

SENATE REVENUE COMMITTEE
JANUARY 25, 2005 9:00 AM STATE CAPITOL BUILDING

Members Present: Senator Ryan Deckert, Chair
Senator Charles Starr, Vice Chair
Senator Gary George
Senator Rick Metsger
Senator Floyd Prozanski

Witnesses Present: Dale Penn, Oregon State Lottery

Staff Present: Paul Warner, Legislative Revenue Officer
Mazen Malik, Economist
Barbara Guardino, Committee Assistant

TAPE 11, SIDE A

004 Chair Deckert Calls meeting to order at 9:06 a.m.

INFORMATIONAL MEETING

020 Mazen Malik Begins slide presentation on Oregon State Lottery (**EXHIBIT 1**), laying groundwork for this week's discussion. Lottery Commission will take up the issue of approving line games.

030 Malik Discusses Lottery Terminology – Revenue and prizes, net receipts, expense, net proceeds, page 2.

057 Malik Discusses Lottery History, created in 1984 by initiative petition.

070 Malik Continues discussion on Lottery History beginning with 1999 legislature action, page 3.

088 Malik Discusses Traditional Lottery Games, 2003-04 Net Receipts, pie chart breakdown.

102 Malik Discusses Traditional Game Revenue, page 4. Examines Traditional Game Revenue in percentages.

127 Sen. George Asks why prize spread keeps getting broader.

130 Malik Responds, this is done partly to maintain public interest. Also, video lottery has a higher threshold for prizes.

150 Malik Resumes discussion on Video Lottery Revenue and revenue percentages, page 5.

164 Malik Discusses Total Lottery Revenue, page 6, combining traditional and video. Growth in prizes has defied all logic and models. Discusses percentages of total lottery revenue including net revenue, prizes and expenses. Revenue continues to decline while prizes increase.

203	Malik	Discusses Lottery Transfers. In particular, bonds continue to increase, page 7.
219	Malik	Explains 2003-05 Lottery Distributions, pie chart.
234	Malik	Discusses Issues, which legislators will address this week, page 8. These include line games, video payout percentage, retailer compensation and lottery expense. Projects intake from line games for next biennium.
266	Chair Deckert	Did the state anticipate the lottery would grow as it has?
270	Malik	Responds, the state did not expect the growth. That is true for all of gambling.
290	Paul Warner	Agrees, growth exceeded expectations, but the going has not all been smooth. It is possible to over-estimate it, as occurred in the 1995-97 session.
315	Malik	Discusses Video Prize Percent, page 9.
324	Malik	Discusses Annual Growth: Video, trends since 1993.
346	Malik	Discusses Compensation Rates (old rates), page 10.
363	Malik	Discusses Video Compensation Rates (new rates 2004), for an overall blended rate of about 28.8%. Looking at year to date through December 2004 runs approximately 30.3 percent.
396	Malik	Discusses Retailer Compensation, one view of revenue, page 11. Debate ensuing on who gets the better deal, the state or the retailer.
426	Malik	Discusses another view of revenue, two points of view in the debate. Compares the two views, page 12.

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031	Malik	Concludes presentation of Oregon Lottery with discussion on Lottery Expense Percents, page 12. With introduction of video games expenses dropped considerably from 16%.
059	Dale Penn	Gives brief definition of line games. They are similar to slot machines but don't have arms and don't pay out in cash. Begins slide presentation, Overview Presentation to Senate Revenue Committee (EXHIBIT 2). Most slot machines can be adjusted to offer line games.
080	Penn	Mission Statement, page 3. Goal is to maximize profits. Integrity is of utmost importance.
101	Penn	Explains Organizational Structure of lottery, page 4.
129	Penn	Skips to page 7, Game Development. Discusses changes that have occurred over the years.
146	Chair Deckert	Asks why Oregon does not expand lottery to sports action. Follow-up questions.

