DIVISION OF GAMING
DEPARTMENT OF REVENUE, STATE OF COLORADO

AUDIT REPORT

YEAR ENDED JUNE 30, 1999

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Gelfond Hochstadt Pangburn, P.C.

DIVISION OF GAMING
DEPARTMENT OF REVENUE, STATE OF COLORADO

YEAR ENDED JUNE 30, 1999

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DIVISION OF GAMING
DEPARTMENT OF REVENUE, STATE OF COLORADO

REPORT SUMMARY

YEAR ENDED JUNE 30, 1999

Authority

The authority for this audit comes from *Colorado Revised Statutes, Section 12-47.1-702(1),* which requires the State Auditor to conduct an annual audit of the Limited Gaming Fund. A contract exists by and between the State of Colorado, through the State Auditor and the Legislative Audit Committee, and Gelfond Hochstadt Pangburn, P.C. ("GHP", or the "Contract Auditors"), whereby the audit of the Division of Gaming, Department of Revenue, State of Colorado (the "Division") for the year ended June 30, 1999, is to be performed by GHP.

Standards

The audit was conducted in accordance with generally accepted auditing standards, as promulgated by the American Institute of Certified Public Accountants in *Statements on Auditing Standards*, and the standards for financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Purpose and scope

The primary purpose of the engagement was to conduct a financial and compliance audit of the Division, as of and for the year ended June 30, 1999, in accordance with standards described above. These standards require that the Contract Auditors plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, tests of the Division's compliance with certain provisions of laws, regulations, and contracts were performed, noncompliance with which could have a direct and material effect on the determination of financial statement amounts.

Auditors' reports

An independent auditors' report on the financial statements of the Division, dated August 10, 1999, has been issued, which states that the financial statements present fairly, in all material respects, the financial position of the Division as of June 30, 1999, and its results of operations for the years ended June 30, 1999 and June 30, 1998, in accordance with generally accepted accounting principles.

In addition, a report dated August 10, 1999, on supplementary information required by the Government Accounting Standards Board concerning Year 2000 preparations has been issued which states that the Contract Auditors have applied certain limited procedures regarding the required supplemental information. However, this information was not audited.

A report on compliance and on internal control over financial reporting based on an audit of financial statements performed in accordance with *Government Auditing Standards*, dated August 10, 1999, has also been issued, which states that the results of the Contract Auditors' tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Summary of finding and recommendations

Evaluate progress of computer system modifications for Year 2000 readiness and potential cost reimbursement

In 1996, the Division began working with the Colorado Department of Revenue's Information Technology Department ("IT Department") to design and implement improvements to certain Division of Gaming computer systems, including Year 2000 compliance modifications. In fiscal year 1999, the Division determined that the designs and modifications implemented during the course of the project were not going to function. The project was abandoned, and approximately $500,000 of computer expenditures incurred during the project period were determined to have no future benefit. In addition, Year 2000 compliance modifications to these systems were not fully implemented.

In response to the project abandonment and to address the need to ensure Year 2000 compliance before December 31, 1999, the Division entered into an $867,000 contract with a third-party computer development firm in March 1999, to perform the system modifications which were originally planned under the abandoned project.

Summary of finding and recommendations (continued)

Because the Division was not able to fully determine until late 1998 that the IT Department project was not going to function, and a new contract was not finalized until March 1999, certain computer system modifications to the licensing system are not expected to be fully completed until mid-December 1999, and Year 2000 compliance testing of these applications may not be completed by December 31, 1999. The Division has stated that only certain computer applications may not be fully tested by December 31, 1999, and the Division has developed a contingency plan that address these remaining systems/applications.

We recommend that the Division continue to monitor the status of the system changes currently in progress, and continue to test back-up systems to ensure they will be available and functional in case the new system is not fully tested by December 31, 1999.

Division response:

Agree. The Division will monitor the progress of the system modifications and take appropriate action to expedite the process. The Division will also continue to test its contingency plan to ensure the Division is ready for Year 2000. The Division believes that it will not be adversely affected by year 2000.

We recommend that the Division should consult with the Department of Revenue to determine if any of the $500,000 expended during the IT Department project may be recoverable by the Division from the Department of Revenue. The Division and Department of Revenue should consider alternatives such as a reduction in future indirect cost allocation rates charged to the Division by the Department of Revenue, or other direct or indirect reductions in future charges.

Division Response:

Disagree. Sections and divisions within the Department of Revenue, including cash-funded agencies, are encouraged to use the DOR Information Technology Division to create or modify information systems whenever possible. The people in the division generally have a higher level of knowledge and expertise with regard to Revenue systems. This does not always mean success is guaranteed. While the Information Technology Division in the Department of Revenue failed in this instance to provide the service requested by Gaming, there does not seem to be a corresponding obligation for the Information Technology Division to pay a damages claim to Gaming. If such a precedent were established, general-funded sections and divisions in the Department of Revenue would be reluctant to provide any service to the cash-funded agencies in the Department.

