CALIFORNIA STATE LOTTERY COMMISSION

Minutes – August 15, 2007 Sacramento, California

1. Call to Order

Chairperson John Mass called the public meeting of the California State Lottery Commission to order at 10:03 a.m. at the California State Lottery Headquarters, 600 North 10th 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, Director

Linh Nguyen, Chief Deputy Director

Don Currier, Chief Legal Counsel

Heather Lambert, Deputy Director Legislative Affairs & Outreach

Ed Fong, Product Development Manager

Ken Weidmann, Deputy General Counsel

Cathleen Dinubilo, Chief of Internal Audits

Rudy Di Massa, Project Manager

Jim Hasegawa, Deputy Director of Marketing

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 August 15, 2007 agenda as proposed. Joan Borucki, Director, advised Mass of a typo under Action Item C. The agenda item reads, "Approval of Amendment to the Contract of DLA Piper Rudnick Gray Cary US LLP to Extend the Term of the Contract for Six Months." It should read "Eight Months." Don Currier, Chief Counsel, advised the Commission that because there has been no action or updates on MEGA Millions® by the court, there would be no need for a closed session unless an item comes up during the meeting

to require it. Ortega moved to approve the amended 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 June 27, 2007 minutes. Montes moved to approve the minutes. Seconded by Ortega. The motion passed unanimously (3-0).

6. Commission Liaison Reports

Commissioner Montes:

Commissioner Montes attended The Big Spin® show taping on July 22, 2007.

Commissioner Ortega:

Commissioner Ortega reported that he had been briefed on the acquisition of a video enhancement system for use in collecting surveillance video from retailers and improving the quality for the Lottery's investigations. Ortega was also briefed on the acquisition of a new Random Number Generator (RNG) for promotional drawings and raffle games. Ortega was informed of a warrant that was issued and served on former Lottery employee Rich Leeson, charging two misdemeanor counts. Ortega was also informed of a second Underage Gaming Education and Enforcement operation in which all retailers have refused to sell to the Lottery's juvenile decoys.

Chairman Mass:

As Procurement Liaison, Mass was briefed on an amendment to the Cambria Solutions contract to allow sufficient time for Cambria to present its recommendations to the Lottery's Executive staff. Mass was also briefed on the amendment to the University Foundation contract to increase funding to support the Lottery's need for student assistants through June 30, 2008. Mass reported that there was a contract with Human Factors International (HFI), to examine the Lottery's current public website to review and make recommendations to staff.

As Marketing Liaison, Mass was briefed on two promotions, 1) The Quest for the Big Eight Hot Spot, which is a promotion that started on July 15 and increased the 8 of 8 prize pool to run until at least six draws produced 8 of 8 winners and, 2) SuperLOTTO Plus® Xtra Rewards. It started on July 29 and runs through September 1. If a player buys five or more plays, the player receives an Xtra Reward number and winners of the drawn Xtra Rewards number will win \$10,000 (100 winners). Mass was advised by staff on a new idea that the Lottery is pursuing which revolves around a film promotion with a company called "Overture Films." The movie called "Mad Money," comes out in January and stars Katie Holmes, Queen Latifah, and Diane Keaton. The film company requested that the Lottery use the movie as a Scratchers® game promotion and theme. Finally, Mass was briefed on Item 9(e), the Scratchers® Game Profiles.

7. Director's Report

a. CAFR Achievement Award

Borucki congratulated Patt Eberhart, Deputy Director of Finance and Administration, and her staff for being awarded from the Government Finance Officers Association (GFOA), the Certificate of Achievement for Excellence in Financial Reporting to the California Lottery for the Comprehensive Annual Financial Report (CAFR) for the year ended June 30, 2006. It is the fourth consecutive year the Lottery has received this award. Borucki also mentioned that the Lottery will have a booth at the California State Fair, which begins August 17.

b. Legislative and Outreach Updates

Heather Lambert, Deputy Director of Legislation and Community Outreach, updated the Commission on Assembly Bill 1251, carried by Assemblyman Tran. The bill, which would address the MEGA Millions® fix, was held in the Senate Governmental Organization Committee and the Chair had requested some amendments that the Lottery was unable to agree on. It has now moved to a two-year bill and will not be passed this session unless there are some changes or it goes before the Rules Committee. Staff looks forward to working with the Senate G.O. Committee on the bill to try and move it forward. Assembly Bill 1339 is the bill to formalize the Problem Gambling Advisory Board Committee. Problem gambling is very important to the committee, the Commission and the Director and staff will continue to track the bill. The last day for bills to pass to go to the Governor is September 15. Lambert stated that even though the State has not passed a budget, because the Lottery operates outside of the General Fund, the distributions to education, payroll and expenditures are all being paid on time as normal business.

