

**Regular Meeting of Board of Directors
New Mexico Lottery Authority
August 19, 2020 via Teleconference**

MINUTES

Call to Order: Board Chair Reta Jones called the meeting to order at 10:03 a.m. and asked for a roll call. Present and constituting a quorum were: Reta Jones, Sal Baragiola, Paul Guerin, Nina Thayer, Othiamba Umi, Leo Romero, and David Keylon.

Present from NMLA were: David Barden, Carolyn Cabell, Wilma Atencio, Sylvia Jaramillo, Kevin Duda, and Michael Boland. Also in attendance were Matt Bone and Elizabeth Nunez with CliftonLarsonAllen (CLA), as well as Mary Stanford and Steve Beck with INTRALOT.

Approve Proposed Agenda: R. Jones entertained a motion. L. Romero made a motion to approve the proposed agenda as presented; second by N. Thayer. Vote: all ayes, no nays. Carried; 7-0.

Approve Minutes of June 10, 2020 Board of Directors Meeting: R. Jones entertained a motion. L. Romero made a motion to approve the June 10 meeting minutes; second by D. Keylon. Vote: all ayes, no nays. Carried; 7-0.

Public Comment: None.

Financial Audit Entrance Meeting - CliftonLarsonAllen: Matt Bone, Engagement Principal, reported on CLA's responsibilities as the Lottery's audit firm to communicate with those charged with governance during the course of the audit and introduced the engagement team, which will consist of himself; Elizabeth Nunez, Engagement Manager; Sheila Quintana, Engagement In-Charge; and other staff members such as an IT auditor and quality control reviewer.

E. Nunez provided a summary of the FY 2020 Financial Audit and outlined the process that will be followed throughout the duration of the audit. The summary included an overview of the required communication, planned scope of services, timeline, and other matters.

E. Nunez reported that the engagement team's responsibilities include forming and expressing opinions about the financial statements and if they are fairly presented in all material aspects, in conformity with generally accepted accounting principles. Responsibilities also include determining whether internal controls over financial reporting are in place and being followed in accordance with policies and procedures, planning and performing the audit to obtain reasonable assurance that the financial statements are free from material misstatement, and communicating significant and particular matters with Lottery staff and management. The financial audit of the financial statements does not relieve the Lottery from governance or management of their responsibilities. CLA determines the risk approach, which changes year to year and will be evaluated and compared to the previous year's financial audit.

E. Nunez stated that field work and sample testing will be completed throughout the audit, which will begin August 24 and run for a two-week period. During this time, CLA will follow guidelines in regard to COVID-19 and adjust accordingly. The reporting and financial review will occur during the months of September and October with a planned submission to the Office of the State Auditor by October 19, 2020. The Lottery will schedule an exit conference with CLA and the Finance Audit Committee.

D. Keylon asked about the number of test samples to be used. E. Nunez stated it varies and is based on a risk-based approach. There is no set number or percentage. There are required standards that CLA must

follow to be in compliance with State audit rules and there are certain areas that require them to have a minimum number of samples.

L. Romero asked whether CLA conducted and/or completed any audits during COVID-19, whether they encountered any issues under those circumstances, and what they learned that will assist them in conducting the audit. E. Nunez stated that audits were completed during this time as part of their state/local government audits. There were some instances where they encountered restrictions due to the capacity of a client's building. CLA overcame these issues by working a rotation schedule and utilizing technology in completing the audit. E. Nunez stated that open communication was the key to success.

R. Jones inquired about the deadline for submitting the audit to the State Auditor. E. Nunez responded that the deadline is November 1, 2020. E. Nunez reported that one of the great things about working with the Lottery is that financial statements are presented throughout the year to the Board at Board meetings. These statements show where the balances are at any given point in time. The fiscal year financial statements are provided to CLA the first week in September. This allows CLA to complete their audit, since they have already completed their testing with samples, and to see if there are any necessary adjustments. Historically, there have not been any adjustments made, just presentation comments. The report is then issued by the second week in October.

No further questions. R. Jones thanked CLA for joining the virtual meeting. CLA representatives left the meeting at 10:26 a.m.

REPORTS:

Board of Director Bylaws: R. Jones reported that Board members received both the draft redlined and proposed final Board Bylaws. The proposed changes were vetted by the prior Board and presented to the current board at a previous meeting. R. Jones deferred to S. Baragiola for additional comments.

