

# CALIFORNIA STATE LOTTERY

Review Report

## **The Ellen DeGeneres Show Scratchers Ticket Promotion Review**

*July 1, 2019, through June 30, 2020*



**BETTY T. YEE**  
California State Controller

March 2021



**BETTY T. YEE**  
California State Controller

March 25, 2021

Alva Vernon Johnson, Director  
California State Lottery  
700 North Tenth Street  
Sacramento, CA 95811

Dear Mr. Johnson:

We conducted a review of the California State Lottery's (Lottery) The Ellen DeGeneres Show Scratchers ticket promotion for the period of July 1, 2019, through June 30, 2020. The purpose of the review was to determine if the Lottery maintained an adequate system of internal controls over The Ellen DeGeneres Show Scratchers ticket promotion.

Our review determined that the Lottery did not maintain adequate controls over The Ellen DeGeneres Show Scratchers ticket promotion's approval process, agreement negotiations, security of promotional Scratchers tickets, and purchases of add-on media.

If you have any questions, please contact Andrew Finlayson, Chief, State Agency Audits Bureau, by telephone at (916) 324-6310, or by email at [afinlayson@sco.ca.gov](mailto:afinlayson@sco.ca.gov).

Sincerely,

*Original signed by*

MICHAEL REEVES, CPA  
Acting Chief, Division of Audits

MR/as

cc: Nathaniel Kirtman III, Chair  
California State Lottery Commission  
Gregory Ahern, Vice Chair  
California State Lottery Commission  
Keetha Mills, Commissioner  
California State Lottery Commission  
Peter Stern, Commissioner  
California State Lottery Commission  
Harjinder Chima, Chief Deputy Director  
California State Lottery  
Fernando Aceves, Chief Counsel  
California State Lottery  
Sharon Allen, Deputy Director, Sales and Marketing Division  
California State Lottery  
James Shannon, Audit Manager, Internal Audits, Executive Division  
California State Lottery

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# Review Report

## Summary

We conducted a review of the California State Lottery's (Lottery) The Ellen DeGeneres Show Scratchers ticket promotion (The Ellen Show promotion) for the period of July 1, 2019, through June 30, 2020. The purpose of the review was to determine if the Lottery maintained an adequate system of internal controls over The Ellen Show promotion.

Our review determined that the Lottery did not maintain adequate controls over The Ellen Show promotion's approval process, agreement negotiations, security of promotional Scratchers tickets, and purchases of add-on media. Further details of these findings are described in the Conclusion, and in the Findings and Recommendations sections of this report.

## Background

On November 6, 1984, California voters passed Proposition 37, the California State Lottery Act of 1984 (Lottery Act), which authorized the creation of a state-operated lottery. The Lottery Act is found in Chapter 12.5, section 8880 et seq., of the Government Code. The Lottery Act created the California State Lottery Commission (Commission) and gave it broad powers to oversee the Lottery's operations. The purpose of the Lottery Act is to provide supplemental money to benefit public education without the imposition of additional or increased taxes.

The Lottery has eight divisions: Executive, Finance, Human Resources, Operations, Public Affairs and Communications, Security and Law Enforcement, Information Technology Services, and Sales and Marketing. As of October 1, 2020, the Lottery has 909 budgeted positions; staff are located at Lottery Headquarters, two distribution centers, and nine district offices.

In November 2019, the Lottery entered into a gift supplier agreement with WAD Productions, Inc. (WAD) to participate in The Ellen DeGeneres Show's 12 Days of Giveaways in December 2019. Under the terms of the agreement, the Lottery would provide 425 Holiday Scratchers gift boxes with a value of \$500 each to viewers and/or audience members in exchange for on-air promotion to emphasize giving "the gift of Scratchers" and to inform individuals about the Lottery's mission to provide supplemental funding to California public schools.

Pursuant to Government Code (GC) section 8880.46.6, the State Controller's Office (SCO) may conduct special post-audits of the Lottery, as the State Controller deems necessary. The Controller or his/her agents conducting an audit under this chapter shall have access and authority to examine any and all records of the Commission.

GC section 12410 states:

The Controller shall superintend the fiscal concerns of the state. The Controller shall audit all claims against the state, and may audit the

disbursement of any state money, for correctness, legality, and for sufficient provision of law for payment.

In addition, GC section 12411 stipulates that “. . . the Controller shall suggest plans for the improvement and management of revenues.”

## **Objectives, Scope, and Methodology**

The objectives of the review were to determine whether the Lottery:

- Maintained adequate internal controls over The Ellen Show promotion;
- Abided with state laws, rules, regulations, and policies as they relate to The Ellen Show promotion;
- Adequately safeguarded and distributed its assets; and
- Ensured that costs associated with The Ellen Show promotion were reasonable, legal, and proper.

The review period was July 1, 2019, through June 30, 2020.

To achieve our review objectives, we:

- Reviewed the Lottery’s policies and procedures related to promotional Scratchers tickets and promotional events;
- Interviewed the Lottery’s Sales and Marketing Division, Finance Division, and Legal Services staff members to gain an understanding of the Lottery’s internal controls over The Ellen Show promotion;
- Interviewed The Ellen DeGeneres Show’s staff members to gain an understanding of their role in The Ellen Show promotion and in the gift supplier agreement negotiations;
- Reviewed and analyzed the agreement, and relevant files and records related to The Ellen Show promotion; and
- Tested all costs associated with The Ellen Show promotion, totaling \$446,148, to determine whether costs were reasonable, legal, and proper.

