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DIVISION OF GAMING

## GAMING ADMINISTRATIVE EXPENSES



JUNE 2018

PERFORMANCE AUDIT

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# OFFICE OF THE STATE AUDITOR



June 6, 2018

DIANNE E. RAY, CPA  
—  
STATE AUDITOR

Members of the Legislative Audit Committee:

This report contains the results of a performance audit of the Division of Gaming within the Department of Revenue. The audit was conducted pursuant to Section 2-3-103, C.R.S., which authorizes the State Auditor to conduct audits of all departments, institutions, and agencies of state government. The report presents our findings, conclusions, and recommendations, and the responses of the Division of Gaming and the Colorado Limited Gaming Control Commission.

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# REPORT HIGHLIGHTS



GAMING ADMINISTRATIVE EXPENSES  
PERFORMANCE AUDIT, JUNE 2018

DIVISION OF GAMING  
DEPARTMENT OF REVENUE

## CONCERN

The Division of Gaming (Division) and the Colorado Limited Gaming Control Commission (Commission) lack certain controls over the \$4.4 million in funding awarded to other state agencies to help administer gaming. Specifically, they lack policies and processes to establish interagency agreements that identify the specific services the agencies should provide, to enforce reporting requirements, and to monitor for compliance with the agreements.

## KEY FINDINGS

- For Fiscal Year 2017, three agencies requested more in gaming funds than they had told the Joint Budget Committee (JBC) they expected to receive from the Commission. Differences in information provided to the Commission and the JBC could lead to the Commission approving funding for some of the same activities as those funded through the JBC.
- All four of the interagency agreements in place for Fiscal Year 2017 lacked either specific descriptions of the services the agency would provide or measures the agency would use to report on their performance and the Commission would use to monitor the agreements. The lack of specified services and measures could lead to agencies using approved funding in a different manner than intended by the Commission.
- The Commission and the Division did not enforce reporting requirements included in the interagency agreements prior to paying agencies the full amounts they had invoiced the Commission. In Fiscal Year 2017 the Commission paid one agency about \$3.2 million without having specified what information the agency should report regarding its use of the funds; two other agencies about \$1.1 million without obtaining required reports on their activities; and the fourth agency about \$161,000, even though all the required reports were submitted late.
- Neither the Commission nor the Division has established written policies or procedures for monitoring compliance with the interagency agreements. Division staff did not monitor or enforce requirements in the interagency agreements because, as they reported, they did not have the authority to do so.

## BACKGROUND

- Colorado voters approved constitutional amendments in 1990 and 2008 authorizing limited and extended casino gaming, respectively.
- The Commission is responsible for administering and regulating gaming in Colorado, including promulgating rules, issuing licenses, levying fines, and establishing fees and taxes.
- The Division is responsible for the day-to-day regulation of gaming, including processing licenses, conducting audits, overseeing gaming technology and devices, and patrolling gaming establishments.
- The Commission entered into interagency agreements with the Colorado State Patrol, the Colorado Bureau of Investigation, the Division of Fire Prevention and Control, and the Department of Local Affairs to help administer and regulate gaming. Each year the Commission approves funding of the agreements. In Fiscal Year 2017, the Commission paid these agencies a total of \$4.4 million.
- Revenue generated from gaming taxes, fees, and fines is used to pay for administering and regulating gaming and is distributed to beneficiaries. Between Fiscal Years 2013 and 2017, an average of \$14 million annually was used to pay the Division's and other state agencies' costs for gaming administration and regulation, and an average of \$98 million was distributed to beneficiaries.

## KEY RECOMMENDATIONS

- Require other state agencies to align their budget requests submitted to the Commission with those submitted to the JBC and ensure agreements include specific descriptions of services and measures of performance.
- Improve monitoring of the interagency agreements for compliance by assigning a staff member to serve as contract manager and developing written policies and procedures for monitoring the agreements.





# CHAPTER 1

## OVERVIEW

The Colorado Constitution permits limited gaming in the cities of Blackhawk, Central City, and Cripple Creek. Limited gaming, which is defined as a maximum single bet of \$5 on slot machines and live blackjack and poker games, was legalized as a result of an amendment to the Colorado Constitution in 1990. In 2008, Colorado voters approved another amendment to allow the three cities the option to approve “extended limited gaming,” which can include (1) having 24-hour gaming, (2) adding the games of craps or roulette, and (3) raising the maximum wager limit from \$5 to up to \$100. All three cities enacted laws to legalize extended limited gaming.

## PROGRAM ADMINISTRATION

Gaming is overseen by the Colorado Limited Gaming Control Commission (Commission) and the Division of Gaming (Division) within the Department of Revenue. The Commission is a Type 2 commission within the Division and consists of five members who are appointed by the Governor: (1) an attorney with experience in regulatory law, (2) a Certified Public Accountant with knowledge of corporate finance, (3) an individual with experience in law enforcement, (4) an individual engaged in business in a management-level capacity, and (5) a registered voter who is not employed in any profession or industry of the other Commission members. Commissioners serve 4-year terms with no more than three commissioners from the same political party and no more than one commissioner from the same federal congressional district [Section 12-47.1-301, C.R.S.].

Under statute [Section 12-47.1-302, C.R.S.], the Commission's powers and duties include:

- Promulgating rules governing the licensing, conducting, and operating of limited gaming.
- Issuing licenses to those involved in the ownership, participation, or conduct of limited gaming. As of March 2018, the Division reports that there were 33 gaming establishments under the jurisdiction of the Commission and Division.
- Levying fines and suspending or revoking licenses the Commission has issued.
- Establishing and collecting limited gaming fees and taxes. According to the Colorado Constitution and statute, gaming taxes may not exceed 40 percent of casinos' adjusted gross proceeds. The Division reports that gaming establishments have generated more than \$2.1 billion in gaming tax revenues and \$15.7 billion in adjusted gross revenues during the first 25 years of gaming.

The Division is responsible for the day-to-day regulation of gaming, including the following:

- Processing new licenses for gaming establishments and their employees. This includes conducting background investigations of all individuals and companies applying for a gaming license.
- Conducting revenue and compliance audits to verify that gaming establishments are following accounting and compliance procedures to ensure the proper reporting and payment of taxes.
- Overseeing all gaming technology such as cashless wagering, wireless technology, and network security.
- Monitoring all gaming devices to ensure that they are approved for use and are in compliance with state law.
- Patrolling gaming establishments during operating hours to manage complaints from patrons and monitor for any possible violations of gaming laws, rules, and regulations.

