D.C. Lottery Needs Standard Procedures to Improve Operations

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A report by the Office of the District of Columbia Auditor

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## Table of Contents

Executive Summary .......................................................................................................................... 1
Background ................................................................................................................................. 2
Objectives, Scope, and Methodology ............................................................................................ 4
Audit Results .............................................................................................................................. 5
Conclusion ................................................................................................................................. 10
Agency Comments .................................................................................................................... 11
ODCA Response to Agency Comments ...................................................................................... 20
Summary of Report Recommendations .......................................................................................... 21
Executive Summary

Why ODCA Did this Audit
D.C. Official Code § 36–601.19 requires the Auditor of the District of Columbia (ODCA) to conduct an audit of all accounts and transactions of lottery games, daily numbers games, and sports wagering.¹

What ODCA Found
We found the Office of Lottery and Gaming (OLG) generally accomplishes its mission of providing revenue-generating entertainment through the sale of D.C. Lottery (Lottery) products. ODCA nevertheless noted the absence of relevant policies and procedures to govern key processes such as collecting funds from retailers following a failed revenue transfer, timely recording of instant tickets in OLG’s central gaming system oversight of the services provided by Intralot, and the communication of licensing requirements to potential retailers. ODCA also found that OLG decided not to penalize retailers that failed to transfer revenue from the sale of Lottery products as required by the OLG Non-Sufficient Funds (NSF) policy.

What ODCA Recommends
ODCA recommends that OLG expand its standard operating procedures (SOPs) to cover key processes summarized below. This includes revising internal SOPs to ensure OLG’s mission is carried out in accordance with OLG policy. Strengthening SOPs to ensure OLG directives are carried out in a timely manner will lead to improved efficiency and consistent application of policy. Specifically, our recommendations include:

- OLG should reevaluate their NSF policy to ensure retailers face monetary penalties for reoccurring NSFs.
- OLG should develop standard operating procedures for when payment is not provided during the weekly electronic funds transfer sweep, which should include acceptable methods of payment.
- OLG should develop, implement, and monitor adherence to an official policy regarding oversight of the revenue reconciliation process. This policy should include a requirement for OLG to review and approve corrective actions taken, as identified within the incident reports.
- OLG should develop SOPs for the timely recording of instant tickets in the BOS.
- OLG should establish and communicate uniform licensing requirements for prospective Lottery retailers.

¹ D.C. Code § 36–601.19. Audit requires ODCA to conduct a “regular post audit of all accounts and transactions of the Chief Financial Officer with respect to the operation of lottery [games], daily numbers games, and sports wagering.”
Background

The District of Columbia Lottery and Gaming Control Board was established as the Office of Lottery and Gaming, a subordinate office within the Office of the Chief Financial Officer (OCFO). The OCFO is charged with overseeing OLG operations, including hiring of personnel to carry out the mission of the Lottery.²

The Lottery’s mission is to provide revenue-generating entertainment through the sale of innovative lottery products and promotions to directly benefit the residents and the economic vitality of the District of Columbia. The primary source of revenue earned by the Lottery is the sale of instant tickets and online gameplay. While the Lottery earns revenue from dividends and interest income, penalties assessed on delinquent agents’ accounts, and charitable gaming fees, the main sources of revenue are terminal and instant ticket games.

Revenue earned through the sale of Lottery products and promotions are deposited in the District of Columbia Lottery, Charitable Games, and Sports Wagering Fund, an enterprise fund administered by the OCFO. This revenue is used to pay for the operation, administration, and capital expenses of the Lottery. Payment of prizes to Lottery winners are also paid from this fund. The remaining amount is then transferred to the D.C. General Fund.³

OLG transferred $45.6 million to the General Fund during Fiscal Year (FY) 2017 through the sale of Lottery products. Although FY 2018 saw a decrease in operating revenue, OLG was able to increase the General Transfer to $49.5 million due to a decrease in prizes awarded. OLG’s contribution to the General Fund declined by 9% to $45 million in FY 2019. This decrease was mostly attributed to increased prize payouts during the fiscal year.

![Figure 1: Summary of D.C. Lottery Revenues and Expenses](image)

<table>
<thead>
<tr>
<th></th>
<th>FY17</th>
<th>FY18</th>
<th>FY19</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Operating Revenues</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Instant Games</td>
<td>$50,318</td>
<td>$49,493</td>
<td>$52,335</td>
</tr>
<tr>
<td>Terminal Games</td>
<td>168,391</td>
<td>160,766</td>
<td>160,727</td>
</tr>
<tr>
<td>License and Permit Fees</td>
<td>23</td>
<td>5</td>
<td>10</td>
</tr>
<tr>
<td><strong>Total Operating Revenues</strong></td>
<td>218,732</td>
<td>210,264</td>
<td>213,072</td>
</tr>
</tbody>
</table>

² D.C. Code § 36–601.01 states “all of the powers, duties, functions, and personnel of the Board are transferred to the Office of the Chief Financial Officer (OCFO) and the D.C. Lottery became a subordinate office within the OCFO.”
³ D.C. Code § 36–601.12 mandates “any monies of the Office, from whatever source derived (including gifts to the Office), shall be for the sole use of the Fund and shall be deposited as soon as practicable in the Fund and shall be disbursed from the Fund...”
## Operating Expenses

