

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

**FINANCIAL STATEMENTS
December 31, 2013 and 2012**

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INDEPENDENT AUDITORS' 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, 2013 and 2012, and the related statements of activities and changes in net assets and cash flows for the years then ended, and the related notes to the financial statements.

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.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Governmental Auditing Standards*, issued by the Comptroller General of the United States. 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 auditors' 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 financial statements referred to above present fairly, in all material respects, the financial position of the Association as of December 31, 2013 and 2012, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Other Information – Statement of Cash Receipts and Cash Disbursements and Changes in Escrow Balances

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The statement of cash receipts and cash disbursements and changes in escrow balances, as required by Chapter 436b of the Pennsylvania Horse Development and Gaming Act, is presented for purposes of additional analysis and is not required as part of the financial statements. Such information is the responsibility of management and was derived from and related directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected 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 Information – Membership Information

The membership information listed in the table of contents is presented for purposes of additional analysis and is not a required part of the financial statements. The information has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated June 23, 2014, on our consideration of the Association’s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the result of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Association’s internal control over financial reporting and compliance.



CliftonLarsonAllen, LLP

Baltimore, Maryland
June 23, 2014

FINANCIAL STATEMENTS

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
STATEMENTS OF FINANCIAL POSITION
December 31, 2013 and 2012

	2013	2012
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 47,644	\$ 239,394
Accounts receivable	50,328	46,501
Prepaid expenses	159,178	164,103
Total current assets	257,150	449,998
FIXED ASSETS		
Furniture and equipment, at cost	107,884	107,884
Less: accumulated depreciation	86,984	70,584
Net fixed assets	20,900	37,300
OTHER ASSETS		
Restricted cash and cash equivalents	15,173,085	21,937,661
Restricted investments	18,470,487	13,019,028
Total other assets	33,643,572	34,956,689
INTANGIBLE ASSETS		
Naming rights, net of accumulated amortization of \$400,000	600,000	-
TOTAL ASSETS	\$ 34,521,622	\$ 35,443,987
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable	\$ 258,586	\$ 275,732
Payroll taxes and deductions	6,840	2,365
Accrued employer retirement plan contribution	39,000	42,000
Accrued payroll	11,880	-
Deferred revenue - insurance reimbursement	1,332	2,593
Total current liabilities	317,638	322,690
NONCURRENT LIABILITIES		
Long term payable	500,000	-
Escrow funds:		
Purses - racing revenue	7,167,882	6,561,342
Purses - slot revenue	6,857,217	11,239,477
Health and pension - slot revenue	19,617,873	17,155,270
Total escrow funds	33,642,972	34,956,089
Total liabilities	34,460,610	35,278,779
NET ASSETS		
Unrestricted	61,012	165,208
TOTAL LIABILITIES AND NET ASSETS	\$ 34,521,622	\$ 35,443,987

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, 2013 and 2012

	<u>2013</u>	<u>2012</u>
REVENUE		
Race track revenues:		
Downs Racing	\$ 2,500,000	\$ 2,550,000
Harrah's Chester	628,900	900,000
Membership dues	28,040	27,452
Race Horse Development Fund	838,507	1,275,921
Member benefit reimbursements	499,777	429,310
Special events	25,000	20,000
Corporate sponsorships	43,000	37,000
Miscellaneous income	1,149	-
Interest income	1,195	4,902
	<u>4,565,568</u>	<u>5,244,585</u>
EXPENSES		
Salaries	396,567	386,566
Payroll taxes	30,416	22,626
Employee benefits	85,465	74,387
General insurance	156,857	141,586
Employee benefits, members	1,338,878	1,531,657
Chaplaincy program	12,600	11,200
Advertising, newsletter and public relations	1,019,695	1,193,562
Promotion expenses - television	158,495	160,383
Meeting expense and travel	72,087	62,424
National dues	12,000	12,000
Office expense	21,473	26,036
Rent	9,300	9,254
Telephone	9,451	12,398
Legal and accounting	106,682	140,875
Legislative fees	105,428	101,012
Donations and gifts	172,655	782,734
Special events	29,847	26,564
Fair maintenance and purses	809,400	740,850
Depreciation	16,400	16,527
Amortization	100,000	-
Miscellaneous expense	6,068	7,975
	<u>4,669,764</u>	<u>5,460,616</u>
CHANGE IN NET ASSETS	(104,196)	(216,031)
NET ASSETS, BEGINNING OF YEAR	<u>165,208</u>	<u>381,239</u>
NET ASSETS, END OF YEAR	<u>\$ 61,012</u>	<u>\$ 165,208</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, 2013 and 2012