## GAMING REVENUE AND EXPENSES

The State collects a tax on the proceeds of gaming and deposits the monies into the Limited Gaming Fund (Fund). The Fund also receives revenue from gaming license fees, reimbursements to the Division for the cost of background investigations, fines paid by licensees, and interest. The Division's financial statements show that for Fiscal Year 2017 it collected the following revenue: \$117 million in gaming tax revenue, \$650,000 in license fees, \$610,000 in interest, \$347,000 in reimbursements for background investigations, and \$158,000 in fines.

The Colorado Constitution [Colo. Const., Art. XVIII, Section 9(5)(b)] gives the Commission the authority to spend gaming funds to administer and regulate gaming in Colorado without any appropriation by the Legislature. Monies remaining after the costs of gaming administration and regulation have been covered are distributed as

defined by the Colorado Constitution and statutes. After each fiscal year, the Department determines the amount of revenue and expenses attributable to extended limited gaming based on Section 12-47.1-701.5, C.R.S., and transfers the extended limited gaming revenue less expenses from the Limited Gaming Fund to the Extended Limited Gaming Fund. The Colorado Constitution [Colo. Const., Art. XVIII, Section 9(7)(c)] requires 78 percent of these funds to be distributed to the Community College System. EXHIBIT 1.1 shows the required distributions and the amounts distributed for Fiscal Year 2017.

EXHIBIT 1.1. LIMITED AND EXTENDED GAMING DISTRIBUTIONS			
	REQUIRED PERCENTAGE	USE OF ALLOCATION	AMOUNT IN FISCAL YEAR 2017
General Fund	50 percent of the monies remaining in the Limited Gaming Fund	Appropriated by the General Assembly <sup>1</sup>	\$ 45,331,192
State Historical Fund	28 percent of the monies remaining in the Limited Gaming Fund	Preservation and restoration of historic sites throughout the state	25,385,467
Gaming Counties (Gilpin and Teller)	12 percent each of the monies remaining in the Limited Gaming Fund and the Extended Limited Gaming Fund	Address local gaming impacts	12,489,870
Gaming Cities (Blackhawk, Central City, and Cripple Creek)	10 percent each of the monies remaining in the Limited Gaming Fund and the Extended Limited Gaming Fund	Address local gaming impacts	10,408,224
Community College System	78 percent of the monies remaining in the Extended Limited Gaming Fund	Supplement existing state funding for student financial aid programs and classroom instruction programs	10,467,496
<b>TOTAL</b>			<b>\$104,082,249</b>

SOURCE: Office of the State Auditor analysis of Division of Gaming audited financial statements, Fiscal Year 2017; the Colorado Constitution [Colo. Const. Art. XVIII, Section 9]; and Colorado Revised Statutes [Sections 12-47.1-701, 12-47.1-701.5, and 12-47.1-1201, C.R.S.].

<sup>1</sup> Recipients included: Colorado Travel and Tourism Promotion Fund; Local Government Limited Gaming Impact Fund; Colorado Office of Film, TV, and Media Operational Account Cash Fund; Advanced Industries Acceleration Cash Fund; Creative Industries Cash Fund; and Innovative Higher Education Research Fund.

EXHIBIT 1.2, below, provides the total revenue and expenses from gaming funds for Fiscal Years 2013 through 2017.

**EXHIBIT 1.2. TOTAL REVENUE AND GAMING DISTRIBUTIONS  
AS A PERCENT OF TOTAL REVENUE (IN MILLIONS)  
FISCAL YEARS 2013 THROUGH 2017**

	2013	2014	2015	2016	2017	OVERALL PERCENTAGE CHANGE
Total Gaming Revenue	\$104.5	\$106.4	\$111.4	\$118.4	\$118.5	13%
Total Division Expenses	\$12.8	\$13.9	\$14.0	\$14.6	\$15.0	17%
Distribution to Beneficiaries <sup>1</sup>	\$92.7	\$92.2	\$97.2	\$103.7	\$104.1	12%
Distribution to Beneficiaries as a Percent of Total Revenue	89%	87%	87%	88%	88%	-1%

SOURCE: Office of the State Auditor analysis of Division of Gaming audited financial statements, Fiscal Years 2013 through 2017.

<sup>1</sup> The Division sets aside a reserve of 2 month's operating expenses before distributing the remaining fund balance in the Limited Gaming Fund to beneficiaries [Colo. Const., Art. XVIII, Section 9(5)(b)] .

We discuss the Commission's and Division's oversight of the costs to administer and regulate gaming in CHAPTER 2.

## AUDIT PURPOSE, SCOPE, AND METHODOLOGY

We conducted this performance audit pursuant to Section 2-3-103, C.R.S., which authorizes the State Auditor to conduct audits of all departments, institutions, and agencies of the state government. The audit was conducted in response to a legislative request by the Joint Budget Committee, which expressed concerns regarding the rising costs of administering gaming. We conducted our audit work from November 2017 through May 2018. We appreciate the assistance provided by the Commission, the Division of Gaming, and the Department of Revenue during this audit.

We conducted this 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.

The key objectives of the audit were to (1) identify changes in gaming administrative costs over time and the key drivers of those costs, (2) evaluate the Commission's processes for approving and monitoring the annual budgets of the Division and the funds provided to other state agencies for administering gaming, and (3) evaluate the Division's methodology for establishing license fees and charging for background investigations.

To accomplish our audit objectives, we performed the following audit work:

- Reviewed relevant requirements in the Colorado Constitution, statutes, policies, and guidance related to the Division and other state agencies that assist in administering limited gaming.
- Interviewed staff at the Division, Department of Revenue, JBC, Office of State Planning and Budgeting (OSPB), Department of Public Safety, and Department of Local Affairs.
- Reviewed and analyzed the Division's budget and expenditures for the last 5 fiscal years.
- Reviewed the Commission's process for approving budget requests from the Division and other state agencies and monitoring funding to other state agencies in Fiscal Year 2017.
- Reviewed the Division's methodology for establishing licensing fees and the hourly rate it charges for background investigations.

We planned our audit work to assess the effectiveness of those internal controls that were significant to our audit objectives. With respect to the Division's methodology for establishing license fees and charging for background investigations, we did not have any findings or

recommendations. The results of our work, as well as specific details about our findings, conclusions, and recommendations, are described in the remainder of this report.

We communicated certain deficiencies in internal control that were not significant to the objectives of the audit but warranted the attention of the Department's management in a separate letter dated May 25, 2018.

A draft of this report was reviewed by the Commission, the Division, and the Department. We have incorporated their comments into the report where relevant. The written responses to the recommendations and the related implementation dates are the responsibility of the Division and Commission.