This engagement was a review and not an audit; therefore, we did not perform this engagement under generally accepted government auditing standards.

## **Conclusion**

Our review determined that the Lottery:

- Lacked adequate documented processes and procedures for the approval of The Ellen Show promotion;
- Did not adequately prevent the risk of promotional Scratchers tickets going to unintended parties;
- Did not track and destruct unused promotional Scratchers tickets, resulting in a risk of improper use and cash-outs; and
- Lacked adequate supporting documentation to justify the purchase of add-on media, resulting in \$100,000 in questioned costs.

**Views of  
Responsible  
Officials**

We issued a draft review report on February 2, 2021. Alva Vernon Johnson, Director, responded by letter dated February 11, 2021 (Attachment), disagreeing with the findings. However, the Lottery indicated that it is currently reviewing its policies and procedures for promotional programs and will strengthen them where necessary. In addition, to strengthen its internal expertise and management of paid media, the Lottery has created a specialized unit to oversee paid media efforts. Our comments on the Lottery's response to Findings 1 through 4 are included in the Findings and Recommendations section. This final review report includes the Lottery's complete response.

**Restricted Use**

This report is intended for the information and use of the Lottery, the Commission, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record, and is available on the SCO website at [www.sco.ca.gov](http://www.sco.ca.gov).

*Original signed by*

MICHAEL REEVES, CPA  
Acting Chief, Division of Audits

March 25, 2021

# Findings and Recommendations

## **FINDING 1— Lack of adequate documented processes and procedures for the approval of The Ellen Show promotion**

The Lottery lacked adequate documented processes and procedures for the management approval of The Ellen Show promotion. Without documented processes and procedures for the red folder approval process, we could not determine what was being approved, what items should have gone through this process, and what information should have been included for The Ellen Show promotion.

The Lottery used a “red folder” approval process, where a physical paper folder was used to route documents related to The Ellen Show promotion for internal review, comment, and approval. The Ellen Show promotion red folder contained a Transmittal Approval Sheet, a request for Scratchers tickets memorandum, a summary of The Ellen Show promotion, the gift supplier agreement with legal edits, and the final gift supplier agreement.

The final approval signature on the red folder was made by the Lottery Director on November 22, 2019. We noted the following actions were taken prior to final approval:

- November 19, 2019 – The Sales and Marketing Division contacted Horizon Media, a subcontractor of the Lottery’s general market advertising agency, David and Goliath, LLC, requesting to purchase add-on media options;
- November 20, 2019 – The Sales and Marketing Division submitted a memo and a Form 0941- Request for Promotional Tickets/Coupons, requesting Scratchers tickets to be used as prize giveaways;
- November 20, 2019 – Alcone Marketing Group, the Lottery’s marketing promotion and point-of-sale services vendor, created a purchase order to purchase gift boxes for the promotional tickets; and
- November 21, 2019 – The Sales and Marketing Division shipped promotional Scratchers tickets from the Northern Distribution Center to Alcone Marketing Group.

According to Sales and Marketing Division’s management, approvals for promotions are not limited to the red folder process but also occur via meetings, conversations, and emails; and that the Lottery Director verbally approved The Ellen Show promotion in a meeting on November 14, 2019. If The Ellen Show promotion was approved by the Lottery Director on November 14, 2019, we are unclear what the Director’s November 22, 2019 red folder approval represents and whether certain actions should have been taken prior to the red folder final approval date. Adequate internal controls over Lottery promotions should include documentation of the Director’s approval prior to executing significant steps for any promotion.

Per the promotions procedures detail sheet of the Lottery’s Marketing Division’s Promotions Procedures Map, the division should secure the Lottery Director’s approval before completing a request for promotional tickets.



In addition, The Ellen Show promotion red folder did not include all estimated expenses associated with the promotion. Only the expenses for the promotional Scratchers ticket were included, which amounted to \$138,125. Additional promotional expenses not mentioned in the red folder were gift boxes, gift box materials, on-stage props, and optional add-on media, totaling an estimated additional \$311,000. Total expenses for The Ellen Show promotion were estimated to be \$449,125. Including all relevant and significant information in the red folder would have ensured that approvers possessed clear and complete knowledge about the entire promotion prior to approval.

GC sections 13400 through 13407 require state agencies to establish and maintain internal controls, including an effective system of internal review. An effective system of internal review will strengthen administrative controls to minimize fraud, errors, abuse, and waste of funds.

Lottery Regulations section 2.6 Promotions/Free Tickets or Merchandise states, in part:

The Lottery Director may authorize promotional and added-value programs, including free Tickets,... in an effort to maintain awareness of Lottery products and motivate future purchases of Lottery tickets.

#### Recommendation

We recommend that the Lottery develop and document detailed, formal red folder procedures for the promotion approval process to ensure that adequate controls are in place over the promotion approval process.

#### Lottery's Response

Lottery Regulations expressly permit the Lottery to conduct promotional activities, such as the Ellen Show television broadcast promotion. The Ellen Show promotional program was fully reviewed and appropriately approved in a timely manner. This promotion followed department procedures and all approvals were documented. Approvals occurred using multiple mechanisms, including meetings, conversations, and emails depending on the item, situation, and timeline. The "red folder" process referenced by the SCO is not the Lottery's only approval mechanism, nor is it a repository of all approvals and documentation for any one program area. In this case, the red folder process was used specifically to route the final contract for the Lottery Director's signature. The Lottery adequately documented this promotion as it unfolded, while remaining agile as marketing items were negotiated and secured by our media agency within a limited timeline.

