

VIRGINIA LOTTERY

Board Meeting
September 15, 2020

As a result of the state of emergency declared in the Commonwealth of Virginia by order of the governor on March 12, 2020, the Virginia Lottery Board met on September 15, 2020, at 9:30 a.m. by electronic-communication means pursuant to Executive Amendment 28 to HB29 (2020). A video recording of the meeting can be viewed here: <https://youtu.be/ZNiGIhAiKt4>

PARTICIPATING MEMBERS:

All Board members participated through electronic-communication means in separate locations.

Ferhan Hamid, Chairman
Cynthia Lawrence, Vice Chairman
Scott Price
Chris Tsui

PARTICIPATING STAFF: The following Lottery staff participated through electronic-communication means in separate locations.

Kevin Hall, Executive Director
Deborah Courtney, Director of Finance
Kelly Gee, Manager of Government Relations
Terri Rose, Director of Marketing
Gina Smith, Deputy Director of Gaming Compliance
Rob Wesley, Director of Digital
Jennifer Mullen, Public Affairs and Community Relations
Manager

The following Lottery staff monitored the meeting through electronic-communication means in separate locations.

Frank Wagner, Deputy Director
Amy Dilworth, General Counsel
Bob Fontaine, Deputy General Counsel - Gaming Compliance
Ted Maxwell, Director of Information Technology Services
Tony Russell, Director of Administration
Tom Sawyer, Director of Sales
Beth Smith, Director of Audit and Security
Jo Murphy, Executive Assistant

As required, the meeting was available to the public via livestream on Virginia Regulatory Town Hall.

Mr. Hamid, chairman, presided, and Jo Murphy was the recording secretary.

CALL TO ORDER

Mr. Hamid called the meeting to order and noted that a quorum was present.

MINUTES OF LAST MEETING

On motion duly made by Mr. Tsui and seconded by Ms. Lawrence, the minutes from the regular meeting held on July 15, 2020, were approved as distributed.

DIRECTOR'S REPORT

Mr. Hall provided an update on the COVID-19 impact on the agency's workforce. He said there has been only a handful of positive COVID-19 exposures among members of the workforce, and it appears none of these exposures occurred in a work-related setting. We are grateful that we have seen very few COVID-19 related illnesses among our employees, and individuals who have displayed COVID-19 symptoms either are recovering at home or have now fully recovered.

Mr. Hall said that our 300 employees have successfully worked from home since mid-March. The Sales team has shifted from 100% telework to one or two monthly store visits per retailer. At headquarters and at our CSCs, we have implemented CDC and state health and safety guidelines to minimize the risk of exposure for staff and customers. The agency will continue to work from home at least through the end of September. At that time, we will make decisions about October and beyond.

Mr. Hall said that since the July meeting the Auditor of Public Accounts (APA) has certified the Lottery's FY20 financial results. The Lottery recorded \$2.1 billion in sales. More than 60% of sales revenue was returned to customers in the form of prizes. Our 5,400 retail partners earned a combined \$120 million in commissions and other incentives. About \$14 million in unclaimed Lottery prize money was deposited in the Literary Fund, which makes low-interest loans to localities for school construction, renovations and technology upgrades. Mr. Hall reported that FY20 was the Lottery's second-best year in sales, and the \$595 million FY20 profits helped the Lottery transfer the second largest fiscal year total amount to the Lottery Proceeds Fund for K-12 public schools.

Mr. Hall said that starting on July 1 we catapulted out of the gate with the strongest iLottery launch of any state in the country. We have now seen online lottery play from close to 60,000 registered customers. At the same time, sales at retail continue to exceed last year's sales and this year's goals. We are continuing to create opportunities to tie digital and traditional Lottery play together in further support of our brick-and-mortar retail partners.

DIRECTOR'S REPORT (Continued)

Mr. Hall said we soft-launched Keno in early August, and it took only five weeks to reach \$1 million in weekly sales. We are still early in the deployment of Keno into the market, so we expect this game will continue to provide significant growth potential moving forward.

