

EMBRACING AN UNCERTAIN FUTURE WITH A FOCUS ON THE OPPORTUNITIES FOR POSITIVE CHANGE

Mary Harville, President & CEO, Kentucky Lottery



PGRI Introduction: While Mary Harville was appointed to the position of CEO in September, she has been a member of the senior management team since joining the Kentucky Lottery as senior vice president, general counsel and corporate secretary sixteen years ago. This inter-disciplinary team collaborated to produce average annual increases in sales of 4.7% over the last fifteen years, 5.6% over the last ten years, and 6.8% over the last five years. And now, not that anyone was entirely prepared for the unique challenges of the current times, the Kentucky Lottery has adapted and is set on a course that continues to meet the expectations of players, retailers, and Lottery stakeholders alike.

Paul Jason: The Kentucky Lottery has been so successful over a long period of time. Are you optimistic about the headroom to sustain your annual growth rate of over 6%?

Mary Harville: Yes. Like many lotteries, at the end of March 2020, our YoY sales were more or less flat. But fourth quarter of the last fiscal year (ending June 30, 2020) was the Kentucky Lottery's best quarter ever. And now, for the first five months of the current fiscal year (i.e., July 1 to November 30), total sales were 579.6 million or \$140.2 million more than last year. That is a 31.9% increase over the same period of FY 2020. Internet sales for FY 2020 increased by 68% over FY 2019. And iLottery sales in Q1 of FY 2021 are up 218.9% over Q1 of FY 2020. While we probably will not end FY 2021 with a 31.9% YoY increase in annual sales, I am confident that our positive momentum will continue into 2021 and beyond. Our stakeholders depend on it.

Wow. Instant scratch-offs must be doing

well along with iLottery during this period of social distancing. But clearly your land-based retailer partners are also doing well and your multichannel approach has proven out for everyone.

M. Harville: Many lotteries did well over the last nine months for a variety of reasons. Not only did racetracks and casinos close down for a while (though Kentucky does not have casinos, they are right across our border), many other forms of recreation and social entertainment like movies and restaurants were closed and even continue to be restricted. Lottery continued to be a viable outlet for entertainment throughout this entire time. Most state governors deemed retailers and grocery stores to be "essential" businesses that were allowed to stay open. Lottery continued to serve existing players, but also attracted new players and increased player-ship from casual and lapsed players. But there is more to the story of why lotteries performed well during this time of severe disruption.



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Like my colleagues all across the country, we leapt into action at the first signs of disruption in the middle of March. Our LSR's (Lottery Service Representatives) were pulled out of the field, but from the start, they determined how to adapt to these unusual circumstances. They have great sales automation tools on their iPads, utilized them effectively, and figured out how to accomplish their job from home and on the phone. When they have been allowed back in the field, it has been under very restrictive conditions. I joined our LSR's to visit retailers and see how the face of Lottery to the customer was holding up. Of course, we were all masked up and followed all our social distancing guidelines. I was very impressed when I saw how our sales force had adjusted their methods to serve the retailers while minimizing in-person interaction. The productivity of the time spent in the store with store managers and staff was fine-tuned to the minute.

Our sales force recognized the critical need for inventory to keep the stores stocked with product and meet an increased demand. I

am so proud of our team for their vision, astute judgment, and execution as they made sure our players always could continue to play the games they love. And our retailers deserve credit for accommodating the need to do things differently and enable our team to apply creative solutions for keeping the dispensers and ticket vending machines stocked with product. It is amazing and wonderful to see how well our retailers and LSR's have worked together to serve the players in spite of not being able to meet face-to-face in the stores for large parts of the last nine months. And when LSR's have been allowed to be in the field, it is only for a maximum of four hours a day, and each store visit must be completed within ten minutes. That can be very difficult when an LSR may have to wait ten minutes to even see the store manager! It takes years to build this kind of trusting relationship between the LSR's and the retailers, and I so appreciate all their efforts and flexibility.

The sales force has been tremendous, but

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our entire organization deserves credit for making everything work so well. The LSR's depend on support from the entire Kentucky Lottery staff and from our commercial partners like IGT and Scientific Games who kept us flush with instant scratch-off games during a time of unanticipated spikes in demand and severe disruption of supply chains.

