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## Introduction

The Saskatchewan Liquor and Gaming Authority (Liquor and Gaming) operates under *The Alcohol and Gaming Regulation Act*. The mandate of Liquor and Gaming is to support, develop, and regulate the Saskatchewan beverage liquor and gaming industries. The mandate also requires Liquor and Gaming to maximize public benefit through high quality services and products, encourage responsible consumption of beverage alcohol, and encourage responsible participation in gaming.

Liquor and Gaming operates retail liquor stores and video lottery terminals. It also owns and operates the slot machines at Saskatchewan Indian Gaming Authority's (SIGA) casinos. Liquor and Gaming supervises SIGA and SIGA's revenues and expenses are Liquor and Gaming revenues and expenses. SIGA's slot machine revenues and expenses are included in Liquor and Gaming's financial statements.

In 2001-02, Liquor and Gaming had revenues of \$645 million, expenses of \$327 million, and net income of \$318 million. At March 31, 2002, Liquor and Gaming held net assets of \$4 million. *Liquor and Gaming's Annual Report 2001-02* includes its financial statements.

In this chapter, we describe our understanding of the key risks that Liquor and Gaming faces, our audit conclusions, and findings.

## Key risks

To carry out our work, we must understand the key risks facing an agency. We think sharing our understanding with legislators and the public will help them better understand and assess the agency's performance.

Under *The Alcohol and Gaming Regulation Act* (Act), Liquor and Gaming regulates establishments selling liquor (e.g., taverns) and all gaming activities in the Province. Liquor and Gaming also operates retail liquor stores. To help assess Liquor and Gaming's performance, it is important for legislators and the public to understand Liquor and Gaming's vision, mission, and how it manages the key risks it faces.

Liquor and Gaming has documented its vision, mission, guiding principles, strategic direction, and objectives in its strategic plan. Its annual report includes some of this information. However, Liquor and Gaming does not make public its strategic plan and how it manages its key risks. We encourage Liquor and Gaming to provide its strategic plan and management of its key risks in its annual report.

In 1998, we identified the key risks that Liquor and Gaming faced and reported those risks in our 1998 Fall Report – Volume 2. During the year, we updated our understanding of the key risks that Liquor and Gaming faces. We reviewed relevant literature on the regulation of the liquor and gaming industry and various documents prepared by Liquor and Gaming. We discussed our understanding with management and confirmed that the key risks that Liquor and Gaming faces today are not different from the key risks we identified in 1998.

We assessed the adequacy of Liquor and Gaming's rules and procedures to regulate and monitor the operations of SIGA's casinos. We reported our findings and recommendations in our previous reports to the Assembly. Liquor and Gaming has not implemented all our previous recommendations. Accordingly, we continue to report that Liquor and Gaming needs to improve its supervision of SIGA's operations.

We have not assessed the adequacy of the processes that Liquor and Gaming uses to address its other key risks.

The following are the key risks that Liquor and Gaming must manage well to be successful. Liquor and Gaming must:

- ◆ develop and maintain fair, clear, and contemporary policies and operating agreements and ensure compliance with policies and operating agreements;
- ◆ ensure the integrity of the liquor and gaming industries;
- ◆ ensure a balance between equitable licensing and revenue opportunities for charities and businesses; and
- ◆ promote the responsible use of liquor and gaming products while optimizing revenue from those products.

The following briefly explains each of the above risks and sets out the systems and practices necessary to manage those risks.

## **Fair, clear, and contemporary policies and operating agreements**

Liquor and Gaming is responsible for regulating all casinos, establishments selling liquor and gaming activities of charitable organizations.

Liquor and Gaming must develop and maintain policies and operating agreements that are fair to all parties involved in the liquor and gaming industries. To be fair, those policies and operating agreements must be clear and contemporary. Effective operation of these industries requires that all parties comply with established policies and operating agreements.

Management told us Liquor and Gaming regularly reviews laws that affect policies relating to regulation and operation of liquor and gaming industries to ensure those laws are fair. When it considers necessary, management told us, Liquor and Gaming recommends to the Government changes to those laws. Also, management told us, to ensure operators understand the laws, Liquor and Gaming educates permittees, licencees, and stakeholder groups about compliance requirements and available assistance. Furthermore, Liquor and Gaming does inspections/audits and conducts investigations to ensure the liquor and gaming establishment operators comply with the laws, the terms of the permits/licences, and operating agreements.