Lambert reported that the Lottery continues to participate in the Major League Baseball events with education. Superintendent of Public Instruction, Jack O'Connell, Joan, some of the local legislators, and area distinguished schools have attended Dodgers, Padres, and Giants games. Staff also plans on attending the Anaheim Angels and Oakland A's games in the future. The events have been very well regarded in the community and the educators and teachers that have attended have enjoyed themselves. The Director and the Superintendent have acknowledged the schools on the field before the game. Some of Lambert's staff is currently at the California Black Chamber of Commerce Conference and will attend the California Hispanic Chamber of Commerce, League of California Cities, California State Association of Counties, California Science Teachers and the California Women's Conferences.

Discussion by Commissioners

c. Audit Plan for Fiscal Year 2007/08

Cathleen Dinubilo, Chief of Internal Audits, went over the process that staff goes through to determine the contents of the audit plan for the upcoming fiscal year,

which is required by professional auditing standards. The plan begins with a review of the prior year audit planning documents, including a review of the current Lottery organization charts and narrative summaries. Potential audit areas, which encompass all the activities that occur around the agency's basic business functions, are then identified. Once identified, staff designs an audit risk model and perform risk assessment and risk ranking for each of the identified audit areas. Staff prioritizes the potential audits by sorting them from highest risk to lowest risk. Staff will then analyze the results to determine if the risk ratings were consistent with what professional judgment would expect. In addition, staff looks at other facts that may influence the timing and necessity of a particular review. This results in the prioritized ranking of audits.

Discussions were held with senior management and Deputy Directors, to obtain important feedback to consider as well as for the planning process. The audit plan covers the 12-month period of July 1, 2007 through June 30, 2008. It incorporates programs from all the Lottery divisions and includes contract compliance reviews for all current Lottery contracts that are over a million dollars that have not yet been audited. In addition, staff will incorporate special projects throughout the year at the request of senior management and continually assess and respond to risks within the organization.

To finalize the plan, Internal Audits considered the available staffing and work hours for scheduled audits identified in the risk assessment, as well as other projects that are done by the department. The audit plan is designed to provide value to the Lottery by focusing on management concerns and high-risk areas identified through the audit risk assessment process.

d. Business Plan Status

Borucki reported that staff went through the Business Plan after it was adopted by the Commission at the last meeting, made all the necessary corrections and had the graphic company put it together more professionally. It is now at the printers and should be completed on August 29, at which time the Lottery will be distributing it to a wide variety of people to keep everyone informed of the upcoming year.

e. Action Plans

Borucki provided the Commissioners with a summary of the individual action plans that have been prepared for each of the action items that were listed under the various initiatives in the Business Plan. Borucki and Linh Nguyen, Chief Deputy Director, meet with the project managers weekly to talk about status, issues or any direction they may need to complete the projects.

Borucki stated that at the last Commission Meeting, Commissioner Ortega expressed an interest in hearing from Scientific Games concerning their acquisition of Oberthur Gaming Technologies (OGT). Tom Hodgkins, Vice President for Governmental Relations and Public Affairs, gave an overview of the acquisition.

Hodgkins went over the period of integration, which was assessing OGT's systems, to create a best-of-breed approach to deliver the best tickets in the industry. One of the systems Scientific Games focused on was the dual-pass technology. The dual-pass system went through an internal investigation and added some quality assurance to the system by investing resources in training personnel, enhancing processes as well as adding additional technology to make sure that staff catches printing errors before they leave or move into the distribution facility.

Discussion by Commissioners

8. Consent Calendar

There were no items on the Consent Calendar.

9. Action Items

a. Approval of Scratchers® Game Profiles for Games 534, 535, 536, 537, 538, and 539 Profiles

Ed Fong of Product Development, presented the December 2007 and January 2008 Scratchers® Game Profiles. Fong advised the Commission of two game profiles that required subtle changes due to a few typos. The two game profiles were approved at the June 2007 Commission Meeting. On Game 526, the total should have been 5,018,052 winners, not 5,018,000. The overall odds and prize pay-outs do not change since the additional 52 winners was so small in quantity to make an impact. The odds and prize pay-outs remain exactly the same. The second change is in the game profile for Game 601. In the line that describes the number of tickets that staff is authorized to print, the amount of 5 million to 100 million tickets is also incorrect. This line should have read "Ticket order quantity may vary between 1 million and 100 million." The number of tickets ordered had no bearing on the odds and prize pay-outs.