	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	\$ (104,196)	\$ (216,031)
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:		
Depreciation and amortization	116,400	16,527
Effects of changes in operating assets and liabilities:		
Accounts receivable	(3,827)	(4,094)
Prepaid expenses	4,925	(37,884)
Accounts payable	(17,146)	178,901
Payroll taxes and deductions	4,475	400
Deferred revenue	(1,261)	2,593
Accrued employer retirement plan contribution	(3,000)	(6,000)
Accrued payroll	11,880	(79,380)
	<u>8,250</u>	<u>(144,968)</u>
Net cash provided by (used in) operating activities		
CASH FLOWS FROM INVESTING ACTIVITIES		
Payments for purchase of furniture and equipment	-	(4,965)
Purchase of naming rights	(700,000)	-
	<u>(700,000)</u>	<u>(4,965)</u>
Net cash used in investing activities		
NET DECREASE IN CASH AND CASH EQUIVALENTS	(691,750)	(149,933)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>239,394</u>	<u>389,327</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ (452,356)</u>	<u>\$ 239,394</u>

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

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

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.

Basis of Presentation

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, 2013 and 2012.

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.

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 and 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.

Accounts Receivable

Accounts receivable consist of uncollateralized sponsorships for Pennsylvania Harness Week and member health benefit reimbursements. The Association uses the direct write-off method for bad debts, the results of which are not materially different from those under the allowance method.

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 components of the escrow funds – health and pension and racing revenue liability accounts.

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

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 in excess of \$1,000 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, 2013.

Intangible

The intangible asset represents the naming rights to an arena located in Wilkes-Barre, Pennsylvania and is amortized over the life of the agreement which is 10 years.

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 2011, 2012, and 2013 are subject to examination by federal authorities.

Reclassifications

Certain amounts from the 2012 financial statements have been reclassified to conform to the 2013 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, 2013 and 2012

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 2013 and 2012 is as follows:

	<u>Purses</u>	<u>Benefits</u>
Escrow balance, January 1, 2012	\$ 13,733,155	\$ 14,336,377
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>11,239,478</u>	<u>17,155,269</u>
Gaming Funds - Chester Downs and Marina, LLC	27,383,835	1,866,413
Gaming Funds - Downs Racing, LP	26,013,173	1,782,747
Unrealized/realized losses on investments	-	(451,796)
Investment income (net of fees)	45,865	450,485
	<u>53,442,873</u>	<u>3,647,849</u>
Purse payments - Chester Downs and Marina, LLC - purse account	(28,326,094)	-
Purse payments - Downs Racing, LP - purse account	(29,499,040)	-
Health insurance payments	-	(1,059,529)
Retirement distributions	-	(125,716)
	<u>(57,825,134)</u>	<u>(1,185,245)</u>
Escrow balance, December 31, 2013	<u>\$ 6,857,217</u>	<u>\$ 19,617,873</u>
	<u>Purses</u>	<u>Benefits</u>
Composition of ending balance:		
Cash and cash equivalents	\$ 6,857,617	\$ 3,132,583
Investments	-	16,485,490
	<u>6,857,617</u>	<u>19,618,073</u>
Opening cash due the Association	<u>(400)</u>	<u>(200)</u>
Ending cash and cash equivalents and investments	<u>\$ 6,857,217</u>	<u>\$ 19,617,873</u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

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

The restricted cash accounts each include 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 2013 is as follows:

	Racing Revenues
Escrow balance, January 1, 2013	\$ 6,561,342
Transfers from Chester Downs and Marina, LLC - racing income	2,277,649
Investment loss (net of fees)	(14,428)
	2,263,221
Racetrack purse pay-outs	(1,027,338)
Racetrack (pari-mutuel) revenues paid to the Association	(628,900)
Bank charges	(443)
	(1,656,681)
Escrow balance, December 31, 2013 - racing revenue	\$ 7,167,882
Composition of ending balance:	
Cash and cash equivalents	\$ 5,182,885
Investments	1,984,997
	\$ 7,167,882
Ending cash and cash equivalents and investments	\$ 7,167,882

