

# CALIFORNIA STATE LOTTERY COMMISSION

Minutes – December 3, 2008

Sacramento, California

## **1. Call to Order**

Chairperson John Mass called the public meeting of the California State Lottery Commission to order at 10:00 a.m. at the 600 North 10<sup>th</sup> Street, Sacramento, CA 95811.

## **2. Pledge of Allegiance**

John Mass led the Pledge of Allegiance.

## **3. Roll Call**

Mass asked Elisa Topete to call the roll. Mass publicly thanked Rachel Montes for her years of service as Commissioner of the California State Lottery.

### Commission Members Present:

Commissioner Manuel Ortega

Commissioner Cynthia Flores

Chairman John Mass

### CSL Staff and presenters:

Joan Borucki, Director

Kate Killeen, Acting Chief Legal Counsel

Richard Woonacott, Deputy Director of Legislative Affairs & Outreach

Bill Hertoghe, Deputy Director of Security/Law Enforcement

Susan Kossack, Deputy Director of Marketing

Jim Hasegawa, Deputy Director of Business Planning

Roberto Zavala, Chief of Internal Affairs

Sandra Lane, Manager of Experiential Marketing & Broadcasting

Elisa Topete, Assistant to the Commission

Stephanie Greenlee, Recording Secretary

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

Mass asked if any of the Commissioners wanted to make changes to the December 3, 2008 agenda as proposed. Joan Borucki, Director, postponed Item 9(e), New Headquarters Design Contract, for the next meeting to allow for public review of the environmental document. Flores moved to approve the amended agenda. Seconded by Ortega. The motion passed unanimously (3-0).

### **5. Approval of Minutes**

Mass asked if there were any additions or corrections to the October 15, 2008 minutes. Ortega abstained from voting on the agenda because of his absence at the last Commission Meeting. No motion was made because of the lack of a quorum.

### **6. Commission Liaison Reports**

#### **Commissioner Flores:**

As Audit Liaison, staff updated Flores on the State Controller's Office (SCO) six open audits: the Office Revolving Fund, CAL-Card Program, Draw Observation Program, Fleet Management Program, GTECH Contract, and the Fourth Quarter Transfer Review, which started on September 2, 2008. The SCO issued draft audit reports for the Office Revolving Fund and Draw Observation Contract audits. The Lottery responded to the draft audit reports and is awaiting the reports to become final. The SCO continues to perform the field work on the CAL-Card program and the Fleet Management program and on the GTECH contract and the Fourth-Quarter review. The KPMG audit began on June 30, 2008, with financial statements on October 16, 2008. The audit rendered an unqualified opinion. KPMG will continue to review additional information for the comprehensive annual financial report that is going to be due December 31, 2008.

Discussion by Commissioners.

#### **Commissioner Ortega:**

Ortega reported that Bill Hertoghe, Deputy Director of Security/Law Enforcement Division (S/LED) attended the NASPL Security Subcommittee meeting in St. Louis. S/LED investigators are working with the Los Angeles Police Department (LAPD) on a cold-case homicide from 1986. LAPD has requested assistance in tracking a Lottery ticket found on the homicide victim.

District Sales Representatives have reported seeing more illegal slot machines in Lottery retailers in Los Angeles. S/LED Investigators are working with LAPD Vice and Department of Justice (DOJ) Gaming to locate the supplier of the machines. S/LED Investigators assisted the FBI and DOJ Gaming with a surveillance operation and eventual arrest of several suspects for operating an illegal lottery in the Central Valley.

Ortega was notified of the pending retirement of Lieutenant Bob Rogers and Investigator Al Romero. The two had more than 40 years of Lottery experience and nearly 80 years of law enforcement background.

#### **Chairman Mass:**

As Procurement Liaison, Mass was briefed by staff and requested approval on an agreement with Technology Integration Group for Dell EqualLogic Storage Area Network (SAN) to replace the existing SAN including three years of Dell support and

next day delivery of replacement parts for the total amount of \$223,683.13, including sales tax.

