



13001 University Avenue
Clive Iowa 50325-8225
www.ialottery.com
515.725.7900

Kim Reynolds · Governor
Adam Gregg · 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 2017



The Iowa Lottery has seen strong results in the opening months of fiscal year 2018, and announcement of another clean audit. Lottery officials remain confident that they will achieve the lottery's stated goals for the current fiscal year and continue to budget conservatively, understanding that lottery results can and do fluctuate over time.

Lottery sales and proceeds for the current year are ahead of projections and ahead of the lottery's results for the same time period in FY 2017. Strong sales of instant-scratch tickets continue to lead the way, but lotto sales also got a solid start to the year when the jackpots in Powerball® and Mega Millions® both topped the \$300 million mark at the same time in early August. It was the first time that had ever occurred, and speaks to the unpredictable factor when it comes to lottery jackpots: You just never know when the next big one will hit. That "chance factor" has made a positive difference in the lottery's FY 2018 results thus far.

Final year-end numbers for FY 2017 show that the Iowa Lottery generated nearly \$81 million in proceeds to state causes. It was the fourth time that its annual proceeds topped the \$80-million mark in the lottery's 32-year history. Annual lottery sales were \$352.2 million, exceeding the \$300 million mark for the sixth year in a row. Prizes to players totaled \$215.6 million, while lottery sales commissions to retailers during the year totaled nearly \$23 million.

There was 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 produced record results for lotteries across the country, including the Iowa Lottery. We at the Iowa Lottery continue to 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.

Here is a year-to-year comparison of lottery sales by product for the past two fiscal years:

	<u>FY 2017</u>	<u>FY 2016</u>
Instant-scratch games	\$237.6 million	\$233.7 million
InstaPlay games*	\$5.8 million	-----
Pick 3	\$7.3 million	\$7.4 million
Powerball	\$54.3 million	\$74.9 million
Mega Millions	\$15 million	\$16.4 million
Hot Lotto	\$8.2 million	\$8.8 million
Pick 4	\$3.9 million	\$3.6 million
All or Nothing	\$3.2 million	\$4 million
Lucky for Life	\$5.6 million	\$3.2 million
Pull-tab games	\$11.3 million	\$15 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**. The lottery's year-end statement of revenues, expenses and changes in net position for FY 2017 is included as **Attachment B**.

FY 2017 Audit Report of Lottery & Our Annual Report



In late December, the State Auditor's Office released the results of its FY 2017 audit of the Iowa Lottery.

In short, it was another "clean report" for the lottery. In its Dec. 13 announcement, the Auditor's Office noted that the financial statements of the lottery for FY 2017 "present fairly, in all material respects, the financial position of the Iowa Lottery Authority as of June 30, 2017, and the changes in its financial position and its cash flows for the year then ended in accordance with U.S. generally accepted accounting principles."

Under state law, the Auditor reviews the lottery's operations annually. That review is in addition to the security and integrity standards the lottery uses throughout its operations to ensure the veracity of its games.

A direct link to the report from the office of State Auditor Mary Mosiman is available here: https://auditor.iowa.gov/sites/default/files/audit_reports/1860-6270-B000.pdf

The lottery's annual report for FY 2017 also is now available. A link to it is here: <http://www.ialottery.com/Pages/AboutUs/AnnualReport.aspx>

FY 2019 Budget Updates

At the Lottery Board's meeting on Sept. 26, the lottery's FY 2019 budget was given approval to adjust some line items to more closely align with FY 2017 actual expenses and reflect sales from the products that the lottery plans to have in the field during the year. The sales and proceeds goals for FY 2019 are both more than is budgeted for FY 2018.

The lottery's FY 2019 budget will be presented to the Board again in June for final modifications needed for salary and benefit changes.

Copies of the lottery's Overall Budget and Operating Expenses for FY 2019 are included with this report as **Attachment C** and **Attachment D**.



Mike Klappholz



Connor Flynn



Mary Rathje



Mary Junge



Michael Fitzgerald

The members of the Lottery Board are: Chairperson Connor Flynn Jr., chairman of an advertising agency in Des Moines, where he also resides; Mike Klappholz of Marion, a retired Cedar Rapids police chief; 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.)

Sentencings In Long-Running Lottery Jackpot Investigation

During the summer, the long-running lottery jackpot investigation came to a close with the confessions and sentencing of three men with Texas ties.