Summary of all escrow accounts:

	Purses - Slot Revenue	Benefits - Slot Revenue	Racing Revenue	Total
Cash and cash equivalents	\$ 6,857,217	\$ 3,132,383	\$ 5,182,885	\$ 15,172,485
Investments	-	16,485,490	1,984,997	18,470,487
	\$ 6,857,217	\$ 19,617,873	\$ 7,167,882	\$ 33,642,972
Escrow balance, December 31, 2013				

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

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

Investments are stated at fair value. Fair value and unrealized appreciation (depreciation) at December 31, 2013 and 2012 and are summarized as follows:

	2013			Fair Value
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Mutual Funds:				
Blend	\$ 98,730	\$ 3,688	\$ (614)	\$ 101,804
Value	339,495	18,692	-	358,187
Growth	10,179	5,297	-	15,476
International	49,568	12,569	-	62,137
Other	66,868	-	(18,389)	48,479
Fixed Income - Domestic	4,568,758	59,977	(60,882)	4,567,853
Fixed Income - International	2,253,548	-	(171,404)	2,082,144
Fixed Income - Other	523,019	6,108	-	529,127
Money Market	976,636	-	-	976,636
Total mutual funds	<u>8,886,801</u>	<u>106,331</u>	<u>(251,289)</u>	<u>8,741,843</u>
Exchange Traded Funds:				
Index	330,786	37,390	(882)	367,294
Fixed Income - Domestic	1,907,922	5,687	(46,228)	1,867,381
Fixed Income - International	359,597	3,413	(2,912)	360,098
Fixed Income - U.S. Government	424,896	-	(4,901)	419,995
Equity	561,356	13,838	(1,395)	573,799
Total exchange traded funds	<u>3,584,557</u>	<u>60,328</u>	<u>(56,318)</u>	<u>3,588,567</u>
Corporate Bonds				
Domestic	3,105,510	10,268	(58,029)	3,057,749
Government	534,112	-	(9,574)	524,538
International	968,421	12,046	(7,858)	972,609
Total corporate bonds	<u>4,608,043</u>	<u>22,314</u>	<u>(75,461)</u>	<u>4,554,896</u>
Other Investments				
FS Investment Corporation II	1,110,163	-	(66,349)	1,043,814
FS Energy and Power Fund	515,660	-	(54,000)	461,660
Real Estate Investment Trust	115,000	-	(35,293)	79,707
Total other investments	<u>1,740,823</u>	<u>-</u>	<u>(155,642)</u>	<u>1,585,181</u>
Total investments	<u>\$ 18,820,224</u>	<u>\$ 188,973</u>	<u>\$ (538,710)</u>	<u>\$ 18,470,487</u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

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

	2012			
	Cost	Gross		Fair Value
		Unrealized Gains	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>

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

	2013	2012
Interest and dividends	\$ 574,460	\$ 419,878
Investment fees	<u>(112,499)</u>	<u>(89,827)</u>
Total	<u>\$ 461,961</u>	<u>\$ 330,051</u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

NOTE 3 – FAIR VALUE MEASUREMENTS

The fair value measurement framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described as follows:

Level 1

Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Plan has the ability to access.

Level 2

Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3

Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

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.

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

NOTE 3 – FAIR VALUE MEASUREMENTS (CONTINUED)

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, 2013 and 2012.

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 1 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.

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.

