

Redbook

LBO Analysis of Executive Budget Proposal

Ohio Lottery Commission

Jean J. Botomogno, Principal Economist
April 2019

TABLE OF CONTENTS

Quick look	1
Agency overview	1
Analysis of FY 2020-FY 2021 budget proposal	1
Summary of executive recommendations.....	1
Operating Expenses (ALI 950321) and Problem Gambling (ALI 950605)	2
Direct Prize Payments (ALI 950601) and Annuity Prizes (ALI 950602)	3
Advertising (ALI 950402) and Gaming Contracts (ALI 950403)	4
Lottery sales, profits, and transfers to education	5
Traditional lottery sales	5
Video lottery terminals	6
Transfers to education	6

Attachment:

Appropriation Spreadsheet

LBO Redbook

Ohio Lottery Commission

Quick look...

- The Ohio Lottery is a self-sustaining non-GRF agency funded through the State Lottery Fund.
- The agency is supported by the sale of traditional lottery tickets and revenue from video lottery terminals (VLTs) at seven Ohio horse racetracks (or racinos).
- Net profits from those operations are transferred to the Lottery Profits Education Fund (LPEF) for use in programs benefiting primary, secondary, vocational, and special education.
- The Ohio Lottery is governed by a nine-member commission. Daily administration is the responsibility of an executive director appointed by the Governor.
- The Ohio Lottery had a full-time staff of 356 in FY 2018.

Fund Group	FY 2018 Actual	FY 2019 Estimate	FY 2020 Introduced	FY 2021 Introduced
State Lottery Fund Group	\$454,077,856	\$367,838,398	\$374,225,454	\$379,653,052
% change	--	-19.0%	1.7%	1.5%

Agency overview

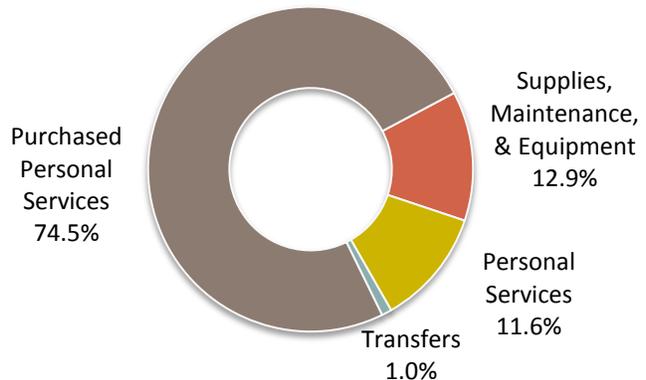
The executive budget proposes transfers of \$2,303.0 million in the next biennium (\$1,126.0 million in FY 2020 and \$1,177.0 million in FY 2021) to the LPEF (Fund 7017). This recommendation would be an increase of \$37.4 million (1.7%) relative to total transfers of \$1,172.0 million in FY 2018, and budgeted transfers of \$1,093.6 million for FY 2019 (H.B. 49 of the 132nd General Assembly).

Analysis of FY 2020-FY 2021 budget proposal

Summary of executive recommendations

The Ohio Lottery Commission's (LOT) budget consists of six appropriation line items (ALIs) made from the State Lottery Fund (SLF) group. The executive budget recommendations total \$374.2 million in FY 2020 and \$379.7 million in FY 2021. Chart 1 summarizes the executive recommendations for the biennium by expense category.

**Chart 1: LOT Budget by Expense Category
FY 2020-FY 2021 Biennium**



LOT appropriations support the computerized gaming systems, the purchase and distribution of Instant tickets, the payment of prizes to winners, funding for programs supporting gambling and related addiction services, and expenditures for the regulation of the VLT Program. Table 1 below provides the agency's staffing level in recent years.

