

**SOUTH CAROLINA EDUCATION LOTTERY  
BOARD OF COMMISSIONERS MEETING  
MINUTES  
May 13, 2009  
10 A.M.**

A meeting of the Board of Commissioners of the South Carolina Education Lottery was held on Wednesday, May 13, 2009, at 10 a.m., in the first-floor conference room located at 1333 Main Street, Columbia, South Carolina, with the following Commissioners participating:

Tim Madden, Chairman  
Jimmy Bailey, Jr., Vice Chairman\*  
Moffatt Burriss, Treasurer\*  
Marvin Quattlebaum, Secretary  
Dr. Edward Keith  
Lisa Stevens  
Boykin Rose\*  
Nathaniel Spells, Sr. \*  
Edie Rodgers

The Chairman called the meeting to order.

**Approval of Minutes**

On a motion of Commissioner Rodgers, seconded by Commissioner Keith, the minutes of the February 11, 2009, meeting were unanimously approved.

**Presentation of Resolution**

The Chairman recognized Tommy Woodham, Midlands Marketing Sales Representative (MSR), and presented a Board Resolution acknowledging Mr. Woodham's extraordinary actions while working in an SCEL retail outlet on February 10, 2009. Mr. Woodham quickly assessed and took control of a life-threatening situation by administering CPR to a man in distress. Mr. Woodham continued to assist the emergency medical personnel in the efforts to save the man's life until the gentleman was transported to the hospital.

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\*These Commissioners participated via teleconference.

## **Fiscal Year 2010 Budget**

The Executive Committee met on April 15, 2009, recessed, and reconvened on April 28, 2009. The Chairman reported the Committee's extensive, detailed analysis and deliberations in reviewing and formulating the FY10 budget considering the dire economic climate facing the private and public sectors. The Committee focused on the underlying policies relating to the level of expenditures for advertising and retailer incentives. The Executive Director, Ernie Passailaigue, was recognized and provided an overview of staff's approach to developing the budget and highlighted significant aspects of the budget.

In preparing the proposed budget, departmental staff conducted a conservative analysis of revenue projections and a detailed assessment on whether each line item of proposed expenditures was necessary. The expenditure proposal before the Board is \$2.1M less than the budget approved for FY09. The FY10 budget proposal is predicated on total revenue of \$946M (\$943M in sales revenue) compared to \$946M (\$943M in sales revenue) for FY09. The net income projection (transfer to the Education Lottery Account (ELA)) of \$252.4M, set by the Board of Economic Advisors (BEA), is unchanged from FY09. Operating expenses, not including retailer commissions, are budgeted at approximately 4.8 percent of total revenue. SCEL's operating expense ratio as a percentage of revenue remains among the lowest in the lottery industry. There are neither provisions for merit increases or other general salary adjustments for employees nor are there any new positions in the proposed budget. During the current fiscal year and in FY10, as employees leave, every effort is being made to reassign responsibilities and/or personnel to avoid filling vacancies.

As addressed in the Executive Committee meeting, Mr. Passailaigue explained his views on advertising expenses and retailer incentives. Citing a study conducted by the BEA on the correlation between lottery sales and advertising spending, Mr. Passailaigue asserted that cutting advertising expenditures will have a direct negative impact on revenue. The study found a multiplier of \$9 in sales for each \$1 spent on advertising. Advertising (media development and placement) is budgeted at \$8.9 million, the same as FY09. Staff seeks to leverage the number and placement of advertising messages through aggressive negotiations rather than increasing overall spending. Staff also remains committed to the Board's philosophy of marketing the lottery in a socially responsible manner while promoting responsible play. Several years ago, in reviewing a proposed reduction in retailer commissions, the BEA projected an adverse impact on sales. Mr. Passailaigue stated that the primary incentive, the selling bonus, is viewed as a commission by the retailers. Overall, SCEL's retailer compensation is in line with North Carolina's and Georgia's when each aspect of their payment programs is taken into account. Mr. Passailaigue reiterated his concern that a reduction in retailer incentives and/or the advertising budget would compromise SCEL's ability to meet the transfer expectations set by the BEA for FY10.

The Chairman thanked the Executive Director and staff for the level of detail and the format of the information presented to the Executive Committee and the Board. After questions from Commissioners regarding several aspects of the budget proposal, the

Chairman presented the report of the Executive Committee for action by the Board. The Committee adopted the Executive Director's budget proposal for FY10, as presented, less a \$414,279 correction adjustment due to an inadvertent overstatement in the funds needed for retailer incentives.

#### **Motion Adopted**

The Board unanimously agreed to adopt the revised FY10 budget as approved by the Executive Committee on April 28, 2009.

