

**U.S. Department of the Interior  
Office of Inspector General**

# **Audit Report**

## **Virgin Islands Lottery Government of the Virgin Islands**



**Report No. 01-I-290  
May 2001**





# United States Department of the Interior

OFFICE OF INSPECTOR GENERAL  
Washington, D.C. 20240

May 11, 2001

Honorable Charles W. Turnbull  
Governor of the Virgin Islands  
No. 21 Kongens Gade  
Charlotte Amalie, Virgin Islands 00802

Subject: Audit Report on the Virgin Islands Lottery, Government of the Virgin Islands  
(Report No. 01-I-290)

Dear Governor Turnbull:

This report presents the results of our audit of operations of the Virgin Islands Lottery.

Section 5(a) of the Inspector General Act (5 U.S.C. app. 3) requires the Office of Inspector General to list this report in its semiannual report to the U.S. Congress. In addition, the Office of Inspector General provides audit reports to the Congress.

Please provide a response to this report by June 29, 2001. The response should provide the information requested in Appendix 4 and should be addressed to our Caribbean Regional Office, Federal Building - Room 207, Charlotte Amalie, Virgin Islands 00802.

Sincerely,

Roger La Rouche  
Assistant Inspector General  
for Audits

cc: Mr. Austin Andrews, Acting Director, Virgin Islands Lottery

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# EXECUTIVE SUMMARY

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## BACKGROUND

The Virgin Islands Lottery was created in 1937 and established as an independent instrumentality of the Government of the Virgin Islands in 1971. The Lottery operates a traditional biweekly lottery and also sells instant lottery tickets. The Lottery's revenues totaled \$27,793,400 during fiscal years 1998 and 1999, and expenditures during the same 2 years totaled \$28,182,366. The Lottery's unaudited financial statements showed losses of \$120,062 in fiscal year 1998 and \$268,904 in fiscal year 1999.

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## OBJECTIVE

The objective of the audit was to determine whether the Lottery (1) had adequate procedures and management controls in place for the disposition of revenues from ticket sales, the payment of prizes, and the disposition of unsold lottery tickets and (2) distributed its revenues in accordance with legal requirements.

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## RESULTS IN BRIEF

The Lottery's internal controls over the payment of prizes were adequate. However, Lottery funds totaling \$1,211,226 were not used for authorized purposes (\$1,066,387) or properly collected and deposited to the Lottery's account (\$144,839). Specifically, (1) Lottery funds totaling \$99,102 were used by the former Director for personal purposes; (2) collections totaling \$11,930 were not deposited to the Lottery's account and may have been stolen; (3) a bank deposit totaling \$40,985 was not credited to the Lottery's bank account and also may have been stolen; (4) accounts receivable totaling \$88,224 were not collected from dealers and agents for unpaid returned checks and for instant lottery tickets delivered to business establishments; (5) instant lottery funds totaling \$916,000 were transferred to the traditional lottery without proper authorization; (6) additional funds of \$51,000 were used to fund a celebrity golf tournament and to pay the cost for 30 students to attend youth games in the United States; (7) licensing fees totaling \$3,700 were not collected from agents who sell instant lottery tickets; and (8) a total of \$285 from two change funds at the instant lottery could not be accounted for.

We also found that unsold instant lottery tickets valued at about \$97,000 were not appropriately returned to the contractor for refund and that unsold traditional lottery tickets valued at \$14,380 were not accounted for and were unavailable for sale until 1 day prior to the drawings. As a result, the Lottery lost revenues of \$97,000 from refunds and lost the potential for revenues of

\$14,380 because tickets were not available for sale. Further, because it had operated at a loss, the Lottery, during fiscal years 1998 to 1999, did not transfer any revenues from the traditional lottery to the General Fund, as required by the Virgin Islands Code. Consequently, as of September 30, 1999, the Lottery had reported an accumulated account payable to the Government's General Fund totaling \$3.3 million.

During the audit, we also noted other issues related to the Lottery's compliance with legal requirements and internal control procedures. These matters pertained to (1) the number of members appointed to the Lottery Commission, (2) the issuance of audited financial statements, (3) the preparation of monthly activity reports, (4) the maintenance of property control records and the performance of periodic physical inventories of equipment, (5) the management of computer operations and the assurance of Y2K compliance, and (6) the methodology used to verify daily cash collections.

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## **RECOMMENDATIONS**

We made 1 recommendation to the Governor of the Virgin Islands and 15 recommendations to the Virgin Islands Lottery to address the possible misuse of Lottery funds and the internal control weaknesses disclosed by the audit.

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## **AUDITEE COMMENTS AND OFFICE OF INSPECTOR GENERAL EVALUATION**

The Governor and the Lottery concurred with the 16 recommendations and indicated that corrective actions had been or would be taken. Based on the responses, we considered 3 recommendations resolved and implemented and 10 recommendations resolved but not implemented and requested additional information for the 3 remaining recommendations.

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# INTRODUCTION

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## BACKGROUND

The Virgin Islands Lottery was created by statute in 1937 and established as an independent instrumentality of the Government of the Virgin Islands in 1971. The Lottery's operations are managed by a Director, who is subject to the supervision of a 7-member Lottery Commission. The Virgin Islands Code (32 V.I.C. Chapter 13) specifies the powers and duties of the Director and the Lottery Commission.

