as employee relations, disciplinary actions, and the complaints and grievance processes. The Agency also developed new performance evaluation training after it developed a new performance evaluation system.</p>
<p>8 The Agency should complete the development and implementation of a training database that allows supervisors and human resources personnel to track training taken by all Agency employees.</p>	<p>Fully Implemented</p>	<p>The Agency has a training database that allows human resources personnel and division directors to track training taken by all Agency employees.</p>
<p>9 The Agency should complete the revisions it is currently making to its performance evaluation system. The revisions should set a relatively small number of factors against which supervisors must measure employees' performance, and they should ensure that all employees are rated against similar factors while allowing for differences among the knowledge, skills, and abilities required for specific jobs.</p>	<p>Fully Implemented</p>	<p>The Agency completed revisions to its performance evaluation system in March 2007. The system evaluates employees on 13 similar factors across the Agency. The Agency has begun to evaluate employees under its new system, but it will not complete roll-out of the system until August 2008.</p>
<p>10 The Agency should require all supervisors to attend periodic training regarding the preparation of employee evaluations.</p>	<p>Fully Implemented</p>	<p>The Agency developed training for supervisors on its new performance evaluation system and provided this training in fiscal year 2007.</p>
<p>11 The Agency should establish a more positive work environment by surveying employees at least every two years on specific issues or topics to determine if changes made by management are having the desired effect, and to identify new issues that may negatively affect the workplace. The ombudsman would be responsible for facilitating ad hoc discussions with Agency employees to give them opportunities to provide the Commission and management with input on organizational and policy changes.</p>	<p>Fully Implemented</p>	<p>The Agency participated in the Survey of Organizational Excellence in January 2007 and performed some analysis of the results it received from the University of Texas at Austin. However, it has not performed additional analysis of areas of concern identified in that survey or developed strategies to address workforce issues identified in that survey.</p>



Status of Implementation of High-risk Audit Recommendations for Workforce Management			
Recommendation	Implementation Status	Auditor Comments	
12	The Agency should establish a more positive work environment by continuing existing employee work groups charged with examining policies and procedures related to the performance evaluation process, merit increases, and programs for recognizing and rewarding employees.	Fully Implemented	The Agency no longer has active workgroups for the topics identified in the previous audit report because these workgroups have concluded their work.
13	The Agency should work with the Appointments Division of the Office of the Governor to ensure a third Commissioner is appointed to fill the current vacancy.	Fully Implemented	Governor Rick Perry appointed Mr. David J. Schenck as the third Commissioner on the Texas Lottery Commission on October 17, 2007.

## Recommendations

The Agency should:

- Establish timeframes for resolving grievances and appeals to ensure that it addresses all employee performance and disciplinary issues appropriately and in a timely manner.
- Clarify its procedures for employee counseling and disciplinary actions to provide additional guidance to supervisors regarding which types of counseling, including verbal counseling, require documentation.
- Specify the course topics that supervisors are required to complete as part of their supervisory training.
- Complete the implementation of its revised employee performance evaluation system.
- Continue to identify workforce issues and concerns, and address these issues and concerns through the use of employee workgroups when appropriate.

## Management's Response

*Management agrees with the recommendations and will take the following actions.*

1. *Timeframes will be added into the employee complaint procedures that outline the process guidelines for grievances and appeals made by employees. These procedures will be modified and implemented by May 1, 2008.*

2. *Additional guidance will be provided to supervisors regarding which types of counseling, including verbal counseling, require documentation. Human Resources will provide guidance to supervisors through clarification of procedures, supervisor/Human Resources interactions, ad hoc training for employee relations matters and through various types of scheduled training. As a proactive approach to employee relations matters, Human Resources will continue to have the goal of encouraging supervisors to bring employee performance matters and workforce issues to Human Resources for guidance, input and possible resolutions. These procedures will be modified and implemented by May 1, 2008.*

3. *Course topics that supervisors are required to complete will be specified. The training database will be adjusted to include mandatory course topics that are specific to supervisors within the agency. The changes to the training database will be completed by May 1, 2008.*

4. *Implementation of the new employee performance evaluation system will continue. Human Resources currently provides training, assists supervisors and staff in the completion of the new form, and addresses other related matters associated with the new evaluation system. This process is ongoing and, as annual evaluations come due for employees, all employees will be evaluated under the new criteria and format.*

5. *Human Resources, the Ombuds, and agency management will continue to identify workforce issues and concerns, and address these issues and concerns through the use of employee workgroups when appropriate. The Ombuds began a practice in August 2006 of reporting trend data about areas of concern to the Executive Director on a weekly basis and to the Commission as needed.*

Chapter 1-A

## **The Agency Should Continue to Strengthen Its Employee Complaint Processes**

Although the Agency has made progress in implementing a recommendation to establish a grievance policy, its implementation of this recommendation remains incomplete and ongoing (see recommendation 1 in Table 1 above). The Agency's Human Resources Department handles formal employee complaints through two processes: a general complaint process and a grievance process. Employees also can bring informal complaints to the Agency's ombudsman, to a manager or division director (supervisor), or to the

internal auditor through EthicsPoint (the Agency's automated system for anonymous complaints or fraud allegations).

The Agency has developed and adopted formal procedures only for the formal complaints filed with its Human Resources Department. These procedures appropriately address the initiation, documentation, investigation, resolution, and communication phases of the complaint process. However, the Agency does not have a defined process for handling informal complaints made to the ombudsman, managers or division directors (supervisors), or the internal auditor. Without a defined process for addressing complaints filed through all methods, the Agency cannot ensure that it appropriately considers and resolves all complaints from employees.

Not all complaints brought to supervisors may warrant initiating a formal complaint investigation. Management should provide guidance to supervisors on how to determine the seriousness of a complaint and what actions, including potential referral to Human Resources, are required. By providing guidance to supervisors, the Agency will (1) assist supervisors in identifying issues that require follow-up beyond the informal complaint process and (2) ensure that employees understand the process through which Agency management will respond to their complaints. However, for complaints made to the Agency's ombudsman or internal auditor, or for complaints that require additional follow-up beyond informal management resolution, a more defined process is needed to ensure appropriate initiation, documentation, investigation, resolution, and communication of these complaints.

The Agency also does not communicate the final resolution of formal and informal complaints to all parties involved, including the employees who initiated the complaints. For 9 of 12 (75 percent) formal and informal complaints auditors reviewed, the Agency did not communicate the specific and final resolution of the complaint to the employee. While the Agency communicated some status information to the employee in most circumstances, this status information was not final or sufficiently detailed. For example, in three cases, the Agency notified the employees only that their complaints had been investigated and were being closed.

In some situations, the Agency may not be able to provide information on the specific resolution of a complaint to an employee. This can occur when the communication would violate another employee's confidentiality or create a legal liability. However, in those situations, the Agency should communicate a general resolution to the employee and explain why a more specific resolution cannot be communicated.

The Agency also has a process by which an employee can appeal the resolution of a formal complaint directly to the executive director. However, this process does not include a timeline for investigation and response by the executive director. Auditors reviewed one instance in which resolution of an

employee's appeal was not reached prior to the employee leaving the Agency. Establishing a timeline for the appeals process would help to ensure that a resolution is reached and communicated to the employee in a timely manner.

## Recommendations

The Agency should:

- Develop guidelines for informal complaints made to the Agency's ombudsman, internal auditors, or supervisors. The Agency's processes for addressing informal complaints should assist supervisors in identifying issues that require follow-up beyond the informal complaint process. Additionally, for complaints made to the Agency's ombudsman or internal auditor, or for complaints that require additional follow-up beyond informal management resolution, these guidelines should provide a defined process to ensure appropriate initiation, investigation, documentation, resolution, and communication of the final resolution of all complaints to all parties involved, as well as timeframes for each of these stages.
- Communicate specific information regarding the resolution of complaints to all parties involved. For situations in which communicating specific information may be a violation of state or federal law, the Agency should communicate to all parties involved its reasons for not providing specific information regarding the resolution.
- Establish a timeline for the resolution of appeals made to the executive director. The Agency's process should include timelines for the investigation, resolution, and communication of the final resolution of appeals to all parties involved.

## Management's Response

*Management agrees with the recommendations and will take the following actions.*

*1. Guidelines for informal complaints made to the Ombuds, internal auditor or supervisors will be developed. Human Resources will assist supervisors through both the formal and informal complaint processes by providing clear guidance on the steps associated with the initiation, documentation, resolution and communication of the resolution. The need to further investigate each individual complaint will occur as deemed necessary and in coordination with Human Resources. Formal supervisory training sessions as well as ad hoc training sessions will be conducted. Key information is currently provided in the Employee General Complaint Procedure. Human Resources will revise*

*this procedure to address guidance in the handling of informal complaints. Human Resources will continue to encourage supervisors to seek advice and assistance from Human Resources in resolving informal complaint matters before these matters escalate to formal complaints. These procedures will be modified and implemented by May 1, 2008.*

*2. Specific information regarding the resolution of complaints will be communicated to all parties involved. The complaint procedure will be revised to reflect this change. For situations in which communicating specific information may be a violation of state or federal law, the agency will communicate its reasons for not providing specific information regarding the resolution to all parties involved. Discretion on the information provided will be used in determining the detail of the information. These procedures will be modified and implemented by May 1, 2008. The policies and procedures for the Ombuds will include policies on the authority and limitations of communicating informal resolutions, in which the Ombuds was consulted, to parties in conflict when permissible by law and appropriate for the resolution of the case. The policies will also clarify the Ombuds role in communicating with parties about the formal complaint processes. The Ombuds policies and procedures will be implemented by May 1, 2008.*

*3. Timelines will be established for the making of appeals to the executive director after the agency's determination of the merits of the complaint and for the resolution of appeals made to the executive director. Currently the personnel handbook does not provide a timeline for employees to make appeals to the Executive Director after their complaints have been investigated and a determination has been made on the merits of their complaints, which could result in a delay in the overall resolution of the employee's complaint by the Executive Director. Changes will be made in the procedure that require timely filing of appeals to the Executive Director. The procedure will be revised to reflect these changes. Language will also be included in the procedure that addresses communicating the final resolution of the appeal process to all parties involved. These procedures will be modified and implemented by May 1, 2008.*

Chapter 1-B

### **The Agency Should Further Develop Its Ombudsman Position to Address Certain Weaknesses**

Although the Agency has made progress in implementing a recommendation to create an ombudsman position, its implementation of this recommendation remains incomplete and ongoing (see recommendation 2 in Table 1 above). The Agency appointed an internal employee to serve part-time as its first ombudsman in August 2006, and it hired a part-time employee to serve in that capacity in August 2007. From August 2006 through November 2007,

employees brought 19 complaints or concerns to the ombudsman's attention. While some of the complaints involved Agency-wide concerns, others involved minor issues such as parking complaints. Survey results indicate that trust in the Agency's Human Resources Division has increased, which may indicate that complaints brought to the ombudsman may be appropriately addressed by an ombudsman function within this division in the future.