#### **SAS 70 Audit**

The Chairman reported the action of the Executive Committee taken on April 15, 2009. As provided in the Board bylaws, the Committee authorized the Director of Audit Services, Bethany Parler, to award a contract within the price range presented to the Executive Committee. Mrs. Parler was recognized to explain the scope of such an audit. The American Institute of Certified Public Accountants (AICPA) issues Statements on Auditing Standards (SAS). Standard 70 is titled "Reports on the Processing of Transactions by Service Organizations." Service organizations are external entities (Intralot) which provide online services that impact the "control environment" of a customer (SCEL). Thus, the audit will relate to Intralot's SCEL operations to include the effectiveness of the internal controls over processing lottery transactions as well as pertinent areas of its financial, administrative, and information systems' processes. Some related processes at SCEL will also be reviewed. The initial, Type I audit, will document the control environment and should be completed by July 1, 2009. The Type II audit tests the documented controls over a six-month period to prove the items identified in the Type I audit perform as intended. The timing for these audit services will avoid the need for another SAS 70 audit until FY11.

Acquiring auditing services is exempt from the provisions of the Procurement Code which would require the issuance of a Request for Proposals (RPF), as well as the other source selection provisions. Staff brought the matter to the Executive Committee because the award exceeds the \$50,000 approval threshold for RFPs (established by the Board in 2002). Subsequent to the Executive Committee meeting, the award to Elliott Davis, LLC, was finalized as it was determined to have submitted the best proposal as well as the lowest fee of \$60,000.

#### **Motion Adopted**

Commissioner Bailey moved to ratify the action of the Executive Committee on April 15, 2009, authorizing the Director of Audit Services to award a contract for the performance of a SAS 70 audit. Commissioner Rose seconded the motion, which was unanimously approved.

#### **Reports**

##### **Marketing Report and Quarterly Advertising Review**

David Barden, Director of Marketing and Product Development, reported on marketing and advertising activities. He gave an overview of the upcoming summer events. A

baseball-themed ticket is the focus of one of the Summer Second-Chance promotions. Players can win a trip to the major league baseball park of their choice to watch a game and receive a special tour of the park. Summer events to support this promotion will be held in Charleston on June 19<sup>th</sup> and in Greenville on July 10<sup>th</sup>. A final second-chance draw will be held in December when one player will win \$100,000. A Beach Boogie and BBQ event in Myrtle Beach is scheduled for September 4<sup>th</sup> and 5<sup>th</sup> (Labor Day weekend). During the second half of the summer, SCEL will launch a Harley Davidson instant ticket which will culminate with a second-chance drawing to win a “Fat Boy” motorcycle in September. Staff believes the chance to win prizes other than cash, such as a baseball trip and prize packages, Harley motorcycles and merchandise, along with other special themed tickets such as *American Idol* and *Deal or No Deal*, where players have the opportunity to attend a game show or live broadcast attracts new players. Expanding the player base for these niche games broadens the demographic profile of SCEL players.

Mr. Barden informed the Board that the number of instant tickets available for sale during the course of a year has increased from forty to more than seventy. The more frequent rotation of the instant games has received positive feedback from players and retailers as they want “fresh” products to choose from.

As previously mentioned in the February 11, 2009, Board meeting, staff plans to review options to replace the MegaMatch 6<sup>SM</sup> game as it is not performing as well as anticipated. Mr. Barden requested direction from the Board as to which Committee to vet any matters relating to a proposed new game concept prior to presentation to the Board. After a brief discussion, the Marketing and Retailer Relations Committee was designated as the appropriate committee by the Chairman.

To facilitate the quarterly advertising review,<sup>1</sup> print media items and a DVD containing broadcast spots were included in the meeting materials provided to Commissioners in advance of the meeting. Mr. Barden called attention to the new series of Powerball® fifteen-second commercial spots designed to attract new or infrequent players. These will air in rotation over the next year. They were all done as part of the same production, which avoided separate set-up charges (and thereby reducing the cost per spot). Among the other items reviewed were:

- Radio – Summer Promotion Big League Baseball and Palmetto Cash 5 Winner Awareness
- Television – Powerball® and Summer Promotion Big League Baseball
- Video Market Place – Summer Promotion Big League Baseball, Charleston Food and Wine Festival, St. Patrick’s in Five Points, and Beneficiary Message
- Play station posters – \$100,000 Taxes Paid and the Big League Baseball Summer Promotion

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<sup>1</sup> SCEL’s enabling legislation requires a quarterly review by the Board of “all past lottery advertising and proposed concepts for major media campaigns to ensure that the advertising did not and does not target with the intent to exploit specific ethnic groups or economic classes of people, and that the content is accurate and not misleading.”

Additional advertising materials were presented, including: the Summer Promotion buckslip, ticket dispenser topper, and t-shirt; Charleston Riverdogs, Powerball® Heritage, Powerball® South Carolina Association of Convenience Stores (SCACS), and “generic” lottery SCACS ads; a Powerball® TriVision Board, and a specialty piece for lottery promotional events.

Commissioner Quattlebaum commented on the noticeable increase of the “Play Responsibly” messages and his belief that this message is even more important, given the economic environment, to communicate to players. Mr. Barden explained that SCEL has the ability to negotiate a percentage of the advertising buys for “Play Responsibly” and beneficiary type messages and has recently launched a “Play Responsibly” website to heighten awareness.

No objection or concern was expressed regarding the advertising material submitted to the Commissioners for review. It was therefore the consensus of the Board that SCEL’s past advertising and proposed concepts for major media campaigns did not, and do not, target, with the intent to exploit, specific ethnic groups or economic classes of people, and that the content is accurate and not misleading.