Game 534 is a \$1 Match 3 playstyle with a specific variant. The variant is a separate "Quick \$10" spot where players can automatically win \$10 by uncovering a "10" symbol in the play area. The top prize if \$1,000 with overall odds of winning at 1 in 5.45. Game 535 is a "7's" themed \$2 game that will have a key number match playstyle with ten of your numbers to match ten winning numbers. The game has two specific variants, an auto win and a seven times multiplier. The top prize is \$10,000 and overall odds of winning the prize are 1 in 4.35.

Game 536 is called "Instant Hot Spot." Staff recommends the game leverage the equity of the popular California draw game Hot Spot®. Game 536 will sell for \$3 and will offer more play value with the five Hot Spot games on one ticket. There are over \$34 million dollars in prizes with a top prize of \$10,000 and the overall odds of winning are 1 in 3.91. Game 537 is a \$1 game with a Key Number Match playstyle with a variant. The variant is a tripler feature. It has a \$1,500 top prize with overall odds of winning at 1 in 5.21.

Game 538 is a \$2 game that will focus on multipliers as the key visuals. Players can either double or win five times the amount on the prize amount shown by uncovering one of the unique multiplier symbols. It has a Key Number Match playstyle with a top prize of \$10,000 and overall odds of winning at 1 in 4.69. Game 539 is called "Royal 7's" and is a \$3 game with a Key Number Match playstyle that focuses on the use of sevens. The top prize is \$47,777 with an overall chance of winning at 1 in 4.32.

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. <u>Approval of Contract Amendment to Extend Term and to Add Funds for The Big</u> Spin® TV Show Production

Jim Hasegawa, Deputy Director of Marketing, stated that staff is asking for both extending the term for one year, which will run from January 1, 2008 to December 31, 2008, and to add \$2.5 million to the contract expenditure authority, raising the total for this authority on the contract to \$15 million. Jonathan Goodson productions provides broadcast television production services for The Big Spin® television show, such as technical staffing, studio space, studio equipment, talent, closed captioning, and transportation and accommodations for contestants scheduled to appear on The Big Spin®.

As discussed in the 2007 – 2010 Business Plan that was presented to the Commission on June 27, 2007, findings of the recent Brand Audit determined that The Big Spin® has a lot of equity with high recognition. Contemporizing the show and leveraging it to reinforce the new brand image of the Lottery furthers the strategic objectives. A formal solicitation will be issued in Fall 2007 for a new contract to be awarded in 2008 for creative development and production of a new Big Spin® TV show. The extension of the current Goodson contract is being requested to give staff the necessary time needed to develop, circulate, and evaluate the formal solicitation to award a new contract. The additional funding requested is to cover production expenditures during the term extension.

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. <u>Approval of Amendment to the Contract of DLA Piper Rudnick Gray Cary US LLP</u> to Extend the Term of the Contract for Six Months

Don Currier, Chief Legal Counsel, stated the Lottery has a small in-house legal staff and is also advised and represented in litigation by the Office of the Attorney General. To supplement those resources, the Lottery has also contracted with private law firms to be available for expert advice as needed. Pursuant to the Lottery's Competitive Bidding Procedures, contracts for specialized advice such as legal services are not competitively bid. By law, the Attorney General's Office must approve any contract for the services of private counsel. The Attorney General's Office approved the initial contract with DLA Piper. A new approval for an amendment is not necessary. The original contract term was from November 1, 2004 to June 30, 2006 for \$200,000 with the option to extend for two years. This was modified in July 2006 to extend the term of the contract for 16 months until October 31, 2007 and increase the amount of the contract to \$360,000. It left eight months still available to use the full two-year extension option, with no additional funding added to this contract.

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.

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

d. <u>Approval of Amendments to Lottery Regulations Creating an Omnibus Lottery Regulation</u>

Ken Weidmann, Legal Counsel, stated that the original regulations were very game-specific, which led to many different regulations. Within the regulations, many of the sections were the same sections, as far as claiming a prize, how to validate a ticket, or governing law. Because they were in individual regulations, occasionally one regulation would be modified of that section, whereas another wouldn't, which led to inconsistencies between some of the particular games, even though it should be applied uniformly across the board. In creating the Omnibus Regulation, all regulation sections that were the same across the board, have been moved to the beginning of the regulations into "General Regulations." All definitions are now located at the beginning of the regulations and apply across the board throughout the regulations. Weidmann also went over the various inconsistencies regarding trademark symbols, capitalization, spelling and language confusion.

