

**PENNSYLVANIA HARNESS
HORSEMEN'S ASSOCIATION
Lemoyne, Pennsylvania**

**FINANCIAL STATEMENTS
December 31, 2012 and 2011**

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Independent Auditor's Report

Board of Directors
Pennsylvania Harness Horsemen's Association
Lemoyne, Pennsylvania

Secretary
Pennsylvania Office of the Budget

Report on the Financial Statements

We have audited the accompanying statement of financial position of the Pennsylvania Harness Horsemen's Association, a nonprofit membership corporation, (the Association) as of December 31, 2012, and the related statements of activities and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Association's management.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the 2012 financial statements referred to above present fairly, in all material respects, the financial position of the Association as of December 31, 2012 , and the change in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Supplemental Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The supplemental information listed in the table of contents is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Other Matter

The financial statements of the Association as of December 31, 2011, were audited by other auditors whose report dated March 26, 2012, expressed an unmodified opinion on those statements.

A handwritten signature in cursive script that reads "CliftonLarsonAllen LLP".**CliftonLarsonAllen, LLP**

Baltimore, Maryland
April 3, 2013

FINANCIAL STATEMENTS

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
STATEMENTS OF FINANCIAL POSITION
December 31, 2012 and 2011

	2012	2011
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 239,394	\$ 389,327
Accounts receivable	46,501	42,407
Prepaid expenses	<u>164,103</u>	<u>126,220</u>
Total current assets	<u>449,998</u>	<u>557,954</u>
FIXED ASSETS		
Furniture and equipment, at cost	107,884	106,241
Less: accumulated depreciation	<u>70,584</u>	<u>57,379</u>
Net fixed assets	<u>37,300</u>	<u>48,862</u>
OTHER ASSETS		
Restricted cash and cash equivalents	21,937,661	22,377,297
Restricted investments	<u>13,019,028</u>	<u>10,926,304</u>
Total other assets	<u>34,956,689</u>	<u>33,303,601</u>
TOTAL ASSETS	<u><u>\$ 35,443,987</u></u>	<u><u>\$ 33,910,417</u></u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable	\$ 275,732	\$ 96,831
Payroll taxes and deductions	2,365	1,965
Accrued employer retirement plan contribution	42,000	48,000
Accrued payroll	-	79,380
Deferred revenue - insurance reimbursement	<u>2,593</u>	<u>-</u>
Total current liabilities	<u>322,690</u>	<u>226,176</u>
NONCURRENT LIABILITIES		
Escrow funds:		
Purses - racing revenue	6,561,342	5,233,469
Purses - slot revenue	11,239,477	13,733,155
Health and pension - slot revenue	<u>17,155,270</u>	<u>14,336,377</u>
Total escrow funds	<u>34,956,089</u>	<u>33,303,001</u>
Total liabilities	35,278,779	33,529,177
NET ASSETS		
Unrestricted	<u>165,208</u>	<u>381,240</u>
TOTAL LIABILITIES AND NET ASSETS	<u><u>\$ 35,443,987</u></u>	<u><u>\$ 33,910,417</u></u>

The accompanying notes are an integral part of the financial statements.

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS
Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
REVENUE		
Race track revenues:		
Downs Racing	\$ 2,550,000	\$ 2,900,000
Harrah's Chester	900,000	825,000
Membership dues	27,452	24,810
Race Horse Development Fund	1,275,921	721,566
Member benefit reimbursements	429,310	374,485
Special events	20,000	20,000
Corporate sponsorships	37,000	39,000
Miscellaneous income	-	359
Interest income	4,902	3,065
	<u>5,244,585</u>	<u>4,908,285</u>
EXPENSES		
Salaries	386,566	377,067
Payroll taxes	22,626	29,468
Employee benefits	74,387	73,738
General insurance	141,586	140,362
Employee benefits, members	1,531,657	1,355,052
Chaplaincy program	11,200	12,600
Advertising, newsletter and public relations	1,193,562	1,095,134
Promotion expenses - television	160,383	204,357
Meeting expense and travel	62,424	70,767
National dues	12,000	12,000
Office expense	26,037	25,232
Rent	9,254	9,162
Telephone	12,398	12,176
Legal and accounting	140,875	65,670
Legislative fees	101,012	89,499
Donations and gifts	782,734	278,417
Special events	26,564	28,961
Fair maintenance and purses	740,850	743,450
Depreciation	16,527	15,285
Bad debt expense	-	2,272
Miscellaneous expense	7,975	7,761
	<u>5,460,617</u>	<u>4,648,430</u>
CHANGE IN NET ASSETS	(216,032)	259,855
NET ASSETS, BEGINNING OF YEAR	<u>381,240</u>	<u>121,385</u>
NET ASSETS, END OF YEAR	<u>\$ 165,208</u>	<u>\$ 381,240</u>

The accompanying notes are an integral part of the financial statements.

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
STATEMENTS OF CASH FLOWS
Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	\$ (216,032)	\$ 259,855
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:		
Depreciation	16,527	15,285
Bad debt expense	-	2,272
Effects of changes in operating assets and liabilities:		
Accounts receivable	(4,094)	100,547
Prepaid expenses	(37,883)	(8,889)
Accounts payable	178,901	(72,650)
Payroll taxes and deductions	400	(4,709)
Deferred revenue	2,593	-
Accrued employer retirement plan contribution	(6,000)	-
Accrued payroll	<u>(79,380)</u>	<u>17,740</u>
Net cash provided by (used in) operating activities	(144,968)	309,451
CASH FLOWS FROM INVESTING ACTIVITIES		
Payments for purchase of furniture and equipment	<u>(4,965)</u>	<u>(15,141)</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(149,933)	294,310
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>389,327</u>	<u>95,017</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 239,394</u>	<u>\$ 389,327</u>

The accompanying notes are an integral part of the financial statements.