S. Baragiola reported that the previous Board identified that the Secretary/Treasurer description in the Bylaws does not accurately represent the duties of the Secretary/Treasurer. A new description of duties that more accurately represents the position was disseminated to the Board for review. In addition, at a previous meeting L. Romero asked if the position of Assistant Secretary/Treasurer was needed and the general consensus was that it was not. Bylaws changes being presented for approval include updated language for the Secretary/Treasurer description, elimination of the Assistant Secretary/Treasurer position, and updated language in the "Moneys of the Authority" section to better represent the Authority's operations.

No further questions.

R. Jones entertained a motion. S. Baragiola made a motion to approve the Board of Directors Bylaws as presented; second by L. Romero. Vote: all ayes, no nays. Carried; 7-0.

Financial Statements: S. Jaramillo reported highlights for Fiscal Year (FY) 2020 financial statements. The New Mexico Lottery returned \$38.1 million to the Lottery Scholarship Fund. The total transfers were nearly \$1.95 million or 5.38% more than the FY 2020 revised budget, but nearly \$5 million or 11.5% less than FY 2019's return of \$43.1 million.

To meet the 30% required return each month, the Lottery used unclaimed prizes in ten months of the fiscal year. Total unclaimed prizes transferred were approximately \$4.24 million or 3.34% of gross revenues. Without the unclaimed prize fund transfers, the revenue return percentage would only have been 26.66% in FY 2020.

In the last thirteen fiscal years, the Lottery has used unclaimed prizes 83.97% of the time to meet the initial 27% and then 30% return. Without these unclaimed prizes, the Lottery would not have been able to meet

the mandated return and would have only returned 27.34% to the scholarship fund. Over \$48 million of unclaimed prizes have gone to the Lottery Scholarship Fund. The balance remaining in the unclaimed prize fund at the end of FY 2020 was \$897,459.60. The Lottery has now returned more than \$860 million to the State of New Mexico for education since the inception of the Lottery.

Net instant sales were approximately \$79.3 million. Instant ticket sales increased by approximately \$4.37 million or 5.83% from the prior fiscal year's net instant sales of \$74.9 million. Instant sales also surpassed the FY 2020 Revised budget by more than \$8.4 million or 11.86%.

During the last quarter of FY 2020, instant sales increased by approximately 30% over the average daily sales for the first three quarters. The increase to instant sales led to more than \$5 million additional net sales for the quarter compared to average sales to the other three quarters, thus returning an additional \$1.5 million to the Lottery Scholarship fund. S. Jaramillo stated that changes to instant game prize structures and possible changes in consumer shopping and purchasing habits due to the coronavirus may have been some of the contributing factors to this increase.

Net drawing game sales for were approximately \$47.7 million, which was \$1.96 million less than the FY 2020 revised budget and \$20.95 million less than FY 2019 sales of \$68.7 million. The difference in sales for the two fiscal years was mainly due to \$10.1 million less in Powerball sales and \$11 million less in Mega Millions sales. Larger jackpots in FY 2019 compared to FY 2020 contributed to the sales differences. In FY 2020, the largest Powerball jackpot was \$396.9 million, with nine smaller jackpots ranging from \$198 million down to \$22 million. In FY 2019, there were two large Powerball jackpots, \$768.4 million and \$687.8 million, which were the second and fourth largest Powerball jackpot to date. Last year we had the record Mega Millions jackpot of \$1.5 billion, while this year the largest jackpot was \$414 million, followed by \$375 million with three smaller jackpots ranging from \$225 million to \$168 million.

Gross Revenues for FY 2020 were nearly \$127 million, which were nearly \$6.5 million less than the FY 2020 revised budget and \$16.6 million less than FY 2019. Total Game Expenses ended the fiscal year 11% less than last year, which is comparable to net sales being 11.54% less than last year. Operating expenses ended the fiscal year at 3.08% of total Gross Revenues. Operating expenses were held as much as possible.

L. Romero observed that the Lottery included comparisons with the revised 2020 budget but did not include comparisons to the original 2020 budget. L. Romero inquired about the differences in revenues and expenses compared to the original budget. S. Jaramillo reported our gross revenue at the end of the year was \$8.5 million less than the original budget. The original budget return was \$40.695 million, we revised to \$36.2 million, and the actual return was \$38.145 million. D. Barden advised L. Romero that he understands the question and will provide the information he is requesting after the meeting.

S. Baragiola asked whether drawing games, particularly Powerball and Mega Millions, have a large impact on unclaimed prizes. S. Jaramillo stated that both Powerball and Mega Millions generally stay at approximately 50% prize payout depending on whether they are contributing to the reserve accounts that are set up to protect these games. Those two games will not impact the unclaimed prizes that we turn over; it is generally the instant games and some other games that fluctuate.