Office	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019
Communications	6	7	7	7	6
Executive	2	2	2	2	1
Finance	20	22	22	22	22
General Services	17	18	19	16	21
Human Resources	8	7	7	7	7
Information Technology	41	44	44	43	41
Internal Audit	4	4	4	4	4
Legal Counsel	4	5	5	6	6
Marketing	6	5	5	7	7
Sales	153	156	159	158	158
Security	15	16	16	16	16
Operations Management	8	8	7	7	8
Government & Community Relations	2	1	2	3	2
VLT Management	60	59	55	58	58
Total	346	354	354	356	357

*Excludes part-time, LOT Commissioners, and interns.

Operating Expenses (ALI 950321) and Problem Gambling (ALI 950605)

FY 2016 Actual	FY 2017 Actual	FY 2018 Actual	FY 2019 Estimate	FY 2020 Introduced	FY 2021 Introduced
Fund 7044 ALI 950321, Operating Expenses					
\$46,439,848	\$49,043,723	\$46,845,178	\$50,371,246	\$59,850,383	\$60,544,470
% change	5.6%	-4.5%	7.5%	18.8%	1.2%
Fund 7044 ALI 950605, Problem Gambling					
\$3,125,311	\$2,573,524	\$2,952,309	\$3,200,000	\$3,400,000	\$3,400,000
% change	-17.7%	14.7%	8.4%	6.3%	0.0%

ALI 950321, Operating Expenses, provides funds for staff payroll and benefits, maintenance and supplies, and equipment. Most of the expenses are for staff compensation. The recommended appropriation in FY 2020 is \$9.5 million above estimated spending in FY 2019. Costs are expected to rise for items funded by this line item in FY 2020, due mainly to raises in compensation of staff. The recommended appropriation for FY 2021 is \$0.7 million above FY 2020 recommended funding.

ALI 950605, Problem Gambling, is funded by a share of commissions (0.5%) received by Lottery sales agents operating VLTs at racinos (R.C. 3769.087). This line item funds expenditures related to problem gambling identification and treatment programs, and supports the Ohio for Responsible Gambling initiative. Recommended appropriation in each year of the biennium is \$3.4 million, \$0.2 million above expected FY 2019 spending. The Ohio Lottery has outsourced the responsibility of providing treatment and counseling services for gamblers to the Ohio Department of Mental Health and Addiction Services by providing funds for the treatment of lottery players that also are addicted to alcohol and drugs. The goal is generally to establish outpatient gambling treatment programs, increase the identification and referral of problem gamblers to appropriate services, and to increase awareness of available services for problem gamblers and their families.

Direct Prize Payments (ALI 950601) and Annuity Prizes (ALI 950602)

FY 2016 Actual	FY 2017 Actual	FY 2018 Actual	FY 2019 Estimate	FY 2020 Introduced	FY 2021 Introduced
Fund 7044 ALI 950601, Direct Prize Payments					
\$274,655,574	\$168,372,356	\$237,777,568	\$143,776,792	\$154,333,000	\$157,440,000
% change	-38.7%	41.2%	-39.5%	7.3%	2.0%
Fund 8710 ALI 950602, Annuity Prizes					
\$82,051,215	\$75,376,988	\$71,906,369	\$75,000,000	\$59,873,000	\$60,279,000
% change	-8.1%	-4.6%	4.3%	-20.2%	0.7%

ALI 950601, Direct Prize Payments, funds bonuses and commissions to vendors and payments for all nondeferred major prizes won by players. The major sources of expenditures from this line item are cash options for large jackpots in games such as Classic Lotto, Powerball, and Mega Millions; first installments of deferred Powerball and Mega Millions prizes; and prize payments of high-tier winners of other On-line games. Expenditures supported by direct prize payments appropriations may also include cash payouts from Instant games, and noncash prizes payouts to winners. Though appropriation amounts are specified in the budget bill for this line item, uncodified language in the bill appropriates additional amounts if the Director of the Ohio Lottery Commission determines that additional amounts are needed to pay out prize winnings. FY 2019 estimated spending for direct prize payments is \$94.0 million below that of FY 2018 (which experienced record Powerball and Mega Millions sales). Spending for direct prize payments is to rise by \$10.6 million in FY 2020. The recommended appropriation for

FY 2021 is \$3.1 million above that of FY 2020. LOT expects increases in sales in the next two years.