According to the Lottery's Acting Director, the Lottery's mission is to operate a lottery system in an efficient, fair, and trustworthy manner, and the Lottery's goals are to improve the efficiency of lottery operations and to reduce operating expenditures in order to increase the amount of revenues transferred to the Government's General Fund.

The Lottery has 44 employees to administer the traditional and instant lotteries and the licensing of 581 lottery agents and dealers. The traditional lottery is conducted on a biweekly basis with 24 regular and 2 special drawings. For each regular drawing, 32,000 sheets of tickets (25 tickets per sheet) are printed and sold to dealers for \$20 per sheet (or \$.80 per ticket). For each special drawing, 40,000 sheets of tickets (25 tickets per sheet) are printed and sold to dealers for \$40 per sheet (or \$1.60 per ticket). Instant lottery tickets are sold for \$1 and \$2, and agent and dealer license fees are \$25 per year.

Although revenues of the Virgin Islands Lottery are derived from the sale of traditional and instant lottery tickets and the licensing of agents and dealers, the Lottery's financial statements reflected revenue and expenditure activity only for the traditional lottery. Revenues totaled \$27,793,400 during fiscal years 1998 and 1999, and expenditures during the same 2 years totaled \$28,182,366. The Lottery's unaudited financial statements showed losses of \$120,062 in fiscal year 1998 and \$268,904 in fiscal year 1999.

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## OBJECTIVE AND SCOPE

The objective of the audit was to determine whether the Lottery (1) had adequate procedures and management controls in place for the disposition of revenues from ticket sales, the payment of prizes, and the disposition of unsold lottery tickets and (2) distributed its revenues in accordance with legal requirements. The scope of the audit included Lottery activities that occurred during fiscal years 1998 and 1999 and other periods as deemed appropriate.



To accomplish our audit objective, we reviewed the Lottery's operating procedures; reports prepared for ticket sales, drawing activities, and financial statements; receipts prepared for ticket sales to dealers and agents and for prize payments; and records for payrolls, expenditures, and equipment. The audit was conducted from February through September 2000 at the offices of the traditional and instant lotteries and at business establishments on St. Thomas and St. Croix where instant lottery tickets were sold.

Our audit was conducted in accordance with the "Government Auditing Standards," issued by the Comptroller General of the United States. Accordingly, we included such tests of records and other auditing procedures that were considered necessary under the circumstances. The "Standards" requires that we obtain sufficient, competent, and relevant evidence to afford a reasonable basis for our findings and conclusions.

As part of our audit, we evaluated the internal controls at the Lottery to the extent we considered necessary to accomplish the audit objective. Internal control weaknesses were identified in the areas of disposition of lottery funds; disposition of unsold lottery tickets; distribution of revenues; and compliance with the laws, rules, and regulations related to the Lottery's operations. These weaknesses are discussed in the Results of Audit section of this report. The recommendations, if implemented, should improve the internal controls in these areas.

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## **PRIOR AUDIT COVERAGE**

The Office of Inspector General has not issued any reports on the Virgin Islands Lottery during the past 5 years. However, since 1984, the Office of Inspector General and the Virgin Islands Bureau of Audit and Control have issued a total of three reports related to the Lottery's operations (see Appendix 2).

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# RESULTS OF AUDIT

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## OVERVIEW

The Lottery's internal controls over the payment of prizes were adequate, but other controls needed improvement. Specifically, we found that Lottery funds totaling \$1,066,387 were used for questionable purposes; revenues totaling \$144,839 were not realized; unsold lottery tickets valued at \$111,380 were not adequately controlled; and the Lottery had not made legally required transfers totaling \$3.3 million to the Government's General Fund. These conditions occurred because the Lottery did not have adequate procedures and management controls in place for (1) the disposition of revenues from ticket sales and fees from agent and dealer licenses and (2) the disposition of unsold lottery tickets. In addition, we concluded that the Lottery did not comply with certain provisions of the Virgin Islands Code related to the required transfer of a percentage of revenues to the General Fund, the required number of Lottery Commission members, the publication of audited financial statements, and the preparation and submission of monthly financial reports. Further, the Lottery did not have adequate controls over equipment, computer operations, and daily cash collections.

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## DISPOSITION OF LOTTERY FUNDS

Lottery funds totaling \$1,211,226 were not used for authorized purposes (\$1,066,387) or properly collected and deposited to the Lottery's account (\$144,839). Specifically, we found that (1) Lottery funds totaling \$99,102 were used by the former Director for personal purposes; (2) collections totaling \$11,930 were not deposited to the Lottery's account and may have been misused; (3) a bank deposit totaling \$40,985 was not credited to the Lottery's bank account and also may have been misused; (4) accounts receivable totaling \$88,224 were not collected from dealers and agents for unpaid returned checks and for instant lottery tickets delivered to business establishments; (5) instant lottery funds totaling \$916,000 were transferred to the traditional lottery without proper authorization and additional funds of \$51,000 were used for purposes that did not add value to the operations of the instant lottery; (6) licensing fees totaling \$3,700 were not collected from agents who sell instant lottery tickets; and (7) a total of \$285 from two change funds at the instant lottery could not be accounted for.

