



## Minutes of the Commission Meeting

Room 412, Capitol Building

March 24, 2017

Vice Chair Putnam called the March 24, 2017 meeting of the South Dakota Lottery Commission to order at 9:30 a.m.

**MEMBERS PRESENT:** Cheryl Laurenz Bogue, Dave Mickelson, Jim Putnam, and William Shorma. Joe Kafka, Robert Faehn, and Brent Dykstra attended via teleconference.

**SUPPORT STAFF PRESENT:** Norm Lingle, Clark Hepper, Sherry Lauseng, Kelly Thompson, Jennifer Baker, John Hepper, Sam Stanforth, Robyn Seibel, Justin Pierson, Andy Gerlach, David Wiest, and Andrew Fergel.

### APPROVAL OF THE AGENDA

Commissioner Kafka moved that the agenda be approved. Commissioner Mickelson seconded. Roll was called: Aye – Bogue, Dykstra, Faehn, Kafka, Mickelson, Putnam, Shorma. Motion carried.

### APPROVAL OF THE MINUTES FROM THE DECEMBER 2, 2016, MEETING

Commissioner Faehn moved that the minutes be approved. Commissioner Bogue seconded. Roll was called: Aye – Bogue, Dykstra, Faehn, Kafka, Mickelson, Putnam, Shorma. Motion carried.

### CONFLICT OF INTEREST

Vice Chair Putnam asked if there were any conflicts of interest and there were none.

### ELECTION OF CHAIR AND VICE CHAIR

Vice Chair Putnam opened the floor up to nominations for Chairman of the Commission. Commissioner Kafka nominated Jim Putnam. Commissioner Dykstra seconded. No other nominations were made. Moved to vote by Commissioner Bogue and seconded by Commissioner Shorma. Vote was taken: Aye – Bogue, Dykstra, Faehn, Kafka, Mickelson, Putnam, Shorma. Motion carried.

Commissioner Bogue nominated Robert Faehn for Vice Chair of the Lottery Commission. Commissioner Mickelson seconded. No other nominations were made. Moved to vote by Commissioner Shorma and seconded by Commissioner Bogue. Vote was taken: Aye – Bogue, Dykstra, Faehn, Kafka, Mickelson, Putnam, Shorma. Motion carried.

### SECRETARY OF REVENUE COMMENTS

*Secretary of Revenue Andy Gerlach reported on the following:*

Commissioner Putnam congratulated Secretary Gerlach on being named the National Tax Administrator of the Year for 2016 by the *State Tax Notes Journal*.

Secretary Gerlach stated that out of the 389 bills brought forth in the 2017 Legislative Session, the Department of Revenue (DOR) was involved in 86. The DOR put forth seven bills and they were all signed into law by the Governor. The DOR supported eight other bills, and all but one were signed into law. The DOR also had a hand in killing five bills.

### Key Legislation

- **HB 1025** to revise certain provisions regarding background checks for applicants, licensees, vendors, and employees of the South Dakota Lottery. This allows for FBI national background checking which shows if there has been a felony conviction not only in South Dakota but in any jurisdiction.

- **HB 1026** to require tracking numbers to be included on the quarterly reports of direct shippers and wine carriers. Requiring tracking numbers on both the direct shipper (winery) and the wine carrier (UPS, FedEx) allows DOR to easily match shipments to licensed wineries.
- **HB 1031** to revise certain restrictions regarding division directors of the Department of Revenue. Previously, division directors in the Department of Revenue could not hold certain positions outside of state government, such as on a school board, town council or in a family corporation; this bill removes that restriction.
- **SB 36** to revise the time to file certain tax returns and remit certain taxes. This bill requires taxes paid electronically to be paid earlier to improve monthly budget cash flow.
- **SB 128** to provide an exception for alcohol manufacturers and wholesaler licensees to participate in certain retail events and to declare an emergency. The three tiered system dates back to prohibition and limits what wholesalers can do. This bill provides a limited exception to state law by allowing manufacturers or wholesalers to serve alcoholic beverages at events conducted by a civic, charitable, educational, fraternal, or veteran's organization which has obtained a temporary alcohol license for a special event.

#### Fiscal Year (FY) 2018 Budget

A \$4.6 billion state budget will be adopted. Funding highlights included a 0.3 percent pay increase for K-12 education and community support providers as well as funding to partially offset health insurance increases for state employees.

The DOR will have about a \$75 million budget for FY18 with about 250 full-time employees (FTE). There was a reduction of \$226,666 in personal services to help reduce the State's budget, but legislators did allow for the addition of one FTE to the Motor Vehicle Division in FY18. A one-time budget sweep of \$500,000 was taken from the Video Lottery Operating Fund to help offset the FY17 budget.

Following the end of the legislative session, DOR will be working on Plate On Demand which allows the ordering of license plates online and with direct delivery to customers, alcohol laws, and tax increment financing (TIF) districts which are not uniform across the state.

Commissioner Putnam asked if the plan was to expand TIFS to more rural areas or just throughout the state. Gerlach explained that the current process for TIFS allows different labels to be used on similar projects. DOR is working to make the process more uniformly and consistently applied.

Commissioner Shorma wondered if there was a summer study planned to deal with TIFs. Gerlach replied that there would be a work group, probably not a summer study. Shorma then asked if the DOR was seeing voluntary compliance in collecting sales taxes on internet sales. Gerlach said 136 companies had voluntarily complied including Amazon.

