STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

A PERFORMANCE AUDIT
OF THE

ARIZONA RACING COMMISSION

APRIL 1981

A REPORT TO THE
ARIZONA STATE LEGISLATURE

REPORT 81-5

DOUGLAS R. NORTON, CPA
AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

April 3, 1981

Members of the Arizona Legislature
The Honorable Bruce Babbitt, Governor
Members of the Arizona Racing Commission

Ladies and Gentlemen:

Transmitted herewith is a report of the Auditor General, A Performance Audit of the Arizona Racing Commission. This report is in response to a September 11, 1980, resolution of the Joint Legislative Budget Committee.

The blue pages present a summary of the report; a response from the Commission is found on the yellow pages preceding the appendices.

My staff and I will be pleased to discuss or clarify items in the report.

Respectfully submitted,

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Enclosure

OFFICE OF THE AUDITOR GENERAL

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SUMMARY

The Office of the Auditor General has conducted a performance audit of the Arizona Racing Commission in response to a September 11, 1980, resolution of the Joint Legislative Budget Committee, in accordance with the provisions of Arizona Revised Statutes (A.R.S.) §41-1279.

The Arizona Racing Commission was created by the Legislature in 1949. The Commission is comprised of five Commissioners who serve without pay. Commissioners are appointed by the Governor and serve six-year terms.

Our review of the Arizona Racing Commission revealed that:

- The Arizona Racing Commission is not fulfilling its statutory responsibility to regulate racing participants through the licensing process. (page 11)

- Changes are needed in the Arizona Racing Commission's administration of capital improvement funds at racing facilities. (page 27)

- Procedures used by the Arizona Racing Commission to select and evaluate the contract chemist are inadequate. (page 49)

- The ability of the Arizona Racing Commission to prevent the use of prohibited drugs in racing has been impaired because certain staff members have not properly discharged their responsibilities. (page 57)

- The Arizona Racing Commission is not complying with the Open Meeting Law and the Workmen's Compensation Law. (page 67)

- Illegal loans have been made to licensees from the Race Track Benevolent Fund and the Greyhound Benevolent Fund. (page 71)

It is recommended that:

- The Commission obtain and process fingerprints of all applicants for licensure by:
  - seeking funding from the Legislature for seasonal, clerical positions to assist during peak workload periods, or
  - adopting the system used by the State Real Estate Department by arranging for a private company to be present at Commission offices for option of obtaining fingerprints from local law enforcement agencies.

- The Commission adopt a rule requiring stewards to enforce its policy to refer applications involving derogatory information to investigators for notification and/or follow-up. In addition, all instances of application falsification should be reviewed by investigators to determine if license revocation is in order.

- Permittees and Commission staff implement procedures readily available to control unlicensed activity, including increased visual checks of licenses and comparisons of racing programs to license files.

- The Commission provide for disciplinary action, including criminal prosecutions against individuals found to be unlicensed and against permittees and State stewards who fail to prevent such activity.

- The Commission ensure that applications are correctly prepared and complete, and that all applications are reviewed and signed. In addition, the Commission should discipline stewards failing to properly review applications.

- The Commission establish individual files for each licensee and consolidate information about each into these files.

- The Commission strengthen controls over existing records and files by locking files containing sensitive data and by implementing sign-out procedures for files.

- The Commission accounting unit verify that the proper fee is assessed for each license category by reconciling the licensing category on the left side of the audit copy of the fee receipt with the amount charged listed on the right side of the receipt.

- Proper accounting controls for cash, including segregation of duties, preparation of receipts, increased security and prompt deposits be established.

- The Commission require licensure of the officers and directors of permittees.

- The officers and directors thus licensed be fingerprinted and subjected to the same background investigation as other licensees.

- The Commission not approve the withholding of interest expense associated with the acquisition of improvements in Turf Paradise Projects TP-1 through TP-5.

- The Commission rescind its approval of rolling stock purchased as capital improvements at Turf Paradise and Prescott Downs. Further, the Commission should direct Turf Paradise not to withhold the funds for Turf Paradise Project TP-5 and should direct Prescott Downs to repay $23,953.61, which already has been withheld.

- The Commission request an opinion from the Attorney General to determine if Prescott Downs should be required to repay the entire $85,974.55 withheld for capital improvements.

- The Commission determine if expenses for a manager-supervisor are necessary for the promotion and betterment of county racing meets.

- The Commission require its staff to conduct detailed reviews of financial reports filed by the counties to verify that all reporting requirements have been met.

- The Commission encourage competitive bidding for the official chemist contract by advertising in national publications and contacting chemists within the State.

- The Commission revise the qualifications to bid to include current analytical chemistry standards.

- The Commission use outside professional services to evaluate the qualifications of competing bidders, based on criteria developed by the Commission.

- The Commission establish procedures for evaluating the performance of the official chemist, including use of split samples.

- The Commission take appropriate corrective action with the present official chemist by executing a probationary contract and enforcing compliance with its terms.

- The Commission study the feasibility of developing in-house facilities for chemical analysis.

- Commission veterinarians discontinue the use of Lasix as a means of collecting urine samples.

- Blood samples be tested for all animals which die immediately before, during or after a race.

- Greater use be made of the practice of testing additional samples from races, including <u>all</u> major races.

- Commission staff submit monthly reports to each Commissioner which include the following information:

  Number and type of samples submitted to the official chemist.

  Results of tests indicating the presence of prohibited substances.

  Animal deaths, causes of death and results of blood tests.

- Stewards' hearings be held in compliance with the provisions of the Open Meeting Law.

- The Commission comply with the provisions of A.C.R.R. R4-27-104.0 relating to the Workmen's Compensation Law.

- The matter of illegal loans made from the Race Track Benevolent Fund and the Greyhound Benevolent Fund be referred to the Attorney General's office to determine whether any liability exists either on the part of the Commissioners or their employees.

- A review be made to determine whether it is feasible to collect the unpaid loans.

INTRODUCTION AND BACKGROUND

The Office of the Auditor General has conducted a performance audit of the Arizona Racing Commission, in response to a September 11, 1980, resolution of the Joint Legislative Budget Committee, and in accordance with the provisions of Arizona Revised Statutes (A.R.S.) §41-1279.

The Arizona Racing Commission was created by the Legislature in 1949. The Commission is comprised of five Commissioners who serve without pay. Commissioners are appointed by the Governor and serve six-year terms.

The principal functions of the Commission include the licensing of racing personnel, the granting of racing permits to commercial greyhound and horse race meets and the granting of horse racing permits to county racing associations.

During fiscal year 1979-80, there were four commercial horse racing meets and seven commercial greyhound meets, which resulted in revenues to the State of $9,573,411. Revenues from licensing fees, fines and other sources totaled $55,791. During fiscal year 1979-80, the Commission granted permits to hold horse racing meets to 13 counties. The State provides purse monies and promotional funds to each county. The State receives no revenues from the county meets.

A.R.S. §5-113 requires that the Commission transmit all monies received as revenues to the State Treasurer, who allocates such revenues to recipients as follows:

1. Five percent for capital outlay to the Arizona Coliseum and Exposition Center Fund.
2. Seven and one half percent to the Arizona County Fairs and Breeders' Award Fund.
3. Ten percent to the Livestock, Agriculture and Breeders' Award Fund.
4. Seventy-seven and one half percent to the State General Fund.

Table 1 illustrates the distribution of the revenues collected by the Commission for fiscal years 1976-77 through 1979-80.

TABLE 1

DISTRIBUTION OF REVENUES COLLECTED BY THE ARIZONA RACING COMMISSION FOR FISCAL YEARS 1976-77 THROUGH 1979-80

Recipient	1976-77	1977-78	1978-79	1979-80
General Fund	$5,951,150	$6,500,102	$6,729,265	$7,464,358
Livestock, Agriculture and Breeders' Award Fund	758,176	838,723	867,734	962,071
Arizona County Fairs and Breeders' Award Fund	568,858	629,042	651,129	721,737
Arizona Coliseum and Exposition Center Fund	379,088	419,361	433,867	481,036
	$7,657,272	$8,387,228	$8,681,995	$9,629,202

During the same period, the total pari-mutuel handled in the State was as follows:

Fiscal Year	Total Pari-mutuel* Handled
1976-77	$137,049,025
1977-78	149,811,919
1978-79	173,963,795
1979-80	185,371,443

The Commission is funded by appropriations from the Legislature. Expenditures for fiscal years 1976-77 through 1980-81 are shown in Table 2.

* Webster's International Dictionary defines pari-mutuel as a form of betting in which those who bet on the winning animal share the total stakes, less a percentage to the track and to the State.

TABLE 2

EXPENDITURES FOR ARIZONA RACING COMMISSION FOR FISCAL YEARS 1976-77 THROUGH 1980-81 (ESTIMATED)

	1976-77	1977-78	1978-79	1979-80	(Estimated) 1980-81
Full-time equivalent positions	16.5	17.5	20.0	20.0	20.0
Personal services	$356,175	$377,810	$434,175	$461,315	$551,100
Employee-related	49,491	62,541	71,388	71,726	99,200
Professional & outside services	91,630	104,636	105,956	140,684	143,600
Travel - in-State	59,340	63,719	56,602	72,098	74,300
Travel - out-of-State	1,700	4,607	5,500	4,822	5,500
Other operating expenses	26,127	36,420	35,938	40,890	46,700
Equipment	600	5,185	1,364	199	
Total	$585,063	$654,918	$710,923	$791,734	$920,400

This is the first of two reports on the Arizona Racing Commission and covers the following areas:

1. Licensing procedures used by the Commission,

2. Capital improvements at commercial and county racing facilities,

3. Procedures used in contracting for drug testing,

4. Ability of the Commission to prevent the use of prohibited drugs in racing,

5. Review for compliance with statutes and administrative rules and regulations, and

6. Improper loans of state funds.

Work on the second report will commence as audit staff resources become available.

We express our gratitude to the Arizona Racing Commission and its staff for their cooperation, assistance and consideration during the course of the audit.

FINDING I

THE ARIZONA RACING COMMISSION IS NOT FULFILLING ITS STATUTORY RESPONSIBILITY TO REGULATE RACING PARTICIPANTS THROUGH THE LICENSING PROCESS.

State statutes require the Arizona Racing Commission to thoroughly investigate license applicants and to exercise discretion in granting licenses. The Commission annually licenses more than 10,000 persons to participate in racing as owners, trainers, jockeys, mutuel employees, exercise boys, jockeys' agents, stable foremen, grooms, valets, veterinarians, horseshoers, concessionaires and officials. Our review of the manner in which the Commission issues licenses revealed that:

- The Commission is not conducting required investigations of license applicants. As a result, license applicants who falsify information on their applications regarding criminal convictions or rulings by other racing jurisdictions go undetected.

- Racing stewards are not forwarding derogatory information about licensees to Commission investigators.

- Commission employees and permittees are not adequately reviewing racing participants. As a result, unlicensed persons participate in racing.

- Racing stewards are not imposing sufficiently stringent penalties against persons found to be participating in racing without a license.

- Commission employees are not following established procedures in issuing licenses, and Commission files are incomplete and disorganized.

- The Commission has not established an adequate system of control over the collection, recording and handling of license fees.

- The Commission's ability to regulate racing is impaired because it does not license officers and directors of racing-permittee organizations.

The Commission Is Not Conducting Required Investigations of Applicants

Arizona Revised Statutes (A.R.S.) §5-108.A requires the Commission to "...conduct a thorough investigation concerning the application for a...license...." The statutes further specify that licenses may be denied for: 1) rulings of or suspensions by other jurisdictions, 2) violations of the racing laws and regulations of Arizona or other states, 3) convictions of felonies or any crime involving moral turpitude, 4) convictions of bookmaking, and 5) applicants not being of good repute and moral character. (Emphasis added)

In spite of the above statutory requirements, the Commission is not thoroughly investigating license applicants. As a result: 1) applicants who falsify information on their applications regarding criminal convictions or rulings by other racing jurisdictions go undetected, and 2) the Commission has issued licenses to some persons who not only pose a threat to the integrity of racing, but to other racing participants as well.

Applicants for license are required to complete an application form giving such general information as name, date of birth, Social Security number, citizenship status and physical description. Applicants also are required to provide information about any criminal history, prior rulings by other racing jurisdictions, interest or ownership in race animals and the names of their previous employers.*

* Appendix I is a sample of a license application.

In order for the Commission to properly exercise its discretionary authority regarding the issuance of licenses it is essential that the information on the license application be truthful and accurate and that the Commission routinely verify the information on license applications. Our review of the Commission's licensing process revealed that such verifications either are not made in a timely manner or are not made at all.

License Application Information Is Not Adequately Verified

Administrative regulations for licensure state that "each applicant shall submit to being fingerprinted." (R4-27-104.B) In prior years applicants were fingerprinted and processed through the Federal Bureau of Investigation of the Department of Justice. However, this procedure was curtailed in recent years and virtually abandoned in 1980-81.

The Commission also has immediate access to the National Association of State Racing Information System (NASRIS), which maintains a computer file of rulings and suspensions issued by racing jurisdictions in the United States, Mexico and Canada. However, the Commission often does not process license applications through NASRIS until three to four weeks after an applicant has been licensed. Thus, applicants can be licensed for up to four weeks without previous violations and rulings coming to light.

As a result of the Commission's failure to adequately investigate license applicants, we estimate that at least seven* percent of the persons licensed by the Commission during fiscal year 1979-80 falsified information on their license applications regarding criminal convictions or rulings by other racing jurisdictions.

* An additional seven percent of the applicants had arrest records, but either had no convictions or else the disposition of the cases could not be determined. Disclosure of arrest data was not required on the 1979-80 application.

Falsified License Applications

Part of our review of the Commission's licensing process was to select a statistical sample of persons licensed by the Commission during fiscal year 1979-80, and to process those persons through the State's Department of Public Safety, the Federal Bureau of Investigation and NASRIS. A finding of this procedure was that seven percent of those persons processed failed to disclose, or only partially disclosed, criminal convictions and/or rulings against them by other racing jurisdictions. The unreported criminal convictions included those for aggravated battery, possession and sale of heroin, grand theft, white slavery, rape, robbery, breaking and entering, and possession of marijuana. In our opinion, some of the persons licensed by the Commission in fiscal year 1979-80 pose a threat not only to the integrity of racing but to other racing participants as well, as the following cases illustrate.

CASE I

The Commission licensed to work on the starting gate an applicant who had been arrested four times and convicted three times for possession with intent to distribute heroin, aggravated battery and leaving the scene of an accident.

CASE II

The Commission licensed an applicant to work as a trainer. The licensee's application stated that he had been convicted for "marijuana pro."* Commission employees did not fingerprint the applicant or conduct further investigation. As of January 24, 1981, this licensee in actuality had the following criminal history:

- two sexual-assault and rape charges,
- four robbery and breaking-and-entering convictions,
- two white-slavery convictions,
- two assault charges,
- several attempted jail escapes, and
- one conviction for transporting a truckload of marijuana.

By the time the Commission investigators became aware of his background, there was also an outstanding warrant for attempted sexual assault.

* Assumed to mean procurement.

Causes of Inadequate License Application Verification

According to the Executive Secretary of the Commission, fingerprinting was discontinued because of workload and budget constraints. Since fiscal year 1977-78, the number of licenses issued has increased by 13 percent while Commission staff has remained constant. In addition, the licensing workload is primarily seasonal, having two peak periods in July and August and between October 1 and December 15,* when approximately 70 percent of all license applications are received. Existing staff is not adequate to handle the workload at these times and backlogs of three to four weeks in license processing occur.

The following three options appear to be available to allow the Commission to resume the practice of fingerprinting license applicants:

- Provide the Commission with additional funds to pay for seasonal employees (totaling 1.5 full-time equivalent positions) to process fingerprints through the Federal Bureau of Investigation and to do other licensing processing to reduce backlogs. We estimate the cost associated with this option to be $21,000 a year.

- Use the services of private fingerprinting companies in the same manner as does the State Real Estate Department, which fingerprints and processes more than 24,000 applicants a year. The State Real Estate Department offers applicants two methods of supplying their fingerprints: 1) applicants may obtain fingerprints at no charge at their local law enforcement agency, or 2) the applicants may use the services of a private company which the Department arranges to have at its offices. Those applicants using the private companies pay $3 for the service. This option would not require additional funding for the Commission, but would not reduce backlogs.

* Currently, all licenses are valid from July 1 to June 30. The Commission plans to change licensing dates to have horse racing licenses valid from January 1 to December 31 and dog racing licenses from July 1 to June 30. Our analysis indicates this may change the timing of the peak periods, but that peak periods still will occur.

- Provide the Commission with additional funds to pay for seasonal employees and use the services of private fingerprinting companies. We estimate the cost associated with this option to be $14,000 a year.

Racing Stewards Are Not Forwarding Derogatory Information About Licensees To Commission Investigators

Racing stewards are responsible for reviewing and approving license applications. As such, stewards have access to information regarding criminal convictions and/or rulings by other racing jurisdictions against license applicants when such information is shown on the application. We determined that only one steward refers such information to investigators for follow-up or notification purposes, and that he does not make such referrals in all cases.

The need to refer such application information to investigators is evidenced by the case detailed on page 14. In that case, the license application did contain information regarding a prior drug conviction. The steward who approved the application did not forward the license information to Commission investigators. As a result, the individual's entire criminal record, involving more than 27 criminal charges and 10 convictions, did not come to light until the investigators heard about it from "backside" track sources -- three months after the license was granted.

The failure of stewards to forward criminal history information to investigators is in sharp contrast to procedures followed by the Department of Insurance, which has its investigators follow-up all license applicants for whom there is evidence of prior wrongdoing.

Current Commission rules and regulations give stewards broad discretionary authority in reviewing and approving licenses. In our opinion, the Commission should adopt a rule to require stewards to forward derogatory information about licensees to Commission investigators for notification and/or follow-up.

Commission Employees and Permittees Are Not Adequately Reviewing Racing Participants

A.R.S. §5-107.01 specifically requires all persons participating in racing in Arizona to obtain licenses and permits. Additionally, administrative regulation R4-27-104.E specifies "if a licensee is employed in more than one category, or changes from one to another, he must be licensed in each category."

Our review of racing participants revealed that unlicensed individuals are participating in racing in spite of administrative requirements that permittees ensure compliance with the above statute and rule.

