



# Texas Lottery Commission Internal Audit

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**Review of  
Charitable Bingo Operations Division  
Audit Services Processes**

The logo for Charitable Bingo, featuring the word "CHARITABLE" in white and "BINGO" in large yellow letters on a blue background. The background also contains several small white bingo balls with numbers. The words "TEXAS LOTTERY COMMISSION" are written in small white letters at the bottom of the logo.

**February 10, 2017  
Report #17-003**

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## Introduction

McConnell & Jones LLP (MJ) serving as the outsourced internal audit function (Internal Audit) for the Texas Lottery Commission (TLC) performed a consulting and advisory services assessment of Charitable Bingo Operations Division (CBOD) Audit Services' audit processes. This consulting and advisory services assessment was completed at the request of CBOD's director to help identify audit process improvements. The consulting and advisory services were conducted in conformance with the International Standards for the Professional Practice of Internal Auditing (IIA Standards) and with the Texas Internal Auditing Act (The Act).

The IIA standards allow internal auditors to provide consulting and advisory services when the engagement has the potential to improve management of risks, add value, improve the organization's operations; provided that internal audit has no conflict of interest and internal audit personnel have no management responsibilities for the area in scope. When providing advisory or consulting services, internal auditors are required to establish an understanding with consulting engagement clients about objectives, scope, respective responsibilities, and other client expectations. Additionally, the established scope must be sufficient to achieve the objectives of the engagement and must include consideration of relevant systems, records, personnel, and physical properties, including those under the control of third parties.

The Act defines internal auditing as an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. Sec. 2102.003 of the Act defines consulting services as advisory and related client service activities, the nature and scope of which are agreed upon with the client and are intended to add value and improve an organization's operations. Consulting services include counsel, advice, facilitation, and training.

### Overview

Texas Occupations Code Title 13. Sports, Amusements and Entertainment, Subtitle A. Gaming Chapter 2001.Bingo is the statute commonly cited as the Bingo Enabling Act (BEA) and is the authoritative document used to govern licensing and enforcement activities. The BEA outlines roles and responsibilities of the Texas Lottery Commission (Commission), the Bingo Division and license holders. The BEA is supported by Administrative Rules that further define roles and responsibilities. **Figure 1** provides excerpts from the BEA sections that provide the Commission's authority to regulate and audit license holders.



Section	Title	Description
Sec. 2001.051	Control and Supervision of Bingo; Bingo Division	(a) The commission shall administer this chapter. (b) The commission has broad authority and shall exercise strict control and close supervision over all bingo conducted in this state so that bingo is fairly conducted and the proceeds derived from bingo are used for an authorized purpose. (c) The commission shall execute its authority through a bingo division established by the commission to administer this chapter.
Sec. 2001.054	Rulemaking Authority	The commission may adopt rules to enforce and administer this chapter.
Sec. 2001.560	Examination of Records; Disclosure of Information	(c) The commission or a person authorized in writing by the commission may examine the books, papers, records, equipment, and place of business of a license holder and may investigate the character of the license holder's business to verify the accuracy of a return, statement, or report made, or, if no return is made by the license holder, to ascertain and determine the amount required to be paid. (c1) The commission by rule shall develop a policy for auditing license holders. The bingo division shall use audit risk analysis procedures established by the commission to: (1) annually identify which license holders are most at risk of violating this chapter or rules adopted under this chapter; and (2) develop a plan for auditing the identified license holders that includes: (A) a schedule for the audits of the identified license holders; (B) procedures to annually update the plan based on successive risk analyses; and (C) a completion date for each audit that is not later than the fifth anniversary of the date the license holder was identified as a candidate for audit. (c2) The bingo division shall provide to the commission a copy of the auditing plan developed under Subsection (c1). (d) The commission may set and charge to the license holder a fee in an amount reasonably necessary to recover the cost of an authorized investigation or audit authorized under this chapter.

Figure 1 BEA Excerpts Related to Regulating and Audit Authority The BEA provides the Commission's authority to regulate and audit license holders.

CBOD's Audit Services department is responsible for performing compliance audits and game inspections. The purpose of these activities is to ensure that information reported to

the Commission by license holders is complete and accurate, that bingo is fairly conducted and the proceeds derived from bingo are used for authorized purposes. CBOD's Audit



Services developed audit policies, procedures and processes to ensure that compliance with regulations cited in the BEA and Administrative Rules are assessed during an audit. Bingo Audit Services developed a detailed Bingo Audit Methodology and Standards Handbook (BAMS) and workpaper templates to guide the audit process.