FS Energy and Power Fund: The underlying investments consist principally of income-oriented securities of privately-held energy and power related or energy companies. The Fund is an externally managed, non-diversified, closed-end management investment company that has elected to be regulated as a business development company under the Investment Company Act of 1940, as amended. The Fund's investment policy is to invest at least 80% of total assets in securities of Energy companies defined as those companies that engage in the exploration, development, production, gathering, transportation, processing, storage, refining, distribution, mining, generation or marketing of natural gas, crude oil, refined products or coal. The investment objectives are to generate current income and long-term capital appreciation. The Company determines the net asset value of its investment portfolio each quarter. Securities that are publicly-traded are valued at the reported closing price on the valuation date. Securities that are not publicly-traded are valued at fair value as determined in good faith by the Company's board of trustees with portfolio company valuations which are based on relevant inputs, including, but not limited to, indicative dealer quotes, values of like securities, recent portfolio company financial statements and forecasts, 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, 2013 and 2012

NOTE 3 – FAIR VALUE MEASUREMENTS (CONTINUED)

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.

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, 2013:

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Mutual Funds:				
Blend	\$ 101,804	\$ 101,804	\$ -	\$ -
Value	358,187	358,187	-	-
Growth	15,476	15,476	-	-
International	62,137	62,137	-	-
Other	48,479	48,479	-	-
Fixed Income - Domestic	4,567,853	4,567,853	-	-
Fixed Income - International	2,082,144	2,082,144	-	-
Fixed Income - Other	529,127	529,127	-	-
Money Market	976,636	976,636	-	-
Total mutual funds	<u>8,741,843</u>	<u>8,741,843</u>	<u>-</u>	<u>-</u>
Exchange Traded Funds:				
Index	367,294	367,294	-	-
Fixed Income - Domestic	1,867,381	1,867,381	-	-
Fixed Income - International	360,098	360,098	-	-
Fixed Income - U.S. Government	419,995	419,995	-	-
Equity	573,799	573,799	-	-
Total exchange traded funds	<u>3,588,567</u>	<u>3,588,567</u>	<u>-</u>	<u>-</u>
Fixed Income				
Domestic	3,057,749	-	3,057,749	-
Government	524,538	-	524,538	-
International	972,609	-	972,609	-
Total corporate bonds	<u>4,554,896</u>	<u>-</u>	<u>4,554,896</u>	<u>-</u>
Other Investments				
FS Investment Corporation II	1,043,814	-	-	1,043,814
FS Energy and Power Fund	461,660	-	-	461,660
Real Estate Investment Trust	79,707	-	-	79,707
Total other investments	<u>1,585,181</u>	<u>-</u>	<u>-</u>	<u>1,585,181</u>
Total	<u>\$ 18,470,487</u>	<u>\$ 12,330,410</u>	<u>\$ 4,554,896</u>	<u>\$ 1,585,181</u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

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:

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Fair Value</u>
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>5,433,226</u>	<u>-</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>\$ 13,019,028</u>	<u>\$ 9,378,620</u>	<u>\$ 2,520,035</u>	<u>\$ 1,120,373</u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

NOTE 3 – FAIR VALUE MEASUREMENTS (CONTINUED)

Level 3 Information

The following table sets forth additional disclosures for the measurements of investments in certain entities that calculate net asset value per share (or its equivalent) at December 31, 2013:

Investment Type	Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Other Investments:				
FS Investment Corporation II	\$ 1,043,814	\$ -	3 months	30 days
FS Energy and Power Fund	461,660	-	3 months	30 days

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, 2013 and 2012.

Balance, January 1, 2012	\$ 97,175
Unrealized losses	(23,517)
Purchases	<u>1,046,715</u>
Balance, December 31, 2012	1,120,373
Unrealized losses	(132,025)
Purchases	<u>596,833</u>
Balance, December 31, 2013	<u>\$ 1,585,181</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 Level 3 in 2013 and 2012.

NOTE 4 – ACCOUNTS RECEIVABLE

Accounts receivable consist of the following:

	<u>2013</u>	<u>2012</u>
Pennsylvania Harness Week sponsorships	\$ 43,000	\$ 37,000
Member benefit reimbursements	<u>7,328</u>	<u>9,501</u>
Total	<u>\$ 50,328</u>	<u>\$ 46,501</u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