Arizona Racing Commission Administrative Regulation R4-27-104.K states:

> "It shall be the responsibility of the permittee to prevent any person not licensed by the Commission from doing or performing any act or acts at its track which requires a license under A.R.S. Chapter 1, Title 5, or these regulations." (Emphasis added)

As a means to determine if permittees are preventing unlicensed persons from participating in racing in Arizona we: 1) selected a sample of persons and corporations listed in the daily racing programs during calendar year 1980 and the month of January 1981, and 2) checked to see if those persons were, in fact, licensed. Our sample included persons and corporations listed as owners, trainers, jockeys and kennels. Five percent of the persons and corporations we checked were not properly licensed as required by statutes and/or regulation.

Some of the individuals in our sample had been unlicensed for as long as a year and were participating as jockeys, owners, permittee officials and stewards. The following cases illustrate some of the unlicensed activity we documented.

CASE I

The participant was listed in the November 1, 1980, Rillito Downs program as a jockey and participated in each racing day during the meet. The individual did not obtain a license until January 27, 1981.

CASE II

The participant was listed as an owner on the Greenlee County Fair racing meet program on April 5, 1980. At that time, the participant was not licensed. The participant subsequently was issued a jockey's license on May 10, 1980.

CASE III

A company or corporate name appears under kennel name on the Phoenix Greyhound Park racing program of March 1, 1980. The company did not have a kennel license and no licensed owner could be found who was directly connected with the kennel.

It appears that permittees could prevent unlicensed persons from participating in racing more effectively if they made better use of enforcement methods currently available. For example, permittees could require individuals to show their licenses (which are photo-identification licenses similar to drivers' licenses) before performing activities such as registering race animals, collecting purse money or entering the jockey room. This would be consistent with administrative regulation R4-27-103.I, which states that the permittees shall:

> "...furnish an officer to be on duty at the stable or kennel area entrance and it shall be the duty of said officer to deny entrance to all persons not holding a license or credentials issued by the Commission or a pass issued by the permittee."

Another enforcement method would be for the permittees and Commission employees to regularly and periodically check the names appearing in the daily racing programs against persons licensed by the Commission. This is the method audit staff used to determine unlicensed activity and is sometimes used by Commission licensing clerks to identify unlicensed participants.

Racing Stewards Are Not Imposing Sufficiently Stringent Penalties Against Unlicensed Persons

Arizona statutes provide for criminal penalties if persons participate in racing without first obtaining a license. However, stewards rarely impose sanctions against persons found to be participating in racing without a license.

A.R.S. §5-115.C states:

> "Any person who holds or conducts any racing meeting without first complying with the provisions of this article, or any person who violates any provision of this article for which no other penalty is prescribed, is guilty of a class 2 misdemeanor."

A.R.S. §5-115.C is a general section prescribing penalties for violations of racing statutory requirements. The maximum penalty for a Class 2 misdemeanor is a fine of $750 and four months imprisonment.

A.R.S. §5-115.C notwithstanding, when stewards identify unlicensed racing participants, disciplinary sanctions rarely are imposed. The single most common disciplinary action taken is to "make them get a license." Such an action appears to provide little incentive for individuals to get licensed or for permittees to ensure that unlicensed activity does not occur.

Similarily, the Commission does not appear to take action against stewards when unlicensed activity is found at a race meeting under their supervision. Inasmuch as the steward is responsible for ensuring compliance with all laws and regulations during a race meeting, the occurrence of unlicensed activity reflects upon the performance of the steward and may warrant disciplinary action by the Commission against the steward.

Commission Employees Are Not Following Established Procedures in Issuing Licenses and Commission Files Are Incomplete and Disorganized

Commission licensing procedures require that license applicants sign their applications in the presence of a Commission official or notary and that Commission officials and stewards review the applications. Further, Administrative Rule R4-27-104 requires stewards to review license applications to ensure that the integrity and ability of an applicant is clearly shown on his application. These procedures are not followed in most cases. In addition, Commission licensing files are incomplete and disorganized.

As part of our review of the licensing procedures of the Commission, we selected a sample of fiscal year 1979-80 license applications and tested for compliance with established Commission licensing procedures and rules. The findings of our review were:

- Sixty-nine percent of the license applications were not reviewed by a steward, and
- Fifty-three percent of the license applications were not signed in the presence of a Commission official or notarized.

In addition, many incomplete applications are accepted. We observed applications lacking such information as dates of birth, employers, names of animals, applicants' signatures, and details of prior rulings and criminal histories.

This observed failure to comply with established procedures not only could result in unqualified persons being licensed, but impairs the Commission's ability to regulate participants as well. For example, information on the ownership of animals is used in regulating hidden ownership, and applicant's date of birth is used in conducting background investigations.

Our review also revealed that Commission files are incomplete and disorganized. For example, files are not maintained by individual licensees. Instead, data on a particular licensee may be in any of four or five different files.

Licensing records also appear to be incomplete. We found that no records exist in the Commissions files for 20 percent of the persons who reported on their license applications that previous rulings and criminal records were "on file" with the Commission. Similarily, we found that fingerprints do not exist for 68 percent of the persons who reported on their license applications that they had been fingerprinted previously by the Commission.

In addition, the Commission has not established "sign-out" procedures for files. Investigators and other Commission personnel often take files without indicating where the file will be in the event somebody needs to locate it.

Finally, we noted that controls over the files and records are weak. For example, although fingerprint cards can contain sensitive information, we noted that fingerprint cards were left lying about on desk tops and that the fingerprint files were not locked.

The Commission Has Not Established An Adequate System of Control over the Collection, Recording and Handling of License Fees

Control over the collection, recording and handling of license fees is weak in the Commission licensing offices. As a result, there is an unaccountable difference of $3,969 in license fees during fiscal year 1979-80.

During our review of the Commission licensing function, we noted the following weaknesses in control over license fees.

- There is incomplete verification of fee receipts. The license categories listed on one part of the license fee receipts do not agree with the fees assessed listed on the same receipts.

- There is no segregation of duties among those Commission employees who collect fees, prepare receipts and prepare daily audit sheets.

- Commission offices located at commercial greyhound and horse racing facilities and at county racing meets do not use cash registers or other security devices. It was noted that cigar boxes are used to secure cash and checks at track facilities, and that these cigar boxes are not safeguarded when Commission employees leave the office.

- Access to the Commission office is not limited to Commission employees. Frequently, the permittee and other individuals have access to the Commission office, because duplicate keys have been provided by stewards to non-State employees.

- Commission employees do not deposit cash on a timely basis. During peak licensing periods, Commission employees do make deposits daily. However, at other times, deposits are made only every two weeks to a month, and at any one time the Commission office may have a significant amount of cash on hand.

As a result of the above weaknesses, there was a $3,969 difference between license fees that should have been collected, based upon the reported number of licenses issued, and fees actually collected during fiscal year 1979-80. The reported numbers and types of licenses issued by the Commission during fiscal year 1979-80 indicate the total fees should have been $51,279. However, the actual license fees for fiscal year 1979-80 were only $47,310.

Neither the Commission accountant nor the licensing unit supervisor was able to explain the $3,969 difference. The Commission accountant suggested the difference might be attributed to persons being charged the wrong fees for licenses. We found, however, that improper assessments can account for only a small portion of the $3,969 difference. Another explanation might be that the number of licenses issued as reported by the Commission's licensing supervisor, and which we used in calculating the $51,279 shown above, is incorrect. In that case, it is not possible, given the current condition of the Commission's licensing records, to determine the amount of licensing fees that should have been collected.

Commission Ability to Regulate Racing Is Impaired Because It Does Not License Officers and Directors of Racing Permittees

The Commission does not require that individual officers and directors of racing permittees be licensed. Consequently, the Commission has no means to discipline those individual officers or directors who violate Commission rules and regulations.

The Commission has the statutory authority to require that individual officers and directors of permittees be licensed. A.R.S. §5-107.01.B requires licensure of occupations involved in racing and "...any other person or official the Commission deems proper." However, the Commission has not chosen to require licensure for officers and directors of permittees. Such licensure is not uncommon in that 15 other state racing jurisdictions require permittee officers to be licensed, and 12 require permittee directors to be licensed.

Because the Commission does not license the officers and directors of permittees, it cannot take action against those individuals who violate the Commission's rules and regulations. Currently, the Commission can take action only against the permittee and can revoke or suspend the permit. However, it may not be desirable, feasible or equitable to revoke the permit for an entire race meet because of the actions of an individual officer or director.

In addition, the licensing of officers and directors of permittees would allow the Commission to obtain fingerprints and background data needed to allow for a complete investigation of these individuals.

CONCLUSION

The Commission is not fulfilling its statutory responsibility to regulate racing participants through the licensing process. As a result, individuals are participating in racing who pose a threat to the integrity of racing and other racing participants, license fees are unnecessarily exposed to loss through theft or defalcation and the Commission's ability to regulate racing is impaired.

RECOMMENDATIONS

It is recommended that:

- The Commission obtain and process fingerprints of all applicants for licensure by:
  - seeking funding from the Legislature for seasonal, clerical positions to assist during peak workload periods, or
  - adopting the system used by the State Real Estate Department by arranging for a private company to be present at Commission offices for applicant fingerprinting, or giving the applicants the option of obtaining fingerprints from local law enforcement agencies.

- The Commission adopt a rule requiring stewards to enforce its policy to refer applications involving derogatory information to investigators for notification and/or follow-up. In addition, all instances of application falsification should be reviewed by investigators to determine if license revocation is in order.

- Permittees and Commission staff implement procedures readily available to control unlicensed activity, including increased visual checks of licenses and comparisons of racing programs to license files.

- The Commission provide for disciplinary action, including criminal prosecutions against individuals found to be unlicensed and against permittees and State stewards who fail to prevent such activity.

- The Commission ensure that applications are correctly prepared and complete, and that all applications are reviewed and signed. In addition, the Commission should discipline stewards failing to properly review applications.

- The Commission establish individual files for each licensee and consolidate information about each into these files.

- The Commission strengthen controls over existing records and files by locking files containing sensitive data and by implementing sign-out procedures for files.

- The Commission accounting unit verify that the proper fee is assessed for each license category by reconciling the licensing category on the left side of the audit copy of the fee receipt with the amount charged listed on the right side of the receipt.

- Proper accounting controls for cash, including segregation of duties, preparation of receipts, increased security and prompt deposits be established.

- The Commission require licensure of the officers and directors of permittees.

- The officers and directors thus licensed be fingerprinted and subjected to the same background investigation as other licensees.

FINDING II

CHANGES ARE NEEDED IN THE ARIZONA RACING COMMISSION'S ADMINISTRATION OF CAPITAL IMPROVEMENT FUNDS AT RACING FACILITIES.

As of January 1, 1981, ten states had legislation which assisted commercial horse racing associations in making capital improvements to their facilities; nine states provided capital improvement funds to their county racing commissions; and two states had legislation which assisted commercial greyhound facilities in making capital improvements.

As a part of our performance audit of the Commission, we reviewed the administration and allocation of capital improvement funds to commercial horse racing facilities and counties in Arizona. Our review revealed that:

- As of December 31, 1980, the $1,505,011 withheld for projects at Turf Paradise are within the provisions of A.R.S. §5-111.02. In addition, some allegations regarding capital improvement funds used at Turf Paradise appear to be true while others appear to be untrue.
- The Commission improperly approved $229,044 in capital improvement funds for Turf Paradise and Prescott Downs for the purchase of rolling stock.
- Prescott Downs may owe the State $85,974.55 if its purchases do not qualify as capital improvements.
- Capital improvement projects at Rillito Downs are within the provisions of A.R.S. §5-111.02.
- Financial improprieties have occurred in at least two counties.
- The Commission has not adequately and consistently reviewed the distribution and expenditure of capital improvement funds awarded to the counties.

Arizona has no provision for financial assistance to commercial greyhound facilities for capital improvements.

A.R.S. §5-111.02* provides for the State to subsidize capital improvements at commercial horse racing facilities. The section was adopted to encourage the improvement of racing facilities for the benefit of the public, breeders and horse owners, and to increase the revenues to the State from the increase in pari-mutuel wagering resulting from such improvements. Commercial horse-racing permittees who receive approval for capital improvements are allowed to reduce the percentage paid to the State by one percent of the total amount wagered.

A.R.S. §5-111.02.B states:

> "In order to qualify for the reduction in percentage, a permittee shall first apply to the commission in such form as the commission shall require. The application shall contain, but is not limited to, full details of the proposed capital improvement and the cost and expenses to be incurred. After receipt of the application the commission may tentatively approve or may disapprove such application and shall, within ten days of such tentative approval or disapproval, transmit a copy of the application and notification of tentative approval or disapproval to the president of the Arizona senate and speaker of the Arizona house of representatives. If the commission tentatively approves an application it shall conduct periodic inspection of at least one per month during the construction period of the capital improvement in order to ascertain compliance with the permittee's application. Upon completion of the construction of the capital improvement, the permittee shall notify the commission and may seek final approval of its application by the commission. When the construction cost has been certified by the commission pursuant to subsection E and the commission has determined the permittee's compliance or noncompliance with its application, the commission shall grant final approval of such application or shall disapprove such application. The commission shall not approve an application unless it determines that the capital improvement will promote the safety of horses, the safety, convenience and comfort of the people and is in the best interest of racing and the State of Arizona generally. If the commission grants final approval of the application the permittee shall qualify for the reduction in percentage."

* See Appendix 2 for the text of A.R.S. §5-111.02.

As of February 28, 1981, five horse-racing permittees at three racing facilities are withholding funds for capital improvements. Table 3 lists each permittee along with the total amount withheld at each facility from July 1, 1978, through December 31, 1980.

TABLE 3

TOTALS WITHHELD BY RACING PERMITTEES FOR CAPITAL IMPROVEMENTS AS AUTHORIZED BY A.R.S. §5-111.02 FROM JULY 1, 1978, TO DECEMBER 31, 1980

Turf Paradise, Inc.*	$1,505,011.28
Turf Paradise	
Arizona Downs	
Desert Downs	
Prescott Downs	85,974.55
Rillito Downs	107,248.94
	$1,698,234.77

Turf Paradise

Turf Paradise has been the primary recipient of capital improvement funds. As of February 24, 1981, a total of eight projects costing $9,653,298 have received tentative Commission approval, of which three projects costing $4,270,375 have received final Commission approval.

Table 4 summarizes the proposed capital improvement projects at Turf Paradise as of February 24, 1981, and includes a description of each project, its estimated cost and the date on which tentative approval was given. For those projects which have received final approval, the date of final approval is noted along with the final cost of the project and the amount withheld by Turf Paradise to recoup those costs.

* Funds are being withheld by the three permittees at Turf Paradise. A.R.S. §5-111.02 directs permittees who lease racing facilities to pass the capital improvement funds withheld on to the owner of the facility. As such, Turf Paradise, Arizona Downs and Desert Downs pass the capital improvement funds to Turf Paradise, Inc.

TABLE 4
SUMMARY OF CAPITAL IMPROVEMENT PROJECTS AT
TURF PARADISE AS OF FEBRUARY 24, 1981

Project Number	Description	Initial Estimated Cost	Date of Tentative Approval	Revised Cost Per Report of March 24, 1980	If Given, Date of Final Approval	Actual Cost	Total Amount Withheld as of December 31, 1980
TP-1	Paving of parking lot, stable areas and drainage system	$ 490,000	June 20, 1978	$ 469,918	September 26, 1978	$ 485,018	$ 485,018
TP-2	Machine shop, warehouse and hay barns	235,000	June 20, 1978	396,837			
TP-3	Grandstand alterations, Phase I	2,300,000	June 20, 1978	3,595,235	January 30, 1979	3,595,235	1,019,993
TP-4	Horse barns	882,000 *	June 20, 1978	1,092,614			
TP-5	Race track and stable area maintenance vehicles	188,298	September 26, 1978	175,413	December 28, 1978	190,122	
TP-6	Grandstand alterations, Phase II	4,450,000	February 7, 1979	5,702,812			
TP-7	Renovation of ground floor to accommodate new pari-mutuel equipment	472,000	February 23, 1979	1,272,014			
TP-8	Installation of turf track	636,000	February 23, 1979	1,032,606			
		$9,653,298		$13,737,449		$4,270,375	$1,505,011

* The original request for TP-4, dated June 20, 1978, was for $432,000. On December 28, 1978, the Commission granted tentative approval to an increased project amount of $882,000.

Our review of the use of capital improvement funds at Turf Paradise revealed that: 1) as of December 31, 1980, the $1,505,011 withheld by Turf Paradise, Inc. is for projects that are within the provisions of A.R.S. §5-111.02, and 2) some allegations regarding capital improvement funds appear to be true while others appear to be untrue.

Funds Withheld As Of December 31, 1980

As a part of our review of the use of capital improvement funds at Turf Paradise, we reviewed all documents which have been filed at the Commission office by Turf Paradise, Inc. Additionally, we reviewed the accounting records of Turf Paradise, Inc., verified the existence of claimed improvements, and reviewed the audit workpapers prepared by the auditors for Turf Paradise, Inc. to support audit reports which have been filed by Turf Paradise, Inc. with the Commission. Based upon these procedures, we have determined that, as of December 31, 1980, the $1,505,011 withheld by Turf Paradise, Arizona Downs and Desert Downs for capital improvements at Turf Paradise are within the provisions of A.R.S. §5-111.02.

Allegations Regarding Capital Improvements

During our preliminary review of the Commission we became aware of several allegations regarding capital improvements at Turf Paradise. We subsequently researched Commission files, reviewed transcripts of Commission meetings and interviewed Commission members and staff to compile a list of all allegations concerning capital improvements at Turf Paradise.

During January and February 1981, Auditor General staff investigated each allegation. These allegations are detailed below.

Allegation

The president and general manager of Turf Paradise used Turf Paradise employees and equipment to work at his residence and that of his brother. Allegedly, the employees' time and equipment charges were charged to the capital improvement account.

Review Results

Labor and equipment charges for work at locations other than Turf Paradise are not included in the cost of capital improvements at Turf Paradise. Further we did not see records or documents relating to work done at the residence of the president's brother. However, we determined that Turf Paradise employees and equipment were used at the residence of the president and general manager of Turf Paradise.

The following is a chronology of the events surrounding this allegation.

