

North Carolina Education Lottery Commission Meeting
WebEx
Meeting Minutes
Wednesday, June 15, 2022

Commissioners in Attendance:

Brad Adcock, Chairperson
Randy Jones
Nigel Long
Joshua Malcolm
Ripley Rand
Jason Roth
Jody Tyson
Pamela Whitaker

Staff in Attendance:

Mark Michalko	Bill Jourdain
Billy Traurig	Randy Spielman
Terri Avery	Terri Rose
George Walker	Susan Singley
Hayden Bauguess	Van Denton
Joe Cosgriff	Joe Norman
Marbet Cuthbert	Michelle Freeman
Mike Suggs	Reggie Barnes
Stacy Askew	Tami Wiggs
Amanda West	Damen Harris
Molly McClure	

Other Participants:

Benjamin T. Spangler,
Assistant Attorney General, Department of Justice

The North Carolina Education Lottery meeting was held on Wednesday, June 15, at 10:00 a.m. via Webex.

Chairperson Brad Adcock opened the meeting, and greeted all Commissioners and meeting attendees.

Roll call of the Commissioners was taken.

Benjamin Spangler, Assistant Attorney General, read the remote meeting announcements.

Chairperson Adcock read the state ethics announcement.

Attendees recited the Pledge of Allegiance.

Approval of Minutes

Commissioner Joshua Malcolm made a motion to approve the minutes for the December 14, 2021 Closed Session and the March 30, 2022 Commission Meeting. Commissioner Nigel Long seconded the motion, which passed unanimously.

Revenue Generating Committee Report

Product Development & Digital Gaming Update

Randy Spielman, Deputy Executive Director of Product Development and Digital Gaming, presented an update to the Commission.

Q4 Scratch Off Review

April

- YoY sales are down 6.5%, but this was anticipated given unusually strong performance last year.
- Launched Scorching Hot 7s \$10 game, with very good performance. Second best \$10 game to date.
- Expanded Loteria subcategory to \$5.

May

- YoY -0.25%
- Introduced \$20 Million Mega Cash - continues to be our highest growth price point.

June

- Introduced Carolina Jackpot family (\$1, \$2, \$5, \$10)
- First scratch off game to feature a 2nd chance drawing with a progressive jackpot that grows with each ticket entered. Positioned to encourage players to sign up for Lucke-Rewards.

FY22 Fast Play

W!n Family introduced in May; we now have 13 games available. Sales are up significantly (+15-18%) with this launch.

Updated Jackpot odds from 1/240,000 to 1/320,000 to reach bigger, faster rolling jackpots.

Digital Scorecard

Q4 Revenue of \$14.1M, +\$1M YoY or 7.7%, led by Powerball and Lucky for Life.

22% of total sales; highest share of sales since inception.

OLP Players 346,000, +13,000. Monthly players (average) 95,000.

FY23 Product Plan

Current Game Trends

- Strong growth in high margin Pick 3 and Pick 4 games. These are 60% of our draw game sales, and will be a heavy emphasis going forward.
- Continuing trend toward higher price point games; product mix will align with this.

Industry Trends

- All lotteries are slowing down from the recent unprecedented growth. North Carolina is one of only two states without a decline.

FY23 Scratch Off Initiatives

- Continue to Optimize Price Point Mix
- Scale back \$1-2 games
- Phase out \$25 game, move value proposition to \$30 price point
- Bookend the year with family of games launches

FY23 Draw Game Initiatives

- New Fireball add-on to drive incremental revenue (September)
- Addition of Pick 3 and Pick 4 to Digital Play Platform (February)
- Sustained promotions throughout the year

Price is Right Contract Overview

The introduction of this new game requires Commission approval. This is a scratch-off game with \$28 million in potential revenue. The game has a second chance opportunity to win a trip to Las Vegas (6 total) to play The Price is Right. Launch date is scheduled for October 4, 2022.

Pricing

- Licensing & Marketing Support (2% of sales, up to \$593,280)
- Prizing (\$432,000, paid out of unclaimed prizes)

Commissioner Pamela Whitaker asked whether NCEL anticipates going in this direction (online play incorporating prize trips) in the future. Mr. Spielman responded that Scientific Games tends to offer 1 or 2 of these per year, usually aligned with a popular brand for name recognition (others include Wheel of Fortune and James Bond). The uniqueness of the game design combined with a familiar brand sparks interest in a new group of people beyond our core lottery players.

Commissioner Randy Jones asked whether the liability for travel is undertaken by Scientific Games or NCEL. Mr. Spielman answered that Scientific Games is responsible for all arrangements & travel liability.