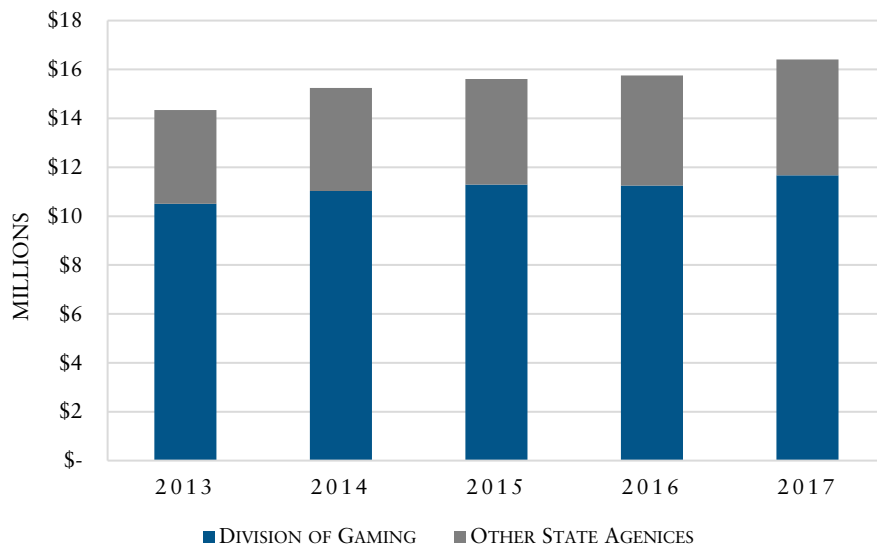
# CHAPTER 2

## BUDGETING AND OVERSIGHT OF GAMING ADMINISTRATIVE EXPENSES

The Colorado Limited Gaming Control Commission (Commission) uses Limited Gaming Funds to pay for the expenses of the Division of Gaming (Division) within the Department of Revenue (Department), as well as some of the expenses of other state agencies that assist in administering and regulating gaming.

The Division and other state agencies submit budget requests for the Commission’s approval each April for the fiscal year starting the following July 1 [Section 12-47.1-203(2)(j), C.R.S., and 1 CCR 207-1, Section 47.1-1803]. EXHIBIT 2.1 shows that approximately three-fourths of the administrative budget approved by the Commission is for the Division’s administration and regulation of gaming and the remainder is for other state agencies’ administration and regulation of gaming.

**EXHIBIT 2.1. GAMING ADMINISTRATIVE EXPENSE BUDGET  
DIVISION OF GAMING AND OTHER STATE AGENICIES  
FISCAL YEARS 2013 THROUGH 2017**

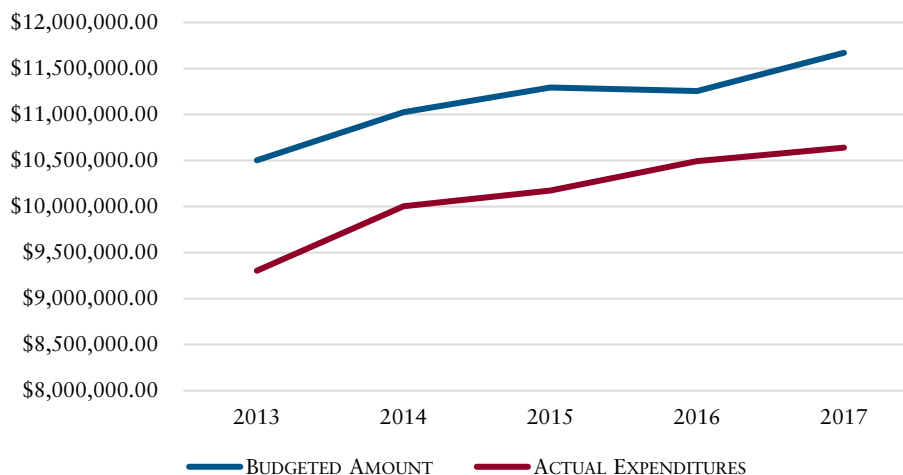


SOURCE: Office of the State Auditor analysis of Colorado Division of Gaming audited financial statements, Fiscal Years 2013 through 2017.

## KEY DRIVERS OF THE DIVISION’S BUDGET

The Division is funded from gaming taxes, fees, and fines; it receives no General Funds. As shown in EXHIBIT 2.2, the Division’s budget increased about 2.7 percent annually between Fiscal Years 2013 and 2017 and its actual expenses grew roughly 3.4 percent each year.

**EXHIBIT 2.2. DIVISION OF GAMING BUDGET AND EXPENSES  
FISCAL YEARS 2013 THROUGH 2017**



SOURCE: Office of the State Auditor analysis of Division of Gaming audited financial statements, Fiscal Years 2013 through 2017.

EXHIBIT 2.3 shows the three main categories of the Division's actual spending. We reviewed these categories to identify the key expense drivers, as discussed in this section.

**EXHIBIT 2.3. DIVISION OF GAMING EXPENSES BY BUDGET CATEGORY  
FISCAL YEARS 2013 THROUGH 2017**

	2013	2014	2015	2016	2017	PERCENTAGE CHANGE
Personal Services	\$ 7,042,470	\$ 7,419,090	\$ 7,744,736	\$ 8,098,996	\$ 7,917,049	12%
Common Policy and Indirect Costs <sup>1</sup>	1,613,824	1,982,755	1,903,438	1,833,687	2,130,002	32%
Operating <sup>2</sup>	646,570	602,334	526,288	561,843	592,845	-8%
<b>TOTAL</b>	<b>\$ 9,302,864</b>	<b>\$10,004,179</b>	<b>\$10,174,462</b>	<b>\$10,494,526</b>	<b>\$10,639,896</b>	<b>14%</b>

SOURCE: Office of the State Auditor analysis of Colorado Division of Gaming audited financial statements, Fiscal Years 2013 through 2017.

<sup>1</sup> Common Policy and Indirect Costs includes all expenses other than personal services and those identified as operating.

<sup>2</sup> Operating includes licensure activities and background investigation expenditures.

## PERSONAL SERVICES

Personal services make up the majority (about 75 percent) of the Division's expenses and generally represent personnel costs, such as

staff salary and benefits. The Division's personal services costs have grown more slowly than the Division's overall expenses (about 12 percent for personal services over the period compared to 14 percent for total expenses). The main drivers of the growth are merit and cost-of-living salary increases and increased costs of benefits approved by the General Assembly and the Governor.

For Fiscal Year 2013 through 2017, the Division requested and the Commission approved a budget for 91 full-time-equivalent staff (FTE). However, the Division has only employed an average of about 82 FTE during these years. The Division reports that the gap between budgeted and actual FTE has occurred due to salaries not being competitive enough to attract and retain investigators. Division staff previously raised this issue with the Commission and the Division has recently started working with the Department and the Commission to try to address it.

