

## Arizona State Lottery Commission

	FY 2012 ACTUAL	FY 2013 ESTIMATE	FY 2014 BASELINE
<b>OPERATING BUDGET</b>			
<i>Full Time Equivalent Positions</i>	104.0	97.8	97.8
Personal Services	4,242,700	4,617,300	4,617,300
Employee Related Expenditures	1,896,200	1,732,500	1,732,500
Professional and Outside Services	314,500	384,300	384,300
Travel - In State	219,700	269,800	269,800
Travel - Out of State	1,800	16,700	16,700
Other Operating Expenditures	810,800	1,156,600	1,156,600
Equipment	218,900	0	0
<b>OPERATING SUBTOTAL</b>	<b>7,704,600</b>	<b>8,177,200</b>	<b>8,177,200</b>
<b>SPECIAL LINE ITEMS</b>			
Advertising	14,354,400	15,500,000	15,500,000
Charitable Commissions	654,000	686,700	721,100
Instant Tickets	9,248,100	16,055,700	16,858,500
On-Line Vendor Fees	8,644,300	9,055,700	9,508,400
Retailer Commissions	43,708,100	46,049,500	48,352,000
<b>AGENCY TOTAL</b>	<b>84,313,500<sup>1/</sup></b>	<b>95,524,800<sup>2/</sup></b>	<b>99,117,200</b>
<b>FUND SOURCES</b>			
<u>Other Appropriated Funds</u>			
State Lottery Fund	84,313,500	95,524,800	99,117,200
SUBTOTAL - Other Appropriated Funds	84,313,500	95,524,800	99,117,200
<b>SUBTOTAL - Appropriated Funds</b>	<b>84,313,500</b>	<b>95,524,800</b>	<b>99,117,200</b>
Other Non-Appropriated Funds	400,641,900	423,334,100	450,653,200
<b>TOTAL - ALL SOURCES</b>	<b>484,955,400</b>	<b>518,858,900</b>	<b>549,770,400</b>

**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 multi-state Powerball and Mega-Millions on-line games.

### Operating Budget

The Baseline includes \$8,177,200 and 97.8 FTE Positions from the State Lottery Fund in FY 2014 for the operating budget. These amounts are unchanged from FY 2013.

### Advertising

The Baseline includes \$15,500,000 from the State Lottery Fund in FY 2014 for Advertising. This amount is unchanged from FY 2013.

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

### Charitable Commissions

The Baseline includes \$721,100 from the State Lottery Fund in FY 2014 for Charitable Commissions. FY 2014 adjustments would be as follows:

<b>Tab Ticket Increase</b>	<b>OF</b>	<b>FY 2014</b>
		<b>\$34,400</b>

The Baseline includes an increase of \$34,400 from the State Lottery Fund in FY 2014 to realign spending with projected revenues.

Monies in this line item are used to compensate charities for selling lottery 'Tab Tickets.' Laws 2010, Chapter 126 established a special type of instant ticket, Tab Tickets, to be sold exclusively by charitable organizations, who

<sup>1/</sup> Includes a total of \$228,800 OF appropriated in FY 2012 for costs associated with an additional pay period. These expenditures were not reflected in the individual agency tables in the *FY 2012 Appropriations Report*.

<sup>2/</sup> In addition to these amounts, the FY 2013 General Appropriation Act included one-time FY 2013 adjustments for a state employee health insurance premium holiday and employee retention payments. The adjustments include an increase of \$146,500 OF for the employee retention payment.

receive a 20% commission for selling the games. The displayed amount is derived by applying the approved percentage, 20%, to the forecasted Tab Ticket sales. A.R.S. § 5-555 also allows the department to collect up to 35% of total Tab Ticket sales for their operating budget and the department will distribute the remainder as prizes.