Eddie Tipton, the man at the center of the case, was sentenced Aug. 22 in Polk County District Court to up to 25 years in prison, the maximum sentence for the felony charge of ongoing criminal conduct to which he pleaded guilty in Iowa. It was the sentence recommended by the prosecutor in the case. While in court that day, Tipton said he regretted his actions in rigging lottery drawings, said he knew what he did was wrong, and that he was sorry for hurting so many people. In handing down the maximum sentence, the judge said he was doing so to send a strong message of deterrence. Tipton was taken into custody at the end of the sentencing hearing.



The case, which generated headlines around the world, began in Iowa in December 2010 when a man bought a Hot Lotto ticket at a convenience store on Des Moines' north side. That ticket went on to win the multi-million-dollar jackpot on the line in the Hot Lotto drawing on Dec. 29, 2010. For nearly a year, the prize went unclaimed.

Then, with less than two hours to go before the prize would have expired on Dec. 29, 2011, the winning ticket was presented by lawyers on behalf of a New York investment trust that had been established to benefit a corporation in the country of Belize. Neither the two lawyers who presented the ticket nor anyone associated with Hexham Investments Trust of Bedford, N.Y., would provide the basic details necessary to verify that the ticket had been legally purchased, legally possessed and legally presented. Those involved said they could not identify the jackpot winner or the man who purchased the winning ticket.

That standard information is routinely requested from jackpot winners in Iowa as part of the lottery's security processes to comply with both state law and lottery game rules. Such details are usually received within minutes of the time that a winning ticket is presented.

On Jan. 26, 2012, Crawford Shaw, a New York attorney who identified himself as the trustee of Hexham Investments Trust, withdrew the claim to the jackpot. That same day, the Iowa Attorney General's Office and Iowa Division of Criminal Investigation opened a criminal investigation into the matter at the request of the Iowa Lottery.

In 2017, Eddie Tipton, his younger brother, and a man who had been his long-time friend all pleaded guilty to felony charges in the case, admitting that they conspired to illegally claim lottery winnings by utilizing malicious computer code to rig lottery drawings in five states.

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. Prosecutors said that he installed malicious computer code that allowed him to predict winning numbers in lottery drawings on three days of the year.

For his central role in the case, Eddie Tipton pleaded guilty to three felony charges in Iowa and Wisconsin of ongoing criminal conduct, theft by fraud, and computer crime. Prosecutors said that Tipton conspired with friends and family in claiming lottery prizes in Colorado, Kansas, Oklahoma and Wisconsin and attempting to claim the lottery jackpot in Iowa, which ultimately was not paid.

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.

Tipton's younger brother, Tommy Tipton of Flatonia, Texas, pleaded guilty in the case to a felony and a misdemeanor charge of conspiracy to commit theft; and Tipton's long-time friend, Robert Rhodes of Sugar Land, Texas, pleaded guilty to a felony charge of being party to a computer crime.

Rhodes was ordered to serve six months' home confinement in Texas and pay \$409,000 in restitution to the state of Wisconsin. Tommy Tipton was sentenced in June to 75 days in jail. The Tipton brothers also agreed to pay \$2.2 million in restitution to the Colorado, Kansas, Oklahoma and Wisconsin lotteries.

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 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. The details we 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.

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

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.

\$1 Million Lottery Prize Claimed Two Months After It Was Won



One of Iowa's most recent big lottery prizes was claimed in December months after it was won, and the winner said she simply hadn't checked her tickets for several weeks.

Karen Harger of Glenwood won a \$1 million prize in the Powerball drawing on Nov. 4. But she said she always sets her tickets aside and doesn't usually check them for a couple months. She said that in mid-December, she sat down at her computer and started checking her numbers.

"I kept re-checking the computer, and I got my husband to come look at it," she said. "I was nervous. I said, 'Oh, we won \$1,000!' And Jim said, 'No, there are three more zeroes!' And it was \$1 million. And the most I had ever won from Powerball before at one time was \$10."

Karen Harger, 65, who is retired from a career with the American Red Cross, said she was so flustered that rather than looking at the details on the lottery's website, she sent her husband, Jim, out to their car to get a play slip for the Powerball game so she could look at it. Jim Harger, 55, a retired engineer, said he took the time to review the details.

"I had a little time to look at this thing," he said. "I walked in there and I said, 'No, Karen, there are a little bit too many zeroes to just be \$1,000.' And then I was nervous! Then we thought, 'This can't be true, this can't happen to us!'"

