



MIKE HARMON
AUDITOR OF PUBLIC ACCOUNTS

October 12, 2018

Marc A. Guilfoil
Kentucky Horse Racing Commission
4063 Iron Works Parkway, Building B
Lexington, Kentucky 40511

RE: Review Results

Dear Mr. Guilfoil:

As you are aware, this office has conducted a review of certain contracts for services between the Kentucky Horse Racing Commission (Commission) and Gaming Laboratories International (GLI), as well as associated contract payments made by the Commission and various local tracks. This review was conducted in response to concerns received by this office. We have completed our review of these contracts and associated payments and are presenting to you, as the Executive Director, our findings and recommendations.

To conduct this review, we requested and examined documentation from the Commission and records collected by the Commission from GLI, local race tracks, and two manufacturers of historical horse race (HHR) wagering systems. Documentation reviewed included, but was not limited to, the August 2011 GLI contract for HHR wagering system testing and subsequent renewals through 2018, the August 2014 GLI consulting contract, as well as invoices, payments, and various correspondence relating to these contracts. After examining documentation provided by the Commission we have identified areas of concern that we believe should be considered and addressed further by the Commission.

Regarding GLI contracts for testing of HHR wagering systems, the Commission did not routinely receive, request, or review the billings associated with these contracts. As a result the Commission was not aware of the amounts billed by GLI to Kentucky tracks in association with this contract. Furthermore, the Commission was not aware of the contractor's billing practices associated with these contracts until attempting to collect the associated invoice and payment records requested by the APA. Initially the Commission indicated that the local tracks were billed directly by the contractor; however, after attempting to fulfill the APA documentation request, the Commission stated that the billing process had changed in 2012 so that the contractor was primarily billing the HHR terminal manufacturers who then would carry that cost forward to the tracks. Review of invoice and payment documentation indicate that this process was not strictly followed as records collected showed one track was directly billed by the

209 ST. CLAIR STREET
FRANKFORT, KY 40601-1817

TELEPHONE 502.564.5841
FACSIMILE 502.564.2912

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contractor from 2011 through 2015 and another track was billed directly in 2015. While payments associated with these contracts are not state funds, as a party to these agreements the Commission should ensure the contractor is performing work consistent with the contract. Based on records collected by the Commission, it appears GLI has billed approximately \$845,293 to Kentucky race tracks and two manufacturers for testing of the HHR wagering systems for use at Kentucky tracks in from January 2012 through June 2017. We recommend the Commission provide adequate monitoring of work performed and billing associated with any contract it establishes to ensure activity is consistent with the contract.

Additionally, the Commission did not follow KRS 45A in establishing the original GLI contract in 2011 and subsequently circumvented the procurement process in 2015 when renewing this one-year contract for a three-year period. Documentation indicates that the Commission determined at the time of the original contract that KRS 45A would not be followed because no state funds would be used toward the contract for testing services because the cost of the contract would be incurred by the tracks; however, the Commission reversed course on that determination when entering into a consulting contract with GLI with similar payment arrangement three years later. The Commission renewed the 2011 contract in 2012, 2013, 2014, and 2015. The 2015 contract renewal was for a period of three years extending the contract to 2018. By its actions in 2015, the Commission circumvented the procurement requirements by renewing the contract beyond the term of the original contract which had a stated term limit of 12 months. The original contract language specifically states “[t]he term of the renewed contract may not be longer than the term of the original contract.” The Commission should ensure all procurement by the agency is performed in accordance with state statute and contract renewals are consistent with the terms of the original contract language.

There are also concerns regarding the procurement of the GLI consulting contract, PON2 374 1500000326, established in 2014 after reviewing related records. The Commission claimed a sole source in awarding the consulting contract stating that they were “unaware of another vendor with the requisite experience and expertise”; however, there were other parties responding to a 2011 RFP/RFQ that indicated they could perform this service. Concerns are further exacerbated by the fact that the Commission did not award the contract for this when first sought in 2011 and the agency recommendation to the Finance and Administration Cabinet that a sole source contract be awarded to GLI in 2014 was based on the contractor’s experience and expertise – including its role as the independent testing laboratory for HHR equipment and software since this form of wagering was first offered in Kentucky. This reference to an existing contract as a basis for a sole source determination is questionable because it gives GLI an unwarranted competitive advantage due to a previous contract award with the same agency. Furthermore, a June 13, 2014, internal memo from the Commission states that GLI had long recommended analyzing the Commission’s current regulatory structure to ensure they are providing the oversight necessary to ensure the integrity of the HHR system. These facts indicate

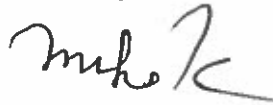
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the Commission did not properly award this contract and the Commission provided the contractor with an unfair competitive advantage. In light of the documentation of events, we are providing the Finance and Administration Cabinet this letter for awareness of the procurement issues raised.

Finally, the APA questions the Commission's authority to pass the cost of drafting regulatory language for testing requirements to individual race tracks. KRS 230.240 gives authority for the expense of testing, along with supplies and equipment used in connection with testing, to be incurred by the tracks; however, we find no authority in state statute or administrative regulation for the Commission to pass the costs of drafting regulatory language for testing requirements down to the tracks. As such, it appears the \$26,073.75 should have been paid by KHRC, as the party responsible for regulating pari-mutuel wagering on horse racing, rather than the tracks. We recommend the Commission reimburse the tracks for this expense.

We would like to thank the Commission for its continued assistance throughout the review process and for providing our office with the requested documentation required to perform this review. If you have any questions regarding this review, please contact me or L. Christopher Hunt, Executive Director, Auditor of Public Accounts.

Sincerely,



Mike Harmon
Auditor of Public Accounts

c: Finance and Administration Cabinet