

**Regular Meeting of Board of Directors  
New Mexico Lottery Authority  
August 23, 2017  
MINUTES**

**Call to Order:** Board Chair Dan Salzwedel called the meeting to order at 1:16 p.m. and asked for a roll call. Present and constituting a quorum were: Mark Koson; John Kubiak, Dan Salzwedel, Paul Guerin and Sal Baragiola. Amy Bailey and Claude Austin were absent.

Present from NMLA were; David Barden; Sylvia Jaramillo; Evelyn McKnight, Karla Wilkinson, Wendy Ahlm, Michael Boland and Wilma Atencio.

Also present were; Jon Zajdel, Steve Beck and Terry Patterson with Intralot; Abel Romero and Othiamba Umi with Think New Mexico.

**Approve Proposed Agenda:** D. Salzwedel entertained a motion to approve the proposed agenda. P. Guerin made a motion to approve the proposed agenda; second by J. Kubiak. Carried; 5-0.

**Approve Minutes of June 07, 2017 Board of Director's Meeting:** D. Salzwedel entertained a motion to approve the June 7<sup>th</sup> minutes. J. Kubiak moved to approve the minutes; second by M. Koson. Carried; 5-0.

**Public Comment:** Abel Romero stated that he is in support of the 30% mandate. He has friends who are recipients of the lottery scholarship program and that it is a great program for NM students. A. Romero's only concern is that the legislature has been trying to eliminate the mandate for the past several years and while there has been discussion that increasing prize payouts will yield a larger dollar amount return to the fund, A. Romero feels that since the 30% mandate, the return to the scholarship fund has been steady and funds have been available for students to continue their education.

## **REPORTS:**

### **Security Operations – S. Baragiola, Committee Chair:**

**Lotto America Game Rules:** S. Baragiola reported that this item was presented by K. Wilkinson at the Security Operations committee for review and discussion. The committee recommends to proceed with the approval process for this game. K. Wilkinson reported that Hot Lotto will be ending on October 28, 2017 and replaced with a new multi-state game called "Lotto America." The game will go on sale November 12; the first draw will occur on November 15, 2017. This will be a \$1.00 game with a starting Jackpot of \$2 million dollars. 14 states will be participating including New Mexico. The states are: Delaware, North Dakota, Iowa, Oklahoma, Idaho, South Dakota, Kansas, Tennessee, Maine, Vermont, Minnesota, West Virginia and Montana. New Hampshire will join in January 2018. All participating states were asked to submit marketing ideas for the new logo and the logo submitted by NM was selected. A great achievement for NM. This drawing will be performed using a draw ball machine and not using a random number generator.

M. Koson asked why the other BIG US Lotteries aren't part of the group. D. Barden reported that this group is comprised of the MUSL Hot Lotto Group, which was under performing during the past few years and Lotto America is the replacement game. This game is for states that don't have the population as other big states and that can support the \$2 million jackpot. Arizona and District of Columbia have both expressed interest in joining the group.

J. Kubiak asked if the new game would adversely impact the 30% mandate? D. Barden reported that the new game would have no impact on the mandate. This game has the same payout as Hot Lotto - 50%.

S. Baragiola made a motion to approve the Lotto America Game Rules in accordance with the memo and attached game rules as presented; second by P. Guerin. Carried; 5-0.

D. Salzwedel asked D. Barden to provide a general overview on game concepts. D. Barden reported that all online games (PB, MM, Hot Lotto) are similar in nature and all have a set payout across the board. Online games cannot be controlled by each individual state in terms of payout percentage. Changes to any particular game may take up to a year to achieve. Scratcher tickets are the only games lotteries can control in terms of payout. Each lottery has its own formula based primarily on their budget.

**Website Privacy Policy & Practices:** S. Baragiola reported that this item was presented by W. Ahlm at the Security Operations committee earlier where it was reviewed and vetted. The changes outlined in the memoranda does not change the intent of the policy, but merely clean-up/clarification language, administrative changes. The committee recommends the acceptance of the changes. The changes are:

- remove “VIP Account collection information.” This information is being adopted in our internal rules that pertain to the gaming side of operations.
- remove last sentence under ‘Linked Sites’. Sentence reads, ‘Please see the Legal Disclaimers on this site for further information about linked sites.’ There is no additional information or necessity for further linked site information at nmllottery.com.
- remove reference to the ‘Contact Page contained on this website.’ The site structure of nmllottery.com has changed and contact information for the Lottery is available in the footer of all pages at nmllottery.com.