**Lottery Credit Card Used  
for Personal Expenses  
Totaling \$99,102**

In June 1995, the former Director opened a management account with an investment firm on St. Thomas. The management account provided the Director and the Assistant Director with credit cards to make cash withdrawals from automated teller machines and to make purchases at business establishments without the authority, knowledge, or consent of the Lottery Commission or the Government. Our analysis of the expenditures incurred by the former Director indicated that the expenditures were primarily of a personal nature and were not related to the operations of the Lottery. However, we concluded that expenditures incurred by the Assistant Director were for Lottery operation purposes.

During the period of June 1995 to March 1999, funds of \$161,387 from the traditional and instant lotteries were deposited into the management account. Our review of the management account monthly statements, which detailed the transaction date, vendor name, vendor location, and dollar amount for each credit card transaction, showed that the former Director used Lottery funds of at least \$99,102 for personal purposes.

Specifically, during the period of July 1995 to January 1999, the former Director incurred \$60,678 in miscellaneous expenditures for charges at restaurants, hotels, boutiques, sports facilities, and department and specialty stores and for Internet service and cellular telephones among other charges; withdrew \$34,638 in cash from various automated teller machines in the Virgin Islands and the continental United States; incurred \$139 for automated teller machine usage fees; incurred \$600 in annual usage fees for the management account and the credit card; and incurred \$3,047 in overdraft fees.

In an October 20, 1998 letter, the Lottery's Special Assistant informed the former Director that the Virgin Islands Code (32 V.I.C. Chapter 13) did not contain a provision that authorized the withdrawal of Lottery funds without adequate supporting documentation to show the Lottery-related purpose of the expenditures. In a January 25, 1999 letter, the then Assistant Director also requested that the former Director "rectify any disallowed expenditures that are still outstanding." As of September 30, 2000, the former Director had not repaid any of the cash withdrawals or personal expenditures.

**Cash Collections  
Totaling \$11,930 Not  
Deposited**

According to the Lottery's Office Manager, the established practice regarding collection of unpaid returned checks is to mail a form letter to dealers and agents requesting payment. The check number, dealer/agent name, check date, payment date, and check amount are logged into a journal for each unpaid returned check. When payment is made, the payment date, payment amount, and receipt number are written in red in the journal. Our review showed that during the period of July to November 1998, on three occasions a dealer made cash payments totaling \$11,930 at the Lottery office to satisfy payment for six unpaid returned checks. Although the dealer was issued receipts for the cash payments, the payment information was not transcribed into the journal and the cash was not included in the days' deposits. In September 1999, the employee who processed these transactions left her position without officially resigning, and as of September 30, 2000, no efforts had been made to recoup the \$11,930.

**Bank Deposit Totaling  
\$40,985 Missing**

On July 11, 1997, an armored delivery service employee picked up two bank deposit bags from the Lottery's sales office in Charlotte Amalie, St. Thomas, for delivery to a local bank. However, the Lottery's bank account was credited only for the money contained in one of the bank bags. Accordingly, the other bank bag, which contained \$40,985, was not credited to the Lottery's bank account, although the records maintained by the armored delivery service company indicated that a bank employee received and signed for two bank bags. In a September 18, 1997 letter, the former Director wrote the bank's branch manager regarding the unaccounted-for bank bag. In an October 26, 1997 letter, the bank's branch manager stated that the bank did not have any record of ever having received the unaccounted-for bank bag. After the initial letter from the former Director, no other efforts were made to recoup the missing \$40,985.

**Accounts Receivable  
Totaling \$88,224  
Not Collected**

On April 6, 1994, the Legislature passed Act No. 5966, which authorized the Lottery Commission to assess a \$25 fee on each unpaid returned check issued to the Lottery by dealers and agents. In addition, Act No. 5966 stated, "The Commission shall establish, within ninety (90) days of the enactment of this Act [April 6, 1994], a standard policy for dealing with lottery dealers or sales agents who deliver more than three unpaid returned checks within a twelve (12) month period." However, we determined that a standard policy was neither developed nor distributed to Lottery employees. As a result, cashiers were not restricted from accepting checks from dealers and agents with outstanding account balances due for unpaid returned checks. As of September 30,

1999, 42 lottery dealers had outstanding account balances totaling \$45,659, and as of March 31, 2000, 16 sales agents had outstanding accounts receivable balances totaling \$8,769 as a result of unpaid returned checks. In addition, we found that as of December 31, 1999, 70 sales agents owed the Lottery \$33,796 for instant lottery tickets delivered to their business establishments but for which funds had not been remitted. Therefore, the total amount of uncollected accounts receivable was about \$88,224.

**Questionable Transfers  
Totaling \$916,000  
Made From Instant  
Lottery**

We found that operating expenses of the instant lottery were initially paid from the operating account of the traditional lottery and that, to reimburse the operating account of the traditional lottery, deductions were made from the operating account of the instant lottery on a quarterly basis. However, five certificates of deposit totaling about \$836,000 were purchased during the period of February to July 1996 using instant lottery funds. When these certificates of deposit were canceled by the Lottery during the period of November 1996 to February 1999, all of the proceeds were deposited into the operating account of the traditional lottery. In addition, we found funds totaling \$80,000 that had been transferred from the operating account of the instant lottery to the operating account of the traditional lottery. Both the certificates of deposit and the transfer were in excess of the amount required for reimbursement of the initial expenditures of the instant lottery. We therefore concluded that instant lottery funds of \$916,000 were used to absorb operating expenditures of the traditional lottery.