The Agency developed a draft charter for the ombudsman function in May 2007. However, it has not formally adopted this charter. The Agency also lacks formal policies and procedures to define the role and responsibilities of the ombudsman. Specifically, these policies and procedures should clarify the ombudsman's reporting relationship to the executive director and the Commission and establish or reference to a standardized process by which the ombudsman handles complaints or concerns that employees express.

Additionally, the Agency's ombudsman does not have a formal role in the employee complaint process. The Agency's draft charter states that "the ombudsman will provide informal dispute resolution services" and will "include facilitating a confidential and neutral process for resolving employee-related concerns..." However, the ombudsman could help to ensure that Agency complaint processes function appropriately with a defined role in those processes.

Finally, the ombudsman has not facilitated discussion groups of Agency employees. Employees continue to have organizational concerns (see Chapter 1-C for additional details), and these concerns could be identified and addressed through discussion sessions with the ombudsman.

## Recommendations

The Agency should:

- Finalize its policies and procedures for the ombudsman position and obtain approval of those policies and procedures from executive management and the Commission.
- Evaluate how the ombudsman position can best address the concerns of employees and, if necessary, revise the ombudsman's duties so that the ombudsman has a formal role in ensuring the success of the employee complaint process.
- Ensure that its ombudsman facilitates informal discussion groups with Agency employees to identify and address organizational and employee concerns.

## Management's Response

*Management agrees with the recommendations and will take the following actions.*

- 1. A policy document and related procedures for the Ombuds will be developed that outlines the principles of confidentiality, neutrality, independence, and informality. The policy and procedures will be made available to all employees. The policy document will include authorizations and limitations of the Ombuds as an alternative to the formal dispute resolution processes. These policies and procedures will be implemented by May 1, 2008.*
- 2. The Ombuds position will be evaluated to determine how the position can best address concerns of employees and, if necessary and appropriate, the duties of the Ombuds will be revised so that the Ombuds has a formal role in ensuring the success of the employee complaint process. This evaluation will take into consideration the traditional roles of confidentiality and neutrality for the Ombuds. An Ombuds Charter will be produced which explains the Ombud's role, principles of the Ombud's office, and the authority and limitations of the Ombuds.*
- 3. Beginning in January 2008, the Ombuds initiated informal discussion groups with agency employees in which employees were invited to meet and greet the Ombuds. Future meetings will be scheduled and designated to address specific concerns from the employee surveys and meeting times will be advertised and provided to staff to allow employees to discuss their views and identify additional workforce development issues.*

## Survey Results Indicate Agency Employees Believe the Culture Has Improved, But Fear of Retaliation Is Still a Concern

Results of an Agency-wide survey the State Auditor's Office conducted in 2007 indicate that Agency staff believe some key aspects of employee relations have improved significantly since the State Auditor's Office conducted a similar survey in February 2006. However, responses and

### 2007 State Auditor's Office Survey of Agency Employees

Auditors conducted an Agency-wide survey of 307 employees at the request of the Chairman of the Commission to determine how employee perceptions of issues and concerns in the workplace had changed since the State Auditor's Office's 2006 survey. A total of 176 (57 percent) employees responded to the 2007 survey. For detailed survey response information, see Appendix 2.

The survey asked employees to rate their level of agreement or disagreement with 33 survey statements regarding communication, job duties and performance, trust and respect, the Agency's ombudsman, and the Agency's overall culture.

Employees also had an opportunity to share comments regarding the Agency. A total of 82 employees (47 percent of respondents) provided comments regarding the work environment and other topics.

### State Auditor's Office Survey Analysis Methodology

Auditors used professional judgment to determine whether changes in employee perceptions for each survey question were significant.

To make these judgments, auditors performed statistical analysis of each survey statement to determine whether the change in responses from 2006 to 2007 was most likely attributable to chance or was an indicator of a significant change in employee perception.

Using this statistical analysis, auditors determined that a change of at least 12 percent from 2006 to 2007 indicated a significant change, while a change of 7 percent or less indicated the change could be attributed to chance.

Auditors also identified key survey questions by selecting questions from the employee survey that were overall indicators of the Agency's work environment and culture (see Figure 1 on the next page).

employee comments also indicate that employees continue to have concerns about key aspects of the work environment, including a fear of retaliation, involvement by employees in the decision-making process, and other general management practice concerns. For detailed survey results, see Appendix 2.

It is important to note that the State Auditor's Office conducted the 2007 survey approximately 20 months after conducting the 2006 survey. Changing employee perceptions of critical issues may take years. Employee attitudes reflected by answers to some survey items may not have changed significantly in the 20 months between the 2006 and 2007 surveys. In addition, many topics covered by those surveys, including perceptions of trust and Agency culture, are difficult to quantify.

Survey responses indicate that some key aspects of employee relations practices have improved.

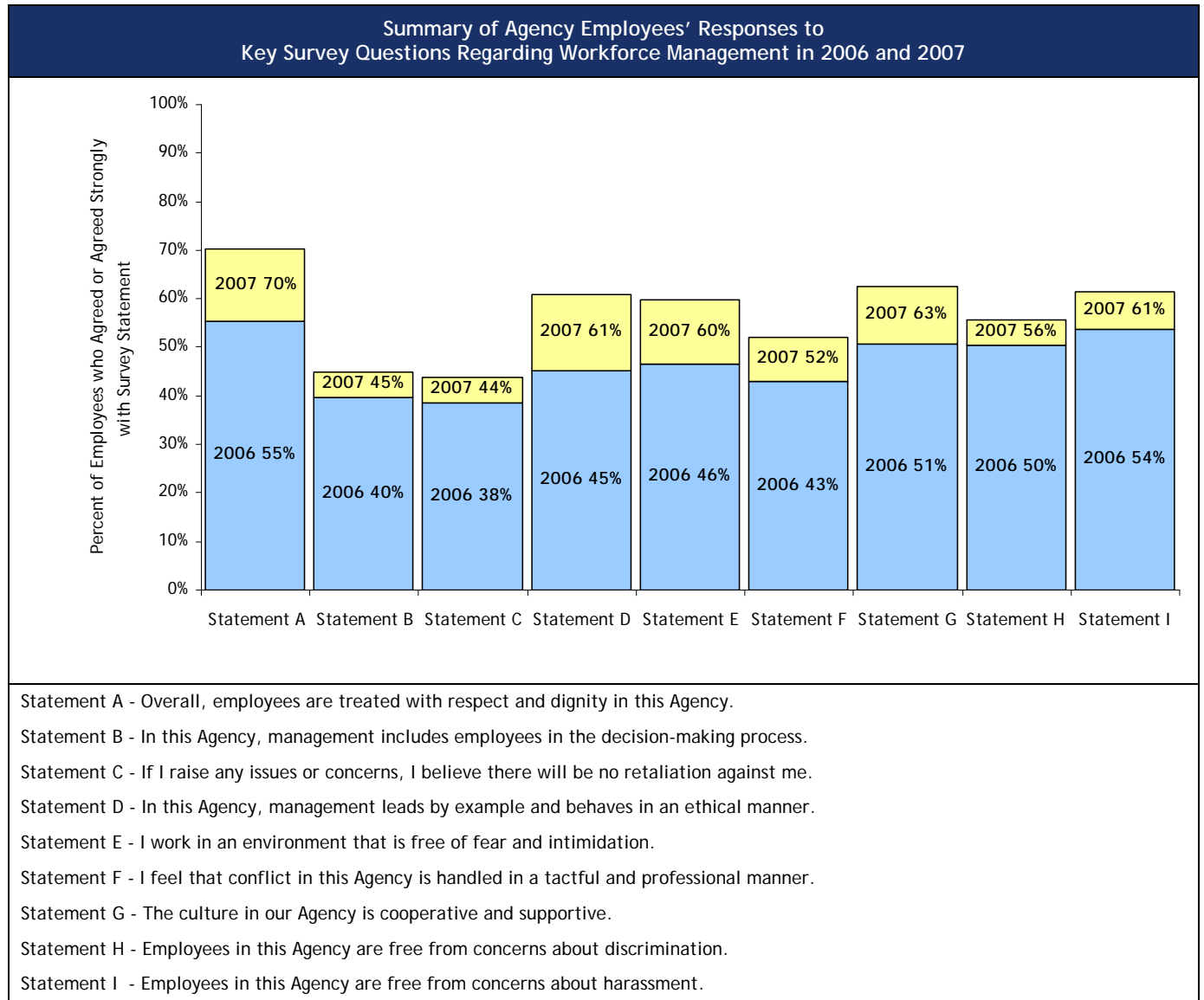
The percentage of employees who agreed that they were treated with respect and dignity increased significantly from 2006 to 2007. In 2007, 70 percent of employees agreed that they were treated with respect and dignity, compared with 55 percent in 2006.

