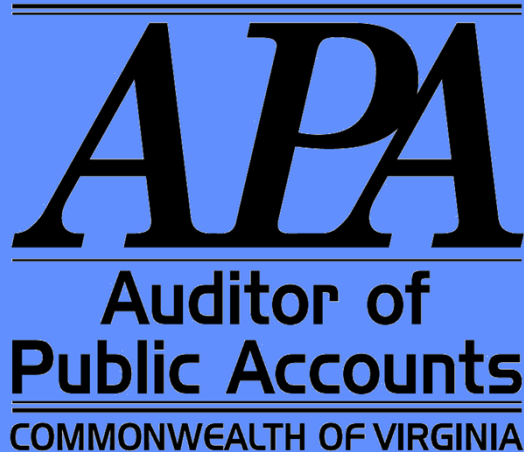


VIRGINIA RACING COMMISSION

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2011**



AUDIT SUMMARY

Our audit of the Virginia Racing Commission for the year ended June 30, 2011, found:

- proper recording and reporting of all transactions, in all material respects, in the Commonwealth Accounting and Reporting System;
- a matter involving internal control and its operations necessary to bring to management's attention; and
- no instances of noncompliance with applicable laws and regulations or other matters that are required to be reported.

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AUDIT FINDING AND RECOMMENDATION

Use Supported Database Software

The Commission is using an unsupported version of the Oracle database system software for its central licensing, veterinary records management, and financial management applications. Industry best practices require that the information system software that supports agencies' essential business functions should be a version that the vendor currently supports and maintains. The impact of not having currently supported systems software places the Commission's information systems at risk for data breach and exposure, loss of availability, and loss of data integrity.

We found that although the current database software is unsupported, the Commission has designed manual processes in the event their application becomes unavailable. The database does hold sensitive information, however there are other controls mitigating the risk of loss of this sensitive information. These controls include physical security at the Commonwealth Enterprise Solutions center where the Commission's servers are housed; logical access control within the Commonwealth of Virginia network; and network and server activity monitoring performed by the Commonwealth Information Technology Infrastructure Partnership.

The Commission does not comply with the industry best practice and Commonwealth's security standard minimum configuration requirements on their licensing system database. We have communicated the details of these weaknesses to management in a separate document marked Freedom of Information Act Exempt under Section 2.2-3705.2 of the Code of Virginia, due to their sensitivity and description of the security system.

We recognize that the Commission attempted to upgrade this database to a current version of Oracle two years ago and settled the resulting lawsuit with Oracle last year after their unsuccessful upgrade. We further acknowledge that the replacement of the existing applications and database requires funding which is limited. Therefore, recommend the Commission dedicate the necessary resources to ensure that its core information systems are upgraded to a supported database to ensure the continued integrity and availability of its data.

COMMISSION HIGHLIGHTS

The Virginia Racing Commission (Commission) controls and prescribes regulations and conditions for all horse racing with pari-mutuel wagering privileges in the Commonwealth. It licenses horse racetracks and satellite facilities, and ensures that all their employees have valid Commission permits. The Commission also issues permits to anyone associated with horse racing, including horse owners, trainers, jockeys, grooms, veterinarians, and blacksmiths. Pari-mutuel horse racing began in the Commonwealth in September 1997 at Colonial Downs, a privately held racetrack in New Kent County. The Code of Virginia permits up to 10 satellite wagering facilities. Currently, there are ten satellite facilities operated by Colonial Downs, which are located in Alberta, Chesapeake, Hampton, Martinsville, Richmond (four), Scott, and Vinton. The Commission monitors each of these facilities as a part of their regulatory oversight.

ADVANCE DEPOSIT WAGERING

The Code of Virginia Section 59.1-369(5) directs the Racing Commission to collect a licensing fee for any provider wishing to offer advance deposit wagering to its customers. Advance deposit wagering includes online or other electronic forms of wagering on simulcast horse races across the world. The Commission also ensures the licensees who operate in Virginia collect a 10 percent fee on all advance deposit wagers made by Virginia residents. Half of the advance deposit wagers' fee goes to the unlimited licensees, and the other half to the Virginia Harness Horse Association and Virginia Thoroughbred Association. The Commission also collects one percent of the total advance deposit wagers statewide and deposits those funds to the Virginia Breeders Fund.

