CONFIDENTIAL

New York State Thoroughbred Breeding and Development Fund

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Executive Summary

Robert T. Williams, then-Executive Director of the New York State Gaming Commission ("Commission") and current Deputy Secretary for Gaming, expressed concerns about New York State Thoroughbred Breeding and Development Fund Corporation ("Fund") expenditures and requested a review be conducted to ensure that the Fund is operating properly and in the most efficient and effective manner. Similarly, Fund Chairman and Commission board member John J. Poklemba requested that a review of the Fund be undertaken to ensure the same.

A number of concerns were specifically cited regarding the Fund, such as its procurement practices and retention of particular vendors; promotional expenditures; subsidy of aftercare programs; approval and issuance of supplemental awards; appropriateness of credit card usage; and other potential conflict of interests matters.

Accordingly, this Office undertook a review of the Fund and analyzed Fund records, including, but not limited to, annual reports, board minutes, policies, financial records (budget proposals, financial summaries, invoices, cancelled checks, credit card statements), and vendor contracts including supporting documentation; third-party vendor records; Accurint, Guidestar, and Office of the New York State Comptroller reports; and conducted numerous interviews, including, but not limited to, the following individuals:

- Tracy Egan, Executive Director;

[redacted]

This review determined the following:

1) The Fund's Audit and Finance and Governance Committees, consist of less than three independent members and are not in compliance with Sections 2824(4) and (7) of the Public Authorities Law.

2) The Fund exercises great discretion in the distribution of its funds in furtherance of its mission, but does not have crucial policies to govern such activities, including policies addressing the use of discretionary funds for its scholarship and fellowship programs, sponsorships, meal expenditures, and travel.

3) Interested members failed to comply with New York State Ethics Commission Advisory Opinion No. 95-13 and did not recuse themselves from voting on the distribution of supplemental awards that yielded a direct financial benefit to themselves or family members. This conduct may also be construed to be a violation of Section 74 of the Public Officers Law.

4) Fund Executive Director Tracy Egan did not enter into an agreement with the Fund to voluntarily abstain from accepting breeders awards. In August of 2010, the New York State Commission on Public Integrity advised that Egan could continue with her activities as a breeder and as a real estate broker. Further, executive session notes retained by the [redacted] revealed that Egan did not wish to forego her awards or outside employment. Although Egan offered the possibility of donating her awards to a charity, there was no further indication this option was pursued by either Egan or the Fund.

5) There is no evidence that Egan violated any provision of the Public Officers Law while engaged in her breeding or real estate business.

6) There were no irregularities noted as it pertains to the use of the Fund's credit cards, including its Exxon, Sunoco, and Bank of America Visa accounts. However, the review noted that Egan's use of the credit card for food and drink raised questions of necessity and appropriateness. Specifically, it was determined that Egan used the Fund's credit card on 46 occasions for expenses ranging from $4 to $334. Three of these charges included the purchase of alcohol, several for incidentals such as a bottle of water or soda, as well as others for meals that did not include the requisite information or justification.

7) There are no policies pertaining to the Fund's scholarship and fellowship programs, nor is there a formal application process. Instead, the Fund relies completely upon the schools to select recipients for the programs. Further, the Fund does not require that the school maintain documentation of its selection process which greatly increases the potential for fraud and abuse within the programs. This review found three students who received scholarships twice, and contrary to Fund guidelines, one recipient was a first-year student.

8) Although the Fund is arguably in compliance with its stated mission and not openly involved in aftercare programs, its promotional activities and sponsorships of aftercare organizations is contrary to the opinion rendered by the Commission that the Fund's use

of its monies is strictly limited to those items specified by the legislature, in that, these expenses do not comport with the spirit of its mandate.

9) In 2009, before Egan's employment with the Fund, she met [redacted] when she sold [redacted] her current residence. Subsequently, in 2011, Egan hired [redacted] as a part-time administrative assistant, but [redacted]'s responsibilities gradually expanded to fill the void left by personnel changes/shortages within the Fund.

10) It was at the Fund's suggestion that [redacted] established her company, [redacted] and became a vendor to the Fund. [redacted] has been providing services to the Fund pursuant to a contract executed in 2012 and which continues in perpetuity. Throughout this period, [redacted] has never been declared a sole or single source provider, nor has an exemption, if applicable, to the procurement process been obtained. Further, although the company has been paid in excess of $25,000 for multiple years, the contract has never been subjected to the competitive bid process.

11) Although the Fund did not violate its prompt payment policies, it knowingly allowed [redacted] to delay invoicing for services rendered in third and fourth quarters of a year, until the following year to enable her to avoid earning the income that would result in a reduction to her social security benefits.

12) The New York Thoroughbred Breeders, Inc. ("NYTB") is recognized as the "statewide thoroughbred breeders organization representing the majority of breeders of registered thoroughbreds" in New York, which grants the NYTB a seat on the Fund's board pursuant to the Laws of New York, Chapter 282 of the Laws of 1994. Notwithstanding, this designation only provides for representation on the Fund's board, and there is no statutory mandate that the NYTB also be awarded a contract with the Fund.

13) The NYTB's contractual relationship with the Fund is more appropriately characterized as a sponsorship and not that of a vendor/vendee. The monies derived from the promotional contract is used to wholly subsidize the NYTB's activities. These activities serve to benefit the NYTB members and the thoroughbred industry and not just the Fund. The NYTB's contract with the Fund contain no metrics, and there is no indication that the NYTB is providing services as an agent of the Fund or that the Fund is the intended recipient of the goods or service.

    In fact, there were clearly expenditures made by the NYTB under the contract that was for the sole benefit of the NYTB's membership. For example, there were costs associated with the NYTB's membership meeting (e.g., breakfast platters and chair and table rentals) which were charged against the Fund's contract. There were also meal expenses incurred by the NYTB that were associated with events that were questionable (e.g., multiple meals attributed to a single cocktail event).

    The mischaracterization of the relationship between the Fund and the NYTB creates unmet expectations for the Fund and result in the Fund employees feeling frustrated over their inability to monitor or control the contract as they would normally deem appropriate for a vendor.

14) The NYTB generates revenue for itself from activities and events wholly subsidized by the Fund.

15) The reporting relationship between the NYTB and the Executive Director of the Fund is awkward at best, because Cannizzo is the executive representing the NYTB and also a Fund member to whom Egan reports. Moreover, as a result of his position as a member on the Fund board and committees, Cannizzo has considerable influence over other members further frustrating the Fund staff and their efforts to monitor the contract.

16) In 2014, the NYTB's contract was increased by \$185,000 or approximately 86%, from \$215,000 to \$400,000. This increase was reportedly to enable the NYTB to provide more services and organize more events. While the NYTB hosted two additional events, almost half or approximately 46% of the \$185,000 was used to fund an increase in the NYTB's labor costs.

    Essentially, if the contract had been treated as a sponsorship, the Fund would not have been responsible for labor costs and could have negotiated for more promotional opportunities instead.

17) Irrespective of the mischaracterization of the NYTBs' contractual relationship to the Fund, the NYTB has been improperly designated as a sole source vendor contrary to the State Finance Law and OGS guidelines and awarded contracts in excess of the Fund's discretionary threshold without being subjected to the competitive bid process.

18) In two of the three audits conducted by the OSC of the Fund, OSC specifically referenced the NYTB contract and expressed concern as to whether the Fund is deriving the most benefits from the money expended on the contract. Further, OSC on both occasions recommended that the contract be competitively bid out to address this concern.

In sum, although this review did not find evidence of malfeasance and/or misappropriation of Fund assets, there are significant weaknesses in the Fund's operation and procurement practices which create corruption hazards. For example, the absence of crucial policies addressing the use of discretionary funds allow for subjective determinations as to how much money is sufficient or what causes/programs are appropriate to support. This review also determined that the contractual relationship between the NYTB and the Fund raises questions and concerns about its intended effect (i.e., sponsorship versus vendor) and whether it is in the best interest of the Fund to continue to award the promotional contract to NYTB without a formal bid process. It was also further determined that certain Fund members were engaged in conduct that may be deemed to be in violation of Section 74 of the Public Officers Law in that, interested members were voting on the distribution of supplemental awards that would knowingly yield a direct financial benefit to themselves or family members.

Origin of Case

Robert T. Williams, then-Executive Director of the New York State Gaming Commission ("Commission") and current Deputy Secretary for Gaming, expressed concerns about New York State Thoroughbred Breeding and Development Fund Corporation ("Fund") expenditures and requested a review be conducted to ensure that the Fund is operating properly and in the most efficient and effective manner. Similarly, Fund Chairman and Commission board member John J. Poklemba requested that a review of the Fund be undertaken to ensure the same.

Nature of Allegation

A number of concerns were specifically cited regarding the Fund, including, but not limited to, its procurement practices and retention of particular vendors; promotional expenditures; subsidy of aftercare programs; approval and issuance of supplemental awards; appropriateness of credit card usage; and other potential conflict of interests matters.

Investigative Action

In furtherance of this review, this Office obtained and analyzed Fund records, such as annual reports, board minutes, policies, financial records (budget proposals, financial summaries, invoices, cancelled checks, credit card statements), and vendor contracts including supporting documentation; third-party vendor records; Accurint, Guidestar, and Office of the New York State Comptroller reports; and conducted numerous interviews, including, but not limited to, the following individuals:

- Tracy Egan, Executive Director;

[redacted]

[redacted]

It should be noted that this Office's review primarily focused on transactions that occurred in the years 2014, 2015, and 2016. In certain instances, however, the review extended beyond those years.

Background

In 1973, the New York State Thoroughbred Breeding and Development Fund Corporation ("Fund") was created for raising, breeding, and improving the breed of horses.[1] A board of directors[2] comprised of the Chairman of the then-New York State Racing and Wagering Board ("RWB"), who would also serve as Chairman of the Fund's Board; the Commissioner of the Department of Agriculture and Markets ("Ag and Markets");[3] and the members of the then-New York State Racing Commission ("SRC")[4] administered the Fund.

Effective July 6, 1994, pursuant to the Laws of New York, Chapter 282 of the Laws of 1994, the composition of the Fund's board of directors was amended to include six members appointed by the Governor, all of whom are experienced or have been actively engaged in the breeding of thoroughbred horses in New York state – one the president or the executive director of the statewide thoroughbred breeders association representing the majority of breeders of registered thoroughbreds in New York state, one upon the recommendation of the majority leader of the senate, one upon the recommendation of the speaker of the assembly, one upon the recommendation of the minority leader of the senate, and one upon the recommendation of the minority leader of the assembly. The Governor is responsible for designating the Fund's chair. Fund members are "not [] entitled to any compensation for their services but [are] entitled to reimbursement for their actual and necessary expenses incurred in the performance of their official duties."[5] However, Fund members, "except as otherwise provided by law, may engage in private employment, or in a profession or business including the breeding and racing of thoroughbred horses. The fund, its members, officers and employees shall be subject to the provision of sections seventy-three and seventy-four of the public officers law."[6]

On February 1, 2013, pursuant to Laws of New York, Chapter 60 of the Laws of 2012, the RWB and the New York State Division of Lottery merged to form the Commission, and at that time, the SRC was abolished. As such, the composition of the Fund's board of directors was

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[1] The Act was entitled "An Act in relation to the formation of corporations for raising and breeding and improving the breed of horses and continuing the state racing commission." Prior to the passage of these laws, the Delafield Commission was created to study the future of horse racing in New York State.
[2] Although the Fund's board is referred to as Directors by statute, this Report will refer to them as members hereinafter.
[3] Pursuant to Agriculture and Markets Law Article 2, Section 17, the Commissioner of Ag and Markets is empowered to designate someone to attend on his/her behalf. The Laws of New York, Chapter 197 of the Laws of 2007, authorized the Chairman of the RWB to do the same.
[4] The SRC was comprised of three members appointed by the Governor with the advice and consent of the Senate, with no more than two members belonging to the same political party. The Chairman was designated by the Governor. *See* PML §201(2) (1973) (repealed).
[5] *See* PML §252(4).
[6] *See* PML §252(5).

changed to be comprised of the chair of the Commission or his/her designee, as well as three members of the Commission as designated by the Governor, in lieu of the Chairman of the RWB and members of the SRC. In addition, the Office of Racing Promotion and Development ("ORPD") was created within the Commission to "promote the breeding of horses and the conduct of equine research" and to administer the Fund, the Agriculture and New York State Horse Breeding and Development Fund and the defunct New York State Quarter Horse Breeding and Development Fund Corporation.[7]

Fund Board, Committees, and Staff

Currently, the Fund's board is comprised of Fund Chairman and Commission Member John J. Poklemba; Ag and Markets Commissioner Richard A. Ball; Breeder Philip S. Birsh; New York Thoroughbred Breeders, Inc. ("NYTB") Executive Director Jeffrey A. Cannizzo; Commission Member John A. Crotty; Breeder John Graziano, Jr.; Breeder Joseph G. McMahon; Breeder and former New York State Senator Howard C. Nolan, Jr.; Commission Chair Barry Sample; and Breeder William B. Wilmot, DVM. The Fund's staff consists of Executive Director Tracy Egan; Comptroller [redacted]; Registrar [redacted]; Inspectors [redacted] and [redacted]; as well as temporary staff. The position of Director of the ORPD is vacant.

The Fund has two standing committees and two ad hoc committees. The Audit and Finance Committee was formed on July 16, 2013, and is chaired by McMahon with Cannizzo and Graziano as members. The Governance Committee was formed on July 29, 2014, and is chaired by Poklemba with McMahon as a member. The Ad Hoc Committee on Advertising, commonly referred to as the Promotions Committee, was formed on December 17, 2013, and is chaired by Wilmot with Birsh, Cannizzo, and McMahon as members. Although not listed on the Fund's website, Egan is also a member of the Promotions Committee. The Ad Hoc Committee on Purse Enrichment was also formed on December 17, 2013, and is chaired by McMahon with Cannizzo and Wilmot as members.

Resources of the Fund

The Fund receives a portion of the handle from the regional Off-Track Betting Corporations ("OTBs") and thoroughbred tracks to support its mission. Subsection 254(2) of the Racing, Pari-Mutuel Wagering and Breeding Law ("PML") proscribes how the Fund distributes its revenue, which is as follows:

	Maximum[8]	Maximum with Board Approval	Required Amount
Breeders Awards	43%	65% (50%)	N/A
Stallion Awards	33%	40%	N/A
Owner Awards	15%	20%	N/A

[7] *See* PML §1201.