Additionally, significantly more employees believe that the culture within the Agency is cooperative and supportive. In 2007, 63 percent of employees agreed with this statement, which was an increase of 12 percent from 2006.

Survey comments also indicated that improvements have been made within the Agency since the 2006 survey. For example, some staff-level employees praised the appointment of the Agency's new executive director and the hiring of the new human resources director. Figure 1 on the next page summarizes responses to key survey questions.



Figure 1



Source: 2006 and 2007 State Auditor's Office surveys of Agency employees.

**Survey responses indicate that employees still have concerns regarding retaliation and involvement in the decision-making process.**

Responses also indicate that employees still have workplace concerns. In 2007, 44 percent of employees agreed that they will not be retaliated against if they raise issues or concerns. In the 2006 survey, 38 percent of employees agreed with that statement. These responses indicate that there may not have been a significant change in the perceptions and attitudes of employees in this area. Additionally, some Agency employees provided survey comments

indicating that they feared retaliation if they raised concerns with management or shared concerns with the State Auditor’s Office.

In 2007, 45 percent of employees agreed that management included them in the decision-making process. This represents an increase of 5 percent from 2006, when 40 percent of employees agreed with that statement.

Survey responses indicate that employee trust for one key Agency official has increased significantly.

In June 2006, the Agency hired a new director for its Human Resources Division. Responses to the 2007 survey indicate that employees believe that they can trust this division significantly more than 2006 survey responses indicated. In 2006, 40 percent of employees agreed that they trusted the Human Resources Division. In 2007, this agreement had risen to 66 percent, representing the highest increase (26 percent) of all survey items. Additionally, four employees shared specific survey comments indicating that the new Human Resources Division director has effected positive changes in the Agency’s work environment.

Survey comments indicate that employees recognize improvements have been made at the Agency, but they also identified new and recurring areas of concern.

Comments made by 82 survey respondents (47 percent of all respondents) indicate that:

- A significant number of employees have concerns regarding management practices within the Agency and a lack of disciplinary action against employees when warranted.
- A significant number of employees praised the positive work environment and improvements the Agency has made in recent years.

Auditors classified the comments that survey respondents made into categories by issue area. Categories in which at least 15 percent of respondents provided comments are summarized in Table 2.

Table 2

Summary of Major Themes Identified in Employee Comments		
Issue Area	Number of Respondents Who Commented	Percent of Respondents Who Commented
Staff has concerns about management practices in the workplace.	40	48.8%
Staff and management have concerns regarding a lack of employee disciplinary action when warranted.	20	24.4%
Staff believe that the Agency has a positive work environment and that improvements have been made.	13	15.9%

## Recommendations

The Agency should:

- Perform critical analysis of State Auditor's Office survey results and results from the Survey of Organizational Excellence to identify underlying causes of workforce concerns.
- Develop and implement tools to address concerns identified by employees in recent surveys.

## Management's Response

*Management agrees with the recommendations and has taken and will take the following actions.*

- 1. Critical analysis of the State Auditor's Office survey results and results from the Survey of Organizational Excellence to identify underlying causes of workforce concerns is ongoing. Human Resources works closely with the Ombuds, supervisors and staff in assessing survey results and identifying and possibly resolving underlying causes of identified workforce concerns. Additionally, the Ombuds discusses issues with employees on an ad hoc basis and in informal discussions that can, when appropriate, include supervisors.*
- 2. Tools will be developed to address concerns identified by employees in recent surveys. The development of such tools will include a continued effort by Human Resources to develop working relationships with supervisory staff in identifying and possibly resolving concerns identified in recent surveys. Human Resources will work closely with the Ombuds and supervisors in developing and implementing such tools. The development of these tools will be ongoing.*

## ***The Agency Has Fully or Substantially Implemented the Majority of High-risk Audit Recommendations Regarding Procurement, But It Should Strengthen Certain Contract Management Processes***

The Agency has made progress in implementing high-risk recommendations to address deficiencies identified in *An Audit Report on Procurement at the Texas Lottery Commission* (State Auditor’s Office Report No. 06-062, August 2006). Of the 12 recommendations auditors reviewed, 7 were fully implemented and 3 were substantially implemented. Table 3 summarizes the implementation status of each of the recommendations auditors reviewed. For the Agency’s self-reported status of recommendations not selected for follow-up audit work, see Appendix 3.

However, the Agency should continue to make certain improvements in contract management:

- The Agency should further develop contract negotiation policies and procedures to ensure that its staff has sufficient guidance in contract negotiations.

### **Definitions of Implementation Status**

- **Fully Implemented:** Successful development and use of a process, system, or policy to implement a prior recommendation.
- **Substantially Implemented:** Successful development but inconsistent use of a process, system, or policy to implement a prior recommendation.
- **Incomplete/Ongoing:** Ongoing development of a process, system, or policy to address a prior recommendation.
- **Not Implemented:** Lack of a formal process, system, or policy to address a prior recommendation.

- The Agency should strengthen processes for monitoring the primary lottery operator’s compliance with the terms of its approximately \$750 million state contract. A third-party reviewer is responsible for monitoring the primary lottery operator, but the third-party reviewer contracts with the primary lottery operator, rather than directly with the Agency.
- The Agency should develop a formal decision-making process for determining situations where it should or should not assess sanctions or liquidated damages against the primary lottery operator.

Table 3

<b>Status of Implementation of High-risk Audit Recommendations for Procurement Activities</b>		
<b>Recommendation</b>	<b>Implementation Status</b>	<b>Auditor Comments</b>
1 The Agency should consistently perform and document needs and risk assessments for all future contracts, regardless of whether a cost-benefit analysis is performed in conjunction with needs and risk assessment.	Fully Implemented	The Agency has implemented policies and procedures that require the completion of a needs and risk assessment prior to the development of a contract solicitation for a good or service.
2 The Agency should use its needs and risk assessment to develop a clear and thorough statement of work to include in each contract.	Fully Implemented	According to Agency staff, several information resources, including the needs and risk assessment, are used to develop the statement of work.

Status of Implementation of High-risk Audit Recommendations for Procurement Activities			
Recommendation	Implementation Status	Auditor Comments	
3	For future contracts, the Agency should assess and document the reasons that it receives fewer than three bids. The Agency should analyze this information to determine whether its contracting process should be modified.	Fully Implemented	The Agency implemented policies and procedures to contact vendors that did not submit bids, after a contract has been awarded, to determine the reasons they chose not to bid.
4	The Agency should determine and document the minimum acceptable qualifications for future contract solicitations based on objective criteria that it can subsequently use during contract monitoring, renewal, and re-bidding.	Fully Implemented	The Agency defines the minimum acceptable qualifications for future contract solicitations within both its requests for proposals and its invitations for bids for a good or service.
5	The Agency should develop written policies and procedures for negotiation with contractors to ensure that it identifies the contract terms and conditions that are essential to its needs, and focus its negotiation efforts on these terms and conditions for future contracts.	Substantially Implemented	The Agency has developed written policies and procedures for negotiating contracts. However, the procedures do not provide sufficient guidance to Agency staff on the specific actions to take during negotiations. See Chapter 2-A of this report for additional details.
6	The Agency should ensure that its contract solicitations and resulting contracts always include a clearly communicated statement of work that defines the goods and services the contractor will provide.	Fully Implemented	The Agency defines the statement of work for its contracts within the applicable request for proposal or the invitation for bid for contracted goods or services.
7	The Agency should develop and implement policies and procedures that address when it should enter into negotiations with contractors.	Not Implemented	The Agency has not developed criteria defining the circumstances under which its staff should or should not enter into contract negotiations. See Chapter 2-A of this report for additional details.
8	The Agency should ensure that the essential and desirable terms and conditions identified in the planning for each contract are included in the Agency's negotiations.	Substantially Implemented	The Agency has developed policies and procedures for conducting contract negotiations that include general steps that require staff to identify essential terms and conditions for contracted goods or services. However, these procedures lack details concerning the retention of specific documentation necessary to ensure the contract terms and conditions that were identified as essential were negotiated and performed consistently. See Chapter 2-A of this report for additional details.
9	The Agency should use the cost-benefit analysis developed in planning as a basis from which it can negotiate rates with its contractors.	Fully Implemented	The Agency has implemented policies and procedures to use a cost-benefit analysis as one of several data resources in negotiating contract rates. Auditors determined that, although the Agency did not use the cost-benefit analyses in negotiating the contract rates for the contracts that were tested, the Agency maintained appropriate documentation of its alternative resources (research and analyses) for its negotiated contract rates

Status of Implementation of High-risk Audit Recommendations for Procurement Activities			
Recommendation	Implementation Status	Auditor Comments	
10	The Agency should strengthen its monitoring efforts for the primary lottery operator contract to ensure compliance with contract terms.	Incomplete/Ongoing	The Agency has made several changes in its approach to monitoring its contract with the primary lottery operator. However, the Agency should make additional changes to ensure that the primary lottery operator complies with contract terms.  See Chapter 2-B of this report for additional details.
11	The Agency should ensure that it (1) assesses and collects all sanctions and liquidated damages in a timely manner and (2) that it clearly references sanctions and liquidated damages back to the contract when it makes deductions from contractor payments.	Substantially Implemented	The Agency has implemented policies and procedures to ensure it both (1) assesses and collects all sanctions and liquidated damages and (2) clearly references sanctions and liquidated damages back to the contract.  However, auditors identified weaknesses in (1) how the Agency reports non-performance issues that are subject to sanctions and liquidated damages and (2) how the Agency makes the decision to assess sanctions and liquidated damages.  See Chapter 2-C of this report for additional details.
12	The Agency should pay contractors in accordance with the existing terms of its contracts or amend the contracts based on agreements with the contractor.	Fully Implemented	Auditors tested the Agency's payments to the primary lottery operator and determined that payments were calculated in accordance with the terms of the contract and recent amendments.

