

**Regular Meeting of Board of Directors  
New Mexico Lottery Authority  
November 15, 2017  
MINUTES**

**Call to Order:** Board Chair Dan Salzwedel called the meeting to order at 2:06 p.m. and asked for a roll call. Present and constituting a quorum were: Mark Koson; Amy Bailey, Dan Salzwedel and Sal Baragiola. John Kubiak and Paul Guerin were absent.

Present from NMLA were; David Barden; Sylvia Jaramillo; Michael Boland and Wilma Atencio.

Also present were; Jon Zajdel and Steve Beck with Intralot; Othiamba Umi with Think New Mexico; Matt Bone and Elizabeth Nunez with CliftonLarsonAllen and Colin Hunter with Barnett Law Firm.

**Approve Proposed Agenda:** D. Salzwedel entertained a motion to approve the proposed agenda. A. Bailey made a motion to approve the proposed agenda; second by M. Koson. Carried; 4-0.

**Approve Minutes of August 23, 2017 Board of Director's Meeting:** D. Salzwedel entertained a motion to approve the August 23<sup>rd</sup> minutes. M. Koson moved to approve the minutes; second by A. Bailey. Carried; 4-0.

**Public Comment:** None.

**REPORTS:**

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

**Approve Minutes of August 23, 2017 Operations Committee Meeting:** S. Baragiola moved to approve the minutes; second by A. Bailey. Carried; 4-0.

**Other:** None.

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

**Approve Minutes of August 23, 2017 Finance Audit Committee Meeting:** M. Koson moved to approve the minutes; second by D. Salzwedel. Carried; 4-0.

**Approve Minutes of October 12, 2017 Finance Audit Committee Meeting:** M. Koson moved to approve the minutes; second by D. Salzwedel. Carried; 4-0.

**FY 2017 Financial Audit:** S. Jaramillo reported that this is the 2<sup>nd</sup> year of a three-year contract with CliftonLarsonAllen LLP, the independent public accountants who performed the Lottery's FY 2017 financial audit. S. Jaramillo introduced Matt Bone and Elizabeth Nunez from CliftonLarsonAllen. Matt Bone provided a brief presentation on the released financial audit to the Board of Directors. The FY 2017 financial audit took place in August; it took two weeks to complete. The exit conference took place on October 12<sup>th</sup> with members of the Finance Audit committee and lottery management. The financial audit was submitted to the State Auditor on October 13<sup>th</sup> and released by the State Auditor's office on October 30, 2017 with a clean opinion and no audit findings.

The audit focused on areas that included internal controls, IT controls, cash/investments, capital assets, prizes, sales/expenses, transfer to the State and lottery act compliance. There were no corrected or uncorrected misstatements. CliftonLarsonAllen issued a clean opinion (unmodified opinion) on the Financial Statements. The audit was completed in accordance with government auditing standards.

M. Bone reported that the two non-financial IT compliance findings from FY 2016 have been resolved. D. Salzwedel asked for a brief synopsis of the two findings from 2016.

M. Bone reported that one finding dealt with the Network Access in which the lottery was unable to provide evidence for user account requests. Management placed procedures in place that corrected this item. The other finding was the Disaster Recovery and Business Continuity Plan. The lottery had developed a disaster recovery plan, but had not fully tested the new plan. Management responded that the lottery will continue to implement a fully functional disaster recovery plan and test the plan annually.

M. Bone reported that it is rare to have a state agency/entity or any business with no audit findings. The Board and the lottery is fortunate to have an employee such as Sylvia with her wealth of knowledge, tenure and ensuring that the policies and controls are consistently updated and followed. Sylvia and her staff were professional and easy to work with and all records/documents presented were in great order.

D. Salzwedel complimented management and staff for its continued diligence in this process.

M. Koson made a motion to approve the FY 2017 Financial Audit as presented; second by D. Salzwedel. Carried; 4-0.

**Financial Statements:** S. Jaramillo provided an update on the September 2017 financial statements. The New Mexico Lottery has met its statutorily required 30% return this month by returning nearly \$2.9 million dollars to the Legislative Lottery Scholarship program. We have now transferred nearly \$10.9 million dollars to the scholarship fund this fiscal year. With this return, the net revenue for the quarter is \$2 million more than the FY 18 YTD budget or nearly 23% more, but only \$1 million more than the first quarter of fiscal year 2017 – a 10.92% increase over the first quarter of fiscal year 2017.

With September's transfer, we have returned more than \$749.6 million dollars to the State of New Mexico for education since the inception of the Lottery. The lottery is close to reaching and surpassing the \$750 million mark.

