

Oklahoma Lottery Commission
Minutes of Regular Meeting
September 18, 2007 – 1:30 p.m.

Members Present:

Mr. James Orbison, Chairman
Mr. William Paul, Vice-Chairman
Mr. George Charlton, Trustee
Ms. Charlotte Edwards, Trustee

Members Absent:

Ms. Cindy Ball, Secretary
Mr. Thomas Riley, Treasurer
Dr. Linda Dzialo, Trustee

Others Present:

Jim Scroggins, OLC	Stan Van Ostran, OLC
Rollo Redburn, OLC	Houston Hunt, Jordan Associates
Allen Blankinship, SGI	Mark Schlachtenhaufen, Capitol Network News
Gay Tudor, AG's Office	Mary Martha Hall, OLC
Mary Wills, SGI	Sarah Clough, The Journal Record
Terri Jackson, OLC	Ron Miguel, Scientific Games
Rich Sanchez, OLC	Rhonda Hooper, Jordan Associates
Bonnie Presley, OLC	Jay Finks, OLC

ITEM 1

Call to Order. Roll Call and Announcement of Quorum

The meeting was called to order at 1:35 p.m.

Roll Call: Mr. Charlton, Ms. Edwards, Mr. Orbison and Mr. Paul were present. Mr. Orbison declared a quorum.

ITEM 2

**Announcement of Filing of Regular Meeting Notice and Posting of the
Agenda in Accordance With the Open Meeting Act**

Posting of Regular Meeting Notice and Posting of the agenda were confirmed, in accordance with the Open Meetings Act.

ITEM 3

Approval of Minutes of the June 26, 2007 Regular Meeting

Mr. Paul made a motion to approve the minutes of the June 26, 2007 meeting. Mr. Charlton seconded the motion.

Roll Call: Mr. Charlton, Ms. Edwards, Mr. Orbison and Mr. Paul voted to approve the minutes. The minutes were approved.

Mr. Orbison stated that Ms. Linda Dzialo has sent a letter of resignation to the Governor and sent a copy to each member. At present, her personal and professional obligations

demand the majority of her attention. Mr. Orbison stated that he personally feels she has done an outstanding job on this commission. Her enthusiasm, leadership and tenacity have proved to be an asset to the commission and she will be missed.

ITEM 4

Executive Director's Report

Mr. Scroggins stated that the upcoming Hot Lotto game has an option on the game that is called Sizzler. The option is a lot like the Power Play option in Powerball. The Sizzler costs an additional \$1, but it triples the winnings for all prizes except the jackpot. The Power Play option accounts for about 40% of sales per week, so we are anticipating picking up an additional 40% in sales on the Sizzler option.

Mr. Scroggins stated that the Oklahoma Lottery Commission accounting staff has been awarded the 2006 Certificate of Achievement for Excellence in Financial Reporting for its comprehensive annual financial report. The Certificate of Achievement is the highest form of recognition in the area of governmental accounting and financial reporting, and its attainment represents a significant accomplishment for the Oklahoma Lottery and its staff. He congratulated Stan Van Ostran, Rich Sanchez, Megan Densow and his staff, for their hard work.

The Lottery Game Show will have its first taping on Wednesday, September 26th, with the taping of four shows that day. The first show will air on October 13th and will be aired on Saturdays at 6:00 pm on KOCB-CW and the following Mondays at 2:00 pm and Wednesdays at 6:30 pm on Cox Channel 7. In Tulsa the show will air the following Mondays at 2:00 pm and Wednesdays at 6:30 pm on Cox Channel 3. We have received approximately 4,300 entries for the game show already; 2,300 on the web and 1,500 mailed in, with entries from seven different states.

Also, October 17th the Tulsa station will begin airing our Powerball drawings as part of the advertising and game show package.

Mr. Scroggins said in an attempt to initiate cost savings the lottery is looking at moving the offices on the first floor upstairs. After the preliminary build out costs this move could potentially save \$27,000 a year in rent costs. The building has conference rooms on the south end that we can schedule for our use as needed.

The NASPL/WLA World Meet is taking place in Louisville, KY on October 3-6, so if anyone is interested in attending, our staff can assist with travel information.

