

MINUTES

ARKANSAS LOTTERY COMMISSION

**Wednesday, February 19, 2014
10:00 a.m.
124 West Capitol Avenue, Third Floor
Little Rock, Arkansas**

Call to Order

Chairman George Hammons called the meeting to order. Commissioners Smokey Campbell, Julie Baldrige, Dianne Lamberth, Raymond Frazier, Bruce Engstrom, Mark Scott, and Doug Pierce were also present. Staff members present included Director Bishop Woosley, Matt Brown, Jean Block, Jerry Fetzer, Robert Stebbins, Joanna Bunten, Lance Huey, Angela Meredith, Patti Vick, Maria Craig, Terry Williams, Valerie Basham, and Jeremy Smith.

Commissioner Pickard

Chairman Hammons began the meeting by noting that it had been announced earlier that Commissioner Ben Pickard was no longer a member of the Arkansas Lottery Commission. He reminded the audience that Commissioner Pickard had been an inaugural member, serving from late spring 2009 to January 2014, and he thanked him for his leadership and for his promotion of meeting the educational needs of Arkansas students. He added that the Commission would miss his wisdom, insightfulness and commitment to the students. Director Woosley stated that the staff was preparing a plaque for Commissioner Pickard to be presented to him in gratitude for his service to the Arkansas Scholarship Lottery.

Approval of Minutes

The first order of business was the approval of the minutes of the meeting held on January 15, 2014. Commissioner Lamberth made a motion to approve the minutes, Commissioner Baldrige seconded the motion, and the minutes were approved unanimously.

Report from the Internal Auditor

Internal Auditor Brown was recognized to give his monthly Internal Audit Update (in file). Mr. Brown reported that fieldwork recently began on Project No. 8, Points for Prizes and Play it Again Audit, and was ongoing. Fieldwork also began on Project No. 9, IT Gaming Operations. A report was issued on January 30, 2014, for Project No. 13, an audit of In-State Draw Security & Controls. No observations or recommendations were reported for that audit. Project No. 29, an audit for Payroll and Leave, was scheduled to begin the week of February 24.

Consulting Project No. 45, Financial Statements and CAFR Review, was complete and a report was issued on February 11. No observations or recommendations were reported.

Mr. Brown reported that review procedures for Consulting Project No. 46, Instant Ticket Vendor Security Review, were scheduled to take place the week of March 3, 2014. Internal Audit expected to receive a report and analyze the results no later than June 15, 2014.

A report was issued for Audit Project No. 47, Instant Ticket Reconstructions, on January 16, 2014. Internal Audit reported that there was no formal monitoring or review by management of the reconstruction requests sent to Scientific Games on a periodic basis. Also noted was that there was one instance of a reconstruction request for which it could not be demonstrated that ALC personnel had viewed the instant ticket in question or had physical custody of the instant ticket. Management responded by stating that physical receipt - or other supporting documentation - of tickets being reconstructed would be required for an future reconstruction requests, that approval of the Director or Deputy Director of Security would be required for all future payments to players resulting from reconstructions, and that the Director or Deputy Director of Security would perform a monthly review of reconstruction requests going forward. Additional follow-up would be necessary in order to consider these observations cleared.

Project No. 36A, an audit of Financial Accounting and CAFR, was complete and a report was issued on February 11, 2014. An observation was made that there were six inaccuracies in schedules presented in the CAFR for June 30, 2012, and one inaccuracy in schedules presented in the CAFR for June 30, 2013. A complete list of June 30, 2012, inaccuracies noted by Internal Audit were provided to management in completion of the June 30, 2013, CAFR so that any necessary actions could be taken to prevent similar inaccuracies from appearing in the June 30, 2013 CAFR. Internal Audit recommended that management continue to perform detailed review of information presented in supplementary and statistical schedules presented in the CAFR. Management concurred with Internal Audit's recommendation. Additional follow-up would be necessary to consider the observation cleared.

