

MINUTES OF THE SENATE FEDERAL AND STATE AFFAIRS COMMITTEE.

The meeting was called to order by Chairperson Senator Nancey Harrington at 10:30 a.m. on January 17, 2001 in Room 245-N of the Capitol.

All members were present.

Committee staff present:      Russell Mills, Legislative Research Department  
   Dennis Hodgins, Legislative Research Department  
   Theresa Kiernan, Revisor of Statutes  
   Nikki Kraus, Committee Secretary

Conferees appearing before the committee:      Randy Tongier, Legislative Division of Post Audit  
   Ed Van Petten, Deputy Executive Director, KS Lottery

Others attending:      See Attached List

Chairman Harrington started the meeting by introducing Mr. Randy Tongier from the Legislative Division of Post Audit.

Mr. Tongier stated that he would be presenting a financial compliance audit done on the Kansas Lottery by an outside audit company CPA firm called Berberich Trahan & Co., P.A. which contracts with the Office of Legislative Post Audit under a statutory requirement for annual financial audits for the lottery which has existed since the late 1980's. He stated that it does not address some of the concerns and allegations which the committee may have against the lottery from reading about it in the paper. He stated that what the report does do is address three main areas. He stated that the first was financial reporting, which includes financial papers which show the results of the lottery's operation for each fiscal year, and the procedures used to prepare those statements so that those records are a fair presentation of what actually happened at the lottery, and that they are presented with what are called generally accepted accounting principles. Mr. Tongier stated that the second area covered by the audit report was compliance with legal requirements as they relate to financial reporting. He stated that the final area covered by the audit was internal controls, which is financial accounting and related procedures that are designed to ensure accurate accounting and financial reporting.

Mr. Tongier then presented a memorandum entitled "Kansas Lottery, Financial and Compliance Audit Report, Years Ended June 30, 2000 and 1999". (Attachment 1).

Chairman Harrington then asked for questions, and there were none.

Chairman Harrington then introduced Mr. Ed Van Petten, Acting Deputy Executive Director for the Kansas Lottery and stated that we would be holding confirmation hearings on Mr. Van Petten in the next week or so.

Mr. Van Petten stated that he appreciated the opportunity to present before the committee. He stated that he brought along several of the top officials from the lottery in order to assist him. He went on to introduce them. He introduced Pat Red, Personnel Manager, Tom Hofts, Director of Sales and Marketing (because the acting director of sales resigned, and for the time being, Mr. Van Petten stated that he was combining the two), Dave Mackey, Information Resource Manager for the Lottery, Gary Herman, Security Division, Gary Oliver, Computer Quality Assurance Management (which does the auditing of the computer systems), Pete Coker, Assistant Attorney General, Gary Seville, Comptroller, and Jim Geradano, Internal Officer.

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Mr. Van Petten then went on to describe the information provided in the packets he distributed to the committee members, including a sheet drafted by the Lottery office based upon the budget recommendations of the governor. (Attachment 2).

Mr. Van Petten stated that Mr. Russell Mills had provided the committee a similar sheet the day before but that this sheet incorporated the payment of \$80,000 for the fund for problem gambling. He stated that there was also a sheet which was from the department of commerce and housing which breaks down by county the payments made for economic development. He stated that the Lottery thought that would be beneficial to the committee members to determine the benefits for their particular areas.

Chairman Harrington stated that she wished to share with the committee that the Secretary of Commerce and Housing, Gary Sherrer, would be with the committee next week to describe how he makes the determination to administer the economic development initiative.

Mr. Van Petten went on to describe the activity sheet inside of the packet he gave to the committee. (Attachment 3).

Mr. Van Petten pointed out the existence of a flow chart in the packet, and stated that it illustrated how lottery funds flow. (Attachment 4).

Mr. Van Petten referred the committee to a tracking study from 1997 which he stated was a part of a demographic survey showing age, education, and income levels of players of the lottery. (Attachment 5).

Mr. Van Petten went on to his testimony. (Attachment 6).

Mr. Van Petten distributed a packet from the Kansas Department of Commerce Housing entitled "FY 2000 EDIF Awards by County". (Attachment 7).

Chairman Harrington thanked Mr. Van Petten, and then asked for questions and recognized Senator Gooch.

Senator Gooch stated that he would like to know if Mr. Van Petten could explain the fact that the investigation of the misuse of Kansas Lottery computers did not find anyone guilty of wrongdoing.

Mr. Van Petten stated that in order to clarify, the two computers involved in those situations were personal computers which had no relationship to the gaming system itself. He stated that both computers were used for maintaining web page information. He stated that the first situation, the computer which was involved was a non-secure computer, which meant that anyone could use it because there was no password required. He stated that anyone who was present in the lottery building could have placed that information on the hard drive, so he had not seen any way to prove who was responsible.