#### **LUCKY FOR LIFE RULES HEARING – 10:00 AM**

*Executive Director Norm Lingle reported on the following:*

##### **BACKGROUND**

Vendors recommended that the Lottery pursue a "for life" game during the Lottery's Strategic Planning Meeting in May 2016. Lucky for Life (LFL) is currently offered by 23 lotteries, including all bordering states except Nebraska which plans to begin sales in August 2017. Lucky for Life is a lotto/draw style game with fixed prizes. The top prize is \$1,000 per day for life with a second prize of \$25,000 per year for life.

##### **HOW THE GAME PLAYS**

A player would choose 5 numbers from 1 to 48 and 1 number from 1 to 18 (Lucky Ball). They can pick their own numbers or ask for a Quick Pick. The odds of winning the top prize are 1 in 30.8 million, with overall odds of 1 in 8. Lucky for Life costs \$2 per play and will have drawings on Monday and Thursday nights. Based on other states' experiences, the Lottery expects \$2 million in sales and \$416,000 in net revenue transferred to the State in the first year.

## PROPOSED ADMINISTRATIVE RULES

- 48:03:18:01- Participation in Lucky for Life game authorized – SD Lottery may participate in LFL game
- 48:03:18:02 – Purchase of Lucky for Life tickets – Allows players to purchase tickets for up to 9 future drawings – consistent with all other lotto style games
- 48:03:18:03 – Ineligible Players – Same language as other draw games – anyone involved with the lottery – or immediate family members living in the same household as anyone involved with the lottery
- 48:03:18:04 – Lucky for Life game rules – Propose adopting LFL game rules for SD Lottery
- 48:03:18:05 – Top prize liability limits – Lottery identifies how to pay players if annuity option is chosen by winner – Players would be paid the first installment upon presenting winning tickets – remaining prize payments would be made annually.
- 48:03:18:06 – Second prize liability limits - Lottery identifies how to pay players if annuity option is chosen by winner – Players would be paid the first installment upon presenting winning tickets – remaining prize payments would be made annually.

Commissioner Faehn asked if any losses in Powerball revenue were factored into the \$416,000 in new lotto revenues. Lingle felt that LFL wouldn't take revenue from other lotto games because it will offer different prizes and draw dates.

Commissioner Putnam asked for proponents or opponents to the LFL rules. There were no comments made and no written comments received regarding these rules.

The hearing was closed at 10:12 a.m.

Commissioner Faehn moved that the Lucky for Life rules be approved. Commissioner Dykstra seconded. Roll was called: Aye – Bogue, Dykstra, Faehn, Kafka, Mickelson, Putnam, Shorma. Motion carried.

Director Lingle said the Legislative Rules Committee on May 1<sup>st</sup> would be the next step and Lottery expected to launch the game no later than June 4, 2017.

## EXECUTIVE DIRECTOR'S COMMENTS

*Executive Director Norm Lingle reported on the following:*

Lingle updated Commissioners on the 2017 Legislative Session.

HB 1025 was an agency bill regarding background checks of all lottery employees, licensees and vendors. The Lottery has always done in-state background checks on these groups. This bill will allow for Federal Bureau of Investigation nationwide background checks to fully comply with the statute that states that no one can be involved with the Lottery if they've been convicted of a felony in South Dakota "or any other jurisdiction". Individuals convicted of a felony cannot work with the South Dakota Lottery or be licensed by the South Dakota Lottery for at least 10 years after the sentence has been served. This bill will go into effect on July 1<sup>st</sup>, 2017. Lottery staff will work with the Department of Criminal Investigation (DCI) to put the law into practice. Existing licensees will be background checked over the next 5 years so as to not overwhelm DCI and Lottery Staff.

HB 1199 to repeal the Lottery was tabled on a 5 to 3 vote by the House Appropriations Committee. Had the bill passed, all lottery style games including pull-tabs, raffle tickets, and bingo would have been illegal. The Lottery, along with partners from the South Dakota Licensed Beverage Dealers and Gaming Association, Music and Vending Association of SD, Associated School Boards of SD, and the SD Retailers Association all spoke against the bill.

Commissioner appointment and reappointments by the South Dakota Legislature included Jim Putnam, Cheryl Laurenz Bogue, Robert Faehn, Joe Kafka, Dave Mickelson, and William Shorma.

The State had a nearly \$25 million deficit for the remainder of FY2017. Senate Bill 32 revised the general appropriations act for 2017 and swept \$500,000 from the Lottery's video lottery operating fund. Eight different funds were swept to make up the State's deficit.

Lingle then explained to new commissioners how the Lottery's budgets work. There is an instant/online budget approved by the commission and a video lottery budget approved by legislators. The Lottery is a self-funded agency. The video lottery operating fund is funded by license fees along with .5% of the net machine income generated. Lingle didn't think the sweep would impact the Lottery's plans to move forward with updating the video lottery operating system.

Commissioner Putnam asked if the funds were swept from the current budget. Lingle stated that the transaction would take place on June 26 and would come out of FY17's budget.

In August of 2019 the Lottery's contract with its current online vendor will expire and the video lottery base contract will end shortly after. A request for information (RFI) pertaining to online (lotto) and video lottery central systems will go out around May 1, 2017. The Lottery will be looking for vendors to show them the latest and greatest operating systems available. This will help decide what to include in a request for proposal (RFP) to look for a new vendor. Responses to the RFI will be due in July, with hopes to sit down and talk to vendors and go over that information shortly thereafter.

The South Dakota Lottery will be celebrating its 30<sup>th</sup> Anniversary this year and has been meeting internally to come up with ideas to commemorate the event. Plans will be presented at the next commission meeting.