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Activities

The Association is a membership organization which promotes the welfare and development of harness racing in Pennsylvania. The primary sources are from two harness race tracks in Pennsylvania.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts of assets, liabilities, revenues and expenses, and the disclosure of contingent gains and losses. Accordingly, actual results could differ from those estimates.

Basis of Presentation and Net Assets

The financial statements of the Association are prepared on the accrual basis of accounting. Under this method, revenues are recognized when earned rather than received, and expenses are recognized when incurred rather than when the obligation is paid. In accordance with FASB ASC 958, *Not-for-Profit Entities*, the Association is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. The Association does not have any temporarily restricted or permanently restricted net assets at December 31, 2012 and 2011.

Cash and Cash Equivalents

For purposes of the statement of cash flows, the Association considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents. The restricted cash accounts are not included in cash balances for the purpose of the statement of cash flows as they are not available for normal operations of the Association.

Restricted Cash, Cash Equivalents and Investments

Certain cash, cash equivalents and investments are restricted as to use by Pennsylvania law and employee benefit plans. These funds are held in separate accounts.

Fair Value of Financial Instruments

The carrying value of cash and cash equivalents, accounts receivable and accounts payable approximates fair value due to the short maturity of these instruments. Investments are stated at fair value. Gains or losses on sales of investments and any unrealized gains or losses are reflected as a component of the escrow funds – health and pension liability account.

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Furniture and Equipment

Furniture and equipment is stated at cost. Depreciation is calculated on the straight-line method over the estimated lives of depreciable assets ranging in life from five to ten years based on management's estimate of the useful lives.

Additions, major replacements and betterments are capitalized. Maintenance and repairs are charged to expense as incurred.

Long-Lived Assets

Long-lived assets, such as property and equipment, are evaluated for impairment when events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable through the estimated undiscounted future cash flows from the use of these assets. When any such impairment exists, the related assets will be reduced to fair value. No impairment losses have been recorded through December 31, 2012.

Functional Allocation of Expenses

The costs of providing the Association's various programs and activities are presented on a functional basis in Note 7 to the financial statements. Accordingly, certain costs have been allocated based on management estimates of the time spent and materials used among the programs and supporting services benefited.

Income Taxes

The Association is a non-profit organization which is exempt from federal income taxes under Section 501(c)(5) of the Internal Revenue Code. FASB ASC 740-10, *Accounting for Uncertainty in Income Taxes*, requires an assessment of the Association's exposure to income taxes at the entity level as a result of uncertain tax positions taken in current and previously filed tax returns. Examples of tax positions taken at the entity level include the continuing validity of its 501(c)(5) status, potential unrelated business activities and other tax positions that could result in income taxes to the Association upon examinations by taxing authorities. The Association's management is not aware of any activities that would jeopardize its tax-exempt status or would be subject to unrelated business or excise tax.

The Association's federal Exempt Organization Business Income Tax Returns (Form 990) for 2010, 2011 and 2012 are subject to examination by federal authorities.

Reclassifications

Certain amounts from the 2011 financial statements have been reclassified to conform to the 2012 presentation. These reclassifications had no impact on financial position, change in net assets, or cash flows.

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 2 – ESCROW FUNDS AND RESTRICTED CASH/INVESTMENTS

Pennsylvania law requires certain portions of revenue from slot machines at Pennsylvania racetracks to be used for horse racing purses and pension and health benefits for horse men and women. The Association acts as a fiduciary in the collection and disbursement of these funds which are required to be maintained in separate accounts. The detail of transactions in these accounts for 2012 and 2011 is as follows:

	<u>Purses</u>	<u>Benefits</u>
Escrow balance, January 1, 2011	\$ 19,559,219	\$ 11,469,445
Gaming Funds - Chester Downs and Marina, LLC	31,487,083	1,978,349
Gaming Funds - Downs Racing, LP	27,282,918	1,717,391
Unrealized/realized gains (losses) on investments	-	(286,824)
Investment income (net of fees)	206,193	249,428
	<u>58,976,194</u>	<u>3,658,344</u>
Purse payments - Chester Downs and Marina, LLC - purse account	(36,692,672)	-
Purse payments - Downs Racing, LP - purse account	(28,109,586)	-
Health insurance payments	-	721,566
Retirement distributions	-	69,846
	<u>(64,802,258)</u>	<u>791,412</u>
Escrow balance, December 31, 2011	<u>13,733,155</u>	<u>14,336,377</u>
Gaming Funds - Chester Downs and Marina, LLC	30,283,658	1,939,779
Gaming Funds - Downs Racing, LP	27,265,655	1,747,916
Unrealized/realized gains on investments	-	116,510
Investment income (net of fees)	99,590	344,446
	<u>57,648,903</u>	<u>4,148,651</u>
Purse payments - Chester Downs and Marina, LLC - purse account	(32,690,565)	-
Purse payments - Downs Racing, LP - purse account	(27,452,015)	-
Health insurance payments	-	(1,275,921)
Retirement distributions	-	(53,838)
	<u>(60,142,580)</u>	<u>(1,329,759)</u>
Escrow balance, December 31, 2012	<u><u>\$ 11,239,478</u></u>	<u><u>\$ 19,814,787</u></u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 2 – ESCROW FUNDS AND RESTRICTED CASH/INVESTMENTS (CONTINUED)

	Purses	Benefits
Composition of ending balance:		
Cash and cash equivalents	\$ 11,239,878	\$ 4,136,441
Investments	-	13,019,028
	11,239,878	17,155,469
Opening cash due the Association	(400)	(200)
Ending cash and cash equivalents and investments	\$ 11,239,478	\$ 17,155,269

The restricted cash accounts each include \$200 deposits made by the Association to open the accounts.