NOTE 5 – NAMING RIGHTS

The Association recognized an intangible asset in the amount for \$700,000 for the benefits derived from an agreement related to naming rights entered into with Downs Racing, LP. Downs Racing, LP owns and operates a gaming and entertainment facility and harness racing track with pari-mutuel wagering in Wilkes-Barre, Pennsylvania known as Mohegan Sun Pocono Downs. Downs Racing entered into an agreement with the Luzerne County Convention Center Authority for the naming rights to the arena located in Wilkes-Barre. This arena is known as the Mohegan Sun Arena at Casey Plaza through January 2020. In consideration of the mutual benefits that the Association and its members and employees will receive relating to the naming rights granted to Downs Racing, the Association has contracted to contribute to Downs Racing \$100,000 annually during the term of Downs Racing's naming rights agreement. The Association will amortize the intangible asset, naming rights, ratably over the term of the agreement with Downs Racing. The Association recognized \$100,000 of amortization expense related to naming rights during 2013. The Association will recognize \$100,000 of amortization expense annually through 2019.

NOTE 6 – RACE TRACK REVENUES

The Association holds a contract with a harness race track in Pennsylvania, Downs Racing, LP, which expires 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 that expires December 31, 2014. 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.

NOTE 7 – SPECIAL EVENTS

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

	2013	2012
Golf outing:		
Revenue	\$ 25,000	\$ 20,000
Direct expenses	29,847	26,564
Net loss	\$ (4,847)	\$ (6,564)

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

NOTE 8 – FUNCTIONAL CLASSIFICATION OF EXPENSES

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

	<u>2013</u>	<u>2012</u>
Program services:		
Health program	\$ 50,840	\$ 76,597
Pension program	73,453	73,389
Member benefits	1,952,034	2,095,408
Racetrack relations	38,453	39,699
Industry promotion	1,944,016	2,560,094
Regulatory matters	264,230	314,036
Supporting services:		
Management and general	<u>346,738</u>	<u>301,393</u>
Total	<u>\$ 4,669,764</u>	<u>\$ 5,460,616</u>

NOTE 9 – 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 is discretionary and is equal to a uniform percentage as determined by the Employer of each participant's elective deferral. The Association may also make a discretionary nonelective contribution. The Association's discretionary contribution for 2013 and 2012 totaled \$39,000 and \$42,000, respectively.

NOTE 10 – LEASE

The Association leased its office space in Lemoyne, Pennsylvania under a one-year lease which expired April 30, 2014. The rental amount was \$736 per month. Total rent expense for 2013 and 2012 was \$9,300 and \$9,254, respectively.

The Association leases several pieces of equipment under operating leases, with a maturity date of March 2015. Monthly payments total \$418 per month. The rental payments for 2013 and 2012 were \$7,503 and \$5,010, respectively.

Minimum lease payments under these leases are:

Minimum Lease Payments

2014	\$ 10,456
2015	<u>1,878</u>
Total	<u>\$ 12,334</u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

NOTE 11 – LONG TERM PAYABLE

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 2013 and 2012, the Association paid \$100,000. Future payments will be:

2014	\$	100,000
2015		100,000
2016		100,000
2017		100,000
2018		100,000
Thereafter		<u>100,000</u>
Total	\$	<u>600,000</u>

NOTE 12 – 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, 2013 and 2012, the Association had cash on deposit of \$15,528,081 and \$22,902,833, respectively.

For the years ended December 31, 2013 and 2012, revenue includes \$3,128,900 and \$3,450,000, 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.

NOTE 13 – SUBSEQUENT EVENTS

Management evaluated subsequent events through June 23, 2014, the date the financial statements were available to be issued. Events or transactions occurring after December 31, 2013, but prior to June 23, 2014, that provided additional evidence about conditions that existed at December 31, 2013, have been recognized in the financial statements for the year ended December 31, 2013. Events or transactions that provided evidence about conditions that did not exist at December 31, 2013, 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, 2013.

This information is an integral part of the accompanying financial statements.

PENNSYLVANIA RACE HORSE DEVELOPMENT FUND

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS 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, 2013, 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 June 23, 2014.

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 as item 2013-001 and 2013-002 that we consider to be significant deficiencies..

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.



Baltimore, Maryland
June 23, 2014

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS THAT
COULD HAVE A DIRECT AND MATERIAL EFFECT ON PENNSYLVANIA RACE HORSE
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, 2013. 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.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for the Association based on our audit of the compliance requirements described in Chapter 436a of the Pennsylvania Horse Development and Gaming Act 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 the Pennsylvania Horse Development and Gaming Act require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the 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

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, 2013.