The pandemic represented a whole new set of unanticipated obstacles to overcome. The leadership of the KLC, and all state lotteries, faced this adversity with ingenuity and the willingness and ability to pivot to make sure we continued to meet our financial obliga-

tions while staying consistent with the values of dedicated public servants. And now we are strategically mapping the pathway forward to ensure a bright future for the good causes that depend on lottery funding and for all lottery stakeholders.

It seems like adversity brought out the best in everybody. Everybody got their creativity and ingenuity engines going and probably invented solutions that will continue to enhance performance long after the pandemic is over?

M. Harville: Absolutely yes. In a way, the pandemic gave us permission to be more decisive and action oriented. The urgency of the situation left no time to over-analyze and conduct ongoing research and discussion before taking action. We threw out our SWOT (Strengths, Weaknesses, Opportunities, Threats) analyses that had been done in December of 2019. Of course, COVID 19 had changed many things, including many of the assumptions of a pre-COVID SWOT. But, as Dwight Eisenhower said, "Plans may

be worthless, but planning is everything." We set about planning for a whole new world. While we had to re-think everything, the trends were not altered lock-stock-and-barrel. Many of the trends identified in our original SWOT analysis were just accelerated by COVID. For instance, cashless functionality in 1,470 ticket vending machines (TVM's) was included in our last contract extension with IGT, even though we did not know a pandemic was coming. Now we see even more consumer demand for cashless purchasing, and we are making the implementation of cashless functionality a priority. We hope to have that completed by the end of the FY 2021 (June 30). We

also received 575 new Gemini Touch 28s (TVM's) under the contract extension, and we were concerned that may be too many. That is no longer a concern. Thankfully, these initiatives were already in place prior to COVID. The pandemic just helped us identify our priorities.

Likewise, new shopping behaviors like BOPUS (Buy Online, Pick Up in Store) began before the pandemic but are gaining momentum much faster than they would have without the impact of social distancing on in-store shopping. Like other lotteries, we are actively looking for ways to loop lottery into the trend of BOPUS.

And even more relevant is iLottery. We had not exactly put iLottery on the front-burner until we saw that the pandemic would cause many consumers to need an alternative to going into the stores to play the lottery or to leaving their homes for other forms of gaming or entertainment. It became very important to ensure that all iLottery functionality was 100% operational and ready for a significant increase in volume and new players. And we were ready, but now we've got to be certain that we keep that momentum and keep those new players. We negotiated the extension of our iLottery contract with IGT during the pandemic, and you can bet that this extension included significant enhancements that will keep the Kentucky Lottery ahead of the curve and exceeding player expectations, including the expectations of our new players. We'll be able to offer more games, include more third-party content, and offer targeted promotions. We will also increase the budget for advertising the digital platform.

What do you do to encourage your team to embrace the opportunities embedded in times of uncertainty like this?

M. Harville: I would point out that the lottery sector has been very fortunate. We have not been beset with the kind of intractable obstacles facing some industries, like airlines and restaurants and many others. We should all be grateful for that good fortune and appreciate the hardship that others are facing through no fault of their own.

Our senior management team is seasoned, experienced, and effective at operating the lottery and leading through difficult situations. One of the things that we have done when dealing with issues, even more than before the pandemic, is to re-frame the issues,

re-visit assumptions, re-define objectives, and organize inter-departmental teams to re-imagine solutions. For example, instead of calling the task force a “COVID crisis management task force”, our V.P. of Marketing, Edie Frakes, named it “Gone Viral” to help us all get into the spirit of forward and positive momentum, rather than just dealing with a problem. Our V.P. of Finance, Rick Kelley, heads up this group and is fondly called Captain COVID. Rick and others like Rick are excited to be involved in areas somewhat outside their primary skill set. They embrace the opportunity to interface with leaders whose vocational discipline and perspective is different from theirs, to learn new things from them and from this process, and to work collaboratively to create new solutions and strategies. I feel that everyone on our team is discovering skills they did not know they had and is excited about the impact they are having on the ongoing success of the enterprise. Heavy reliance on inter-departmental task forces is definitely something we will continue into the post-COVID era.

I should also point out that Marty Gibbs was the interim CEO through the initial months of the pandemic, assuming that role the second week of March. I was not appointed CEO until September. So, much of our pandemic response was undertaken by our senior team, under Marty’s leadership. This team has been very effective at sorting out the problems and obstacles, quickly addressing the short-term needs in a crisis and clarifying action-plans, as well as setting the stage for longer-term goals.