American Health Care Reform Act of 2017 would make Lottery winners ineligible to participate in the Health Care Reform Act. The Lottery already has a debt set-off program to collect child support and other money owed from winnings before the check is printed. The player's social security number is used to match them with Department of Social Services (DSS) information on those behind on child support. The Obligations Recovery Center and Supplemental Nutrition Assistance Program (SNAP) are also part of the set-off program.

Sherry Lauseng, Finance Manager for the Lottery, will be retiring in June. Sherry has been with the Lottery since August of 1987 and was with Legislative Audit before that.

#### **DECLARATORY RULING 17-2: LOTTO RETAILER INCENTIVES**

*Executive Director Norm Lingle reported on the following:*

Director Lingle explained that the reason for this ruling is to set up a pay structure for commission bonus payments to retailers for selling winning LFL tickets. Retailers would receive a \$5,000 bonus for selling a top prize winning ticket and a \$500 bonus for selling a second prize winning ticket.

Commissioner Shorma moved that Declaratory Ruling 17-2 be approved. Commissioner Dykstra seconded. Roll was called: Aye – Bogue, Dykstra, Faehn, Kafka, Mickelson, Putnam, Shorma. Motion carried.

#### **Gaming Labs International (GLI) SECURITY REVIEW**

*Director of Video Lottery and Security Robyn Seibel and Michael Capen from GLI reported on the following:*

In 2015, Lottery met with the Sioux Falls and Rapid City police departments to discuss the security of VL establishments. After that meeting, an RFP was put out to develop a list of best security practices for video lottery establishments. After reviewing two proposals, Lottery staff asked the Commission to approve GLI to do the security study.

#### **VL SITE SECURITY AUDIT APPROACH AND SCOPE**

GLI conducted a security site audit of 26 SD Lottery selected video lottery (VL) sites between January 9<sup>th</sup> and January 12<sup>th</sup>, 2017 in Sioux Falls (9), North Sioux City (5), Aberdeen (7), and Rapid City (5). All kinds of establishments – restaurants, bars, casinos, gas stations, etc. – were included to get a broad overview of security but the study did not go into more rural communities. The audit was conducted by two field teams in each consisting of a GLI staff member accompanied by Lottery staff. The objective was to obtain a benchmark in VL site physical security and to develop a baseline for best practice recommendations. Currently establishments use a self-assessment document provided by the Lottery. The scope of the audit encompassed 41 physical security best practice controls (security policies and procedures, security measures and practices) and assessed the implementation levels of those 41 controls through on-site observation and interviews.

Michael Capen of GLI said the locations knew they were being reviewed ahead of time. GLI observed the outside of buildings first, then talked with the owners. Capen felt the owners were forthcoming about what they did and didn't have as far as security.

#### AUDIT CONCLUSIONS

- While the relatively small sample size (26 sites of a population of around 1,300) provides a good status snapshot, audits of larger sample sizes would be required for more detailed analysis with geographical and metadata trending.
- Multiple external factors influence the risk profile of VL site operations (socio-economic, environmental and demographic factors).
- The key physical security measures and best practices are preventive (deterrent) and detective but cannot eliminate the residual risk of e.g. armed robberies. All best practices and measures only "go so far".
- The overall level of best practice implementation as measured is at around 74%.
- The audit provided the baseline for a list of Top Ten VL Site Security Best Practices as well as key observations and opportunities for improvement for individual sites.
- The security maturity levels vary between the VL site categories (C-Store, Restaurant/Bar, VL only sites).
- VL only sites under multi-site ownership tend to exhibit higher maturity levels through corporate policies, while single site security is more ad-hoc.
- SD Lottery can use the results and best practices to develop a continuous audit and monitoring program.

#### LEVELS OF IMPLEMENTATION

74% of the best practice security controls were fully implemented, but there was a wide range with one location at 93% fully implemented and another at 27%. Top three security areas met were fully lit building entrances, surveillance cameras, and internal controls about how to do business. Top three security measures not met were door buzzers when walking in, active monitoring of cameras, and key control (no procedures for duplicating keys).

#### THE TOP TEN BEST SECURITY PRACTICES AT VIDEO LOTTERY SITES

1. Visible security measures and deterrents (cameras/signs).
2. Floor layout enables detection/visibility of persons entering – can you get in the building without being seen?
3. Alarm system installed and monitored.
4. Alarm and safe codes regular change policy and procedure and key management – when employees leave, change alarm codes and get keys back.
5. Staff trained on emergency and security procedures.
6. Door chime(s) implemented and operational.
7. Door lock and buzz-in capability implemented in stand-alone locations or high crime areas.
8. Panic Buttons – staff can hit to call police.
9. Security policies and procedures documented.
10. Periodic review/update of security policies and procedures.

Lottery will be sending these top ten practices to establishments along with the self-assessment already given out. There is a plan to use this checklist to follow up by checking establishments periodically.

#### CODE OF CONDUCT

*Assistant Deputy Director Clark Hepper reported on the following:*

2016 LEGISLATURE CREATED THE STATE BOARD OF INTERNAL CONTROL (SBIC)

The seven member State Board of Internal Control consists of three members from state agencies under control of the Governor and appointed by the Governor for three year terms, the commissioner of the Bureau of Finance and

Management, the state auditor, a Board of Regents administrator's designee, and a member appointed by the Chief Justice of the Supreme Court. The commissioner of the Bureau of Finance and Management is the chair of the board.

The Board establishes and maintains guidelines for an effective system of internal controls to be implemented by state agencies that is in accordance with internal control standards; a code of conduct for use by state agencies excluding the Unified Judicial System; and a conflict of interest policy for use by state agencies excluding the Unified Judicial System.

