

CALIFORNIA STATE LOTTERY COMMISSION

Minutes – September 24, 2020

Sacramento, California

1. **Call to Order**

Vice Chair Peter Stern called the meeting of the California State Lottery Commission to order at 10:00 a.m. The meeting was held via Microsoft Teams and teleconference.

2. **Pledge of Allegiance**

Vice Chair Stern led the Pledge of Allegiance.

3. **Roll Call**

Vice Chair Stern asked Elisa Topete to call the roll.

Commission Members Present:

Vice Chair Peter Stern

Commissioner Nathaniel Kirtman

Commissioner Keetha Mills

Commission Members Not Present:

Chairman Gregory Ahern

California State Lottery staff and presenters:

Alva V. Johnson, Director

Fernando Aceves, Chief Counsel

Roberto Zavala, Deputy Director of Internal Audits

Sharon Allen, Deputy Director of Sales and Marketing

Nicholas Buchen, Deputy Director of Finance

Jeremy Linson, Acting Deputy Director of Security and Law Enforcement

Elisa Topete, Assistant to the Commission

4. **Consider Approval of the Agenda**

Vice Chair Stern asked if any of the Commissioners wanted to make changes to the September 24, 2020, proposed agenda. Commissioner Mills made the motion to approve the agenda and was seconded by Commissioner Kirtman. The agenda passed unanimously.

5. **Approval of the Minutes**

Vice Chair Stern asked if there were any additions or corrections to the June 25, 2020, minutes. Commissioner Mills made the motion to approve the minutes for the June 25, 2020, Commission Meeting and was seconded by Commissioner Kirtman. The minutes passed unanimously.

6. Informational Items

a. Director's Comments

Director Alva Johnson provided estimates of Lottery sales through September 19th that were just shy of \$1.78 billion, which is 16% higher or about \$240 million above the sales goal through the first 2½ months of this fiscal year and 31% higher than sales through the same time period last fiscal year.

In a typical year, consumer sales and distribution sales are roughly the same as the Lottery sends Scratchers[®] tickets to retailers that will replenish their inventory based on the amount consumers have purchased. Due to the pandemic, the last few months of FY 2019-20 saw consumer sales being significantly higher than distribution sales as Lottery operations in our Distribution Centers had to be modified to accommodate social distancing protocols resulting in a reduced capacity.

The strong sales thus far this fiscal year come from stellar performances from Scratchers, Daily Games, and Hot Spot[®]. After having back-to-back weeks with brand new Scratchers games being introduced, including last week's launch of the PAC-MAN[®] family of games, sales broke an all-time record of nearly \$120 million worth of tickets sold in one week. Director Johnson provided an overview of sales by product.

In addition to sales, staff also assess the Lottery's contribution to public education. The calculations are based on the Lottery's monthly financials through August. Over the first two months of the fiscal year, sales were running 15% ahead of goal while contributions to education were about 8% ahead of goal over the same time period. Because Scratchers sales are well above their sales goal and Jackpot Game sales are behind their goal, the Lottery's contribution to education have a more modest increase than sales since Scratchers have lower profit margins than Jackpot Games. Although it is only 2½ months into this fiscal year, early signs are very positive in terms of the Lottery's sales rebounding from the decrease seen last year due to the pandemic.

October 3rd will mark the Lottery's 35th Anniversary and Director Johnson acknowledged and thanked the several Lottery staff members who have been with the Lottery the entire 35 years for their dedicated service.

Commissioner Keetha Mills asked what the difference was between the two ways sales were presented and which one ultimately gets reported in the Lottery's public-facing financial statements. Commissioner Mills also asked why staff felt the change was important to present. Director Johnson explained that due to the disruptions in the Lottery's distribution, the material presented shows exactly how the product is distributed to the retailers and how they can sell their product, as compared to consumers buying the products and what is shown in the Lottery's

financials is the retailers minus the returns. Deputy Director of Business Planning, Jim Hasegawa, stated that the reason for showing the distribution sales is because of the upheaval from the pandemic and the impact it had on our distribution of tickets. Therefore, it is the actual measure of what the Lottery's financials will ultimately show.

b. Overview of the Lottery Audit Committee

Deputy Director of Internal Audits, Roberto Zavala, stated that the Committee was established in 2008 and is responsible for ensuring audit findings are reported to the appropriate levels of government. The Committee provides the Lottery Commission additional guidance on financial statements, compliance with statutory and regulatory requirements and qualifications and performance of audit personnel. The Committee also ensures that audits be conducted in the most ethical, professional, and efficient manner to protect the people of the State of California.

