



LOTTERY®

OHIO LOTTERY COMMISSION

BIENNIUM

BUDGET

TESTIMONY

FISCAL YEARS

2020 - 2021

Mike DeWine

Governor

•

Provided By:

Pat McDonald

Director, Ohio Lottery Commission

Introduction

Co-Chairman Cupp, Co-Chairman Patterson, and members of the Primary and Secondary Education subcommittee, the Ohio Lottery Commission is pleased to present this fiscally responsible budget request for the next biennium. This request was crafted with careful consideration of the resources necessary to help the Lottery achieve its core mission of maximizing profits for primary, secondary, vocational, and special education in Ohio via the Lottery Profits Education Fund (LPEF).

Brief Background

Beginning with the first ticket sold in 1974 through the end of the most recent fiscal year, the Lottery has generated more than \$25 billion in profit for the state of Ohio. Additionally, the Lottery has awarded over \$43.7 billion in prizes since its inception. Today, the Lottery offers draw, instant ticket, monitor and terminal-based games and regulates the Video Lottery Terminal (VLT) games at the seven racetracks throughout Ohio.

The Lottery is unique among other state agencies in that it functions like a business—generating profit for the state while providing consumer protections through regulatory oversight and fiscal accountability. As an enterprise fund of the state, the Lottery receives **zero** General Revenue Fund (GRF) dollars to operate. Operational expenses are approximately 4.5 percent of sales and this has translated into annual profit transfers of over **\$1 billion** to the LPEF in each of the past three fiscal years, including a record profit of **\$1.087 billion** in fiscal year 2018.

Traditional Lottery

The Lottery has been able to achieve the record results mentioned above through a continual commitment to innovation, strong partnerships with our network of over 9,800 retailers, vendor collaboration, and by providing entertaining lottery products to our players.

Total traditional product sales for fiscal year 2018 set an all-time sales record of over \$3.16 billion, exceeding the previous sales record set in fiscal year 2016 by more than \$100 million.

Instant ticket sales were \$1.60 billion. This was an increase of more than \$73.5 million over fiscal year 2017 and the highest instant ticket sales in Lottery history.

Draw game sales totaled \$1.56 billion, an increase of more than \$84.8 million over the prior fiscal year.

Record sales of the traditional lottery products in fiscal year 2018 can be attributed to several factors:

Category	2016	2017	2018
Daily Draw	\$ 579.8	\$ 582.4	\$ 586.0
Pick 3	\$ 343.0	\$ 339.6	\$ 340.1
Pick 4	\$ 200.3	\$ 201.0	\$ 205.1
Pick 5	\$ 36.4	\$ 38.1	\$ 40.8
Raffle		\$ 3.6	
Lotto	\$ 95.9	\$ 86.5	\$ 87.4
Rolling Cash 5	\$ 60.3	\$ 55.5	\$ 53.0
Classic Lotto	\$ 35.6	\$ 31.0	\$ 34.4
Multistate	\$ 309.9	\$ 243.0	\$ 288.9
Mega Millions	\$ 102.2	\$ 93.3	\$ 120.1
Powerball	\$ 193.5	\$ 129.8	\$ 148.1
Lucky for Life	\$ 14.1	\$ 19.9	\$ 20.7
Monitor	\$ 365.9	\$ 396.3	\$ 432.7
Keno	\$ 365.9	\$ 396.3	\$ 421.1
The Lucky One			\$ 11.6
Terminal-Based	\$ 147.4	\$ 166.4	\$ 164.5
EZPLAY	\$ 115.2	\$ 120.2	\$ 113.2
EZPLAY Tap	\$ 31.5	\$ 30.0	\$ 31.8
Touch and Win	\$ 0.7	\$ 16.2	\$ 19.5
Total Draw	\$ 1,498.9	\$ 1,474.6	\$ 1,559.5
Total Instant	\$ 1,560.7	\$ 1,527.1	\$ 1,600.6
Total Traditional	\$ 3,059.6	\$ 3,001.7	\$ 3,160.1

The daily draw game category, which includes Pick 3, Pick 4, and Pick 5, grew by \$7.2 million or 1.2 percent over fiscal year 2017.

