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Governor  
  
Kim Reynolds  
Lt. Governor



Terry Rich  
Chief Executive Officer

## Iowa Lottery Report On Operations

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

**From: Terry Rich, CEO**

**Date: June 2016**

**The Iowa Lottery is on pace to set records for sales, proceeds to state causes and prizes to players, with some exceptional circumstances combining to put fiscal year 2016 on pace to become the most successful in the lottery's history.**

**The world-record Powerball jackpot in January produced extremely strong lotto sales for the year and instant-scratch game sales continued to be strong throughout the year, fueled by an emphasis on game variety in the marketplace.**

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 \$300 million, marking the fifth year in a row that the total has exceeded that threshold. Here is a year-to-year comparison of lottery sales (July-May) by product:

	<u>FY 2016</u>	<u>FY 2015</u>
Instant-scratch games	\$214.6 million	\$195.1 million
Pick 3	\$6.8 million	\$6.4 million
Powerball	\$71 million	\$49.3 million
Mega Millions	\$13.7 million	\$16.6 million
Hot Lotto	\$8.1 million	\$10.1 million
Pick 4	\$3.2 million	\$2.9 million
All or Nothing	\$3.7 million	\$4.2 million
Lucky for Life*	\$2.6 million	-----
Monopoly Millionaires' Club**	-----	\$0.6 million
Pull-tab games	\$13.9 million	\$14.7 million

\*The Lucky for Life game was introduced in Iowa in January 2016.

\*\*The Monopoly Millionaires' Club game was introduced in October 2014 and ended sales in Iowa in December 2014.

As always, we are closely tracking lottery results and will keep your committees apprised of significant developments. We also provide regular updates about sales and proceeds through the state's I-3

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

## FY 2017 Budget Updates

At the Lottery Board's meeting on June 28, the lottery's FY 2017 budget was given final approval to adjust some line items to more closely align with FY 2015 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 2017 are included with this report as **Attachment B** and **Attachment C**.



Mike Klappholz



Connor Flynn



Mary Rathje



Ying Sa



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; Ying Sa, the founder and principal certified public accountant at a CPA firm in Des Moines, 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.

## Board Approval For Lottery Product



As the lottery has emphasized many times through the years, we evaluate our existing product line and watch developments from other states in an effort to provide a fresh variety of games in the marketplace. A product that has succeeded in several other states recently caught our attention and has been presented to the Lottery Board for consideration.

At its June 28 meeting in Cedar Rapids, the Iowa Lottery Board approved plans for the Iowa Lottery to move ahead with a product that has proven successful in 13 other states. The product is known by a few different names in the other states where it is offered – Print-N-Play, EZ Play, Fast Play – but in Iowa, it will be called InstaPlay. It is a “scratchless” version of traditional lottery scratch tickets, meaning that InstaPlay tickets do not have a latex coating on the play area. InstaPlay tickets are printed from a lottery terminal, as are tickets in lotto games.

As with the lottery's other products, InstaPlay tickets can be sold at several different price points, depending upon the specifics of the game involved.

Rather than printing tickets in advance as occurs in traditional scratch and pull-tab games, InstaPlay tickets are printed on demand from the lottery terminal. The retailer presses a button on the terminal to print a ticket, just as occurs in games

like Powerball and Mega Millions.

InstaPlay tickets contain game graphics and play instructions that describe how to play the game and determine if the ticket has won a prize. The tickets also can include an area for a progressive jackpot if that option were to be offered. In that instance, the jackpot would grow with each ticket sold and the current jackpot amount would be displayed on the ticket as it was printed.

Now that the Lottery Board has approved the new product, the lottery is developing three InstaPlay games and preparing to make upgrades to its central communications system to incorporate the new games. Testing, development of educational materials about the games, retailer training and administrative rules changes will follow.

The goal is to begin selling InstaPlay games as a new lottery product sometime in fall 2016.

## **Latest Audit of Lottery & Our Annual Report**

Each year, the Iowa Lottery is audited by the State Auditor's Office. The auditors review the Lottery's operations as required by state law. The auditor's efforts are in addition to the security and integrity standards the lottery has adopted and employed throughout its operations to ensure the veracity of its games.

