

MINNESOTA DEPARTMENT OF PUBLIC SAFETY



06 - 0132



Introduction:

Type of Report: **2005 LOTTERY AUDIT REPORT**

Pages: 8

Submitted by: SA Jill Ahart

Case Number: 05000211

Synopsis:

The Alcohol and Gambling Enforcement Division conducted an annual security audit for the Minnesota State Lottery. SA Jill Ahart conducted the audit between May 18 and June 17, 2005.

Summary:

Between May 18 and June 17, 2005, SA Ahart and SA Cincotta of the Minnesota Alcohol and Gambling Enforcement Division conducted a review of the four Regional Lottery Offices located in Virginia, Detroit Lakes, Marshall, and Owatonna and the Lottery Headquarters in Roseville, Minnesota. This year's review primarily centered around the internal controls related to scratch-off tickets, including ticket inventory and the distribution and return of games between Lottery Headquarters and their Regional Offices and retailers.

The Lottery has multiple internal controls in place surrounding the distribution and return of games between Lottery Headquarters and their Regional Offices and retailers to help ensure the security of those games. It has been reported that the proper scanning practice is not being adhered to in all cases. This may make them vulnerable to fraudulent cashing efforts.

To also further protect the security of scratch ticket games, the Lottery may want to explore the idea of having Speedy Delivery and their drivers more directly accountable for the specific games they are transporting rather than for general packages. Also to further protect the security of the games, the Lottery may want to have a policy that their Regional Offices and retailers verify their deliveries of games against the bill of lading as soon as possible after they are delivered to verify they received their proper allocation.

It was reported the Lottery has an agreement with Speedy Delivery that allocations picked up in Roseville by Speedy Delivery are supposed to be delivered to their destinations within a specified period of time. Often times this is taking several extra days. The Lottery may want to research this matter further.

Conclusions:

The Minnesota State Lottery has several internal controls in place to ensure the integrity of scratch ticket games. These internal controls appear to be satisfactory and well adhered to in most cases. Only a few possible improvements have been noted.

Individual Lottery Headquarters and Regional Offices Audit Reports:

~~Minnesota State Lottery Regional Office - Detroit Lakes~~

1111 Highway 10 East

Detroit Lakes, Minnesota 56501

On May 18, 2005, a review of the Detroit Lakes Regional Office of the Minnesota State Lottery was conducted by SA Ahart at the request of the Minnesota State Lottery. The review was conducted with the assistance of Manager Jerry Ouren, Administrative Assistant Erica Germain, and Stores Clerk Roxanne Ramberg.

During the Fall of 2004, the Minnesota State Retirement System and the Teachers Retirement System began renting one quarter of the Lottery's office space due to budget cuts suffered by the Lottery. Certain building security measures were adjusted to accommodate this change. Additional physical security measures were also discussed. Ouren had no concerns to note about the Detroit Lakes Regional Office's physical security.

Ouren described the process and internal controls pertaining to the receiving and returning of scratch ticket Lottery games to/from Roseville Headquarters. The Detroit Lakes Regional Office receives new games from Roseville Lottery Headquarters on an established schedule. The office usually receives two or three new games at a time. The office knows which and how many new games are going to be delivered according to a notice they receive from Roseville. This list of games is determined by Roseville Headquarters. The new games are sent to the regional offices automatically. Each Regional Office receives the same new games. Once delivered, the new games become part of the Detroit Office's inventory because they are "assigned" to their office. The Detroit Regional Office no longer carries back up backs at their office as they previously did for theirs and local retailers' use.

When a new pack of games is delivered, it is accompanied by a bill of lading. When the games are signed for at the time of delivery, they are signed for as a package, not as the specific games listed on the bill of lading. The games the Detroit Lakes Office receives are automatically assigned to their office through the Lottery's computer system and can be tracked in that way. The games can also be tracked through Speedy Delivery's barcode system.

At the same time the new games are being put into play, the same number of games are taken out of play. Lottery Headquarters predetermines which games are to be closed and sent back to Roseville, which consist of the 2-3 oldest games. An exception to this practice would be if the top prize of a particular game had already been paid out somewhere in the state or if there was a popular game and there was little of the game remaining. In those cases, the games would be returned outside of the predetermined schedule.