Is it a priority to build out the cross-channel promotional infrastructure that drives online players to retail and vice-versa?

M. Harville: I would not describe it that way. At least at present, our priority is to give our players what they want, where they want it. We are extremely focused on modernizing at retail and truly optimizing the in-store player experience, particularly with TVMs and cashless functionality. We are doing everything we can to optimize the iLottery player experience too. And we will have

cross-promotions that incent the players to interact with the Kentucky Lottery on all channels. But we do not presume to drive the players to play in any particular way, or on any particular channel, other than how and where they want to play. We simply want to give the consumer what they want, whenever and however and wherever they want it. The pandemic has shown us that all boats rise with the tide. Retailers and iLottery have both done well and that is because we focus on the customer, the lottery player, and not so much on achieving a pre-determined mix of channels or products.

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I Lottery has been successful, no doubt. But we remain committed to the success of our retailers. Many of our core players love playing at retail and we want these players to continue to feel that way, so we will always have a fabulous portfolio of lottery games that are only available at retail, and this includes our popular Fast Play games, introduced in 2019, and our new Kentucky Jackpot family of scratch off games, which offer a unique second chance promotion.

The pandemic seems to have illuminated the fact that the consumer is more able and willing to migrate to new and different game categories. Is that a trend that will accelerate and, if so, what does it mean for traditional lottery?

M. Harville: Yes, for sure, this trend will continue. It started several years ago. Many players and especially younger players do everything on their mobile smart phones, so offering the Kentucky Lottery app became a priority. Now, the pandemic has accelerated this trend and we see we must focus on

improving our iLottery channel to be able to meet consumer expectations and compete with other, similar forms of entertainment. But we will remain committed to meeting consumer expectations at retail as well, because, as the pandemic has shown, many players will continue to purchase at retail. That being said, modernization of the retail channel is important to meet their changing expectations, including promoting our TVMs and cashless functionality, finding ways to tap into the new purchasing behaviors, like BOPUS, and, as well, offering products in new types of retailers.

With effective modernization at retail, I believe lottery will continue to be the game that so many people love to play. Online is where the competition will be intensifying. I think we can expect sports betting operators to raise the bar when it comes to online player attraction and retention strategies. What it means for lottery is that we need to raise our own game to deliver the best iLottery-playing experience we can.

We have been talking about external realities, and the need for customer-facing changes motivated by the pandemic. What about internal operational changes?

M. Harville: Many of our operations are being re-assessed for opportunities to improve. An example is that we have closed our last regional office. We have effective retailer cashing agents that cash up to \$5000, and several retailers throughout the state are designated as super cashing agents with authority to cash up to \$25,000. We closed this regional office for the pandemic, and it soon became clear that we didn’t need that office at all. In addition, we discontinued the use of external auditors for our daily drawings. Our process is robust and built to ensure integrity without the application of external auditors. Even so, we continued to use auditors until COVID made that problematic. So COVID became the catalyst to doing what could have been done sooner.

Pre-pandemic, we were still doing ball machine drawings for several games. RNG (Random Number Generator) was used

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for every new game we introduced, but we kept the ball machines for the daily games. There was no reason to continue to use ball machines for the dailies, except for the concern that players might complain. So now, no more external auditors and no more ball machines. We considered whether to announce that these changes were being done as a result of COVID, leaving the option to return to the former process. But we decided not to go in that direction, because, while the pandemic certainly was the impetus for the change, the reality is that it was time for the change to be made. We received only a couple of complaints.

I think everyone has learned how to adapt and take advantage of the opportunity to change our methods, execute more decisively, and end up improving operations going forward.

The pandemic definitely has caused us to look at things differently. When we think something should change, we are much more likely to go for it now than before. We, as an organization, have learned how to adapt and take advantage of the opportunity to change our methods, execute more decisively, and end up improving operations going forward.