[8] The percentages do not add up to 100% of the Fund's revenue; rather, there are statutory caps to how much the Fund may spend. With the exception of the Zweig Fund, there are no statutory minimums to what the Fund must contribute in each category.

Purse Enrichment	44%	N/A	N/A
Promotion[9]	6% (5%)	N/A	N/A
Administration	5% (4%)	N/A	N/A
Zweig	N/A	N/A	2%

Additionally, at the end of the calendar year, any money in excess of $75,000 should be paid to the State and regional OTBs, based on the level of contributions of the racing corporations and regional OTBs during the year.

In 2010, legislation was passed amending Sections 254(2)(a), (e), and (f) of the PML to allow for increases in the amount of revenue that the Fund may distribute. Specifically, up to 65% of Fund revenue may be awarded to breeders with board approval, and the maximum for promotions and administration were increased to 5% and 6%, respectively. However, the amendments contained an expiration provision related to the commencement of operation of the video lottery terminal facility at Aqueduct racetrack. As a result, each subsequent year, legislation is passed extending the expiration date.

Relevant Public Officers Law and Ethics Advisory Opinion

Every Fund board member is to file a certificate acknowledging receipt of a copy of Public Officers Law ("POL") sections 73 through 78, as well as 73-a, that s/he has read the aforementioned sections, and affirming that s/he will conform to the provisions, purposes, and intent of the sections and the norms of conduct.[10]

Public Officers Law §73 – Business or Professional Activities by State Officers and Employees and Party Officers

State officers and employees are prohibited from "receiv[ing], directly or indirectly, or enter[ing] into any agreement express or implied, for any compensation, in whatever form, for the rendering of consulting, representational, advisory or other services by himself or herself or another in connection with any proposed or pending bill or resolution in the senate or assembly."[11]

State officers and employees are prohibited in participating in any contracting decision involving the payment of more than $1,000 to him/herself, any relative of that individual, or an entity in which that individual or any relative has a financial interest.[12]

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[9] Specifically, Fund monies may be spent to "advance and promote breeding and raising of thoroughbreds in this state by the publication and dissemination of information relating thereto, and the encouragement of interest, including among youth, in the breeding and raising of New York-breds, and to advance and promote interest generally in agricultural pursuits." *See* PML §254(2)(e). This definition will be discussed in more detail, *infra*, at "Aftercare Donations/Sponsorships."

[10] *See* POL §78.

[11] *See* POL §73(7-a).

[12] *See* POL §73(15(a). Financial interest is determined by whether someone "owns or controls ten percent or more of stock in such entity (or one percent in the case of a corporation whose stock is regularly traded on an established securities exchange)" or "serves as an officer, director or partner of that entity." *See* POL §73(1)(l). Relative is defined as "any person living in the same household as the individual and any person who is a direct descendant of that individual's grandparents or the spouse of such descendant." *See* POL §73(1)(m).

Public Officers Law §74 - Code of Ethics

Generally, "[n]o officer or employee of a state agency . . . should have any interest, financial or otherwise, direct or indirect, or engage in any business or transaction or professional activity or incur any obligation of any nature, which is in substantial conflict with the proper discharge of his or her duties in the public interest."[13] This prohibition includes not only actual conflicts, but also perceived conflicts as well. Specifically, one's conduct should not "give reasonable basis for the impression that any person can improperly influence him or her or unduly enjoy his or her favor in the performance of his or her official duties, or that he or she is affected by the kinship, rank, position or influence of any party or person"[14] nor "raise suspicion among the public that he or she is likely to be engaged in acts that are in violation of his or her trust."[15]

Further, no officer of employee should "use or attempt to use his official position to secure unwarranted privileges or exemptions for himself or others,"[16] "engage in any transaction as representative or agent of the state with any business entity in which he has a direct or indirect financial interest that might reasonably tend to conflict with the proper discharge of his official duties,"[17] or "mak[e] personal investments in enterprises which he has reason to believe may be directly involved in decisions to be made by him or which will otherwise create substantial conflict between his duty in the public interest and his private interest."[18]

New York State Ethics Commission[19] Advisory Opinion No. 95-13

After the PML was amended in 1994 to appoint additional members to the Fund's board, guidance was sought from the then-New York State Ethics Commission ("NYSEC") regarding the application of Section 74 of the POL to the Fund's members. Specifically, the Fund inquired as to whether those members eligible to receive payments as breeders, stallion owners, or owners are allowed to participate in deliberations and vote on resolutions (1) allocating of Fund resources (percentages for awards and purses); (2) fixing the amount of awards, purses, and conditions of New York-bred races; and (3) setting qualifications of horses earning payments. Lastly, the NYSEC was also asked whether board members of the NYTB, including its President or Executive Director, may participate in deliberations or vote on resolutions regarding payments, subsidies, or other arrangements with the NYTB.[20]

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[13] *See* POL §74(2).
[14] *See* POL §74(3)(f).
[15] *See* POL §74(3)(h).
[16] *See* POL §74(3)(d).
[17] *See* POL §74(3)(e).
[18] *See* POL §74(g).
[19] The Public Employee Ethics Reform Act of 2007 abolished the State Ethics Commission and merged it with the Temporary State Commission on Lobbying to form the Commission on Public Integrity. The Public Integrity Reform Act of 2011 abolished the Commission on Public Integrity and created the Joint Commission on Public Ethics, adding the investigative function of the Legislative Ethics Commission and retaining the authority over Executive Branch ethics and lobbying.
[20] *See* N.Y.S. Ethics Comm. Adv. Op. No. 95-13, annexed hereto as Exhibit "1," at "Questions Presented." The last question regarding whether the Fund may continue to pay NYTB a percentage of the New York-bred foal and stallion registration fees for which NYTB does not render any services will not be discussed, as this arrangement is no longer in effect.

The NYSEC began its discussion by explaining that when confronted with inconsistent statutes, an effort should be made to look at the history and purpose to determine legislative intent and "harmonize" inconsistencies, so as not to make legislation a nullity.[21] It noted that the Governor's memorandum approving the 1994 legislation cited it as a "significant step toward "returning the responsibility for decisions affecting the future of horse racing in New York to the people who have invested their time and money into the industry" and that "for too long, we in government have dictated to the breeders . . . rather than listened to them."[22] As such, the legislation specifically created a situation where interested individuals would have a say over setting standards and allocating resources. Nevertheless, "in order to meet their obligation to the public trust, [Fund members] must recuse themselves from deliberating and voting on any matter from which they may directly and personally benefit due to their activities as owners or breeders, but they may fully participate in other matters."[23]

The NYSEC determined that Fund members could engage in (1) and (2) since the allocation of resources is proscribed by statute and that "any individual [member's] potential to benefit from the allocation of the awards is *speculative*, as an award would be received only if the board member's horse places first through fourth in an eligible race *to be held in the future*."[24] (emphasis added) Similarly, a member could engage in (3), except if the matter involved "his or her own qualifications; nor could a director participate in a matter involving the approval of a qualification that would allow his or her horse to participate where, absent approval, the horse could not."[25] With respect to voting on resolutions regarding payments, the NYSEC determined that owners or breeders who are also directors or officers of the NYTB are required to recuse themselves from deliberations and voting, but those who are merely members of the NYTB may participate.

Relevant Public Authorities Law[26] and Authorities Budget Office Guidance

The Fund is a public benefit corporation classified as a state authority and subject to the Public Authorities Law ("PAL").[27] The Authorities Budget Office ("ABO") was created to ensure that public authorities are more accountable and transparent, in part, by providing training and technical assistance, as well as issuing policy guidance and recommended best practices.

In order for an authority to function effectively and ethically, the PAL states that, among other things, an authority's board execute oversight over the authority's chief executive and other management, including establishing policies for salary and compensation; understand, review, and monitor implementation of fundamental financial and management controls and operational decisions; adopt a code of ethics; and establish written policies and procedures for travel and

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[21] *See id.*, at "Discussion," paras. 4-5.
[22] *Id.*, at "Discussion," para. 2.
[23] *Id.*, at "Discussion," para. 8.
[24] *Id.*, at "Discussion," "Question 1." *See also id.*, at "Discussion," "Question 2."
[25] *Id.*, at "Discussion," "Question 3."
[26] The PAL was amended by the Public Authorities Accountability Act of 2005 ("PAAA") and the Public Authorities Reform Act of 2009 ("PARA"), which also created the Authorities Budget Office.
[27] The Fund is considered a state authority because one or more of its members is appointed by the Governor. *See* PAL §2(1).

procurement guidelines.[28] Board members are required to sign an acknowledgment of his/her fiduciary duty.[29]

The PAL specifies that except for board members who serve by virtue of his/her civil office, "[n]otwithstanding the provisions of any general, special or local law, municipal charter or ordinance:"

> the majority of the remaining members of the governing body of every state or local authority shall be independent members; provided, however, that this provision shall apply to appointments made on or after the effective date of chapter seven hundred sixty-six of the laws of two thousand five which added this subdivision.[30] The official or officials having the authority to appoint or remove such remaining members shall take such actions as may be necessary to satisfy this requirement and further, shall consider the prospective diversity of the members of a state authority when making their determinations to appoint any member. For the purposes of this section, an independent member is one who:
> (a) is not, and in the past two years has not been, employed by the public authority or an affiliate in an executive capacity;
> (b) *is not, and in the past two years has not been, employed by an entity that received remuneration valued at more than fifteen thousand dollars for goods and services provided to the public authority or received any other form of financial assistance valued at more than fifteen thousand dollars from the public authority*;
> (c) is not a relative of an executive officer or employee in an executive position of the public authority or an affiliate; and
> (d) is not, and in the past two years has not been, a lobbyist registered under a state or local law and paid by a client to influence the management decisions, contract awards, rate determinations or any other similar actions of the public authority or an affiliate.[31] (emphasis added)

It should be noted that Cannizzo is a Fund board member by virtue of his position as the NYTB's Executive Director, a position he has held since January 2010.[32] Further, the Fund contracts with the NYTB to provide promotional services at an annual cost of $400,000. As such, Cannizzo would not be considered an independent member of the Fund's board.

The PAL requires the establishment of audit[33] and governance[34] committees comprised of no less than three independent members. The Fund's Audit and Finance Committee has three members, one of whom is Cannizzo, who, as noted above, would not be considered an independent

[28] *See* PAL §2824(1).
[29] *See* PAL §2824(h) (added by PARA).
[30] This section was added by the PAAA, which became effective on January 13, 2006.
[31] *See* PAL §2825(2), subsection of "Membership on authorities and commissions; independence; and financial disclosure."
[32] As noted *supra*, pursuant to the Laws of New York, Chapter 282 of the Laws of 1994, the president or the executive director of the statewide thoroughbred breeders association representing the majority of breeders of registered thoroughbreds in New York state shall be appointed as a member.
[33] *See* PAL §2824(4).
[34] *See* PAL §2824(7).

member. The Fund's Governance Committee only has two members, one of whom is Commissioner Poklemba whose membership to the Fund is a function of his civil office and so is not an independent member. Thus, the Fund's committees currently do not meet the PAL requirements.

With respect to procurement guidelines, the PAL states that they should be annually reviewed and approved by the authority.[35] Relatedly, an authority's prompt payment policy should include, but is not limited to, a description of the procedure for a contractor to request payment; a schedule setting forth the time frame for making payment; a declaration that interest will be paid, and at what rate, if prompt payment is not made; a list of sources of funds to pay an interest penalty on each type of contract; and a list of facts and conditions that would reasonably justify extension of payment.[36]

With respect to other policies and procedures not specifically discussed in the PAL, the ABO recommends that all public authorities "adopt written policies that specifically delineate the proper use of an authority's discretionary funds," as well as what would be considered an improper use.[37] For example, meals expenses may be "incurred through participation in, or sponsorship of, activities integral to meeting the core public purpose of the authority. Similar to appropriate travel expenses, eligible meal costs must be properly documented and reasonable cost thresholds established."[38]

Further, the ABO lists, among other things, the following as inappropriate expenses because they "do not advance a public purpose and should be considered personal in nature":[39]

- Food, beverages, and other refreshments purchased for the personal use of directors, management or other employees, or by persons with whom the authority conducts business (unless prior authorization is received); . . .
- Charitable contributions or sponsorships of events not associated with the authority's mission;
- Purchases of alcohol or tobacco products.[40]

A review of the Fund's records has found spending on the above-referenced prohibited expenses, which is discussed in greater detail, *infra*, at "Review of Discretionary Spending."

<u>State Finance Law and Office of General Services Procurement Guidelines</u>

The New York State Finance Law ("SFL") defines a sole source contract as a "procurement in which only one offeror is *capable* of supplying the required commodities or services" (emphasis

[35] *See* PAL §2879(1).
[36] *See* PAL §2880(3).
[37] *See* ABO, Recommended Practice "Written Policies Governing the Use of Authority Discretionary Funds," annexed hereto as Exhibit "2."
[38] *Id.*
[39] *Id.*
[40] *Id.*

added), and the agency must document why proposed vendor is the only viable source for commodities or services.[41] Relatedly, the SFL defines a single source contract as:

> a procurement in which although two or more offerors can supply the required commodities or services, the commissioner or state agency, upon written findings setting forth the material and substantial reasons therefor, may award a contract or non-technical amendment to a contract to one offeror over the other. The commissioner or state agency shall document in the procurement record the circumstances leading to the selection of the vendor, including the alternatives considered, the rationale for selecting the specific vendor and the basis upon which it determined the cost was reasonable.[42]

For both a sole source and a single source contract, the Office of the New York State Comptroller ("OSC") must approve the contract if its value is over the discretionary threshold and grant an exemption, if the agency seeks a waiver from advertising in the New York State Contract Reporter.[43]

Review of Fund By-Laws and Relevant Policies[44]

By-Laws

According to the Fund's by-laws, the Fund's officers consist of the Chairman of the board, the remaining nine members, the Executive Administrator, the Secretary, the Treasurer, and any other officers the board deems as required. The Executive Administrator is appointed by the Fund's board, "serv[ing] at the will of the board and under its direct supervision and control." The role of Secretary can be assigned to the Fund's Counsel. The Treasurer and Executive Staff, who assist the Executive Administrator, are also appointed by the Fund's board.[45] The Fund's Organizational Chart, which is posted on the Fund's website under "Reports & Filings," however,

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[41] *See* SFL §163(g). *See also* Ofc. of Gen. Servs., "N.Y.S. Procurement Guidelines," (May 2014), annexed hereto as Exhibit "3," at 52.