Chapter 2-A

### The Agency Should Further Develop Its Policies and Procedures to Provide Additional Guidance on Managing Contract Negotiations

The Agency has developed policies and procedures for negotiating contract terms and conditions. However, weaknesses in the Agency's procedures increase the risk that the most favorable terms and conditions may not be obtained. Auditors reviewed the procurement records for five of nine contracts solicited and awarded in fiscal year 2007. Of the five contracts reviewed, three were awarded through the request for proposal process.<sup>1</sup> Auditors identified the following concerns regarding these three contracts:

- The Agency did not implement a recommendation to identify the circumstances under which it should or should not negotiate contract terms and conditions (see recommendation 7 in Table 3 above). Auditors identified that, for one of the three contracts tested, the Agency did not enter into contract negotiations for a contract for audit services with an

<sup>1</sup> Six contracts were awarded using the invitation to bid process. Three contracts were awarded using the request for proposal process. The *State of Texas Contract Management Guide* states that negotiations are not necessary for procurements awarded through the invitation to bid process because the requirements are clearly defined and price is the major determining factor for selection. However, negotiations are allowed under the request for proposal process.

estimated cost of \$78,000. The procurement files lacked documentation that clearly described the reasons contract negotiations were waived, although the Agency reported it accepted the contractor's proposal terms and further negotiations were not necessary.

- The Agency has substantially implemented a recommendation to develop policies and procedures for negotiations with contractors (see recommendation 5 in Table 3 above). To fully implement the recommendation, the procedures should provide detailed guidance to negotiating staff on specific actions to take during negotiations. The procedures list techniques that can be used in this process, but they do not include guidance on how to apply the techniques. Without this guidance, Agency staff may not implement these techniques properly.
- The Agency has substantially implemented a recommendation to ensure that the essential and desirable terms and conditions identified in the planning for each contract are included in the Agency's negotiations by creating policies and procedures that require staff to identify these terms and conditions during negotiations (see recommendation 8 in Table 3 above). However, these policies and procedures lack guidance regarding the specific documentation that should be retained during negotiations to ensure the essential contract terms and conditions were negotiated appropriately. As a result, there were inconsistencies in the types of documentation the Agency did retain from contract negotiations.

## Recommendations

The Agency should revise its policies and procedures for contract negotiations to include the following:

- Criteria defining the circumstances under which the Agency should or should not enter into contract negotiations with a vendor.
- Guidance on specific actions to take during negotiations to ensure that techniques are implemented properly.
- Guidance on specific documentation that should be retained in contract files regarding the negotiation of each contract.

## Management's Response

*Management agrees with the recommendations and will take the following actions.*

- 1. The Contract Negotiations procedure will be revised to define the circumstances under which the Agency should or should not enter into contract negotiations with a vendor. This procedure will be implemented by March 1, 2008.*
- 2. The Contract Negotiations procedure will be revised to reference the Negotiation Techniques section of the State of Texas Contract Management Guide to provide guidance on actions taken during contract negotiations. This procedure will be implemented by March 1, 2008.*
- 3. The Contract Negotiations procedure will be revised to include a checklist and/or template that identifies the specific documentation required for all contract negotiations. This procedure will be implemented by March 1, 2008.*

Chapter 2-B

### The Agency Should Fully Implement Recommendations to Strengthen Its Monitoring of the Primary Lottery Operator

Although the Agency has made progress in implementing a recommendation to monitor the primary lottery operator's contract compliance, its implementation of this recommendation remains incomplete and ongoing (see recommendation 10 in Table 3 above). Weaknesses in its contract monitoring process continue to hinder the Agency's ability to appropriately identify, report, and address its contractor's unsatisfactory performance and contract non-compliance.

#### Third-party Reviewer

On a quarterly basis, a third-party reviews the primary lottery operator's compliance with the terms of its approximately \$750 million Agency contract.

Amendment seven to the contract between the Agency and the primary lottery operator states that the primary lottery operator will provide the Agency with quarterly contract compliance reports to be performed by an independent [third party reviewer] that is selected and paid by the primary lottery operator, with approval by the Agency.

The third-party reviewer may appear to lack adequate independence from the primary lottery operator to perform objective contract compliance reviews.

A third-party reviewer contracts with the primary lottery operator, rather than directly with the Agency, to monitor the primary lottery operator's contract compliance (see text box for additional details). Therefore, the third-party reviewer may appear to lack independence from the primary lottery operator. This may impair the third-party reviewer's ability to ensure it conducts its reviews in the best interests of the Agency. Additionally, while the Agency has authority to approve the third-party monitor through its contract with the primary lottery operator, it lacked documentation indicating that it approved



the third-party reviewer that the primary lottery operator selected.

In addition, the Agency relies on the third-party reviewer to verify the accuracy and completeness of self-reported information provided by the primary lottery operator. It is reasonable for the Agency to rely on an independent third-party reviewer to verify this information, but the third-party reviewer should contract with and report directly to the Agency to ensure that it is independent.

**The Agency lacks formal, objective policies and procedures for identifying and reporting unsatisfactory performance on the part of the primary lottery operator.**

Auditors reviewed the Agency's monitoring activities for 30 contract requirements that subject the primary lottery operator to potential sanctions and liquidated damages. The Agency lacks formal policies and procedures for the following:

- The Agency did not define and document a process for monitoring and reporting contract compliance for 16 of 30 (53 percent) contract requirements reviewed. Examples of these 16 requirements include requirements regarding the timely installation of instant ticket machines; the timely handling of all retailer hotline calls; and the timely receipt of deliverables, such as quarterly accounting reports, annual compliance reports, and annual inventory reports. Without a defined process, the Agency cannot ensure that unsatisfactory performance is consistently identified and reported to contract administration staff in an appropriate and timely manner. This limits the Agency's ability to take corrective action or assess sanctions and liquidated damages in a timely manner.
- The Agency has 13 contract requirements that rely on self-reported data from the primary lottery operator. Although the Agency verifies the self-reported data for nine of these contract requirements, it does not verify the accuracy of self-reported data for one contract requirement and it relies on the third-party reviewer to verify the accuracy of the primary lottery operator's self-reported data for the remaining three contract requirements. As discussed above, issues regarding the third-party reviewer's independence from the primary lottery operator could impair the third-party reviewer's objectivity in verifying this information.

The Agency has established a policy to hold quarterly contract compliance meetings of Agency staff who monitor the primary lottery operator concerning the operator's performance. However, the Agency held only one contract compliance meeting during fiscal year 2007. Without these meetings, staff with oversight responsibilities for the primary lottery operator do not have the opportunity to discuss and address performance and related issues.

## Recommendations

The Agency should:

- Contract directly with a third-party reviewer to monitor its primary lottery operator's compliance with contract terms and requirements. The Agency may choose to continue to rely on the third-party reviewer's reports until the current contract is expired, but the Agency should take additional steps to verify the accuracy and completeness of these reports. The Agency may also consider contracting directly with the current third-party reviewer until such time as it can conduct a competitive procurement process to avoid an interruption in service.
- Develop, document, and implement policies and procedures for all activities designed to monitor the primary lottery operator.
- Ensure that all data self-reported by the primary lottery operator is verified by entities that are independent of the primary lottery operator.
- Establish criteria for the circumstances under which a contract compliance meeting can be waived. In addition, it should ensure that it holds contract compliance meetings as frequently as required by Agency policy.

## Management's Response

*Management agrees with the recommendations and will take the following actions.*

- 1. The procurement process to contract directly with a third-party reviewer of its primary lottery operator will be immediately initiated. Included among the responsibilities of the contracted vendor will be the verification of all data self-reported by the lottery operator.*
- 2. Procedures related to contract monitoring activities for the lottery operator will be reviewed, updated and/or developed. These procedures will be implemented by March 1, 2008.*

3. *The agency will update the Contract Maintenance-Contract Compliance Meetings procedure to establish criteria for the circumstances under which a meeting can be waived. This procedure will be implemented by March 1, 2008.*

Chapter 2-C

### **The Agency Should Fully Implement Recommendations to Strengthen Its Process for Assessing Sanctions and Liquidated Damages**

The Agency has substantially implemented a recommendation concerning the assessment of sanctions and liquidated damages against contractors (see recommendation 11 in Table 3 above). Specifically, it has developed policies and procedures for reporting non-compliance and unsatisfactory compliance to the support services manager, and it has adequately referenced sanctions assessed against the primary lottery operator. To fully implement the recommendation, it should define formal criteria and a process for determining the circumstances under which sanctions or liquidated damages should be assessed after they are reported to the contract administration division. The Agency relies on its support services manager to assess sanctions or liquidated damages for unsatisfactory performance or contract non-compliance. However, this manager does not have a defined process for determining when a sanction should or should not be assessed. This increases the risk that the Agency will not assess sanctions for contractor non-performance.

#### **Recommendation**

The Agency should develop, document, and implement policies and procedures for the formal decision-making process used to determine whether to assess sanctions or liquidated damages against the primary lottery operator.

