



**TEXAS LOTTERY COMMISSION
INTERNAL AUDIT**

**ANNUAL INTERNAL AUDIT REPORT
FY 2017**



McCONNELL & JONES LLP
CERTIFIED PUBLIC ACCOUNTANTS



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October 5, 2017

The Honorable Greg Abbott, Governor
Members of the Legislative Budget Board
Members of the Sunset Advisory Commission
Internal Audit Coordinator, State Auditor's Office

Dear Ladies and Gentlemen:

Attached is the fiscal year 2017 Internal Audit Report for the Texas Lottery Commission (TLC). This annual internal audit report is submitted in accordance with the Texas Internal Auditing Act requirement for state agency internal auditors to prepare and distribute an annual report (Government Code, Chapter 2102). TLC engaged McConnell & Jones LLP (MJ) on January 1, 2014 to provide internal audit services to the TLC in accordance with The Texas Internal Auditing Act, pursuant to the Request for Proposals (RFP) issued October 22, 2013. MJ submits this FY2017 Annual Internal Audit Report on behalf of the TLC Commissioners.

The Texas Internal Auditing Act requires agencies to file an annual report on their internal audit activities and the internal audit reports prepared for their governing board. The purpose of the annual internal audit report is to provide information on the assurance services, consulting services, and other activities of the internal audit function. In addition, the annual internal audit report assists oversight agencies in their planning and coordination efforts. According to Texas Government Code, Sections 2102.009 and 2102.0091, the FY2016 Annual Internal Audit Report is due November 1, 2017.

Please contact Wayne McConnell at 713.968.1600 or Commissioner J. Winston Krause at 512.477.6707 if you should have any questions about this audit report.

Sincerely,

Ira Wayne McConnell, CPA
Partner



I. COMPLIANCE WITH TEXAS GOVERNMENT CODE, SECTION 2102.015: POSTING THE AUDIT PLAN AND ANNUAL REPORT ON THE INTERNET

Texas Government Code, Section 2102.015, requires state agencies and institutions of higher education to post agency internal audit plans and internal audit annual reports to the agency's internet website within 30 days of approval. Texas Government Code, Section 2102.015, also requires agencies to update the posting on the website to include a detailed summary of any weaknesses, deficiencies, wrongdoings, or other concerns raised by the audit plan or annual report and include a summary of the actions taken by the agency to address the issues raised.

In accordance with requirements of Texas Government Code, Section 2102.015, McConnell & Jones LLP (MJ) will ensure the required internal audit plan, internal audit annual report and any other required internal audit information is provided to the Texas Lottery Commission (TLC) for posting to their website.

II. FISCAL YEAR 2017 INTERNAL AUDIT PLAN STATUS

McConnell & Jones LLP prepared the Fiscal Year 2017 Annual Internal Audit plan based on a comprehensive risk assessment which was approved by the TLC commissioners on October 13, 2016. The chart below reflects the status of the approved FY2017 Internal Audit Plan.

FY2017 Internal Audit Plan Status as of August 31, 2017

Task #	Description	Report Number	Report Date	Report Title	Audit Status
1	Scratch Ticket Warehouse Receiving Controls	17-000	December 19, 2016	Scratch Ticket Warehouse Receiving	Completed
4	Scratch Ticket Pack Reconstruction Controls	17-002	January 19, 2016	Scratch Ticket Reconstruction Controls	Completed
2	CBOD Audit Processes	17-003	February 10, 2017	Charitable Bingo Operations Division Audit Services Processes	Completed
3	Enforcement – Background Check and Investigation Processes	17-004			Audit Completed – Draft Report to be Issued in November 2017
5	Retailer Management	17-005	April 20, 2017	Retailer Management Processes	Completed
6	Fraud Awareness Training	N/A	N/A	N/A	Completed
7	Employee Time and Attendance recording, Monitoring and Reporting	17-006	August 25, 2017	Employee Time and Leave Processes	Completed
8	Second Chance Drawing Controls	17-008	August 31, 2017	Second-Chance Drawing Processes	Completed



