

Terry E. Branstad
Governor

Kim Reynolds
Lt. Governor



Terry Rich
Chief Executive Officer

Iowa Lottery Report On Operations

To: Members of the House Government Oversight Committee and Senate Government Oversight Committee

From: Terry Rich, CEO

Date: December 2015

The Iowa Lottery finished fiscal year 2015 with annual results among the Top 4 in its 30-year history, and its sales and proceeds in the current year continue to run ahead of budget through November.

The lottery puts emphasis on having variety in the games it has in the marketplace to give choices to consumers. We believe those efforts are reflected in our successful results.

We know that lottery results can and will fluctuate from year to year, but we anticipate that lottery games will continue to be a consistent, key source of proceeds for vital state causes here in Iowa.

Lottery sales in FY 2015 totaled more than \$324 million, marking the fourth year in a row that they have topped the \$300 million mark. Proceeds to state causes totaled nearly \$75 million, the fourth-highest amount for the lottery since its start in 1985. Prizes to lottery players totaled \$197 million in FY 15, the second-highest total in the lottery's history. And local Iowa businesses received nearly \$21 million in commissions from the lottery for selling its products in FY 2015.

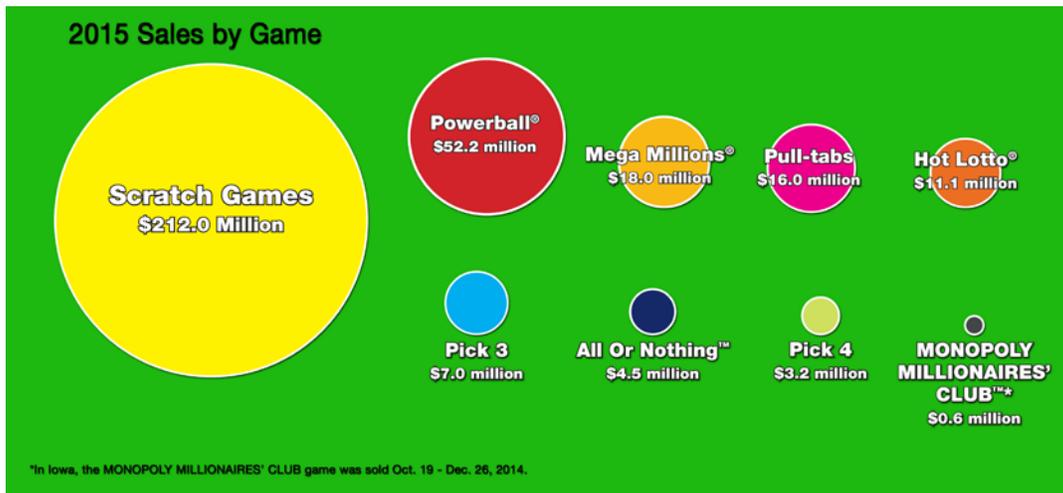
Here is a year-to-year comparison of lottery product sales in the last two fiscal years:

	<u>FY 2015</u>	<u>FY 2014</u>
Instant-scratch games	\$212 million	\$188.8 million
Pick 3	\$7 million	\$6.9 million
Powerball	\$52.2 million	\$61.2 million
Mega Millions	\$18 million	\$21.8 million
Hot Lotto	\$11.1 million	\$10.4 million
Pick 4	\$3.2 million	\$3.2 million
Iowa's \$100,000 Cash Game	\$ -----	\$2.5 million
All or Nothing*	\$4.5 million	\$3.2 million
Pull-tab games	\$16 million	\$15.7 million
Raffle game**	\$ -----	\$0.2 million
Monopoly Millionaires' Club***	\$0.6 million	\$ -----

*The All or Nothing lotto game replaced Iowa's \$100,000 Cash Game. All or Nothing began sales in January 2014.

**The lottery offers raffle games only occasionally, so there will be years, such as FY 2015, when it does not sell such a product.

***The Monopoly Millionaires' Club game was sold from October-December 2014.



As always, we are closely tracking lottery results and will keep your committees apprised of significant developments. We also provide regular updates about sales and proceeds through the state's I-3 accounting system for review. The lottery's latest financial performance figures (through November 2015) are included in this report as **Attachment A**.

Eastern Iowa Lottery Sales Related To Illinois Budget Situation



A situation involving the state budget in Illinois has had a positive impact on lottery sales in eastern Iowa.

Because of an ongoing budget impasse in the state of Illinois, the Illinois Lottery was unable to pay prizes of more than \$25,000 beginning in August. Then on Oct. 15, that threshold was lowered to any prize of more than \$600, again because of the ongoing budget impasse. Anyone who won a lottery prize larger than that was given an IOU.