DIVISION OF GAMING
DEPARTMENT OF REVENUE, STATE OF COLORADO

RECOMMENDATION LOCATOR

YEAR ENDED JUNE 30, 1999

Rec. No.	Page No.	Recommendation summary	Agency response	Implementation date
1	8	The Division should continue to monitor the status of the system changes currently in progress, and continue to test back-up systems to ensure they will be available and functional in case the new system is not fully tested by December 31, 1999.	Agree	August 10, 1999
2	8	The Division should consult with the Department of Revenue to determine if any of the $500,000 expended during the IT Department project may be recoverable by the Division from the Department of Revenue. The Division and Department of Revenue should consider alternatives such as a reduction in future indirect cost allocation rates charged to the Division by the Department of Revenue, or other direct or indirect reductions in future charges.	Disagree	

DIVISION OF GAMING
DEPARTMENT OF REVENUE, STATE OF COLORADO

DESCRIPTION OF THE DIVISION OF GAMING

YEAR ENDED JUNE 30, 1999

Effective October 1, 1991, Article XVIII, Section 9 of the Colorado Constitution was amended to allow limited stakes gaming in three Colorado cities. The Amendment, along with the Limited Gaming Act of 1991 (the "Act"), established the framework for regulating limited gaming in Colorado. The Act created the Division of Gaming within the Department of Revenue, established the Limited Gaming Fund, and gave the Limited Gaming Control Commission (the "Commission") the authority and responsibility for regulating limited gaming in Colorado.

The Division operates with a staff of about 73 full-time employees and a budget of approximately $9 million. The Commission is made up of a five member board. Gaming revenues deposited in the Limited Gaming Fund are used to pay operating expenses for the Division and the Commission during the year. After setting aside a reserve for two months operating expenses at the end of each fiscal year, the remaining fund balance in the Limited Gaming fund is distributed to state and local governments according to the provisions in the Colorado Constitution and the Act.

EVALUATE PROGRESS OF COMPUTER SYSTEM MODIFICATIONS FOR YEAR 2000 READINESS AND POTENTIAL COST REIMBURSEMENT

In January 1996, the Division determined that it was necessary to redesign and make improvements to its automated gaming licensing system. Pursuant to Department of Revenue policies, the Division was required to utilize the Colorado Department of Revenue's Information Technology Department ("IT Department") to assist in the system design, development, and implementation of this project. The system changes were to consist primarily of computer software upgrades, which were to provide efficiencies in processing and storing gaming license information, and more importantly, to make the system Year 2000 ("Y2K") compliant. The project was originally planned to be completed in June 1998.

Significant delays, modifications, and unsuccessful testing occurred between January 1996 and June 1998. In July 1998, based primarily on a Division-requested evaluation and report of a third-party computer consulting firm, the Division and the IT Department determined that the system modifications that had been made were not going to work, and the costs incurred during the period had no future benefit. As a result, the Division and the IT Department abandoned the project. Total costs incurred in connection with the project during the period from January 1996 through July 1998 were approximately $500,000, which primarily represented Colorado Department of Revenue costs, recorded as expenditures by the Division, and paid to the Department of Revenue.

As a result of the project abandonment, the Division's automated gaming licensing system still had to be modified to become Year 2000 compliant. In order to address this issue, in March 1999, the Division entered into a contract with a third-party computer development firm (through a formal bidding process) in order to modify and/or implement Year 2000-compliant licensing and imaging system software. Contracted costs related to the development, installation, and maintenance of this new system are estimated to be approximately $867,000, of which approximately $273,000 represent Y2K remediation costs.

Because the Division was not able to fully determine until late 1998 that the IT Department project was not going to function, and a new contract was not finalized until March 1999, certain computer system modifications to the licensing system are not expected to be fully completed until mid-December 1999.

The Division informed us that the modifications to the licensing system are being addressed in two phases, as follows:

Phase I: Phase I of the II-phase process represents implementation of the computer software applications necessary to process, document, and track gaming licenses. The Division informed us that as of June 30, 1999, Phase I was near completion, and in mid-September 1999, the Division completed Phase I installation, and is now operating under this phase of the system.

Phase II: Phase II represents implementation of the computer software applications necessary to track time and expenses related to Division background investigations. This phase is not expected to be completed until mid-December 1999, and the Division is not certain as to whether the Phase II, Year 2000 modifications will be completed by December 31, 1999.

The Division believes that Phase II is not as critical to the operations of the Division as Phase I, and that the Division has developed a contingency plan should the installation and testing of Phase II extend beyond December 31, 1999.

The Division has informed us that the contingency plan primarily consists of the Division's intentions to utilize existing computer systems to process information, in which the date function can be altered to avoid failing on January 1, 2000. The Division has informed us that these systems and procedures have been tested.

Recommendation No. 1:

We recommend that the Division continue to monitor the status of the system changes currently in progress, and continue to test back-up systems to ensure they will be available and functional in case the new system is not fully tested by December 31, 1999.

Division Response:

Agree. The Division will monitor the progress of the Phase II stage of the project and take appropriate action to expedite the process. In addition, the Division will continue to test and evaluate its contingency plan to ensure the Division is ready for Year 2000. The Division believes that it will not be adversely affected by Year 2000.

Recommendation No. 2:

We recommend that the Division should consult with the Department of Revenue to determine if any of the $500,000 expended during the IT Department project may be recoverable by the Division from the Department of Revenue. The Division and Department of Revenue should consider alternatives such as a reduction in future indirect cost allocation rates charged to the Division by the Department of Revenue, or other direct or indirect reductions in future charges.

Division Response:

Disagree. Sections and divisions within the Department of Revenue, including cash-funded agencies, are encouraged to use the DOR Information Technology Division to create or modify information systems whenever possible. The people in the division generally have a higher level of knowledge and expertise with regard to Revenue systems. This does not always mean success is guaranteed. While the Information Technology Division in the Department of Revenue failed in this instance to provide the service requested by Gaming, there does not seem to be a corresponding obligation for the Information Technology Division to pay a damages claim to Gaming. If such a precedent were established, general-funded sections and divisions in the Department of Revenue would be reluctant to provide any service to the cash-funded agencies in the Department.

