

# Arizona State Lottery Commission

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	FY 2009 ACTUAL	FY 2010 ESTIMATE	FY 2011 BASELINE
<b>OPERATING BUDGET</b>			
<i>Full Time Equivalent Positions</i>	110.0	104.0	104.0
Personal Services	4,387,400	4,824,500	4,824,500
Employee Related Expenditures	1,684,600	1,721,200	1,721,200
Professional and Outside Services	386,400	383,400	383,400
Travel - In State	231,800	269,800	269,800
Travel - Out of State	7,700	16,700	16,700
Other Operating Expenditures	572,800	353,300	1,152,300
Equipment	87,800	0	0
<b>OPERATING SUBTOTAL</b>	<b>7,358,500</b>	<b>7,568,900</b>	<b>8,367,900</b>
<b>SPECIAL LINE ITEMS</b>			
Advertising	15,669,700	16,000,000	16,000,000
Instant Tickets	10,038,800	11,537,200	12,451,000
On-Line Vendor Fees	7,813,800	7,843,000	7,717,100
Retailer Commissions	32,455,400	35,373,600	37,147,000
Sales Incentive Program	38,100	50,000	50,000
Telecommunications	393,000	629,400	0
5th Special Session Reduction	0	(528,400)	(528,400)
<b>AGENCY TOTAL</b>	<b>73,767,300</b>	<b>78,473,700</b>	<b>81,204,600</b>

## FUND SOURCES

### Other Appropriated Funds

State Lottery Fund	73,767,300	78,473,700	81,204,600
SUBTOTAL - Other Appropriated Funds	73,767,300	78,473,700	81,204,600
<b>SUBTOTAL - Appropriated Funds</b>	<b>73,767,300</b>	<b>78,473,700</b>	<b>81,204,600</b>
Other Non-Appropriated Funds	284,661,600	313,043,000	330,662,300
<b>TOTAL - ALL SOURCES</b>	<b>358,428,900</b>	<b>391,516,700</b>	<b>411,866,900</b>

## CHANGE IN FUNDING SUMMARY

	FY 2010 to FY 2011 Baseline	
	\$ Change	% Change
Other Appropriated Funds	2,730,900	3.5%
Total Appropriated Funds	2,730,900	3.5%
Non-Appropriated Funds	17,619,300	5.6%
Total - All Sources	20,350,200	5.2%

**AGENCY DESCRIPTION** — The Arizona Lottery is responsible for administering sanctioned games of chance. Arizona-specific games include instant tickets, the Pick, Pick 3, and Pick 5 on-line games. Arizona also participates in the multi-state Powerball on-line game.

### **Operating Budget**

The Baseline includes \$8,367,900 and 104 FTE Positions from the State Lottery Fund for the operating budget in FY 2011. FY 2011 adjustments would be as follows:

### **Telecommunications Funding Shift**

**OF \$629,400**

The Baseline includes a funding shift of \$629,400 from the State Lottery Fund in FY 2011. Telecommunications funding will now be included in the operating budget instead of the Telecommunications line item beginning in FY 2011. The shift would not result in a net change in the Lottery's overall funding level.

**Restore Spending Reduction OF 169,600**

The Baseline includes an increase of \$169,600 from the State Lottery Fund in FY 2011 to restore a spending reduction. This restoration is offset by a reduction in on-line vendor fees, which were renegotiated in October 2009. (See the On-line Vendor Fees line item for more information.)

**Advertising**

The Baseline includes \$16,000,000 from the State Lottery Fund for Advertising in FY 2011. This amount is unchanged from FY 2010.

Monies in this line item are used to promote and market Lottery games.

**Instant Tickets**

The Baseline includes \$12,451,000 from the State Lottery Fund for Instant Tickets in FY 2011. FY 2011 adjustments would be as follows:

**Instant Ticket Sales Increase OF 913,800**

The Baseline includes an increase of \$913,800 from the State Lottery Fund in FY 2011 for Instant Tickets due to higher projected sales. (See "Other Issues for Legislative Consideration – Lottery Forecast" for more information.)

Monies in this line item are used to pay for instant ticket printing and distribution costs. The actual appropriation is for 3.6% of instant ticket sales. The amount displayed is derived by applying the approved spending percentage to the forecasted sales total.