<table>
<thead>
<tr>
<th></th>
<th>FY17</th>
<th>FY18</th>
<th>FY19</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prizes</td>
<td>130,035</td>
<td>117,365</td>
<td>123,375</td>
</tr>
<tr>
<td>Agent Commissions</td>
<td>14,409</td>
<td>13,766</td>
<td>13,860</td>
</tr>
<tr>
<td>Other*</td>
<td>28,797</td>
<td>30,266</td>
<td>31,219</td>
</tr>
<tr>
<td>Total Operating Expenses</td>
<td>173,241</td>
<td>161,397</td>
<td>168,454</td>
</tr>
<tr>
<td>Operating Income</td>
<td>45,491</td>
<td>48,867</td>
<td>44,618</td>
</tr>
<tr>
<td>Interest and Dividend Income</td>
<td>192</td>
<td>253</td>
<td>467</td>
</tr>
<tr>
<td>Other Income</td>
<td>-</td>
<td>443</td>
<td>-</td>
</tr>
<tr>
<td>Net Income Before Transfers</td>
<td>45,683</td>
<td>49,563</td>
<td>45,085</td>
</tr>
</tbody>
</table>

## Transfers

| Transfer to General Fund | (45,600) | (49,500) | (45,050) |

Source: OLG Statement of Revenues, Expenses and changes in Net Position

*Other Operating Expenses include contractor fees, advertising, salaries, professional fees, contractual services, administration, and depreciation.

OLG’s annual contribution to the General Fund is used to promote the District’s economy and benefit the residents of the District of Columbia. The General Fund supports essential services such as education, recreation and parks, public safety, housing, and senior and child services.

In an effort to generate additional revenue, the District enacted the Sports Wagering Lottery Amendment Act of 2018. The Act, which went into effect on May 3, 2019, authorized licensed and regulated sports wagering in the District of Columbia.\(^5\)

Participating local businesses benefit from commissions earned through the sale of Lottery gaming products. Commission rates are established by OLG based on the selling and cashing of Lottery products. Transactions from the sale of Lottery tickets are captured by OLG’s central gaming system Back-Office System (BOS). The BOS provides administrative and reporting functionality such as retailer sales activity reports, game liability, and retailer invoicing reports. OLG contracted with the international gambling vendor Intralot to oversee the design, development, production, and operation of BOS systems, equipment, and services.

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\(^5\) D.C. Law 22-312, the Sports Wagering Lottery Amendment Act of 2018 authorizes sports wagering in the District of Columbia.
Objective, Scope, and Methodology

Objective
ODCA’s objective was to determine whether proceeds received from the sale of online and instant Lottery tickets, as administered by OLG, are appropriately accounted for and disbursed as mandated by law, and to conduct a review of key internal controls to determine the efficiency and effectiveness of operations in maximizing revenue to improve the economic vitality of the District.

Scope
The scope for this report was Fiscal Year 2018 through June 2019.

Methodology
To conduct this audit, ODCA reviewed D.C. Code and District Municipal Regulations, interviewed key DC Lottery personnel, arranged process walk-throughs, and analyzed documentation provided by OLG. ODCA analyzed the following processes:

- The receipt of funds from licensed lottery retailers.
- The transfer of lottery revenue to the D.C. General Fund.
- The safeguarding and recording of instant tickets.
- The retailer licensure process.

Specifically, OLG provided ODCA with documentation to support revenue generated through the sale of Lottery products. This included Retailer Activity Sales Summary Reports, periodic bank statements, and the General Fund Transfer Analysis developed to assist with the accurate transfer of Lottery revenue to the General Fund. ODCA also reviewed OLG’s process of collecting funds from retailers in compliance with OLG’s Non-Sufficient Funds (NSF) Policy. Documentation such as internally generated NSF reports, and corresponding NSF notifications were provided in support.

In addition, ODCA reviewed OLG procedures for safeguarding and recording of instant tickets. In addition to conducting interviews, ODCA requested OLG invoices for the purchase of instant tickets, related shipping manifests and relevant SOAR reports to show the recording of instant tickets within the System of Accounting and Reporting (SOAR), the District’s financial management system.

Finally, ODCA reviewed publicly available information published on OLG’s website. Critical information such as prior year financial statements and licensing requirements were reviewed in conjunction with evidence provided by OLG.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.
Audit Results

Overall, ODCA found that OLG accomplishes its mission of providing revenue-generating entertainment through the sale of Lottery products. ODCA nevertheless noted a lack of policies and procedures in place to govern key processes.

OLG did not enforce a 5% penalty for late payment of revenue generated through Lottery gameplay.

OLG withdraws revenue generated through the sale of Lottery gaming from retailers through a weekly electronic funds transfer. Participating retailers are required to hold in trust all monies received by the agent from the sale of Lottery and daily numbers games tickets until such monies are transferred to OLG.6

In cases where licensed retailers fail to deposit funds owed to the Lottery for the period, a non-sufficient funds (NSF) event occurs, and OLG is notified. A retailer’s online terminals may be deactivated in the event of an NSF in addition to OLG placing a phone call to the retailer regarding the delinquency.