Key Definitions to consider:

- "Code of conduct," a set of ethical principles and guidelines that constitutes appropriate behavior within an organization;
- "Internal control," a process that integrates the plans, activities, policies, attitudes, procedures, systems, resources, and efforts of an organization and that is designed to provide reasonable assurance that the organization will achieve its objectives and missions and to detect and prevent financial malfeasance;
- "State agency," the Legislature, any constitutional officer, the Unified Judicial System, and any department, division, bureau, board, commission, committee, authority, or agency of the State of South Dakota;

At the July 27, 2016 meeting the SBIC passed a motion which stated that **ALL** State Agencies shall adopt the Code of Conduct contained in the South Dakota Employee handbook as a code of conduct for State employees.

For non-employees each State Agency shall adopt the Code of Conduct as contained in the South Dakota Bureau of Human Resources Employee Handbook or a code of conduct substantially similar as if a person were an employee.

Resolution 17-1

- The South Dakota Lottery Commission hereby adopts the Code of Conduct as contained in the Bureau of Human Resources Employee Handbook in effect March 24, 2017 as set forth on page 3-11 attached hereto as the Code of Conduct for Commission employees.
- The Commission also adopts those sections of the Code of Conduct pertaining to acceptance of gratuities, rebates, reward points and other perquisites, anti-harassment and discrimination, conflicts of interest laws, and fraud of theft in the workplace, attached hereto, as set forth on pages 4-11 to apply to members of the Commission and non-employees.

Putnam asked if all commissions across the state needed to adopt the same rules. Hepper said it is consistent with all commissions and needed to be adopted in 2017.

Putnam asked if there are penalties for not complying. Hepper assumes penalties are within the guidelines of the state statute. Lingle added that the Commission needed to adopt the rules or it would be noted in the Legislative Audit. Andrew Fergel said that most of what is in the Code of Conduct was already covered in SDCL 42-7A-27 & 28.

Commissioner Faehn moved that the adoption of Resolution 17-1 regarding the Code of Conduct be approved. Commissioner Shorma seconded. Roll was called: Aye – Bogue, Dykstra, Faehn, Kafka, Mickelson, Putnam, Shorma. Motion carried.

#### **ADMINISTRATIVE HEARING ON LICENSE DENIAL – THE POUR HOUSE LLC – 11:25 AM**

*Hearing Examiner Catherine Duenwald:*

The Administrative Hearing of The Pour House LLC and Sean M. McDannel versus the SD Lottery (Office of Hearing Examiners Revenue number 17-03) was held on March 24, 2017 beginning at 11:25 a.m. in Room 412 of the State Capitol. Hearing Examiner Catherine Duenwald presided over the hearing regarding the license denial of The Pour House LLC and Sean McDannel with Casey Bridgeman as the attorney for McDannel and Andrew Fergel as the attorney for the SD Lottery.

Duenwald asked the Commission to decide when they'd make their determination on the denial. Chair Putnam said the Commission would listen to testimony and wait until the next meeting to come to a decision. Commissioner Bogue

asked for clarification on whether the decision would be made at the next meeting or in the interim. Duenwald said the Commission would receive a write up in the interim and vote to accept or reject it at their next meeting. Fergel asked the hearing examiner to make a proposed decision prior to the next meeting that Commissioners could accept or reject at the meeting in June. There were no objections to this.

Fergel called John Hepper, Lottery Licensing Manager for the past 27 years, to testify. Hepper was sworn in and described his duties and the steps involved in the license application process. Hepper testified that two background forms were required and needed to be notarized in the application process: the individual history form and the investigation authorization form. Fergel then handed Hepper Exhibit 1, a copy of the application for video lottery license submitted by The Pour House LLC along with the individual history form and the investigation authorization form. Hepper stated that he received the application the same day it arrived in the mail, on January 11 or 17 (he couldn't read the date stamp). Hepper stated that he reviewed the application to make sure it was complete and accurate, assigned it a control number, initiated a background check, entered it into the data base, and sent it to the Department of Criminal Investigation (DCI). Fergel then handed Hepper Exhibit 2. Hepper recognized it as paperwork McDannel had included along with the application and background forms. It was a copy of McDannel's arrest records from the South Dakota Unified Judicial System. Fergel asked if this was required; Hepper stated that one question asks if the applicant had ever been arrested and Mr. McDannel included Exhibit 2 to answer that question. Fergel asked if Hepper took any other steps after receiving Exhibits 1 & 2. Hepper said he sent the paperwork off to DCI for a background check, reviewed the information from DCI, and compared it with information received from McDannel. Fergel then handed McDannel and Hepper Exhibit 3. Hepper recognized it as a copy of the information the Lottery received from DCI's background and driver's license check, which was a listing of McDannel's arrest record. Fergel asked when that information was received and processed. Hepper answered that after receiving the application and criminal history from Mr. McDannel, he took it to Director of Security Robyn Seibel for review to see if further action was required. Fergel had no further questions.

Bridgeman, attorney for McDannel, began his questioning of Hepper by asking if there was documentation of the credit report. Hepper stated that there was credit report but it was not part of the decision making process in this case. Bridgeman asked if all the information in Exhibit 2 was included in the DCI background check. Hepper stated that the speeding tickets and similar violations would not have been on the DCI check. Hepper said he provided the information but Seibel and Lingle made the final decision. When asked if he made recommendations on whether or not to grant the license, Hepper responded that he had not. Bridgeman asked if charges made and later dismissed would be included in the DCI background report. Hepper stated that if the case didn't go to court, it probably would not be included. Bridgeman then pointed out that Exhibit 2 had eighteen pages of information and Exhibit 3 had four pages.