The Ellen Show promotion, including the add-on paid media, was presented, and reviewed with the Lottery Director on November 14, 2019 in a formal briefing meeting with Sales & Marketing management and staff. The Lottery Director approved the promotion at this meeting, and additional approvals for elements of the promotion were received in emails on November 15, 2019 and November 18, 2019. Nevertheless, the Lottery will evaluate ways to improve the documentation of decisions, including verbal approvals that occur in meetings in the future...

See the Attachment for the Lottery's complete response.

### SCO Comment

Our finding remains unchanged.

We appreciate the Lottery's response regarding its actions in reviewing relevant policies and procedures for promotional programs. The Lottery stated that The Ellen Show promotion followed department procedures and that it documented all approvals. However, as noted in our finding, there were no documented procedures for the "red folder" process, and The Ellen Show promotion was verbally approved by the Director on November 14, 2019. While we understand that approvals could occur through multiple mechanisms, including meetings, conversations, and emails, a well-documented process would help ensure that the Director has clear and complete knowledge about the entire promotion prior to approval.

**FINDING 2—  
The Lottery did  
not adequately  
prevent the risk  
of promotional  
tickets going to  
unintended  
parties**

The Lottery did not adequately protect its assets by ensuring more specific verbiage about gift recipients or collection of left over gift boxes were included in the gift supplier agreement to prevent the risk of promotional tickets from being distributed to unintended parties. This left the Lottery at risk of incurring additional expenses that could have been avoided or reduced, or gifting a top prize from a promotional Scratchers ticket.

The gift supplier agreement states that the gift boxes would be distributed to viewers and/or audience members as designated by WAD in connection with the television series and related digital properties. According to the Lottery, it was WAD's discretion to determine who the recipients of the gift boxes were. The broadness of the term "viewer" could essentially be anyone.

After the promotional episode aired, a YouTube "influencer" received a Scratchers ticket gift box from an Ellen DeGeneres Show staff member. This YouTube influencer was not in the audience nor a contest winner through The Ellen DeGeneres Show series or related digital properties, and therefore, did not appear to be an intended gift recipient. Sales and Marketing management stated that having a YouTuber receive the gift helped promote the Lottery. However, how the gift was presented in the YouTuber's video did not indicate or imply that she was connected to the show, nor did she promote the "gift of Scratchers" or Lottery's mission in providing funds to education. This is the only known individual to be an unintended recipient. However, given that the Lottery left distribution of the gift boxes solely on WAD, there could have been additional unintended recipients that the Lottery is unaware of. Allowing The Ellen DeGeneres Show to have flexibility in determining who received a Scratchers gift box does not adequately protect the Lottery's assets as the distribution of Scratchers tickets could result in payouts of several millions of dollars.

The Lottery provided 72 Scratchers tickets in each gift box, which included ten \$20 Scratchers tickets with a top prize of \$5,000,000. This

provided each gift recipient a chance to win \$5,000,000. To reduce the chances of large prize payouts from promotional tickets, the agreement should have included provisions clearly stating the intended gift recipients and the return of unused tickets. This would have limited WAD's discretion on the term "viewer". In addition, it would have ensured that leftover gift boxes be returned, reducing the Lottery's prize expense and also reduce the chances of providing winning tickets. If The Ellen DeGeneres Show would have not allowed these provisions, then the Lottery should have considered whether it was prudent to participate in this promotion.

GC sections 13400 through 13407 require state agencies to establish and maintain internal controls, including an effective system of internal review. An effective system of internal review will strengthen administrative controls to minimize fraud, errors, abuse, and waste of funds.

Lottery Act section 8880.25 states:

The Lottery shall be initiated and operated so as to produce the maximum amount of net revenues to supplement the total amount of money allocated for public education in California.

#### Recommendation

We recommend that the Lottery implement policies and procedures to ensure that it takes into consideration the security of tickets when participating in promotions.

#### Lottery's Response

The Lottery respectfully disagrees with this finding. No gift boxes from the promotion went to unintended parties and tickets were securely handled throughout the promotion.

The Lottery entered into a standard agreement with WAD Productions Inc (WAD), the production company for *The Ellen DeGeneres Show*, to provide a specific number of Holiday Scratchers® gift boxes in exchange for on-air integration into the hugely popular *12 Days of Giveaways* segment on the show. The agreement allowed WAD to distribute the gift boxes at their discretion to gift recipients. This type of barter arrangement is a standard business practice where a fixed amount of product is exchanged for a specific amount of value. The benefit of this practice is that it reduces out-of-pocket expenses by trading product at cost, instead of paying outright...

See the Attachment for the Lottery's complete response.

#### SCO Comment

Our finding remains unchanged.

We appreciate the Lottery's response that it is reviewing its policies and procedures, including the use of goodwill tickets in promotions, and will strengthen them where necessary. To ensure that the Lottery maintains

public trust and a positive perception, it should have considered negotiating the terms regarding the recipients of the gift boxes to include only audience members and at-home winners.

