

October 1, 2007

The Honorable Timothy M. Kaine
Governor
Commonwealth of Virginia
Patrick Henry Building, 3rd floor
Richmond, VA 23219

Dear Governor Kaine:

I am pleased to provide our report of monthly activities and financial update for the months of July and August 2007, as well as a recap of FY 2007 activities, as required in Section 58.1-4006 of the *Code of Virginia*.

Fiscal Year 2007 Lottery sales exceeded the official forecast, and finished the year only \$3 million behind last year's record levels. Total sales of \$1.362 billion were \$57.9 million (+4%) more than the forecast. Most of the excess sales were the result of new and expanded products introduced during the year and not included in the official forecast, specifically \$13 million from Fast Play Bingo, \$6.6 million from the first Millionaire Raffle, and \$25 million from the expansion of daily games' drawings. Fiscal Year 2008 began with sales totaling \$236.3 million in July and August, up \$31.5 million (+15%) compared to last year, primarily due to the \$330 million Mega Millions jackpot roll experienced in August 2007.

Fiscal Year 2007 net income of \$437.2 million was \$17.8 million (-4%) less than the prior year's earnings, but \$31.8 million (+8%) ahead of the forecast. Fiscal Year 2008 began with profits totaling \$84.1 million through August, up \$20.7 million (+33%) from last year.

We are very proud of the year just ended and our contributions toward public K-12 education funding in Virginia, and thank you for celebrating our record year with us at the news conference on September 5th. As for Fiscal Year 2008, we continue to monitor and assess Virginia sales and profits. It should be anticipated that the Virginia Lottery will continue to creatively address the challenges ahead. As always, we will participate in the statewide revenue re-forecasting process, coordinated through the Department of Taxation, this fall.

Please let me know if you have any questions or if you would like more information.

Very truly yours,

Sheila Hill-Christian

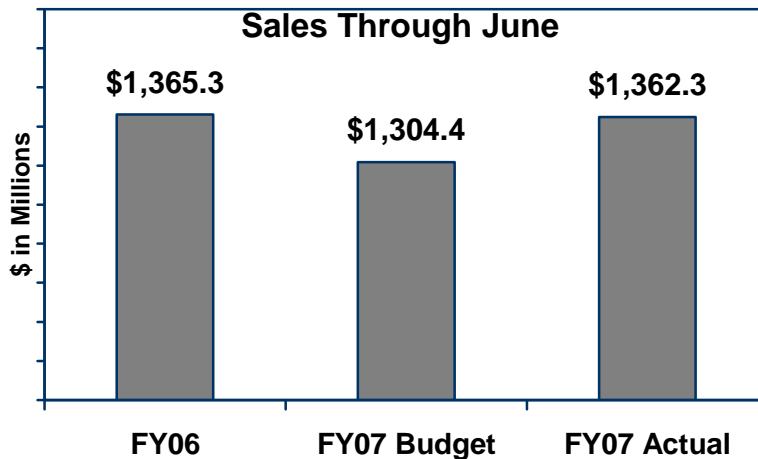
- c: The Honorable John H. Chichester, Chairman – Senate Finance Committee
- The Honorable Vincent F. Callahan, Jr., Chairman – House Appropriations Committee
- The Honorable Harry R. Purkey, Acting Chairman – House Finance Committee
- The Honorable Wayne M. Turnage, Chief of Staff – Office of the Governor
- The Honorable Jody M. Wagner, Secretary of Finance
- Mr. Richard D. Brown, Director – Department of Planning & Budget
- Mr. David A. Von Moll, State Comptroller
- Ms. Elizabeth B. Daley, Staff Director – Senate Finance Committee
- Mr. Robert P. Vaughn, Staff Director – House Appropriations Committee

VIRGINIA LOTTERY
Report to the Governor and
Selected Members of
the General Assembly
October 1, 2007

Fiscal Year 2007 Sales

Lottery sales for the 2007 fiscal year totaled \$1.362 billion, which was \$3 million (-0.2%) less than the prior year, but \$57.9 million (+4.4%) more than the forecast.

Sales increased in all product categories except for the jackpot games. Scratcher sales were up \$9 million or 1% compared to last year, and \$5.6 million (+0.8%) ahead of budget. Daily games (Pick 3, Pick 4, and Cash 5) sales finished strong, up \$18.3 million or 4% over last year due to the addition of Sunday drawings in January 2007. Compared to budget, daily game sales of \$472.8 million were \$28.7 million (+6.5%) ahead of forecast. Sales of the jackpot games, Mega Millions and Win for Life, declined \$49.9 million (-22.5%) from last year, but \$3.9 million (+2.4%) ahead of forecast.