In rebuttal, Fergel clarified that Exhibit 1 was the video lottery application for The Pour House LLC and Exhibits 2 and 3 contained information regarding Sean M. McDannel's criminal history. Hepper agreed. Fergel asked why the Lottery was looking at his criminal history. Hepper stated that the Lottery couldn't check an entity, only the owners, managers or stock holders of the entity, and that requirement is set out in statute. Fergel had no further questions. Bridgeman had no further questions.

Duenwald called for Commissioner questions. There were none and Mr. Hepper was dismissed.

Fergel called Director of Video Lottery and Security Robyn Seibel to testify. After she was sworn in, Fergel asked how long Seibel had been with the Lottery and where she was employed before that. Seibel stated she had been with the Lottery for two and a half years and had previously worked for the Department of Corrections. Seibel described her job duties as overseeing the processes and security of video lottery. Fergel asked if her job duties require her to review applications for video lottery and if she had reviewed the application that Hepper had testified on previously. Seibel answered yes to both questions.

Fergel asked if Seibel was given all three exhibits to determine The Pour House's licensing. Seibel answered in the affirmative. Fergel then asked what Seibel did after reviewing the application and background check. She stated that she had concerns due to McDannel's criminal history and promptly relayed those concerns to Norm Lingle after receiving the application. Seibel couldn't recall the exact date but agreed it was before Feb. 1, 2017. Fergel asked if she discussed those concerns with Lingle on more than one occasion; she said yes. Fergel asked if a final decision was made

regarding the application before Feb. 1, 2017. Seibel responded affirmatively. Fergel wondered who made the final decision. Seibel said Lingle made the final decision but she participated in the decision to deny the license. Fergel asked what she was directed to do once the decision was made. Seibel stated Lingle asked her to develop a letter of denial for the applicant and send it out, which she did.

Fergel handed Seibel and Bridgeman Exhibit 4. Seibel recognized the exhibit as a copy of the letter she sent out denying a video lottery license for The Pour House LLC. She mentioned that state statutes and administrative rules were also sent to Mr. McDannel to reference the reasons for denying the license. The letter was dated Feb. 1, 2017 and was mailed that day through priority mail. Fergel asked if Seibel was aware that the letter had been received by McDannel. Seibel said she knew it had been received because McDannel called to ask questions about the letter.

Fergel handed Seibel and Bridgeman Exhibit 5 and asked if Seibel recognized it. Seibel noted it was a copy of a letter from Mr. McDannel requesting an appeal on the license denial along with a detailed letter as to why he should receive a license. Fergel had no further questions for Seibel.

In his cross examination, Bridgeman pointed out that before McDannel could apply for a video lottery license, he would have had to have a liquor license. He asked Seibel if McDannel had successfully acquired a liquor license. Seibel stated that he had but she did not process liquor licenses and didn't know how that licensing process worked. Bridgeman noted that McDannel passed the test to obtain a liquor license and asked Seibel if the denial was solely based on McDannel's criminal history. Seibel responded in the affirmative. Bridgeman asked if McDannel was delinquent in excise taxes or sales taxes to which Seibel responded that he was not. Bridgeman stated that in Exhibit 4, SDCL 42-7A-14 was cited and referenced the subsection concerning the conviction of a felony; he inquired if the denial of McDannel's license had anything to do with the conviction of a felony. Seibel replied no. Bridgeman asked if she applied that to misdemeanors. Seibel said no but the Lottery did consider the span of time in which those misdemeanors took place. Bridgeman referenced 42-7A-14(03) and asked if Seibel felt Mr. McDannel's reputation, habits, and criminal history somehow posed a threat to the security and integrity of the Lottery. Seibel felt it did. Bridgeman asked if the Lottery had granted licenses previously to people with misdemeanors. Seibel answered yes. He then asked if she had taken into account all violations taking place over the last 10 years. Seibel stated that she looked at all violations from 1995 to the most recent. Bridgeman asked if Seibel and Lingle had given consideration to those crimes that occurred only over the last 10 years. Seibel said they looked at the number of crimes committed on a repetitive basis over a number of years. Bridgeman then asked if the Lottery usually considered only crimes committed in the last 10 years. Seibel had no specific case references.

Duenwald asked Seibel if they looked at the types of crimes committed. Seibel stated that the crimes were misdemeanors and that the overall pattern and number of crimes in the criminal history were considered.

Bridgeman asked if the list of crimes in Exhibit 2 that were charged but dismissed were considered. Seibel stated that all of the information was considered and that there was a pattern of criminal behavior over an extended period. Fergel asked if the crimes listed in Exhibit 2 provided by Mr. McDannel to the Lottery indicating numerous contacts with law enforcement were taken into account. Seibel answered in the affirmative.

Commissioner Bogue asked if McDannel had any convictions within the last ten years. Seibel responded in the affirmative. Bogue then asked if the dismissed charges were pursuant to plea agreements to a lesser charge. Seibel began referencing Exhibit 2 in response to the question. Bridgeman objected to using Exhibit 2 to answer the question. Fergel stated that he could address the question with McDannel when he is called and Duenwald overruled Bridgeman's objection. Seibel listed the following violations: a seat belt violation filed on Jan. 22, 2016 in Charles Mix County; a speeding violation filed in Beadle County on Dec. 12, 2014; a domestic abuse/simple assault charge filed in Jerauld County on Sept. 29, 2014 which was pled down to disorderly conduct; another seat belt violation; four speeding violations in 2014 resulting in fines; a speeding violation in 2013 along with a seat belt violation; and driving with a suspended not revoked license to which McDannel pleaded guilty and paid a fine. Bridgeman objected to Seibel reading from Exhibit 2. Bogue said she was satisfied with the answer.