INDEPENDENT AUDITORS' REPORT

Members of the Legislative
Audit Committee

We have audited the accompanying financial statements of the Division of Gaming, Department of Revenue, State of Colorado (the "Division") as of June 30, 1999 and for the years ended June 30, 1999 and June 30, 1998, as listed in the table of contents. These financial statements are the responsibility of the Division's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements of the Division are intended to present the financial position and results of operations of special revenue fund types and account groups of only that portion of the financial reporting entity of the Department of Revenue, State of Colorado that is attributable to the transactions of the Division.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Division as of June 30, 1999, and the results of its operations for the years ended June 30, 1999 and 1998, in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 10, 1999, on our consideration of the Division's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, and contracts.

August 10, 1999

DIVISION OF GAMING
DEPARTMENT OF REVENUE, STATE OF COLORADO
BALANCE SHEET - SPECIAL REVENUE FUND TYPE AND ACCOUNT GROUPS
JUNE 30, 1999

	GOVERNMENTAL FUND TYPE	ACCOUNT GROUPS		TOTALS MEMORANDUM ONLY	
	SPECIAL REVENUE	FIXED ASSETS	LONG-TERM DEBT	1999	1998
ASSETS:					
Cash and temporary cash investments (Note 2)	$ 64,631,734			$ 64,631,734	$ 55,609,341
Accounts receivable (Note 3)					
Gaming taxes	7,839,896			7,839,896	6,243,635
Accounts receivable from other agencies	16,339			16,339	335,780
Other	52,598			52,598	5,059
	7,908,833			7,908,833	6,584,474
Prepaid expenses	1,214			1,214	4,062
Fixed assets (Note 4)		$ 736,962		736,962	649,301
Amount to be provided for retirement of long-term obligations (Note 8)			$ 402,532	402,532	408,986
TOTAL ASSETS	$ 72,541,781	$ 736,962	$ 402,532	$ 73,681,275	$ 63,256,164
LIABILITIES AND FUND EQUITY:					
Liabilities:					
Accounts payable (Note 5)	$ 160,136			$ 160,136	$ 73,044
Due to other State agencies (Note 13)	26,914,237			26,914,237	23,939,186
Due to other governments (Note 13)	16,141,515			16,141,515	13,542,324
Due to the State General Fund (Note 13)	27,322,158			27,322,158	21,543,896
Deposits (Note 6)	185,818			185,818	260,502
Deferred revenue (Note 7)	348,250			348,250	1,177,125
Accrued compensated absences (Note 8)			$ 402,532	402,532	408,986
Total liabilities	71,072,114		402,532	71,474,646	60,945,063
Commitments and contingencies (Note 10)					
Fund equity:					
Fund balance - unrestricted	1,469,667			1,469,667	1,229,842
Designated unreserved fund balance					431,958
Investment in fixed assets (Note 4)		$ 736,962		736,962	649,301
Total fund equity	1,469,667	736,962		2,206,629	2,311,101
TOTAL LIABILITIES AND FUND EQUITY	$ 72,541,781	$ 736,962	$ 402,532	$ 73,681,275	$ 63,256,164

See accompanying notes to financial statements.

DIVISION OF GAMING
DEPARTMENT OF REVENUE, STATE OF COLORADO
STATEMENTS OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
YEARS ENDED JUNE 30, 1999 AND 1998

	1999	1998
REVENUES:		
Gaming taxes	$ 74,217,106	$ 61,739,951
Gaming device fees	1,290,975	867,319
License and application fees	785,165	842,866
Background investigations	409,480	664,301
Fines	337,854	617,565
Other	1,649	40,876
TOTAL REVENUES	77,042,229	64,772,878
EXPENDITURES:		
Salaries and benefits	4,219,682	4,009,060
State agency services	2,937,666	2,735,701
Background investigation expenditures	147,571	258,970
Travel and automobiles	251,556	220,951
Professional services	123,549	91,766
Computer services	110,046	109,516
Materials, supplies, and services	365,630	194,002
Telephone	68,702	96,881
Leased space (Note 10)	71,400	64,554
Capital outlay	186,373	79,509
Other	78,205	87,264
TOTAL EXPENDITURES	8,560,380	7,948,174
NON-OPERATING REVENUES:		
Interest (Note 2)	2,023,457	1,915,357
Investment income (loss) (Notes 1D and 2)	(516,936)	293,337
TOTAL NON-OPERATING REVENUES	1,506,521	2,208,694
EXCESS OF REVENUES OVER EXPENDITURES	69,988,370	59,033,398
FUND BALANCE, BEGINNING OF YEAR	1,661,800	1,369,447
Add adjustment for the cumulative effect on prior years of applying retroactively the new method of accounting and reporting for investments (Note 1D)		138,623
FUND BALANCE, BEGINNING OF YEAR, AS ADJUSTED	1,661,800	1,508,070
GAMING DISTRIBUTION (NOTE 9)	(70,180,503)	(58,879,668)
FUND BALANCE, END OF YEAR	$ 1,469,667	$ 1,661,800

See accompanying notes to financial statements.

DIVISION OF GAMING
DEPARTMENT OF REVENUE, STATE OF COLORADO
STATEMENT OF REVENUES AND EXPENDITURES - BUDGET TO ACTUAL
YEAR ENDED JUNE 30, 1999

