

Regular Meeting of Board of Directors
New Mexico Lottery Authority
June 07, 2017
MINUTES

Call to Order: Board Chair Dan Salzwedel called the meeting to order at 2:02 p.m. and asked for a roll call. Present and constituting a quorum were: Mark Koson; Dan Salzwedel, Paul Guerin and Sal Baragiola. Amy Bailey, John Kubiak and Claude Austin were absent.

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

Also present were; Jon Zajdel with Intralot; Frank Duran, Richard Kilmer and Erin Killian with K2MD; Travis Dulany with LFC; Charlie Scannella with SGI; Othiamba Umi and Shea Fallick 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 M. Koson. Carried; 4-0.

Approve Minutes of March 16, 2017 Board of Director's Meeting: D. Salzwedel entertained a motion to approve the March 16th minutes. M. Koson moved to approve the minutes; second by P. Guerin. Carried; 4-0.

Public Comment: None.

REPORTS:

Finance/Audit – M. Koson, Committee Chair:

Approve Minutes of March 16, 2017 Finance Audit Committee Meeting: M. Koson moved to approve the minutes; second by D. Salzwedel. Carried; 4-0.

Advertising RFP: M. Koson reported that this item was presented by W. Ahlm at the finance audit committee earlier today and was reviewed and vetted. The committee approved the recommendation that the advertising RFP be awarded to the successful vendor. M. Koson asked W. Ahlm to provide a brief overview of the process.

W. Ahlm reported that the lottery issued an RFP for Professional Advertising and Related services on April 13, 2017. A legal notice was issued in the Albuquerque Journal from April 13 - April 17, 2017 and was also published on the NMLA website. The RFP notice was sent to 34 advertising agencies - 27 agencies requested a copy of the RFP. The lottery received 3 proposals from; Griffin and Associates (GA); Kilmer and Kilmer, Marshall Duran (K2MD) and Wilson-Binkley Advertising & Marketing (WB).

The proposals were evaluated on the criteria outlined in the RFP: experience and capability, responsiveness to NMLA, technical capabilities and samples of work. The proposals including the cost proposal were scored and based on the total scoring K2MD was determined to be the successful ad agency with a total 96.8 points out of 100 possible points, versus 81.1 for Griffin and Associates and 80.1 for Wilson-Binkley.

K2MD's proposal offers a cost savings of more than \$142,000 over the term of a 4-year contract compared to GA. K2MD's proposal equates to a 2.5% reduction in gross cost from their current contract rate – a savings of \$254,000 over the next four years. The total contract based on a \$2 million Advertising Budget for K2MD would be \$222,200.00.

06/21/17 wa

W. Ahlm requests approval from the Board to award the advertising and related services contract to K2MD and authority for the CEO to execute a contract with K2MD effective July 1, 2017 for a four-year contract subject to provisions of the RFP.

M. Koson made a motion to approve and award the Advertising RFP for Professional Advertising and Related Services to K2MD and provide the CEO authority to execute a four-year contract subject to provisions of the RFP; second by D. Salzwedel. Carried; 4-0.

FY 2018 Consolidated Original Annual Budget: M. Koson reported that this item is an action item and was presented by S. Jaramillo to the Finance Audit committee where it was reviewed and vetted. The committee recommends that the FY 2018 Consolidated Original Annual Budget be submitted to the Board for acceptance for approval. M. Koson deferred to S. Jaramillo.

S. Jaramillo reported that the FY 2018 Original Annual Budget is in line with the FY 2017 Revised Annual Budget with a few changes. We are reducing Hot Lotto sales by \$1.9 million, which will be concluding at the end of October 2017 and adding a new game called Lotto America. The lottery is adding \$2 million for that game. The lottery is also adding another new game called Miss/Match and adding \$600 thousand for that game. Quickster sales will be reduced by \$300 thousand dollars.

The only other change to arrive at Net Ticket sales is to tickets provided as prizes. We are adding \$1 million for tickets provided as prizes. These are tickets we put into our instant games instead of actual cash prizes and they help to create the churn. By placing these tickets into the game, players will win a prize and purchase one, two or three more tickets, creating a churn.

The total game expenses are 66.98% of Gross Revenues in FY 18, while they were 67.22% in the FY 17 Revised Budget - .24% less for game expenses.

