

TEXAS DEPARTMENT OF LICENSING AND REGULATION
Austin, Texas

INTERNAL AUDIT REPORT

on

Combative Sports

Fiscal Year 2017



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Garza/Gonzalez & Associates

CERTIFIED PUBLIC ACCOUNTANTS

Commissioners and Audit Committee Members
Texas Department of Licensing and Regulation
Austin, Texas

We performed tests of management's assertion about the effectiveness and efficiency of the internal control structure over the Combative Sports Program of the Texas Department of Licensing and Regulation (TDLR); and, its established policies and procedures for the purpose of determining TDLR's compliance with applicable laws and regulations provided in the Texas Occupations Code (TOC) and Texas Administrative Code (TAC), for the 8 months ended April 30, 2017.

The results of our tests disclosed that TDLR's internal control structure over the Combative Sports Program and its established policies and procedures, were generally adequate and no material instances of noncompliance were noted; however, we did identify certain matters, included in this report, that are opportunities for strengthening internal controls and ensuring compliance with state requirements and TDLR's established policies and procedures. Based on the degree of risk or effect of these matters in relation to the audit objective(s), these matters were rated as either Priority, High, Medium, or Low, which is further described in the "Summary and Related Rating of Observations/Findings and Recommendations," included in page 11 of this report.

We have discussed the comments and recommendations with various TDLR personnel; and, will be pleased to discuss them in further detail; to perform an additional study of these matters; or, to assist you in implementing the recommendations.



September 28, 2017

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INTRODUCTION

In 1989, the Legislature established The Texas Department of Licensing and Regulation (TDLR), with the purpose of licensing and regulating businesses, industries, individuals, and occupations. TDLR accomplishes its purpose by developing clear and simple standards, providing guidance, ensuring compliance, and limiting the regulatory burden on individuals and businesses.

TDLR's responsibilities include regulating 32 diverse programs with 173 different license types and the oversight of more than 727,000 licensees.

Texas Occupations Code (TOC) Chapter 51 establishes TDLR and its responsibilities; and, Title 16, Part 4, of the Texas Administrative Code provides the applicable rules and regulations for the administration of TDLR and its programs.

The Texas Commission of Licensing and Regulation (Commission) is the governing board and policy-making body of TDLR. The 7 public members of the Commission are appointed to staggered 6-year terms by the Governor with the consent of the Senate. The role of the Commission is to:

- select and supervise the executive director;
- set policy for the agency;
- approve TDLR's strategic plan, operating budget, and requests for funding;
- set fees to cover program costs;
- adopt and repeal rules; and,
- impose fines and sanctions for violations of laws, rules, and orders.

In addition to the Commission, there are 26 Advisory Boards that serve the programs regulated by TDLR. Advisory board members provide technical knowledge and industry expertise, giving the Commission real-world insight into the occupations regulated by TDLR. Commission members serve as liaisons between the Commission and each Advisory Board to gain a better understanding of these industries. These Boards meet as necessary to study, review, and make recommendations to the Commission on:

- rules and technical standards;
- examination development;
- continuing education requirements; and,
- other trends affecting their regulated industries.

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2017 Internal Audit Plan

Following are the internal audits and other functions to be performed, as identified in TDLR's approved 2017 Internal Audit Plan, dated April 6, 2017.

- Combative Sports
- Performance Measures Reporting
- Other Programs (Polygraph Examiners; Temporary Common Worker Employers; Vehicle Protection Product Warrantors; and, Weather Modification) ¹
- Follow-up on Prior Year Internal Audits
- Other Tasks

This report contains the results of the Combative Sports Program audit. The reports for the remaining internal audits and other functions to be performed will be issued upon completion.

¹ Subsequent to the approval of the 2017 Internal Audit Plan, the 85th Legislature passed Senate Bill (SB) 2065, which the governor signed into law on June 15, 2017. Article 1 of SB 2065 deregulates the Vehicle Protection Product Warrantors Program and, Article 7 deregulates the Temporary Common Worker Employers Program. As such, effective September 1, 2017, TDLR no longer regulates either of these industries. Upon consultation with TDLR's Audit Committee Chair, it was decided that only the 2 programs (Polygraph Examiners and Weather Modification) that continue to be regulated by TDLR will be audited as "Other Programs."

