



**TEXAS LOTTERY
COMMISSION**

Internal Audit Services

Audit Report of:

17-001

Scratch Ticket Warehouse

Receiving

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Prepared By:



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CERTIFIED PUBLIC ACCOUNTANTS



Introduction

McConnell & Jones LLP (MJ), serving as the outsourced internal audit function (Internal Audit) for the Texas Lottery Commission (TLC), performed an internal audit of the scratch ticket warehouse receiving processes and internal controls. This audit was performed at the request of the Texas Lottery Commissioners and was included in the approved FY2017 internal audit plan. We conducted this audit in accordance with generally accepted government audit standards (GAGAS). Those standards require that we plan and perform the audit to obtain sufficient appropriate evidence to provide a reasonable basis for the audit findings and conclusions based on the audit objectives. We believe the evidence obtained meet these requirements.

Pertinent information has not been omitted because it was not deemed privileged or confidential by law. This report summarizes the audit scope, our assessment based on the audit objectives and the analysis of Texas Lottery Commission's scratch ticket warehouse receiving business process.

Report Format:

This report contains the following sections:

- ❖ Introduction – Provides an overview of scratch ticket warehouse receiving process and the audit objectives.
- ❖ Scratch Ticket Warehouse Receiving Business Risks and Controls – Summary of business objectives, risks assessed and the audit outcomes.
- ❖ Internal Control Environment - Evaluation of the high level controls that govern the scratch ticket receiving processes.

Objectives and Scope:

The audit of scratch ticket warehouse receiving processes was conducted to ensure the internal control environment addresses the associated risks related to scratch ticket games while in transportation from the supplier to the TLC warehouse and receiving the scratch ticket games at the TLC warehouse. .

Audit Period:

The audit period included September 1, 2015 – August 31, 2016.



Results and Conclusions:

The audit procedures performed during this audit determined that internal controls over the scratch ticket game transportation process and warehouse receiving processes are effective and working as intended. We believe that both the scratch ticket manufacturing vendors and the Texas Lottery Commission have adequate controls in place to ensure that scratch tickets are transported in a secure manner and that controls are in place to ensure that contraband of any nature is not able to be introduced into the transportation vehicle without the vehicle's security breach being identified by TLC upon delivery. Additionally, suppliers printing scratch tickets in facilities outside of the United States borders hold high level transportation certifications issued by the United States Department of Homeland Security. The certifications add an additional layer of security for transporting scratch tickets across borders.

The internal control environment is performed through shipping and transportation security requirements identified in the scratch ticket game request for proposals (RFP) and each supplier's contract; monitoring and verification of scratch ticket deliveries; documented policy and procedures, defined roles and responsibilities, best practices and institutional knowledge.

Background:

The Texas Lottery Commission currently receives scratch ticket games from three contracted vendors. These vendors and the Texas Lottery Commission follow documented processes to ensure scratch tickets are transported and delivered from the respective contracted vendor to the Texas Lottery Warehouse in a secure manner. It is also the responsibility of the Texas Lottery Commission to certify the delivery security and to ensure the correct scratch games were received.

The Texas Lottery Commission determined the transportation and receiving of scratch ticket games processes to be high risk to the Agency and developed processes to ensure the risks are mitigated. The Agency's internal controls begin by ensuring their contracted vendors can meet specific criteria pertaining to the transporting and delivery of the scratch ticket inventory and ensures they are monitored by the warehouse staff during each shipment. In the rare occasion where a transportation problem does arise the shipment is returned and the vendor is notified. The Texas Lottery Commission also sends the vendor a warning advisement or a notification letter. These letters and notification are then taken into consideration when vendor performance is assessed by the Texas Lottery Commission.

The Agency also developed specific policies and procedures that pertain to the receiving of scratch ticket inventory at the warehouse. These policies and procedures specify the processes to be completed and the roles and responsibilities of those involved in the process. The policies and procedures are also supported by employee's in-depth understanding of the process as noted through the walkthrough and interview processes.



Acknowledgement:

We wish to thank all the staff involved in the audit for their professionalism and positive outlook towards the audit process performed on the business processes. The timely completion of this audit was due to their efforts and responsiveness to our requests.

Scratch Ticket Receiving Business Risks and Controls

Objective #	1 – Scratch Ticket Shipping & Receiving Governance (Oversight)
Business Objective	To ensure scratch ticket receiving policies are established by the leadership team and are understood by staff involved in the receiving processes.
Business Risk	<ul style="list-style-type: none"> Scratch ticket receiving processes are not defined by the leadership team which results in lack of internal controls and staff not following consistent processes.
Management Controls	<ul style="list-style-type: none"> TLC’s leadership team established and reviews policies and procedures to manage and monitor the scratch ticket receiving process. TLC staff have defined roles and an in-depth understanding of their roles and responsibilities with the warehouse receiving processes. Management’s monitoring activities are documented and maintained.
Control Effectiveness Rating	Effective
Audit Testing Results	No Observations Noted
Recommended Actions	None
Observation Risk Rating	N/A – No Observations Noted
Management Action Plans	None Required