The games that Roseville has directed to be sent back are processed according to set procedures and sent back to Roseville. Ouren noted that once the games go through the Altura (G-Tech) system, they can no longer be sold. The system now knows which numbers of tickets are left, and it will put out a flag if anyone would try to redeem any of these tickets. The system then prints out two confirmation-type tickets. One ticket is initialed by the person closing out the game and is kept with the office's paperwork. The second ticket is put in with the game(s) being sent back to Roseville. The games are then packaged and processed according to Speedy Delivery's policies and procedures. The package is tracked in transit through the use of barcodes. Games are picked up from the Detroit Lakes Regional Office by Speedy Delivery according to an established schedule.

Ouren stated there have never been any discrepancies in the game inventory at the Detroit Lakes Regional Office. Ouren was unaware of there ever being a theft of tickets/games while in transit or otherwise. Ouren was aware of a game(s) being delivered to the wrong retailer. Ouren added that those tickets could not be sold because they were not at the correct retailer location. Ouren stated that when there is an issue of lost or stolen tickets at the retailer level, the retailer contacts Lottery Security. Lost or stolen tickets are ultimately accounted for by Games Control at Roseville Headquarters.

The Detroit Lakes Regional Office has five sales representatives assigned to their office. The representatives come into the Detroit Lakes Office at a minimum of every other Tuesday. Half of the representatives come in on one Tuesday and the other half come in the following Tuesday. When the representatives come in to the office, they attend meetings and do their payroll and other computer work. Each representative has a take-home van equipped with various items they may need to supply to the Detroit Lakes Office's 480 retailers. These retailers include convenience stores, bars, restaurants, and grocery stores. They also carry various promotional items. The representatives never carry cash or games in their vans.

In addition to the above internal controls, the internal controls for cashing winning scratch tickets were also reviewed. These internal controls appear to be satisfactory and well adhered to. Ouren stated that retailers receive credit and also get 1% back for all ticket redemptions. Retailers do not get credit for cashing bad tickets.

Daily and monthly inventory and balancing procedures were also discussed. These procedures also appeared to be satisfactory and well adhered to.

Minnesota State Lottery Regional Office - Owatonna
205 Cedardale Drive SE
Owatonna, Minnesota 55060

On May 20, 2005, a review of the Owatonna Regional Office of the Minnesota State Lottery was conducted by SA Ahart and SA Cincotta at the request of the Minnesota State Lottery. The review was conducted with the assistance of Stores Clerk Julie Starkson and Secretary Jackie Rosendahl.

In late Fall of 2004, the Owatonna Regional Office became the new computer back-up site (disaster recovery site) for the Lottery. The former Eagan Regional Office was the previous computer back-up site for the Lottery until it closed due to budget cuts in Fall of 2003. Certain security improvements have been made to the Owatonna Regional Office to accommodate the computer back-up system. Other physical security measures were also discussed. Starkson and Rosendahl had no concerns to note about the Owatonna Regional Office's security.

Starkson and Rosendahl described the process and internal controls pertaining to the receiving and returning of scratch ticket Lottery games to/from Roseville Headquarters. Starkson and Rosendahl stated that Speedy Delivery comes to the Owatonna Regional Office on a relatively established schedule to drop items off from Roseville and pick up any items the office may have to send back to Roseville.

The Owatonna Regional Office receives new games from the Roseville Lottery Headquarters on an established schedule. The office usually receives two or three new games at a time. The office knows which and how many new games are going to be delivered according to a notice they receive from Roseville. This list of games is determined by Roseville Headquarters. The new games are sent to the regional offices automatically.

When a new pack of games is delivered, it is accompanied by a bill of lading. In addition, a Speedy Delivery barcode sticker is attached to the package before it is shipped from Roseville. The barcode has a record

associated with it that describes the specific games that are being shipped with the barcode. When the new games are signed for at the time of delivery, they are being signed for as a package, not as the specific games listed on the bill of lading.

