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Iowa Lottery Report On Operations

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

**From: Ken Brickman, Chief Operating Officer and Acting CEO
Mary Neubauer, Vice President, External Relations**

Date: December 2007

Fiscal year 2008 has started on a lucky note for Iowa Lottery players, with two men claiming \$1 million prizes in the “Set For Life” instant-scratch game. The two top prizes are the first of eight available in the game, which began sales in June.



Martin Rodriguez of
Davenport

The first \$1 million prize to be claimed in the game went to a Davenport man, who bought his winning ticket and played it while taking a break between two baseball games. Martin Rodriguez, 47, who works as a custodian for the Davenport School District, said he just happened to stop at a convenience store in Davenport to get something to eat in between baseball games he was playing during a July weekend. After discovering he had won a \$1 million prize, Rodriguez drove home and hid the ticket so he could play in the second game!

“Set for Life” is a \$20 scratch game. When players match any of “their numbers” to any “winning number,” they win the prize shown for that play area. If they find a “\$\$” symbol, they win the prize shown instantly. The overall odds of winning in the game are about 1 in 3.

Set for Life offers eight top prizes of \$1 million. Players who win the top prize have the option of receiving it as an annuity or lump-sum payment. If the winner chooses to take the annuity, he/she will be paid \$40,000 per year for a period of 25 years. If the winner chooses to receive the lump-sum payment, he/she will receive \$650,000 before taxes.

Rodriguez chose to receive the prize in a lump-sum payment. He claimed his prize July 23 at lottery headquarters in Des Moines. He said he planned to continue working, and that he would use his winnings to buy a house and invest.

The second \$1 million prize winner in the game also said he planned to continue working, and that he would invest his winnings.

Larry Shupe Jr. of West Frankfort, Ill., a railroad contractor, was working in southern Iowa when he went out for pizza, bought a lottery ticket and ended up winning a \$1 million prize in Set For Life.

Shupe, 32, said he went to two places where he couldn't find pizza before ending up at a Casey's convenience store in



Larry Shupe Jr. of West Frankfort, Ill.

Chariton where he bought pizza - and his winning scratch ticket. Shupe claimed his prize Nov. 26 at Iowa Lottery headquarters in Des Moines.

FY 2007: Record Combined Sales of Lotto, Scratch and Pull-Tab Tickets

The final figures are in, and they show that the combined sales from lotto, scratch and pull-tab games set records during its latest fiscal year, fueled by increases in sales of instant-scratch, pull-tab and Hot Lotto tickets. Here are some key financial highlights from fiscal year 2007:

- Lottery sales totaled \$235 million in fiscal year 2007, which ended June 30. That mark is the highest combined sales total for lotto, instant-scratch and pull-tab games since the Lottery's start in 1985, but is down from total lottery sales of \$339.5 in fiscal year 2006, which included TouchPlay revenue. Overall, sales were down nearly 31 percent in fiscal year 2007 after a 61 percent increase in fiscal year 2006 and a 1 percent increase in fiscal year 2005. The Lottery's fiscal year 2007 results were impacted by the discontinuation of the TouchPlay program, which ended in May 2006. TouchPlay sales had totaled \$121.4 million in fiscal year 2006. The Lottery had no sales in that category in fiscal year 2007.
- Lottery proceeds for state programs totaled more than \$58.1 million for fiscal year 2007, the second-highest proceeds total achieved from the sale of lotto, instant-scratch and pull-tab games. The Lottery's record for proceeds to the state from the sale of lotto, scratch and pull-tab games was set in fiscal year 1995, when \$58.2 million was raised for state programs. Lottery proceeds in FY 2007 were down more than 28 percent from the previous year, which had included TouchPlay sales.
- Hot Lotto sales rose 50 percent to \$14.5 million in fiscal year 2007, due in large part to the game's record jackpot of nearly \$20 million, which was claimed by an Indianola man in February. Hot Lotto sales in fiscal year 2006 had totaled \$9.6 million.
- Powerball sales continued at a strong rate in the lottery's latest year, totaling \$61.5 million. However, they were down from \$71.1 million in fiscal year 2006, which had seen a record jackpot of \$365 million in the game.
- Sales of instant-scratch tickets, the first product introduced by the Lottery and always one of its top-selling product lines, rose more than 17 percent to a record \$125.1 million in fiscal year 2007. The Lottery's previous record for instant-scratch sales had been set in fiscal year 2006, when \$106.6 million in scratch tickets were sold.
- Sales of pull-tab tickets also saw a double-digit increase in fiscal year 2007, rising to more than \$21 million compared to \$18.3 million in fiscal year 2006.
- Since the Lottery's inception in 1985, more than \$2.1 billion has been awarded in prizes and nearly \$1.1 billion has been raised for state programs.

Lottery 2009 Budget

In the lottery's June report to the Oversight Committees, it noted that the Lottery Board had voted to revise the lottery's FY 2008 budget to accommodate the salary-adjustment decisions made by the Iowa Legislature during the 2007 session.

At its meeting in September, the Lottery Board approved the FY 2009 budget for the lottery. There are few differences from the lottery's results in FY 2007, the latest year for which the lottery has final figures.

As part of the lottery's standard procedures, the lottery budget figures have been entered into the state's I-3 accounting system and are available for review by all interested parties.

The voting members of the Iowa Lottery Board are: Chairperson Tim Clausen, a Sioux City

attorney; Vice Chair Mary Junge, an accountant and lawyer from Cedar Rapids; Elaine Baxter, a former secretary of state from Burlington; Mike Klappholz of Cedar Rapids, the Cedar Rapids chief of police; and Tom Rial, a Des Moines marketing consultant. State Treasurer Michael Fitzgerald is an ex-officio member of the Board.

Copies of the Lottery Operations budget and the budget for the Lottery Fund are both included with this report as Attachments A and B. In an effort to address a committee member's request at a previous meeting to see the lottery's budget in a different format, we also are presenting the details of the lottery's budget in a format similar to previous presentations from the Department of Management. That version is included as Attachment C.