July – August 2007 Sales

Fiscal year 2008 began with sales of \$236.3 million, an increase of \$31.5 million (+15.4%) compared to FY2007. The most significant increase occurred in the jackpot games, up \$20 million due to the Mega Millions jackpot roll to \$330 million in August 2007. Daily games' sales were also strong, up \$6.5 million as a result of the additional drawings in FY2008 compared to last year. Scratcher sales were very near last year's level, up \$3.1 million or 3% from last year.

Fiscal Year 2007 Expenses

The overall prize expense rate (prize expense as a percent of sales) finished the year at 58.1%, 1.4% higher than FY2006 and 0.4% lower than budget. The scratcher prize rate increased 0.8% to 66.6%, and the daily games prize rate of 49.6% was 4.1% more than FY2006 and 0.3% more than the expected rate. Jackpot prize expenses were 48.2% of sales, down 2.7% from last year due to the favorable jackpot rolls and more favorable long-term bond rates.

In spite of the slight overall sales decline, retailers earned \$0.3 million more than last year for a total record \$76.5 million in earnings. Administrative operating costs, including ticket printing and distribution expenses, were \$1.7 million less than during the same period last year.

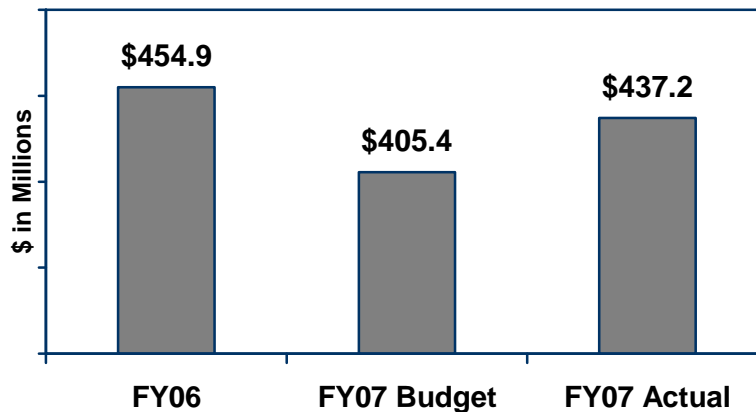
July – August 2007 Expenses

The luck of the draw continued to dampen overall prize expense rates, with daily games' prizes totaling only 41.2% of sales. Overall, prizes comprised 54.7% of total sales, compared to 58.5% of sales for the same period in FY2007. Retailer compensation increased \$1.2 million due to the increase in sales, with the retailer compensation rate steady at 5.4%. Operating expenses totaled \$9.5 million, up \$0.4 million compared to FY2007 year to date.

Fiscal Year 2007 Net Income

Fiscal Year 2007 ended with profits totaling \$437.2 million, \$17.8 (-4%) million behind FY2006 but \$31.8 million (+7.8%) ahead of forecast. The significant increase in earnings over the forecast was the direct result of new and expanded product offerings in FY2007 that were not included in the official forecast.

Net Income Through June



July – August 2007 Net Income

The lower overall prize expense rate combined with sales increases resulted in earnings of \$84.1 million, up \$20.7 million (+33%) compared to last year.

CONTRIBUTIONS TO DEBT SETOFF & LITERARY FUND

Pursuant to the Setoff Debt Collection Act, the Lottery made payments to the Department of Taxation totaling \$1,231,535 for Fiscal Year 2007. Also, the Lottery transferred unclaimed prizes of \$10,747,271 for the year.

For the 2007 fiscal year to date, the Lottery made payments to the Department of Taxation totaling \$156,333. Unclaimed prizes totaling \$1,393,886 were also transferred to the Literary Fund for the months of July and August 2007.

MEETINGS

The State Lottery Board held a regularly scheduled business meeting on Wednesday August 1, 2007, in Richmond. The Board reviewed financial results and upcoming games as part of their regular business. The next Board meeting is scheduled for October 24, 2007, in Richmond.

On Monday September 17, 2007, I was invited to speak to the House Appropriations Committee about our FY2007 results, and plans for the 2008 fiscal year.