Other Matters

The results of our auditing procedures disclosed an instance of noncompliance, which is required to be reported in accordance with Chapter 436a of the Horse Development and Gaming Act and which is described in the accompanying schedule of findings and questioned costs as item 2013-002. Our opinion is not modified with respect to this matter.

The Association's response to the noncompliance finding identified in our audit is described in the schedule of findings and questioned costs. The Association's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

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. However, we identified a certain deficiencies in internal control over compliance, as described in the accompanying schedule of findings and questioned costs as items 2013-001 and 2013-002 that we consider to be significant deficiencies.

The Association's response to the internal control over compliance finding identified in our audit is described in the schedule of findings and questioned costs. The Association's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

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 Chapter 436a of the Pennsylvania Horse Development and Gaming Act. Accordingly, this report is not suitable for any other purpose.

CliftonLarsonAllen LLP

Baltimore, Maryland
June 23, 2014

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
STATEMENT OF CASH RECEIPTS AND CASH DISBURSEMENTS AND CHANGES IN ESCROW BALANCES
Period January 1, 2013 through December 31, 2013

	<u>Purses</u>	<u>Benefits</u>	<u>Total</u>
CASH RECEIPTS			
Gaming Funds - Chester Downs and Marina, LLC	\$ 27,383,835	\$ 1,866,413	\$ 29,250,248
Gaming funds - Downs Racing LLP	26,013,173	1,782,747	27,795,920
Interest and investment income, net of fees	45,865	450,485	496,350
Total cash receipts	<u>53,442,873</u>	<u>4,099,645</u>	<u>57,542,518</u>
CASH DISBURSEMENTS			
Purse payments - Chester Downs and Marina, LLC	28,326,094	-	28,326,094
Purse payments - Downs Racing, LP	29,499,040	-	29,499,040
Health insurance payments	-	1,059,529	1,059,529
Retirement distributions	-	125,716	125,716
Total cash disbursements	<u>57,825,134</u>	<u>1,185,245</u>	<u>59,010,379</u>
OTHER			
Net unrealized and realized losses on restricted investments	-	(451,796)	(451,796)
CHANGES IN ESCROW BALANCES	(4,382,261)	2,462,604	(1,919,657)
ESCROW BALANCE AT JANUARY 1, 2013	<u>11,239,478</u>	<u>17,155,269</u>	<u>28,394,747</u>
ESCROW BALANCE AT DECEMBER 31, 2013	<u>\$ 6,857,217</u>	<u>\$ 19,617,873</u>	<u>\$ 26,475,090</u>

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
NOTES TO THE STATEMENT OF CASH RECEIPTS AND CASH DISBURSEMENTS
AND CHANGES IN ESCROW BALANCES
Period January 1, 2013 through December 31, 2013

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 2013.

**PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
December 31, 2013**

I. Summary of Independent Auditors' Results

Financial Statements

Type of auditors' report issued: Unmodified

Internal control over financial reporting:

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

Pennsylvania Racehorse Development Funds

Type of auditors' report on compliance issued: Unmodified

Internal control over state programs:

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

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
December 31, 2013

II. Financial Statement Findings

Finding Reference: 2013-001
Description: Segregation of Duties
Type of Finding: Significant Deficiency in Internal Control, Compliance

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 review current policies and procedures to determine additional duties which may be segregated or compensating controls which may be instituted. With limited personnel to segregate duties, focus should concentrate on the most vulnerable areas. Accordingly, we believe this focus should be in the areas of cash receipts and disbursements. The Association management and board should continue to closely monitor financial related duties, including the review of interim financial statements at least quarterly.

Management's Response

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

PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
December 31, 2013

III. Pennsylvania Race Horse Development Funds Findings

Finding Reference: 2013-002
Description: Inaccurate Quarterly Reporting
Type of Finding: Significant Deficiency in Internal Control, Compliance

Condition

The fourth quarter report filed with the Pennsylvania Gaming Control Board (the Board) included certain cash receipts and cash disbursements amounts that did not reconcile to the Association's accounting records.