## **Integrity of the liquor and gaming industries**

The continuous growth of the gaming industry is a concern for anti-gambling interest groups in the Province. The steady consumption of beverage alcohol in Saskatchewan also continues the pressure to promote responsible use of beverage alcohol. Liquor and Gaming, as regulator of the liquor and gaming industries, has a responsibility to maintain and ensure the integrity (legality, honesty, fairness, consistency, and transparency) of these industries.

Citizens expect their Government to ensure the integrity of the liquor and gaming industries. The introduction of various partners in the liquor and gaming industries makes it challenging for Liquor and Gaming to ensure the integrity of these industries.

To ensure the integrity of liquor and gaming operations in the Province, Liquor and Gaming, in consultation with the industries, must establish standards of integrity for those industries. Those standards must be fair and clear. Liquor and Gaming should also ensure that all those operating in the gaming and liquor industries comply with those standards.

Liquor and Gaming currently licenses both liquor and gaming activities in the Province. Those licenses stipulate conditions for liquor and gaming operations. Also, Liquor and Gaming requires that all gaming employees and gaming suppliers in the Province meet Liquor and Gaming's integrity standards. Liquor and Gaming conducts inspections/audits of liquor establishments to ensure the operators comply with conditions of their licenses. Management told us that Liquor and Gaming staff routinely observe gaming operations at various establishments.

### **Balancing equitable licensing and revenue opportunities for charities and businesses**

Liquor and Gaming is responsible for licensing, registering, monitoring, and enforcing compliance with the policies by all parties involved in the liquor and gaming industries. Those industries contribute toward general economic development and to charities. Many charities rely heavily on the income generated from gaming activities (e.g., bingos, raffles).

To assist charities, Liquor and Gaming must ensure the licensing of charities is effective, efficient, accountable and fair. Because of the recent expansion of the gaming industry, charities face challenges to protect and stabilize their revenue sources. Liquor and Gaming must balance equitable licensing for charities and businesses with fair opportunities to raise revenue.

Management told us Liquor and Gaming inquires about the financial needs of the charities before providing them licences for gaming activities. Also, Liquor and Gaming has processes to ensure the charities use income from gaming activities for charitable purposes only.

## **Responsible use of liquor and gaming products while optimizing revenues**

The recent growth in the liquor and gaming industries has provided the Government with increased revenues to maintain its current programs. This growth has also continued pressure on the Government to promote responsible use of liquor and gaming products.

The net income for the Government from liquor and gaming products amounted to \$318 million in 2001-2002. This is a significant amount of revenue to the Government. The Government faces a challenge to balance its need to optimize this source of revenue with the responsible use of these products.

To achieve this balance, the Government, through Liquor and Gaming and other health and welfare agencies, must gather information about the negative social impacts of liquor and gaming products. Liquor and Gaming can then establish, and co-ordinate with other health and welfare agencies, promotion of responsible use of these products. Liquor and Gaming together with other agencies should then explain to the public how they are reducing the negative social impact of liquor and gaming. Also, Liquor and Gaming must work with the liquor and gaming industries to ensure pricing and marketing policies meet its revenue expectations within the boundaries set for social responsibility.

Management told us Liquor and Gaming has policies to set prices for liquor products to meet revenue expectations within the boundaries set for social responsibility (e.g., set profits margins, no sale to minors or those who appear intoxicated). Management also told us that Liquor and Gaming has a process to manage and regulate its gaming operations within the limits set by the Government (i.e., maximum province wide 4,000 VLTs and 1,240 slot machines). Also, Liquor and Gaming sponsors, in partnership with hospitality, liquor and gaming operators, and other government agencies, the Designated Driver Program and the Fetal Alcohol Syndrome Program.

## Our audit conclusions and findings

In our opinion, for the year ended March 31, 2002:

- ♦ Liquor and Gaming's financial statements are reliable;
- ♦ Liquor and Gaming had adequate rules and procedures to safeguard and control its assets, except for the matters described in this chapter; and
- ♦ Liquor and Gaming complied with the authorities governing its activities relating to financial reporting, safeguarding assets, revenue raising, spending, borrowing, and investing, except for the matters described in this chapter.