Like most lotteries, we did have a solid, detailed business continuity plan. Although we did not specifically anticipate a pandemic, our IT department had taken steps to ensure we were prepared to switch to telecommuting and videoconferencing. We did not anticipate prolonged telecommuting, but we quickly implemented a policy to cover it, and now, for the future post-pandemic workplace, HR is in the process of determining any roles that can be performed just as effectively at home, which roles can be performed with a divided schedule of home and office, and which roles require a full-time presence in the office. This plan is being readied for implementation and hopefully will be in place when we are in a position to allow staff back in our corporate office and in the field.

Our field staff has done such a fantastic job over the last year and is now re-thinking how they might further optimize their

talents and capabilities to enhance productivity. The basic idea is that whatever amount of time is invested in pre-planning the field work delivers a superlative ROI. The cost of time spent in the field has always been extremely high. Our field staff is working on ways to get more work done at home, to conduct more of the business on the phone and via e-mail and sales wizard so that the time spent with the retailer in the store is highly focused and delivering benefit to the retailer and the players. Retailers have adapted and worked with us to make this approach work to everyone's advantage.

Another high-priority initiative is Corporate Social Responsibility. Arch Gleason (former KLC President) was, and Chip Polston, our Sr. V.P. of Communications, is, a leader in the field of responsible gaming. RG continues to be a mission-critical value to the Kentucky Lottery. But we are expanding the purview of RG to include diversity, inclusion, and gender equality as core values that we are dedicated to advancing. This is particularly important to me, as the first woman to be president of our state lottery. We feel we need to be a part of the movement that is reinventing a more just society that embraces diversity and a culture of civility as the right pathway, not only because that's what is fair, but because it will make us a more effective and productive corporate enterprise. All our stakeholders, including millions of lottery players, expect nothing less than for us to genuinely walk-the-talk. It is more important than ever that the corporate culture reflect the values of the dedicated members of the Kentucky Lottery team. Moreover, research shows that an organization's public commitment to corporate social responsibility, being a good corporate citizen, does have an impact on consumers, especially younger consumers. They want to do business with an organization they can feel good about.

Sports betting is the other top-of-mind topic. Does Kentucky have a sports betting agenda?

M. Harville: The governor's office and legislature are considering the possibilities for regulating sports betting. But their plates are quite full right now so it is difficult to predict what will happen or when it may happen. When PASPA (the federal prohibition of sports betting) was overturned a couple years ago, the Lottery was asked to make a presentation to the committee of our legislature that vets proposed gaming legislation. We invited Scientific Games and IGT to demonstrate the electronic devices that process sports betting wagers for legislators to see how they worked. Our presentation also illustrated the different regulatory models that could be applied to the sports betting sector. It was basically an introduction to sports wagering. We discussed the possible venues for offering sports wagering, the pros and cons of restricting it to horse-race tracks or to opening it up to a broader range of locations, including appropriate lottery retailers and the internet.

We also communicated that the Kentucky Lottery is able and willing to perform in any capacity that is helpful to the Commonwealth of Kentucky. We are certainly capable of implementing a regulatory framework, administering a licensing process, and/or operating the games. The main idea is that the manner and methods in which sports betting should be regulated are political policy decisions made by the governor and the state legislature. We act strictly in the service to the state, support whatever model the elected representatives of the people determine serves the best interests of the people, and are pleased to assist in whatever ways our political stakeholders deem best.

I believe we've established a foundation of trust with the legislature, because we don't advocate for a particular course of action but instead, are available to objectively share our expertise in the gaming industry to help inform their decision-making process. We appreciate their willingness to ask us to be a part of the discussion.

You played a decisive role in the shepherding of all the regulatory changes, new games, and new channels of distribution that have taken place in Kentucky over the last sixteen years, and the last five years in particular.

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M. Harville: The velocity of change certainly accelerated in recent years. Prior to then, innovation was focused on updating existing draw games or producing a new draw game every now and then, creating new instant scratch-off games, and getting more inventive in the advertising and promotion space. This steady-as-you-go approach has been upended by the explosion of gaming options that compete with lottery, by the internet which delivers easy access to those gaming options, by digitization of the in-store shopping experience, inventory management and the business of supporting our retail partners, and just by the application of technology to enhance all aspects of both back-office and customer-facing operations. Much of what was not viable a few years ago is now mandated by players who have higher and higher expectations in the world of evolving technology. Ensuring that modernization stayed aligned with our political stakeholders as well as compliant with all regulatory statutes became a mission-critical component of strategic planning.