The Lottery states that it understood that the gift boxes would be distributed to in-person, at-home audience members and individuals over 18 years of age, as outlined in the agreement. However, we noted that the Lottery questioned whether the Youtuber was part of the contract as they reached out to The Ellen DeGeneres Show after it discovered that the Youtuber had received a gift box to determine whether this fell within the contract terms. In the documentation provided by the Lottery, The Ellen DeGeneres Show did not specifically state that this individual fell within contract terms. The agreement should have included provisions clearly stating the intended gift recipients

**FINDING 3—  
The Lottery did  
not properly  
track and collect  
unused  
promotional  
Scratchers tickets**

The Lottery did not properly track and collect unused promotional Scratchers tickets designated for The Ellen DeGeneres Show. The Ellen Show promotion aired on December 3, 2019, however for several months after The Ellen Show promotion ended, it was identified that the Show still had 35 Scratchers gift boxes at the Warner Brothers Studio lot. This left active Scratchers tickets at risk of improper use and cash-outs.

The Lottery's Sales and Marketing Division's Requesting Promotional Tickets for Events/Fairs/Festivals procedures state:

- Field event staff oversees the event to confirm the promotional tickets are used properly as approved; and
- After the event, field event staff documents in box 16 on CSL 0941 form the quantity of promotional tickets used and unused at the event. Partial packs must be documented as unused promotional tickets.

Sales and Marketing Division management stated that The Ellen Show promotion was not an event and, therefore, the procedures for promotional events were appropriately modified for The Ellen Show promotion. However, as noted in Finding 2, the agreement did not mention the return of unused tickets. The Ellen DeGeneres Show staff stated that the Lottery did not indicate that any unused gift boxes had to be returned while the Sales and Marketing Division's management stated that it was their understanding that all gift boxes would be distributed. With no discussions regarding unused tickets, the Lottery did not implement any measures to collect them.

With the games active, this left remaining unused boxes at risk of improper use and cash outs since the end of The Ellen Show promotion. The Lottery followed up with The Ellen DeGeneres Show staff in August 2020, eight months later, in regards to potential remaining gift boxes. Due to COVID-19, The Ellen DeGeneres Show staff were not able to verify until September 2020 and determined that there were still 35 Scratchers gift boxes at the Warner Brothers Studio lot.

On October 1, 2020, the Lottery collected the 35 boxes and inventoried

their contents, and destroyed the unused tickets. While COVID-19 caused the lock down of the Warner Brothers facilities for several months, the Lottery should have attempted to collect the unused boxes shortly after The Ellen Show promotion ended to reduce prize expense and the risk of any improper cash outs.

In addition, the Lottery did not properly complete Form 0941- Request for Promotional Tickets/Coupons. Lottery staff did not sign and date the form, thereby certifying the release, transfer, and number of unused tickets. An incomplete form constitutes improper tracking, authorization, and review, which is necessary to ensure controls are operating effectively.

GC section 13401 states, in part:

Each state agency must maintain effective systems of internal accounting and administrative control as an integral part of its management practices.

The systems of internal accounting and administrative control of each state agency shall be evaluated on an ongoing basis and, when detected, weaknesses must be promptly corrected.

All levels of management of the state agencies must be involved in assessing and strengthening the systems of internal accounting and administrative control to minimize fraud, errors, abuse, and waste of government funds.

### Recommendation

We recommend that the Lottery:

- Implement adequate controls for all promotions to ensure that excess promotional Scratchers tickets are properly tracked, collected, and destroyed; and
- Follow procedures to ensure that Form 0941-Request for Promotional Tickets/Coupons is properly completed.

### Lottery's Response

The Lottery respectfully disagrees with this finding. Per the Lottery's contract, all Scratchers® gift boxes belonged to WAD to distribute to gift recipients at their discretion. As previously outlined, this was a trade partnership of Scratchers® product in exchange for the in-show segment on the *Ellen Show's 12 Days of Giveaways*.

All Lottery procedures and promotional forms were accurately documented. Staff properly completed the CSL 0941 form based on the fact that tickets were not to be returned...

See the Attachment for the Lottery's complete response.

### SCO Comment

Our finding remains unchanged.

Sales and Marketing Division management stated that The Ellen Show promotion was not an event; therefore, promotional event procedures were modified. However, after The Ellen Show promotion occurred, Lottery staff did not document the quantity of promotional tickets used and unused. If the Lottery had completed form CSL 0941 completely and in a timely manner, it would have become aware of the 35 unused Scratchers ticket gift boxes. As the Lottery did not negotiate the return of unused tickets, it did not implement any measures to collect them or ensure that promotional tickets were used properly as approved.

**FINDING 4—  
Lack of  
supporting  
documentation to  
justify add-on  
media purchases,  
resulting in  
\$100,000 in  
questioned costs**

The Lottery could not provide adequate supporting documentation to justify certain add-on media purchases associated with The Ellen Show promotion. We questioned \$100,000 of add-on media options purchased as these options provided minimal exposure to the Lottery's target market in California, and the consumer impression estimates did not justify the purchases.<sup>1</sup>

The Lottery spent a total of \$281,000 in add-on media costs to leverage The Ellen DeGeneres Show's endorsement. These costs were additional and separate from the cost of the Scratchers ticket gifts provided for in the gift supplier agreement. This consisted of social media posts on Ellen DeGeneres' Facebook, Instagram, and Twitter accounts; pre-roll advertisement on Ellen's YouTube channel, Ellentube, and Ellen's Game of Games app; local TV ad spots during The Ellen DeGeneres Show; and social media boosting on Lottery's social media accounts.<sup>2</sup>

Sales and Marketing Division management stated that a media plan proposal created by the Lottery's marketing specialist was used to discuss and make decisions for the add-on media purchases. We requested that the Lottery provide support for estimated consumer impression numbers on the media plan proposal. The Lottery provided information from Horizon Media, a subcontractor of the Lottery's general market advertising agency, David and Goliath, LLC. We determined that the Lottery spent \$65,000 to purchase a Facebook post and \$35,000 to purchase an Instagram Story post on Ellen's social media accounts. Horizon Media provided estimated national impression numbers for Ellen's Facebook and Instagram add-on options to be 1.9 million and 1.3 million, respectively. While the impression numbers appear high, the estimated impression numbers for Lottery's target market of over 18 years of age in California was much lower. Horizon Media estimated impressions for California to be 228,000 for the Facebook post and 156,000 for the Instagram post.