Multi-state games, which include Mega Millions®, Powerball®, and Lucky for Life®, benefited from high jackpots in fiscal year 2018. This category grew by \$45.8 million or 18.9 percent when compared to fiscal year 2017. While no jackpots set records during fiscal year 2018, there were seven instances where the jackpot for these games exceeded \$300 million or more, with a high of \$758 million. The Mega Millions game went through a transformation in October of 2017, which delivered a redesigned game that offered significantly higher average jackpots, large 2nd tier prizes and more player excitement and engagement.

Monitor games, which include Keno and The Lucky One, were \$421 million in fiscal year 2018, or 6.3 percent higher than fiscal year 2017. This marked the tenth consecutive year of growth for this product category. In fact, Keno sales have increased every year due to aggressive recruitment of the Keno retailer base, the installation of additional self-service equipment, and by offering targeted promotions geared toward social engagement.

These products can be purchased directly from retailers, from gaming kiosks in stores, and from terminals that may also allow players to play touch and win games or other instant games. While this trade channel continues to grow, the lottery is pursuing the ability to allow these games to be purchased in new ways, to keep up with demand from the playing public.

Video Lottery

Protecting the integrity of gaming in Ohio is one of the Lottery’s core values. Since 2012, Lottery has been able to provide Ohio’s consumers with confidence that the Video Lottery Terminal (VLT) games at Ohio’s seven racinos are offered with the utmost security, honesty and fairness.

Gross gaming revenue (GGR) constitutes wagers minus prizes and is allocated between the Video Lottery Sales Agents (Racinos) as commissions at a rate of 66.5 percent and the Lottery at a rate of 33.5 percent. Additionally, 0.5 percent of the Racinos’ commission is earmarked for responsible gaming programs.

The Lottery prides itself on striking a balance as a strong regulator and a business partner. This has allowed Ohio’s education fund to benefit tremendously over the past seven years as demonstrated in this chart.

Distribution of Net Win <i>(in millions)</i>				
Fiscal Year	GGR	Racino	Lottery	Problem Gambling
2012	\$ 11.1	\$ 7.4	\$ 3.7	-
2013	\$ 165.5	\$ 110.1	\$ 55.5	-
2014	\$ 437.6	\$ 289.5	\$ 146.6	\$ 1.5
2015	\$ 772.9	\$ 511.4	\$ 258.9	\$ 2.6
2016	\$ 868.9	\$ 574.9	\$ 291.1	\$ 2.9
2017	\$ 926.6	\$ 613.1	\$ 310.4	\$ 3.1
2018	\$ 987.3	\$ 653.30	\$ 330.7	\$ 3.3

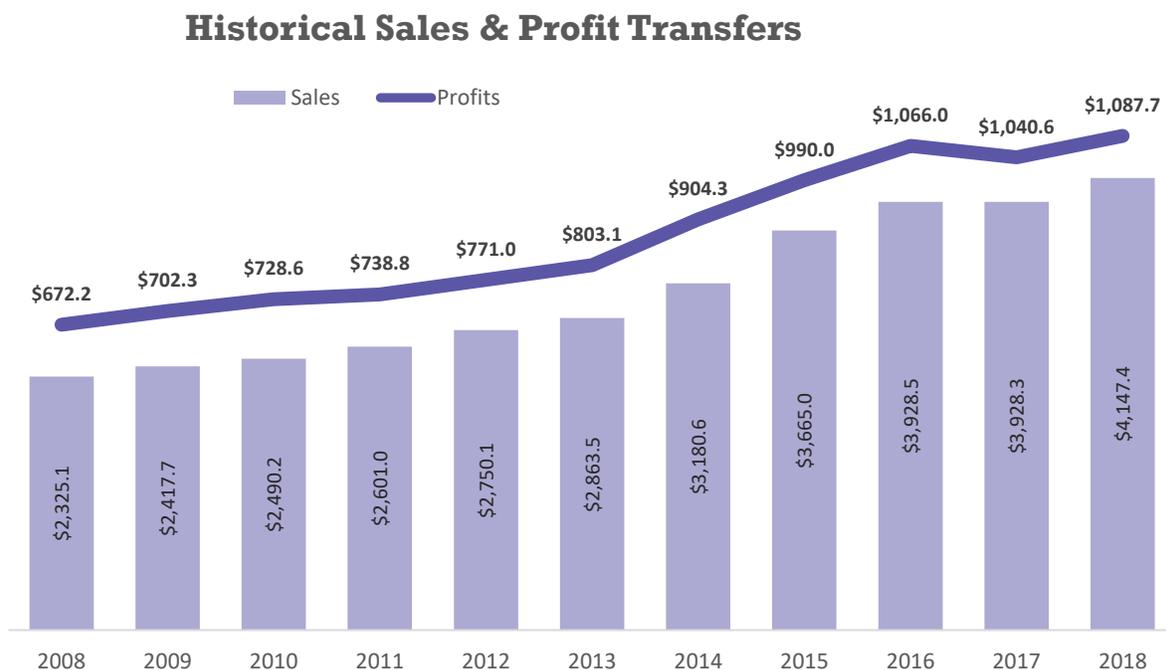
In fact, fiscal year 2018 represented a record year for revenue generated from Video Lottery Terminal (VLT) games at the Lottery’s seven racinos. Gross gaming revenue was \$987.3 million, which represented an increase of \$60.1 million over fiscal year 2017. The Lottery’s share of GGR increased from \$310.4 million to \$330.7 million, or 6.5 percent.



