

**Regular Meeting of Board of Directors
New Mexico Lottery Authority
February 23, 2011
MINUTES**

Call to Order: Board Chair Marcus Rael called the meeting to order at 11:05 a.m. M. Rael asked for roll call. Present and constituting a quorum were Nino Trujillo, Herman Tabet, Marcus Rael, Reta Jones, Ken Hoeksema and Clifford Stroud.

Introductions: The following employees were present from NMLA: Tom Romero, Adriana Binns, Sylvia Jaramillo, Evelyn McKnight, Dave Ramirez, Vince Torrez, Linda Hamlin, Michael Boland, Karla Wilkinson, Wilma Atencio and Randy Bertram. Also present were Frank Duran of Kilmer and Kilmer and Marshall Puckett, private citizen.

Approve Proposed Agenda: M. Rael entertained a motion to approve the proposed agenda. R. Jones moved that the agenda be accepted as presented. Second by K. Hoeksema. All in favor, 6-0. There was no further discussion.

Approve Minutes of October 20, 2010 Board of Directors Meeting: M. Rael entertained a motion to approve the minutes from the October 20, 2010 Board meeting. H. Tabet moved to approve the minutes. Second by N. Trujillo. All in favor, 6-0.

Approve Minutes of December 13, 2010 Board of Directors Special Meeting: M. Rael entertained a motion to approve the minutes from the December 13, 2010 Board meeting. K. Hoeksema moved to approve the minutes. Second by C. Stroud. All in favor, 6-0.

Executive Reports:

CEO:

General Update: T. Romero reported that sales to date are tracking 5% behind last year's sales or about \$4.5 million dollars. Powerball is approximately \$9 million behind and Hot Lotto is down a little over a million dollars behind last year at this time. Scratchers are behind \$2 million compared to last year at this time. Sales are behind due to the lack of Jackpot run ups. Lottery sales are at \$88.3 million year to date compared to \$92 million for last year. The return to the state is tracking about a million less than last year to date.

T. Romero reported that Lottery staff is working on several new ideas for sales, such as prize structures, making the games more fun and interesting. The Sales, Marketing and Finance departments are looking at retailer incentives and the current advertising plan. T. Romero also reported that with the current economy and gas prices rising over the past several weeks, sales will take a hit, as it did last time. The lottery is certainly anticipating the loss.

T. Romero reported on Legislative issues. There are a number of bills that have been introduced that would expand the Lottery Tuition Scholarships to tribal colleges, home based education programs, extend the eligibility to sixteen months, and restricting colleges from increasing tuition cost beyond when students enter into the program and a repayment loan bill, if college is not completed. Several bills have gone to one or two committees, some haven't gone anywhere.

M. Rael requested additional information on the bill "limiting tuition rate increase". T. Romero reported that this bill was introduced by Senator Ingle, Michael Sanchez, and Tim Jennings. The purpose of this bill is that once a student enters college on a lottery scholarship; the tuition rate will remain in effect, until the student graduates, remains in college on the lottery scholarship. This bill keeps colleges from raising tuition rates for recipients of the lottery scholarship and not depleting the Lottery Scholarship Fund. HED has estimated by FY 2014, the legislative lottery scholarship fund will be in the red. HED has reported that New Mexico colleges have increased the tuition rates up 40% in the last two years.

K. Hoeksema inquired about any upcoming changes to Powerball. K. Hoeksema advised that he and R. Jones attended a lottery conference back in October 2010 and there was discussion of increasing the cost from \$1 to \$2, adding a new National game and possibly a World game. T. Romero responded that there is no movement or any changes to Powerball. There was some discussion back in December 2010, but a large number of directors, who are members of the Powerball group, were not in favor of any changes (cost or matrix changes) to Powerball at this time.

Open Meetings Act and Notice Resolution: T. Romero presented the Open Meetings Act and Notice Resolution for Board adoption. The resolution specifies that the Board will follow the Open Meetings Act adopted by the Board at the beginning of each year. M. Rael requested that an item be added to the Resolution; posting board agenda's on the NMLA website. Legal should be contacted to insert appropriate language to address this in the Open Meetings Act and Notice Resolution.

