

STATE LOTTERY DEPARTMENT
Lottery Board Meeting
October 30, 2002

The State Lottery Board met on Wednesday, October 30, 2002, at 9:30 a.m., at the State Lottery Department, 900 East Main Street, Richmond, Virginia.

MEMBERS PRESENT: Stephen C. Fogleman (Chairman)
Virginia D. Hall (Vice Chairman)
Gilliam M. Cobbs
Stuart C. Siegel

MEMBER ABSENT: Paul J. Lanteigne

STAFF PRESENT: Penelope W. Kyle, Executive Director
Mary L. Stafford, Chief of Staff
Mark D. Cannon, Director – Internal Audit
Shelton M. Coleman, Director - Information Technology
Mickey K. Collins, Director – Human Resources
Frank S. Ferguson, General Counsel and Director -
Legislative & Regulatory Affairs
Mark R. Merritt, Director – Sales
S. Kyle Rogers, Director - Marketing
Edward A. Scarborough, Director - Public Affairs
Dennis P. Shaw, Director - Security
Donna M. VanCleave, Director – Finance
Richard G. Wilkinson, Director – Lottery Operations
Catherine B. Akers, Licensing Coordinator – Lottery
Operations
Alan W. Hussey, Economic & Research Manager –
Marketing
Barbara L. Robertson, Board, Legislative & Regulatory
Coordinator - Legislative & Regulatory Affairs

OTHERS PRESENT: Dennis J. Yecke, Senior Analyst - Department of Planning
& Budget

Mr. Stephen C. Fogleman, chairman, presided and Barbara L. Robertson was the recording secretary.

CALL TO ORDER

The chairman called the meeting to order and stated that a quorum was present.

CALL TO ORDER (Continued)

Ms. Kyle introduced Frank Ferguson, who is the Lottery's new General Counsel and Director of Legislative and Regulatory Affairs. Mr. Ferguson came to the Lottery from the Office of the Attorney General.

MINUTES OF LAST MEETING

On motion duly made and seconded, the minutes from the regular and closed meetings held on September 11, 2002 were approved as distributed.

PUBLIC COMMENT

Mr. Fogleman then opened the floor for public comment. There was none.

FINANCIAL REPORT

Ms. VanCleave reported the Lottery's financial performance for the first quarter of FY 2003 through September.

Total lottery sales through September 2002 were \$269.2 million, which was \$16 million or 6% more than sales for the same period in FY 2002. The increase resulted primarily from strong scratch ticket sales which were \$19.4 million or 20% higher than those in the prior year. Sales of all online products were \$3.4 million or 2% less than the prior year when online sales during the same period last year were supported by significantly higher than expected Pick 3 prize payouts to players. In FY 2003, although online sales were lower, gross profit on the games was almost \$12 million higher because of the lower prize payouts.

The total prize expense rate (prizes as a percentage of sales) was 2.2% lower through September than at this same time last year. The overall prize payout rate was 55.9% of sales, compared with 58.1% at this point last year.

She reported that the retailer compensation rate through September was 5.6% of sales, equal to last year. Due to the increased sales, however, retailers have earned almost \$1 million more in FY 2003 than at the same point last year.

Operating costs for FY 2003 through September were \$15.1 million, which was almost \$2 million less than last year when much of the additional spending was for the launch of the Lotto South game.

With strong sales and overall prize expense close to the expected rate, net income generated through September 2002 was \$87.8 million, which was \$13.3 million or 18%

FINANCIAL REPORT (Continued)

more than for the same period in FY 2002. She pointed out that this first quarter was the best ever first quarter for the Virginia Lottery.

In response to a question from Mr. Siegel about the Lotto South game, Ms. Kyle and Mr. Hussey stated that Lotto South is more profitable than the other games, even though sales have been slightly lower, and that the jackpot level for the game climbs twice as rapidly as its predecessor game, Lotto Virginia.