Mr. Hall shared the overall trend line we have seen over the course of this extraordinary calendar year. In January and February, sales were tracking slightly below last year's performance. There was a sharp impact from the COVID-19 lockdown beginning in March and into the first half of April. In the second half of April and continuing into May and June, there was a noticeable sales rebound. Other lotteries across the country saw the same rebound. During this period, retailers had modified their stores to promote a safer environment, and retail restrictions were gradually being relaxed. Mr. Hall also noted that the Lottery literally was the only game in town during this period. The gray machines were unplugged; Colonial Downs and Rosie's were closed, as were casinos in adjoining states. In July, the rebound at retail continued; plus, we had the strong launch of the new iLottery online sales channel. In August, we saw more strength at retail, continued upside from iLottery and the addition of the soft launch of Keno. Mr. Hall said monthly sales data fluctuates from month to month. Looking over a longer-term evens out the swings and provides a better sense of overall performance. He said we are off to a strong start in FY21. We are seeing good work and solid performance from the entire team in these challenging circumstances. We continue to expand popular self-serve vending opportunities at retail. The Scratcher portfolio is ahead of last year and ahead of goal for this fiscal year. The daily-draw games are also ahead of FY20 and ahead of goal. We are still waiting for Powerball and Mega Millions to roll to jackpot levels that generate excitement among occasional players.

Mr. Hall said casinos have partially reopened across the country in recent weeks. In Virginia, Colonial Downs and Rosie's have reopened with health and safety restrictions. At Ms. Lawrence's request, Mr. Hall asked Manager of Government Relations Kelly Gee to provide an overview of the current state of play in the gaming industry, both nationally and in Virginia.

Ms. Gee provided an overview of how the gaming industry is performing. COVID-19 certainly had an impact on operations, but movement has started again in the gaming field. In Virginia, Rosie's closed March 15 and remained closed through June 30. All four of its locations reopened July 1 with some significant health safety changes. Face coverings and temperature screenings are required upon entry, crowd shields were installed, and terminals were rearranged to provide adequate physical distancing.

Ms. Gee provided data showing the combined handle, or all bets made, for all four Rosie's locations. February was its last full month of operations, and, in the first month since reopening, sales were at about 84% of what they were pre-COVID-19. In August, Colonial Downs announced the cancellation of its live races for 2020. Virginia has also experienced the first two full months of regulated skill-machine activity. ABC's first revenue reports have not been published yet, but press reports said that just one provider of the games, Queen of Virginia, turned over \$6.8 million to the Virginia treasury in July, which was the first month of regulated

DIRECTOR'S REPORT (Continued)

operations. Of that amount, \$5.75 million went to the COVID-19 Relief Fund the governor established, and around \$800,000 went to localities that host Queen of Virginia games. Press reports said that Queen of Virginia has over 5,700 skill games in operation across Virginia.

Ms. Gee said the pandemic caused all 989 commercial and tribal casinos in the U.S. to close. The American Gaming Association reports that as of September 14, 896 of them, or around 90%, have reopened. At a recent LaFleur's conference, the Michigan Lottery reported a poll that showed 58% of respondents would feel comfortable visiting a casino either immediately or within the first month of reopening, 24% said it would take a few months, and 18% said they would not visit a casino until there is a COVID-19 vaccine. Maryland, where casinos are operating at 50% capacity, still generated almost \$140 million in gaming revenue during July, which was the first full month of operation after being closed for three months. That figure is only a 6.3% decrease from last year's revenue. Three of the six Maryland casinos saw increases from July 2019 gaming revenue. Layoffs, entertainment cancellations and property closures are common right now. It was announced in August that MGM National Harbor is laying off 779 employees as part of a larger workforce reduction. MGM International is instituting company-wide layoffs that are estimated to reach 18,000 previously furloughed employees or about 25% of MGM's pre-pandemic workforce.

Ms. Gee said that, within the last year, nine new states began offering sports betting, which brings the total to 19 live sports betting jurisdictions. From March through June, the near complete closure of physical sportsbooks and limited sporting events resulted in the first negative year-over-year growth the industry has seen since the Supreme Court PASPA ruling. However, by July, betting on what some call "second tier" sports such as NASCAR and UFC fighting saw more wagers than ever before. Currently, baseball, basketball and hockey are back and generating significant sports betting revenue. If states expect to see continued revenue growth, these professional sports are going to have to make up for the cancellation of many college football seasons. Vegas experts expect to see a 25% decline in sports betting revenue this fall because of fewer college football games.

