

May 22, 2008

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

Dear Governor Kaine:

I am pleased to provide our report of monthly activities and financial update for the month of April 2008, as required in Section 58.1-4006 of the *Code of Virginia*.

Sales for the month of April 2008 totaled \$115.7 million, down \$7.1 million (-6%) from last month, but \$1.9 million (2%) more than April 2007. For the year to date, sales totaled \$1,154.9 million, which was \$24.0 million (+2%) more than the same period last year. April net income totaled \$37.7 million, for year to date earnings of \$382.2 million, up \$21.4 million (+6%) compared to the same period last year.

Fiscal Year 2008 continues with very strong profits, primarily from the strength of Mega Millions sales resulting from the unusually strong jackpot growth during the period. While total sales continue to lag behind the forecast, with a cumulative shortfall of \$7.1 million, net income is very close (+ \$0.2 million) to the revised net income target included in Chapter 847 for FY2008. Strong net income, in comparison to sales shortfalls, is the result of lower than expected prize expenses and strong interest earnings on cash balances. The main sources of this additional operating net income – low prize expense rates and large jackpots – are both environmental factors and will continue to be unpredictable, by definition, especially over the short term.

Lottery net income goals for the final two months of the year will be negatively affected by (1) the loss of interest earnings because of the required interim transfers that were not planned when the original forecast was prepared and (2) the delayed introduction of one product and the cancellation of another from the original sales plan for FY2008. These adjustments to the operating plan were made for business reasons, to best position Lottery product offerings both in terms of consumer demand and operational capacity. The delayed product launch is the result of the lottery systems conversion project taking longer than originally anticipated and related software development delays for new fast play products; the original forecast anticipated new fast play product offerings in February and May, but in actuality there will only be one new offering introduced in early June. The planned June raffle was cancelled because of lower than expected consumer response to the holiday raffle and further research into the best timing and frequency of these types of game

offerings based on other lotteries' experiences. While we continue to strive to generate additional profits for K-12 public education, meeting the net income targets for May and June will require the positive influence of environmental factors beyond our control – low prize payouts, in particular. The jackpot run that ended in May helped to support sales and profits; however, there is not sufficient time remaining in this fiscal year for the jackpot to grow to levels that would generate significant sales and profits in excess of the levels already anticipated.

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

Very truly yours,

Paula I. Otto

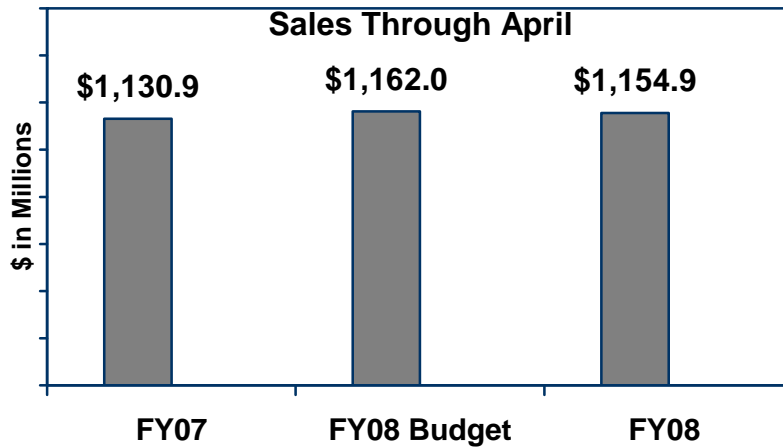
c: The Honorable Charles J. Colgan, Chairman – Senate Finance Committee
The Honorable Lacey E. Putney, Chairman – House Appropriations Committee
The Honorable Harry R. Purkey, Chairman – House Finance Committee
The Honorable Wayne M. Turnage, Chief of Staff – Office of the Governor
The Honorable Jody M. Wagner, Secretary of Finance
Richard D. Brown, Director – Department of Planning & Budget
David A. Von Moll, State Comptroller
Elizabeth B. Daley, Staff Director – Senate Finance Committee
Robert P. Vaughn, Staff Director – House Appropriations Committee

VIRGINIA LOTTERY
Report to the Governor and
Selected Members of
the General Assembly
May 22, 2008

Sales

Lottery sales for the 2008 fiscal year through April totaled \$1,154.9 million, which was \$24.0 million (+2.1%) more than the prior year. However, sales were \$7.1 million (-0.6%) lower than expected for the year.

Scratcher sales were down \$5.6 million (-1.0%) compared to last year. Daily games (Pick 3, Pick 4, and Cash 5) sales increased \$236,000 or 0.1% over last year. Sales of the jackpot games, Mega Millions and Win for Life, increased \$25.2 million (+17.3%) from last year due to the incidence of significantly higher Mega Millions jackpots during the current fiscal year. Fast Play Bingo sales are down \$4.6 million or (-43.3%) from last year; this product launched in February 2007, and strong initial sales followed by a continual decline are typical for this type of product. Fiscal year 2008 also includes sales of raffle (+\$8.8 million) that are not included in last year's sales totals.

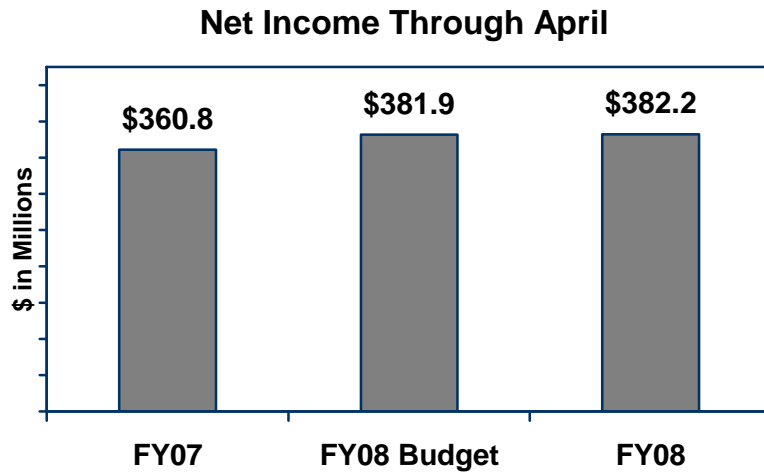


Expenses

Prize expense rates for the year continue to be below the statistically expected levels. Overall, prizes comprised 57.2% of total sales, compared to 58.1% of sales for the same period in FY2007 and 57.4% as expected for the current year. Retailer compensation increased \$0.9 million because of higher sales. The retailer compensation rate is 5.6%. Operating expenses totaled \$59.2 million, an increase of \$2.6 million (+4.5%) compared to FY2007, but nearly \$5.8 million (-9.8%) less than budgeted for the year.

Net Income

The lower overall prize expense rate combined with sales increases resulted in net income of \$382.2 million for the FY2008 year to date, up \$21.4 million (+5.9%) compared to last year and \$0.2 million (+0%) compared to budget.



CONTRIBUTIONS TO DEBT SETOFF & LITERARY FUND

For the 2008 fiscal year to date, the Lottery made payments to the Department of Taxation totaling \$899,610. Unclaimed prizes totaling \$8,798,294 were also transferred to the Literary Fund for the first ten months of fiscal year 2008.

MEETINGS

The next meeting of the State Lottery Board is scheduled for July 9, 2008, in Richmond.