Two members are appointed by the Lottery Commission and serve at the pleasure of the Commission and shall have a member with financial experience. The Committee meets at least two times per year and additional times as necessary. The Committee also meets with the Chief Internal Auditor, the Chief Counsel or any other Lottery staff that they deem necessary.

Specific functions include reporting to the Lottery Commission annually and reviewing and commenting on the annual Lottery Audit Plan. They support Internal Audits on issues and promptly consider reports from them. They review complaints, changes in audit personnel, suspected fraud, or other wrongdoing that may require attention. The Committee also reviews audit reports, significant correspondence between the Audit Chief, and management responses. The Audit Committee monitors statutory and regulatory changes that impact internal audits and review the Incompatible Activities and Ethical Conduct Standards to establish that they are adequate, effective and consistent with current law. Additional roles are to provide input on coordination of all audit functions and decisions to employ audit firms for services. They serve as a liaison between the Lottery and the State Controllers Office and provide input in connection with the engagement of independent/external auditors.

Vice Chair Stern and Commissioner Mills thanked Mr. Zavala for his leadership of the Audit Committee. As Chair of the Audit Committee, Commissioner Mills stated that the audit work is extremely important given the Lottery's Strategic Plan's core pillars about making sure that the staff are being good stewards of public funds to meet the Lottery's mission. Ms. Mills asked Mr. Zavala to explain the processes, procedures and controls of the audits and how his team, external auditors or the State Controller's Office may identify areas of continuous improvement.

Mr. Zavala stated that staff share their work with the State Controller's Office to make sure there is no redundancies of additional audit work that needs to occur and that there is a process in place when findings are brought forward to the Commission. Staff track every single audit report and solutions to the findings from internal audits, the State Controller's Office, the State Auditor and external auditors. Staff meets with audit parties to review additional areas such as past audit findings.

c. Field Operations Update

Deputy Director of Sales and Marketing, Sharon Allen, provided an update on field operations, the impact of COVID, and the modifications that have been made to continue operations while prioritizing the health and safety of the Lottery's team members, retailers and the public.

In mid-March, the Lottery decided to delay on of the biggest initiatives of the year – the release of new games scheduled for March 24th and supporting the PAC MAN Scratchers marketing campaign.

When the stay at home orders were first issued, all district offices were closed to the public. The district offices accepted completed claim forms from players for prizes over \$600. Although players could still file claim forms via mail, some players were not comfortable mailing claims for large prizes. In July, the Lottery implemented a secure drop off process at the district offices and received nearly 9,000 claims in the first nine weeks of the program. The Sacramento District Office successfully piloted a program where qualified claimants can receive checks for prizes up to \$1000 on the spot. In the modified process, claimants now receive their checks in the mail in less than a week, versus the average six to eight weeks.

Strict social distancing protocols were implemented in the two distribution centers which are responsible for shipping Scratchers tickets to retailers. This resulted in significant disruption to the Lottery's players and retailers. Ms. Allen went over the implementation of several strategies to help mitigate the impacts while maximizing health and safety. While the Lottery is not back to pre-pandemic levels, staff has made great progress with two back-to-back weeks of new Scratchers games. The distribution centers resumed daily order fulfillment at the beginning of September and are keeping on track with only slight delays.

Lottery staff has not been providing in-person service to its retailers since mid-March. They have been servicing the retailers remotely while plans are being developed to safely return the team to the field. The plan includes the appropriate personal protective equipment, modifying safety procedures and additional extensive training. Initially, the focus will be on high priority activities such as supplemental ticket distribution, point-of-sale drop off only and ticket returns. Retailers must meet the Lottery's safety requirements in order to get service. District Sales Representatives will have the discretion to avoid servicing retailers

that are deemed not safe. Lastly, management will closely monitor and adjust as necessary, always prioritizing health and safety.

Vice Chair Stern asked if staff is reassessing process improvements to field operations that might be relevant in a non-COVID era that the Lottery can adopt. Ms. Allen stated that staff on the marketing side has been able to work remotely, however, on the field sales side, it is important to have the in-person contact. Thus, management is looking at ways to re-evaluate the Lottery's processes in order to appropriately serve the players as their consumer behavior shifts.