INTERNAL AUDIT OBJECTIVES

In accordance with the **International Standards for the Professional Practice of Internal Auditing**, the audit scope encompassed the examination and evaluation of the adequacy and effectiveness of TDLR's system of internal control and the quality of performance in carrying out assigned responsibilities. The audit scope included the following objectives:

- **Reliability and Integrity of Financial and Operational Information** – Review the reliability and integrity of financial and operating information and the means used to identify, measure, classify, and report such information.
- **Compliance with Policies, Procedures, Laws, Regulations, and Contracts** – Review the systems established to ensure compliance with those policies, procedures, laws, regulations, and contracts which could have a significant impact on operations and reports, and determine whether the organization is in compliance.
- **Safeguarding of Assets** – Review the means of safeguarding assets and, as appropriate, verify the existence of such assets.
- **Effectiveness and Efficiency of Operations and Programs** – Appraise the effectiveness and efficiency with which resources are employed.
- **Achievement of the Organization's Strategic Objectives** – Review operations or programs to ascertain whether results are consistent with established objectives and goals and whether the operations or programs are being carried out as planned.

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EXECUTIVE SUMMARY

BACKGROUND

The Texas Department of Licensing and Regulation (TDLR) is responsible for licensing and regulating the Combative Sports Program (Program). In 2016, the 84th Legislature passed HB 3315, which changed the name of the Medical Advisory Committee appointed by the Commissioners, to the Combative Sports Advisory Board (AB). In accordance with HB 3315, the Commission approved the appointment of the AB to advise TDLR concerning health issues relating to combative sports events and contestants. A combative sport is defined as a full contact competition between contestants; which, includes boxing, kickboxing, martial arts, and mixed martial arts, where participants score points, and cause an opponent to submit, or disable an opponent in a contest match, or exhibition.

The Program is comprised of the following license types: (1) Contestant; (2) Judge; (3) Manager; (4) Matchmaker; (5) Promoter; (6) Referee; (7) Second; (8) Amateur Combative Sports Association; and, (9) Event Coordinator. The following table lists the number of active Program licensees, by type, as of April 30, 2017 along with the respective fees:

License Type	Number Licensed	Application & Renewal Fee
1. Contestant	726	\$20
2. Judge	58	\$100
3. Manager	32	\$100
4. Matchmaker	10	\$100
5. Promoter	44	\$900
6. Referee	54	\$125
7. Second	2,027	\$20
8. Amateur Combative Sports Association	15	\$50
9. Event Coordinator	6	\$200

Organizational Structure

TDLR's Mechanical and Business Section (Compliance Section) of the Compliance Division provides oversight of the Program's operations. The Combative Sports Program is overseen by a Regulatory Programs Manager and is comprised of a Program Manager and 6.5 Program Specialists.

TDLR's Business and Occupations Section (Licensing Section) of the Licensing Division is responsible for processing applications and issuing licenses for the Program. The Section is supervised by a Licensing Manager, who reports to the Licensing Director, and is comprised of 3 Licensing Specialists.

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Licensing Division

New Applications:

Applicants for Program licenses are required to complete an application and additional documents, which are available on the TDLR website, and mail them to TDLR along with the required fees. Applications for all TDLR programs are received in the mailroom where they are date stamped, separated by program, and combined into batches by the mailroom staff. The batches are then sent to the Financial Services Division where the fees are processed and recorded in the Tulip system; then, to the Compliance Section, where the Program Specialist will perform the initial review; and, finally, to the Licensing Section for final processing.

A Licensing Specialist from the Licensing Section will ensure the applicant is not already registered in the Tulip system and will begin processing the application. If an application is incomplete and/or the required fee is not submitted, the Licensing Specialist will prompt the Tulip system to generate a Request for Information letter that is mailed to the applicant.

