

**COMPLIANCE PROCEDURES FOR COUNTIES, CITIES, AND VILLAGES
LICENSED TO CONDUCT A KENO LOTTERY**

Issue:

What compliance procedures should a county, city, or village follow to perform the required annual examination of its keno lottery?

Conclusion:

The Nebraska Department of Revenue (Department) has adopted [Nebraska County and City Lottery Regulation 35-616](#) to require the performance of annual compliance procedures of keno lotteries conducted by counties, cities, and villages. The attached “Annual Compliance Procedures” documents the minimum procedures to be performed annually for county, city, or village keno lottery activity.

Definitions:

Keno Manager. Keno manager means the shift manager, supervisor, or person in charge of the daily operation of a keno game.

Lottery Operator. Lottery operator means an individual or business with whom a county, city, or village contracts to run a keno game on its behalf.

Sales Outlet Location. Sales outlet location means a location other than the lottery operator where keno wagers are placed.

Sponsor. Sponsor means the county, city, or village conducting the lottery.

Sponsor’s Representative. The sponsor’s representative means personnel or contracted staff of the county, city, or village conducting the lottery.

Analysis:

The Department’s authority to require an annual examination of a county, city, or village keno lottery is found in [Neb. Rev. Stat. § 9-620\(7\) and \(13\)](#) of the Nebraska County and City Lottery Act (Act) which provide, respectively:

The department shall have the following powers, functions, and duties:

...

(7) To require periodic reports of lottery activity from licensed counties, cities, villages, manufacturer-distributors, and lottery operators and any other persons,

organizations, limited liability companies, or corporations as the department deems necessary to carry out the act;

...

(13) To adopt and promulgate such rules and regulations and prescribe all forms as are necessary to carry out the act; . . .

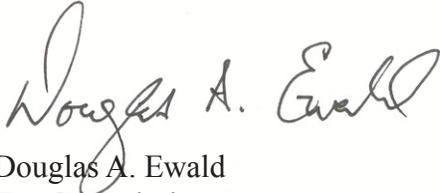
The procedures can be completed by a sponsor's representative, a contracted professional (e.g., certified public accountant), or a combination of the two. The lottery operator may not conduct the compliance procedures, nor can the lottery operator contract for the performance of the compliance procedures on behalf of the sponsor.

A sponsor conducting a keno lottery pursuant to the Act is required to perform annual compliance procedures of its keno activity. This Annual Compliance Procedures document is the basis for the keno compliance procedures referenced in this revenue ruling as published by the Department, and is intended to supplement [Regulation 35-616](#).

The compliance procedures in the revenue ruling are not limited to the performance of the procedures specified. The sponsor may require additional procedures to be performed. If additional procedures are performed (e.g., increased sample sizes, expanded testing, or additional visits to the keno site), the results must be included in the required report to the Department.

The sponsor's representative will be required to perform these minimum procedures on an annual basis to coincide with the fiscal year of the sponsor. A report outlining the findings of the procedures must be submitted by the sponsor or the sponsor's representative to the Department within 90 days of the end of the fiscal year of the sponsor.

APPROVED:



Douglas A. Ewald
Tax Commissioner

December 2, 2010

See attached [Annual Compliance Procedures of the Keno Activity of Counties, Cities, and Villages](#).

**ANNUAL COMPLIANCE PROCEDURES OF THE KENO ACTIVITY OF
COUNTIES, CITIES, AND VILLAGES**

The compliance requirements pertaining to the conduct of keno are derived from two sources:

- (1) The Nebraska County and City Lottery Act; and
- (2) The County and City Lottery Regulations.

Procedures may be conducted either by the sponsor’s representative or a contracted professional.

Compliance Requirements 1 and 2 must be performed during an unannounced visit while keno is being conducted for all sponsors who use a manual ball draw method for selection of the winning numbers.

1. **COMPLIANCE REQUIREMENT:** An unannounced observation of the keno activity must be made at least annually for all sponsors who use a manual ball draw method for selection of winning numbers during the conduct of a keno lottery. [Regulation 35-616.01](#).

PROCEDURE: For the purpose of this requirement, unannounced means that no individual involved directly or indirectly with the operation of the keno lottery will have knowledge of, or be given any advance information regarding the dates or times of, the observation. In addition to observing the operation of the keno activity, the steps outlined in Procedure 2 must be performed.

2. **COMPLIANCE REQUIREMENT:** [Regulations 35-613.03L, 35-613.04, 35-613.04A, 35-613.04B, 35-613.04B\(1\), 35-613.04B\(2\), 35-613.04B\(3\)](#), and Nebraska County and City Lottery Act, [Neb. Rev. Stat. § 9-607\(4\)](#).

PROCEDURE: During the unannounced visit, observe five keno games and verify that the keno operator (lottery operator or sales outlet location) has a minimum of three lottery workers involved during the drawing of the 20 keno numbers when a manual ball draw method of winning number selection is used, without exception. A keno lottery using an automated ball draw system may be conducted with less than three lottery workers as prescribed in Regulation 35-621.06B.

The sponsor’s representative should observe that:

- a. The number of the game being drawn is recorded on a blank keno draw ticket;
- b. One lottery worker calls the ball numbers as they enter the rabbit ears;
- c. A different lottery worker enters the numbers on the draw ticket on which the number of the game is recorded;
- d. The keno manager verifies the numbers drawn by comparing the rabbit ears to the draw ticket and to the numbers entered into the keno system prior to computing the game; and
- e. At the time of the unannounced visit, the lottery operator is using the method of winning number selection which agrees with the designated selection method on file with the sponsor and the Department.