ITEM 5

Discussion and Possible Action on Proposed Rule Changes

Mr. Scroggins said that the lottery has received consistent requests from the retail community that they wish to receive a bonus for selling a jackpot ticket. Adding such a bonus is reflected in the proposed rule change. The retailer would receive a \$25,000 bonus for selling a winning Powerball jackpot ticket (6 of 6 matching balls) and a \$5,000 bonus for selling a winning Powerball ticket that matches 5 of 5 white balls with no matching Powerball. In the Hot Lotto game the bonus would be \$5,000 for selling a winning jackpot ticket (6 of 6 matching balls) and \$1,000 for selling a winning ticket that matches 5 of 5 white balls with no Sizzler match. The wording states that the bonus will be paid to the retailer in a manner as determined by the Oklahoma Lottery Commission regardless of whether the winning prize ticket is claimed by the apparent winner. The reason this statement was added was to give the retailer the option to have their account credited or receive the bonus by check. Historically, if this compensation

structure had been in place it would have cost the lottery approximately \$150,000, but the increase in ticket sales would have off-set the cost. This is not only a sales incentive for the retail stores, but it promotes good will.

The second proposed rule change relates to the time frames for returning inactive and partial packs from three (3) weeks to six (6) weeks. In reality the process takes about six (6) weeks so it would make the rules consistent with this practice.

The process to make rule changes starts with the Board approving the change. Then notice is sent to the Secretary of State, they will publish a notice of our intent to change the rules. The lottery will make it known to those who have expressed interest in the rules that we are having a public hearing for comments. Notices are given to our retail community so that they are given an opportunity to comment. The public hearing would be scheduled for some time in November or December. Once all the comments from the public have been collected they would be presented to the board at the December board meeting. The board will review the comments, and at that stage the board has several options: make changes to the proposed changes and request that the process be started over again; make changes and deem that they are too minor to require the process to be repeated; or adopt the changes. Once the board has adopted the changes the lottery has 10 days to send them to the Governor and to the Legislature. The Governor has 45 calendar days to consider the information and approve or reject them, and the Legislature has 30 legislative days, which start in February when they come into session. Once approval is received from all various stages the rules are considered "finally adopted". The lottery sends notice to the Secretary of State and they publish that approval has been given by both the Governor and the Legislature. When published, they are considered "promulgated" and 10 days after they are published, the changes can be effective. The last two times the lottery proposed rule changes, there were no attendees at either public hearing.

A motion was made by Mr. Paul that the proposed rule changes be approved and that the process be started. The motion was seconded by Ms. Edwards.

Roll Call: Mr. Charlton, Ms. Edwards, Mr. Orbison and Mr. Paul all voted to approve the motion. The motion carried.

ITEM 6

Discussion and Possible Action on Budget and Strategic Plan for FY2008 through FY2010

Mr. Scroggins said there are three issues to discuss: the Strategic Plan process, the actual budget that we are going to recommend and issues facing the Oklahoma Lottery Commission.

Mr. Scroggins stated that the Strategic Planning process is fairly well defined as to how it is done internally. Basically, we go to each unit and gather their input.

Our approved budget provided for \$227.2 million as gross revenues. However, even after going through the big Powerball jackpot, it is apparent that the Oklahoma Lottery is a \$4.0 million a week lottery, which brings us to \$208 million in gross sales. For instant ticket sales the average YTD is about \$1.519 million per week. Our proposed revised FY2008 budget of \$83 million is \$1.596 million per week. Pick 3 is averaging about \$131,400 per week; we have budgeted \$132,692 per week, showing some expected modest growth. Powerball, after factoring out the recent run where the jackpot exceeded \$300 million, is averaging \$1,762,726. That puts Powerball at between \$1.7-1.8 million per week. We have budgeted \$106 million,

which is \$2,038,461 per week, capturing the impact of the recent run and looking at promotions in FY2008. Cash 5 is similar to Pick 3, averaging \$131,355 per week with a revised budget of \$136,538. In January, Hot Lotto will begin, so there will be 26 weeks of sales this fiscal year. We have budgeted approximately \$200,000 per week.

Mr. Scroggins stated that there are several issues that have resulted in a decrease in ticket sales: the mandated profit percentage of 30-35% of gross proceeds (the first two full fiscal years plus our partial year the mandate is 30% and thereafter 35%); prize payout percentages are too low, particularly in instant games; gaming casinos; illegal gaming; restrictions on the types of games that can be offered; and restrictions on selling locations.

Mr. Scroggins stated that mandating a minimum profit percentage inhibits the lottery's ability to provide a greater prize percentage payout in various games, particularly instant games. This in turn inhibits sales and thus profits. By increasing prizes in lottery games, greater sales can be achieved and even though the profit percentage achieved may be smaller, the level of real, spendable dollars will increase.