	ANNUAL REVISED ESTIMATE/ BUDGET *	ACTUAL	OVER/ (UNDER)	% EARNED % EXPENDED
REVENUES:				
Gaming taxes	$ 67,913,946	$ 74,217,106	$ 6,303,160	109.28%
Gaming device fees	1,193,325	1,290,975	97,650	108.18%
License and application fees	918,400	785,165	(133,235)	85.49%
Background investigations	365,777	409,480	43,703	111.95%
Fines		337,854	337,854	-
Other		1,649	1,649	-
TOTAL REVENUES	70,391,448	77,042,229	6,650,781	109.45%
EXPENDITURES:				
Personal services	4,701,830	4,343,231	(358,599)	92.37%
Operating expenditures	855,443	874,139	18,696	102.19%
Legal services	143,825	85,666	(58,159)	59.56%
Leased space	71,400	71,400		-
Capital outlay	236,820	186,373	(50,447)	78.70%
State agency services	2,914,421	2,852,000	(62,421)	97.86%
Division expenditures	8,923,739	8,412,809	(510,930)	94.27%
Passthrough expenditures	290,634	147,571	(143,063)	50.78%
TOTAL EXPENDITURES	9,214,373	8,560,380	(653,993)	92.90%
NON - OPERATING REVENUES (LOSS):				
Interest income	1,812,106	2,023,457	211,351	111.66%
Investment loss		(516,936)	(516,936)	-
TOTAL NON - OPERATING REVENUES	1,812,106	1,506,521	(305,585)	83.14%
EXCESS OF REVENUES OVER EXPENDITURES	$ 62,989,181	$ 69,988,370	$ 6,999,189	111.11%

* Amount includes Long Bill items, and Supplemental Appropriations by the Gaming Commission.

See accompanying notes to financial statements.

DIVISION OF GAMING
DEPARTMENT OF REVENUE, STATE OF COLORADO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 1999

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Colorado Division of Gaming (the "Division") is an agency of the Department of Revenue of the State of Colorado and was created June 4, 1991, under Section 12-47.1-201, Colorado Revised Statutes (C.R.S.). The Division operates under the Colorado Department of Revenue, through the Limited Gaming Control Commission (the "Commission"). The Division implements, regulates, and supervises the conduct of limited gaming in the State of Colorado, as authorized by statute.

The State of Colorado is the primary reporting entity for State financial activities. Therefore, the Division's accounts are presented in a manner consistent with presentation of statewide financial activities, which are reported in accordance with generally accepted accounting principles for governmental organizations.

A. FUND STRUCTURE AND BASIS OF ACCOUNTING

The financial activities of the Division are accounted for and reported on the basis of individual fund and account groups, each of which is considered to be a separate entity. The operations of the Division are recorded in a Special Revenue Fund, which consists of a discrete set of self-balancing accounts that comprise the assets, liabilities, fund equity, revenues and expenditures of the entity. The account groups are used to account for fixed assets and long-term liabilities which are not recorded in the Special Revenue Fund.

GOVERNMENTAL FUND

Special Revenue Fund

Transactions related to resources obtained from specific sources, which are restricted to specific purposes, are accounted for in the special revenue fund. The Division's resources are obtained from specific gaming related activities such as license fees, application fees, gaming device fees, and gaming taxes.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

A. FUND STRUCTURE AND BASIS OF ACCOUNTING (CONTINUED)

ACCOUNT GROUPS

Fixed Assets

This account group is used to account for fixed assets used in the Division's operations.

All fixed assets are stated at historical cost, or estimated historical cost, if actual historical cost is not available. Donated fixed assets are stated at their estimated fair value on the date donated. No depreciation has been provided on general fixed assets.

Long-Term Debt

This account group represents long-term liabilities of the Division and consists of accrued compensated absences.

BASIS OF ACCOUNTING

The Division uses the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recorded when both measurable and available. Measurable means the amount can be determined. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Expenditures are recorded when the related fund liability is incurred, if measurable.

B. BUDGET

The statement of revenues and expenditures - budget to actual, compares those revenues and expenditures which are legally authorized by State statute. The fiscal year 1999 revenue estimates were provided by the Department of Revenue, Office of Tax Analysis, based on the tax rate structure established by the Commission.

Each year, the Division Director submits to the Commission a proposed budget for the fiscal year commencing the following July 1. The budget includes proposed expenditures and the means of financing them. Public hearings are conducted by the Commission to obtain comments and approval. During the fiscal year, the approved budget may be modified due to roll-forward authorization or supplemental budget approval.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

B. BUDGET (CONTINUED)

The Commission must approve all modifications. Appropriations lapse at fiscal year-end unless a roll-forward of the unexpended budget is approved. Total appropriations for the fiscal years ended June 30, 1999 and 1998 were as follows:

	1999	1998
Appropriations	$ 9,127,933	$ 8,883,390
Supplemental appropriations	86,440	(577,820)
Total appropriations	$ 9,214,373	$ 8,305,570

C. TOTAL COLUMNS ON FINANCIAL STATEMENTS

The total column presented on the financial statements is captioned "Memorandum Only" to indicate that it is presented only to facilitate financial analysis. Data in this column does not present financial position in conformity with generally accepted accounting principles. Nor is it comparable to a consolidation, as interfund eliminations have not been made in the aggregation of this data. In addition, certain prior year balances have been reclassified to conform with the current year presentation.

D. CHANGE IN ACCOUNTING POLICY

During the year ended June 30, 1998, the Division adopted *Governmental Accounting Standards Board* Statement No. 31 ("GASB No. 31"). GASB No. 31 provides for the reporting of investments at fair value and the recording of investment income, including changes in the fair value of investments, as revenue in the statement of revenues, expenditures, and changes in fund balance. GASB No. 31 states that accounting changes adopted to conform to the statement are to be applied retroactively, if practical, by restating financial statements for all prior periods presented. If restatement of financial statements for prior periods presented is not practical, the cumulative effect should be reported as a restatement of beginning fund balance for the earliest period restated.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

D. CHANGE IN ACCOUNTING POLICY (CONTINUED)

The 1998 adjustment to beginning fund balance represents the cumulative difference between amortized cost and fair value of the Division's participation in the State Treasurer's pooled cash investments at the beginning of the 1998 fiscal year. The Division recorded $431,960 as cash and temporary cash investments for the net fair market valuation of investments in 1998 due to the implementation of GASB No. 31, of which $293,337 represented the 1998 increase and $138,623 represented the increase prior to July 1, 1997.