## COMMON POLICIES AND INDIRECT COSTS

The Department of Personnel and Administration and the Governor's Office of Information Technology (OIT), in conjunction with the Office of State Planning and Budgeting (OSP), establish common policies for all state departments to use when developing budget requests in specific areas, including leased space, information technology, legal services, workers' compensation, and CORE operations. Each department then allocates these amounts to its divisions and offices. With respect to the Division of Gaming, the Department of Revenue reports that it allocates costs based largely on the number of FTE the Division has budgeted, as well as the estimated need of the Division for the services when this information is available.

The Department also charges the Division indirect costs to pay for the salaries of the Department's senior management, budget personnel, and administrative staff. The Department charges the Division for indirect costs based on the Division's budgeted FTE.

The most significant increases in common policies and indirect costs allocated to the Division have occurred in its payments for information technology (IT) services, such as server management and hosting, service desk, and IT security. For Fiscal Year 2014, the Department requested an increase in its budget to perform IT infrastructure enhancements throughout all of its divisions. Since that increase, the Division's costs for IT services have averaged about \$450,000 per fiscal year. In addition, one of the reasons for the 16 percent increase in Fiscal Year 2017 over Fiscal Year 2016 was that the Department charged the Division about \$260,000 more for indirect costs than in prior years. The Department reported that it had previously incorrectly calculated the Division's indirect costs.

## OPERATING

Operating expenses include costs such as telecommunications, general office supplies, staff training, equipment, printing, and travel.

The Division has spent an average of about \$450,000 less than budgeted for operating each year from Fiscal Year 2013 through 2017. The Division reports that it requests additional funds each year in case it encounters any unanticipated costs, such as costly repairs for its historical building that it owns and uses for office space in a gaming city. The Division reports that it will expend more of its operating budget in Fiscal Year 2018 due to maintenance on one of its buildings.

# FUNDING OTHER AGENCIES FOR GAMING ADMINISTRATION AND REGULATION

The Colorado Constitution [Colo. Const., Art. XVIII, Section 9(5)(b)] gives the Commission the authority to use limited gaming funds to pay for other state agencies' expenses to administer and regulate gaming in Colorado. The Colorado Limited Gaming Act of 1991 (Limited Gaming Act) [Section 12-47.1-302(1)(o), C.R.S.] gives the Commission the authority to enter into contracts with any governmental entity to which it provides funding. Commission rule [1 CCR 207-1, Section 47.1-1805] requires any entity that receives funding from the Commission to enter into a formal agreement with the Commission.

The Commission provides funding to the following four agencies:

- The Colorado State Patrol (State Patrol) within the Department of Public Safety to provide law enforcement services on the highways surrounding Colorado's limited gaming areas.
- The Colorado Bureau of Investigation (CBI) within the Department of Public Safety to investigate violations of the Colorado Organized Crime Act.
- The Division of Fire Prevention and Control (Fire Prevention) within the Department of Public Safety to review local fire and building inspection reports, issue certificates of compliance, and provide technical assistance.
- The Department of Local Affairs (Local Affairs) to provide staff assistance to the Local Government Limited Gaming Impact Advisory Committee.

EXHIBIT 2.4 outlines the amounts paid or budgeted for the Commission's four agreements in place at the time of our audit.

**EXHIBIT 2.4. DIVISION OF GAMING PAYMENTS TO OTHER STATE AGENCIES**  
**FISCAL YEARS 2013 THROUGH 2018**

STATE AGENCY	FISCAL YEAR 2013	FISCAL YEAR 2014	FISCAL YEAR 2015	FISCAL YEAR 2016	FISCAL YEAR 2017	FISCAL YEAR 2018 APPROVED BUDGET
State Patrol	\$2,400,400	\$2,731,841	\$2,696,126	\$2,917,645	\$3,151,749	\$3,476,928
CBI	838,268	795,159	752,072	801,869	885,943	1,063,488
Fire Prevention	177,247	189,373	193,276	182,276	188,070	193,504
Local Affairs	153,939	156,633	165,789	165,389	156,805	164,060
<b>TOTAL</b>	<b>\$ 3,569,854</b>	<b>\$ 3,873,006</b>	<b>\$3,807,263</b>	<b>\$4,067,179</b>	<b>\$ 4,382,567</b>	<b>\$ 4,897,980</b>

SOURCE: Office of the State Auditor analysis of Division of Gaming audited financial statements for Fiscal Years 2013 through 2017, and Fiscal Year 2018 budget requests approved by the Colorado Limited Gaming Control Commission.

The Commission's current interagency agreements with the four state agencies are 5-year agreements that started in July 2013. When the current agreements were executed in 2013, they provided for a maximum financial obligation for Fiscal Year 2014. For each subsequent year of the agreements, the Commission issues what it calls an allocation letter to the agency, specifying the maximum funding approved for the coming year.

The request that prompted this audit asked whether the increasing costs of administering limited gaming were reasonable. In reviewing the total costs to administer and regulate limited gaming that are under the control of the Commission and the Division, we found that although the Division's own expenses comprise the bulk of such costs (roughly 75 percent, as shown in EXHIBIT 2.1), the funds the Commission provides to other state agencies are the most significant driver of cost increases. Specifically, while the Division's costs increased about 14 percent between Fiscal Years 2013 and 2017, the funds the Commission provided to other state agencies increased almost twice as much—about 23 percent. We found several weaknesses in the Commission's and Division's processes that may result in inadequate oversight of the funds the Commission awards to other state agencies through its interagency agreements.

## WHAT AUDIT WORK WAS PERFORMED AND WHAT WAS THE PURPOSE?

For Fiscal Year 2017, we reviewed each of the Commission’s interagency agreements with other state agencies; reviewed each agency’s budget requests approved by the Commission and those submitted to the JBC and reflected in the Long Bill [House Bill 16-1405]; listened to the Commission’s hearing where the agencies’ budget requests were discussed; and interviewed staff at the Division, the Department of Public Safety, and the Department of Local Affairs, and also the Commission chair. The purpose of our work was to evaluate the Commission’s processes for approving and establishing agreements for funds awarded to other agencies.

## HOW WERE THE RESULTS MEASURED?

**INFORMATION NEEDED FOR THE COMMISSION TO APPROVE AND MONITOR FUNDING AWARDED TO OTHER STATE AGENCIES.** Statute, Commission rules, and State Controller policy all contain provisions about the information the Commission needs to establish agreements to fund other state agency activities, as follows:

- **COORDINATION BETWEEN COMMISSION AND JBC BUDGET REQUESTS.** Commission rule [1 CCR 207-1, Section 47.1-1803] states that there should be coordination between an agency’s state budget request, as submitted to the JBC, and a budget request submitted to the Commission. Rule [1 CCR 207-1, Section 47.1-1805] specifies that, “In determining whether to fund any service..., the Commission shall consider the [agency’s] ability to secure funding...from any other source, including the Colorado General Assembly...”
- **IDENTIFICATION OF SPECIFIC DUTIES OR SERVICES.** A number of sources emphasize the importance of determining the specific activities to be funded with Commission approved funds. First, Commission rule [1 CCR 207-1, Section 47.1-1801] requires any state agency with which the Commission is entering into an agreement to provide the “specific duties or services to be completed” as part of their budget requests.