Referring to page 7 of the Internal Audit Update, Commissioner Engstrom asked where the commission stood regarding the major procurement contracts. He asked Director Woosley to provide to the commissioners a section-by-section explanation of the contracts in plain English so that by the time the [contract process] started, they would be prepared. Director Woosley responded that the only contract looming was the one for Advertising, Marketing, and Media Services that he had forwarded to the commission last month. He stated that the proposal he and Ms. Bunten would be bringing to the Commission was for approval of renewing the advertising contract, as well as for approval of two supplemental contracts for creative [advertising]. He asked Commissioner Engstrom if he needed to go section by section on that particular contract, and then present it. Commissioner Engstrom said that he would prefer that method, to ensure he properly understood the language prior to voting to approve or disapprove the contract. He added that it could be done in either a written format or orally. There was a brief discussion regarding timelines, in which Director Woosley informed the Commission that the advertising contract was up for renewal in August of this year and added that it was not as complicated as the two major vendor contracts, although it did have its intricacies. He stated that ALC used very little of the contract services, doing mostly media buys and a little creative through one of the agency's supplemental vendors. He said that in April he

could bring an explanation of the contract before the commission, along with justification for renewal of the contract and for the supplemental contracts. After some discussion, it was determined that this process would be assigned to the Audit and Legal Committee. Commissioner Engstrom commented that because the discussion of the advertising contract could conceivably take much longer than 30 minutes, the committee may need to consider meeting on a separate date.

Report from the Director

Director Woosley was recognized to give his regular report (in file). He reported that the Comparative Income Statement reflected that instant ticket sales were down \$1.9 Million compared to January 2013, while online ticket sales were up \$484,988. He attributed the increase in online ticket sales to ASL's Fast Play games, as well as to the growth of [Powerball and Mega Millions] jackpots during the last part of the month. Net proceeds for January 2014 compared to January 2013 were down by \$922,672, which was a 14.1% drop. Chairman Hammons asked if it was fairly typical that if online ticket sales go up, the online prizes net goes down. Director Woosley replied that it depended on what ALC was selling that particular month. For example, he explained, any time there is a Powerball or Mega Millions run, [ALC] prize percentage is 50% of every dollar, so [ALC] prize expense is not that high, but [ALC] income is higher. Commissioner Engstrom asked Director Woosley if the Raffle loss was included in the \$992,672 drop in net proceeds. Director Woosley responded that a \$284,000 Raffle loss was included in that amount.

Next, he discussed the January Actual versus Budget Comparative Income Statement. He noted that there was again a shortfall in the instant ticket sales, with \$24.8 Million in actual ticket sales as opposed to the \$30.9 Million budgeted amount. The actual amount of online ticket sales for January 2014 was \$6.2 Million, whereas \$7.09 Million had been budgeted for the month. He stated that from a revenue standpoint, everything was lower than anticipated. He said that the net proceeds, although down, would be supplemented by the January unclaimed prize amount. Commissioner Scott noted that expenses for the month were less than the budgeted amounts and he asked if there was a conscious effort to keep expenses down. Director Woosley explained that there was not a conscious effort to keep expenses down, but rather, if sales were down, the operating expenses would be down.

Director Woosley then reported on the Year-to-Date Comparative Income Statement. He said that instant tickets were down over \$15 Million compared to this time last year. Commissioner Engstrom asked if the instant ticket vendor had an explanation as to why the instant ticket sales were down. Mr. Woosley said that it was probably a combination of several things, including the economy or the fact that the lottery had settled in a little bit. He said that he did not want to speak for the vendor, but he offered to have a vendor representative come before the Commission and explain the lower sales. Commissioner Engstrom said he would like for that to happen and Director Woosley responded that he would contact them. Director Woosley reported that while instant ticket sales were down, online ticket sales were up \$7.2 Million for the year. He attributed it partly to the continued popularity of Fast Play games and also to Mega Millions, which had a large jackpot in January.

Commissioner Scott noted that the advertising expenses increased, reflecting 21.3% over budget. He asked if that was an attempt to make up lost ground or if it was just the way the numbers fell. Director Woosley responded that it was just the way the numbers fell in any given month, that management tries to annuitize the advertising budget through the course of the year. He added that currently there was a \$400 Million Powerball jackpot and that would affect the advertising budget accordingly.

