



**TEXAS LOTTERY
COMMISSION**



**An Internal Audit of
Retail Management Processes**

April 20, 2017

Report #17-005



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 retailer management processes. We conducted this audit in accordance with generally accepted government auditing standards (GAGAS). 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 observations and conclusions based on our audit objectives.

Pertinent information has not been omitted from this report. This report summarizes the audit objective and scope, our assessment based on our audit objectives and the audit approach.

Objectives and Scope

The purpose of this audit is to review business processes and internal controls related to the Texas Lottery Commission’s (TLC) retailer management processes to determine if management controls are in place to achieve business objectives and comply with Texas Lottery Commission’s policy and procedures, Legislative Statutes and Administrative Rules. Internal Audit examined the following business processes during the audit process:

1. Retailer Recruitment
2. Retailer Application & Licensing
3. Licensed Retailer and Sales Agent Training
4. Licensed Retailer Monitoring
5. Retailer License Terminations
6. Consumer Complaints

Internal controls over retailer management activities are effective and working as intended.

The audit scope of the audit was September 1, 2015 through November 30, 2016. The review of the internal control environment required documentary evidence from the current period for assurance on process efficiency.

Results and Conclusions:

The internal controls governing retailer management are effective and working as intended to achieve the business objectives and compliance with regulatory requirements. Our audit work identified no reportable findings.

Acknowledgement:

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



Executive Summary

This section of our report provides a summary of TLC’s retailer management business objectives, risks, management controls and our assessment of internal controls based on audit procedures. We noted that the Texas Lottery Commission’s internal controls for key processes related to retailer management activities are effective and working as intended. A graphic of the high level retailer management functions is shown below.





The following tables describe TLC’s key retailer management business processes and controls.

BUSINESS OBJECTIVE 1: Lottery Operator and Licensed Retailer Performance Expectations	
Business Objective	Performance expectations and requirements for licensed lottery product retailers, TLC support staff and the TLC’s lottery operator are clearly defined and communicated. Risk-based policies, procedures and supporting documentation ensure licensed lottery product retailers, TLC support staff and TLC’s lottery operator understand TLC’s standards, code of ethics, roles, and responsibilities.
Business Risk	Licensed lottery product retailers, TLC support staff and TLC’s lottery operator sales representatives do not understand or perform their business operations according to TLC standards.
Management Controls	<ul style="list-style-type: none"> ➤ TLC management guides the licensed lottery product retailers, TLC staff and TLC’s lottery operator with risk-based policies, procedures, and supporting documentation. These policies, procedures and documentation ensure awareness of TLC’s standards, their respective roles and responsibilities. ➤ Key documents are located on TLC’s website for easy access.
Control Tests	<ul style="list-style-type: none"> ➤ Conducted interviews. ➤ Reviewed statutes relating to lottery product retailer management. ➤ Reviewed policy and procedures. ➤ Reviewed training topic approvals and training documentation.
Control Environment	TLC controls to ensure compliance, communication of standards, code of ethics and policies are effective.
Recommended Actions	None
Management Action Plan	None Required



BUSINESS OBJECTIVE 2: Lottery Operator Roles and Responsibilities

Business Objective	<p>The Texas Lottery Commission strategically determines retailer management roles and responsibilities between TLC and their lottery operator.</p> <p>The Texas Lottery Commission has a comprehensive and documented understanding of the activities performed by their lottery operator as it pertains to retailer management responsibilities.</p>
Business Risk	<p>The Texas Lottery Commission’s strategic planning process does not formally evaluate the cost/benefit and risks associated with sourcing key tasks to third party vendors. This may also cause a risk of over reliance on the third party lottery operator.</p>
Management Controls	<ul style="list-style-type: none"> ➤ TLC contracts with an independent vendor to review adherence with TLC’s lottery operator contract requirements and the memorandum of understanding (MOU). ➤ TLC staff have a comprehensive understanding of the key processes performed by the TLC’s lottery operator as it pertains to retailer management and services. ➤ TLC’s contract with their lottery operator clearly defines each entities’ roles and responsibilities.
Control Tests	<ul style="list-style-type: none"> ➤ Conducted interviews. ➤ Performed audit testing. ➤ Reviewed third party monitoring reports. ➤ Analyzed applicable documentation.
Control Environment	<p>The control environment assuring a risk-based approach to using a third party vendor to complete retailer management services is effective.</p>
Recommended Actions	<p>None</p>
Management Action Plan	<p>None Required</p>