March 1979 to November 1979 - Employees of Turf Paradise and the construction company under contract to construct improvements at Turf Paradise built a retaining wall and made other improvements at the residence of the president.

March 1979 to February 1980 - A construction company owned largely by the president provided heavy equipment used in the construction of improvements at Turf Paradise without charge to Turf Paradise.

January to May 1980 - Staff from the Commission questioned the president and other officials regarding the use of Turf Paradise employees and equipment at his residence.

February 1980 - The president contracted with an independent accounting firm to examine the cost summary report.

April 1980 - The president submitted a cost summary report to the Commission to support his contention that the cost of equipment donated to Turf Paradise by his company offset the cost of the labor and equipment used on his residence. According to the cost summary, the cost of the equipment donated to Turf Paradise was $54,408 and the cost of the labor and equipment used on the president's residence was $51,231.

April 3, 1980 - Specific allegations of impropriety were raised at a meeting of the Commission. Officials of Arizona Downs questioned whether capital improvement funds at Turf Paradise are being managed properly.

April 28, 1980 - In a report submitted to the Commission the accounting firm concluded that the cost of labor and equipment used at the president's residence exceeded the cost of the equipment donated to Turf Paradise by $7,352. According to the accounting firm, the cost of the labor, material and equipment used on the president's residence was $216,126 and the cost of the equipment donated to Turf Paradise was $208,772. It was noted on the report that the president had paid the $7,352 difference on April 21, 1980.

It should be noted that Auditor General staff reviewed the work by Turf Paradise's auditors in examining the cost summary report. Our review determined that time cards were not prepared by employees of Turf Paradise nor were they prepared by employees of the general contractor. Time cards were prepared in December 1980 for work at the residence of the president, and were used to support the labor charges shown in the cost summary prepared by the president. However, these time cards were prepared up to nine months after the actual work. The auditors who examined the cost summary did not rely on those time cards to determine appropriate labor expenses. Instead, they used labor reports which were prepared on a weekly basis by job superintendents to determine appropriate labor costs.

In our opinion, their examination was adequate and their conclusions reasonable and supportable. Therefore, as of February 24, 1981, it appears that labor and equipment charges for work at locations other than Turf Paradise are not included in the cost of capital improvements at Turf Paradise.

Allegation

Turf Paradise did not solicit bids on capital projects in spite of Commission orders to do so.

Review Results

On June 20, 1978, the president submitted a request for preliminary approval for TP-1 through TP-4 (see Table 4). These requests received tentative approval from the Commission on June 20, 1978. Immediately thereafter, the Commission requested that Turf Paradise solicit bids for future requests for tentative Commission approval. Turf Paradise did solicit bids for the vehicles obtained as TP-5; however, no bids were solicited for TP-6, TP-7 or TP-8 (see Table 4). These are major construction projects, and Turf Paradise intends to use the same general contractor for all construction work.

A review of the transcript of an April 3, 1980, meeting of the Commission revealed that the Commissioners were aware of the fact that bids had not been solicited for TP-6, TP-7 and TP-8. The transcript states, in part:

(Representative of Turf Paradise):

> "We did not go out for competitive bids. There is no way we could have taken competitive bids on that project and do it in the time frame...We got competitive bids on the equipment purchases, but there was no way, under the time elements that were involved, that we could have gotten competitive bids..."

(Commissioner):

> "As I remember, that was done with a concurrence of the Commission. I know we discussed it, at the time...but we did okay not getting competitive bids on the general contractor because we felt that he was the best man to get it done."

Members of the audit staff met with the Commission to discuss this allegation. The Commissioners stated that while they expect competitive bids to be solicited whenever possible, they also recognize that it may not be possible to solicit bids in every instance.

Allegation

Turf Paradise received tentative Commission approval for capital projects estimated to cost $9.2 million. However, cost information submitted by Turf Paradise on March 19, 1980, showed that costs had risen to more than $13.7 million. Allegations have been made that the increase in costs for capital improvements is not fully justified.

Review Results

Costs to modify and expand the grandstands at Turf Paradise were significantly higher than expected initially because, before the new structure could be attached to the original structure, unexpected and extensive modifications had to be made to the original structure. These modifications were required because the original structure did not meet current building safety codes. There are change orders to the original contract to support these costs.

We reviewed the original contract for capital improvements at Turf Paradise, each contract change order and safety code compliance orders. We also inspected the structures in question. All of the contract change orders did involve capital improvements and, as such, should be classified as capital improvements in accordance with the provisions of A.R.S. §5-111.02.

Allegation

Despite the payment of capital improvements funds to Turf Paradise, the general contractor for Turf Paradise has not been paid about $300,000 for work already completed.

Review Results

Our review revealed that the allegation stems from a problem which developed over a contractor's refusal to make contractuarily required repairs to improvements until he was paid the $295,000 by Turf Paradise. Similarly, Turf Paradise refused to pay the contractor until the work was completed.

Attorneys for both parties met and the dispute was settled. The work has been completed and Turf Paradise has paid the $295,000 to the contractor.

Allegation

Capital improvement funds were used to build office space for a private company owned largely by the president of Turf Paradise. The office facilities are located at Turf Paradise.

Review Results

During the course of our review, we did not discover information which would support this allegation.

Allegation

Capital improvement funds were used to acquire antiques and other expensive furnishings for the "board rooms" at Turf Paradise.

Review Results

Our review of the audit workpapers prepared by the auditors for Turf Paradise, the accounting records at Turf Paradise and all available documents on file with the Commission revealed that Turf Paradise has not purchased furniture or antiques as capital improvements.

Allegation

Turf Paradise had added costs to the capital improvement accounts beyond those charged by the contractor. Turf Paradise received a permit from the city to remove sand from two locations. It was alleged that Turf Paradise charged more than $100,000 for the cost of the sand to the capital improvements account.

Review Results

As of February 28, 1981, the allegation cannot be confirmed or refuted. During 1979, Turf Paradise had several tons of dirt removed from two river bottoms in the Valley area for use on the track and in the construction of its new turf course. According to the president and his legal counsel, the costs of labor and transportation required to move the sand to the turf course are the only costs associated with the sand that will be included in TP-8.

The turf course is TP-8 (see Table 4). Tentative approval for this project was given by the Commission on February 23, 1979. Turf Paradise has not submitted the audit report for TP-8 as of February 28, 1981. Therefore, it is not possible to confirm or refute the allegation.

Allegation

Turf Paradise intends not only to withhold funds to offset the cost of capital improvements, but also to withhold the interest expense associated with loans Turf Paradise entered into in order to finance improvements.

Review Results

According to the president, he intends to request permission to withhold funds to cover the interest expense associated with the cost of financing improvements at Turf Paradise. He stated that withheld funds first would be used to recoup the cost of the improvements and then withheld to recoup the interest expense associated with loans Turf Paradise entered into in order to finance the improvements. Our review of the accounting records relating to the construction and acquisition of capital improvements at Turf Paradise revealed that the total interest expense associated with those acquisitions is approximately $3,750,000.

Transcripts of Commission meetings reveal that the Commission had interpreted A.R.S. §5-111.02 to allow Turf Paradise to recoup the interest expense associated with the acquisition of capital improvements. That interpretation appears to be incorrect.

According to Financial Accounting Standards Board (FASB)-34,* interest expense associated with the acquisition of an asset may be capitalized only during the period the asset is being acquired or made ready for use. Once the asset is in place and ready for use, additional interest expense should not be capitalized. Accordingly, we estimate the maximum interest expense that Turf Paradise may capitalize is $376,000, rather than total interest expense of $3,750,000. However, it should be noted that FASB-34 states that interest that has been capitalized must be disclosed in financial statements as a note or footnote. Such a disclosure has <u>not</u> been made in reports filed by Turf Paradise with the Commission for TP-1 through TP-5. Therefore, Turf Paradise may not be able to capitalize and/or recoup <u>any</u> interest expense associated with TP-1 through TP-5.

<u>Allegation</u>

Turf Paradise purchased equipment as capital improvements and subsequently sold the equipment.

<u>Review Results</u>

Our review did not indicate that the cost of the electrical items had been claimed as part of capital improvements. Turf Paradise acquired electrical items to be used in the construction of the grandstand. The items subsequently were not required and they were sold, at cost, to an outside party.

* See Appendix 3 for the major provisions of FASB-34.

The Commission Improperly Approved $229,044 in Capital Improvements To Turf Paradise And Prescott Downs for the Purchase of Rolling Stock

Our review of reports filed with the Commission revealed that the Commission approved requests from Turf Paradise and Prescott Downs to use capital improvement funds to purchase tractors, trucks and equipment. The cost of these items purchased by Turf Paradise and Prescott Downs was $190,122.00 and $38,921.64, respectively. These acquisitions do not appear to qualify as capital improvements under the provisions of A.R.S. §5-111.02.D.

In a February 13, 1981, opinion, the Legislative Council stated:

> "The State accounting manual classifies the purchase of automobiles and trucks as a capital outlay expenditure. However, in the situation described, a special more limited legislative definition of capital improvement controls.
>
> "To qualify for approval, a capital improvement, under the definition prescribed by A.R.S. Section 5-111.02, Subsection D, must be at least a $100,000 addition, replacement or remodeling of a race track facility and must also fall within the standard prescribed by Subsection B of that Section in that it must:
>
> > "Promote the safety of horses, the safety, convenience and comfort of the people and is in the best interests of racing and the State of Arizona generally.
>
> "The purchase of automobiles or trucks clearly would not comply with these standards."*

Based upon the above interpretation, the Commission should not have approved the acquisition of rolling stock as a capital improvement, and Turf Paradise and Prescott Downs should not be allowed to withhold funds to cover the costs of those vehicles.

* See Appendix 4 for the full text of this opinion.

Prescott Downs May Owe the State $85,974.55 If Its Purchases Do Not Qualify As Capital Improvements

On August 17, 1978, the Commission granted final approval to Prescott Downs to withhold $100,943 to cover the cost of building horse stalls and acquiring a tractor and a water truck. If the tractor and water truck do not qualify as a capital improvement (see page 39), then: 1) the remaining cost for horse stalls at Prescott Downs will not qualify as a capital improvement because it is less than $100,000, and 2) Prescott Downs will have to repay the State the $85,974.55 it had withheld as of December 31, 1980, to cover the cost of the horse stalls, tractors and water truck.

On June 20, 1978, officials for Prescott Downs appeared before the Commission to present a proposed program of capital improvements. The proposal estimated that the cost of the project would be $103,850.

The Commission granted tentative approval to the project on June 20, 1978. On August 17 of the same year the Commission was notified that the improvements had been completed at a total cost of $100,943. The Commission granted final approval to the project on the same day. On August 19, Prescott Downs began withholding one percent of total wagers as provided for by A.R.S. §5-111.02. As of December 31, 1980, Prescott Downs had withheld a total of $85,974.55.

Table 5 summarizes the capital improvements project for Prescott Downs as approved by the Commission as of December 31, 1980.

TABLE 5

APPROVED CAPITAL IMPROVEMENTS AT PRESCOTT DOWNS AS OF DECEMBER 31, 1980

Description	Tentatively Approved Amount	Finally Approved Amount	Amount Withheld
55 horse stalls	$ 65,450.00	$ 62,020.94	$62,020.94
Diesel tractor and equipment	15,000.00	20,914.79	20,914.79
Water truck	23,400.00	18,006.85	3,038.82
	$103,850.00	$100,942.58	$85,974.55

Our review revealed that the Commission apparently approved improperly $38,921.64 in capital improvements for the purchase of the diesel tractor and water truck (see page 39). Additionally, if the $38,921.64 for vehicles at Prescott Downs is disallowed, the entire $100,942.58 approved for Prescott Downs may be invalid.

A.R.S. §5-111.02.D states:

> "The term 'capital improvement' means an addition, replacement, or remodeling of a race track facility involving an expenditure of at least one hundred thousand dollars. Capital improvement does not include the cost of ordinary repairs and maintenance required to keep a race track facility in ordinary operating condition." (Emphasis added)

The total cost of the 55 horse stalls does not comply with the provisions of A.R.S. §5-111.02.D in that it does not involve an expenditure of at least $100,000. As a result, Prescott Downs may not have been entitled to withhold the cost of the horse stalls and may be required to repay the $85,974.55 withheld as of December 31, 1980.

Capital Improvements At Rillito Downs

Rillito Downs has reported capital improvements of $242,427.07 for enclosing a portion of the grandstand and improvements to the clubhouse. On November 16, 1978, the Commission received a financial audit report for Rillito Downs. After the Commission granted final approval for the improvements, Rillito Downs began withholding funds on November 24, 1978. As of December 31, 1980, Rillito Downs had withheld $107,248.94.

During the course of our performance audit of the Commission, we reviewed all records relating to the capital improvement projects at Rillito Downs. In our opinion, capital improvement projects at Rillito Downs are within the provisions of A.R.S. §5-111.02.

Allocation of Capital Improvement Funds to Counties

A.R.S. §5-113.B states:

> "The Arizona county fairs racing and breeders' award fund shall be under the jurisdiction of the commission and, subject to the provisions of subsection D of this section, shall be distributed by the commission to the county fair association or county fair racing association of each county conducting a county fair racing meeting in such proportion as the commission deems necessary for the promotion and betterment of county fair racing meets. All expenditures from the Arizona county fairs racing and breeders' award fund shall be made upon claims approved by the commission."

It should be noted that the allocation of these funds to the counties is at the discretion of the Commission. There is no statutory requirement regarding county uses of these funds.

From July 1, 1975, to December 31, 1980, the Commission distributed a total of $1,282,300 for capital improvements to the 14 Arizona counties. Table 6 summarizes the distribution of capital improvement funds to the counties for fiscal years 1975-76 through 1979-80 and the period from July 1980 through December 1980.

TABLE 6

SUMMARY OF RACING COMMISSION CAPITAL IMPROVEMENT FUNDS
PAID TO COUNTIES FROM FISCAL YEAR 1975-76 THROUGH 1979-80
AND THE PERIOD FROM JULY 1980 THROUGH DECEMBER 1980

County	1975-76	1976-77	1977-78	1978-79	1979-80	July 1980-December 1980	Total
Apache	$ 18,000	$ 18,000	$ 18,400	$ 18,400			$ 72,800
Cochise	18,000	18,000	18,400	18,400	18,700	$18,700	110,200
Coconino	18,000	18,000	18,400	18,400	18,700		91,500
Gila	18,000	18,000	18,400	18,400	18,700		91,500
Graham	18,000	18,000	18,400	18,400	18,700	20,000	111,500
Greenlee	18,000	18,000	18,400	18,400	18,700		91,500
Maricopa	18,000	18,000	18,400	18,400			72,800
Mohave	18,000	18,000	18,400	18,400	18,700		91,500
Navajo	18,000	18,000	18,400	18,400	18,700		91,500
Pima	18,000	18,000	18,400	18,400	18,700		91,500
Pinal	18,000	18,000	18,400	18,400			72,800
Santa Cruz	18,000	18,000	18,400	18,400	18,700	18,700	110,200
Yavapai	18,000	18,000	18,400	18,400	18,700		91,500
Yuma	18,000	18,000	18,400	18,400	18,700		91,500
	$252,000	$252,000	$257,600	$257,600	$205,700	$57,400	$1,282,300

In order to qualify for capital improvement funds, a county must:

1. File an application to conduct a racing meeting,
2. Submit a certified audit of the prior year's racing meet, and
3. Submit a certified audit of the prior year's use of capital improvement funds.

If the county fails to submit the required information, the Commission has the discretionary authority to refuse allocation of capital improvement funds to the county.

Our review of county uses of capital improvement funds included: examining all documents filed by the 14 counties with the Commission; reviewing all Commission investigator reports, stewards reports and correspondence files; meeting with representatives of the county racing commissions to discuss uses of capital improvement funds provided by the Commission; reviewing in detail the accounting records of seven of the counties; and visiting seven of the county racing facilities to verify the existence of reported improvements.

The findings of the above review of County uses of capital improvement funds are that: 1) financial improprieties have occurred in at least two counties, and 2) the Commission has not adequately or consistently reviewed county uses of capital improvement funds.

Financial Improprieties In At Least Two Counties

Our review of the files of the Commission disclosed indications of financial improprieties in four counties. A further review of the accounting records and other documents for these counties produced sufficient evidence to conclude that: 1) improprieties surely have occurred in two counties, and 2) improprieties have not occurred in a third county. We were unable to either confirm or refute indications of improprieties in the fourth county because of statutory vagueness regarding county uses of capital improvement funds.

Apache County

Our review revealed that Apache County had reported that capital improvements projects were completed when, in fact, the projects had not been built. Additionally, the auditor for Apache County prepared a financial audit report based on estimates of proposed capital projects. Further, the auditor did not actually inspect purported projects to determine if they actually existed.

Navajo County

For fiscal year 1979-80, Navajo County received $18,700 for capital improvements. A review by the Commission's investigators revealed that the County has no invoices or other documentation to support the expenditure of $2,952.60 for labor expenses and $1,756.42 for improvements.

In addition, the certified public accountant who prepared the audit report for Navajo County refused to express an opinion on the financial statements because of material weaknesses in the county racing commission's internal accounting controls in that records of cash receipts and disbursements "have been lost or were never kept."

Mohave County

The Mohave County Racing Commission erected a new concrete grandstand at the racing facility during fiscal year 1976-77 at a cost of $31,206.02. Our review revealed that, while the County Racing Commission had failed to report the expenditure to the Arizona Racing Commission, it had applied the capital improvement funds in a proper manner.

Cochise County

Our review of the expenditures of Cochise County revealed that the county had spent: 1) $5,750 from the capital improvements funds to pay the salary of a manager-supervisor, and 2) $4,340 for vehicles.

In an opinion dated December 5, 1980, the Legislative Council stated:

> "The use of the county fairs and racing breeders' award fund is not limited to capital improvements under the terms of A.R.S. section 5-113, subsection B. Expenditures do not have to come from capital improvement funds nor must they be for capital improvements. The Commission has complete discretion in the allocation of monies from the award fund so long as the use of the monies is deemed 'necessary for the promotion and betterment of county fair racing meets'."*

Our review of the transcripts of the meetings of the Commission revealed that it has determined that the acquisition of vehicles by the county racing commissions was necessary for the promotion and betterment of county fair racing meets. The Commission has not made a similar determination regarding the manager-supervisor salary.

