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 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: June 2017**

**The Iowa Lottery finished fiscal year 2017 with strong sales and proceeds to state causes; another clean audit; and announcement of guilty pleas in the long-running lottery jackpot investigation that began with a prize won in Iowa but never paid.**

Those looking at the numbers will see a noticeable difference, however, in lottery financial results from FY 2016 to FY 2017, stemming mainly from the world-record Powerball jackpot drawing of nearly \$1.6 billion in January 2016. Sales leading up to that drawing ultimately produced record results for lotteries across the country, including the Iowa Lottery. Understanding that lottery results can and do fluctuate over time, we at the Iowa Lottery continue to budget conservatively and base our sales and proceeds projections on a five-year rolling average. We do our best to factor in the natural fluctuations in lottery results that will occur and should be expected.

Statistically, we know that lottery results will fluctuate from year to year, but the tide has steadily risen for lottery sales in the past few years. We anticipate that lottery games will continue to be a consistent, key source of proceeds for vital state causes here in Iowa.

Lottery sales through May had topped \$322 million for FY 2017 and were well ahead of the lottery's budgeted results with one month still remaining in the fiscal year. Here is a year-to-year comparison of lottery sales (July-May) by product:

	<u>FY 2017</u>	<u>FY 2016</u>
Instant-scratch games	\$218 million	\$214.7 million
InstaPlay games*	\$5.2 million	-----
Pick 3	\$6.7 million	\$6.8 million
Powerball	\$49.2 million	\$71 million
Mega Millions	\$13.7 million	\$13.7 million
Hot Lotto	\$7.5 million	\$8.1 million
Pick 4	\$3.6 million	\$3.2 million
All or Nothing	\$2.9 million	\$3.7 million
Lucky for Life	\$5.2 million	\$2.6 million
Pull-tab games	\$10.5 million	\$13.9 million

\*InstaPlay games were introduced in Iowa in November 2016.

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. The lottery's latest monthly financial statement is included in this report as **Attachment A**.

## **FY 2018 Budget Updates**

At the Lottery Board's meeting on June 27, the lottery's FY 2018 budget was given final approval to adjust some line items to more closely align with FY 2016 actual expenses and to reflect sales from the products that the lottery plans to have in the field during the year.

Copies of the lottery's Overall Budget and Operating Expenses for FY 2018 are included with this report as **Attachment B** and **Attachment C**.



Mike Klappholz



Connor Flynn



Mary Rathje



Mary Junge



Michael Fitzgerald

The members of the Lottery Board are: Chairperson Mike Klappholz of Marion, a retired Cedar Rapids police chief; Vice Chair 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 resides; Mary Junge of Cedar Rapids, a CPA and practicing tax- and estate-planning attorney; and State Treasurer Michael Fitzgerald, who serves on the Board as a nonvoting member. (One position of the Board is currently vacant.)

## **Guilty Pleas In Long-Running Lottery Jackpot Investigation**



Two men pleaded guilty in June to theft and fraud charges in the long-running lottery jackpot investigation that began with a lottery prize that was won in 2010 in Iowa but ultimately never paid.

Eddie Tipton, formerly of Norwalk, Iowa, and his younger brother Tommy Tipton of Flatonia, Texas, have reached comprehensive plea agreements that will resolve all pending criminal proceedings relating to the attempt to claim the 2010 Hot Lotto® jackpot prize in Iowa, as well as lottery prizes paid in Wisconsin, Kansas, Oklahoma and Colorado.

At the time that all the jackpots were won, Eddie Tipton worked as an information security consultant at a vendor organization within the lottery industry. He later became the director of information security at that 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.

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.

As a first step in the process, Eddie Tipton pleaded guilty on June 12 in Wisconsin to a felony charge of theft by fraud and a felony charge of a computer crime. Eddie Tipton then pleaded guilty on June 29 to a single count of felony ongoing criminal conduct in Iowa's Polk County District Court. Tommy Tipton also pleaded guilty that day in Iowa to a felony and a misdemeanor count of conspiracy to commit theft.

Tommy Tipton was then immediately sentenced and ordered to report to jail in Texas no later than July 1. He was sentenced to 75 days' incarceration and associated probation and ordered pay to a civil penalty of \$5,000 and make restitution totaling \$804,095 to the Colorado and Oklahoma Lotteries.

Eddie Tipton will be sentenced at a date yet to be determined.

The plea agreement is a crucial step in bringing to a close one of the biggest lottery mysteries in history. The details we've already learned through this long-running investigation have allowed us at the Iowa Lottery to develop security enhancements across our games and procedures, and we remain mindful of the need to continually review our operations to make improvements.