BUSINESS OBJECTIVE 3: Retailer Recruitment Activity

Business Objective	Texas Lottery Commission establishes and monitors their lottery operator’s sale representative recruitment goals and activities.
Business Risk	TLC’s lottery operator is not provided key performance indicators to ensure quality recruitment activities are performed.
Management Controls	<ul style="list-style-type: none"> ➤ TLC develops an annual business plan, which documents and promotes the fiscal year’s retailer recruitment goals. ➤ TLC’s lottery operator provides monthly reporting on retailer recruitment activities. ➤ An agreement between TLC and their lottery operator ensures that retailer recruitment incentives are not paid.
Control Tests	<ul style="list-style-type: none"> ➤ Conducted interviews. ➤ Performed audit testing. ➤ Analyzed applicable documentation.
Control Environment	Controls used to manage TLC’s lottery operator’s recruitment activities are effective.
Recommended Actions	None
Management Action Plan	None Required



BUSINESS OBJECTIVE 4: Retailer License Requirements Communication

Business Objective	Texas Lottery Commission ensures the requirements to become a licensed retailer are transparent and communicated to all potential retailers.
Business Risk	Retailers are not aware of the requirements to become a licensed retailer to sell lottery products.
Management Controls	<ul style="list-style-type: none"> ➤ Licensing documentation provided to retailers is clear on TLC’s standards and requirements. ➤ Licensing documentation complies with state statute and are accessible to potential retailers.
Control Tests	<ul style="list-style-type: none"> ➤ Conducted interviews. ➤ Performed audit testing. ➤ Analyzed applicable documentation.
Control Environment	Texas Lottery Commission’s control environment ensuring potential retailers understand the requirements to become a licensed retailer are effective.
Recommended Actions	None
Management Action Plan	None Required



BUSINESS OBJECTIVE 5: Retailer License Application and Renewal Process

Business Objective	The retailer license application and renewal processes has a strong internal control environment to ensure compliance with statute and TLC policies. (Approvals, Monitoring, Segregation of Duties and Efficiency).
Business Risk	TLC’s retailer license application policies and processes do not ensure compliance and consistency of retailers representing the Texas Lottery Commission in selling lottery products.
Management Controls	<ul style="list-style-type: none"> ➤ State Statute governed the retailer license application development process. ➤ TLC documents retailer information, background checks and license decision-making using the designated information system. ➤ TLC has documented key roles and responsibilities within the licensing process to ensure adequate segregation of duties.
Control Tests	<ul style="list-style-type: none"> ➤ Conducted interviews. ➤ Performed audit testing. ➤ Analyzed applicable documentation.
Control Environment	The controls governing the retailer license application process are effective.
Recommended Actions	None
Management Action Plan	None Required



BUSINESS OBJECTIVE 6: Retailer Training

Business Objective	Risk-based training programs are developed to ensure licensed lottery product retailers and TLC’s lottery operator sales representatives maintain TLC’s established standards and product knowledge.
Business Risk	Licensed lottery product retailers and TLC’s lottery operator sales representatives training does not provide the information needed to ensure compliance with TLC standards, expectations and lottery product knowledge.
Management Controls	<ul style="list-style-type: none"> ➤ TLC staff develops and approves training materials used for licensed lottery product retailers and TLC lottery operator sales representatives. ➤ TLC tracks retailer-training activities using work orders in the designated information system to ensure completion, efficiency and documentation. ➤ Agreements between TLC and their lottery operator ensure training is provided within 14 days of the retailer license approval. The training activities are reported to TLC. Additionally, mechanisms are in place to issue sanctions against TLC’s lottery operator when training is not provided within established time frames. ➤ TLC conducts training on new programs or program changes. ➤ TLC’s lottery operator ensures lottery sales representatives receive onboard training which is reported to TLC.
Control Tests	<ul style="list-style-type: none"> ➤ Conducted interviews. ➤ Performed audit testing. ➤ Reviewed training topic approvals and training documentation. ➤ Analyzed applicable documentation.
Control Environment	The control environment supporting training activities for licensed lottery product retailers and the lottery operator’s sales representatives is effective.
Recommended Actions	None
Management Action Plan	None Required



