

California Horse Racing Board

2015 SLAA REPORT

December 28, 2015

Alexis Podesta, Acting Secretary
California Business, Consumer Services and Housing Agency
915 Capitol Mall, Suite 350-A
Sacramento, CA 95814

Dear Ms. Podesta,

In accordance with the State Leadership Accountability Act (SLAA), the California Horse Racing Board submits this report on the review of our systems of internal control and monitoring processes for the biennial period ended December 31, 2015.

Should you have any questions please contact Francisco G Gonzalez, Audit Unit Supervisor, at (916) 263-6010, franciscog@chr.ca.gov.

BACKGROUND

The California Horse Racing Board (Board/CHRB) was established in 1933 by constitutional amendment and is overseen by a seven member Board, appointed by the Governor. The CHRB regulates horse racing and pari-mutuel wagering, adopts rules and regulations to protect the public, ensures the safety and health of human and equine participants, promotes horse racing, breeding, and wagering opportunities. The Board directs a statewide staff in the licensure and oversight of all race meetings in the state where pari-mutuel wagering is conducted, as well as off-site simulcast wagering locations and Advance Deposit Wagering (ADW) companies. As a Special Fund department, the CHRB's revenue is principally derived from the horse racing industry. General Fund revenue is derived from occupational license fees collected and from fines imposed for violations of the Board's horse racing rules and regulations.

RISK ASSESSMENT PROCESS

The CHRB SLAA monitor requested the CHRB management team:

- Identify relevant risks within their units
- Determine the nature of the risk, where the risk originates, and the impact of the risk to the CHRB
- Determine the likelihood of the risk occurring and how and why the risks affect the CHRB
- Provide a description of control(s) in place to address identified risks and how the control(s) help to mitigate these risks
- Indicate whether the control(s) is new or existing

The SLAA monitor used the Risk Aggregation Worksheet to solicit input from the CHRB management team.

EVALUATION OF RISKS AND CONTROLS

Compliance- Internal- Staff Not Adhering to Policies, Procedures, or Standards

The Generally Accepted Auditing Standards require audit shops to have a system of quality control and assurance which includes an external peer review at least once every three years. For an audit report to be valid it must be executed following Generally Accepted Auditing Standards. When conducting internal audits government auditors follow the International Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors. For external audits government auditors follow the Government Auditing Standards issues by the Comptroller General of the United States. Not

participating in external peer review prevents staff auditors from citing Generally Accepted Auditing Standards in their audit reports, which lessens audit report credibility, which is a risk the CHRB must avoid as the oversight body for the racing industry.

Initiate participation in the California Association of State Auditors (CASA) peer review process.

Operations- Internal- Staff—Key Person Dependence, Succession Planning

The policy and regulations unit provides a substantial volume of data necessary for commissioners to evaluate during publically noticed monthly board meetings. Examples include regulatory changes to strengthen enforcement procedures; to distinguish and clarify medication violations that impact equine race day medications; the production of regulatory material for statutorily required public comment affording the industry a voice for their concerns. The estimated time period necessary to train policy and regulation analysts can be excessive, creating a work production risk that can impact regulatory enforcement.

Procedures should be established to address staff retention to create an upward mobility path for Policy and Regulation unit employees. The path could begin at the Licensing Technician level, and continue to the Staff Services Analyst (SSA) series. Seasoned Licensing Technicians are excellent candidates, equipped with industry knowledge to become Staff Services Analysts in the Policy and Regulation unit. An identified upward mobility path has the potential to increase staff retention and reduces the new hire subject matter learning curve.

Operations- Internal- Physical Resources—Maintenance, Upgrades, Replacements, Security

Improving the secure storage of existing licensing fees collected during the summer fair season will minimize the risk of loss, further protect the state's share of revenue collected, and improve overall office safety for state assets.

The CHRB will install locking storage cabinets, and replace cabinet locks at the beginning of each fair season, to improve money box security, and improve the protection of state assets.

Operations- Internal- Technology—Inadequate Support, Tools, Design, or Maintenance

CHRB Information technology must be vigilant in its security defense measures in an ever evolving technological environment. CHRB IT recognizes that a review process at planned intervals needs to be implemented to ensure the continuing suitability and effectiveness of the department's approach to managing information security. If the CHRB IT environment remains stagnant, the department runs the risk of malicious system access.

CHRB will implement specialized scanning tools and techniques that evaluate information technology configuration, patches, and services for known vulnerabilities. Further, CHRB will partner with the Cyber Network Defense Team within the California Military Department, which is managed by the California Coast Guard to schedule a periodic IT risk assessment review process.

Operations- Internal- Technology—Inadequate Support, Tools, Design, or Maintenance

CHRB categorizes electronic data equally without regard for classification of value, legal requirements, or sensitivity. If allowed to continue, CHRB may overstate resources needed. To avoid data collection risks the CHRB needs to assess information efficiently and effectively with respect to business requirements to determine the best use of data security resources. CHRB must establish procedures to classify stored, processed, shared or transmitted data with respect to the type and value to critical business functionality.