Powerball Happenings



Powerball® sales got off to a strong start for fiscal year 2008 when the jackpot climbed to more than \$314 million for the Aug. 25 drawing. A ticket sold in Indiana won that jackpot, the fourth-largest in the history of the game, but nine Iowa players came close to a share of the prize, with tickets that were just one number away.

Just a month later, there was another interesting twist in the Powerball game when hundreds of tickets across the country all matched four numbers plus the Powerball to win prizes of at least \$10,000. Eight of those tickets were purchased by Iowa Lottery players. Numerous players in different states all reported that they played numbers they saw during a television show.

One of those players was Paul Sparks of Estherville, who claimed a \$20,000 Powerball prize on Sept. 28. Sparks said he played numbers mentioned during a television documentary as being those frequently selected in lottery drawings. The Learning Channel (TLC) recently had aired a documentary called "The Lottery Changed My Life" that followed the experiences of recent lottery jackpot winners. The program also mentioned some frequently drawn numbers.

There have been common themes among Powerball winners a few times. In 2005, for example, more than 200 tickets nationwide matched the first five numbers selected in two different drawings. The winners reported that they had chosen their Powerball numbers from the "lucky numbers" they had found inside fortune cookies.

The fortune cookies all were produced by a New York company that makes about 4 million cookies each day. The company started printing lottery numbers for entertainment on fortunes more than a decade ago, with employees choosing numbers from those mixed in a big bowl.

Another Successful Year At The Fair



A Truro woman was one of the winners in the "Deal or No Deal" promotions this year at the lottery's booth at the Iowa State Fair.

Iowa Lottery sales began in August 1985 with a kick-off celebration at the Iowa State Fair, and lottery tickets have been sold at the fair during all the years since. The lottery has had a booth in the Varied Industries Building at the Fair for 19 years and 2007 was a banner year for the lottery booth. In addition to being a valuable opportunity for the lottery to interact with the public and provide information, the Lottery sells tickets at its fair booth, and 2007 was a record year for sales there. Lottery sales during the 10-day fair topped \$201,000 this year, the highest total ever for the lottery's State Fair booth.

cash or compete on the real game show; the other drawing will offer a grand prize of \$1 million. Players can enter the second-chance drawings by visiting the Iowa Lottery's Web site at www.ialottery.com and filling out an electronic entry form there.

Entries in the second-chance drawings will be accepted through midnight on Sunday, Aug. 24. Entries received by Feb. 24 will be eligible for a drawing on Feb. 26 to determine the three Iowa Lottery players who each will win a trip for four to Hollywood valued at more than \$13,500. Once there, each of those players will win a cash amount from \$5,000 to \$25,000 or they'll have the opportunity to compete in a "Deal or No Deal" show and could win up to \$1 million.

All entries that did not win a trip in that initial drawing and all other entries received by Aug. 24 will be eligible for a second Iowa Lottery drawing on Aug. 26 that will determine three semifinalists for a \$1 million grand prize. The drawing for that prize will be held Sept. 17 in Alpharetta, Ga., and the winner will be chosen from all semifinalists selected by Iowa and the other lotteries that are participating in the Deal or No Deal promotion.

Lottery Raffle Game

This spring, the Iowa Lottery will begin sales in a raffle game offering a top prize of \$1 million. Sales in "Iowa's Million Dollar Raffle" will start April 13, with the drawing in the \$20 game scheduled for June 14, near the first day of summer.

Several lotteries around the country have offered raffle games over the past few years with great success. The Iowa Lottery is modeling its game upon some of the best practices from those games. Iowa's raffle game will offer:

- A total of 120,000 tickets with overall odds of 1 in 1,071.
- Top prize of \$1 million.
- One prize of \$100,000, 10 prizes of \$5,000 and 100 prizes of \$500.



Hot Lotto Sizzler



In January, a new option will be added to the Hot Lotto® game that is much like the Power Play option in the Powerball game. Hot Lotto started in 2002 as a game based upon the Powerball concept, but with smaller jackpots and easier odds. The game has grown through the years and now is sold by Iowa and 10 other lotteries.

Hot Lotto players currently choose five numbers from a pool of 39 and another number – called the Hot Ball – from a pool of 19 numbers. Tickets in the game cost \$1 and drawings are on Wednesdays and Saturdays.

Beginning Jan. 3, players will be able to add a \$1 Hot Lotto Sizzler option to each play they make in the game. If their ticket with the Hot Lotto Sizzler option wins a prize, that prize will be multiplied to three times the usual amount. The new option does not apply to jackpot prizes.

International Game Discussions

In the lottery's June report to the Oversight Committees and in memos provided to the committees since then, the lottery has provided initial details about discussions for a possible international lotto game.

As the lottery has reported earlier, possible plans for such a game remain in the discussion stage, and any game agreement will require approval from the Iowa Lottery Board. Discussion of a possible international game has been underway since 2001. Several different game ideas, prize structures and game names have been discussed through the years, although final decisions have never been made.

The Board of the Iowa Lottery voted in 2003 to approve an agreement to participate in what was then being called the International Lottery Alliance, which was administered by the Urbandale-based Multi-State Lottery Association, the same organization that administers games such as Powerball and Hot Lotto on behalf of member lotteries (including the Iowa Lottery). After the start of the Iraq war, however, the venture was put on hold indefinitely after some participants withdrew.

The idea has continued to percolate in the years since, and as has earlier been reported to the committees, it is being discussed again now. The issues that must be considered include tax and international business law, organizational structure, currency differences and game design.

Text Messaging Service

In December, the Iowa Lottery added text messaging to the list of options people have to learn about winning numbers in lottery drawings, the latest jackpot amounts, and other lottery news.

The lottery has offered a variety of tools through the years for players and the public to use to check the results of tickets and learn about lottery games and procedures. Those include:

- Watching the televised drawings in lotto games.
- Checking the information available on the lottery Web site at www.ialottery.com.
- Asking retailers to print out winning numbers from the lottery terminal.
- Call one of the lottery's five regional offices around the state for information.
- Listening to lottery results on local radio stations.
- And checking lottery results in local newspapers.