That situation continued through mid-December, when legislation was signed that provided legal authority for the Illinois Lottery to resume prize payments.

During the months that many lottery prizes could not be paid in Illinois, it appears that some residents from that state crossed the Mississippi River to buy tickets in Iowa, as sales in areas along Iowa's eastern border saw a bump up.

Through late November, statewide lottery sales in Iowa had increased by about 3 percent from the same time period the prior year. But of the eight Iowa counties that border Illinois, five had seen sales increases that far outpaced the statewide average. Some retail locations near the bridges spanning the river between Iowa and Illinois saw significant sales increases ranging as high as 63 percent, which the lottery believes is attributable at least in part to the situation in Illinois.

FY 2017 Budget Updates

In prior reports to your committees, we have noted that the Iowa Lottery Board approved the lottery's preliminary budgets for FY 2016 and FY 2017 in September 2014 in accordance with state budgeting guidelines. The FY 2016 budget was then given final approval by the Lottery Board in June just prior to the start of the fiscal year. And at the Board's Sept. 29 meeting, members approved adjustments to the lottery's FY 2017 budget to adjust for salary and benefit increases that have been approved for the AFSCME contract and adjust other line items to more closely align with the FY 15 actual expenses.

The lottery's anticipated results for sales and proceeds during both years are an increase from the lottery's budgeted figures for FY 2015.

Copies of the lottery's Overall Budget and Operating Expenses for FY 2017 are included with this report as **Attachments B** and **Attachment C**.



Matt McDermott



Mike Klappholz



Connor Flynn



Mary Rathje



Ying Sa



Michael Fitzgerald

The members of the Lottery Board are: Chairperson Matt McDermott of West Des Moines, a shareholder at a Des Moines law firm; Vice Chair Mike Klappholz of Marion, a retired Cedar Rapids police chief; Connor Flynn Jr., chairman of an advertising agency in Des Moines, where he also resides; Mary Rathje, manager and controller at a construction company in Marion, where she also resides; Ying Sa, the founder and principal certified public accountant at a CPA firm in Des Moines, where she also resides; and State Treasurer Michael Fitzgerald, who serves on the Board as a nonvoting member.

Ongoing Lottery Jackpot Investigation



The long-running lottery jackpot investigation that began here in Iowa has been expanded again, now involving jackpot prizes in five states: Iowa, Colorado, Kansas, Oklahoma and Wisconsin.

At the time that all of the jackpots were won, the man charged in the case worked as an information security consultant at a vendor organization within the lottery industry. That man, Eddie Tipton, later became the director of information security at that same vendor organization, the Multi-State Lottery Association (MUSL), which is based in Urbandale. MUSL handles day-to-day functions such as prize drawings in some lotto games on behalf of U.S. lotteries. In his work at MUSL, Tipton evaluated security systems at many U.S. lotteries and provided other information-technology duties, including software programming.

Tipton was convicted in July on two felony counts of fraud in the case that started the investigation nearly five years ago: the attempted claim of a lottery jackpot in 2010 here in Iowa. Then in October, a felony charge of ongoing criminal conduct was filed against Tipton that initially encompassed lottery

jackpot prizes won in three different states: the attempted claim here in Iowa; a jackpot claimed in 2005 in Colorado; and another in 2007 in Wisconsin. Another jackpot prize claim from 2011 in Oklahoma was incorporated into the criminal conduct charge in November, and in December, two jackpot claims from 2010 in Kansas also were added into the charge.

Tipton is charged with violating Iowa's ongoing criminal conduct statute. The criminal complaint against him stipulates that he helped build the random-number generator equipment used in the jackpot drawings for the prizes involved. The complaint also stipulates that according to court testimony earlier this year, he had the technical ability and opportunity to tamper with the drawing equipment that picks the winning lottery numbers in order to make the numbers predictable.

The Iowa and Oklahoma jackpots were both won in the multi-state Hot Lotto game, while the jackpots in Colorado and Wisconsin were won in different games offered only in those states. The Kansas jackpots also were won in a separate game.

This remains an active, ongoing investigation, with officials continuing to gather and review evidence.

From the beginning, we here at the Iowa Lottery asked investigators to follow the evidence wherever it leads to help us get to the bottom of the situation. This latest development is another step in the process to protect lotteries, our games, our players and the billions of dollars at stake for the worthy causes that lotteries benefit.

