

# CALIFORNIA STATE LOTTERY COMMISSION

Minutes – June 27, 2007

Sacramento, California

## **1. Call to Order**

Chairperson John Mass called the public meeting of the California State Lottery Commission to order at 10:04 a.m. at the California State Lottery Headquarters, 600 North 10<sup>th</sup> Street, Sacramento, California 95811.

## **2. Pledge of Allegiance**

John Mass led the Pledge of Allegiance.

## **3. Roll Call**

Mass asked Elisa Topete to call the roll.

### Commission Members Present:

Commissioner Rachel Montes  
Commissioner Manuel Ortega  
Chairman John Mass

### CSL Staff and presenters:

Joan Borucki, Executive Division  
Linh Nguyen, Executive Division  
Don Currier, Executive Division  
Heather Lambert, Executive Division  
Susan Kossack, Executive Division  
Elisa Topete, Assistant to the Commission  
Mary Montelongo, Recording Secretary

## **4. Consider Approval of the Agenda**

Mass asked if any of the Commissioners wanted to make changes to the June 27, 2007 agenda as proposed. Ortega moved to approve the agenda. Seconded by Montes. The motion passed unanimously (3-0).

## **5. Approval of Minutes**

Mass asked if there were any additions or corrections to the May 24, 2007 minutes. Montes moved to approve the minutes. Seconded by Ortega. The motion passed unanimously (3-0).

## **6. Commission Liaison Reports**

### **Commissioner Montes :**

Montes attended The Big Spin® show taping on June 24. Montes also attended the Retailer of the Year event, held June 7 in South El Monte. The retailer has been selling Lottery products since August, 2001 and has sold over \$4.6 million, which means \$1.5 million to education.

### **Commissioner Ortega:**

Ortega was given a status by Security/Law Enforcement (S/LED) Deputy Director, Bill Hertoghe, on vehicle replacements. The division will receive 13 new vehicles to replace existing fleet with more than 100,000 miles. Ortega was updated on the California Peace Officers' Association Gaming and Gambling Sub-Committee, which S/LED is now a part of. Ortega was briefed on the recruitment activities for the open Lottery Agent position located in Fresno, the testing process for the open Supervising Lottery Agent position, and S/LED's participation in the State of California Information Officer (ISO) draft procedures project. Ortega has been updated on several confidential criminal investigations.

### **Chairman Mass:**

As Procurement Liaison, Mass was briefed by staff and requested approval on several projects: an amendment to the Bank of America contract to provide sufficient time to conduct a solicitation and award a new, competitively bid contract, an amendment to the California Council on Problem Gambling contract to revise the scope of service, add funds and extend the current term by one year, and the purchase of a renewal of Cisco Maintenance contracts required for the Cisco Local Area Network equipment for network application routers, switches and firewalls for the period of ten months. As Marketing Liaison, he was briefed by staff on Item 9(e), the Scratchers® Game Profiles.

## **7. Director's Report**

Joan Borucki, Director asked Chief Legal Counsel Don Currier to introduce a new staff member. Currier introduced Kate Killeen, the Lottery's new supervising Deputy General Counsel.

### **a. Incite Workshop**

Borucki reported that staff held an Incite Workshop which was moderated by the Lottery's primary advertising agency, BBDO West. In attendance were Lottery personnel, game vendors and advertising agencies. The purpose was to try to approach a new way to market the Lottery's products and market the overall brand a little differently so staff can form a foundation for a comprehensive marketing strategy. The next steps will be to meet with BBDO West to discuss all the ideas and see what would fit into the Lottery's marketing future.

Discussion by Commissioners.

**b. Website Redesign**

Borucki reported that Daniel Gullahorn, Assistant Deputy Director of E-Communications, will be working on the Lottery's website redesign. The website is one of the most heavily used in state government, but is not user-friendly, is not updated, and is difficult for people to find information. The redesign is aimed to take advantage of progress previously made through Lottery programs such as Jackpot Captains and online second chance draws, which the Lottery currently depends on outside consultants.

Discussion by Commissioners.

**c. Legislative and Outreach Updates**

Heather Lambert, Deputy Director of Legislative Affairs and Outreach, provided the Commissioners with a list of bill summaries. Lambert focused on Assembly Bill 1251, which is the bill to resolve the issue with the MEGA Millions® time frame, and Senate Bill 440, Senator Florez's bill to prohibit the Lottery from joining or running an international or internet-run lottery. Lambert advised the Commission that the State does not yet have a budget for the 07-08 Fiscal Year. The Governor and the Legislature continue to work on the budget and Lambert will provide an update at the next Commission Meeting.