S. Baragiola made a motion to accept and approve the Website Privacy Policy & Practices as presented; second by P. Guerin. Carried; 5-0.

S. Baragiola commented that at the August 17, 2016 meeting, the Board approved to allow the CEO and Executive staff to make editorial and/or corrections/deletions/omissions to any policy without impeding a substantive change to the intent of the policy and wanted to remind all board members of this approval given to lottery staff. D. Salzwedel stated that any editorial changes to policies external or internal do not need to be presented to the full board of directors. If the intent of the policy changes, those policies need board approval.

**Other:** None.

**Finance Audit – M. Koson, Committee Chair:**

**Approve Minutes of June 07, 2017 Finance Audit Committee Meeting:** M. Koson moved to approve the minutes; second by J. Kubiak. Carried; 5-0.

**Financial Statements:** M. Koson reported that S. Jaramillo presented the financial statements to the finance audit committee and deferred to S. Jaramillo. S. Jaramillo reported that she will be presenting three documents this afternoon and will begin with the FY 2017 Financial Statements. For FY17, the lottery has returned \$37.8 million to the Legislative Lottery Scholarship fund and has met the statutorily required 30% return each month. The net revenue is nearly \$287,500 more than the FY17 revised budget, but nearly \$5.8 million less than fiscal year 2016 – a 18.3% decrease. We have now returned over \$738.7 million to the State of New Mexico for education since the inception of the Lottery.

FY17 net instant sales were approximately \$72.4 million, whereas last year they were \$83.1 million. Instant ticket sales have decreased more than \$10.7 million from last year or a 12.9% decrease which represents about \$3.2 million dollars less to the scholarship fund. The lottery couldn’t sustain the FY16 sales for instant tickets due to our 30% net return. Instant sales surpassed the revised budget by \$1.3 million and were \$10.6 million less than the original budget.

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The average payout last year was 60.75%; in our record year in 2007 before the 30% mandate, we were at 63.13%. Calculating the numbers for 2017 using the number from 2007 of \$91.4 million and even though we would be returning 28%, the lottery would be returning after all costs, at least \$3 or \$4 million more.

Even though the percentage is less, the dollars would be more and the lottery scholarship gets paid with dollars and not a percentage. Increasing prize payout generates more dollars; you can see that when the CEO increased the prize payout two years ago, the scholarship received more dollars.

S. Jaramillo reported that she conducted a rough calculation – if the lottery kept increasing its sales at a rate of 4%, which was the average rate until 2008, the lottery would've returned \$60 million dollars more to the scholarship fund. With our current expenses, we have lost \$60 million in the 10 years since the mandate went into effect.

D. Barden reported based on industry statistics the rest of the world every year had a 5.51% increase; 51% over a ten-year period. The lottery was at a -1% over the same 10-year period.

Net Drawing Sales for FY17 were approximately \$53.6 million - \$414 thousand less than the revised budget, nearly \$17.6 million less than FY16 which had sales at \$71.2 million. The online sales difference was a result of PB sales. The lottery had a decrease from FY16 to FY17 – about \$17 million which was a direct result from the \$1.6 Billion PB Jackpot run-up.

Mega Million sales were \$853 thousand less than last year; Roadrunner Cash were \$253 thousand less than last year; Hot Lotto sales were nearly \$11 thousand more than last year and PICK 3 sales were \$475 thousand more than last year. Total Operating revenues for FY 2017 were nearly \$126.1 million - \$910 thousand more than the revised budget. Nearly \$28.3 million less than last fiscal year (*\$17 million PB sale losses and \$10 million in instant ticket sales losses*)

Non-Operating revenues are ahead of the budget by \$41 thousand dollars. Total game expenses at the end of the year were 99.79% of the revised budget, while operating revenues at the end of the year were 100.73%; both tracking within 1% of each other.

Actual game expenses were 66.57% of gross revenue and budget was 67.22%; again, less than budget.

Operating expenses ended the year at 3.41% of total gross revenue. Costs were held as much as possible and came in less than budgeted amounts.

Comparing each line item – operating expenses compared with last fiscal year shows a \$598 thousand decrease with \$259 thousand for salaries, wages and benefits. In addition, by purchasing this building we have saved over \$200 thousand over leasing the property. We have also save \$11 thousand in utilities by switching to LED lights in our warehouse.