The OLG Financial Division Non-Sufficient Funds Standard Operating Procedures state the following:

- “Upon receipt of a second NSF notification within a 12-month cycle from DCLB’s banking institution...the agent may be assessed a penalty of 5% on the amount due...”
- “Upon receipt of a third NSF notification within a 12-month cycle from DCLB’s banking institution; the Retailer’s terminal may be deactivated immediately. A 5% penalty, not to exceed $1,000, on the amount due may be imposed, and a recommendation may be sent to the Executive Director requesting the Retailer’s license be suspended for one week...”
- “Upon receipt of a fourth NSF notification within a 12-month cycle from DCLB’s banking institution may result in an immediate deactivation of the on-line terminal, a 5% penalty, not to exceed $1,000, on the amount due and license revocation.”

ODCA found that 73 independent retailers failed to have sufficient funds in their bank account prior to the weekly funds sweep, resulting in 129 NSFs during the audit period. Of the 73 retailers that were issued NSF’s, 32 received a second NSF and were therefore subject to the 5% penalty per OLG’s NSF policy outlined above.

In addition, ODCA found that 7 of the 73 retailers were issued between 4 and 8 NSFs within a 12-month cycle. As stated by the NSF Policy, retailers’ online terminals are eligible for immediate deactivation, in addition to enforcement of the 5% penalty, and license revocation following the 4th NSF occurrence.

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6 See § 36–601.16(b).
ODCA conducted a detailed review of 23 retailers that were issued a NSF during the audit period. A review of that sample revealed:

- None (0) of the retailers were assessed the 5% penalty.
- All (23) retailers were deactivated upon notification of an NSF.
- All 7 of the retailers eligible for license revocation had their licenses revoked.

OLG experienced a downturn in revenue earned from the sale of Lottery products between FY 2017 and FY 2018. Increased competition led OLG management to consider the consequences of penalizing licensed agents for non-compliance. OLG management concluded that enforcement of the NSF 5% penalty would further discourage retailers from continuing to sell Lottery products. As a result, OLG management decided not to penalize retailers for NSFs.

However, failure to fully enforce the NSF policy has itself led to a loss of additional revenue. Approximately $13,075 in revenue was not collected as a result of OLG’s decision to not enforce the 5% penalty.

**Recommendation**

1. OLG should reevaluate their NSF policy to ensure retailers face monetary penalties for reoccurring NSFs.

**OLG allowed retailers to deposit outstanding funds owed via in-branch deposit.**

The D.C. Lottery Non-Sufficient Funds Notification Policy states:

> “Upon receipt of the first non-sufficient fund notification... the agent’s on-line terminal will be deactivated ... upon receipt of a certified or cashier check of payment in full, the agent’s terminal will be reactivated.”

ODCA reviewed controls surrounding OLG’s process of collecting Lottery revenue from licensed retailers that failed to provide timely payments to OLG. ODCA’s review uncovered OLG’s practice of allowing retailers to make in-branch deposits for the amount(s) due to OLG as a result of an NSF. We found that 16 of the 23 retailers reviewed had OLG’s bank account information and made in-branch bank deposits to OLG’s bank account.

OLG was unable to provide standard operating procedures regulating the process of collecting and recording payments when retailers receive NSF notifications. The only official document outlining acceptable forms of payment is the Non-Sufficient Funds Notification Policy in the retailer agreement which is signed by retailers during the Lottery licensure process.

Collecting funds owed to OLG is an essential operation for OLG. Formal standard operating procedures are needed to reduce exposure to fraud and to ensure that only acceptable forms of payment are received. By divulging sensitive information, OLG could be susceptible to fraudulent activity, therefore adequate controls over this process are necessary to safeguard OLG’s assets.
Recommendation

2. OLG should develop standard operating procedures for when payment is not provided during the weekly electronic funds transfer sweep, which should include acceptable methods of payment.

OLG management failed to adequately oversee the process of resolving revenue discrepancies.

OLG is required to maintain full and complete records of the conduct and operation of daily numbers games and lotteries and the records are required to include a statement of revenues.

Revenue earned through the sale of Lottery products is verified by the Internal Control System (ICS), administered by Elsym. ICS verifies pertinent retailer information including revenue earned during the period. Imbalances between ICS and the BOS are flagged for review and resolved by personnel from Elsym (ICS) and Intralot (BOS).

Revenue discrepancies that are not resolved in a timely manner are documented within incident reports. OLG incident reports include brief descriptions of the incident that caused the revenue discrepancies between the ICS and BOS systems. The root cause, as well as corrective and preventative action(s) taken to address revenue discrepancies, are also listed within this report.

OLG was unable to provide evidence of their oversight of the revenue reconciliation process. Incident reports constructed by Intralot to identify the root cause of any revenue imbalances were not reviewed and approved by OLG management.

In addition, ODCA’s review of 10 incident reports revealed three incidents in which Intralot was unable to determine the root cause of the revenue imbalance. OLG was unable to provide evidence of the corrective action taken to resolve the underlying issue causing the identified imbalance. These issues remained outstanding at the end of our review period.