Given the cost of the media options chosen and the impression estimates for California, we question whether the Lottery should have pursued these options. Per Sales and Marketing Division staff, there is typically a high premium leveraging celebrity talent with costs per thousand impressions (CPM, cost per mille) of up to \$100. While most of the Lottery's The Ellen Show promotion add-on media purchases came under that benchmark, the

<sup>1</sup> An impression represents the number of times an advertisement could have been seen by potential consumers.

<sup>2</sup> A pre-roll advertisement is an ad that is ran before the user's desired content is viewed. Paid advertisements boost a specific social post to increase the number of people that see the content.

Facebook and Instagram purchases did not, when only considering its target market. In addition, since the Instagram post could not be geo-targeted to California only, the Lottery could not verify actual impressions delivered in California.

The following table shows the consumer impression numbers associated with the questioned add-on media purchased:

<b>Add-On Media Option</b>	<b>Cost</b>	<b>Estimated Impressions (National)</b>	<b>Estimated Impressions (California)</b>	<b>Actual Impressions <sup>a</sup></b>	<b>Estimated CPM (California)</b>
Facebook Post from Ellen’s organic page	\$ 65,000	1,900,000	228,000	472,000	\$ 285.09
Instagram Story from Ellen’s organic Instagram	35,000	1,300,000	156,000	165,917	224.36
<b>Total</b>	<b>\$ 100,000</b>	<b>3,200,000</b>	<b>384,000</b>	<b>637,917</b>	

<sup>a</sup> Since the Instagram Story post could not be geo-targeted, actual California impressions could not be verified. Horizon Media took national impressions tracked within Facebook’s system of views of the post and applied 12% (California’s population) to national figures.

In addition, the media plan prepared by the marketing specialist did not recommend the \$65,000 add-on media of the Facebook Post from Ellen’s organic page. However, Sales and Marketing Division’s management stated that, after discussion in the meeting, they believed the added media exposure with Ellen’s endorsement justified the purchase; estimated California impression numbers, however, did not indicate much additional exposure.

Sales and Marketing Division staff stated that media programs are evaluated based on a variety of key performance indicators, such as consumer impressions, reach, awareness, engagement, and other qualitative and quantitative factors. However, reach, awareness, and engagement appear to be dependent on consumer impressions. With low impression numbers this would indicate lower reach, awareness, and engagement. The Lottery could not provide any supporting documentation on how these key performance indicators were evaluated for The Ellen Show promotion.

Lottery act section 8880.4 states, in part: “Revenues of the state lottery shall be allocated so as to maximize the amount of funding allocated to public education....”

GC section 13401 states, in part:

Each state agency must maintain effective systems of internal accounting and administrative control as an integral part of its management practices.

The systems of internal accounting and administrative control of each state agency shall be evaluated on an ongoing basis and, when detected, weaknesses must be promptly corrected.

All levels of management of the state agencies must be involved in assessing and strengthening the systems of internal accounting and administrative control to minimize fraud, errors, abuse, and waste of government funds.

### Recommendation

We recommend that the Lottery ensure that all purchase decisions related to Lottery promotions are:

- Adequately supported and justified with complete information; and
- Made prudently to ensure that the amount of funding allocated to public education is maximized.

### Lottery's Response

The Lottery respectfully disagrees with this finding. The add-on media purchased for the Ellen Show promotion followed the Lottery's review, approval, and documentation process. The Holiday Scratchers® campaign in its entirety successfully supported the Lottery's Scratchers® sales and its Fiscal Year 2019-20 contributions to education.

Planning and buying media is a complex and technical process requiring specialized skills and tools. To accomplish this task, the Lottery uses Horizon Media, the third largest media agency in the United States. Horizon's services to the Lottery include analyses, recommendations, and measurement as part of their stewardship of the Lottery's paid media investment in support of public education...

See the Attachment for the Lottery's complete response.

### SCO Comment

Our finding remains unchanged.

We appreciate the Lottery taking action in implementing a new specialized unit in the Sales and Marketing division to provide additional oversight and guidance over paid media efforts. While we understand that planning and buying media is a complex and technical process, the Lottery did not provide any documented analyses, recommendations, or measurements from Horizon Media before making these purchases. Only after we requested that the Lottery provide source documents to support impression numbers did the Lottery reach out to Horizon Media for its methodology on estimated and delivered impression numbers. The Lottery did not readily have this information when we requested it.

While the actual CPMs for Facebook and Instagram were lower than estimated, the actual CPMs for both were still over 230% more costly than the other The Ellen DeGeneres Show media options purchased. Actual CPMs for Twitter and custom digital media (pre-roll ads on Ellen's Youtube channel, Game of Games app, and Ellentube) posts were \$19.39 and \$41.67, respectively. All purchase decisions related to promotions should be made prudently to ensure the Lottery is maximizing funding to public education.



