

MINUTES

ARKANSAS LOTTERY COMMISSION

Wednesday, May 21, 2014

10:00 a.m.

124 West Capitol Avenue, Third Floor
Little Rock, Arkansas

Call to Order

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

Approval of Minutes

The first order of business was the approval of the minutes of the meeting held on April 16, 2014. Chairman Hammons noted a typographical error on page 2. Commissioner Frazier moved to accept the minutes as corrected, and the motion was seconded by Commissioner Engstrom. The motion was approved unanimously.

Succession of ALC Chairman

Commissioner Hammons welcomed 2014-2015 ALC Chairman Smokey Campbell and turned the meeting over to him. Chairman Campbell thanked Commissioner Hammons for his leadership as ALC Chairman during the past year and, on behalf of the Commission, presented to him an engraved gavel and block set.

Succession of ALC Vice Chair

Commissioner Julie Baldrige succeeded Commissioner Campbell as 2014-2015 ALC Vice Chair.

Election of ALC Secretary-Treasurer

Commissioner Scott made a motion to elect Commissioner Doug Pierce to serve as 2014-2015 ALC Secretary-Treasurer. Commissioner Frazier seconded the motion and the motion passed unanimously.

Committee Assignments

A list of committee assignments was distributed (in file) and elections of committee officers would be held immediately after the Commission meeting.

Fiscal Year 2015 Annual Budget

Chairman Campbell recognized Director Woosley to brief the Commission on the proposed FY 2015 annual budget. Director Woosley thanked CFO Fetzer, Controller Williams, and Gaming Director Smith for their help in preparing what he considered a very challenging budget. He

said that it is anticipated that instant ticket sales will increase slightly due to having the supplemental advertising RFQ in place, as well as because of the excitement generated for ALC's 5th Anniversary which will include the introduction of anniversary-related instant tickets.

Regarding online ticket sales, Director Woosley said he expects an uptick in FY 2015 sales due to the introduction of new online terminal games, but that there is also a great deal of uncertainty. ALC is preparing to launch monitor games in September, beginning with approximately 250 retailers, and it has hopes that 400 retailers will be offering the games by the end of the fiscal year. However, there is talk in the legislature of removing the monitor game option. Director Woosley said that a national premium game, Monopoly Millionaires Club, will begin in October. This \$5 terminal-generated game will have a \$1 million grand prize and a second-chance offer to appear on a national game show, and he added that it promises to be an exciting game. He said the only issue is that ALC doesn't yet know what revenue it will generate. It will be launched in the middle of the political season, there will be a soft launch nationally, and it is still not certain the number of states that will be participating. ALC will be withdrawing from Decades of Dollars in October and in January that will be replaced by Lucky for Life. There will be a two-month period in which no revenue will be generated for that type of game. Additionally, the per capita study of Lucky for Life will not be available until June of next year. Director Woosley stated that ALC has taken all of these uncertainties into consideration regarding the impact it will have on the budget.

Director Woosley said that, adding to the budget uncertainty, two major vendor contracts are up in the air, both of which will include percentage changes, i.e., he anticipates reductions in the percentages that ALC pays them. However, ALC cannot budget the anticipated reduced amounts because there are no changes to date. Commissioner Engstrom reminded Director Woosley that the Commission had tasked him to meet with the Director to review the vendor contracts and that he would be setting up a time to meet by the end of the week.

Director Woosley next addressed the proposed budget for staffing compensation and benefits. He explained that one vacant position, V.P. Gaming Operations/V.P. Administration, had been added to the vacant positions report for the purpose of potentially chopping it up for draw auditors and new C-grade staff. He explained that he would be taking that request to the ALC Legislative Oversight Committee.

Commissioner Engstrom asked if the performance audit had been added to the FY 2015 budget. Director Woosley asked CFO Fetzer to respond, and Mr. Fetzer replied that \$50,000 had been budgeted for the performance audit.

Director Woosley stated that the very conservative budget anticipated \$81.2 million net proceeds to ADHE for FY 2015.

Commissioner Scott noted that revenue is anticipated to increase \$11 million and expenses will increase \$13 million. Director Woosley agreed that it was "a perfect storm" regarding expenses because the agency is reaching that time in which high ticket items including computers and

vehicles have reached the end of their use cycle and will need to be replaced. He said that there was additional retailer commission expense added to the budget for incentivizing the retailers. He said that although the expenses have gone up, the very conservative budgeting on the sales side makes it appear more unbalanced than it truly is.