Net instant ticket sales through September were approximately \$17.9 million, whereas last September's YTD net instant sales were approximately \$17.6 million – a \$264,000 increase this year or an increase of 1.5% from last year. Net Instant sales for the quarter surpassed the FY 18 YTD budget by more than \$1.8 million or 11.4%. Preliminary Instant sales figures for October are \$75,000 or half a percent less than last October YTD. Instant sales lagged behind the prior year by nearly \$340,000.

Net drawing game sales for the quarter were approximately \$18.4 million. Net drawing sales ended approximately \$4.5 million more than the YTD Budget or 32% more than budget. Net drawing sales through September were nearly \$3.3 million more than net drawing sales for the first quarter in fiscal year 2017 or 21.9% more. Powerball sales were nearly \$2.9 million more than last year, but Mega Millions sales were \$500,000 less than last year.

In July 2016, Powerball had a jackpot run-up to \$487 Million and Mega Millions had a jackpot run-up of \$536 million. In August 2017, we had both Powerball and Mega Millions run-ups - \$758.7 million for Powerball and \$393 million for Mega Millions. The differences in jackpot amounts and some jackpot fatigue account for the differences in sales between the two fiscal years.

Roadrunner Cash sales were \$307,000 more than last year and Hot Lotto Sales were \$494,000 more than last year. When the Hot Lotto game ended on October 28, 2017, the jackpot was over \$12 million.

Altogether, Total Operating Revenues for September were nearly \$36.3 million, which were nearly \$6.3 million more than the FY 18 YTD Budget or 21% more, but only \$3.6 million more than last September or 10.9% more.

Total Game Expenses are tracking with operating reserves with game expenses ending at 121.12% of the YTD Budget—while operating revenues ended at 121.06% of budget—tracking close to each other.

Operating expenses are at 3.94% of total Gross Revenues. Operating expenses for this fiscal year are being held as much as possible and are less than 100% of the budgeted amounts.

S. Baragiola asked when did PATP go live? D. Barden reported July 2016. The lottery currently has 22 retailers and hoping to have 100 additional retailer outlets in the coming year. There have been some issues with retailers having old pumps and software upgrades. PATP is currently generating \$1,700 in weekly sales and when we get up to 100 retailers, we anticipate that our annual PATP sales may be \$500 to \$750 thousand dollars.

S. Baragiola asked for clarification on S. Jaramillo's statement on instant sales that October is behind September and is that statewide. S. Jaramillo reported that instant sales were ahead YTD compared to the previous year in September, but because October's performance in instant sales wasn't that great, we're behind compared to the previous year. Sal asked if that can be mapped on a statewide basis to show where sales are up and down. Is it mapped geographically based on retailers? D. Barden reported that it can be mapped by retailers; 80% of our retailers are in Albuquerque and statistically the population is greater in Albuquerque, so sales in the metro area will be generally higher than outlying areas. D. Barden reported that the scratcher product is the only product in our portfolio that we have control over.

Mega Millions jackpot game is now a \$2 game, instead of a \$1 game. The percentage return on the game is approximately the same for Powerball and Mega Millions. In 2010 and 2013, we had PB and MM jackpot run ups and each of those years, the lottery returned over \$43 million to the scholarship fund. 2016 was a little different because during the previous two years we had an increase of 19% in our scratcher program due to an increase in our prize payout, but the high return in FY 2016 would not have occurred if we didn't have both jackpot run-ups and an increase in scratcher sales due to the higher prize payout.

Jackpot fatigue is our biggest challenge when it comes to online games. In 2016, the jackpot was won after 20 draws and we received \$2.4 million dollars and in 2017, the jackpot was won after 18 draws and we received only \$1.2 million. Players want the \$1.5 billion jackpot and statistically that will only occur once every 15 years or more.

**Online Gaming System Vendor Penetration Testing Report:** M. Boland provided a brief overview of the Online Gaming System Vendor Penetration Testing report. As part of the lottery's Online Gaming System RFP and contract, the online vendor is required to perform annual security assessment and penetration testing to assess and test the security and integrity of their online gaming system. M. Boland reiterated that this testing is critical due to the ever-changing and increasingly complex nature of cybersecurity. A third-party vendor conducted testing and issued a report in May 2017. A total of 21 risk findings were found ranging from high, medium and low risk findings. As of today, 11 risk findings (medium/low) need remediation. Intralot provided NMLA management with a revised Project Scope Statement outlining the expected timeline for remediating the remaining risk findings - January 14, 2018. Based on the testing performed, the gaming system appears to have sufficient controls present and functioning to mitigate risks and vulnerabilities to an acceptable level. Internal Audit further recommends two best practice recommendations; 1. the gaming system vendor should meet penetration testing contractual timelines; 2. the gaming system vendor should complete remediation of penetration testing findings in a more timely manner.