A lack of established policies and procedures contributes to OLG’s failure to oversee Intralot (BOS) and Elsym (ICS) during the revenue reconciliation process. Management oversight is a critical part of OLG operations. This includes oversight of the services provided by Intralot such as the resolution of technical issues within the BOS.

Failure to identify and correct the root causes identified within sample incident reports increases the likelihood of recurring revenue imbalances. Additionally, failing to correct issues in a timely manner forces OLG to bypass key system controls. Override of controls by management is counterproductive to the controls established to prevent inaccurate reporting of revenue. Failure to oversee the revenue reconciliation process affects the reporting of revenue earned through the sale of Lottery games.

7 The Internal Control System (ICS) is a “back-end system” managed by Elsym. BOS revenue reports are reconciled with ICS revenue reports to validate accuracy of data. The 777 Out of Balance Report is generated as a result of this reconciliation, imbalances identified are flagged for review and resolution.
Recommendation

3. OLG should develop, implement, and monitor adherence to an official policy regarding oversight of the revenue reconciliation process. This policy should include a requirement for OLG to review and approve corrective actions taken, as identified within the incident reports.

Instant tickets are not promptly recorded in the Back-Office System (BOS) upon receipt from suppliers.

The U.S. Government Accountability Office (GAO) Executive Guide in Best Practices in Achieving Consistent, Accurate Physical Counts of Inventory and Related Property states that “managing the acquisition, production, storage, and distribution of inventory is critical to controlling cost, operational efficiency, and mission readiness.” It also states that “proper inventory accountability requires that detailed records of produced or acquired inventory be maintained, and that this inventory be properly reported in the entity’s financial management records and reports.”

OLG purchases Lottery instant tickets from various suppliers. Once tickets are purchased, they are transported to the OLG office where OLG verifies receipt of the order and stores the tickets in the warehouse until purchased by retailers.

ODCA reviewed a sample of 10 instant ticket purchases and found:

- In one case, the instant tickets were uploaded into BOS on the same day the instant tickets were received by OLG from the supplier.
- In eight cases, instant tickets were not uploaded promptly into BOS; it took OLG three to 14 days to upload them in BOS upon receipt from suppliers.
- In one case, ODCA found the instant tickets were uploaded into BOS two days prior to OLG’s receipt of the instant tickets.

While the sample of instant tickets reviewed by ODCA have no financial value until delivered to licensed retailers and activated in the BOS, the total cost to generate the sample of tickets reviewed totaled $486,552.

Per OLG staff, it is not critical for ticket inventory to be immediately recorded in the BOS upon receipt from suppliers. Instead, recording of instant tickets into the system is prompted by the launch dates of Lottery games. ODCA found that for the 10 samples reviewed, the number of days between entry dates into the BOS and launch dates ranged from two to 15 days.

OLG lacks SOPs surrounding the process of receiving and recording instant tickets into BOS. The lack of these guidelines and failure to record instant tickets in a timely manner may increase the risk of undetected theft and lead to a loss of inventory.

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9 Ibid.
Recommendation

4. OLG should develop SOPs for the timely recording of instant tickets in the BOS.

OLG publishes conflicting Licensing Requirements which makes it unclear what documentation is required to obtain a retailer license.

The Government Accountability Office’s Standards for Internal Control in the Federal Government sets the standards for an effective internal control system for federal agencies, which may also be adopted by state and local government entities. An effective internal control system helps an entity adapt to shifting environments, evolving demands, changing risks, and new priorities. Internal control comprises the plans, methods, policies, and procedures used to fulfill the mission, strategic plan, goals, and objectives of the entity. Policies and procedures provide direction to employees and customers and set standards for an entity’s operation, and they work well if consistent and are effectively communicated.

The requirements to obtain a Lottery retailer license in the District are documented on the OLG official website, in OLG SOPs entitled Processing New Applications, and in internal New Agent Application Control Sheets that are used by OLG staff when processing applications.

ODCA’s review of these sources revealed conflicting requirements for obtaining a retailer license. In fact, ODCA found OLG utilized three different versions of the New Agent Application Control Sheet simultaneously to review and approve license applications. ODCA noted OLG’s oversight of the conflicting licensure requirements published. As changes were made to licensure requirements and as new checklists were developed, previous versions of the checklist were still used by OLG staff during the application review process.

The use of inconsistent criteria to gauge the qualifications of retailer applicants may cause licenses to be granted to unqualified retailers. Inconsistent criteria could also cause confusion among license applicants and OLG staff and hamper the licensing application process. Further, requiring applicants to provide additional, unnecessary documentation may lead to prolonged licensing application processing times.

Recommendation

5. OLG should establish and communicate uniform licensing requirements for prospective Lottery retailers.
Conclusion

Overall ODCA determined that proceeds received from the sale of online and Lottery instant tickets, as administered by OLG, are appropriately accounted for and disbursed as mandated by law. Despite this, ODCA noted a lack of relevant policies and procedures to govern key processes such as collecting funds from retailers following a failed revenue transfer, timely recording of instant tickets in OLG’s central gaming system (BOS), oversight of Intralot’s management of the BOS, and the communication of licensing requirements. ODCA also noted OLG’s decision to not penalize retailers that do not transfer revenue from the sale of Lottery products in accordance with the NSF policy.
Agency Comments

On February 4, 2021, we sent a draft copy of this report to the Office of Lottery and Gaming (OLG) for review and written comment. OLG responded with comments on February 19, 2021. Agency comments are included here in their entirety, followed by ODCA's response.
Finding #1 – OLG did not enforce a 5% penalty for late payment of revenue generated through Lottery gameplay.