[42] *See* SFL §163(h). *See* Exhibit "3," at 51.

[43] *See* Exhibit "3," at 8-9.

[44] The Fund's by-laws and policies do not indicate the date that they were adopted and/or amended. However, the Fund board minutes from May 10, 2007, indicate that the By-Laws were amended to be in compliance with the PAAA, though it is unclear what those changes were, except for the adoption of Audit and Governance Committees and their charters. *See* Fund Board Minutes dated May 10, 2007, annexed hereto as Exhibit "4A." The Fund's board minutes are collectively referred to as Exhibit "4," with each date assigned its own letter. The minutes are also listed in order of appearance and not chronologically. The Fund board minutes from August 4, 2011; November 29, 2012; and March 28, 2017 (annexed hereto as Exhibits "4B-4D," respectively) reference reviewing and/or reapproving policies. The 2011 and 2012 minutes named each of the policies, but the 2017 minutes did not. The 2017 minutes indicate that the policies circulated for review were "identical, or substantially similar" to those in effect, but did not indicate which policies were not identical.

[45] *See* Fund By-Laws, annexed hereto as Exhibit "5A," at Article IV, "Officers." The Fund's by-laws and policies are collectively referred to as Exhibit "5," with each document assigned its own letter. These documents may also be found on the Fund's website.

use titles that differ from its by-laws and does not show the reporting relationship of the Executive Director to the Chairman and members, who are omitted from the chart.[46]

Credit Card Policy[47]

Fund credit cards are issued to the Executive Director, Treasurer, and Field Inspection staff, and charges must be for Fund-related business and documented within 30 days. The hotel and meal reimbursement rates should be consistent with those posted on the OSC website, unless approved by Fund management. Those OSC rates are for employees in travel status. It is unclear to whom "Fund management" refers based on the Fund Organizational Chart, although the Fund website has a section entitled "Executive Management," which includes Egan and all the Fund members.[48]

The Credit Card policy also refers to a "new" Travel Reimbursement Expense Form and describes what information should be included, but a sample of the form is not attached.[49] More importantly, the Fund does not have a Travel Policy, as required by Subsection 2824(1)(e) of the PAL.

Procurement Contract Guidelines Policy[50]

The Fund's Procurement Contract Guidelines govern procurement for goods or services valued at $5,000 or more. Notably, the supervision of procurements for goods or services is the responsibility of the Fund's Executive Director. According to the Fund's policy, procurement contracts shall contain provisions requiring the contractor to report periodically to the Executive Director on the status of work and the costs incurred to date. Moreover, "[w]hen possible, Fund staff, space, and supplies shall be used in order to reduce contract costs."[51]

For goods or services valued at $5,000 or more, "[c]ontractors shall be selected through competitive bidding from at least three sources, unless the services are available from only one source or there is only one source in the judgment of the directors suitably qualified to perform the services."[52] However, competitive bidding is not required for "editorial work, for the services of journalists selected to write on matters relating to the breeding of horses, or for outside accounting services unless the directors shall elect to replace the public accounting firm that has previously audited the Fund's accounts."[53]

Typically, contracts in excess of $5,000 must be approved by the Fund's board. However, effective July 29, 2014, the Promotions Committee was given authority to spend up to $25,000 on

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[46] *See* Fund Organizational Chart, at http://www.nybreds.com/wp-content/uploads/2013-Organizational-Chart.pdf, last accessed Aug. 2, 2018.
[47] *See* Fund Credit Card Policy, annexed hereto as Exhibit "5B."
[48] *See* Fund Executive Management, at http://www.nybreds.com/aboutus/executive-management/, last accessed Aug. 2, 2018.
[49] Although the reference is to a new form, the policy has been in place since at least 2015.
[50] *See* Fund Procurements Contract Guidelines, annexed hereto as Exhibit "5C."
[51] *Id.*, at para. 8.
[52] *Id.*, at para. 4.
[53] *Id.*

a single procurement of goods and services without seeking full board approval.[54] Lastly, any contract involving services for a period in excess of one year is also subject to an annual review and approval by the board.[55]

Prompt Payment Policy[56]

The Fund's Prompt Payment Policy states that for contracts involving "independent auditing services, promotional/public relations materials, temporary staffing, legal services, and other office services agreements," as well as "purchases of other services and/or commodities as needed during the year."[57] Payments will be made within "thirty (30) days of completion of service or delivery of commodity and presentation of invoice."[58]

The Fund should consider whether revisions to the policy for clarification purposes are necessary. "SECTION 2880 (11)" is listed beneath the Prompt Payment Policy heading, but there is no reference to what statute or regulation it cites. Presumably, this is a reference to Section 2880 of the PAL, "Prompt Payment." However, subsection 11 refers specifically to Annual Reports to be prepared within 90 days of the completion of the Fund's fiscal year and provided to OSC, the state director of the budget, the chairman of the senate finance committee, and the chairman of the assembly ways and means committee. Further, the Fund's Prompt Payment Policy and Reports from 2015 through 2017 have a section detailing the policy, but does not use the same language. Notably, the reports omit reference to temporary staffing, office service agreements, and other services and/or commodities as needed during the year.[59]

Additional Policies Warranted

As noted previously, the ABO recommends that all public authorities "adopt written policies that specifically delineate the proper use of an authority's discretionary funds,"[60] as well as what would be considered an improper use. The Fund does not have such a policy, and the absence of one create risks that money may be inappropriately expended. Not only would the policy be important as it relates to travel and meal expenses, but also in the following areas, which may require their own specific policies:

<u>Fellowship and Scholarship Programs</u>

The Fund does not have a policy governing its Fellowship and Scholarship Programs, as recommended by the ABO for the proper use of discretionary funds. There is no formal application form or process utilizing uniform criteria to determine who should be awarded a fellowship or

[54] *See id.*, at para. 5. It should be noted that the first paragraph states that the "following resolution" was adopted in 1986, though this provision went into effect in 2014. Clearly, the guidelines were amended, but there is no indication when this occurred as the language in the first paragraph was not updated.
[55] *See id.*, at para. 6.
[56] *See* Fund Prompt Payment Policy, annexed hereto as Exhibit "5D."
[57] *Id.*
[58] *Id.*
[59] *See* Exhibit "5D" and Fund Prompt Payment Policy & Reports for 2015-2017, annexed hereto as Exhibits "5D-5F," respectively.
[60] *See* Exhibit "2."

scholarship, including whether someone may receive a fellowship or scholarship more than once. There is also no monetary threshold as to how much may be awarded for the fellowship or scholarship programs except for the value and number of awards approved annually during a board meeting. The absence of documentation pertaining to the application and deliberative process (to demonstrate how the candidates were selected) creates the opportunity for misuse and abuse within the programs.

Sponsorships

The Fund also does not have a policy governing how it decides to enter into sponsorship agreements (e.g., advertising at events) nor how much may be spent. A review of the Fund's sponsorships indicates that the Fund often does so without any clear indication of how the Fund will be promoted by the entity.

The review of these programs and sponsorships are discussed in greater detail, *infra*, at "Review of Discretionary Spending."

Potential Conflict of Interests

Distribution of Awards to Fund Members

The Fund achieves its mission to promote breeding and preserve farmland primarily through the use of monetary incentives. These incentives include awards to breeders, owners, and stallion owners and purse enrichments. The incentives offered are of a significant amount. In 2017, the Fund distributed approximately $15,078,741 in awards alone and a total of $17,203,494 in awards and purse enrichments. Given the statutory mandate that only those involved in the industry be board members, it is highly conceivable that the members may be placed in a position where their actions would result in financial benefits to themselves. As discussed, *supra*, the NYSEC Advisory Opinion No. 95-13 found that Fund members who are eligible to receive incentives may vote on speculative awards. However, the same would not apply to voting on supplemental awards.

As a result of the statutory restriction on how much money may be carried-over into the next year by the Fund, when there is excess revenue,[61] the board votes on whether to release the 10% holdback on awards and, if there are additional funds, whether to distribute the monies as purse enrichment and/or distribute as a supplemental award payment to the various award categories (Owner, Breeder, Stallion Owner) which is usually consistent with the percentages previously determined. The decision is typically made in December, after the end of the racing season, and the distribution of the monies take place in the first quarter of the following year. This practice of deciding to distribute surplus revenue at the end of the year creates a situation wherein the members knowingly stand to reap a direct financial benefit as a result of his/her vote, as the potential for receiving awards is no longer speculative. Thus, in order to comply with Section 74 of the POL and the NYSEC Advisory Opinion No. 95-13, any member who would directly benefit from his/her decision must recuse him/herself. Nevertheless, a review of board minutes and Fund

[61] This surplus revenue is generally a result of higher than anticipated revenue (e.g., higher than budgeted video lottery terminal earnings) and/or the lower than anticipated distribution of awards.

records dating back to 2010 indicate that generally such members did not recuse themselves from this process, and instead, voted on matters that yielded direct financial benefits to themselves which can be construed to be a violation of Section 74 of the POL.[62]

The following directors were noted as having benefitted from such actions during the period of this Office's review:

Member	**Year[63]**	**Vote**	**Supplemental Award Amount Received**
John Graziano, Jr.	2014	Yes	$1,224.48
	2015	Yes	$842.00
Joseph McMahon	2014	Yes	$42,300.89
	2015	Yes	$30,909.00
Howard C. Nolan	2014	Yes	$3,483.72
	2015	Yes	$6,105.00
William Wilmot	2014	Yes	$5,666.41
	2015	Yes	$3,327.00

It should be noted that the supplemental payments related to member Graziano were made to his [redacted] As there is a familial relationship, Graziano's action may be construed as a violation of Section 74(f) and 74(h) of the POL, as discussed *infra*.

Although supplemental awards have not been distributed in the last two years, the members should be reminded to recuse themselves from voting on the distribution of supplemental awards if they stand to derive a financial benefit to avoid violating provisions of the POL and the appearance of a conflict.

Tracy Egan, Appointment as Executive Director and Outside Activities

On May 12, 2010, Tracy Egan was appointed Executive Director of the Fund. As Executive Director, Egan is responsible for the daily operation of the Fund including, but not limited to, developing, implementing, and enforcing policies and managing the Fund's staff.[64] Egan regularly reports to the Fund's board and has no authority to vote on matters before the Board. According to her biography posted on the Fund's website, Egan owns a farm in Saratoga and "has been a hands-on breeder for more than two decades and formerly raced as Seven Furlong Farm."[65] Prior to her current position, Egan worked as an anchor/reporter covering the capital region for ABC and CBS affiliates in Albany and for WABC-TV/Eyewitness News in New York

[62] Interestingly, McMahon recused himself from voting on the distribution of supplemental awards at the February 2012 board meeting, but not during any other vote on supplemental awards.

[63] *See* Dec. 4, 2014 and Dec. 1, 2015 Fund Meeting Minutes, annexed here to as Exhibit "4E" and "4F," respectively. Supplemental awards were not distributed in 2016 or 2017 as monies were provided to Finger Lakes.

[64] The Fund's By-Laws explicitly state that the "Board of Directors shall appoint an Executive Administrator to serve at the will of the Board of Directors and under its direct supervision and control. He shall be the General Manager and Chief Operating Officer of the Corporation and shall be in charge of the administration of its affairs. He shall perform any other duties assigned to him by the Corporation." *See* Exhibit "5A."

[65] *See* Fund Executive Management, at http://www.nybreds.com/aboutus/executive-management/, last accessed Aug. 2, 2018.

City. Egan is also a licensed real estate broker in New York and is affiliated with [redacted] An internet search recently revealed that Egan has four listings (three single family and one land listing).[67]

At the time of Egan's hire in 2010, she was an active breeder and real estate broker. Accordingly, the Fund members sought assurances that Egan's outside activities would not conflict with her duties as Executive Director. The Fund's June 24, 2010 meeting minutes reflect that [redacted] requested a formal opinion from the New York State Commission on Public Integrity ("NYSCOPI") as to "whether Ms. Egan, an active breeder and real estate broker in New York, could continue with those activities while serving as Executive Director."[68] The NYSCOPI opinion, issued on August 19, 2010, indicated that Ms. Egan "may continue to register her horses with the Fund and continue to serve as a real estate agent, provided that she receives the approval of her appointing authority" and refrains from performing duties related to her real estate business during state work hours and/or using state resources, including subordinates.[69]

Although Egan was permitted to continue with her activities as a breeder and real estate broker, it was reported to this Office that in order to avoid any appearance of a conflict of interest, Egan had voluntarily agreed to refrain from accepting any awards due to her as a result of horses foaled while she is employed with the Fund. This Office, however, received conflicting responses as to whether Egan had indeed voluntarily agreed to forego any awards she was entitled to receive. Many individuals interviewed, including those who were present at the May 2010 meeting (when the vote was taken to appoint Egan) and current Board members, either denied having any knowledge or could not recall with any certainty if Egan had made such a concession. At least one board member believed that Egan had done so and that, to date, Egan had not accepted any awards. When interviewed, Egan denied that there were any conditions attached to her employment as it related to her breeding activities. In fact, records demonstrate that Egan continued to receive Breeder Awards in the amounts as follows:

Award Year	Amount Received
2011	\$6,415.50
2012	\$5,792.58
2013	\$24,948.00
2014	\$32,259.75
2015	\$52,459.00
2016	\$23,640.00
2017	\$38,643.68
Total	**\$184,158.51**

This Office also reviewed records to determine whether Egan had made such an agreement with the Fund. Board meeting minutes are devoid of any indication that such an agreement was made or that any discussion had taken place other than the fact that [redacted] had sought a formal

66 [redacted]

67 *See* Egan Real Estate Listings annexed hereto as Exhibit "6."

68 *See* Jun. 24, 2010 Fund Meeting Minutes, annexed hereto as Exhibit "4G."