D. Barden reported that vendor penetration testing was not required of the vendor in the past. The CEO will amend the contract with no specific date and future testing will be conducted at the CEO's direction based on business needs. D. Barden reported that this is a closed in system that has no interaction with any external environments. The lottery has four (4) software releases per year to implement programming changes. The vendor chooses the most critical action items for deployment based on the CEO's priority list.

The Board reported that the testing and resolution of the findings is an administration function of the lottery and further recommends that the CEO and management are following due process with the vendor in ensuring that the findings, testing and remediation thus far are of an acceptable level. The board further denotes that their position is to accept the report as presented and any further action be at the discretion of the CEO and staff.

S. Baragiola made a motion that the Board adopt recommendation #1 and #2 as a high priority item and implementation and oversight of both of these recommendations will be the sole responsibility of the CEO and his authority. In addition, any updates, be submitted to the security committee on an ongoing basis; second by D. Salzwedel. Carried; 4-0.

M. Koson made a motion to accept the Online Gaming System Vendor Penetration Testing Report as presented; second by D. Salzwedel. Carried; 4-0.

**Change Management Review:** M. Boland reported that the Change Management Review evaluates the controls of NMLA's network when changes are made by the online vendor and by the lottery. Intralot was provided operational control of the lottery's instant ticket and online games processing. Internal Audit periodically ensures that the lottery has sufficient internal controls in place regarding policies and procedures by having proper approvals, proper documentation and authorization prior to release of the changes on the NMLA network and BOS System. There were no findings. The lottery has good controls in place. Internal Audit has some recommendations that are not critical and serve as suggestions to enhance current controls and best practices.

M. Koson made a motion to approve the four recommendations as presented in addition to accept the Change Management Review report as presented; second by D. Salzwedel. Carried; 4-0.

**Other:** None.

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

**Approve Minutes of August 23, 2017 Personnel Committee Meeting:** D. Salzwedel moved to approve the minutes; second by M. Koson. Carried; 4-0.

**Other:** None.

**CEO Update:** D. Barden provided a quick update. D. Barden provided a slide to the Board titled FY 18 Instant National Sales Trends, which provides a glimpse of what is happening nationally and what has transpired with Oklahoma Lottery who had their mandate repealed. The average national instant sales increased by 6.9%; NM is down -.5% and Oklahoma is up 52% in scratcher sales. This shows that prize payouts make a difference. Players play to win and when players play, students win by receiving more educational dollars for scholarships and other funding.

During the past 10/11 years, the lottery has been down 21% in instant ticket growth compared to the nation, nationally the growth is up 45.3%. The lottery has lost tens of millions of dollars in sales and returns for its beneficiaries. The business model NM is using is no longer working - its broken and we

need to fix it. NM has shown that when prizes go up, proceeds goes up. It's a win-win for NM. It's time for a change.

M. Koson asked how much Oklahoma lottery netted last year and what are they projecting in netting this year? D. Barden reported he doesn't have that information, but will get the information for the board.

The Oklahoma lottery is expecting an additional \$110 million dollars for education over the course of the next 5 years. Oklahoma increased their prize payout by 10% across the board. They now have a \$10 and \$20 scratcher. NM, Louisiana and South Carolina are the only states that don't have a \$20 scratcher ticket. South Carolina doesn't have one because their \$10 scratcher is like a \$20 scratcher in terms of prizes and prize payout.

D. Barden reported the new Lotto America game began its sales on November 12<sup>th</sup> and took Hot Lotto's place. As Sylvia stated earlier, Hot Lotto ended with a high jackpot - \$12 million; the Lotto America group voted to roll the Hot Lotto ending jackpot into Lotto America. Jackpots for Lotto America normally start at \$2 million, but on November 12<sup>th</sup> the starting jackpot for Lotto America was \$15 million. Lotto America is a \$1 game.

D. Barden reported he met with LFC and it was a good meeting and received very positive feedback and members were in agreement that it's time for a change.


D. Barden also reported that there will be a couple of policies that will be presented at the next regular board meeting – Online Game Policy and Document Retention Policy.


**Other:** None.

**Other Items:** D. Salzwedel requested that the CEO author a letter on behalf of the Board of Directors and the lottery expressing appreciation for Mr. Claude Austin's efforts, performance, leadership and integrity while serving on the New Mexico Lottery Authority Board of Directors. In addition, the CEO is directed to contact the Governor's office for a similar document. D. Barden reported that he will also have a resolution ready for the Board's approval at the next regular scheduled board meeting.

The next interim board meeting will occur in February 2018.

**Adjournment:** D. Salzwedel entertained a motion to adjourn. S. Baragiola moved to adjourn the meeting; second by A. Bailey. Carried; 4-0. The meeting adjourned at 3:19 p.m.

  
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Dan Salzwedel, Chairman  
Date 3/20/18

  
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John Kublak, Secretary/Treasurer  
Date 3/20/18