### Proper management of public money under SIGA's control needed

Liquor and Gaming needs to continue to strengthen its rules and procedures to ensure proper management of public money under SIGA's control.

To implement the 1995 Framework Agreement<sup>1</sup> and because *The Criminal Code of Canada* gives only provinces the authority to conduct and manage electronic gaming devices, Liquor and Gaming and SIGA signed the Casino Operating Agreement<sup>1</sup>. The Casino Operating Agreement permits SIGA to manage slot machines at SIGA's four casinos.

Under the Casino Operating Agreement, the revenue and expenses from the slot machines belong to Liquor and Gaming. The Agreement also addresses the management of table games. SIGA has the right to deduct reasonable table games losses and ancillary operation losses from the slot machine net profits.

Also, under the Agreement, Liquor and Gaming has the right to determine what expenses SIGA can reasonably incur and deduct from slot machine revenues, to decide SIGA's operating policies, and to approve SIGA's

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<sup>1</sup> See Chapter 6B on page 139.



financial plans. These authorities are necessary because the expenses SIGA incurs to operate slot machines are Liquor and Gaming's expenses.

In our 2000 Fall Report – Volume 2, we make recommendations for Liquor and Gaming to strengthen its management of public money under SIGA's control. In our 2001 Fall Report – Volume 2, we say Liquor and Gaming needs to do more work to fully implement the recommendations we made in our previous reports.

Liquor and Gaming, and SIGA accepted all of our past recommendations. While Liquor and Gaming, and SIGA implemented some of our past recommendations, their progress towards implementing all our recommendations has slowed.

Liquor and Gaming, as the owner and operator of the slot machines in SIGA casinos, needs to ensure that all costs SIGA charges Liquor and Gaming to operate slot machines are for that purpose and are reasonable. Liquor and Gaming has not done enough to know this.

We describe below areas where Liquor and Gaming needs to do more work to ensure proper management of public money under SIGA's control.

### **SIGA's business and financial plan**

Liquor and Gaming approved SIGA's financial plan (budget) without receiving a complete business plan.

In our past reports, we said Liquor and Gaming must ensure SIGA prepares appropriate business and financial plans. SIGA did not prepare a business plan for 2001 or 2002. Management of SIGA could not do so because SIGA's Board of Directors has not prepared and communicated strategic directions for SIGA.

Liquor and Gaming received SIGA's budget for 2001 and 2002 and approved those budgets. However, without a business plan, Liquor and Gaming does not know what SIGA wants to achieve, how it will do that, and what resources SIGA needs to achieve its objectives. Also, because SIGA's Board has not prepared and communicated its long-term strategic

directions, Liquor and Gaming does not know whether SIGA's strategic direction is consistent with Liquor and Gaming's strategic direction.

**1. We continue to recommend that Liquor and Gaming ensures:**

- ◆ **SIGA's Board prepares and communicates its long-term strategic direction to management; and**
- ◆ **SIGA prepares and submits for approval a complete business and financial plan setting out performance targets**

**Policies and procedures**

In our past reports, we said that Liquor and Gaming must ensure that SIGA has adequate policies and procedures for managing public money. It has been now two years since we made this recommendation. However, Liquor and Gaming has not ensured that SIGA has appropriate policies and procedures in all areas<sup>2</sup>.

Annually, SIGA spends approximately \$28 million and \$8 million on employees' pay and benefits, and for marketing and promotion activities (including sponsorship) respectively. These are SIGA's two biggest expenses. In our past reports, we recommended that Liquor and Gaming ensure SIGA establishes adequate processes for controlling these expenses including rules and procedures for evaluating the results of SIGA's activities. Liquor and Gaming continues to approve SIGA's budgets without ensuring that SIGA has established such processes.

Also, Liquor and Gaming has not ensured that SIGA has established:

- ◆ accounting policies to ensure all transactions are properly supported and recorded; and
- ◆ adequate segregation of duties for its employees.