Operating Expenses are 3% of Gross Revenues, a low percentage of gross revenues. With these changes, we will be able to return 30% to the scholarship fund, but it will be \$194 thousand less to the scholarship fund.

D. Salzwedel asked what factors were used to determine the \$300 thousand reduction to Quickster. S. Jaramillo reported that the CEO, Karla Wilkinson and herself met and discussed the new game Miss/Match, Quickster sales trend and historical data and determined as a consensus group that the Quickster game would be impacted by Miss/Match and with an educated guess reduced the sales by \$300 thousand.

S. Jaramillo reported to balance the budget the prize payout was adjusted.

D. Salzwedel asked what is the percentage decrease for the operational budget. S. Jaramillo reported that it's not decreasing, but increasing slightly due to a couple of positions the lottery is considering and the cost of Insurance (health, dental, etc.) will likely increase in July. However, lottery is always looking for ways to reduce cost in any area and this past year, the lottery replaced the lighting in the warehouse to LED lights, resulting in a \$9 thousand-dollar savings year to date.

P. Guerin asked comparatively, are the operating expenses for the lottery fairly low compared to other lotteries? D. Barden stated yes, that is correct. The lottery probably has one of the lowest expense ratios when compared to other state entities. P. Guerin reiterated that you can only save so much in operating expenses; you have to have expenses to operate. P. Guerin commended the lottery and CEO on doing a great job in always seeking savings in all areas.

M. Koson made a motion to approve the FY 2018 Consolidated Original Annual Budget as submitted; second by D. Salzwedel. Carried; 4-0.

Financial Statements: M. Koson reported that S. Jaramillo presented the financial statements to the finance audit committee. M. Koson deferred to S. Jaramillo who provided a summary. S. Jaramillo reported for the first ten months of fiscal year 2017, the lottery has returned \$31.6 million to the Legislative Lottery Scholarship fund and has met the statutorily required 30% return each month. The net revenue is \$215,579 less than the FY 17 revised budget that was approved in March or 0.68% less than budget and \$7.6 million less than for the first ten months of fiscal year 2016 – a 19.37% decrease. We have now returned over \$732.5 million to the State of New Mexico for education since the inception of the Lottery.

Net instant sales for the first ten months were approximately \$60.9 million, whereas last year net instant sales were nearly \$70 million. Instant ticket sales have decreased more than \$9.1 million from last year or a 13% drop, but we are \$1.4 million more than the FY 17 YTD Revised Budget or 2.33% more. But if you look at the original budget approved last year, we are only at 86% of our YTD Original Budget and even though we are ahead of the revised budget, we are down from where we started. This in large part to our prize payout expense for instant tickets which was 60.84% for the first ten months compared to 63.29% last year a 2.45% drop in prize payout which is reflected in our current sales. Our players realize that there aren't as many prizes in the instant games as compared to last year's scratchers.

In our record setting year of 2007, the prize payout was at 63.13% - this year's payout is 2.29% less than the record year. Being that we are strapped by the 30% return, we are returning \$2.7 million less for the scholarship fund because of instant ticket sales. A projected loss of over \$3 million annualized.

Net drawing game sales for the first ten months of were approximately \$44.6 million. Net drawing sales were \$792 thousand less than the revised budget and \$16.2 million less than for the first ten months of last year. This is mainly due to Powerball sales.

Powerball sales were nearly \$16.7 million less than last fiscal year. Powerball was also nearly \$1.4 million behind the YTD Revised Budget or 94.1% of the YTD Revised budget but 73% of the YTD Original Budget. Mega Millions sales were ahead of last fiscal year by \$437 thousand; Roadrunner Cash sales were \$149 thousand less than last year and Hot Lotto sales were \$102 thousand less than last year. Pick 3 game sales were ahead of last year by \$332 thousand which may be due to the added Sunday sales. Mega Millions, Roadrunner Cash, Hot Lotto and Pick 3 were all ahead of their individual budget amounts.

Total Operating Revenues were just over \$105.5 million, which were \$605,000 more than the FY 17 YTD Revised Budget or 0.58% more, but \$25.3 million less than last fiscal year mainly due to the drop in instant ticket sales and Powerball sales compared to last year.

