

**Regular Meeting of Board of Directors
New Mexico Lottery Authority
October 28, 2020**

MINUTES

Call to Order: Board Chair Reta Jones called the meeting to order at 1:04 p.m. and asked for a roll call. Present and constituting a quorum were: Othiamba Umi, Paul Guerin, Leo Romero, Reta Jones, Sai Baragiola, David Keylon, and Nina Thayer (virtual).

Present from NMLA were David Barden and Wilma Atencio. Attending virtually were Carolyn Cabell, Michael Boland, Sylvia Jaramillo, and Tyson Payton. Also, in attendance virtually were Mary Stanford and Steve Beck with INTRALOT; Ron Miguel, Howard Glaser, and Steven DiMasi with Scientific Games; Joe Thompson; Pat Rogers; and Dominic Gabello.

Approve Proposed Agenda: R. Jones entertained a motion to approve the proposed agenda and a roll call vote. L. Romero made a motion to approve the proposed agenda as presented; second by D. Keylon. Vote: O. Umi, aye; P. Guerin, aye; L. Romero, aye; R. Jones, aye; S. Baragiola, aye; D. Keylon, aye; and N. Thayer, aye. No nays. Carried; 7-0.

Public Comment: None.

R. Jones stated this is a follow up meeting to the prior planning session. R. Jones stated she would like to have an open discussion and come up with a plan for where the Lottery should be headed and possible steps to take in the upcoming legislative session. No votes or action will take place today.

CEO Update: D. Barden reported that jackpot game sales are down 10%, which is on top of the 39% we were down last year. Scratcher sales are up 19%, most likely due to the pandemic, and once the state reopens, Scratcher sales may return to where they were. The Lottery is estimating a \$39-\$40 million transfer to the State for scholarships.

D. Barden presented examples of proposed Lottery Act changes from bills in past legislative sessions, including eliminating the 30% mandate, placing a cap on operating expenses, guaranteeing a return amount to the tuition fund on a yearly basis, and requiring that unclaimed prizes be transferred to the tuition fund.

D. Barden reported that the Lottery's current operating expenses are approximately 16.5% of gross revenue. The Lottery could work with a 16% or 17% operating expense cap. D. Barden reported that some state lotteries do not have a return requirement but do have a threshold for operating expenses. L. Romero asked what the operating expense percentage has been. D. Barden responded that the operating expenses have averaged approximately 16.5% of revenue.

D. Barden stated that none of the proposed changes mentioned are complicated by themselves, but when combined in one legislation become unattainable as a whole. R. Jones asked D. Barden for clarification that the examples shown were parts of past proposed legislation and not proposals made by the Board.

S. Baragiola asked how far the last legislation proceeded through the legislative process. D. Barden responded that the legislation died on the final day in third reading in the House of Representatives. The bill was sponsored by Senator Jacob Candelaria and Senator John Arthur Smith.

O. Umi asked whether the examples provided are part of past legislations or new concepts. D. Barden responded that these are all existing legislative suggestions contained in bills introduced over the years. O.

Umi stated it would be helpful to have the bills that have been introduced in the past. D. Barden responded that the Lottery will provide this information to the Board.

D. Barden provided information from the La Fleur's industry publication that shows sales, percentages, and prize payouts for instant games. New Mexico is ranked at the bottom for prize payout and low for per capita sales. Oklahoma had the most improved sales with growth of 46%.

L. Romero asked about the example regarding a guaranteed return amount and whether the legislation would revert back to the 30% requirement if the minimum is not met going forward. D. Barden confirmed that the past proposed legislation would revert back to the 30%.

L. Romero stated there are three factors: the percentage that goes to the tuition fund, the cap on expenses, and minimum payout, with the third being the most difficult to determine. D. Barden stated it was a leap of faith to get to a compromise on legislation and he believes the Lottery could have met the goals if given time to grow.