Lambert continues to work with educational and community groups to educate them on the California State Lottery. Staff attended the Greater Los Angeles African-American Chamber of Commerce scholarship luncheon and will also attend state conferences in August for the Hispanic Chamber of Commerce and California Black Chamber of Commerce and will also attend the League of California Cities Conference in September. Erin Sasse, Assistant Deputy Director of Legislative Affairs and Outreach, and Helen Brean, Lottery Agent (S/LED), recently attended the California District Attorney's conference to provide Lottery information to the District Attorneys and Deputy District Attorneys.

In coordination with the Marketing Department, staff is utilizing its contracts with the Major League Baseball teams to acknowledge the California Distinguished Schools regionally. Superintendent of Public Instruction Jack O'Connell and Director Borucki will be attending the events to help celebrate the remarkable schools in pre-game programs.

Montes asked Lambert if a copy of the 2007/10 Business Plan could be delivered to the Chairman of the Senate Organizational Committee. Lambert advised Montes that copies of the Business Plan would be delivered to some of the key legislative offices and committees, including the Chairman.

Borucki updated the Commission on the hearing with Senator Florez regarding the Glendale Hilton Contract. As a result of the hearing, Borucki has asked Currier to look at information regarding ethics and conduct. Currier reminded the Commission

of the memo that was drafted in January concerning staff's ethical responsibilities towards the Lottery. Based on the recent events, Currier will have Legal staff review Form 700 from FPPC, Government codes, the Lottery's own regulations, and a variety of additional items such as training that staff goes through with the Department of Justice's Website. Currier is trying to reconcile those and update a memo to have a one-source document of ethical references to be published yearly to all staff as well.

**d. Facilities Study**

Borucki gave an update on the study that was prepared by the AlfaTech Cambridge Group (AlfaTech) regarding the Lottery's Headquarters facility. The group reported there was quite a bit of maintenance and rehabilitation work that needs to be done on the buildings. The buildings are meant to hold 1,200 people and the Lottery's current staff at Headquarters is over 400 employees. Alfatech was brought in to help the Lottery take a look at the facility and at all the different options that were available to make a recommendation of whether the Lottery should put money into rehabilitation of the building, build something new, or lease a building.

AlfaTech's recommendation was to not rehabilitate the building and remain at this location because of the maintenance, the on-going operational costs, and the size of the building versus the size of the staff that is housed in the building. It was recommended that the Lottery procure a new facility and stay with the ownership option rather than go out and lease. It is still undecided as to whether the new facility will be on-site or look at other properties within a certain geographic area in Sacramento. Sites are also being looked at for the Sacramento District Office as well as a Northern California warehouse, which would free up another huge amount of square footage in this building once they are moved off-site. Staff will bring the item back to the Commission for action once a recommendation is reached.

Discussion by Commission.

**e. Financial Statements for March 31, 2007**

The quarterly Financial Statements are prepared in accordance with GAAP and were distributed to the Governor, Attorney General, State Controller, State Treasurer, and the California State Legislature. The Lottery requested the transfer of approximately \$341.7 million on May 21. The financial statements are included in the Lottery Commission public meeting booklet.

**8. Consent Calendar**

There were no items on the Consent Calendar.

## **9. Action Items**

### a. Approval of Amendment to Prize Assignment Regulations to Conform with Statutes and Define Voluntary and Non-voluntary Assignments

Don Currier, Chief Legal Counsel, reported that staff reviewed the Prize Assignment Regulations and realized that the current regulations were not reflective of current law. The first set of amendments updates the Prize Assignment Regulations to comply with amendments to the statute underlying the Regulations, Government Code section 8880.325(e). The second change is to clarify the language concerning non-voluntary assignments. The current language does not clearly differentiate between voluntary and non-voluntary assignments, which is a necessity so California courts can issue appropriate orders and avoid violating the Lottery Act's restrictions regarding a winner's final three payments. The Regulations are also unclear on the appropriate duties and assignments of a conservator with relation to the Lottery winnings. The change will allow only involuntary assignment of the last three installment payments when the court appoints a guardian or conservator for the purpose of determining ownership or protection of a winner.

Currier also stated there was a technical change to reflect a change in last year's law that restricts assignments to companies insured by the FDIC or a member of the Securities Investors Protection Corporation, known as the SIPC, which is on page 4. The change was done with a typo, the word "notwithstanding," is spelled incorrectly and Currier wanted to make note of it before taking a vote.

Discussion by Commissioners.

Mass asked if anyone from the audience had any questions on Action Item 9(a). No one came forward so he proceeded to the motion of approval.

Ortega made the motion to approve Action Item 9(a). Seconded by Montes. The motion passed unanimously (3-0).