State Auditor Mary Mosiman released the results of the FY 2015 audit of the lottery on Jan. 11, providing another **clean report** for Iowa's lottery. The audit report is available on the state auditor's website at: <http://auditor.iowa.gov/reports/1660-6270-B000.pdf>.

The official language in the report includes these highlights:

- In the opinion of the Auditor's Office, the financial statements of the lottery for FY 2015 "present fairly, in all material respects, the financial position of the Iowa Lottery Authority as of June 30, 2015."
- The Auditor's Office "did not identify any deficiencies in internal control we consider to be material weaknesses."
- The results of tests conducted by the Auditor's Office "disclosed no instances of non-compliance or other matters that are required to be reported under Government Auditing Standards."

Once the lottery has received its audited figures from the Auditor's Office, it releases its annual report for the year. A link to the Lottery's Annual Report for FY 2015 is available here: <http://www.ialottery.com/AboutUs/AnnualReport.asp>.

## **Iowa's Biggest Winner So Far This Calendar Year**



A western Iowa man has the distinction of being Iowa's biggest lottery winner to date in calendar year 2016.

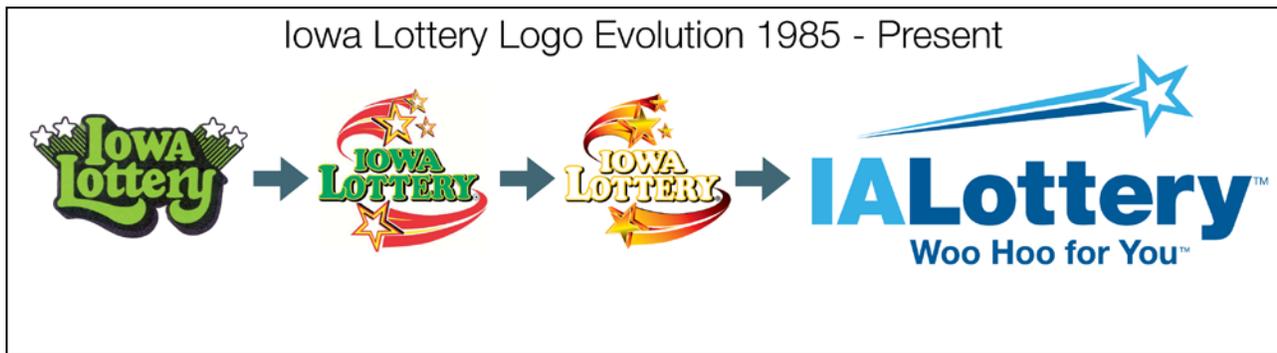
Bryon Stewart, 23, of Onawa, claimed a \$2 million prize in mid-January that he had won on a Powerball ticket he purchased as the game's jackpot was climbing to a world record that month. Stewart, a security officer at WinnaVegas Casino & Resort in Onawa, said he bought a total of three tickets for the drawing, and won big on one of them.

He said he planned to share his winnings with his girlfriend, Taylor Kuhlman.

## **A New Look For The Iowa Lottery**

Fiscal year 2015 marked the lottery's 30<sup>th</sup> anniversary, which means the lottery now has entered its fourth decade in business. At the same time, it has introduced its fourth logo.

The new look maintains the shooting star that has been central to the lottery's identity since its start, but abbreviates the lottery's name in a nod to today's shortened communications style. The new logo for the lottery moves from a circular symbol utilizing reds, yellows and oranges to a streamlined look in blue and white.



The lottery's original logo at its start in August 1985 was largely green with four shooting stars bracketing the words "Iowa Lottery" in the center. That logo was replaced in August 1994 as the lottery celebrated its 10<sup>th</sup> anniversary.

The lottery's second logo maintained the shooting stars, but circled them around the words "Iowa Lottery." That version of the logo, with green letters, yellow stars and red streaks of light behind them, was used until September 2002 when it was updated. The new version of that image, with white letters in the center surrounded by graduated red, orange and red stars, has been used since that time.

On July 1, the lottery will begin to utilize its new blue-and-white logo that features just one shooting star above the term IALottery.