D. Barden stated if unclaimed prizes were not available, the return percentage and actual transfer to the fund would be reduced. R. Jones reported in the last four years, without the unclaimed prize fund, the Lottery would have averaged a 26% return to the fund. The Lottery uses the unclaimed prizes to balance and meet the 30% return. In 2020, the Lottery transferred \$38.1 million, but without unclaimed prizes it would have returned \$33.9 million with a percentage return of 26.7%. In 2019, the Lottery transferred \$43.1 million, but without unclaimed prizes it would have returned \$38 million with a return percentage of 26.4%. In 2018, the Lottery transferred \$40.2 million, but without unclaimed prizes it would have returned \$37.1 million with a return percentage of 27.7%. From 2016-2020, on average the transfer percentage without unclaimed prizes would have been 26.5%.

Strategic Direction: R. Jones stated that everyone is committed to returning the maximum amount to the students, while providing checks and balances. The difficult part is looking at those controls and how they overlay into lottery operations and not cause any detriments to the organization without getting real results.

R. Jones provided historical information on financial statements from 1998-2020. There are things that the Lottery can control, like Scratchers, but the Lottery cannot control draw games. The Lottery has done a great job in stabilizing by purchasing the building, moving sales employees to its online vendor INTRALOT, and negotiating better contracts with its online and instant ticket vendors. Vendor fees are based on a percentage of revenue and declining revenue could have an impact on their rates.

R. Jones provided an analysis from the third-party source La Fleur's Magazine, which compiles data on lotteries in the U.S. and abroad. The report shows sales and returns. Only one other state, Louisiana, returned a higher percentage than New Mexico to their beneficiary. New Mexico has the lowest prize payout of all the states reported. If players do not see an opportunity to win, they do not play. S. Baragiola asked whether the report includes Powerball and R. Jones confirmed that it does.

R. Jones reported this document shows lotteries across the U.S. are not the same and do not have the same portfolios. Some lotteries offer racing, pull tab, video gaming, sports gaming, and varying other activities. New Mexico offers draw games and Scratcher games. The Lottery and Board need to consider what our options are for increasing revenue and how to remove reliance on draw game jackpots over which we have no control. If a jackpot does not happen, then we need to cut other places dramatically. We have contracts with vendors in place and have minimized costs, so the only place to cut is prize payouts. D. Barden concurred.

L. Romero asked whether there could be a mandate on the prize payout percentage. For example, could that percentage be set at 65% to give the Lottery flexibility in pricing different games. R. Jones stated that the Lottery has a mandatory minimum prize payout of at least 50% currently. We may be nearing a point where the Lottery is unable to meet the statutory obligations. D. Barden agreed and stated that with a 30% return mandate and an average prize payout of 65%, the Lottery would be left with very little to pay operating costs. L. Romero asked if the 30% were eliminated, could the payout be used as a control to still maximize the return to the students. D. Barden responded that it could.

D. Barden stated that the only part of our portfolio that can control is our Scratchier games. Multi-state draw games are set at the national level and all lotteries have the same payouts. When there are no large jackpots, the Lottery has to find funds elsewhere. D. Barden advised that the Lottery does not budget to a dollar amount, but rather to a percentage. The Lottery conducted a pilot project from 2014-2016 and each 1% increase in Scratchier payout resulted in approximately \$1 million more to students. We are the only lottery in the U.S. that has a prize payout of 54% on all its Scratchier games. Our neighboring state like Arizona and Texas have prize payouts around 70%. Oklahoma's percentage mandate was removed, and Louisiana had their mandated percentage lowered. Another issue that the Lottery contends with is anti-gaming sentiment, which hinders the Lottery's ability to discuss these issues.

S. Baragiola suggested it is important to understand the original spirit and intent of the 30% mandate. Proposed legislation took that spirit into account by giving people a comfort level that nothing would be done to jeopardize returns. S. Baragiola invited anyone in attendance to have an open discussion about the intent of the 30%.

R. Jones reported that the 30% mandate was implemented in 2007 and at that time, the Lottery did not have input into legislation. R. Jones reported her understanding was there was an overall sense that expenditures were being incurred that needed checks and balances. There was also a review of other lotteries and a trend toward checks and balances nationally.