Criteria

Chapter 436a, subsection 5, Reports, requires that the registered horsemen's organizations file quarterly reports with the Pennsylvania Gaming Control Board of a.) funds received from the Race Horse Development Funds through the Category 1 licensee conducting live racing, b.) funds distributed for purse supplements and C.) funds received for health and pension benefits from the account established by and for the benefit of the horsemen.

Cause

The Association did not sufficiently monitor controls to ensure compliance with Chapter 436a, reporting requirements of the Pennsylvania Gaming Control Board.

Effect

The Association is not in compliance with Chapter 436a, Reports.

Recommendation

We recommend that management amend the incorrect quarterly report and review current procedures and controls to ensure future reports are accurately filed. Management filed a corrected fourth-quarter report with the Gaming Control Board as of the financial statement date.

Management's Response

PHHA has filed a corrected fourth quarter report with the Gaming Board. The difference was due to an inadvertently missed deposit when summing total cash receipts for the quarter, and timing differences.

**PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS
December 31, 2013**

PRIOR YEAR FINDING

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.

Status:

Repeat Finding No. 2013-001. PHHA is still considering additional staffing.

**PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS
December 31, 2013**

PRIOR YEAR FINDING

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.

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.

Status:

Remitting insurance contracts to the Gaming Board within 90 days of their effective date is no longer a requirement.

**PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS
December 31, 2013**

PRIOR YEAR FINDING

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 Race horse 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 Race horse 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 to 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.

Status:

Repeat Finding No. 2013-002. As of December 31, 2013, PHHA has not effectively implemented procedures to prevent or detect errors in quarterly reporting to the Gaming Board.

MEMBERSHIP 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 PLANS**

- 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) – 25 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
SCHEDULE OF MEMBERSHIP BY STATE**

State	Number of Members
Canada	10
CT	4
DE	73
FL	33
IA	1
IL	11
IN	2
Ireland	1
KY	2
MD	30
NC	3
NH	1
NJ	122
NY	48
OH	9
PA	342
TN	1
VA	1
WV	1
TOTAL MEMBERS AS OF DECEMBER 31, 2013	695

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

<u>State</u>	<u>Participants</u>
PA	80
NJ	35
MD	6
FL	3
DE	5
NY	4
VA	2
RI	1
NC	<u>1</u>
TOTAL PARTICIPANTS AS OF DECEMBER 31, 2013	<u><u>137</u></u>

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

State	Number of Participants
Driver	7
Employee	3
Groom	28
Spouse	1
Trainer	84
Trainer Driver	<u>14</u>
TOTAL PARTICIPANTS AS OF DECEMBER 31, 2013	<u><u>137</u></u>

**PENNSYLVANIA HORSEMEN'S ASSOCIATION
PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
SCHEDULE OF RETIREMENT PLAN PARTICIPANTS SUMMARY**

State	Number of Participants- Drivers	Number of Participants- Trainers	Number of Participants- Total
AUSTRALIA	-	1	1
CANADA	3	5	8
CT	-	1	1
DE	12	51	63
FL	4	15	19
IL	1	7	8
KT	-	1	1
ME	-	1	1
MD	2	19	21
NC	-	2	2
NJ	23	91	114
NY	8	18	26
OH	1	7	8
PA	24	133	157
	<u>78</u>	<u>352</u>	<u>430</u>

**PENNSYLVANIA HORSEMEN'S ASSOCIATION
PENNSYLVANIA HARNESS HORSEMEN'S ASSOCIATION
SCHEDULE OF RETIREMENT PLAN PARTICIPANTS BY CATEGORY**

State	Number of Participants
Trainer	323
Driver	<u>75</u>
TOTAL PARTICIPANTS AS OF DECEMBER 31, 2013	<u><u>398</u></u>

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

TRAINERS

Range of Starts	Number of Participants
Under 35	61
35-69	117
70-104	54
105-139	36
>=140	<u>55</u>
TOTAL PARTICIPANTS AS OF DECEMBER 31, 2013	<u><u>323</u></u>

DRIVERS

Range of Starts	
Under 50	12
50-99	23
100-149	5
150-199	5
>=200	<u>30</u>
TOTAL PARTICIPANTS AS OF DECEMBER 31, 2013	<u><u>75</u></u>