FINANCIAL SUMMARY

The Code of Virginia directs the distribution of the funds in the horse racing wagering pools. The percentage distribution varies based on factors such as the type of wagering, whether the race took place within or outside of the Commonwealth, and whether the wagering occurred at the racetrack or at a satellite facility. The Commonwealth retains as a license tax a portion of the wagering pools ranging from 0.75 to 2.25 percent as directed by the Code of Virginia. All revenues received by the Commission go to a special fund known as the State Racing Operations Fund. The Appropriations Act requires the Commission to transfer any funds in excess of the Commission's operating expenses to the General Fund of the Commonwealth. However, the Appropriations Act contains language allowing the Commission to carry forward a portion of its unspent appropriation related to the promotion and marketing, sustenance and growth of the Virginia horse industry as long as it makes its required transfer to the General Fund. At June 30, 2011, the Commission had a cash balance of \$33,434 in its operating fund.. The Commission transferred \$577,685 to the General Fund as required by the Appropriations Act and transferred \$13,225 to the Literary Fund.

The Code of Virginia also created the Virginia Breeders Fund to support an incentive program to foster the industry of breeding racehorses in Virginia. It receives a one percent distribution of the horse racing wagering conducted in the Commonwealth. The Commission contracted with the Virginia Thoroughbred Association and the Virginia Harness Horse Association to manage the funds. The incentive program provides purses for races, restricted to Virginia bred or sired horses, and awards to the owners and breeders of Virginia bred horses that win or earn purse money in races designated by the Commission. During fiscal year 2011, the Commission made payments totaling \$1,390,794 from the Breeders Fund consisting of \$1,103,294 in incentives to owners and breeders, and \$287,500 in management fees to the Virginia Thoroughbred Association and the Virginia Harness Horse Association. At year-end, the cash balance in the Breeder's Fund was \$569,994. The cash balance does not revert to the General Fund.

The results of the fiscal year 2011 financial operations of the Virginia Racing Commission are on page three. The total amount wagered on horse racing in the Commonwealth declined again from fiscal year 2010 to 2011, but at a slower rate than in previous fiscal periods. The amount of tax revenue in the operating fund generated from wagering on horse racing was down 9.6 percent from 2010 compared to the 16.8 percent decline in revenue from fiscal years 2009 to 2010. However, Breeders Fund revenue increased 9.1 percent from 2010 compared to the 14.4 percent decline in revenue from fiscal years 2009 to 2010. This is mostly attributable to growth in advance deposit wagering.

VIRGINIA RACING COMMISSION
SCHEDULE OF REVENUES, EXPENSES, AND CHANGES
IN CASH BALANCES - BUDGET AND ACTUAL

For the Twelve Months Ending June 30, 2011

	Budget	Actual			Total Variance
	Total Budget	Breeders Fund	Operations Fund *	Total	Positive/ (Negative)
Revenues:					
Taxes and pari-mutuel wagering	\$ 3,425,000	\$ 1,536,852	\$ 2,023,654	\$ 3,560,506	\$ 135,506
Application fees	180,000	-	189,345	189,345	9,345
Fines and assessments	-	-	13,225	13,225	13,225
Interest	20,000	-	-	-	(20,000)
Total revenues	<u>3,625,000</u>	<u>1,536,852</u>	<u>2,226,224</u>	<u>3,763,076</u>	<u>138,076</u>
Expenses:					
Personal services	914,800	-	788,625	788,625	126,175
Contractual services	469,794	-	415,465	415,465	54,329
Supplies and materials	17,250	-	16,045	16,045	1,205
Incentive and marketing payments	1,789,000	1,390,794	369,156	1,759,951	29,049
Continuous charges	119,800	-	116,113	116,113	3,687
Total expenses:	<u>3,310,644</u>	<u>1,390,794</u>	<u>1,705,404</u>	<u>3,096,199</u>	<u>214,445</u>
Transfers out:					
General fund	571,856	-	577,685	577,685	(5,829)
Literary fund	-	-	13,225	13,225	(13,225)
Total transfers	<u>571,856</u>	<u>-</u>	<u>590,910</u>	<u>590,910</u>	<u>(19,054)</u>
Revenues over (under) expenditures and transfers out	<u>\$ (257,500)</u>	<u>146,058</u>	<u>(70,091)</u>	<u>75,967</u>	<u>\$ 333,467</u>
Cash balance at June 30, 2010		<u>423,936</u>	<u>121,875</u>	<u>545,811</u>	
Transfer to Literary Fund for 2010 Collections		-	(18,350)	(18,350)	
Cash balance at June 30, 2011		<u>\$ 569,994</u>	<u>\$ 33,434</u>	<u>\$ 603,428</u>	

* Operations Fund includes amounts collected and directly deposited to the literary fund, which were transferred out.

