



# The Commonwealth of Massachusetts

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NO. 2007-1352-30

**INDEPENDENT STATE AUDITOR'S REPORT ON  
CERTAIN ACTIVITIES OF THE  
MASSACHUSETTS THOROUGHBRED BREEDERS  
ASSOCIATION, INC.**

**JULY 1, 2004 TO DECEMBER 31, 2006**

**OFFICIAL AUDIT  
REPORT  
JUNE 20, 2007**

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The Massachusetts Thoroughbred Breeders Association, Inc. (MTBA) is a nonprofit organization, incorporated on March 23, 1981, whose purpose is to engage in activities and programs designed to encourage and promote the breeding, propagation, ownership, raising, racing, and marketing of Thoroughbred horses bred and foaled within the Commonwealth of Massachusetts. The purpose of our audit, which covered the period July 1, 2004 to December 31, 2006, was to review receipts and expenditures for compliance and allowability under Chapter 128, Section 2, of the Massachusetts General Laws. Specifically, the objectives of our review were to determine whether (1) MTBA's financial activity and related items were fairly presented in accordance with generally accepted accounting principles, and (2) MTBA complied with applicable laws, rules, and regulations that may have a material effect upon its financial activities. We also conducted a follow-up review of MTBA's progress in addressing the issues noted in our prior audit report.

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### AUDIT RESULTS

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#### 1. PRIOR AUDIT RESULTS RESOLVED

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During our follow-up review, we determined that the Massachusetts Thoroughbred Breeders Association, Inc. (MTBA) has taken corrective action to resolve issues revealed in our prior audit report regarding inadequate documentation of cash disbursements, improvements needed in MTBA's cash management system, and a potential overpayment of \$10,785 made to MTBA's Executive Director.

##### a. Documentation of Cash Disbursements Improved

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Our prior audits of MTBA noted that administrative expenses lacked supporting documentation, contrary to MTBA's bylaws and sound business practices. Without adequate supporting documentation, there is limited assurance that these payments were expended properly. Our follow-up review revealed that MTBA implemented our prior recommendations and resolved this issue. MTBA is now maintaining proper vouchers for administrative expenses, and we found that all expenditures had adequate supporting documentation and were for administrative-related expenses as outlined in MTBA's bylaws.

##### b. Improvements Made in MTBA's Cash Management System

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As part of our analysis of MTBA's financial records, our prior audit identified potential improvements that could be made to MTBA's cash management system related to the reconciliation of its two checking accounts. We noted that, without such improvements, MTBA could not make proper financial decisions, particularly when setting award purses for races it sponsors.

Our follow-up review found that MTBA implemented our prior recommendations and has established adequate internal controls over its cash management system. Specifically, we found that MTBA has written policies and procedures for the reconciliation of its bank accounts and financial recordkeeping. Moreover, the Secretary/Treasurer

researched long-outstanding checks identified in the prior audit, verified the checks' validity, located the recipients, and issued replacement checks.

**c. Overpayment of \$10,785 Made to Former Executive Director Recovered** **5**

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Our prior audit report disclosed that MTBA's former Executive Director was overpaid \$10,785. Specifically, based on his contract, the Executive Director should have received \$77,603 for the fiscal year ended December 31, 2001. However, our review of MTBA's financial statements indicated that the Executive Director actually received \$88,388. Our follow-up review revealed that this amount was repaid in May 2005 and deposited into MTBA's Administrative Account, as recommended in our prior audit report.

**2. PENALTIES AND INTEREST TOTALING APPROXIMATELY \$73,000 OWED TO THE INTERNAL REVENUE SERVICE FOR LATE FILINGS OF TAX FORMS** **6**

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During our audit, MTBA disclosed that it currently owes the Internal Revenue Service (IRS) approximately \$73,000 in interest and penalties for failing to file tax returns in a timely manner. Specifically, during tax years 1996, 2001, and 2004, MTBA did not file Form 990 within the timeframe required by the IRS. Form 990 is a return filed for organizations exempt from income tax that, in MTBA's case, is required to be filed annually by May 15. MTBA also did not file Form 1099 for tax years 2000 and 2001 in a timely manner. MTBA annually files Form 1099 for any non-employee compensations or for horsemen who earned prize money in excess of \$600 during the tax year. Form 1099 is required to be filed each year by February 28.

## INTRODUCTION

### ***Background***

The Massachusetts Thoroughbred Breeders Association, Inc. (MTBA) is a nonprofit organization, incorporated on March 23, 1981, whose purpose is to engage in activities and programs designed to encourage and promote the breeding, propagation, ownership, raising, racing, and marketing of Thoroughbred horses bred and foaled within the Commonwealth of Massachusetts.