Commissioner Long moved that the Commission approve the NCEL staff to negotiate and execute a licensing agreement for the Price is Right game in an amount not to exceed \$1,025,280. No second was required, and the motion passed unanimously.

Commissioner Long commented that, although this is the first time we have experienced negative growth in several years, he feels positively about the number of exciting new initiatives planned and NCEL's long term growth trends.

Brand Management & Communications Update

Terri Rose, Deputy Executive Director of Brand Management & Communications, gave an update to the Commission.

April

- Launched 4 new scratch off games
 - TV & radio on air April 5-24
 - Social media promotion - 1300 people shared stories about winning moments
- April Beneficiary messaging: real NC residents sharing stories about funding school workers, scholarships, building schools, and sponsoring pre-K
 - Digital/Social Media - over 10M impressions
 - New beneficiary brochure online and in store
- Partnerships with Education Focused Groups
 - 2022 Conference on Education Leadership recognized NCEL for our contributions toward school construction funding
- High Jackpot Genie support for high Powerball jackpot + messaging about how tickets are available through online play
- Jackpot Value Pack promotion: 12,000 people bought tickets via promotion

May

- 4 new Fast Play Games introduced, supported by Fast Play Digital & Social Media campaign. We offered a total of 300 coupons for players who responded within 15 minutes. These coupons had a 70% redemption rate.
- 4 new scratch off games, supported by a social media campaign with virtual photo landscape of winners' club encouraging players to search for hidden scratch-offs.
- Marketing Sponsorships
 - Carolina Hurricanes playoffs
 - Nine minor league baseball partnerships
 - NC200 Truck Race on May 27
- Community Events
 - Azalea Festival
 - Dogwood Festival
 - NHRA Four Wide Nationals
 - Coca Cola 600 / NCEL 200 race weekend (\$33,000 worth of games sold during weekend)

June

- 4 new scratch off games supported by TV and interactive social media

FY23 BMC Initiatives

- Maintain Scratch off support with 12 advertised launches
- Continue building Fast Play Awareness by advertising new games
- Increase support of high jackpot messaging
- Support draw game promotions with digital advertising
- Grow online player base and awareness
- Increase consistency of beneficiary messaging
- Evaluate and grow Play Smart responsible gaming program
- Increase social media efforts
- Evaluate digital and over the top video options (including Netflix)
- Build on segmentation learnings
- Collegiate partnerships
- Community Events
- Sports Sponsorships
- Winner Awareness

Sales Update

Terri Avery, Deputy Executive Director of Sales, gave an update to the Commission.

Keno Update

- Social Environments are reopening
- Installed 45 new Game Touch Draw machines
- Sales are up 1.09% or \$806,304 over budget (through May 31)
- Continue to focus on this next year

New Game Launch Penetration

- 98% overall, well above industry average
- Five months of the year were 99%

FY22 Vending Performance

- We have placed intentional focus on vending this year to support short-staffed retailers
- +13.58% on GT-28
- +17\$ on GT-20 (Walmart)
- \$62M increase in FY2022

Finance & Audit Committee Report

FY2023 Budget Plan

Bill Jourdain, Deputy Executive Director of Finance, Administration, and Security, presented the FY2023 Budget Plan to the Commission.

FY 2021 was a record year with a 26% increase in sales. We are starting to see a return to expected sales levels, making this record increase in performance difficult to maintain.

Lottery sales are being challenged by competition from the following:

- Post-COVID options for entertainment dollars
- Fuel and food prices
- Inflation effect on consumer spending habits

Players are migrating to higher priced, higher payout valued games in instant scratch-off portfolio.

We do not anticipate increased participation in multi-state jackpot games. Even with Powerball transitioning to 3x per week, higher margin games will only see increased participation when jackpot levels are greater than \$500M.

Since 2018 we are anticipating a compound annual growth rate (CAGR) of 6.6%.

The budget anticipates average sales per day of \$10.1M.

Proposed Budget Summary

- \$3.69B in revenue
- \$2.76B in expenses, including \$2.43B in prizes, \$254.7M in retailer commissions and incentives, \$76.2M in gaming systems & licenses.
- Administrative expenses of \$93.6M, or 2.54% of sales. Total of 4.6% in administrative spending (which includes gaming systems & licenses) is under the 5% statute-mandated cap.
- Net proceeds to education \$834M (22.6% of sales)
 - Any surpluses over revenue targets are earmarked for need based school construction.

Administrative Expense includes 2.5% in legislated salary increase. Currently there is a proposal from the governor's office to raise this to 5%, which would cost another \$575,000. The state does not appropriate any money to fund this; it has to come out of our revenue.