Pursuant to an agreement with Chester Downs and Marina, LLC, dated January 1, 2011, certain racing revenues are to be paid to the Association. The Association is required to maintain these funds in a separate account. These funds are to be used to finance the Association's operating expenses, marketing and promotional costs, or fund purses at the Chester racetrack. The detail of the transactions for 2012 is as follows:

	Racing Revenues
Escrow balance, January 1, 2012	\$ 5,233,469
Transfers from Chester Downs and Marina, LLC - racing income	2,223,770
Investment income (net of fees)	4,598
	2,228,368
Racetrack (pari-mutuel) revenues paid to the Association	(900,000)
Bank charges	(495)
	(900,495)
Escrow balance, December 31, 2012 - racing revenue	6,561,342
Composition of ending balance:	
Cash and cash equivalents	\$ 6,561,342

Summary of all escrow accounts:

	Purses - Slot Revenue	Benefits - Slot Revenue	Racing Revenue	Total
Cash and cash equivalents	\$ 11,239,478	\$ 4,136,241	\$ 6,561,342	\$ 21,937,061
Investments	-	13,019,028	-	13,019,028
Escrow balance, December 31, 2012	\$ 11,239,478	\$ 17,155,269	\$ 6,561,342	\$ 34,956,089

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 2 – ESCROW FUNDS AND RESTRICTED CASH/INVESTMENTS (CONTINUED)

Investments are stated at fair value. Fair value and unrealized appreciation at December 31, 2012 and 2011 and are summarized as follows:

	2012			Fair Value
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Mutual Funds:				
Blend	\$ 117,356	\$ 1,106	\$ (49)	\$ 118,413
Value	249,053	6,659	(1,228)	254,484
Growth	10,067	941	-	11,008
International	39,555	4,664	(1,279)	42,940
Other	55,578	-	(4,180)	51,398
Fixed Income - Domestic	3,267,536	84,050	(643)	3,350,943
Fixed Income - International	1,201,000	39,392	-	1,240,392
Fixed Income - U.S.Government	56,187	-	(952)	55,235
Money Market	308,413	-	-	308,413
Total mutual funds	<u>5,304,745</u>	<u>136,812</u>	<u>(8,331)</u>	<u>5,433,226</u>
Exchange Traded Funds:				
Index	254,743	6,307	(1,226)	259,824
Fixed Income - Domestic	2,275,048	4,285	(6,759)	2,272,574
Fixed Income - International	380,977	4,532	-	385,509
Fixed Income - U.S. Government	564,991	-	(7,402)	557,589
Equity	476,669	-	(6,771)	469,898
Total exchange traded funds	<u>3,952,428</u>	<u>15,124</u>	<u>(22,158)</u>	<u>3,945,394</u>
Corporate Bonds				
Domestic	1,899,518	-	(11,492)	1,888,026
International	617,762	14,247	-	632,009
Total corporate bonds	<u>2,517,280</u>	<u>14,247</u>	<u>(11,492)</u>	<u>2,520,035</u>
Other Investments				
FS Investment Corporation II	1,028,890	14,364	-	1,043,254
Real Estate Investment Trust	115,000	-	(37,881)	77,119
Total other investments	<u>1,143,890</u>	<u>14,364</u>	<u>(37,881)</u>	<u>1,120,373</u>
Total investments	<u>\$ 12,918,343</u>	<u>\$ 180,547</u>	<u>\$ (79,862)</u>	<u>\$ 13,019,028</u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 2 – ESCROW FUNDS AND RESTRICTED CASH/INVESTMENTS (CONTINUED)

	2011			
		Gross	Gross	
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Mutual Funds:				
Blend	\$ 132,017	\$ 348	\$ (55)	\$ 132,310
Value	315,654	-	(34,860)	280,794
International	78,398	499	(4,615)	74,282
Other	237,836	211	(6,378)	231,669
Fixed Income - Domestic	2,825,414	33,939	(1,614)	2,857,739
Fixed Income - International	1,193,166	-	(29,409)	1,163,757
Fixed Income - U. S. Government	1,210,237	11,902	(163)	1,221,976
Money Market	192,584	-	-	192,584
Total mutual funds	<u>6,185,306</u>	<u>46,899</u>	<u>(77,094)</u>	<u>6,155,111</u>
Exchange Traded Funds:				
Index	249,737	4,281	(5,193)	248,825
Equity	51,063	-	(8,062)	43,001
Blend	29,800	-	(433)	29,367
Value	59,466	815	-	60,281
Fixed Income - Domestic	443,387	18	-	443,405
Fixed Income - U.S. Government	744,275	6,204	-	750,479
Total exchange traded funds	<u>1,577,728</u>	<u>11,318</u>	<u>(13,688)</u>	<u>1,575,358</u>
Corporate Bonds				
Domestic	2,154,074	-	(3,829)	2,150,245
International	431,371	7,990	-	439,361
Total corporate bonds	<u>2,585,445</u>	<u>7,990</u>	<u>(3,829)</u>	<u>2,589,606</u>
AXA Life Insurance Annuity	<u>509,054</u>	<u>-</u>	<u>-</u>	<u>509,054</u>
Other Investments				
Real Estate Investment Trust	<u>115,000</u>	<u>-</u>	<u>(17,825)</u>	<u>97,175</u>
Total other investments	<u>115,000</u>	<u>-</u>	<u>(17,825)</u>	<u>97,175</u>
Total investments	<u>\$ 10,972,533</u>	<u>\$ 66,207</u>	<u>\$ (112,436)</u>	<u>\$ 10,926,304</u>

Investment income (restricted) is excluded from the statement of activities and consists of:

	2012	2011
Interest and dividends	\$ 419,878	\$ 531,045
Investment fees	<u>(89,827)</u>	<u>(67,541)</u>
Total	<u>\$ 330,051</u>	<u>\$ 463,504</u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 3 – FAIR VALUE MEASUREMENTS

ASC 820-10 establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring the most observable inputs be used when available. This hierarchy consists of three broad levels: Level 1 inputs consist of unadjusted quoted prices in active markets for identical assets or liabilities and have the highest priority. Level 1 assets may include securities that are traded in an active exchange market, or actively traded over-the-counter markets. Level 2 valuation is based on directly or indirectly observable inputs other than quoted prices for identical assets. Level 3 valuation is based on unobservable inputs and has the lowest priority. Level 3 assets may include financial instruments whose value is determined using pricing models with internally developed assumptions, discounted cash flows methodologies, or similar techniques.