The shooting star has always been central to the Iowa Lottery. It's a symbol of luck but also represents celebration, and is aspirational in terms of the vital difference lottery proceeds have made in the state.

The new logo will be phased in over time as current supplies run out and equipment is replaced.

The lottery for several years also has used a distinctive "Woo-hoo!" recording to punctuate its advertising and as the sound that plays from lottery terminals in Iowa when a winning ticket is scanned. The new logo incorporates a "Woo Hoo for You™" tagline that, like the shooting star, references luck and excitement.

## **Industry Recognition for Iowa Lottery**

In late May, the Iowa Lottery received a best-practices designation within the lottery industry for the testing procedures it utilizes in its statewide gaming system.



The lottery received the quality-assurance verification from the North American Association of State and Provincial Lotteries (NASPL) and its third-party assessor, The Open Group, an international consortium that is a leader in I.T. standards and certifications.

NASPL, which represents 52 lotteries in the United States, Canada and Mexico, has developed best practices intended to provide lotteries and vendors with a simple, documented method for building quality into their procedures.

**NASPL**

The Iowa Lottery gained its quality assurance verification from NASPL after having the organization review the testing procedures it utilized in updating its statewide gaming system to accommodate the Oct. 4 matrix change in the Powerball® game and Iowa's introduction of the Lucky for Life™ game on Jan. 24. The lottery's gaming system is integral to the organization's operation, as the system is used in the sale of lottery tickets and payment of prizes at retail locations across the state.

Before making any changes to its gaming system, the lottery documents the tests it plans to conduct to ensure a change successfully can be made, then carries out the testing and documents and reviews the results. The change is implemented on the system only after the lottery is satisfied with its testing results. The process is designed to ensure that changes can be made as seamlessly as possible.

NASPL's review of the Iowa Lottery's procedures was a five-month process. The verification designation for the Iowa Lottery is good for three years, at which time the lottery could apply for another review.

## **Updates To Lottery Vending Machines/Self-Service Kiosks**

As you will recall, legislation was approved during the 2016 session allowing the Iowa Lottery to move forward with replacement of its vending equipment for lottery tickets. House File 2146 was signed into law March 30 and took effect upon enactment.

The lottery's current vending machines are more than a decade old and need to be replaced. As with other types of vending equipment, many lottery ticket-dispensing devices today utilize touch-screen technology. The change in law in HF 2146 makes it clear that the lottery can utilize such self-service kiosks.

With passage of the legislation, replacement of lottery vending equipment will begin this fall.

The lottery currently has vending machines for instant-scratch tickets in about 260 retail locations and pull-tab vending machines in about 765 locations. Understanding that there is a cost to new equipment and that there must be a volume of business for its installation to be profitable, the lottery anticipates having fewer machines in fewer locations as it moves ahead.

The lottery has placed orders for 115 new machines to vend scratch tickets and lotto tickets, and 325 machines to vend pull-tab tickets. The lottery was able to arrange for the maintenance and removal of existing vending equipment during a transition period.

The lottery anticipates that its new vending equipment/self-service kiosks will begin to be installed in retail locations in fall 2016, with the transition of equipment continuing for a number of months. The lottery's goal is for the swap-out of equipment to be completed by the end of fiscal year 2017.

## **Ongoing Lottery Jackpot Investigation**

Trial that had been scheduled in July in Polk County for the first man charged in the long-running lottery jackpot investigation has been delayed, likely until February 2017. That trial will be moved out of Polk County after concerns regarding pretrial publicity, but a new location for the trial has not yet been set.

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



Tipton was convicted in July 2015 on two felony counts of fraud in the incident that started the investigation nearly five years ago: the attempted claim of a lottery jackpot in 2010 here in Iowa. Then in October, a felony charge of ongoing criminal conduct was filed against Tipton that initially encompassed lottery jackpot prizes won in three different states: the attempted claim here in Iowa; a jackpot claimed in 2005 in Colorado; and another in 2007 in Wisconsin. Another jackpot prize claim from 2011 in Oklahoma was incorporated into the criminal conduct charge in November, and in December, two jackpot claims from 2010 in Kansas also were added into the charge. Tipton also is charged with money laundering in the case.