BUSINESS OBJECTIVE 7: Licensed Lottery Product Retailer Monitoring

Business Objective	Texas Lottery Commission has established reporting and other monitoring activities to ensure licensed lottery product retailers and TLC’s lottery operator are meeting expectations and high standards.
Business Risk	TLC’s monitoring activities do not support the agencies internal control environment.
Management Controls	<ul style="list-style-type: none"> ➤ TLC uses the designated information system to record and monitor licensed lottery product retailer service activities. ➤ TLC’s lottery operator provides TLC with reporting to monitor licensed lottery product retailer sales activities and to certify incentive programs. ➤ TLC has developed processes for licensed lottery product retailers to voice concerns with the services provided by the lottery operator. ➤ TLC uses an internal complaint information system to track consumer complaints and other key retailer issues.
Control Tests	<ul style="list-style-type: none"> ➤ Conducted interviews. ➤ Performed audit testing. ➤ Analyzed applicable documentation.
Control Environment	TLC’s controls associated with licensed lottery product retailer activities, incentive programs, customer service and work order completion are effective.
Recommended Actions	None
Management Action Plan	None Required



BUSINESS OBJECTIVE 8: Retailer License Termination Criteria and Process

Business Objective	The retailer license termination criteria and process is transparent to licensed lottery product retailers and is effective in preventing terminated retailers from selling lottery products.
Business Risk	License termination criteria and processes is not clear and retailers continue to sell lottery products with a terminated license.
Management Controls	<ul style="list-style-type: none"> ➤ TLC uses an internal complaint system to track and monitor retailer violations that can result in terminations. ➤ The Enforcement Division conducts investigations separately from retailer services. ➤ Retailer license termination processes follow state statute requirements. ➤ Final retailer license termination communication is provided to the lottery operator to ensure removal of all lottery product point of sale equipment. ➤ Work orders are opened and tracked in the designated information system to ensure lottery product equipment and marketing materials removal.
Control Tests	<ul style="list-style-type: none"> ➤ Conducted interviews. ➤ Performed audit testing. ➤ Analyzed applicable documentation.
Control Environment	The control environment for retailer license terminations and prevention of lottery product sales is effective and transparent.
Recommended Actions	None
Management Action Plan	None Required



BUSINESS OBJECTIVE 9: Consumer Complaints

Business Objective	Texas Lottery Commission ensures consumer complaints are documented, reviewed and followed-up on in a timely manner.
Business Risk	Processes for addressing consumer complaints is not effective and results in reputational and financial loss to the state.
Management Controls	<ul style="list-style-type: none"> ➤ The customer and retailer complaint process is transparent to the public. ➤ TLC’s internal complaint system monitors and tracks consumer complaints received. ➤ TLC’s policy and procedures for retailers are clear on the consumer complaint process. ➤ TLC established multiple methods for consumers and the public to submit complaints.
Control Tests	<ul style="list-style-type: none"> ➤ Conducted interviews. ➤ Performed audit testing. ➤ Analyzed applicable documentation.
Control Environment	The control environment governing consumer complaints is effective.
Recommended Actions	None
Management Action Plan	None Required



Retailer Management Processes Internal Control Environment

The Texas Lottery Commission developed and instituted many internal controls to ensure that the retailer recruiting, licensing and monitoring processes align with the Agency’s mission and comply with state statutes. The chart below reflects these key controls and the respective control rating based on audit procedures applied.

Internal Controls Practices	Rating
Risk-based policy, procedures and retailer support documentation exists and are accessible.	★
Texas Lottery Commission’s management of retailers is compliant with State Statute.	★
Documentation used for retailer training and marketing provided by TLC’s lottery operator sales representatives is created, reviewed and approved by the Texas Lottery Commission.	★
The Texas Lottery Commission ensures training for retailers and their lottery operator’s sales representatives is reflective of TLC standards, code of ethics and compliance initiatives.	★
Licensed retailers must complete training prior to the sale of lottery products and receive updated training as products and incentive programs change.	★
Retailer recruitment goals are transparent and communicated to the Texas Lottery Commission’s lottery operator.	★
Texas Lottery Commission manages and monitors their lottery operator’s retailer recruitment activities.	★
The Texas Lottery Commission manages, monitors and defines roles and responsibilities within the retailer license application process.	★
TLC’s lottery operator provides sales activity data, which supports the oversight activities to ensure consistent business practices and fair payouts on incentive programs.	★
The Texas Lottery Commission monitors their lottery operator’s sales representative’s service activities for retailers through surveys, reporting and effective agreements.	★
Management of vendor performance is monitored and documented.	★
The Texas Lottery Commission ensure retailers are aware of the activities resulting in suspension of licenses.	★
The Texas Lottery Commission has developed controls to ensure terminated licensed retailers cannot sell lottery product.	★



Internal Controls Practices	Rating
Effective investigation and reporting process controls support the management of consumer complaints.	

Legend:



Adequate



Improvement Recommended



Not Adequate