At the same time the new games are being put into play, the same number of games are taken out of play. Lottery Headquarters predetermines which games are to be closed and sent back to Roseville. A list of these games is recorded on the same notice the office receives that says which new games they will be receiving. An exception to this practice would be if the top prize of a particular game was paid out somewhere in the state. When this happens, an email is sent out to the regional offices stating the top prize of the game was paid out and advises the office to close the game and send it back to Roseville immediately.

Under the usual circumstances, the games that Roseville has directed to be sent back via written notice are processed and sent back to Roseville on specified days. As part of the process, the G-Tech system prints out two confirmation-type tickets. One ticket is kept with the office's paperwork and the second is put with the game(s) being sent back to Roseville. The status of the games being returned is referred to as "not available to be cashed." The games are then packaged and processed according to Speedy Delivery policies and procedures. Speedy Delivery picks up packages from the Owatonna Regional Office according to a relatively established schedule. Packages are tracked in transit through the use of barcodes.

Starkson and Rosendahl were not aware of there ever being any discrepancies in the game inventory being sent between Roseville Headquarters and the Owatonna Regional Office. Starkson and Rosendahl were also unaware of there ever being a theft of tickets/games while in transit or otherwise. Starkson and Rosendahl were further unaware of how stolen tickets/games are accounted for. Starkson and Rosendahl did state that they were aware of tickets being previously cashed or stolen through retailers. Those tickets are listed by ticket and pack numbers on a weekly ticket report which is distributed statewide.

The Owatonna Office's region spans generally from the Mankato area to the Wisconsin border down to the Iowa border. The Owatonna Regional Office has four sales representatives assigned to their office. The representatives come in to the Owatonna Office approximately once a week to once every two weeks. Each representative has a take-home van equipped with various forms and other items they may need to supply to the Owatonna Office's 430-440 retailers. They also carry various promotional items. The representatives never carry cash or games in their vans.

Minnesota State Lottery Regional Office - Virginia
5463 17th Avenue West
Virginia, Minnesota 55792

On June 2, 2005, a review of the Virginia Regional Office of the Minnesota State Lottery was conducted by SA Ahart and SA Cincotta. The review was conducted with the assistance of Manager Greg Moir, Stores Clerk Edith Hoyum and Secretary Terri Holcomb.

Moir stated that there have been no recent changes to the office with regards to building security. Moir had no concerns to note about the Virginia Regional Office's security. Moir stated that there have been no changes in the Virginia Regional Office's internal controls regarding ticket inventory since last year.

Moir described the process and internal controls pertaining to the receiving and returning of scratch ticket Lottery games to/from Roseville Headquarters. The Virginia Regional Office receives new games from Roseville Lottery Headquarters on an established schedule. The office receives two or three new games at a time. The office knows which and how many new games are going to be delivered according to a notice they

receive from Roseville. This list of games is determined by Roseville Headquarters. The new games are sent to the regional offices automatically.

When a new pack of games is delivered, it is accompanied by a bill of lading. When the new games are signed for at the time of delivery, they are being signed for as a package, not as the specific games listed on the bill of lading. New games are put into play according to a specified schedule. At the same time the new games are being put into play, the same number of games are taken out of play. Lottery Headquarters predetermines which games are to be closed and sent back to Roseville.

The games that Roseville has directed to be sent back via written notice are processed according to set procedures and are sent back to Roseville on the day new games are put into play. Moir described the game return process on the G-Tech system. The system prints out two confirmation-type tickets; one ticket is kept with the office's paperwork and the second is put with the game(s) being sent back to Roseville via Speedy Delivery. The games are then packaged and processed according to Speedy Delivery's policies and procedures. The package is tracked in transit through the use of barcodes. Games are picked up from the Virginia Regional Office according to an established schedule.

Moir was not aware of there ever being any discrepancies in the game inventory being sent between Roseville Headquarters and the Virginia Regional Office. Moir did state that on approximately two occasions, they have had a discrepancy in their weekly balancing because tickets were sent back a day late due to a holiday or being short staffed, and they were not credited properly. These instances were merely temporary discrepancies and were quickly resolved.

Moir was unaware, during his fifteen years with the Minnesota State Lottery, of there ever being a theft of tickets/games while in transit or otherwise. Moir stated that there are occasionally instances where retailers have not wanded scratch off tickets as they should and cashed tickets that were "not at retail status." Games Control at the Roseville Lottery Headquarters handles these cases of ticket theft.