#### **Management's Response**

*Management agrees with the recommendations and will take the following action.*

*The agency will update all procedures to include the process for determining when to assess sanctions or liquidated damages. These procedures will be implemented by March 15, 2008.*

## ***The Agency Has Fully Implemented the Majority of High-risk Recommendations for Lotto Texas Activities***

The Agency has made significant progress in implementing recommendations to address weaknesses identified in *An Audit Report on Lotto Texas Activities at the Texas Lottery Commission* (State Auditor’s Office Report No. 06-046, July 2006). The Agency has fully implemented eight of the nine (89 percent) recommendations auditors reviewed. Table 4 summarizes the implementation

status of each of the recommendations auditors reviewed. For the Agency’s self-reported status of recommendations not selected for follow-up audit work, see Appendix 3.

The Agency has not implemented a prior audit recommendation that it publish proposed policies and procedures that affect Lotto Texas players on its Web site and in the *Texas Register*. While the Agency publishes these policies and procedures after final approval by the Commission, it does not provide an opportunity for public comment on proposed policies and procedures prior to approval by the Commission.

### Definitions of Implementation Status

- **Fully Implemented:** Successful development and use of a process, system, or policy to implement a prior recommendation.
- **Substantially Implemented:** Successful development but inconsistent use of a process, system, or policy to implement a prior recommendation.
- **Incomplete/Ongoing:** Ongoing development of a process, system, or policy to address a prior recommendation.
- **Not Implemented:** Lack of a formal process, system, or policy to address a prior recommendation.

Table 4

Status of Implementation of High-risk Audit Recommendations for Lotto Texas Activities		
Recommendation	Implementation Status	Auditor Comments
1 The Agency should provide all final and approved jackpot estimation worksheets to the Legislative Budget Board and the Governor’s Office.	Fully Implemented	The Agency provides the approved jackpot estimation worksheets to the Legislative Budget Board and Governor’s Office for each drawing. The Agency also provided training to the personnel who receive and review these reports to familiarize them with the jackpot estimation process.
2 The Agency should continue to publish all jackpot estimation worksheets on its Web site.	Fully Implemented	The Agency posts all jackpot estimation worksheets on its Web site.
3 The Agency should update policies and procedures to reflect its current practices.	Fully Implemented	The Agency has updated its policies and procedures for Lotto Texas jackpot estimation to reflect the current estimation practices.

**Status of Implementation of High-risk Audit Recommendations for Lotto Texas Activities**

Recommendation	Implementation Status	Auditor Comments
<p>4 The Agency should ensure that all required approvals are obtained and documented on jackpot estimation worksheets and, within policies and procedures, assign responsibility for approving estimates to individual(s) in specific position(s). Individuals who approve estimates should have sufficient knowledge of the jackpot estimation process to be able to make an informed and responsible decision. The Agency should obtain a written and signed approval from the Executive Director for any exceptions to policies and procedures.</p>	<p>Fully Implemented</p>	<p>Current Agency policies and procedures assign responsibility for approving Lotto Texas jackpot estimates to individuals in positions who have knowledge of the jackpot estimation process. Specifically, the controller, products manager, lottery operations director, deputy executive director, and executive director approve jackpot estimation worksheets. Auditors tested 30 jackpot estimation worksheets completed during fiscal year 2007 and determined that all of them contained the required approvals. Additionally, the Agency has a documented procedure for delegating jackpot estimation approvals when the individuals in the assigned positions are not available to approve the estimations. In fiscal year 2007, there were no exceptions to the Agency's policies and procedures for jackpot estimation that required approval by the executive director.</p>
<p>5 The Agency should document the effective date of all policies and procedures.</p>	<p>Fully Implemented</p>	<p>The Agency documented effective dates for all current Lotto Texas procedures. Additionally, Agency directives that describe the creation and approval of new policies and procedures specify that all policies and procedures must include the effective date. The Agency's policies and procedures coordinator reviews policies and procedures to ensure that they comply with this requirement.</p>
<p>6 The Agency should document which policies and procedures are being replaced or revised by new policies and procedures.</p>	<p>Fully Implemented</p>	<p>Current Lotto Texas procedures require the Agency to document which prior policies and procedures it is replacing. Agency directives require that all policies and procedures identify any previous policy that the new policy or procedure replaces. The Agency's policies and procedures coordinator reviews policies and procedures to ensure that they comply with this requirement.</p>
<p>7 The Agency should establish a formal, documented process to communicate revised or new policies and procedures and their effective dates to staff.</p>	<p>Fully Implemented</p>	<p>The Agency has established a formal, documented process for developing, approving, posting, and amending policies and procedures. This process includes direction on how to communicate new or revised policies and procedures to staff. Management of each Agency department is responsible for informing necessary staff of new or revised policies and procedures. Additionally, new and revised policies and procedures are posted on the Agency's intranet.</p>
<p>8 The Agency should publish proposed policies and procedures that affect Lotto Texas players in the <i>Texas Register</i> and on its Web site. It should then present these proposed policies and procedures to the Texas Lottery Commission at public Commission meetings and request that the Commission publicly approve the policies and procedures. After these policies and procedures are approved, the Agency should make them available to the public by publishing them in the <i>Texas Register</i> and on its Web site.</p>	<p>Not Implemented</p>	<p>Policies and procedures that affect Lotto Texas players are published in both the <i>Texas Register</i> and the Lotto Texas Web site. The Agency also presents these proposed policies and procedures to the Commission for public approval. However, the Agency posts these to the <i>Texas Register</i> and its Web site after they are approved at the Commission meeting. This process does not provide an opportunity for public comment on proposed policies and procedures prior to seeking the Commission's approval.</p>
<p>9 The Agency should comply with policies and procedures regarding the calculation and payment of Lotto Texas jackpot prizes and obtain written and signed approval from the Executive Director for any exceptions.</p>	<p>Fully Implemented</p>	<p>The Agency complies with policies and procedures in calculating and paying Lotto Texas jackpot prizes. Auditors tested all prize calculations and payments for jackpot winners in fiscal year 2007 and determined that the Agency calculated and paid the jackpot prizes in accordance with its policies and procedures.</p>

## Recommendations

The Legislature should consider requiring the Commission to post proposed policies and procedures that affect Lotto Texas players on the Agency's Web site and in the *Texas Register* for public comment prior to its approval of policies and procedures. (For proposed statutory language for this recommendation, see Appendix 4.)

The Commission should post proposed policies and procedures that affect Lotto Texas players on the Agency's Web site and in the *Texas Register* for public comment prior to its approval of policies and procedures.

## Management's Response

*Management agrees with the recommendations and will take the following actions.*

*The Commission will post proposed policies and procedures that affect Lotto Texas players on the Agency's Web site and in the Texas Register for public comment prior to its approval of policies and procedures. This practice will be implemented by May 1, 2008.*

# Appendices

Appendix 1

## *Objective, Scope, and Methodology*

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### Objective

The objective of this audit was to determine whether the Texas Lottery Commission (Agency) has made progress in implementing recommendations to correct deficiencies identified in the following reports:

- *An Audit Report on Procurement at the Texas Lottery Commission* (State Auditor's Office Report No. 06-062, August 2006).
- *An Audit Report on Workforce Management at the Texas Lottery Commission* (State Auditor's Office Report No. 06-047, July 2006).
- *An Audit Report on Lotto Texas Activities at the Texas Lottery Commission* (State Auditor's Office Report No. 06-046, July 2006).

### Scope

The scope of this audit included (1) reviewing the Agency's implementation of high-risk audit recommendations concerning workforce management, procurement, and Lotto Texas activities during the period from September 1, 2006, through August 31, 2007, and (2) conducting an Agency-wide employee survey.

### Methodology

The audit methodology consisted of identifying high-risk recommendations from three recent State Auditor's Office audits and collecting information to determine the implementation status of those recommendations. Identification of high-risk recommendations was based on the following:

- Inherent business, financial, and service risk.
- The Agency's preliminary management responses to each audit report, and its actions to implement prior recommendations.
- The Agency's February 2007 self-reported status of implementation for each prior recommendation.

This audit did not include a review of information technology.

Information collected and reviewed included the following:

- Agency policies and procedures related to workforce management, procurement, and Lotto Texas activities.
- Documentation of formal and informal employee complaints.
- 2006 and 2007 surveys of Agency employees conducted by the State Auditor's Office.
- 2007 Survey of Organizational Excellence conducted by the University of Texas at Austin.
- Agency organizational chart.
- Agency training database and tracking tools.
- Contract procurement files.
- Contract management files.
- Invoice payment files.
- Third-party reviewer quarterly reports.
- Lotto Texas jackpot estimation worksheets.
- Lotto Texas jackpot sales data.
- Lotto Texas prize calculation and jackpot payment data.
- Agency Commission meeting transcripts.

Procedures and tests conducted included the following:

- Interviewed Agency Commissioners, executives, division management, and staff.
- Reviewed the Agency's policies and documentation related to workforce management, procurement, and Lotto Texas activities.
- Reviewed and analyzed responses to the State Auditor's Office employee survey and the Survey of Organizational Excellence conducted by the University of Texas at Austin.
- Reviewed the Agency's training database and tracking tools.
- Performed limited testing and analysis of selected Agency contracts for compliance with policies and procedures.



- Tested jackpot estimation worksheets for compliance with policies and procedures.
- Recalculated jackpot prize payments for compliance with rules and policies and procedures

Criteria used included the following:

- Prior State Auditor's Office recommendations.
- Texas Administrative Code and Texas Government Code.
- Comptroller of Public Accounts' *State of Texas Contract Management Guide*, Version 1.4.
- Agency policies and procedures related to workforce management, procurement, and Lotto Texas activities.