2. CASH AND TEMPORARY CASH INVESTMENTS

The State Treasury acts as a bank for all state agencies. Monies deposited in the Treasury are invested until the cash is needed. Interest earnings on these investments are credited to the General Fund unless a specific statute directs otherwise. Cash held by the State Treasurer for the Division as of June 30, 1999 and 1998, was approximately $64.6 million and $55.6 million, respectively.

The State Treasurer pools these deposits and invests them in securities approved by *C.R.S. 24-75-601.1*. The Division reports its share of the State Treasury's unrealized gains and losses based on its participation in the State Treasurer's pool. All of the Treasurer's investments are reported at fair value, which is determined based on quoted market prices at year end. The State Treasurer does not invest any of the pool resources in any external investment pool, and there is no assignment of income related to participation in the pool. Additional information on the State Treasurer's pool may be obtained in the State of Colorado's Comprehensive Annual Financial Report.

The fair value adjustments for the fiscal years ended June 30, 1999 and 1998 were $(516,936) and $293,337. At June 30, 1998, unrealized gains of $431,958 on cash and temporary cash investments were considered to be "Designated Unreserved Fund Balance", which was not available for use in the Division's calculation of funds distributed. At June 30, 1999, the Designated Unreserved Fund Balance has been reduced to $0 as a result of the $516,936 fair value adjustment.

The Division receives interest payments from the State Treasurer's Office on cash held on behalf of the Division. During the years ended June 30, 1999 and 1998, $2,023,457 and $1,915,357, respectively, was earned on the average daily cash and temporary cash investments balance. In June 1999 and 1998, the State Treasurer was paying interest at 5.70% and 6.084%, respectively, annualized.

3. ACCOUNTS RECEIVABLE AND GAMING TAX REVENUES

The Division had $7,839,896 and $6,243,635 of gaming taxes receivable from 49 Colorado casinos at June 30, 1999 and 1998, respectively. These receivables primarily represent June 1999 and 1998 gaming taxes which were due on July 15, 1999 and 1998, and which were substantially collected by the Department of Revenue in July 1999 and 1998, on behalf of the Division.

Accounts receivable from other agencies of $16,339 and $335,780 at June 30, 1999 and 1998, respectively, primarily represent amounts held by the Department of Revenue for license fees, gaming device fees, fines, background deposits, and other fees, that were collected on behalf of the Division as of June 30, 1999 and 1998.

In June 1999, the Commission voted to change the gaming tax structure for fiscal year 2000, beginning July 1, 1999, as follows:

Threshold in adjusted gross proceeds (AGP)	Gaming tax rate: As of and subsequent to July 1, 1999	Gaming tax rate: Prior to July 1, 1999
$0 -$2 million	0.25%	2%
$2 million - $4 million	2%	4%
$4 million - $5 million	4%	14%
$5 million - $10 million	11%	18%
$10 million - $15 million	16%	20%
Above $15 million	20%	20%

4. CHANGES IN FIXED ASSETS

A summary of changes in fixed assets is as follows:

	Computer equipment	Office equipment	Investigative equipment	Leasehold improvements	Total
Balances, July 1, 1997	$ 435,591	$ 76,847	$ 82,377	$ 24,757	$ 619,572
Additions	71,568	7,867	74		79,509
Deletions	(38,687)	(10,894)	(199)		(49,780)
Balances, June 30, 1998	468,472	73,820	82,252	24,757	649,301
Additions	183,041	3,333			186,374
Deletions	(98,713)				(98,713)
Balances, June 30, 1999	$ 552,800	$ 77,153	$ 82,252	$ 24,757	$ 736,962

5. ACCOUNTS PAYABLE

Accounts payable at June 30, 1999 and 1998 consisted of the following:

	1999	1998
Warrants payable	$ 42,680	$ 12,596
Accounts payable	96,625	55,263
Wages and salaries payable	2,463	5,185
Retainage payable contracts	18,367	
Total accounts payable	$ 160,135	$ 73,044

6. DEPOSITS

Applicants applying for gaming licenses are required to remit deposits to the Division, which are used to perform background investigations of these applicants. These deposits are recorded as liabilities until the Division incurs expenditures to perform the background investigations, or until any remaining balance is refunded to the applicant. Deposits for background investigations were $174,805 and $249,489 at June 30, 1999 and 1998, respectively. At June 30, 1999 and 1998, the Division also held $11,013 on deposit, which primarily represents funds seized during criminal investigations that are pending court order releases.

7. DEFERRED REVENUE

The Division issues a 2-year license to individuals, who are subject to an investigative review on an annual basis. The fees for the second year of the license period are recorded as deferred revenue until the Division incurs the expense during the review period. As of June 30, 1999 and 1998, deferred license fees are $348,250 and $151,950, respectively.

Included in deferred revenue at June 30, 1998, is $1,025,175 of gaming device fees which were collected in advance during the year ended June 30, 1998, for the tax year beginning July 1, 1998. In June 1999, the Commission discontinued assessing annual device fees. However, casinos are still required to obtain device stamps and to continue following device tracking procedures. Therefore, there is no deferred gaming device fee revenues as of June 30, 1999.