Practical Guidance: Determine that the manual draw tickets are verified by the keno manager, as evidenced by the signature or initials of the manager, in addition to observing the conduct of the game. Determining the method of winning number selection may be accomplished at the unannounced visit or by reviewing the transaction log if the number selection method is designated on the log.

3. **COMPLIANCE REQUIREMENT:** [Regulation 35-621.06J](#)

PROCEDURE: Sponsors who use an automated ball draw method of winning number selection must verify that keno management personnel have performed a next-day review of all “no read”

and duplicate number occurrences. A written log of reviews must be maintained by the lottery operator or sales outlet location where the automated ball draw equipment is in use.

4. COMPLIANCE REQUIREMENT: [Regulations 35-613.04C\(1\) through 35-613.04C\(5\)](#) and [Regulations 35-621.06C\(1\) through 35-621.06C\(6\)](#).

PROCEDURE: View the video tape or digital recording for a minimum of five games for each month (from at least two different weeks within each month) to determine that the following items are in compliance with the regulations –

- a. The video tape or digital recording has a clear image to show (1) the empty rabbit ears or wheel, (2) the date and time, and (3) the full rabbit ears or wheel. The video tape or digital recording must also show the game number or the time and date which will relate to the game number.
- b. The winning numbers drawn per the video tape or digital recording agree with the draw ticket prepared by a lottery worker in the case of a manual ball draw, and the winning numbers are recorded on the transaction log. Verify that all discrepancies were reported to the Department, by the lottery operator, sales outlet location, or sponsor. Report all discrepancies not previously reported directly to the Department. Compare the time of the video tape or digital recording to the transaction log; also examine any procedures which would allow the lottery operator or sales outlet location the opportunity to affect the outcome of the keno game.
- c. The video tapes are retained and are not reused until the sponsor has performed the compliance procedures on the tapes and has released the tapes.

5. COMPLIANCE REQUIREMENT: [Regulation 35-616.01](#).

PROCEDURE: Verify the accuracy of monthly game summary information provided by the lottery operator, by reconciling the gross proceeds and prize payouts from the keno system's transaction log, to the monthly summary information.

Practical Guidance: The Department recommends that this procedure be conducted on a monthly basis. If the volume of transactions warrants it, the sponsor may submit a written request to Department detailing an alternative procedure they would like to use. The sponsor may not use the alternative procedure until written approval by the Department is received.

6. COMPLIANCE REQUIREMENT: [Regulation 35-622.03E](#) and Nebraska County and City Lottery Act, [Neb. Rev. Stat. § 9-650](#).

PROCEDURE: Determine that the gross proceeds of the keno lottery, less prizes paid in cash, are deposited into a separate bank account of the sponsor or lottery operator. On a monthly basis, reconcile the deposits per the daily cash summary and the transaction log to the keno operations bank account, to determine that the proper amount has been deposited within a commercially reasonable time frame and report any discrepancies.

Practical Guidance: If the volume of transactions warrants it, the sponsor may submit a written request to Department detailing an alternative procedure they prefer to use. The sponsor may not use the alternative procedure until written approval by the Department is received.

Determine that the amount of interest credited to the sponsor's share of the gross proceeds while in the custody of the lottery operator has been properly transferred to the sponsor. Any interest earned on the sponsor's share of the gross proceeds due to any time lag in remittance to the sponsor is the property of the sponsor, not the lottery operator.

7. COMPLIANCE REQUIREMENT: [Regulation 35-622.03D](#).

PROCEDURE: Examine any cash overage or shortage in excess of \$25 per keno writer, per shift, per day, and report unexplained and unresolved discrepancies and irregularities.

Practical Guidance: Report the lottery operator's and sponsor's actions with respect to the unexplained overage or shortage.

8. COMPLIANCE REQUIREMENT: [Regulation 35-614.05](#).

PROCEDURE: The computer-generated prize pay tables for all types of wagers must agree with the published prize pay tables. Verify that the lottery operator has a procedure to maintain a log of all updates and changes to the prize pay tables and that the active prize pay tables on the keno system agree with the published prize pay tables.

9. COMPLIANCE REQUIREMENT: [Regulations 35-613.11, 35-613.11A, and 35-613.11B](#).

PROCEDURE: Examine the financial security provided for prize payments to verify that the funds are guaranteed and in compliance with the regulations.

Practical Guidance: The funds must be insured or guaranteed by (1) funds deposited into an insured account maintained at a financial institution, (2) an Irrevocable Letter of Credit issued by a financial institution, or (3) another form of security approved by the Department.

10. COMPLIANCE REQUIREMENT: [Regulation 35-622](#).

PROCEDURE: Ensure that all lottery records are maintained as prescribed in Schedule 59 - County/City Lottery Records approved by the Records Management Division of the Nebraska Secretary of State's office and Regulation 35-622.

Practical Guidance: Records required to be maintained must be stored at a location other than the actual locations where the keno lottery is conducted.

11. COMPLIANCE REQUIREMENT: [Regulation 35-622.04](#).

PROCEDURE: The sponsor must file a [Nebraska County/City Lottery Report, Form 35K](#), for the annual period corresponding to the sponsor's fiscal year. The report must be filed with the Department within 90 days of the end of the sponsor's fiscal year.

Practical Guidance: Form 35K must be prepared using the same method of accounting used for the quarterly county/city lottery tax returns. Indicate whether the cash basis or accrual basis is used, or identify the specific method if another method is used.