The agreements themselves reiterate this requirement by requiring the agency to provide, with its proposed budget to the Commission, an annual projection of the services for the upcoming fiscal year. Second, Commission rule [1 CCR 207-1, Section 47.1-1802] requires that agencies submit “detailed statements” and that, “Payment may be conditioned upon the receipt of further detail or data concerning the statement.” The latter rule aligns with the statutory requirement that the Commission’s agreements with governmental entities be “based on pre-established commission criteria specifying minimum levels of cooperation and conditions for payment” [Section 12-47.1-302(1)(o), C.R.S.]. Third, State Controller policy related to mandatory provisions in state contracts states that an agreement shall describe “the services to be performed...in enough detail for a third party without prior knowledge of the contract to be able to easily determine if the parties successfully completed their requirements under the contract.” The policy further defines the standard as including (1) a clear description of each deliverable, or the tangible outcomes of the work performed, including what the deliverable must contain and when it is due; and (2) a clear description of the performance standard to be met, if any, including how the standard will be measured and the timeframe for measurement.

**AMENDMENTS TO AGREEMENTS.** Fiscal rules require that any modifications to written agreements must be documented in formal written amendments [1 CCR 101-1, State Fiscal Rule 3-1, 6.3].

## WHAT PROBLEMS DID THE AUDIT WORK IDENTIFY AND WHY DID THE PROBLEMS OCCUR?

We found a number of gaps in the information the Commission uses to establish and oversee agreements with other state agencies, as described in this section.

**BUDGET INFORMATION PROVIDED TO THE COMMISSION AND THE JBC IS NOT ALWAYS COORDINATED.** We found that, for Fiscal Year 2017, three agencies requested more in gaming funds from the Commission than

they had told the JBC they expected to receive, as shown in EXHIBIT 2.5.

EXHIBIT 2.5. STATE AGENCY REQUESTS FOR LIMITED GAMING FUNDS FISCAL YEAR 2017		
AGENCY	LIMITED GAMING FUNDS NOTED IN LONG BILL <sup>1</sup>	LIMITED GAMING FUNDS REQUESTED AND APPROVED FROM COMMISSION
State Patrol	\$2,260,954	\$3,415,545
CBI	851,177	970,924
Fire Prevention	163,393	188,070
Local Affairs	Not indicated	247,125 <sup>2</sup>

SOURCE: Office of the State Auditor analysis of Fiscal Year 2017 Long Bill [House Bill 16-1405] and Fiscal Year 2017 budget requests submitted to the Colorado Limited Gaming Control Commission.

<sup>1</sup> The Long Bill includes footnotes containing the amounts Colorado State Patrol, Colorado Bureau of Investigation, and the Division of Fire Prevention and Safety reported they expected to receive from the Commission, as indicated in the table. The Long Bill also includes an additional \$48,000 for administration of the Department of Public Safety's Executive Director's Office; this amount is not included in the table.

<sup>2</sup> Department of Local Affairs requested a budget amendment from the Commission in November 2016, which was approved, to reduce the budget amount to \$161,347.

The Department of Public Safety and Department of Local Affairs report that the Long Bill incorporates all the funds they anticipate receiving from the Commission for Fiscal Year 2017, but does not always specify the source as being gaming funds. For example, CBI reported approximately \$80,000 of its personal services costs funded by the Commission are not footnoted as gaming funds in the Fiscal Year 2017 Long Bill. Therefore, it is not clear from the Long Bill how much in gaming funds the agency is depending on to support its operations during the fiscal year. As part of the Commission's budget request process, agencies do not inform the Commission of the amounts they request from the JBC or the amounts they told the JBC they expected to receive from the Commission. The Commission's rules and policies do not specifically require agencies to indicate whether they have sought or received funding from other sources to pay for the activities they are asking the Commission to fund, even though the rules do state that the approach between the JBC and the Commission should be coordinated and policies outline some requirements for budget submissions. The Commission chair reported to

us that the Commission does not review agencies' budget requests to the OSPB or the General Assembly; instead the Commission expects the agencies to ensure that they match. Also, the Commission did not ask about other sources of funding as part of the Fiscal Year 2017 budget process. However, the Commission could consider the funds the agency plans to receive from the General Assembly and other sources if it reviews the Long Bill as introduced to the General Assembly in late March or early April and asks agencies whether they have sought other funding. By not requiring such information, the Commission precludes itself from adhering to its own rule that, "In determining whether to fund any service..., the Commission shall consider the [agency's] ability to secure funding...from any other source, including the Colorado General Assembly..."

**INTERAGENCY AGREEMENTS DO NOT ALWAYS DESCRIBE SPECIFIC SERVICES OR MEASURES.** All four of the agreements in place for Fiscal Year 2017 lack either specific descriptions of the services to be performed or measures for monitoring and clear guidance for reporting performance of the services, as outlined below.

- **ONE AGREEMENT DOES NOT DESCRIBE THE SPECIFIC SERVICES TO BE PERFORMED OR MEASURES OF PERFORMANCE.** The agreement with State Patrol states that it "will provide specified law enforcement on the highways surrounding Colorado's limited gaming areas..." The agreement goes on to state, "The parties to the agreement share the following *goals*," [emphasis added], including to (1) enforce traffic laws; (2) investigate and report traffic incidents; (3) apprehend intoxicated and reckless drivers; (4) assist stranded motorists; and (5) control the number of accidents, injuries, and deaths on the highways. The agreement does not specify the law enforcement activities to be completed that would allow the Commission to monitor accomplishment of these goals, such as the number of highway miles to be patrolled, the number of troopers or man hours to be paid for using gaming funds, or the expected number of investigations the funds will pay for.
- **TWO AGREEMENTS INCLUDE SPECIFIC ACTIVITIES, BUT NOT MEASURES OF PERFORMANCE.** First, CBI is required by its agreement to report to the Commission monthly on a total of 14 specified activities,

including number of hours spent on investigations, number of investigations opened, number of intelligence reports completed, number of hours spent per case, number of crime victims identified per case, percentage of intelligence initiated case investigations, and percentage of arrests resulting in conviction. However, the agreement does not contain any information on the expected hours or activities required to carry out the agreement that the Commission could use to measure performance.

