Arizona State Lottery Commission

	FY 2016 ACTUAL	FY 2017 ESTIMATE	FY 2018 BASELINE
OPERATING BUDGET			
Full Time Equivalent Positions	98.8	98.8	98.8
Personal Services	3,765,800	4,812,000	4,812,000
Employee Related Expenditures	1,584,400	1,693,300	1,693,300
Professional and Outside Services	423,700	386,800	386,800
Travel - In State	241,400	271,600	271,600
Travel - Out of State	19,500	16,800	16,800
Other Operating Expenditures	853,000	1,173,200	1,173,200
Equipment	33,300	0	0
OPERATING SUBTOTAL	**6,921,100**	**8,353,700**	**8,353,700**
SPECIAL LINE ITEMS			
Advertising	9,743,600	15,500,000	15,500,000
Charitable Commissions	1,157,200	1,335,200	1,468,700
Instant Tickets	13,317,600	22,143,800	23,481,900
On-Line Vendor Fees	9,343,300	9,625,400	10,019,000
Retailer Commissions	57,025,600	56,267,000	59,080,300
AGENCY TOTAL	**97,508,400**	**113,225,100**	**117,903,600**
FUND SOURCES			
Other Appropriated Funds			
State Lottery Fund	97,508,400	113,225,100	117,903,600
SUBTOTAL - Other Appropriated Funds	97,508,400	113,225,100	117,903,600
SUBTOTAL - Appropriated Funds	**97,508,400**	**113,225,100**	**117,903,600**
Other Non-Appropriated Funds	571,668,100	539,847,400	567,528,900
TOTAL - ALL SOURCES	669,176,500	653,072,500	685,432,500

AGENCY DESCRIPTION — The Arizona Lottery is responsible for administering sanctioned games of chance. In addition to Arizona-specific games, the state also participates in multi-state Powerball and Mega-Millions on-line games.

Operating Budget

The Baseline includes $8,353,700 and 98.8 FTE Positions from the State Lottery Fund in FY 2018 for the operating budget. These amounts are unchanged from FY 2017.

Advertising

The Baseline includes $15,500,000 from the State Lottery Fund in FY 2018 for Advertising. This amount is unchanged from FY 2017.

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

Charitable Commissions

The Baseline includes $1,468,700 from the State Lottery Fund in FY 2018 for Charitable Commissions. FY 2018 adjustments would be as follows:

		FY 2018
Tab Ticket Increase	**OF**	**$133,500**

The Baseline includes an increase of $133,500 from the State Lottery Fund in FY 2018 to realign spending with projected revenues. *(See Table 1 for more information.)*

Monies in this line item are used to compensate charities for selling lottery 'Tab Tickets.' Tab Tickets are games sold exclusively by charitable organizations, who 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 (which includes the 20% commission) for their operating budget, with the remainder distributed as prizes.

Instant Tickets

The Baseline includes $23,481,900 from the State Lottery Fund in FY 2018 for Instant Tickets. FY 2018 adjustments would be as follows:

Instant Ticket Sales Increase OF 1,338,100
The Baseline includes an increase of $1,338,100 from the State Lottery Fund in FY 2018 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 $10,019,000 from the State Lottery Fund in FY 2018 for On-Line Vendor Fees. FY 2018 adjustments would be as follows:

On-Line Sales Increase OF 393,600
The Baseline includes an increase of $393,600 from the State Lottery Fund in FY 2018 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 4.256% as of September 2016. Under the previous contract agreement the percentage was 3.7%.

Retailer Commissions

The Baseline includes $59,080,300 from the State Lottery Fund in FY 2018 for Retailer Commissions. FY 2018 adjustments would be as follows:

Retailer Commissions Increase OF 2,813,300
The Baseline includes an increase of $2,813,300 from the State Lottery Fund in FY 2018 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. A.R.S. § 5-555 specifies that compensation to retailers will be at least 5.5% but not more than 8% of non-Tab Ticket sales. The actual appropriation is equal to 6.5% of these 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 $1,468,700 in FY 2018.

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 $23,481,900 in FY 2018.

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 $10,019,000, or 4.256% of actual on-line ticket sales in FY 2018.

An amount equal to 6.5% of gross lottery game sales, minus Tab Tickets, is appropriated for payment of sales commissions to ticket retailers. An additional amount 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 $59,080,300 in FY 2018.

Other Issues

Lottery Forecast and Distributions

The Baseline assumes a (2.9)% decrease in overall Lottery ticket sales in FY 2017, followed by a 4.9% increase in FY 2018. For FY 2017 and FY 2018, the Baseline assumes

Lottery ticket sales of $846,481,700 and $887,685,400, 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 2016 and the JLBC Staff projected distributions for FY 2017 and FY 2018. 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

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 principal and interest payments in FY 2017 and FY 2018 are expected to be $37,501,500 and $37,500,800, 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 $11,502,000 in each FY 2017 and FY 2018.