Although MTBA was originally incorporated in 1981, it took on a new role in the administration of the Massachusetts Thoroughbred Breeding Program with the passage of Chapter 114, Section 1, of the Acts of 1991; Chapter 163 of the Acts of 1999; Chapter 354 of the Acts of 2000; Chapter 139 of the Acts of 2001; and Chapter 128, Section 2, of the Massachusetts General Laws, which were enacted to promote, develop, and encourage the breeding of Thoroughbred horses in the Commonwealth by offering cash prizes to breeders of Massachusetts-bred Thoroughbred horses.

MTBA is primarily funded by a percentage of the handle of all live and simulcast racing at Sterling Suffolk Racecourse Limited Partnership (Suffolk Downs). The percentage received varies according to the requirements of the law that governs MTBA. This funding, which is MTBA's major revenue source, totaled \$820,072 for the six-month period ended December 31, 2004. Revenue collected from Suffolk Downs for calendar years 2005 and 2006 totaled \$1,140,459 and \$1,011,809, respectively.

A 12-member Board of Directors, which oversees all operations of MTBA, contracted with a consulting association to act as MTBA's Executive Director and govern the day-to-day operations of MTBA. Under the payment terms of his contract with MTBA, the Executive Director's annual compensation is calculated at the rate of 7.5% of the total revenues received from Suffolk Downs. As of April 2006, MTBA's longtime Executive Director resigned his position, and these duties are currently performed by MTBA's Treasurer.

### ***Audit Scope, Objectives, and Methodology***

The scope of our audit was to review receipts and expenditures for compliance and allowability under Chapter 139 of the Acts of 2001 and Chapter 128, Section 2, of the General Laws for the period July 1, 2004 through December 31, 2006. Our audit was conducted in accordance with

applicable generally accepted government auditing standards for performance audits and, accordingly, included such audit procedures and tests as we considered necessary.

The objectives of our review were to perform an evaluation of internal controls over financial and programmatic operations and to analyze whether (1) MTBA's financial activity and related items were fairly presented in accordance with generally accepted accounting principles and (2) MTBA complied with applicable laws, rules, and regulations that may have a material effect upon its financial activities.

Our specific objectives were to:

1. Review and analyze controls over cash receipts and cash disbursements to determine whether controls were adequate to safeguard funds and were in compliance with laws, rules, and regulations.
2. Conduct transaction testing to determine whether expenditures were reasonable, allowable, and applicable to the program.
3. Determine whether MTBA fulfilled the requirements of the laws administering the breeding programs.
4. Review MTBA's progress in addressing the issues noted in our prior audit report (No. 2004-1352-3O).

In order to meet our objectives, we reviewed MTBA's internal policies and procedures. We reviewed applicable laws, rules, and regulations and examined MTBA's financial records, cost reports, invoices, and other pertinent financial records to ensure that expenses incurred, award payments made, and revenues reported were reasonable, allowable, properly authorized, and recorded in compliance with applicable laws, rules, and regulations. We also determined whether revenues received from Suffolk Downs to MTBA were properly recorded and disbursed in accordance with regulations.

Based on our audit, except for the issue discussed in Audit Result No. 2, we have determined that MTBA has complied with laws and regulations regarding payments of awards, eligibility of Thoroughbred horses, and revenue received. In addition, we found that MTBA had (1) maintained adequate internal controls over cash receipts and disbursements; (2) complied with laws, rules, and regulations regarding payment of awards, administrative expenditures, eligibility of registered

Massachusetts-bred horses, and revenue received; and (3) satisfactorily implemented the recommendations contained in our prior audit report.

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## AUDIT RESULTS

### 1. PRIOR AUDIT RESULTS RESOLVED

Our prior audit report (No. 2004-1352-30) of the Massachusetts Thoroughbred Breeders Association, Inc. (MTBA) revealed deficiencies in MTBA's (a) documentation of cash disbursements, (b) cash management system, and (c) overpayment of \$10,785 made to its Executive Director. During our follow-up review, which covered the period July 1, 2004 to December 31, 2006, we determined that MTBA has taken corrective action to resolve these issues, as discussed below.

#### a. Documentation of Cash Disbursements Improved

Our prior audit report indicated that MTBA did not adhere to prudent business practices by requiring submission of a vendor's invoice (bill) requesting payment for services rendered or goods provided in accordance with Article 8, Section 8, of MTBA's bylaws, which stipulate:

*The Secretary-Treasurer shall disburse the funds of the corporation as may be ordered by the Board of Directors taking proper vouchers for such disbursements.*

Our prior audit report recommended that, prior to making any payments, MTBA ensure that appropriate supporting documentation is obtained and reviewed for propriety, the check signer documents his review of the supporting documentation prior to signing the check, and all supporting documentation for all expenditures are retained for the purpose of review by appropriate agencies and officials.