### **Project Information**

Audit fieldwork was conducted from October 2007 through January 2008. 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 that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The following members of the State Auditor's staff performed the audit:

- Audrey O'Neill, CGAP (Project Manager)
- Willie J. Hicks, MBA (Assistant Project Manager)
- Joseph Mungai, CIA, CISA
- Robert Pagenkopf
- Sajil Scaria
- Leslie Ashton, CPA (Quality Control Reviewer)
- Sandra Vice, CIA, CGAP, CISA (Assistant State Auditor)

## Results of the State Auditor's Office 2006 and 2007 Survey of Agency Staff and Management

Table 5 shows the results of survey questions regarding workforce management that the State Auditor's Office asked Texas Lottery Commission (Agency) staff and management in 2006 and 2007. Table 6 shows the results of survey questions regarding contact with the Agency's ombudsman position that the State Auditor's Office asked Agency management and staff in 2007.

Table 5

Results of 2006 and 2007 Survey Questions Regarding Workforce Management			
	Strongly Agree or Agree	Neutral	Disagree or Strongly Disagree
<b>1. I receive adequate information about organizational decisions that affect my job.</b>			
Staff Responses 2007	73%	14%	13%
Staff Responses 2006	62%	18%	20%
Management Responses 2007	86%	0%	14%
Management Responses 2006	92%	4%	4%
<b>2. I receive adequate information about important new rules or policy changes or other developments.</b>			
Staff Responses 2007	75%	18%	8%
Staff Responses 2006	64%	16%	20%
Management Responses 2007	86%	5%	9%
Management Responses 2006	96%	0%	4%
<b>3. I receive adequate information about my job from my manager. (For Managers—I provide adequate communication to my employees regarding their job.)</b>			
Staff Responses 2007	73%	14%	12%
Staff Responses 2006	66%	18%	16%
Management Responses 2007	95%	0%	5%
Management Responses 2006	92%	4%	4%
<b>4. Major organizational changes are clearly communicated to me.</b>			
Staff Responses 2007	69%	13%	18%
Staff Responses 2006	58%	18%	24%
Management Responses 2007	86%	0%	14%
Management Responses 2006	88%	4%	8%
<b>5. The Agency provides me information about how I am being judged or evaluated in my job. (For Managers—I provide information to my employees about how they will be judged or evaluated in their jobs.)</b>			
Staff Responses 2007	82%	9%	8%
Staff Responses 2006	65%	15%	20%
Management Responses 2007	100%	0%	0%
Management Responses 2006	100%	0%	0%

Results of 2006 and 2007 Survey Questions Regarding Workforce Management			
	Strongly Agree or Agree	Neutral	Disagree or Strongly Disagree
<b>6. I understand how my job relates to the total operation of the Agency.</b>			
Staff Responses 2007	88%	6%	6%
Staff Responses 2006	86%	8%	6%
Management Responses 2007	91%	5%	5%
Management Responses 2006	96%	0%	4%
<b>7. I am allowed to take the training necessary to improve my work skills.</b>			
Staff Responses 2007	89%	4%	7%
Staff Responses 2006	83%	7%	10%
Management Responses 2007	100%	0%	0%
Management Responses 2006	100%	0%	0%
<b>8. Training and development is encouraged at all levels of the Agency.</b>			
Staff Responses 2007	75%	17%	8%
Staff Responses 2006	70%	19%	11%
Management Responses 2007	91%	9%	0%
Management Responses 2006	100%	0%	0%
<b>9. Overall, employees are treated with respect and dignity in this Agency.</b>			
Staff Responses 2007	70%	14%	16%
Staff Responses 2006	55%	20%	25%
Management Responses 2007	82%	5%	14%
Management Responses 2006	83%	13%	4%
<b>10. In this Agency, management includes employees in the decision-making process.</b>			
Staff Responses 2007	45%	32%	23%
Staff Responses 2006	40%	26%	35%
Management Responses 2007	64%	23%	14%
Management Responses 2006	63%	29%	8%
<b>11. I trust my immediate supervisor. (For Managers—My employees trust me.)</b>			
Staff Responses 2007	66%	14%	20%
Staff Responses 2006	69%	14%	17%
Management Responses 2007	100%	0%	0%
Management Responses 2006	100%	0%	0%
<b>12. I trust my Division Director. (Skip if not applicable)</b>			
Staff Responses 2007	68%	16%	16%
Staff Responses 2006	63%	20%	17%
Management Responses 2007	94%	0%	6%
Management Responses 2006	95%	0%	5%

Results of 2006 and 2007 Survey Questions Regarding Workforce Management			
	Strongly Agree or Agree	Neutral	Disagree or Strongly Disagree
<b>13. I trust Internal Audit.</b>			
Staff Responses 2007	57%	33%	10%
Staff Responses 2006	58%	32%	10%
Management Responses 2007	73%	18%	9%
Management Responses 2006	88%	4%	8%
<b>14. I trust Human Resources.</b>			
Staff Responses 2007	66%	21%	13%
Staff Responses 2006	40%	28%	32%
Management Responses 2007	91%	5%	5%
Management Responses 2006	79%	8%	13%
<b>15. I trust Legal Counsel.</b>			
Staff Responses 2007	45%	37%	18%
Staff Responses 2006	41%	31%	27%
Management Responses 2007	73%	9%	18%
Management Responses 2006	83%	8%	8%
<b>16. I trust the Deputy Director.</b>			
Staff Responses 2007	47%	30%	23%
Staff Responses 2006	50%	28%	22%
Management Responses 2007	77%	9%	14%
Management Responses 2006	86%	5%	9%
<b>17. I trust the Executive Director.</b> (Note: This item was not included in the 2006 survey because the position was vacant.)			
Staff Responses 2007	66%	29%	5%
Management Responses 2007	50%	9%	41%
<b>18. I trust the Commissioners.</b>			
Staff Responses 2007	53%	40%	7%
Staff Responses 2006	55%	32%	13%
Management Responses 2007	77%	14%	9%
Management Responses 2006	92%	4%	4%
<b>19. If I raise any issues or concerns, I believe there will be no retaliation against me.</b>			
Staff Responses 2007	44%	28%	28%
Staff Responses 2006	38%	21%	40%
Management Responses 2007	73%	14%	14%
Management Responses 2006	79%	17%	4%

Results of 2006 and 2007 Survey Questions Regarding Workforce Management			
	Strongly Agree or Agree	Neutral	Disagree or Strongly Disagree
<b>20. In this agency, management leads by example and behaves in an ethical manner.</b>			
Staff Responses 2007	61%	17%	22%
Staff Responses 2006	45%	26%	29%
Management Responses 2007	77%	14%	9%
Management Responses 2006	92%	0%	8%
<b>21. I trust that the Ombudsman function of the Agency can independently address concerns I voice. (Note: This item was not included in the 2006 survey because the position did not exist at the Agency.)</b>			
Staff Responses 2007	46%	46%	8%
Management Responses 2007	41%	23%	36%
<b>22. Policies and procedures are consistently applied within our Agency.</b>			
Staff Responses 2007	69%	14%	17%
Staff Responses 2006	56%	23%	21%
Management Responses 2007	81%	10%	10%
Management Responses 2006	83%	4%	13%
<b>23. I work in an environment that is free of fear and intimidation.</b>			
Staff Responses 2007	60%	14%	27%
Staff Responses 2006	46%	17%	37%
Management Responses 2007	77%	0%	23%
Management Responses 2006	83%	9%	9%
<b>24. Although there is some stress in my job, I feel that it is generally manageable.</b>			
Staff Responses 2007	82%	12%	6%
Staff Responses 2006	72%	18%	10%
Management Responses 2007	86%	9%	5%
Management Responses 2006	83%	13%	4%
<b>25. I feel that my values and beliefs are the same as those of Lottery Commission managers.</b>			
Staff Responses 2007	60%	20%	20%
Staff Responses 2006	51%	25%	24%
Management Responses 2007	77%	14%	9%
Management Responses 2006	74%	26%	0%
<b>26. I am loyal to the Lottery Commission.</b>			
Staff Responses 2007	94%	5%	1%
Staff Responses 2006	86%	11%	3%
Management Responses 2007	82%	18%	0%
Management Responses 2006	78%	22%	0%

Results of 2006 and 2007 Survey Questions Regarding Workforce Management			
	Strongly Agree or Agree	Neutral	Disagree or Strongly Disagree
<b>27. I feel that conflict in this Agency is handled in a tactful and professional manner.</b>			
Staff Responses 2007	52%	26%	22%
Staff Responses 2006	43%	24%	34%
Management Responses 2007	73%	9%	18%
Management Responses 2006	79%	4%	17%
<b>28. The culture in our Agency is cooperative and supportive.</b>			
Staff Responses 2007	63%	20%	17%
Staff Responses 2006	51%	22%	28%
Management Responses 2007	73%	14%	14%
Management Responses 2006	79%	8%	13%
<b>29. Employees in this Agency are free from concerns about discrimination.</b>			
Staff Responses 2007	56%	24%	20%
Staff Responses 2006	50%	24%	26%
Management Responses 2007	82%	9%	9%
Management Responses 2006	83%	4%	13%
<b>30. Employees in this Agency are free from concerns about harassment.</b>			
Staff Responses 2007	61%	23%	16%
Staff Responses 2006	54%	26%	20%
Management Responses 2007	82%	5%	14%
Management Responses 2006	91%	4%	4%
Note: Percentages in this table do not always sum to 100 percent due to rounding.			

Table 6

Results of 2007 Survey Questions Regarding Employee Contact with the Agency's Ombudsman			
<b>1. Have you contacted the Ombudsman within the past year with a complaint, concern, or other issue?</b>			
Staff and Management Responses 2007 <sup>a</sup>	Yes - 6%		No - 94%
	Strongly Agree or Agree	Neutral	Disagree or Strongly Disagree
<b>2. If yes, my concern was addressed appropriately by the Ombudsman.</b>			
Staff and Management Responses 2007	64%	18%	18%
<b>3. If yes, the resolution of the issue was communicated to me.</b>			
Staff and Management Responses 2007	55%	18%	27%
<sup>a</sup> Few Agency employees have contacted the Ombudsman with a complaint. To protect their anonymity, management and staff responses were combined for these survey items.			