J. Kubiak asked with the reduction in salaries, wages and benefits are we reaching a point where our mission will be compromised with not having the proper staff? D. Barden reported that's a great question and every time the lottery meets with the LFC we hear, you have to cut, you have to reduce costs but you cannot cut your way into providing more money for scholarships when you have already cut, cut, cut. At some point the dynamics have to change; rethink how we conduct business. The lottery could use an additional 10-15 employees. We are not like any other governmental entity, we are supposed to sell product. D. Barden reported that when the lottery was established it was set up to run like any other enterprise/entrepreneur business with no limitations and push the envelope in creating and maximizing revenue. The only prohibitions we have are the ones stated in the statutes and in the constitution.

D. Barden reported that the lottery Facebook page received a comment from a player that stated “you should have \$20 scratchers with over 80% payout like most states; players don’t win anymore, so Texas lottery here I come”! These types of comments are becoming more common from our players, they know there aren’t as many winners and they would rather go to neighboring states to purchase their lottery products because they are keenly aware that the neighboring states have a higher prize payout on their scratcher products.

S. Jaramillo provided a brief overview of the July 2017 Financial Statements. The return for July was \$3.1 million; nearly \$345,500 more than FY18 YTD Budget or 12.2% more and \$822 thousand less than July in FY17 – a 20.6% decrease over last year. With July’s transfer, we will return nearly \$741.9 million to education.

Net instant sales for July were approximately \$6.1 million whereas last year they were \$6.097 million, a \$36 thousand increase of .59% increase.

Instant sales for July surpassed the YTD Budget by more than \$900 thousand or 17.2%.

Net Drawing game sales for July were approximately \$4.5 million, \$186 thousand less than YTD Budget or 4% less than budget and nearly \$2.8 million less than FY17 – 38.4%. Powerball sales were \$1.9 million less than last year; Mega Million was \$1.1 million less than last year. In July 2016, the PB Jackpot was at \$487 million and Mega Million Jackpot was at \$536 million. As of August 2017, the PB Jackpot is at \$239 million and Mega Million has a Jackpot of \$282 million, a significant difference in jackpots. Roadrunner Cash sales were \$127 thousand more than last year and Hot Lotto sales were \$54 thousand more than last year.

Total game expenses at the end of July were 107.8% of the YTD Budget, while Operating Revenues ended at 107.26% of Budget – tracking close to each other.

Operating expense at the end of July was 2.46% of total gross revenue and costs are being held down. We are 72% of YTD Budget.

No Further discussion or questions.

**Banking Resolution – Line of Credit:** M. Koson reported that this item was reviewed and vetted and requested S. Jaramillo to provide a brief overview of the Banking Resolution. S. Jaramillo reported that the resolution and certificate of incumbency is for a Line of Credit that the lottery has with Wells Fargo Bank. The Line of Credit has been in place since May 2012 and renews annually. This resolution is part of the lottery’s Banking and Related Services agreement with Wells Fargo. This year, Wells Fargo requested that this document be approved by the Board of Directors. The line of credit is established in case the lottery needs to access cash for any reason. S. Jaramillo reported that the lottery’s cash balance has been dwindling and this would allow the lottery to access cash to pay winners until the cash balance has been re-established. There are no fees if the line of credit isn’t used.

The CEO and Director of Administration requested one change to the resolution. Initially the resolution stated that any one person can implement the line of credit via telephone or written communication. After internal discussion between the CEO and Director of Administration and with consultation with Finance Audit committee, it was determined that the resolution would require “ANY TWO” of Three individuals listed on the resolution must be in agreement to implement the line of credit through written communication only.

M. Koson made a motion to approve the Banking Resolution – Line of Credit document as presented; second by J. Kubiak. Carried; 5-0.

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**Online Gaming System Vendor Penetration Testing Report:** M. Koson reported that this item was presented by M. Boland to the Finance Audit committee where it was reviewed and vetted. The committee made a conditional approval based on the discussion that took place during that meeting. M. Boland distributed revised document for board's review.

A brief background on this report: As part of the NMLA Online Gaming System RFP and contract, the online vendor is required, at a minimum to perform security assessment and penetration testing to assess and test the security and integrity of their online gaming system. This activity is important due to the ever-changing and increasingly complex nature of cyber-security attacks. The first penetration test was scheduled for Nov. 2016, but was rescheduled until the second quarter of 2017 because of game programming enhancements. PriceWaterhouseCooper's (PWC) penetration testing report issued May 18, 2017 had a number of findings – a total of 21 risk findings. The lottery met with PWC and the Online Vendor on July 10<sup>th</sup> to discuss report results and a timeline for remediation was provided - August 14, 2017.

One high risk finding was remediated between August 14<sup>th</sup> and 23<sup>rd</sup>; Eight medium risk findings were remediated between August 14<sup>th</sup>-15<sup>th</sup>. The remaining 12 risk findings (medium and low risk) were deferred for remediation until the first quarter of 2018.