**Instant Lottery  
Funds Totaling \$51,000  
Not Used for Instant  
Lottery Purposes**

We also found that in April 1996 and September 1997, instant lottery funds of \$30,000 were transferred to a management account for use at the discretion of the Director and the Assistant Director. Additionally, in August 1997, instant lottery funds of \$21,000 were used to fund the cost for 30 students to attend youth games in the continental United States and to fund a portion of a celebrity golf tournament. These expenditures, which totaled \$51,000, did not add value to the operations of the instant lottery.

**Lottery Agent License  
Fees Totaling \$3,700  
Not Collected**

Although traditional lottery dealers were required to renew their licenses on an annual basis, no such requirement existed for agents who sold instant lottery tickets. However, we believe that the intent of the Lottery was to require renewal of the agent license on an annual basis because the agent application form was valid for a period of 1 year, with extensions for successive 1-year periods. Moreover, during the period of 1994 through 1997, when the instant lottery was run by a contracted firm, instant lottery agents

were required to renew their licenses on an annual basis. In 1998, when management of the instant lottery was transferred from the contracted firm to the Lottery, fees for agent licenses were not requested or collected by staff at the instant lottery or the administration at the traditional lottery, although instant lottery tickets continued to be delivered to the agents' places of business. During fiscal years 1998 and 1999, 74 agents sold instant lottery tickets. Based on the annual renewal fee of \$25, we determined that the Lottery did not collect \$3,700 in agent licensing fees over the 2-year period.

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## **CONTROLS OVER UNSOLD LOTTERY TICKETS**

At least 1,165 packets of unsold instant lottery tickets valued at about \$97,000 were not appropriately returned to the contractor for refund, and 604 sheets of unsold traditional lottery tickets valued at \$14,380 were not accounted for until 1 day prior to the drawings. As a result, the Lottery lost revenues of \$111,380 from refunds and potential sales.

### **Instant Lottery Tickets Valued at \$97,000 Not Returned for Refund**

The contract with the firm that managed the instant lottery from 1994 to 1997 contained a clause which stated that the contractor would "assume [the] risk of all unsold tickets." Despite this provision, we found 1,165 packages of instant lottery tickets valued at about \$97,000 that the Lottery did not return to the contractor for refund. This occurred because the Lottery did not have adequate control over unsold tickets.

### **Traditional Lottery Tickets Valued at \$14,380 Not Available for Sale**

During fiscal years 1998, 1999, and 2000 (through July 31), 604 sheets of unsold tickets valued at \$14,380 remained unaccounted for until 1 day prior to the drawings, although inventories of tickets should have been conducted on a daily basis and documented on forms entitled "Daily Inventory of Ticket Sales." Of the 604 sheets of tickets, 295 sheets valued at \$8,000 were unaccounted for at the Sunny Isle, St. Croix, branch; 262 sheets valued at \$5,240 had been reprinted for Drawing No. 25 in September 1998 and were unaccounted for; and 47 sheets valued at \$1,140 were not accounted for on St. Thomas and St. John and at Frederiksted, St. Croix. Because these 604 sheets of tickets were not available for sale, the Lottery lost potential ticket sales revenue of \$14,380.

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## **DISTRIBUTION OF LOTTERY REVENUES**

Although not expressly stated in the Virgin Islands Code, it appears that the Virgin Islands Lottery was established primarily for the purpose of providing funds to help support the operations of the Government of the Virgin Islands. This assumption is based on 32 V.I.C. § 246(a)11(i), which requires the Lottery to "transfer . . . not less than five percent (5%) of the revenues of the official lottery . . . to the General Fund of the Treasury of the United States Virgin Islands." However, because it has operated at a loss, the Lottery, during fiscal years 1998 to 1999, did not transfer any revenues from the traditional lottery to the General Fund. Accordingly, as of September 30, 1999, the Lottery had an accumulated account payable to the Government's General Fund totaling \$3.2 million. This amount is reported in the Lottery's unaudited financial statements for the fiscal year ending September 30, 1999.

Regarding the instant lottery, we found that during fiscal years 1994 to 2000 (through June 30, 2000), the Lottery transferred \$530,372 from the instant lottery to the General Fund. However, based on our review of quarterly sales reports prepared by the instant lottery's accountant, we estimated that the contributions to the General Fund should have been \$643,460, or \$113,088 more than the amount actually transferred by the Lottery. We attributed the difference to the Lottery's not always including instant lottery sales for the entire month when calculating the required contribution amounts.

In order to improve the ability of the Lottery to generate sufficient revenues to make required transfers to the Government's General Fund, the Lottery must reduce expenditures and maximize collections, as discussed in this report. Additionally, the Lottery should investigate ways, including new types of lottery games, to make itself more attractive to potential customers while improving its profitability.

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## **OTHER LOTTERY-RELATED ISSUES**

During the audit, we noted certain other matters related to the Lottery's compliance with legal requirements and internal control procedures. These matters pertained to (1) the number of members appointed to the Lottery Commission, (2) the issuance of audited financial statements, (3) the preparation of monthly activity reports, (4) the maintenance of property control records and the performance of periodic physical inventories of equipment, (5) the management of computer operations and the assurance of Y2K compliance, and (6) the methodology used to verify daily cash collections.