We had expected that Liquor and Gaming would have set out a plan to improve its supervisory practices over SIGA's spending. Such a plan would have included who would do what, and by when, to implement all of our recommendations. Liquor and Gaming does not have an adequate

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<sup>2</sup> See exhibit 1 in Chapter 6B on page 165.

plan to ensure timely implementation of all of our recommendations. As a result, most of our recommendations are still not implemented<sup>3</sup>. Accordingly, Liquor and Gaming's progress towards implementing our recommendations has slowed.

For example, we recommended Liquor and Gaming should do more frequent audits of SIGA's spending. We also expected Liquor and Gaming to report and follow up its audit findings with SIGA and recover unreasonable expenses, if any.

During the year, Liquor and Gaming did more work to audit SIGA's spending. Liquor and Gaming prepared written reports to communicate its audit findings to SIGA. However, Liquor and Gaming did not adequately follow up the matters reported to SIGA to ensure SIGA changed its spending practices. For example, Liquor and Gaming audited SIGA's payments for promotions and sponsorships and identified transactions that were questionable or not properly supported. Liquor and Gaming, however, did not adequately follow up its audit findings with SIGA to ensure SIGA changed its' spending practices.

Liquor and Gaming may have paid SIGA for expenses that are not reasonable for operating slot machines at SIGA casinos because of its slow progress in improving its supervising practices.

**2. We continue to recommend that Liquor and Gaming implement all our past recommendations listed in Exhibit 1.**

**Exhibit 1**

In our 2000 Fall Report – Volume 2, we recommended Liquor and Gaming:

3. Ensure SIGA implements the recommendations we make in our 2000 Fall Report – Volume 2, and ensure it has necessary resources to frequently audit SIGA;
4. Frequently audit SIGA's operations to ensure:
  - SIGA complies with the Framework and Casino Operating Agreements;
  - and
  - SIGA incurs and deducts only reasonable expenses from public money.

In our 1999 Spring Report, we recommended Liquor and Gaming:

5. Prepares a formal training plan for its employees and should co-ordinate work among its branches;

<sup>3</sup> See exhibit 1 in Chapter 6B on page 165.

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| <ol style="list-style-type: none"><li>6. Ensures inspections/audits are completed as planned or document why the plan was changed;</li><li>7. Documents procedures for reporting and following up its audit/inspection findings with SIGA;</li><li>8. Receive and formally approves SIGA's casino operating policies and procedures on a timely basis; and</li><li>9. Receive and approve SIGA's budget on a timely basis and should have procedures for approving changes to the budget.</li></ol> |
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## **Improper use of public money**

Liquor and Gaming authorized SIGA to pay \$400,000 to the Federation of Saskatchewan Indian Nations (FSIN) and \$150,000 to Saskatchewan Indian Gaming Licensing (SIGL). The 1995 Casino Operating Agreement does not allow SIGA to make these payments.

The Government of Saskatchewan and the FSIN signed a new Framework Agreement on June 11, 2002. The FSIN negotiated on behalf of its member First Nations, and Liquor and Gaming negotiated the new agreement on behalf of the Government. SIGA is not a direct party to this agreement.

SIGA, with the approval of Liquor and Gaming, paid the FSIN \$400,000 to cover the FSIN negotiation costs for a new agreement. The 1995 Casino Operating Agreement restricts SIGA's activities to operate casinos. The Agreement allows SIGA to incur and deduct only costs of operating the casinos. Payment to the FSIN is not a necessary cost to operate casinos.

As stated earlier, the revenues and expenses of SIGA are the revenues and expenses of Liquor and Gaming. Accordingly, the payment to FSIN resulted in the Government paying costs for both Liquor and Gaming's negotiation team and the team that negotiated for the FSIN.

Also, Liquor and Gaming authorized SIGA to pay SIGL \$150,000. Under the 1995 Framework Agreement, the Government agreed to authorize SIGL to issue licenses to charitable and religious organizations located on reserves to conduct charitable gaming on reserves. The Government, however, has not yet authorized SIGL to issue any licenses. Management told us, that the Government has not done so because SIGL is still learning how to regulate and monitor gaming on reserves. The payment to SIGL is not a necessary cost to operate casinos.