The Hargers said they didn't tell anyone else that they had won a big lottery prize until they had the ticket verified Dec. 18 at the Iowa Lottery's regional office in Council Bluffs. Karen Harger realized that day that she dropped some drug-store coupons on the floor as she was trying to check her winning ticket.

"I don't plan to stop using coupons. I've done it all of my adult life," she said. "And we talked about that – this is not changing what we do. It just makes things a little easier."

Karen Harger bought her winning Powerball ticket at Casey's convenience store, 701 32nd Ave. in Council Bluffs, while running errands and going to appointments in that city. Her ticket came within one number of having at least a share of the \$62.9 million jackpot in the Nov. 4 drawing, matching the first five numbers but missing the Powerball. Harger's ticket was one of only two across the country that won a \$1 million prize that night, with the other purchased in Florida.

Casey's received a \$1,000 bonus from the Iowa Lottery for selling the \$1 million-winning ticket at one of its stores.

The Hargers said they plan to use their winnings to establish college savings accounts for their four grandchildren; remodel their home; and invest for the rest of their retirement years. Jim also has his heart set on a new wood-burning stove for their home.

Four Iowa Lottery players have now claimed prizes of at least \$1 million in calendar year 2017, all of them in the Powerball game.

IOWA LOTTERY
PERFORMANCE MEASURES
FY 2018
November 30, 2017

		JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN
MONTH													
Gross Sales	Budget FY 2018	25,040,187	26,514,716	25,199,976	26,063,594	27,126,655	27,334,007	32,204,745	29,923,071	30,850,681	28,329,991	29,995,886	25,836,491
	Actual '18	28,206,485	38,467,880	26,630,836	26,964,621	27,665,819	-	-	-	-	-	-	-
Prize Expense	Budget FY 2018	14,858,996	15,742,543	14,954,742	15,472,229	16,254,469	16,378,716	19,297,294	17,930,100	18,485,931	16,891,189	17,891,887	15,399,545
	Actual '18	17,143,244	22,941,217	16,472,093	16,851,231	16,580,357	-	-	-	-	-	-	-
Operating Expenses	Budget FY 2018	1,221,802	1,311,871	1,222,236	1,291,537	1,273,991	1,224,256	1,316,795	1,174,968	1,259,991	1,221,196	1,322,765	1,428,719
	Actual '18	1,106,067	1,200,084	1,034,238	1,190,849	1,157,260	-	-	-	-	-	-	-
Total Proceeds	Budget FY 2018	5,183,039	5,469,502	5,223,408	5,374,638	5,663,645	5,766,329	6,917,570	6,476,754	6,628,603	6,023,721	6,347,551	5,179,461
	Actual '18	6,524,204	9,995,533	6,097,014	5,957,452	6,396,948	-	-	-	-	-	-	-
YEAR TO DATE													
Gross Sales	Budget FY 2018	25,040,187	51,554,903	76,754,879	102,818,473	129,945,128	157,279,135	189,483,880	219,406,951	250,257,632	278,587,623	308,583,509	334,420,000
	Actual '18	28,206,485	66,674,365	93,305,201	120,269,822	147,935,641	-	-	-	-	-	-	-
Prize Expense	Budget FY 2018	14,858,996	30,601,539	45,556,281	61,028,510	77,282,979	93,661,695	112,958,989	130,889,089	149,375,020	166,266,209	184,158,096	199,557,641
	Actual '18	17,143,244	40,084,461	56,556,554	73,407,785	89,988,142	-	-	-	-	-	-	-
Operating Expenses	Budget FY 2018	1,221,802	2,533,673	3,755,909	5,047,446	6,321,437	7,545,693	8,862,488	10,037,456	11,297,447	12,518,643	13,841,408	15,270,127
	Actual '18	1,106,067	2,306,151	3,340,389	4,531,238	5,688,498	-	-	-	-	-	-	-
Total Proceeds	Budget FY 2018	5,183,039	10,652,541	15,875,949	21,250,587	26,914,232	32,680,561	39,598,131	46,074,885	52,703,488	58,727,209	65,074,760	70,254,221
	Actual '18	6,524,204	16,519,737	22,616,751	28,574,203	34,971,151	-	-	-	-	-	-	-