As Marketing Liaison, Mass was updated by staff in writing, on the Happy Cows Scratchers® co-promotion with the California Milk Advisory Board. The Lottery continues the second chance consumer promotion where players can win one of five \$1,000 prizes by entering non-winning tickets. The final drawing will be held the week of December 8 and 66,000 entries have been received to date.

The Lottery is conducting the "Let it Dough" holiday tour with 30 events throughout California top selling retailers. The promotion educates consumers on the Lottery's new holiday games and gives them the opportunity to participate in the famous holiday whirling Snow Globe. Consumers can purchase \$20 in Lottery products to enter in the Snow Globe to grab for Lottery coupons redeemable for Lottery tickets and gift cards. Lastly, Broadcast Director Sandra Lane, will be presenting the exciting highlights of the Lottery's new TV Game Show, "Make me a Millionaire" which debuts January 17, 2009.

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

### **a. Financial Statements for June 30, 2008**

Borucki reported on the Financial Statements for June 30, 2008. Pursuant to Government Code section 8880.43, an independent firm of certified public accountants will conduct an annual audit of all accounts and transactions of the Lottery. The financial statements are prepared and have been distributed to the Governor, the Attorney General, the State Controller, the State Treasurer, and the California State Legislature. The Lottery requested the final transfer for the last fiscal year to education, which brought the total amount transferred to the Lottery education fund for fiscal year 2007-08 to \$1,094,945,000. The report is now public and will be published on the Lottery's Web site.

### **b. Sales Update**

Borucki and Jim Hasegawa, Deputy Director of Business Planning, presented a comprehensive sales update. During the Lottery's 23 years, it has seen periods of sales growth and decline. First-year sales were at \$1.76 billion; and the lowest fiscal year's sales were in fiscal 1992, at \$1.358 billion. The highest sales were in fiscal year 2006, at \$3.58 billion. Some of the key reasons for growth have been product improvement in terms of higher prize payouts. The other key strategy has been a strong and continuous marketing effort; not just the launch of a new product, but being able to support it on an ongoing basis to build that product's brand image.

Scratchers® game sales more than doubled between fiscal years 1997 and 2000 with the higher prize payout strategy. The year before the strategy started, sales were at \$525 million and by fiscal year 2000, sales were nearly \$1.2 billion as a result of putting more prize money and making the product better. The next period where sales grew was from fiscal year 2003 to fiscal year 2006. Additional dollars were available to fund

more prize pay-outs due to lower costs associated with a new GTECH gaming contract. Borucki stated that it was a strategic move to take that one-time savings and put it into the prize fund, which allowed the Lottery to increase prize pay-outs. Also during that time period, the growth in the \$3 Scratchers® was principally because the Lottery started using Bingo. Bingo was one of the themes that originally was restricted, but the Legislature gave the Lottery the authority to use it. Borucki noted that in the Business Plan, one of the five restrictions that the Lottery would like to see lifted is “themes.”

Hasegawa said the mandate to have 34 percent of sales going to education limits the amount of funding available for such programs as higher prize payouts in the Scratchers® area or for strong and continuous marketing campaigns. In the private sector, a real business would probably invest in proven sales builders. They would be driven by growing the bottom line dollars rather than maintaining a fixed percentage of profit. The Lottery has fallen behind in the industry because it has not been able to maximize these strategies in terms of higher prize payouts and the marketing support.

Industry sales and profits have grown dramatically in the past several years, primarily in the Scratchers® area because of \$5, \$10, and the introduction of \$20 and in some cases, even higher price points. A higher prize payout is needed because people buy a \$10 or \$20 product because it is a better value proposition. This is what has driven the successes in other lotteries. Because the California Lottery has not been able to maximize these strategies, fiscal year 2007-08 had the largest sales decline of any of the lotteries in the U.S., about 15 percent. Borucki stated that even with the decline, the Lottery still had the seventh highest sales in the country; producing the third largest profit in terms of dollars with sales of \$3.05 billion. New York was number one and Florida was number two in profits. Both states do not have the restrictions that California has on the prize payouts, and those states have seen tremendous growth in Scratchers® sales.