Administrative spending increases are due to:

- Consumable supplies
- Fuel costs for field staff
- Advertising and marketing (media purchases & production costs, sponsorship relationships)
- Cyber insurance, which has doubled over the past year
- 24/7 Capitol police coverage of Raleigh facility

We usually end up spending about 92% of budgeted administrative expenses, via an ongoing effort to search for cost savings throughout the year. Any excess will go directly to education.

Commissioner Jones thanked Mr. Jourdain & the NCEL finance team for their work on putting together the FY23 budget. He asked Mr. Jourdain if the potential 5% salary increase proposed by the governor would put us over the 5% legislatively mandated administrative expense limit. Mr. Jourdain responded that there is enough wiggle room in the budget to accommodate this increase.

Commissioner Malcolm asked if NCEL is required to comply with salary increases for state employees passed by the General Assembly. Mr. Spangler responded that we are not required by law, but generally we do follow the guidance of state directives.

Commissioner Jason Roth made a motion to approve the FY2023 Budget. No second was required, and the motion passed unanimously.

Financial Update for the 10 months ending in April 2022

- Total assets of \$210M, including \$67M in Cash, \$84M in annuity award investments, accounts receivable of \$33.7M, \$31.9M of which was collected in May
- Total liabilities of \$252M: \$40M in outstanding prize awards, \$84M in annuity prize awards, \$78M due to state for education
- Sales are up 2.9%, 10.2% (or \$297M) over budget.
- Total revenue to date: \$3.22B
- Administration expenses are \$125M, or 3.9% of revenue
- Net revenue to education is 0.1% above last year and 14.5% above budget
- Year to date transfers to the Office of State Budget through April 30: \$754.2M. Balance of lottery reserve fund totaled \$47M.
- More than \$9B has been transferred to the state of North Carolina since inception.

Audit Update

Mike Suggs, Internal Audit Director, presented an update to the Commission

Internal Audit Activity Charter

The Charter has been updated with some additional language clarifying the roles & responsibilities of the Internal Audit Director with respect to their relationship with the Commission. Commissioner Roth moved that the Commission approve the Internal Audit Activity Charter as submitted. No second was required, and the motion passed unanimously.

FY 2023 Risk Assessment and Audit Plan

Mr. Suggs presented the FY2023 Risk Assessment and Audit Plan to the Commission. The most substantive change is moving from a calendar year to fiscal year plan.

13 audits are planned for FY 2023.

Commissioner Roth moved to approve the Risk Assessment and Audit Plan. A second was not required, and the motion passed unanimously.

Audit of IT Production and General Controls

This audit's scope included a review of NCEL's IT general controls related to policies and procedures,

computer operations, information systems, and system development and maintenance controls related to IT and gaming systems. The period covered was January 2020 through March 2022.

The audit opinion was that NCEL's internal controls over IT Production appear to be adequate and have been sufficiently designed to mitigate potential risk.

Audit of Regional Claims Offices

The scope of this audit included conducting a review of claims centers from March 2020 to present, to ensure compliance with policies and procedures, testing the accuracy, timeliness, and reasonableness of transactions, and assessing the safety and security of the regional offices.

The audit opinion was that the internal controls over NCEL's Regional Claims offices appear to be adequate and have been sufficiently designed to mitigate potential risk.

Audit of Customer Services and Public Communications

The scope of this audit was an assessment of the effectiveness and efficiency of the NCEL's customer service and communications to the public, including compliance, operations, coordination, and assurance aspects of the customer service and communications provided to the organization's players and retailers. The period covered was March 2019 through May 2022.

The audit opinion was that NCEL's internal controls over Customer Service and Public Communications appear to be adequate and have been sufficiently designed to mitigate potential risk.

External Security Audit

External auditors have completed the audit and Mr. Suggs is reviewing the report. Results will be presented at the September meeting.

IVR and Related Services Contract

George Walker, Chief Technology Officer, informed the Commissioners that the contract for NCEL's Interactive Voice Response (IVR) system, allowing incoming callers to access prerecorded messages without having to speak with a customer service agent, is expiring. This is a heavily used system, around 200,000 calls per month. We have been evaluating replacements and have identified Cisco Contact Center as the best option. This system uses modern technology that is also lower cost. We hope to have it in place by the beginning of December to ensure a smooth transition. This expense is already included in 2023 budget.

Operations & Personnel Committee Report

Commissioner Whitaker presented several Human Resources items for the Commission's information.

- Executive Director Annual Evaluation is upcoming. Feedback will be gathered from Commissioners & selected staff members and ultimately shared in a one-on-one discussion by Chairperson Adcock with Executive Director Mark Michalko. All information gathered from Commissioners and employees will be kept confidential, including the identity of staff members interviewed. The evaluation will be completed by September 15, 2022.