Total Game Expenses for the first ten months of the fiscal year were 99.85% of its YTD Revised budget, while net sales were 100.57%. Actual game expenses were 66.46% of Gross Revenues; the Budget was 66.95% of gross revenues. Game Expenses were \$17.1 million less than last fiscal year or 19.62% less; this was tracking with 19.4% less in total net sales.

Operating expenses are at 3.51% of total Gross Revenues.

P. Guerin asked what are the national trends compared to our sales. D. Barden reported that everyone is lagging in sales across the country. Game expenses are \$15 million down, retailer commissions are down. People are always stating that the lottery is paying too much for its online vendor and retailer commissions and that simply isn't true. When sales are down, every area is down. It should be noted that

only one online vendor responded to the lottery RFP. We are a small state with low sales and any cuts will be catastrophic. There is a new initiative on gross receipt taxes for lottery products, if this passes, it will be catastrophic. Brewer oil advised if retailer commissions are cut and the gross receipt gets enacted, Brewer Oil won't be a retailer anymore and many more may follow.

The Board appreciates everything the CEO has done and knows that the CEO will continue fighting for the lottery and its beneficiaries.

Disposal of Obsolete, Worn Out or Unusable Tangible Personal Property: M. Koson reported that this item is an action item and was presented by S. Jaramillo to the Finance Audit committee where it was reviewed and vetted. S. Jaramillo reported that the list includes 14 categories of various items from a camera, fax, laptop, 10 printers, rack server and other miscellaneous items that are non-capital items and that have a current resale value of five thousand dollars or less and are either worn-out, unusable or obsolete to the extent that the items are no longer economical or safe for use by the New Mexico Lottery Authority. The lottery requests for your approval to dispose of these items in accordance to our Capital Asset management policy.

S. Baragiola requested that schools in need should be given items first instead of public auction. S. Jaramillo reported that the lottery will do so.

M. Koson made a motion to approve the document for the Disposal of Obsolete, Worn Out or Unusable Tangible Personal Property as presented; second by D. Salzwedel. Carried; 4-0.

FY 2017 Internal Audit Plan: M. Koson reported that this item was presented by M. Boland to the Finance Audit committee where it was thoroughly reviewed and vetted and M. Boland outlined some key areas. D. Salzwedel asked M. Boland to provide an overview of the audit plan. M. Boland presented the FY 2018 Internal Audit Plan which is developed on an annual basis with consensus of the CEO and executive staff. The plan is based on a priority assessment. This plan assists Internal Audit to improve the effectiveness of lottery operations. The items listed are new and based on discussions with executive staff and process owners on what their priorities are for the lottery.

M. Boland reported that the scheduling is designed and based upon when testing occurs on items in the audit plan and the different levels of risk – moderate/high. By scheduling some items quarterly this provides flexibility for the auditor and lottery.

D. Salzwedel asked M. Boland to explain how the CSR area gets audited. M. Boland reported that the customer service representatives contact retailers on a daily basis and order scratchers and retailer equipment on behalf of the lottery. Internal Audit will determine what metrics are in place and quantitatively assess what sort of job they're doing. If there aren't any metrics/procedures in place, Internal Audit would recommend different metrics. This is an area that has not been audited.

In addition, M. Boland is requesting approval from the Board an extension of the financial audit contract to CliftonLarsonAllen. The State Auditor has already approved the extension. M. Boland reported that this is the first extension and one extension left, for a total of 3 years.

M. Koson made a motion as recommended by the finance audit committee to approve the FY 2018 Internal Audit Plan, as well as the extension of the FY 2017 Financial Audit Contract with CliftonLarsonAllen; second by M. Koson. Carried; 4-0.

Lottery Bucks Compliance Audit: 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 compliance audit to ensure lottery employees who have been assigned lottery bucks are distributing the

tickets in accordance with the Policy and procedures and the accounting of these tickets in our accounting system is sufficient. A lottery buck is a coupon valued at one dollar and is redeemable by players for lottery products. There were no reportable observations and one recommendation for Intralot FSR's (Field Service Representative) to distribute more lottery bucks to players which will incentivize increased sales. The audit revealed that several FSR's did not distribute any lottery bucks during the period under testing and has been addressed by Intralot management.

S. Baragiola asked when will there be a follow up audit. M. Boland reported that this is the 8th and final year of the lottery bucks program, which will end March 2018.

1st motion made by M. Koson to approve the Lottery Bucks Compliance Audit as presented; second by D. Salzwedel.