M. Rael entertained a motion to amend and pass the Open Meetings Act and Resolution to contain a statement that the agenda is posted on the lottery website. C. Stroud made a motion to adopt the Open Meetings Act with approved amendments. Second by H. Tabet. All in favor, 6-0. There was no further discussion.

T. Romero reported that two Lottery Sales Representatives have reached their 10 year anniversary and will be introduced at the next board meeting to the Board of Directors. T. Romero also announced that several staff members have reached their 15 year anniversary with the lottery (Gina Borrego, Vince Torrez, Evelyn McKnight, Adriana Binns, Karla Wilkinson and Tom Romero) and by summer, there will be additional seven staff members who will also reach their 15 year milestone.

Financial Statements: S. Jaramillo presented a detailed review of the January 31, 2011 financial statements. With the transfer that will be made on February 28th, for January's net revenues, the lottery will have transferred over 23.8 million dollars to the State of NM for fiscal year 2011, translating into 30.68% return of the lottery's gross revenues. Last year, at this time, we transferred 24.8 million dollars, for a 30.40% return. This year's return is slightly higher in terms of percentage, lower in dollars. Net instant sales, after deducting prize, promotional and stolen tickets was approximately 43.4 million dollars, which were 2.8 million dollars less than YTD net instant sales budget and almost 1.6 million dollars less than net instant for the same period in fiscal year 2010. Net on line sales were nearly 34.3 million dollars and were about 4.1 million dollars less than YTD budget and about 2.2 million dollars less than the same period in fiscal year 2010. Total operating revenues through January 2011 were 6.9 million dollars less than YTD budget and nearly 3.8 million dollars less than the total operating revenues from last year.

This is 8.2% less than the YTD budget and 4.64% less than the actual period from January 2010. Total game expenses are tracking with the YTD operating revenues at 91.43% of the budget versus 91.8% of the budget for operating revenues. YTD for last year's, the Total game expenses were at 65.97% of gross revenues. This fiscal year, total game expenses are lower at 65.57% of gross revenues. Operating expenses were at 3.75% of the total gross revenues at the end of January. With total operating expenses at 80.49% of the YTD budget. This is \$47,000 less than last year at this same time, which is 1.6% less. This is about \$706,000 less than the YTD budget, 19.51% less than budget. Net income is approximately 1.5 million dollars less than the YTD budget and \$929,000 less than this year than last year or 3.75% less this year. Thus far, we've been able to meet the thirty percent return every month.

M. Rael asked about the PB Jackpot. The current jackpot is at \$155 million, does the lottery think this will help or does it need to go higher for the lottery to see any benefits. T. Romero responded that the PB jackpot generally needs to be over \$200 million to see any increase in sales. S. Jaramillo stated that marketing is currently advertising on the PB jackpot, so hopefully it will help. Ever since the cross selling of Mega Million, the effects are not quite as big anymore.

K. Hoeksema asked about the big jackpot in December/January, did we see any impact overall in revenue. Has the lottery analyzed data? How did it cannibalize Power Ball? Did the increase in Mega Millions, create an offset by a decrease in Power Ball? A. Binns responded that what happened with Mega Millions in December was fantastic; it created a lot of awareness and increase in sales for the lottery. S. Jaramillo advised that the gross income for Mega Millions in December/January was \$1.3 million. In November it was at \$548 thousand and for October, the gross income was at \$788 thousand, but it didn't generate the sales that Power Ball jackpot that high usually does.

