

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

Dear Ms. Alexis Podesta,

In accordance with the State Leadership Accountability Act (Leadership Accountability), the California Horse Racing Board submits this report on the review of our internal control and monitoring systems for the biennial period ending December 31, 2019.

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

GOVERNANCE

Mission and Strategic Plan

The mission of the California Horse Racing Board (CHRB) is to ensure the integrity, viability, and safety of California's horse racing industry by regulating pari-mutuel wagering for the protection of the public, promoting horse racing, breeding, and wagering opportunities, and fostering safe racing through the development and enforcement of track safety standards and regulations for the health and welfare of all participants.

The CHRB's objectives are:

- Assuring protection of the public.
- Encouraging agriculture and the breeding of horses in this state.
- Providing uniformity of regulation for each type of horse racing.
- Providing for maximum expansion of horse-racing opportunities in the public interest.

Control Environment

The CHRB is a department of the California Business and Consumer Services, and Housing Agency (Agency). The CHRB is directed by a seven-member board appointed by the Governor. The seven-member board (the Board) elects its chairperson and vice chairperson. The chairperson presides over meetings of the Board. The CHRB's oversight body is the Agency Secretary. The Board appoints an executive director to carry out the CHRB's mission and objectives. The Board and the executive director are responsible for establishing and demonstrating integrity and ethical values for the overall organization. The CHRB organizational structure and responsibilities are as follows:

- The executive director is responsible for the department's operations and regulation of the horse racing industry.
- The executive director is supported in this regard by the assistant executive director.
- The Board counsel, the staff counsel, and supervisorial staff at CHRB offices and at all of the

state's racetracks support the executive director in this endeavor.

- The executive and management team plans and oversees the CHRB's budget and directs the department's operational divisions:
 - Administrative Services;
 - Legislation and Regulations;
 - Audits;
 - Licensing;
 - Information Technology; and
 - Enforcement.

The CHRB issues and maintains internal policies and procedures geared towards the achievement of its mission and objectives. The policies are maintained at a centralized location at the headquarters office. In addition, the CHRB operational divisions maintain individual desk manuals for their areas of work.

In 2017, the CHRB implemented its "Workforce Plan" and presented an introduction of its "Succession Plan." In 2018, the CHRB combined the Workforce Plan and Succession Plan (the Plan) to better suit the Board. In 2018, the Plan was updated to ensure that the CHRB continued to meet its core mission, through the recruitment and retention of a qualified workforce. Currently the Plan serves as a guide and action planning tool to support the CHRB's effort to maintain a competent workforce. As with many other state agencies, the CHRB is facing an aging workforce and is at risk of losing specialized knowledge from its experienced workforce. The data demonstrates that a large number of CHRB staff is at retirement age. In response to this finding, the CHRB developed a strategy to close competency gaps within the department. The strategy is as follows:

- Reinforce the importance and increase the overall use of the Individual Development Plan for all CHRB employees.
- Ensure managers and supervisors attend leadership development training courses on a regular basis.
- Develop training/knowledge share sessions at all staff meetings to address competency gaps within the candidate pool.
- Continually update desk manuals and provide them to new staff as a guide and training tool.

The executive director reports to both the Board and Agency and seeks direction from the Board and Agency on highly controversial and sensitive matters affecting the CHRB. The Board has the ultimate authority to direct the CHRB activities through its executive director.

Information and Communication

The CHRB has a process to collect and communicate both internally and externally, quality information needed to achieve its mission and objectives.

The executive director presents a status report to the Board and the public at the monthly regular Board meeting. The status report communicates industry updates, including developments, changes, goals, challenges, and an economic report on the health of the industry.

The CHRB executive staff and managers meet monthly with the executive director to discuss industry changes and issues. During the monthly management meeting supervisors and managers communicate issues, goals, and tasks, affecting their divisions.

Simultaneously, quality information is communicated down, across, and up the organization. Following the management monthly meeting, supervisors and managers conduct division staff meetings to communicate current goals and tasks. In addition, the executive director conducts a monthly staff meeting to communicate directly with staff. At the staff meetings CHRB staff has the opportunity to communicate across and up the organization by having the ability to ask questions and/or share concerns. The monthly staff meeting is made available to all CHRB staff via Skype. Internally, CHRB employees can confidentially report improper activity by contacting the Auditor of the State of California using the Whistleblower Hotline via phone, web, or mail. Externally, industry stakeholders and the general public can report improper activity or concerns to the CHRB by utilizing the CHRB Hotline via phone or email.

MONITORING

The information included here discusses the entity-wide, continuous process to ensure internal control systems are working as intended. The role of the executive monitoring sponsor includes facilitating and verifying that the California Horse Racing Board monitoring practices are implemented and functioning. The responsibilities as the executive monitoring sponsor(s) have been given to:
Susan Bitcon, Chief of Administration.

The CHRB conducts ongoing monitoring of its internal control system. The CHRB executive staff and managers meet monthly to discuss areas of concern, including any necessary operational improvements. The executive director, as head of the CHRB, is responsible for the overall establishment and maintenance of the internal control and monitoring systems. With the support of the executive director, supervisors and managers address risk vulnerabilities. The division manager where the vulnerability resides is responsible for identifying and implementing a solution. The manager revisits the implemented solution to determine the efficacy of the solution. During the monthly managers meeting the executive director communicates directly with the Leadership Accountability administrator and CHRB managers regarding progress in the reduction of identified vulnerabilities. Furthermore, the CHRB has a designated executive monitoring sponsor. Responsibilities of the executive monitoring sponsor include facilitating and verifying that the CHRB internal control monitoring practices are implemented and functioning as intended. The Audit Unit also performs separate operational integrity evaluations, and any findings of risk are brought to the attention of the executive director.