**On-Line Vendor Fees**

The Baseline includes \$7,717,100 from the State Lottery Fund for On-line Vendor Fees in FY 2011. FY 2011 adjustments would be as follows:

**New Vendor Contract Rate OF (125,900)**

The Baseline includes a decrease of \$(125,900) from the State Lottery Fund in FY 2011 for On-line Vendor Fees due to a new on-line vendor contract rate.

Monies in this line item are used to pay the vendor that operates the on-line game computer system. The actual appropriation is equal to a percentage of on-line ticket sales specified in the Lottery's contractual agreement with the vendor. The new contract specifies that the new contract rate is 3.7% of total on-line sales beginning October 2009.

The displayed amount is derived by applying the approved percentage to the forecasted sales total. The old contract of 4.0322% was applied to the first 3 months of FY 2010 and the new contract rate of 3.7% was applied to the next 9 months of FY 2010 and all of FY 2011.

**Retailer Commissions**

The Baseline includes \$37,147,000 from the State Lottery Fund for Retailer Commissions in FY 2011. FY 2011 adjustments would be as follows:

**Retailer Commission Increase OF 1,773,400**

The Baseline includes an increase of \$1,773,400 from the State Lottery Fund in FY 2011 for Retailer Commissions due to higher projected sales. (See "Other Issues for Legislative Consideration – Lottery Forecast" for more information.)

Monies in this line item are used to compensate retailers for selling lottery tickets. The actual appropriation is equal to 6.5% of total ticket sales. Pursuant to statute, an additional 0.5% of total ticket sales may be paid to retailers based on their attainment of specified sales and marketing objectives. Since 40% of retailers are estimated to meet these objectives, this would result in an additional 0.2% in retailer commissions and a total retail commission rate of 6.7%. The displayed amount is derived by applying the approved percentage to the forecasted sales total.

**Sales Incentive Program**

The Baseline includes \$50,000 from the State Lottery Fund for the Sales Incentive Program in FY 2011. This amount is unchanged from FY 2010.

Monies in this line item are used to provide monetary incentives to employees in the Lottery's Marketing Division for working with retailers to increase sales.

**Telecommunications**

The Baseline includes no funding from the State Lottery Fund for Telecommunications in FY 2011. FY 2011 adjustments would be as follows:

**Telecommunications OF (629,400) Funding Shift**

The Baseline includes a funding shift of \$(629,400) from the State Lottery Fund in FY 2011. Telecommunications funding will now be included in the operating budget instead of the Telecommunications line item beginning in FY 2011. The shift would not result in a net change in the Lottery's overall funding level.

Monies in this line item were used to pay for all costs related to the Lottery's telecommunications network. The Lottery provides telecommunications services to retailers who sell on-line game tickets through a contract with private vendors.

**5<sup>th</sup> Special Session Reduction**

The Baseline includes \$(528,400) from the State Lottery Fund in FY 2011 to continue the 5<sup>th</sup> Special Session FY 2010 Lump Sum Reduction. This lump sum reduction

would be allocated to specific line items in the FY 2011 General Appropriation Act.

\* \* \*

**FORMAT** — Operating Lump Sum with Special Line Items by Agency

## FOOTNOTES

### *Standard Footnotes*

An amount equal to 3.6% of actual instant ticket sales is appropriated for the printing of instant tickets or for contractual obligations concerning instant ticket distribution. This amount is currently estimated to be \$12,451,000 in FY 2011.

An amount equal to a percentage of actual on-line game sales as determined by contract is appropriated for payment of on-line vendor fees. This amount is currently estimated to be \$7,717,100, or 3.7% of actual on-line ticket sales, in FY 2011.

An amount equal to 6.5% of gross lottery game sales is appropriated for payment of sales commissions to ticket retailers. An additional amount of not to exceed 0.5% of gross lottery game sales is appropriated for payment of sales commissions to ticket retailers. The combined amount is currently estimated to be 6.7% of total ticket sales, or \$37,147,000, in FY 2011.