Bridgeman asked Seibel if, based on her testimony, she and Norm Lingle would have granted or denied this video lottery license had they considered crimes committed only within the last 10 years. Fergel objected, citing speculation



on Seibel's part. Duenwald overruled the objection. Seibel answered that they looked at the application as a whole. Fergel asked who made the final decision to deny the license. Seibel stated that the final decision was made by Executive Director Norm Lingle.

There were no further questions and Seibel was released.

Fergel called Shawn McDannel to testify and he was sworn in by Duenwald. McDannel stated that he has been the owner and operator of Dakota Drywall and Stone for 17 years in South Dakota and started working in construction at the age of 18 in Bemidji, MN.

Fergel asked if McDannel was looking into other business ventures. McDannel stated that he was in the process of renovating the building for The Pour House in Wessington Springs. Fergel asked when the legal entity of The Pour House LLC was established. McDannel answered that it was established in May of 2016 and that he was the sole member. Fergel asked if he had an EIN number for an LLC from the Internal Revenue Service (IRS) and if all appropriate paperwork had been filed with the South Dakota Secretary of State's office. McDannel replied in the affirmative.

Fergel asked if McDannel recognized Exhibit 1. McDannel replied that it was the application for video lottery license he had completed. Fergel asked if he recognized Exhibit 2 and what it was. McDannel stated that he went to the Sheriff's Department and had them print out his criminal history to send to the Lottery. Fergel asked if he sent the document to the Lottery willingly and if it accurately depicted his criminal history. Bridgeman objected and Duenwald overruled the objection. McDannel stated that the document showed the bad choices he had made as a young man and that he had a problem with speeding. Fergel asked if Exhibit 2 was accurate and McDannel answered in the affirmative. Fergel asked if McDannel agreed that Exhibit 2 reflected approximately twenty traffic violations, ten class 1 misdemeanors and two class 2 misdemeanors. McDannel said yes.

Fergel asked that Exhibits 1-5 be admitted into evidence. Bridgeman objected to Exhibit 2 because it contained extraneous information. The objection was overruled by Duenwald and Exhibits 1-5 were entered into evidence.

Fergel asked McDannel to agree or disagree that on Jan. 6, 2015 there was a conviction of disorderly conduct, on Oct. 31, 2012 there was another conviction for disorderly conduct, on May 19, 2011 a conviction of failure to report an accident causing damage, on July 27, 2011 a conviction of failure to report an accident causing property damage and possession of marijuana (a class 1 misdemeanor), on Jan. 13, 2009 a conviction for driving with a revoked license (a class 1 misdemeanor), on April 25, 2008 there was a 2<sup>nd</sup> DUI conviction (class 1 misdemeanor) – all within the last 10 years. McDannel agreed that this was all accurate.

Fergel asked McDannel why he felt he should be granted a video lottery license. McDannel said his driving violations didn't make him a criminal. He explained that the information wasn't all in the criminal report and that the failures to report were accidents where he hit a tree and a sign. He stated that he no longer acts that way, is not proud of his past, and appreciates the time given to him for the hearing. He didn't feel his past driving convictions and criminal record should result in the Lottery denying him a video lottery license.

Fergel had no further questions. Bridgeman asked Duenwald if he should ask his questions of McDannel at that time. Duenwald decided to let Fergel complete his case saying McDannel could be called back to the stand.

Fergel called Norman Lingle to the stand and Lingle was sworn in by Duenwald. Lingle stated his occupation as executive director with the SD lottery for the past 12 years. Lingle described his duties as to insure the integrity and security of the SD Lottery, to ensure the games are honest and fair, and to generate revenue for the State of SD. Lingle's duties also included approving or denying licensure with the SD Lottery.

When asked if he had reviewed Exhibits 1-3, Lingle responded in the affirmative. Fergel inquired when those documents were brought to his attention; Lingle could not recall the exact date but knew it was before Feb. 1, 2017. Lingle stated that he met with Seibel and Hepper to review the documents but said only he and Seibel had input into whether to accept or deny the license. Fergel asked if Lingle reviewed all 18 pages of Exhibit 2 and if he knew of anything in SD Law or rule that would exclude the Lottery from reviewing all the information provided. Lingle stated that he had reviewed all of Exhibit 2 and that he was not aware of any laws or rules excluding the information. Lingle

was then asked if after reviewing Exhibits 1-3 he had made a decision on whether or not to give a license to The Pour House LLC. Lingle stated that he decided the license should be denied, because after looking at the number of arrests included in the application he feared Mr. McDannel would not follow the standards and rules set forth by the Lottery had he received a license. When asked if he considered McDannel's criminal history as an indicator of his inability to follow rules; Lingle answered in the affirmative. Fergel asked if following rules was important to the Lottery. Lingle felt the information he reviewed called into question McDannel's ability to comply with the laws and rules set forth by the SD Lottery. Lingle was then asked if he instructed Seibel to send McDannel Exhibit 4, and he answered that he had.