Text messaging has now been added to the list. By sending a request from your mobile phone or by signing up on the lottery Web site, you can receive messages from the lottery. The sign-up process requires those who want to receive the service to give their birth date to provide age verification. While the service from the lottery is free, standard carrier fees apply.

The current text-messaging options from the lottery are:

- Text NUMBERS to 97063 for twice-weekly updates on the winning numbers and jackpot amounts in Powerball and Hot Lotto.
- Text ALERT to 97063 for updates when the Powerball jackpot is \$100 million or more.
- Text PROMO to 97063 for periodic announcements about new games, promotions and special events.
- Text IALOT to 97063 for all text messages originated by the Iowa Lottery.

Spreading The Word About Iowa Initiatives

Homeland Security and Emergency Preparedness

In September, the Iowa Lottery was a part of state efforts to call attention to the importance of family emergency preparedness. Iowa Homeland Security and Emergency Management has established a Web site – www.bereadyiowa.org – with easy-to-follow tips on preparing for an emergency, and in the fall, several organizations, including the Iowa Lottery, put on a push to call attention to emergency preparedness efforts.

From Sept. 1-17, the Iowa Lottery printed messages about emergency preparedness on each lotto ticket it sold and ran messages on the customer display units that are installed in most lottery retail locations. The effort meant millions of messages about emergency preparedness being distributed to the public. As an example, the message that ran on the lottery's customer display units read: "Is your family ready for an emergency? Go to www.bereadyiowa.org for preparedness tips."

"Let's Talk Turkey" Game



Ongoing efforts by the Iowa Lottery to support the state's turkey industry continue this year.

In October, the lottery introduced the "Let's Talk Turkey" instant-scratch game, which features the Web site address for the Iowa Turkey Federation (www.iowaturkey.org) on each of its tickets. One of the game's goals is to drive Iowans to the new site, where they can access educational information and order a free turkey cookbook.

The Lottery has been happy to support Turkey Federation efforts in years past as well. In 2002, 2003, 2005 and 2007, the federation provided coupons to lottery patrons during the Iowa State Fair. In a new event this year, the turkey federation and the lottery held a turkey toss event at a hockey game in Des Moines. The lottery distributed free \$1 "Let's Talk Turkey" scratch tickets to the first 250 people age 21 and older who attended the Buccaneers hockey game Nov. 17 in Des Moines. Then, 50 contestants were randomly selected to take part in a turkey toss event at the game's first-period break. Those contestants were given a small squeezable plastic turkey to throw at a target on the ice. The three contestants whose turkeys landed closest to the target received free lottery tickets, gift certificates from the turkey federation and radio station T-shirts.

On-Going Issues

Consumer Reporting and Security Procedures At Lottery

In November, the lottery provided to the Oversight Committees and legislative leadership a copy of a report that had been presented to the Iowa Lottery Board regarding consumer reporting and security processes at the Iowa Lottery.

The report to the Lottery Board followed consultant reports that had been released in Canada concerning security matters at some lotteries there.

The Iowa Lottery takes great pride in the work done by its security department and believes those efforts are integral to maintaining the integrity of the lottery. We wanted to have an in-depth discussion

with the Lottery Board about the matters, and if the Board indicated that it wanted the Iowa Lottery to pursue a similar consultant here, the lottery stood ready to do that.

At their Nov. 1 meeting, Lottery Board members indicated that they believe the lottery's security and reporting procedures are quite robust and they see no need for a consultant to review the matters. The Board members, however, advised the lottery to be open to possible improvements to its system, which it certainly is and will continue to be.

A copy of the report to the Board is included in this report as Attachment D for anyone who wishes to review it again.

TouchPlay Lawsuits

During the 2006 session of the Iowa Legislature, legislation was passed that banned the operation of TouchPlay machines in Iowa. The lottery took steps to ensure that all machines were shut down by the deadline established in the legislation and all machines in the state were disabled by 11:59 p.m. May 3, 2006. The companies that owned the equipment have since removed the machines from retail locations.

More than 30 companies involved in the TouchPlay project have filed lawsuits over the shutdown of the program. As of December, three separate lawsuits remain pending in state courts. In addition, several companies that were retailer-operators in the TouchPlay program owe the lottery money from the sales on the machines. The lottery collected revenues through electronic funds transfers (EFT) from the companies' accounts. In the final weeks of the program, the lottery was unable to collect funds from some of those accounts. As of December, 14 companies owed the lottery a total of about \$2.4 million, and the lottery had filed counter-claims in court against 12 of those companies to try to collect the money that is owed.

The lottery continues to work with the Iowa Attorney General's Office about the TouchPlay-related legal matters. Under instructions from the Attorney General's office, the lottery is refraining from commenting further about the TouchPlay-related legal matters, other than to provide this listing of the lawsuits and their status:

1. Hawkeye Commodity Promotions, Inc.
(U.S. District Court, Northern District of Iowa, No. 06-CV-2026)
(8th Circuit Court of Appeals, No. 06-2406)
Hawkeye Commodity's request for an injunction was denied by the U.S. District Court. The case was appealed to the 8th Circuit Court of Appeals, which upheld the lower court's ruling. The time period for appealing that decision to the U.S. Supreme Court has expired and the case is closed.
2. Royal Financial; No. CL102586 (Polk County District Court)
The case was settled in August. The state of Iowa paid \$1,671,370.50 to Royal Financial.
3. Camden; No. LACV055187 (Linn County District Court)
Trial date scheduled for Jan. 28, 2008.
4. Siggins et al.; No. EQCL53324 (Polk County District Court)
Trial date scheduled for April 21, 2008.
Settlement was reached in October with one of the plaintiffs in the Siggins lawsuit. In that instance, the state paid \$388,000 to B&B Games of Ankeny. However, claims by the other litigants remain.
5. Howard Music; No. 107194 (Scott County District Court)
Trial date is scheduled for June 9, 2008.