## OTHER ISSUES FOR LEGISLATIVE CONSIDERATION

### **Lottery Forecast**

The JLBC Staff forecasts a 9.0% increase in overall Lottery ticket sales in FY 2010, followed by a 5.0% increase in FY 2011. For FY 2010 and FY 2011, the JLBC forecasts Lottery ticket sales of \$527,964,600 and \$554,432,300, respectively.

The JLBC Staff forecasts a 14.9% increase in instant ticket sales for FY 2010, followed by a 7.9% increase in FY 2011. The Instant Scratchers game remains the largest contributor to both FY 2010 and FY 2011 forecasts with estimated sales of \$267,415,300 and \$290,145,600, respectively.

In regards to state-only on-line ticket sales (excluding Powerball), the JLBC Staff forecasts a 2.2% increase in on-line ticket sales in FY 2010, followed by a 1.2% increase in FY 2011. Due to the uncertainty of when large Powerball jackpots will occur, the forecast includes no growth in Powerball ticket sales for FY 2010 and FY 2011.

As a result of offering higher prizes as well as increasing aggregate game payouts, FY 2009 total ticket sales were \$11,548,800 above FY 2008. However, this caused the percentage of ticket sales that is used for beneficiary distribution to drop from 30% prior to FY 2009 to 26% in FY 2009. Therefore, despite an increase in total ticket

sales in FY 2009, actual profits available for distribution to beneficiaries, excluding fund transfers, dropped by \$(21,675,800) as compared to the prior year. A.R.S. § 5-505B requires the Lottery to deposit at least 50% of total ticket sales in the non-appropriated portion of the State Lottery Fund, which is used for prize payouts. If the Lottery chooses to deposit more than 50% of total ticket sales for prize payouts, then the remaining amount for beneficiary distribution decreases. In FY 2009, approximately 59% of total ticket sales were used for prizes. Excluding fund transfers, monies available for distribution are estimated to be \$126,701,800 in FY 2010 and \$142,037,000 in FY 2011, based on an approximate 59% prize payout.

### **Sources and Uses of Lottery Profit Distribution**

Table 1 shows the sources of forecasted Lottery profits by revenue stream and illustrates the actual distributions to fund beneficiaries for FY 2009 and the JLBC projected distributions for FY 2010 and FY 2011. A brief description of each beneficiary follows in the order that they receive Lottery-generated revenue in accordance with A.R.S. § 5-522.

#### General Fund – Part 1

The General Fund receives up to \$31,000,000 prior to other distributions. The General Fund could receive an additional \$15,490,000 (for a total of \$46,490,000) after the statutory funding obligations have been met through the Homeless Shelters distribution. The General Fund is estimated to receive \$31,000,000 in both FY 2010 and FY 2011 from this distribution plus \$10,847,200 in FY 2010 and \$15,490,000 in FY 2011 from the Part 2 distribution. In addition, the General Fund is estimated to receive an additional \$125,000 in FY 2011 after all statutory funding obligations have been met.

#### Mass Transit Fund

The Mass Transit Fund (otherwise known as LTAF II) receives its monies after the \$31,000,000 distribution to the General Fund is met. Starting in FY 2009, it receives a maximum of \$9,000,000 increasing by up to 10% every year until total revenues reach a maximum of \$18,000,000. The funds are used by the counties to enhance existing public transportation systems. LTAF II is estimated to receive \$8,910,000 in FY 2010 and \$10,890,000 in FY 2011. The FY 2010 distribution would have been \$9,900,000, however, Laws 2009, 4<sup>th</sup> Special Session, Chapter 3 transferred 10% of these monies to the General Fund.

#### Local Transportation Assistance Fund (LTAF)

LTAF receives a maximum of \$23,000,000 annually. Funds are distributed to cities and towns. The uses include road building, traffic signals, sidewalk and alley repair, general maintenance, and Dial-a-Ride operating expenses. LTAF is estimated to receive \$20,700,000 in FY 2010 and \$23,000,000 FY 2011. The FY 2010 distribution would have been \$23,000,000, however, Laws 2009, 4<sup>th</sup> Special