It was important to us at the Iowa Lottery to hear Eddie Tipton acknowledge in court that he wrote malicious computer code, then used that code to predict winning numbers in lottery drawings and passed those numbers to others, including his younger brother, Tommy, multiple times in years past to fraudulently claim prizes. This information will be invaluable to the Iowa Lottery and the lottery industry as a whole to help us safeguard our games and protect our players.

We at the Iowa Lottery are thankful for the extensive work in this nationwide lottery investigation by the Iowa Division of Criminal Investigation, the Iowa Attorney General's office and authorities from around the country.

As this case reaches conclusion and Eddie Tipton's sentencing occurs, we look forward to the process to help answer any remaining questions about exactly what occurred. We have said through the entire process that the Iowa Lottery would follow the facts of the investigation wherever they may lead.

We continue to have confidence that Iowa Lottery games today are fair. Our lottery has strong layers of security in place to protect our players, our games and lottery prizes. We will continue to do all we can to protect the integrity of our lottery games.

### **Changes In Lottery's Voluntary Self-Exclusion Program**

At its meeting June 27, the Iowa Lottery Board approved a policy change so that the specifics of the Iowa Lottery's voluntary self-exclusion program match up with those signed into law this spring for Iowa casinos in SF 442.

When lawmakers were debating the self-exclusion changes on the casino side, lottery representatives said that if the legislation were signed into law, we would ask the Lottery Board to make similar changes to lottery policy so we would utilize a consistent approach.

As background, the Iowa Lottery has had a self-exclusion program since 2005, established by Iowa Lottery Board policy. The goal of the program today remains the same as it was at implementation: to provide one more tool that people can use in their efforts to address the issue of problem gambling.

Under state law, the Iowa Lottery pays prizes for tickets that are valid and are winners, but the Lottery Board is empowered to establish validation criteria. So, for example, some of the security criteria established are that tickets cannot be cashed if they are stolen, counterfeit, altered or unreadable. State law also empowers the Board to establish lottery policies.

The lottery's self-exclusion policy and that for Iowa casinos utilize slightly different approaches but have the same goal: to provide a deterrent for someone who is being impacted by problem gambling.

On the casino side, a voluntary self-exclusion means that the person signing the ban can't enter the wagering area (defined as the gaming floor) at a state-regulated casino in Iowa. However, should the person still find a way to enter the gaming floor, any prize that he or she tried to claim at the casino would be denied.

On the lottery side, a voluntary self-exclusion bans the person from the lottery's five regional offices and allows the lottery to deny payment of any prize at a lottery office to that person. That eliminates the person's ability to ever claim a big lottery prize, since all prizes of more than \$600 must be claimed directly from the lottery. The lottery also removes from any mailing or promotional lists the names of those players who have entered into its self-ban contract. It is our belief that this approach can help take away the incentive to play lottery games for those who have issues with compulsive behavior.

With the changes in law that will take effect July 1, the self-ban program for state-regulated casinos will involve two separate groups: Those who signed casino self-exclusion forms on June 30, 2017, or before; and those who sign self-exclusion forms on July 1, 2017, or after.

For those who signed a self-exclusion form on June 30 or before:

- The Iowa Racing and Gaming Commission has established a process to allow anyone on the casino self-exclusion list for at least five years to request re-instatement of his/her ability to visit the gaming floor of an Iowa casino. Once the person applies, his/her information has been verified with the statewide self-exclusion list and it is confirmed that the person has been on the list for at least five years, that person would be removed from the list and would again be able to visit the wagering area of a casino.
- Anyone on the self-exclusion list for state-regulated casinos in Iowa for less than five years who requests to be removed will be informed that he/she must wait until at least the five-year mark to apply for re-instatement.

For those who sign a self-exclusion form on July 1 or after:

- Anyone signing a casino self-exclusion form will have two options: a five-year voluntary self-exclusion or a lifetime, irrevocable voluntary exclusion. *(Please note that the lifetime option will still be irrevocable after July 1.)* In an effort to ensure the

person applying for self-exclusion is aware of the help available in Iowa for problem gaming, the person making the request will be presented with information about the Iowa Gambling Treatment Program and 1-800-BETSOFF, the program's 24-hour hotline for assistance.

The Lottery Board voted 4-0 to change the Lottery's Voluntary Self-Exclusion Policy as of July 1, 2017, to also include a five-year option. With the changes, the self-ban program for the lottery also will involve two separate groups: Those who signed lottery self-exclusion forms on June 30, 2017, or before; and those who sign self-exclusion forms on July 1, 2017, or after.