Recommendation:

OLG should reevaluate their NSF policy to ensure retailers face monetary penalties for reoccurring NSFs.

Management Response:

The Lottery does not concur with the finding.

The Lottery has reviewed this issue on several occasions and has concluded that implementing a fee for NSFs is not currently in the best business interest of the District and Lottery.

D.C. Official Code § 36-601.21(a) provides the Lottery with the authority to impose a fine of not more than $1,000 for any violation of its rules and regulations. In implementing its statutory authority, the Lottery promulgated 30 DCMR § 305.10, which states the following: “The Agency may assess a monetary penalty not to exceed one thousand dollars ($1,000) for failure to comply with the requirements of this section.”

The regulation does not require the assessment of monetary penalties in all cases, but rather provides the Lottery with the discretion to assess monetary penalties where appropriate.

The Lottery has considered the following factors in making the decision not to impose monetary penalties in all cases:

- The Lottery has averaged revenue exceeding $216 million over the past five years and has amassed over $1 billion dollars in revenue during that same period. In FY 2019, the Lottery had a total of 63 retailer NSFs, all of which were paid. The Lottery believes that

1 Section 305.10 requires that lottery sales agents have sufficient funds available to be transferred to the Lottery on a weekly basis.
not imposing an additional financial burden upon retailers contributed to the NSF collection rate of 100% and collection within a maximum of 45 days in FY 2019. A significant majority (67%) of NSFs were paid to the Lottery within 24 hours. See Table 1 for a complete breakdown.

Table 1 – FY 2019 NSFs

<table>
<thead>
<tr>
<th>NSF Paid</th>
<th>NSF Quantity</th>
<th>Paid %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Same Day</td>
<td>32</td>
<td>50.79%</td>
</tr>
<tr>
<td>Next Day</td>
<td>10</td>
<td>15.87%</td>
</tr>
<tr>
<td>Within 24 hours</td>
<td>42</td>
<td>66.67%</td>
</tr>
<tr>
<td>2 - 10 Days</td>
<td>13</td>
<td>20.63%</td>
</tr>
<tr>
<td>11 - 19 Days</td>
<td>3</td>
<td>4.76%</td>
</tr>
<tr>
<td>20 - 44 Days</td>
<td>5</td>
<td>7.94%</td>
</tr>
<tr>
<td>Within 45 Days</td>
<td>21</td>
<td>33.33%</td>
</tr>
<tr>
<td>Total</td>
<td>63</td>
<td>100.00%</td>
</tr>
</tbody>
</table>

- The Lottery believes that adding an additional financial burden on its retailers does not deter the occurrences, as experienced in the past, nor does it increase the promptness of payment. The primary goal when an NSF occurs is to collect the funds within 24 hours, and a fee assessment may have the undesired consequence of hindering that result and possibly further prolonging receipt of that payment while not yielding any material benefit.

- The Lottery has continually faced challenges with increasing revenue, increasing its retailer base and increased competition from lotteries and casinos in surrounding jurisdictions. The Lottery’s retailer partners play a significant role in helping to thwart these challenges. The Lottery believes adding an additional financial barrier (fees for NSFs usually paid within 24 hours) does not assist with retaining or increasing the retailer base.

Finally, the Lottery has a tiered NSF policy that increases the consequence for non-compliant retailers beginning with their third NSF. After the third NSF, retailers are required to attend an administrative hearing to explain the NSFs, and are subsequently required to provide a security deposit, a bond, or overdraft protection in order to remain a retailer. If a retailer incurs four NSFs within a 12-month period, their license is revoked.

Finding #2 - OLG allowed retailers to deposit outstanding funds owed via in-branch deposit.

Recommendation:

OLG should develop standard operating procedures for when payment is not provided during the weekly electronic funds transfer sweep, which should include acceptable methods of payment.
Management Response:

The Lottery does not concur with the finding.

The Lottery had revenue that exceeded $213 million dollars in FY 2019 and a collection rate of 100% of funds due. In accordance with 30 DCMR § 305.02, the Lottery collects funds owed by retailers for lottery ticket sales on a weekly basis through Electronic Funds Transfers (weekly sweeps) from retailers’ bank accounts. When a retailer does not have the full balance owed to the Lottery at the time their bank account is swept for ticket sales, they incur a Non-Sufficient Funds (NSF) and their lottery terminal is disabled. When an NSF occurs, the Lottery’s primary goal is to collect the funds owed within 24 hours, and in the applicable situations, get the retailer’s terminal reactivated in order for them to continue selling lottery products and generating revenue for the District. The Lottery allows for retailers to make payment for their NSF by either bringing a certified cashier’s check to Lottery headquarters or by making a cash deposit for the amount owed directly into the Lottery’s bank account.