156	Penn	Responds, Oregon was sued by National Football League. Oregon is the only state with a program that allows for betting on games. As punishment, NFL will not allow any professional football team to come here.
176	Penn	Discusses Game Timeline, page 8.
193	Penn	Explains Planning/Budget Process, page 9.
198	Penn	Reviews FY04 Revenue and Expense Distribution, Traditional Games, page 10. Compares this with Video Lottery, page 11. Prize payouts for traditional games is at 64.8 %; video lottery prize payout is 93.82%. It is important to be precise about what is an appropriate payout. Commission will examine this issue for line games.
240	Penn	Discusses Contingency Reserve & Administrative Savings, page 12.
265	Penn	Discusses 05/07 Capital Requirements, page 13. This includes replacing obsolete equipment. The software on the old machines cannot support line games.
335	Sen. Metsger	Asks if commission is satisfied with past negotiations with manufacturers for lease or purchase of machines in regard to support and replacement.
364	Penn	Responds, organization looks at this now. Oregon is the only video lottery that confines itself to poker. Other states have line games. Most manufacturers get a percentage of the take. Not so in Oregon, which owns its machines.
425	Penn	Discusses Update of Oregon Lottery Audits, page 14. Oregon's lottery meets or exceeds best practices.
441	Chair Deckert	Comments, it sounds as though past audit problems have been dealt with.
448	Penn	Responds affirmatively.
464	Penn	Discusses Forecast 05/07, page 15. Governor's budget requests \$933 million in transfers from the Oregon Lottery. This biennium lottery will transfer \$770 million, although \$813 million is projected.

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041	Penn	Continues discussion on forecast with a comparison to income spent on video retail network games in West Virginia minus its casino operation.
075	Penn	Discusses Video Lottery, Net Sales, page 16, shows growth of video lottery sales.
082	Penn	Concludes with discussion on 20 Years of Doing Good Things for Oregon. The lottery has produced over \$4 billion since its inception. Anticipates lottery could transfer \$1 billion every biennium.

106	Chair Deckert	Asks questions and makes comments concerning the issue of retailer compensation. What is the rationale behind a 26.5% recommendation?
137	Penn	Responds, Oregon is being sued over commission rates, which are a blended rate between 28 and 29%.
174	Penn	Expresses concern that the video product is projected to produce \$660 million for state budget without discussing line games. If line games come into play, that number rises to \$780 million as base. Over the last 2 years this retail network produced \$600 million, and state would reduce that by 10%, while requiring retailers to produce additional revenues. All this and they would also take a 50% cut in returns. Line games will increase sales. Problem is to identify how much. Retailers are the lottery's sales force.
247	Penn	Continues comments on retail compensation. Oregon has the lowest commission rates in the United States. Difference is other states purchase their machines. Compares Oregon's rates to Canada. Rate will be under debate over the next two months.
305	Chair Deckert	Agrees, Oregon Lottery is trying to find proper compensation. Would argue that Oregon has guessed high. Given this, he questions the wisdom of signing 6-year contracts.
326	Penn	Responds to question of 6-year issue.
414	Sen. Prozanski	Asks, how does the lottery define a reasonable rate of return? Expresses concern on state's increasing dependence on lottery funds. Asks Penn to provide information on how many retail licenses exist. Understands higher-end restaurants such as Elmer's and Shari's are getting into the lottery. Believes the lottery is helping the hospitality industry make a greater profit.

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030	Penn	Responds to Sen. Prozanski's points. Does not have a good definition of a reasonable rate of return. Hopes a definition will come out of the upcoming litigation.
078	Sen. Metsger	Believes it is important to indicate that there are arguments that counter Mr. Penn's arguments. The original intent of the lottery was not to create state support of gaming organizations, but to help support restaurants as well as the state. Other issue is deciding a reasonable percentage. If someone starts an enterprise and predicts smaller revenues, then a greater return will be needed.
109	Sen. Metsger	Asks how the governor will get around the constitutional limitations of the lottery.
116	Penn	Responds, Ways and Means Committee has asked for attorney general's opinion on this issue. Governor's office sees state police as connected to ability to support economic development.
149	Chair Deckert	Asks what role the legislature can play in setting commission rates.

Follow-up questions.

159	Penn	Encourages legislators to participate on the issue of line games.
198	Warner	Provides information requested in January 24 involving the local option issue. See School Local Option Property Tax (EXHIBIT 4). Refers to research report pages 6-8.
251	Chair Deckert	Adjourns meeting at 10:45 a.m.

Tape Log Submitted by,

Barbara Guardino, Committee Assistant

Reviewed by Kim Taylor James

Exhibit Summary:

1. Oregon Lottery, 2005 presentation, Malik, 12 pp.
2. Oregon Lottery Overview Presentation to State Revenue Committee, Penn, 17 pp.
3. Oregon Lottery Handouts, Penn, 60 pp.
4. Research Report, School Local Option Property Tax, Warner, 8 pp.