Prize payout relief has been known to be a crucial component for the long-term success of the Lottery. As early as 2001, a bill has been in the Legislature to increase prize payouts. That year, Senate Bill 930 went to a floor vote, but did not reach the two-thirds majority necessary. As a result, there have been other bills introduced to remove the restriction. Because there has been no change in the law, schools have ultimately lost some potential money. If the Lottery could sell more products that people want, sales would go up and the dollar amount going to public schools would dramatically increase.  
Discussion by Commissioners.

Hasegawa stated that MEGA Millions® is similar to the changes that were done to the SuperLOTTO Plus® product, in that if the Lottery was able to obtain more sales from a more profitable game, that would be able to fund additional marketing programs as well as put more dollars into more Scratchers® prizes and, therefore, increase total sales even further. The impact of MEGA Millions® had a much shorter-lived impact than anticipated. The jackpot fatigue quickly set in as large jackpots came about, such as \$100 million jackpots. Those jackpots became very common and people became desensitized to it much more quickly than anticipated.

Hasegawa went over sales from the financials of the current fiscal year. Total sales for the first four months amounted to \$985 million. Last year at this same time, sales were at about \$1,090,000,000, which is down approximately 10 percent. The decline is coming from the jackpot games of Super LOTTO Plus® and MEGA Millions®, which together have a 26 percent decline in sales. Hasegawa stated that there were far more big jackpots last fiscal year for both of these games. Players are winning at the lower jackpot levels. The pattern that is seen is that sales are very slow until the jackpot gets to a certain level, and then sales grow dramatically.

The Scratchers® games are at \$555 million this year, down 2 percent compared to last year at this same time. For the daily games, with the addition of Daily 4, year-to-date sales are up about three percent. While Daily 3® is down relative to last year, the total of Daily 3® and Daily 4 out-sell what Daily 3® alone brought in last year. Hot Spot® sales continue to decline as they have for the last couple of years. It is down seven percent relative to the same period last fiscal year. Borucki stated that Hot Spot®, in addition to the Scratchers®, is a product that would greatly benefit from having prize payout relief as well as being able to offer fixed prizes in this venue as well. Hasegawa stated that many of the other lotteries are showing a decline in sales this fiscal year. About three-quarters of U.S. lottery jurisdictions had flat or declining sales in the period of July through September. Even Las Vegas is also showing recent declines in gaming revenue and visitor volumes.

From January to June, various strategies and tactics will be employed by the Lottery such as the new television show. Staff will continue to develop no-cost or low-cost promotions, such as Happy Cow Scratchers®, Mad Money and the free-gas give-away. Such promotions helped stretch the marketing budgets because other people helped promote the Lottery product. Earned media was also generated in the press by these types of events. Later in the fiscal year, the Lottery will be launching the second-chance draws for all of the Scratchers® games. Finally, pursuing administrative efficiencies such as eliminating some manual processes in the back office system will make the Lottery more efficient resulting in some cost savings.

#### Discussion by Commissioners

Borucki introduced new employees; Richard Woonacott, Deputy Director of Legislative Affairs and Outreach, Bill Ainsworth, Deputy Director of Communications, and Alex Traverso, Assistant Deputy Director of Communications.

#### **c. Legislative and Outreach Updates**

Woonacott stated that approximately 31 new Legislative Members were sworn in December 1. The new Senate G.O. Chair will be Rod Wright of the Los Angeles area. Two particular pieces of legislation that made various technical and statutory changes to the Lottery in order to implement the 2008-09 Budget Act, were both Assembly Bill (AB) 1654 and 1741. Specifically, AB1654 provided us the opportunity to modernize our operations and improve financial performance by providing flexibility for increase and

decrease of prize payouts. AB 1741 was the securitization measure. Both measures will be up in June, 2010.

**d. Consumer Protection Update**

Bill Hertoghe, Deputy Director of S/LED, reported that there have been a few more retailer terminations as a result of the undercover operations. Hertoghe provided some initiatives of the Consumer Protection Strategic Plan. K-9 is an alert system that GTECH has that notifies the Lottery in real-time, if there is aberrant wagering activity. This is to protect the retailer from clerks who might be playing the Lottery but not paying for it. S/LED also investigates quite a bit of embezzlements.