OLG believes creating a formal procedure that does not parallel 30 DCMR § 305.02 is not appropriate. However, we realize NSFs may occur and we informally address the collection methods with the retailers in their orientation, and more specifically when they have an occurrence.

Following is the Lottery’s rationale for allowing retailers to make cash deposits for NSFs directly into its bank account:

1. **Requiring payments be made at the Lottery’s headquarters would create an unnecessary burden on small business owners in the District.** The Lottery’s retailer base is primarily made up of small business owners that spend a significant amount of time in their stores running their business. Finding the time to leave their stores, retrieve a cashier’s check, and then deliver it to Lottery headquarters during business hours can be challenging in respect to their time and prompt payment of their NSF. Retailers have often expressed the limited time they have to leave their locations. Allowing retailers to make payment for deficient funds owed to the Lottery is the most expedient option for the Lottery to receive NSF funds, and for the retailer to have terminal reactivated so that they may continue selling lottery tickets on behalf of the District and their business.

2. **Providing the option to allow retailers that have incurred an NSF to make payments at Wells Fargo Bank locations is a reasonable option to collect funds owed to the District.** The Lottery has more than 400 retailers located throughout the District; however, Lottery headquarters is located in the Southeast quadrant of the city. Leaving their businesses during working hours and traveling to Lottery headquarters can present challenges for a great number of our small business retailers. There are 34 Wells Fargo bank branches in the District that provide our retailers the flexibility, convenience, and efficiency to make their NSF payments promptly by depositing directly into the Lottery’s bank account.
3. **Providing information to Retailers to make Payment into the Lottery’s bank account does not create additional risk.** The Lottery has paid more than $615 million dollars in prizes over the past five years and has issued thousands of checks to prize winners during that time period. The Lottery checks contain standard information found on most checks – the organization’s name, routing number, and account number; the same information used for depositing. In addition, banking activity on the Lottery’s bank account is closely monitored by Wells Fargo and Lottery personnel on a daily basis.

4. **The Lottery has procedures in place to closely monitor its banking transactions.** Bank reconciliations are performed monthly by Lottery personnel. Because the Lottery closely monitors its bank account on a daily basis, allowing retailers that have incurred an NSF to deposit funds directly into the Lottery’s bank account does not create an increased risk of fraud and allows the Lottery to more efficiently collect funds owed to the District. The Lottery is not aware of any fraudulent banking activity that has occurred by allowing this method of payment.

**Finding #3 - OLG management failed to adequately oversee the process of resolving revenue discrepancies.**

**Recommendation:**

OLG should develop, implement, and monitor adherence to an official policy regarding oversight of the revenue reconciliation process. This policy should include a requirement for OLG to review and approve corrective actions taken, as identified within the incident reports.

**Management Response:**

The Lottery does not concur with the finding.

The Lottery believes it has a more than adequate process for overseeing and resolving Out-of-Balance (OoB) issues occurring within the Back-Office System (BOS). All OoB issues are resolved manually by the gaming system vendor on the same day as the occurrence, not causing any delay in the resolving of revenue or any other affected transactions. In some instances, further research is required by the gaming system vendor to determine the root cause of the issue, and the necessary corrective or preventative action. The gaming system vendor is responsible for promptly providing the Lottery with an Incident Report stating as many details as readily available on the issue. When an OoB occurs, the following actions take place:

- The Lottery’s IT Director emails the Lottery’s Executive Team notifying them of the OoB issue and requesting authorization from the Executive Director to bypass the OoB. The Executive Director responds to the entire Executive Team providing authorization to bypass to the IT Director.
• The OoB is initially researched and manually resolved by the gaming system vendor the same day as the occurrence, not causing any delay in resolving revenue recognition or any other affected transactions.

• An initial Incident Report is prepared by the gaming system vendor detailing the incident description and the report is submitted to the Lottery. If a root cause and corrective or preventative action has been immediately determined and implemented, the report will contain all three components at the time of submittal to the Lottery. If the root cause and corrective action has not been identified, the report will indicate that the incident is under research.

• Depending on the incident, a meeting may be called by the Executive Director to include members of the Lottery’s Executive Team and the gaming system vendor’s team to discuss the details known at the current time of the OoB.

• The Lottery’s IT Director and Executive Director communicate regularly with the gaming system vendor’s team to get status updates on the Incident Reports that remain open without a determined root cause and implemented corrective or preventative action. Additionally, members of the IT staff and other pertinent Lottery departments meet weekly with the gaming system vendor, among the agenda items are open Incident Report issues.

• In the event it is determined that the corrective or preventative action requires a modification to the gaming system, the change must go through the Lottery’s Change Advisory Board (CAB) Review Team for review and approval. After approval, the modification is then added to a system release schedule for implementation.

• Additionally, in October 2019 Lottery management gained access to the gaming system vendor’s issue tracking system which allows us to further track the progress of remediation; and the Lottery’s IT team is in the process of completing an internal database that details the nature and status of detected issues within the various components of the gaming system.