The Association uses the following valuation techniques to measure fair value of assets on a recurring basis. There have been no changes in the methodologies used at December 31, 2012 and 2011.

Mutual Funds and Exchange Traded Funds

Fair value of mutual funds and exchange traded funds are based on quoted market prices for identical securities. These investments are classified within Level 1 of the valuation hierarchy.

Money Market Mutual Funds

Money market mutual funds are valued at a stable \$1.00 net assets value which is the value at which the fund is traded and approximates fair value based on the fair value of the underlying investment. Such securities are classified within Level 2 of the valuation hierarchy.

Corporate Bonds

Certain corporate bonds are valued at the closing price reported in the active market in which the bond is traded. Other corporate bonds are valued based on yields currently available on comparable securities of issuers with similar credit ratings. When quoted prices are not available for identical or similar bonds, the bond is valued using a discounted cash flows approach that maximizes observable inputs, such as current yields of similar instruments, but includes adjustments for certain risks that may not be observable, such as credit and liquidity risks. These investments are classified within Level 2 of the valuation hierarchy.

FS Investment Corporation II

The underlying investments consist principally of debt securities, including senior secured loans, second lien secured loans and, to a lesser extent, subordinated loans. The net asset value of the investment portfolio is determined quarterly using a combination of quoted market prices and estimations based on relevant inputs such as indicative dealer quotes, values of like securities, and valuations prepared by third-party valuation services. This investment is classified within Level 3 of the valuation hierarchy.

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 3 – FAIR VALUE MEASUREMENTS (CONTINUED)

Real Estate Investment Trust

Valued at an estimated amount based on overall economic and real estate market conditions of the underlying properties. This investment is classified within Level 3 of the valuation hierarchy.

AXA Equitable Life Insurance Annuity

Valued at fair value by discounting the related cash flows based on current yields of similar instruments with comparable durations considering the credit-worthiness of the issuer. This investment is classified within Level 2 of the valuation hierarchy.

The preceding methods may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Association believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 3 – FAIR VALUE MEASUREMENTS (CONTINUED)

The following table sets forth by level, within the fair value hierarchy, the Association's assets at fair value on a recurring basis as of December 31, 2012 and 2011:

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
December 31, 2012				
Mutual Funds:				
Blend	\$ 118,413	\$ 118,413	\$ -	\$ -
Value	254,484	254,484	-	-
Growth	11,008	11,008	-	-
International	42,940	42,940	-	-
Other	51,398	51,398	-	-
Fixed Income - Domestic	3,350,943	3,350,943	-	-
Fixed Income - International	1,240,392	1,240,392	-	-
Fixed Income - U.S. Government	55,235	55,235	-	-
Money Market	308,413	-	308,413	-
Total mutual funds	<u>5,433,226</u>	<u>5,124,813</u>	<u>308,413</u>	<u>-</u>
Exchange Traded Funds:				
Index	259,824	259,824	-	-
Fixed Income - Domestic	2,272,574	2,272,574	-	-
Fixed Income - International	385,509	385,509	-	-
Fixed Income - U.S. Government	557,589	557,589	-	-
Equity	469,898	469,898	-	-
Total exchange traded funds	<u>3,945,394</u>	<u>3,945,394</u>	<u>-</u>	<u>-</u>
Corporate Bonds				
Domestic	1,888,026	-	1,888,026	-
International	632,009	-	632,009	-
Total corporate bonds	<u>2,520,035</u>	<u>-</u>	<u>2,520,035</u>	<u>-</u>
Other Investments				
FS Investment Corporation II	1,043,254	-	-	1,043,254
Real Estate Investment Trust	77,119	-	-	77,119
Total other investments	<u>1,120,373</u>	<u>-</u>	<u>-</u>	<u>1,120,373</u>
Total	<u><u>\$ 13,019,028</u></u>	<u><u>\$ 9,070,207</u></u>	<u><u>\$ 2,828,448</u></u>	<u><u>\$ 1,120,373</u></u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 3 – FAIR VALUE MEASUREMENTS (CONTINUED)

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Fair Value</u>
December 31, 2011				
Mutual Funds:				
Blend	\$ 132,310	\$ 132,310	\$ -	\$ -
Value	280,794	280,794	-	-
International	74,282	74,282	-	-
Other	231,669	231,669	-	-
Fixed Income - Domestic	2,857,739	2,857,739	-	-
Fixed Income - International	1,163,757	1,163,757	-	-
Fixed Income - U.S. Government	1,221,976	1,221,976	-	-
Money Market	192,584	-	192,584	-
Total mutual funds	<u>6,155,111</u>	<u>5,962,527</u>	<u>192,584</u>	<u>-</u>
Exchange Traded Funds:				
Index	248,825	248,825	-	-
Equity	43,001	43,001	-	-
Blend	29,367	29,367	-	-
Value	60,281	60,281	-	-
Fixed Income - Domestic	443,405	443,405	-	-
Fixed Income - U.S. Government	750,479	750,479	-	-
Total exchange traded funds	<u>1,575,358</u>	<u>1,575,358</u>	<u>-</u>	<u>-</u>
Corporate Bonds				
Domestic	2,150,245	-	2,150,245	-
International	439,361	-	439,361	-
Total corporate bonds	<u>2,589,606</u>	<u>-</u>	<u>2,589,606</u>	<u>-</u>
AXA Life Insurance Annuity Obligations	509,054	-	509,054	-
Other Investments				
Real Estate Investment Trust	97,175	-	-	97,175
Total other investments	<u>97,175</u>	<u>-</u>	<u>-</u>	<u>97,175</u>
Total	<u>\$ 10,926,304</u>	<u>\$ 7,537,885</u>	<u>\$ 3,291,244</u>	<u>\$ 97,175</u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 3 – FAIR VALUE MEASUREMENTS (CONTINUED)

Level 3 Gains and Losses

The following table sets forth a summary of changes in the fair value of the Association's level 3 assets for the years ended December 31, 2012 and 2011.