CEO Retirement

On Oct. 31, Ed Stanek retired as the Iowa Lottery's CEO. Stanek, 61, had led the lottery since its start in 1985 and had worked in state government for 35 years. Stanek's successor will be appointed by Governor Chet Culver and require confirmation by the Iowa Senate.

New And Expanding Casinos In Iowa

In calendar year 2006, three new casinos opened in Iowa while another opened in early 2007. Expansions also are underway at several existing casino properties in Iowa, and a riverboat casino that currently splits its time between Fort Madison and Burlington has been given permission to operate as two permanent casinos in each of those communities.

While the Iowa Lottery does not consider itself to be in direct competition with casinos, it does compete with them and any other entertainment venue for consumers' disposable income. When riverboat gambling was introduced in Iowa in the early 1990s and slot machines underwent a major expansion in the mid-1990s, there was a noticeable, negative impact on Iowa Lottery sales. After experiencing multiple-year declines, lottery sales in Iowa eventually stabilized and began to rebound in 2002. Lottery executives will continue to monitor casino expansion in Iowa and the potential impact that could have on lottery sales.

High Fuel Prices

Iowa Lottery executives continue to closely monitor fuel prices to determine their effects on lottery sales, operations and profits. Gasoline prices around the world have been in record territory for much of the past year and home heating and cooling costs also have been high.

With fuel prices cutting into consumers' discretionary income, sales of lottery products and other convenience items could be impacted. And the lottery, like other businesses, has faced higher delivery costs and seen other budget impacts from the higher fuel costs.

But while some businesses can adjust the price of their products to pass along higher costs to consumers, that is not a possibility for lotteries, which sell products for firmly established prices such as 25 cents or \$1. An increase in the price of a lottery ticket from \$1 to \$1.05 would be shunned by consumers and have an extremely detrimental effect on sales.

U.S. Internet Gambling Legislation And The World Trade Organization

The U.S. Congress passed legislation in September 2006 designed to prohibit illegal Internet gambling. The legislation is intended to make it illegal for banks and credit card companies to make payments to illegal online gambling sites. Estimates before Congress took action were that more than \$12 billion was being wagered annually through more than 2,300 gambling Web sites, many of which were run from outside the United States.

Media reports from around the globe continue to warn that Internet gambling operators are looking for loopholes in the new law.

In addition, leaders from the small Caribbean nation of Antigua and Barbuda informed the Bush administration in late June that their country was preparing to withdraw intellectual property protections for U.S. trademarks, patents and industrial designs because of the U.S. gambling legislation. The island nation claims that its annual revenue from Internet gambling has dropped from \$1 billion to \$130 million following implementation of the U.S. Internet gambling legislation, and is trying to impose \$3.4 billion in trade sanctions against the United States.

Antigua and Barbuda had filed a complaint against the United States with the World Trade Organization, basing its arguments on the General Agreement on Trade in Services (GATS) that was signed in 1994.

A WTO dispute panel and appeals body both have found for the island nation. Under GATS, the United States agreed that it would not enact any laws or take any action that would be counter to open trade among nations signing the agreement. The United States agreed that entertainment and recreational services would be covered in GATS, but later argued that it did not mean for gambling to be included in that category.

Antigua & Barbuda had argued that because the United States allows casinos, lotteries and other forms of betting, it has no basis to claim that gambling shouldn't be included in GATS.

The outcome of the Antigua & Barbuda dispute remains to be seen. Iowa Lottery executives will continue to monitor developments.

Lottery Operations - Budget Detail

Attachment A
Page 1 of 2

| | 2007 PRELIMINARY ACTUAL | 2008 BOARD APPROVED BUDGET | 2009 BOARD APPROVED BUDGET |
|---|----------------------------|-------------------------------|-------------------------------|
| Personal Services | 8,405,129 | 9,360,541 | 9,360,541 |
| Personal Travel in State | 85,689 | 100,000 | 110,000 |
| State Vehicle Operation | 285,158 | 229,648 | 300,000 |
| Vehicle Depreciation | 164,874 | 170,111 | 170,010 |
| Personal Travel Out of State | 29,006 | 45,000 | 40,000 |
| Office Supplies | 82,945 | 99,294 | 85,000 |
| Facility Maintenance Supplies | 14,441 | 11,753 | 15,000 |
| Other Supplies | 855 | 1,996 | 1,000 |
| Printing and Binding | 21,348 | 30,000 | 22,000 |
| Postage | 44,942 | 35,000 | 45,000 |
| Communications | 128,913 | 141,300 | 130,000 |
| Rentals | 276,385 | 311,500 | 280,000 |
| Utilities | 97,640 | 116,515 | 116,515 |
| Prof & Scientific Services | 89,259 | 78,875 | 90,000 |
| Outside Services | 52,087 | 104,340 | 74,060 |
| Outside Repairs | 100,945 | 66,188 | 100,000 |
| Attorney General | 102,961 | 116,190 | 116,190 |
| Auditor of State | 59,302 | 92,750 | 80,000 |
| Reimbursement to Other Agencies | 199,503 | 257,665 | 202,000 |
| ITS Reimbursement | 38,385 | 22,000 | 40,000 |
| Equipment | - | 30,000 | 20,000 |
| Equipment Non Inventory | 23,985 | 20,000 | 25,000 |
| IT Equipment (Inventory, non-inventory) | 102,037 | 70,000 | 70,000 |
| Other Expenses | 112,079 | 91,650 | 110,000 |
| Fees | 2,125 | 2,300 | 2,300 |
| Total Lottery Operations | 10,519,993 | 11,604,616 | 11,604,616 |

Increase (Decrease) In Net Assets

| | 2007 PRELIMINARY ACTUAL | 2008 BOARD APPROVED BUDGET | 2009 BOARD APPROVED BUDGET |
|---|----------------------------|-------------------------------|-------------------------------|
| Bonds payment | 2,000,000 | 2,000,000 | 100,000 |
| Depreciation Expense (ITVM/PTVM/BUILDING) | (1,222,472) | (1,401,245) | (1,222,588) |
| Other adjustments - capital assets | (132,841) | - | - |
| Total Change in Net Assets | 644,687 | 598,755 | (1,122,588) |