### b. Approval of Amendments to Retailer Regulations regarding Duties of the Director, Applications for Retailer Contracts, and Contract Sanctions by the Lottery

Currier reported that the first amendment defines "Director" in the Regulations as the Director or a designee of the Director. The Regulations require the Director to take most of the actions in the Retailer Regulations. Most of the actions taken against retailers are currently implemented by designees, primarily the Deputy Director of Security and Law Enforcement and the Deputy Director of Sales and Marketing. By defining Director to mean Director or designee, the Regulations permit some of the actions to be taken by designees of the Director rather than the Director herself. It aids in the due process procedures of retailer appeals by showing that the Director is an impartial decision-maker concerning retailer

appeals and is not simply reviewing her own initial decision of terminating the retailer's contract with the Lottery.

The second amendment is a technical change correcting a spelling error by changing "on" to "or."

The third amendment gives the Lottery Security and Law Enforcement Division additional enforcement tools. Currently, the Deputy Director for Security and Law Enforcement has only two options; to either send a warning letter to the retailer or terminate the retailer's contract. There is no middle ground which will allow the Lottery to take action against a retailer while still protecting the business interest of the Lottery. It has led to decreased sales because the retailer's contracts are terminated while their appeal is pending. During the appeal process, the retailer is unable to sell Lottery products, thereby decreasing overall Lottery sales. Once the appeal is heard, if the retailer is approved for probation, it takes several more days before their Lottery terminal is activated, again causing a loss of income for both the Lottery and the retailer. The new addition will give the Lottery an intermediate sanction which will provide for a penalty that is more appropriately tailored to the violation. The addition on page 7 states, "the sanction of suspension as a term of probation and providing for the recovery of supervision costs that come with probation." Staff is asking as a term of probation, that a retailer be told that they cannot sell Lottery products for a finite period of time.

Discussion by Commissioners.

Mass asked if anyone from the audience had any questions on Action Item 9(b). No one came forward so he proceeded to the motion of approval.

Ortega made the motion to approve Action Item 9(b). Seconded by Montes. The motion passed unanimously (3-0).

c. Approval of the Business Plan

Linh Nguyen, Chief Deputy Director, went over key sections of the Business Plan. The Commission was presented with the California Lottery's proposed business strategies at the May 24, 2007 Commission Meeting. After approval, staff began development of the formal Business Plan and put together the strategic direction for the future, given the current state of affairs and the analysis of industry trends. The plan is laid out in seven sections; 1) Introduction, 2) Business Overview, 3) Integrity, Security, Honesty, and Fairness (words taken from the Lottery Act itself), 4) Market Analysis, 5) Performance Assessment, 6) Strategic Vision, and 7) Key Strategic Initiatives.

After careful analysis and the consideration of many options, staff believe the proposed Business Plan captures the following business strategies as approved by the Commission: 1) Focus on long-term planning, 2) Improve brand image, 3)

Shift the jackpot paradigm, and 4) Modernize operations. Approval of the Business Plan will allow staff to begin the process of committing resources and implementing the key strategic initiatives as outline in the Plan (see attached slides). The resources required to implement the key strategic initiatives are incorporated in the Fiscal Year 2007-08 Budget.

Ortega asked Borucki if the Commissioners could be kept updated, either through phone calls or the next Commission Meeting, on the Business Plan timelines.

Mass asked if anyone from the audience had any questions on Action Item 9(c). No one came forward so he proceeded to the motion of approval.

Montes made the motion to approve Action Item 9(c). Seconded by Ortega. The motion passed unanimously (3-0).

d. Approval of Fiscal Year 2007-08 Budget

Borucki reported that the budget process was an interactive budget development process. It took a balance across the different numbers that the Lottery deals with, the development of the sales goals by product, the establishment of the prize funding levels by games, providing funding for the administrative expenses, and ensuring that 34% percent of sales was going to education. Sales are affected by several things including prize payout levels, jackpot levels, marketing efforts, new games, promotions and the economy. As a result, modeling and simulations can never predict future sales with absolute certainty so budget projections and actual sales differ.

For the 2006-07 year, the original budget was at \$3.6 billion. In February, the Commission was asked to take action to revise it downward to \$3.2 billion. The Lottery afterward, had a record \$390 million MEGA Millions® jackpot that allowed staff to put more money into Scratchers® which then drove overall sales. Staff is now estimating the closeout of fiscal year 2006-07 with \$3.3 billion, which brings the education contribution up to \$1.7 billion (see attached slides for sales estimates by product line for 2007-08). The data supports a sales projection of \$3.125 billion, however staff would like to propose to the Commission a sales goal of \$3.35 billion.