Bridgeman began his cross examination by asking Lingle how many applications for video lottery license the Lottery received. Lingle stated that there were over 1,350 establishments in the state that were either new or renewed annually. When asked if he recalled denying a license to any other entity due to misdemeanors, Lingle said he did not recall if he had. When asked if in the last 12 years, he had granted a license to a video lottery applicant with a felony on their record, Lingle stated that he would only do that if 10 years had passed since the successful completion of their sentence. Bridgeman inquired if he recalled granting a license to a felon with those circumstances; Lingle could not recall a situation like that. Lingle also could not recall denying or granting a license to an entity based on DUI charges or speeding tickets. When asked if he believed speeding tickets were a reason to deny a license, Lingle said he believed the number and frequency indicated an inability to follow rules. In response to whether he reviewed all charges going back to 1995, Lingle responded that he had reviewed all exhibits in their entirety. Bridgeman then asked if Lingle, Seibel and Hepper had considered the crimes committed in the last 10 years. Lingle answered that they had, but that it was the number and accumulation of the crimes that were being considered. Bridgeman next asked if Lingle believed it a fair statement that if consideration was limited to felonies in which at least 10 years had passed then consideration of misdemeanors should also be limited to those in which 10 years had passed. Lingle again stated that the Lottery looked at the frequency of the offenses and didn't see that the pattern of crime had changed. Bridgeman inquired if 10 years had passed since the resisting arrest charge, and there was no pattern involved, would he have denied the license. Lingle stated that the Lottery wanted licensees who will follow the rules governing video lottery operations. Bridgeman then asked if a 10 year passage of time would not take a crime off the review. Lingle stated again that he looked at McDannel's history as a whole, from a cumulative effect, and at all documents submitted as part of the application.

There were no further questions asked of Mr. Lingle. The State rested its case.

Bridgeman called Sean McDannel to the stand and he was reminded that he was still under oath. Bridgeman asked if McDannel had employees that he paid wages to and McDannel responded that he did. When asked if he had paid all payroll taxes and all taxes due to the IRS, McDannel responded in the affirmative. As to why he wanted to start up The Pour House, McDannel said that people in Wessington Springs wanted a place to drink and play video lottery. Regarding his plan for operating The Pour House LLC, McDannel stated that he had hired Lacy Shimpkey to manage it and that Lacey had experience working for other video lottery establishments as well as business training.

Bridgeman asked if McDannel felt he had been unfairly judged for his past acts. McDannel admitted that in the past he drank and drove a lot and had left the scene of an accident, but said he no longer did those things. He admitted to having issues with speeding, but didn't feel that meant he could not follow rules. He said his speeding problem was because he was trying to get to construction jobs on time. He felt the proof that he can follow rules was that he'd been in business for 17 years and if he didn't follow rules, he wouldn't have paid taxes or had returning customers. He also offered consistently paying his excise and state taxes for his business as further proof.

Bridgeman referenced Exhibit 3, specifically a DUI that took place on May 16, 2007 and was disposed of on July 17, 2008, and asked why it took so long to complete that sentence. McDannel stated that he postponed it as long as possible so he could finish up jobs before serving a 10 day jail sentence. McDannel admitted that he still drinks but not as much, and felt he no longer had a problem with drinking and driving. Bridgeman asked about the Mispriison of a Felony that happened in 1995. McDannel explained that the charges of burglary in the 4<sup>th</sup> degree stemmed from an incident where his friend stole CDs from a vehicle and kept them in McDannel's car. The stolen CDs were found in McDannel's car and he was charged with a felony, but when his friend confessed, the charges were reduced. When asked about the disorderly conduct charges, McDannel stated that those charges were for urinating in public and

arguing with his girlfriend, Lacey Shimpkey, whom he is still dating and intends to put in charge of operating The Pour House, LLC.

When asked to explain to the Commission why he'd like a video lottery license, McDannel stated that he already had an establishment, would like to make money off of video lottery, and would like to add a 2<sup>nd</sup> bar in town for the public to enjoy. When asked if he would follow the rules, McDannel said he would and that he followed the rules for his current business. He stated that he had complied with E-Path and excise taxes even though the bar hadn't opened yet.

Neither Bridgeman nor Fergel had any further questions.

Duenwald asked how McDannel got from Sioux Falls to Wessington Springs. McDannel said that it was partly due to his girlfriend, Lacey Shimpkey, and partly because word of mouth had spread about his drywall business. He said he'd been in Wessington Springs for three years but his job takes him all over the state. McDannel stated that he had three employees and subcontracted a lot of the work. Duenwald then asked if he would continue to run the bar without a video lottery license. McDannel said he would because he had too much money invested to back out of the project. Duenwald mentioned that McDannel had referenced some work he'd done with non-profits in his appeal letter (Exhibit 5), and wondered what type of work it was. McDannel stated that he donated money three times a year to Farm Financial which goes to the city in trade for advertising at a few rodeo events. Duenwald then asked how many hours he put in at his construction job. McDannel responded that he had put in 214 hours since March 9<sup>th</sup>.

There were no further questions and no further witnesses from either side.

When asked for closing arguments, both sides agreed that since no decision would be made until June 1<sup>st</sup>, they'd rather argue the law with briefs in lieu of closing arguments. Fergel asked that a briefing schedule be set so all conclusions of law would be ready prior to the next meeting. Bridgeman stated he was open to a shorter briefing but asked that it be done after April 15. Duenwald stated that the burden of proof would be briefed by both simultaneously and due April 24, 2017, with final simultaneous replies due two weeks later on May 12, 2017.

The hearing went off the record at 1:18 p.m.

A 10 minute break was taken at 1:19 p.m. and the meeting was back in session at 1:26 p.m.

#### **VIDEO LOTTERY REPORT**

*Director of Video Lottery and Security Robyn Seibel reported on the following:*

Seibel reported on net machine revenue and terminal and establishment averages for FY17 as of Feb. 28, 2017. Net machine income (NMI) for FY17 was \$138.79 million which was a 1.50% increase over FY16. The number of terminals was at 9,060, which was up 1.20% from the previous year. The number of establishments was at 1,353, which was .52% more than in FY16.

Video lottery FY17 revenue projection as of Feb. 28, 2017 was \$104.30 million versus \$102.76 million in FY16.