The Commission Has Not Consistently and Adequately Reviewed the Distribution and Expenditure of Capital Improvement Funds Awarded to Counties

Our review of County capital improvement funds revealed that the Commission has been inconsistent in its review and final determination of fund allocation. For fiscal year 1979-80, the Commission distributed $18,700 to each of 11 counties. The Commission did not allocate capital improvement funds to the remaining three counties for the following reasons:

- Maricopa County failed to provide a breakdown of the prior year's expenditures of capital improvement funds**.
- Apache County had supposedly misstated its handling of the prior year's funds (see page 45).
- Pinal County had failed to submit a certified financial audit of the prior year's expenditures.

* See Appendix 5 for the full text of this opinion.

** On May 21, 1980, the Maricopa County Fair, Inc. returned $34,070 in capital improvement funds in accordance with the direction of the Commission.

The Commission was inconsistent in its treatment of the three counties because it did approve capital improvement funds for: 1) three counties accused of financial improprieties in their handling of capital improvement funds, and 2) seven counties that had not submitted audited financial statements as required. As a result, the Commission approved funds for three counties whose certified financial statements included an auditors' opinion section that specifically disclaimed an opinion as to whether capital improvement funds were fairly stated and seven counties whose financial statements had not been audited.

A review of the transcripts of Commission meetings and interviews with Commission staff revealed that it is the staff members who determine if each county has complied with the reporting requirements of the Commission. However, Commission staff members do not differentiate between certified financial statements or unaudited financial statements in making that determination. As a result, the Commission frequently allocates capital improvement funds to a county on the assumption that reporting requirements have been met when, in fact, they have not.

CONCLUSIONS

Our review revealed that some allegations of impropriety regarding capital improvement funds used at Turf Paradise appear to be true while others appear to be untrue. We also determined that the Commission improperly approved $229,044 in capital improvements to Turf Paradise and Prescott Downs for the purchase of rolling stock. Further, we determined that Prescott Downs may owe the State $85,974.55 if the acquisition of rolling stock does not qualify as capital improvements. Additionally, we determined that financial improprieties have occurred in at least two counties and that the Commission has not adequately and consistently reviewed the distribution and expenditures of capital improvement funds awarded to the counties. Finally, we determined that capital improvements at Rillito Downs are within the provisions of A.R.S. §5-111.02.

RECOMMENATIONS

It is recommended that:

1. The Commission not approve the withholding of interest expense associated with the acquisition of improvements in Turf Paradise Projects TP-1 through TP-5.

2. The Commission rescind its approval of rolling stock purchased as capital improvements at Turf Paradise and Prescott Downs. Further, the Commission should direct Turf Paradise not to withhold funds for Turf Paradise Project TP-5 and should direct Prescott Downs to repay $23,953.61, which already has been withheld.

3. The Commission request an opinion from the Attorney General to determine if Prescott Downs should be required to repay the entire $85,974.55 withheld for capital improvements.

4. The Commission determine if expenses for a manager-supervisor are necessary for the promotion and betterment of county racing meets.

5. The Commission require its staff to conduct detailed reviews of financial reports filed by the counties to verify that all reporting requirements have been met.

FINDING III

PROCEDURES USED BY THE ARIZONA RACING COMMISSION TO SELECT AND EVALUATE THE CONTRACT CHEMIST ARE INADEQUATE.

Arizona Revised Statutes (A.R.S.) §5-105 authorizes the Commission to employ a racing chemist or to contract with outside chemical laboratories for analysis of saliva, urine and blood samples of horses and greyhounds. The Commission relies on the expertise of a chemist and the accuracy of his analytical testing to control and regulate the usage of drugs in racing animals in the State of Arizona. To this end the Commission spent more than $130,000 in fiscal year 1979-80 for analyses of samples from race animals.

Our review of the procedures used by the Commission to solicit bids for a contract chemist has revealed that the procedures are not in compliance with the guidelines set forth in Arizona Revised Statutes and administrative rules and regulations. Our review also revealed that the Commission has not made a consistent effort to evaluate the performance of the current contract chemist. Further, our review revealed that the Commission failed to take corrective action in a timely manner when it was learned that the contract chemist had failed to detect prohibited drugs in urine samples. Finally, our review of the files relating to the contract chemist revealed that the Commission has failed to obtain a valid written contract with the contract chemist.

As a result, the Commission may have no recourse against the contract chemist for substandard performance.

Procedures Used to Solicit Bids Are Not in Compliance with Guidelines Set Forth in Arizona Revised Statutes and Administrative Rules and Regulations

Since 1949,* the Commission has awarded the contract for blood, saliva and urine testing to the same chemical laboratory. During that time, several other chemical laboratories have expressed an interest in participating in the bidding for the contract with the Commission. However, the Commission has discouraged the efforts of these chemical laboratories.

The Commission Has Discouraged Competitive Bids From Qualifed Laboratories

In 1969, an Arizona-based chemical laboratory requested permission to appear before the Commission. The laboratory stated that it wished to present a list of its qualifications and to request an opportunity to bid for the contract with the Commission. The representative of the laboratory was informed that the bidding for the contract was closed and that the contract always was awarded to the same laboratory.

In May 1969, the chemical company filed a protest with several State agencies. As a result of these protests, the Purchasing Division of the Department of Finance recommended that the Commission establish criteria as to competence and reliability, and contact all chemists in the State prior to the issuance of an invitation to bid. The Purchasing Division also recommended that the "...present contract for chemical testing be extended no longer than 120 days, and that immediate steps be taken to secure a contract for this service under a competitive sealed bid procedure."

Our review revealed that the Commission and the Association of Official Racing Chemists (AORC) jointly developed a list of minimum qualifications for the bidding laboratories. However, the Commission did not follow the other recommendations of the Purchasing Division and the contract was not put out for rebid.

* The laboratory changed ownership in 1971, when it was purchased by one of the employees of the laboratory. The Commission has contracted with the current owner since that time.

A.R.S. §§41-1051 through 41-1056, effective in August 1973, specify requirements for soliciting bids and awarding contracts for outside professional services. The statutory requirements are similar to the recommendations made by the Purchasing Division, and state in part:

> "A State budget unit desiring to contract for services...shall issue a request for proposals containing but not limited to:
> 1. The criteria for qualifications required of persons to be selected to perform outside professional services." (A.R.S. §41-1052)

> "...a State budget unit shall encourage persons engaged in the lawful practice of their profession to submit annually a statement of qualifications and performance data." (A.R.S. §41-1053)

Our review revealed that the Commission has not adequately solicited bids from qualified chemical laboratories. Although the major racing laboratories are located outside of Arizona, the Commission places notices in Phoenix and Tucson newspapers stating that interested parties wishing to bid on the contract should notify the Commission office. No advertisements are placed in national trade journals, nor are parties who previously have submitted bids contacted. Further, while the notices state that "...specifications to bid are available at the Commission office...", Commission staff members are not aware of the existence of these specifications and, therefore, could not provide them to interested parties.

During an unrelated search of Commission files, members of the Auditor General staff did locate a listing, "Qualifications to Bid." It was noted that the qualifications, developed in 1970, never had been updated, and may now be obsolete because of technological changes in the industry.

In 1975, the Commission received a bid from an out-of-State chemical company. Nonetheless, the Commission elected to renew the contract of the same chemist because it felt the chemist had done a good job. Our review of the bids from the two companies revealed that the out-of-State chemist had a larger staff, was involved in a significantly larger research program and provided services to several racing commissions in other states. The out-of-State company also reported that required test equipment was located in Phoenix and that a branch laboratory already was established in the Valley. The out-of-State company bid $10 a sample -- exactly the bid of the in-State company. We were unable to locate documentation to show that the Commission made an effort to evaluate the two bids adequately prior to the awarding of the contract.

It should be noted that we were unable to determine if other chemical companies contacted the Commission with regard to the blood, saliva and urine testing contract. As previously noted, one of the two chemical laboratories cited above stated that it did not attempt to submit additional bids to the Commission because they felt that the Commission would not consider any bid other than that of the current contract chemist. As a result, the Commission may have failed to contract with the most qualified laboratory that offered the most competitive price.

The Commission Has Not Adequately Evaluated the Performance of the Contract Chemist

Effective laboratory analyses are the keystones of effective control and regulation of drug usage in racing animals. However, based on documentation in file at the Commission office, the Commission instituted no procedures to evaluate the effectiveness and accuracy of the contract chemist until February 1980. Further, the tests conducted in February 1980 did not evaluate the laboratory's effectiveness in detecting prohibited drugs.

Between February and April 1980, the Commission's veterinarian at Turf Paradise injected several animals with Lasix* to determine if the chemist could identify the drug in urine samples. The contract chemist did correctly identify the Lasix in the samples. The result of this review, then, was verification that the contract chemist could identify permissible medications in urine samples in racing animals. The Commission did not, however, attempt to test the chemist's ability to identify prohibited substances.**

Immediately after these tests, the Commission was informed of allegations of substandard work by the contract chemist. During August, September and October, 1980, on the recommendation of the Commission's investigators, the Commission authorized urine samples to be "split." Splitting means dividing a single sample into two or more containers. One container was sent to a chemical laboratory in Colorado. A second container was sent to the contract chemist in the usual manner. It should be noted that the out-of-State laboratory serves as official chemical laboratory for other state racing commissions. The out-of-State laboratory identified the presence of prohibited substances in <u>four</u> samples***. The Commission's contract chemist did not report the presence of prohibited substances in any samples. One of the substances which the contract chemist failed to identify was Nubain, a synthetic morphine. Our review revealed that the contract chemist, almost a year earlier, had notified the Commission that he had developed procedures which enabled him to test for the presence of Nubain.

Because he failed to identify any prohibited substances in the positive samples, the performance of the contract chemist appears to be inadequate.

* Lasix is a medication that may be used in racing animals, providing use of the substance is reported to the Commission prior to entering an animal in a race.

** It should be noted that Lasix masks the presence of prohibited drugs in urine samples. Thus, by injecting horses with Lasix, the Commission's veterinarians destroyed the integrity of the sampling process (see page 59).

*** Prohibited substances were identified by the Colorado laboratory on two occasions. On the first occasion, the Colorado laboratory "re-split" its sample and sent it to a University laboratory in New York. This laboratory, which also serves as an official chemist for other states, confirmed the results found by the Colorado laboratory.

Although the last split sample conducted in October 1980 showed the chemist failed to identify positive samples, the Commission did not split additional samples until March 15, 1981. Thus, the Commission was precluded from further assessing the effectiveness of the laboratory. The reason the practice of splitting samples was discontinued was a lack of funds, according to the Executive Secretary.

Corrective Action

In addition to the split sample results, the Commission has had other evidence that the contract chemist was not performing effectively. For example, in September 1980, the Commission was urged by a representative of a racing industry association to upgrade the performance of the contract chemist. However, the Commission did not initiate corrective action for almost three months, and has taken very few steps to ensure that any corrective action which has been taken is effective.

Our review of the minutes of the Commission's meeting of November 25, 1980, revealed that the Commission directed the contract chemist be placed on a three-month probationary contract. The terms of the probationary contract were: 1) to include the use of adequate test equipment and test procedures, 2) participation in a continuing education program, and 3) the posting of a performance bond. However, as of March 4, 1981, the probationary contract has not been prepared, the performance bond has not been posted and the Commission has not determined if adequate testing procedures are used.

Commission May Have No Recourse Against the Contract Chemist for Substandard Performance

Our review of the contract between the Commission and the contract chemist revealed that the contract: 1) does not contain a performance clause which specifies the procedures to be used in testing saliva, urine and blood samples for prohibited substances, 2) contains no provision for Commission recourse in the event of substandard performance on the part of the contract chemist, and 3) has remained virtually unchanged from at least 1975 to the present. Additionally, the Assistant Attorney General assigned to the Commission recently determined that the present contract may not be valid, in that proper notice of contracting procedures was not given, the contract does not comply with statutory requirements as to form and content, and the contract does not contain a termination clause as required by A.R.S. §38-511. Therefore, the Commission has operated without an effective contract for saliva, urine and blood testing for at least five years.

Finally, because the Commission may have no legal recourse against the contract chemist, payments to him for substandard work may not be recoverable. From July 1, 1980, to February 28, 1981, the Commission paid the contract chemist approximately $83,000. During that period, the Commission had reason to believe that some of the work of the contract chemist was substandard.

CONCLUSIONS

Procedures used by the Commission to select and evaluate a contract chemist are inadequate to ensure the services of the most qualified laboratory. Further, the Commission failed to take corrective action in a timely manner when it determined that the current contract chemist failed to detect prohibited drugs in urine samples. Finally, the Commission may not have a valid written contract with the contract chemist.

RECOMMENDATIONS

It is recommended that the Commission:

- Encourage competitive bidding for the official chemist contract by advertising in national publications and contacting chemists within the State.

- Revise the qualifications to bid to include current analytical chemistry standards.

- Use outside professional services to evaluate the qualifications of competing bidders, based on criteria developed by the Commission.

- Establish procedures for evaluating the performance of the contract chemist, including use of split samples.

- Take appropriate corrective action with the present contract chemist by executing a probationary contract and enforcing compliance with its terms.

- Study the feasibility of developing in-house facilities for chemical analysis.

FINDING IV

THE ABILITY OF THE ARIZONA RACING COMMISSION TO PREVENT THE USE OF PROHIBITED DRUGS IN RACING HAS BEEN IMPAIRED BECAUSE CERTAIN STAFF MEMBERS HAVE NOT PROPERLY DISCHARGED THEIR RESPONSIBILITIES.

Arizona statutes prohibit the use of certain drugs in racing, and require that the Arizona Racing Commission promulgate rules and regulations to promote the proper conduct of racing, obtain the services of a duly qualified chemical laboratory and appoint as many employees as may be necessary for the enforcement of racing statutes, rules and regulations. Our review of the Commission revealed that its ability to prevent the use of prohibited drugs in racing is impaired in that:

- Certain Commission veterinarians have not properly discharged their duties.

- Recent trends in testing procedures are counterproductive to Commission efforts to control drug usage.

- The Commission is not receiving complete or accurate information from its staff.

Statutory Requirements

Arizona Revised Statutes §5-115 makes it a class 4 felony for persons to administer "...a drug, narcotic or hypnotic to a horse or dog with the intent to affect the result of a horse, harness or dog race."

The Commission is the regulatory body primarily responsible for enforcing the above statutes. Arizona Revised Statutes §5-104.B states:

> "The commission shall prepare and promulgate such complete rules and regulations to govern the racing meetings as may be required to protect and promote the safety and welfare of the animals participating in such racing meetings, to protect and promote public health, safety and the proper conduct of racing and pari-mutuel wagering and any other matter pertaining to the proper conduct of racing within this state. The commission may delegate to stewards such of its powers and duties as are necessary to fully carry out and effectuate the purposes of this article."

Arizona Revised Statutes §5-105 states in part:

> "The commission shall employ a chemist or contract with a duly qualified chemical laboratory to determine by chemical testing and analysis of saliva, urine, blood or other excretions or body fluids whether or not any substance or drug has been introduced which would affect the outcome of any race or whether or not any action has been taken or any substance or drug has been introduced which may interfere with the testing procedure..."

And Arizona Revised Statutes §5-106.A states in part:

> "The commission shall appoint...as many other employees as may be necessary for the enforcement of the laws of this state and the rules and regulations relating to racing."

Accordingly, the Commission has promulgated rules regarding the use of drugs, testing procedures to detect drugs and reporting and follow-up procedures in the event of drug detection.

During our review we noted numerous instances of noncompliance by Commission veterinarians with the Commission's rules regarding drugs.

Commission Veterinarians Have Not Properly Discharged their Duties

Our review revealed that Commission veterinarians have adopted procedures for use at horse-race facilities which 1) frequently interfere with the chemical integrity of the samples, 2) constitute a violation of the Commission's own rules and 3) may cause individuals who use prohibited drugs to remain undetected. In addition Commission veterinarians are not taking blood samples from all deceased animals to determine if the use of prohibited drugs was a contributing factor to the animal's death.

Procedures Used in the Test Barns Frequently Interfere with the Chemical Integrity of the Test Samples

At the end of each horse race, the winning horse* is immediately transported to the test barn for a blood, urine or saliva test. The sample is then sent to the contract chemist for analytical testing. The purpose of this test is to verify that the horse was not administered a prohibited substance which could have affected the outcome of the race. If the analysis of the sample taken is reported as a "negative", that is, no prohibited substances were detected, the winning purses are distributed. If the sample taken is reported as a "positive" the purse money is ordered held, and the Board of Stewards holds a hearing to collect evidence. If the Board determines appropriate, it disciplines the trainer and the persons administering a prohibited substance to the horse. The stewards then restructure the finish position of the other horses and distribute the purse money accordingly.

During the course of our review, we noted that the majority of samples taken from horses were urine samples (more than 90 percent). As a part of our audit, we reviewed the specific procedures used to collect urine samples. We noted that the procedures manual specifies the steps to be taken if a horse cannot produce a urine sample within a specified time (usually 90 minutes). The manual instructs test barn personnel to request the permission of the owner or trainer to inject the horse with a drug that will force the horse to urinate. If approved by the owner or trainer, test barn personnel will direct a veterinarian to inject the race horse with the drug Lasix, a diuretic.

* Winning horses are not the only horses tested. (See page 63)

Our review revealed that the use of Lasix injections to obtain a urine sample destroys the integrity of sample testing (see page 79). According to the official chemists for several other racing jurisdictions Lasix masks the presence of prohibited substances. These chemists claim that Lasix takes effect within minutes and masks virtually all known substances which are used in racing animals. Therefore, Lasix never should be used prior to the collection of a sample because of its masking effect.

Administrative regulation R4-27-107 R states:

> "Samples of saliva, urine or any other test substance shall be taken by persons appointed by the Arizona Racing Commission, under the supervision of the Commission veterinarian. During the taking and sealing of such tests the owner, trainer, or their authorized agent may be present at all times. The sample shall be immediately sealed in a container and the evidence of such procedure witnessed by the signature of the owner, or trainer, or their representative. The sample shall thereupon be forwarded with dispatch to the Official Racing Commission Laboratory for chemical analysis and report to the Arizona Racing Commission. No person shall interfere in any manner with the testing procedures under this Rule. (Ephasis Added)

As a result, by injecting horses with Lasix the Commission veterinarian violated the above rule regarding interfering with the testing procedures.