Senator Gooch stated that he understood that these computers were public and that they did not deal with money, but that it reflected on the people and the inability to limit those possibly accountable down to less than eight people. He stated that it seemed a little weak to him.

Mr. Van Petten stated that Senator Gooch was absolutely right, and within a month after that, software was installed in all the computers to require individual passwords so that any actions taken now can be audited. Mr. Van Petten stated that passwords were also required for the gaming system.

Senator Gooch then stated that the next thing that he wanted to ask about was in the audits that had been done, if there had been any audit that Mr. Van Petten could point to which would give any indication of a desire to do something illegal.

Mr. Van Petten said that he would try to answer the question to the best of his ability. He stated that in addition to showing who accesses the gaming system, the auditing software that has been installed at this

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time audits anyone accessing the financial information maintained on the computer as a result of sales of products which shows sales at the retail level, so those figures would not be able to be tampered with in any way or modified without an indication by profile who it was who accessed that information and made any type of modification. He stated that it would show up in the auditing at this time, but that it had not been the case previously, and that with the audit software which had been installed in the last quarter, that was the case. Mr. Van Petten stated that the information on those computers was the information used by the Finance Department in developing the financial information which is present in the auditor's review.

Senator Gooch stated that he was concerned with the accuracy of the information provided by Mr. Van Petten about who plays the lottery. He asked Mr. Van Petten to give him an indication of how that demographic sheet was developed and obtained Mr. Van Petten stated that there was a detailed survey developed by Market Strategies, Inc., and it was conducted as a telephone survey.

Senator Gooch stated that he felt that this method of obtaining information was worth the paper on which it was written and that he believed that he could conduct a survey of one hundred homes and not one would have been called.

Chairman Harrington suggested to Senator Gooch that his question might be better asked at the hearings because it might be better and more clearly answered during that time.

Senator Gooch replied that he felt that the question was answered very directly and that he had not had a problem with the response.

Chairman Harrington thanked Senator Gooch for his question and recognized Senator Vratil.

Senator Vratil asked Mr. Van Petten if he was able to tell the committee what had been the size of the sample for the survey.

Mr. Van Petten stated that he would defer to Mr. Hofts, Acting Director of the Departments of Sales and Marketing for the Kansas Lottery, to answer that question.

Mr. Hofts stated that the sample size had been 1,000 valid responses, which were weighted geographically across the state balanced by population per county.

Senator Vratil asked what the margin of error would have been with a sample that size weighted graphically.

Mr. Hofts responded that the statistical probability was 95 per cent, and that the margin of error was 5 per cent.

Senator Barnett stated that the day before, the committee had spoken about statutes with GTECH regarding contracts made by the KBI, and that he wanted to know if the lottery did background checks with KBI.

Mr. Van Petten stated that for most individuals, the security division of the lottery handles background checks. He stated that the KBI would be used for information obtained from the national computer system on criminal history and record checks. He stated that occasionally with interstate companies, the lottery would review additional information obtained by other states as well. He stated that recently they had obtained some records from California's security division regarding security information.

Senator Lyon stated that he was interested in Mr. Van Petten speaking more about the security audit of the lottery.

Mr. Van Petten stated that a contract was made with RMS Lab Company which was a subsidiary of H&R Block, and specializes in these types of security audits. In response to further questions from Senator

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Lyon, Mr. Van Petten explained that the audit lasted two to three months and covered not only computer security, but also warehouses and retailers. Mr. Van Petten also stated that he did not believe that the gag order placed on certain lottery related issues would reveal any new information to the public.

In response to Chairman Harrington's questions, Mr. Van Petten explained that one of the computers had a commercial pornographic video on it. He stated that two other computers which had been found with inappropriate material on them also, but that none of the three had depicted lottery workers. Mr. Van Petten went on to assure the Chair that other inappropriate material found on lottery computers, including a picture of a worker posed in front of a Nazi flag in caricature, would not happen again and that those employees had received counseling for their actions. He went on to say that he would not condone any such action. He also stated that the background check for workers at the lottery included contacting all previous employers possible and reviewing the work habits of the individual.

Chairman Harrington stated that it was unfortunate how Mr. Van Petten had inherited all of the lottery problems, and he responded that he had a great deal of help. The committee complimented Mr. Van Petten on his thoroughness.

Chairman Harrington reminded the committee that next Tuesday the Commerce and Housing Secretary Gary Sherrer would come in to conclude information on **SB 22** - Extension of KS Lottery until 2007, and that the hearings for the bill would begin Wednesday.

Senator Vratil moved to amend the minutes from January 10, 2001.

Senator Gooch moved to accept the amended minutes from January 10 and January 11, 2001; Senator Vratil seconded the motion. The motion passed.

The meeting adjourned at 11:50 a.m.

The next scheduled meeting will be at 10:30 a.m. on January 18, 2001.