**Required Number of  
Commission Members  
Not Appointed**

The Virgin Islands Code (32 V.I.C. §244(a)) states:

The Virgin Islands Lottery Commission shall be composed of the Commissioner of Finance who shall be the Chairman of the Commission, five additional members appointed by the Governor, subject to confirmation by the Legislature, for a term of four years. Of the five members appointed by the Governor and confirmed by the Legislature, two members shall be licensed lottery sales agents, one from the District of St. Thomas-St. John and one from the District of St. Croix; of the remaining three members, one each shall be a resident of St. Croix, St. Thomas and St. John, respectively.

We found that since at least 1997, the Governor had not appointed the "five additional members" required by the Code. Therefore, since at least 1997, the Lottery Commission has been inactive, and rules and regulations to add value to the operations of the Lottery have not been promulgated.

In addition, as of January 1999, the Governor had not appointed a permanent Lottery Director in accordance with the Virgin Islands Code (32 V.I.C. §245(a)).

**Audited Financial  
Statements Not Issued**

The Virgin Islands Code (32 V.I.C. §260a) states, "The financial records of the Commission, as they pertain to Lottery revenues, shall be subjected to an annual independent audit by a certified public accountant or firm of certified public accountants to be designated by the President of the Legislature." However, the most recent financial statements to be audited were for the fiscal year ended September 30, 1988. Accordingly, during fiscal years 1989 to 1999, or a period of 11 years, the Lottery had not had an independent evaluation of its financial statements.

In June 2000, the Lottery's Special Assistant provided us with unaudited financial statements for fiscal years 1998 and 1999. Our limited review of these financial statements showed that much of the information compiled by the Special Assistant could not be corroborated or was inaccurate. For example, we found the following:

- Revenues from the "Sales of Tickets" as reported in the Statement of Revenues and Expenses did not include revenues from the instant lottery.



- "Cash and Cash Equivalents" as reported in the Balance Sheet did not include the amounts of existing change funds.

- "Property, Plant and Equipment" as reported on the Balance Sheet could not be corroborated because the Lottery did not have an accurate, current, and complete property list. In addition, accumulated depreciation increased from \$127,623 in fiscal year 1998 to \$516,124 in fiscal year 1999 without any corresponding increase in the reported amounts for depreciable assets. Furthermore, the notes to the financial statements indicated that the Lottery's assets were depreciated using the straight-line method.

### **Monthly Reports Not Prepared**

The Virgin Islands Code (32 V.I.C. Chapter 13 § 247(i)) states that the Lottery's Director has the duty "[t]o certify monthly to the Commissioner of Finance and the Commission a full and complete statement of lottery revenues, prize disbursements and other expenses for the preceding month." In addition, the Code (32 V.I.C. § 246(a)(12)(d)) states that the Lottery Commission has the duty "[t]o report monthly to the Governor and the Legislature the total lottery revenues, prize disbursements and other expenses for the preceding month, and to make an annual report, which shall include a full and complete statement of lottery revenues, prize disbursements, and other expenses, to the Governor and the Legislature." Despite these requirements, the last monthly report prepared by the Lottery was for August 1995. Because there has been no active Lottery Commission since 1997, monthly reports also have not been submitted to the Governor and the Legislature.

### **Adequate Property Control Records Not Maintained**

The Lottery did not have an accurate, current, and complete property list and had no record of ever having conducted a physical inventory of equipment. We found that the Lottery's administration unit had a property list prepared in 1997, that the Lottery's Special Assistant had a list of computer equipment but the list did not contain the cost or location of the items, and that the Lottery's accountant maintained paid vouchers for equipment items purchased since 1997.

We reviewed a sample of 30 equipment items from the three property record sources maintained by the Lottery. Based on our review, we located 19 pieces of equipment but were unable to locate 11 pieces of equipment.

To strengthen internal controls in this area, we believe that the Lottery should prepare master property records to include, but not necessarily be limited to, (1) a description of the property; (2) a

serial number; (3) a Lottery property tag number; (4) the name of the person who has custody of the property; (5) the location, use, and condition of the property; (6) the acquisition date; (7) the cost of the property; and (8) any ultimate disposition data, including date of disposal and sale price of the property. In addition, we believe that physical inventories should be conducted at least once every 2 years and that the results of the physical inventories should be reconciled to the property records.

### **Computer Operations Not Adequately Supervised**

The Lottery did not have a computer specialist to oversee the data processing needs of the traditional and instant lotteries. Regarding the traditional lottery, we found that desktop computers in the administrative unit were not connected to the Lottery's mainframe computer, the accounting software did not contain cash management and payroll modules, and only the prize payment module had been installed in the ticket sales and prize payment unit on St. Thomas. In addition, nine desktop computers on St. Thomas, St. John, and St. Croix were not being used because operating software had not been appropriately installed.

Regarding the instant lottery, computers had not been upgraded as of June 30, 2000 to ensure that they were Y2K compliant because the contract to perform this work had not been approved by the Department of Justice and the Government's Office of Information Technology.

To strengthen internal controls in this area, we believe that the Lottery should hire a computer specialist to assist it in meeting its data processing needs and that the contract to perform Y2K upgrades should be finalized and approved.