Staff is on schedule to have 100 percent Check-A-Ticket capability in stores that will support the Check-A-Ticket terminal. The PDF bar code that indicates the dollar amounts on the Scratchers® tickets are soon to be in every Scratchers® the Lottery produces. The technology already exists on the Lottery's online games, so a consumer can go into the Check-A-Ticket and find out whether or not they are a winner and what dollar amount.

Hertoghe advised that the sting operations are continuing and are being run out of Headquarters, with an undercover operation team supported by local Lottery agents at the different district offices. S/LED is working on having the undercover operations run out of the districts with an adjacent investigator going over to assist. Staff expects to see more arrests in January and February. Discussion by Commissioners. Staff is also more closely scrutinizing retailers who file claims. On the claim form, it now says you have to self-identify if you are a retailer or if you work for a retailer, so it has dramatically increased the number of investigations. It has reduced the number of what is presumed to be the number of insider fraud at the retailer level and the clerk level. Discussion by Commissioners.

Mystery Shopper is a retail firm that would be hired by the Lottery. The shoppers or "auditors" as they call themselves, may go into a retailer to redeem a ticket or buy a ticket and then report on that shopping experience, not only to S/LED but to Sales and Marketing. The auditor would report on security issues as well as providing information on that particular store such as if the terminal was facing the correct way, if the store was clean, and if they were treated properly. The Mystery Shopper is still in the exploration state, and is still at staff level.

The Lottery Scam Awareness is proceeding well. The "Don't be a Victim" brochure has been updated and will be going to all the retailer outlets as well as the Lottery's Web site. S/LED is working with the Lottery's Information Technology staff in trying to develop a security link and also a Consumer Protection side. Hertoghe reported on Retailer Sanctions, specifically retailer probation, which is monitored by S/LED and paid for by the retailer. Staff is working on consistency with the sanctions, almost like a bail

schedule. When the Director sees a retailer appeal, she would also like to see what S/LED's position has been in prior sanctions of a similar nature so that the Lottery is consistent.

Discussion by Commissioners.

Borucki advised the Commission that the Lottery has a contract with CVS Pharmacies and will be expanding to 348 stores in Southern California.

**e. Make Me a Millionaire TV Show Update**

Borucki introduced Sandra Lane as the project manager for the new TV game show. Lane did a terrific job in an incredibly short time to get the TV show up and into production. The first taping will be December 14 and will air on January 17, 2009. Borucki thanked Lane and all the staff for the incredible amount of work that has been accomplished. Lane stated that the new TV game show will be showcasing the Lottery as a fun, exciting, and entertaining product. The show is supported by the Make Me a Millionaire® ticket, which sold over 600,000 the previous week; and more than The Big Spin® ticket. Total sales are over \$1.1 million for both tickets. Consumers who have won the "Aces High" on The Big Spin® will have an opportunity to choose to go to the Make Me a Millionaire® show.

A study was done approximately two years ago, and it was discovered that The Big Spin® lacked entertainment and excitement value. The Lottery also learned that players loved the prospect of being on TV and game shows are currently very popular. Staff had great potential to use the show to create a positive image for the brand and to use the TV time slot to develop viewership and appeal to new players. The company producing the show is 3Ball Productions, which has also created "The Biggest Loser," "Beauty and the Geek," and "Age of Love." Milestone Entertainment is also a producer experienced in lottery game shows worldwide.

There are a variety of ways to go to the show: Make Me a Millionaire Scratchers® ticket, Fantasy 5 coupon, and the Holiday Bonus Promotion. All non-winning holiday and Make Me a Millionaire Scratchers® tickets can be entered online and Draw Management staff will draw from those tickets three times, ten winners each. There has been over 300,000 entries for the Holiday Bonus promotion. Staff will continue to develop a variety of ways to go to the show.