In conclusion, the Lottery strongly believes the process it has in place to oversee OoB incidents is more than adequate and provides sufficient supervision of the gaming system vendor. The Lottery believes that signing the Incident Reports is not a necessary step. The gaming system contract only requires the vendor notify the Lottery on incidents, it does not require that the Lottery sign or accept the Incident Report. The vendor has the expertise and access to research the functionality of their Back-Office System (BOS) to determine root causes and corrective actions. The Lottery and vendor are in continuous communication to resolve the incidents. In addition, if a corrective or preventative action identified requires a system modification, there is a process that involves approval by the Lottery’s Change Advisory Board (CAB).
Finding #4 - Instant tickets are not promptly recorded in the Back-Office System (BOS) upon receipt from suppliers.

Recommendation:

OLG should develop SOPs for the timely recording of instant tickets in the BOS.

Management Response:

The Lottery does not concur with the finding.

The Lottery has extremely high security measures and internal controls in place that protect the integrity of Instant (Scratcher) ticket inventory. The Lottery sells Instant tickets as part of its lottery products portfolio. Instant tickets are printed by a vendor and shipped to the Lottery on scheduled dates agreed to by the Lottery and the vendor. Prior to Instant tickets being shipped to the Lottery, game specifications are developed by the Lottery and vendor. The specifications include the quantity of tickets that will be printed and shipped. The Lottery uses the industry’s three print vendors for its Instant ticket. The security and internal controls employed by the Lottery surrounding the shipment and delivery of Instant tickets are as follows:

- Ticket deliveries are coordinated and scheduled based on the vendor’s contracted trucking company schedules; therefore, deliveries will sometimes need to be made further in advance of a game launch than typically received. Instant tickets are shipped under a secure protocol that requires the Lottery’s security personnel, who are present at all deliveries, to verify that no tampering occurred during shipping and delivery. There are no other items shipped with the Lottery’s Instant ticket deliveries.

- The Bill of Lading (BoL) accompanying the ticket delivery is not seen by the Lottery prior to delivery, and in most cases will include the quantity depending on the vendor; however, as long as the name or number of the games are included, its acceptable to the Lottery. The Lottery has knowledge of, and access to the quantity of each game prior to shipping. The Lottery performs a physical count of the delivery prior to signing the BoL.

- The shipment is verified and accepted by security, warehouse, and support services personnel, and then loaded into a vault that is outfitted with several monitored security cameras, an alarm, and swipe access that only allows for limited personnel to access. The tickets are in boxes, stacked on pallets and sealed with heavy duty plastic wrap until distribution. Distribution preparation begins prior to the scheduled launch date (1st day game available to public).

- The Lottery’s goal is to have Instant tickets available for sale at retailer locations on the day the game is scheduled to launch. The Lottery’s Marketing, Warehouse and IT teams
coordinate the schedule to upload the electronic game file(s) that contain game specifics (e.g. game name, price point, pack size and weight) that the Warehouse team needs to prepare ticket orders for shipment to retailers.

- As an internal control to prevent Instant tickets from inadvertently being distributed earlier than the launch schedule, the electronic file containing the game details is not uploaded into the Back-Office System (BOS) until the picking and packing process (distribution) is set to begin. The uploading of the electronic file is driven by the game(s) scheduled launch date, not by when the tickets are delivered/received. The tickets remain under tight security in a vault with security cameras, an alarm and swipe access. Instant tickets have no value or financial liability until they are activated at retail.

- The risk of having Instant tickets inadvertently shipped to retailers and sold un-activated to the public prior to the game’s scheduled launch date would be greatly increased by uploading the game file into BOS too far in advance of scheduled distribution to retailers. The damage to the integrity of the game and the Lottery brand may be immeasurable.

- Immediately prior to preparing a game for distribution, the electronic file containing the game details for the Instant ticket has to be uploaded into the BOS by an IT team member. The electronic file contains sensitive game details, and as an internal control, only a single Lottery employee has the access to upload the file; however, if ever necessary, access can immediately be granted to another employee with a written request to the gaming system vendor from the IT Director or Executive Director.

In FY 2019, Instant ticket sales made up almost 25% of overall ticket sales. It is the most dynamic product in the Lottery’s portfolio. The Lottery believes that the processes it currently has in place surrounding the receiving of Instant tickets are sound, effective and efficient. The processes take into consideration every facet of operations that are required for this activity. The OCFO promotes continuous improvement and the Lottery engages by periodically reviewing all of its processes and adjusting whenever necessary.

**Finding #5 – OLG publishes conflicting Licensing Requirements which makes it unclear what documentation is required to obtain a retailer license.**

**Recommendation:**

OLG should establish and communicate uniform licensing requirements for prospective Lottery retailers.

**Management Response:**

The Lottery concurs with the finding.
The issue was resolved in September 2020 when the recommendation was initially presented.