Mr. Hall said that since spring our team has worked hard to turn about nine pages of broad legislative language into about 70 pages of very specific sports betting regulations. He acknowledged the hard work of Deputy Director of Gaming Compliance Gina Smith, General Counsel Amy Dilworth and Deputy General Counsel Bob Fontaine.

Mr. Hall said the entire package of draft regulations has been available for public comment from citizens and stakeholders for the last 30 days. Significant parts of the draft regulations have been available for 60 days. The public comment period closed September 9. Mr. Hall said the team has been poring over several hundred comments and suggestions submitted by about 50 individuals and organizations. Feedback and suggestions were received from citizens, many of the largest sports betting platforms and casino operators, and most of the major professional sports leagues including the NFL, MLB, NBA and PGA.

DIRECTOR'S REPORT (Continued)

Mr. Hall said creating a responsible regulatory structure for sports betting on the aggressive timeline mandated by the legislature consumed a lot of bandwidth over the summer, and today's Board action represents a significant step forward.

Mr. Hall pointed out that it is not the only accomplishment in the expanded gaming space. He noted that we continue to build the structure of our new Gaming Compliance division and have recruited and hired key talent for several important regulatory roles. It also is significant that we have identified existing space within our headquarters building in Richmond to accommodate the team responsible for regulating sports betting and casino gaming. Mr. Hall said we are pleased we will be able to keep the entire enterprise in one location.

Mr. Hall said we have hired experienced consultants to help with the initial rounds of criminal background checks and suitability investigations. A key part of the contract includes training our own staff, so we can take on more of these responsibilities ourselves as we build the enterprise. We also signed a contract to piggyback on a custom online licensing system built by the Maryland Lottery. The online portal will be used to receive and process license applications for casino and sportsbook operators, including their principal owners, key managers, suppliers and vendors. Ultimately, this online licensing system will be expanded to handle applications from the thousands of individuals required to undergo a background check before receiving a gaming license to work at a Virginia casino.

In summary, Mr. Hall said we are successfully meeting the aggressive legislative deadlines as the lead regulator for sports betting and are now in a position to move ahead on regulations for casino gaming. At the same time, we are maintaining focus on the core Lottery business, which continues to perform well. Mr. Hall said we are especially pleased with the strong initial performance of new Lottery products such as Keno, and we have seen extraordinary early success with our new online platform. He said that after more than six months into a global pandemic and the switch to remote work, the Lottery workforce continues to amaze with its commitment and creativity. To our knowledge, everyone remains safe and healthy.

Ms. Lawrence asked how many additional employees are anticipated for the new Gaming Compliance division. Mr. Hall said the fiscal impact statement that we produced with the Department of Planning and Budget was based heavily on the JLARC study. We are looking at 100 additional people and not all would be based in Richmond.

FINANCIAL REPORT

Ms. Courtney provided preliminary results through August 31, 2020.

Total sales were \$460.3 million, \$119.2 million (35.0%) more than last year. Scratcher sales were \$203.8 million, \$17.0 million (9.1%) more than last year. Print 'n Play sales were \$12.1 million, \$1.3 million (11.8%) more than last year. Daily games sales were \$136.0 million, \$27.2

FINANCIAL REPORT (Continued)

million (25.0%) more than last year. Jackpot games sales were \$32.2 million, \$2.1 million (6.1%) less than last year. The national games did not experience good jackpot luck last year and have not so far this year. Cash4Life® is now comparing daily drawings to the same frequency as last year, and there continues to be good growth in that product. It also is available on the iLottery platform and is helping that game to continue to grow as well. Ms. Courtney said two-thirds of the year-over-year sales growth is coming from the addition of two new products - Keno and iLottery instants. Keno sales were \$3.7 million. Sales for instants on the iLottery platform were \$72.5 million.

Ms. Courtney reviewed the FY21 sales versus prior years. She also reviewed expense rates versus the prior year. Prize expense was 64.6%, which was 5.4% more than last year (59.2%) and is a significant growth. Daily games continue to pay out prizes lower than statistically expected. With more drawings and over more time, the results end up evening out to about 50%, but, in the short term, the highs and lows can have a significant impact on the rate. As we experience sales increases and the higher prize payouts in the two new categories (Keno and iLottery instants) it will make an overall prize rate in the 65-70% range the new normal. Next year, the change will not be as noticeable. Retailer compensation was 5.5%, which was the same as last year and does not include iLottery instants. Operating expenses were 4.2%, which was 1.6% less than last year (5.8%). When sales are high, it drives the operating expense rate down.