Budget for Lottery Fund

| | 2007 PRELIMINARY ACTUAL | 2008 BOARD APPROVED BUDGET | 2009 BOARD APPROVED BUDGET |
|---|----------------------------|-------------------------------|-------------------------------|
| Resources | | | |
| Lottery Sales | 235,001,239 | 213,500,000 | 235,000,000 |
| Interest | 781,091 | 500,000 | 570,000 |
| Application Fees | 6,300 | 25,000 | 5,000 |
| Other | 147,249 | 5,000 | 5,000 |
| Total Resources | 235,935,879 | 214,030,000 | 235,580,000 |
| Expenditures | | | |
| Prizes | 133,356,857 | 115,146,436 | 130,645,384 |
| Retailer Compensation | 14,674,744 | 13,742,595 | 14,500,000 |
| Marketing, Education and Information | 6,204,924 | 8,540,000 | 9,400,000 |
| Retailer Lottery System | 7,339,692 | 6,797,131 | 7,300,000 |
| Instant/PT Ticket Expense | 2,569,848 | 2,361,972 | 2,400,000 |
| Terminal Communications | 416,579 | 500,000 | 425,000 |
| Terminal equipment/Ticket dispensers | 112,875 | 100,000 | 100,000 |
| PTVM/ITVM Servicing | 521,517 | 550,000 | 525,000 |
| Interest Expense (ITVM/PTVM/BUILDING) | 175,147 | 115,000 | 50,000 |
| Depreciation Expense (ITVM/PTVM/BUILDING) | 1,222,472 | 1,401,245 | 1,222,588 |
| Refunds/Other | 6,756 | 2,100 | 2,100 |
| Lottery Operations | 10,519,993 | 11,604,616 | 11,604,616 |
| Total Expenditures | 177,121,404 | 160,861,095 | 178,174,688 |
| Net Income | | | |
| Prior to Net Asset Change | 58,814,475 | 53,168,905 | 57,405,312 |
| Increase (decrease) in net assets | 644,687 | 598,755 | (1,122,588) |
| After Net Asset Change | 58,169,788 | 52,570,150 | 58,527,900 |
| Transfers | | | |
| Proceeds Transfer | 56,990,862 | 51,500,000 | 57,350,000 |
| Gamblers Assistance Transfer | 1,178,926 | 1,070,150 | 1,177,900 |
| Total Expenditures, Transfers & Change in Net Assets | 235,935,879 | 214,030,000 | 235,580,000 |

Iowa Lottery Authority

Mission Statement

The Iowa Lottery strives to administer lottery games in a secure manner to maximize revenue while maintaining the dignity of the state and the welfare of its people.

Description

To achieve its mission the Iowa Lottery Authority has established three subunits: 1) Administrative Division, 2) Securities and Licensing Division, and 3) Marketing Education & Information Division.

The Administrative Division develops and implements strategies to increase gross revenue and develops and implements controls to increase the net revenue. Manages the activities affecting the entire Lottery; including personnel, budget, training, accounting, data processing, purchasing, supplies and services. Sets Lottery goals and objectives and makes final determination on games, prizes and marketing programs. The Security Division designs and implements security policies and procedures

affecting computer systems, facilities, Lottery and vendor personnel, and product control to insure the total and complete honesty and integrity of the Lottery. Protects the Lottery's premises from intrusion or harm, and recommends unusual circumstances for investigation. Coordinates all licensing matters pertaining to the Lottery. Interprets license rules and recommends appropriate action. Reviews and recommends the selection of all equipment used for Lottery drawings and events. Maintains all equipment to insure randomization of drawings and jackpot events. The Marketing Division is responsible for marketing Lottery products to the State's consumers to achieve projected sales goals. Develops and implements strategies to encourage sales productivity of the Lottery retailer base, develops and implements advertising strategies for the marketing of Lottery products to maximize sales potential, and designs future Lottery products that incorporate elements the public prefers, thus maximizing public acceptance and participation. Monitors the volume of ticket sales, reviews statistical reports of regional data and sales trends so that optimum sales can be achieved.

Performance Measures

| Measure | FY 2007 Actuals Achieved | FY 2008 Board Approved Budget | FY 2009 Board Approved Budget |
|---------------------------------|--------------------------------|-------------------------------------|-------------------------------------|
| Total Dollar Transfers to State | 56,970,554 | 51,500,000 | 57,350,000 |
| Total Dollar Sales | 235,001,239 | 213,500,000 | 235,000,000 |

Financial Summary

| Object Category | FY 2007 Actuals | FY 2008 Board Approved Budget | FY 2009 Board Approved Budget |
|------------------------------------|--------------------|-------------------------------------|-------------------------------------|
| Resources | | | |
| Receipts from Other Entities | 0 | 500 | 500 |
| Interest, Dividends, Bonds & Loans | 1,805,083 | 1,500,000 | 1,470,000 |
| Fees, Licenses & Permits | 6,522 | 25,000 | 5,000 |
| Refunds & Reimbursements | 4,017 | 100 | 100 |
| Sales, Rents & Services | 234,861,450 | 213,500,500 | 235,000,500 |
| Miscellaneous | 8,746,327 | 6,683,900 | 5,110,900 |
| Income Offsets | 18,500,218 | 16,252,414 | 0 |
| Total Resources | 263,923,617 | 237,962,414 | 241,587,000 |
| Expenditures | | | |
| Personal Services | 8,366,954 | 9,360,541 | 9,360,541 |
| Travel & Subsistence | 522,139 | 544,759 | 620,010 |
| Supplies & Materials | 164,596 | 178,043 | 168,000 |
| Contractual Services and Transfers | 73,824,352 | 70,264,604 | 77,406,665 |
| Equipment & Repairs | 270,340 | 220,000 | 215,000 |
| Claims & Miscellaneous | 164,486,883 | 141,137,653 | 153,812,384 |
| Licenses, Permits, Refunds & Other | 8,881 | 4,400 | 4,400 |
| Plant Improvements & Additions | 27,059 | 0 | 0 |
| Balance Carry Forward | 16,252,414 | 16,252,414 | 0 |
| Total Expenditures | 263,923,617 | 237,962,414 | 241,587,000 |
| Full Time Equivalents | 112 | 115 | 115 |

Fund Detail

Iowa Lottery Authority Fund Detail

| Funds | FY 2007 Actuals | FY 2008 Board Approved Budget | FY 2009 Board Approved Budget |
|-------------------------|--------------------|-------------------------------------|-------------------------------------|
| Lottery Authority | 263,923,617 | 237,962,414 | 241,587,000 |
| Lottery Fund | 239,808,260 | 216,984,715 | 235,580,000 |
| Lottery Jackpot Winners | 24,115,357 | 20,977,699 | 6,007,000 |

Lottery Fund

Fund Description

This account receives proceeds from lottery sales to provide for non- appropriated lottery expenses.