Commissioner Pierce commented that he had a copy of the Retail Sales by County and asked if the Director knew if there were any specific trends by county, or if the decline [in instant tickets] appeared to be consistent throughout the state. The Director replied that there are obviously some areas of the state, such as Northwest Arkansas, that just played fewer lottery games. He said that during recent retailer visits throughout the state, he had been told consistently by the stores that sales were down. He added that weather this winter was a big factor in affecting sales, with ice or snow hitting at the worst possible time, especially the weekend, normally the best time for ticket sales. Commissioner Pierce noted that lottery sales density averaged about one retailer per 1,560 residents throughout the state, but that in the counties of Benton, Washington, and Crawford County, the lottery sales retailer density was much lower (approximately 1 in 2,000 in Benton County, 1 in 2,800 in Washington County, and 1 in 2,600 in Crawford County). He added that each retailer was worth an average of \$16,000 per year in ticket sales. Robert Stebbins, ALC Sales Director, reported that the Arkansas counties of Benton, Boone, and Clark had recently approved the sale of liquor; new liquor stores were opening on a regular basis and lottery management was hopeful that it would impact sales upward. Commissioner Pierce said that if the Lottery could increase its monthly sales in those counties by as little as \$1 per person, it could increase sales by over \$600,000 per month. He added that whatever the lottery needed to do, however it needed to do it, the focus needed to be on that area of the state. He asked Director Woosley if he saw a time in which lottery tickets could be purchased via computer or by smart phone app. Director Woosley responded that it was his job to foresee that, or the lottery risked being a dinosaur that didn't make much money.

Commissioner Scott stated that he thought messaging was very different in Northwest Arkansas. He said that education was very important to the residents in those areas, with a lot of Academic Challenge Scholarships going to students in that region - perhaps the marketing should reflect that. Director Woosley said that Commissioner Scott made a very good point and that he wanted to revisit the subject of campus advertising. He reminded the commission that back in 2009 an informal agreement had made not to advertise with colleges or universities. The concern for ALC management had been budgetary, and the commission was concerned that if one school was chosen over another, it would appear as if the Lottery was playing favorites. Chairman Hammons suggested that the subject of campus advertising be sent to the Higher Education Committee.

Director Woosley then reported on the ADHE Transfer Analysis Year-to-Date. He noted a negative increase in the Cumulative Balance for the year of \$4.2 million.

Director Woosley said he wanted to offer a little perspective in ALC's apparent slide in sales. He showed a slide of the Top 20 Lotteries by Rank, which reflected where ALC stood on the national scene. The Calendar Year 2013 ranking for Arkansas was No. 16 in instant ticket sales, with weekly per capita sales of \$2.29.

He also presented a slide of Powerball Sales Comparisons, which reflected larger jackpots but continually decreasing sales. Chairman Hammons asked if there was something structural going on with the Powerball game. Director Woosley responded that he had a few theories about what was going on. He said that the Powerball game change which occurred in January 2012, had raised the price of the ticket to \$2.00, and the jackpots grew faster and larger. Larger jackpots, being a regular occurrence, were no longer as impressive. The other theory was that MUSL had changed the game three or four times since January 2012 and players were tired of the changes. He advised the commission that MUSL was having a meeting in Phoenix in March to discuss Powerball, possibly to change the matrix. He said he would be attending in person to ensure Arkansas was heard, stressing that Arkansas had a problem with a game like Powerball being changed every six months because there were four software loads per year and things had to be moved out of the way to make the changes. He said the other concern was that Powerball players were being continually confused. Commissioner Engstrom asked if the same drop in Powerball sales was occurring in all of the states. Director Woosley said that he did not have exact numbers, but he could state that the jackpots were not meeting their sales projections.

Next, Director Woosley reported that for the week ending February 16, 2014, the Lottery had its best instant tickets sales (\$8,087,610) since the week ending February 17, 2013 (\$9,276,939). The week ending February 16, 2014, was also the best total sales week (\$10,203,013) since the week ending May 19, 2013, when sales were \$13,065,078 (the Powerball jackpot was \$590 Million and the Mega Millions jackpot was \$198 Million). Chairman Hammons asked if higher sales could possibly be because of the instant ticket mix. Director Woosley stated that they specifically schedule the launch of the best games during the months of January, February, and March to maximize sales during the most profitable time of the year.

Director Woosley announced that K-Mart had recently begun selling lottery tickets in five of its Arkansas stores, making it the first Big Box Lottery retailer in Arkansas, adding that TVMs would be sent to those locations shortly.