Objective #	2 – Scratch Ticket Contract Management
Business Objective	To ensure that scratch ticket vendor contracts define roles and responsibilities for transportation security and that the contract terms are followed.
Business Risk	<ul style="list-style-type: none"> • Scratch ticket vendors do not take appropriate measures to safeguard scratch tickets and the shipping container while in route to TLC’s warehouse. • Scratch ticket vendors contracts are not clear on the roles and responsibilities of the vendor and Texas Lottery Commission with regards to the scratch ticket shipping and receiving. • Scratch Ticket vendor contracts do not address the security of shipping and receiving of tickets to the Texas Lottery Warehouse. • Scratch ticket vendor contracts are not on file or monitored for vendor performance.
Management Controls	<ul style="list-style-type: none"> • TLC establishes the criteria that must be adhered to by the vendor prior to entering into a signed contract. • Contracts are maintained by TLC’s contracts coordinator. • Vendors are monitored and advised of infractions through sanctions and warnings. • Contracts are reviewed annually by key personnel in the of scratch ticket warehouse receiving processes. • TLC warehouse staff understand who to contact when issues are noted.
Control Effectiveness Rating	Effective
Audit Testing Results	No Observations Noted
Recommended Actions	None
Observation Risk Rating	N/A – No Observations Noted
Management Action Plans	None Required



Objective #	3 – Scratch Ticket Transportation Security
Business Objective	To ensure that scratch tickets are appropriately secured while in route to the TLC warehouse, including that the shipping container is secured from tampering and unauthorized access.
Business Risk	<ul style="list-style-type: none"> • Shipping containers carrying scratch tickets could be compromised which could result in unauthorized items being included in the container. • Scratch tickets could be lost or damaged. • TLC warehouse staff are unable to determine scratch ticket security upon arrival due to lack of shipping notification information. • TLC warehouse staff are unable to determine unauthorized access to the shipping container due to broken seals (locks).
Management Controls	<ul style="list-style-type: none"> • Vendor contracts document transportation security requirements which include using certified, tamper-proof serialized seals (locks) on shipping container and providing TLC with seal and shipping information in a timely manner once the scratch tickets are loaded. • Suppliers printing scratch tickets in facilities outside of the United States borders hold high level transportation certifications issued by the United States Department of Homeland Security. • Shipment notification sheets are emailed to TLC and include: <ul style="list-style-type: none"> • Shipment Date • Truck Contents • Number of Samples • Truck Seal Numbers • Drivers Identification Information • TLC warehouse receiving processes include multiple individuals inspecting the shipping container doors and verifying truck seal data to the shipping notification to ensure that shipping containers have not been compromised.
Control Effectiveness Rating	Effective
Audit Testing Results	No Observations Noted
Recommended Actions	None
Observation Risk Rating	N/A – No Observations Noted
Management Action Plans	None Required



Objective #	4 – Scratch Ticket Receiving
Business Objective	To ensure that scratch ticket deliveries are inspected upon arrival at the TLC warehouse and then appropriately received into the inventory tracking system.
Business Risk	Scratch tickets deliveries are not independently verified to ensure security was maintained during the transportation process.
Management Controls	<ul style="list-style-type: none"> • Responsibility for receipt, verification and safeguarding of the scratch ticket warehouse receiving processes are segregated. • Proper authority and authorization is documented for key positions involved in the scratch ticket receipt process. • Authorized warehouse and TLC personnel ensure scratch ticket inventory received from the vendor is secured and verified prior to signing off and accepting the received scratch ticket inventory. • Truck seal is physically verified to be secure and in-tact upon arrival to TLC’s warehouse loading docks. • Visual inspection of each scratch ticket skid occurs. • Verification of scratch ticket carton ranges for each skid occurs. • Shipping notifications and shipping orders are signed and maintained. • All issues with shipments are reported to management.
Control Effectiveness Rating	Effective
Audit Testing Results	No Observations Noted
Recommended Actions	None
Observation Risk Rating	N/A – No Observations Noted
Management Action Plans	None Required



Scratch Ticket Internal Control Environment

The following table notes the general controls documented during the audit process and how they are functioning to ensure effective management of the risks associated with receiving scratch ticket games from vendors at that the Texas Lottery Warehouse.

Adequate Improvement Recommended Not Adequate

Internal Controls Practices	Rating
Policies and procedures are well-documented.	
Effective monitoring by management and staff of the process and controls that manage the receipt of scratch ticket games.	
Documentation supporting the vendor’s shipping notification and verification of the scratch ticket games received is maintained.	
Vendor performance is managed and measured.	
Employees involved in the scratch ticket receiving processes have extensive experience and a comprehensive understanding of the process and how issues should be reported through the Agency and to the respective vendor.	