#### **Instant Tickets**

The Baseline includes \$16,858,500 from the State Lottery Fund in FY 2014 for Instant Tickets. FY 2014 adjustments would be as follows:

#### **Instant Ticket Sales Increase OF 802,800**

The Baseline includes an increase of \$802,800 from the State Lottery Fund in FY 2014 for Instant Tickets due to higher projected sales. (See Table 1 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 \$9,508,400 from the State Lottery Fund in FY 2014 for On-Line Vendor Fees. FY 2014 adjustments would be as follows:

#### **On-Line Vendor Fees Increase OF 452,700**

The Baseline includes an increase of \$452,700 from the State Lottery Fund in FY 2014 for On-Line Vendor Fees due to higher projected sales. (See Table 1 for more information.)

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, which is 3.7%.

#### **Retailer Commissions**

The Baseline includes \$48,352,000 from the State Lottery Fund in FY 2014 for Retailer Commissions. FY 2014 adjustments would be as follows:

#### **Retailer Commissions Increase OF 2,302,500**

The Baseline includes an increase of \$2,302,500 from the State Lottery Fund in FY 2014 for Retailer Commissions due to higher projected sales. (See Table 1 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 non-Tab Ticket sales. Pursuant to statute, an additional 0.5% of total non-Tab 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.

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

#### **FOOTNOTES**

##### *Standard Footnotes*

An amount equal to 20% of tab ticket sales is appropriated for payment of sales commissions to charitable organizations. This amount is currently estimated to be \$721,100 in FY 2014.

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 \$16,858,500 in FY 2014.

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 \$9,508,400, or 3.7% of actual on-line ticket sales in FY 2014.

An amount equal to 6.5% of gross lottery game sales, less Tab Tickets, 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 \$48,352,000 in FY 2014.

#### **OTHER ISSUES FOR LEGISLATIVE CONSIDERATION**

##### *Lottery Forecast*

The JLBC Staff forecasts a 6.8% increase in overall Lottery ticket sales in FY 2013, followed by a 6% increase in FY 2014. For FY 2013 and FY 2014, the JLBC Staff forecasts Lottery ticket sales of \$690,740,100 and \$731,902,400, respectively.

##### *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 2012 and the JLBC Staff projected distributions for FY 2013 and FY 2014. A brief description of each beneficiary follows in the order that they receive Lottery-generated revenue in accordance with A.R.S. § 5-534 and 5-572.

### State Lottery Revenue Bond Debt Service Payment Fund

Laws 2010, 6th Special Session, Chapter 4 authorized the Arizona Department of Administration (ADOA) to issue a 20-year, \$450,000,000 Lottery revenue bond by December 31, 2010 to be deposited into the General Fund. The payments are made from Lottery revenues that would have otherwise been deposited into the General Fund. The FY 2012 bond payment was \$20,709,600, which was interest only. The principal and interest payments in FY 2013 and FY 2014 are expected to be \$37,499,600 and \$37,499,800, respectively. Chapter 4 requires the first Lottery proceeds to be distributed to the State Lottery Revenue Bond Debt Service Payment Fund.

### Maricopa County Mass Transit

The projected annual distribution of Powerball proceeds to the Maricopa Public Transportation Fund is \$12,040,000 in FY 2013 and \$12,642,000 in FY 2014.

Laws 1993, 6th Special Session, Chapter 1 allocated not less than 31.5% of multi-state Powerball revenues to public transportation programs, otherwise known as Local Transportation Assistance Fund (LTAF) II. This allocation was capped at \$18,000,000 and was contingent upon the General Fund receiving \$45,000,000 in Lottery revenues.

Laws 2010, 7<sup>th</sup> Special Session, Chapter 12 redirected these monies to the General Fund. In September 2011, the U.S. District Court in the case of *Paisley v. Darwin* ruled that the Arizona Legislature must restore the distribution of mass transit monies to Maricopa County because the distribution was part of the state implementation plan to ensure compliance with the Clean Air Act. As a result, the state must calculate Maricopa County's share of 31.5% of statewide Powerball proceeds and distribute those monies to the county.

### General Fund - Part 1

The statutory distribution requires the General Fund to receive up to \$84,150,000. The General Fund - Part 2 would receive up to an additional \$15,490,000 (for a total of \$99,640,000) after the statutory funding obligations have been met through the Homeless Shelters distribution. After all other statutory obligations have been met, the General Fund - Part 3 would receive all remaining revenues.