A criminal background check is then conducted through the Texas Department of Public Safety by the Licensing Support and Analytics team within the Licensing Division. The Licensing Support and Analytics team enters an event code in the Tulip system, as applicable, upon the applicant successfully passing the criminal background check and a license is automatically printed from the Tulip system and mailed to the applicant. The license includes the applicant's unique license number and is valid for one year from the date of licensure.

Renewal Applications:

Renewal applications are automatically generated from the Tulip system 65 days prior to the expiration of the license and mailed to the licensee. The licensee is required to complete the renewal application and mail it back with the appropriate fee and any additional documents, if necessary, by the expiration date. If not renewed by the expiration date, licensees have 36 months from the expiration date to renew before having to re-apply for a new license. There are no late fees assessed with the Program renewals; they are processed in the same manner as new applications.

As of April 30, 2017, the Licensing Division processed 1,503 new applications and 275 renewals; and, collected \$105,430 in licensing fees.

Compliance Division (Division)

Scheduling of Events:

Proposed Program event dates are emailed from licensed promoters or amateur associations to the Program Manager, who will approve the event only after review and approval of the contestants' fight records and weight classes. Upon approval by the Program Manager, the event is assigned an event number, and added to TDLR's calendar.

A monthly schedule, which is prepared by the Program Manager and approved by the Regulatory Programs Manager, reflects scheduled events and the assigned program specialists and inspectors.

Program specialists are responsible for the following:

- Contacting the promoter or amateur association and explaining the procedures and deadlines for the event;
- Verifying contestants' license status in Tulip; and,

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- Completing the Event Sheet, which documents event information such as the event date, number, location, and participant's license numbers and expiration dates, etc. Event Sheets are maintained in the respective event folder in the Division's network drive.

An unlicensed contestant may participate in an event if they meet all licensing requirements within 72 hours of the respective event for professional events and within 48 hours for amateur events.

Weigh-Ins:

Weigh-ins take place for all types of events and are scheduled at a time and place approved by the Program Specialist, between the hours of 2:00 p.m. the day before the event and 9:30 a.m. the day of the event. A Contestant Information Sheet is completed by the contestant at the weigh-in, which includes information about their second (trainer). If the second is not licensed, they will be asked to apply for a license and pay the required fee, at the time of weigh-in. Once paperwork is completed, the contestant is administered a pre-fight physical and is weighed in by a physician. A Contestant Consent Authorizing Drug Testing & Release of Results Form is signed by the contestant and the inspector, also at the weigh-in.

Drug Testing:

Contestants participating in *professional* events are subject to random drug tests, which are administered on the day of the event. The Program Specialist will provide a list of contestants for their assigned event along with the contestant's D.O.B., to another Program Specialist within the Compliance Section who will generate a random selection of 6 contestants for drug testing. The names of the randomly selected contestants are provided to TDLR's drug testing vendor and the promoter, at least 10 days prior to the event. Contestants are notified by letter via mail and email only when drug test results are positive, and all results, whether positive or negative, are provided to the Compliance Section to be filed in the respective event folder. When drug test results are positive or if the contestant refuses to take a drug test, a complaint is submitted to the Enforcement Division, and the contestant is placed on an automatic 90-day suspension. If a contestant whose drug test results were positive or who refused to take a drug test, won the fight, the results will be changed from "Win" to "No Decision".

Inspections:

Inspections are performed on the day of the event by 2 TDLR employees and 4 to 7 contracted inspectors, depending on the size of the event. On the day of the event, the Program Specialist assigns each employee and inspector to a station (dressing rooms, corners, etc.). Inspectors are contracted by TDLR for a one year period.

Permit Fee:

In accordance with Texas Administrative Code 16.80, for events that charge for admission, a permit fee of \$100 is required to be paid by the Promoter per live professional event and simultaneous telecast of a live contest on a closed circuit telecast. The Promoter is required to complete a Permit Fee Form that is returned to TDLR along with the permit fee of \$100 prior to the event date.

