

Of Icebergs and Lotteries: Retailer fraud, the invisible threat

The threat of retailer fraud is not to be underestimated. It can severely disrupt your lottery operation and damage its reputation for a considerable time. Thomas Bierbach, Vice President of Baseline Business Geographics Inc., explains how retailer-fraud risks can be dealt with proactively and cost effectively through player protection controls and retailer compliance monitoring. Baseline's end-to-end compliance management solution, Baseline Compliance Manager, facilitates retailer compliance monitoring and integrity testing programs, thereby ensuring a lottery operation's reputation.

Were icebergs bad for the Titanic? We all know the answer to this rhetorical question. But really, what are the odds of hitting an iceberg? They are very small, are they not?

You may be wondering where I am going with this, but please indulge me — it is a simple example of a risk management exercise. Say you are sailing along in your ship, the HMS Lottery, and you think you have everything well under control. Sales are good, new products abound, technology works, players and shareholders are happy, you are staying out of the news, and then — the unthinkable happens. You run into an iceberg and it rattles your vessel from bow to stern.

Your passengers, the public, stakeholders and media alike, start to question your seaworthiness. Your organization is taking a tremendous blow to its reputation. Everybody wonders, how could this happen? If you are lucky enough to keep the ship afloat — as well as your career — and continue the cruise, you will be asked what you are going to do to prevent this from happening again. Do you have all the answers? Not many have.

This parable serves well to illustrate a particular risk that virtually all lotteries face, a risk that is profoundly underestimated both in its likelihood of occurrence and in its detrimental impact. That risk is retailer fraud. Of course instead of seaworthiness, it is primarily the reputation and the integrity of the lottery operation that are at stake.

Retailer fraud

Retailer fraud is a crime of opportunity. The temptation for a lottery retailer or staff member to defraud unsuspecting players of their winnings has been around for as long as the retail channel has been part of the lottery business model. The risk of tickets getting swapped, palmed, or switched varies, depending on the lottery terminal equipment and validation procedures in use — but it is there nonetheless.



*Thomas Bierbach,
Vice President, Business Development,
Baseline Business Geographics Inc.*

Just a few years ago, a number of lotteries in Canada experienced the unwanted attention an incident of fraud can draw. Lotteries across the country had their reputations

damaged and their integrity challenged. Player confidence was shaken, jobs were lost, and millions were spent in correcting operational shortcomings. The haste with which the issue at hand was addressed and the after-the-fact overreaction to risks that could have been proactively mitigated in the first place, further aggravated the situation. But, like the awareness of a leaky roof and the urge to fix it, both are diminished while the sun is shining.

We have learned from such occurrences that the likelihood and impact of retailer fraud can easily be underestimated. Lotteries are often not fully aware of the real threats and the associated risks posed by retailer fraud until a major incident occurs. In the event of a retailer fraud incident, it becomes less a matter of the monetary impact on the lottery than a matter of the reputational damage to the lottery and its retailer base, and the ensuing adverse consequences thereof.

Past incidents have proven that recovery from reputational damage and the resulting decline in player and stakeholder trust is not only costly, but takes significant time. Licensed operators of a state lottery have even more at stake than other government-run lotteries, as license renewal is crucial to their continued success in executing growth strategies in other markets. Lotteries are not just lotteries anymore. Changes in the industry have driven many organizations to expand their horizons and growth strategies beyond their core business areas and to venture outside their jurisdictions. Striving

to be a world-class contender and maintaining a competitive edge are essential in this changing environment. Shortcomings in operational excellence will be harmful to those competing in bids for licenses and contracts.

In seeking to understand and manage retailer security risks, lotteries can profit from the experiences of lotteries from other jurisdictions. Such practical knowledge can help a lottery organization address retailer fraud risks proactively and cost effectively, which is preferable to an after-the-fact reaction to a retailer fraud incident.

Lottery regulators, stakeholders, and the public are looking for demonstrated integrity, compliance, and player protection from fraud in lottery retail operations. Lottery shareholders and business management are looking for a return on the security investment and operational efficiency. The lottery security and compliance function has to ensure security, integrity, and regulatory compliance in balance and alignment with business objectives. Although many lotteries are implementing retail compliance testing and mystery shopper programs, the ability for them to compile data on the efficacy of such programs remains a challenge.