For those who signed a self-exclusion form on June 30 or before:

- Anyone on the lottery's self-exclusion list for at least five years can request that the lottery remove them from the list. Once the person's information has been verified with the lottery's self-exclusion list and it is confirmed that the person has been on the list for at least five years, that person would be removed from the list and would again be allowed to visit lottery offices.
- Anyone on the lottery's self-exclusion list for less than five years who applies to be removed from it will be informed that he/she must wait until at least the five-year mark to apply for re-instatement.

For those who sign a self-exclusion form on July 1 or after:

- Anyone signing a lottery self-exclusion form will have two options: a five-year voluntary self-exclusion or a lifetime, irrevocable voluntary exclusion. *(Please note that the lifetime option will still be irrevocable after July 1.)* In an effort to ensure that the person applying for self-exclusion is aware of the help available statewide for problem gaming, the person making the request will be presented with information about the Iowa Gambling Treatment Program and 1-800-BETSOFF, the program's 24-hour hotline for assistance.

## **\$2 Million Lottery Prize Claimed Nine Months After It Was Won**



A \$2 million Powerball® prize that remained unclaimed for nine months finally went home with the winner, Jeff Wolf of Iowa City, who claimed his winnings on April 27.

Wolf said he had known since shortly after the July 16 Powerball drawing that he had won a big prize. He said he took his time to claim the winnings while he thought through what to do with the money. He plans to invest.

Wolf, 54, who owns two mobile home parks in the Iowa City area, said that the convenience store where he bought his winning ticket is near an automotive supply store in Cedar Rapids where he buys truck parts. He remembers stopping to buy some easy-pick plays for the July 16 drawing.

He said that a couple days after the drawing, he called the Iowa Lottery's winning numbers line and realized that one of the plays on his ticket had matched the first five winning numbers. Wolf said he told only his sister about his big win and put the ticket away in a safe place. But after realizing in late April that time was passing by, he decided to claim the prize.

Wolf said he was aware that people were wondering about the mystery lottery winner in Cedar Rapids. He said he even happened to drive by the convenience store as the lottery held a news conference there in August about the unclaimed prize. But he said he was happy to lay low as he continued to think through his plans.

Wolf bought his \$2 million-winning ticket at the Hawkeye Convenience Store, 2330 Wiley Blvd. SW in Cedar Rapids. He initially matched the first five numbers but missed the Powerball to win a \$1 million prize in the July 16 drawing. But he also had added the Power Play<sup>®</sup> option to the purchase, which multiplied his prize to \$2 million. Hawkeye Convenience Store received a \$2,000 bonus from the lottery for selling the \$2 million-winning ticket at one of its stores.

Powerball prizes in Iowa expire a year from the date of the drawing in which a prize is won.

**IOWA LOTTERY AUTHORITY**  
**Statement of Revenues, Expenses and Changes in Net Position**  
**For the Eleven Months Ending Wednesday, May 31, 2017**