Source: Commonwealth Accounting and Reporting System



Commonwealth of Virginia

Auditor of Public Accounts

Walter J. Kucharski
Auditor of Public Accounts

P.O. Box 1295
Richmond, Virginia 23218

October 12, 2011

The Honorable Robert F. McDonnell
Governor of Virginia

The Honorable Charles J. Colgan
Chairman, Joint Legislative Audit
and Review Commission

We have audited the financial records and operations of the **Virginia Racing Commission** for the year ended June 30, 2011. We conducted this performance audit in accordance with generally accepted government auditing standards. 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 findings and conclusions based on our audit objectives.

Audit Objectives

Our audit's primary objectives were to evaluate the accuracy of recorded financial transactions in the Commonwealth Accounting and Reporting System, review the adequacy of the Commission's internal controls, and test compliance with applicable laws and regulations.

Audit Scope and Methodology

The Commission's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

We gained an understanding of the overall internal controls, both automated and manual, sufficient to plan the audit. We considered significance and risk in determining the nature and extent of our audit procedures. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances.

Tax and pari-mutuel wagering revenues
Incentive and marketing payments
License and permit fees

Purchases and Purchase Card Controls
Application Controls
Database Security

We performed audit tests to determine whether the Commission's controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations. Our audit procedures included inquiries of appropriate personnel, and observation of the Commission's operations. We inspected documents including reconciliations, deposit slips and certificates, wagering reports provided by Colonial Downs, revenue summary reports and contracts. We tested transactions and performed analytical procedures.

Conclusions

We found that the Commission properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System. The Commission records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System.

We noted a matter involving internal control and its operation that we consider necessary to be reported to management. This matter is described in the section entitled "Audit Finding and Recommendation." The results of our tests of compliance with applicable laws and regulations disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

Exit Conference and Report Distribution

We discussed this report with management on September 15, 2011 and on October 12, 2011, following the conclusion of our database security review. Management's response to the finding identified in our audit is included in the section titled "Agency Response." We did not audit management's response and, accordingly, we express no opinion on it.

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

AUDITOR OF PUBLIC ACCOUNTS

AWP/alh



COMMONWEALTH of VIRGINIA

Virginia Racing Commission

*10700 Horsemen's Road
New Kent, Virginia 23124
(804) 966-7400; FAX (804) 966-7418*

October 17, 2011

Mr. Walter J. Kucharski
Auditor of Public Accounts
P.O. Box 1295
Richmond, VA 23218

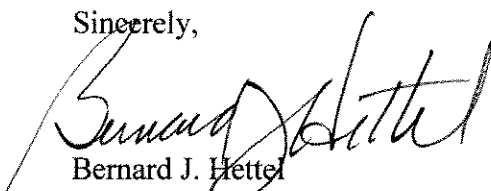
Dear Mr. Kucharski:

I am writing this letter to you in response to the audit finding "Use Supported Database Software" as stated in the report for our FY 2011 audit performed by the Auditor of Public Accounts.

The Virginia Racing Commission (VRC) is a very small agency with limited resources dependant on the business levels of our sole racetrack licensee, Colonial Downs. As noted in the finding, VRC did attempt to upgrade our old database several years ago, but unfortunately due to disagreements with Oracle over the work that was performed, the project was never completed and ended in a lawsuit with Oracle which has since been settled.

VRC is currently in the process of looking at new software that will not only meet our needs but also comply with the Commonwealth's security standard minimum configuration requirements in the future. VRC wants to be prepared so that when our financial position improves, we will possess the knowledge about which licensing system best meets our needs in an effort to expedite the process of purchasing a new database.

Sincerely,


Bernard J. Hettel
Executive Secretary

VIRGINIA RACING COMMISSION

Clinton Miller
Chairman

Mark T. Brown
Vice Chairman

Stuart Siegel
David C. Reynolds
J. Sargeant Reynolds, Jr.

Bernard J. Hettel
Executive Secretary

David Lermond, Jr.
Deputy Executive Secretary