8. ACCRUED COMPENSATED ABSENCES

All permanent employees of the Division may accrue annual and sick leave based on length of service. The accrued amount will be paid upon termination, subject to certain limitations. The current and long-term portion of vacation and sick leave benefits are recorded in the General Long-Term Debt Account Group, and consist of the following:

	1999	1998
Annual leave	$ 331,770	$ 325,484
Sick leave	70,762	83,502
	$ 402,532	$ 408,986

9. GAMING DISTRIBUTION

In accordance with Section 12-47.1-701, C.R.S., at the end of each State fiscal year, the balance remaining in the Limited Gaming Fund is to be distributed by the State Treasurer according to the following formula:

- 50% to the State General Fund of which .2% of the total distribution goes to the Colorado Tourism Promotion Fund;
- 28% to the Colorado State Historical Fund;
- 12% to Gilpin and Teller Counties, in proportion to the gaming revenues generated in these respective counties; and,
- 10% to the cities of Cripple Creek, Central City, and Black Hawk, in proportion to the gaming revenues generated in these respective cities.

In addition, the State General Fund distribution is further divided as follows:

- 2% to the Municipal Limited Gaming Impact Fund; and,
- 11% to the Local Government Limited Gaming Impact Fund.

9. GAMING DISTRIBUTION (CONTINUED)

The amount to be distributed is derived from revenues collected by the Division for the preceding fiscal year, after payment of the operating expenditures of the Commission and other regulatory expenditures, and after reserving an amount equal to expenditures for the preceding two-month period. As of June 30, 1999 and 1998, the amount reserved by the Division based on expenditures for the preceding two-month period was $1,554,645 and $1,229,842, respectively. The designated unreserved fund balance of $1,469,667 at June 30, 1999, consists of the $1,554,645 reserve balance, less the $84,978 unrealized loss on temporary cash investments.

On August 20, 1999, the Commission approved the distribution of $70,180,503 for the fiscal year ended June 30, 1999 in accordance with C.R.S., 12-47.1-701. In August 1998, $58,879,668 was approved as the 1998 distribution. The distributions are summarized as follows:

Distribution entity	1999	1998
State General Fund	$ 34,949,891	$ 29,322,075
Colorado Tourism Promotion Fund	140,361	117,759
Colorado State Historical Fund	19,650,541	16,486,307
Gilpin and Teller Counties	8,421,660	7,065,560
Cities of Cripple Creek, Central City, and Black Hawk	7,018,050	5,887,967
	$ 70,180,503	$ 58,879,668

The State General Fund distribution is further divided as follows:

	1999	1998
State General Fund Restricted	$ 27,322,158	$ 21,543,896
Municipal Limited Gaming Impact Fund	701,805	588,797
Local Government Limited Gaming Impact Fund	3,859,928	3,238,382
Colorado Department of Transportation	3,066,000	3,951,000
	$ 34,949,891	$ 29,322,075

10. COMMITMENTS AND CONTINGENCIES

A. LEASES

The Division occupies office space in Central City and Cripple Creek. In January 1995, the Division entered into a five-year lease agreement for office space in Central City, Colorado. The term of the lease began in February 1995 and ends in January 2000. Annual rent is $33,000, to be paid in monthly installments of $2,750.

In July 1994, the Division entered into a five-year lease agreement for office space in Cripple Creek, Colorado. Annual rent was $27,600, paid in monthly installments of $2,300. The Division terminated this lease and vacated this office space in February 1998. In connection with this lease termination, in December 1997, the Division entered into a lease agreement with another party to lease other office space in Cripple Creek. The term of this lease began in February 1998 and ends in June 2002. Cripple Creek lease expenditures were $38,400 and $31,554 in 1999 and 1998, respectively.

Future minimum rentals under these leases are as follows:

Years ending June 30,	Totals	Central City	Cripple Creek
2000	$ 61,250	$ 19,250	$ 42,000
2001	42,000		42,000
2002	42,000		42,000
Total Estimated Payments	$ 145,250	$ 19,250	$ 126,000

B. YEAR 2000 CONVERSION

The Division recognizes the need to ensure its operations will not be adversely impacted by Year 2000 software failures. Software failures due to processing errors potentially arising from calculations using the Year 2000 date are a known risk. The Division is addressing the risk to the availability and integrity of financial systems and the reliability of the operational systems.

10. COMMITMENTS AND CONTINGENCIES (CONTINUED)

B. YEAR 2000 CONVERSION (CONTINUED)

The Division has determined that Year 2000 compliance modifications to certain computer applications, currently in process, may not be fully implemented and tested by December 31, 1999. The Division has implemented a contingency plan to address this concern, and believes that based on its plans and continuing efforts, the Division will not be adversely affected.

C. OTHER

In March 1999, the Division entered into a four-year contract with a third party to develop, integrate, and service a regulatory licensing and document imaging computer system. During 1999, the Division expended $184,000 under this contract. The contract requires the Division to pay approximately $496,000 in fiscal year 2000 to complete the development and integration of the system, of which approximately $273,000 is planned for Year 2000 compliance modifications. The contract also requires the Division to pay approximately $50,000 per year through fiscal year 2004 for maintenance and service.

11. PENSION PLAN

A. PLAN DESCRIPTION

Virtually all of the Division's employees participate in a defined benefit pension plan. The plan's purpose is to provide income to members and their families at retirement or in case of death or disability. The plan is a cost sharing multiple employer plan administered by the Public Employees' Retirement Association (PERA). PERA was established by State statute in 1931. Responsibility for the organization and administration of the plan is placed with the Board of Trustees of PERA. Changes to the plan require legislation by the General Assembly. The State plan, as well as the other Division plans, are included in PERA's financial statements, which may be obtained by writing PERA at 1300 Logan Street, Denver, Colorado 80203.

Plan members vest after five years of service and are eligible for retirement benefits at age 50 with 30 years of service, age 60 with 20 years of service, or at age 65 with 5 years of service. State troopers and judges comprise a small percentage of plan members, but have higher contribution rates and are eligible for retirement benefits at different ages and years of service. Monthly benefits are calculated as a percentage of highest average salary (HAS). HAS is one-twelfth of the average of the highest salaries on which contributions were paid, associated with three periods of 12 consecutive months of service credit.