### **Procedures To Verify Daily Collections Not Adequate**

The Lottery's accounting unit reviewed the work of the Lottery's cashiers to determine whether receipts were appropriately prepared and whether each day's deposit could be validated by the receipts. Despite this practice, we found that cash shortages and overages were not properly reconciled and accounted for. For example, on June 15, 2000 a cashier sold 25 sheets of special drawing tickets to a dealer at \$40 per sheet, for a total sales price of \$1,000. Although the cashier indicated on the sales receipt that 25 sheets of tickets had been sold, the cashier inadvertently wrote \$100 as the amount collected. In reviewing this transaction, the accountant recorded the error but incorrectly assumed that there was a cash overage because the day's deposit was \$900 more than could be validated by the day's sales receipts. Had the situation involved a cash shortage, the accountant would have established

an account receivable from the cashier in the amount of the shortage. However, this control procedure did not consider whether the value of the tickets sold and the amount of lottery license fees collected each day were equal to the total amount of funds collected and deposited. We also found that the supervisors located at the Lottery's branch offices did not conduct detailed reviews of daily collections and receipt documents to identify and correct the frequent errors made by the cashiers. Accordingly, we believe that (1) the control procedures used by the accounting unit should include a reconciliation of the number of tickets sold to the amount of cash collected and deposited and, in the case of cash shortages, the establishment of accounts receivable from cashiers and (2) branch office supervisors should review and reconcile the daily collections and receipt documents.

### **Unauthorized Change Funds Established**

During the period of April 1994 to January 1998, the instant lottery was managed by a contracted firm. As part of the contracted firm's operations, change funds were established at both the St. Thomas and the St. Croix offices. In February 1998, the lottery assumed the day-to-day operations of the instant lottery. As part of the transition, the employees who worked for the contracted firm became employees of the lottery. These employees continued the use of the change funds but did not inform lottery officials of the existence of the change funds.

We found that although documentation of authorization was not provided for the establishment of change funds at the instant lottery offices on St. Thomas and St. Croix, each office had a change fund of \$300. At the time of our cash counts, the change fund on St. Thomas had a balance of \$17, or \$283 less than required, and the change fund on St. Croix had a balance of \$298, or \$2 less than required. The St. Thomas cashier was not aware of the methodology to account for a change fund. In addition, Lottery officials were not aware that the change fund for the St. Thomas office had been depleted.

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# RECOMMENDATIONS

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## TO THE GOVERNOR OF THE VIRGIN ISLANDS

We recommend that the Governor of the Virgin Islands:

1. Appoint five additional members to the Lottery Commission in accordance with the Virgin Islands Code (32 V.I.C. § 244(a)) and appoint a permanent Lottery Director, also in accordance with the Code (32 V.I.C. § 245(a)).

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## TO THE VIRGIN ISLANDS LOTTERY

We recommend that the Virgin Islands Lottery:

2. Seek reimbursement of the \$99,102 used by the former Director for personal purposes; the \$40,985 from the missing bank deposit bag; and the \$11,905 in collections unaccounted for from a former Lottery employee.

3. Develop and implement, in accordance with Act No. 5966, a standard policy for dealing with lottery dealers or sales agents who deliver more than three unpaid returned checks to the Lottery within a 12-month period

4. Develop and implement a policy to actively pursue collection of accounts receivable for unpaid returned checks and for instant lottery tickets delivered to business establishments and not paid for.

5. Refrain from transferring funds from the operating account of the instant lottery to the operating account of the traditional lottery except for purposes of reimbursing the account of the traditional lottery for validated operating expenses of the instant lottery initially paid from the operating account of the traditional lottery.

6. Develop and implement a policy that requires the annual renewal of agent licenses and payment of licensing fees.

7. Submit to the former management firm of the instant lottery the 1,165 unsold instant tickets valued at \$97,000 and request reimbursement in accordance with the terms and conditions of the management contract.

8. Prepare the form "Daily Inventory of Ticket Sales" on a daily basis in order to accurately record and document the daily inventory of unsold lottery tickets.

9. Establish and implement, in accordance with the Virgin Islands Code (32 V.I.C. § 246(a)(11)(i)), a plan of action to improve the profitability of the Lottery so that it will be financially able to remit the \$3.3 million owed the Government's General Fund and continue to remit a portion of revenues.

10. Request, in accordance with the Virgin Islands Code (32 V.I.C. § 260a), that the Legislature designate a certified public accountant or certified public accounting firm to audit the annual financial statements of the Lottery.

11. Require, in accordance with the Virgin Islands Code (32 V.I.C. § 246(a)(12)(d)), that the Lottery report monthly to the Governor and the Legislature the total amounts of lottery revenues (from the traditional and instant lotteries and fees collected from dealers and agents for licenses), prize disbursements, and other expenses of the Lottery.

12. Establish a time frame to begin preparation of a certified monthly report to the Commissioner of Finance and the Lottery Commission, in accordance with the Virgin Islands Code (32 V.I.C. § 247(i)), which provides a full and complete statement of lottery revenues, prize disbursements, and other expenses.

13. Develop and implement procedures to maintain master property records that include the specific information detailed in the section "Other Lottery-Related Issues" on property control records, perform physical inventories of equipment at least once every 2 years, and reconcile the results of the inventories to the property records.

14. Hire a computer specialist to assist the Lottery in meeting its data processing needs and take action to finalize and implement the proposed contract for Y2K upgrades to the Lottery's computers.