As part of the CHRB's system data upgrade (CHRIS 2), CHRB IT will design data security

classifications driven by the CHRB mission statement and critical business functionality.

Operations- Internal- Technology—Inadequate Support, Tools, Design, or Maintenance

In order to avoid the risk of providing unauthorized information technology access rights to users, CHRB IT must partner with key CHRB managers and leaders to establish policies and procedures for identification and authentication to identify roles, responsibilities and compliance standards for individuals requesting system access.

As part of the CHRB's system data upgrade (CHRIS 2), CHRB IT will design data security classifications driven by the CHRB mission statement and critical business functionality.

Operations- Internal- Technology—Inadequate Support, Tools, Design, or Maintenance

CHRB IT recognizes that a well prepared IT Unit is proactive and prevents users from being affected by IT threats. The CHRB IT Unit runs the risk of user dissatisfaction and loss of customer confidence without adequate information technology support, should technological events occur impacting critical business functions. The CHRB needs to develop security alerts and regular advisories to notify the appropriate staff of actions in response to alerts. In addition, the CHRB needs to monitor system logging and develop routine procedures to audit logs, security events, system use, system alerts or failures.

As part of the implementation of the virtual server system, CHRB IT will develop and implement monitoring procedures and tools into the system domain. CHRB will develop an Event Management service continuity process, supported by automated Event Management software.

Operations- Internal- Staff—Training, Knowledge, Competence

CHRB IT recognizes that some of its practices may be out of compliance with best computing practices detailed in the State Administrative Manual. To alleviate this issue, the CHRB needs to establish annual department-wide security and system training to address acceptable use and good computing practices for authorized user access.

CHRB will provide periodic user surveys and Computer Based Training (CBTs) to help manage user security awareness.

Operations- Internal- Technology—Outdated, Incompatible

CHRB needs to continue to eliminate aged security software technology that cannot be vendor supported. CHRB's outdated technology is not properly supported and thus places the CHRB at risk of unauthorized access and hacking.

CHRB IT will create formal policy documents and formal processes to provide security oversight details and controls necessary to meet and maintain optimum information technology security and provide written protocol regarding software replacement.

Operations- Internal- Technology—Outdated, Incompatible

The CHRB currently lacks systems and applications to verify data inputs with accuracy, completeness and validation. Without controls in place to enhance data integrity the data generated and stored is at risk of being deemed unreliable.

As part of the CHRB's system data upgrade (CHRIS 2), cross-referenced data entry and validation will be incorporated in the form of 'drop-down,' 'type-ahead,' options.

ONGOING MONITORING

Through our ongoing monitoring processes, the California Horse Racing Board reviews, evaluates, and improves our systems of internal controls and monitoring processes. The California Horse Racing Board is in the process of formalizing and documenting our ongoing monitoring and as such, we have determined we partially comply with California Government Code sections 13400-13407.

Roles and Responsibilities

As the head of California Horse Racing Board, Rick Baedeker, Executive Director, is responsible for the overall establishment and maintenance of the internal control system. We have identified Jacqueline Wagner, Assistant Executive Director, as our designated agency monitor(s).

Frequency of Monitoring Activities

The CHRB will conduct on-going monitoring through quarterly management meetings. Managers will be required to revisit their areas of responsibility and evaluate new and existing risks. The on-going monitoring meetings will take place during the executive management meetings. In addition, the Audit Unit through separate evaluations will bring to the attention of the Executive Director the result of audits conducted where risk areas are discovered.

Reporting and Documenting Monitoring Activities

During quarterly monitoring meetings the SLAA monitor will make available to CHRB managers a blank Risk Assessment Matrix worksheet to complete. After the Risk Assessment Matrix gets completed the SLAA monitor will facilitate with management the completion of the Risk Aggregation Worksheet. Results of the on-going monitoring will be kept in a file and the SLAA monitor will follow up with managers to determine whether controls addressing risks were fully implemented. The SLAA monitor will continue to follow up on controls not fully implemented and will bring to the attention of the Executive Director the controls that are not fully implemented and if applicable the risks will be included in the following biennial SLAA Report.

Procedure for Addressing Identified Internal Control Deficiencies

The manager responsible for the area in which risk(s) are identified will be responsible for the development of a plan to mitigate the risk(s). The manager will have thirty days to develop the plan. The plan will be shared with the Executive Director and the SLAA monitor. Once the Executive Director approves the plan the manager will have sixty days to implement the plan. The approved plan will be shared with the Audit Unit. The Audit Unit will test controls at the direction of the Executive Director.

CONCLUSION

The California Horse Racing Board strives to reduce the risks inherent in our work through ongoing monitoring. The California Horse Racing Board accepts the responsibility to continuously improve by addressing newly recognized risks and revising risk mitigation strategies. I certify our systems of internal control and monitoring processes are adequate to identify and address material inadequacies or material weaknesses facing the organization.

Rick Baedeker, Executive Director
California Horse Racing Board

cc: Department of Finance

Legislature
State Auditor
State Library
State Controller
Secretary of Government Operations