Lane provided information on the shows four different games: Lucky Penny, Safe Cracker, California Cool, and Millionaire. Lucky Penny has a minimum prize of \$2,000 and a maximum prize of a car. Staff is negotiating with General Motors for a fuel-efficient, American-made car. Safe-Cracker has a minimum prize of \$2,000, with a maximum prize of \$92,000. California Cool players can win from \$5,000 to \$200,000. Millionaire players can win a minimum of \$10,000 and the top prize will start at \$1 million. It is a progressive jackpot, so every week that it is not won, \$200,000 will be added to the prize. Lane went over the specifics of each game.

The set and play design will add fun and excitement to the show supporting the re-branding efforts of the Lottery. The goal is to create a “prime time” look and feel for the show. Staff plans on introducing new games over time to keep the format fresh and exciting. Ortega asked how the names are selected to be on the show. Lane explained that Draw Management has put together an extensive draw process that will be a random draw. Draw Management and the auditors will maintain possession of names and random numbers until players are available each taping. The numbers/names will be taken to the first show taping where they will be announced from game to game. Lane thanked Jeff Aills and Karen Alexander for their work on the draws. The host of the show will be Mark L. Walberg, who is the host of “Moment of Truth” and the “Antiques Roadshow.”

Discussion by Commissioners

**f. Report on “Who Plays the Lottery”**

Hasegawa stated that the Lottery had a contract with UCLA to conduct a study on who plays the Lottery. The two professors who conducted the study were Ed Leamer, Professor of Economics and Statistics, and Don Ylvisaker, an emeritus Professor of Mathematics.

In general, Lottery sales reflect the statewide population. This is particularly true in terms of household income and ethnicity.

In terms of the largest differences observed, lottery spending varies by age group. Per capita sales increase as people get older peaking among 55-64 year olds. This coincides with the fact that people’s peak earning years and maximum disposable income are between the ages of 45 to 64. A significantly greater share of Lottery sales comes from those in 45 to 74 year old age group. While they represent 40 percent of the adult population in California, 55 percent of Lottery sales come from those age groups. On the other hand, 18 to 34 year-olds represent 33 percent of the adult population and only about 19 percent of Lottery’s sales.

Going by product, Scratchers® accounted for just over 50 percent of sales last year; and the preference of games by different age groups varies dramatically. The 18 to 24 year-olds and 25-34 year-olds prefer the Scratchers® product because it fits their lifestyle better since it is much more of a convenient product. Scratchers® can be bought and played at anytime and provides instantaneous results. In contrast, among Californians that are 55 or older, the plurality of their dollars goes to the jackpot games. These games have more rules - the draw happens at a specific time and on a specific day.

The second largest difference that UCLA found comes in geography. The highest per capita sales come from two counties; Los Angeles and Orange County. These two counties represent about 36 percent of the state’s population, but 42 percent of Lottery sales come from there. This geographic information shows the importance of winner awareness and how it impacts the Lottery’s brand image and ultimately sales.

Previously, most of the winner awareness information from earned media was in the Los Angeles market, which has the largest population. As such, many of the Lottery's jackpot winners do come from the Los Angeles area. Discussion by Commissioners.

Borucki stated that because there are more players in the Los Angeles and Orange County areas, there is a higher probability of generating more winners. Those winners will generate the publicity, which then generates more sales. The Lottery would like that to happen to the rest of the state. Hasegawa stated that staff doing more publicity about all the different types of winners throughout the state. Once people hear about winners, there does seem to definitely be a correlation with their image of the Lottery and therefore, ultimately with sales.

The UCLA Study found fewer differences when looking at other demographic characteristics. For example, in terms of income, outside of those who reside in areas where the median household income is greater than \$70,000, Lottery sales reflect the distribution in the state. Approximately 23 percent of the population resides in areas where the median household income is between \$40,000 and \$50,000, and the Lottery is getting about that same percentage in sales from that group. This same conclusion can be said about ethnicity and Lottery sales.

In terms of the methodology used in this study, UCLA used Winner Claim Forms submitted between March 2004 and March 2007. Winners are required to report their age and an address so that the check can be mailed to them. The study does not look at where the ticket was bought, but where the person resides. Calculations of sales for age and address are based on the statistical odds of winning that prize, because winning a Lottery prize is randomly distributed. UCLA combined the census data with the Lottery data from the claim forms to infer sales levels for the various populations based on income, ethnicity, education, and so forth.