FY 2016 Lottery Transfer To Iowa Veterans Trust Fund

The Iowa Lottery made its FY 2016 contribution of \$2.5 million to the Iowa Veterans Trust Fund (IVTF) as part of its quarterly proceeds transfer to state causes in late October. That brings the total that the lottery has raised for the IVTF since 2008 to nearly \$20 million.



On July 1, a change in state law took effect regarding lottery proceeds to the IVTF. As of that date, the process by which the lottery raises proceeds for veterans' causes changed from specific games dedicated to the cause to a set amount in proceeds – \$2.5 million – going to the IVTF each year.

Moving ahead, we anticipate that the lottery will continue to make a \$2.5 million annual contribution to the IVTF each October. A portion of the proceeds from the sale of all lottery games now is dedicated to the Veterans Trust Fund.

Art In State Buildings Project At Lottery Headquarters



In November, 15 metal sculptures of clovers “sprouted up” at lottery headquarters as part of the Art in State Buildings Program.

The Iowa Lottery's purchase and renovation of its headquarters location at 13001 University Ave. in Clive met the requirements of the art program, which was enacted by state lawmakers in 1979 to ensure that fine arts are a part of eligible state building construction projects.

Iowa Code language specifies that one half of one percent of the total cost of an eligible state building project will be used to include fine arts into the building, renovation or addition to an existing building.

The lottery ultimately chose a concept from Des Moines artists TJ Moberg and Dennis Reynolds for its art project. They proposed metal sculptures of clovers to represent lottery luck while also creating eye-catching artwork.

The sculptures were installed in November, ranging in size from 12 inches up to 5 feet in diameter. Moberg and Reynolds selected a variety of materials and finishes that bring additional depth of meaning to the project.

For example, one of the clovers is made from pieces of an old corn crib to represent Iowa's agricultural heritage and our state's leadership in developing new products and techniques in agriculture. Another clover is cut from the top of an old school bus to represent education, one of the largest recipients of money from the state General Fund, which receives a portion of lottery proceeds each year. Still another of the clovers has five leaves, one for each branch of the U.S. Armed Forces, and is imprinted with the logo for the Iowa Veterans Trust Fund, which receives a portion of lottery proceeds each year.

The lottery has added a page to its website with full details about the art project, including pictures and an explanation about each of the clovers. Here is a direct link:

<http://www.ialottery.com/AboutUs/ArtInStateBuildings.asp>

Two Winners of \$1 Million On The Same Day

Nov. 23 was an unusual day at the Iowa Lottery, with two winners of \$1 million prizes in the Mega Millions® game both claiming their winnings at lottery headquarters. And they're both from southeastern Iowa.

Betty Downs of Burlington was the first to arrive, but shortly after she got to the lottery, Mike Hartman from Winfield came in with his own winning ticket. He joked that if they had known, they could have carpooled.



Downs, 75, who is retired, won her \$1 million prize in the Mega Millions drawing on Nov. 10, but didn't realize she'd won a prize until she checked her ticket several days later. Hartman, 49, a Marine Corps veteran who now drives a truck and has his own business, won his big prize in the Nov. 20 drawing. They both won with easy-pick tickets.

Downs bought her winning ticket at the River Mart convenience store, 2107 Agency St. in Burlington, while Hartman hit big with a ticket he bought at the Countrestore, 2455 120th St. in Winfield. Both businesses received a \$1,000 bonus from the lottery for selling a \$1 million-winning ticket.

Downs and Hartman claimed the fifth and sixth Iowa Lottery tickets, respectively, to win prizes of \$1 million in calendar year 2015.

Internet Gambling Discussions In D.C.

Members of the Iowa Lottery's leadership team continue to work with Iowa's Office of State and Federal Relations to provide information about the regulation of Internet gaming to members of our state's Congressional delegation.

Terry Rich and Mary Neubauer were part of Congressional visits March 24-25 on behalf of the North American Association of State and Provincial Lotteries (NASPL). At the time, Terry was the president of NASPL, the industry group that represents lotteries in the United States, Canada and Mexico.



Three pieces of legislation concerning the federal regulation of Internet gaming have been filed in the current session of Congress: H.R. 707 from U.S. Rep. Jason Chaffetz, R-Utah, and S-1668 from U.S. Sen. Lindsey Graham, R-S.C., who each propose differing federal prohibitions on some forms of Internet wagering; and H.R. 2888 from U.S. Rep. Joe Barton, R-Texas, which would allow online poker.

A Congressional hearing was held Dec. 9 regarding H.R. 707 before the U.S. House Committee on Oversight and Government Reform.