### Assessment Procedures

We performed the following activities for this consulting and advisory services review:

- Gained an understanding of Bingo Audit Services processes from risk assessment and audit planning to audit steps and reporting.
- Mapped the Bingo Enabling Act and Administrative Rule requirements to Bingo Audit Services audit procedures.
- Observed audit entrance and exit conferences.
- Observed a game inspection.
- Observed bingo operations at a bingo hall.
- Reviewed Bingo Audit Services forms and workpaper templates.

### Acknowledgement

We wish to thank all staff involved in this audit for their professionalism and positive outlook toward the assessment of their respective role within the performance measure business processes. The timely completion of this audit was due to their efforts and responsiveness to our requests.

We also want to thank the conductors, manufacturers, distributors and lessors that provided their perspective on the documentation requirements and audit processes and also allowed us to observe their bingo operations.

### Results and Conclusions

*Thank you to all staff, conductors, manufacturers, distributors and lessors involved in this assessment. Their professionalism and timely responsiveness to our requests allowed us to identify improvement opportunities and facilitated the recommendations being made in this report.*

We determined that **Bingo Audit Services audit steps are effective to ensure license holder compliance with the BEA and Administrative Rules.** However, there are opportunities to improve license holder and charitable organization's perceptions of the audit function, expand the number of audits performed, increase efficiencies and shorten the audit completion times. Incorporating organizational change management concepts

and principals into implementing these recommendations is crucial to the acceptance of changes and long-term success.

### Report Structure

This report is divided into two sections:

1. Brief discussion of observations and recommendations.
2. Project plan to guide implementation of the revised Bingo Audit Services processes.



## Observations and Recommendations Summary

This section of the report contains a discussion of the overarching observations related to Charitable Bingo Operations Division Audit Services processes. CBOD's director requested an independent, objective assessment of CBOD's Audit Services processes to identify ways to improve audit timeframes and efficiencies. Accordingly our focus was to assess current processes and determine:

1. What are the root causes leading to lengthy audit completion times?
2. How can we change the customer, and license holders' perception of the Audit Services Department and processes?
3. How can we improve audit transparency?
4. What audit processes can be enhanced or eliminated?
5. How can the audit procedures be organized to be more efficient?
6. Is the Audit Services Department appropriately staffed?

### **Question 1: What are the root causes leading to lengthy audit completion times?**

Lengthy audit completion times can be attributed to many factors that are both internal to CBOD audit processes and audited organizations either not understanding the documentation requests or not maintaining the required documents. The process of not scheduling audit activities in advance on a comprehensive master schedule also contributes to lengthy audit timeframes.

#### *Recommendation:*

Restructure audit process from the risk assessment to planning, audit and reporting. This includes scheduling audits and audit activities in advance, earlier audit notifications to organizations and clearer communications. Provide early audit notification letters and

engagement letters to audit organizations that outline the responsibilities, expectations and audit processes.

Require conductors, manufacturers, distributors and lessors to submit documents to CBOD in advance of the audit. CBOD Audit Services Department staff will perform interviews, games observations and some audit activities on-site. Data analysis and document review will be completed prior to the on-site activities.

**Figure 2** at the end of this discussion section provides a graphic of the proposed audit process. It is placed at the end because it captures all recommended changes.

### **Question 2: How can we change the customer, and license holders' perception of the Audit Services Department and processes?**

CBOD Audit Services staffs approach audits from a compliance perspective and as a tool to educate license holders on the regulations.

The nature of audits has a natural tendency to increase anxiety which can lead to resistance and misunderstandings. Furthermore, being regulators places emphasis on compliance for regulations which organizations do not always understand. It is important for auditors to exercise professional skepticism but also realize that they are in a position to help organizations understand the regulations, documentation expectations and provide best practice examples in cases where deficiencies are noted.

#### *Recommendation:*

Establish processes to improve perceptions, provide guidance or examples to organizations and obtain feedback from auditees. Examples of actions that can be taken include, but are not limited to the following:



- Changing the mindset of the auditor from being solely a “regulator” and “authoritarian” to that of a “partner in assessing” if organizations have processes in place to ensure compliance with regulations and documentation to substantiate information reported to CBOD.
- Include an “audit tips” section in the Director’s message that is published and distributed.
- Develop audit customer service surveys to obtain feedback and potential improvement opportunities. Use this feedback to make changes in the audit process when feasible.
- Develop a “best practices” document that lists “model” processes or documentation methods used by organizations. Work with CBOD’s education staff to provide the information to organizations.

### **Question 3: How can we improve audit transparency?**

The current audit process is not always clear to auditees. This can contribute to audit delays, misunderstanding of documents being requested and anxiety. This can also contribute to low perceptions of the audit function.

The current audit process includes notifying an organization that they are scheduled for audit, providing a list of documents required to be provided and asking them to complete a questionnaire. The entrance conference is a face-to-face meeting that discusses the high-level audit process, estimated milestones, a review of the available documents and signing of documentation receipt. There may also be telephone conversations and email communications to clarify questions that the auditee or auditor may have.