Fund Justification

The Lottery Fund budget for the Iowa Lottery Authority has been prepared and approved in accordance with Senate File 453 and does not require any

action on the part of the Iowa Legislature. The budget presented herein is for informational purposes only. The Lottery Fund represents the receipt of all revenue from the sales of lottery instant, pull tab, and on-line tickets along with the receipts, application fees and interest. The funds received are allocated and/or transferred to various accounts/activities including prizes, advertising, and general operating expenses including ticket costs, vendor costs, retailer commissions and line charges. The balance is then transferred to the General Fund.

Lottery Fund Detail

| Object Class | FY 2007 Actuals | FY 2008 Board Approved Budget | FY 2009 Board Approved Budget |
|-----------------------------------|--------------------|-------------------------------------|-------------------------------------|
| Resources | | | |
| Balance Brought Forward (Funds) | 3,979,621 | 2,954,715 | 0 |
| Adjustment to Balance Forward | 125 | 0 | 0 |
| Reimbursement from Other Agencies | 0 | 500 | 500 |
| Interest | 844,530 | 500,000 | 570,000 |
| Fees, Licenses & Permits | 6,522 | 25,000 | 5,000 |
| Refunds & Reimbursements | 4,017 | 100 | 100 |
| Other Sales & Services | 234,861,450 | 213,500,500 | 235,000,500 |
| Other | 111,993 | 3,900 | 3,900 |
| Total Lottery Fund | 239,808,260 | 216,984,715 | 235,580,000 |
| Expenditures | | | |
| Personal Services-Salaries | 8,366,954 | 9,360,541 | 9,360,541 |
| Personal Travel In State | 85,526 | 100,000 | 110,000 |
| State Vehicle Operation | 285,158 | 229,648 | 300,000 |
| Depreciation | 126,380 | 170,111 | 170,010 |
| Personal Travel Out of State | 25,075 | 45,000 | 40,000 |
| Office Supplies | 81,872 | 99,294 | 84,500 |
| Facility Maintenance Supplies | 14,441 | 11,753 | 15,000 |
| Other Supplies | 354 | 1,496 | 1,000 |
| Printing & Binding | 22,485 | 30,000 | 22,000 |
| Food | 501 | 500 | 500 |
| Postage | 44,942 | 35,000 | 45,000 |
| Communications | 543,857 | 601,300 | 520,000 |

Lottery Fund Detail (Continued)

| Object Class | FY 2007 Actuals | FY 2008 Board Approved Budget | FY 2009 Board Approved Budget |
|------------------------------------|--------------------|-------------------------------------|-------------------------------------|
| Rentals | 276,385 | 311,500 | 280,000 |
| Utilities | 91,013 | 116,515 | 116,515 |
| Professional & Scientific Services | 7,423,962 | 6,876,006 | 7,390,000 |
| Outside Services | 573,875 | 669,340 | 634,060 |
| Intra-State Transfers | 58,150,436 | 52,570,150 | 58,527,900 |
| Advertising & Publicity | 6,274,912 | 8,540,000 | 9,400,000 |
| Outside Repairs/Service | 100,858 | 91,188 | 100,000 |
| Attorney General Reimbursements | 102,961 | 116,190 | 116,190 |
| Auditor of State Reimbursements | 59,444 | 92,750 | 80,000 |
| Reimbursement to Other Agencies | 188,269 | 257,665 | 202,000 |
| ITS Reimbursements | 38,380 | 22,000 | 40,000 |
| Equipment | 11,000 | 30,000 | 20,000 |
| Office Equipment | 15,177 | 0 | 0 |
| Equipment - Non-Inventory | 136,860 | 120,000 | 125,000 |
| Claims | 134,201,013 | 115,146,436 | 130,645,384 |
| Other Expense & Obligations | 14,851,815 | 13,834,245 | 14,610,000 |
| Inventory | 2,435,777 | 2,361,972 | 2,400,000 |
| Interest Expense/Princ/Securities | 2,180,620 | 2,115,000 | 150,000 |
| Licenses | 455 | 300 | 300 |
| Fees | 1,670 | 2,000 | 2,000 |
| Refunds-Other | 6,756 | 2,100 | 2,100 |
| Capitals | 27,059 | 0 | 0 |
| Balance Carry Forward (Funds) | 2,954,715 | 2,954,715 | 0 |
| IT Equipment | 107,303 | 70,000 | 70,000 |
| Total Lottery Fund | 239,808,260 | 216,984,715 | 235,580,000 |

Chester J. Culver
Governor



Patty Judge
Lt. Governor

To: Iowa Lottery Board

**From: Mary Neubauer
Vice President, External Relations**

Date: Nov. 1, 2007

Re: Review of Consumer Reporting and Security Processes

For about a year, we at the Iowa Lottery have been tracking a series of security-related, consumer protection issues that have arisen at lotteries in Canada. Ed Stanek has been sending along information regarding the Canadian developments to you as we continued to monitor the situation.

There are fundamental differences between the way consumer concerns and security issues were handled at some of the lotteries in Canada and the processes we have in place here. We also believe that the Iowa Lottery has taken many proactive steps through the years to remind consumers about the security tips they can follow to be fully informed when they play lottery games. Nevertheless, the issues that have arisen in Canada deserve attention by all lotteries.