Overall Performance

Overall combined traditional sales and VLT Lottery revenue in fiscal year 2018 were \$4.1 billion, marking the first-time gross sales exceeded \$4 billion. Prizes were \$2 billion and profits for the state education fund were a historic \$1.087 billion. This was accomplished through a rigorous focus on fiscal accountability and cost containment. This achievement is primarily the result of the Lottery holding operating costs at or below the rate of profit growth.

Below is an illustration of our sales and profit growth over the last decade.



Through February of 2019, traditional sales are up from last year by \$142.3 million. The multi-state category is up due to the October 2018 Mega Millions jackpot of \$1.5 billion. Daily draw, monitor, terminal-based games have all grown against the previous fiscal year. Instant tickets are up once again, an increase of \$47.7 million compared to fiscal year 2018. VLT net revenue is up \$16.7 million versus last fiscal year. Overall, lottery trends for the first eight months of fiscal year 2019 have been positive.

Therefore, the Lottery is optimistic that the agency will exceed its profit commitment of \$1.093 billion.

2020 – 2021 Biennium Budget Request

As mentioned previously, the Lottery is self-sufficient and thus does not require GRF dollars. The Lottery supports the Governor’s priority of investing in Ohio’s children. With a focused approach to ensure efficient operations, this request will allow the Lottery to grow profits. Also, included in this request is an increased commitment to Responsible Gambling and resources to address industry challenges by using innovation and new technology to meet its commitments to the LPEF, including the introduction of iLottery.

By approving this budget, you will provide the necessary resources for the Lottery to achieve profits transfers of **\$1.126 billion** in fiscal year 2020, and **\$1.177 billion** in fiscal year 2021 to the Lottery Profits Education Fund (LPEF). This is \$72 million more than the current biennium’s profit transfer.

Responsible Gambling Commitment

The Lottery has always been committed to responsible gambling. The Lottery practices corporate social responsibility in the management and sale of its games, while increasing awareness of problem gambling and available treatment resources. Pursuant to statutory directive, the Lottery has developed multiple agreements with Ohio Department of Mental Health and Addiction Services (OMHAS) to fund programs which address problem gambling issues in Ohio. Specifically, the Lottery provides funding for: free treatment across the State; for workforce training of problem gambling counselors; for Ohio for Responsible Gambling (ORG), which is a multi-agency initiative of the Lottery, the Ohio Casino Control Commission (OCCC), OMHAS, and the Ohio State Racing Commission (OSRC); and for the development of prevention and awareness campaigns. Additionally, the Lottery serves in leadership roles in national responsible gambling organizations. The Lottery has been certified by North American State & Provincial Lotteries (NASPL) and National Council on Problem Gambling (NCPG) as having met best practice standards in the industry.

Recently, the Lottery and OCCC created a new statewide Ohio Voluntary Exclusion Program (VEP). This new VEP initiative was driven by the Lottery after the agency amended its statute in the previous budget cycle in response to suggestions by stakeholders in the problem gambling community. In one of the first in the nation multi-agency state run programs, the Lottery and the OCCC have collaborated to permit individuals to voluntarily exclude themselves from all of Ohio's seven racinos and four casinos. Individuals may apply one time at the location of their choice which relieves them of the undo pressure of having to travel to multiple gaming facilities to voluntarily self-exclude.