M. Boland reported that in the "conclusion" the first paragraph is where the majority of the changes were made. M. Boland asked M. Koson if the changes address the committee's concern.

J. Kubiak stated that he wants it clear in the follow up, the remediation of the recommendations is the Online Vendors responsibility and not the lottery. M. Boland pointed out that in the conclusion it states "the online vendor taking appropriate actions to successfully remediate the outstanding findings in an expeditious matter and no later than the next scheduled board meeting. Further discussion took place on the wording and suggestions presented for the conclusion.

D. Barden recommends since the Finance Audit committee had a concern over the "high" risk finding that now has been remediated, since the end of the Finance Audit committee to the beginning of the Board meeting, based on the remaining risks deferred to the first quarter of 2018 perhaps M. Boland can re-present his recommendation at the next meeting all this would be cured and carried over. D. Salzwedel asked if the high-risk finding has been remediated. D. Barden stated yes. The Board recommended that this item be tabled for further discussion until the next Board of Director's meeting.

M. Koson made a motion to table the Online Gaming System Vendor Penetration Testing Report until the next scheduled Board of Director's meeting; second by J. Kubiak. Carried; 5-0.

**Lottery Bucks Compliance Audit Recommendation Update:** M. Koson reported that this item was presented by M. Boland to the Finance Audit committee where it was reviewed and vetted. M. Boland reported that this is a follow up report only. At the previous Finance Audit meeting, it was recommended that Intralot should consider increasing the number of lottery buck's distribution by their Field Lottery Representatives. This goal has been achieved and has significantly increased its distribution to players (400% increase in a two-month period) and the online vendor is committed to maintaining these distribution level acceptable to the lottery. This item is now remediated and considered closed.

**Other:** None.

**Personnel – A. Bailey, Committee Chair:**

**Approve Minutes of June 07, 2017 Personnel Committee Meeting:** M. Koson moved to approve the minutes; second by D. Salzwedel. Carried; 5-0.

## Revised External Policies

**Family and Medical Leave for NM Lottery Employees Policy:** D. Salzwedel reported that the Personnel Committee members recommended that this item be tabled until the next Board of Director's meeting.

The FMLA Policy provides for leave for birth/care of employee's child; or serious health condition, illness or injury for employee, spouse, child or parent of adult. The lottery is no longer considered a covered employer as defined by the federal government Family Medical Leave Act because the lottery has downsized and fall under 50 or more employee's thresholds. The lottery currently has 33 full time employees and 3 part-time employees.

D. Salzwedel made a motion to table this item to the next scheduled Board of Director's meeting; second by M. Koson. Carried; 5-0.

**Business and Operational Policy:** D. Salzwedel reported that this item was reviewed and vetted during the personnel committee meeting and further recommends the approval of the changes. D. Barden reported that the changes were made in two sections by clarifying and updating existing language. The changes are:

- The term "lottery" was added back due to a publication error and "governmental" has been added to help in the recruitment of employees that have governmental experience.
- Employees that are on unpaid leave should not be eligible for holiday pay.

M. Koson made a motion to approve the changes to the Business and Operational Policy as presented; second by D. Salzwedel. Carried; 5-0.

**Compensation Guidelines:** D. Salzwedel reported that this item was reviewed and vetted during the committee meeting. The committee recommends the approval of the changes. D. Barden reported that the changes to the compensation guidelines has been modified in two sections and language has been added to existing language in the policy for clarification purposes. The changes are:

- Performance Evaluations – dates were deleted for the evaluation period and new language was added allowing the CEO the flexibility to determine the evaluation period based on business needs.

M. Koson made a motion to approve the summary of changes for the Compensation Guidelines as presented; second by D. Salzwedel. Carried; 5-0.

**Other:** None.

**CEO Update:** D. Barden provided a fiscal year-end presentation/update on operations. D. Barden reported on "Where the Money Goes" comparing FY 16 and FY 17. The below table shows a decrease in all areas with the exception of Prizes paid out – includes the \$1 Billion PB Jackpot in 2016. The lottery will continue a declining trend unless changes are made.

	FY 16	FY 17
Gross Revenue:	\$154.4 million	\$126.1 million
Prizes Paid Out	\$84.8 million	\$67.2 million
Retailer Commissions	\$10.0 million	\$8.2 million
Cost of Product	\$8.4 million	\$8.6 million
Administrative Costs	\$4.9 million	\$4.3 million
Lottery Tuition Fund	\$46.3 million	\$37.8 million