Current Month Year to Date

Prize Payout - Budget	59.92%	59.47%
Prize Payout - Actual	59.93%	60.83%
Sales - Actual increase (decrease) vs. Budget		13.84%
Proceeds - Actual increase (decrease) vs. Budget		29.94%

IOWA LOTTERY AUTHORITY
Statement of Revenues, Expenses and Changes in Net Position
For the Twelve Months Ending June 30, 2017
FINAL

Attachment B

	Month ended 6/30/2017	Month ended 6/30/2016	Year-to-date 6/30/2017	Year-to-date 6/30/2016
Operating revenues:				
Instant-scratch ticket sales	\$19,635,274.00	\$19,045,232.53	\$237,617,703.00	\$233,681,883.53
InstaPlay sales	608,480.00	-	5,820,274.00	-
Pick 3 sales	628,003.50	574,552.50	7,318,686.00	7,376,765.50
Powerball sales	5,139,655.00	3,821,622.00	54,292,902.00	74,851,132.50
Mega Millions Sales	1,272,065.00	2,714,269.00	14,957,109.00	16,401,018.00
Hot Lotto sales	743,419.00	717,415.00	8,210,714.00	8,827,600.00
Pick 4 sales	337,338.50	307,539.50	3,946,272.50	3,554,718.50
All or Nothing sales	246,581.00	277,314.00	3,186,443.00	3,989,479.00
Lucky for Life sales	436,098.00	560,814.00	5,599,966.00	3,154,994.00
Pull-tab sales	838,935.29	1,192,547.79	11,292,740.27	15,073,332.46
Application fees	100.00	850.00	3,600.00	4,175.00
Other	620.10	343.58	18,841.41	33,065.40
Total operating revenues	<u>29,886,569.39</u>	<u>29,212,499.90</u>	<u>352,265,251.18</u>	<u>366,948,163.89</u>
Operating expenses:				
Scratch ticket prizes	12,099,487.00	11,779,238.00	155,043,946.65	151,760,770.95
InstaPlay prizes	406,040.41	-	3,781,705.83	-
Pick 3 prizes	372,582.10	339,631.50	4,261,970.20	4,369,699.30
Powerball prizes	2,521,186.71	1,877,360.50	25,876,219.71	36,729,335.50
Mega Millions prizes	598,885.50	1,339,034.50	7,351,574.63	7,975,529.00
Hot Lotto prizes	364,255.50	345,606.50	4,000,053.00	4,223,017.65
Pick 4 prizes	238,120.10	173,183.70	2,367,035.50	2,082,846.10
All or Nothing prizes	144,702.63	164,936.27	1,882,219.97	2,363,458.77
Monopoly Millionaires' Club prizes	-	-	-	(21,052.29)
Lucky for Life prizes	185,160.08	766,614.52	3,521,939.77	2,525,898.69
Pull-tab prizes	523,804.18	742,030.73	7,056,493.93	9,422,427.90
VIP Club prize expense	14,894.75	12,853.13	252,465.45	168,607.42
Promotional prize expense	13,167.38	7,854.23	224,942.73	166,862.17
Advertising/publicity	555,441.56	579,443.67	6,592,551.64	6,822,152.18
Retailer compensation expense	1,966,339.43	2,716,255.37	22,914,755.08	24,560,884.62
Ticket expense	272,948.55	230,029.01	3,264,974.90	3,242,036.39
Vendor compensation expense	622,629.10	610,283.38	7,183,035.12	7,597,515.86
Salary and benefits	1,148,124.60	844,133.40	10,714,712.56	9,977,828.08
Travel	19,477.01	22,123.30	278,278.77	281,549.13
Supplies	15,175.68	13,328.00	109,650.58	133,163.71
Printing	-	7,358.58	3,201.90	8,389.98
Postage	247.50	357.10	5,817.18	6,636.17
Communications	114,922.06	119,998.96	253,908.18	263,414.08
Rentals	25,414.24	26,015.67	304,713.92	309,411.76
Utilities	12,156.48	15,280.71	90,824.36	87,941.83
Professional fees	45,182.18	100,178.58	191,333.99	183,403.18
Vending machine maintenance	37,045.59	50,390.76	526,285.21	598,961.53
Outside services and repairs	71,462.46	90,159.81	791,219.47	825,169.37
Data processing	8,245.21	9,887.68	117,020.94	122,421.34
Equipment	91,057.03	241,509.97	1,071,249.44	655,521.07
Reimbursement to other state agencies	30,042.99	38,166.98	427,884.20	430,088.05
Depreciation	45,884.70	27,301.65	460,967.26	333,223.38
Other	6,189.39	4,980.07	68,936.24	56,015.91
MUSL/Lotto administrative expense	12,862.30	10,282.82	154,543.33	127,705.14
Total operating expenses	<u>22,583,134.40</u>	<u>23,305,809.05</u>	<u>271,146,431.64</u>	<u>278,390,833.92</u>
Operating income	<u>7,303,434.99</u>	<u>5,906,690.85</u>	<u>81,118,819.54</u>	<u>88,557,329.97</u>
Non-operating revenue (expenses):				
Proceeds provided to State General Fund	(7,523,811.46)	(5,866,079.53)	(78,274,726.75)	(85,524,619.37)
Proceeds provided to Veteran's Trust Fund	-	-	(2,500,000.00)	(2,500,000.00)
Interest income	48,682.21	43,077.35	182,107.48	194,872.94
Gain (Loss) on disposal of capital assets	3,252.02	(4,043.84)	(722,748.04)	28,156.16
Net non-operating revenues (expenses)	<u>(7,471,877.23)</u>	<u>(5,827,046.02)</u>	<u>(81,315,367.31)</u>	<u>(87,801,590.27)</u>
Change in net position	<u>(168,442.24)</u>	<u>79,644.83</u>	<u>(196,547.77)</u>	<u>755,739.70</u>
Net position beginning of period	6,525,971.95	6,474,432.65	6,554,077.48	5,798,337.78
Net position end of period	<u>6,357,529.71</u>	<u>6,554,077.48</u>	<u>6,357,529.71</u>	<u>6,554,077.48</u>