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**Table 1**

**Forecast of Lottery Revenue Distribution**  
(\$ in Millions)

<b>Sales</b>	<b>FY 2009</b>	<b>FY 2010</b>	<b>FY 2011</b>
Instant Sales	\$278.9	\$320.5	\$345.8
On-Line Sales	<u>205.6</u>	<u>207.5</u>	<u>208.6</u>
Total Sales	\$484.5	\$528.0	\$554.4
<i>Less:</i>			
Operating Budget	\$ 73.8	\$ 78.5	\$ 81.2
Fund Transfer <sup>1/</sup>	12.2	9.8	0.5
Prizes <sup>2/</sup>	<u>284.7</u>	<u>313.0</u>	<u>330.7</u>
Net Profit <sup>3/</sup>	\$113.8	\$126.7	\$142.0
<b>Profit Transfers</b>			
General Fund <sup>4/</sup>	\$ 31.0	\$ 31.0	\$ 31.0
LTAI II <sup>5/</sup>	9.0	8.9	10.9
LTAI <sup>5/</sup>	21.8	20.7	23.0
CAF <sup>5/</sup>	7.3	6.9	7.7
Heritage	20.0	20.0	20.0
Health and Welfare Programs	20.9	22.2	22.4
Homeless Shelters	0	1.0	1.0
General Fund <sup>4/</sup>	0	10.9	15.5
University Capital	NA	0	5.0
General Fund <sup>4/</sup>	0	0	0.1
Economic Development <sup>6/</sup>	<u>3.8</u>	<u>5.1</u>	<u>5.4</u>
<b>Total Transfer</b>	\$113.8	\$126.7	\$142.0

<sup>1/</sup> Transfers in FY 2009 included a \$4,543,600 mandated fund transfer and \$84,900 due to a hiring freeze, as originally approved in the FY 2009 General Appropriation Act. This amount also includes the following transfers approved in the midyear FY 2009 revisions; a \$4,898,500 mandated fund transfer, \$690,600 due to a combined Fund Reduction and Transfer (FRAT) and a personnel expense reduction, and \$2,007,500 due to a 5% county proceeds transfer. The FY 2010 amount represents an advertising fund transfer of \$4,162,700, \$1,000,000 due to a combined FRAT and personnel expense reduction, \$4,055,000 due to a 10% county proceeds transfer, and an additional FRAT of \$528,400 as enacted by Laws 2009, 5<sup>th</sup> Special Session, Chapter 1.

<sup>2/</sup> Prizes are estimated by subtracting net profit and operating budget expenditures from total Lottery sales.

<sup>3/</sup> To derive the profit transfer amounts, the actual FY 2009 rate of return for each game was applied to the current forecast.

<sup>4/</sup> Total distributions to the General Fund totaled \$31,000,000 in FY 2009 and are estimated to be \$41,847,200 in FY 2010 and \$46,615,000 in FY 2011.

<sup>5/</sup> Distribution cumulatively reduced by \$(2,007,500) in FY 2009 and \$(4,055,000) in FY 2010.

<sup>6/</sup> Dedicated funding from 2 instant ticket games.

**County Assistance Fund (CAF)**

CAF receives a maximum of \$7,650,000 each fiscal year. The monies are distributed to the General Funds of each of the counties to be used at their discretion. CAF is estimated to receive \$6,885,000 in FY 2010 and \$7,650,000 in FY 2011. The FY 2010 distribution would have been \$7,650,000, however, Laws 2009, 4<sup>th</sup> Special

**Heritage Fund**

The Heritage Fund receives up to a maximum of \$20,000,000. Monies are divided equally between the Game and Fish Commission Heritage Fund and the State Parks Board Heritage Fund. The funds are used to promote wildlife habitat and education programs, rehabilitate historic buildings, acquire and develop park land, and renovate trail systems, among other purposes. The Heritage Fund is estimated to receive \$20,000,000 in both FY 2010 and FY 2011.

**Health and Welfare Programs**

Statute requires annual inflation adjustments for the Health and Welfare distribution. The allocation cap is \$22,234,800 in FY 2010 and \$22,472,300 in FY 2011. These amounts are distributed among the following agencies:

- 29.4% to the Department of Economic Security for the Healthy Families program.
- 23.5% to the Board of Regents for the Arizona Health Education Center program.
- 17.6% to the Department of Health Services (DHS) for teenage pregnancy prevention.
- 11.8% to the Arizona Biomedical Research Commission for Disease Control Research.
- 11.8% to DHS for the Health Start program.
- 5.9% to DHS for the Women, Infants and Children food program.