**Attachment—  
California State Lottery’s  
Response to Draft Review Report**

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February 11, 2021

Andrew Finlayson,  
State Agency Audits Bureau Chief  
State Controller's Office  
Division of Audits  
P.O. Box 942850  
Sacramento, CA 94250

Re: Response to SCO Draft Ellen DeGeneres Show Scratchers® Ticket Promotion Review

Dear Mr. Finlayson:

Thank you for allowing the California State Lottery (Lottery) the opportunity to review the State Controller's Office (SCO) *Ellen DeGeneres Show* Promotion (Report) that covers the period July 1, 2019 through June 30, 2020.

The Lottery takes seriously its essential mission as a state department working in support of public education. The Lottery also understands that an important part of this mission is to perform duties in a cost-effective and transparent manner to ensure that the public trust is maintained and to fully maximize opportunities to generate additional funds for public education in California. The Lottery values constructive criticism from any source that helps us improve our integrity, transparency, and consumer confidence in the products we sell in over 23,000 retailers throughout the state.

The Lottery is pleased that the State Controller's Office confirmed that this promotion followed all state laws, rules, regulations, and policies, and that it did not identify any fraud, waste, or abuse.

However, the Lottery respectfully disagrees with some findings. Specifically, the required approvals of this promotion were obtained and sufficiently documented, there was no risk of Scratchers® going to unintended parties, and the Lottery fulfilled its contractual agreement to provide the required amount of Scratchers® gift boxes with no expectation of unused tickets to be returned. Additionally, the costs for the add-on social media supporting the promotion were adequately justified.

*The Ellen DeGeneres Show (Ellen Show)* television promotion successfully advanced product sales and increased department profits, furthering the Lottery's mission to provide supplemental funding for public education in California. The Lottery's 2019 Holiday Scratchers® sales were higher than the previous ten years and increased 74% over the prior year while the entire Scratchers® category was up 3% year over year. These strong

Andy Finlayson  
February 11, 2021  
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results were fueled by a comprehensive marketing campaign, including the *Ellen Show* promotion.

The Lottery is reviewing each recommendation in the Report against our current practices to ensure that they adequately address the challenges noted. If our internal review indicates the current practices are insufficient to address the noted deficiencies, the Lottery will take appropriate corrective steps to implement additional internal controls. The Lottery continues to maintain the highest level of integrity and legitimacy when marketing our products to consumers to achieve our essential mission.

It is important to note the unique nature of the California State Lottery. Unlike other state departments, the Lottery does not utilize General Fund money; its revenue is derived solely from the sale of Lottery products. Thus, the Lottery must continually develop fun and exciting lottery games and invest in a variety of marketing strategies and tactics to persuade California adults to voluntarily purchase Lottery tickets, to meet its mandate to maximize supplemental funding for public education. To achieve these goals the Lottery uniquely competes with other consumer goods and entertainment options for discretionary spending. To this end, the Lottery must continually invest in a variety of marketing strategies and tactics to engage consumers and our retail partners.

A cornerstone in the Lottery's annual marketing plan is the release of new holiday-themed Scratchers® and its associated marketing campaign encouraging Californians to "Give the Gift of Scratchers®." This comprehensive campaign includes a mix of advertising including television, radio, billboards, social media, promotions, and experiential marketing. One component of the 2019 Holiday Scratchers® marketing effort was a promotional agreement with the highly-rated television program, *The Ellen DeGeneres Show*, for Holiday Scratchers® to be featured as one of the prizes in the show's extremely popular *12 Days of Giveaways* segment.

This *Ellen Show* partnership offered a unique opportunity to increase consumer awareness of the Lottery's contributions to public education while at the same time helping to generate sales of Holiday Scratchers® and support the Lottery's education beneficiaries. To participate in *Ellen's 12 Days of Giveaways*, the Lottery was contractually required to provide a fixed number of gift boxes containing Scratchers® tickets in exchange for an in-show segment promoting Holiday Scratchers® and the Lottery.

This television broadcast segment featured popular host Ellen DeGeneres and her celebrity guest Jimmy Kimmel endorsing the California Lottery and Holiday Scratchers®. This type of endorsement has been shown to be more impactful, and more valuable, than traditional television commercials. The integration within a broadly popular program like the *Ellen Show* also helps reach new players that may not otherwise consider purchasing Lottery products in general. Moreover, Ms. DeGeneres is also a longstanding supporter of public schools, thus aligning perfectly with the Lottery and its mission.

This successful promotion followed all department policies, regulations and state laws and provided significant value to the Lottery's beneficiaries at minimal expense. Through the *Ellen Show* promotion alone, the Lottery was able to generate over two million impressions in California creating consumer awareness, engagement, and product trial. This included

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exposure of Holiday Scratchers® to consumers on-air during the show as well as across *Ellen Show* digital platforms, social media, and a popular YouTube influencer. The Lottery also benefited from gift recipients receiving and playing the Scratchers® games, thus creating awareness and word-of-mouth excitement about the Lottery and its products to help expand playership.

The 2019 Holiday Scratchers® marketing campaign, including the *Ellen Show* promotion, increased awareness, and purchase intent of Scratchers®. Consumer research showed that among those who had seen the Holiday Scratchers® advertising, top-of-mind awareness, an important measure of consumers' unprompted recall of Scratchers®, more than doubled while purchase intent, or the likelihood of a consumer to buy Scratchers®, increased by 28%. Overall, Scratchers® sales through the holiday season amounted to \$1.2 billion, or roughly 24% of total Fiscal Year 2019-20 Scratchers® sales, representing a significant contributor in our mission to generate funding for public education.