Table 7 shows the response rates to the surveys the State Auditor’s Office conducted at the Agency in 2006 and 2007.

Table 7

Summary of Employee Survey Response Rate 2007 and 2006				
Year	Employee Category	Response Rate	Number of Employees Who Responded	Total Number of Employees in Category
2007	All Employees	57.33%	176	307
	Staff	56.00%	154	275
	Management	68.75%	22	32
2006	All Employees	65.92%	207	314
	Staff	64.66%	183	283
	Management	77.42%	24	31

## ***The Agency's Self-reported Status of Recommendations That Were Not Selected for Follow-up Audit Work***

Texas Government Code, Section 321.014, requires state agencies to report to the State Auditor's Office on the status of their implementation of audit recommendations. The State Auditor's Office requires agencies to submit this information on an annual basis. Tables 8 through 10 show the Texas Lottery Commission's (Agency) self-reported status for recommendations that were not selected for follow-up audit work. Unless otherwise noted, the Agency's responses were as of December 31, 2007.

Table 8

Recommendations Not Selected for Follow-up from <i>An Audit Report on Workforce Management at the Texas Lottery Commission</i> (SAO Report No. 06-047, July 2006)		
Recommendation	Agency Self-reported Implementation Status	Agency Comments
1 The Agency should establish controls to ensure that the Agency honors all assurances in its job postings.  The Agency should refine its existing policies and procedures to make it clear that, if a manager deviates from the results of a screening matrix, the manager must document the rationale for such deviations.  The Agency should adopt a policy that ensures the screening matrix includes the identity of the person who prepares the matrix, along with date it is prepared.	Fully Implemented  Fully Implemented  Fully Implemented	1) Application screening matrices submitted to Human Resources are now required to include a signature indicating the name of the employee who prepared the matrix and the date of the preparation. This requirement has been incorporated into TLC procedure HR 036 Employment Selection Process, and is addressed in the supervisor training curriculum.  2) TLC procedure HR 036 Employment Selection Process has been revised to include addressing documentation requirements when deviations are appropriate and are being considered.
2 The Agency should clarify the roles and responsibilities of the Commissioners and executive management to ensure independence and establish an effective system of checks and balances.  The Agency should establish workgroups or subcommittees, including subcommittees of one member, to address key operational areas such as those covered in this report.	Fully Implemented  Fully Implemented	...With regard to clarifying the roles and responsibilities of the Commissioners and executive management to ensure independence and establish an effective system of checks and balances, discussions have occurred among Chairman Cox, Anthony Sadberry (Executive Director), Gary Grief (Deputy Executive Director), and Kim Kiplin (General Counsel). Those discussions focused on the roles of Commissioners and the Executive Director, as well as senior management. Specifically, the discussions focused on the concept of leadership versus management, as well as policy versus day to day operations. During these discussions, Chairman Cox provided direction on the kinds of matters about which he believed a Commissioner should be involved. The basis for Chairman Cox's direction stemmed from his position that a Commissioner's role is to provide leadership and an Executive Director and executive management's role is to provide both leadership and management. Chairman Cox's view is that matters that are new initiatives or policy are within the purview of the Commissioners and, therefore, should be brought to the Commissioners' attention during the formative process of development in order to provide leadership to Commission staff. Executive staff has an overlapping role in providing both leadership and management. Where new initiatives or policy is developed, executive management provides leadership but also is charged with the responsibility to implement the new initiatives and policy. Additionally,



**Recommendations Not Selected for Follow-up from  
An Audit Report on Workforce Management at the Texas Lottery Commission  
(SAO Report No. 06-047, July 2006)**

Recommendation	Agency Self-reported Implementation Status	Agency Comments
		<p>Chairman Cox's view is that, given the responsibilities with which a Commissioner is charged, a Commissioner must be able to have access to key staff and information in order to carry out the duties and responsibilities of a Commissioner.</p> <p>Other topics discussed during the course of the meetings concerned the means by which Commissioners are kept informed or included in the operations of the agency so that an effective system of checks and balances exists. Information to Commissioners is provided in a variety of ways. The specific mode of communication used depends on the nature of the information to be provided. For example, information that requires no action by the Commission is distributed in weekly packets to the individual Commissioners. Information that is time-sensitive and/or requires input by a Commissioner is conveyed through telephone calls and/or emails. Meetings are also scheduled with individual Commissioners to discuss matters with executive management that involve or may lead to the development of new initiatives or policy. The Chairman of the agency is the main point of initial Commissioner contact for the Executive Director and executive management in connection with the conveyance of information that is time-sensitive, requires input, and/or relates to the development of new initiatives or policy. Additionally, the Commission holds meetings monthly. Items on the Commission meeting agenda are report items, as well as action items. Examples of report items are fiscal, contract, and lottery game performance matters. Examples of action items are rulemaking matters and the entry of administrative orders relating to licensees or applicants for licenses.</p> <p>The creation of workgroups or subcommittees in numbers greater than one Commissioner would trigger the application of the Texas Open Meetings Act and would require the meeting of the workgroup or subcommittee to be an open meeting. With regard to the creation of a subcommittee of one member, currently, the Commission has established such a practice for certain key operational areas. For example, currently, Chairman Cox acts as the Commission point of contact or liaison for the Internal Audit operations. Additionally, the Commissioner identified as the Bingo Commissioner acts as the Commission point of contact or liaison for the Charitable Bingo Operations. Once a third Commissioner is appointed, the Commission may want to identify other operational areas similarly. These points of contacts are not to the exclusion of involvement by other Commissioners; but, staff is mindful of a Commissioner reporting structure in the sense that staff contact is generally made first to the identified Commissioner. Perhaps this practice should be formalized through the creation of a Commission policy so that it addresses other key operational areas. This matter was an agenda item at the June 25, 2007, Commission meeting.</p>
<p>3 The Commission should consider including a performance incentive for the executive director (through a salary increase or a bonus) within its biennial Legislative Appropriations Request and discuss the merits of such an increase with Legislative Leadership and in hearings before the Senate Finance Committee and House Appropriation Committee.</p>	Fully Implemented	<p>The agency included in its Legislative Appropriations Request (LAR) a request to increase the salary for the Executive Director position.</p> <p>The 80th Legislature increased the exempt position salary cap for the Executive Director in the agency's bill pattern to \$135,000 annually. In the June 2007 Commission meeting, the Commission approved an increase in salary for the current Executive Director from \$115,000 to \$135,000 annually, effective September 1, 2007. Required notification was provided to the LBB, Comptroller of Public Accounts and the Governors Office on September 20, 2007. In addition, the agency has also been included in those agencies listed in Article IX of the GAA as having the authority to request additional salary increases for the Executive Director up to the maximum salary allowed for in Group 6.</p>

**Recommendations Not Selected for Follow-up from  
An Audit Report on Workforce Management at the Texas Lottery Commission  
(SAO Report No. 06-047, July 2006)**

Recommendation	Agency Self-reported Implementation Status	Agency Comments
<p>4 The Agency should implement a systematic, consistent job analysis process that includes regular reviews of positions to ensure the appropriate classification of Agency employees.</p> <p>The Agency should revise its job description process and develop more accurate job descriptions that reflect the essential functions of the position and include information about the physical and mental demands of the position.</p> <p>The Agency should update its policies and procedures to reflect current guidelines for determining employee exemptions under the U.S. Fair Labor Standards Act.</p>	<p>Fully Implemented</p> <p>Fully Implemented</p> <p>Fully Implemented</p>	<p>The Human Resources Division has developed and implemented an agency-wide Job Grid and related Intent and Methods of the Job Grid in which the essential functions for each position in the agency have been clearly identified. These tools will also assist agency management in ensuring current guidelines are used to determine whether employees are exempt from the FLSA.</p>
<p>5 The Agency should continue to complete the development and implementation of its policies and procedures related to ethics, recruitment and selections, performance evaluations, demotion, and the U.S. Family Medical Leave Act.</p> <p>The Agency should continue to develop and implement a training program for employees by completing the training database and providing annual management training to supervisors regarding employee discipline issues.</p>	<p>Fully Implemented</p> <p>Fully Implemented</p>	<p>The Agency stated that there is no current response to these recommendations.</p>

Table 9

Recommendations Not Selected for Follow-up from <i>An Audit Report on Procurement at the Texas Lottery Commission</i> (SAO Report No. 06-062, August 2006)		
Recommendation	Agency Self-reported Implementation Status	Agency Comments
1 The Texas Legislature should consider amending Texas Government Code, Section 466.105, to remove the Agency's exemptions from contracting statutes.	No Follow Up Needed <sup>a</sup>	
2 The Agency should periodically verify that the lottery operator's back-up data center is operational.	Incomplete/Ongoing	This is an ongoing business practice. [The third-party reviewer] completed its first review of the backup data center.
3 The Agency should establish formal policies and procedures for modifying its contracts.	Incomplete/Ongoing	A procedure for modifying or amending a contract was approved and posted on the agency's Intranet on November 1, 2006.
4 The Agency should ensure that it thoroughly evaluates all contract amendments prior to their adoption. This evaluation should include review of amendments' financial and operational impact.	Incomplete/Ongoing	The new Needs and Risk Assessment procedure was approved and posted on the Commissions Intranet on November 3, 2006.
5 The Agency should implement controls in its Contract Management Database that prevent unauthorized changes and allow it to track user changes to this system.	Incomplete/Ongoing	The specifications related to the Contract Management Database were completed June 30, 2007, and the system is currently in User Acceptance Testing. The new system should be fully implemented by December 31, 2007.
6 The Agency should ensure that it has appropriate justification for all purchases it makes.	Fully Implemented	This is an ongoing business practice.
7 The Agency should ensure that employees consistently comply with the Agency's purchasing policies and procedures.	Fully Implemented	This is an ongoing business practice. Employees responsible for purchasing goods or services are required to attend annual training.
8 The Agency should strengthen its password administration function.	Fully Implemented	The agency implemented a new Financial Interface system on September 1, 2007, which includes an electronic requisitions module.
9 The Agency should require users to access the purchasing system using their own user ids and passwords. It should not allow employees to use other employees' user ids and passwords.	Fully Implemented	An agency Directive addressing password administration has been developed and was posted on the agency's Intranet on September 19, 2006.
10 The Agency should restrict the system administrator's access to initiate purchase requests in the purchasing system.	Fully Implemented	The new Financial Interface system that was implemented on September 1, 2007, allows for unique User IDs that are the same as the employee's network login. In addition, each User ID requires a password with a minimum of 8 characters.
<sup>a</sup> Implementation status was designated as "No Follow Up Needed" by the State Auditor's Office because this recommendation was addressed to the Legislature.		