We found that from October 1, 1980 through March 8, 1981, 36 horses at Turf Paradise* had been injected with Lasix by test barn personnel prior to collection of a sample. When we reviewed the names of the trainers for those 36 horses, we found one trainer who had been suspended for one year for using prohibited substances in his racing horses. During the period under review, this same trainer had four winning horses whose samples possibly were masked by Lasix.

* The Commission veterinarian stated that the use of Lasix to assist in the collection of urine samples is a common practice at all horse racing facilities in the State.

Further, we identified seven other instances of the Commission veterinarian injecting winning horses with Lasix as a means to evaluate the effectiveness of the contract chemist (see page 52). Not only did this procedure interfere with testing procedures and violate Commission rules but it was unnecessary as well, because the Commission maintains two horses at a cost of $500 a year for such testing purposes.

Blood Samples from Deceased Horses

Blood samples are not taken from all deceased horses. During fiscal years 1979-80 and 1980-81, at least 65 race horses died at racing facilities, of which 36 died immediately before, during or after a race. The Commission granted the veterinarians discretion in determining which animals were to be tested. An August 1979 memorandum from the Executive Secretary to the veterinarians stated:

> "Effective immediately, upon the death of a racing animal on the racetrack in which there is any concern or suspicion as to the cause of death, the State Veterinarian will take a blood sample and send it to the lab for examination." (Emphasis Added)

Since the memorandum was issued, blood samples have not been taken for all deceased horses, and no autopsies performed. Blood samples were not taken for any of eight horses known to have died at Rillito Downs between November 1, 1980, and February 15, 1981. Further, blood samples have been taken for only half the horses that died immediately before, during or after a race at Turf Paradise from July 1, 1980 to February 28, 1981.

The following incident illustrates the need for blood sampling of deceased horses and autopsies.

During the Graham County Fair in April 1979, for no apparent reason a horse turned abruptly and ran through a three-inch steel rail after crossing the finish line. The horse was practically cut in two and died instantaneously . The jockey was hospitalized with serious injuries, including "...a broken wrist, some broken ribs and possibly a broken neck..." One observer, who was a Commission employee at the time of the incident, told audit staff that he believes the horse was drugged, and that the fact the horse was drugged had been discussed openly on the backside (stable area) after the incident.

A blood sample was not taken and the cause of death was not investigated. The veterinarian reported the incident to the Commission as follows:

> "Fourth Race
> (Name of the horse), No. 2. Over the inside rail - expired."

The Commission veterinarian who was at the track at the time of the incident claimed blood samples were not taken at that time because adequate testing equipment was not available. However, our review revealed that the equipment required for blood testing <u>was</u> available at the time of the incident.

It should be noted that the trainer of the horse in the above incident recently was suspended and fined by the Commission for using a prohibited substance on one of his horses.

Recent Trends in Testing Procedures are Counterproductive to Commission Efforts to Control Drug Usage

Sampling procedures used to detect the presence of prohibited substances do not support the Commission's intent to increase enforcement of medication rules. In addition to urine, blood or saliva samples from winning horses, samples may be obtained from other horses as well. These additional samples are taken at the discretion of the stewards and are usually taken from horses that perform differently than expected. Our review revealed that the practice of taking additional samples 1) is not consistent among tracks and 2) has decreased since the Commission adopted stricter drug rules*. Table 7 shows the percentage of races for which additional samples were drawn from July 1, 1980, to February 15, 1981.

* In late 1980 the Commission adopted rules prohibiting the use of phenylbutazone except in training, and Lasix. These medications previously were allowed if Commission approval were obtained prior to usage. For details of the new medication rules, see page 73.

TABLE 7

PERCENTAGE OF RACES FOR WHICH ADDITIONAL SAMPLES WERE DRAWN
FROM JULY 1, 1980, TO FEBRUARY 15, 1981

	PERCENTAGE OF RACES		
	July 1, 1980, to September 1, 1980	December 18, 1980*** to December 31, 1980	January 1, 1981**** to February 15, 1981
Prescott Downs*	40%	N/A	N/A
Rillito Downs (Tucson)	50%	11%	0
Turf Paradise (Phoenix)**	10%	11%	8%

As shown above the practice of taking additional samples at Rillito Downs ceased when the new medication rules became effective.

It should be noted that other states make greater use of additional samples (the term used for discretionary steward testing) than Arizona does. Thirteen of the 30 states that allow racing take additional samples and seven of these states take additional samples in every race.

The Commission Is Not Receiving Complete or Accurate Information from its Staff

The information provided to the Commission by track personnel is incomplete. As a result, the Commission lacks sufficient information regarding detection activities to monitor proper conduct.

* Meet ended August 24, 1980. Included Yavapai County Fair held August 30, 1980, through September 1, 1980.

** Includes Arizona Downs, Desert Downs and Turf Paradise meets held at Turf Paradise facility.

*** Date of Commission adoption of new rules.

**** Effective date.

The Commission's veterinarians submit bimonthly reports to the Commission which include the number of samples submitted to the official chemist and number of injuries and deaths of horses on the track. Our review of these reports revealed the following deficiencies:

1. The reports submitted by veterinarians at Rillito Downs do not indicate the number of additional urine or blood samples taken.

2. The number of blood samples reported by the veterinarian at Turf Paradise does not agree to the number of blood samples received by the official chemist.

3. Reports of injured or deceased animals prepared by the Commission veterinarian at Rillito Downs do not clearly indicate if an animal died on the racetrack or was euthanised if injured.

4. The deceased animal lists for Turf Paradise and Prescott Downs do not indicate the causes of death for all animals.

CONCLUSIONS

Our review revealed that certain Commission veterinarians have not properly discharged their duties, that recent trends in testing procedures are counterproductive to Commission efforts to control drug usage and that the Commission is not receiving complete or accurate information from its staff.

RECOMMENDATIONS

It is recommended that:

- Commission veterinarians discontinue using Lasix to collect urine samples.

- Blood samples be tested for all animals which die immediately before, during or after a race.

- Additional test samples be taken more often and for all major races.

- Commission staff submit monthly reports to each Commissioner which include the following information:

  Number and type of samples submitted to the official chemist.

  Results of tests indicating the presence of prohibited substances.

  Animal deaths, causes of death and results of blood tests and autopsies.

FINDING V

THE ARIZONA RACING COMMISSION IS NOT COMPLYING WITH THE OPEN MEETING LAW AND THE WORKMEN'S COMPENSATION LAW.

As a part of our audit of the Arizona Racing Commission, we made a review to determine if the Commission is in compliance with statutory and administrative requirements. We determined that stewards' hearings did not comply with the Open Meeting Law and that the Commission's enforcement of an administrative rule requiring compliance with the Workmen's Compensation Law was untimely and inadequate.

Stewards' Hearings Did Not Comply With The Open Meeting Law

During the course of our audit, we noted that two stewards employed by a permittee and one steward employed by the Commission jointly decide the outcome of contested races and hold hearings for individuals charged with violations of the statutes and administrative rules and regulations. Stewards' rulings may include suspension of a license and/or imposition of fines. Decisions are binding on the licensee, who may appeal such decisions to the Commission.

Arizona Racing Commission Rule R4-27-209.G.18 provides that "no special announcement of the hearing or of the alleged infraction...shall be made until after said hearing." When asked if stewards' hearings for individuals charged with violations of the statutes and administrative rules and regulations are subject to the provisions of the Open Meeting Law, the Legislative Council, in an opinion dated December 12, 1980, stated:

"Hearings held for violations of the statutes or rules relating to horse and dog racing are subject to the open meeting law.

"Arizona Revised Statutes section 5-104, subsection B allows the commission to delegate to stewards its powers and duties as necessary to fully carry out and effectuate the purposes of the statutes relating to horse and dog racing.

. . . . . .

"The provisions of the open meeting law apply to all standing, special and advisory committees or subcommittees of a public body....By the terms of A.R.S. section 5-104, subsection B, the commission has authority to delegate its powers and duties to the racing stewards. By virtue of this authority, the commission has given the stewards the power to impose fines and suspend licenses. Therefore, it can be said that the stewards are acting on behalf of the commission. To the extent then that the stewards meet to propose or take legal action they are subject to the requirement that the meeting be open to the public.

. . . . . .

"...considering the purpose of the open meeting act, in each case all doubts should be resolved in favor of opening a meeting to the public. In addition, commission rules require the stewards to take some sort of action relating to a rules violation. For these reasons, the hearing required by the commission appears to be subject to the public notice requirement of A.R.S. section 38-431.02. Based on this conclusion, A.C.R.R. R4-27-209G, 18(f) violates the open meeting requirement under Arizona law."*

This opinion was discussed with the members of the Commission and its legal representative. The Commission has directed the stewards to provide adequate notice of hearings in compliance with the Open Meeting Law. The Commission also has taken steps to amend its administrative rules and regulations to comply with the provisions of the Open Meeting Law.

* See Appendix VI for the full text of this opinion.

Enforcement of an Administrative Rule Requiring Compliance with the Workmen's Compensation Law Was Untimely and Inadequate

The Commission did not act in a timely manner to ensure compliance with an administrative rule concerning the Workmen's Compensation Law. In addition, actions taken by some stewards to enforce the rule were not in compliance with established procedure.

Untimely Enforcement

Administrative Rule R4-27-104.0. requires compliance with the Workmen's Compensation Law and states in part:

> "All persons who perform occupational or personal services under a license issued by the Commission shall be required to be insured under the provisions of the Arizona Workmen's Compensation Law..."

Enforcement of the Workmen's Compensation Law is the responsibility of the Industrial Commission of Arizona. However, the Racing Commission is responsible for providing for the safety and protection of persons on the track, which may include ensuring that licensees are protected in case of accident. This responsibility was not fulfilled in a timely manner. Although the above rule went into effect in March 1980, the Commission took no action to enforce the rule until October 1980, seven months later.

Noncompliance with Established Procedures

Responsibility for ensuring compliance with administrative rule R4-27-104.0, was delegated to the stewards. An October 1980 memorandum to the stewards requested that a notice be posted "...in a conspicuous place." The notice informed permittees and licensees that: 1) a certificate of insurance coverage must be on file in the Commission office, and 2) failure to provide such a certificate would result in refusal or suspension of a license.

Our review indicates that the Commission did not: 1) post notices, 2) attempt to contact licensees at Turf Paradise and Rillito Downs to whom the rules applied, or 3) obtain proof of insurance coverage at Turf Paradise and Rillito Downs. In addition, the Commission has not taken appropriate disciplinary action against uninsured licensees. As a result, licensees of the Commission may not be adequately protected in case of accident.

Finally, the license application form currently used by the Commission does not require disclosure of workmen's compensation coverage. At least ten other racing regulatory bodies require: 1) disclosure of the firm with which the insurance is carried, 2) the policy number, or 3) other evidence of coverage.

CONCLUSIONS

Stewards' hearings do not comply with the provisions of the Open Meeting Law and the Commission's enforcement of an administrative rule requiring compliance with the Workmen's Compensation Law was untimely and inadequate.

RECOMMENDATIONS

It is recommended that:

1. Stewards' hearings be held in compliance with the provisions of the Open Meeting Law.

2. The Commission comply with the provisions of A.C.R.R. R4-27-104.0 relating to the Workmen's Compensation Law.

FINDING VI

ILLEGAL LOANS HAVE BEEN MADE FROM THE RACE TRACK BENEVOLENT FUND AND THE GREYHOUND BENEVOLENT FUND.

The Race Track Benevolent Fund (RTBF) and the Greyhound Benevolent Fund (GBF) were created to provide an emergency source of funds for needy individuals employed at the race tracks. Fines levied against licensees at the various tracks were used to establish and sustain RTBF and GBF. The Board of Stewards at each track controlled RTBF and GBF. The funds were abolished in 1978, when the remaining balances in the funds were deposited to the General Fund. Our review revealed that as of December 31, 1980, 1) $66,102.68 was illegally distributed from those funds, and 2) $50,656.38 in interest free loans remain outstanding.

From December 1953 to March 1978, the RTBF distributed a total of $63,852.68 of which $15,086.30 was donated to individuals at various tracks for such items as Thanksgiving and Christmas dinners, funeral expenses and emergency medical expenses. The remaining $48,766.38 was distributed as interest-free loans to licensees of the Commission, of which only $360 has been repaid. Thus, as of December 31, 1980, there was $48,406.38 in outstanding loans from the benevolent fund.

From 1961 to 1977, the Greyhound Benevolent Fund distributed $2,250 as interest-free loans to licensees at the various tracks. None of these loans has been repaid.

In an opinion dated December 22, 1980, the Legislative Council stated:

"...a search of the horse and dog racing statutes added or amended prior to 1978 disclosed no power of the commission to grant loans to licensees from race track benevolent funds.

"Additionally, Article IX, section 7 of the Arizona Constitution would prohibit the granting of a loan to a licensee. That section states that public monies may not be used to give gifts or loans to an individual, association or corporation. Granting monies to a licensee for loans to the needy, although a worthy cause, is not enough to justify giving public monies to an individual, association or corporation. Udall v. State Loan Board 35 Ariz. 1, 273 P. 721 (1929)"*

Therefore, it appears that the Race Track Benevolent Fund and the Greyhound Benevolent Fund were both illegal and unconstitutional.

CONCLUSION

From 1953 to 1978, $66,102.68 were illegally distributed from the Race Track Benevolent Fund and the Greyhound Benevolent Fund and as of December 31, 1980, $50,656.38 in interest free loans remain outstanding.

RECOMMENDATIONS

It is recommended that:

1. This matter be referred to the Attorney General's office to determine whether any liability exists either on the part of the Commissioners or their employees.

2. A review be made to determine whether it is feasible to collect the unpaid loans.

* See Appendix 7 for full text of this opinion.

OTHER PERTINENT INFORMATION

ARIZONA RACING COMMISSION IMPLEMENTATION OF NEW DRUG USAGE RULES

During 1980, the Arizona Racing Commission promulgated new rules regarding the use of drugs in accordance with National Association of State Racing Commissioners (NASRC) guidelines. Our review revealed that the Commission postponed the implementation of these rules longer than most other states that have adopted similar rules.

NASRC GUIDELINES

NASRC adopted model medication rules in 1980. The rules prohibit the use of foreign substances except Lasix. NASRC advocated a ban on the use of phenylbutazone because its research determined that the chemical can be used to mask the presence of other prohibited substances in blood, saliva or urine samples. NASRC did state that phenylbutazone could be used for training purposes, but should not be permitted to be used prior to a race. NASRC established a standard on residual levels which may be present in an animal's system on race days. The tolerance level is measured in units of blood plasma. Residual levels were not established for urine samples.

At the present time, 21 of 24 other states which regulate horse racing have adopted or are attempting to adopt medication rules which are at least as stringent as the NASRC guidelines. It should be noted that seven states have adopted statutes or rules which prohibit all drugs, including phenylbutazone and Lasix. Table 8 shows the status of other states' medication rules with respect to NASRC guidelines.

Subsequently, the NASRC medication committee has proposed that Lasix also be banned, due to its interference with chemical testing procedures. The proposal will be voted upon by the NASRC membership at its next meeting in April 1981.

TABLE 8

TYPES OF MEDICATION RULES ADOPTED BY OTHER STATES

	Within NASRC Guidelines				
			Allows Phenylbutazone at Residual Levels Only		
State*	Complete Ban	Lasix Only	Allows Lasix	No Lasix	Permissive
Arkansas		X			
California**					X
Colorado					X
Delaware	X				
Florida***	X				
Idaho	X				
Illinois				X	
Kentucky**					X
Louisiana		X			
Maryland		X			
Massachusetts				X	
Michigan			X		
Montana	X				
Nebraska	No response				
Nevada			X		
New Jersey		X			
New Mexico**					X
New York	X				
Ohio	X				
Oregon	X				
Pennsylvania			X		
South Dakota**				X	
Washington**			X		
West Virginia**					X

* Excludes states without thoroughbred and/or quarterhorse racing and New Hampshire, which will not be active in thoroughbred racing until 1982.

** Attempting to adopt NASRC guidelines.

*** Adopted complete ban. Industry group is challenging the constitutionality of the law. Ban is not effective until court case is decided.

Unnecessary Delays

Administrative Rule R4-27-107 defines fraudulent and corrupt practices in the racing industry. Subsections E, F and G specify the corrupt practices with regards to prohibited drugs and prohibited devices. These subsections state:

> " E. It is further prohibited for any person to administer or cause to be administered to any horse or greyhound after the overnight entries are finally closed or the day before the race in the case of early entries, either internally or externally any prohibited drug. With the exception of F.1. and F.5.
>
> " F. 'Prohibited drug' includes any drug, medicine or other substance which is of such character as could affect the racing condition of a horse or greyhound or which might interfere with the testing procedures. These drugs include but are not limited to stimulants, depressants, local anesthetics, narcotics and certain analgesics.
>
> " 1. The oral administration of Phenylbutazone or its metabolites may be administered the day prior to the race by a trainer upon prescription of a licensed veterinarian. Phenylbutazone which is injected must be administered by a veterinarian licensed by the Arizona Racing Commission. No entry shall be accepted unless it is indicated on the entry blank that said horse is on or off Phenylbutazone.
>
> " 2. Permission will not be granted for the use of Phenylbutazone or its metabolities in two (2) year olds.
>
> " 3. No change shall be made in the declared medication without the advice of a veterinarian and the consent of the stewards.
>
> " 4. If any horse on the Phenylbutazone program changes hands either by sale, claim or otherwise, it shall be the responsibility of the new trainer to continue said horse on the Phenylbutazone program, or request removal.
>
> " 4. With the permission of the stewards, an approved medication may be administered to a known bleeder to control epistaxis on the day of the race, but no less than four hours prior to post time.
>
> " G. 'The possession, including without limitation, on the person, in the living or sleeping quarters or assigned stall, tack room, compound or in the motor vehicle or trailer of any person within the grounds of any permittee, of any implement which might be used for the administering of a prohibited drug, or a device, electrical, mechanical or otherwise, other than ordinary equipment, of such a nature as to affect the speed or racing condition of a horse or greyhound, unless the written permission for such possession has been obtained from the stewards is prohibited'."