For the Administrative budget, each divisional Deputy Director was asked to prepare a 2007-08 baseline budget using functional hierarchy. The Deputy Directors provided comprehensive detail to justify ongoing expenditures. It was reviewed and approved by the Director. Staff then moved to the special projects proposals, which is everything over and above what is needed to keep the games going. The special projects had to be supported by new initiatives that were tied to the business plan. The Administrative expenses overall totaled \$460 million, or 12.4% of projected sales.

Borucki listed four major categories of expense: retailer compensation, game operations, communications, and general administration (please see attached slides). The contribution that is being estimated from next year's budget would equal about \$1.18 or \$1.19 million.

Mass asked Borucki if there was a way to provide incentives through bonuses to the Lottery's vendors. Borucki was going to look at the possibilities and see if it could be included in the next round of contracts.

Mass asked if anyone from the audience had any questions on Action Item 9(d). No one came forward so he proceeded to the motion of approval.

Montes made the motion to approve Action Item 9(d). Seconded by Ortega. The motion passed unanimously (3-0).

e. Approval of Scratchers® Game Profiles for Games 526, 527, 528, 529, 530, 531, 532, 533, and 601

Susan Kossack, Chief of Product and Development, reported on the Scratchers® Games beginning in October. Game 526 is a \$1 game with a Match 3 playstyle and specific variant. The top prize is \$2,500, with overall odds of winning at 1 in 4.97. Game 527, "Fire and Ice" will feature a Key Number Match playstyle. Staff recommends a \$10,000 top prize, with overall odds of winning at 1 in 4.67. Game 528 is a \$3 crossword game utilizing the doubler feature offered in Game 522, "Doubling Star Crossword." The top prize is \$20,000 and overall odds of winning are 1 in 3.27.

Game 529 is a \$5 game with a Key Number Match playstyle offering 16 chances to win a prize on a ticket. The game delivers over \$46 million in cash prizes. Staff recommends a top prize of \$100,000 with overall odds of winning at 1 in 3.53. Game 530 is a \$1 holiday gift tag themed game which features a Match 3 playstyle with a separate "Quick \$10" spot. The game has 12 different holiday scenes and offers a top prize of \$1,000 with overall odds of winning at 1 in 4.71. Game 531 is the \$1 "Golden Goose" animal themed game. The game features a Key Number Match playstyle with an opportunity to double the prize won using a special symbol. The odds for the game are 1 in 5.02 and the top prize is \$1,000.

Game 532 is a \$2 game entitled, "Double It!" The game will be a Match 3 playstyle and will feature four games on one ticket with an additional opportunity to win double the prize with a symbol. The game has a \$12,000 top prize with overall odds at 1 in 4.52. Game 533 is a \$3 holiday bingo-themed game. It will offer a doubler feature and will contain two scenes; a holiday scene and a non-holiday scene. Staff plans to distribute the tickets with the second scene after the holiday bingo tickets are depleted, or when the holiday season has ended. The non-holiday bingo game will extend the game beyond the holiday season. Overall odds are 1 in 3.79 with a top prize of \$20,000. Game 601 is a \$1 game that features a Match 3 playstyle with a separate "Quick \$10" spot. The game

has eight different scenes and offers a top prize of \$1,000. The overall odds of winning are 1 in 4.98. Game 601 is being developed for inclusion in the anticipated "Value Gift Pack."

Mass asked if anyone from the audience had any questions on Action Item 9(e). No one came forward so he proceeded to the motion of approval.

Montes made the motion to approve Action Item 9(e). Seconded by Ortega. The motion passed unanimously (3-0).

### **10. Commissioner General Discussion**

Ortega would like Borucki to arrange for the CEO of Scientific Games to attend a Commission Meeting to discuss the acquisition of Oberthur by Scientific Games.

### **11. Scheduling Next Meetings**

The next Commission meetings are tentatively scheduled for August 15 and November 7, 2007 at the Lottery Headquarters in Sacramento. The times for the meetings will be determined.

### **12. Public Discussion**

Mass asked if anyone from the public had anything to discuss. No one had signed up prior to the meeting and no one came forward, so he proceeded to the next item on the agenda.

### **13. Closed Session**

The Commission convened in a closed session at 11:35 a.m. to confer with and receive advice from counsel regarding pending litigation: California Coalition Against Gambling Expansion, et al. v. California State Lottery Commission; Lee v. California State Lottery Commission; Glendale Hilton Contract; Stone Street Capital, LLC v. California State Lottery Commission

### **14. Adjournment**

Meeting adjourned at 12:08 p.m.