Discussion by Commissioners

Borucki updated the Commissioners on the Lottery's Headquarters building. Over the last few months, the building has had problems with odors and mold. Air and swab testing was appropriately completed throughout the building, not just in the locations where the odors were coming from. Some of the areas tested positive for mold and cleanup is either underway currently or has already been completed. The issue did require the relocation of some staff as a precautionary measure. There is no health and safety issues currently for the staff, but affected areas are continuing to be found. As those areas are found, retesting will be done and staff will either be moved to another area of the building or the necessary clean-up will be done. Staff will continue to test on a routine basis and provide the air scrubbers that are needed to rectify the situation as well.

### **8. Consent Calendar**

There were no items on the Consent Calendar.

## **9. Action Items**

a. Scratchers® Game Profiles for Games 587, 588, 589, 591, and 592 and Alternative Profiles for Future Games

Susan Kossack, Deputy Director of Marketing, presented the Scratchers® games to be launched in April and May 2009. Game 587, "Diamond Dazzler" is a Match 3 playstyle with a specific variant, using diamonds as the graphic theme. The top prize for the \$1 game is \$1,000 and the overall odds of winning are 1 in 5.38. Game 588 is a collaboration between the Lottery and the California Peace Officers' Memorial Foundation (CPOMF). Ticket graphics will pair CPOMF's logo with fresh lottery-industry designs. The Lottery will compensate CPOMF for the use of its properties through licensing fees based on the number of tickets sold (total fee amount not to exceed \$300,000). CPOMF will dedicate \$100,000 in strategic marketing to promote the game. The \$2 game utilizes a Key Symbol Match playstyle with an auto-win feature. The top prize is \$10,000 and the overall odds of winning are 1 in 4.70.

Game 589 is a \$1 Key Number Match playstyle featuring hot-food themed graphics, which is very well received during the Cinco de Mayo season, with a doubler feature. The game offers a spicy \$500 top prize which allows prizes to be claimed at retail locations. The odds of winning any prizes are 1 in 4.88. Game 591 is a \$2 game that offers a Key Number Match playstyle with two specific variants. It offers over \$18 million in cash prizes with a \$10,000 top prize and overall odds of winning are 1 in 4.49. Game 592 is a \$3 poker-themed Scratchers® ticket featuring fresh and trendy graphics. Players scratch off the "Your Hands" area and if they beat the "Dealer's Hand" they win the indicated prize. Players can win up to six times and the top prize is \$25,000 with overall odds of winning at 1 in 3.95.

In light of the possible pay-out legislation relief, staff is proactively developing alternate game profiles with higher prize payouts to provide players with increased winning experiences. It represents another positive step in the direction towards a new and improved Lottery, and focuses on creating more winners throughout California. The approval of these game profiles will provide staff the ability to implement these higher payout prize structures into the Lottery's game portfolio "tool chest" as soon as legislation is lifted.

Alternate Game Profile A will be a \$1 game with a Key Number Match playstyle with a tripler feature. Players have a chance to win a \$1,000 top prize with overall odds of winning at 1 in 4.67. Alternate Game Profile B will be a \$1 game with a Match 3 playstyle with a specific variant and a \$500 to prize. The overall odds of winning are 1 in 4.82.

Alternate \$2 Scratchers® Game Profile will be a Key Number Match playstyle with two specific variants, 5X and 10X multipliers. The game will have a \$20,000 top prize and overall odds of winning are 1 in 4.01. Alternate \$3 Scratchers®

Game Profile will be a Key Number Match playstyle with three specific variants, 2X, 4X, and 8X multipliers. The top prize will be \$50,000 and overall odds of winning are 1 in 3.65. Alternate \$5 Scratchers® Game Profile will utilize a Key Number Match playstyle with 10X and 20X multipliers and a Fast \$50 spot. The top prize will be \$100,000 with overall odds of winning at 1 in 3.48.