We believe we have a well-developed system here in Iowa that provides consumers with information about lottery tickets and their results. In addition, our security and integrity standards ensure that 100 percent of issues referred to our security department are investigated. But, that does not mean that there aren't other approaches we could consider using here.

Let's start a discussion today and continue it at future Board meetings so we all can examine the issues together as part of our public meetings.

The issues in Canada date back to 2001 when an Ontario man visited a variety store that sold lottery tickets and asked the store owner's wife, who was working at the check-out counter that day, to check his lotto tickets. She told him he had won a free ticket, but didn't mention any other prizes. The man later became suspicious when he read in the paper that the store owner and his wife had won a \$250,000 prize. He contacted the Ontario Lottery Corporation and was able to provide documentation to the lottery showing that he had regularly played the numbers that were on the \$250,000-winning ticket. He also provided details about what happened when he went into the store to have his lotto tickets checked that day.

The man's account was in stark contrast to that of the supposed winning couple, who could not say when or where the ticket was obtained or if there was any significance to the numbers chosen. Despite that, it appears that it took the lottery months to look into the matter. And even then, much of the lottery's activity began only after local police had arrested the husband-and-wife team who ran the store and charged them with fraud and theft. After that, the man still had to go to court to try to collect his winnings. The civil litigation lasted for three years, but he did eventually receive a \$150,000 settlement from the retailers involved and a \$200,000 settlement from the Ontario Lottery.

It's important to point out that there are no complaints of situations reported by Iowa Lottery players being ignored or left uninvestigated. Any issues relating to security or possible matters of impropriety are referred to the Iowa Lottery's security department, where 100 percent of referrals are investigated, and when appropriate, referred to law enforcement.

We want to go over some other key differences between the situation that existed in Ontario and the processes and standards we have in place here.

First and foremost, the Iowa Lottery requires that those applying for a lottery retail license undergo background checks by the Iowa Division of Criminal Investigation. Anyone who has been convicted of a fraud, felony or gambling violation is not licensed as a lottery retailer in Iowa. At the time of the case we've been discussing in Ontario, no pre-screening was done of those who applied to sell lottery products there.

In addition, the Iowa Lottery issues terms and conditions for its retail licenses and those businesses that are licensed to sell lottery tickets must comply with those terms and conditions. A first-time violation of the terms and conditions results in a one-week suspension of the retail license and therefore, the store's ability to sell lottery products. A second violation within a year results in a one-month suspension of the retail license; and a third violation within a year results in a one-year suspension of the retail license. Any suspected criminal activity would be referred to law enforcement. Any conviction for fraud, compromising the security or integrity of the lottery, illegal gambling, or any felony, would lead to a license revocation. In Iowa a revoked license applies for 10 years unless the Board finds that the violation was minor or unintentional.

At the time of the case in Ontario, there was no specific "Code of Conduct" for retailers there.

There have been instances where retailer licenses have been suspended in Iowa. In 2006, for example, two retail licenses were suspended after documented cases of underage sales at those stores. Such instances have been rare -- retailers in Iowa in general have a strong record of handling and selling a wide range of products, including lottery tickets. But in the instances where there have been violations, the lottery has dealt with them according to its retailer terms and conditions.

Another major difference between the situation described in Canada and the procedures of the Iowa Lottery lies in the key area of investigation. The Iowa Lottery has its own staff of five investigators, all of whom are required to have a history of law enforcement work and training.

Our investigators must have law enforcement academy training at a minimum and complete annual continuing education classes in law enforcement matters. Through the years, Harry Braafhart, our Vice President of Security, has provided you with reports at Board meetings about the investigations conducted by the Iowa Lottery's security department. Many of those investigations have been prompted by reports of stolen tickets or ownership disputes over lottery tickets. The lottery's security department has a strong record of investigation and apprehension in its cases.

Let me give you a couple key examples. One is a case many of us remember well. In 1999, an Urbandale convenience store clerk came to lottery headquarters and claimed a \$28 million Powerball jackpot. After he made his claim but before the prize was paid, an underage co-worker came forward and claimed a share of the prize. The lottery investigated the claim and involved the Attorney General's office. The co-worker filed a lawsuit against the claimant. It was determined that the case was not a criminal matter, so the details of the lottery's investigation were made available to the parties, who then reached a settlement agreement, ending the litigation.

The other case involves a \$100,000-winning Powerball ticket that was claimed in 2001 by an 85-year-old woman from Sperry in southeastern Iowa. After the prize had been paid, the lottery received a telephone call from a man who said he suspected that the winning ticket had been stolen from a group of co-workers at a Mediapolis company who pooled their money to buy Powerball tickets. The lottery investigated the case and was able to show that the winning ticket had been switched out from among those that were purchased for the group of co-workers. As it turned out, the woman who bought tickets on behalf of the group lived with her grandmother. The grandmother pleaded guilty later that year to felony theft in the case. She had stolen the winning ticket from its hiding place under a bird cage in the home she shared with her granddaughter.

There are two different examples for you – one involving a dispute before a prize was paid and the other involving questions that arose after the prize was paid. In both instances, the lottery investigated the matter and sought and received the assistance of outside law enforcement, which ultimately brought the cases to resolution.

We're proud of the success rate lottery security has achieved through the years. Nationally, arrests are made in just 16 percent of burglary cases, but because of the specific information that can be provided about lottery tickets, arrests have been achieved in 88 percent of burglaries investigated by lottery security. Theft cases investigated by lottery security are solved about 85 percent of the time.

That is not to say there haven't been concerns expressed by lottery players about retailers in the state. There have been, and those instances have been investigated by the lottery. A case earlier this year in Burlington is a good example. In that instance, an elderly woman called the lottery and spoke with one of our security officers. She said she had recently redeemed a Powerball ticket at a local supermarket and was certain that she had won \$200,000, but the clerk had only paid her \$35. She was not sure where she had purchased the ticket and couldn't remember exactly when she had redeemed it, but thought it was on one of two days.