Commissioner Hammons commented that net proceeds budgeted for FY 2015 were less than last year's proceeds. Director Woosley explained that part of that could be attributed to the higher expenses and part of it was also because "Play It Again" expenses would be coming due this year. Director Woosley stated that part of his "wish List" was to revisit and rethink "Play it Again" and examine whether or not it was cost effective, either doing away with it or restructuring the program.

Commissioner Scott said that it was important to note that 1.5% of total revenue went toward staff compensation and benefits, which he considered a significantly low number, and added that he was pleased that personnel costs weren't negatively affecting the budget. He said that he also wanted to note that ALC anticipates over \$75 million in revenue directly to scholarships for Arkansas students. Director Woosley confirmed that, assuming unclaimed prizes total \$5.7 million, the total amount of revenue for FY 2015 is anticipated to be \$81.2 million.

Commissioner Engstrom made a motion to approve the ALC FY 2015 budget and submit it to the ALC Legislative Oversight Committee for review. Commissioner Frazier seconded the motion and the motion passed unanimously.

Chairman Campbell asked Commission members to review the DFA merit payment memo (in file) that approved merit bonus payments for Fiscal year 2014. **Commissioner Hammons made a motion that ALC grant Merit Bonuses for FY 2014 and potentially COLA, contingent upon approval of the Governor and DFA. Commissioner Lamberth seconded the motion. The motion passed unanimously.**

Performance Audit

Chairman Campbell recognized Commissioner Scott, who presented to the ALC for consideration the criteria for the performance audit to be incorporated into an RFP, approved by the Vendor Committee earlier this date. Director Woosley asked that any motion passed include the provision that ALC staff will have the ability to make insignificant changes such as grammar, dates, and addenda without having to reconvene to have those changes approved by the Commission. **Commissioner Engstrom made a motion to approve the criteria to be incorporated into an RFP, with the understanding that the originating committee and ALC Chairman review the changes and let them make the determination as to whether or not the full Commission needs to accept the changes. Commissioner Frazier seconded the motion. The motion passed unanimously.** Mr. Brown reminded the Commission that the draft RFP will return to the Commission for final approval.

Supplemental Advertising RFQ

Chairman Campbell stated that on May 16, the Audit and Legal Committee approved a Supplemental Advertising, Marketing and Media Services RFQ, which he now brought before the Commission for consideration. **Commissioner Engstrom made a motion to accept the Supplemental Advertising, Marketing, and Media Services RFQ as proposed. Commissioner Frazier seconded the motion. The motion passed unanimously.**

Report from the Internal Auditor

Internal Auditor Brown was recognized to give his monthly Internal Audit Update (in file). Mr. Brown reported that substantial progress had been made on Project No. 1, Online Games & Gaming System Contract Compliance audit, which began on May 6. Project No. 7, Instant & Online Ticket Game Development audit, was completed and a final report was issued on May 12. No observations or recommendations were reported. Project No. 17, Security Investigations audit, began on April 29 and fieldwork is ongoing. Project No. 29, Payroll & Leave audit, was substantially complete, with final report issuance expected before the end of May. He said that Internal Audit was very close to completion of the FY 2014 Plan. Mr. Brown also gave an update on follow-up audit projects from previous audits. He reported that fieldwork for Project No. 14F2, Back Office System (BOS) Administration Follow-Up Procedures, began the week of May 5. The audit follow-up for Project No. 19F, Human Resources Follow-up Procedures, was in the planning stages and would begin in June. Fieldwork for the audit follow-up for Project No. 47F, Instant Ticket Reconstructions Follow-Up Procedures, began the week of May 12. The follow-up audit for Project No. 30F, Federal & State Withholding & Reporting Follow-Up Procedures, will be performed as part of the FY 2015 Audit Plan. The follow-up audit for Project No. 36AF, Financial Accounting & CAFR, will also be completed in FY 2015, as it cannot be performed until after the production of the FY 2014 CAFR.

Report from the Director

Director Woosley updated the Commission on Candace Stratford, an Arkansas Challenge Scholarship recipient who had visited with the Commission last month. Ms. Stratford agreed to tell her story in a video ad that will be used in beneficiary campaigns and Director Woosley presented the ad to the Commissioners.