O. Umi stated the Chair is correct in why the 30% requirement was put in place. Contracts and vendor fees were higher prior to 2007. When the 30% was implemented, it forced the Lottery and vendors to lower the percentage rates and more monies were returned to the tuition fund. Other states have reduced their requirement and increased their overall revenue significantly, but the returns have plateaued and not increased at the same level. Moving forward, if the revenues increase, our return to the scholarship fund should have the same increase as well.

R. Jones stated the actual dollar returns are not going up, even under the current 30%; they plateaued as well. The returns are fairly consistent since 2008, generally moving up and down based on draw game sales and jackpots. R. Jones asked O. Umi to confirm that his concern is if revenues go up, that the beneficiaries should participate in the revenue gain. O. Umi concurred.

R. Jones stated that the challenge when building something new is the unknown. In order to increase revenue, especially on Scratchier tickets, the Lottery needs to increase prize payouts. S. Baragiola stated the pilot project tested well and there is data from across the country. There should be a high confidence level that revenues will go up and there is not a lot of jeopardy in going forward, in conjunction with other ways to maximize revenue such as new games, new venues, and new methods of reaching people who are not playing the lottery now like smartphone apps. Increasing prizes leads to the ability to try new things and adopt new technology.

S. Baragiola stated that if the intent of the 30% was to reduce operating costs, then that has been done. There have been millions in savings over the past four to five years. D. Barden reported that there are major vendors not bidding because they cannot make money here and with fewer vendors, rates will go up in the future.

L. Romero asked whether the 30% mandate resulted in a reduction in expenses. D. Barden responded there has been a gradual reduction in expenses since that time. The Lottery continually looks for ways to save, including buying the building and having the vendor take over the field staff.

L. Romero asked whether mistakes were made at the time the 30% was implemented. D. Barden responded that the discussion at that time was that people thought the vendor contracts were too high. R. Jones stated that operating expenses need to be looked at in conjunction with what was happening at the time. If the Lottery is operating efficiently, she is not sure where else to go to continue to cut costs. For example, even a 10% cut in all operating expenses would not have a significant impact on the return to students. D. Barden advised that the rate for our gaming system vendor was lower in the previous contract because the company wanted to get into the U.S. market.

L. Romero stated there are two ways of making reductions: reduce expenses to meet 30% or reduce the prize payout on Scratchers. D. Barden concurred and explained that prize payouts have come down recently due to the lack of draw game jackpots. D. Barden advised that changes are being considered for Powerball, including adding a draw day and contracting with Australia to offer the game.

D. Keylon asked whether cutting expenses was the reason for years with higher returns to the scholarship fund. D. Barden responded that it was a combination of cutting expenses and adjusting Scratcher payout. The pilot project of higher Scratcher payouts worked. However, we did not have the funds to sustain it, which resulted in Scratcher sales declining after the Lottery lowered prize payout. With the higher prize payout, sales were \$13-\$14 million more.

O. Umi stated that the 30% encompasses both the draw game sales and instant tickets. O. Umi asked how much Scratcher sales could increase overall revenue to where jackpots would not matter. D. Barden responded if the Lottery were at the national norm for Scratcher games, 65-66% prize payout would be ideal and with this, the Lottery could bring in an additional \$8-\$12 million in Scratcher sales, enough money to stabilize. Any sales from large jackpots would be an added benefit. We would continue to look at minimum expectations for draw game sales, because no lottery can control draw game jackpots. R. Jones stated this is a challenge and in order to balance, we would have a minimum Powerball budget in order to get to the return we want and if we get more than the minimum, then that goes to the bottom line.

D. Keylon asked whether the Lottery has an optimum prize payout. D. Barden responded that having a prize payout between 65-67% would be ideal, but the Lottery could start at the lower end during the first year to grow with a tempered and responsible approach. D. Keylon asked about the short-term adjustment in prize payout. D. Barden responded that he would like to get back to the 61% prize payout from before the Lottery cut it to 54% and bring it up slowly to 65-67%. Players would recognize the changes and that would lead to an increase in Scratcher sales. S. Baragiola reported he hears from people who recognize the higher payouts in neighboring states.