69 *See* Aug. 19, 2010 NYSCOPI Letter, annexed hereto as Exhibit "7."

opinion from NYSCOPI. Other documentation though, including an email from [redacted] addressed to [redacted] of the RWB and now [redacted] as well as notes belonging to the [redacted] seemed to indicate that Egan had agreed to certain concessions. [redacted]'s notes for the May 12, 2010 board meeting, which contain the watermark "draft," demonstrate that there was an intent to have Egan formally declare that she would forego the receipt of any awards from the Fund as long as she was employed by it.[70]

Nevertheless, notes retained by [redacted] of the May 12, 2010 executive session indicate otherwise.[71] According to [redacted]'s handwritten notes, Egan wished to continue accepting awards for horses she had already enrolled in the Fund's programs. Further, as it relates to horses that may be registered in the Fund's programs in the future, Egan wanted the awards to be donated to a charitable organization.[72] Lastly, [redacted]'s notes also indicated that Egan wished to continue her real estate business. Therefore, any belief that Egan agreed to forego breeders awards is erroneous.

With respect to Egan's outside real estate business, this Office has found no evidence that Egan has failed to comply with the conditions imposed upon her. Egan stated that her real estate practice is not very active and that in 2017, she earned only [redacted] from her real estate business. Egan denied that her real estate business crossed over and/or involved people associated with the Fund, though she reported that her clients may include sellers/buyers of farms, including horse farms in the Saratoga area. She also stated that her listings consist of her own farm land and 33 acres of farm land in Saratoga belonging to [redacted] a good friend. Thus, the potential exists for Egan to be involved in a sale of property where one or more of the parties involved are participants in the Fund's programs, especially if the property is a farm. Interestingly, Egan was also the real estate agent for [redacted] a vendor to the Fund. This transaction, though, occurred in 2009, prior to Egan becoming Executive Director.[73] (This relationship is discussed in greater detail, *infra*, "Procurement Practices".) As such, it is important that Egan be regularly reminded of the potential for conflict. The Fund should also consider if other measures are warranted, such as requiring Egan to disclose to the Board in writing any listings which involve a horse farm or individuals who have any financial/business relationship with the Fund so that a determination may be rendered as to whether a conflict of interests exists.

Review of Discretionary Spending

Use of Fund Credit Cards

Pursuant to the Fund's credit card policy, designated employees, including Egan, may use a Fund credit card if it is related to a Fund purpose. The expense must be properly documented,

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[70] *See* May 10, 2010 Email from [redacted] to [redacted] and [redacted] notes for May 12, 2010 Fund Board Meeting, annexed hereto as Exhibits "8A" and "8B," respectively.
[71] *See* May 10, 2010 [redacted] notes, annexed hereto as Exhibit "8C."
[72] This Office could not find any further mention or documentation of Egan's initial proposal to donate her awards to a charitable organization, nor did Egan reference any such arrangement in her interview.
[73] *See* [redacted] Property Records, annexed hereto as Exhibit "9."

and hotel and meal reimbursement rates should mirror OSC guidelines, which apply when an employee is deemed to be in "travel status."[74] It should be noted that in those instances when an employee is assigned to an alternate work location that is less than 25 miles from their home or official station, OSC considers that employee as merely "traveling in the proximity of his or her official station," and meals are typically not reimbursed or paid for by the State.[75]

This Office conducted a review of each authorized employee's use of credit cards, including, but not limited to, the Fund's Bank of America Visa, Exxon and Sunoco accounts. No irregularities were noted as it relates to charges incurred by Fund Inspectors [redacted] and [redacted][76] or by Fund Comptroller [redacted] As it relates to Egan's use of the Fund credit card, each expenditure is arguably related to Fund business, although there may be questions of necessity and reasonableness related to select charges.

A review of Egan's credit card expenditures for the time period of January 2014 through August 2016 revealed that she regularly charged offices supplies and recurring administrative services (e.g., QuickBooks subscriptions, domain renewals, etc.). The review also found that Egan used the Fund's credit card on 46 separate occasions for food and drink.[77] The amounts charged ranged from as little as $4.00 (receipt submitted, but no indication as to what the charge was related) to as much as $334.43 (receipt submitted, but no description provided other than "NY Showcase Day"). More than two-thirds of the expenses, or 31 of the 46 charges, were reportedly related to the fellowship or scholarship program. The remaining occasions included, but were not limited to, Yearling Sales, Showcase Day, promotional events, or meetings. The receipts submitted not only encompassed meals, but also incidentals, such as a bottle of water or a soda, which would be considered personal and more appropriately borne by the individual. Conceivably, since each expense may be associated with a Fund event or program, the charges may be deemed to be legitimate. However, contrary to the Fund's credit card policy, the information Egan provided, which consisted of names (sometimes illegibly written) on the back of receipts, did not always contain sufficient details as to the reason for the meal and/or for whom.

Lastly, it should be noted that in the rare instance where an itemized bill was attached, this Office found that on at least three occasions, alcoholic beverages were consumed and paid for by the Fund. Specifically, alcoholic beverages were noted on the receipts for the following dates: May 25, 2015, one "Ketel One Bloody;" June 23, 2015, four glasses of wine; and October 4, 2015, one glass of wine. Although the drinks were for a nominal cost totaling $62.25, the use of public funds to purchase alcohol is not acceptable practice and contrary to ABO guidelines.

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[74] According to the OSC Travel Manual, one is deemed to be in "travel status" when an employee is "more than 35 miles from both their official station and home." *See* OSC Travel Manual rev. Dec. 14, 2015, annexed hereto as Exhibit "10," at 1. Official station is defined as "the employee's usual work location." *Id.*, at 3.

[75] The OSC Travel Manual states that exceptions may be made when it is "in the best interest of the State." *Id.*, at 4. It is important to note though, that all travel begins with the premise that "only actual, necessary and reasonable business expenses" are to be reimbursed. *Id.*, at 1.

[76] This Office was advised that [redacted] retired this fall.

[77] *See* Schedule of Egan Meal Charges, annexed hereto as Exhibit "11." In 2014, Egan utilized the Fund's credit card for food and drink purchases on nine occasions and expenses totaled $754.87. In 2015, Egan utilized the Fund's credit card for food and drink purchases on 17 occasions and expenses totaled $2,665.31. In 2016, she utilized the Fund's credit card for food and drink purchases on 21 occasions and expenses totaled $2,344.01.

The issue of whether a credit card charge is appropriate would be more easily answered if examples were included in the Fund's credit card policy, as recommended by the ABO, and would provide clear guidance to Fund staff. In conjunction with a more detailed policy, it is recommended that the Fund also establish a dollar threshold for such discretionary expenditures as suggested by the ABO. Consideration should also be given to drafting a policy prohibiting the purchase or consumption of alcohol or other controlled substances during work hours and/or the use of Fund money/credit cards to make such purchases.[78]

Scholarship and Fellowship Programs

At the February 16, 2012 Fund board meeting, members unanimously approved the creation of a scholarship for students attending State University of New York schools that provide equine and/or agricultural courses.[79] At the time, it was determined that the Fund would allocate $15,000 from the budget to fund six $2,500 scholarships to be divided equally among Cobleskill, Cornell University, and Morrisville. According to meeting minutes, the scholarships are to be awarded to students in their second, third or fourth year of study. Selected recipients should have demonstrated through course selection, performance and extra-curricular activities, a sincere interest in pursuing a career in breeding, racing, or agricultural industry in New York. It was also announced during the February meeting that Egan would contact each school for assistance with the awarding of such scholarships. In 2015, the scholarship amount was increased from $2,500 to $3,000.[80]

The fellowship program was established in 2015 at the suggestion of Fund member William B. Wilmot, DVM, and [redacted] The program was inspired by the Kentucky Equine Management Internship ("KEMI") and is intended to similarly provide New York equine studies students the opportunity to gain experience in equine management at a farm or racetrack. There are key differences between the Fund's program and KEMI. For example, the Fund's program is free whereas the KEMI program costs participants $2,500. The Fund also pays half of the cost of the fellows' housing at Skidmore College for the summer. Further, fellows are guaranteed to earn minimum wage for the hours they work at their placement, either at a farm or with a trainer for approximately 12 to 13 weeks. The fellows also attend biweekly lectures and are afforded the opportunity to be participate in other activities, including visiting the National Museum of Racing and Hall of Fame, witnessing the Yearling Sales preparation and spending a day at the races. Prospective fellows are solicited from Cazenovia College, Cobleskill, and Morrisville. Both Morrisville and Cobleskill also provide course credit to the fellows.

A review of the Fund's documentation pertaining to its scholarship and fellowship programs revealed that both programs lack a formal application process, as well as a policy clearly

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[78] This Office interviewed a number of Fund staff and members regarding the use of Fund resources to purchase alcohol, as well as the serving of alcohol (e.g., open bar etc.) at Fund events. All individuals interviewed indicated that they were not aware of any Fund policy, or other prohibition, which prevented the Fund from doing so, and none expressed concern that the Fund was engaged in such a practice. More importantly, all promotional events and galas, for which the Fund contracts with the NYTB to organize, are not deemed to be the Fund's events so would not be subject to any prohibitions applicable to the Fund. Instead, the Fund is merely viewed as a "sole sponsor" of such events. This issue is discussed in greater detail, *infra*, at "New York Thoroughbred Breeders, Inc."

[79] *See* Feb. 16, 2012 Fund Meeting Minutes, annexed hereto as Exhibit "4H."

[80] *See* 2015 Emails related to Fund scholarship program, annexed hereto as Exhibit "12."

delineating program criteria and funding. The Fund's records generally consisted of press clippings, email correspondence, and copies of checks and invoices. There were no application forms either from the Fund or the school, nor any documentation of the deliberative process. The absence of such records is the result of the Fund's reliance upon the schools to select the students for both programs. Egan confirmed that the schools chooses the recipients for the programs and that there is no formal application process. She noted, however, that the exploratory scholarship committee had proposed guidelines, such as 1) likelihood of staying in New York after graduation; 2) sophomore or other upper classmen only; 3) demonstrated commitment and interests via studies and outside activities; and 4) financial need (in the school's discretion) but did not formalize these guidelines in a policy. Egan further explained that once the school identifies the recipients, there are no other conditions imposed by the Fund or the school, except for providing Egan with a resume. The Fund simply issues a check upon receipt of an invoice from the school. Egan also conceded that there are repeat scholarship recipients, but noted that the Fund does not have a policy prohibiting it and claimed that sometimes there are not enough applicants for the program.

According to Fund records, three individuals received a scholarship from the Fund more than once. They are Cobleskill students [redacted] and [redacted], and Morrisville student, [redacted] Another Cobleskill student, [redacted] was both a scholarship and fellowship recipient in [redacted][81] Furthermore, although the programs are supposed to be open only to upper classmen records demonstrate that on at least one occasion, a first-year student, [redacted] received a scholarship in [redacted]

The practice of solely relying upon the schools to select the recipients of Fund scholarships and fellowships in the absence of established program criteria, a formal application process, and documentation creates the opportunity for abuse of the programs (e.g., multiple scholarships may be awarded to a relative of a faculty member.) If the Fund is unaware of the number of students applying to or being considered for either program or of the credentials and interests of the applicants, it would also be difficult for the Fund to determine if there are enough applicants, if the programs are successful in achieving its goals, or if the students chosen are the appropriate recipients.[82] As such, the criteria, selection process, restrictions, if any, on receiving a scholarship or fellowship more than once, and funding parameters should be clearly stated in a policy. Further, if the Fund continues to rely solely upon the schools to pick the recipients, then there should be a formal application and clear documentation of the selection process to justify their selections.

Aftercare Donations/Sponsorships

In 2015, the Fund sought an opinion from the Commission to determine if the Fund was permitted to use a portion of the revenue generated from registration fees to support Thoroughbred aftercare facilities. On October 13, 2015, [redacted] the Commission's [redacted], and [redacted] stated that "the legislature has strictly constrained the Fund's

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[81] The Fund did not, however, have to subsidize a dorm at Skidmore for [redacted] because she chose to live at home. Currently, [redacted] is a full-time employee of the Fund [redacted]

[82] Although the Fund announces the recipients of the scholarships and fellowships, consideration should be given to having the Fund promote both programs. At a minimum, this would help broaden the candidate pool even if restricted to the schools already identified and also mitigate any potential for the school to steer select students.

discretion in many respects, including the manner in which and purposes for which the Fund spends money it collects."[83] Further, the Fund may only use its money for those purposes specifically delineated in Section 254(2) of the PML which was determined not to encompass Thoroughbred aftercare programs. Additionally, they concluded that the distribution of money to such programs does not qualify as "the publication and dissemination of information" nor does it lead to the "encouragement of interest . . . in the breeding and raising of New York-breds, and to advance and promote interest generally in agricultural pursuits."[84] Instead, "such expenditures would be supporting the actual care of horses, which is not authorized."[85]

Nonetheless, as a part of its promotional endeavors, the Fund has entered into various sponsorships, including, but not limited to, Akindale Thoroughbred Rescue, Dr. Axel Sondhof's Equine Clinic at Oakencroft, Finger Lakes Thoroughbred Adoption Program, Saratoga Horse Symposium, Old Friends at Cabin Creek, ReRun, Inc., and WNY Polo Club. Many of these entities are accredited by the Thoroughbred Aftercare Alliance, a non-profit organization dedicated to accrediting, inspecting, and awarding grants to aftercare organizations.

Records disclosed that the Fund distributed approximately \$63,115 in 2014, \$95,000 in 2015, and \$12,000 in 2016 to aftercare organizations. These amounts do not include the \$10,000 budgeted annually by the Fund to distribute to the Take2 Second Career Thoroughbred Program ("Take2") via the NYTB.[86] Although the Fund contends that these agreements with aftercare facilities is a part of their promotional efforts, this position is arguably lacking in good faith, especially in light of the October 13, 2015 opinion. Thus, if the Fund wishes to continue this practice, it should seek a legal opinion as to whether the distribution of money to aftercare organizations, even if "promotional," is consistent with the Commission's determination that the expenditure of Fund monies is limited to supporting only those items delineated in statute.

Procurement Practices

[redacted]

[redacted] has been contracted with the Fund since 2012 to provide various services, including "financial management, internal control assessment and development, software review, and book keeping."[87] The agreement has no specified duration, but instead is terminable upon written notice from either party. Prior to being awarded a formal contract for services with the Fund, [redacted] the sole principal owner, was employed part-time with the Fund to assist with administrative duties.