Ms. Courtney said year-to-date profits are \$122.1 million compared to \$100.9 million last year. This is strong early performance; most of the increase is coming from sales. The General Assembly and the administration are looking at the budget, among other things, during the current special session. The budget reforecast process only applies to the general fund and does not include a reforecast of Lottery sales and profits. Ms. Courtney said we have been in close contact with the legislative money committees and the administration about how sales and profits are trending. The estimate from the last session and in the FY21 budget is aggressive because it did not consider the change in the skill machines position. She said we are advising that we do not think the current number is what our forecast will be, but it is simply a placeholder in the budget. As the governor reforecasts in the fall, we will be a part of that process. We also will consider the residual profit transfer from the APA certifying our FY20 profits. All of that will be a part of the normal process of the revenue reforecast that we will bring back to the Board in early November.

Mr. Hamid asked why the payout rate for iLottery is high and whether that is normal. Ms. Courtney said iLottery has a higher payout rate, and that is standard in the industry.

Mr. Hamid asked if we expect the reduction in the administrative rate due to iLottery to become significant over time. Ms. Courtney said the percentage will decline because we are dividing by a larger sales amount, but she does not expect the total dollars to decline.

FINANCIAL REPORT (Continued)

Mr. Hamid asked how much of the increased sales can be attributed to the fact that casinos were closed for a while and are now open in a limited capacity. Ms. Courtney said it is one of the contributing factors. She said we will continue to monitor sales at Rosie's and casinos as those businesses move toward operating at full capacity. We also will review data on skill machines as it becomes available.

BOARD ISSUES

Audit Committee Report

Mr. Tsui reported that the Audit Committee met at 8:45 a.m. Mr. Tsui, Ms. Lawrence, Mr. Price, Mr. Hall, Ms. Smith and Ms. Whitney attended the meeting.

The Audit Committee approved the audit plan for FY21 that includes working on audits with a continued emphasis on information security.

Internal Audit follows up semi-annually to determine the status of management actions to address audit reports. On June 30, 2020, there were no open findings from audit reports issued prior to July 1, 2020.

Mr. Tsui reported that Ms. Smith confirmed the organizational independence of the department as required by the International Standards for the Professional Practice of Internal Auditing.

The Audit Committee Charter was reviewed by the committee. No changes were required. The committee confirmed that all responsibilities outlined in the charter have been carried out.

The Internal Audit Charter was reviewed by the committee. No changes were required.

The committee plans to hold its next scheduled meeting in early 2021 to review results of the APA FY20 audit and progress on achieving the FY21 audit plan.

Marketing Promotion

Ms. Rose presented a player promotion designed to build on the success of iLottery and promote playing both a Scratcher and an online instant game. She said the Holiday Gold Scratcher launches in November, and there is an offer for iLottery on the back of the ticket. When players take advantage of the offer online, they will receive an email from the Lottery with a coupon to be used at retail. The promotion will start in November, one of the highest-selling Holiday Scratcher months, and will present a huge acquisition opportunity for iLottery. She said we would like to repeat the promotion in February with the Wheel of Fortune® Scratcher. Holiday

BOARD ISSUES (Continued)

Gold and Wheel of Fortune® also are offered as separate instant games on the iLottery platform. Ms. Rose said they will use the results to identify games for future months.

Ms. Rose said they looked at models from other states, specifically Michigan and Pennsylvania, who have had iLottery for some time. Marketing also is working closely with the Digital and Sales teams, and they are excited to see the results of the first iLottery promotion.

On motion duly made by Mr. Tsui and seconded by Mr. Price, the Board approved Marketing Promotion #OC91520 as presented.

Sports Betting Regulations

Ms. Smith provided an overview of the regulations by section and highlighted the material changes that were made as a result of the public comments. When the regulations are approved, the stakeholders will be able to see all the revisions made as a result of their comments. Public comment closed on September 9, and all input received from the stakeholders was appreciated. The team reviewed every comment posted on the Virginia Regulatory Town Hall site.