The Commission began discussions of possible changes to the above rule in August 1980. The Commission specifically stated its intention to change Arizona medication rules to comply with NASRC guidelines and prohibit the use of Lasix and phenylbutazone for any purpose other than training. At the request of a horse-racing industry association, the Commission agreed in September 1980 to delay adoption of these rules for one month to allow the representatives of the association to notify its members of the proposed rule changes.

In compliance with the Administrative Procedures Act, the Commission posted a formal notice of proposed rule changes and invited interested parties to attend a public meeting to discuss the proposed rules. On October 8, 1980, the Commission adopted rules which prohibited the use of all medications, except for phenylbutazone, which could be used only for training purposes and could not be given to a racing animal on the day of a race. Each horse metabolizes phenylbutazone differently. Therefore, it was determined that a transition period would be needed to allow owners and trainers an opportunity to determine how far in advance of a race their horses should be taken off phenylbutazone to comply with residual levels set by the Commission. Thus, the effective date for the new rule was set for January 1, 1981. This allowed for an 84-day transition period.

Our review revealed that the Office of the Attorney General did not certify the new drug rules. As a result, the Commission met on December 18, 1980, to adopt the same medication rules under the provisions for emergency adoption. The proposed rule changes submitted to the Attorney General constituted comprehensive revisions in all areas regulated by the Commission. The request for certification was withdrawn when it was decided that some additional refinements were necessary. The Commission proposed that the rule still would become effective on January 1, 1981. However, representatives for the same horse-race industry association that had asked for a delay in September 1980, objected to the January 1, 1981, effective date because it did not give them sufficient time to notify the membership of the rule changes. It should be noted that the association knew of these rule changes at least three-and-a-half months earlier. Nevertheless, the Commission acquiesced and adopted a staggered effective date for the new medication rules. Table 9 summarizes the effective dates for the new medication rules and the days between the date of original adoption and the effective date.

Table 9

SUMMARY OF EFFECTIVE DATES FOR NEW MEDICATION RULES AND DAYS BETWEEN DATE OF ORIGINAL ADOPTION AND EFFECTIVE DATE

Effective Date	Regulatees Affected by Rule Change	Lead Time at Original Adoption (Days)	Additional Lead Time (Days)	Total Lead Time (Days)
January 1, 1981	Two- and three-year-olds	84	0	84
March 28, 1981	County Fair Meets	84	86	170
May 11, 1981	Commercial Meets	84	130	214

In comparing the lead time between the original adoption of the rules and the effective dates in Arizona and other states, it appears that the additional lead times given in Arizona were unnecessary. So far, nine other states have amended their medication rules to comply with the April 1980 NASRC guidelines. Table 10 summarizes the states that have adopted the NASRC guidelines, the effective date of the new medication rule and the days between the date the rule was adopted and its effective date.

TABLE 10

SUMMARY OF STATES ADOPTING NASRC GUIDELINES,
EFFECTIVE DATES OF NEW MEDICATION RULE, AND DAYS
BETWEEN DATE THE RULE WAS ADOPTED AND ITS EFFECTIVE DATE

State	Effective Date	Lead Time
Arkansas	April 1981*	60 days
Delaware	December 1980	None
Florida	**	2 days
Illinois	January 1981	14 days
Louisiana	November 1980	180 days
Nevada	July 1980	Did not respond
Ohio	March 1981	180 days
Oregon	May 1981	240 days
Pennsylvania	July 1980	45 days
Average lead time		90.13 days

Based on the information in Table 10, it appears that the revised effective dates established by the Commission at its December 18, 1980, meeting are unnecessary extensions of the original effective date. Particularly in view of the fact the Commission publicly stated the original effective date would be January 1, 1981, as early as October, 1980.

* Arkansas always has banned phenylbutazone. The new rule extends the ban to include Lasix.

** Florida passed legislation prohibiting the use of all medications on race day. The legislation has been challenged in court by a horsemen's association. The Florida Racing Commission originally provided two days lead time and has stated if the statute is upheld it will again provide two days lead time.

Unnecessary Weakness in the Regulatory Process

Because of Commission delay in the effective date of the new medication rules, owners and trainers will be allowed to use phenylbutazone and Lasix on their racing animals longer. As a result, the Commission's ability to control drugs will be impaired longer than necessary because of the masking properties of phenylbutazone and Lasix.

During the course of our audit we conducted a test which demonstrated that Lasix can mask the presence of a prohibited drug. The details of that test follow.

The Office of the Auditor General requested that Sublimaze*, a prohibited drug, be administered to two horses in dosages which were significantly larger than those usually administered.** One of the horses was also given Lasix. Two urine samples were collected from each horse. One sample was sent to the Commission's contract chemist and the other sample was sent to a chemical laboratory in Colorado, which serves as the official chemist for several racing commissions in other states. Both laboratories reported the presence of Sublimaze in the sample from the horse that did not receive Lasix. However, neither laboratory was able to report the presence of any prohibited substances in the sample from the horse which received Lasix. It is important to note that both horses received identical dosages of Sublimaze. The only difference was that one horse had also received Lasix. Apparently, the Lasix masked the presence of the Sublimaze in the test horse.

Thus, it appears that because the Commission delayed adopting the new medication rules, a serious weakness in its ability to control usage would be allowed to continue unnecessarily.

* Sublimaze, or fentanyl, is a commonly used drug, according to the Colorado State Veterinarian. It is proven to be detectable using available analytical chemistry tests.

** The drugs were administered by veterinarians. The test was conducted under the supervision of Department of Public Safety and Commission investigative staff members.

COMMISSION

Michael J. O'Haco, Chairman
Chet E. Johns, Vice Chairman
John K. Goodman, Commissioner
Ronald A. Lebowitz, Commissioner
L. Wardell Larson, Commissioner

ARIZONA RACING COMMISSION

BRUCE BABBITT
GOVERNOR

EXECUTIVE SECRETARY

William R. Billing
1645 West Jefferson
Room 437
Phoenix, Arizona 85007
(602) 255-5151

March 31, 1981

Douglas R. Norton
Auditor General
Legislative Services Wing
Suite 200 - State Capitol
Phoenix, Arizona 85007

Comments of Commissioners O'Haco, Johns and Lebowitz, Arizona Racing Commission*

Dear Mr. Norton:

We have reviewed a preliminary draft report of the first phase of a performance audit of the Arizona Racing Commission. We wish to commend the members of your staff for the courteous and expeditious manner in which they performed their task. We also wish to thank you for affording us the opportunity to comment on that preliminary draft prior to its release to the general public. Due to time constraints, these comments will be brief in comparison to the report itself. As such, it is necessary for us to comment on matters set forth in the report in accordance with what we perceive to be a real order of priority and not necessarily pursuant to the order of items set out in the report.

With respect to a section of the report entitled "other pertinent information," it is gratifying to note that the Auditor General concurs with the Commission's stated need for legislation to prohibit any drugging or numbing within the racing industry in Arizona. It is true that the Commission's attempts to temporarily address the problem through the passage of emergency administrative rules have been hampered by delay.

---

*Commissioner Goodman was in Europe at the time of the issuance of the preliminary draft report and was unavailable for comment.

Nevertheless, the report fails to mention the continuing parallel attempts of Commissioners O'Haco, Johns, Goodman, and Lebowitz to bring about more permanent reform by way of legislative statutory enactment. The Commission realizes that many special interests within the racing industry have complained bitterly about the immediate burden caused by being forced to comply with an overnight enactment of an administrative rule prohibiting medication of any kind. The Commission has been willing to extend the effective date of such a rule in order to remove a possible legal claim by various members of the Arizona racing industry of lack of either notice or due process of law. There has not been any misinterpretation, however, as to the Commission's intent to make such a prohibition permanent in this state. That is precisely why the Commission has pursued a course of promoting statutory reform. To the extent that your office, an arm of the legislature, will aid in these efforts, this Commission is grateful.

When your performance audit commenced in the fall of 1980, the Commissioners were concerned about certain allegations being made by one racing permitee against another -- allegations restated by a member of the legislature as a basis for insisting on the commencement of such an audit. These allegations related to a so-called misuse of capital improvement funds previously approved by the Commission for the improvement of the Turf Paradise racing facility. Your audit has shown that the overwhelming number of these allegations were not only unsubstantiated but were, in fact, totally groundless. Many of these allegations were so false and so reckless that the Commission cannot assume that they were made in good faith. The report addresses these allegations as a whole in more than one placing saying, "some . . . appear to be true while others appear to be untrue." That statement, particularly the order in which it is written (emphasizing positive over negative) is misleading. Of all the allegations that could be utilized by those that wish, for personal reasons, to attack the Turf Paradise permitee, the only one that was true and which could serve such a purpose dealt with a withholding of an interest expense. This appears to the Comission to be nothing more than an accounting dispute which the Commission will resolve in due course. Some eight additional

allegations made against Turf Paradise were shown by your investigation to be false, either patently so, or through the spirit or motivation under which they were asserted by these "accusers." Since this portion of the audit was apparently intended to be used as the flagship for those who have sought to attack both the Commission and certain private members of the racing industry, we thank you for bringing the whole truth to the attention of the public.

With respect to your finding IV relating to regulation of the use of drugs within the Arizona racing industry, and your finding III relating to selection and evaluation of a contract chemist, it should be noted that the Commissioners are currently taking appropriate steps to upgrade the performance of their own personnel and persons contracting with the Commission for such services as chemical testing related to racing. Beyond this, the Commissioners intend to continue to place all employees' activities under great scrutiny and will take all appropriate administrative steps against any subordinate who performs his duties in a substandard manner or who resists any directive to improve his performance. Certain changes in Commission personnel are currently underway and others are scheduled for review within the near future. With respect to the chemist mentioned in the report, the Commission has already expressed dissatisfaction with his performance and placed him on a probationary status. More distressing to the Commission than the somewhat suspect results reached by this chemist during the previous year of testing are the results reached by chemists on a nationwide basis as reflected by the statistical report of the performance of 53 AORC Laboratories for the calendar year 1980, a copy of which is attached hereto and incorporated herein by this reference. It is the Commission's resolve to intensify all efforts to accurately detect and prosecute all drugging violations which occur within the racing industry in Arizona.

Not unlike those problems set forth in findings III and IV of your report, your finding I, relating to licensing procedures, has, by necessity, taken an historical view of a problem. The Commission has never been unaware of problems

within its own history. It is for that very reason that the present Commission has attempted to obtain reform legislation and a realistic budget in order to make great strides to improve those problems. As historical as the problems themselves is the fact that the Commission has never obtained a budget sufficient to attack those problems in a thoroughly systematic and professional fashion. We sincerely hope that this report will underscore that need.

With respect to particular licensing problems that have been pointed out in the report, at least two deserve further commentary. First, it is true that a former executive secretary did unilaterally suspend the fingerprinting of license applicants. Although his reasons were subsequently stated as being motivated by cost-saving desires, the fact that he has been under criminal investigation by the Attorney General for many months (thus disqualifying this Commission from taking any administrative steps against him) may shed further light upon the propriety of his actions. He has not been associated with the Commission for more than one year, and fingerprinting has been reinstated as a normal procedure to be followed by the Commission. Second, your report discusses certain failures to submit information to the National Association of State Racing Information System computer (NASRIS). What your report failed to mention is that virtually every racing commission in the United States has similarly been delinquent in submitting this information to NASRIS. Although NASRIS is a meritorious concept, in practice it has been a failure. Regardless of whether or not the Arizona Racing Commission expedites the submission of information to NASRIS, your investigation has conclusively shown that NASRIS is not presently a reliable source of information with respect to the checking of the background of a licensing applicant.

Although the Commissioners have been aware of the existence of problems, both within its own management of the racing industry, as well as within the industry itself, your report has focused upon many problems with great particularity. As unpaid and voluntary appointees, the Commissioners are grateful for the services of people possessing the expertise displayed by your staff. You have pinpointed certain problems. We will consider all of your suggestions, and, with

the budgetary assistance presently sought from the legislature, we will have the tools to finish the job.

Respectfully submitted,

MICHAEL J. O'HACO
Chairman

CHESTER E. "CHET" JOHNS
Vice-Chairman

RONALD A. LEBOWITZ
Commissioner

Summary of Samples and Detected Drugs as Reported by 53 AORC Laboratories
Calendar Year, 1980

UNITED STATES HORSE RACE SAMPLES

STATE	JOCKEY			HARNESS			TOTAL	POSITIVE	%
	Saliva	Urine	Blood	Saliva	Urine	Blood			
Arizona	65	2,777					2,842	3	.11
Arkansas		747					747	3	.40
California		18,993	857		6,729	416	26,995	7	.03
Colorado		4,017					4,017	2	.05
Delaware		496	5	3,200	3,200	385	7,286	16	.22
Florida		8,426	865		2,021	269	11,581	5	.04
Idaho		1,382					1,382	7	
Illinois		32			7		39	2	
Indiana		76			43		119	0	
Kansas		303					303	2	
Kentucky		2,803	3,336		2,803	4,226	13,168	18[1]	.14
Louisiana		4,123	160				4,283	13	
Maine					2,667	1	2,668	9	
Maryland		5,998	3,566		5,035	405	15,004	15	
Massachusetts		4,150	298		2,054	34	6,536	19	
Michigan		4,264	198		6,355	1,029	11,846	28	
Montana		1,101					1,101	4	
Nebraska	69	2,520	61				2,650	2	
Nevada		89					89	2	
New Hampshire		630			2,483		3,113	7	
New Mexico		3,615	4				3,619	7	
Ohio		7,657	680		7,649	28,357	44,343	61[2]	.10
Oregon		1,857					1,857	13	
Pennsylvania	2	10,000	2,500		11,000	35,100	58,602	306[3]	.19
South Dakota		996	10				1,006	1	
Texas		2,067					2,067	27	
Utah		227					227	0	
Washington		3,447	215				3,662	10	
Wyoming			166				166	1	
West Virginia		7,618	45				7,663	30[4]	
	136	100,411	12,966	3,200	52,046	70,222	238,981	620	

Footnotes
1. Permitted drugs: 283 harness; 3,628 jockey.
2. 24,600 harness pre-race blood samples; 18 positive (16 phenylbutazone).
3. 12,500 jockey race samples: 26 phenylbutazone, 68 furosemide, 59 flunixin
   35,000 harness race samples: 34 phenylbutazone, 33 flunixin, 18 nalbuphine, 13 furosemide.
4. 10 furosemide, 9 polyethylene glycol.

ATTACHMENT

APPENDIX I

ARIZONA RACING COMMISSION

LICENSE APPLICATION

HORSE ☐ GREYHOUND ☐

NEW ☐ RENEWAL ☐

LICENSE NO. ISSUED

_____ TRACK

THIS APPLICATION MUST BE COMPLETED IN ITS ENTIRETY (front and back)
GIVE FULL NAME – INITIALS NOT ACCEPTABLE:

DATE: _____

LICENSE FEE:

$11
Owner-Trainer ☐ Jockey Agent ☐
Jockey ☐ Appr. Jockey ☐

$6
Owner ☐ Trainer ☐ Vet ☐
Lessee ☐ Official ☐
Assistant Trainer (Dogs Only) ☐

$2
Groom ☐ Mutuel ☐
Pony Rider ☐ Concession ☐
Exer. Rider ☐ Peace Officer ☐
Outrider ☐ Asst. Starter ☐
Plater ☐ Lead-Out ☐
Jockey Valet ☐ Cool-Out ☐
Maint. ☐ Other ☐

PRINT LAST NAME _____ FIRST NAME _____ MIDDLE NAME _____

LOCAL ADDRESS _____
STREET CITY STATE ZIP

SOCIAL SECURITY NUMBER _____ TELEPHONE _____

(Answering this question is voluntary. If answered the information will be used as provided in ARS-5-106-G)

NEAREST OF KIN _____ RELATIONSHIP _____

PERMANENT ADDRESS _____
STREET CITY STATE ZIP

TRAINER _____

EMPLOYER _____
(MUST BE SIGNED BY EMPLOYER)

AGE	HEIGHT	WEIGHT	HAIR	EYES	U.S. CITIZEN YES ☐ NO ☐

Other Ident. _____

Date of Birth _____ Place of Birth _____

1. HAVE YOU EVER BEEN ARRESTED, FINED, CONVICTED, OR RELEASED AFTER BOOKING FOR ANY CRIMINAL OFFENSE EXCEPT MINOR TRAFFIC MATTERS, WHETHER A MISDEMEANOR OR FELONY? . . . . . YES ☐ NO ☐

_____

2. HAVE YOU BEEN CONVICTED OF HANDBOOK OR BOOKMAKING? . . . . . YES ☐ NO ☐

3. HAVE YOU EVER BEEN ASSOCIATED IN ANY MANNER WITH HANDBOOK OR BOOKMAKING? . . . . . YES ☐ NO ☐

_____

4. HAVE YOU EVER BEEN FINGERPRINTED FOR OR BY THE ARIZONA RACING COMMISSION? . . . . . YES ☐ NO ☐

5. HAVE YOU EVER BEEN FINED, SUSPENDED, SET DOWN, EJECTED FROM, OR DENIED PRIVILEGES OF ANY RACE TRACK? YES ☐ NO ☐

6. GIVE DETAILS ON ALL RULINGS, CONVICTIONS, ETC., IF NOT DECLARED WITH THE ARIZONA RACING COMMISSION.

_____

_____

7. HAVE YOU PREVIOUSLY BEEN LICENSED BY ANY RACING COMMISSION OR AUTHORITY INCLUDING ARIZONA? . . . . . YES ☐ NO ☐

_____ AS A _____
STATE

_____ AS A _____
STATE

8. AT THE TIME OF MAKING THIS APPLICATION ARE YOU UNDER SUSPENSION OR OTHERWISE BARRED FROM RACING BY A RACING ASSOCIATION OR COMMISSION? . . . . . YES ☐ NO ☐

IF YES, GIVE DETAILS _____

_____

STEWARD _____ TYPED _____ PROCESSED _____

TRAINERS

(TO BE ANSWERED BY TRAINER APPLICANTS)

Where are Greyhounds Kenneled / Horses Stabled? _____

List each owner for whom you are training and number of greyhounds / horses owned by them now in your possession:

Owner _____ Address _____ Number of Greyhounds _____ Number of Horses _____

Owner _____ Address _____ Number of Greyhounds _____ Number of Horses _____

Owner _____ Address _____ Number of Greyhounds _____ Number of Horses _____

Owner _____ Address _____ Number of Greyhounds _____ Number of Horses _____

OWNERS

I am the owner of the following named greyhounds or horses:

NAME	NAME	NAME

List anyone having an interest with you in any of the above named greyhounds or horses:

Name _____ Address _____ Nature of Interest _____

Name _____ Address _____ Nature of Interest _____

Name _____ Address _____ Nature of Interest _____

A FALSE ANSWER TO ANY QUESTION IN THIS APPLICATION CONSTITUTES GROUNDS FOR SUSPENSION OR REVOCATION OF YOUR LICENSE

I hereby make application for license to be issued in accordance with the terms and provisions of the Rules and Regulations of the Arizona Racing Commission.