10. **We recommend that Liquor and Gaming authorize SIGA to spend money on expenses only necessary to operate casinos.**

## **Timely calculation and payment of Goods and Services Tax needed**

Liquor and Gaming needs to ensure that it calculates and pays Goods and Services Tax (GST) for its slot machine operations on a timely basis.

As stated earlier, Liquor and Gaming owns all the slot machines in SIGA's casinos and all VLTs. Liquor and Gaming is a lottery corporation under section 188 of the *Excise Tax Act* (Canada). The law requires lottery corporations to calculate and pay GST according to a set formula, instead of calculating and paying GST on slot machine and VLT revenues. The formula requires Liquor and Gaming to pay 14% on the purchase of taxable goods and services related to slot machine operations and 7% on VLT site contractor commissions.

Although Liquor and Gaming regularly calculated and paid GST on VLT site contractors' commissions, it did not calculate and pay GST on taxable purchases for slot machine operations for the last two years. For the annual financial statements, Liquor and Gaming estimated it owed \$3.6 million for outstanding GST relating to slot machines.

11. **We recommend that Liquor and Gaming establish rules and procedures to ensure timely calculation and payment of GST on its slot machine operations.**

Management told us, Liquor and Gaming has now paid the outstanding GST relating to slot machines.

## **Better monitoring of gaming operators needed**

Liquor and Gaming needs to ensure that all gaming establishments (gaming operators) use only registered gaming suppliers.

*The Alcohol and Gaming Regulation Act* (Act) requires Liquor and Gaming to license all gaming operators in the Province. Liquor and Gaming issues licences to gaming operators. The terms and conditions of

those licences require the operators to ensure all their employees and those who provide gaming services hold a certificate of registration (licence) from Liquor and Gaming. Liquor and Gaming also licenses employees who work in gaming establishments and suppliers of gaming services.

As a regulator, Liquor and Gaming, must ensure all gaming operators comply with the law. Liquor and Gaming requires its inspectors to seek lists of gaming suppliers that gaming operators use. Inspectors are then required to ensure those gaming suppliers are licensed. However, Liquor and Gaming also needs to ensure that the lists of gaming suppliers its' inspectors receive from gaming operators is complete and accurate. Without this information Liquor and Gaming does not know if all gaming operators complied with the Act.

- 12. We recommend that Liquor and Gaming strengthen its rules and procedures to ensure gaming operators use only registered gaming suppliers.**

## **Electronic gaming devices need proper testing**

Liquor and Gaming must establish standards for testing electronic gaming devices (slot machines and video lottery terminals) before making them available for public use.

The laws set out minimum payout percentages for electronic gaming devices. To ensure those devices pay out in accordance with the law, regulators require gaming operators to have the devices tested by an independent gaming laboratory. In addition, independent testing of those devices provides assurance about the technical integrity of the software, e.g., random number generation. Liquor and Gaming, as a gaming regulator, requires gaming operators to have the electronic gaming devices tested by an independent gaming laboratory before authorizing those devices for public use. As the owner of the slot machines at SIGA's casinos and all VLTs in the Province, Liquor and Gaming asks an independent gaming laboratory to test those devices before making them available to the public.

Because Liquor and Gaming has not established standards for the testing of electronic gaming devices, the independent gaming laboratory uses

standards established by other regulators. Gaming rules in Saskatchewan are different from other jurisdictions. When independent laboratories use other regulators' standards to test the devices for use in Saskatchewan, there is risk that those devices may not comply with gaming rules in Saskatchewan.

Also, Liquor and Gaming does not have a formal agreement with the testing laboratory setting out what it should test and what assurance it needs to provide to Liquor and Gaming. When expectations are not clearly documented and communicated there is risk of confusion between parties resulting in malfunctioning electronic gaming devices for public use. Malfunctioning gaming devices could result in the loss of public confidence and loss of revenues.

**13. We recommend that Liquor and Gaming:**

- ◆ **establish standards for independent testing laboratories to use when testing slot machines and VLTs; and**
- ◆ **ensure that the laboratories use those standards to test Liquor and Gaming's slot machines and VLTs.**

Management told us Liquor and Gaming has begun to develop standards for testing slot machines and VLTs.