11. PENSION PLAN (CONTINUED)

A. PLAN DESCRIPTION (CONTINUED)

Members disabled, who have five or more years of service credit, nine months of which has been earned since the most recent period of membership, may receive retirement benefits if determined to be permanently disabled. If a member dies before retirement, their eligible children under the age of 18 (23 if a full time student) or their spouse are entitled to monthly benefit payments. If there is no eligible spouse, financially dependent parents will receive a survivor’s benefit.

B. FUNDING POLICY

Most employees contribute 8 percent (11.5 percent for state troopers) of their annual gross covered wages to an individual account in the plan. The State contributes 10.6 percent (12.3 percent for state troopers) of the employee's gross covered wages. The annual gross covered wages subject to PERA is the gross earnings less any reduction in pay to offset employer contributions to the State-sponsored IRC 125 plan established under Section 125 of the Internal Revenue Code. The contribution requirements of plan members and their employers are established, and may be amended, by the General Assembly. Included in salaries and benefits for the years ended June 30, 1999, 1998, and 1997, are the Division's contributions to PERA of $368,186, $349,938 and $322,859, respectively.

12. POST RETIREMENT HEALTH CARE AND LIFE INSURANCE BENEFITS

A. HEALTH CARE PROGRAM

The PERA Health Care Program began covering benefit recipients and qualified dependents on July 1, 1986. This benefit was developed after legislation in 1985 established the Program and the Health Care Fund. Under this program, PERA subsidizes a portion of the monthly premium for health care coverage. The benefit recipient pays any remaining amount of that premium through an automatic deduction from the monthly retirement benefit. During 1998, the subsidy was $115.00 for those with 20 years of service credit, reduced by $5.75 for each year under 20.

The Health Care Fund is maintained by an employer’s contribution of 0.8% of covered salary. Included in salaries and benefits for the years ended June 30, 1999 and 1998, is $27,713 and $26,339 that the Division paid into this fund.

12. POST RETIREMENT HEALTH CARE AND LIFE INSURANCE BENEFITS (CONTINUED)

A. HEALTH CARE PROGRAM (CONTINUED)

Monthly premium costs for participants depend on the health care plan selected, the number of persons being covered, Medicare eligibility, and the number of years of service credit a retiree has. PERA contracts with a major medical indemnity carrier to administer claims for self-insured plans, and with health maintenance organizations providing services within Colorado. During 1998 there were approximately 37,388 participants, including spouses and dependents, from all contributors to the plan.

PERA provides its members access to two group life insurance plans offered by Prudential and Rocky Mountain Life. Members may join one or both plans, and they may continue coverage into retirement. Premiums are paid monthly by payroll deduction.

13. RELATED PARTY TRANSACTIONS

On May 23, 1996, *SB 96-216* was signed, authorizing the Department of Personnel to execute a ten-year lease purchase agreement on behalf of the Department of Revenue for the acquisition of a building located at 1881 Pierce Street, Lakewood, Colorado. The lease purchase occurred on October 31, 1996. The Division estimates that its share of the purchase price, including both principal and interest, will be approximately $2,100,000. The Division transfers funds annually to the Department of Revenue for its share of the building purchase. The future obligations to be paid to the Department of Revenue for the Division's portion for the purchase of the building are estimated to be approximately $206,000 per year. The Division paid approximately $206,000 in each of the years ended June 30, 1999 and 1998.

13. RELATED PARTY TRANSACTIONS (CONTINUED)

The Division, as an agency of the State of Colorado, paid fees to the State for legal and audit services, payment for the Division's share of the building purchase, and other direct and indirect expenses incurred. Interagency charges in 1999 and 1998, consist of the following:

State agency services:	1999	1998
Colorado State Patrol	$ 1,035,405	$ 1,030,181
Colorado Bureau of Investigation	588,586	563,239
Colorado Department of Fire Safety	129,309	140,179
Total payments to State agencies	1,753,300	1,733,599
Legal Services (Department of Law)	85,666	122,863
Indirect Costs (Department of Revenue)	974,112	792,099
Office of the State Auditor	60,757	17,250
Local Affairs	63,831	69,890
	$ 2,937,666	$ 2,735,701

As of June 30, 1999 and 1998, the Division had liabilities to other State agencies, the State's General Fund, and other governments as follows:

State agencies:	1999	1998
Colorado Historical Society	$ 19,650,541	$ 16,486,307
Colorado Department of Transportation	3,066,000	3,951,000
Colorado Department of Local Affairs	4,000,289	3,356,141
Colorado State Patrol	81,323	85,453
Colorado Bureau of Investigation	62,857	51,115
Colorado Department of Fire Safety	53,227	9,170
	26,914,237	23,939,186
State's General Fund:	27,322,158	21,543,896

13. RELATED PARTY TRANSACTIONS (CONTINUED)

Other governments:

City of Black Hawk	4,308,662	3,226,488
City of Central	1,118,607	1,216,042
City of Cripple Creek	1,590,781	1,445,437
City of Victor	175,451	147,199
City of Woodland Park	526,354	441,598
Gilpin County	6,512,722	5,331,036
Teller County	1,908,938	1,734,524
	16,141,515	13,542,324
	$ 70,377,910	$ 59,025,406

Total liabilities of $70,377,911 and $59,025,406 include liabilities due to the Colorado State Patrol, Bureau of Investigation, and Department of Fire Safety which total $197,407 and $145,738, and represent liabilities related to contractual agreements with these agencies. The remaining liabilities of $70,180,503 and $58,879,668 are related to the 1999 and 1998 gaming distributions.