Task #	Description	Report Number	Report Date	Report Title	Audit Status
9	Crisis Management Plan	17-007	August 30, 2017	Crisis Management Plan	Completed
10	Active Directory Audit	17-009	August 25, 2017	Active Directory	Completed
11	Jackpot Estimation System	17-011	August 31, 2017	Jackpot Estimation System Controls	Completed
12	Scratch Ticket Working Paper Workflow System	17-010	August 31, 2017	Scratch Ticket Working Paper Workflow System Controls	Completed
13	Follow-Up On Prior Audit Findings	N/A	N/A	N/A	On-Going
14	Management of Fraud/Complaint Hotlines Lines	N/A	N/A	N/A	On-Going
15	External Audit / Review Assistance	N/A	N/A	N/A	No Assistance Requested
16	Update Risk Assessment & Develop 2018 Audit Plan	N/A	N/A	N/A	Completed
17	Annual Audit Report	N/A	N/A	N/A	Completed
18	Audit Communications, Committee Meetings, Project Management	N/A	N/A	N/A	On-Going

Deviation from Fiscal Year 2017 Internal Audit Plan

Internal audit executed the FY2017 Annual Internal Audit Plan as originally approved.

III. CONSULTING SERVICES AND NON-AUDIT SERVICES COMPLETED

Internal Audit provided consultative assistance to Charitable Bingo Operations Division (CBOD) management to review and redesign their audit services' operations. We reviewed the processes involved with performing annual risk assessments, audit planning and audit execution to identify potential efficiencies. Our audit objectives were to

1. Improve the audit and game inspection experience for bingo operators and charities.
2. Streamline the audit and game inspection processes.
3. Reduce audit completion time.
4. Reduce required documentation (licensee and audit workpapers).
5. Increase audit automation.
6. Increase internal transparency (audit scheduling and audit progression monitoring).
7. Align audit processes with Statute and Rules.



Our recommendations are included in report number 17-003 Charitable Bingo Operations Division Audit Services Processes issued on February 10, 2017.

IV. EXTERNAL QUALITY ASSURANCE REVIEW (PEER REVIEW)

MJ has been a member of the AICPA since 1987, and is subject to the AICPA's peer review process every three years. Our commitment to quality is underscored by the fact that we have consistently received an unqualified opinion in our external peer review of our accounting and auditing practice by the AICPA in the most recent four peer reviews. After a thorough review of our procedures and work practices, which include reviews of our nonprofit, governmental, and commercial engagements, the reviewers concluded that MJ complies with the stringent quality control standards established by the American Institute of Certified Public Accountants. We provide a copy of our most recent peer review letter below.



Your Vision Our Focus



System Review Report

February 20, 2016

To the Partners of
McConnell & Jones, LLP
and the National Peer Review Committee

We have reviewed the system of quality control for the accounting and auditing practice of McConnell & Jones, LLP (the firm) applicable to engagements not subject to PCAOB permanent inspection in effect for the year ended June 30, 2014. Our peer review was conducted in accordance with the Standards for Performing and Reporting on Peer Reviews established by the Peer Review Board of the American Institute of Certified Public Accountants. As a part of our peer review, we considered reviews by regulatory entities, if applicable, in determining the nature and extent of our procedures. The firm is responsible for designing a system of quality control and complying with it to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Our responsibility is to express an opinion on the design of the system of quality control and the firm's compliance therewith based on our review. The nature, objectives, scope, limitations of, and the procedures performed in a System Review are described in the standards at www.aicpa.org/prsummary.

As required by the standards, engagements selected for review included audits of employee benefit plans and audits performed under Government Auditing Standards.

In our opinion, the system of quality control for the accounting and auditing practice of McConnell & Jones, LLP (the firm) applicable to engagements not subject to PCAOB permanent inspection in effect for the year ended June 30, 2014, has been suitably designed and complied with to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Firms can receive a rating of pass, pass with deficiency(ies) or fail. McConnell & Jones, LLP has received a peer review rating of pass.

Turner, Stone & Company, LLP

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V. FISCAL YEAR 2018 INTERNAL AUDIT PLAN

MJ developed the Fiscal Year 2018 Internal Audit Plan based on results of the annual risk assessment. The risk assessment included reviewing the agency's strategic plan, the Legislative Appropriations Request and the Survey of Employee Engagement results; reviewing prior audit reports and findings; and conducting discussions with management. Our assessment evaluated risk exposures relating to the TLC's governance, operations, and information systems regarding the reliability and integrity of financial and operational information; effectiveness and efficiency of operations; safeguarding of assets; and compliance with laws, regulations, and contracts.