Table 10

Recommendations Not Selected for Follow-up from <i>An Audit Report on Lotto Texas Activities at the Texas Lottery Commission</i> (SAO Report No. 06-046, July 2006)		
Recommendation	Agency Self-Reported Implementation Status	Agency Comments
1 The Agency should ensure that it always completes the forms it uses to communicate approved advertised jackpots to the lottery operator.	Fully Implemented <sup>a</sup>	Practices are in place and procedure LO-PD-012 is being revised to reflect monitoring/auditing of the forms used to communicate approved advertised jackpots to the lottery operator for completeness.
2 The Agency should fully implement its process for using the checklist to document the completion and review of significant steps in the jackpot estimation process. The Agency should incorporate this checklist into policies and procedures. Agency management should ensure that staff consistently complete the checklist or document why items on the checklist are not completed.	Fully Implemented <sup>a</sup>	Jackpot Estimation Procedure OC-JE-002 was approved on July 31, 2006.
3 The Agency should ensure that appropriate members of management consistently review and approve prize annuity schedules provided by the Texas Treasury Safekeeping Trust Company.	Fully Implemented	In its July 2006 response to this recommendation, the Agency reported that this recommendation was fully implemented.
4 The Agency should follow policies and procedures and ensure that Agency management consistently reviews, approves, and signs all transfers to the Foundation School Fund. The Agency should also obtain written and signed approval from the Executive Director for any exceptions to policies and procedures.	Fully Implemented	In its July 2006 response to this recommendation, the Agency reported that this recommendation was fully implemented.
5 The Agency should maintain all documentation related to Foundation School Fund transfers in accordance with its records retention schedule.	Fully Implemented	In its July 2006 response to this recommendation, the Agency reported that this recommendation was fully implemented.
6 The Agency should develop and enforce a formal agreement with the lottery operator that describes the lottery operator's responsibilities regarding incomplete transactions and any penalties or sanctions for any errors made by the lottery operator that are associated with these transactions.  The Agency should develop and implement policies and procedures for monitoring incomplete transactions that include (1) obtaining information from the lottery operator that identifies number combinations associated with incomplete transactions and (2) verifying whether these incomplete transactions are	Substantially Implemented  Substantially Implemented	The agency has thoroughly researched and investigated the issue of incomplete transactions, with a focus on a subset of these transactions known as retry transactions. Retry transactions, caused by telecommunication problems, result in the central lottery gaming system receiving and logging a transaction while the related ticket is potentially not printed. While the terminal continues in a retry mode to complete confirmation of the transaction, a ticket cannot be printed. This may continue for an extended period of time, depending on the cause and how quickly the telecommunication problem is resolved. Retry transactions may span draw breaks or even calendar days, and the terminal attempts to print the ticket only upon reestablishment of the connection between the terminal and the central system. Once the terminal comes out of retry mode, a ticket may or may not be printed.  As previously reported, the agency has been diligently studying this issue for several months and, with assistance from [the primary lottery operator], the lottery operator, has attempted to be responsive to the recommendations of the SAO in this matter. During the agency's

**Recommendations Not Selected for Follow-up from  
An Audit Report on Lotto Texas Activities at the Texas Lottery Commission  
(SAO Report No. 06-046, July 2006)**

Recommendation	Agency Self-Reported Implementation Status	Agency Comments
<p>associated with winning number combinations.</p> <p>The Agency should develop and implement a formal policy to address situations in which the numbers on incomplete transactions win a high-tier or jackpot prize. The policy should (1) identify Agency personnel to be notified; (2) explain what happens to the prize money, including instances in which another winner with a ticket has been identified; and (3) describe what the Agency will report to the public.</p>	<p>Substantially Implemented</p>	<p>review of this issue, the staff has challenged [the primary lottery operator] to pursue all potential solutions or efforts to mitigate this situation.</p> <p>As a result, [the primary lottery operator] recently brought forward supplemental information indicating that no assurance can be provided, using available technology, that tickets are printed or not during a retry transaction. This information represents a fundamental change in both the agency's and the SAO's understanding of this issue. At the time of SAO review of this issue, the understanding of both the SAO and the agency was that transactions of this nature never resulted in a printed ticket.</p> <p>This new information has caused the agency to revise its approach to addressing retry transactions, and additional work is needed in this regard. In the August 2007 Commission meeting, staff presented this new information to the Commission and informed the Commission of staff's change in approach regarding this matter. In the September 2007 Commission meeting, staff plans to bring before the Commission a rule change related to a technological enhancement [the primary lottery operator] is implementing which will substantially reduce the number of retry transactions occurrences. In addition, staff will be proposing an amendment to the lottery operator contract regarding retry transactions.</p> <p>The SAO has been informed of the new information recently provided by [the primary lottery operator] related to retry transactions and the agency will take the necessary steps to modify the agency management response to the SAO audit through the proper reporting mechanisms.</p> <p>Ultimately, staff will make available on the agency website an appropriate record of the agency's communication with the SAO regarding retry transactions along with any revision to the management response to the SAO Lotto Texas audit.</p> <p>The necessary rule changes were adopted by the Commission in the December 2007 Commission meeting. The necessary contract amendment was executed November 30, 2007. Communication with the SAO and posting to the agency website will occur by January 31, 2008.</p>
<p>7 The Agency should perform regular reviews of access rights to its administrative systems and ensure that access is based on current job roles and responsibilities.</p>	<p>Fully Implemented</p>	<p>In its July 2006 response to this recommendation, the Agency reported that this recommendation was fully implemented.</p>
<p><sup>a</sup> These recommendations were reported as "Fully Implemented" by the Agency in February 2007. Therefore, no Agency responses to these items were requested or provided in December 2007. Comments listed in this table are from the Agency's February 2007 self-reported status of recommendations.</p>		

## Proposed Statutory Language

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Below is a draft of statutory language the State Auditor's Office developed regarding the Texas Lottery Commission's policies and procedures related to Lotto Texas activities.<sup>2</sup>

467.001 DEFINITIONS.

(13) "Proposed policy or procedure" means any proposal to add, modify, or delete a policy or procedure relating to the operation of Lotto Texas.

467.1011. PUBLICATION OF PROPOSED POLICIES OR PROCEDURES.

- (a) The Commission shall publish all proposed policies or procedures affecting Lotto Texas players for a minimum of 30 days prior to taking public comments on the proposed policies or procedures.
- (b) All publications required by this section shall be made in the *Texas Register* and on the Commission's Web site.

467.1012. ACTION ON PROPOSED POLICIES AND PROCEDURES.

- (a) After the Commission has published the proposed policies or procedures pursuant to Section 467.1011 of this chapter, the Commission shall conduct a public hearing during which members of the public may comment on the proposed policies or procedures.
- (b) Notice of this public hearing shall be given in the same manner as notice for regular meetings of the Commission. The notice of the meeting must include a list of the proposed policies and procedures on which public comments will be accepted.
- (c) The Commission may not take action on any proposed policy or procedure at a meeting at which public comment on the proposed policy or procedure is being taken.
- (d) Any action to adopt, modify, or delete a proposed policy or procedure may only be taken at a Commission meeting held at least 30 days following the public hearing on the proposed policy or procedure.

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<sup>2</sup> This statutory language is in draft form and is subject to review and redraft by the Texas Legislative Council.

## Recent State Auditor's Office Work

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Recent SAO Work		
Number	Product Name	Release Date
07-008	A Report on an Audit of the Texas Lottery Commission's Annual Financial Report for the Fiscal Year Ended August 31, 2006	December 2006
06-062	An Audit Report on Procurement at the Texas Lottery Commission	August 2006
06-047	An Audit Report on Workforce Management at the Texas Lottery Commission	July 2006
06-046	An Audit Report on Lotto Texas Activities at the Texas Lottery Commission	July 2006
06-035	An Audit Report on Security at the Texas Lottery Commission	May 2006

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The Honorable Tom Craddick, Speaker of the House, Joint Chair  
The Honorable Steve Ogden, Senate Finance Committee  
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The Honorable Warren Chisum, House Appropriations Committee  
The Honorable Jim Keffer, House Ways and Means Committee

### **Office of the Governor**

The Honorable Rick Perry, Governor

### **Texas Lottery Commission**

Members of the Texas Lottery Commission

Mr. James A. Cox, Jr., Chairman

Mr. C. Thomas Clowe, Jr.

Mr. David J. Schenck

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