Second, Fire Prevention is required by its agreement to report quarterly on six activities, including number of inspections of existing gaming establishments, number of inspections of new or remodeled gaming establishments, number of fire safety deficiencies cited upon inspection, and number of advanced technical support activities. The agreement provides a target number for each of these activities for the coming year. For example, the 2013 agreement indicates a target of 110 inspections of existing gaming establishments for Fiscal Year 2014. However, the agreement does not state how close to the targets Fire Prevention must come to be paid the full agreement amount.

- **ALL FOUR AGREEMENTS LACK CLEAR DESCRIPTIONS OF THE CONTENT AND DUE DATES OF REQUIRED REPORTS.** Each of the four agreements require quarterly financial or activity reporting, but lack specificity about what the reports should contain and, in three cases, when the reports were due. For example, the agreement with State Patrol requires the quarterly activity reports to include the “performance as it relates to the agreed upon measurements and projections detailed in Exhibit A” and “necessary management strategies to meet the objectives.” However, neither Exhibit A nor any other part of the agreement contains any measurements or projections or specify what the objectives are.

Commission rule [1 CCR 207-1, Section 47.1-1801(3)] references performance measures, stating, “At the discretion of the Commission...reports may include specific performance measure data applicable to the execution of the...agreement.” However, the Commission has not always required the establishment of or reporting

on such measures. In addition, although agencies are required by the interagency agreements to include performance measures with their budget requests, agencies do not always provide information on the specific activities they will complete as part of their budget requests, so the Commission cannot incorporate this into the agreements. Specifically, two agencies that have agreements with the Commission—the State Patrol and Local Affairs—did not provide projections of services for the coming year as part of their budget requests to the Commission. The Division and Commission indicated that one reason this information has not been routinely obtained is that Division staff have not been assigned responsibility to review the requests for completeness and the Division and Commission acknowledged that they have not consistently enforced this rule.

**THE COMMISSION AND DIVISION DID NOT AMEND AGREEMENTS.** The Commission’s agreement with CBI requires it to provide monthly briefings before the Commission. Division staff reported that a couple of years ago, the Commission asked CBI to provide quarterly briefings instead. This change in expectations was never formalized as an amendment to the agreement.

Similarly, the agreement with Local Affairs specifies due dates for its reports as 15 days following September 30, December 31, March 31, and June 30. For Fiscal Year 2017, none of the agency’s quarterly reports were provided to the Commission by the deadline. On average the agency submitted the reports about 1 month after the due date, ranging from 9 to 65 days late. Division staff reported that it is not possible for Local Affairs to have all the necessary information, such as payroll information, within 15 days of the close of the quarter, and therefore considered the late submissions acceptable. However, the agreement has not been amended to reflect realistic dates.

## WHY DO THESE PROBLEMS MATTER?

Not requiring agencies to align their Commission budget requests with information provided to the JBC prevents the Commission from being able to consider whether the agencies have the ability to secure funds

from other sources, including the General Assembly, as referenced in Commission rules. One of the Commission’s goals in appropriating funds to other agencies for administering gaming is to avoid double funding. The Commission’s agreement with CBI specifically notes the intent that they avoid double funding of the same activities. Without specific projections of the duties agencies will perform, the amounts they requested from the General Assembly, or what they told the JBC they expected to receive in gaming funds, the Commission is hindered in its ability to ensure that double funding does not occur. For example, the agreement with Local Affairs states that the Commission provides funds “to administer the [Local Government Limited Gaming] [I]mpact [F]und since no direct compensation was specified in the Colorado Limited Gaming Act for this function,” and Local Affairs reports that it does not use any grant funding for its administration. However, the Long Bill contains a footnote indicating that Local Affairs receives \$34,000 from Local Government Limited Gaming Impact Fund to pay for its indirect costs, indicating that grant funds may actually be used to fund administration. As a result, the Commission could be double funding some of the same activities.

The lack of coordination also resulted in Local Affairs not being able to use some of its gaming funds as intended. For Fiscal Year 2017 Local Affairs requested and received from the Commission increased funds compared to previous years to fund an additional .7 FTE to administer grants. However, Local Affairs had not submitted this request through the State’s budget process, so lacked spending authority for these funds. Finally, the lack of coordination leads to the Commission approving more than the agencies need. In Fiscal Year 2017, the Commission approved a total of about \$4,736,000, but the agencies did not use \$349,000 of that amount. The unspent funds remained in the Limited Gaming Fund for distribution to beneficiaries at the end of the fiscal year. Not obtaining projections of the specific activities agencies will perform for requested funds, and not reflecting such projections in the agreements, may create a disconnect between how the Commission expects funds to be used and how agencies actually use them. For example, State Patrol’s agreement does not specify which law enforcement services it intends to carry out. In Fiscal Year 2017, some of the activities State Patrol reported

funding with gaming funds included:

- Participating in Gilpin County School Safety Day to teach children the importance of wearing their seatbelts.
- Providing DUI training to partner law enforcement agencies.
- Participating in the Gilpin High School Homecoming parade.

The Commission chair told us that the first two activities seem reasonably related to law enforcement, but that participating in a homecoming parade may not be an appropriate use of the funds.

Not specifying the information agencies should report on and not amending agreements also increases the risk that agencies may not use gaming funds as intended or that double funding may occur. For example, the lack of clarity about what activity and financial reports should include may prevent the Commission from identifying unallowable uses.

# RECOMMENDATION 1

The Colorado Limited Gaming Control Commission (Commission) should strengthen its budgeting for and establishment of agreements with other state agencies for gaming administration by:

- A Implementing a requirement for agencies to align their budget requests submitted to the Commission with those submitted to the Joint Budget Committee (JBC) and provide supporting documentation, in accordance with the Commission’s rule that there should be coordination between an agency’s state budget request, as submitted to the JBC, and a budget request submitted to the Commission.
- B Implementing a process for the Commission to consider other sources of funding as part of the budget request in accordance with its rule specifying that in determining whether to fund any service the Commission shall consider the agency’s ability to secure funding from other sources including the General Assembly.
- C Enforcing requirements for agencies to provide projections of the activities they will perform for requested funding as stipulated in the interagency agreements.
- D Ensuring that agreements include specific descriptions of services and measures of performance under the agreement in accordance with the Commission rule requiring that the interagency agreements list the specific duties to be performed and with State Controller policy requiring agreements to describe the services to be performed and the performance standards to be met through the agreement.
- E Implementing controls to ensure that agreements are amended when expectations change in accordance with the State Fiscal Rule requirement that any modifications to written agreements be documented in formal written amendments.



# RESPONSE

## COLORADO LIMITED GAMING CONTROL COMMISSION

### A AGREE. IMPLEMENTATION DATE: JULY 2018.

The Director of Gaming met with the Commission and discussed the requirements for budget request submissions.