K. Hoeksema asked a related question from the last board meeting minutes, the lottery had over budgeted for Mega Million in the amount of \$900 thousand and we don't come close to that. We discussed a revised budget based on the numbers, do we do that mid-year or do we budget downward? S. Jaramillo responded that the lottery will present a revised budget, which takes place in the springtime. The lottery waits to see what sales are doing and revise in several different categories, along with direct expenses and any other line items that the lottery was able to save money in. T. Romero reported that historically the revised budget is presented at the Budget workshop in April/May. It's still hard to tell with Mega Millions, if the jackpot starts to climb it could put us a lot closer to our budget than we anticipated. Executive staff looks at the expense that is going out and working with finance, we try to keep the expenses consistent, in case the budget has to be adjusted.

H. Tabet asked about the lease and getting someone into the empty building next door, maybe offer an incentive, like a discount or negotiate new terms with the owners. S. Jaramillo advised that the lottery did meet with landlord on the building next door; the lottery is trying to pursue other avenues to lease it, and has considered taking a hit on the lease, to at least get something back from it. S. Jaramillo further reported that the landlord has protested the property taxes and the lottery saved some money with this protest. There was no further discussion.

AUDIT:

Internal Audit Reports: M. Boland presented two Audit Reports for acceptance by the board and a request by the audit committee. A full detailed report was made during the Finance/Audit committee meeting.

M. Boland reported that there were no observations noted in the implementation of the Great Outdoors 2nd Chance Prize Drawing promotion - November drawing. M. Boland would like to submit this report for acceptance by the board.

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M. Rael entertained a motion to accept the audit report for the Great Outdoors 2nd Chance Prize Drawing promotion - November drawing. H. Tabet moved to accept the audit report. R. Jones second. All in favor, 6-0.

M. Boland presented the MUSL minimum game security standards compliance audit. As a member of the Multi-State Lottery Association, the lottery must stay in compliance with MUSL Standards. This audit is conducted every year because it is a high risk area. There were three observations noted. Two of the observations have been remediated and have been cleared. The third, which is observation number two, will be cleared once the lottery visits the on-line vendor computer site.

M. Rael asked V. Torrez if there's a schedule of when the lottery is supposed to review these on-line sites and what it entails. V. Torrez reported that the lottery has no formal schedule. Given that the lottery has a new on-line vendor with its primary site in Idaho and with the conversion, the lottery just didn't visit the site. The lottery has things in place that the lottery was able to mitigate any concerns that we had, as far as them having ticket stock in those areas. V. Torrez further reported that from Security's viewpoint this was a low risk type issue. In addition, the Idaho Lottery Security does serve as a representative of the NM Lottery Security and ensures that there is no NM lottery ticket stock at the primary site. The Idaho on-line vendor site is also the primary site for the Idaho Lottery. A visit to the primary and secondary site will soon occur. A schedule will be implemented by the lottery security division.

M. Boland reported that Internal Audit has a lot of comfort that the lottery has strong controls over the ticket stock. The standards were written some time ago, prior to a lot of the technology we have now and the validation, using a protocol called "ISecure" is 99.9% accurate to the validation of tickets. When winning tickets come through the lottery, we are sure that they are valid tickets. Some standards are outdated; however, the lottery needs to stay in compliance with those standards. Internal Audit rated this observation as "low risk", because of all the mitigating controls that are in place.

R. Jones asked if there are any opportunities to influence MUSL on getting some of these standards updated. It appears that if we are relying on the Idaho Lottery to conduct a visit on our behalf, it seems like a reasonable alternative to the procedure. It saves the lottery a lot of money from going up to Idaho for a site visit. The standards don't provide for a third party alternative verification that would provide us the comfort level to be a low risk.

R. Jones asked T. Romero, if MUSL can be encouraged to look at these standards and provide more flexibility. T. Romero reported that MUSL is looking at this. The Security and Integrity committee is looking at new standards and has staff looking into this. The committee will make a recommendation to the MUSL Board.

M. Rael asked for a quick rundown of observation one that was listed as high risk by Internal Audit. Why wasn't Intralot following the stock issuance procedure and what is the lottery doing about it. There is a recommendation to resolve this observation. Is there any verification in place that Intralot is following procedures? M. Boland reported that it has been verified that Intralot is following procedures. There was no further discussion.