7. Consent Calendar

8. Action Items

a. Lottery Investment Strategy and Investment Policy

Deputy Director of Finance, Nicholas Buchen, presented the Lottery's Investment Policy which requires that the Commission review and adopt not less than annually, including the approval of any changes to the Investment Policy. The Lottery's current Investment Strategy and Investment Policy focus on the management of ongoing investment activity in support of draw games and Scratchers® games that offer an annuity option to winners. It also focuses on maintenance of the Lottery's Investment Portfolio to monitor and mitigate potential investment risk. This ensures that scheduled payments to annuity prize winners are fully funded.

Vice Chair Stern asked if anyone from the audience had any questions on Action Item 8(a) Investment Policy. No one came forward, so he proceeded to the motion.

Commissioner Mills made the motion to approve Action Item 8(a) Investment Policy, and it was seconded by Commissioner Kirtman. The motion passed unanimously.

Vice Chair Stern asked if anyone from the audience had any questions on Action Item 8(a) Investment Strategy. No one came forward, so he proceeded to the motion.

Commissioner Kirtman made the motion to approve Action Item 8(a) Investment Strategy, and it was seconded by Commissioner Mills. The motion passed unanimously.

b. Changes to Stolen Tickets Regulations and Policy

Deputy Director of Finance, Nicholas Buchen, requested Commission approval for changes to the Lottery Regulations and its stolen ticket policy to better incentivize Lottery retailers to maintain Scratchers inventory. The proposed

policy will also encourage retailers to report more thefts, both of which will prevent redemption of stolen tickets and allow for more robust data that can lead to additional process changes in the future.

Vice Chair Stern asked if anyone from the audience had any questions on Action Item 8(b). An unknown caller asked if data was available on the percentage of Lottery tickets that are stolen each year and the number of retailers licensed to sell that have experienced thefts this year. Acting Deputy Director Jeremy Linson stated that a newly created Ticket Theft Committee has been formed and are taking a closer look at the numbers. The Lottery's retailers had experienced at times, one theft within a hundred retailers. Staff is closely monitoring this matter. There has been a steady decline of thefts in the last month. Currently, there is approximately one theft in every 200 retailers. Because this data is fairly new, hopefully within a year, staff will be able to ascertain a more accurate total loss for the Lottery.

The caller asked if there was any sort of evaluation on any commonalities around access to Lottery tickets. Mr. Linson stated that in the short time of collecting this data, most of the thefts occur after hours through broken glass into the retailer. Staff will continue to collect and analyze data so that information can be passed along to the retailers to protect themselves and their products.

Commissioner Mills made the motion to approve Action Item 8(b) and was seconded by Commissioner Kirtman. The motion passed unanimously.

c. Termination of Stanley Convergent Security Solutions, Inc. Contract

Acting Deputy Director of Security and Law Enforcement, Jeremy Linson, requested Commission approval for the early termination of the existing contract with Stanley Convergent Security Solutions, Inc. The Lottery has decided to create two in-house Information Technology Specialist positions to oversee the Lottery's security system.

Commissioner Mills expressed her appreciation for the care and diligence that went into the review that created the outcome to determine that staff can perform this task better and more cost-effectively. It is a great example of an organization coming together across many divisions for a better outcome for the Lottery's operations.

Vice Chair Stern asked if anyone from the audience had any questions on Action Item 8(c). No one came forward, so he proceeded to the motion.

Commissioner Mills made the motion to approve Action Item 8(c) and was seconded by Commissioner Kirtman. The motion passed unanimously.

9. Commissioner General Discussion

10. Scheduling Next Meetings

The next Commission Meeting is tentatively scheduled for November 19, 2020.

11. Public Discussion

For Public Discussion, Vice Chair Stern sought public comments or questions. No one came forward. Director Johnson recognized the tremendous work that the entire Lottery family has been putting in the last several months where staff has stepped up to face the many challenges to help serve the Lottery's mission. Although we are still in the middle of the pandemic, staff is still working on solutions as a team and the spirit shows in the great work that the entire Lottery is doing, and he thanked staff for their accomplishments.

12. Adjournment

Meeting adjourned at 11:09 a.m.