Director Woosley reported on the April 2014 and 2013 Comparative Income Statements, stating that instant ticket sales were down about \$2.5 million, but online ticket sales were up by over \$900,000. Total revenues for April 2014 were down \$1.5 million compared to April 2013. Prize expenses also went down, with April 2014 expenses of about \$1.5 million less than in April 2013. Net proceeds were down about \$667,000.

Director Woosley next reported on the April 2014 Actual versus Budget Comparative Income Statement. He said that total revenues were down slightly from what was budgeted, about \$1.09 Million, but that operating expenses were also less than budgeted. From a net proceeds standpoint, ALC was actually ahead of what was budgeted, by over \$345,000.

Reporting on the Year to Date Comparative Income Statement, he noted that online ticket sales had increased \$10.5 million compared to YTD April 2013. He noted that online ticket sales were up in spite of the underperformance of Powerball and Mega Millions. Instant game prizes were down about \$18 million YTD and online prizes were up \$7.5 million. Total operating expenses were about \$12.6 million lower than last YTD April 2013. Net proceeds YTD April 30, 2014, compared to April 30, 2013, were down about \$8.4 million.

He reported that the ADHE Transfer Analysis reflected not only the drop in instant ticket sales, but it seemed to illustrate that online ticket sales were underperforming. He said that Powerball and Mega Millions were poised for jackpot runs, and with the launching of new instant tickets, he hoped that ALC would be able to reach the FY 2014 revised budget.

Director Woosley gave an update on Quick Draw, the monitor game that ALC anticipates releasing in September. He said it was the same game that was talked about in the monitor game presentation. He said there would be a select number of retailers who would be equipped with television monitors that would display drawings every four minutes during draw times. Some of the retailers would sell the game but would not have monitors. He added that ALC is currently actively recruiting retailers for the game and hopes to have about 250 retailers selling the game at the time of launch in late September.

Commissioner Lamberth asked if the 250 retailers would all be new retailers, or did that number include retailers that already sell lottery tickets. Director Woosley responded that his goal was about half and half, i.e., half new and half current lottery retailers. He said when ALC first started talking about monitor games, he asked Gaming Director Smith to talk to the Kentucky lottery because they were the most recent state to begin selling monitor game tickets. He asked Mr. Smith to get data on Kentucky's monitor game sales, how many retailers they had at start-up, how many retailers they were projected to have, what their sales were per retailer, and whether or not the monitor games cannibalized other lottery sales. He said he was surprised to discover that 60% of Kentucky's traditional retailers accounted for monitor game sales. Based on that number, he added, it appeared that ALC would be relying on its traditional retailers to sell the game. He said based on Kentucky's numbers, he is expecting about 125 new and 125 existing retailers and that by the end of the fiscal year he hopes to have 400 retailers selling the game with monitors in the store.

Commissioner Hammons asked if there were any tentative projections on monitor game sales. Director Woosley said that projected sales were between \$3.5 and \$3.6 million. Commissioner Hammons asked if there was any concern about negative consequences on sales of other lottery products. Director Woosley stated that in Kentucky's case, there was very little cannibalism, with it very slightly affecting instant ticket sales. ALC based its numbers on Kentucky's sales data, took the basis of sales of the Decades of Dollars game and reduced it accordingly, and then reduced it a little more, just to be cautious.

Chairman Campbell asked how monitor game sales in Kentucky were performing. Gaming Director Smith responded that Kentucky was projecting a little over \$30 million in monitor

game sales for the fiscal year and added that Kentucky introduced monitor games six months ago. It reflected 21 cents per capita per week and the state's population is around 4.6 million. Director Woosley stated that ALC estimated monitor game sales of 9 to 12 cents per capita per week. He added that Kentucky had gone beyond their projections, both in number of retailers and in the income generated, and that he hoped ALC would follow that trend. Chairman Campbell then asked when ALC could expect the monitor games to be fully active. Director Woosley responded that the launch was set for September 29.

Commissioner Lamberth asked what percentage we were anticipating and Director Woosley stated it was between 63%-64%.

Commissioner Baldrige noted that Director Woosley had not used the word Bingo, and asked if what he had been talking about was the same thing. Director Woosley responded that staff had determined it wanted to start with a known quantity. Quick Draw is a game that sells in New York. Bingo is a game licensed by Intralot and ALC is currently in a contract situation with Intralot. Director Woosley explained that he did not want to tie ALC to a game for which it might have to pay a licensing fee if at some point it became very popular. He added that the Bingo game is not yet selling anywhere, but will begin selling in New Mexico in June or August, which will allow ALC the opportunity to see how it performs. He said that if monitor games perform well for ALC, Bingo is something ALC could consider in the future.