M. Rael entertained a motion to accept the MUSL minimum game security standards compliance audit. R. Jones made the motion to accept the MUSL minimum game security standards compliance audit. K. Hoeksema second. All in favor, 6-0.

M. Boland reported that Internal Audit has been requested by the audit and finance committee to investigate how many retailers are actually winning prizes either playing the on-line games or the Instant Scratchers. To find out what sort of percentage people, retailers are actually playing and winning. In addition, Internal Audit will also investigate what the lottery proactively has in place to capture this type of information and what controls are in place so that retailers can't manipulate instant scratchers and its on-line games, being that retailers can play.

BOARD CHAIR:

Announcements: M. Rael requested a brief overview of the Lucky Dog Photo contest from L. Hamlin. What were the issues on the fallout of the voting process and was the lottery negatively affected by this promotion. L. Hamlin deferred to A. Binns.

A. Binns reported that the lottery launched "Lucky Dog Photo Contest" in January. Other lotteries have launched a similar contest and have had success with it. People were asked to submit photos of their dogs and asked to choose which photo would appear on a lucky dog scratcher. Based on experience of other lotteries, the lottery set a goal of a 1,000 photos. The lottery immediately determined that, it would far exceed that amount. The lottery viewed more than 7,700 entries and approved 4,700 entries. KOB TV was the lottery's website partner in this photo contest and initially KOB estimated that there would be 200 entries based on their past experience.

We went into our voting phase. The public would choose the top 25 the lottery would then choose six to appear on the scratcher. It became obvious within a day and a half that some people seemed to be voting more than allowed, which is once per day, per computer. Based on the advice of the third party vendor "U Pick'em" and that of KOB TV, the lottery decided to eliminate those prior votes from the day and a half and then required registration. The lottery immediately saw a decrease in the suspicious voting at that point.

L. Hamlin reported that in the first 36 hours, there were 53,000 entries. Once the registration application was put in place, the voting irregularities began to subside. Over the remaining 9 days of voting opportunities, the voting total ended up at 110,000 to 112,000 votes. The lottery received hundreds of emails from people, many of them were very angry and wanted to know why the lottery threw out their votes and the lottery explained that and some of them were very appreciative. They seemed to notice that there were in ornate number of votes for some dogs. Every email was answered.

As for the media, not one of the TV stations covered it. There was coverage in the Albuquerque journal. It wasn't a negative story, just stating what happened, but poking fun that some of the people took the contest so seriously that would cheat in that manner. There was other newspaper that picked up the story. The lottery didn't see a decrease in sales. The press coverage that was generated was pro active on the part of the lottery. We want the lottery to be open and transparent when we experience these types of issues, we wanted to continue that so the lottery issued a news release informing people what had occurred and what the lottery was going to do. The lottery will launch the "Lucky Dog" scratcher in May and there will be a total of six dogs which will be featured on the scratcher. 720,000 tickets will be printed with a price point of \$2. The prize structure has not been completed to determine what the top prize will be. Overall, this was a learning experience. The lottery was overwhelmed with the response that we got; we achieved our goal of engaging players and venturing out to social media.

T. Romero asked the board to select a date for the budget workshop meeting and a regular meeting that same day. Executive staff was looking at possibly May 4, 2011 starting at 9 am and having a short meeting thereafter. M. Rael announced that the Budget workshop meeting and regular board meeting will take place on May 4, 2011 beginning at 9 am.

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M. Rael announced that there may be four new members of the board. Governor Martinez withdrew the nominations of M. Rael, H. Tabet and N. Trujillo. There's also the law enforcement position that is open. M. Rael, H. Tabet, and N. Trujillo will continue to serve until the replacements are named. T. Romero advised that he was not aware that the Governor had withdrawn the nominations. M. Rael reported that someone directed him to a website that Governor Martinez withdrew all the nominations for every board that Governor Richardson had appointed or reappointed and were not confirmed or re-confirmed by the senate.