The Iowa Lottery and NASPL respectfully urge opposition to any legislation that would pre-empt or encroach on states' sovereignty regarding gaming matters. Multi-state lottery games such as Powerball® and Mega Millions® already are conducted across multiple jurisdictions, as is pari-mutuel wagering. The states have a long and successful history of joining together to provide gaming options that appeal to their citizens while complying with both state and federal law.

Members of the National Governor's Association (NGA), the National Council of Legislators from Gaming States (NCLGS), and the National Conference of State Legislators (NCSL) have all contacted Congressional leadership in recent months, urging Congress to include state input in any decisions at the federal level that could affect state regulatory authority concerning gaming; and to respect the sovereignty of states in deciding if they want to participate in online gaming.

The Iowa Lottery has the authority to conduct Internet gaming and continues to study the issue, remaining cognizant of the fact that there would be a negative impact on proceeds to state causes if it does not adapt to player expectations for convenience and use of technology. The lottery will continue to monitor developments on the federal level to analyze their potential impact on Iowa.

IOWA LOTTERY
PERFORMANCE MEASURES
FY 2016

Attachment A

		JUL	AUG	SEP	OCT	NOV		DEC	JAN	FEB	MAR	APR	MAY	JUN
Month														
Gross Sales	Budget '16	23,834,084	25,461,659	23,733,551	24,811,289	27,194,561		26,705,439	26,858,803	29,997,407	31,388,556	27,291,539	28,928,003	24,945,109
	5-year av.	23,411,245	25,009,945	23,312,496	24,371,114	26,712,104		26,231,659	26,382,303	28,787,466	30,153,935	26,129,603	27,737,035	23,824,802
	Actual '16	25,907,997	25,180,933	26,791,422	26,284,951	25,413,630		-	-	-	-	-	-	-
Prize Expense	Budget '16	14,116,232	15,080,197	14,056,689	14,695,002	16,106,544	59.23% 1)	15,816,852	15,907,685	17,766,588	18,590,525	16,163,982	17,133,211	14,774,260
	5-year av.	14,170,986	14,598,857	13,709,047	14,346,043	15,220,681	56.98% 2)	16,164,184	16,073,258	17,141,508	17,868,628	15,188,040	16,429,395	14,296,686
	Actual '16	15,690,151	15,581,596	15,908,821	16,370,729	14,944,595	58.81% 3)	-	-	-	-	-	-	-
Operating Expenses	Budget '16	503,008	1,092,391	1,579,119	953,326	1,092,391		1,092,391	1,092,391	1,092,391	1,579,119	1,092,391	953,326	2,039,118
	5-year av.	508,168	841,926	1,067,719	1,035,796	1,004,500		862,588	923,101	979,081	1,002,573	1,087,245	1,021,482	1,419,524
	Actual '16	452,290	958,895	1,402,002	832,037	950,019		-	-	-	-	-	-	-
Total Proceeds	Budget '16	5,680,642	5,513,526	4,578,448	5,483,856	5,963,120		5,836,220	5,876,009	6,690,306	6,564,506	5,988,281	6,551,919	4,432,783
	5-year av.	5,566,219	6,066,103	6,037,982	6,196,005	7,314,599		5,605,872	6,159,970	7,271,757	7,422,268	6,634,641	6,935,723	4,809,997
	Actual '16	6,188,361	5,102,911	6,813,453	5,656,822	6,099,550		-	-	-	-	-	-	-
YEAR TO DATE														
Gross Sales	Budget '16	23,834,084	49,295,743	73,029,294	97,840,583	125,035,144		151,740,583	178,599,386	208,596,793	239,985,349	267,276,888	296,204,891	321,150,000
	5-year av.	23,411,245	48,421,190	71,733,686	96,104,800	122,816,904	5.51% 4)	149,048,563	175,430,866	204,218,332	234,372,267	260,501,870	288,238,905	312,063,707
	Actual '16	25,907,997	51,088,930	77,880,352	104,165,303	129,578,933	3.63% 5)							
Prize Expense	Budget '16	14,116,232	29,196,429	43,253,118	57,948,120	74,054,664	59.23% 1)	89,871,516	105,779,201	123,545,789	142,136,314	158,300,296	175,433,507	190,207,767
	5-year av.	14,170,986	28,769,843	42,478,890	56,824,933	72,045,614	58.66% 2)	88,209,798	104,283,056	121,424,564	139,293,192	154,481,232	170,910,627	185,207,313
	Actual '16	15,690,151	31,271,747	47,180,568	63,551,297	78,495,892	60.58% 3)							
Operating Expenses	Budget '16	503,008	1,595,399	3,174,518	4,127,844	5,220,235		6,312,626	7,405,017	8,497,408	10,076,527	11,168,918	12,122,244	14,161,362
	5-year av.	508,168	1,350,094	2,417,813	3,453,609	4,458,109		5,320,697	6,243,798	7,222,879	8,225,452	9,312,697	10,334,179	11,753,703
	Actual '16	452,290	1,411,185	2,813,187	3,645,224	4,595,243								
Total Proceeds	Budget '16	5,680,642	11,194,168	15,772,616	21,256,472	27,219,592		33,055,812	38,931,821	45,622,127	52,186,633	58,174,914	64,726,833	69,159,616
	5-year av.	5,566,219	11,632,322	17,670,304	23,866,309	31,180,908	-4.23% 4)	36,786,780	42,946,750	50,218,507	57,640,775	64,275,416	71,211,139	76,021,136
	Actual '16	6,188,361	11,291,272	18,104,725	23,761,547	29,861,097	9.70% 5)							