The Virginia Office's region spans generally from Koochiching in the north and down to Sauk Rapids, Big Lake, and Rush City towards the south. The Virginia Regional Office has four sales representatives assigned to their office. Each representative has a take-home van assigned to them. The representatives carry various promotional items to supply to the Virginia Office's 400 - 410 retailers. The Virginia Office's major sponsorship is the Bayfront Blues Festival held during the second week of August in Duluth. Moir stated that they have always sponsored that event but have not in the last one or two years due to the Lottery's reorganization. The Lottery will be sponsoring the festival again this year in 2005.

Minnesota State Lottery Regional Office - Marshall
750 West College Drive
Marshall, Minnesota 56258

On June 14, 2005, a review of the Marshall Regional Office of the Minnesota State Lottery was conducted by SA Ahart and SA Cincotta at the request of the Minnesota State Lottery. The review was conducted with the assistance of Store Clerk Ted De Rode. Manager Doug Landsman briefly assisted with the audit prior to its conclusion.

De Rode stated that there have been no recent changes to the office with regards to building security and access. De Rode stated that there has been a change since last year in the Marshall Regional Office's internal controls regarding ticket inventory. In prior years, the Marshall office would have extra packs of games on hand for their

own use or to distribute to area retailers who had run out of tickets. The Marshall Office no longer has extra packs of games on hand for themselves or for area retailers.

De Rode described the process and internal controls pertaining to the receiving and returning of scratch ticket Lottery games to/from Roseville Headquarters. De Rode stated that Speedy Delivery comes to the Marshall Regional Office to drop items off and pick items up on a relatively established schedule. New games are delivered and put into play based on an established schedule.

The office receives two or three new games at a time. The office knows which and how many new games are going to be delivered according to a notice they receive from Roseville. This list of games is determined by Roseville Headquarters. The new games are sent to the regional offices automatically.

When a new pack of games comes in, they are accompanied by a bill of lading. When the new games are signed for at the time of delivery, they are being signed for as a package, not as the specific games listed on the bill of lading.

At the same time the new games are being put into play, the same number of games are taken out of play. Lottery Headquarters predetermines which games are to be closed and sent back to Roseville. The games that are to be returned are processed according to set procedures and sent back to Roseville. De Rode described the game return process on the G-Tech system. The system prints out two confirmation-type tickets; one ticket is stapled to the activation/settlement card and is kept at the office and the second is put with the game(s) being sent back to Roseville via Speedy Delivery. The games are then packaged and processed according to Speedy Delivery's policies and procedures. Packages are tracked in transit through the use of barcodes.

De Rode was not aware of there ever being any discrepancies in the game inventory being sent between the Roseville Headquarters and the Marshall Regional Office. De Rode was unaware of there ever being a theft of tickets/games while in transit or otherwise. Landsman stated that there are occasionally instances where retailers have not wanded scratch off tickets as they should and cashed tickets that had already been cashed. Landsman stated that they recommend to their retailers that they scan every ticket they cash. Landsman stated that retailers have always had a scanner to check tickets since the Lottery began. The original scanners were called Zipcash and operated via a dial-up modem.

The Marshall Regional Office has four sales representatives assigned to their office. Each representative has a take-home van assigned to them. The representatives carry various promotional items in their vans. Landsman noted that the representatives never have promotional items in their vans more than a couple of days, as they pick them up from the Marshall Regional Office on Tuesdays and distribute them to retailers in the next day or two. Representatives never carry cash or games in their vans.

The Marshall Regional Office does an annual promotion with a Hutchinson radio station called KDUZ. The promotion consists of listeners calling in to answer trivia questions to win approximately 15 – 20 scratch-off tickets. The promotion is a ticket trade out where the radio station gives the Lottery x-amount of air time and the Lottery gives the radio station x-amount of scratch-off tickets. This kind of promotion is negotiated by various Lottery personnel, reviewed by the Lottery's legal counsel, Dale McDonnell, and is given final approval by the Lottery Director, Clint Harris.