PUBLIC COMMENT: M. Puckett inquired about Trucks and Bucks, a scratcher ticket that the lottery used to put out years ago. Was the game not profitable? T. Romero responded that initially this game was a good game and very profitable, a couple of different things happened over the years. One was that initially the lottery could directly go to Chevy, Dodge, and Ford and obtain the trucks for the game. The lottery industry has changed and now you must go through a third party lottery vendor, such as MDI or GTECH printing or someone similar. They bought the licensing rights to Ford, Chevy, Dodge and some of these others, so if the lottery wanted to do a Trucks and Bucks scratcher game, the lottery must go through one of these vendors and pay a commission fee on top of the cost of the game. The second issue was that the last couple of times we ran the game, the game did not sell as well as it did in the past. We actually had a problem with the last game as far as the last vehicle being claimed.

K. Wilkinson reported that you could instantly win one of the trucks or win a truck in a 2nd chance drawing. The vehicles have gotten extremely expensive; the lottery would pay in addition to the cost of the truck, tax, title, and license and income tax. When the lottery introduced Trucks and Bucks initially the cost of the tickets were \$1 and \$2 games and we bumped it up to \$5 a game. Since Trucks and Bucks became a licensed product, not only was there a licensing fee, the cost of the truck, but the lottery had to purchase merchandise. It got to the point where the lottery couldn't afford it. T. Romero that in addition to the cost of the licensed product and the statutorily mandate to return monthly 30% to the state, this has caused the lottery to look at our expenses, analyze the games and determine if the game sold well. K. Wilkinson reported that the lottery will be conducting some focus test and there is a game with a vehicle on it. It may be a specialty vehicle to see if it will generate some interest, but we will see how the testing goes on that first. If the lottery decides to put out a ticket, more than likely the cost of the ticket will be \$3 or \$5.

M. Puckett then inquired about the process for scratcher development, like the new Darius Rucker ticket. How does the lottery determine what will be introduced and has the Darius Rucker ticket been introduced by other states? T. Romero responded that members of the executive staff, the instant product manager and other staff members look at what the game line-up is going to be for the year. We look at what kind of games we want to put out based on themes, game styles and price points. The lottery looks at how we market our games to a wide diversity here in New Mexico. In New Mexico we do have a lot of people that like country/western and we wanted to reach that demographic. The lottery was looking for a country/western theme and that is how the Darius Rucker ticket came to fruition. Similar to Trucks and Bucks, the lottery conducts focus testing; we look at what historically have been popular games and what has worked well here in NM. We've tried games that did well in other states, but failed miserably here in NM and we have tried games that didn't do well in other states, but did well here.

M. Puckett stated he's in the aviation business and wanted to discuss the possibility of an aviation oriented scratcher ticket. T. Romero responded that the lottery has received suggestions on theme games and most recently was a bowling scratcher ticket. This idea is great, except that when you look at the number of bowling alleys in NM and the fact that we have tried bowling tickets in the past, they were not highly successful and we had problems with them. Those are things we start looking at and factoring in how well are they going to sell statewide in NM.

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M. Puckett asked if there is more than one scratcher vendor. Some scratchers scratch easy, some scratchers you practically have to tear apart. K. Wilkinson responded that over a year ago, the lottery switched instant ticket printers, from Scientific Games to GTECH Printing Corporation. The first tickets that hit the market from GTECH were at the end of June. Currently there's a combination of games out there from Scientific Games and GTECH, the majority of tickets out there are GTECH tickets. The life of the scratch off coating is usually 3-5 years. V. Torrez reported that both vendors go through a process to make sure that the scratch off coating is what the lottery expects it to be and they provide a report to Security ensuring they're meeting specifications. M. Puckett asked how big is the empty building next door? T. Romero responded that the building is 14,000 square feet. The building was originally created as a computer data center for our original on line vendor GTECH in 1995-1996.

ADJOURNMENT: M. Rael entertained a motion to adjourn the meeting. N. Trujillo moved to adjourn the meeting. H. Tabet second. All in favor, 6-0. The meeting was adjourned at 12:10 pm.