In making this application for a license to participate in racing, it is understood that an investigative report may be made whereby information is obtained through personal interviews with third parties, such as family members, business associates, financial sources, friends, neighbors, or others with whom you are acquainted. This inquiry includes information as to your character, general reputation, and personal characteristics which may be applicable. You have the right to make a written request within a reasonable period of time for a complete and accurate disclosure of additional information concerning the nature and scope of the investigation.

The undersigned, being duly sworn, says that he/she is the applicant above named; that he/she has read the complete application and know the contents thereof; that the same is true of the applicant's own knowledge, and is made for the purpose of inducing the Arizona Racing Commission to issue the license applied for; that he/she does assent and agrees, as a condition precedent to receiving said license, that he/she will strictly comply with the laws of the State of Arizona and with the Rules and Regulations of the Arizona Racing Commission, and further assents and agrees that said license may be at any time suspended or revoked by the Arizona Racing Commission. I CERTIFY UNDER PENALTY OF PERJURY THAT THE STATEMENTS AND ANSWERS I HAVE MADE IN THIS APPLICATION ARE TRUE AND CORRECT.

STATE OF _____ } ss.

COUNTY OF _____

Sworn to before me this _____ day of _____, 19____.

(SEAL)

X _____

SIGNATURE MUST BE NOTARIZED UNLESS SIGNED IN THE PRESENCE OF AN EMPLOYEE OF THE ARIZONA RACING COMMISSION

_____ NOTARY PUBLIC

_____ EMPLOYEE - ARIZONA RACING COMMISSION

My Commission Expires: _____

§ 5-111.02. Capital improvements at horse tracks; reduction in percentage to state; approval by commission

A. To encourage the improvement of racing facilities for the benefit of the public, breeders, and horse owners, and to increase the revenue to the state from the increase in pari-mutuel wagering resulting from such improvements, the percentage paid by a permittee to the state as provided in § 5-111, subsection C, shall be reduced by one per cent of the total amount wagered for those permittees who make capital improvements to existing race tracks and such amount shall be paid to the permittees making such capital improvements. When a permittee other than the permittee making the capital improvements, such as a lessee, is authorized to conduct racing at the facility being improved, the percentage paid by such permittee to the state as provided in § 5-111, subsection C, shall be reduced by one per cent of the total amount wagered and such amount shall be paid by such permittee to the permittee making the capital improvements.

B. In order to qualify for the reduction in percentage, a permittee shall first apply to the commission in such form as the commission shall require. The application shall contain, but is not limited to, full details of the proposed capital improvement and the cost and expenses to be incurred. After receipt of the application the commission may tentatively approve or may disapprove such application and shall, within ten days of such tentative approval or disapproval, transmit a copy of the application and notification of tentative approval or disapproval to the president of the Arizona senate and speaker of the Arizona house of representatives. If the commission tentatively approves an application it shall conduct periodic inspections of at least one per month during the construction period of the capital improvement in order to ascertain compliance with the permittee's application. Upon completion of the construction of the capital improvement, the permittee shall notify the commission and may seek final approval of its application by the commission. When the construction cost has been certified by the commission pursuant to subsection E and the commission has determined the permittee's compliance or noncompliance with its application, the commission shall grant final approval of such application or shall disapprove such application. The commission shall not approve an application unless it determines that the capital improvement will promote the safety of horses, the safety, convenience and comfort of the people and is in the best interest of racing and the state of Arizona generally. If the commission grants final approval of the application the permittee shall qualify for the reduction in percentage.

C. The reduction in percentage shall start from the day racing is first conducted following the date construction of each capital improvement is completed and the commission has granted final approval of the permittee's application and shall continue for a period of ten years or until the total reduction equals one hundred per cent of the cost of the capital improvement, whichever occurs first. The total reduction because of capital improvements shall not during any one year exceed for all permittees using any one track one per cent of the total amount wagered, regardless of the number or cost of capital improvements made, but several improvements to a race track may be consolidated in an application. The commission shall notify the state treasurer when the reduction in percentage begins and ends and shall annually, on the third Monday in January, notify the president of the Arizona senate and the speaker of the Arizona house of representatives of the permittee or permittees receiving a reduction in percentage for capital improvements during the preceding year and the amount of such reduction for each permittee. If more than one application is filed for any one race track within a ten-year period, the percentage reduction granted for each application subsequent to the first application shall not commence, nor shall the ten-year period begin to run, until the percentage reduction has ended for any prior application.

D. The term "capital improvement" means an addition, replacement, or remodeling of a race track facility involving an expenditure of at least one hundred thousand dollars. Capital improvement does not include the cost of ordinary repairs and maintenance required to keep a race track facility in ordinary operating condition.

E. The cost of a capital improvement shall be determined by generally accepted accounting principles and verified upon completion of the project by an audit of the permittee's records conducted by the commission or by an independent certified public accountant selected by the permittee and approved by the commission. Added Laws 1978, Ch. 124, § 2, eff. June 1, 1978.

Library References
Gaming ⟹4.
C.J.S. Gaming §§ 50, 82.

APPENDIX III

FINANCIAL ACCOUNTING STANDARDS BOARD PRONOUNCEMENT 34

APPENDIX III

Statement of Financial Accounting Standards No. 34

Capitalization of Interest Cost

October 1979

Financial Accounting Standards Board
of the Financial Accounting Foundation
HIGH RIDGE PARK, STAMFORD, CONNECTICUT 06905

Statement of Financial Accounting Standards No. 34

Capitalization of Interest Cost

October 1979

INTRODUCTION

1. This Statement establishes standards of financial accounting and reporting for capitalizing interest cost as a part of the historical cost of acquiring certain assets. For the purposes of this Statement, *interest cost* includes interest recognized on obligations having explicit interest rates,[1] interest imputed on certain types of payables in accordance with APB Opinion No. 21, *Interest on Receivables and Payables,* and interest related to a capital lease determined in accordance with FASB Statement No. 13, *Accounting for Leases.*

2. Paragraphs 15 and 16 of Opinion 21 provide that the discount or premium that results from imputing interest for certain types of payables should be amortized as interest expense over the life of the payable and reported as such in the statement of income. Paragraph 12 of Statement 13 provides that, during the term of a capital lease, a portion of each minimum lease payment shall be recorded as interest expense. This Statement modifies Opinion 21 and Statement 13 in that the amount chargeable to interest expense under the provisions of those paragraphs is eligible for inclusion in the amount of interest cost capitalizable in accordance with this Statement.

3. Some enterprises now charge all interest cost to expense when incurred; some enterprises capitalize interest cost in some circumstances; and some enterprises, primarily public utilities, also capitalize a cost for equity funds in some circumstances. This diversity of practice and an observation that an increasing number of nonutility registrants were adopting a policy of capitalizing interest led the Securities and Exchange Commission to

[1] Interest cost on these obligations includes amounts resulting from periodic amortization of discount or premium and issue costs on debt.

impose, in November 1974, a moratorium on adoption or extension of such a policy by most nonutility registrants until such time as the FASB established standards in this area.[2]

4. Appendix A provides additional background information. Appendix B sets forth the basis for the Board's conclusions, including alternatives considered and reasons for accepting some and rejecting others.

5. The Addendum to APB Opinion No. 2, *Accounting for the 'Investment Credit'*, states that "differences may arise in the application of generally accepted accounting principles as between regulated and nonregulated businesses, because of the effect in regulated businesses of the rate-making process," and discusses the application of generally accepted accounting principles to regulated industries. Accordingly, the provisions of the Addendum shall govern the application of this Statement to those operations of an enterprise that are regulated for rate-making purposes on an individual-company-cost-of-service basis.

STANDARDS OF FINANCIAL ACCOUNTING AND REPORTING

6. The historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.[3] If an asset requires a period of time in which to carry out the activities[4] necessary to bring it to that condition and location, the interest cost incurred during that period as a result of expenditures for the asset is a part of the historical cost of acquiring the asset.

7. The objectives of capitalizing interest are (a) to obtain a measure of acquisition cost that more closely reflects the enter-

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[2] Securities and Exchange Commission, ASR No. 163, *Capitalization of Interest by Companies Other Than Public Utilities* (Washington: November 14, 1974).

[3] The term *intended use* embraces both readiness for use and readiness for sale, depending on the purpose of acquisition.

[4] See paragraph 17 for a definition of those activities for purposes of this Statement.

prise's total investment in the asset and (b) to charge a cost that relates to the acquisition of a resource that will benefit future periods against the revenues of the periods benefited.

8. In concept, interest cost is capitalizable for all assets that require a period of time to get them ready for their intended use (an "acquisition period"). However, in many cases, the benefit in terms of information about enterprise resources and earnings may not justify the additional accounting and administrative cost involved in providing the information. The benefit may be less than the cost because the effect of interest capitalization and its subsequent amortization or other disposition, compared with the effect of charging it to expense when incurred, would not be material. In that circumstance, interest capitalization is not *required* by this Statement.

Assets Qualifying for Interest Capitalization

9. Subject to the provisions of paragraph 8, interest shall be capitalized for the following types of assets ("qualifying assets"):

a. Assets that are constructed or otherwise produced for an enterprise's own use (including assets constructed or produced for the enterprise by others for which deposits or progress payments have been made)
b. Assets intended for sale or lease that are constructed or otherwise produced as discrete projects (e.g., ships or real estate developments).

10. However, interest cost shall not be capitalized for inventories that are routinely manufactured or otherwise produced in large quantities on a repetitive basis because, in the Board's judgment, the informational benefit does not justify the cost of so doing. In addition, interest shall not be capitalized for the following types of assets:

a. Assets that are in use or ready for their intended use in the earning activities of the enterprise
b. Assets that are not being used in the earning activities of the

enterprise and that are not undergoing the activities necessary to get them ready for use.

11. Land that is not undergoing activities necessary to get it ready for its intended use is not a qualifying asset. If activities are undertaken for the purpose of developing land for a particular use, the expenditures to acquire the land qualify for interest capitalization while those activities are in progress. The interest cost capitalized on those expenditures is a cost of acquiring the asset that results from those activities. If the resulting asset is a structure, such as a plant or a shopping center, interest capitalized on the land expenditures is part of the acquisition cost of the structure. If the resulting asset is developed land, such as land that is to be sold as developed lots, interest capitalized on the land expenditures is part of the acquisition cost of the developed land.

The Amount of Interest Cost to Be Capitalized

12. The amount of interest cost to be capitalized for qualifying assets is intended to be that portion of the interest cost incurred during the assets' acquisition periods that theoretically could have been avoided (for example, by avoiding additional borrowings or by using the funds expended for the assets to repay existing borrowings) if expenditures for the assets had not been made.

13. The amount capitalized in an accounting period shall be determined by applying an interest rate(s) ("the capitalization rate") to the average amount of accumulated expenditures for the asset during the period. The capitalization rates used in an accounting period shall be based on the rates applicable to borrowings outstanding during the period. If an enterprise's financing plans associate a specific new borrowing with a qualifying asset, the enterprise may use the rate on that borrowing as the capitalization rate to be applied to that portion of the average accumulated expenditures for the asset that does not exceed the amount of that borrowing. If average accumulated expenditures for the asset exceed the amounts of specific new borrowings associated with the asset, the capitalization rate to be applied to such excess shall

be a weighted average of the rates applicable to other borrowings of the enterprise.

14. In identifying the borrowings to be included in the weighted average rate, the objective is a reasonable measure of the cost of financing acquisition of the asset in terms of the interest cost incurred that otherwise could have been avoided. Accordingly, judgment will be required to make a selection of borrowings that best accomplishes that objective in the circumstances. For example, in some circumstances, it will be appropriate to include all borrowings of the parent company and its consolidated subsidiaries; for some multinational enterprises, it may be appropriate for each foreign subsidiary to use an average of the rates applicable to its own borrowings. However, the use of judgment in determining capitalization rates shall not circumvent the requirement that a capitalization rate be applied to all capitalized expenditures for a qualifying asset to the extent that interest cost has been incurred during an accounting period.

15. The total amount of interest cost capitalized in an accounting period shall not exceed the total amount of interest cost incurred by the enterprise in that period. In consolidated financial statements, that limitation shall be applied by reference to the total amount of interest cost incurred by the parent company and consolidated subsidiaries on a consolidated basis. In any separately issued financial statements of a parent company or a consolidated subsidiary and in the financial statements (whether separately issued or not) of unconsolidated subsidiaries and other investees accounted for by the equity method, the limitation shall be applied by reference to the total amount of interest cost (including interest on intercompany borrowings) incurred by the separate entity.

16. For the purposes of this Statement, *expenditures* to which capitalization rates are to be applied are capitalized expenditures (net of progress payment collections) for the qualifying asset that have required the payment of cash, the transfer of other assets, or the incurring of a liability on which interest is recognized (in contrast to liabilities, such as trade payables, accruals, and retainages on which interest is not recognized). However, reasonable approximations of net capitalized expenditures may be used.

For example, capitalized costs for an asset may be used as a reasonable approximation of capitalized expenditures unless the difference is material.

The Capitalization Period

17. The capitalization period shall begin when three conditions are present:

a. Expenditures (as defined in paragraph 16) for the asset have been made.
b. Activities that are necessary to get the asset ready for its intended use are in progress.
c. Interest cost is being incurred.

Interest capitalization shall continue as long as those three conditions are present. The term *activities* is to be construed broadly. It encompasses more than physical construction; it includes all the steps required to prepare the asset for its intended use. For example, it includes administrative and technical activities during the preconstruction stage, such as the development of plans or the process of obtaining permits from governmental authorities; it includes activities undertaken after construction has begun in order to overcome unforeseen obstacles, such as technical problems, labor disputes, or litigation. If the enterprise suspends substantially all activities related to acquisition of the asset, interest capitalization shall cease until activities are resumed. However, brief interruptions in activities, interruptions that are externally imposed, and delays that are inherent in the asset acquisition process shall not require cessation of interest capitalization.

18. The capitalization period shall end when the asset is substantially complete and ready for its intended use. Some assets are completed in parts, and each part is capable of being used independently while work is continuing on other parts. An example is a condominium. For such assets, interest capitalization shall stop on each part when it is substantially complete and ready for use. Some assets must be completed in their entirety before any part of the asset can be used. An example is a facility designed to manufacture products by sequential processes. For

such assets, interest capitalization shall continue until the entire asset is substantially complete and ready for use. Some assets cannot be used effectively until a separate facility has been completed. Examples are the oil wells drilled in Alaska before completion of the pipeline. For such assets, interest capitalization shall continue until the separate facility is substantially complete and ready for use.

19. Interest capitalization shall not cease when present accounting principles require recognition of a lower value for the asset than acquisition cost; the provision required to reduce acquisition cost to such lower value shall be increased appropriately.

Disposition of the Amount Capitalized

20. Because interest cost is an integral part of the total cost of acquiring a qualifying asset, its disposition shall be the same as that of other components of asset cost.

Disclosures

21. The following information with respect to interest cost shall be disclosed in the financial statements or related notes:

a. For an accounting period in which no interest cost is capitalized, the amount of interest cost incurred and charged to expense during the period
b. For an accounting period in which some interest cost is capitalized, the total amount of interest cost incurred during the period and the amount thereof that has been capitalized.

Effective Date and Transition

22. This Statement shall be applied prospectively in fiscal years beginning after December 15, 1979. Earlier application is permitted, but not required, in financial statements for fiscal years beginning before December 16, 1979 that have not been previously issued. With respect to qualifying assets in existence at the

beginning of the fiscal year in which this Statement is first applied for which interest cost has not been previously capitalized, interest capitalization shall begin at that time. With respect to qualifying assets for which interest cost has been capitalized according to a method that differs from the provisions of this Statement, no adjustment shall be made to the amounts of interest cost previously capitalized, but interest cost capitalized after this Statement is first applied shall be determined according to the provisions of this Statement. With respect to assets in existence when this Statement is first applied for which interest cost has been capitalized but which do not qualify for interest capitalization according to the provisions of this Statement, no adjustments shall be made, but no additional amounts of interest cost shall be capitalized.

23. If early application is adopted in financial reports for interim periods of a fiscal year beginning before December 16, 1979, previously issued financial information for any interim periods of that fiscal year that precede the period of adoption shall be restated to give effect to the provisions of this Statement, and any subsequent presentation of that information shall be on the restated basis. This Statement shall not be applied retroactively for previously issued annual financial statements.

The provisions of this Statement need not be applied to immaterial items.

APPENDIX IV

LEGISLATIVE COUNCIL OPINION O-81-5
FEBRUARY 13,1981

APPENDIX IV

ARIZONA LEGISLATIVE COUNCIL

MEMO

February 13, 1981

TO: Douglas R. Norton
Auditor General

FROM: Arizona Legislative Council

RE: Request for Research and Statutory Interpretation (0-81-5)

This is in response to a request submitted on your behalf by Gerald A. Silva in a memo dated February 4, 1981. No input was received from the attorney general concerning this request.

FACT SITUATION:

Arizona Revised Statutes (A.R.S.) section 5-111.02 allows commercial racing permittees to reduce the state's percentage of the total amount wagered by one percent of the total wager. These funds are to be used to make capital improvements to horse racing facilities.

A.R.S. section 5-111.02, subsection D states:

> The term "capital improvement" means an addition, replacement, or remodeling of a race track facility involving an expenditure of at least one hundred thousand dollars. Capital improvement does not include the cost of ordinary repairs and maintenance required to keep a race track facility in ordinary operating condition.

During the course of our review it was noted that several of the permittees requested approval for the acquisition of automobiles, trucks and other vehicles as capital improvements.