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 Flores. The motion passed unanimously (3-0).

b. Lottery Regulation Amendments

Kate Killeen, Acting Chief Counsel, proposed updates to the Regulations that would remove or revise unnecessarily restrictive language, allowing the Lottery to be more responsive to the marketplace and the needs of its customers. The first one pertains to Section 1.2, at page 23 of the existing regulations which would merely add that if a draw is interrupted or disrupted due to system problems, the Director shall determine the appropriate corrective action to take. All tickets which were originally eligible for the draw shall remain eligible. It would essentially bring these regulations online and consistent with other regulations that are already in place for other games, such as Hot Spot®. It reflects the reality that if a draw disruption occurs, a remedial decision must be made to address the situation and protect the player eligibility in the system.

The second regulatory proposal is pertaining to Section A.4.c, which deals with the time period for investments that support annuitized prizes. It reflects the reality of the investment process in that due to East Coast-West Coast time zone differentials and other investment-related timing factors, investments cannot always be made immediately on the next business day. This would merely add "as soon as feasible" to the regulatory language. The third regulation change, Section C.10.a, deals with Lottery sales directly to the public. The Lottery Act, under Government Code Section 8880.33, allows the Commission to regulate the sale of Lottery tickets directly to the public. The current regulation has a limitation for Lottery sales directly to the public on two promotional sponsorship circumstances, which are unnecessary. The regulation would merely remove the confining context so that the Lottery would have greater flexibility in going forward with new business models. It could offer a kiosk that is staffed by Lottery employees in a transportation terminal for instance, and would help create a regulatory environment that is broader and more flexible.

Finally, the last revision is the Competitive Bidding Procedures, Section S.2.b. The revision would expand the list of pre-qualified bidders that the Lottery is already allowed to use, which are developed by other government agencies, to also include county and local lists of pre-qualified bidders. It would provide the

Lottery with additional resources of renewable and competitively bid vendors that can be chosen for the best value and can best meet our needs.

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.

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

c. KPMG LLP Contract Extension for Financial Services

Roberto Zavala, Chief of Internal Audits, stated that the Lottery Act requires the Lottery to contract with independent Certified Public Accountants (CPAs) to conduct annual audits of the financial statements. The financial statements are due 120 days after the fiscal year ends or by October 31. Currently the Lottery has a contract with KPMG that started on January 21, 2006, and will expire on December 31, 2008. According to the contract terms, the Lottery may unilaterally extend the contract for up to two additional one-year terms. Lottery staff has been satisfied with KPMG, who have provided on-time reports and professional service. KPMG requested that both one-year options be exercised concurrently. KPMG would receive a nominal three percent increase for the first year and then the following year. Exercising the two one-year options concurrently will provide the Lottery the best value. Past annual increases were at six percent. Approving the extensions concurrently will add \$289,000 and extend the contract to December 31, 2010.

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 Flores. The motion passed unanimously (3-0).

d. Establishment of an Audit Committee

Zavala advised the Commission that the State of California has passed legislation, Senate Bill 1452, which requires any governing body that oversees a state agency that performs internal audits to establish an audit committee. The Audit Committee can assist the Commission in its oversight responsibilities by providing guidance in the areas of financial statements, making sure that the Lottery is complying with legal and regulatory requirements, and also look at the qualifications of the Internal Audits office, the Chief of Internal Audits, and also independent auditors. If approved, Lottery staff will assist the Commission on nominating members and a chairperson at later meetings.

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.

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

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

Commissioner Flores asked Director Joan Borucki for a status on obtaining a fourth Commissioner with a financial background. Chairman Mass asked Borucki to contact the Appointments Secretary for an update on a Commissioner.

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

The next Commission meetings for 2008 are tentatively scheduled for January 28, March 18, April 15, May 20, July 8, August 19, October 21, and December 3 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 12:05 p.m. to confer and receive advice from legal counsel regarding pending litigation (including adjudicatory proceedings, potential litigation exposure or initiation): Tom McVeigh v. California State Lottery; Lorenzo Wheeler v. California State Lottery; Sales and Use Tax Issues.

### **14. Adjournment**

Meeting adjourned at 12:30 p.m.