Budget For Lottery Fund

	FY 2017 ACTUAL	FY 2018 BOARD APPROVED FINAL BUDGET	FY 2019 FALL BOARD APPROVED BUDGET
<u>Resources</u>			
Lottery sales	352,242,810	334,420,000	337,300,000
Interest income	182,107	500,000	500,000
Application fees	3,600	5,000	5,000
Other	18,841	5,000	5,000
Total Resources	352,447,359	334,930,000	337,810,000
<u>Expenses and Change in Net Assets</u>			
Prizes	215,620,567	199,557,641	204,057,000
Retailer compensation	22,915,600	22,352,605	22,579,862
Advertising production and media purchases	6,591,778	13,356,800	13,512,000
Retailer Lottery system/Terminal Communications	7,408,979	9,489,381	6,566,227
Instant/Pull-tab ticket expense	3,272,386	3,928,000	3,957,500
Vending machines & maintenance/Ticket dispensers	1,384,720	508,500	548,940
Courier delivery of instant tickets	594,509	660,000	660,000
Lottery operating expense	13,357,893	15,270,127	15,228,127
Increase (decrease) in net assets	526,200	(447,275)	(412,100)
Total Expenses and Change in Net Assets	271,672,632	264,675,779	266,697,556
<u>Proceeds</u>			
Proceeds Transfer to General Fund	78,274,727	67,754,221	68,612,444
Proceeds Transfer to Veterans Trust Fund	2,500,000	2,500,000	2,500,000
Total Proceeds Transfers	80,774,727	70,254,221	71,112,444
Total Expenses and Proceeds	352,447,359	334,930,000	337,810,000

Lottery Operations

	FY 2017 ACTUAL	FY 2018 BOARD APPROVED FINAL BUDGET	FY 2019 FALL BOARD APPROVED BUDGET
Administrative payroll*	10,714,713	11,534,327	11,534,327
Travel	273,368	435,000	410,000
Supplies	77,856	105,000	105,000
Printing	3,202	20,000	20,000
Postage	5,817	7,000	7,000
Communications	253,908	186,000	186,000
Rentals	304,714	320,000	320,000
Utilities	90,824	101,000	101,000
Professional fees	169,933	259,500	259,500
Outside services and repair	202,040	341,500	419,000
Data processing	117,021	125,000	125,000
Equipment	189,281	696,200	494,200
Reimbursement to state agencies	427,884	506,000	506,000
Depreciation	460,967	547,600	655,100
Other expenses	66,365	86,000	86,000
Total operating expenses	\$ 13,357,893	\$ 15,270,127	\$ 15,228,127

* FY 2019 Fall Board Approved Budget for "Administrative Payroll" does not include salary and benefit cost increases.