MJ will conduct seven scheduled audits, update the risk assessment, conduct prior audit finding follow-up activities, prepare the fiscal year 2019 Annual Internal Audit Plan and prepare the fiscal year 2018 Internal Audit Annual Report in accordance with the Texas Internal Auditing Act. These activities are estimated to require **2,285 hours**. The planned audits, timing and estimated hours are summarized in the chart below.

Fiscal Year 2018 Annual Internal Audit Plan Activities

Audit Activity #	Description	Risk Rating	Estimated Timing	Estimated Hours
1	CBOD Licensee Education Program	Medium	Nov. 2017 – Jan.2018	280
2	Personal Identifiable Information – (Agency-Wide including CBOD)	High	Jan.2018 – April 2017	401
2	Social Responsibility	Medium	Jan. 2018 – April 2018	387
4	Drawing Equipment Maintenance Process and Controls	High	April 2018 – May 2018	205
5	Unclaimed Prize Processes	Medium	April 2018 – May 2018	281
6	Instant Game Closing Process	High	May 2018 – June 2018	240
7	Mail Room Processes	High	June 2018 – July 2018	184
8	Follow-Up on Prior Audit Findings (including security study)	Compliance	On-Going	145
9	Monitor Fraud/Complaint Hotline	Compliance	On-Going	8
10	External Audit / Review Assistance	N/A	On-Going	8
11	Update Risk Assessment & Annual Audit Plan	Compliance	July 2018	81
12	Annual Internal Audit Report	Compliance	August 2018	9
13	Audit Communications, Committee Meetings, Project Management	N/A	On-Going	56
	Total			2,285

Proposed audits will focus on internal controls and business processes



VI. EXTERNAL AUDIT SERVICES PROCURED IN FISCAL YEAR 2017

The following represent external audit services that were procured by the Texas Lottery Commission or were ongoing in fiscal year 2017.

<i>Audit / Review</i>	<i>Auditor</i>
<i>Drawings Audit</i>	<i>DK Partners, P.C.</i>
<i>FY17 Financial Audit Services</i>	<i>Weaver and Tidwell, LLP</i>
<i>Security Study</i>	<i>Berry Dunn</i>

VII. REPORTING SUSPECTED FRAUD AND ABUSE

Texas Lottery Commission has implemented measures to comply with Article IX, Section 7.10, the General Appropriations Act (81st Legislature) and Texas Government Code, Section 321.022. These measures include, but are not limited to, the following:

The Texas Lottery Commission included a link to the State Auditor’s Office (SAO) website for fraud reporting at the footer of the Texas Lottery Commission website. In addition, information on reporting suspected fraud to the State Auditor’s Office is included in the agency’s policies and procedures.

The Texas Lottery Commission utilizes EthicsPoint Reporting. EthicsPoint is a third-party vendor that provides an Internet and telephone based reporting system that can be accessed by Commission employees. This system is intended to supplement the existing avenues within the Commission for employees to report concerns. All EthicsPoint complaints are reviewed by the agency’s General Counsel and reported to SAO as applicable.

VIII. SIGNIFICANT INTERIM CHANGES

Interim changes to the annual audit plan may occur from time to time due to changes in management direction, objectives, business risks, timing of initiatives, and staff availability. In accordance with IIA Performance Standard 2020, MJ will communicate any significant changes of the audit plan to TLC’s executive management and present these changes to the TLC Commissioners for review and approval. Notification of significant changes to the Internal Audit Plan approved by the Audit Committee will be submitted to the State Auditor’s Office (SAO).

This annual internal audit report was presented to the Commissioners and approved on October 5, 2017.

J. Winston Krause, Chairman



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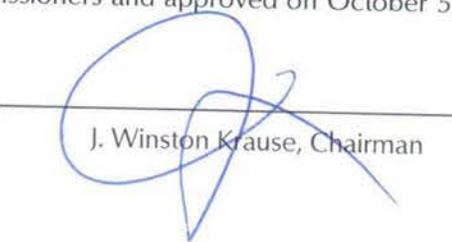
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J. Winston Krause, Chairman