Mr. Scroggins stated that for our first two years the lottery had a profit of 33.6% and 32.2%. We were able to accomplish that because we did everything we could to hold our expenses down. We have one of the smallest lottery staffs with only 40 full time employees. This is about half the staff of the other lotteries with a comparable size. To maximize our funds to education we have also chosen not to fill several positions that opened during the last two years. One of the reasons we chose to move offices upstairs was to do what we need to maximize the profit we send to education.

Oklahoma averages 53.5% on prize payouts, the other states average about 63.5%. Annual sales per capita for Oklahoma is \$60 and the other states average \$137. Oklahoma is 10 percentage points below the average for prize payouts and our annual per capita is considerably less.

Mr. Scroggins said another issue that affects ticket sales is the number of gaming casinos. There are currently 33 Native American tribes in Oklahoma with State-Tribal compacts that operate approximately 100 gaming establishments. They can offer a 97-98% payout on slot machines and their return to the State is about 6%. The lottery offers a 53.5% prize payout with a 30-35% return to the state. He said he is not saying the casinos shouldn't be here, he's just pointing out that this isn't a level playing field. Data provided by the Office of State Finance shows that in FY2007 the gross revenue for casinos was \$777 million with \$46.8 million (6.02%) being provided to the state.

Mr. Scroggins stated that quasi-legal/illegal gaming machines are noticeably on the rise and have a negative impact on lottery sales and profits. Currently the Oklahoma Tax Commission issues more than 89,000 tax stamps for vending machines. A recent letter from the Office of the Attorney General indicates that many of these machines, the quarter pusher machines and the ones that are currently dispensing token merchandise for a "spin" on the machine, would be illegal. The State of Oklahoma does not currently have a system in place to monitor or regulate these illegal machines and enforcement is up to local law enforcement and the County DA's.

Mr. Scroggins stated that another issue that limits lottery sales is the restriction on the types of games the lottery can offer. The Oklahoma Education Lottery Act prohibits the lottery offering video lottery, keno and pull-tabs, which in turn limit potential sales. We are not advocating that we do these games, but offer this for information. When evaluating the sales of other states that offer these games in their lottery, and assuming the lowest annual per capita

rate achieved by other states, Oklahoma could be missing out on approximately \$41 million in potential sales. The report shows that for Keno, the annual sales could potentially reach \$3.58 million, and pull-tabs could reach .96 million.

Mr. Scroggins stated that the restriction on liquor stores selling lottery tickets is another issue that limits ticket sales. Although the sales level that could be achieved through these types of locations is unknown, other states utilize these locations and many of them are quite successful.

Mr. Scroggins stated that after some research, it appears that selling online games in a casino would be classified as Class 3 gaming and the only way that would be legal is for the tribe to have a compact with the state. If the establishment has an existing bingo operation they could potentially sell the instant tickets but more research is still required regarding proper interpretation of federal regulations.

All these issues have been taken into consideration in decreasing the sales figures in the budget from \$227.2 million to \$208.2 million. By the budget year 2009, with the mandated 35% and current sales, the lottery will have to cut \$1.4 million out of our operating expenses in order to make 35%. Currently, the majority of our operating expenses are fixed, so the cut would likely be in advertising and reduction of staff. Mr. Scroggins recommended to the board that we take the necessary steps to initiate legislative action to eliminate the 30-35% mandated profit percentage with the intention to pay more money on prizes, which in turn enables more ticket sales, and thus provides more money to education.

Mr. Charlton asked if the staff has done any projections on what the budget would reflect if the mandated 35% were not in place. Mr. Scroggins stated that looking at other lotteries and comparing the effect of additional prize payouts and lowered mandated percentages, sales would show a net increase of approximately \$70 million. Mr. Scroggins said they had the same experience in Missouri. When they put more into prizes, sales increased. The players won more and more often, and this spread to others. If the people that play win more often, they play more often and they tell others. Mr. Charlton asked if Mr. Scroggins knew of an instance where the numbers were not positive and Mr. Scroggins stated that he did not. Some efforts were more successful than others, but all had positive impact on sales and dollars available to the beneficiaries.