#### **PUBLIC RELATIONS/ADVERTISING REPORT**

*Director of Advertising and Public Relations Kelly Thompson reported on the following:*

##### BIG WINNERS CLAIMED (SINCE 12/2/16)

###### LOTTO GAMES

Joan Minor of Beloit, IA won the \$138,779 Dakota Cash jackpot in the Feb. 15 drawing. There was one \$50,000 Powerball winner from Whitewood in the March 18 drawing, three \$9,000 Hot Lotto winners from Aberdeen, Sioux Falls and Rapid City, and two \$3,000 Hot Lotto winners from Brandon and Sioux Falls.

###### INSTANT GAMES

There were nineteen top prize winners of \$2,200 - \$500,000 since Dec. 2, 2016 in eighteen different games.

## POWERBALL POWER CRUISE

The promotion began Feb. 6 with 24 state lotteries participating. All Powerball tickets purchased between Feb. 6 and March 29 were eligible. Six South Dakota players won a Caribbean cruise for 2 on the special Royal Caribbean Powerball ship that will set sail in January of 2018. Two drawings were held, the first was March 1 with 2 winners randomly drawn and the second was March 31 with 4 winners drawn. As of March 18 there were 2,949 active players participating with 15,626 tickets entered and 11,101 entries completed. 35% of the entries were made through the mobile app. It was the first time the Lottery utilized entry by app, but since they're in the process of developing a mobile app for Lottery, they were anxious to see how players like entering through the Power Cruise app. A survey asking players what they liked about the Power Cruise app was sent out and posted to social media to gain an understanding of players' wants regarding second chance entries by app.

## PLAY IT AGAIN (PIA) - \$30K DASH FOR CASH

The \$30K Dash for Cash second chance promotion began at the end of August 2016 and included monthly drawings of 3 winners of \$100 in scratch tickets or a gift card and a \$30,000 grand prize drawing that was held Feb. 28, 2017. There were 204,601 total entries and the grand prize winner was Linda Price of Britton.

## PLAY IT AGAIN – MONTHLY MOOLA

Monthly Moola is the new second chance promotion that began March 1 and runs through June 30. The sales division was looking to change up how PIA works to improve scratch ticket sell-thru and reignite interest in the program. The changes include a monthly cash prize of \$2,500 instead of one big \$30,000 cash prize at the end of the promotion with three winners drawn monthly (one cash prize of \$2,500, 2 - \$100 in scratch tickets). The first drawing was scheduled for March 30, 2017.

## PROBLEM GAMBLING AWARENESS MONTH

The National Council on Problem Gambling program runs March 1 thru 30. Usually the Lottery blacks out the rest of its advertising during this period, but couldn't this year due to the Powerball Power Cruise promotion. They were instead alternating campaigns so advertising wouldn't conflict. Problem gambling advertising consisted of commercial radio, promoted posts on Facebook and Twitter, website updates, Players Club messages, and terminal messages to retailers.

## MOBILE APP

The Lottery has completed discovery and research on the mobile app project and is working on strategy and design. They are working with the Bureau of Information and Telecommunications (BIT) to vet and test a content management system and customer relationship management system. Lawrence & Schiller's (L&S) user experience map which determined how the user moved through the app was approved by the Lottery. BIT and L&S were asked to begin collaboration on the app design based on that user experience map with a target launch date of this summer.

## ADVERTISING CONTRACT

The initial two-year base contract with Lawrence & Schiller will be up on June 30. There are three one-year extensions available for a total contract of five years. The Lottery will bring its recommendation to the next meeting for commission approval.

Commissioner Putnam asked the Lottery to bring some performance measurements to the next meeting for the Commission to review.

## SALES REPORT

*Sales Director Justin Pierson reported on the following:*

Instant game sales were down 5.49%, sitting at \$17.13 million versus \$18.12 million the previous year.

- New Game releases
  - January – The X-Family 5X, 10X, and 20X
  - February - \$100,000 Jackpot (purple colored ticket), new \$20 ticket \$250,000 Show Stopper, Bullseye Cash, and Jokers Wild
  - Coming up in April is \$10 ticket Silver 7's

Lotto sales were down 28.91% at \$15.42 million versus \$21.69 million the previous year. Last year's \$1.5 billion Powerball jackpot is the reason for the decline.

#### **GAME BY GAME**

- Powerball was down 37.38%, at \$9.43 million versus \$15.06 million the previous year.
- Mega Millions was up 30.3%, at \$2.56 million versus \$1.97 million the previous year.
- Hot Lotto was up 20.06%, at \$1.89 million versus \$1.58 million the previous year.
- Dakota Cash was up 27.7%, at \$1.76 million versus \$1.37 million the previous year.

#### **REVENUE PROJECTIONS**

- Instant - \$5.04 million
- Lotto - \$6.86 million
- Video - \$104.30 million
- TOTAL - \$116.20 million

Commissioner Shorma asked if sales were on track if the 2016 anomaly of the billion dollar Powerball jackpot was removed from the equation. Lingle answered that year over year sales were trending up, but that jackpots really increase sales and Powerball makes up around 50% of total lotto sales.

#### **NEXT MEETING DATE**

Director Lingle was looking at June 1, Aug. 24, and Dec. 14, 2017, for the meeting dates and offered a tour of the Lottery office to any Commissioners interested.

#### **ADJOURNMENT**

Commissioner Dykstra moved to adjourn the meeting. Commissioner Faehn seconded. Roll was called: Aye – Bogue, Dykstra, Faehn, Kafka, Mickelson, Putnam, Shorma. Motion carried. Chairman Putnam adjourned the meeting at 1:48 p.m.