#### **Executive Director’s Report**

Mr. Passailaigue presented sales results by product type from July 1, 2008 through April 30, 2009, compared with the corresponding time period in FY08. Total revenue was \$6.2M above prior year-to-date sales due to an increase in instant ticket sales of approximately \$25M, which offset an \$18M decrease in online sales. Revenue for the first ten months of FY09 (\$834.5M) equals 88.5 percent of the budgeted sales goal of \$943M. Through April, SCEL has transferred \$216M to the Education Lottery Account (ELA), which is 85.6 percent of the BEA’s FY09 revenue transfer estimate of \$252.4M. Assuming these trends continue, SCEL is on track to meet the BEA revenue transfer forecast and possibly exceed expectations. Mr. Passailaigue noted the slight decrease of net proceeds (\$9.8M), when compared with the corresponding time period in FY08. This decline is attributable to increased sales in the higher price point instant tickets that have a higher prize payout (generally above 70%) than the lower price points. In addition, the gaming expense percentage has increased slightly from the preceding fiscal years (1.17% to 1.96% compared with the corresponding time period in FY08) due, in part, to the demand by players to purchase more licensed property games such as Deal or No Deal™, Major League Baseball® theme tickets, Wheel of Fortune®, and other similar tickets through MDI that give players unique prize opportunities.

Mr. Passailaigue highlighted several items regarding SCEL’s performance during fiscal year 2008, the most recent information available. Based upon *La Fleur’s* rankings among other U.S. lotteries, SCEL ranks 10<sup>th</sup> lowest in administrative expenses as a

percentage of gross sales, 6<sup>th</sup> lowest in advertising expense as a percentage of revenue (based upon the FY09 budget), and 12<sup>th</sup> highest in net income per capita for FY08, which takes into account gross sales and expenses. SCEL ranks 7<sup>th</sup> in per capita instant ticket sales worldwide, up from 8<sup>th</sup> in the preceding year (based upon entire population of the respective jurisdictions).

Extrapolating from claims in excess of \$500, which must be made at an SCEL claims centers, it estimated that fifteen percent of sales come from North Carolina residents compared to an estimated thirty percent before the launch of the North Carolina lottery.

This percentage has remained stable over the past two years. Mr. Passailaigue believes some players are brand loyal and appreciate the higher prize percentage payouts offered by SCEL. Lower cigarette and gas taxes in South Carolina may also encourage cross-border traffic.

Mr. Passailaigue reported on the “The Lottery Dollar” breakdown for FY09 through April 30, 2009. It is distributed as follows:

- 63.0% Prizes
- 25.7% Net Proceeds
- 7.1% Retailer Commissions and Selling Bonuses
- 2.0% Gaming Costs (Vendor)
- 1.5% SCEL Internal Administrative Costs
- 0.7% Advertising

Mr. Passailaigue briefed the Board on the recent activities in the lottery industry. As the Chairman of the Powerball® Game Group, he is a member of the special committee comprised of Directors from the Multi-State Lottery Association (MUSL) and Mega Millions jurisdictions. The committee is continuing to discuss the establishment of a joint venture or joint licensing agreement, whereby both products could be offered within the respective jurisdictions of both game groups. Offering both games within the same jurisdiction could increase revenue, without significant cannibalization of one game to the other due to the different draw dates. Past demographic research indicates these games appeal especially to the “infrequent player,” which, in turn, may increase overall participation and broaden the demographic player base. Another meeting is scheduled for Thursday, May 21<sup>st</sup> and Friday, May 22<sup>nd</sup> in Chicago, which may resolve whether the efforts will come to fruition or not. A meeting of the North American Association of State and Provincial Directors (NASPL) in Nashville, Tenn., in June could then provide an opportunity to review and consider a draft agreement to facilitate a joint venture.

The new Chairman of the Arkansas Lottery Commission, Ray Thornton, has extended an invitation for Mr. Passailaigue to go to Arkansas, at their expense, to brief its Commissioners on what is involved in establishing a lottery, and to describe SCEL’s operations since launch. Margaret R. DeFrancisco, President and CEO of the Georgia Lottery Corporation, will also be attending the briefing in Arkansas. The Arkansas

Lottery's governance structure and enabling legislation are very similar to SCEL. He noted the visit is strictly to act as a resource to provide information similar to the assistance provided to SCEL in 2001.

Chairman Madden noted that the assistance provided by other lotteries was instrumental to SCEL's early success. The Arkansas Lottery seeking advice and counsel from SCEL is testament to what has been accomplished in South Carolina.

**Other Business**

There being no further business, the meeting was adjourned.

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/s/  
Timothy E. Madden, Chairman

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Marvin Quattlebaum, Secretary

As required by Section 30-4-80, notification for this meeting was posted at SCEL headquarters, 1333 Main Street in Columbia. As provided in the Board bylaws, the meeting notice and agenda were also posted on the SCEL website, [sceducationlottery.com](http://sceducationlottery.com), and sent via facsimile transmission pursuant to requests made by media outlets and other organizations. These notifications included the time, date, place and agenda of the meeting.