S. Baragiola asked why Powerball and Mega Millions do not impact unclaimed prizes. S. Jaramillo stated that for every dollar, the prize expense is generally 50% and so we have them budgeted that way. They are not fluctuating like other games each month.

P. Guerin observed that because of the number of months the Lottery used the unclaimed prize fund to meet the 30% mandate, it appears the small prize fund may impact our ability to return the 30% in the coming months. S. Jaramillo responded that this is correct to some extent. Prize structures were adjusted for instant games because the unclaimed prize fund had gone down to a zero balance in February. We had been using

more from unclaimed because as drawing games sales go down, the prize percentage goes up. In February, instant games were designed with lower prize payouts to push the prize percentage down. We would not have had the unclaimed prizes to cover the previous prize payouts and we would not have been able to reach the 30% return. We rebuilt the unclaimed prize fund back up to \$897,000 over time.

D. Barden stated that this past year has been challenging with COVID-19. The Lottery is lucky to have the return that we have garnered. The questions from Board members are great questions and he hopes to get into more detail during the upcoming Board planning session.

D. Barden described the "Lottery Dollar;" 30% is returned to the State for scholarships and 16% goes to operating expenses, which includes paying product and vendor fees. What remains is 54%. Last year we changed the instant game prize payouts to 54%. D. Barden stated that in the past, as he has informed the Board, jackpot games have balanced the budget. It is difficult to take \$21 million out of sales for games with a 50% payout in any given year, like we did this past year. We have grown our unclaimed prize fund a little, but as to P. Guerin or S. Baragiola's questions earlier, when you have big jackpots, you also have more unclaimed prize money. This past year, Powerball sales came in at \$16.6 million, which is the lowest since the Lottery started selling Powerball. We are trying to combat jackpot fatigue, as has been discussed for several years. Without these jackpot games, it is critical that we manage the instant games because we do not have a lot of room in our monthly income to meet our 30% requirement. There are a lot of things that come into play with the 30% mandate and we have been fortunate to manage it. It makes it a lot harder when we lose \$21 million in sales that we have no control over. COVID-19 has been a factor though we had seen slumping sales over the last two years.

No further questions.

Banking Resolution: S. Jaramillo described a resolution being requested as part of the RFP for Banking and Related Services that was awarded to Wells Fargo Bank. As part of these services, a \$4 million line of credit is to be provided by Wells Fargo Bank. This line of credit will be provided throughout the four-year contract ending May 14, 2024 with the possibility of extension for six additional years. This line of credit is an automatic unsecured line of credit to meet unexpected cash requirements. The line of credit will automatically protect the Lottery from overdrawing its accounts and provide payment for any checks or transactions presented against the Lottery's accounts.

The line of credit has been in place the last sixteen years and at least eight years at \$4 million. The line of credit has never been used because we have had adequate cash flow, but we have it in place in case of an emergency or in the event that we have higher-than-usual prize claims. A requirement by Wells Fargo for this line of credit is for a quorum of the Board of Directors to pass and adopt the provided Resolutions and Certificate of Incumbency Borrower.

L. Romero inquired about the interest rate on this line of credit and whether we pay interest only if we draw on this line of credit. S. Jaramillo reported that the interest rate is the prime rate of interest at the time we borrow the money. The Lottery does not pay any fees or interest unless we have an outstanding balance. No fees have ever been assessed since the line of credit has been in place.

L. Romero asked whether a single officer can draw on the line of credit or whether it requires two or three of the officers to authorize a draw on the line of credit. S. Jaramillo reported that when this was put in place in 2017, it was decided that the line of credit would require signatures from two of the three officers. L. Romero stated that the current resolution being presented states one officer can draw on the line of credit. S. Jaramillo reported that this is an oversight and with the Board's permission we can change the resolution to reflect that language. L. Romero stated that making this change would be best.

No further discussion or questions.

R. Jones entertained a motion regarding the resolution. D. Keylon made a motion to approve the resolution with amended language that two signatures are required from the authorized officers to draw on the line of credit; second by L. Romero. Vote: all ayes, no nays. Carried; 7-0.

R. Jones thanked S. Jaramillo and her staff for their hard work and continued efforts during this pandemic.

CEO Update: D. Barden thanked the Board and stated we have had many challenges over the past months and will likely have many more in the weeks ahead.