- 1) Budget FY16 Prize Payout
- 2) Actual 5-year average Prize Payout
- 3) Actual FY16 Prize Payout
- 4) Actual FY16 compared to Actual 5-year average
- 5) Actual FY16 compared to Budget FY16

Budget for Lottery Fund

Attachment B

	FY 2014 ACTUAL	FY 2015 ACTUAL	FY 2016 BOARD APPROVED FINAL BUDGET	FY 2017 BOARD APPROVED BUDGET
<u>Resources</u>				
Lottery sales	314,055,429	324,767,416	321,150,000	321,020,000
Interest income	51,716	76,038	500,000	500,000
Application fees	4,375	3,800	5,000	5,000
Other	99,932	6,220	5,000	5,000
Total Resources	314,211,452	324,853,474	321,660,000	321,530,000
<u>Expenses and Change in Net Assets</u>				
Prizes	186,948,985	196,882,289	190,207,767	189,611,640
Retailer compensation	20,131,428	20,977,399	20,586,201	20,735,345
Advertising production and media purchases	6,933,352	6,766,994	12,846,000	12,840,800
Retailer Lottery system/Terminal Communications	6,453,429	6,733,505	7,643,516	7,503,301
Instant/Pull-tab ticket expense & machine maintenance	4,077,813	3,890,208	4,593,000	3,942,000
Vending machines/Ticket dispensers	81,787	177,000	1,723,333	2,018,000
Courier delivery of instant tickets	322,729	572,194	710,000	660,000
Interest expense	12,622	8,046	3,805	-
Lottery operating expense	12,073,776	12,408,648	14,161,362	14,559,330
Building (purchase and sale)	3,432,016	-	-	-
Increase (decrease) in net assets	(202,339)	1,920,125	25,400	(85,000)
Total Expenses and Change in Net Assets	240,265,598	250,336,406	252,500,384	251,785,416
<u>Proceeds</u>				
Proceeds Transfer to General Fund	72,141,420	72,365,900	66,659,616	67,244,584
Proceeds Transfer to Veterans Trust Fund	1,804,434	2,151,167	2,500,000	2,500,000
Total Proceeds Transfers	73,945,854	74,517,068	69,159,616	69,744,584
Total Expenses and Proceeds	314,211,452	324,853,474	321,660,000	321,530,000

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Lottery Operations - Budget Detail

Attachment C

	FY 2014 ACTUAL	FY 2015 ACTUAL	FY 2016 BOARD APPROVED FINAL BUDGET	FY 2017 BOARD APPROVED BUDGET
Administrative payroll*	9,461,004	9,565,122	10,965,362	11,443,330
Travel	400,279	410,225	495,000	435,000
Supplies	88,328	99,454	125,000	105,000
Printing	20,435	6,291	20,000	20,000
Postage	6,993	6,118	7,000	7,000
Communications	178,880	227,509	180,000	180,000
Rentals	307,286	308,922	320,000	320,000
Utilities	120,101	126,902	101,000	101,000
Professional fees	123,287	157,782	260,000	220,000
Outside services and repair	256,838	289,302	246,000	315,000
Data processing	89,573	105,400	90,000	110,000
Equipment	220,684	329,016	370,000	386,000
Reimbursement to state agencies	424,834	418,625	495,000	480,000
Depreciation	287,356	278,004	400,000	350,000
Other expenses	87,898	79,976	87,000	87,000
Total operating expenses	\$ 12,073,776	\$ 12,408,648	\$ 14,161,362	\$ 14,559,330

* FY 2017 Budget for "Administrative Payroll" includes salary and benefit cost increases per DOM projections (as a change from FY 2016 Final)