15. Develop and implement new operating procedures to ensure that the daily verification of collections and deposits also includes a reconciliation to the value of lottery tickets sold and lottery license fees collected each day and the recording of cash shortages as accounts receivable due from the responsible cashier. In addition, the branch office supervisors should review and reconcile the daily collections and receipt documents of each cashier.

16. Develop and implement a policy to ensure that change funds are properly accounted for on a daily basis. In addition,

assurance should be provided that change funds are included in the "Cash and Other Equivalents" account in the Lottery's balance sheet.

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**GOVERNOR OF THE  
VIRGIN ISLANDS AND  
VIRGIN ISLANDS  
LOTTERY  
RESPONSES**

The February 15, 2001 response (Appendix 3) to the draft report from the Governor of the Virgin Islands, which transmitted a February 8, 2001 response from the Virgin Islands Lottery, concurred with the 16 recommendations and indicated that corrective actions had been or were being taken.

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**OFFICE OF  
INSPECTOR  
GENERAL  
REPLY**

Based on the responses, we consider Recommendations 6, 8, and 16 resolved and implemented and Recommendations 1, 3, 4, 5, 9, 10, 11, 12, 14, and 15 resolved but not implemented. We also requested additional information for Recommendations 2, 7, and 13 (see Appendix 4).

## APPENDIX 1 - MONETARY IMPACT

<b>FINDING AREAS</b>	<u>Questioned Costs*</u>	<u>Unrealized Revenues*</u>	<u>Funds To Be Put To Better Use*</u>
Disposition of Lottery Funds	\$1,066,387	\$144,839	
Controls Over Unsold Lottery Tickets		111,380	
Distribution of Lottery Revenues	<u>                    </u>	<u>                    </u>	<u>\$3,313,088</u>
Totals	<u>\$1,066,387</u>	<u>\$256,219</u>	<u>\$3,313,088</u>

\* Amounts represent local funds.

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## APPENDIX 2 - PRIOR AUDIT REPORTS

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### OFFICE OF INSPECTOR GENERAL REPORTS

The August 1984 memorandum report "Review of Virgin Islands Lottery Office" (No. V-TG-VIS-22-84) stated that internal controls over Lottery operations were adequate. Specifically, procedures were in place for the proper disposition of ticket sales and prize payments, drawings were apparently random and there was no evidence of drawings being influenced by outside sources, advertising was used effectively, and operating expenses were valid and properly recorded. The report included six recommendations to improve the profitability of the Lottery.

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### VIRGIN ISLANDS BUREAU OF AUDIT AND CONTROL REPORTS

The 1997 letter report "Limited Review of Employee Accounts Receivable at the [Virgin Islands] Lottery" (No. AM-01-36-98) stated that in 1996, the Lottery (1) overpaid prize winners by at least \$10,000 and underpaid prize winners by at least \$8,000; (2) allowed employee accounts receivable to increase to more than \$45,000 and failed to recoup losses from these employees; and (3) did not enforce punitive sanctions against defaulting cashiers in an attempt to either minimize or deter the incidence of transaction inaccuracies and/or fraudulent activities. During our current review, we found that as of December 31, 1999, employee accounts receivable had increased to \$144,788 but that the methodology used by Lottery accountants to determine the accounts receivable amounts may not have captured all cases of cash shortages.

The 1993 letter report "Followup Review of Recommendations Made in the Audit of the Internal Controls Over the Virgin Islands Lottery System Operations" (No. AM-10-31-93) stated that although the Lottery Commission concurred with the findings and recommendations contained in the prior (1991) report, only limited corrective actions had been taken. Of the 20 recommendations contained in the 1991 report, 11 recommendations were considered resolved and implemented, 8 recommendations were considered unresolved, and 1 recommendation was considered partially resolved and implemented. Specifically, the followup review found that the Lottery did not (1) segregate duties for the issuance, sale, accountability, and inventory of tickets; (2) collect monies due from dealers whose checks were returned unpaid by issuing banks; (3) refrain from selling lottery tickets to individuals not authorized to be dealers; (4) correct flaws in the data processing program designed to control lottery ticket inventories; (5) verify the authenticity of tickets submitted as winners of minor prizes; (6) implement adequate security of cashier cages and



storage of lottery tickets; (7) prepare and submit reports required by the Virgin Islands Code (32 V.I.C. Chapter 13); (8) develop and implement adequate internal controls over the special paper used to print lottery tickets; and (9) conduct performance reviews of supervisors and employee staff members. During our current review, we found that these internal control weaknesses had not been corrected.

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## APPENDIX 3 - RESPONSES TO DRAFT REPORT



### THE UNITED STATES VIRGIN ISLANDS

OFFICE OF THE GOVERNOR  
GOVERNMENT HOUSE

Charlotte Amalie, V.I. 00802  
340-774-0001

February 15, 2001

Mr. Arnold E. Van Beverhoudt, Jr.  
Office of the Inspector General  
Caribbean Regional Office  
Federal Building, Room 207  
St. Thomas, V.I. 00802

Dear Mr. Van Beverhoudt:

The attached information is the Virgin Islands Lottery response to the Draft Audit Report No. V-IN-VIS-002-00-M. I am aware that this response was due on 2/15/01. However, because of a change in leadership at the V.I. Lottery, we realized that there might be a slight delay with our response. Mr. Alric Simmonds of my office spoke to Ms. Stacy Chados, Senior Auditor, explained the possible delay, and was granted an extension to March 1, 2001. I am very grateful for this accommodation.