Balance, January 1, 2011	\$ 115,000
Unrealized gains/(losses)	<u>(17,825)</u>
Balance, December 31, 2011	97,175
Unrealized gains/(losses)	(23,517)
Purchases	<u>1,046,715</u>
Balance, December 31, 2012	<u>\$ 1,120,373</u>

Gains and losses (realized and unrealized) included in changes in value for the period above are reflected as a component of the escrow funds – health and pension liability account. There were no transfers in or out of the level 3 in 2012 and 2011.

NOTE 4 – ACCOUNTS RECEIVABLE

Accounts receivable consist of the following:

	<u>2012</u>	<u>2011</u>
Pennsylvania Harness week sponsorships	\$ 37,000	\$ 39,000
Member benefit reimbursements	<u>9,501</u>	<u>3,407</u>
Total	<u>\$ 46,501</u>	<u>\$ 42,407</u>

The Association uses the direct write-off method for bad debts, the results of which are not materially different from those allowed under the allowance method.

NOTE 5 – RACE TRACK REVENUES

The Association holds a contract with a harness race track in Pennsylvania, Downs Racing, L.P., for the period January 1, 2011 to December 31, 2014. Under the terms of this contract, the Association will receive \$1,200,000 annually. In addition, the Association can request additional payments exceeding \$100,000 if deemed necessary. These amounts may be used toward Association operating expenses, dues to any national organization, group health insurance for drivers, trainers and grooms, accident and disability insurance for trainers and drivers and for marketing and promotional items.

In addition, the Association holds a contract with Chester Downs and Marina, LLC for the period January 1, 2011 to December 31, 2013. Under this contract a percentage of wagering handle shall be paid to the Association to be used toward Association operating expenses, dues to national horsemen organizations, group health insurance, marketing and promotional costs to fund purses as determined by the Association in consultation with Chester Downs, or for administrative costs.

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 6 – SPECIAL EVENTS

The following is a schedule of income and direct expenses from the Association's special events for the years ended December 31:

	<u>2012</u>	<u>2011</u>
Golf outing:		
Revenue	\$ 20,000	\$ 20,000
Direct expenses	<u>26,564</u>	<u>28,961</u>
Net golf outing income (expense)	<u>\$ (6,564)</u>	<u>\$ (8,961)</u>

NOTE 7 – FUNCTIONAL CLASSIFICATION OF EXPENSES

Expenses by function for the year ended December 31 are as follows:

	<u>2012</u>	<u>2011</u>
Program services:		
Health program	\$ 76,597	\$ 81,131
Pension program	73,389	64,732
Member benefits	1,755,947	1,479,088
Racetrack relations	39,699	107,357
Industry promotion	2,251,860	1,527,566
Regulatory matters	1,054,886	1,037,869
Supporting services:		
Management and general	<u>208,239</u>	<u>350,687</u>
Total	<u>\$ 5,460,617</u>	<u>\$ 4,648,430</u>

NOTE 8 – 401(k) PLAN

The Association established a deferred salary arrangement under I.R.C. Section 401(k). The plan covers substantially all its eligible employees. The Association's matching contribution for 2012 and 2011 totaled \$42,000 and \$48,000, respectively.

NOTE 9 – LEASE

The Association is currently leasing its office space in Lemoyne, Pennsylvania under a one-year lease which expires April 30, 2013. The current rental is \$736 per month. Total rent expense for 2012 and 2011 was \$9,254 and \$9,162, respectively.

The Association leases several pieces of equipment with a maturity date of March 2015. Monthly payments total \$418 per month. The rental payments for 2012 and 2011 were \$5,010 for each year.

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 9 – LEASE (CONTINUED)

Minimum lease payments under these leases are:

2013	\$	5,010
2014		5,010
2015		<u>418</u>
Total	\$	<u>10,438</u>

NOTE 10 – COMMITMENTS

In November 2007, the Board of Directors for the Association approved the live racing agreement with Valley Downs, LP. At this point in time the track has not been built.

The Association entered into a naming rights agreement January 1, 2011 with Downs Racing, L.P. to become a party to naming the arena located in Wilkes Barre, Pennsylvania. The Association contributes \$100,000 per year for a ten year period. In 2012, the Association paid \$100,000. Future payments will be:

2013	\$	100,000
2014		100,000
2015		100,000
2016		100,000
2017		100,000
Thereafter		<u>300,000</u>
Total	\$	<u>800,000</u>

NOTE 11 – CONCENTRATIONS OF CREDIT RISK

The Association maintains several cash balances (restricted and unrestricted) at financial institutions located in Pennsylvania. Accounts in these financial institutions are secured by Federal Deposit Insurance Corporation (FDIC) up to specified limits. In the normal course of business, the Association may have deposits that exceed the insured limit which management considers to be a normal business risk. As of December 31, 2012 and 2011, the Association had cash on deposit of \$22,902,833 and \$22,501,659, respectively.

For the years ended December 31, 2012 and 2011, revenue includes \$3,450,000 and \$3,725,000, respectively, arising from race track revenues received from two race tracks. The loss of either of these revenue sources could have a material effect on the Association.

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 12 – SUBSEQUENT EVENTS

Management evaluated subsequent events through April 3, 2013, the date the financial statements were available to be issued. Events or transactions occurring after December 31, 2012, but prior to April 3, 2013, that provided additional evidence about conditions that existed at December 31, 2012, have been recognized in the financial statements for the year ended December 31, 2012. Events or transactions that provided evidence about conditions that did not exist at December 31, 2012, but arose before the financial statements were available to be issued, have not been recognized in the financial statements for the year ended December 31, 2012.