This biennium budget request includes an increase in Responsible Gambling funding. The Lottery will provide a portion of the funding needed by OMHAS to conduct a comprehensive study over the next two years. The purpose of this study is to evaluate the efficacy of our screening, intervention, and referral protocol in multiple Ohio settings, as well as, to assess individuals with problem gambling and/or gambling disorder who may need services for substance use disorders, mental illness disorders, and/or physical health challenges. This collaborative research study, involving three state agencies, will inform future funding priorities.

Addressing Challenges

Like other lotteries with mature product portfolios, the Lottery faces ongoing challenges to maintain and increase future revenue for the State. Numerous factors can affect lottery performance, such as the product mix and design of games offered, jackpot fatigue, distribution channels including number and quality of retailers, legislative budget decisions, and competition.

Competition from other gaming activities remains a challenge. Ohioans now have an unprecedented number of gaming alternatives in which to use their discretionary income. Ohio's legal gambling landscape has grown to include casinos and daily fantasy sports. There has also been an expansion of the unregulated market including "grey" machines, "Queen of Hearts" and offshore sportsbook markets. Sales from traditional products may be constrained by these added pressures.

A decade ago, lottery products consisted of draw and instant ticket games. Players were easier to reach via traditional network television and radio advertising. Today, the Ohio Lottery's portfolio consists of eleven different draw games with three unique add-on features, approximately 65 instant games at several price points, monitor games, and terminal-based fast play games. As technology continues to change how

citizens acquire information and make purchases, the Lottery must also adapt. Marketing messages need to be delivered in environments that are immediate, relevant, and convenient for consumers.

The Lottery continues to modernize communication via enhancements to our loyalty program, increased presence on social media, and a myriad of other promotional and marketing efforts to expand our player base. Due to consumer demands for alternative payment methods, the Lottery implemented “cashless” payment options on its 7,100+ self-service vending machines and in the 9,800+ retailers across the state. This payment method will continue to drive sales.

In the next biennium, the agency will continue to seek ways to modernize and better position itself to reach the next generation. To that end, the Lottery will begin offering existing products over the internet through the implementation of iLottery. By allowing additional options of purchasing existing content, the Lottery can keep up with the way in which people have become accustomed to buying everything from music and books to their groceries. It is imperative that the Lottery continue to adapt and simplify the player’s experience to match current consumer purchasing trends. Likewise, the Lottery will continue to make it more convenient for retailers and consumers to cash prizes. These efforts are critical to reach new players and maintain current customer interest which will ultimately generate more revenue for Ohio. The advancement in the technology which players can purchase lottery tickets is the driver behind the large increase in the LPEF transfer in the second year of the biennium.

Generating Revenue to Invest in Ohio’s Education

The requested appropriations have been made after a careful process that has prioritized the most pressing need of maximizing profits for education, while scrutinizing every dollar spent. This budget request, if approved, will allow the Lottery to quickly adapt to the rapidly changing demands of customers as well as the emergence of new competition. In order to sustain growth over the next biennium, the Lottery must provide players with easy access to products through all channels and continue to innovate to bring new games to market.

The requested budget provides the Lottery with the flexibility and opportunity to overcome industry challenges. Ultimately, this will generate over \$2.3 billion for education in Ohio over the next biennium. Below is a chart of the Lottery’s request and an explanation of each line item, for which the Lottery respectfully requests your approval.

Budget Request	FY 2020	FY 2021
Operating Expenses	\$ 147,966,184	\$ 149,673,753
Video Lottery Operations	12,053,270	12,260,299
Vouchered Prizes	214,206,000	217,719,000
	<u>\$ 374,225,454</u>	<u>\$ 379,653,052</u>

Budget Request by Appropriation Line Item (ALI)

Competitive procurement and contract monitoring are routine resources and techniques used by the Lottery to ensure operations are streamlined and business partners are performing as expected.

These efforts help the Lottery focus its activities on areas most likely to support the agency goals identified herein. Resources are evaluated at every opportunity to determine the return on investment and/or available alternatives.

ALI 950321: Operating Expenses

This ALI encompasses the following items: payroll, benefits, personal services such as training and employee development, legal services, rent, telecommunications, software licensing fees, IT equipment, point of sale merchandise, and vehicles for our sales force.