- Compensation Study: Gallagher Benefit Services, Inc. will conduct a compensation study, beginning July 1, to determine whether our pay rates are appropriate for the market. The study will conclude in March 2023. If pay adjustments are recommended, they will be included in the FY 2024 budget.
- Director of Supplier Diversity & Outreach: This open position will be posted once the job description has been reviewed for updates.

Policy 6.05 - Retailer Dispute Resolution Policy

This policy has recently been edited and reviewed by the Operations and Personnel Committee, who approved the changes and now requests approval by the full Commission. Commissioner Whitaker made a motion to approve this updated policy. No second was required, and the motion passed unanimously, with Commissioner Jones abstaining.

Return to Office

At the June 8 Operations & Personnel Committee meeting, Commissioner Tyson requested statistics on how many of our employees are currently working on-site in NCEL offices. The statistics compiled by NCEL's Human Resources Department found that:

- 50.2% of full-time employees are working on-site or in the field
- 18.3% are working in the office 1-2 days/week
- 8% are working in the office 3-4 days/week
- 23.6% are working remotely full time

NCEL is constantly monitoring the ongoing COVID situation, which seems to be worsening in recent weeks. We have also begun to experience turnover by some office-based employees who are seeking full time remote work. We are placing priority both on safety and best practices for retaining our employees.

Commissioner Whitaker stated that throughout the pandemic NCEL has done a remarkable job of meeting our customers' needs while also ensuring employees remain safe. Our employees have demonstrated that they continue to prioritize customer needs working remotely; therefore, we are willing to adapt to a hybrid schedule that meets business needs while also attracting and maintaining staff.

Commissioner Tyson requested that the above statistics be sent in writing to the Commissioners.

Demographics Report

NCEL's turnover rate is 2.62%, which is outstanding compared with the private sector average of 12-20%.

Executive Directors Report

Mr. Michalko presented an update to the Commission.

Contracts Over \$90,000

The usual report has been distributed to the Commissioners; there were no questions.

HUB Report

A high-level summary has provided to Commissioners this quarter. When the Director of Supplier Diversity & Outreach position is filled we will be able to provide a more robust and detailed report.

Beneficiary Update

Van Denton, Director of Communication, presented an update to the Commission regarding \$395M in NCEL proceeds which funded new school construction this year.

- This is the largest amount of state funds for school construction since 1996.
- The grants fund 42 projects in 28 counties, mainly to smaller, rural counties that lack the resources to raise the amount of money needed to build new schools.
- A separate fund is also shared between all 100 counties, which means the larger counties are getting some allocation as well.
- Needs-Based Public School Capital Fund will have anticipated funding of \$153M for FY22-23.
- Mr. Denton & his team have visited 3 sites (NW Harnett Elementary School, Granite Falls Middle School [Caldwell County], and Ahoskie Elementary School in Hertford County).

Legislative Update

Hayden Bauguess, Director of Legislative Affairs, presented an update to the Commission.

- The General Assembly is in session now, with plans to adjourn July 1.
- Budget expected next week.
- Sports Betting: The bill passed by the Senate is in the House now. It is not calendared at this time but we expect it to be heard soon. A trailer bill with some technical corrections is still in the drafting phase. NCEL participated in a meeting with legislative staff to go through needed changes to make our administration of a sports betting program more efficient and effective, and we were pleased with the outcome.

Other Business

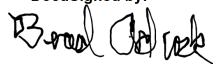
Chairperson Adcock acknowledged that the Commission has 2 members with terms expiring in August.

Chairperson Adcock recognized Commissioner Jones, whose 5-year term ends next month, and thanked him for his service. Commissioner Jones thanked Chairperson Adcock and stated that he has enjoyed his time on the Commission, has learned a great deal, and greatly appreciates the NCEL staff & other Commissioners. Commissioner Jones expects that the Speaker will reappoint him for another 5-year term and looks forward to a continued relationship.

Commissioner Jody Tyson, the NCEL Commission's longest-serving member, will be leaving next month. He is the only Commissioner in NCEL history to serve two full five-year terms. During Commissioner Tyson's tenure, the NCEL has become one of the most successful lotteries in the country: sales have increased from \$1.59B to \$3.8B over this period, and the proceeds to education have more than

doubled. Commissioner Tyson thanked Chairperson Adcock for the recognition, and stated that he has been pleased to be part of the lottery's success, including making the motion to move forward with Keno. He congratulated the staff on their great work and the positive path ahead.

With no other business to discuss, a motion was made by Commissioner Tyson to adjourn. Seconded by Commissioner Jones and passed unanimously. The meeting adjourned at 12:19pm.

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Chair Brad Adcock

10/4/2022

Date