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[83] *See* Oct. 13, 2015 Memorandum from Burns and Stuart, "Authority to Use Registration Fees to Fund Thoroughbred Aftercare Programs," annexed hereto as Exhibit "13."
[84] *Id.*
[85] *Id.*
[86] It should be noted that Take2 was founded by the New York Thoroughbred Horsemen's Association ("NYTHA") and the NYTB to "promot[e] and develop[] second careers" for retired racehorses. Further, the Fund annually budgets \$10,000 as a line item expense in NYTB's promotional contract to be distributed to Take 2, but Take2 only received \$5,000 annually (from 2014 to 2016) as NYTB deducted administrative and materials costs from the \$10,000.
[87] *See* Aug. 17, 2012 [redacted] Consulting Agreement, annexed hereto as Exhibit "14A." Documents related to [redacted] are collectively referred to as Exhibit "14," with each document assigned its own letter.

A search of the New York State Department of State Division of Corporations indicates that the company incorporated in New York in May of 2012, the same year it was awarded a consulting agreement with the Fund.[88] The address listed for service of process is the same as the residential address of [redacted] [redacted] is also listed in the New York State M/WBE Certified Directory as a company that provides accounting services.[89]

According to [redacted] and confirmed by Egan, they knew one another prior to [redacted] employment and contractual relationship with the Fund. They met when [redacted] was looking to purchase a home in New York [redacted] and Egan was the real estate broker who sold her the home [redacted][90] Egan stated that they remained friendly after this transaction, and [redacted] noted that she had mentioned to Egan that she was seeking part-time employment. Sometime thereafter, Egan contacted her and offered her a part-time position at the Fund performing clerical duties.[91]

The position soon morphed into a bigger role at the Fund. [redacted] has an accounting background and was asked to assist the then-Fund Comptroller, [redacted] with bank reconciliations. Reportedly, [redacted] and the previous Comptroller, [redacted] had signed off on reports despite variances in the bank accounts. [redacted] resigned shortly thereafter, and [redacted] recounted feeling obligated to stay and help Egan with the Fund which she described as "a wreck," working 60 hours per week. Egan stated that the Fund had difficulty finding a comptroller, but was finally able to hire [redacted] [redacted] however, remained employed with the Fund as a consultant.

As the Fund hired additional staff, especially [redacted] and as operational weaknesses were addressed, [redacted] was able to reduce her hours to 10 to 25 hours a week. [redacted] stated that it was the "board" that advised her to create [redacted] in 2012. Her decision to heed this advice is consistent with the date of the company's incorporation and execution of the consulting agreement. Over the course of time, 2012 through the present, [redacted] stated that she helped the Fund establish internal controls for the field inspection teams, registry system, and awards payment system. She added that she was instrumental in outsourcing payroll and quarterly tax filings as well as working with the bank to establish overdrafts for the accounts. She also worked on the upgrades to the award payment and registry systems. Currently, she is assisting with the Jockey Club system rewrite.

Egan explained that the responsibilities between [redacted] and [redacted] differed and that [redacted] "made a lot of system improvements" and set up procedures and processes, while [redacted] is "truly a comptroller" and manages the day-to-day fiscal operations. Egan agreed that [redacted] was established by [redacted] after she started working for the Fund, but she could not recall if anyone at the Fund, including [redacted] had advised her to do so.

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[88] *See* NYS Department of State Division of Corporation record, annexed hereto as Exhibit "14B."
[89] *See* New York State Directory of Certified Firms at https://ny.newnycontracts.com, last accessed on Dec. 6, 2018.
[90] *See* Exhibit "9."
[91] Egan said that she thought of [redacted] adding that [redacted] was so meticulous that she "weighed the hay she gave her horses."

A review of the invoices and payments made to [redacted] revealed that the Fund paid the company a total of $73,107 for 2013; $39,930 for 2014; and $52,772.50 for 2015. Interestingly, this review also found that [redacted] had carried over $23,567.50 in income earned in 2014 to 2015. Similarly, [redacted] carried over $24,035 in income earned in 2015 to 2016. The carrying over of income was accomplished by submitting an invoice in January of the following year for services rendered approximately the last half (July or August through December) of the prior year. According to [redacted] she requested that income be carried over from year to year so that she may defer her earnings [redacted] This practice was confirmed by Egan and [redacted] both of whom indicated that the Fund allowed [redacted] to delay invoicing for services for the admitted purpose of deferring income.[92] However, Egan denied having been consulted about this practice, as it is financial and in the purview of [redacted] responsibilities, and did not know whether it comported with the Fund's prompt payment policy.

The practice of allowing [redacted] to delay receiving payment enabled [redacted] to circumvent the income cap set by Social Security. Any income earned in excess of the cap results in a deduction of benefits. This applies to those individuals who have not reached full retirement age, which for [redacted] was [redacted][93] Although, the Fund and [redacted] have not technically violated any laws or the Fund's Prompt Payment policy, it is contrary to public policy to knowingly enable a vendor/consultant to avoid declaring income earned so that the vendor could receive a benefit it would not otherwise be entitled to receive. In addition, in furtherance of transparent and accurate reporting of Fund finances, vendors should submit invoices on a timely basis upon completion of a receivable.

Lastly, the Fund should review whether it is in compliance with state procurement guidelines, as well as its own policies, as it relates to the [redacted] agreement. Although one of the services provided is accounting services, which arguably may negate the need to competitively bid for the service, [redacted] did not solely provide accounting services (e.g., rewrite of software, internal control reviews, etc.). Consideration should be given to whether its contract should be competitively bid out in order to ensure that the Fund is receiving the most value.

New York Thoroughbred Breeders, Inc.

According to its website, the NYTB was founded in 1974 and "formed in order to provide those individuals involved in the New York breeding and racing industry with an organization dedicated to the advancement of Thoroughbred breeding and racing in New York State."[94] One of its reported purposes is "conducting and coordinating activities with breeding and racing associations and agencies." This is accomplished by working in conjunction with a number of other stakeholders, including the Fund. The NYTB is currently overseen by a board of 11 members

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[92] It was suggested to Egan that she confer with an accountant or tax adviser regarding the practice.

[redacted]

[94] Contrary to Cannizzo's assertion at the August 2018 Fund board meeting, the NYTB could not have lobbied to create the Fund as the NYTB did not exist at the time the Fund was enabled by legislation.

and its day-to-day operation is managed by its Executive Director, Jeffrey Cannizzo, who is also a member of the Fund.[95]

The NYTB has a long-standing history of involvement with the Fund. This Office reviewed agreements between the Fund and the NYTB dating back almost two decades. In general, the terms of the contract remained the same except for pricing which typically increased over time. The most significant change in terms, however, was the 2017 addition of a clause allowing NYTB to retain any revenue generated from events. Currently, the Fund's contract extension with the NYTB is set to expire on December 31, 2018.

In sum, the agreement calls for the NYTB to perform the following services:

> NYTB, on behalf of the Fund, shall sponsor, arrange, structure, staff, and implement a wide range of promotional services designed to advance and promote the breeding of thoroughbreds throughout the State of New York, and the racing of those thoroughbreds, including, but not limited to, the publication and dissemination of information relating to the thoroughbred industry in New York State, such as the publication and distribution of industry brochures, directories, and a monthly newsletter; the sponsorship of New York-Bred Championship Awards and New York Bred stakes presentations; the sponsorship and/or promotion of New York-Bred Showcase Day, maintenance of outreach programs at various New York racetracks; the development and management of a promotional website with prominent links or portals to the Fund's website www.nybreds.com; management of social media websites promoting New York-Bred's; the promotion of New York-Bred's in industry publications and other advertising media; promotion of the Take2 Thoroughbred Second Career Program; the sponsorship of meetings, receptions, seminars and farm tours for potential or current industry participants, and the publications of annual stallion roster magazine. NYTB further agrees that it shall use its best efforts to promote the New York Breeding and Development Fund's Award Program and the New York Bred Racing program at national and regional sales and seminars. NYTB shall provide the Fund's executive Director with prior notice of all promotional activities performed by NYTB under this Agreement and, subject to applicable law, shall provide to the Fund a reasonable number of complimentary tickets to any event that the Fund subsidizes under this Agreement. Consistent with its longstanding practice, the parties acknowledge and agree that NYTB may sell products and/or raise and generate revenues from any event that it sponsors, including events that the Fund subsidizes.[96]

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[95] The NYTB's website identifies the following individuals as its members: [redacted]

[96] *See* Aug. 10, 2017 Fund Letter regarding renewal of Aug. 22, 2016 Agreement, annexed hereto as Exhibit "15A." A copy of the previous agreement is also annexed hereto as Exhibit "15B" for comparative purposes. Documents related to the NYTB contract are collectively referred to as Exhibit "15," with each document assigned its own letter.

The Fund's procurement policy allows for three different procurement methods which are also used by the State: competitive bidding, sole source, and single source procurements. Since 2000, the NYTB has been recognized by the Fund as a "Sole Source Provider." However, the Fund's definition of sole source is not consistent with the SFL or the OGS guidelines, as defined *supra*, as it does not state that the NYTB is the only vendor who can provide the services, but rather that it is the only one "suitably qualified." The Fund's Sole Source Provider Document related to the NYTB contract states that the Fund has long recognized the NYTB as "a sole source vendor with respect to the effective and efficient promotion of the thoroughbred breeding industry as contemplated by the Racing Law."[97] Additionally, the Board recognized "that (i) the mission of NYTB is substantially aligned with the mission of the Fund, and (ii) NYTB, as the statewide thoroughbred breeders association representing the majority of the breeders . . . is uniquely positioned to carry out, on a cost-effective basis, the measureable objectives of the Fund by advancing and the promoting the thoroughbred racing industry."[98] The Sole Source Provider Document lists the Fund's promotional objectives and states that the NYTB is "uniquely positioned to deliver" those objectives on behalf of the Fund.[99] Thus, the NYTB would more accurately be characterized as a Single Source Provider, though the Fund does not detail any other vendors it has considered.[100]

It is also important to note that some individuals reported to this Office that the Fund is mandated to retain the NYTB to perform the promotional and advertising functions for the Fund as the NYTB represents the majority of the breeders in the state. This erroneous belief may stem from the fact that the enabling statute for the Fund, which sets forth the composition of the Fund's board, requires that "the president or the executive director of the statewide thoroughbred breeders association representing the majority of breeders of registered thoroughbreds in New York State" be granted a seat on the board.[101] This Office found no statutory provisions mandating the Fund to use a particular party to provide services or goods.

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[97] *See* Sole Source Provider document, annexed hereto as Exhibit "15C." It should be noted that this document incorrectly cites Section247(e) of the PML which does not exist. Instead, it should have been noted as Section 247(2)(e). Moreover, this provision was renumbered in 2008 to Section 254(2)(e) of the PML. Should the Fund continue to designate the NYTB as a Sole Source Provider, then the document should be revised to accurately cite the statute it is referencing.

[98] *See id.*

[99] At the August 2018 Fund board meeting, a recitation of the NYTB's relationship with the Fund was provided by Cannizzo. He explained that the NYTB used to be the recipient of registration fees, but when the decision was made for the Fund to assume responsibility for the registry, the NYTB was awarded the promotional work as an offset to the loss in revenue. Additionally, at that meeting, Fund member McMahon stated that the retention of the NYTB to provide services also served as an avenue for the Fund to indirectly hire a lobbyist, which may be construed to violate Section 73(7-a) of the POL, discussed *supra*. It should be noted that the NYSEC Advisory Opinion No. 95-13 was asked to consider whether the Fund may continue to pay the NYTB a percentage of registration fees collected by the Fund when the NYTB *did not render any services*. (emphasis added), discussed *supra*.

[100] The single source procurement method would be most apt if the Fund sought to establish such a contractual relationship and not a sponsorship, discussed in detail *infra*. Interestingly, in a 2011 email from [redacted] to [redacted], [redacted] correctly referred to the need of a "single source" justification in order for the Fund to award the contract to the NYTB. *See* Dec. 29, 2011 Email from [redacted] (last email in string beginning Dec. 20, 2011), annexed hereto as Exhibit "15D."

[101] *See* PML §252(1).

Vendor Contract versus Sponsorship Agreement

By all appearances, the agreement between the Fund and the NYTB establishes a standard vendor relationship wherein the NYTB is also identified as a sole source. However, a review of records provided by the Fund and the NYTB, as well as descriptions of the work and relationship by various people, indicate otherwise. The records do not show that the NYTB is acting on behalf of the Fund or that the Fund is the intended beneficiary or recipient of the goods and services purchased by the NYTB. Rather, the Fund pays for the activities of the NYTB and then is allowed to advertise at events for free. The Fund is not a signator on any third-party vendor agreement or noted as the beneficiary of such agreements. The NYTB also pays the requisite taxes on all goods and services and does not utilize the Fund's exemption as a public benefit corporation from such taxes. Furthermore, the NYTB is allowed to sell tickets, products, advertising, or otherwise generate revenue at events and for print and electronic publications paid for by the Fund. The NYTB retains all the proceeds of those sales for its own benefit.

Although the Fund bears the entire cost of holding various events, it is widely acknowledged that the events are the NYTB's events and that the Fund is merely the sole or main sponsor of the event, in that the Fund's logo is present on publications, banners, and the like. Thus, this Office finds that to describe the NYTB as a vendor to the Fund is not only inaccurate, but also results in unmet expectations. Instead, the relationship is best characterized as a corporate sponsorship. In fact, Cannizzo explained that the agreement between the two entities as such and stated that the Fund "underwrites" and/or is simply the sole sponsor of events held by the NYTB. Further, the claim that the goals of the NYTB and the Fund are so closely aligned that one cannot tell if an event or activity was conducted in furtherance of the contract or merely as a part of the NYTB's mission is more evidence of a sponsor relationship. In a traditional vendor/vendee relationship, the benefits derived by the Fund would not be incidental or in conjunction with the NYTB, but rather wholly attributed to the Fund.

Merriam-Webster defines sponsor as "a person or an organization that pays for or plans and carries out a project or activity."[102] Corporate sponsorships are further defined as "a form of marketing in which a payment is made by a company for the right to be associated with a project or program."[103] The sponsor's logo and name may be displayed alongside of the organization undertaking the project or program, with specific mention that the sponsor has provided funding. Hence, the manner in which the NYTB secures goods and services in the performance of its contract most closely resembles a corporate sponsorship and not a "sole source provider."