The Draft Audit Report made sixteen (16) recommendations for corrective action. The management of the V.I. Lottery concurs with all the recommendations and has indicated in their response corrective actions, and targeted dates for completion. My office will follow up with the V.I. Lottery to ensure that these corrective measures will be achieved.

I am thankful for the assistance your office provides the Government through the audit findings, and I hope the attached responses are acceptable.

Sincerely,

A handwritten signature in cursive script that reads "Charles W. Turnbull".

Charles W. Turnbull  
Governor



## **Virgin Islands Lottery.**

Barbel Plaza South, 8A Est. Ross  
Charlotte Amalie, St. Thomas, V. I. 00802-0118  
Tel: (340) 774-2502  
Fax: (340) 774-4730

February 8, 2001

Roger La Rouché  
Acting Assistant Inspector General for Audits  
Office of Inspector General  
Caribbean Regional Office  
Federal Building, Room 207  
St. Thomas, Virgin Islands 00802

SUBJECT: Response to Draft Audit Report on the  
Virgin Islands Lottery, Government of the  
Virgin Islands (V\_IN\_VIS\_002\_00\_M)

Dear Mr. Van Beverhoudt:

Our response to your findings and recommendations are as follows:  
Recommendation 1:

We concur. The Commissioner of Finance, Mrs. Bernice Turnbull who is also the chairperson of the lottery commission and Mr. Austin Andrews, Acting Executive Director of the Virgin Islands Lottery, is in the process of submitting the names of five prospective candidates for the commission to Governor Charles Turnbull. This will be completed by March 5, 2001.

Recommendation 2:

We concur. A joint task force is actively pursuing the reimbursement of funds from former employees. The Virgin Islands Lottery, under the leadership of Mr. Austin Andrews, has already made initial contact with the bank in order to pursue the reimbursement.

Recommendation 3:

We concur. The Executive Director will present to the Lottery Commission, a new standard return check policy that encompasses Act No. 5966 to include any Legislative changes deemed necessary by May 2001.

**Official Lottery Sponsored by the Government of the U.S. Virgin Islands.**

Recommendation 4:

We concur and the Executive Director will include as part of the standard return check policy for the commission's approval and implementation an action plan detailing a firm procedure for the recovery of outstanding funds.

Recommendation 5:

We concur and have instituted a policy by which any funds transferred from the instant lottery will be pursuant to the government standard accounting procedures. The lottery will outline this procedure in its operations manual outlined under the functions of the agency's fiscal officer by July 2001.

Recommendation 6:

We concur and the Executive Director has re-instituted the policy of annual renewal of agents licenses forth with.

Recommendation 7:

We concur, however, the former Executive Director Mr. Dizon, and Scientific Games Inc. agreed that the Virgin Islands Lottery will accept the loss.

Recommendation 8:

We concur. We now have in place, a daily inventory record of ticket sales. It is the responsibility of each district sales supervisor for the completion of this report.

Recommendation 9:

We concur and as Executive Director will prepare a comprehensive plan of action to improve the lottery's profitability for the commission's approval by July 2001.

Recommendation 10:

We concur and the Executive Director will proceed through formal correspondence with the president of the 24<sup>th</sup> Legislature to insure compliance by June 2001.

Recommendation 11:

We concur. The Executive Director in conjunction with its Fiscal Officer will prepare the required documentation for implementation of this recommendation during April 2001.

Recommendation 12:

We concur and the Executive Director in conjunction with its fiscal officer has established a time frame of July 2001 to begin compliance of Virgin Islands Code Chapter 32 section 247(i).

Recommendation 13:

We concur and have received correspondence from the Department of Property and Procurement to develop and implement a procedure for the maintenance of master property records.

Recommendation 14:

We concur. We are in the process of hiring a computer specialist on a permanent basis. The lottery should complete this by March 2001. In the interim the lottery brought in a consultant to assist with the immediate computer needs.

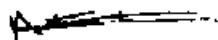
Recommendation 15:

We concur. The operations procedural manual is in the process of being revised to ensure all points outlined in the recommendation by the executive staff. The new procedures will outline the detail functions of the district sale supervisors. The completion of the revision will be May 2001.

Recommendation 16:

We concur. There is an existing policy to ensure that the lottery properly accounts for change funds on a daily basis. Change funds are also included in the lottery's financial reports.

Respectfully,

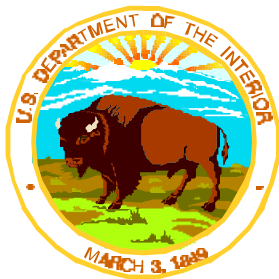


Austin Andrews  
Acting Executive Director

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## APPENDIX 4 - STATUS OF RECOMMENDATIONS

Finding/Recommendation Reference	Status	Action Required
1, 3, 4, 5, 9, 10, 11, 12, 14, and 15	Resolved; not implemented.	Provide this office supporting documentation upon completion of the corrective actions.
2 and 13	Management concurs; additional information requested.	Provide target dates for completing the proposed corrective actions. Also, supporting documentation should be provided upon completion of the corrective actions.
6, 8, and 16	Implemented.	No further action is required.
7	Management concurs; additional information requested.	Provide documentation regarding the agreement between the former Director and the former management firm regarding the disposition of unsold lottery tickets.



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## Mission Statement

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