

VIRGINIA STATE LOTTERY DEPARTMENT

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2012**

APA

**Auditor of
Public Accounts**

COMMONWEALTH OF VIRGINIA

AUDIT SUMMARY

Our audit of the Virginia State Lottery Department (Lottery) for the year ended June 30, 2012, found:

- the financial statements are presented fairly, in all material respects;
- internal control findings requiring management's attention; however, we do not consider them to be material weaknesses; and
- instances of noncompliance or other matters required to be reported under Government Auditing Standards.

We have audited the basic financial statements of the Virginia State Lottery Department (Lottery) as of and for the year ended June 30, 2012, and issued our report thereon, dated August 15, 2012. Our report is included in the Lottery's Annual Report that it anticipates releasing on or around October 2012.

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INTERNAL CONTROL FINDINGS AND RECOMMENDATIONS

Ensure Timely Risk Assessment Updates

Lottery has not updated the risk assessment for one of its five sensitive Information Technology (IT) systems since fiscal year 2009. Without current risk assessments for sensitive systems, Lottery cannot identify and implement effective security safeguards to protect data or develop adequate contingency plans. Additionally, the Commonwealth's Information Security Standard, SEC501-06, requires agencies to update risk assessments at least every three years, or earlier if the agency introduces major changes into its IT environment.

Updated risk assessments identify, analyze, and mitigate risks that may compromise Lottery's IT systems. While the undocumented system has no direct impact on the integrity of Lottery's games, the system processes personally identifiable information, such as social security numbers.

We recommend that Lottery dedicate the necessary resources to update the risk assessment. Lottery should also take this opportunity to update their business impact analysis and continuity of operations plan to ensure those documents reflect the results of the IT systems risk assessment.

Update IT Infrastructure Device

Lottery operates a legacy Information Technology (IT) infrastructure device that the vendor has not supported since December 2009. While several interconnected devices and controls protect Lottery's infrastructure, operating an unsupported device weakens Lottery's security posture and the concept of layered security.

Since our recommendation includes descriptions of security mechanisms, we have communicated the details of this weakness to Lottery's management in a separate document marked Freedom of Information Act Exempt under Section 2.2-3705.2 of the Code of Virginia.

We recognize that Lottery plans to upgrade this device in September 2012. Therefore, we recommend that Lottery follow through with this plan and continue to dedicate the necessary resources to achieve this due date.

Secure Data on Backup Media

Lottery does not secure data on backup media transferred to an off-site storage location. While the backup media does not contain any information that may compromise the integrity of any lottery games, the media does contain personal information protected under Section 2.2-3800-C (8) of the Code of Virginia. Further, The Commonwealth's security standard, SEC501-06 Section 6.2.2.8, also requires agencies to either encrypt sensitive data on backup media or implement mitigating controls to reduce the risk of data compromise.

We recommend that Lottery dedicate the necessary resources to either encrypt sensitive data while stored on backup media, or to establish mitigating controls, such as improving physical security of unencrypted data while in transit to and from off-site storage locations.



Commonwealth of Virginia

Auditor of Public Accounts

Walter J. Kucharski
Auditor of Public Accounts

P.O. Box 1295
Richmond, Virginia 23218

August 15, 2012

The Honorable Robert F. McDonnell
Governor of Virginia

The Honorable John M. O'Bannon, III
Chairman, Joint Legislative Audit
And Review Commission

Members
Virginia State Lottery Board

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS

We have audited the basic financial statements of the **Virginia State Lottery Department** (Lottery) as of and for the year ended June 30, 2012, and have issued our report thereon dated August 15, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

Management of the Lottery is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered Lottery's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Lottery's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Lottery's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting entitled "Ensure Timely Risk Assessment Updates," "Update IT Infrastructure Device," and

“Secure Data on Backup Media” which are described in the section titled “Internal Control Findings and Recommendations,” that we consider to be significant deficiencies in internal control over financial reporting. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Lottery’s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards. Instances of noncompliance and other matters, entitled “Ensure Timely Risk Assessment Updates,” “Update IT Infrastructure Device,” and “Secure Data on Backup Media” are described in the section titled “Internal Control Findings and Recommendations.”

Lottery’s response to the findings identified in our audit is included in the section titled “Agency Response.” We did not audit Lottery’s response and, accordingly, we express no opinion on it.

Report Distribution and Exit Conference

The “Independent Auditor’s Report on Internal Control over Financial Reporting and on Compliance and Other Matters” is intended solely for the information and use of the Governor and General Assembly of Virginia, Virginia State Lottery Board, and management, and is not intended to be and should not be used by anyone, other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

We discussed this report with management at an exit conference held on September 6, 2012.

AUDITOR OF PUBLIC ACCOUNTS

AG: alh

Robert F. McDonnell
Governor

September 14, 2012

Mr. Walter J. Kucharski
Auditor of Public Accounts
101 North 14th Street
Richmond, Virginia 23219

Paula I. Otto
Executive Director

Dear Mr. Kucharski:

Attached are the Virginia Lottery's responses to the Auditor of Public Accounts Internal Control Findings and Recommendations for inclusion in the auditor's report for the period ended June 30, 2012.

Ensure Timely Risk Assessment Updates

The Lottery remains committed to ensuring the security, integrity, and availability of our Information Systems, and to effectively safeguarding our data. As such, we recognized the tremendous value and insight several precursory activities could bring to the sole outstanding risk assessment, and made a conscious business decision to delay that assessment until those precursory activities could be completed. Now that those activities have been accomplished, the Lottery is positioned to update the final sensitive system risk assessment by December 31, 2012.

Update IT Infrastructure Device

The Lottery completed the scheduled upgrade to the referenced Information Technology infrastructure device on September 13, 2012.

Secure Data on Backup Media

The Lottery has made substantial improvements to the physical security of unencrypted data while in transit to and from the off-site storage location. These improvements better obscure the contents of the containers used for transport, as well as better protect the containers from unauthorized entry. These mitigating controls will effectively reduce the risk of data compromise while the Lottery explores encryption options during the coming year.

Please contact me if you have any questions.

Very truly yours,



Paula I. Otto

Helping Virginia's Public Schools

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VIRGINIA STATE LOTTERY DEPARTMENT

BOARD MEMBERS

As of June 30, 2012

Albert H. Poole
Chairman

Cynthia D. Lawrence

David H. Hallock, Jr.

Robert Howard

AGENCY OFFICIALS

Paula I. Otto
Executive Director