

CALIFORNIA STATE LOTTERY

Review Report

OFFICE REVOLVING FUND AND TRAVEL EXPENSES FOLLOW-UP

May 1, 2019, through October 31, 2020



BETTY T. YEE
California State Controller

June 2021



BETTY T. YEE
California State Controller

June 10, 2021

Alva Vernon Johnson, Director
California State Lottery
700 North Tenth Street
Sacramento, CA 95811

Dear Mr. Johnson:

The State Controller's Office conducted a review of the California State Lottery's (Lottery) Office Revolving Fund and travel expenses to determine the adequacy of the Lottery's implementation of corrective actions related to the findings in our prior audit report, issued April 9, 2019. The period for this review was May 1, 2019, through October 31, 2020.

Our review found that the Lottery fully implemented corrective actions for Findings 3, 5, 8, and 11; and that corrective actions to address the recommendations are still in progress for Findings 1, 2, 4, 6, 7, 9, and 10. The Lottery is recovering overpayments, addressing Lottery retailer training, and updating its procurement process. We will follow up on the in-progress corrective actions in a future engagement.

If you have any questions, please contact Andrew Finlayson, Bureau Chief, Division of Audits, by telephone at (916) 324-6310 or by email at afinlayson@sco.ca.gov.

Sincerely,

Original signed by

KIMBERLY TARVIN, CPA
Chief, Division of Audits

KT/as

cc: Gregory Ahern, Chair

California State Lottery Commission

Nathaniel Kirtman III, Commissioner

California State Lottery Commission

Keetha Mills, Commissioner

California State Lottery Commission

Peter Stern, Commissioner

California State Lottery Commission

Harjinder Chima, Chief Deputy Director

California State Lottery

Nicholas Buchen, Deputy Director, Finance Division

California State Lottery

Sharon Allen, Deputy Director, Sales and Marketing Division

California State Lottery

Tiffany Donohue, Deputy Director, Operations Division

California State Lottery

Vincent Espinosa, Chief Enterprise Risk Officer, Executive Division

California State Lottery

Fernando Aceves, Chief Counsel, Legal Services, Executive Division

California State Lottery

Christopher Fernandez, Deputy Director, Human Resources Division

California State Lottery

Sara Sheikholislam, Deputy Director, Internal Audits, Executive Division

California State Lottery

James Shannon, Audit Manager, Internal Audits, Executive Division

California State Lottery

Contents

Review Report

Summary	1
Background	1
Objective, Scope, and Methodology	2
Conclusion	3
Views of Responsible Officials	3
Restricted Use	3
Schedule—Summary of Corrective Action Plan Follow-Up	4

Review Report

Summary

The State Controller's Office (SCO) conducted a review of the California State Lottery's (Lottery) Office Revolving Fund (ORF) and travel expenses to determine the adequacy of the Lottery's implementation of corrective actions related to the findings in our prior audit report, issued April 9, 2019. The period for this review was May 1, 2019, through October 31, 2020.

Our review found that the Lottery fully implemented corrective actions for Findings 3, 5, 8, and 11; and that corrective actions to address the recommendations are still in progress for Findings 1, 2, 4, 6, 7, 9, and 10. The Lottery is recovering overpayments, addressing Lottery retailer training, and updating its procurement process. See the Schedule for details on the status of each corrective action to address the 11 findings in the April 9, 2019 audit report. We will follow up on the in-progress corrective actions in a future engagement.

Background

On November 6, 1984, California voters passed Proposition 37, the California State Lottery Act of 1984 (Lottery Act), which authorized the creation of a state-operated lottery. The Lottery Act is found in Chapter 12.5, section 8880 et seq., of the Government Code. The Lottery Act created the California State Lottery Commission (Commission) and gave it broad powers to oversee the Lottery's operations. The purpose of the Lottery Act is to provide supplemental money to benefit public education without the imposition of additional or increased taxes.

The Lottery has eight divisions: Executive, Finance, Human Resources, Operations, Public Affairs and Communications, Security and Law Enforcement, Information Technology Services, and Sales and Marketing. As of February 1, 2021, the Lottery has 917 budgeted positions; staff are located at Lottery Headquarters, two distribution centers, and nine district offices.

On April 9, 2019, the SCO issued an audit report on the Lottery's ORF and travel expenses for the period of July 1, 2014, through June 30, 2018. The audit identified 11 findings and recommended that the Lottery develop a detailed corrective action plan to address the findings. The SCO conducted this review to follow up on the Lottery's corrective action plan.

Lottery Office Revolving Fund

The ORF is used to draw funds for payment of compensation earned, travel expenses, travel advances, or where immediate payment is otherwise necessary. The Lottery's Finance Division is responsible for processing payments and ensuring that the ORF is replenished in a timely manner. Payments that do not meet the criteria for the ORF must go through the regular claim schedule process.