Following an Event:

All license applications and fees collected by the Program Specialist on the day of the event are submitted to the Licensing Division for processing. Fight results are documented in the Event Sheet by the Program Specialist, submitted to the National Registries, and uploaded to the TDLR website for public viewing. The Program Specialist will then complete and organize all information related to the event and event participants in an event folder, which is located in the Division's network drive.

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Promoter Tax Reports:

In accordance with Section 2052.151 of the Texas Occupations Code, promoters of combative sports events that charge an admission fee are assessed a 3% tax of gross ticket sales receipts, plus an additional 3% tax of gross sales of broadcast rights; or, \$30,000, whichever is less. Within 3 business days after the event date, the promoter is required to complete the Promoter Tax Report, which documents the number of tickets sold, the price per ticket, the amount collected for broadcast rights, the proceeds subject to tax, and the amount of tax owed. If the Promoter Tax Report is not completed on the day of the event, it is mailed to TDLR along with a check for the amount of tax owed. Paid taxes are provided to the Financial Services Division for processing and then forwarded to the Compliance Section for review.

During the period from September 1, 2016 through April 30, 2017, TDLR collected \$495,987 in promoter tax revenue.

Event Ticket Audit:

Event ticket audits are performed by the Compliance Section after every event to ensure that the proper amount of tax was received based on the number of tickets sold. The promoter must provide:

- Ticket manifest (if tickets are sold online or by phone); or
- Copy of the invoice of the physical tickets ordered;
- Deadwood (unsold tickets); and,
- Promoter Tax Report.

During the period from September 1, 2016 through April 30, 2017 event ticket audits were performed for the 87 combative sports events held across the state during this same period.

Commissioner/Guest Combative Sports Program Attendance Report (Report):

TDLR is required, by the Legislative Budget Board (LBB), to submit (to LBB) a report of any TDLR employee and/or guest of TDLR who attends an event with complimentary or reduced rate tickets provided by the Promoter. The Program Manager from the Compliance Section prepares a quarterly internal report that documents the number of tickets requested from TDLR employees and its Commissioners, which is provided to the Budget Analyst to complete the LBB formatted Report. The Budget Analyst also makes inquiries of the Press Officer, who attends the majority of the fights, of any TDLR guests that attended events during the quarter, which is also used to complete the LBB formatted Report. The LBB formatted Report is submitted to the LBB via email within a month following the end of each quarter.

AUDIT OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

The objective of our audit was to gain an understanding of the processes and controls in place over the Combative Sports Program and TDLR's established policies and procedures, to determine whether they provide reasonable assurance for compliance with applicable state laws and regulations.

Scope

The scope of our audit was to review TDLR's established policies and procedures and the processes and controls over the combative sports events that occurred during the 8-month period from September 1, 2016 through April 30, 2017 to ensure compliance with applicable state laws and regulations.

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Methodology

The audit methodology included a review of applicable laws and regulations; TDLR's established policies and procedures, and other internal and external documentation; and, an interview with selected TDLR personnel.

We obtained and/or reviewed the following information:

1. TDLR's organizational chart.
2. TDLR's Combative Sports Procedures Manual.
3. Listing of combative sports new and renewal applications for the period from September 1, 2016 to April 30, 2017.
4. A listing of all combative sports events held during the period from September 1, 2016 to April 30, 2017.
5. Financial reports summarizing revenues received from combative sports events.
6. Minutes from Combative Sports Advisory Board meetings held during the audited period.
7. For 30 applications (20 new applications and 10 renewals):
 - 1) Submitted application;
 - 2) Surety bonds;
 - 3) Blood results;
 - 4) Ophthalmologic examination;
 - 5) Insurance;
 - 6) Rules of the Association; and
 - 7) Proof of non-profit organization status.
8. For 10 combative sports events, the proposed event date requests.
9. Commissioner/Guest Combative Sports Program Attendance Reports for the first 3 quarters of fiscal year 2017.