Mr. Cobbs noted that there appeared to be a decline in sales for Pick 3 and Pick 4. He suggested that one of the causes may be unfriendly retailer behavior related to those games. He requested that at a future meeting of the board, discussion be held regarding retailer attitudes toward the different types of lottery games.

BOARD ISSUES

FY 2003 and FY 2004 Budgets

Ms. Kyle reminded the members that, pursuant to § 58.1-4008 of the *Code of Virginia*, the board has the authority to accept, reject or modify the Lottery's revenue projections before they are submitted to the Governor.

Mr. Hussey then reviewed the Lottery's FY 2003-2004 proposed sales forecast of \$1,128.3 million and \$1,163.8 million, respectively. Net income was projected at \$362.8 million for FY 2003 and \$370.4 million in each fiscal year, 2004 through 2006. He then reviewed the forecast by product and by category.

Ms. VanCleave then reviewed the projected expenses. Because sales are expected to increase, prize expense is forecast to increase to 56.4% in FY 2003 and to 56.7% in FY 2004. Retailer compensation is projected to be 5.6%, and retailers are expected to earn additional compensation from incentives during the year. Operating expenses are expected to decrease by \$1.4 million to 6.5%.

Ms. VanCleave advised that the Lottery's official forecast will be submitted to the Governor's Office in November. In December the Governor will propose his budget. The General Assembly will develop the budget during the upcoming session. In April the Governor will sign the 2003 budget bill.

On motion duly made and seconded, the board adopted the Lottery's revenue projections, subject to annual revisions.

Retailer Licensing Fees for CY 2003

Ms. Akers, the Lottery's licensing coordinator, proposed lottery retailer licensing fees for CY 2003. She explained that the current retailer licensing fees are \$50 for the initial application fee and \$25 annual renewal fee for each retailer location. The \$50 application fee was established by the board in 1997; the \$25 renewal fee has remained unchanged since the beginning of the Lottery. At current fee levels, licensing revenue is projected to total \$148,000 in FY 2003. The licensing budget for this year is \$136,040, which does not include costs such as rent, security, credit checks, retailer hearings, etc. Therefore, she recommended retaining the current application fee of \$50 for new retailers and increasing to \$35 per location the annual license renewal fee for existing retailers. Based on current retailer renewals, this would generate approximately \$48,180 in additional revenue and would cover licensing costs not included in the current budget.

Following discussion, on motion duly made and seconded, all board members present voted to adopt the recommended fee structure of \$50 application fee and \$35 renewal fee for CY 2003, as presented.

DIRECTOR'S REPORT

Ms. Kyle reported that pursuant to the Setoff Debt Collection Act, the Lottery made a payment to the Department of Taxation totaling \$37,304 in September, and in accordance with provisions in the Lottery Law, the department transferred unclaimed prizes of \$1,044,794 in September to the Literary Fund. The year-to-date total for debt setoff was \$130,491 and for the Literary Fund was \$2,643,962.

Ms. Kyle then announced the names and hometowns of several \$100,000 Cash 5 winners, Lotto South jackpot winners from Virginia and Kentucky, and Mega Millions jackpot and \$175,000 winners. The current Lotto South jackpot is \$4.0 million. The current Mega Millions jackpot is \$69.0 million.

In procurement action, Ms. Kyle announced that a \$1.7 million, two-year contract has been awarded to PAP Security Printing for on-line ticket stock.

She updated the board on lottery-related issues in North Carolina and Tennessee. The North Carolina legislature has defeated a proposal to put a state lottery to a vote of the people in November; therefore, the lottery proposal is dead for at least another year in that state. Tennessee voters, however, will vote on a lottery referendum that would empower their General Assembly to initiate a state lottery and to would allow not-for-profit agencies to hold gambling fund-raisers once a year.

Ms. Kyle announced that this is the fourth year that the Virginia Lottery has honored outstanding public school educators from across the Commonwealth. This year's second

DIRCTOR'S REPORT (Continued)

Virginia Lottery Excellence in Education Award was presented to Mr. Pete Schumacher of Chesterfield County.