A specific issue in the area of retailer security and player protection is the significant lack of control players have when validating their tickets. Players must often rely on the integrity of the retailer for accurate validation results. Without proactive retailer compliance monitoring and testing a lottery cannot keep track of retailer fraud occurrences and must therefore refer to player complaints and allegations. To preserve reputational equity, lotteries need to be aware of the actual occurrences of retailer fraud, the associated risk levels involved, the likelihood of fraud being perpetrated, and the impact it may have on their organization.

A broad variety of player protection measures are available to lotteries, from simple controls around the validation procedure to high technology solutions, such as ticket self-checkers or player card systems. The effectiveness and viability of any of these measures largely depend on the regulatory and legal requirements within a lottery's jurisdiction, and the size of the lottery's retailer network.

During my time as Director of Security and Compliance at Atlantic Lottery of Canada,

a retailer fraud incident caused significant disruption to the organization's operations. Through this experience, I learned that a balance of player protection controls around the validation process at the retail site was most cost effective and efficient. Putting emphasis on the control the player has over the ticket validation procedure has been more effective than the broad implementation of technology. The most significant learning outcome, however, was that regardless of how many controls are in place, only continuous monitoring, testing, and enforcement provide measures as to the effectiveness of the controls and compliance requirements. The old adage, "what cannot be measured cannot be managed", is especially relevant here.

This lesson acted as a catalyst for Baseline Business Geographics to develop an automated compliance monitoring solution. They created a solution that couples Geographic Information Systems (GIS) and Global Positioning Systems (GPS) with mobile device technology. This allows for a cohesive workflow approach for retailer compliance inspection and testing, whereby inspectors can interact with retailers. Atlantic Lottery served as a pilot project for the Baseline Business Geographics solution.

Working with lottery operators and regulators, Baseline Business Geographics has gained considerable lottery experience in security and risk management. They provide support in the management of retailer security risks and conduct retailer security assessments, implementing effective and balanced controls while optimizing compliance and inspection management solutions.

Baseline Compliance Manager

Baseline's core solution, Baseline Compliance Manager, is a risk-based, automated management program designed to meet the regulatory and policy requirements of compliance monitoring in a lottery's distributed retailer network. Baseline Compliance Manager renders operational efficiency and delivers result-oriented metrics. It comprises an end-to-end management system that enables lotteries to demonstrably improve retailer compliance and integrity testing programs. This ensures that corporate policy and procedures as well as jurisdictional regulations are met. Baseline Compliance Manager also provides optimization for lotteries with existing compliance programs. Alternatively, it can serve as a framework for

operators that are in the process of establishing a compliance program.

On the front end, Baseline Compliance Manager offers electronic forms on GIS- and GPS-enabled mobile devices, to facilitate data capture during field inspection and testing. Mobile devices, such as tablets, have a real time data link to a compliance back end database. On the back end, Baseline Compliance Manager supports workflow planning, inspection result analysis, and provides for immediate trending and performance reporting, as well as a progressive disciplinary follow up.

In a distributed retailer and site network, Baseline Compliance Manager creates enterprise value through operational excellence by optimizing and automating a lottery's security and compliance monitoring and inspection processes. It provides your organization with the operational measures and effective monitoring necessary to counter the retailer security risks common in most lottery operations.

*By Thomas Bierbach CISM, CISA
Vice President, Business Development
Baseline Business Geographics Inc.*

About Baseline



Baseline Business Geographics Inc. is a global provider of integrated desktop, mobile, and Internet mapping and management solutions. They specialize in customized software development of GIS/GPS and mobile systems. As a solutions integrator, Baseline offers complete enterprise applications including data, training, consulting, project management and more. Baseline Compliance Manager, its end-to-end compliance management solution, enables lotteries to demonstrably improve their retailer compliance and integrity testing programs to ensure compliance with corporate policy, procedures and regulations. For more information on how Baseline can help your lottery, please contact Thomas Bierbach at thomasb@baselinegeo.com.