The draft audit report then lists the audit components and results. A face-to-face exit conference is then held to discuss the audit report and return documents provided during the audit.

#### **Recommendation:**

Revise audit processes to issue an audit notification letter at least six months in advance of the scheduled audit. The announcement letter should provide details of the audit process, the audit timing and required documents. Follow-up with an engagement letter that defines roles and responsibilities. Hold an entrance conference via conference call to clarify the audit process and expectations.

### **Question 4: What audit processes can be enhanced or eliminated?**

Each audit is manually intensive and conducted based on submitted documents. The audits do not incorporate game operations’ observations, cash handling observations, physical inventory counts, internal control observations and face-to-face interviews with Chairperson, hall operators, charity point of contacts, bookkeepers and bingo workers. Additionally, organizations are not required to submit electronic records to facilitate the audit process and data analysis.

Some Administrative Rules and audit procedures are based on old business environments and technologies. One example is the requirement for the auditor to verify check endorsements yet most banks only provide copies of the front of checks.

#### **Recommendation:**

Obtain data analytics software to facilitate the data analysis and identify potential anomalies. Require license holders to submit documentation and records electronically in advance of the audit’s on-site activities.

Review administrative rules to determine required revisions, repeal or additions based on the current business environment and available technologies.



**Question 5: How can the audit procedures be organized to be more efficient?**

CBOD's audit procedures are comprehensive and sound. However, the working paper flow is based on audit objectives instead of being compartmentalized and self-contained into subject areas. The current working paper flow causes that auditor to not be in a position to finalize a workpaper for review until the bulk of the audit is finished because source documents are used and tested in more than one section of the working paper template.

*Recommendation:*

Organize the working paper audit steps into the following self-contained components to minimize overlap.

1. Bank
2. Cash/Revenues
3. Expenses
4. Inventory

5. Distributions
6. Reconciliations
7. Sampling

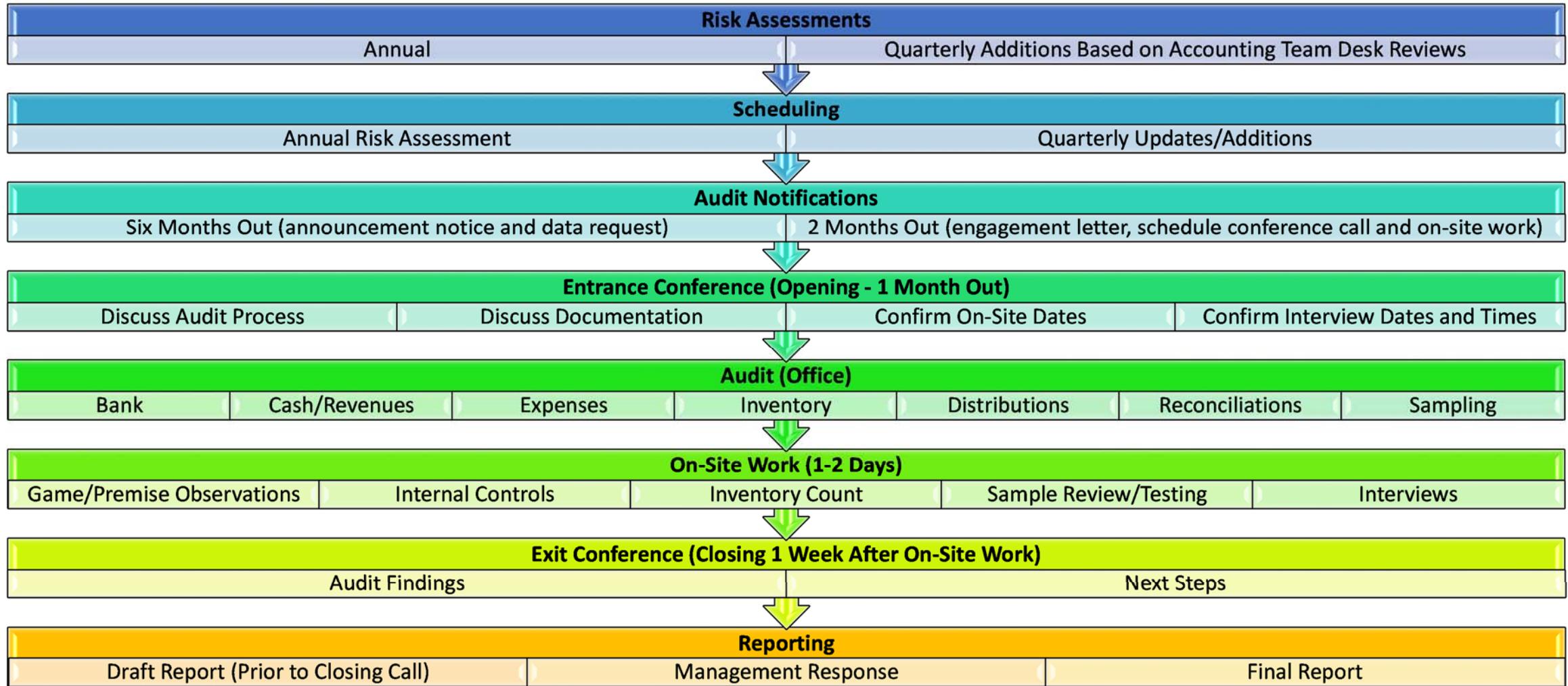
**Question 6: Is the Audit Services Department appropriately staffed?**