The Director discussed the requirements of Colorado Limited Gaming Regulation 47.1-1805(b) and Commission Policy 96-01 with each agency to ensure budgets are submitted properly in the future. In order to ensure submitted budget requests align with those submitted to the JBC, the Commission will request that the agencies provide their budgets as presented in the Long Appropriations Bill (Act) as justification for their request. If the requests differ, the agencies must provide justification to the Commission. The Director and Contract Manager will follow up with the agencies to ensure understanding about the budget requests.

In addition, this year the allocation letters signed by the Commission Chair were amended to require the signature of an authorized representative from each agency receiving funds from the Commission. This will ensure understanding as to the agreed upon maximum financial obligation and be in accordance with the inter-agency agreement.

### B AGREE. IMPLEMENTATION DATE: APRIL 2019.

The Commission is required to consider requests of those who are impacted by Limited Gaming per statute.

The Contract Manager and Director will work with the agencies, who receive funding to ensure information about additional funding

is included in the presentation. The Commission will expect each agency to indicate whether other sources of funding are available during their budget presentations, ensuring they meet the requirements set forth in 47.1-1805.

C AGREE. IMPLEMENTATION DATE: APRIL 2019.

The agencies will be asked to provide projections of the activities they will perform for requested funding.

If the projections change, the Contract Manager (Director of Administration) will be communicating with the agencies to ensure that any changes to projections that occur are forwarded to the Director, and included in the upcoming monthly Commission packet and meeting. The Division will confer with the Commission in how to proceed with the changes in the contract.

Each agency provides a statement on how requested funds will be spent through the annual budget request process. The statement includes a synopsis of the activities that occurred in previous years. The Commission is mindful that the activities of an agency may change during the course of the year, due to the agency's own determination of what is needed. The Commission standard is that the activity must be related to a legitimate gaming purpose.

D AGREE. IMPLEMENTATION DATE: APRIL 2019.

As of May 2018, all interagency agreements were amended to clarify the reporting responsibilities of the agencies. The Division will work with the Commission to identify what specific descriptions regarding services and measures the Commission needs to determine performance, and will modify the agreements accordingly.

E AGREE. IMPLEMENTATION DATE: MAY 2018.

This year, the Division implemented a process whereby interagency agreements will be reviewed by the Contract Manager (Director of

Administration), as well as the Commission, for the Commission's approval on an annual basis. The agreements will be included every year in the April Commission packet. The Commission will be able to review the information and proposed changes prior to and during the April Commission meeting. If the changes are approved, the amended agreements will be adopted.

If the expectations change during the year, the Contract Manager (Director of Administration) will communicate with the agencies to ensure that any changes in expectations are forwarded to the Director, and included in the upcoming monthly Commission packet and meeting. The Division will confer with the Commission in how to proceed with the changes in the contract.

On a five-year cycle the agreements will also be reviewed again for purposes of renewal. At that time, the Contract Manager (Director of Administration), with the assistance of the DOR Contract Administrator, will ensure that all of the amendments that were made over the course of the five year period are included in the new agreements. The agreements will then be included in the Commission packets to be reviewed and approved by the Commission.

# MONITORING OF AGREEMENTS

The Commission provides funding to four other state agencies to administer gaming in Colorado through interagency agreements. Commission rules reference the concept of the Commission overseeing the agreements by requiring agencies to provide supporting data for their budget requests; stating that it may, at its discretion, require reporting on performance measures by the agencies; and stipulating that the Commission will consider other possible funding sources when determining whether to approve requests.

## WHAT AUDIT WORK WAS PERFORMED, WHAT WAS THE PURPOSE, AND HOW WERE THE RESULTS MEASURED?

For Fiscal Year 2017, we reviewed each of the Commission’s interagency agreements with other state agencies; reviewed all reports, invoices, and other documentation the Division had received from the agencies; and interviewed Division staff and the Commission chair. The purpose of our work was to evaluate the Commission’s and Division’s monitoring of the agreements in accordance with the following:

- **AGENCIES ARE TO PROVIDE FINANCIAL AND ACTIVITY REPORTS TO THE COMMISSION.** The agreements indicate that the reporting is intended to allow the Commission to monitor funding levels. Reporting requirements are consistent with statute, which requires the Commission’s contracts with governmental entities to be “based on...conditions for payment” [Section 12-47.1-302(1)(o), C.R.S.]. The agreements also require the agencies to submit invoices on either a monthly or quarterly basis.
- **CONTRACTS MUST BE MONITORED.** State Fiscal Rules [1 CCR 101-1, State Fiscal Rule 3-1, 11.1] require designating one person who will

be responsible for monitoring compliance with the contract for satisfactory completion of the scope of work and ensuring that performance measures and standards in the contract provide a valid basis for assessing performance. In addition, the agreements themselves identify a contract manager who is responsible for managing the contract in accordance with Department of Revenue Policy #DOR106A, which requires the contract manager to, “Ensure all goods/services are being delivered as required by the contract,” “Approve...payment of invoices...based on completion of deliverables in the contract,” and “Intercede to correct problems proactively,” among other monitoring duties.

## WHAT PROBLEMS DID THE AUDIT WORK IDENTIFY AND WHY DID THE PROBLEMS OCCUR?

THE COMMISSION AND DIVISION DID NOT ENFORCE REPORTING REQUIREMENTS cited in their agreements for Fiscal Year 2017, yet the Division paid all the agencies according to what they had invoiced. Specifically:

- CBI did not submit any quarterly financial reports or provide monthly briefings to the Commission, as required. Instead CBI provided quarterly briefings. The Commission paid CBI the full \$885,943 invoiced.
- Fire Prevention did not submit any quarterly financial or activity reports, as required. The Commission paid Fire Prevention the full \$188,070 invoiced.
- Local Affairs submitted all of its quarterly financial/activity reports between 9 and 65 days late. The Commission paid Local Affairs the full \$161,347 invoiced.
- State Patrol provided reports on the quarterly frequency required that contained a variety of data on the activities it carried out.

However, since the agreement does not specify what they should be reporting, the reports may not completely align with what the Commission needs. The Commission paid State Patrol the full \$3,151,696 invoiced.

Division staff told us that they do not have authority to deny any payment requests unless the request exceeds the full annual allocation. Rather, they consider the Commission's allocation letter, outlining the maximum financial obligation for the year, to be approval for the year's invoices. Further, the Commission does not delay or deny payment when agencies do not submit reports as required.