California Automated Travel Expense Reimbursement System

The Lottery uses the California Automated Travel Expense Reimbursement System (CalATERS). CalATERS is a web-based application used by agencies to process travel advances and expense reimbursements. Travel advances are still paid through the Lottery's ORF, while expense reimbursements are issued by the SCO.

Pursuant to Government Code (GC) section 8880.46.6, the SCO may conduct special post-payment audits of the Lottery, as the State Controller deems necessary. The Controller or his/her agents conducting an audit under this chapter shall have access and authority to examine any and all records of the Commission.

GC section 12410 states, in part:

The Controller shall superintend the fiscal concerns of the state. The Controller shall audit all claims against the state, and may audit the disbursement of any state money, for correctness, legality, and for sufficient provision of law for payment.

In addition, GC section 12411 states that “. . . the Controller shall suggest plans for the improvement and management of revenues.”

Objective, Scope, and Methodology

The objective of our review was to determine whether the Lottery implemented corrective actions to address the findings noted in the April 9, 2019 audit report.

The review period was May 1, 2019, through October 31, 2020.

To achieve our objective, we performed the following:

- Reviewed the Lottery's corrective action plan for the ORF and travel expenses audit;
- Reviewed the State Administrative Manual; the Lottery Act; the Lottery's policies and procedures; California Department of Human Resources (CalHR) rules; collective bargaining agreements; and contracts; as they relate to ORF transactions and travel expenses;
- Reviewed prior audits performed by the Lottery's Internal Audits Office related to the ORF and travel expenses;
- Interviewed the Lottery's Finance Division, Human Resources Division, Operations Division, and Sales and Marketing Division staff members to verify whether corrective actions were implemented;
- Judgmentally selected transactions for testing based on employee, date, and dollar amount to verify whether corrective actions were implemented. We tested:
 - ORF corporate credit card transactions—eight of 29 (\$82,156 of \$477,330);

- ORF individual/employee transactions—six of 65 (\$43,169 of \$85,083);
- CalATERS transactions—50 of 1992 (\$28,130 of \$425,134);
- International Game Technology PLC (IGT) reimbursement transactions—14 of 155 (\$9,909 of \$57,734);
- Employee travel accounts receivables—10 of 78 (\$963 of \$15,713);

This engagement is classified as a review and not an audit; therefore, we did not perform the engagement under generally accepted government auditing standards.

Conclusion

Our review found that the Lottery fully implemented corrective actions for Findings 3, 5, 8, and 11; and that corrective actions to address the recommendations are still in progress for Findings 1, 2, 4, 6, 7, 9, and 10. The Lottery is recovering overpayments, addressing Lottery retailer training, and updating its procurement process. We will follow up on the in-progress corrective actions in a future engagement.

Views of Responsible Officials

We discussed our review results with Lottery representatives at an exit conference held on March 29, 2021. We agreed that the report could be issued as final.

Restricted Use

This report is intended for the information and use of the Lottery, the California Lottery Commission, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record, and is available on the SCO website at www.sco.ca.gov.

Original signed by

KIMBRELY TARVIN, CPA
Chief, Division of Audits

June 10, 2021

Schedule— Summary of Corrective Action Plan Follow-Up

Finding No.	Recommendation	Status	SCO Comments
1. Sales Division management did not implement adequate controls over its operations	<p>We recommend that:</p> <ul style="list-style-type: none"> • The Lottery’s Sales Division management set the tone and lead by example; strong and effective leadership is fundamental to an effective internal control system; and • The Lottery regularly oversee and monitor the activities of the Sales Division to ensure that all applicable policies, procedures, rules, and regulations are being followed. 	In progress	The Sales and Marketing Division is exploring ways to inform and educate Lottery retailers. Due to the COVID-19 pandemic, priority was shifted to maintaining core operations. We will follow up on the status in a future engagement.
2. Inappropriate and/or unnecessary employee travel expenses for Sales Division staff events	<p>We recommend that the Lottery:</p> <ul style="list-style-type: none"> • Establish adequate controls to ensure that travel charges are appropriate and in accordance with CalHR rules; • Recover overpayments from the hotels that made errors on billing invoices; and • Consider recovering payment of unallowable lodging and per diem in accordance with GC section 19838. 	In progress	The Lottery recovered overpayments due to error from hotels to the greatest extent possible, and sent accounts receivable collection letters to individuals who received inappropriate travel reimbursements. As of February 2021, the Lottery has sent second collection letters. Of the total accounts receivable amount of \$15,724, the Lottery has collected \$1,481, and written off \$342. The Lottery intends to pursue the payroll deduction process with its Human Resources Division if the collection letter process is not successful. We will follow up on the status in a future engagement.