PENNSYLVANIA RACE HORSE DEVELOPMENT FUND



Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of the Statement of Cash Receipts and Cash Disbursements of the Pennsylvania Racehorse Development Funds Performed in Accordance with *Government Auditing Standards*

Board of Directors
Pennsylvania Harness Horsemen's Association
Lemoyne, Pennsylvania

Secretary
Pennsylvania Office of the Budget

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Pennsylvania Harness Horsemen's Association (the Association), which comprise the statement of financial position as of December 31, 2012, and the related statements of activities, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated April 3, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Association's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Association's internal control. Accordingly, we do not express an opinion on the effectiveness of the Association's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and questioned costs that we consider to be significant deficiencies as items 2012-01 through 2012-03.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Association's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Response to Findings

The Association's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. The Association's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the Association's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Association's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

The image shows a handwritten signature in cursive script that reads "CliftonLarsonAllen LLP". The signature is written in black ink and is positioned above the printed name and date.

Baltimore, Maryland
April 3, 2013



**Independent Auditor's Report on Compliance with Requirements
That Could Have a Direct and Material Effect on Pennsylvania Racehorse Development
Funds and on Internal Control Over Compliance with the
Pennsylvania Horse Development and Gaming Act**

Board of Directors
Pennsylvania Harness Horsemen's Association
Lemoyne, Pennsylvania

Secretary
Pennsylvania Office of the Budget

Report on Compliance

We have audited the Pennsylvania Harness Horsemen's Association's (the Association) compliance with the types of compliance requirements described in Chapter 436a of the Pennsylvania Horse Development and Gaming Act that could have a direct and material effect on each of the Association's Race Horse Development Funds for the year ended December 31, 2012. The Association's Race Horse Development Funds are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to Race Horse Development Funds.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for the Association based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards and Chapter 436a of Pennsylvania Horse Development and Gaming Act require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on Race Horse Development Funds occurred. An audit includes examining, on a test basis, evidence about the Association's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for Race Horse Development Funds. However, our audit does not provide a legal determination of the Association's compliance.

Opinion on Chapter 436a Program

In our opinion, the Association complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on the Race Horse Development Funds for the year ended December 31, 2012.

Report on Internal Control Over Compliance

Management of the Association is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Association's internal control over compliance with the types of requirements that could have a direct and material effect on the Race Horse Development Funds to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the Race Horse Development Funds and to test and report on internal control over compliance in accordance with the Pennsylvania Horse Development and Gaming Act, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Association's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of the Race Horse Development Funds on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of Race Horse Development Funds that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the result of that testing based on the requirements of the Pennsylvania Horse Development and Gaming Act. Accordingly, this report is not suitable for any other purpose.



Baltimore, Maryland
April 3, 2013

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
STATEMENT OF CASH RECEIPTS AND CASH DISBURSEMENTS AND CHANGES IN ESCROW BALANCES
Period January 1, 2012 through December 31, 2012

	<u>Purses</u>	<u>Benefits</u>	<u>Total</u>
CASH RECEIPTS			
Gaming Funds - Chester Downs and Marina, LLC	\$ 30,283,658	\$ 1,939,779	\$ 32,223,437
Gaming funds - Downs Racing LLP	27,265,655	1,747,916	29,013,571
Interest and investment income, net of fees	99,590	344,446	444,036
Total cash receipts	<u>57,648,903</u>	<u>4,032,141</u>	<u>61,681,044</u>
CASH DISBURSEMENTS			
Purse payments - Chester Downs and Marina, LLC	32,690,565	-	32,690,565
Purse payments - Downs Racing, LP	27,452,015	-	27,452,015
Health insurance payments	-	1,275,921	1,275,921
Retirement distributions	-	53,838	53,838
Total cash disbursements	<u>60,142,580</u>	<u>1,329,759</u>	<u>61,472,339</u>
OTHER			
Net unrealized and realized gains on restricted investments	-	116,510	116,510
CHANGES IN ESCROW BALANCES	(2,493,677)	2,818,892	325,215
ESCROW BALANCE AT JANUARY 1, 2012	<u>13,733,155</u>	<u>14,336,377</u>	<u>28,069,532</u>
ESCROW BALANCE AT DECEMBER 31, 2012	<u>\$ 11,239,478</u>	<u>\$ 17,155,269</u>	<u>\$ 28,394,747</u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
STATEMENT OF CASH RECEIPTS AND CASH DISBURSEMENTS AND CHANGES IN ESCROW BALANCES
Period January 1, 2012 through December 31, 2012

RECONCILIATION TO AUDITED FINANCIAL STATEMENTS

Gaming funds, as reported above:			
Chester Downs and Marina, LLC	\$ 30,283,658	\$ 1,939,779	\$ 32,223,437
Downs Racing, LP	<u>27,265,655</u>	<u>1,747,916</u>	<u>29,013,571</u>
Total gaming funds, as reported above	<u>\$ 57,549,313</u>	<u>\$ 3,687,695</u>	<u>\$ 61,237,008</u>
Gaming funds, as reported in Note 2 to the audited financial statements:			
Chester Downs and Marina, LLC	\$ 30,283,658	\$ 1,939,779	\$ 32,223,437
Downs Racing, LP	<u>27,265,655</u>	<u>1,747,916</u>	<u>29,013,571</u>
Total gaming funds, as reported in Note 2 to the audited financial statements	<u>\$ 57,549,313</u>	<u>\$ 3,687,695</u>	<u>\$ 61,237,008</u>
Purse payments, as reported above:			
Chester Downs and Marina, LLC	\$ 32,690,565	\$ -	\$ 32,690,565
Downs Racing, LP	<u>27,452,015</u>	<u>-</u>	<u>27,452,015</u>
Total purse payments, as reported above	<u>\$ 60,142,580</u>	<u>\$ -</u>	<u>\$ 60,142,580</u>
Purse payments, as reported in Note 2 to the audited financial statements			
Chester Downs and Marina, LLC	\$ 32,690,565	\$ -	\$ 32,690,565
Downs Racing, LP	<u>27,452,015</u>	<u>-</u>	<u>27,452,015</u>
Total purse payments, as reported in Note 2 to the audited financial statements	<u>\$ 60,142,580</u>	<u>\$ -</u>	<u>\$ 60,142,580</u>
COMPOSITION OF ENDING BALANCE			
Restricted cash and cash equivalents	\$ 11,239,478	\$ 4,136,441	\$ 15,375,919
Restricted investments	<u>-</u>	<u>13,019,028</u>	<u>13,019,028</u>
TOTAL	<u>\$ 11,239,478</u>	<u>\$ 17,155,469</u>	<u>\$ 28,394,947</u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO THE STATEMENT OF CASH RECEIPTS AND CASH DISBURSEMENTS
AND CHANGES IN ESCROW BALANCES
Period January 1, 2012 through December 31, 2012