**NO CLEAR AUTHORIZATION FOR STAFF TO MONITOR OR ENFORCE AGREEMENTS.** Neither the Commission nor the Division has established any written policies or procedures regarding the role of Division staff in monitoring compliance with the interagency agreements. Division staff told us they have not been authorized to oversee the agreements, such as by questioning information provided by the agencies, requesting additional or revised information, or sharing the reports with the Commission. For example:

- The Accounts Payable staff review the invoices from the agencies. However, they only review to ensure that the invoiced amount does not exceed the budget allocation approved by the Commission for the year. They do not review financial or activities reports, or service projections included in an agency's budget requests to verify that the agency is only invoicing for the services outlined in the contract or projected in the approved budget request. According to Accounts Payable staff, they are not authorized to do any verification that deliverables were received before payment is issued or to take any other action to monitor compliance with the agreements.
- The staff members who receive activities reports review the reports, but do not use them to verify compliance with the contract. These staff told us that they are not authorized to question an agency's activities or bring information in the reports to the Commission's attention. Rather, they believe it is the commissioners' prerogative to

question whether an agency's reported activities are in line with the agreement. However, we found that for Fiscal Year 2017, although Accounts Payable staff received Local Affairs' reports and reported they passed them on to the Division Director after the invoices were paid, Division staff did not pass the reports on to the Commission for its review. Neither Division staff nor the Commission received reports in Fiscal Year 2017 from Fire Safety.

- The staff person who receives agencies' budget requests reviews them for anything that "stands out" or is different from prior year budgets, but is not authorized to question an agency's budget request or ask for revisions if they are incomplete, such as when they do not include projected services. This staff person believes that this is a role the commissioners hold.
- The staff member designated by the agreements as the contract manager left the Division in 2015, but her successor told us that overseeing the agreements was not a responsibility that was known to her. She does not receive any of the reports or review invoices before they are paid.
- A member of Division management told us that he feels that it is the Commission's role to determine whether agencies are spending money in accordance with the Commission's expectations; it is more of a policy decision for commissioners and not a determination that Division staff can make.

We also found that there are no written policies or procedures that describe how the Commission intends to use the reports and briefings from agencies to oversee the agreements. For example, Commission policies address requirements for agencies' budget submissions, but do not address other deliverables such as reports and briefings the agencies provide to the Commission or the Commission's approach to overseeing agreements. The Department's contract management policy also does not address the involvement of a commission in overseeing a contract.

## WHY DO THESE PROBLEMS MATTER?

**THE COMMISSION LACKS ASSURANCE THAT AGENCIES ARE ACHIEVING PROGRAM OUTCOMES AND THAT FUNDS ARE BEING SPENT AS INTENDED.** When the Commission does not enforce requirements for agencies to report on the activities they carried out under their agreements, and does not have controls in place to review the reports themselves or have staff conduct reviews, the Commission cannot evaluate whether the agencies are carrying out the activities they were funded for or whether the activities are achieving the desired outcomes.

As an example, in 2015 the Commission became aware that CBI was sometimes using gaming funds to train investigators in polygraph testing then moving them to units that did not carry out any gaming-related activities. The Commission told CBI this was not acceptable under the agreement. One Division staff person told us that, prior to 2015, she had been aware of CBI's practice but did not inform the Commission because she did not feel she was authorized to do so. Had she been empowered to share the information with the Commission, the practice may have been stopped earlier.

**REPORTING AND REVIEW PROCESSES CREATE INEFFICIENCIES WHEN THOSE REPORTS ARE NOT USED FOR MONITORING.** When the Commission requires the agencies with which it has agreements to submit invoices and reports and provide briefings that are not used to monitor compliance with the agreements, it creates work for both the agencies and Division staff that is not productive. For example, the agencies submit to the Division monthly or quarterly invoices that contain line item detail showing budget, current month expenses, year to date expenses, previously billed expenses, and remaining budget. However, according to the Division, the only purpose of the invoices is to track spending to date to ensure the Division does not overpay the total funding allocation. Therefore, the agency spends time preparing a more detailed invoice than is used by the Division. For three agencies, the invoice includes detail for more than 40 line items. Similarly, when the Commission requires agencies to provide quarterly reports on their activities, and staff spend time reviewing them, but the reports are not



used to assess the accomplishments of the agency and hold them accountable for the use of the gaming funds, the resources used to create and review the reports are wasted.

To improve oversight of the agreements, the Commission could direct staff to review reports submitted in accordance with the agreements to ensure that agencies are carrying out the activities specified in the agreements and report to the Commission based on the reviews, including bringing to its attention any questions or concerns about whether the reporting demonstrates compliance with the agreements. Further, by specifying expectations more clearly in the agreements (see RECOMMENDATION 1), the Commission may have more assurance that staff can accurately determine whether agencies are spending money according to those expectations.

## RECOMMENDATION 2

The Colorado Limited Gaming Control Commission (Commission) and Division of Gaming (Division) should improve monitoring of the interagency agreements for compliance by:

- A Assigning a staff member to serve as the contract manager who is responsible for reviewing reports from the agencies, enforcing compliance with the agreements, and approving payments.
- B Developing written policies and procedures that explain how staff should report to the Commission regarding their monitoring efforts.

## RESPONSE

### DIVISION OF GAMING

- A AGREE. IMPLEMENTATION DATE: MAY 2018.

The Director of Administration was assigned as the contract manager; however, a new procedure has been implemented whereby the Director of Administration will now be responsible for the entire process, which includes review of reports for compliance with the assistance of the Director of Gaming, and approval of payments with the assistance of budget and accounting.

The Director of Administration will ensure the agreements are reviewed, enforced and the payments are approved according to the reports. If any issues are identified the Director of Administration will notify the Director of Gaming and include any pertinent issues or changes in the Commission packet for follow up at the next Commission meeting. After reviewing the information the Commission will be able to determine agency compliance.

B AGREE. IMPLEMENTATION DATE: JULY 2018.

The Division has reviewed policy 96-01 and has suggested changes that include how Division staff should report to the Commission regarding their monitoring efforts of the interagency agreements. Upon Commission review and approval, the new policy will become effective. If changes are required to any of the agreements, the Director of Administration will inform the Director of Gaming and the information will be included in the Commission packet for review at the next Commission meeting.

If there are any concerns the with the compliance monitoring the Contract Manager (Director of Administration) will communicate with the agencies and ensure the issues are forwarded to the Director, and included in the upcoming monthly Commission packet and meeting. The Division will confer with the Commission in how to proceed with the concerns to ensure they are addressed with the agency receiving the funding.

## COLORADO LIMITED GAMING CONTROL COMMISSION

A AGREE. IMPLEMENTATION DATE: MAY 2018.

We are in agreement with the response provided by the Division.

B AGREE. IMPLEMENTATION DATE: JULY 2018.

We are in agreement with the response provided by the Division.