The proposed change addresses the problems of the inconsistent language between the various Lottery regulations. The change also address the need for the Lottery regulations to be general guidelines for Lottery actions with a global view of Lottery actions as opposed to the more specific implementation rules that are now in place. By removing some of the detail of the current regulations, the Lottery is granted greater flexibility in the future for how to operate without having to amend the Omnibus Lottery Regulation further.

Discussion by Commissioners.

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. <u>Approval of Amendments to Lottery Regulations Concerning Claiming a Prize or</u> Award

Weidmann advised the Commission that currently, the language in the Lottery regulations required that a claimant who wants to claim a prize of \$599 or less at the Lottery must complete the information required on the back of the ticket and submit it with a completed claim form. When claiming a prize or award of \$599 or less at a Lottery Retailer, the only requirement is that the player completes the information on the back of the ticket. There is no mention of a claim form needed. When the claimant wants to claim a prize of \$600 or more, the claim can only be filed at the Lottery and a claim form must be filed with the claim.

The regulations are incorrect in requiring the claim form for claims of \$599 or less and this causes confusion when claimants insist that they must fill out a claim form in order to have their claim processed by the Lottery. Removing the language will alleviate the confusion of our players and conform to the processes that are being followed currently in the Lottery offices.

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).

f. <u>Approval of Amendments to Lottery Regulations Concerning Payment of</u> Winnings to a Natural Person

Weidmann reported that the various Lottery regulations give different definitions of who may be paid winnings of Lottery prizes. Some of the regulations only allow payment to natural persons while other regulations allow payment to natural persons or named business entities. By requiring the payment to be to a natural person it ensures that the winnings are tied to that person's social security number and ensures that any offsets against that person will be satisfied before the payment of the Lottery winnings is released. By allowing the winnings to be paid to a revocable trust where the grantor and the winner are the same person, likewise ensures that the payment is tied to the winner's social security number and allows for the payment of any offsets prior to the release of the winnings. It would prevent someone from creating a trust simply to hide their winnings from any offsets for child support or anything else that was filed with the

State Controller's Office. It allows the Director to approve the payments for any of those entities.

Discussion by Commissioners.

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

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

g. <u>Approval of Amendments to Lottery Regulations Concerning Public Disclosure of</u> a Winner's Name

Weidmann stated that the primary purpose for the amendment to the language of the Lottery regulations concerning public disclosure of a winner's name is to protect the unnecessary invasion into the privacy of players. It is also to ensure the uniformity of the language in the regulations. Staff has changed the language to where the winner's name is the only name that may be subject to public disclosure. With the other definitions of claimant, player or contestant, anyone who played the Lottery could have their names revealed.

Individuals who were going to participate in The Big Spin® had their names released under a Public Records Act request because they were a player or a claimant, not officially a winner. It led to some distribution of literature to our players prior to their appearance on The Big Spin® and prior to them being an official winner. It shows that it is an open avenue where players' names could be released prior to them becoming winners. The Lottery is trying to protect the winners' names and it will now just be "winners."

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

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

h1. Approval of Amendments to Raffle Game Regulations

Weidmann stated that the final four to five pages of the current raffle regulations concern the specifics of the Million Dollar Raffle from last year. In order to use the regulations for more of a guidance, staff is eliminating those specific pages. The new language will allow for the implementation of new Raffle games without a need to amend the Omnibus Lottery Regulation each time a new game is introduced. Language has been inserted so that the Game Profile for any new raffle game, which is not materially similar to a past Commission-approved raffle game, will be submitted to the Commission for approval.

h2. Approval of Game Profile for the New Year's Raffle Million Dollar Game Rudy DiMassa of the Business Planning Office, presented the new game profile for the second Lottery raffle game. DiMassa stated the Lottery held its first raffle in March and although the game did not sell out, it was a success because it sold 3.9 million of the 5 million available raffle numbers. The Lottery raised approximately \$5.7 million for public education. The game generated considerable interest on the part of both the players and retailers.

The Lottery's second raffle game, New Year's Million Dollar Raffle, will be tied to the New Year's holiday and it will be a key component of the Lottery's 2007 holiday product offerings. The game is also a part of the Lottery's 2007 – 2010 Business Plan that was approved by the Commission on June 27, 2007.