The profit distributions in FY 2013 and FY 2014 are forecasted to fulfill requirements for General Fund - Part 1 and Part 2. The Lottery revenue bond payments of \$37,499,600 in FY 2013 and \$37,499,800 in FY 2014 count towards the \$84,150,000 General Fund - Part 1 requirement. Total General Fund distributions, net of bond payments, are therefore projected to be \$73,671,900 in FY 2013 and \$77,829,900 in FY 2014.

### Heritage Fund

Statute caps annual distributions to the Arizona Game and Fish Commission's Heritage Fund at \$10,000,000. The funds are used to promote wildlife habitat and education programs and to rehabilitate historic buildings. In FY 2013 and FY 2014, the fund is projected to receive its entire allocation.

### Health and Welfare Programs

Statute requires annual inflation adjustments for the Health and Welfare distribution. The revised allocation cap is \$20,539,000 in FY 2013 and \$20,829,100 in FY 2014. These amounts are distributed among the following agencies:

- 29.4% to the Department of Economic Security (DES) for the Healthy Families program.
- 23.5% to the Arizona Board of Regents (ABOR) for the Arizona Health Education Center program.
- 17.6% to the Department of Health Services (DHS) for teenage pregnancy prevention.
- 11.8% to DHS 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 2013 and FY 2014.

### Homeless Shelters

Under the statutory distribution, DES would receive up to \$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. The fund is estimated to receive its full allocation in both FY 2013 and FY 2014.

### General Fund - Part 2

As noted above, the General Fund would receive up to an additional \$15,490,000 after all prior allocations have been met. In FY 2013 and FY 2014, the General Fund is estimated to receive its entire allocation of \$15,490,000.

### Arizona Competes Fund

Statute caps annual distributions to the Arizona Competes Fund at \$3,500,000. Allotments to this fund are used for administering grants to qualifying businesses for the purpose of attracting, retaining, and expanding business within the state. This fund is estimated to receive its full allocation in both FY 2013 and FY 2014.

### University Capital Improvement Fund

This fund serves as the source for up to 80% of the annual debt service associated with \$800,000,000 of University Capital construction lease-purchase agreements. This fund received \$10,298,500 in FY 2012, which was 80% of the annual debt service payments on the \$316,590,000 of lease-purchase agreements that have been issued to date.

The UCI Fund is expected to require \$13,330,600 in FY 2013 and \$18,531,200 in FY 2014 to make the expected level of debt service payments. The FY 2014 estimate includes debt service payments on \$524,533,000 of lease-purchase agreements that have already been or will be issued by the end of FY 2014. Once the full \$800,000,000 has been issued, debt service payments could total \$41,632,800, depending on assumptions of repayment lengths and interest rates. *(Please see the FY 2014 ABOR Capital Outlay section for more details.)*

#### General Fund - Part 3

The General Fund receives all remaining revenues after all statutory funding obligations have been met. These payments to the General Fund are expected to equal \$11,531,500 in FY 2013 and \$15,689,700 in FY 2014.

#### ***Additional Staff***

The Legislature may want to consider the Lottery Commission's FY 2014 request for additional staff to enhance sales. The Legislature could either appropriate this additional funding (\$284,800 and 4 FTE Positions from the State Lottery Fund) or require the State Lottery Commission to reallocate resources within its existing funding base. Of the total request, \$71,400 would be one-time costs for equipping new staff.

#### Sales Representatives

Of the Lottery request, \$233,300 and 3 FTE Positions would fund an additional 3 Sales Representatives. Of this amount, \$69,900 would be one-time costs for vehicles and field equipment used in the positions. These representatives would assist Lottery in maintaining service levels for training and resupplying vendors as Lottery sales increase. From FY 2006 to FY 2012, the amount of vendor accounts served per representative grew 15% (from 144 to 166 accounts per representative) and currently exceeds the average of all other lotteries in the nation by 46% (166 compared to the national average of 114 accounts).