The following addresses each finding in the Report specifically.

***Finding 1 – Lack of adequate documented processes and procedures for the approval of The Ellen Show promotion***

**RECOMMENDATION:**

We recommend that the Lottery develop and document detailed, formal red folder procedures for the promotion approval process to ensure that adequate controls are in place over the promotional approval process.

**RESPONSE:**

Lottery Regulations expressly permit the Lottery to conduct promotional activities, such as the *Ellen Show* television broadcast promotion. The *Ellen Show* promotional program was fully reviewed and appropriately approved in a timely manner. This promotion followed department procedures and all approvals were documented. Approvals occurred using multiple mechanisms, including meetings, conversations, and emails depending on the item, situation, and timeline. The "red folder" process referenced by the SCO is not the Lottery's only approval mechanism, nor is it a repository of all approvals and documentation for any one program area. In this case, the red folder process was used specifically to route the final contract for the Lottery Director's signature. The Lottery adequately documented this promotion as it unfolded, while remaining agile as marketing items were negotiated and secured by our media agency within a limited timeline.

The *Ellen Show* promotion, including the add-on paid media, was presented, and reviewed with the Lottery Director on November 14, 2019 in a formal briefing meeting with Sales & Marketing management and staff. The Lottery Director approved the promotion at this meeting, and additional approvals for elements of the promotion were received in emails on November 15, 2019 and November 18, 2019. Nevertheless, the Lottery will evaluate ways to improve the documentation of decisions, including verbal approvals, that occur in meetings in the future.

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In 2019, the Lottery began an ongoing enterprise-wide initiative to review and revise existing policies and procedures. Additionally, in 2020, the department began a separate initiative to identify enterprise risks in order to strengthen documentation practices and improve governance and accountability. These efforts will include a thorough review of the relevant policies and procedures for promotional programs such as the *Ellen Show* promotion.

***Finding 2 – The Lottery did not adequately prevent the risk of promotional tickets going to unintended parties.***

**RECOMMENDATION:**

We recommend that the Lottery implement policies and procedures to ensure that it takes into consideration the security of tickets when participating in promotions.

**RESPONSE:**

The Lottery respectfully disagrees with this finding. No gift boxes from the promotion went to unintended parties and tickets were securely handled throughout the promotion.

The Lottery entered into a standard agreement with WAD Productions Inc (WAD), the production company for *The Ellen DeGeneres Show*, to provide a specific number of Holiday Scratchers® gift boxes in exchange for on-air integration into the hugely popular *12 Days of Giveaways* segment on the show. The agreement allowed WAD to distribute the gift boxes at their discretion to gift recipients. This type of barter arrangement is a standard business practice where a fixed amount of product is exchanged for a specific amount of value. The benefit of this practice is that it reduces out-of-pocket expenses by trading product at cost, instead of paying outright.

As specified under its contract with the *Ellen Show*, the Lottery provided gift boxes of Holiday Scratchers® in exchange for the specific and high-value benefit of an in-show segment and endorsement by celebrities Ellen DeGeneres and Jimmy Kimmel. The Lottery received the value of this celebrity endorsement at a minimal cost relative to the millions of dollars it typically costs commercial brands and companies to secure a direct celebrity endorsement.

In addition to the in-show segment, the Lottery intended to gain word-of-mouth promotion from the recipients of the gift boxes. Product giveaways and free sampling is a tried-and-true marketing strategy that provides products for free to potential customers for trial and to talk about with their friends. With the Lottery's target audience being all California adults over age 18, product sampling among any adult has great value.

After the show aired, the Lottery discovered that a YouTube Influencer had received a Scratchers® gift box. In her video, the YouTuber said it was from someone in the show's production staff. Per the contract terms, the *Ellen Show* had full ownership of the gift boxes and had full discretion as to how the boxes would be distributed. The Lottery understood that the gift boxes would be distributed to the in-person and at home *Ellen Show* audience and individuals over the age of 18, as outlined in the agreement.

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The value received by the Lottery from the YouTube Influencer sharing her experiences with the Holiday Scratchers® aligned with the Lottery's intention to create consumer awareness, product trial, and generate word-of-mouth promotion. In fact, the Lottery received over \$95,000 in free media value from the YouTuber, who shared her enthusiasm for receiving the gift box and her excitement to play Scratchers®. Influencer Marketing like this has been proven effective at not only extending reach to additional audiences but also in demonstrating that the message from a trusted source can be more persuasive than many other forms of advertising.

Given the contract parameters and execution, the Lottery maintains that there were no unintended recipients. Additionally, there was no additional liability or cost in prize expense by executing the *Ellen Show* promotion, regardless of who received the tickets or who wins a prize. The Scratchers® tickets used in the promotion were part of existing games already in market with a set pool of tickets and prizes. The number of tickets provided to the *Ellen Show* represented less than one tenth of one percent (0.04%) of the total tickets available for these Scratchers® games. The Lottery does not know which tickets are winners, and the odds of winning are the same for each ticket.

As previously noted, the Lottery is currently reviewing its policies and procedures, including the use of goodwill tickets as used in this promotion, and will strengthen them where necessary.