Mr. Paul stated that the Audit and Finance Committee has looked at these changes very closely and discussed the various options available. By eliminating advertising, history and experience reflects that this will create a decline in sales. The data that has been submitted shows for FY2008 we have a current work program budget of \$227 million. That number is too high. As soon as we have the knowledge and education to be as realistic as we can, which is now, we should use realistic numbers. We know that the Oklahoma Lottery is closer to being a \$4 million a week lottery, or \$208 million a year. Even at \$208 million gross we will be within the law and we will turn over more than 30% to education.

After much discussion, the board asked that the staff include the issue on the next board meeting agenda and present a pro-forma that reflects the budget without the mandated percentages, with increased prize payouts.

Mr. Paul made a motion to approve the budget revisions, as submitted to the board, of the FY2007-FY2010 budget. The motion was seconded by Mr. Charlton.

Roll Call: Mr. Charlton, Ms. Edwards, Mr. Orbison and Mr. Paul voted to approve the motion. The motion carried.

ITEM 7

Discussion and Possible Action on 2008 Meeting Dates

Mr. Orbison stated that according to law we must report to the Secretary of State our 2008 schedule of regular meetings by December 15, 2007.

Ms. Edwards made a motion to establish the 2008 meeting dates as March 18, 2008, June 17, 2008, September 16, 2008 and December 16, 2008. Mr. Charlton seconded the motion.

Roll Call: Mr. Charlton, Ms. Edwards, Mr. Orbison and Mr. Paul voted to approve the motion. The motion carried.

ITEM 8

Report of Audit and Finance Committee (Mr. Paul)

Mr. Paul stated that the Audit and Finance Committee met prior to the Board Meeting today with Cole & Reed, the auditors of record. A draft of Cole & Reed's audit report was reviewed with and without the OLC staff during the meeting. The audit report is clean and there are no exceptions. Cole & Reed was highly complimentary of the financial staff. The committee reviewed the preliminary draft of the Audited Financial Statements for FY2007, which is the first complete fiscal year. The work of Carl Selby, the OLC internal auditor, was reviewed with no significant exceptions. Once the October payment is made to the Oklahoma Education Lottery Trust Fund, the funds transferred will surpass a total \$150 million.

ITEM 9

Discussion and Possible Action on FY2007 Year End Financial Audit

After discussion noted above, the board took no action.

ITEM 10

Discussion and Possible Action Regarding a Nominating Committee for Calendar Year 2008 Board of Trustees Officers

Mr. Orbison stated that this board has a tradition that we have a nominating committee to recommend officers for the next calendar year. Mr. Orbison stated he would like the Nominating Committee to consist of himself, Mr. George Charlton and Ms. Charlotte Edwards if they and the board agree. The committee would make recommendations at the December 18, 2007 meeting.

A motion was made by Mr. Paul that the Nominating Committee would consist of Mr. Orbison, Ms. Edwards and Mr. Charlton and the Committee would exist to make recommendations for officers. The motion was seconded by Mr. Charlton.

Roll Call: Mr. Charlton, Ms. Edwards, Mr. Orbison and Mr. Paul voted to approve the motion. The motion was carried.

After additional discussions a motion was made by Mr. Paul to amend the previous motion to include additional duties of the Nominating Committee: to make suggestions for chairman and members of additional committees. Mr. Charlton seconded the motion.

Roll Call: Mr. Charlton, Ms. Edwards, Mr. Orbison and Mr. Paul voted to approve the motion. The motion was carried.

ITEM 11

New Business

Mr. Orbison stated the committee had no new business at this time.

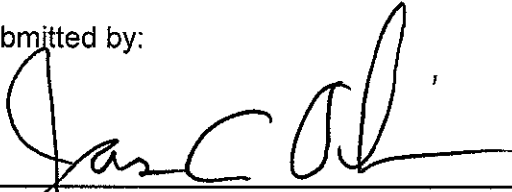
ITEM 12

Adjournment

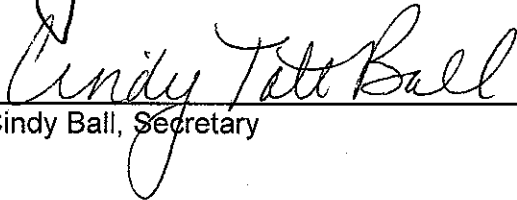
Mr. Paul made a motion to adjourn. The motion was seconded by Ms. Edwards.

Roll Call: Mr. Charlton, Ms. Edwards, Mr. Orbison and Mr. Paul vote to approve the motion. The motion carried and the meeting adjourned at 3:16 p.m.

Submitted by:



James Orbison, Chairman



Cindy Ball, Secretary