O. Umi stated that whatever direction the Board decides on the Lottery's legislative vision going forward, there are upcoming changes with the elections and both the House and Senate will be changing. He asked whether the Lottery has spoken to a legislator or whether they have someone in mind to sponsor a bill repealing the 30%. R. Jones responded that the first step has been contacting the Governor's office. R. Jones reported that Dominic Gabello, senior advisor from the Governor's office, attended part of today's meeting. As Board Chair, it was important to reach out and get an understanding and direction from the Governor's office regarding support for changes related to the Lottery.

R. Jones stated the Lottery should also have open discussion with Think New Mexico about the challenges facing the Lottery and see whether we can work together for the students and scholarship fund. S. Baragiola stated it should be easy to move forward with removing the 30% provided students receive more when

revenue increases. O. Umi stated that though he works for Think New Mexico, he is a member of this Board and his own individual. It is difficult to come to a consensus; the bottom line is guaranteeing students are not hurt by changes.

L. Romero asked if there is modeling that proves the assumption that increasing prize payout increases sales. Both R. Jones and D. Barden stated yes. L. Romero stated this is crucial information for members to review and determine the best course of action for the Lottery. P. Guerin stated the Board received detailed information at the recent Board planning session and there is information from other states. What we do know is that it is getting more difficult to meet the 30%.

L. Romero asked whether a proposal eliminating the 30% for a trial period would fare better at the legislature. D. Barden reported that a sunset has been discussed before. D. Keylon asked whether reducing the percentage, for example to 25%, has been proposed. D. Barden responded that this option has also been discussed.

L. Romero suggested the Lottery provide scenarios of what revenue and returns could have been under different assumptions had there not been a 30% mandate. D. Barden responded that the Lottery has this information and can provide it to the Board. D. Keylon suggested simple charts showing projections, local results when we increased payouts, and evidence from other states when they increased their payouts. R. Jones recommended keeping information simple and easy to understand.

R. Jones asked each member for input on a potential proposal and whether there is additional information needed before proceeding.

S. Baragiola stated he has a high confidence level that increasing prize payout would increase revenue. Staying within the spirit of the 30% is important for success at the legislature. S. Baragiola stated the Lottery has enough information on hand to create a proposal.

D. Keylon concurred and added he would not recommend putting specific dollar amount requirements in the proposal.

O. Umi stated he would not consider eliminating the 30% mandate without some guarantee for students that they would benefit. In 2007, the Lottery had leeway and were not maximizing revenue for students. There need to be accountability measures along with any removal of the 30%.

P. Guerin stated that during his time on the Board he has come to believe the 30% is what is holding the Lottery back from returning more for students. P. Guerin stated he is in favor of eliminating the 30% requirement and while he is not sure it is necessary; he understands having accountability measures for the legislature.

L. Romero stated he is persuaded we should eliminate the 30% mandate and is comfortable that the assumptions will prove to be correct. L. Romero agreed with D. Keylon that there should not be a set dollar amount in legislation because revenue cannot always be predicted. L. Romero would be interested in hearing other ways to have accountability other than the 30%. D. Barden discussed the option of a cap on operating expenses, potentially at the current 16.5% of revenue level.

N. Thayer stated she would consider lowering the 30% mandate to 25% with a four-year sunset clause, as an experiment.

R. Jones stated the next step is for the Lottery to provide projections in a simple format. Board members will then have the next several weeks to review, discuss, and solidify recommendations. The Board needs

to have a common proposal we can support prior to any activity with the legislature. S. Baragiola thanked the Chair for leading this effort.


No further discussion.

Other Items: None.

Adjournment: R. Jones entertained a motion to adjourn. D. Keylon made a motion to adjourn the meeting; second by N. Thayer. Vote: all ayes, no nays. Carried; 7-0. The meeting adjourned at 2:57 p.m.



R. Jones, Chairman
Date: 2/24/21



P. Guerin, Secretary/Treasurer
Date: 2/23/2021