In an effort to improve on the first raffle game, staff conducted a thorough review of the Lottery's experience with the Million Dollar Raffle game as well as an analysis of industry best practices. Based on this analysis as well as the results of an internet survey conducted by the Business Planning Office, staff feels strongly that the Lottery should offer a new raffle game that is more similar to those that have sold out in other states.

Game sales will begin on November 19, 2007 and end at midnight on New Year's Eve or when the game sells out, whichever occurs first. The tickets will have a \$20 price point and each ticket will contain five raffle numbers. There will be a total of 650,000 tickets, containing a total of 3.25 million raffle numbers. The Lottery is going to offer five guaranteed \$1 million cash prizes. There will also be 50 prizes of \$10,000 and 500 prizes of \$2,008, which are tied to the new year. The Game Profile will offer players better odds of winning any prize than the first Raffle game did. The odds of winning \$1 million on a single \$20 purchase will be 1 in 130,000 and the odds of winning any prize will be 1 in 1,171. If the game sells out, it will generate \$13 million in revenue and at least \$4.4 million for public education.

Mass asked if anyone from the audience had any questions on Action Item 9(h1 & h2). No one came forward so he proceeded to the motion of approval.

Montes made the motion to approve Action Item 9(h1 & h2). Seconded by Ortega. The motion passed unanimously (3-0).

i. Approval to Purchase Real Property in West Sacramento for the Northern California Distribution Center

Borucki reported that the Lottery engaged an independent consultant, Studley, to assess the Lottery's needs and provide recommendations for efficiencies and financially viable solutions for the Lottery's distribution centers. One of the issues raised by Studley was regarding the Northern and Southern California warehouse operations and the limitations the warehouses were putting on the Lottery's ability to expand the business. Studley provided a list of

recommendations concerning the Lottery's warehouse operations and inventory control.

Staff has been working with brokerage firms to look for new properties and the Business Planning Office is doing an analysis of lease versus purchasing of facilities. With the exception of the headquarters building, the Lottery has been engaged in leasing properties, which has not been the best operationally or financially. Therefore, the Lottery would like to own its facilities and purchase real property in West Sacramento for the Northern California Distribution Center. The property would allow the Lottery to move forward with the warehousing improvements and be sized more appropriately. It would allow the Lottery to get out of an additional warehouse that is leased just north of the existing facility, thereby cancelling that lease and consolidating it into one Northern California Distribution Center. The property has a purchase value of \$4.9 million. The purchase was anticipated when the budget was adopted in June and will allow staff to make the necessary facility improvements. The current warehouse needs some basic fire, life-safety improvements so it will allow the Lottery to incorporate it all into the new facility.

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

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

j. <u>Approval to Purchase Real Property in Sacramento for the Sacramento District Office</u>

Borucki reported that the Sacramento District Office has occupied space at California State Lottery Headquarters for the last 12 years. The location is only 5500 square feet and has a very small warehouse that cannot accommodate the number of Scratchers® games offered or the number of point-of-sale items that the district office needs to maintain. An appropriately sized and priced building has been located on East Commerce Way in North Natomas. The property has prominent visibility from Interstate 5 and Arco Arena in an easily accessible portion of Sacramento.

Staff would like to start using the district offices for advertising opportunities. Because it is close to Arco Arena, Borucki would like to see promotional events on the night of the Kings games out in the parking lot. The Lottery will take advantage of the real estate and put it to good use for more than just housing the employees. The property is a larger facility and brand new at a purchase cost of \$2.37 million. With a larger facility, there will be better opportunities to hold press conferences on Lottery winners. With the new office and the template put together by Patt Eberhart and her staff on improvements to the office, it will afford us those kinds of media opportunities in the future.

Tenant improvements totaling approximately \$450,000 will need to be made because it is currently an empty building. The tenant improvements will include a security system, telecom cabling, and some modular furniture. It should be done rather quickly once the Lottery gets through the due diligence in acquiring the property.

Discussion by Commissioners.

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

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

10. Commissioner General Discussion

Commissioner Montes wanted an update on the Orange County Fair. Tricia Metzger, Deputy Director of Sales, reported that it was the best year ever for attendance as well as sales. Scratchers® sales were very good, especially the \$5 game. Sales were up 27.4% over last year. Draw game sales were up 64%.

11. Scheduling Next Meetings

The next Commission meeting is tentatively scheduled for October 16, 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

There was no Closed Session

14. Adjournment

Meeting adjourned at 11:40 a.m.