RISK ASSESSMENT PROCESS

The following personnel were involved in the California Horse Racing Board risk assessment process: executive management, middle management, and front line management.

The following methods were used to identify risks: brainstorming meetings, ongoing monitoring activities, other/prior risk assessments, and consideration of potential fraud.

The following criteria were used to rank risks: likelihood of occurrence, potential impact to mission/goals/objectives, potential impact of remediation efforts, and tolerance level for the type of risk.

The CHRB SLAA Administrator requested the CHRB management team to:

- Identify relevant risks within their divisions;
- 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 Administrator used the Risk Aggregation Worksheet to solicit input from the CHRB management team.

RISKS AND CONTROLS

Risk: Outdated Reconciliation Procedures

The CHRB has outdated procedures to perform revenue reconciliations. Having outdated procedures can lead to missing revenue. Not accounting for all revenue affects the department's business operations.

Control: Update Reconciliation Procedures

The procedures for revenue reconciliations will be reviewed, evaluated, and updated accordingly. The updated procedures will include language establishing a reconciliation schedule. This is a new control.

Risk: FI\$Cal Implementation

The CHRB is unable to conduct disbursement and budget functions in the FI\$Cal system. The identified functions create risks that affect the day to day operations and causes a "stop" in the workflow. Consequently, those risks further affect the reconciliations function and staff are unable to complete timely reconciliations. Lastly, the identified risks prevent the department from being able to produce financial statements.

Control: FI\$Cal System Training

Job aids and training provide instruction to perform tasks in the FI\$Cal system. This is an existing control; staff will continue using this resource and work closely with the Department of General Services, Contract Fiscal Services to help remedy existing issues.

Control: FI\$Cal System Assistance

The CHRB will also seek to contract with FI\$Cal for additional training and assistance for the system. Once the department is able to fully utilize the FI\$Cal system with the help of consulting services, the CHRB will have the ability to complete business tasks on a timely basis. This is a new control.

Risk: Aging Workforce

The CHRB is at risk of losing specialized knowledge from its experienced workforce. The CHRB has experienced an increase in the number of employees retiring from state service. The loss of knowledge is affecting the department.

Control: Workforce Plan

In 2017, the CHRB implemented its Workforce Plan and presented its Succession Plan. The department plans to continue utilizing the strategies developed in the Workforce Plan through 2023. This is an existing control.

Risk: Outdated Policy and Procedures

The CHRB Enforcement Division's Policies & Procedures Manual is outdated and does not reflect recent changes in state law and internal procedures. Without up-to-date policies and procedures, enforcement staff do not have a reference for understanding the current directives to conduct their daily work. There is no accountability if enforcement staff is not able to follow existing directives due to lack of proper documentation and distribution.

Control: Update Policy and Procedures

The Enforcement Division Policy & Procedure Manual is currently being updated. Some preliminary documents have been distributed to enforcement staff with a request for feedback. Once feedback is received, the documents and procedures manual will be finalized. The manual will be a living document with continuous additions and changes as necessary (based on law or procedural changes). This will ensure that there is a means for addressing situations of documented policies and procedures and ensures that all enforcement staff have the same baseline understanding of expectations. This is a new control recently put into action.

CONCLUSION

The California Horse Racing Board strives to reduce the risks inherent in our work and accepts the responsibility to continuously improve by addressing newly recognized risks and revising risk mitigation strategies as appropriate. I certify our internal control and monitoring systems are adequate to identify and address current and potential risks facing the organization.

Rick Baedeker, Executive Director

CC: California Legislature [Senate (2), Assembly (1)]
California State Auditor
California State Library
California State Controller
Director of California Department of Finance
Secretary of California Government Operations Agency

Check List (will not appear in the submitted report)

Governance

- Management establishes and demonstrates integrity and ethical values
- Oversight is provided by a board, outside entity, or top executive
- The entity ensures appropriate levels of responsibility and authority, and documentation of internal control systems
- Management recruits, develops, and maintains a competent workforce
- Management evaluates performance and enforces accountability
- Information requirements are established and met with reliable and relevant sources
- Quality information is communicated to internal parties within the entity
- Quality information is communicated to external parties

Risk Assessment

- Management establishes clearly defined objectives to enable identification of risks and definition of risk tolerances.
- Management identifies, analyzes, and responds to risks.
- Potential for fraud is considered when identifying, analyzing, and responding to risks.
- Significant changes are considered when identifying, analyzing, and responding to risks.

Risks and Controls

- Management designs control activities to achieve objectives and respond to risks.
- Information systems and control activities are designed to achieve objectives and respond to risks (Checking this box indicates management considered information systems risks during the risk assessment process).
- Control activities are implemented and documented in policies, procedures, or other similar documentation

Monitoring

- Monitoring activities are performed, documented, and measured against a baseline.
- Management evaluates results and ensures appropriate corrective actions are implemented and documented.