We performed various procedures to achieve the objective of this audit; to include, the following:

1. Reviewed and obtained an understanding of the applicable sections of the Texas Occupations Code (TOC), the TAC, and TDLR's policies, procedures, and practices in place related to the Combative Sports Program.
2. Conducted interviews with the Combative Sports Program Manager and the Licensing Manager to document formal and/or informal processes and controls in place related to the processing of licenses.
3. Obtained a listing of new and renewal applications received from September 1, 2016 to April 30, 2017, and selected a sample of 20 new and 10 renewal applications to test for the following attributes, to ensure the applicant was licensed in accordance with the TOC, TAC, and TDLR's policies:
 - a. Applicant completed required forms.

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- b. Applicant paid the applicable fee, as required per 16 TAC §61.80.
 - c. Contestants provided proof of a passing a comprehensive medical exam within the last 6 months of filing an application.
 - d. Contestants and judges provided proof of passing an ophthalmologic medical exam within the last 6 months of filing an application.
 - e. Promoters and amateur associations provided proof of surety bonds.
 - f. Amateur associations provided proof of insurance, rules of the association, and proof of non-profit status.
4. Obtained a listing of events conducted from September 1, 2016 to April 30, 2017 and selected 3 Event Promoter Tax Reports and 2 Permit Fee Forms to test the following attributes:
 - a. Promoters were assessed the promoter tax for events where an admission fee was collected.
 - b. The promoter tax was computed in accordance with Section 2052.151 of the TOC.
 - c. Information and calculations reflected in the Event Promoter Tax Report were complete and accurate.
 - d. The Permit Fee Form was complete.
 - e. Agreed the tax owed amount per the Promoter Tax Report to the Combative Sports revenue report.
5. Obtained a listing of events held from September 1, 2016 to April 30, 2017 and selected 10 events to ensure prior approval by the Program Manager.
6. Obtained 2 event sheets from September 1, 2016 to April 30, 2017 and selected 10 participants (contestants, judges, referees, promoters, etc.) to test the following attributes:
 - a. Participants were licensed on the day of the event.
 - b. Contestants selected for drug testing completed the Consent Authorizing Drug Testing & Release of Results form.
7. Obtained internal attendance quarterly reports prepared by the Program Manager and ensured the data was accurately reflected in the quarterly Reports submitted to the LBB and that the Reports were timely submitted.

OBSERVATIONS/FINDINGS AND RECOMMENDATIONS

Summary and Related Rating of Observations/Findings and Recommendations

As TDLR’s internal auditors, we used our professional judgment in rating the audit findings identified in this report. The rating system used was developed by the Texas State Auditor’s Office and is based on the degree of risk or effect of the findings in relation to the audit objective(s). The table below presents a summary of the findings in this report and the related rating.

Summary of Observations/Findings & Recommendations and Related Ratings		
Finding No.	Title	Rating
1	Event Ticket Audit	Medium
2	Promoter Tax Reports	Medium
3	Inspections	Low
4	Administration of Drug Tests	Low
Observation No.		
1	Submission of Applications and Fees	Low
	<p style="text-align: center;"><u>Description of Rating</u></p> <p>A finding is rated <i>Priority</i> if the issues identified present risks or effects that if not addressed could critically affect the audited entity’s ability to effectively administer the program(s)/function(s) audited. Immediate action is required to address the noted concern and reduce risks to the audited entity.</p> <p>A finding is rated <i>High</i> if the issues identified present risks or effects that if not addressed could substantially affect the audited entity’s ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern and reduce risks to the audited entity.</p> <p>A finding is rated <i>Medium</i> if the issues identified present risks or effects that if not addressed could moderately affect the audited entity’s ability to effectively administer program(s)/function(s) audited. Action is needed to address the noted concern and reduce risks to a more desirable level.</p> <p>A finding is rated <i>Low</i> if the audit identified strengths that support the audited entity’s ability to administer the program(s)/functions(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity’s ability to effectively administer the program(s)/function(s) audited.</p> <p>Note: Observations are always rated <i>Low</i>.</p>	