S. Baragiola made an amended motion to approve the Lottery Bucks Compliance Audit as presented and to get a follow up report on the remediation component of the audit no later than December 2017; second by M. Koson. Carried; 4-0.

#2 amended motion. S. Baragiola made a motion to approve the Lottery Bucks Compliance Audit as presented with a follow up remediation report no later than the next regular board meeting; second by M. Koson. Vote: Carried; 4-0.

Other: None.

Personnel – A. Bailey, Committee Chair:

CEO – Evaluation/Contract: D. Salzwedel reported on behalf of A. Bailey who is absent from today's meeting that he and M. Koson met at the Personnel Committee meeting and reviewed and formally vetted the CEO's evaluation and contract with input from the entire board. The Board is pleased with the CEO and who has always performed at the highest level in his position with prioritization and his many accomplishments and leadership skills with his staff – a job well done.

P. Guerin commented that in the future, the NMLA Board consider the CEO contract be extended beyond the 2-years.

M. Koson made a motion to approve a new 2-year contract for the CEO and authorize the Board Chair to finalize negotiations on this agreement; second by D. Salzwedel. Carried; 4-0.

D. Salzwedel reported that he has J. Kubiak's proxy vote for the CEO's evaluation and contract, as well as the Board elections. The vote is changed to "Carried; 5-0.

D. Salzwedel thanked the CEO again for a great job!

Other: None.

Operations – S. Baragiola, Committee Chair:

Other: None.

CEO Update: D. Barden reported on lottery operations. D. Barden reported that legislatively things are progressing, which is a far cry from the past 10 years, legislators and individuals didn't really know much about the lottery, but with each passing year, the lottery has made progress by educating people and by getting people to understand that something needs to be done with the 30% mandate. Some NM Students have reached out to the CEO and perhaps a meeting is imminent along with their support.

D. Barden reported that he came across a recent newspaper article that stated "as colorful as the bottles on the shelves, the lottery tickets at Cliffs Liquor Store on old Pecos Road, are not selling quite as well as they did a year ago. The manager stated "Nobody's telling me why", but if you ask people, I bet most would say "I'm not winning; that's why I'm not buying"! The lottery completed a pilot project las year and increased scratcher sales by 18%. The lottery couldn't afford the higher prize payout this year and reduced the prize payout and now sales are down. People buy lottery to win and have fun; they don't play for people to go to school, that is the benefit of the lottery.

D. Barden reported on Play at the Pump. The estimated sales are ½ million with 23 locations. The lottery expects to add 35 new locations in June and hope to have 10-100 stores at the end of the first year of the program. PATP is very popular with players and a new way to deliver lottery product.

Hot Lotto will be ending in October and will be replaced with a new game called Lotto America and will be run by the "Lotto America" group, similar to MUSL and Mega Million group. Miss/Match is another new \$5 game that will be added to the lottery product mix.

Lastly, D. Barden reported that the lottery will be going out to bid for its Instant Products mid-September.

The Board thanked the CEO again and appreciate his passion and commitment to the lottery.

Other: None.

Board Chair:

Board Officer Elections: D. Salzwedel entertained discussion or decision from Board on how to proceed with the annual elections, either individually or aggregate group.

S. Baragiola made a motion that everyone in their current position continue for another 12-month period and would like to have a discussion if board members want to remain in their current position; second by P. Guerin.

All present board members and by proxy vote J. Kubiak affirm that they will remain in their current board and committee chair and committee appointments.


D. Salzwedel reiterated that the motion made by S. Baragiola and second by P. Guerin that all Board members retain their current board membership along with retaining committee chair and committee appointments. Carried; 5-0.

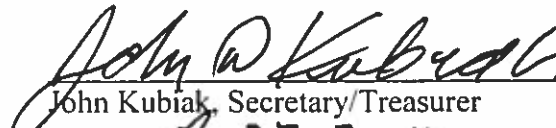
Committee Appointments and Committee Chair Appointments: None.

Announcements: None.

Other Items: None.

Adjournment: D. Salzwedel entertained a motion to adjourn. S. Baragiola moved to adjourn the meeting; second by M. Koson. Carried; 4-0. The meeting adjourned at 3:36 p.m.


 Dan Salzwedel, Chairman
 Date 8-23-17


 John Kubiak, Secretary/Treasurer
 Date 8-23-2017