More importantly, with corporate sponsorships, the sponsor is not responsible for paying the labor costs, or what the NYTB refers to as "professional fees," of the sponsored entity's employees. Here, the NYTB's professional fees comprise a significant portion of the contract amount. On the other hand, with traditional vendor/vendee relationships, all goods and services obtained are exclusively for the benefit of the vendee, and as such, labor costs would be included.

[102] *See* https://www.merriam-webster.com/dictionary/sponsor, last accessed Oct. 16, 2018.
[103] *See* https://www.investopedia.com/terms/c/corporate sponsorship, last accessed Oct. 16, 2018. *See also* https://www.inc.com/encyclopedia/corporate-sponsorship.html, last accessed Oct. 16, 2018.

Typically, a traditional vendor contract would include performance metrics to determine if the vendor is fulfilling its obligations. All costs incurred by the NYTB in the performance of the contract are offset by fixed monthly payments, not based on milestones or work accomplished.[104] In addition, the NYTB only provides select documentation on a quarterly basis to the Fund for review, though the Fund may request records from the NYTB to support the reported expenditures. The NYTB is also required to provide the Fund's Executive Director with prior notice of its promotional activities and regularly report on its endeavors and expenses.

Nevertheless, the NYTB's obligation to report to the Fund's Executive Director effectively places Egan in a difficult position to question or disagree with the activities of Cannizzo, to whom she reports, as he is a Fund member. It has been expressed to this Office by Fund staff that questions raised with Cannizzo regarding expenditures at times are met with an air of dismissiveness and that there is reluctance to challenge a member of the board. Further, Cannizzo is a member of the two committees that have direct involvement with allocating and determining promotional services and spending, namely, the Audit and Finance and Promotions Committees. Although Cannizzo recuses himself from voting on any matters that impact the NYTB, he is nonetheless in a position to influence other members of the committee and/or the course of action that is contemplated. It has also been expressed to this Office that, at times, Cannizzo's prominence on the board leave the staff believing that any effort to challenge the NYTB is futile.

Consequently, the Fund is merely an underwriter to many of the NYTB's endeavors rather than a vendee receiving services from a vendor. Further, the perception that the NYTB is held to a different or even lower standard of performance then other Fund vendors reasonably exists because Cannizzo, the Executive Director of the NYTB, is a Fund member. Moreover, Fund staff tasked with ensuring that limited resources are expended appropriately may become frustrated or feel conflicted in their effort to be diligent. This frustration may be further compounded by the awkward reporting relationship between the NYTB and the Fund's Executive Director.

<u>NYTB Expenses</u>

One of the most frequently cited concerns regarding the NYTB's agreement with the Fund revolves around the 2014 increase in the award amount from \$215,000 to \$400,000 and whether the increase was justified. The NYTB's 2018 contract rate remains at \$400,000. A review of the records demonstrates that between 2013 and 2014, the NYTB changed the manner in which it categorized its promotional activities and how spending was captured. For example, in 2013, with the exception of [redacted] labor costs for Cannizzo and [redacted] were captured in the category "Professional fees" and not attributed to specific line items as in 2014; and Association Dues and Partner Promotions were line items in 2013, but not in 2014, as those costs now appear to be attributed to Advertising. Presumably, the changes in NYTB's reporting was an effort to be more transparent about its spending.

According to the NYTB's 2014 Promotional Spend proposal, the NYTB requested an increase in its contract so that it may perform more services on behalf of the Fund, including new owner seminars and tours, Take2, additional promotional materials, brochures and flyers,

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[104] The monthly payment is simply the value of the annual contract paid in equal installments throughout the year (\$400,000/12 = \$33,333.33 per month).

additional advertising (e.g., print and radio), and social media (e.g., Twitter and Facebook). Yet, the estimated cost for the new activities was only listed at \$100,000. Moreover, these efforts are in addition to the preexisting services provided to the Fund, including website, e-newsletters, NY Stallion Directory, monthly magazine, and events (the five listed in the 2014 proposal are Awards, (two) Showcase Days, Sales, and Winter Pre-Breeding Season). These items were estimated to be \$300,000, an increase of \$85,000.[105]

In an effort to ascertain where and how the NYTB was spending the increase in contract price, a comparison of 2013 and 2014 expenditures was conducted.[106] Significantly, the review determined that \$182,764.02 or approximately 46% of the \$400,000 from the 2014 contract was used to pay for NYTB labor costs.[107] The second largest expenditure was for the various events that the NYTB organizes throughout the year, including the annual Awards Banquet, the annual Holiday Party, NY Showcase Days, and the Pre-Sale Cocktail Receptions.[108] Records disclosed that the NYTB hosted two additional cocktail parties in 2014. The number of attendees to the events appear to remain fairly consistent, with a slight uptick for the Showcase Day events. The cost of the events, however, increased and often went over the projected budget. However, since the NYTB's contract does not require the NYTB to spend only the amount budgeted for specific line items, it has the discretion to spend Fund monies as it sees fit without conferring with the Fund, and there is no mechanism for the Fund to object or otherwise comment. Further, although Cannizzo and others advised this Office that the NYTB did not charge the Fund for costs incurred in excess of the contracted \$400,000 amount,[109] the NYTB is able to offset any losses/overruns with revenue it generated from ticket sales and/or advertising related to the events.

The review also noted instances in which the Fund paid for expenses exclusively for the NYTB's benefit. Records related to the 2013 cocktail event contained notations that suggested that the charges were strictly related to a NYTB membership meeting.[110] Research revealed that the NYTB held its annual membership meeting at 10 A.M. the morning of the cocktail event, which commenced at 6 P.M. At least two of the expenses – a \$409.69 expense to set up chairs and tables on Friday night and scheduled to be dismantled after 1 P.M. on Saturday and \$151 for the purchase of breakfast platters – were attributed to the cocktail event. In 2014, the NYTB's third quarter Promotional Expenses and Accounting report captured a \$474.88 expense in the line item "Breeder Materials." This expense was paid by the NYTB via check [redacted] Supporting documentation indicated that the expense was related to a "Breeder Meeting/Educational Seminar," and the invoice from [redacted] stated that it was for

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[105] *See* NYTB 2014 Promotional Spend Proposal, annexed hereto as Exhibit "15E."

[106] A line by line comparison of expenditures was difficult as the NYTB revised the manner in which expenses were captured and reported between 2013 and 2014. Tables related to the NYTB's expenses are collectively referred to as Exhibit "16," with each table assigned its own letter.

[107] *See* Table of Professional Fees 2013-2016, annexed hereto as Exhibit "16A."

[108] *See* Table of NYTB Functions 2013-2014, annexed hereto as Exhibit "16B."

[109] Contrary to Cannizzo's assertions, January 2013 records indicated though that two charges totaling \$185.61 related to the 2012 Holiday Party were carried over and invoiced to the Fund even though the money paid to NYTB for contract year 2012 had been completely expended. *See* NYTB January 2013 Promotional Expenses & Accounting, annexed hereto as Exhibit "15F."

[110] *See* 2013 Cocktail Event Transaction Report and Receipts, annexed hereto as Exhibit "15G".

services rendered on August 24, 2014, the same day as NYTB's annual meeting.[111] This Office, however, could not find any evidence that an educational seminar was held on that day.

Lastly, the review also found instances where food and drink were attributed to events raised questions about their necessity and reasonableness, including the following:

Event	Event Date	Meal/Details	Transaction Date	Cost
2013 Awards Banquet	April 15, 2013	[redacted]	March 22, 2013	\$172.45
2013 Holiday Party	December 5, 2013		November 9, 2013	\$119.51
2013 Showcase Day	October 19, 2013		October 19, 2013	\$146.20
2013 Cocktail Event	August 10, 2013 (6 P.M. event)		August 10, 2013	\$151.00
2013 Cocktail Event	August 10, 2013		August 5, 2013	\$103.74
2013 Cocktail Event	August 10, 2013		August 6, 2013	\$102.67
2013 Cocktail Event	August 11, 2013		August 11, 2013	\$34.00
2014 Cocktail Event	August 9-10, 2014		August 4, 2014	\$63.00
2014 Cocktail Event	August 9-10, 2014		August 5, 2014	\$35.00
2014 Cocktail Event	August 9-10, 2014		August 5, 2014	\$54.01
2014 Cocktail Event	August 9-10, 2014		August 7, 2014	\$24.33
2014 Cocktail/Sales Seminar	October 5, 2014		October 7, 2014	\$67.78
			Total	\$1,073.69

In general, the review found that the increase in the 2014 contract price was largely spent on increased costs for labor, events, website, as well as new endeavors such as social media and Take2. Nonetheless, the review also found instances where expenditures were inappropriately borne by the Fund or which raised questions about their appropriateness. Subsequent to 2014, the contract amount remained at \$400,000, and a review of the 2015 and 2016 expenditures indicate that spending remained fairly consistent and that the NYTB continued to retain discretion as it pertains to the allocation of money to the various line items.

[111] *See* 2014 NYTB Third Quarter Promotional Expenses and Accounting Report, [redacted] Invoice, and Proof of Payment, and NY Breeder announcement of annual membership meeting, annexed hereto as Exhibit "15H."

In sum, the Fund should undertake a comprehensive review of its contractual relationship with the NYTB and determine if a sponsorship agreement would be a more appropriate vehicle for achieving its promotional objectives. Additionally, the Fund's procurement policy should be revised to be consistent with the SFL and the OGS guidelines with respect to sole source and single source vendors, especially if the Fund wishes to continue the vendor/vendee relationship with the NYTB. As noted above, the NYTB is not properly deemed a sole source vendor, nor has the Fund endeavored to determine whether there are any other vendors available, as would be necessary for a single source finding. Nonetheless, if the Fund opts to retain the NYTB as a vendor, it would be prudent for the Fund to competitively bid out the contract as suggested by the OSC.[112] Lastly, the Fund should also undertake a review of the contract terms to ensure that it serves the Fund's best interests.

Key Interviews

Tracy Egan, Fund Executive Director[113]

Discretionary Spending – Credit Card Usage and Aftercare Programs

Egan stated that credit cards are issued to her, [redacted] and the field investigators. She could not specifically recall what the Fund's credit card policy stated off-hand, but surmised that it is based on "common sense" noting that it should be "something for the Fund" and "a reasonable cost." Egan added that the credit cards have a modest limit "probably \$5000" and that anything over that threshold requires board approval.[114] The charges and supporting documents are reviewed by [redacted]

Egan explained that the Fund credit card is used to purchase lunches or catering services perhaps "twice a year" when the "guys from down below" travel to the office for staff meetings. She also acknowledged that she paid for board members to have lunch, as well as a "lunch and lecture" series for Fellowship recipients and guest speakers at [redacted] a local restaurant near the track. Egan was questioned if alcohol was purchased with the meals, and she recounted a board meeting held at Belmont Park on Showcase Day. She recalled that the former Comptroller [redacted] was furious when he received the bill because the board members had ordered multiple glasses of Johnny Walker Blue, an expensive scotch. Following that incident, Egan informed the board that the Fund would continue to pay for meals, but not alcohol. While Egan acknowledged that the Fund had no policy regarding the purchase of alcohol, she agreed with [redacted] that the public would not be pleased if they thought she was having a "three martini lunch" with Fund money.

Egan asserted that she had conferred with the Joint Committee on Public Ethics ("JCOPE") regarding the purchase of lunches, but her inquiry was limited to food for board meetings. She

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[112] As discussed *infra*, the OSC also made this recommendation on two separate occasions following audits of the Fund.

[113] Statements made by Egan pertaining to her outside employment, the sponsorship and fellowship programs, and [redacted] will not be repeated here as they were incorporated into the relevant sections *infra*.

[114] As noted *supra*, only those items in excess of \$25,000, if an expense stemming from the Promotions Committee, requires full board approval.

claimed to have been advised that such expenditures were permissible provided that the meetings are public, and the food is also made available to the public. Egan's query to JCOPE did not address whether it is appropriate for the Fund to pay for meals taken by its members outside of the public meetings or for the "lunch and lecture" series.

Egan conceded that the Commission's [redacted] determined that the Fund's statutory authority prohibits the Fund from making donations to aftercare facilities. Nevertheless, Egan stated that aftercare is a public concern and consistent with the Fund's mission. Purportedly, the ABO advised the Fund that over the course of time the mission of the Fund can, and may, change. Egan commented that the Fund's board has to make the difficult of choice of finding money in the budget to support aftercare even if it has to come from the 10% holdback and opined that the Fund should "give till it hurts." Egan, however, claimed that the Fund did not make donations to such entities, but instead, the Fund "advertises" at aftercare functions for promotional purposes. Such agreements are entered into with the Fund's share of the promotional budget and not through the NYTB contracts, with the exception of Take2. Egan explained that she would survey aftercare organizations to determine how many horses were saved and adopted to determine to which aftercare organizations the Fund would "distribute" money.[115]

Egan was specifically asked if there has been any discussion with the board that the promotional efforts involving aftercare facilities may be construed to be contrary to [redacted] opinion. Her explanation did not suggest that there was any discussion, but she indicated that the Fund's outside counsel advised that the Fund could continue to contribute to aftercare programs through the promotional budget.

Procurement Practices – New York Thoroughbred Breeders, Inc.

Promotional activities are undertaken by the NYTB, as well as by the Fund. Egan explained that the NYTB is responsible for organizing the events, while the Fund is responsible for advertising in periodicals (i.e., BloodHorse, Daily Racing Form, Thoroughbred Daily News), and media (i.e, radio and social media).[116] Egan explained that the NYTB's contract is paid out of the Fund's promotional budget, which is generally set at \$500,000 to \$600,000 annually or 5% to 6% of the Fund's budget. She stated that the same contract between the Fund and the NYTB had been used for several years and contains no benchmarks. According to Egan, neither the board, the promotions committee, and/or Fund counsel, have discussed or raised the possibility of revising the terms and conditions of the contract, as no one sees a problem with it.

[115] Egan expressed her reservations about how effectively the NYTB is performing this function. She stated that there were years where donations were made to Take2, and the Fund did not receive any recognition. Egan also cited an instance wherein the NYTB had represented to the Fund that it would donate either \$10,000 or \$20,000 of Fund monies for promotional activities to Take 2, but Egan saw that the line item budgeted for the expense had decreased by \$7,500 before any money was actually given to the program. Egan stated that when she inquired of Cannizzo, he retorted that there was a lot of work involved with the program, including meetings. Subsequently, though, Egan learned from NYTHA that the meetings were conducted over the telephone. Consequently, Egan instructed [redacted] to inform NYTB that such "antics" would not be tolerated.