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

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

From the beginning of this case, we here at the Iowa Lottery asked investigators to follow the evidence to help us get to the bottom of the situation. We absolutely believe we made the right decision in refusing to pay the prize until our security questions could be answered – and they never were. We have continued to give our support and assistance to law enforcement throughout the investigation and will continue to do so. The developments in the case have helped us make improvements to protect lotteries, our games, our players and the billions of dollars at stake for the worthy causes that lotteries benefit.

**IOWA LOTTERY AUTHORITY**  
**Statement of Revenues, Expenses and Changes in Net Position**  
**For the Eleven Months Ending Tuesday, May 31, 2016**

**Attachment A**

	Month ended 5/31/2016	Month ended 5/31/2015	Year-to-date 5/31/2016	Year-to-date 5/31/2015
<b>Operating revenues:</b>				
Instant-scratch ticket sales	\$20,758,858.00	\$18,438,340.00	\$214,636,651.00	\$195,100,035.00
Pick 3 sales	624,138.50	628,247.00	6,802,213.00	6,433,606.06
Powerball sales	4,975,110.00	3,813,134.00	71,029,510.50	49,308,610.00
Mega Millions Sales	1,655,480.00	1,955,779.00	13,686,749.00	16,642,771.00
Hot Lotto sales	640,944.00	1,038,888.00	8,110,185.00	10,138,277.00
Pick 4 sales	325,983.50	282,243.50	3,247,179.00	2,946,757.50
All or Nothing sales	296,650.00	356,339.00	3,712,165.00	4,200,347.00
Monopoly Millionaires' Club sales				591,605.00
Lucky for Life sales	639,438.00		2,594,180.00	
Pull-tab sales	1,211,555.49	1,251,797.19	13,880,784.67	14,671,660.33
Application fees	250.00	500.00	3,325.00	3,525.00
Other	8,330.48	412.75	32,721.82	5,790.13
Total operating revenues	<u>31,136,737.97</u>	<u>27,765,680.44</u>	<u>337,735,663.99</u>	<u>300,042,984.02</u>
<b>Operating expenses:</b>				
Scratch ticket	13,414,679.07	12,327,972.51	139,981,532.95	126,556,669.05
Pick 3	371,923.10	372,818.20	4,030,067.80	3,802,873.60
Powerball	2,397,241.00	1,871,781.00	34,851,975.00	24,011,800.50
Mega Millions	797,319.00	939,868.96	6,636,494.50	7,935,350.39
Hot Lotto	276,839.00	490,470.43	3,877,411.15	4,877,202.44
Pick 4	190,340.10	164,756.10	1,909,662.40	1,824,240.20
All or Nothing	175,891.54	207,278.47	2,198,522.50	2,486,885.01
Monopoly Millionaires' Club			(21,052.29)	668,442.74
Lucky for Life	380,039.05		1,759,284.17	
Pull-tab	757,856.75	780,298.02	8,680,397.17	9,170,550.06
VIP Club prize expense			155,754.29	240,810.90
Promotional	12,115.88	21,953.43	159,007.94	131,218.73
Advertising/publicity	667,331.55	620,383.11	6,242,708.51	6,186,608.07
Retailer compensation expense	2,032,260.39	1,795,648.71	21,844,629.25	19,347,263.51
Ticket expense	233,943.66	233,573.78	3,012,007.38	3,031,399.68
Vendor compensation expense	656,758.54	557,206.61	6,987,232.48	6,121,166.98
Online game expense				6,563.40
Salary and benefits	872,532.82	774,321.39	9,133,694.68	8,861,848.84
Travel	25,662.48	28,693.15	259,425.83	380,228.53
Supplies	14,355.36	13,103.08	119,835.71	126,231.86
Printing		59.99	1,031.40	5,990.93
Postage	273.90	254.63	6,279.07	5,353.00
Communications	12,655.29	12,237.75	143,415.12	199,136.18
Rentals	25,418.39	23,443.15	283,396.09	279,272.60
Utilities	3,938.87	4,705.18	72,661.12	116,974.75
Professional fees	6,811.43	21,447.86	83,224.60	159,366.74
Vending machine maintenance	50,390.76	48,486.61	548,570.77	530,524.23
Outside services and repairs	47,450.60	75,207.99	735,009.56	775,651.41
Data processing	9,856.47	9,637.84	112,533.66	96,116.20
Equipment	57,926.55	36,681.13	414,011.10	445,248.96
Reimbursement to other state agencies	51,204.48	54,531.48	391,921.07	389,611.84
Depreciation	29,242.76	25,590.05	305,921.73	255,485.75
Other	3,842.54	5,411.60	51,035.84	100,737.67
MUSL/Lotto administrative expense	10,112.05	10,329.47	117,422.32	96,179.25
Total operating expenses	<u>23,586,213.38</u>	<u>21,528,151.68</u>	<u>255,085,024.87</u>	<u>229,223,004.00</u>
Operating income	<u>7,550,524.59</u>	<u>6,237,528.76</u>	<u>82,650,639.12</u>	<u>70,819,980.02</u>
<b>Non-operating revenue (expenses):</b>				
Proceeds provided to State General Fund	(6,809,084.72)	(6,110,050.28)	(79,658,539.84)	(67,246,945.45)
Proceeds provided to Veteran's Trust Fund		(30,390.20)	(2,500,000.00)	(2,177,397.34)
Interest income	13,573.61	2,775.23	151,795.59	51,246.40
Interest expense		(645.28)		(7,369.57)
Gain (Loss) on disposal of capital assets		625.00	32,200.00	(364,251.59)
Net non-operating revenues (expenses)	<u>(6,795,511.11)</u>	<u>(6,137,685.53)</u>	<u>(81,974,544.25)</u>	<u>(69,744,717.55)</u>
Change in net position	755,013.48	99,843.23	676,094.87	1,075,262.47
Net position beginning of year	5,719,419.17	10,489,275.03	5,798,337.78	9,513,855.79
Net position end of year	<u>6,474,432.65</u>	<u>10,589,118.26</u>	<u>6,474,432.65</u>	<u>10,589,118.26</u>