NOTE 1 – BASIS OF PRESENTATION

The accompanying Statement of Racing Fund Cash Receipts and Disbursements includes the Pennsylvania Race Horse Development Fund activity of the Pennsylvania Harness Horsemen's Association (the Association) and is presented on the cash basis of accounting. The information in this schedule is presented in accordance with Chapter 436a of the Pennsylvania Horse Development and Gaming Act, and fiscal code (72 P.S. § 1701-O). Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of the basic financial statements.

NOTE 2 – FLOW OF THE PENNSYLVANIA HORSE FUNDS

The Pennsylvania Department of Revenue transfers Pennsylvania Racehorse Development Funds to the casinos on a weekly basis designating amounts for purses and health and retirement benefits. The casinos then transfer these funds to the Association to separate accounts established by the casinos, by purpose.

Management of the Association determines the portion of the Race Horse Development Funds to transfer to the casinos for purse purposes based on an estimate provided by the casinos. The frequency of purse payments to the casinos is dependent on the established racing schedules. The Association maintains schedules detailing all purse fund payments. The purse payments are reconciled to the actual purses paid by the casinos. Health disbursements are made directly to the carriers based on invoiced amounts. There were no administrative expenses charged to those funds in 2012.

NOTE 3 – FINDINGS AND QUESTIONED COSTS

The findings and questioned costs identified in connection with the 2012 audit report are disclosed in Schedule I and the status of the prior year findings and questioned costs are included in a separate report.

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
December 31, 2012

I. Summary of Independent Auditor's Results

Financial Statements

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

Material weakness(es) identified?	_____	Yes	_____	X	No
Significant deficiency(ies) identified that are not considered to be material weakness?	_____	X	Yes	_____	None reported
Noncompliance material to financial statements noted?	_____	Yes	_____	X	No

Racehorse Development Funds

Internal control over state programs:

Material weakness(es) identified?	_____	Yes	_____	X	No
Significant deficiency(ies) identified that are not considered to be material weakness?	_____	Yes	_____	X	None reported

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
December 31, 2012

II. Financial Statement Findings

Finding No. 12-01: Segregation of Duties

Condition

The Association does not have controls to prevent or detect misstatements on a timely basis as a result of a lack of segregation of duties. This condition increases the possibility that errors or irregularities may occur and not be detected on a timely basis. Due to the small number of people employed in administrative functions, the Association may not be able to fully achieve ideal segregation of duties. Currently, management's and the board's close oversight and review of accounting information are the best means available to prevent or detect errors or irregularities.

Criteria

The Internal Control Integrated Framework (COSO report) requires adequate internal controls over segregation of duties to ensure that transactions are properly recorded and reduce the risk that errors will be undetected.

Cause

This is a result of the level of staffing maintained by the Association.

Effect

An increased risk that error or inconsistencies may occur and not be detected.

Recommendation

We recommend management and the board provide close oversight and review of financial information.

Management's Response

In addition to Board oversight, PHHA is considering the option of additional staffing in the future.

Finding No. 12-02: Timeliness of Insurance Contract Submittals

Condition

It was noted that the Health Insurance contracts were not submitted to the Pennsylvania Gaming Control Board at least 90 days prior to their effective date.

Criteria

The Association is required to provide timely insurance contracts to the Pennsylvania Gaming Control Board to allow for adequate review by the board prior to the insurance contract's effective date.

Cause

This is a result of staff oversight.

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
December 31, 2012

Effect

An increased risk that the insurance contracts are not adequately reviewed prior to their effective date.

Recommendation

Management should implement controls to ensure that all health contracts are submitted to the Pennsylvania Gaming Control Board at least 90 days prior to their effective date.

Management's Response

The delay in timely sending the health insurance contract to the Gaming Control Board was due to the fact that PHHA was waiting for a competitive quote from Highmark Blue Cross that ultimately resulted in PHHA receiving a quote from Health Assurance with no increase. The industry trend was a 9% premium increase. The alternate quote from IBC enabled PHHA to renew with no increase in premium. It should also be noted that the benefits have been unchanged since inception.

Finding No. 12-03: Accuracy of Quarterly Reports

Condition

It was noted that the second, third and fourth quarter reports filed with the Pennsylvania Gaming Control Board included certain cash receipts and cash disbursement amounts that did not reconcile to the Association's accounting records.

Criteria

The Association is required to submit accurate quarterly reports to the Pennsylvania Gaming Control Board. These reports summarize the quarterly cash receipts and cash disbursements of the Pennsylvania Racehorse Development Fund monies.

Cause

This is a result of staff error.

Effect

The Board does not have completely accurate information concerning the receipt and disbursement of Pennsylvania Racehorse Development Fund monies.

Recommendation

We recommend management amend the incorrect quarterly reports and ensure that controls are in place to prevent and detect errors in reporting.

Management's Response

PHHA will re-file reports the gaming board. The second quarter difference was due to counting a transfer twice. We were aware of that but did not re-file in a timely manner. The third quarter difference, we believe, was due to an uncashed check returned after submission and subsequently returned and journal entry made. The fourth quarter will be researched and re-submitted. We believe some of the differences were due to journal entries and/or corrections made after submission.