In addition, there are various fees/charges that have a large impact on this ALI, which are not necessarily controllable. This includes charges from the Department of Administrative Services (DAS) such as the IT Optimization, Attorney General Office (AGO), Office of Budget & Management (OBM) and Auditor of State (AOS).

The increase within this ALI, when compared to fiscal year 2019 estimates, is also due to the payroll budget. There are increased costs associated with healthcare (10 percent), and the cost of living adjustment (2.75 percent in Fiscal Year 2020 and 3.0 percent in Fiscal Year 2021).

ALI 950402: Advertising Contracts

Advertising plays an important role in the Lottery's ability to promote its full line of products. The budget expenditure requested represents 0.8 percent of total traditional sales, which is lower than the industry standard and is necessary to meet the objectives of providing adequate media/marketing coverage throughout the State. A decade ago, lottery products consisted of only a few draw games and instant ticket games. Players were easier to reach via traditional network television and radio advertising.

Today, the Lottery has a more robust portfolio and the advertising industry is segmented through the proliferation of new media choices for consumers. A few examples of new media include the internet, social media, and mobile applications. Streaming and on-demand media have also played a significant role in the increasingly fragmented media landscape. Due to the continued expansion of the product mix and distribution network, including self-service machines, the internal challenge is to execute annual marketing plans that meet the changing needs of the customers. The advertising budget requested is essential for the Lottery to achieve its sales targets and maximize its contributions to the Lottery Profits Education Fund.

In addition, this line item also supports the weekly production of the Lottery's Cash Explosion® show and the production and transmission of the daily drawings which continue to be popular among the Lottery's core consumer.

ALI 950403: Gaming Services Contracts:

All gaming contracts are included within this line item. This includes the printing of instant tickets, the gaming system, paper stock for draw games and bet cards, the operation of the VLT program and funds for the player loyalty program. Funding for gaming-related contracts, a majority of which are variable in nature and dependent upon sales activity, will increase slightly when compared to the current biennium. This is primarily due to increases in the Lottery's traditional sales and VLT revenue forecasts which ultimately mean more profit for the education fund.

ALI 950601 & 950602: Direct Prize Payments & Annuity Prizes

Direct prize payments include all nondeferred major prizes won by players. This appropriation line item facilitates prize payments that are paid through a state warrant. Prize funding within this ALI will vary based on sales levels

and certain high-tier prizes won, which cannot be controlled or projected. Examples of large prizes include cash options for large jackpots in games such as Classic Lotto, Lucky for Life, Powerball and Mega Millions.

Other direct prize payments also include cash payouts from Instant games, and non-cash prize payouts to winners (Loyalty Program). Appropriations for direct prize payments are \$154.3 million in fiscal year 2020 and \$157.4 million in fiscal year 2021.

The annuity prize line item 950602, supports the annual payment for the annuity prize winnings for winners who select to be paid in installments rather than in one lump sum payment. The appropriation within this line item will vary based on the number of winners who elect the annuity option. Funding for this appropriation is \$59.8 million in fiscal year 2020 and \$60.2 million in fiscal year 2021. The decreased amount is due to more winners choosing the cash option rather than the annuity.

ALI 950605: Problem Gambling

This line item funds programs related to problem gambling treatment and prevention expended by the Lottery itself and in conjunction with the Ohio Department of Mental Health and Addiction Services. Pursuant to Revised Code Sec. 3770.02(K), the Lottery supports six (6) best practice treatment centers throughout the state, training of problem gambling counselors, an annual problem gambling conference, public awareness media campaigns and a multi-disciplinary research study. This appropriation is slated to increase to \$3.4 million in each year of the biennium.

Conclusion

This budget request represents an investment in people, products, and technology through which the Lottery will maximize profit for the education of Ohio's children via the Lottery Profits Education Fund (LPEF). The Lottery strongly believes that its expected sales levels, supported by the requested appropriations within this request, will provide for the successful attainment of the its goals and objectives.

By approving the budget respectfully submitted today, you will allow the Lottery to transfer over **\$2.3 billion** to the Lottery Profits Education Fund in the next biennium. Specifically, the Lottery has targeted a transfer commitment of \$1.126 billion in fiscal year 2020, and \$1.177 billion in fiscal year 2021.

Thank you for your time and consideration.