	Month ended 5/31/2017	Month ended 5/31/2016	Year-to-date 5/31/2017	Year-to-date 5/31/2016
<b>Operating revenues:</b>				
Instant-scratch ticket sales	\$22,024,009.00	\$20,758,858.00	\$217,982,429.00	\$214,636,651.00
InstaPlay sales	904,594.00	-	5,211,794.00	-
Pick 3 sales	664,329.00	624,138.50	6,690,682.50	6,802,213.00
Powerball sales	4,874,424.00	4,975,110.00	49,153,247.00	71,029,510.50
Mega Millions Sales	892,479.00	1,655,480.00	13,685,044.00	13,686,749.00
Hot Lotto sales	792,008.00	640,944.00	7,467,295.00	8,110,185.00
Pick 4 sales	347,536.50	325,983.50	3,608,934.00	3,247,179.00
All or Nothing sales	260,741.00	296,650.00	2,939,862.00	3,712,165.00
Lucky for Life sales	460,652.00	639,438.00	5,163,868.00	2,594,180.00
Pull-tab sales	916,619.02	1,211,555.49	10,453,804.98	13,880,784.67
Application fees	150.00	250.00	3,500.00	3,325.00
Other	797.18	8,330.48	18,221.31	32,721.82
Total operating revenues	<u>32,138,338.70</u>	<u>31,136,737.97</u>	<u>322,378,681.79</u>	<u>337,735,663.99</u>
<b>Operating expenses:</b>				
Scratch ticket prizes	13,684,048.92	13,414,679.07	142,944,459.65	139,981,532.95
InstaPlay prizes	550,335.71	-	3,375,665.42	-
Pick 3 prizes	394,357.40	371,923.10	3,889,388.10	4,030,067.80
Powerball prizes	2,295,534.00	2,397,241.00	23,355,033.00	34,851,975.00
Mega Millions prizes	426,833.50	797,319.00	6,752,689.13	6,636,494.50
Hot Lotto prizes	387,262.00	276,839.00	3,635,797.50	3,877,411.15
Pick 4 prizes	206,491.90	190,340.10	2,128,915.40	1,909,662.40
All or Nothing prizes	155,199.91	175,891.54	1,737,517.34	2,198,522.50
Monopoly Millionaires' Club prizes	-	-	-	(21,052.29)
Lucky for Life prizes	380,053.37	380,039.05	3,336,779.69	1,759,284.17
Pull-tab prizes	573,940.72	757,856.75	6,532,689.75	8,680,397.17
VIP Club prize expense	3,000.00	-	237,570.70	155,754.29
Promotional prize expense	5,138.84	12,115.88	211,775.35	159,007.94
Advertising/publicity	625,085.32	667,331.55	6,037,110.08	6,242,708.51
Retailer compensation expense	2,095,363.72	2,032,260.39	20,948,415.65	21,844,629.25
Ticket expense	317,147.32	233,943.66	2,992,026.35	3,012,007.38
Vendor compensation expense	668,191.96	656,758.54	6,560,406.02	6,987,232.48
Salary and benefits	1,025,822.17	872,532.82	9,566,587.96	9,133,694.68
Travel	19,499.97	25,662.48	258,801.76	259,425.83
Supplies	9,651.57	14,355.36	94,474.90	119,835.71
Printing	120.60	-	3,201.90	1,031.40
Postage	249.37	273.90	5,569.68	6,279.07
Communications	12,810.92	12,655.29	138,986.12	143,415.12
Rentals	25,414.73	25,418.39	279,299.68	283,396.09
Utilities	5,424.03	3,938.87	78,667.88	72,661.12
Professional fees	11,191.03	6,811.43	146,151.81	83,224.60
Vending machine maintenance	37,045.59	50,390.76	489,239.62	548,570.77
Outside services and repairs	70,406.48	47,450.60	719,757.01	735,009.56
Data processing	9,351.44	9,856.47	108,775.73	112,533.66
Equipment	30,987.22	57,926.55	980,192.41	414,011.10
Reimbursement to other state agencies	57,418.12	51,204.48	397,841.21	391,921.07
Depreciation	46,006.19	29,242.76	415,082.56	305,921.73
Other	6,088.66	3,842.54	62,746.85	51,035.84
MUSL/Lotto administrative expense	12,840.75	10,112.05	141,681.03	117,422.32
Total operating expenses	<u>24,148,313.43</u>	<u>23,586,213.38</u>	<u>248,563,297.24</u>	<u>255,085,024.87</u>
Operating income	<u>7,990,025.27</u>	<u>7,550,524.59</u>	<u>73,815,384.55</u>	<u>82,650,639.12</u>
<b>Non-operating revenue (expenses):</b>				
Proceeds provided to State General Fund	(8,327,087.05)	(6,809,084.72)	(70,750,915.29)	(79,658,539.84)
Proceeds provided to Veteran's Trust Fund	-	-	(2,500,000.00)	(2,500,000.00)
Interest income	19,709.14	13,573.61	133,425.27	151,795.59
Gain (Loss) on disposal of capital assets	3,625.00	-	(726,000.06)	32,200.00
Net non-operating revenues (expenses)	<u>(8,303,752.91)</u>	<u>(6,795,511.11)</u>	<u>(73,843,490.08)</u>	<u>(81,974,544.25)</u>
Change in net position	<u>(313,727.64)</u>	<u>755,013.48</u>	<u>(28,105.53)</u>	<u>676,094.87</u>
Net position beginning of period	6,839,699.59	5,719,419.17	6,554,077.48	5,798,337.78
Net position end of period	<u>6,525,971.95</u>	<u>6,474,432.65</u>	<u>6,525,971.95</u>	<u>6,474,432.65</u>