During our follow-up review, we found that MTBA has implemented our prior audit recommendations and improved its administrative and accounting controls, as follows:

- Proper vouchers are required prior to payment of all administrative expenditures to ensure that these payments are related to the official business of MTBA.
- Prior to check preparation, all expenditures are reviewed and approved by MTBA's Treasurer.
- All supporting documentation for all expenditures are retained for the purpose of review by appropriate agencies and officials to ensure that all expenses are administrative-related.
- MTBA's Treasurer reviews all bank reconciliations and financial data prepared by its private accountant on a monthly basis for accuracy.

**b. Improvements Made in MTBA's Cash Management System**

Our prior audit revealed that MTBA had not established adequate controls over certain aspects of its cash management system. Specifically, MTBA had not developed policies and procedures for the bank reconciliation of its two operating checking accounts (Awards Account and Administrative Account). As a result, MTBA's reconciled bank statement indicated that the Awards Account checking account balance was overdrawn. Additionally, we identified numerous outstanding checks in both checking accounts, some dating back several years, which should have been remitted to the State Treasurer as abandoned property. Without proper reconciliation of the two accounts, the MTBA could not make proper financial decisions, particularly when setting award purses for races it sponsors.

Our follow-up review revealed that MTBA has implemented our prior recommendations and improved its cash management systems, as follows:

- MTBA has established written policies and procedures to ensure its checking accounts are properly reconciled in a timely manner. In addition, all outstanding checks were being followed up on immediately.
- The Treasurer located the payees of all outstanding checks in both the Awards and Administrative Accounts, ensured the validity of outstanding checks, verified that replacement checks were not already issued, and issued replacement checks.
- MTBA established a policy whereby an annual documented review of all outstanding checks is performed. The policy states that checks deemed abandoned (outstanding for over three years) will be remitted to the State Treasurer.

**c. Overpayment of \$10,785 Made to Former Executive Director Recovered**

Our prior review of MTBA's administrative expenditures revealed that MTBA's Executive Director received an overpayment of \$10,785 for the fiscal year ended December 31, 2001. Specifically, although the Executive Director's contract indicated that he should have received \$77,603, our review of MTBA's financial statements and records indicated the Executive Director actually received \$88,388. MTBA indicated that this payment might have represented a "bonus" approved at a Board of Directors meeting; however, MTBA could not produce any board meeting minutes to support this claim or, in fact, any minutes of Board meetings held during fiscal years 2001 and 2002.



Our follow-up review revealed that MTBA implemented our recommendation that it seek repayment from the former Executive Director. Specifically, in May 2005 the Executive Director repaid the full \$10,785 by check, which was subsequently deposited into MTBA's Administrative Account. Additionally, we found that MTBA now maintains detailed minutes of all business conducted at its Board of Directors meetings.

**2. PENALTIES AND INTEREST TOTALING APPROXIMATELY \$73,000 OWED TO THE INTERNAL REVENUE SERVICE FOR LATE FILINGS OF TAX FORMS**

During our audit, MTBA disclosed that it currently owes the Internal Revenue Service (IRS) approximately \$73,000 in interest and penalties for failing to file tax returns in a timely manner. Specifically, during tax years 1996, 2001, and 2004, MTBA did not file Form 990 within the timeframe required by the IRS. Form 990 is a return filed for organizations exempt from income tax that, in MTBA's case, is required to be filed annually by May 15. MTBA also did not file Form 1099 for tax years 2000 and 2001 in a timely manner. MTBA annually files Form 1099 for any non-employee compensations or for horsemen who earned prize money in excess of \$600 during the tax year. Form 1099 is required to be filed each year by February 28.

MTBA's private accountant informed us that IRS officials indicated that the tax forms were filed late, and that the previous administrators of MTBA did not respond to correspondence from the IRS. He also stated, "since learning of the issue, we have stayed in constant contact with the IRS and are trying to work toward a resolution that is favorable to the members of the organization." If the issue is settled favorably, these penalty and interest payments will be paid from MTBA's Administrative Account.

***Recommendation***

MTBA should continue to work with the IRS to resolve this issue and ensure that in the future, all required paperwork is filed in a timely manner.

***Auditee's Response***

The MTBA's Treasurer responded as follows:

*We have received favorable correspondence from the IRS regarding the penalty and interest assessments for the 2004 Form 990, which has been completely abated.*