She reported that the Lottery won several awards during the recent conference of the North American State and Provincial Lotteries (NASPL): (i) "Winners Video" was a Hickey Award finalist for Audio/Visual Presentation; (ii) "Fortune 500/Efficiency" won a Batchy Award for Radio Advertising/Corporate/Beneficiary; (iii) "Annual Report" was a Batchy Award finalist for Corporate Communications; (iv) "Lotto South Introduction" won the Delegates Award for Point of Sales Materials; and (v) "Virginia Lottery Team Racing" won the Delegates Award for Promotional Premium Items.

Also, she reported that the Lottery's neon sign won the Gold Award at the 2002 Point-of-Purchase Advertising International (POPAI) awards ceremony. The POPAI show, held earlier this year, had nearly 800 entries for honors in 73 categories. More than 60 judges, representing leading brand marketer and producer companies, evaluated entries based on criteria such as the entry's effectiveness in creating or reinforcing awareness of the product and its success in achieving stated objectives. The Lottery's sign took top honors in the Permanent Sign category for convenience stores.

Last Tuesday, at Ms. Kyle's invitation, Governor Warner visited the Lottery to meet employees and to thank them for the tremendous year the department produced last year. He challenged the department to even greater results this year.

Finally, Ms. Kyle distributed the proposed board meeting dates for next year.

OTHER BUSINESS

Mr. Fogleman then announced that the next meeting of the board is scheduled for Wednesday, December 11, 2002.

On behalf of the board members, Mr. Fogleman presented Ms. Stafford with a board resolution recognizing her many years of service to the Lottery and to the Commonwealth. A copy of the resolution is attached to and made a part of these minutes.

CLOSED MEETING

Ms. Hall made the following motion:

MOVED: that, in accordance with the provisions of § 2.2-3712 of the *Code of Virginia*, the board go into a closed meeting for the purpose of

CLOSED MEETING (Continued)

discussion, consideration or review of: (i) pursuant to subdivision A 16 of Section 2.2-3711, State Lottery Department matters related to proprietary lottery game information exempted from disclosure under subdivision A 37 of Section 2.2-3705, specifically, game information for proposed instant games; (ii) pursuant to subdivision A 7 of Section 2.2-3711, legal matters, including consultation with legal counsel and briefings by staff members, pertaining to specific legal matters requiring the provision of legal advice by counsel regarding current litigation; and (iii) pursuant to subdivision A 1 of Section 2.2-3711, personnel matters, regarding the assignment of specific employees of the Department .

The motion was seconded by Mr. Siegel and approved by all members present. Mr. Fogleman then announced the conclusion of the open session, and the board went into a closed meeting.

RECONVENED MEETING

Following its closed meeting, the board reconvened in open session. Ms. Hall read the following certification for the closed meeting:

WHEREAS, the State Lottery Board has convened a closed meeting on this date pursuant to an affirmative recorded vote and in accordance with the provisions of The Virginia Freedom of Information Act; and

WHEREAS, § 2.2-3712 of the *Code of Virginia* requires a certification by this Board that such closed meeting was conducted in conformity with Virginia law and the motion by which the closed meeting was convened;

NOW, THEREFORE, BE IT RESOLVED that the State Lottery Board certifies that, to the best of each member's knowledge, (i) only public business matters lawfully exempted from open meeting requirements by Virginia law were discussed in the closed meeting to which this certification resolution applies, and (ii) only such public business matters as were identified in the motion convening the closed meeting were heard, discussed or considered by the Board.

By roll call, all members present voted in the affirmative that the certification was accurate as read.

RECONVENED MEETING (Continued)

On motion duly made and seconded, the board members present approved, as presented in the closed meeting, prize structures for Instant Games 245, 246 and 551 through 555, including the $\pm 0.5\%$ prize structure policy adopted by the board on September 13, 2000.

ADJOURNMENT

There being no further business to come before the board, the chairman declared the meeting adjourned.

Penelope W. Kyle
Secretary

Stephen C. Fogleman
Chairman