Schedule (continued)

Finding No.	Recommendation	Status	SCO Comments
3. Inadequate controls over the processing of travel expense claims (TECs)	<p>We recommend that, to prevent improper TEC payments from recurring, the Lottery:</p> <ul style="list-style-type: none"> • Establish adequate internal controls to ensure that payments for TECs are accurate and comply with collective bargaining agreements and CalHR rules; • Provide training to the Travel Unit staff who process TECs to ensure that they understand the requirements under collective bargaining agreements and CalHR rules; and • Maintain supporting documentation for mileage claims on TECs for future audits. 	Completed	The Lottery implemented corrective actions to address this finding. We verified that the Lottery provided travel training classes for supervisors and managers. In addition, clarification emails were sent regarding personal mileage claims and documentation requirements.
4. Improper food and beverage purchases for IGT-hosted events	<p>We recommend that the Lottery:</p> <ul style="list-style-type: none"> • Establish adequate internal controls to ensure that payments for corporate card charges comply with state law to prevent improper corporate card charges or payments; and • Provide adequate oversight to ensure that accounts payable staff processes only valid and authorized payments that comply with state law. 	In progress	The Lottery is updating its procurement process. Sales conferences and retailer trade shows are currently suspended. We will follow up on the status in a future engagement.
5. Improperly authorized short-term rates for a long-term out-of-class assignment	For future long-term assignments, we recommend that the Lottery comply with the long-term travel provisions set forth in collective bargaining agreements and the <i>CalHR Human Resources Manual</i> .	Completed	The Lottery stated that it will not apply short-term lodging and per diem rates to long-term assignments. The Lottery did not have any employees on long-term assignments during the review period.
6. Inadequate controls over Sales Division vendor purchases	We recommend that the Lottery strengthen its internal controls over the purchase order process and ensure that procurement procedures are followed by each division as well as by Contract Development Services.	In progress	The Sales and Marketing Division did not make any vendor purchases during the review period. The Lottery is updating its procurement process. We will follow up on the status in a future engagement.

Schedule (continued)

Finding No.	Recommendation	Status	SCO Comments
7. Unallowable items purchased for Lottery staff at sales conferences	We recommend that the Lottery adhere to GC section 8880.64 to ensure that Sales Division purchases are necessary and appropriate.	In progress	The Sales and Marketing Division did not make any branded purchases during the review period. The Lottery is updating its procurement process. We will follow up on the status in a future engagement.
8. Misclassification of transportation costs related to sales conferences and retailer trade shows	<p>We recommend that the Lottery:</p> <ul style="list-style-type: none"> • Provide training to staff and implement adequate oversight over the allocation of transportation expenses; and • Monitor expenses on a regular basis to identify any irregularities. 	Completed	The Lottery implemented corrective actions to address this finding. No transportation costs were identified in the Lottery's sales conferences expense account during the review period. All transportation costs reviewed were properly classified.
9. Improperly signed and authorized hotel agreements and costs	<p>We recommend that the Lottery implement:</p> <ul style="list-style-type: none"> • Procedures to ensure that the appropriate individual signs contracts, including hotel agreements; and • A review and approval procedure for when actual costs exceed the delegated signatory's authority. 	In progress	No hotel contracts were executed during the review period. The Lottery is updating its procurement process. New procedures will require a justification memo, an estimated budget for all anticipated costs, and the Director's signature on all hotel contracts. We will follow up on the status in a future engagement.

Schedule (continued)

Finding No.	Recommendation	Status	SCO Comments
10. Lack of review over IGT retailer trade show expenses	We recommend that the Lottery adequately review IGT invoices and supporting documentation for any expenses claimed by IGT.	In progress	The Lottery is finalizing procurement guidelines for IGT purchases. No costs by IGT were billed against the \$200,000 reimbursement amount during the review period. The Lottery billed IGT for employee training and travel costs after the ORF and travel expenses audit was completed. During this review, we identified and communicated to the Lottery about additional training costs that could be reimbursed. We will follow up on the status in a future engagement.
11. Excess Lodging Rate Request forms (STD 2554C) were not properly completed and submitted	We recommend that the Lottery: <ul style="list-style-type: none"> • Ensure that STD 255C forms are adequately supported and submitted in a timely manner; and • Ensure that excess lodging requests are approved before execution of agreement. 	Completed	The Lottery implemented corrective actions to address this finding. The Lottery provided training to supervisors and managers regarding excess lodging and the submittal process for Form STD 255C.

**State Controller's Office
Division of Audits
Post Office Box 942850
Sacramento, CA 94250**

<http://www.sco.ca.gov>