Appropriations for ALI 950602, Annuity Prizes, support the annual payment for the annuity prize winnings for winners who selected to be paid over a period of time rather than in one lump sum payment. The Ohio Lottery is required to set aside and transfer to the Treasurer of State, for investment, any annuity jackpots won in Mega Millions, Powerball, and other games. Prizes are then paid out over time as they are due to winners. Though appropriation amounts are specified in the budget bill for this line item, uncodified language in the bill appropriates additional amounts if the Director of the Ohio Lottery Commission determines that additional amounts are needed to pay out prize winnings. The recommended appropriation for FY 2020 is \$15.1 million below FY 2019 estimated spending. The executive recommendation in FY 2021 is an increase of \$0.4 million from that of the previous year. Appropriations related to annuity prizes have generally decreased, as an increasing number of players over the years have chosen the cash option after winning large prizes.

Advertising (ALI 950402) and Gaming Contracts (ALI 950403)

FY 2016 Actual	FY 2017 Actual	FY 2018 Actual	FY 2019 Estimate	FY 2020 Introduced	FY 2021 Introduced
Fund 7044 ALI 950402, Advertising Contracts					
\$24,362,873	\$25,731,325	\$24,395,404	\$27,075,000	\$26,750,000	\$26,750,000
% change	5.6%	-5.2%	11.0%	-1.2%	0.0%
Fund 7044 ALI 950403, Gaming Contracts					
\$61,628,415	\$78,015,884	\$70,201,028	\$68,415,360	\$70,019,071	\$71,239,582
% change	26.6%	-10.0%	-2.5%	2.3%	1.7%

LOT spending for advertising expenses covers the production of print, radio, Internet, and television advertisements and the cost of post-production media placement of those advertisements. The recommended appropriation for FY 2020 is \$0.3 million below FY 2019 estimated spending. No appropriation increase is recommended in FY 2021.

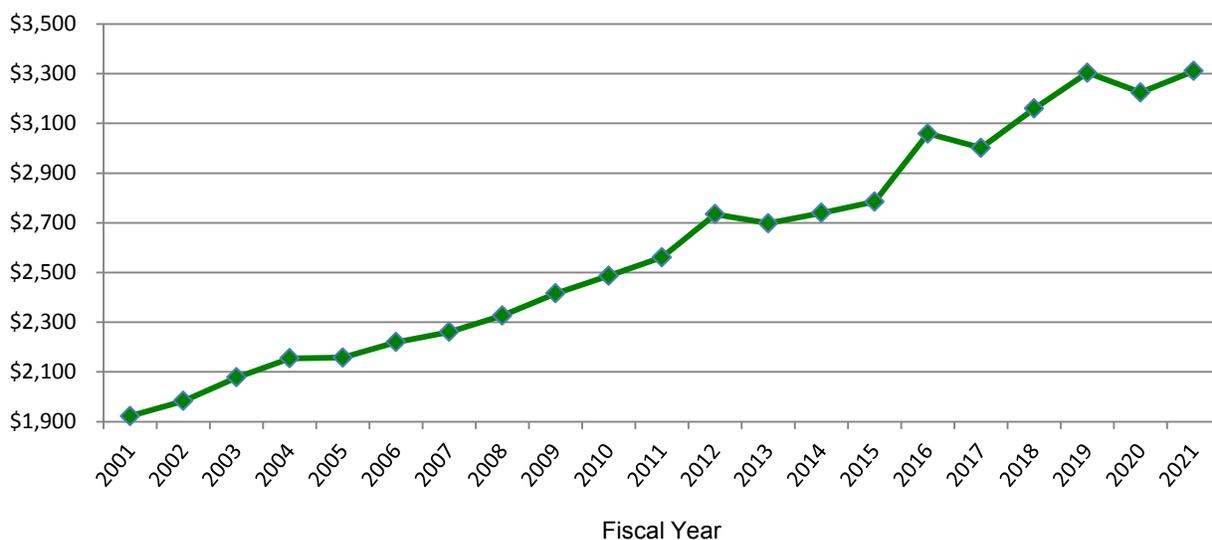
Spending on gaming contracts is directly related to the level of sales, which are expected to rise in the biennium. Funding within this line item also accounts for additional gaming equipment necessary to support the retailer base. The executive recommends an increase of \$1.6 million for this appropriation item in FY 2020. The recommended spending for FY 2021 is \$1.2 million higher than in FY 2020. High jackpots of multi-state games (Powerball and Mega Millions) generally boost gaming contracts spending.