# Budget for Lottery Fund

Attachment B

	FY 2014 ACTUAL	FY 2015 ACTUAL	FY 2016 BOARD APPROVED FINAL BUDGET	FY 2017 BOARD APPROVED PRELIMINARY BUDGET	FY 2017 BOARD APPROVED FINAL BUDGET
<u>Resources</u>					
Lottery sales	\$314,055,429	\$324,767,416	\$321,150,000	\$ 321,020,000	\$324,920,000
Interest income	\$ 51,716	\$ 76,038	\$ 500,000	\$ 500,000	\$ 500,000
Application fees	\$ 4,375	\$ 3,800	\$ 5,000	\$ 5,000	\$ 5,000
Other	\$ 99,932	\$ 6,220	\$ 5,000	\$ 5,000	\$ 5,000
<b>Total Resources</b>	<b>\$314,211,452</b>	<b>\$324,853,474</b>	<b>\$321,660,000</b>	<b>\$ 321,530,000</b>	<b>\$325,430,000</b>
<u>Expenses and Change in Net Assets</u>					
Prizes	\$186,948,985	\$196,882,288	\$190,207,767	\$ 189,611,640	\$193,151,514
Retailer compensation	\$ 20,131,428	\$ 20,977,399	\$ 20,586,201	\$ 20,735,345	\$ 20,987,254
Advertising production and media purchases	\$ 6,933,352	\$ 6,766,994	\$ 12,846,000	\$ 12,840,800	\$ 12,996,800
Retailer Lottery system/Terminal Communications	\$ 6,453,429	\$ 6,733,505	\$ 7,643,516	\$ 7,503,301	\$ 7,593,157
Instant/Pull-tab ticket expense	\$ 3,463,298	\$ 3,267,564	\$ 3,938,000	\$ 3,942,000	\$ 3,942,000
Vending machines & maintenance/Ticket dispensers	\$ 696,302	\$ 799,644	\$ 2,378,333	\$ 2,018,000	\$ 1,819,000
Courier delivery of instant tickets	\$ 322,729	\$ 572,194	\$ 710,000	\$ 660,000	\$ 660,000
Interest expense	\$ 12,622	\$ 8,046	\$ 3,805	\$ -	\$ -
Lottery operating expense	\$ 12,073,776	\$ 12,408,648	\$ 14,161,362	\$ 14,559,330	\$ 14,620,690
Building (purchase and sale)	\$ 3,432,016	\$ -	\$ -	\$ -	\$ -
Increase (decrease) in net assets	\$ (202,339)	\$ 1,920,125	\$ 25,400	\$ (85,000)	\$ (85,000)
<b>Total Expenses and Change in Net Assets</b>	<b>\$240,265,598</b>	<b>\$250,336,407</b>	<b>\$252,500,384</b>	<b>\$ 251,785,416</b>	<b>\$255,685,415</b>
<u>Proceeds</u>					
Proceeds Transfer to General Fund	\$ 72,141,420	\$ 72,365,900	\$ 66,659,616	\$ 67,544,584	\$ 67,244,585
Proceeds Transfer to Veterans Trust Fund	\$ 1,804,434	\$ 2,151,167	\$ 2,500,000	\$ 2,200,000	\$ 2,500,000
<b>Total Proceeds Transfers</b>	<b>\$ 73,945,854</b>	<b>\$ 74,517,067</b>	<b>\$ 69,159,616</b>	<b>\$ 69,744,584</b>	<b>\$ 69,744,585</b>
<b>Total Expenses and Proceeds</b>	<b>\$314,211,452</b>	<b>\$324,853,474</b>	<b>\$321,660,000</b>	<b>\$ 321,530,000</b>	<b>\$325,430,000</b>