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Report No.	Report Date	Name of Report	Observations/ Findings and Recommendations	Current Status (Fully Implemented, Substantially Implemented, Incomplete/Ongoing, or Not Implemented) with brief description if not yet implemented	Fiscal Impact/Other Impact
1	9/28/2017	Combative Sports	<p>a. In one instance, the Report for an event that occurred on November 19, 2016 was incorrectly prepared by the promoter, which was later discovered through the event ticket audit performed by TDLR. The event ticket audit indicated that the number of tickets sold, as reflected in the Report, was understated by 6 tickets. Thus, in this instance, since the cost per ticket was \$75, there was a total of \$450 of unreported gross sales, which computes to an additional \$13.50 in the 3% tax owed. Furthermore, documentation was not available to determine if the promoter paid the additional tax owed.</p> <p>b. In this same instance, the Report was received by TDLR on November 28, 2016, which is a longer period than the required 3 business days from the day of the event.</p> <p>Recommendation We recommend that TDLR implement a tracking system that will improve the monitoring of Reports to ensure they are received in a timely manner; and, to monitor the status of issues identified in event ticket audits performed to ensure they are addressed in a timely manner.</p> <p>Management's Response The agency agrees with the recommendation. Agency staff will ensure that all reports and associated submissions are done in compliance with agency policies and procedures. Event folders will not be closed until all documents have been received and accuracy requirements are met.</p> <p>3. Inspections</p> <p>TDLR contracts with inspectors to be present at each combative sports event to supervise and inspect designated areas of the event and ensure illegal violations do not occur. During the hiring process, inspectors are required to watch all 11 online training videos that are available on the TDLR website; and, complete and pass a 20 question quiz to demonstrate their understanding of inspector responsibilities. However, during an event, the inspectors are not required to complete any form of documentation; such as, a checklist, to denote adherence to TDLR's established inspector responsibilities.</p> <p>Recommendation We recommend that TDLR develop a tool; such as, a checklist, to provide inspectors with guidance and keep them aware of items they are required to inspect in their designated areas; and, which would also provide TDLR with documentation to indicate that the inspector performed the required functions of an inspector, as expected by TDLR.</p>		To formally document items reviewed during inspections

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1	9/28/2017	Combative Sports	<p>Management's Response The agency agrees with the recommendation and will create an inspector responsibilities checklist to provide additional guidance and assistance while performing inspection duties.</p> <p>4. Administration of Drug Tests</p> <p>Beginning August 4, 2016, the Program began making a random selection of 6 contestants from each <i>professional</i> event for the administration of a drug test. The names of the randomly selected contestants are provided to TDLR's drug testing vendor and the promoter, at least 10 days prior to the event. We requested the listing of the randomly selected contestants for 2 selected events; however, the listing could not be located for 1 event. Therefore, we were unable to verify if any of the contestants from this event were randomly selected; and, therefore properly administered a drug test.</p> <p>Recommendation We recommend that TDLR retain documentation to support compliance with Program requirements.</p> <p>Management's Response The agency agrees with the recommendation. The agency has incorporated the requirement to maintain the program drug testing requirements, verification that the random selection, consent, and chain of custody forms and ensure that they are in the event folder prior to closure.</p> <p style="text-align: center;">OBSERVATIONS</p> <p>1. Submission of Applications and Fees</p> <p>Contestants and Seconds who are not licensed by the scheduled weigh-in day, are able to provide license applications and required license fees to the Program Specialist on the day of the event The Program Specialist will then submit all applications and fees to the Licensing and Finance divisions, respectively, one business day following the event. However, the Licensing and Finance divisions are not provided with "pending" information prior to an event to ensure the information received after an event is complete and accurate.</p> <p>Recommendation We recommend that TDLR implement controls that will allow the Licensing and Finance divisions to ensure that information received after an event is complete and accurate.</p>		<p>To retain documentation to support compliance with program requirements.</p> <p>To ensure the submission of complete and accurate information after an event.</p>

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1	9/28/2017	Combative Sports	<p>Management's Response The agency will take the observation and recommendation under consideration. There are many variables as to who will ultimately be working an event as seconds (i.e. no-shows and replacements) and the agency does not know prior to an event when these changes in licensing needs will occur. All efforts are currently made, and will continue to be made, by the event supervisor to completely and accurately gather information needed to license the specified individuals.</p>		