CBOD's Audit Services Department is not optimally staffed to improve audit completion times and efficiencies. Additionally, there is no career progression opportunities to attract and retain qualified staff.

*Recommendation:*

Refine the CBOD Audit Services staffing model to reflect revised audit processes, redefine staff roles and responsibilities and add a Sr. Lead/scheduler and Sr. auditor positions.

**Figure 2** provides a graphical overview of the proposed Bingo Audit Services process flow.



**Figure 2 Proposed CBOD Audit Services Department Audit Process** *Implementing streamlined processes, changing the audit progression steps and enhancing communications should result in shorter audit completion times and value added audits.*



# Project Plan

The project plan below represents high level activities that should be undertaken to improve CBOD's Audit Services processes. As previously stated, incorporating organizational change management concepts and principals into implementing these recommendations is crucial to the acceptance of changes and long-term success.

#	Description
<b>1</b>	<b>Staffing</b>
1a	Determine staffing model based on revised processes
1b	Obtain authorization for revised and new position
1c	Develop job descriptions for revised and new positions
1d	Phase-in job assignments based on new processes and location needs
<b>2</b>	<b>Mission Statement</b>
2a	Develop a Bingo Audit Services mission statement promotes value added services and customer sensitivities
2b	Communicate Bingo Audit Services mission statement to all stakeholders
<b>3</b>	<b>Administrative Rules</b>
3a	Determine which Administrative Rules need revision as a result of revised audit processes
3b	Determine which Administrative Rules may be eliminated as a result of revised audit processes
3c	Determine any new Administrative Rules that may be needed as a result of revised audit processes
3d	Complete the Administrative Rule revision and adoption processes
<b>4</b>	<b>Risk Assessment</b>
4a	Revise annual risk assessment factors & weights
4b	Develop quarterly risk assessment factors & weights
4c	Update BOSS with revised risk assessment factors & weights
4d	Test revised BOSS risk assessment factors & weights
4e	Implement revised risk assessment factors & weights



#	Description
<b>5</b>	<b>Document/Form/Work Paper</b>
5a	Revise planning memo template
5b	Develop audit announcement letter template
5c	Develop audit engagement letter template
5d	Revise internal control questionnaire
5e	Revise workpapers to be self-contained in new modules and update for process changes
5e1	Bank
5e2	Cash/Revenues
5e3	Expenses
5e4	Inventory
5e5	Distributions
5e6	Reconciliations
5e7	Sampling
5e8	Reconciliations
5e9	Findings Summary
5f	Develop opening conference call template
5g	Develop closing conference call template
5h	Revise audit report template
5i	Update audit services procedures manual to reflect revised processes and forms
<b>6</b>	<b>Scheduling</b>
6a	Develop annual master calendar
6b	Develop written procedures for scheduling audit activities
6c	Develop tracking tool for monitoring audit scheduling, planning, execution and reporting progression including documents submitted by organizations
6d	Implement revised scheduling process
6e	Schedule audits identified on annual risk assessment



#	Description
6f	Schedule audits identified through quarterly report assessments
6g	Schedule audits requested by CBOD director
6h	Implement audit progression tracking tool
<b>7</b>	<b>Automation</b>
7a	Acquire data analytics software
7b	Acquire data analytics software training for all audit and accounting staff
7c	Develop scripts to automate key analysis
7d	Implement data analytics into the quarterly risk assessments
7e	Implement data analytics into the audit processes
<b>8</b>	<b>Training</b>
8a	Develop training materials for revised audit processes
8a1	Data analytics
8a2	Risk assessment
8a3	Scheduling
8a4	Planning
8a5	Notifications
8a6	Audit steps & documentation
8a7	Reports (draft and final)
8a8	Communications
8a9	Follow-up
<b>9</b>	<b>Continuous Improvement</b>
9a	Develop metrics to monitor and measure Bingo Audit Services efficiencies and effectiveness
9b	Establish process to review audit processes and templates on an annual basis then update accordingly.