#### Product Development Assistant

Another \$51,500 and 1 FTE Position would fund a new Product Development Assistant. Of this amount, \$1,500 would be one-time costs for office equipment. This FTE Position would assist the Lottery in maintaining service levels in developing new instant ticket games. From FY 2006 to FY 2012, the amount of instant ticket games the Lottery introduced per year grew 42% (from 45 to 65 games per year) and currently exceeds the average of all other lotteries in the nation by 23% (64 compared to the national average of 52 games). The position would also relieve staff from other agency departments from needing to assist in product development on an ad-hoc basis.

<b>Table 1</b>			
<b>Forecast of Lottery Revenue Distribution</b>			
<b>(\$ in Millions)</b>			
<b>Sales</b>	<b>FY 2012</b>	<b>FY 2013</b>	<b>FY 2014</b>
Instant Sales	\$413.1	\$446.0	\$481.6
On-Line Sales	<u>233.6</u>	<u>244.7</u>	<u>250.3</u>
Total Sales	\$646.7	\$690.7	\$731.9
<i>Less:</i>			
Operating Budget <sup>1/</sup>	\$ 84.3	\$ 95.5	\$ 99.1
Fund Transfers <sup>2/</sup>	1.9	0.0	0.0
Gaming Distribution	0.3	0.3	0.3
Prizes <sup>3/</sup>	<u>400.6</u>	<u>423.3</u>	<u>450.7</u>
<b>Net Profit <sup>4/</sup></b>	<b>\$159.6</b>	<b>\$171.6</b>	<b>\$181.8</b>
<b>Profit Transfers</b>			
Debt Service Fund	\$ 20.7	\$ 37.5	\$ 37.5
Maricopa County Mass Transit <sup>5/</sup>	11.2	12.0	12.6
General Fund - Part 1 <sup>6/</sup>	59.9	46.7	46.7
Heritage	10.0	10.0	10.0
Health and Welfare Programs	19.3	20.5	20.8
Homeless Shelters	1.0	1.0	1.0
General Fund - Part 2 <sup>6/</sup>	15.5	15.5	15.5
Arizona Commerce Authority <sup>7/</sup>	3.5	3.5	3.5
University Capital	10.3	13.3	18.5
General Fund - Part 3 <sup>6/</sup>	<u>8.2</u>	<u>11.6</u>	<u>15.7</u>
<b>Total Transfer</b>	<b>\$159.6</b>	<b>\$171.6</b>	<b>\$181.8</b>
<p><sup>1/</sup> Of this amount, an estimated \$686,700 in FY 2013 and an estimated \$721,100 in FY 2014 will be distributed to charities.</p> <p><sup>2/</sup> In FY 2012, there was a \$1,352,400 continued Fund Reduction Transfer and a \$509,400 pay/benefit reduction.</p> <p><sup>3/</sup> Prizes are estimated by subtracting net profit and operating budget expenditures from total Lottery sales.</p> <p><sup>4/</sup> To derive the profit transfer amounts, the actual FY 2012 rate of return for each game was applied to the current Baseline forecast. The cumulative profit transfer rate is 25.01%.</p> <p><sup>5/</sup> As a result of a federal court order, Maricopa County's share of Local Transportation Assistance Fund II monies was reinstated starting September 2011. (See <i>Lottery Forecast and Distributions for more information.</i>)</p> <p><sup>6/</sup> Excluding fund transfers, distributions to the General Fund totaled \$83,578,300 in FY 2012 and are estimated to be \$73,671,900 in FY 2013 and \$77,829,900 in FY 2014.</p> <p><sup>7/</sup> Laws 2012, Chapter 297 moved the Arizona Competes Fund distribution from the before General Fund – Part 1 to after General Fund – Part 2, beginning in FY 2013.</p>			

<b>SUMMARY OF FUNDS</b>	<b>FY 2012 Actual</b>	<b>FY 2013 Estimate</b>
<b>State Lottery Fund (LOA2122/A.R.S. § 5-571)</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 a number of different functions.		
<b>Appropriated Funds Expended</b>	84,313,500	95,524,800
<b>Non-Appropriated Funds Expended</b>	400,641,900	423,334,100
<b>Year-End Fund Balance</b>	3,612,300	3,043,000