Even with just those few details to work with, our security department was able to check the lottery records from the store involved. Our security officer was able to show that the woman had indeed won \$35 in the Powerball drawing on July 11. She had matched three numbers to win a \$7 prize and by adding the Power Play to her ticket, her prize had been multiplied to \$35.

Our security officer then called the woman back with his findings and she thanked him for his help and his time.

That is the same approach our security department uses in any case it investigates. If there is something amiss, we want to know that so we can rectify the situation. If there is nothing wrong, we want to know that as well and be able to share that information with those involved so they can have peace of mind.

Another major area of difference between the procedures of the Iowa Lottery and those that were highlighted in Ontario has to do with the issue of so-called “insider wins.” In Ontario, it is legal for lottery employees and their immediate family members to play the lottery. In addition, it is legal for employees of the lottery’s key contractors and subcontractors to play the lottery. There are additional security checks that are conducted if any of those people wins a large prize, but they are not prevented from playing. There have been concerns expressed in Ontario and some other Canadian provinces about the issues involved when retailers or retail employees play the lottery, but not as much discussion about lottery employees or employees of lottery contractors playing the games.

That is in stark contrast to state law here in Iowa and the security requirements of our lottery. Iowa Code section 99G.31 makes it illegal for lottery tickets to be purchased or for prizes to be paid to Iowa Lottery Board members; employees of the lottery, or to any spouse, child, brother, sister or parent residing as a member of the same household in the principal place of residence of any of those people. The law also puts those same restrictions on employees, agents and subcontractors of lottery vendors who have access to confidential information that could compromise the integrity of the lottery. Specified family members of those people also are prohibited from purchasing tickets or winning lottery prizes.

So, here in Iowa, lawmakers considered “insiders” to be employees of the lottery and employees of subcontractors or vendors with inside information that could compromise the lottery if they were allowed to play. The lottery maintains a database of the Social Security numbers of all its employees; the employees of the independent auditors assigned to work at lottery drawings; and those employees of subcontractors and vendors who have inside access to information that might compromise the integrity of the lottery. The database also includes the Social Security numbers of the appropriate relatives of those people. When tickets are claimed at the lottery, the identity of the person claiming the prize is checked against that database so a prize won’t be paid to an “inside” person.

Retailers, by contrast, don’t have access to confidential information associated with the lottery and they can’t affect the outcome of drawings. Yes, they sell lottery tickets, but they can’t get into the computer system that contains game information or generates plays. They also aren’t

included in the state law defining “insiders” in Iowa, so they aren’t included in the lottery’s database that’s checked during prize redemption.

The lottery’s efforts to protect its sales and validations system are double-checked on an annual basis by the state Auditor’s office, which contracts with an auditing firm to conduct an SAS 70 audit of the lottery system. In addition, every two years, the Multi-State Lottery Association reviews the Iowa Lottery’s computer system and associated controls to ensure they meet the security and integrity standards for participation in multi-jurisdictional games.

Finally, we come to the issue of consumer protection. The lottery has taken a number of steps through the years to provide the public with information about lottery games and prizes. But we have been putting on an especially heavy push in that area since early this year, when we conducted a news conference and began a public-service campaign with the Attorney General’s office to warn people about the lottery scams that have been sweeping the country.

Leading up to the January news conference, we expanded and centralized the security information we have on our Web site and made “Player Security” one of the main links on our home page. We announced the expanded player security information in a statewide news release; we advertised the new security pages for months with Web banners on our Web site and other prominent sites around the state; and we mentioned it in statewide public service radio ads we produced and paid for along with the attorney general’s office.

In addition to those security reminders, the lottery for years has provided information in its game brochures about its office locations, telephone numbers and Web site address. We also include that information in many of the news releases we send out every day.

But that’s not all. For more than a decade, the lottery also has provided informational stickers on its sales terminals, vending machines, play stations and ticket dispensers that remind players to check the accuracy of their tickets when they purchase them. The stickers advise players to sign the backs of their tickets before they claim them and to contact the lottery if they have any concerns. All of that information, as well as lists of prizes still available in our games and lists of prizes that have yet to be claimed, are available on our Web site. That’s in addition to the security reminders that are printed on the backs of our tickets.

Our information also advises players that there are several ways they can check the results of their tickets: They can watch the televised drawings in lotto games, check the information on the lottery Web site, ask retailers to print out winning numbers from the lottery terminal, call one of the lottery’s five regional offices around the state, listen to lottery results on local radio stations, and check lottery results in local newspapers.

The first line of defense in consumer protection is always for players to arm themselves with the information they need to determine whether their tickets have won a prize. That’s much the same thing we all should be doing to ensure, for example, that a clerk has given us the proper change or that the milk we buy at the local store rings up for the right price. The lottery offers its players a plethora of information they can use to determine the outcome of their tickets. However, we

have felt that there is no substitute for player responsibility and player diligence, despite all the assistance that we can provide.

Hopefully, this has provided you with an overview of many of the security issues the lottery deals with on a daily basis. Again, there have been no consumer complaints here like those that have occurred in Canada. But we're not saying that we think our system is flawless. There may be improvements that can be made.

After consumer complaints in Ontario and Quebec, the lotteries there each have spent hundreds of thousands of dollars on consultants' evaluations of their systems. They are now in the process of implementing many of the consultants' suggestions for improvements, which have turned out to be some of the things we already have been doing for years.

We're not sure of the merit of some of the improvements prescribed in Canada, however. One of the relatively simple ideas is for a musical "jingle" that would play from the lottery terminal each time a winning ticket was scanned. Our terminals are capable of that change and we've discussed that idea in the past. But we've chosen not to use it because of concerns over public safety. A winning jingle might tip off stalkers to a particular player's good fortune, leaving that person vulnerable to attack once they left the retail establishment. Those are the types of issues that must be weighed when you're talking about new ideas that could be implemented.

We welcome your comments today regarding the security details we've covered, and whether you think it would be a good idea for the lottery to pursue an outside consultant to evaluate our security processes. At future Board meetings, we'd like to continue this conversation and focus in on particular areas we've covered in general today.