D. Barden stated that the Powerball and Mega Millions games have evolved over time, for example the price point and matrix changed making it harder to win and population was added to the games. The Lottery is a member of the Multi-State Lottery Association (MUSL), which runs Powerball. D. Barden is a member of the MUSL Executive Committee and chairs the Legal Committee. MUSL is currently in discussion with Australia to bring two of their states on board to sell Powerball. If this happens, Powerball becomes an international game with increased population, which would help the game. The \$16.6 million in Powerball sales last year is an all-time low for our state. Last year, Powerball sales were down 39.75% nationally. This year, we are down 12% making it even more important to make changes to the game. Adding population would boost the sales and when you boost the sales the jackpots climb faster.

In a typical year, there are 104 drawings (2 drawings per week x 52 weeks). Last year we had 56 Powerball drawings with jackpots that were not over \$100 million and zero drawings over \$400 million. There were 38 drawings with jackpots that ranged from \$100-\$200 million. In the past, players have said Powerball was a non-winnable game. Last year, players were winning all over the country. In the past, a \$100 million jackpot would excite players. Today, even a \$400 million jackpot does not excite players like it used to. Sales for Powerball and Mega Millions were \$28.2 million, which is low compared to previous years. In 2019, our sales were \$49.4 million; Scratchers were not quite as high, but you must have a balance in your portfolio.

The Scratcher program is something we can manage. The Lottery re-booted the Scratcher program in February and all the games were recalibrated for a 54% prize payout in order to meet the 30% return mandate. We are the only state in the country that does this. During years with our four highest transfers to the scholarship fund, the prize payout on Scratchers was above 58%. In our highest transfer year, Scratcher prize payout was at 63.3% when we launched our pilot program and had a good Powerball year. We continually work on our Scratcher products to keep them within margins each month. The Lottery uses unclaimed prize fund frugally for its operations to ensure we have enough money to make the required transfers. The students receive the unclaimed prize fund; it is not additional money.

D. Barden advised that the Lottery is reviewing and enhancing the Pick 3 and Pick 4 games and looking at all game prize payouts. The prize payout for Roadrunner Cash was recently adjusted to meet game specifications. A grand prize calculating error resulted in higher prize payouts for several years. The payout adjustment should result in significant financial savings in the future. The game is now balanced and where it should be.

D. Barden reported that the Lottery has adopted automation processes that allow us to do things remotely, save time and money, and allow staff to undertake more important functions within the organization.

D. Barden reported that Walmart is ready to come on board as a retailer. Walmart wants us to procure approximately 60 vending machines for their use. Each vending machine is about \$21,000 so we may come to the Board about budgeting and how to buy these machines. Having more retail locations is a plus for the Lottery. Walmart does not want on-counter sales, which the Lottery usually requires. As a compromise, Walmart will receive a 5% commission. We need to have a discussion about restructuring the retailer

commission, which would lead to cost savings, possibly by having retailers receive a bonus for doing certain things, like an add on commission. Having a total 6.5% retailer commission is one of our biggest expenses. Most states pay 5-5.5%.

N. Thayer thanked D. Barden for his steady leadership in the last six months and that it has been important. D. Barden thanked N. Thayer for her comment and advised we have a great team in place who are dedicated to the cause of providing scholarships to students.

R. Jones thanked D. Barden for his report and enjoys working with him and helping to advance the Lottery.

Other: D. Barden mentioned that the Lottery is working on the Board planning session.

Board Chair

Announcements: R. Jones stated that a Board planning session had initially been considered for August, but that did not occur because of COVID-19. The new proposed timeframe is the end of September. R. Jones stated her concerns about going further into the year without this planning session. There will be the upcoming legislative session and issues remaining regarding COVID-19. New Board members would benefit from an in-depth presentation.

D. Keylon is in favor of the planning session and advised that he will be out of town for a few days after September 23. N. Thayer commented that her only conflict is the fourth Wednesday of each month. No other members commented on issues with the date.


R. Jones stated that the goal is to conduct this planning session in person and follow the health order guidelines at that time.

No further discussion.


Other: None.

Other Items: None.

Adjournment: R. Jones entertained a motion to adjourn. N. Thayer made a motion to adjourn the meeting; second by S. Baragiola. Vote: all ayes, no nays. Carried; 7-0. The meeting adjourned at 11:18 a.m.



 R. Jones, Chairman
 Date: 10/7/20



 P. Guerin, Secretary/Treasurer
 Date: 10/7/20