[116] Social media efforts are taken in conjunction with the NYTB. It should be noted that the NYTB, using the Fund's monies, also advertises in the same periodicals as the Fund.

Egan recounted that in 2010, NYTB's contract was $125,000, but in 2014, the contract amount essentially doubled overnight going from $215,000 to $400,000.[117] Egan relayed that, in 2013, she was dismayed to learn from Cannizzo that NYTB would be receiving an increase in its contract. She claimed to have expressed her concerns to the board[118] about the increase in contract price as the matter was not presented to the audit and finance committee, nor was her input solicited. She was also unsure what increase in services would be afforded to the Fund. Egan added that the Fund could only audit those expenses incurred on behalf of the Fund, noting that questions about expenses were usually dismissed. She further stated that Cannizzo had received large bonuses from the NYTB and surmised that the bonuses were funded with the increase.

Egan was asked why other vendors were not considered for the promotional contract, and she explained that since the NYTB represents the majority of the breeders in the state, it is designated as the sole source provider of such services. When this Office indicated that the requirement regarding representation of a majority of the New York breeders pertained to a seat on the board and not the promotional contract, Egan replied that she was not aware of such a distinction and that the NYTB has always been awarded the contract. Egan was vague when asked how she came to believe that NYTB was the only viable vendor. However, she stated that everyone, including [redacted] is under the impression that it was necessary for the vendor to be a representative of the majority of breeders in the state.

Egan described her relationship with Cannizzo as having improved, but that she still cannot get "an answer out of him." There are also questions as to which "hat" Cannizzo is wearing (Fund member or NYTB Executive Director) when she speaks with him. Egan relayed that there were occasions where she emailed Cannizzo in confidence about Fund matters, but he shared her emails with the NYTB's board. [redacted] She also expressed concern about Cannizzo's position on the New York Racing Association ("NYRA")'s Board and the potential for conflict, as the Fund gives NYRA money for purses, and Cannizzo is a voting member of the Fund.[119] Egan believes that Cannizzo has competing fiduciary obligations and is not confident that the Fund will always be his first priority.

Egan seemed skeptical that the Fund's money was used solely for promoting the Fund. She stated that one year, Cannizzo reportedly spent $80,000 on advertising for the Fund, which she questioned because the advertising efforts did not support his claim. That same year, Egan learned that Cannizzo had instructed vendors not to print the Fund's phone number and to use the NYTB's instead since "no one knew what the Fund was anyway." Egan stated that she informed other members of this, but Cannizzo got along well with the other members; thus, her comments and concerns went (and often go) unheeded. The recent changes to the Board, including the appointment of a Chair, however, seem to have alleviated the problem.

[117] In 2010, NYTB's contract price was approximately $195,000 and based upon a fixed percentage (45% in 2010) of the Fund's promotional budget. In 2011 the contract price was fixed at $215,000, $300,000 in 2012, $215,000 in 2013, and has been set at $400,000 since 2014.

[118] This Office found emails detailing Egan's concerns for NYTB's contract price increase in 2012 from $215,000 to $300,000, but did not find documentation as it relates to the 2014 increase to $400,000.

[119] Although Cannizzo is not a voting member of the NYRA board, he should be reminded of the potential for conflict and recuse himself from voting on matters before the Fund which pertain to NYRA.

Egan discussed NYTB's performance in detail, including the services that the NYTB provided and reported under the expense categories of website, e-Newsletter, Breeder Magazine, and events. According to Egan, the NYTB had attempted to "purloin" the Fund's website (NYbreds.com) as their own. She stated that she informed Cannizzo that the Fund's website was copyrighted and "took it back." Egan commented that it was difficult for one to navigate from the NYTB's website to the Fund's, but conversely, it was easy to navigate in the reverse. Egan stated that there are no agreements as it relates to the website, including how or what information is used, whether the information is proprietary, or if the Fund is entitled to a share of revenue generated by the NYTB's site. Egan stated that the material posted on the NYTB's site is the same as the Fund's, with links back to the Fund's site for awards information. She also claimed that with the exception of the YouTube videos, the other material posted on the NYTB's site are items the NYTB copied and pasted from the Fund. She added that everything on the NYTB's website is about the NYTB although it is paid for with Fund money. Egan stated that she had complained for months before Cannizzo relented and posted the Fund's logo on the NYTB's site. She also expressed her annoyance with the NYTB copying data and materials from the Fund and presenting it as their own. Egan commented that she once advised Cannizzo that "he should give credit where credit is due."

Egan could not explain why the Fund subsidizes the NYTB's website other than to say that the Fund is "advertised" or "promoted" on it. She clearly felt though, that it was not fiscally prudent for the Fund to pay NYTB for this service. Egan was also unaware of what the NYTB reported to the Fund as it related to the NYTB website and speculated that the NYTB was charging for things unrelated to the Fund. Egan reiterated that if the Board gives the NYTB the authority to do what it does, and Cannizzo himself is a member, it is difficult to challenge any of the NYTB's actions.

Similarly, Egan stated that there has also been no discussion regarding the material contained in the NYTB's e-Newsletter, including what is disseminated, what the Fund is paying for, and if the Fund is entitled to any of the revenue generated by the newsletter. Likewise, Egan said there was no discussion between the Fund and the NYTB regarding the NY Breeder's Magazine's content, costs, and revenue. The Fund does not have proprietary rights to any material used. Egan explained that the NYTB utilizes their own mailing list to distribute the magazine, and the list is not shared with the Fund. The Fund, however, receives "free" advertising in the magazine, which is distributed locally and nationally.

Egan stated that the Fund has always been a "sponsor" of the NYTB events as opposed to an organizer even though the Fund pays for the entire cost of the event. She admitted that Cannizzo has been successful in increasing attendance at the events, but added that the NYTB is also able to generate revenue from ticket sales to these events. Egan expressed frustration with the Fund's inability to see the NYTB's books or knowing how much revenue has been generated from ticket sales.

Throughout her interview, Egan expressed concerns about the NYTB contract and questioned whether it served the Fund's best interest. She repeatedly stated that the Fund's inability to conduct an in-depth review of the NYTB's finances left her skeptical that the money was utilized solely for the Fund's benefit.

Jeffrey Cannizzo, Fund Board Member and Executive Director of the NYTB

Cannizzo stated that his family has been involved in the horse racing industry for many decades, but although he was knowledgeable about racing, he had never worked in the industry until he assumed the Executive Director position for the NYTB in July 2008. Prior to that, Cannizzo worked in digital advertising in New York City.

Cannizzo described his role as the NYTB Executive Director as running a small business that is a membership organization. The primary mission of the NYTB is to promote and grow horse breeding in New York State, which it does by conducting several seminars each year, including educational seminars on ownership, breeding, and healthcare of foals and horses. The NYTB has approximately 750 to 900 members comprised of both New York residents and others, but the number fluctuates year to year. Cannizzo reports to the NYTB's board and has a small staff, comprised of [redacted] and [redacted] to assist him with his responsibilities. Cannizzo stated that he does not own any horses.

Cannizzo explained that he is a member of the Fund by operation of statute as Executive Director of the NYTB. Cannizzo has also been a member of the Fund's Audit and Finance and Promotions Committees for about five years. The Audit and Finance Committee's function is to provide budget and financial controls for the Fund, and its members are Graziano, McMahon and Cannizzo. The Promotions Committee is responsible for determining how best to use the Fund's promotional budget to promote breeding in New York, and the other members are Wilmot, McMahon, and Egan.[120]

Cannizzo stated that the Fund had contracted with the NYTB long before he became Executive Director of the NYTB. He noted that the Fund does not have the resources to perform all the necessary promotional activities themselves. As a result, the effort is "divided" between both entities. The Fund is responsible for radio, online, and print advertising, as well as the scholarship program. The promotional services currently provided by the NYTB include a website, social media, a monthly NY Breeder Magazine, an annual stallion directory book, a weekly e-Newsletter, a national owners conference, an annual awards event, Showcase Day events, pre-sale events, and a holiday party. He added that there is also a small line item involving advertisements placed with thoroughbred industry magazines. Cannizzo acknowledged that there is nothing in the statute that requires that the Fund have a promotional contract or that the NYTB perform the service. Remarkably, he candidly stated that the NYTB does not have the resources to conduct and/or maintain many of its activities and events without the sponsorship of the Fund.

Similar to how Egan manages her promotional budget, the NYTB has discretion as to how much is expended for goods or services provided, but a promotional proposal with a budgeted amount for each line item is provided to the Fund's promotions committee for review and approval. If approved, the proposal is then presented to the Fund's full board for a vote. Cannizzo stated that he recuses himself from voting on any matters relating to the award and execution of the NYTB's contract, including the declaration of the NYTB as a sole source provider.

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[120] Cannizzo was unsure if member Phil Birsh had been appointed to the Promotions Committee.

Cannizzo stated that the NYTB is a sole source provider because it has the same exact mission as the Fund, namely, to promote breeding in New York State. He explained that in most other states, the trade association is responsible for both promoting the industry and administering the awards program. In New York, however, the duties are "divided" among the NYTB and the Fund. Cannizzo was asked how the NYTB segregates services provided for the Fund versus the services provided for its membership, and he responded that they are "one and the same" adding that the NYTB members are the very people that the Fund is targeting to promote breeding. Hence, the activities between the two entities are often intertwined and that the promotional events are for the benefit of both the NYTB and the Fund.

Nevertheless, Cannizzo acknowledged that the Fund is responsible for all the expenses of the NYTB's events, but the revenue from ticket sales belong exclusively to the NYTB.[121] (Tickets are sold for all the events with the exception of the Fall Sales event which is free). In return, the Fund is identified as a sponsor in all of NYTB's advertising for those events. He cited four different events held annually, including the awards ceremony, which honors the best performing horses and takes place in Saratoga every April and attended by over 200 people; three Showcase Day events, which usually take place on big race days, and attended by 20 to 45 people; two pre-sale events at Fasig-Tipton which are typically attended by 200 plus people; and the holiday party which is attended by about 150 people.[122] The NYTB uses direct mailings, electronic mailings, and social media to advertise these events locally and nationally. Food and beverages are provided by local catering companies, and the budget is set based on historical data.[123]

Cannizzo stated that in addition to those social functions, the NYTB also promotes breeding and the Fund on the NYTB website, while also providing the public with statistical data, videos, articles, and leaderboards. The costs associated with the website, including maintenance and web development fees, staff writing, statistical data (purchased from the Jockey Club) are paid for by the Fund. Cannizzo was unsure if the NYTB's website licensing and domain/hosting fees are also underwritten by the Fund, but this Office determined that the expenses were accounted for and attributed to the Fund's contract. The NYTB's Stallion Registry is also available on the website and maintained and updated by [redacted] Cannizzo explained that the NYTB purchases data from BloodHorse utilizing money from its contract with the Fund, and the information is uploaded into the registry. The registry is unique to the NYTB, and the Fund does not offer anything similar. Revenue is generated from advertising on the website, but similar to ticket sales for events, the NYTB retains all advertising income despite its website being wholly subsidized by the Fund.

The NYTB's publication, NY Breeder Magazine, is issued monthly and provides statistics, breeder profiles, and information about awards distributed by the Fund. The magazine is largely authored by [redacted] but some of the articles are outsourced. The NYTB accepts advertising in the magazine at fixed rates. The magazine is provided to both members (free of charge) and non-

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[121] Cannizzo explained that this understanding regarding ticket sales revenue "has been this way forever" and is reflected in the contract. However, as noted *infra*, only the NYTB's most recent contract mentions this arrangement.
[122] In the summer, the NYTB also operates a promotional booth at Saratoga. Cannizzo stated that the NYTB employs temporary help for approximately six weeks and that information about the industry and the Fund is provided to the public.
[123] Cannizzo also stated that alcoholic beverages are provided at all of these events and included in the catering fee paid for by the Fund. When asked if it was an appropriate expense for the Fund to bear, he replied that he has never received any indication from the Fund that it was not, nor is he, as a Fund board member, aware of it being an issue.

members (at a subscription fee) of the NYTB. Cannizzo stated that the magazine has grown due to the Fund's support. In fact, the magazine would not be distributed at all without the Fund, as it underwrites the entire publication. The NYTB generates revenue from advertisements in the magazine, except from the Fund. Again, all revenue generated from the advertising belongs to the NYTB. The Fund is also promoted via the NYTB's e-Newsletter. The e-Newsletter is sent out in a weekly email blast to all those who signed up to receive it and is one of [redacted] primary responsibilities.

When asked why all the print and digital publications discussed above are owned by the NYTB instead of the Fund. Cannizzo responded that the question was never raised and asserted that the Fund is saving money by using the NYTB's services. Further, although only 40% of the Fund's promotional budget is awarded to the NYTB, a lot of work is being done, and the Fund's board has had nothing but praise for the NYTB. When asked about the 2014 increase in the NYTB's contract, Cannizzo explained that the increase in the contract amount allowed the NYTB to provide additional services, such as the website, e-Newsletter, the publication of nationally distributed NY Breeder Magazine issues, social media, and additional Showcase Day and pre-sale events. He added that the items are labor intensive and that prior to the increase, the NYTB's services were a much smaller effort. In sum, Cannizzo opined that the NYTB has executed its contract with the Fund flawlessly. He also reiterated that the NYTB's interests are uniquely aligned to that of the Fund, that the NYTB has a direct connection to the Fund's target audience, and that the two entities work together seamlessly.

Board and/or Audit and Finance or Promotions Committee Members

Interviews of board and/or audit and finance or promotions committee members revealed that the board is very pleased with the NYTB's performance, and all opined that Cannizzo is doing an excellent job promoting the Thoroughbred industry.[124] The members reported that Cannizzo provided updates on the NYTB's efforts at every Fund and committee meeting and is very responsive to questions, as well as the Fund's needs, despite the absence of metrics or deliverables in the contract. In addition to the NYTB's regular reporting and the requisite board approvals, some members opined that there is much oversight from the Commission and the Governor's Office, suggesting that the NYTB's contract is closely monitored and that the Fund's business is transparent.