The Lottery has established licensing requirements, works diligently, and prides itself on ensuring that potential retailers are well informed as to what documents are required of them to become a retailer. While the criteria for licensure is established, the Lottery periodically reviews and updates this criteria to create greater efficiencies in the licensing process. When these updates occur, the Licensing team works to immediately update all documents distributed to potential applicants, and in the past would work through the third-party vendor that previously maintained the Lottery’s website to update content accordingly. Unfortunately, at times the Lottery experienced challenges getting timely updates made to the website with the previous vendor which led to a lag time between updating internally created documents and the posting of updates to the website; however, the updated information is consistently communicated to internal and external stakeholders. This issue has been resolved as the Lottery on-boarded a new website vendor during the audit review process and launched a new web platform that allows for Lottery personnel to access the backend of the web platform to make content updates immediately. The process implemented to ensure uniformity is as follows:

- The Licensing team will submit the necessary change to the Marketing team via email, with a subject of Retailer Information Update and a “read receipt.” The email will provide the language and/or a mark-up of the document to be revised.

- The Licensing team will monitor the reading of the email and contact the Marketing team by phone or visit if the email has not been read within 2 working hours.

- The Marketing team will make the update to the website within 2 working hours of the Licensing team’s read receipt. When the change has been completed, the Marketing team will reply to the original email, adding a “read receipt,” confirming completion of the requested change.

- The Marketing team will monitor the reading of the email and contact the Licensing team by phone or visit if the email has not been read within 1 working hour.

- The Licensing team will go to the website and review the revised language or document for accurate completion of the requested change within 1 working hour. If the change is not accurate, the Licensing team will immediately contact the Marketing team by phone to immediately resolve the discrepancy.

- The Marketing team will send a final email acknowledging the resolution.

As such, OLG no longer anticipates any delay between updating information on paper documents and content posted to the website.
Response to Agency Comments

As has been the case throughout this audit, our team appreciates OLG’s prompt reply to our requests and inquiries.

ODCA appreciates OLG’s response which outlines internal controls over the key processes we reviewed. Despite their ability to describe these processes, OLG has not developed and published clearly defined policies and procedures that are available for review. Written policies and procedures serve as a guide for employees to meet organizational objectives and provide high-quality services and products to the public. Therefore, we are hopeful that OLG will reconsider their objection to our recommendations and implement them as outlined in our report by developing formal policies and procedures. These policies should include the kind of controls described in their response to this report covering the retailer payment, revenue reconciliations, and inventory management processes.

In response to our third finding, ODCA acknowledges the Lottery’s efforts to streamline its revenue reconciliation policy by implementing a vendor issue tracking system in October 2019. These efforts will assist OLG with monitoring issues identified during the revenue reconciliation process. Since this process was implemented after the end of our scope, June 2019, ODCA was unable to review this process.

Throughout the span of this review, OLG has provided ODCA with significant insight into key processes that sustain Lottery operations. Due to these efforts, ODCA was able to conduct a comprehensive review of these processes as discussed within the Draft Audit Report. We are aware that OLG’s Executive Director has recently resigned, and we are hopeful that management will reevaluate the recommendations set forth in this report and implement formal policies and procedures for key agency operations. Formal implementation of the controls outlined in OLG’s response should help mitigate the findings in this report.
## Summary of Report Recommendations

Most of the recommendations in this report can be implemented without any additional costs to the agency/entity, and/or help to advance the goals of OLG, as seen below.

<table>
<thead>
<tr>
<th>Recommendation</th>
<th>Is There a Cost to the Agency/Entity to Implement?</th>
<th>Potential to Generate Revenue or Savings to the District?</th>
<th>Specific Agency/Entity or District-Wide Goal Advanced by Recommendation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. OLG should reevaluate their NSF policy to ensure retailers face monetary penalties for reoccurring NSFs.</td>
<td>No</td>
<td>Yes</td>
<td>D.C. Lottery Mission</td>
</tr>
<tr>
<td>2. OLG should develop standard operating procedures for when payment is not provided during the weekly electronic funds transfer sweep, which should include acceptable methods of payment.</td>
<td>No</td>
<td>Yes</td>
<td>OCFO 2017–2021 Strategic Plan includes a strategic objective of improving transparency and quality of information.</td>
</tr>
<tr>
<td>3. OLG should develop, implement, and monitor adherence to an official policy regarding oversight of the revenue reconciliation process. This policy should include a requirement for OLG to review and approve corrective actions taken, as identified within the incident reports.</td>
<td>No</td>
<td>No</td>
<td>OCFO 2017–2021 Strategic Plan includes a strategic objective of improving transparency and quality of information.</td>
</tr>
<tr>
<td>4. OLG should develop SOPs for the timely recording of instant tickets in the BOS.</td>
<td>No</td>
<td>No</td>
<td>OCFO 2017–2021 Strategic Plan includes a strategic objective of managing risk and preventing fraud.</td>
</tr>
<tr>
<td>5. OLG should establish and communicate uniform licensing requirements for prospective Lottery retailers.</td>
<td>No</td>
<td>No</td>
<td>OCFO 2017–2021 Strategic Plan includes a strategic objective of improving transparency and quality of information.</td>
</tr>
</tbody>
</table>
About ODCA

The mission of the Office of the District of Columbia Auditor (ODCA) is to support the Council of the District of Columbia by making sound recommendations that improve the effectiveness, efficiency, and accountability of the District government.

To fulfill our mission, we conduct performance audits, non-audit reviews, and revenue certifications. The residents of the District of Columbia are one of our primary customers and we strive to keep the residents of the District of Columbia informed on how their government is operating and how their tax money is being spent.

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