Ms. Smith provided an overview of the following:

- Self Exclusion (11 VAC 5-60)
- Definitions (11 VAC 5-70-10)
- Application Process (11 VAC 5-70-20)
- Consent for Investigations (11 VAC 5-70-30)
- Waiver of Requirement (11 VAC 5-70-40)
- Sports Betting Permit Applications (11 VAC 5-70-50)
- Principal Applications (11 VAC 5-70-60)
- Supplier Applications (11 VAC 5-70-70)
- Vendor Registration (11 VAC 5-70-80)
- Employee Application (11 VAC 5-70-90)
- Bonds (11 VAC 5-70-100)
- Denial of Permit, License or Registration (11 VAC 5-70-110)
- Sanctions (11 VAC 5-70-120)
- Identification Cards (11 VAC 5-70-130). This section was deleted in its entirety based on public comment.
- Reserve and Insurance Requirements (11 VAC 5-70-140)
- Liability Pooling (11 VAC 5-70-150)
- Audit, Financial, Record-keeping and Banking (11 VAC 5-70-160)
- Permissible Wagers (11 VAC 5-70-170)
- Requests from Sports Governing Bodies (11 VAC 5-70-180)

BOARD ISSUES (Continued)

Use of Official League Data (11 VAC 5-70-190)
System Integrity and Security Assessment (11 VAC 5-70-200)
Minors and Prohibited Players (11 VAC 5-70-210)
Integrity Monitoring (11 VAC 5-70-220)
Investigations; Reporting (11 VAC 5-70-230)
Advertising and Marketing (11 VAC 5-70-240)
Reporting Requirements (11 VAC 5-70-250)
House Rules (11 VAC 5-70-260)
Sports Betting Platform Requirements (11 VAC 5-70-270)
Geolocation Requirements (11 VAC 5-70-280)
Player Accounts (11 VAC 5-70-290)
Internal Controls (11 VAC 5-70-300)
Information Security System (11 VAC 5-70-310). This is a newly created section based on public comments.
Sports Betting Consumer Program (11 VAC 5-80-10-160)

Ms. Lawrence asked if there is sufficient staff in place to help applicants navigate the complicated process. Ms. Smith said that in the coming days the website will be expanded to include information on how potential applicants can contact us. Meetings will be set up with the individual applicants to discuss their structure in order to start with a full understanding of expectations. The online licensing-application process will include instructions and user manuals. We also intend to walk applicants through the system. She said we will give them ample time to study the documents. When the system is active, they should be well-prepared to proceed.

Mr. Hamid said that, after reviewing the regulations, it appears to him that a good balance was struck between regulating and allowing the business to operate. He congratulated the team on a job well done. While reviewing the public comments, he read objections to a restriction of betting on the Olympics but noticed that the restriction remains in the regulations. He asked Ms. Smith to expand on the Lottery's stance on betting on the Olympics. Ms. Smith said that, after reviewing this topic in great detail, we did not adopt any of the recommended changes related to the Olympics. We reviewed the definitions included in the statute as they related to college sports, youth sports and professional sports. Betting on youth sports is prohibited. Many Olympic events could include minors, and we were concerned about going outside of the boundaries of the statute. Mr. Hamid asked if this would be revisited in the future. Ms. Smith said the Olympics do not take place until July, so there is an opportunity to make a legislative change.

Mr. Price asked when we will start accepting applications and begin awarding licenses; he also asked when Virginians will be able to legally bet on sports. Ms. Smith said that after the regulations are approved by the Board they will be posted on the Lottery's website and will become effective in mid-October. Once they are effective, we will begin accepting applications.

BOARD ISSUES (Continued)

When a completed application and the requested documents are received, the investigation will take place. We will issue a decision within 90 days of receiving a completed application. If all goes as planned, sports betting could begin in January 2021.

Mr. Hamid asked about public comments regarding fast withdrawal of money from bank accounts. Ms. Smith said no changes were made because it was a standard practice.

Mr. Hamid asked how much we relied on existing regulations from other states. Ms. Smith said we looked at many states that have sports betting and adopted what we thought was appropriate for Virginia. Early in the process, we solicited input from stakeholders as to what they wanted to see in our regulations. Their input was incorporated into the first draft. She said we relied on best practices and gave everyone ample opportunity to provide input.