Commissioner Baldrige then asked if all lottery retailers could offer monitor games, whether or not they had monitors. Director Woosley explained that all of the retailers would be able to sell monitor game tickets, but they would not all have monitors in which the purchasers could watch the 4-minute draws.

Continuing with his monthly report, Director Woosley noted that there were no big, big winners, but there were some notable ones, including a \$160,000 Natural State Jackpot winner and a Mega Millions winning ticket worth \$25,000. Another player purchased a \$10 Quarter Million Jackpot instant ticket and won \$250,000.

Director Woosley presented a list of Play It Again winners and said that the list illustrated the big hit ALC took every few months when end-of-game prizes were awarded. Commissioner Lamberth commented that there was a Play It Again winner from her hometown of Batesville, and she didn't hear one word about it through the local media or through advertising, adding that she didn't see that ALC was getting its money's worth. She said there was usually talk around town if there were winners of other lottery prizes, but the Play It Again winners never seemed to count as news. Director Woosley agreed and said that there were a few issues with Play It Again that concerned him. He said he would rather take that money and put it back into the game so that the players get more prizes. He said it also bothered him that the drawings occur sometimes six months after a game has ended and the press releases don't get picked up. He added that staff has some good ideas on how to reform the program which he will bring back to the Commission once those ideas have been firmed up.

Director Woosley presented to the Commissioners a timeline of planned activities for the coming months. He said that he had relayed to his staff that they should consider the lottery to be in start-up mode and that the next six to eight months would be very busy. He said that regardless of whether or not the advertising RFQ had been approved, he would probably have approached the commission to ask for more [advertising] money because so many initiatives were being launched.

Director Woosley congratulated CFO Fetzer and Advertising & Marketing Director Bunten and their respective teams for being awarded a third consecutive Award of Financial Reporting Excellence for their work on the FY 2013 CAFR.

Director Woosley reported that ALC had very recently received notification that the Arkansas Public Employee Retirement System (APERS) had agreed to pay to ALC \$12,790.42, the full amount of Remmele Mazyck's retirement balance.

Reports from ALC Committees

Vendor Committee: Nothing to report.

Higher Education Committee: Nothing to report.

Audit and Legal Committee: Nothing to report.

Personnel Committee: Nothing to report.

Retail and Marketing Committee: nothing to report.

Executive Session

Chairman Campbell read the following statement from A.C.A 25-19-106 (c) (1):

Executive sessions will be permitted only for the purpose of considering employment, appointment, promotion, demotion, disciplining, or resignation of any public officer or employee. The specific purpose of the executive session shall be announced in public before going into executive session.

He stated that the Commission would go into executive session for the above stated purpose(s) in regard to the Commission's two employees and said that the Commission would ask each of them to meet with the Commission at the appropriate time. **Commissioner Scott made a motion for the Commission to go into Executive Session, Commissioner Lamberth seconded the motion, and the motion passed unanimously.** The executive session began at 11:18 and ended at 12:38 p.m.

Return to Open Meeting

Chairman Campbell stated that during executive session, no resolution, ordinance, rule, contract, regulation, or motion was considered or arrived at during that time.

Other Business

Commissioner Streett stated that the last time ALC met, it had taken into consideration the divided opinions of the ALC Legislative Oversight Committee and had voted to approve monitor games. Subsequent to that meeting, ALC received an e-mail from Senator Hickey of the ALC Legislative Oversight Committee asking the Commission to reconsider that decision. Commissioner Streett said that he believed it was important to acknowledge receipt of the e-mail and to discuss it. He said that if any member of the Commission had a discussion with Senator Hickey, it would be helpful if that member could enlighten the Commission regarding Senator Hickey's thought process. Commissioner Scott said he reached out to Senator Hickey and they had a very good conversation. Commissioner Scott said that Senator Hickey was a very thoughtful legislator who was acting in the best interests of the state. The Senator's concern was that ALC would be spending a lot of money on something that the legislature might make decisions to reverse. His desire was that the ALC not proceed with monitor games until the 2015 General Assembly had a chance to weigh in on the subject. Commissioner Scott added that he did not doubt Senator Hickey's sincerity and added that he was appreciative that the Senator reached out to the Commission.

Meeting Date

The next Commission meeting was set for 10:00 a.m. on Wednesday, June 25, 2014.

There being no further business, the meeting was adjourned.