The catalyst that started everything for us and for many lotteries, as far as the Internet is concerned, was the Department of Justice ruling that clarified the meaning of the Wire Act to apply to sports betting and not to lottery. That 2012 ruling basically opened the doors for lotteries to make their games available online and within their own borders, so long as legal within the state. Regulatory policy in the games-of-chance industry is decided at the state level, and fortunately, the statute governing the sales of lottery in Kentucky is broad enough to be interpreted to include the internet as a sales channel. We immediately began laying the groundwork to be able to offer internet sales.

Things started to take off in 2013 when we implemented Keno as a precursor to developing a full-blown internet strategy. Sequencing the implementation of new initiatives in this way worked very well for us. With the success of Keno locked in, we turned our attention right back to the internet and soft-launched iLottery in 2016. Like most lotteries, we did meet with some resistance from various interest groups. But we worked diligently to be transparent and address their concerns. We internalized their input and I feel we ended up with a more thoughtful and balanced

approach for enabling a diverse set of voices to guide our iLottery strategy and action-plan.

Did the process of interacting with your legislative constituents for Keno create a foundation of relationships that contributed to your ability to manage the political environment and retain support, or at least defuse opposition, for iLottery?

M. Harville: Yes, I would have to say it did. Interfacing with legislators, retailers, and others for the process of launching Keno did establish a pattern of communication and trust that I think translated well when we came back around with our proposed introduction of internet lottery sales. We educated our stakeholders as to exactly how we would conduct internet sales, with geo-location, deposit limits, and other protections for the consumer. Our stakeholders were and are very aware of our commitment to responsible gaming, to transparency in communications, and to doing everything the way we said we would.

How does your background in law prepare you for leading a state lottery?

M. Harville: Over 32 years practicing law, and especially the past 16 years as the KLC's Sr. V.P. and General Counsel, have served me well and made the transition to President & CEO and very natural one. My years spent in private practice, engaged in business litigation and representing a number of state agencies, provided a solid background in addressing legal and business matters, from contracts to regulatory compliance and employment matters. Being general counsel for the lottery took it to a new and different level. An effective general counsel in the lottery industry (and there are a number of excellent lottery lawyers across the U.S.) not only knows the business and mission, inside and out, but must be strategic, be able to build consensus, and identify the pathways forward that effectively balance a wide variety of sometimes conflicting objectives.

A lottery is unlike any other market-driven consumer-focused business in the world because it has no singular mission to maximize shareholder value. Its mission includes maximizing funds generated for the benefit of good causes – in the Commonwealth of Kentucky, the Lottery funds college scholarship and grant programs.

But our mission also includes service to all the people of Kentucky and the diversity of leaders who represent their interests. Our statutory duty requires the maximization of revenues, but also that we ensure the welfare of our players. Our mission necessarily must include compliance with regulatory constraints which are constantly evolving. And we must also be sensitive to the spirit as well as the letter of the law and stay aligned with our political constituents who sometimes have conflicting agendas. A vital skill set for leadership in this business is strategic thinking to address and manage this broad range of expectations and obligations, and to forge a cohesive approach towards fulfillment of a complex set of goals.

You have always, not just upon your appointment to CEO but from the very beginning sixteen years ago, embraced the opportunity to engage in the broader issue of how to optimize performance, how to integrate the legal, regulatory, and political dimension into the corporate mission.

M. Harville: Operations, marketing, sales management, advertising are all fascinating areas. While I do have an affinity for the discipline of the law, when I joined the Kentucky Lottery sixteen years ago, not just as general counsel but as senior vice president and member of the executive management team, I was immediately intrigued by the bigger-picture strategic challenge of integrating all perspectives into a thoughtful action-plan. It went far beyond legal analysis and advising, and required sorting out the best overall strategies and action-plans to maximize potential, minimize risk, and deliver the best results for the people of Kentucky.

I consider myself very fortunate and blessed to be able to learn from and collaborate with some of the most innovative and effective strategists in the industry, and these are the members of the experienced and talented team at the Kentucky Lottery. I want to thank our entire team for their laser-sharp focus on our mission, even during the unprecedented circumstances of a pandemic, and for being fine people and wonderful friends as well. I am so proud to be a part of our team and very excited for the great things that we will accomplish together over the coming months and years. ■