Director Woosley discussed the launch of a new \$20 instant ticket, Platinum Payout, which offered more \$500 prizes than any other instant game the ASL had ever released. He said it appeared to be selling very well. He also discussed a coupon campaign that began this month. The \$1.00 Instant Ticket coupons were distributed as inserts in various newspapers throughout the state. Thousands of the coupons had been already been redeemed and management was hopeful that the campaign would continue to create excitement.

Director Woosley reported that from March 1 through March 31, 2014, a 5% retailer bonus would be offered. During that period a lottery retailer would receive a 5% bonus of 10% total

commission on additional instant ticket sales compared with instant ticket sales during the same month period from the previous year. Commissioner Engstrom asked if it was possible to offer these types of incentives to individual regions of the state. Director Woosley responded that it could be done, but would most likely upset retailers in other areas of the state. Commissioner Pierce stated that ALC tended to approach marketing in the state as a whole, when there were actually different demographics and different driving forces throughout the regions. He recommended that the lottery move toward more segmented and targeted marketing from this point forward. Director Woosley agreed with his assessment.

Reports from ALC Committees

Higher Education Committee: Nothing to report.

Personnel Committee: Commissioner Lamberth reported that the Personnel Committee met at 9:00 a.m. on this date. She reported that two issues were discussed and both were approved by the Personnel Committee to bring before the full Commission:

- a. *Catastrophic Leave Policy (with amendments):* Commissioner Lamberth brought forward to the Commission on behalf of the Personnel Committee a motion to approve the Catastrophic Leave Policy, with certain changes: (1) *Chief Legal Counsel* was added to the approval process, that is, Shared/Catastrophic Leave requests would be approved by a majority vote of the ALC Director, HR Director and *Chief Legal Counsel*. (2) In the event any of the aforementioned individuals either applied for shared/catastrophic leave or was unavailable to vote on an individual shared/catastrophic leave request, an alternate ALC Director would be appointed by the Chairman of the ALC. Commissioner Engstrom seconded the motion to approve the Catastrophic Leave Policy as amended and the motion passed without dissent.
- b. *360 Evaluation Presentation by Mitchell Communications Group:* The second issue was a motion brought forward by Commissioner Lamberth on behalf of the Personnel Committee to the Commission to approve the proposal of a 360 Evaluation presentation to the ALC Personnel Committee by Mitchell Communications Group, at a cost not to exceed \$1,000.00. Commissioner Scott seconded the motion to approve and the motion passed unanimously.

Audit and Legal Committee: Nothing to report.

Retail and Marketing Committee: Commissioner Pierce reported that the committee met at 9:30 a.m. this date to address whether or not it was appropriate to seek legislative approval to permit the use of debit cards in the purchasing of lottery tickets. After much discussion, it was determined that further research was required and the decision in the form of a motion regarding debit cards would be postponed to June or July in order to give Director Woosley and his team enough time to prepare for the October ALC Legislative Oversight Committee meeting. He stated that there would be a Retail and Marketing Committee meeting at 9:30 on the day of

the next regularly scheduled Commission meeting and the discussion regarding debit cards would continue at that time.

Vendor Committee: Commissioner Scott reported that the Vendor Committee would meet directly following the ALC meeting on this date.

Other Business

Director Woosley presented a Budget Reforecast for the remainder of fiscal year 2014. He reminded the Commission that he had reported at the last meeting that ALC would revise its projections for the benefit of the Legislature so that they would know what to anticipate based on sales of the last six months. He reported that the projection was revised from \$89.5 Million to \$82.78 Million, based on the fact that ALC was behind approximately \$4.2 Million for the current fiscal year. He added that the projection added a \$2.9 Million cushion; management wanted to be as conservative and cautious as possible, while being as accurate as possible. He stated that the majority of the shortfall was because of lower instant ticket revenue, which over the course of the year was about \$15 Million less than projected. After much discussion, Commissioner Scott asked Director Woosley, as a way of addressing declining revenues, to provide the Commission with a “wish list” of items the Director believed would improve sales. Commissioner Lamberth made a motion to approve the budget reforecast, Commissioner Engstrom seconded the motion, and the motion passed unanimously.

Meeting Date

The next commission meeting was set for 10:00 a.m. on Wednesday, March 19, 2014.

There being no further business, the meeting was adjourned.