Ms. Lawrence asked if casinos also offer dual sports betting online. Ms. Smith said they can apply.

Mr. Hamid thanked Ms. Smith for her hard work.

Mr. Tsui moved for the approval as presented of the sports betting regulations drafted to implement the provisions of Virginia Code section 58.1-4015.1 (Voluntary Exclusion Program) and the provisions of Article 2 of Chapter 40 of the *Code of Virginia* (Sports Betting), as enacted by the Virginia General Assembly in its 2020 Regular Session. The motion was seconded by Ms. Lawrence.

Mr. Hamid stated that the motion passes. In accordance with Enactment 2 of the Virginia Sports Betting Law, which took effect July 1, 2020, the regulations are exempt from the provisions of the Virginia Administrative Process Act, except that, as set forth in Enactment 2, the Department has made available the draft regulations for a public comment period, which opened July 15, 2020 and closed September 9, 2020. The Board hereby promulgates the regulations to be published as Chapters 60, 70 and 80, inclusive, of Title 11, Agency 5 of the Virginia Administrative Code, including the “Virginia Sports Bettors’ Bill of Rights.” The Department is hereby directed to submit the foregoing regulations, as approved by the Board, to the Registrar of the Commonwealth of Virginia to be duly published in the Virginia Register of Regulations.

Link to the approved sports betting regulations:

<http://register.dls.virginia.gov/details.aspx?id=9209>

OTHER BUSINESS

The next Lottery Board meeting is scheduled to take place on November 4, 2020.

BOARD MEMBERS' OPEN DISCUSSION

None.

CLOSED MEETING

Ms. Lawrence made the following motion, which was seconded by Mr. Price:

In accordance with the provisions of Section 2.2-3712 of the *Code of Virginia*, I move that the Board convene a closed meeting for the discussion, consideration or review of:

- Pursuant to subdivision A 17 of section 2.2-3711, matters relating to specific lottery game design, prize structure and odds of winning; and matters related to proprietary lottery game information excluded from disclosure under subdivision 11 of § 2.2-3705.7

RECONVENED MEETING

Following its closed meeting, the Board reconvened in open session. Mr. Price read the following certification for the closed meeting:

WHEREAS, the Virginia Lottery Board has convened a closed meeting on this date pursuant to an affirmative recorded vote and in accordance with the provisions of The Virginia Freedom of Information Act; and

WHEREAS, § 2.2-3712 of the *Code of Virginia* requires a certification by this Board that such closed meeting was conducted in conformity with Virginia law and the motion by which the closed meeting was convened;

NOW, THEREFORE, BE IT RESOLVED that the Virginia Lottery Board certifies that, to the best of each member's knowledge, (i) only public business matters lawfully exempted from open meeting requirements by Virginia law were discussed in the closed meeting to which this certification resolution applies, and (ii) only such public business matters as were identified in the motion convening the closed meeting were heard, discussed, or considered by the Board.

By roll call, all members voted in the affirmative that the certification was accurate as read.

On motion duly made by Ms. Lawrence and seconded by Mr. Price, the Board approved, as presented in the closed meeting, the prize structures for Scratcher Games 2073 and 2075 through 2084 including the 0.5% prize-structure variance.

RECONVENED MEETING (Continued)

On motion duly made by Ms. Lawrence and seconded by Mr. Price, the Board approved, as presented in the closed meeting, the prize structures for Instant Games 265, 272, 1128, 1132 and 1158.

Ms. Lawrence asked for an update on the teacher-recognition initiative. Mr. Hall said it has been a difficult back-to-school period, which made it hard for us to do a typical launch. Ms. Mullen said we are working in partnership with a popular show in the Northern Virginia area, “The Tommy + Kelly Show.” We partnered with them last year, and we are doing something similar this year. Accommodations will be made for schools that are meeting virtually. We are working on an opportunity for our employees to create virtual thank-you notes that will be used on our social platforms to thank teachers. The Thank a Teacher Art Contest launches in January. We are creatively thinking of ways to continue to share our mission and support educators by honoring and recognizing them.

ADJOURNMENT

There being no further business to come before the Board, the chairman declared the meeting adjourned.

Kevin Hall, Secretary

Ferhan Hamid, Chairman