## Budget For Lottery Fund

	FY 2016 ACTUAL	FY 2017 BOARD APPROVED FINAL BUDGET	FY 2018 BOARD APPROVED PRELIMINARY BUDGET	FY 2018 BOARD APPROVED FINAL BUDGET
<b>Resources</b>				
Lottery sales	\$ 366,910,923	\$ 324,920,000	\$ 333,820,000	\$ 334,420,000
Interest income	\$ 194,873	\$ 500,000	\$ 500,000	\$ 500,000
Application fees	\$ 4,175	\$ 5,000	\$ 5,000	\$ 5,000
Other	\$ 33,065	\$ 5,000	\$ 5,000	\$ 5,000
<b>Total Resources</b>	<b>\$ 367,143,037</b>	<b>\$ 325,430,000</b>	<b>\$ 334,330,000</b>	<b>\$ 334,930,000</b>
<b>Expenses and Change in Net Assets</b>				
Prizes	\$ 221,767,401	\$ 193,151,515	\$ 199,136,196	\$ 199,557,641
Retailer compensation	\$ 24,561,634	\$ 20,987,254	\$ 22,347,472	\$ 22,352,605
Advertising production and media purchases	\$ 6,821,537	\$ 12,996,800	\$ 13,352,800	\$ 13,356,800
Retailer Lottery system/Terminal Communications	\$ 7,942,965	\$ 7,593,157	\$ 7,851,213	\$ 9,489,381
Instant/Pull-tab ticket expense	\$ 3,258,644	\$ 3,942,000	\$ 4,142,000	\$ 3,928,000
Vending machines & maintenance/Ticket dispensers	\$ 820,542	\$ 1,819,000	\$ 1,965,800	\$ 508,500
Courier delivery of instant tickets	\$ 563,738	\$ 660,000	\$ 660,000	\$ 660,000
Lottery operating expense	\$ 12,654,373	\$ 14,620,690	\$ 14,996,492	\$ 15,270,127
Increase (decrease) in net assets	\$ 727,584	\$ (85,000)	\$ (332,700)	\$ (447,275)
<b>Total Expenses and Change in Net Assets</b>	<b>\$ 279,118,417</b>	<b>\$ 255,685,415</b>	<b>\$ 264,119,273</b>	<b>\$ 264,675,779</b>
<b>Proceeds</b>				
Proceeds Transfer to General Fund	\$ 85,524,619	\$ 67,244,585	\$ 67,710,727	\$ 67,754,221
Proceeds Transfer to Veterans Trust Fund	\$ 2,500,000	\$ 2,500,000	\$ 2,500,000	\$ 2,500,000
<b>Total Proceeds Transfers</b>	<b>\$ 88,024,619</b>	<b>\$ 69,744,585</b>	<b>\$ 70,210,727</b>	<b>\$ 70,254,221</b>
<b>Total Expenses and Proceeds</b>	<b>\$ 367,143,037</b>	<b>\$ 325,430,000</b>	<b>\$ 334,330,000</b>	<b>\$ 334,930,000</b>

### Lottery Operations - Budget Detail

	FY 2016 ACTUAL	FY 2017 BOARD APPROVED FINAL BUDGET	FY 2018 BOARD APPROVED PRELIMINARY BUDGET	FY 2018 BOARD APPROVED FINAL BUDGET
Administrative payroll*	\$ 9,977,828	\$ 11,302,592	\$ 11,302,592	\$ 11,534,327
Travel	\$ 275,272	\$ 435,000	\$ 435,000	\$ 435,000
Supplies	\$ 104,490	\$ 105,000	\$ 105,000	\$ 105,000
Printing	\$ 4,190	\$ 20,000	\$ 20,000	\$ 20,000
Postage	\$ 6,636	\$ 7,000	\$ 7,000	\$ 7,000
Communications	\$ 263,414	\$ 317,098	\$ 186,000	\$ 186,000
Rentals	\$ 309,412	\$ 320,000	\$ 320,000	\$ 320,000
Utilities	\$ 87,942	\$ 101,000	\$ 101,000	\$ 101,000
Professional fees	\$ 135,660	\$ 220,000	\$ 225,000	\$ 259,500
Outside services and repair	\$ 243,794	\$ 315,000	\$ 334,000	\$ 341,500
Data processing	\$ 122,421	\$ 125,000	\$ 125,000	\$ 125,000
Equipment	\$ 306,251	\$ 436,000	\$ 593,200	\$ 696,200
Reimbursement to state agencies	\$ 430,088	\$ 480,000	\$ 506,000	\$ 506,000
Depreciation	\$ 333,223	\$ 350,000	\$ 650,700	\$ 547,600
Other expenses	\$ 53,751	\$ 87,000	\$ 86,000	\$ 86,000
<b>Total operating expenses</b>	<b>\$ 12,654,373</b>	<b>\$ 14,620,690</b>	<b>\$ 14,996,492</b>	<b>\$ 15,270,127</b>

\* FY 2018 Proposed Final Budget for "Administrative Payroll" includes salary and benefit cost increases per DOM projections