INDEPENDENT AUDITORS' REPORT
ON REQUIRED SUPPLEMENTARY INFORMATION

Members of the Legislative
Audit Committee

The required supplementary information on pages 28-30 is not a required part of the basic financial statements of the Division of Gaming, Department of Revenue, State of Colorado (the "Division") as of June 30, 1999 and for the years ended June 30, 1999 and June 30, 1998, but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

August 10, 1999

DIVISION OF GAMING
DEPARTMENT OF REVENUE, STATE OF COLORADO
REQUIRED SUPPLEMENTARY INFORMATION
ON YEAR 2000 PREPARATIONS (UNAUDITED)
JUNE 30, 1999

The Year 2000 issue ("Y2K") arises because most computer software programs allocate two digits to the year date field on the assumption that the first two digits will be 19. Without reprogramming, such programs may interpret the Year 2000 as the year 1900. In addition, some programs may be unable to recognize the year 2000 as a leap year.

The Y2K issue may affect electronic equipment containing computer chips that have date recognition features - such as, environmental systems, elevators, and vehicles - as well as computer software programs. In addition, the Y2K issue affects not only computer applications and equipment under the Division's direct control, but also the systems of other entities with which the Division transacts business. Some of the Division's systems-related remediation efforts will not be fully determinable until the Y2K and thereafter. Management cannot guarantee that the Division is or will be Y2K ready, that the Division's remediation efforts will be successful in whole or in part, or that parties with whom the Division does business will be Y2K ready.

In early 1997, the legislature directed the Office of State Planning and Budgeting ("OSPB") and the Commission on Information Management ("IMC") to assess and report on the cost of Y2K readiness preparations. The IMC developed a process for assessing and monitoring Y2K project progress, and has asked State agencies other than higher education institutions to report on completion of stages for each critical system.

During the year ended June 30, 1999, the Division expended $116,687 in connection with various Y2K projects, primarily through contracts with parties external to the State. In addition, the Division has committed approximately $273,000 to these projects for Y2K compliance, which are planned for expenditure during fiscal year 2000.

At any given time, work on the Year 2000 issue with respect to each system deemed critical falls predominantly in one of the following stages:

- *Awareness stage -* Establishing a budget and project plan for dealing with the Year 2000 issue.
- *Assessment stage -* Identifying the systems and components for which Year 2000 work is needed.
- *Remediation stage -* Making changes to systems and equipment.
- *Validation/Testing stage -* Validating and testing changes that were made during the remediation stage.

Completion of any or all of the stages does not mean the Division's systems are, or will be Year 2000 ready or compliant.

The Division identified the Gaming Licensing and the Electronic Data Interchange ("EDI") systems as being deemed critical. The following table shows for each stage the number and percentage of total critical systems where the Division has completed work as of June 30, 1999.

	System		
	Stage of completion		
	Gaming Licensing		EDI
Stage	Phase I	Phase II	
Awareness	100%	100%	100%
Assessment	100%	100%	100%
Remediation	100%	70%	100%
Validation/testing	80%	0%	50%

The gaming licensing system is the Division's regulatory licensing and document imaging system. As discussed further in the "Audit Finding, Recommendations, and Division Responses" section of this report, the Division's original plan to implement a new gaming licensing system, along with Y2K compliance modifications was initiated in 1996 through a project to be performed in conjunction with the Department of Revenue's Information Technology Department. However, the project was abandoned in August 1998.

In March 1999, a contract was entered into with a third-party firm to implement the new gaming licensing system and Y2K modifications. However, the project is not expected to be completed until mid-December 1999. The installation of the gaming licensing system is being performed in two phases. Phase I consists primarily of the computer software applications necessary to process, document and track gaming licenses. Phase II consists primarily of computer software applications necessary to track time and expenses related to Division background investigations. At June 30, 1999, Phase I validation/testing was determined to be 80% complete, and in September 1999, the Division completed the validation/testing stage of Phase I, and began operating the Phase I application.

At June 30, 1999, Phase II remediation was determined to be 70% complete. The Division continues to monitor the progress of the Phase II remediation efforts. Because the remediation is not expected to be completed until mid-December 1999, the Division has developed a contingency plan, should Phase II not be operational. This contingency plan consists primarily of the Division utilizing existing computer systems, which have been tested by the Division, in with the date function can be altered to avoid failing on January 1, 2000.

DIVISION OF GAMING
DEPARTMENT OF REVENUE, STATE OF COLORADO
REQUIRED SUPPLEMENTARY INFORMATION
ON YEAR 2000 PREPARATIONS (UNAUDITED) (CONTINUED)
JUNE 30, 1999

The EDI system is the current tax filing system utilized by the Division. At June 30, 1999, EDI system testing was determined to be approximately 50% complete. In September 1999, the Division determined that EDI system testing was approximately 90% complete, and anticipates 100% completion in October 1999.

The Division does business with many external entities that may have Year 2000 problems. The Division makes no representation that these external entities are or will be Year 2000 ready or compliant.

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Members of the Legislative
Audit Committee

We have audited the financial statements of the Division of Gaming, Department of Revenue, State of Colorado (the "Division") as of June 30, 1999, and for the years ended June 30, 1999 and June 30, 1998, and have issued our report thereon dated August 10, 1999. We conducted our audits in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Division's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audits and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards.*

Internal Control Over Financial Reporting

In planning and performing our audits, we considered the Division's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level, the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended for the information of the members of the Legislative Audit Committee of the State of Colorado, and management of the Division. However, this report is a matter of public record and its distribution is not limited.

August 10, 1999

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Division of Gaming (10)

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Executive Director (2)
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