QUESTION PRESENTED:

Are permittees allowed to purchase automobiles, trucks and other vehicles as capital improvements under the provisions of A.R.S. section 5-111.02?

ANSWER:

No.

DISCUSSION:

The state accounting manual classifies the purchase of automobiles and trucks as a capital outlay expenditure. However in the situation described, a special more limited legislative definition of capital improvement controls.

To qualify for approval, a capital improvement, under the definition prescribed by A.R.S. section 5-111.02, subsection D, must be at least a $100,000 addition, replacement or remodeling of a race track facility and must also fall within the standard prescribed by subsection B of that section in that it must:

> /P/romote the safety of horses, the safety, convenience and comfort of the people and is in the best interests of racing and the state of Arizona generally.

The purchase of automobiles or trucks clearly would not comply with these standards.

cc: Gerald A. Silva
Performance Audit Manager

APPENDIX V

LEGISLATIVE COUNCIL OPINION 0-80-62
DECEMBER 5, 1980

APPENDIX V

ARIZONA LEGISLATIVE COUNCIL

MEMO

December 5, 1980

TO: Douglas R. Norton
Auditor General

FROM: Arizona Legislative Council

RE: Request for Research and Statutory Interpretation (0-80-62)

This is in response to a request submitted on your behalf by Gerald A. Silva in a memo dated November 21, 1980. No input was received from the attorney general concerning this request.

FACT SITUATION:

Arizona Revised Statutes (A.R.S.) section 5-111.02, subsection A provides for the use of state funds for capital improvements at horse tracks. Subsection D defines a capital improvement as:

> /A/n addition, replacement, or remodeling of a race track facility involving an expenditure of at least one hundred thousand dollars. Capital improvement does not include the cost of ordinary repairs and maintenance required to keep a race track facility in ordinary operating condition.

Subsection E requires that capital improvements records be audited by:

> /T/he /Arizona racing/ commission or by an independent certified public accountant selected by the permittee and approved by the commission.

A.R.S. section 5-113, subsection B provides for the distribution of county fairs and breeders' award funds to the county fair associations "for the promotion . . . of county fair racing meets."

Expenditures by one horse track for birds and plants have been approved by the commission as capital improvements. Expenditures by a county fair for items such as a coffee pot, copy machine and special typewriter head were also approved by the commission.

The commission requires that the counties submit financial statements which itemize the capital expenditures. The statements include a disclaimer to the attest function from a CPA, but do not contain a statement of opinion.

QUESTIONS PRESENTED:

1. What constitutes a capital improvement for which funds may be allocated to A) horse tracks, and B) county fairs? Specifically, what types of items may or may not be purchased with capital improvements funds?

2. Should the financial statements supporting expenditures by the counties include a traditional statement of opinion by a CPA concerning the fair and accurate presentation of information?

DISCUSSION:

1. Normally, when an agency follows standard accounting procedures, capital outlay expenditures for a regular operating budget would properly include such items as desks, potted plants or copy machines while items such as pencils would be properly classified as supplies. In this case, however, the controlling statute limits purchases to major capital improvements. To qualify for approval, a capital improvement, under the definition prescribed by A.R.S. section 5-111.02, subsection D, must be at least a $100,000 addition, replacement or remodeling of a race track facility and must also fall within the standard prescribed by subsection B of that section in that it must:

> /P/romote the safety of horses, the safety, convenience and comfort of the people and is in the best interests of racing and the state of Arizona generally.

With respect to the items mentioned, it is difficult to see how birds could be a capital improvement. The purchase of plants, whether bought separately and costing over $100,000 or as part of a remodeling plan costing over $100,000, could very well be properly classified as a capital improvement. Certainly extensive landscape improvements are within contemplation of legislative intent. The propriety of classifying other items as capital improvements, however, can only be evaluated on a case-by-case basis using the guidelines prescribed in A.R.S. section 5-111.02.

The use of the county fairs racing and breeders' award fund is not limited to capital improvements under the terms of A.R.S. section 5-113, subsection B. Expenditures do not have to come from capital improvement funds nor must they be for capital improvements. The commission has complete discretion in the allocation of monies from the award fund so long as the use of the monies is deemed "necessary for the promotion and betterment of county fair racing meets." A.R.S. section 5-113, subsection B. It is conceivable that the items mentioned were appropriately approved by the commission.

2. A.R.S. section 5-111.02, subsection E does not apply to financial statements concerning the expenditure of county fairs racing and breeders' award fund monies authorized by A.R.S. section 5-113. All that is required by statute is that expenditures must be made on "claims approved by the commission." A.R.S. section 5-113, subsection B. So long as the commission is satisfied with the financial statements currently being filed by county fair associations, such statements would not have to include statements of opinion.

cc: Gerald A. Silva
Performance Audit Manager

APPENDIX VI

LEGISLATIVE COUNCIL OPINION O-80-63
DECEMBER 12, 1980

ARIZONA LEGISLATIVE COUNCIL

MEMO

December 12, 1980

TO: Douglas R. Norton, Auditor General

FROM: Arizona Legislative Council

RE: Request for Research and Statutory Interpretation (0-80-63)

This is in response to a request submitted on your behalf by Gerald A. Silva in a memo dated November 20, 1980. No input was received from the attorney general concerning this request.

FACT SITUATION:

The two stewards employed by the permittee and one steward employed by the Arizona racing commission (commission) jointly decide the outcome of contested races and hold hearings for individuals charged with violations of the statutes and rules and regulations. Stewards' rulings may include suspension of a license and/or imposition of fines. Decisions are binding on the licensee and may be appealed to the commission.

Arizona racing commission rule R4-27-209.G.18.(f). provides that "/n 7o special announcement of the hearing or of the alleged infraction . . . shall be made until after said hearing."

QUESTIONS PRESENTED:

1. Are sessions during which contested races are decided and hearings for violations held subject to the provisions of the open meeting law?

2. What documentation of these sessions must be maintained? Specifically, must there be documentation concerning:

(a) The individuals involved in a contested race and the nature of the objection.

(b) Statements made by persons charged with violations.

(c) The votes cast by each steward.

ANSWERS:

1. Hearings held for violations of the statutes or rules relating to horse and dog racing are subject to the open meeting law. Sessions held to decide contested races are not subject to the law.

2. There is no statutory guideline as to what documentation of these sessions must be maintained. Requiring the types of documentation mentioned in your letter does not appear overly harsh.

DISCUSSION:

1. Arizona Revised Statutes (A.R.S.) section 5-104, subsection B allows the commission to delegate to stewards its powers and duties as necessary to fully carry out and effectuate the purposes of the statutes relating to horse and dog racing. Subsection E of that section provides that a person may apply to the commission for a review of a decision of the track stewards within three days after that decision. In conjunction with the review, the commission may issue subpoenas and administer oaths. A.R.S. section 5-104, subsection F.

In performing their duties, the stewards:

> . . . may impose a civil penalty on any person subject to their control, for violation of these Rules, in an amount not exceeding $500.00. In addition, the stewards may suspend for a period of time not exceeding 30 days on any person violating any of these Rules. Nothing in these Rules shall be construed to prevent the stewards from imposing a civil penalty and suspension for the same violation. . . . A.C.R.R. R4-27-209 F.

The commission, by regulation, has prescribed the procedure to be taken by track stewards if they feel that a person has violated a rule of the commission. A.C.R.R. R4-27-209 G, 18, 19 states:

> 18. Stewards hearings. When the stewards feel that a Rule has been violated by any person the procedure shall be as follows:
>
> a. The person shall be summoned to a hearing before the stewards, called for that purpose, at which all stewards shall be present;
>
> b. Twenty-four hour notice of said hearing shall be given to the person in writing, on a form supplied by the Commission. This notice shall be timed and dated and signed by the person, the original shall remain with the State steward, and if referred shall be part of the case file and a copy shall be kept by the person.
>
> c. No penalty shall be imposed until such hearing;
>
> d. Nonappearance of the summoned party after adequate notice shall be construed as a waiver of right to hearing before the stewards, and
>
> e. The person summoned to a hearing shall be permitted to present witnesses on his own behalf.

f. No special announcement of the hearing or of the alleged infraction of Rules shall be made until after said hearing.

g. If after hearing there is substantial evidence to invoke a civil penalty on a violation of these Rules the appropriate action shall be taken by the stewards including suspension or civil penalty. The stewards shall promptly forward their written decision or ruling to the Commission and to the party in question.

h. In the interest of the health, safety and welfare of the people of the State of Arizona the stewards may summarily declare a horse scratched and may suspend a license pending a steward's hearing.

i. All monies collected from civil penalties imposed by the stewards of the meeting shall be paid to the Arizona Racing Commission within 72 hours, for deposit with the State Treasurer.

19. All matters within their jurisdiction shall be determined by a majority vote of the stewards.

The purpose of the Arizona open meeting act is to open state government to public scrutiny. See Laws 1962, Chapter 138, section 1. A.R.S. section 38-431.01 prescribes the general rule relating to the open meeting law. Subsection A of that section states that "/a /ll meetings of any public body shall be public meetings and all persons so desiring shall be permitted to attend and listen to the deliberations and proceedings." The relevant definitions to the above rule are contained in A.R.S. section 38-431, which states in part:

2. "Legal action" means a collective decision, commitment or promise made by a majority of the members of a public body pursuant to the constitution, their charter or bylaws or specified scope of appointment or authority, and the laws of this state.

3. "Meeting" means the gathering of a quorum of members of a public body to propose or take legal action, including any deliberations with respect to such action.

4. "Public body" means the governing bodies and all boards and commissions which are supported in whole or in part by tax revenues or which expend tax revenues, of the state, its political subdivisions, incorporated cities and towns, and any standing, special or advisory committee or subcommittee of, or appointed by, such governing body, board or commission. Public body also includes any quasi-judicial body of the state, its political subdivisions or incorporated cities and towns.

5. "Quasi-judicial body" means a public body, other than a court of law, possessing the power to hold hearings on disputed matters between a private person and a public agency and to make decisions in the general manner of a court regarding such disputed claims.

Notice of meetings falling under the open meeting law must be given to the public at least 24 hours prior to the meeting. See A.R.S. section 38-431.02.

Clearly the commission is an entity of the state, supported in part by tax revenues. Therefore, the commission is a public body, subject to the open meeting laws. The question then becomes whether hearings held by stewards are also subject to this requirement.

The provisions of the open meeting law apply to all standing, special and advisory committees or subcommittees of a public body. A committee or subcommittee is any group of two or more people appointed by or authorized to act on behalf of a public body. By the terms of A.R.S. section 5-104, subsection B, the commission has authority to delegate its powers and duties to the racing stewards. By virtue of this authority, the commission has given the stewards the power to impose fines and suspend licenses. Therefore, it can be said that the stewards are acting on behalf of the commission. To the extent then that the stewards meet to propose or take legal action they are subject to the requirement that the meeting be open to the public.

The attorney general has stated that "/a/ll discussions, deliberations, considerations or consultations . . . regarding matters which may foreseeably require final action or a final decision of the governing body constitute legal action." 75 Op. Att'y Gen. 75-8 (1975). There is no precise test as to when this criterion has been met and each case must be decided on its own merits. However, considering the purpose of the open meeting act, in each case all doubts should be resolved in favor of opening a meeting to the public. In addition, commission rules require the stewards to take some sort of action relating to a rules violation. For these reasons, the hearing required by the commission appears to be subject to the public notice requirement of A.R.S. section 38-431.02. Based on this conclusion, A.C.R.R. R4-27-209 G, 18 (f) violates the open meeting requirement under Arizona law.

A different set of circumstances exists for sessions by which contested races are decided. These sessions are held immediately after the running of the race and are solely for the purpose of deciding the winner of the race. Thus, the stewards are not taking "legal action" and the sessions are exempt from the open meeting requirement. However, any penalty imposed for a violation of the rules during the running of the race would be subject to a hearing and, as discussed above, would require notice to the public. In addition, it should be pointed out that sessions held immediately after a race could not possibly comply with the 24 hour notice requirement of A.R.S. section 38-431.02.

2. A search of the statutes and the commission rules revealed no requirement as to what documentation is needed of those sessions which decide contested races. However, since a person may request commission review of any decision of track stewards, some type of record should be maintained by the stewards. Requiring the types of documentation mentioned in your letter does not appear to be overly harsh or burdensome. You may wish to recommend that the legislature act to clarify this matter.

CONCLUSION AND RECOMMENDATION:

1. Hearings for possible violations of the statutes or rules relating to horse and dog racing are subject to the provisions of the open meeting law. However, sessions during which contested races are decided are not subject to this law.

2. There is no statutory guideline as to what documentation must be maintained of those sessions which decide contested races. You may wish to recommend that the legislature act to require specific types of documentation.

cc: Gerald A. Silva
Performance Audit Manager

APPENDIX VII

LEGISLATIVE COUNCIL OPINION O-80-65
DECEMBER 22, 1980

ARIZONA LEGISLATIVE COUNCIL

MEMO

December 22, 1980

TO: Douglas R. Norton, Auditor General

FROM: Arizona Legislative Council

RE: Request for Research and Statutory Interpretation (O-80-65)

This is in response to a request submitted on your behalf by Gerald A. Silva in a memo dated December 4, 1980. No input was received from the attorney general concerning this request.

FACT SITUATION:

Until mid-1978, the monies received from fines imposed by the racing stewards were deposited by the Arizona racing commission (commission) in "race track benevolent funds" with the managements of the various tracks. Loans, approved by the stewards, were made to licensees from these "race track benevolent funds". The loans were to be made to the needy. Subsequent to mid-1978, monies received from fines have been deposited to the general fund.

QUESTION:

Did the commission have the authority to:

1. Deposit the monies in these "benevolent funds", and

2. Grant loans to licensees from these funds?

ANSWERS:

1. No. A search of the Arizona Revised Statutes (A.R.S.) relating to horse and dog racing that were added or amended prior to 1978 revealed no explicit authority for the commission to establish any "race track benevolent fund".

However, in 56 Op. Att'y. Gen. 56-113 (1956), the attorney general assumed that certain funds derived from nomination and starting fees from individual horse owners could be established under the general supervisory power granted to the racing commission under A.R.S. section 5-104, subsection A. A copy of this opinion is enclosed.

Nevertheless, assuming the rationale of the 1956 attorney general opinion is still correct, the 1956 opinion can be distinguished from the facts of the present case.

In the first place, the funds created in 1956 were used to establish a purse that was divided by the winners of an "Arizona Breeder's Futurity" and "Arizona Derby" race. As noted in the opinion, establishment of "futurity" races was customary throughout the country. In this case, the facts indicate that monies in the fund were used as loans to licensees rather than as payment to a winner of a horse race.

Secondly, the 1956 funds were derived from nomination and starting fees of individual horse owners. The facts in this case state that the benevolent funds were derived from monies received from fines.

Therefore, the use of A.R.S. section 5-104, subsection A as implicit authority for the commission to establish benevolent funds from fines imposed by racing stewards is suspect.

2. No. Similarly, a search of the horse and dog racing statutes added or amended prior to 1978 disclosed no power of the commission to grant loans to licensees from race track benevolent funds.

Additionally, Article IX, section 7 of the Arizona Constitution would prohibit the granting of a loan to a licensee. That section states that public monies may not be used to give gifts or loans to an individual, association or corporation. Granting monies to a licensee for loans to the needy, although a worthy cause, is not enough to justify giving public monies to an individual, association or corporation. Udall v. State Loan Board 35 Ariz. 1, 273 P. 721 (1929)

CONCLUSION:

Arizona Revised Statutes relating to horse and dog racing that were added or amended prior to 1978 contained no authority for the racing commission to deposit monies into "race track benevolent funds" or to grant loans to licensees from these funds.

Encl.

cc: Gerald A. Silva
Performance Audit Manager

of the legislative appropriation. The last sentence, providing for the apportionment of additional costs on a per pupil basis requiring them to be a charge *against the districts involved* clearly contemplates a homebound school on a county-wide basis. Where there are additional costs, each school district sending children to the homebound school must pay a share of those additional costs on the basis of the number of pupils from the district enrolled in the homebound school.

Opinion No. 56-113 June 13, 1956

REQUESTED BY: Arizona Racing Commission

OPINION BY: Robert Morrison, The Attorney General
Robert E. Kersting, Special Assistant Attorney General

QUESTION: May the Arizona Racing Commission transfer funds now held as the "Futurity and Derby Fund" to the Turf Paradise, Inc., Race Track?

CONCLUSION: No.

The Arizona Racing Commission created by regulatory order on August 24, 1951, the "Arizona Breeders' Futurity" and the "Arizona Derby". By virtue of said order, two funds were established for each of said races resulting from nomination fees and starting fees deposited with the Racing Commission by individual horse owners over respective periods of two and three years. These fees have customarily been made payable to th secretary of the Racing Commission and deposited in a private bank account designated as the "Futurity and Derby Fund." At the time of the annual running of the particular races, said funds are used to establish a purse to be divided by the winners of the subject race.

The Arizona statutes governing racing are silent relative to authority for the creation or disposition of any such funds. However, futurity races of this nature are customary throughout the United States and it might accordingly be assumed that the general supervisory powers granted to the Racing Commission would include the establishment of such races and the creation of the subject funds. (A. R. S. § 5-104(A)).

It would seem that the following Arizona statutes should be considered in formulating an answer to the proposed question: A. R. S. § 5-113, 35-142, 35-148, 35-149 and 35-302.

It seems clear that the subject funds have been acquired by an agent of the state acting in his official capacity, and it is accordingly the opinion of this department that said funds may not be transferred to a private individual but that they must be deposited with the state treasurer as "private funds" and disbursed in accordance with the foregoing statutes.

Opinion No. 56-114 June 14, 1956

REQUESTED BY: Arizona Highway Patrol

OPINION BY: Robert Morrison, The Attorney General
Ronald M. Bond, Assistant Attorney General

QUESTION: What constitutes a violation of the laws of Arizona with regard to noisy mufflers on motor vehicles?

CONCLUSION: Mufflers must be attached to all motor vehicles and kept in constant good working order to prevent excessive or unusual noise.

The answer to the above question is found in A. R. S. § 28-955 A, and an interpretation of that statute.

A very recent case from the State of Texas and the only case we have found interpreting the above statute is *Ex parte William Forest Trafton*, 271 S.W. 2d 814, which discusses the meaning of the term "excessive and