## **Better monitoring of table games needed**

Liquor and Gaming needs better rules and procedures to monitor table games at casinos.

Liquor and Gaming approves the rules of all table games played in Saskatchewan casinos. Table game rules include a planned house advantage. The planned house advantage is the percentage of the player's bet that the casino should retain over time if the game is played according to the approved rules.

Liquor and Gaming does not have rules and procedures to regularly monitor gaming operators' house advantage for table games. Management told us that if gaming operators play the table games according to the approved rules, they would achieve the approved house

advantage. Management also told us that Liquor and Gaming is satisfied that table games in the casinos are played according to the approved rules because its staff observe live table games at casinos to ensure gaming staff comply with approved rules. However, Liquor and Gaming should also require gaming operators to calculate and monitor the actual house advantage for some table games. Such monitoring provides added assurance that all table games are played according to the approved rules.

Alternatively, Liquor and Gaming could establish a range of expected “hold” for approved table games. Expected “hold” represents the revenue from the table games that an operator can expect to achieve. Most gaming operators calculate and monitor the “hold” for table games. Liquor and Gaming could then monitor gaming operators’ actual “hold” for table games against the approved range for those table games. This will help ensure that the table games are played fairly and generate revenue according to expectations.

- 14. We recommend that Liquor and Gaming establish rules and procedures to periodically monitor the actual house advantage for table games.**

## **Complete contingency plan needed**

Liquor and Gaming needs to prepare a complete contingency plan for its computer systems and test the plan to ensure it works.

Liquor and Gaming is dependent upon its computer systems. To provide continuous services, Liquor and Gaming must ensure its systems and data are available when needed.

A contingency plan is an important part of an organization’s business interruption plans. Business interruption plans reduce the risks resulting from business disruptions due to unforeseen incidents including systems failure. Liquor and Gaming needs a written and tested contingency plan to ensure the recovery of systems and data in case Liquor and Gaming’s electronic systems fail, or if key service providers’ systems fail.



We reported this matter in our previous reports. The Standing Committee on Public Accounts (PAC) considered this matter in January 1999 and concurred with our recommendation.

Liquor and Gaming has established some procedures to recover data in case of systems failure. However, Liquor and Gaming does not yet have a complete and tested contingency plan. Once the plan is completed, the Board of Directors should approve it.

We continue to recommend that Liquor and Gaming complete a written contingency plan and tests that plan to ensure it works.

### **Written rules and procedures needed for computer systems operations**

Liquor and Gaming needs written rules and procedures for its computer systems operations including security so that the staff understand what they must do.

We reported this matter in our previous reports. PAC considered this matter in January 1999 and concurred with our recommendation.

Liquor and Gaming has drafted some rules and procedures for computer systems operations. However, Liquor and Gaming has not approved or implemented these rules and procedures.

We continue to recommend that Liquor and Gaming document its rules and procedures for its computer systems operations and ensure that staff understand those rules and procedures.

### **Annual report needs improvement**

Liquor and Gaming needs to further improve its annual report.

To assess the performance of a public sector agency, legislators and the public need to know how the agency is managing its key risks. They also need information about the agency's goals and objectives and how successful the agency has been in achieving those goals and objectives. Good annual reports provide this information. Annual reports should describe what the public agency is all about, how it manages its key risks,

what it has done, where it is now, and what it plans to do. In addition, the annual report should be timely, relevant, and understandable.

Liquor and Gaming's 2002 annual report provides limited information on its performance. Future reports should include a summary of its key performance indicators and targets compared to actual results. A discussion and analysis of Liquor and Gaming's plans and the actual results would help readers assess Liquor and Gaming's performance in achieving its goals. Liquor and Gaming's 2002 annual report provides little information about its future directions or the outlook for the liquor and gaming industries generally. Future reports should include a discussion of Liquor and Gaming's future directions. Such a discussion would help readers to understand how Liquor and Gaming intends to achieve its goals.

Future reports should also describe the key risks Liquor and Gaming faces and how it manages those risks. This information will help readers better understand and assess Liquor and Gaming's performance.

We also reported this matter in our previous reports.

- 15. We continue to recommend that Liquor and Gaming improve its annual report.**