Health and Welfare Programs are expected to receive their entire allocation in both FY 2010 and FY 2011.

**Homeless Shelters**

The Department of Economic Security receives \$1,000,000 for Homeless Shelters. The department shall use the funding to distribute grants to nonprofit organizations, including faith based organizations, for homeless emergency and transitional shelters and related support services. They are estimated to receive \$1,000,000 in both FY 2010 and FY 2011.

**General Fund – Part 2**

As noted above, the General Fund could receive an additional \$15,490,000 after all prior allocations have been met. The General Fund is estimated to receive an additional \$10,847,200 in FY 2010 and \$15,490,000 in FY 2011.

**University Capital Improvement Fund**

The FY 2009 Education Budget Reconciliation Bill (BRB) (Laws 2008, Chapter 287) required that after all Lottery revenue beneficiaries have received their statutory distributions, up to a maximum of \$20,000,000 shall be deposited into the University Capital Improvement (UCI)

Fund in FY 2009. However, this fund received no monies in FY 2009.

This fund will serve as the source for 80% of the debt service associated with \$800,000,000 University Capital construction lease-purchase. UCI is expected to receive no monies in FY 2010 and \$5,028,600 FY 2011, which is 80% of the total debt service payment of \$6,285,700. (Please see the FY 2010 Arizona Board of Regents Capital Outlay section for more details.)

The FY 2010 Higher Education BRB (Laws 2009, 3<sup>rd</sup> Special Session, Chapter 9) restricts Lottery distributions in FY 2010 and FY 2011 into the UCI Fund by not allowing Lottery revenues to exceed 80% of the required annual debt service for \$167,671,200 of debt in both years.

Water Supply Development and Community Protection Initiative Funding

Laws 2008, Chapter 287, added the Department of Environmental Quality's Water Supply Development Fund and the State Land Department's Community Protection Initiative Fund as new recipients beginning in FY 2010. However, Laws 2009, 4<sup>th</sup> Special Session, Chapter 3 repealed both these funds from the list of recipients of Lottery monies in FY 2010.

General Fund – Part 3

The General Fund receives all remaining revenues after all statutory funding obligations have been met. In FY 2011, the General Fund is estimated to receive \$125,000.

Commerce and Economic Development (CEDC) Fund

Administered by the Arizona Department of Commerce, CEDC receives its funds from the sales of 2 Instant Scratchers games. The funds are used to support the state's community and economic development goals, initiatives, and strategic plans as defined and developed by the CEDC. CEDC is estimated to receive \$5,124,800 in FY 2010 and \$5,381,100 in FY 2011.

SUMMARY OF FUNDS	FY 2009 Actual	FY 2010 Estimate
<b>State Lottery Fund (LOA2122/A.R.S. § 5-521)</b>		<b>Partially-Appropriated</b>
<b>Source of Revenue:</b> Sales of lottery tickets, retailer license fees, and interest earnings.		
<b>Purpose of Fund:</b> A portion of the fund is appropriated to pay for all costs of the Arizona State Lottery Commission. After all expenses are paid including the prize monies displayed below in the Non-Appropriated Funds Expended line, Lottery profits are distributed to the General Fund, Local Transportation Assistance Fund II (Mass Transit), Local Transportation Assistance Fund, County Assistance Fund, Heritage Fund, Health and Welfare programs, Homeless Shelters, University Capital Improvement Lease-to-Own and Bond Fund, Water Supply Development Fund, Community Protection Initiative Fund, and the Economic Development Commission, revenues permitting. Laws 2009, 4th Special Session, Chapter 3 permanently repealed both the Water Supply Development Fund and the Community Protection Initiative Fund from the list of recipients of Lottery monies.		
<b>Appropriated Funds Expended</b>	73,767,300	78,473,700
<b>Non-Appropriated Funds Expended</b>	284,661,600	313,043,000
<b>Year-End Fund Balance</b>	24,639,200	24,675,100