Lottery Operations - Budget Detail

	<b>FY 2014 ACTUAL</b>	<b>FY 2015 ACTUAL</b>	<b>FY 2016 BOARD APPROVED FINAL BUDGET</b>	<b>FY 2017 BOARD APPROVED PRELIMINARY BUDGET</b>	<b>FY 2017 BOARD APPROVED FINAL BUDGET</b>
Administrative payroll*	\$ 9,461,004	\$ 9,565,122	\$ 10,965,362	\$ 11,443,330	\$ 11,302,592
Travel	\$ 400,279	\$ 410,225	\$ 495,000	\$ 435,000	\$ 435,000
Supplies	\$ 88,328	\$ 99,454	\$ 125,000	\$ 105,000	\$ 105,000
Printing	\$ 20,435	\$ 6,291	\$ 20,000	\$ 20,000	\$ 20,000
Postage	\$ 6,993	\$ 6,118	\$ 7,000	\$ 7,000	\$ 7,000
Communications	\$ 178,880	\$ 227,509	\$ 180,000	\$ 180,000	\$ 317,098
Rentals	\$ 307,286	\$ 308,922	\$ 320,000	\$ 320,000	\$ 320,000
Utilities	\$ 120,101	\$ 126,902	\$ 101,000	\$ 101,000	\$ 101,000
Professional fees	\$ 123,287	\$ 157,782	\$ 260,000	\$ 220,000	\$ 220,000
Outside services and repair	\$ 256,838	\$ 289,302	\$ 246,000	\$ 315,000	\$ 315,000
Data processing	\$ 89,573	\$ 105,400	\$ 90,000	\$ 110,000	\$ 125,000
Equipment	\$ 220,684	\$ 329,016	\$ 370,000	\$ 386,000	\$ 436,000
Reimbursement to state agencies	\$ 424,834	\$ 418,625	\$ 495,000	\$ 480,000	\$ 480,000
Depreciation	\$ 287,356	\$ 278,004	\$ 400,000	\$ 350,000	\$ 350,000
Other expenses	\$ 87,898	\$ 79,976	\$ 87,000	\$ 87,000	\$ 87,000
<b>Total operating expenses</b>	<b>\$ 12,073,776</b>	<b>\$ 12,408,648</b>	<b>\$ 14,161,362</b>	<b>\$ 14,559,330</b>	<b>\$ 14,620,690</b>

\* FY 2017 Proposed Final Budget for "Administrative Payroll" includes salary and benefit cost increases per DOM projections