

# **CALIFORNIA STATE LOTTERY**

Audit Report

## **ECONOMY AND EFFICIENCY OF MARKETING CONTRACTS**

David & Goliath LLC;  
Casanova, Pendrill Publicidad, Inc.;  
and Circus LAX LLC

*January 1, 2019, through December 31, 2020*



**BETTY T. YEE**  
California State Controller

September 2022



**BETTY T. YEE**  
California State Controller

September 22, 2022

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

Dear Mr. Johnson:

We audited the economy and efficiency of the California State Lottery's marketing contracts for the period of January 1, 2019, through December 31, 2020. We conducted this performance audit in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States.

Based on our audit, we determined that money spent on marketing contracts produced expected and trackable returns on investments. There are no audit findings.

If you have any questions, please contact Roochel Espilla, Chief, State Agency Audits Bureau, by telephone at (916) 323-5744 or by email at [respilla@sco.ca.gov](mailto:respilla@sco.ca.gov).

Sincerely,

*Original signed by*

KIMBERLY TARVIN, CPA  
Chief, Division of Audits

KT/lis

cc: Harjinder Shergill-Chima, Chief Deputy Director  
California State Lottery  
Sharon Allen, Deputy Director, Sales and Marketing Division  
California State Lottery  
Jim Hasegawa, Deputy Director, Business Planning  
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Sara Sheikholislam, Deputy Director, Internal Audits  
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Emily Nguyen, Audit Manager, Internal Audits  
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Gregory Ahern, Chair  
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California State Lottery Commission  
Anthony Garrison-Engbrecht, Commissioner  
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Keetha Mills, Commissioner  
California State Lottery Commission  
Peter Stern, Commissioner  
California State Lottery Commission

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# Audit Report

## Summary

We conducted an audit of the economy and efficiency of the California State Lottery's (Lottery) marketing contracts for the period of January 1, 2019, through December 31, 2020. Based on our audit, we determined that money spent on marketing contracts produced expected and trackable returns on investments.

## 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 Government Code. The Lottery Act created the California State Lottery 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's eight divisions support the Lottery's sole mission, to supplement funding for California's public schools and colleges. As of August 1, 2021, the Lottery has 934 budgeted positions; staff are located at Lottery Headquarters, two distribution centers, and nine district offices.

The Consumer Marketing Unit of the Lottery's Sales and Marketing Division and the Business Planning and Research Unit of the Lottery's Executive Division produce metrics for tracking and measuring performance of the marketing contractors.

The Consumer Marketing Unit encourages positive player and public attitudes toward the Lottery and its games. In addition, the Consumer Marketing Unit oversees the development of advertising and marketing campaigns that promote the sale of Lottery products and support marketing plans, and coordinates marketing-related projects and programs.

The Business Planning and Research Unit assists the Sales and Marketing Division in developing the Lottery's marketing plans, creating predictive data models to help solve business problems, and conducting independent assessments of the effectiveness of implemented tactics.

David & Goliath LLC provides general market advertising services to the Lottery. Casanova, Pendrill Publicidad, Inc. and Circus LAX LLC provide the Lottery with Hispanic market advertising services. The total contract amount for all three marketing contractors is \$416,600,000.

## Audit Authority

Pursuant to Government Code (GC) section 8880.46.6, the SCO may conduct special 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 California State Lottery 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 “[t]he Controller shall suggest plans for the improvement and management of the public revenues.”

## **Objective, Scope, and Methodology**

The objective of our audit was to determine whether money spent on marketing contracts produced expected and trackable returns on investments. The audit covered the period of January 1, 2019, through December 31, 2020.

To achieve our audit objective, we performed the following procedures:

- We reviewed various Lottery policies and procedures, including the *Contract Manager's Handbook–Post Award*, Ad Tracker Contract and Project Management Tasks, the *Tracking Study Manual*, and the *Contract Operating Manual* as they relate to evaluating Marketing Contractors' performance and advertising campaigns.
- We interviewed Lottery staff members from the Consumer Marketing Unit and the Business Planning and Research Unit to gain an understanding of processes related to planning and developing advertising campaigns, and evaluating marketing contractors' performance.
- We reviewed prior engagements performed by SCO and the Lottery's Internal Audits Office related to the Consumer Marketing Unit and the Business Planning and Research Unit.
- We reviewed the sole marketing contract awarded during the audit period and determined whether it complied with the Lottery's procurement policies.
- We selected a sample of quarterly key marketing initiatives to determine whether the Lottery tracked and measured the marketing contractors' performance by reviewing the following:
  - Contract manager's annual evaluations of the marketing contractors;
  - Comparative presentations outlining the Lottery's performance versus other state lotteries and private companies;
  - Ad Tracker and Tracking Data report evaluations of campaign performances; and
  - Analytic and Return on Investment (ROI) evaluations provided by Horizon Media.
- We identified and reviewed the methodology used by Horizon Media to calculate the ROI of each media driver on Lottery products, and

conducted analyses and recalculations. ROI quantifies the financial return of each marketing dollar spent; it is expressed as:

$$\text{ROI} = \text{Sales Contribution} / \text{Spend}$$

We considered a marketing spending that generates at least \$1.00 ROI to be a good ROI. This indicates that a dollar spent on marketing contributed a dollar to Lottery sales.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. We limited our review of internal control to gain an understanding of the Lottery's processes for evaluating and analyzing marketing contractor performance. We did not audit the Lottery's financial statements.

## **Conclusion**

Our audit determined that money spent on marketing contracts produced expected and trackable returns on investments. The Lottery conducts annual evaluations of the marketing contractors and uses return-on-investment evaluations to analyze marketing contractors' performance and marketing campaigns.

## **Follow-up on Prior Audit Findings**

We last performed an audit of David and Goliath LLC, and issued a final report in February 2020. As there were no findings noted in the previous audit, a follow-up was not necessary.

## **Views of Responsible Officials**

We discussed our audit results with Lottery representatives. As there are no findings, Lottery representatives waived the exit conference and draft report on September 16, 2021. We agreed to issue the report as final.

## **Restricted Use**

This report is intended for the information and use of the Lottery, the California State Lottery 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*

KIMBERLY TARVIN, CPA  
Chief, Division of Audits

September 22, 2022

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