Lottery sales, profits, and transfers to education

Traditional lottery sales

The Ohio Lottery operates a variety of draw games¹ and Instant ticket games at more than 9,800 retailers. The draw games are Pick 3, Pick 4, Pick 5, Rolling Cash 5, Classic Lotto, Raffle, Kicker, Keno, EZ Play, EZ Play Tap, EZ Play Quick Keno, Lucky for Life, Powerball, and Mega Millions. Occasionally, LOT offers raffle games. The traditional lottery ticket sales have exceeded \$3.0 billion since FY 2016, and were a record \$3.16 billion in FY 2018; that year saw record Mega Millions and Powerball sales. Draw games provided \$1.56 billion (49.4%) of the total. Instant games sales, including special theme games that coincide with major holidays or events, were \$1.60 billion (50.6%) of revenue in FY 2018. Traditional lottery ticket sales have experienced solid growth over the years. The rise in receipts is due to the introduction of new On-line games, including multi-state games, additional drawings for existing games, and new Instant games. The graph below shows annual sales from traditional ticket sales from FY 2001 to FY 2018 and estimated sales in FY 2019. Sales are expected to exceed \$3.20 billion per year in the FY 2020-FY 2021 biennium.

Chart 2: Annual Traditional Lottery Sales
(\$ in millions)



Ticket sales for “mature” lotteries such as the Ohio Lottery are usually flat or decline, unless new games are introduced, changes to existing games are made, or increases in the number of drawings boost sales. Although incomes continue to grow, attitudes toward gaming remain generally favorable, and total gaming expenditures increase, the increased competition in the gaming market limits the upside potential of Lottery ticket sales. Regular and riverboat

¹ These On-line games are played via a terminal at a Lottery sales agent. Those terminals are linked to Ohio Lottery headquarters computers. “On-line” games in this report do not refer to Internet lottery sales.

casinos, racetrack video lottery terminals, Internet-based gaming, and charitable gaming have all contributed to limit the growth of traditional ticket sales.

Video lottery terminals

The VLT Program at horse racetracks has operated at seven Ohio racinos since September 2014. Table 2 below provides wagered amounts, VLT income, and revenue to the Racing Commission (for distribution to racino owners), LOT, and for problem gambling services in recent years. Revenue from the VLT Program is shared by the racetrack owners (66.5%) and LOT (33.5%). The yield of the VLT Program in FY 2018 was \$987.3 million (after payout to players) on total wagers of \$10.78 billion. Of that amount, LOT received \$330.7 million, of which \$293.0 million was transferred to the LPEF (Fund 7017). The Racing Commission received \$653.3 million, the substantial majority of which was distributed to racino owners, and \$3.3 million in revenue was directed toward problem gambling services.

Fiscal Year	Wagers	Gross Revenue	Number of VLTs	Daily Income per VLT	Racing Commission	Lottery Commission	Problem Gambling
FY 2016	\$9,472.9	\$868.9	10,587	\$224	\$574.9	\$291.1	\$2.9
FY 2017	\$10,201.3	\$926.6	10,963	\$232	\$613.1	\$310.4	\$3.1
FY 2018	\$10,780.2	\$987.3	11,207	\$242	\$653.3	\$330.7	\$3.3

LOT forecasts VLT gross revenue of about \$1.01 billion in FY 2019, \$1.06 billion in FY 2020, and \$1.07 billion in FY 2021. Those amounts imply wagers would exceed \$11.0 billion this year and in each year of the next biennium.