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, 7th 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 2017 and FY 2018 are forecasted to fulfill requirements for General Fund - Part 1 and Part 2. The Lottery revenue bond payments of $37,501,500 in FY 2017 and $37,500,800 in FY 2018 count towards the $84,150,000 General Fund - Part 1 requirement.

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 2017 and FY 2018, 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 $20,917,600 in FY 2017 and $21,352,400 in FY 2018. These amounts are distributed among the following agencies:

- 29.4% to the Department of Child Safety 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 2017 and FY 2018.

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 2017 and FY 2018.

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 2017 and FY 2018, 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 2017 and FY 2018.

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 $38,647,500 in FY 2016. The UCI Fund is expected to require $39,927,000 in FY 2017 and $39,923,200 in FY 2018 to make the expected 80% level of debt service payments. The Universities do not plan to issue any additional lease-purchase agreements in FY 2018 above the $668,710,000 of lease-purchase agreements that have already been or will be issued by the end of FY 2017. Once the full $800,000,000 has been issued, debt service payments could total $41,632,900, depending on assumptions of repayment lengths and interest rates. *(Please see the FY 2017 Arizona Board of Regents 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 estimated to equal $6,622,800 in FY 2017 and $15,035,200 in FY 2018. Total General Fund distributions, net of bond payments, are therefore estimated to be $68,761,300 in FY 2017 and $77,174,400 in FY 2018.

Table 1

Forecast of Lottery Revenue Distribution
($ in Millions)

Sales	**FY 2016**	**FY 2017**	**FY 2018**
Instant Sales	$596.8	$615.1	$652.3
On-Line Sales	274.1	231.3	235.4
Total Sales	$870.9	$846.4	$887.7
Less:			
Operating Budget 1/	$ 97.5	$ 113.2	$ 117.9
Gaming Distribution	0.3	0.3	0.3
Prizes 2/	571.7	539.8	567.5
Net Profit 3/	**$201.4**	**$193.1**	**$202.0**
Profit Transfers 4/			
Debt Service Fund	$ 37.5	$ 37.5	$ 37.5
Maricopa County Mass Transit 5/	11.5	11.5	11.5
General Fund - Part 1 6/	46.7	46.7	46.7
Heritage	10.0	10.0	10.0
Health and Welfare Programs	20.5	20.9	21.4
Homeless Shelters	1.0	1.0	1.0
General Fund - Part 2 6/	15.5	15.5	15.5
Arizona Commerce Authority	3.5	3.5	3.5
University Capital	38.6	39.9	39.9
General Fund - Part 3 6/ 7/	16.6	6.6	15.0
Total Transfer	**$201.4**	**$193.1**	**$202.0**

1/ Of this amount, an estimated $1,335,200 in FY 2017 and an estimated $1,468,700 in FY 2018 will be distributed as commissions to charities that sell lottery Tab Tickets.

2/ Prizes are estimated by subtracting net profit, operating budget expenditures, and the Department of Gaming transfer from total Lottery sales.

3/ To derive the profit transfer amounts, the actual FY 2016 rate of return for each game was applied to the current Baseline forecast. The total rate of rate turn on all games in FY 2016 was 23.17%. The estimated total profit margin is 22.85% in FY 2017 and 22.78% in FY 2018.

4/ In addition to these listed transfers, the following monies are distributed:
- $900,000 and $100,000 from vending machine sales in age-restricted areas to the Internet Crimes Against Children Enforcement Fund and the Victims' Rights Enforcement Fund, respectively.
- 30% of unclaimed prizes to the Court Appointed Special Advocates program.
- 15% of unclaimed prizes, not to exceed $250,000 to the Tribal College Dual Enrollment Program Fund (This distribution was $160,000 in FY 2016, but was increased pursuant to Laws 2016, Chapter 124).

5/ 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 Other Issues section for more information.)*

6/ Excluding fund transfers, distributions to the General Fund totaled $78,775,000 in FY 2016 and are estimated to be $68,761,300 in FY 2017 and $77,174,400 in FY 2018.

7/ The table includes $10,596,800 in FY 2016 General Fund transfers that were processed through the state's accounting system after the end of FY 2016.

SUMMARY OF FUNDS	**FY 2016 Actual**	**FY 2017 Estimate**

State Lottery Fund (LOA2122/A.R.S. § 5-571) **Partially-Appropriated**

Source of Revenue: Sales of lottery tickets, retailer license fees, and interest earnings.

Purpose of Fund: 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.

Appropriated Funds Expended	97,508,400	113,225,100
Non-Appropriated Funds Expended	571,668,100	539,847,400
Year-End Fund Balance*	17,425,300	(5,130,400)

* As reported by the agency. Actual ending balance will not be negative.