The Marshall Office used to sponsor a music festival in Winstead, Minnesota called Winstock. Landsman stated that this was the third year the Lottery has not sponsored that event due to the Catholic Church associated with it and their conservative views regarding the Lottery and gambling.

Minnesota State Lottery Headquarters - Roseville
2645 Long Lake Road
Roseville, Minnesota 55113

On June 17, 2005, a review of the Minnesota State Lottery Office Headquarters in Roseville was conducted by SA Ahart at the request of the Minnesota State Lottery. The review was conducted with the assistance of Investigator Andy Gohl and Warehouse Manager Mike Haffley.

Since June of 2004, G-Tech has moved back to the Lottery Office building. G-Tech previously officed out of the Lottery Office but later moved to a nearby Roseville location. G-Tech moved back to improve the efficiency of their working relationship with the Lottery. G-Tech now leases space from the Lottery on the second floor of the building. Haffley stated that there were various physical security adjustments made to the building to accommodate G-Tech's presence in the building. G-Tech has public access at the opposite, west end of the building so that the public can get to G-Tech directly from the outside rather than being escorted through the Lottery portion of the building.

Investigator Gohl stated that there are no concerns regarding physical building security at Roseville Headquarters. Gohl stated that there have been no known changes to the internal controls regarding ticket inventory.

Haffley explained the majority of the process and internal controls pertaining to the distribution and return of scratch ticket Lottery games to/from Roseville Headquarters. Haffley stated that the Lottery Regional Offices are treated just like any other retailer in that they, too, receive "an allocation" of games according to an established schedule just like all the other 3100 retailers in the state. Haffley stated that retailers are capable of carrying 12 or 20 games at a time, which include a mix of games. Haffley stated that it is his supervisor, Don Masterson, and the Lottery's marketing department that determine which six games are to be considered mandatory games at any given time and must be in play at all retailer locations.

Haffley stated that Speedy Delivery comes to Roseville Headquarters periodically to pick-up and deliver various miscellaneous items. A separate Speedy Delivery semi-truck comes to Roseville Headquarters to pick-up allocations which, again, occurs according to an established schedule and are for all Lottery retailers statewide. Per the Lottery's agreement with Speedy Delivery, the allocations are expected to be delivered to each retailer statewide within a specified period of time. All other deliveries are expected to be delivered within 24 hours.

There are various safety features in place with regards to the scratch ticket games that help to ensure their security is not compromised. These safety features were discussed with Haffley and also representatives from the various Regional Offices.

The process involved with retailers sending games back to Roseville Headquarters was also discussed with Haffley. This process includes the retailers' G-Tech system "talking" to the Lottery System and essentially coordinating the return of the games with Speedy Delivery. Like the Lottery works in terms of the Lottery System and games, Speedy Delivery works in terms of packages and the packages' bar codes.

When the games are returned back to Roseville Headquarters via Speedy Delivery, they are entered into the Lottery System. They are then inspected and processed by Haffley's staff who consist of Store Clerks. If there is any issue regarding a returned game, the game is put aside for Games Control to review so that the issue can be resolved. Haffley stated that out of the 3100 Lottery retailers that send 2-3 games back to Roseville Headquarters at any given time during an established schedule, approximately 100 of those returned games have issues.

Game shipments are tracked in various ways. Haffley stated that whenever there are actual discrepancies in game inventory being sent between retailers and Roseville Headquarters, Games Control resolves those discrepancies. When there is a case of lost or stolen games/tickets, the tickets are put into lost or stolen status and Games Control generates a report for Lottery Security to investigate the matter. Gohl stated that it is decided on a case by case basis as to whether the retailer or Lottery Headquarters will assume responsibility for the lost or stolen tickets and the losses associated with those tickets. Gohl stated that the Lottery does keep a database of lost or stolen tickets.

The Roseville Office has thirteen sales representatives assigned to their seven county metro area. The representatives come in to the Roseville Office once a week, half of the representatives come in on one day and the other half come in on another day. Each representative has a take-home van equipped with various forms and other items they may need to supply to the seven county metro area's 1700 retailers. They also carry various promotional items. The representatives never carry cash or games in their vans.