The members stated that the NYTB is performing work that the Fund could not do itself due to a lack of resources or skill set. Some members added that it was easier to hire the NYTB to perform certain functions, as there are less restrictions on their ability to do things such as lobbying, donating to aftercare programs, and hosting events that serve alcohol. As it relates to the Fund's decision to declare the NYTB as a sole source provider, the members responded that it was a legal determination for which they relied on counsel and added that it was difficult to find another entity to take on the amount of work the NYTB does. Equally important to the members is that there purportedly is no other entity that has the ability to reach as many people in the industry as the NYTB.

[124] Interestingly, the members often spoke of what the NYTB and Cannizzo were doing for the industry as a whole and not specifically for the Fund.

The members were asked about the Fund's decision to be the sole sponsor of the NYTB events and for allowing the NYTB to retain revenue generated from events and publications (print and digital) paid for by the Fund. One member offered that the contract has always been that way, s/he was not involved in the day-to-day minutiae, and s/he believed that the NYTB did a good job. Some members responded that the revenue generated is small and ultimately ends up benefitting the same causes. At least two members, however, indicated that they were not aware of the agreement regarding ticket sales revenue and indicated the need for further review. One of the two also pondered the possibility of using the revenue as an offset to the contract price.

Regardless, the members described the Fund as a "pass through" for funding that has been doing well without interference from "outsiders." One member opined that individuals who do not have any involvement or true understanding of the Fund often have an opinion and want to meddle, while another recited the old adage "if it ain't broke, don't fix it." The members generally believe that it is more effective and economical to outsource promotional activities to the NYTB. In fact, one member opined that if s/he had to choose between the Fund and the NYTB, s/he would opt to have the NYTB handle everything. Conversely, one member opined that it is preferable that the State be involved via the Fund, as it would ensure more scrutiny, better management, and less self-dealing.

Office of the State Comptroller Audit Reports

The OSC conducted three audits of the Fund resulting in reports being issued in 1995 (Operating and Reporting Practices), 2004 (Internal Controls over Financial Operations) and 2011 (Selected Operating Practices).[125] It is important to note that two of the three OSC audits specifically referenced the Fund's contract with NYTB and expressed concern with whether the Fund is deriving the most benefits from the money expended on this contract. The OSC has recommended on both occasions that the promotional contract be bid out to address this concern.

The 1995 audit scope encompassed the time period of January 1, 1991, through September 20, 1996, and primarily focused on whether the Fund properly reported on its operation and if the Fund's activities had positively impacted the industry. Further, as a part of this audit, the OSC also undertook a review of the Fund's promotional activity and its contractual relationship with the NYTB. The OSC noted that the promotional activities conducted by both the Fund and the NYTB appeared to overlap in areas and raised questions about the efficiency of the arrangement. The OSC pointed out that the Fund did not properly monitor its contract with the NYTB to ensure that the NYTB was fulfilling its obligations. Notably, the OSC determined that the Fund failed to solicit bids for the contract, but instead, entered into a direct negotiation with the NYTB.[126] Additionally, the OSC found that the Fund's annual report failed to meet statutory mandates and that the Fund's revenue was not properly reported.

[125] *See* OSC 1995 (Operating and Reporting Practices), 2004 (Internal Controls over Financial Operations) and 2011 (Selected Operating Practices) Reports and follow-up Reports, annexed hereto as Exhibits "17A1," "17A2," "17B1," "17B2," and "17C," respectively.

[126] In its response to the 1995 audit, the Fund asserted that its promotions committee, as a part of a routine procedure, solicited bids from qualified firms and reported back to the Board regarding bids. This Office, however, did not find any evidence of a bid process as it relates to any contract the NYTB has been awarded and has been consistently informed that the NYTB has been awarded a contract without the use of any bid process.

The 1999 follow-up of the 1995 audit report found that the Fund implemented all of the OSC's recommendations, with the exception of two things: the solicitation of bids for the promotional contract and a comprehensive timekeeping system. In response, the Fund averred that it did not seek bids because it believed that the NYTB was best suited to perform the task. Consequently, the OSC again raised its concern regarding whether the Fund had obtained the best available services for their money adding that "soliciting new ideas and approached through competitive bids from other qualified firms helps ensure that the best services are obtained at a reasonable price."[127] The Fund did not provide a response as to why a timekeeping system had not yet been implemented.

The 2004 OSC audit focused primarily on financial internal controls. In sum, the OSC found severe deficiencies in internal controls the Fund had over its financial operations, such as the absence of separation of duties and the failure to audit or reconcile revenue streams. The OSC also cited the absence of policies and procedures and noted that in two instances payments in excess of $5,000 were made to vendors in the absence of a contract and board approval. The 2008 follow-up audit report found that the Fund made significant strides in improving internal controls, including obtaining board approval for contracts and that only one of the 20 recommendations was not addressed, namely, the recording of registry fees as revenue.[128]

The 2011 OSC audit focused upon select operational practices including the Fund's internal controls over revenue and the propriety of certain expenses. The OSC's review also encompassed whether the Fund had been properly receiving revenue from the race tracks, the OTBs, and the video lottery terminal operators. Ultimately, the OSC determined that NYRA had been utilizing the incorrect retainage rate for exotic bets, and thus, had improperly withheld in excess of $7 million from bettors. Subsequently, the OSC informed the RWB of its finding, and the RWB took immediate corrective action with NYRA and directed it to reimburse the bettors.[129]

The OSC also noted that the NYTB's contract for promotional services increased to $300,000, and although it submitted quarterly financials to the Fund, the reports lacked sufficient detail to ensure that "the money the Fund is paying to NYTB is spent in the best interest of the Fund." The OSC also commented that if the NYTB continued to resist the addition of an audit clause in its contract with the Fund, it should consider placing the contract out for bid.

Findings

This review determined the following:

1) The Fund's Audit and Finance and Governance Committees, consist of less than three independent members and are not in compliance with Sections 2824(4) and (7) of the Public Authorities Law.

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[127] *See* Exhibit "17A2."

[128] *See* Exhibit "17B2." According to correspondence dated February 7, 2013, from the Fund to the OSC, a resolution was passed at the January 2013 board meeting to report all registration and advertising fees as distributable revenue. *Ibid.*

[129] *See* Exhibit "17C."

2) The Fund exercises great discretion in the distribution of its funds in furtherance of its mission, but does not have crucial policies to govern such activities, including policies addressing the use of discretionary funds for its scholarship and fellowship programs, sponsorships, meal expenditures, and travel.

3) Interested members failed to comply with New York State Ethics Commission Advisory Opinion No. 95-13 and did not recuse themselves from voting on the distribution of supplemental awards that yielded a direct financial benefit to themselves or family members. This conduct may also be construed to be a violation of Section 74 of the Public Officers Law.

4) Fund Executive Director Tracy Egan did not enter into an agreement with the Fund to voluntarily abstain from accepting breeders awards. In August of 2010, the New York State Commission on Public Integrity advised that Egan could continue with her activities as a breeder and as a real estate broker. Further, executive session notes retained by the Fund's Counsel, [redacted] revealed that Egan did not wish to forego her awards or outside employment. Although Egan offered the possibility of donating her awards to a charity, there was no further indication this option was pursued by either Egan or the Fund.

5) There is no evidence that Egan violated any provision of the Public Officers Law while engaged in her breeding or real estate business.

6) There were no irregularities noted as it pertains to the use of the Fund's credit cards, including its Exxon, Sunoco, and Bank of America Visa accounts. However, the review noted that Egan's use of the credit card for food and drink raised questions of necessity and appropriateness. Specifically, it was determined that Egan used the Fund's credit card on 46 occasions for expenses ranging from \$4 to \$334. Three of these charges included the purchase of alcohol, several for incidentals such as a bottle of water or soda, as well as others for meals that did not include the requisite information or justification.

7) There are no policies pertaining to the Fund's scholarship and fellowship programs, nor is there a formal application process. Instead, the Fund relies completely upon the schools to select recipients for the programs. Further, the Fund does not require that the school maintain documentation of its selection process which greatly increases the potential for fraud and abuse within the programs. This review found three students who received scholarships twice, and one recipient who was a first-year student.

8) Although the Fund is arguably in compliance with its stated mission and not openly involved in aftercare programs, its promotional activities and sponsorships of aftercare organizations is contrary to the opinion rendered by the Commission that the Fund's use of its monies is strictly limited to those items specified by the legislature, in that, these expenses do not comport with the spirit of its mandate.

9) In 2009, before Egan's employment with the Fund, she met [redacted] when she sold [redacted] Subsequently, in 2011, Egan hired [redacted] as a part-

time administrative assistant, but [redacted] responsibilities expanded to fill the void left by personnel changes/shortages within the Fund.

10) It was at the Fund's suggestion that [redacted] established her company, [redacted] and became a vendor to the Fund. [redacted] has been providing services to the Fund pursuant to a contract executed in 2012 and which continues in perpetuity. Throughout this period, [redacted] has never been declared a sole or single source provider, nor has an exemption, if applicable, to the procurement process been obtained. Further, although the company has been paid in excess of $25,000 for multiple years, the contract has never been subjected to the competitive bid process.

11) Although the Fund did not violate its prompt payment policies, it knowingly allowed [redacted] to delay invoicing for services rendered in the third and fourth quarters of a year, until the following year to enable her to avoid earning income that would result in a reduction to her social security benefits.

12) The New York Thoroughbred Breeders, Inc. ("NYTB") is recognized as the "statewide thoroughbred breeders organization representing the majority of breeders of registered thoroughbreds" in New York, which grants the NYTB a seat on the Fund's board pursuant to the Laws of New York, Chapter 282 of the Laws of 1994. Notwithstanding, this designation only provides for representation on the Fund's board, and there is no statutory mandate that the NYTB also be awarded a contract with the Fund.

13) The NYTB's contractual relationship with the Fund is more appropriately characterized as a sponsorship and not that of a vendor/vendee. The monies derived from the promotional contract is used to wholly subsidize the NYTB's activities. These activities serve to benefit the NYTB members and the thoroughbred industry and not just the Fund. The NYTB's contract with the Fund contain no metrics, and there is no indication that the NYTB is providing services as an agent of the Fund or that the Fund is the intended recipient of the goods or service.

    In fact, there were clearly expenditures made by the NYTB under the contract that was for the sole benefit of the NYTB's membership. For example, there were costs associated with the NYTB's membership meeting (e.g., breakfast platters and chair and table rentals) which were charged against the Fund's contract. There were also meal expenses incurred by the NYTB that were associated with events that were questionable (e.g., multiple meals attributed to a single cocktail event).

    The mischaracterization of the relationship between the Fund and the NYTB creates unmet expectations for the Fund and result in the Fund employees feeling frustrated over their inability to monitor or control the contract as they would normally deem appropriate for a vendor.

14) The NYTB generates revenue for itself from activities and events wholly subsidized by the Fund.

15) The reporting relationship between the NYTB and the Executive Director of the Fund is awkward at best, because Cannizzo is the executive representing the NYTB and also a Fund member to whom Egan reports. Moreover, as a result of his position as a member on the Fund board and committees, Cannizzo has considerable influence over other members further frustrating the Fund staff and their efforts to monitor the contract.

16) In 2014, the NYTB's contract was increased by \$185,000 or approximately 86%, from \$215,000 to \$400,000. This increase was reportedly to enable the NYTB to provide more services and organize more events. While the NYTB hosted two additional events, almost half or approximately 46% of the \$185,000 was used to fund an increase in the NYTB's labor costs.

    Essentially, if the contract had been treated as a sponsorship, the Fund would not have been responsible for labor costs and could have negotiated for more promotional opportunities instead.

17) Irrespective of the mischaracterization of the NYTB's contractual relationship to the Fund, the NYTB has been improperly designated as a sole source vendor contrary to the State Finance Law and OGS guidelines and awarded contracts in excess of the Fund's discretionary threshold without being subjected to the competitive bid process.

18) In two of the three audits conducted by the OSC of the Fund, the OSC specifically referenced the NYTB contract and expressed concern as to whether the Fund is deriving the most benefits from the money expended on the contract. Further, OSC on both occasions recommended that the contract be competitively bid out to address this concern.

Conclusion and Recommendations

As a result of the above findings, it is recommended that this case be closed as substantiated in part. This review found that although there was no evidence to support malfeasance and/or misappropriation of the Fund's assets, there are significant weaknesses in the Fund's operation and procurement practices which create corruption hazards. For example, the absence of crucial policies addressing the use of discretionary funds allow for subjective determinations as to how much money is sufficient or what causes/programs are appropriate to support. This review also determined that the contractual relationship between the NYTB and the Fund raises questions and concerns about its intended effect (i.e., sponsorship versus vendor) and whether it is in the best interest of the Fund to continue to award the promotional contract to the NYTB without a formal bid process. It was also further determined that certain Fund members were engaged in conduct that may be deemed to be in violation of Section 74 of the Public Officers Law in that, interested members were voting on the distribution of supplemental awards that would knowingly yield a direct financial benefit to themselves or family members.

Accordingly, the following is recommended:

1) The Fund should undertake a comprehensive review of its current policies to ensure compliance with state laws, rules, and regulations, as well as accuracy, clarity, and completeness. The Fund should also promulgate additional policies as it pertains to the discretionary distribution of its funds, including but not limited to, credit card use, travel, scholarship and fellowship programs, and sponsorships.

2) Fund members, officers, and employees should be regularly reminded of the prohibitions on conflicts of interest and their fiduciary obligations to the Fund. All agents of the Fund should disclose if they have any personal or financial interests in a matter that is before the Fund and should advise if anyone associated with the Fund is acting or making decisions that violate its statutes, by-laws, and/or policies and procedures.

   Most importantly, interested Fund members should recuse themselves from voting on supplemental awards when they stand to directly benefit.

3) The Fund should consider whether additional reporting measures are necessary to ensure that all employees engaged in outside employment, including Egan, are not in conflict with their employment by the Fund.

4) The Fund should seek a legal opinion as to whether the distribution of money to aftercare organizations, even if "promotional," is consistent with the Commission's determination that the expenditure of Fund monies is limited to supporting only those items delineated in statute.

5) The Fund should review its contractual relationships with [redacted] and the NYTB, including the use of a competitive bid process. With regard to the NYTB, the Fund should determine what manner the nature of its contractual relationship should be, whether vendor/vendee or as corporate sponsorship.

6) As it relates to those members who previously voted on the distribution of supplemental awards and knowingly reaped a financial benefit, they should be referred to the Joint Commission of Public Ethics for further review.