***Finding 3 – The Lottery did not properly track and collect unused promotional Scratchers® tickets.***

**RECOMMENDATION:**

We recommend that the Lottery:

- Implement adequate controls for all promotions to ensure that excess promotional Scratchers® tickets are properly tracked, collected, and destroyed; and
- Follow procedures to ensure that Form 0941 – Request for Promotional Tickets/Coupons is properly completed.

**RESPONSE:**

The Lottery respectfully disagrees with this finding. Per the Lottery's contract, all Scratchers® gift boxes belonged to WAD to distribute to gift recipients at their discretion. As previously outlined, this was a trade partnership of Scratchers® product in exchange for the in-show segment on the *Ellen Show's 12 Days of Giveaways*.

All Lottery procedures and promotional forms were accurately documented. Staff properly completed the CSL 0941 form based on the fact that tickets were not to be returned.

Nevertheless, the Lottery did inquire with *Ellen Show* staff in December 2019 and again in January 2020 regarding any remaining gift boxes and the show reiterated that they had the right to distribute all boxes per our agreement.

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The circumstances surrounding this SCO review prompted *Ellen Show* staff to later reveal they had remaining gift boxes in their possession. The show had stored these gift boxes continuously in a locked facility; they were never at risk for improper use. The show agreed to return ownership of the tickets to the Lottery and as soon as access to the studio facility was permitted, the Lottery took immediate actions to collect, inventory, and properly dispose of these tickets. This included updating the CSL 0941 form to reconcile the unused tickets.

***Finding 4 – Lack of supporting documentation to justify add-on media purchases, resulting in \$100,000 in questioned costs.***

**RECOMMENDATION:**

We recommend that the Lottery ensure that all purchase decisions related to Lottery promotions are:

- Adequately supported and justified with complete information: and
- Made prudently to ensure that the amount of funding allocated to public education be maximized.

**RESPONSE:**

The Lottery respectfully disagrees with this finding. The add-on media purchased for the *Ellen Show* promotion followed the Lottery's review, approval, and documentation process. The Holiday Scratchers® campaign in its entirety successfully supported the Lottery's Scratchers® sales and its Fiscal Year 2019-20 contributions to education.

Planning and buying media is a complex and technical process requiring specialized skills and tools. To accomplish this task, the Lottery uses Horizon Media, the third largest media agency in the United States. Horizon's services to the Lottery include analyses, recommendations, and measurement as part of their stewardship of the Lottery's paid media investment in support of public education.

Based on Horizon's recommendation, the Lottery shifted funds in the overall Holiday Scratchers campaign to purchase add-on media on the *Ellen Show's* digital and social media platforms to amplify the in-show segment featuring popular television personalities Ellen DeGeneres and Jimmy Kimmel endorsing the California Lottery and Holiday Scratchers®. This add-on media was used to reach the large segment of consumers who do not watch *The Ellen DeGeneres Show* on traditional television. This type of amplification is a marketing best practice.

Social media marketing has proven itself to be an integral part of the overall marketing strategy for most brands, including the Lottery. For this promotion, the add-on social media purchased was so that the Lottery's *Ellen Show* segment would appear as organic content from Ellen DeGeneres' Facebook and Instagram profiles directly to her fans on each of these platforms. This created more impactful and meaningful impressions because her followers are actively engaged with her content and would be more receptive to the message. This type of branded content has a premium cost compared to typical Facebook

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or Instagram advertising. Also, the Facebook post had the additional benefit of remaining on Ellen's feed permanently, allowing users to like, share, and comment on the post.

Due to the extraordinary value and benefits associated with this type of social media engagement at a relatively low cost, Sales & Marketing management and the marketing specialist who prepared the media plan agreed to proceed with the Facebook post and Instagram Story on Ellen DeGeneres' profiles even though they had to run nationally. However, the California impressions alone delivered significant value for the Lottery and provided justification for this purchase decision.

Furthermore, the actual posts delivered more California consumer impressions than initially projected as outlined in the chart on page 9 of the Report. The Facebook post generated over 200% more impressions, and the Instagram Story yielded a 7% increase over estimated impressions. As a result, the Lottery was able to reach more highly engaged Ellen DeGeneres fans in California at the same cost, which equates to a lower CPM, or cost per thousand impressions delivered.

The actual CPM for the Facebook post was \$137.71 (vs \$285.09 estimated) and the actual CPM for the Instagram Story was \$210.95 (vs \$224.36 estimated). The Lottery acknowledges that Horizon Media subsequently was able to geotarget Facebook to California without negotiating a specific price reduction while the Instagram Story ran nationally as expected.

To strengthen the Lottery's internal expertise and management of paid media, the Lottery has created a new, specialized unit in the Sales & Marketing division that will oversee paid media efforts with a dedicated manager to provide guidance and additional oversight.

#### **CONCLUSION:**

The Lottery appreciates the recommendations outlined within this Report and values the necessary oversight and review that helps us serve our essential mission to support public education. As noted, we have already begun a thorough review of our policies and procedures as well as promotions.

Thank you again for the opportunity to review the Report. If you have any additional questions, please contact Lottery's Acting Deputy Director of Internal Audits, James Shannon at (916) 822-8360.

Sincerely,

DocuSigned by:  
  
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Alva V. Johnson



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cc:

Gregory Ahern, Chair  
California State Lottery Commission  
Nathaniel Kirtman III, Commissioner  
California State Lottery Commission  
Keetha Mills, Commissioner  
California State Lottery Commission  
Peter Stern, Commissioner  
California State Lottery Commission  
Harjinder Chima, Chief Deputy Director, Executive Division  
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