SUPPLEMENTAL INFORMATION

**PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
ELIGIBILITY FOR MEMBERSHIP, HEALTH, AND PENSION PLANS**

Eligibility for Membership, Health, and Pension Plans

Eligibility requirements to become a Member of the Association:

- Active member – any person who is a member of the United States Trotting Association, and licensed in good standing by the Commonwealth of Pennsylvania as an owner, trainer, or driver, becomes an active member of PHHA upon payment of the annual dues.
- Associate member – Any interested party not eligible under “native member” above, becomes an associate member of PHHA upon payment of the annual dues.
- Exceptions – Prohibited by both active and associate membership in PHHA are officials of pari-mutuel racetracks and owners of more than 5% (five percent) pari-mutuel racetrack stock.
- Notwithstanding the above, the PHHA Board of Directors shall be the final judge of member eligibility, and may approve or reject any membership applications.

Eligibility requirements for Health Plan:

- 75% of the individual's income must come from harness racing.
- Only trainers, drivers, and grooms are eligible for PHHA health insurance.
- Individuals are not eligible for coverage from PHHA if the individual is a licensed owner.
- An owner-trainer, owner-driver, or owner-trainer-driver is eligible for health insurance if the required number of starts is reached.
- There will be a required number of starts for trainers and drivers. The grooms' eligibility for insurance coverage is determined by the required number of starts for the trainer the individual is employed by.
- There will be a three (3) month waiting period following the filing of the individual's application. The individual will then be eligible the next billing period.
- If the individual has been on PHHA health insurance previously, and cancelled or resigned, the wait will be six (6) months.
- If the individual is a participant transferred in from another state or filing an application from another association, the individual will be required to meet PHHA guidelines.
- Payment will be due on the 15th of each month. The individual will receive a reminder each month; this is not a bill. The individual is responsible for making sure the payment is received in the Lemoyne office by the 15th of the month.
- The participants will pay a percentage of the bill premium for health insurance. That percentage will be determined monthly.
- PHHA employees must work at least twenty-five (25) hours per week to be eligible for coverage.

Eligibility requirements for Dental Plan:

- Members in good standing under the constitution and by-laws.

Eligibility requirements for Retirement Savings Plan:

- The individual must be a member of the Association.
- The individual must be either a Driver or a Trainer who competes at the racetracks and makes the required number of qualified starts.
 - The number of qualified starts may vary each year depending on the number of nice days at the tracks.

**PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
ELIGIBILITY FOR MEMBERSHIP, HEALTH, AND PENSION PALNS**

- Contributions are made to the plan on behalf of plan participants based on a point system as follows:
 - Trainers:
 - One-quarter point (1/4 point) – 25 to 40 qualified starts each calendar year.
 - One-half point (1/2 point) – 41 to 60 qualified starts each calendar year.
 - Three-quarter (3/4 point) – 61 to 79 qualified starts each calendar year.
 - One point (1 point) – 80 qualified starts and higher each calendar year.
 - Drivers:
 - One-quarter point (1/4 point) – 30 to 55 qualified starts each calendar year.
 - One half point (1/2 point) – 56 to 85 qualified starts each calendar year.
 - Three-quarter point (3/4 point) – 86 to 140 qualified starts each calendar year.
 - One point (1 point) – 140 qualified starts and higher each calendar year.
- Participants in the plan are 100% vested upon accumulation of 5 points. In the event of death or a total disability, as defined in the plan document, participants become 100% vested in the participant account.

**PENNSYLVANIA HORSEMEN'S ASSOCIATION
PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
MEMBERS BY STATE**

Based on information provided to us during our fieldwork, the Members By State of the Association are as follows:

<u>State</u>	<u>Number of Members</u>
Canada	4
CT	5
DE	71
FL	35
IL	8
IN	2
Ireland	1
KY	3
MA	1
MD	25
MI	4
NC	2
NJ	145
NY	50
OH	17
PA	335
VA	2
WV	<u>1</u>
TOTAL MEMBERS AS OF DECEMBER 31, 2012	<u><u>711</u></u>

**PENNSYLVANIA HORSEMEN'S ASSOCIATION
PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
HEALTH PLAN – PARTICIPANTS BY STATE**

Based on information provided to us during our fieldwork, the Health Plan Participants By State of the Association are as follows:

State	Number of Participants
PA	73
NJ	34
MD	6
FL	6
DE	5
NY	4
IL	2
VA	2
MS	1
NC	1
TOTAL PARTICIPANTS AS OF DECEMBER 31, 2012	<u>134</u>

**PENNSYLVANIA HORSEMEN'S ASSOCIATION
PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
HEALTH PLAN – PARTICIPANTS BY CATEGORY**

Based on information provided to us during our fieldwork, the Health Plan Participants By Category of the Association are as follows:

State	Number of Participants
Driver	13
Employee	3
Groom	19
Spouse	1
Trainer	84
Trainer Driver	<u>14</u>
TOTAL PARTICIPANTS AS OF DECEMBER 31, 2012	<u>134</u>

**PENNSYLVANIA HORSEMEN'S ASSOCIATION
PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
RETIREMENT PLAN PARTICIPANTS**

Based on information provided to us during our fieldwork, the Retirement Plan Range of Starts of the Association are as follows:

<u>State</u>	<u>Number of Participants</u>
Trainer	328
Driver	<u>75</u>
TOTAL PARTICIPANTS AS OF DECEMBER 31, 2012	<u><u>403</u></u>

**PENNSYLVANIA HORSEMEN'S ASSOCIATION
PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
RETIREMENT PLAN RANGE OF STARTS**

Based on information provided to us during our fieldwork, the Retirement Plan Participants of the Association are as follows:

Trainers	
Range of Starts	Number of Participants
under 35	118
35-69	79
70-104	49
105-139	32
>=140	50
TOTAL PARTICIPANTS AS OF DECEMBER 31, 2012	328

Drivers	
Range of Starts	Number of Participants
under 50	24
50-99	13
100-149	4
150-199	4
>=200	30
TOTAL PARTICIPANTS AS OF DECEMBER 31, 2012	75