Transfers to education

The executive budget is recommending transfers to the LPEF of \$1,126.0 million in FY 2020 and \$1,177.0 million in FY 2021. This recommendation would be an increase of \$37.4 million (1.7%) relative to total transfers of \$1,172.0 million in FY 2018, and budgeted transfers of \$1,093.6 million for FY 2019 (H.B. 49 of the 132nd General Assembly).²

Table 3 below provides actual transfers in FY 2018, estimated transfers in FY 2019, and budgeted transfers in FY 2020 and FY 2021. FY 2018 transfers were provided by the Office of Budget and Management (OBM). Estimated transfers for FY 2019 were provided by the Ohio Lottery Commission. Budgeted transfers in the biennium are specified in H.B. 166, the executive budget bill.

² However, total transfers in FY 2019 are likely to be higher than the budgeted transfer amount. Assuming FY 2019 potential transfers of \$1,143.0 million as provided by LOT, total transfers in the FY 2020-FY 2021 biennium would be \$12.0 million below transfers in the current biennium.

Table 3. Actual and Estimated Transfers to LPEF, FY 2018-FY 2021 (\$ in millions)				
	FY 2018	FY 2019 Estimated	FY 2020	FY 2021
Traditional Lottery Profits	\$879.0	\$801.0	\$779.7	\$827.6
VLT Profits	\$293.0	\$342.0	\$346.3	\$349.4
Total Transfers	\$1,172.0	\$1,143.0	\$1,126.0	\$1,177.0

An accounting change resulted in an outsized profit transfer in FY 2018. OBM, in June 2018, made an additional transfer of \$65 million in profits from traditional lottery games which represented profits earned in June. Historically, June profits included traditional lottery games and VLT revenues, some of which were transferred in July. OBM stated that this accounting change was initiated to better align LOT financial statements to the state's Comprehensive Annual Financial Report.

FY 2020 - FY 2021 Appropriations - As Introduced

All Fund Groups

Line Item Detail by Agency			Estimate	Introduced	FY 2019 to FY 2020	Introduced	FY 2020 to FY 2021	
			FY 2018	FY 2019	FY 2020	% Change	FY 2021	% Change
Report For: Main Operating Appropriations Bill			Version: As Introduced					
LOT	Ohio Lottery Commission							
7044	950321	Operating Expenses	\$ 46,845,178	\$ 50,371,246	\$ 59,850,383	18.82%	\$ 60,544,470	1.16%
7044	950402	Advertising Contracts	\$ 24,395,404	\$ 27,075,000	\$ 26,750,000	-1.20%	\$ 26,750,000	0.00%
7044	950403	Gaming Contracts	\$ 70,201,028	\$ 68,415,360	\$ 70,019,071	2.34%	\$ 71,239,582	1.74%
7044	950601	Direct Prize Payments	\$ 237,777,568	\$ 143,776,792	\$ 154,333,000	7.34%	\$ 157,440,000	2.01%
7044	950605	Problem Gambling	\$ 2,952,309	\$ 3,200,000	\$ 3,400,000	6.25%	\$ 3,400,000	0.00%
8710	950602	Annuity Prizes	\$ 71,906,369	\$ 75,000,000	\$ 59,873,000	-20.17%	\$ 60,279,000	0.68%
State Lottery Fund Group Total			\$ 454,077,856	\$ 367,838,398	\$ 374,225,454	1.74%	\$ 379,653,052	1.45%
Ohio Lottery Commission Total			\$ 454,077,856	\$ 367,838,398	\$ 374,225,454	1.74%	\$ 379,653,052	1.45%