



OHIO LOTTERY COMMISSION

**BIENNIUM BUDGET
TESTIMONY**

**FISCAL YEARS
2022 – 2023**

Mike DeWine
Governor

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Provided By:

Pat McDonald

Director, Ohio Lottery Commission

Introduction

Chair Richardson and Members of the Primary and Secondary Education Subcommittee, the Ohio Lottery Commission is pleased to present a fiscally responsible budget 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 \$27 billion in profit for the State of Ohio. Additionally, the Lottery has awarded over \$48 billion in prizes since its inception. Today, the Lottery offers draw, scratch-off tickets, 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 four percent of sales and this has translated into annual profit transfers of over \$1 billion to the LPEF in each of the last five fiscal years, including a record profit of \$1.154 billion in fiscal year 2019.

Traditional Lottery

Traditional lottery products include instant scratch-off games as well as draw-based games such as the daily draws, multistate games, monitor games, and terminal games. The chart below shows total traditional lottery product sales over the past three fiscal years (\$ in millions).

Category	2018	2019	2020
Daily Draw	\$ 586.0	\$ 615.4	\$ 692.3
Pick 3	\$ 340.1	\$ 354.0	\$ 400.6
Pick 4	\$ 205.1	\$ 216.9	\$ 240.5
Pick 5	\$40.8	\$ 44.5	\$ 51.2
Lotto	\$ 87.4	\$ 83.5	\$ 80.5
Rolling Cash 5	\$ 53.0	\$ 52.0	\$ 51.7
Classic Lotto	\$ 34.4	\$ 31.5	\$ 28.8
Multistate	\$288.9	\$ 356.9	\$ 206.6
Mega Millions	\$ 120.1	\$ 192.7	\$ 101.9
Powerball	\$ 148.1	\$ 143.3	\$ 85.1
Lucky for Life	\$ 20.7	\$ 20.4	\$ 19.5
Monitor	\$ 432.7	\$ 470.8	\$ 459.5
Keno	\$ 421.1	\$ 453.9	\$ 439.4
The Lucky One	\$11.6	\$16.9	\$20.1
Terminal-Based	\$ 164.5	\$ 171.6	\$ 158.7
EZPLAY	\$ 113.2	\$ 100.3	\$ 88.4
EZPLAY Tap	\$ 31.8	\$ 40.8	\$ 38.9
Touch and Win	\$19.5	\$ 30.4	\$ 31.4
Total Draw	\$ 1,559.5	\$ 1,697.7	\$ 1,597.7
Total Instant	\$ 1,600.6	\$ 1,663.0	\$ 1,873.8
Total Traditional	\$ 3,160.1	\$ 3,360.7	\$ 3,471.5

As indicated by the chart, total traditional product sales for fiscal year 2020 were \$3.47 billion. This amount set an all-time sales record, exceeding the previous sales record set in fiscal year 2019 by more than \$111 million. Scratch-off ticket sales of \$1.87 billion represented an increase of nearly \$211 million over fiscal year 2019 and the highest instant ticket sales in Lottery history. Draw-based game sales totaled \$1.59 billion, a decrease of more than \$100 million over the prior fiscal year. The decline in draw game sales can be directly attributed to the lack of large jackpots for multistate games like Mega Millions and Powerball, as well as the impact of the COVID-19 pandemic on monitor and terminal-based games that are generally played in social environments like bars and restaurants.

Video Lottery

Protecting the integrity of gaming in Ohio is one of the Lottery’s core values. Since 2012, the 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% and the Lottery at a rate of 33.5%. Additionally, 0.5% of the Racinos’ commission is earmarked for responsible gambling 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.

In March of 2020, COVID-19 pandemic began to impact lottery revenues. Net win from video lottery terminals, which was up by almost \$20 million or nearly 9% at the end of February, finished the year down by approximately \$238 million or 22.5% compared to the prior year.

Distribution of Net Win (in millions)				
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	\$ 653.3	\$ 330.7	\$ 3.3
2019	\$ 1,058.6	\$ 700.5	\$ 354.6	\$ 3.5
*2020	\$ 820.9	\$ 543.2	\$ 275.0	\$ 2.7

*All Ohio racinos were closed due to the COVID-19 pandemic from March 14th through June 18th.

Overall Performance

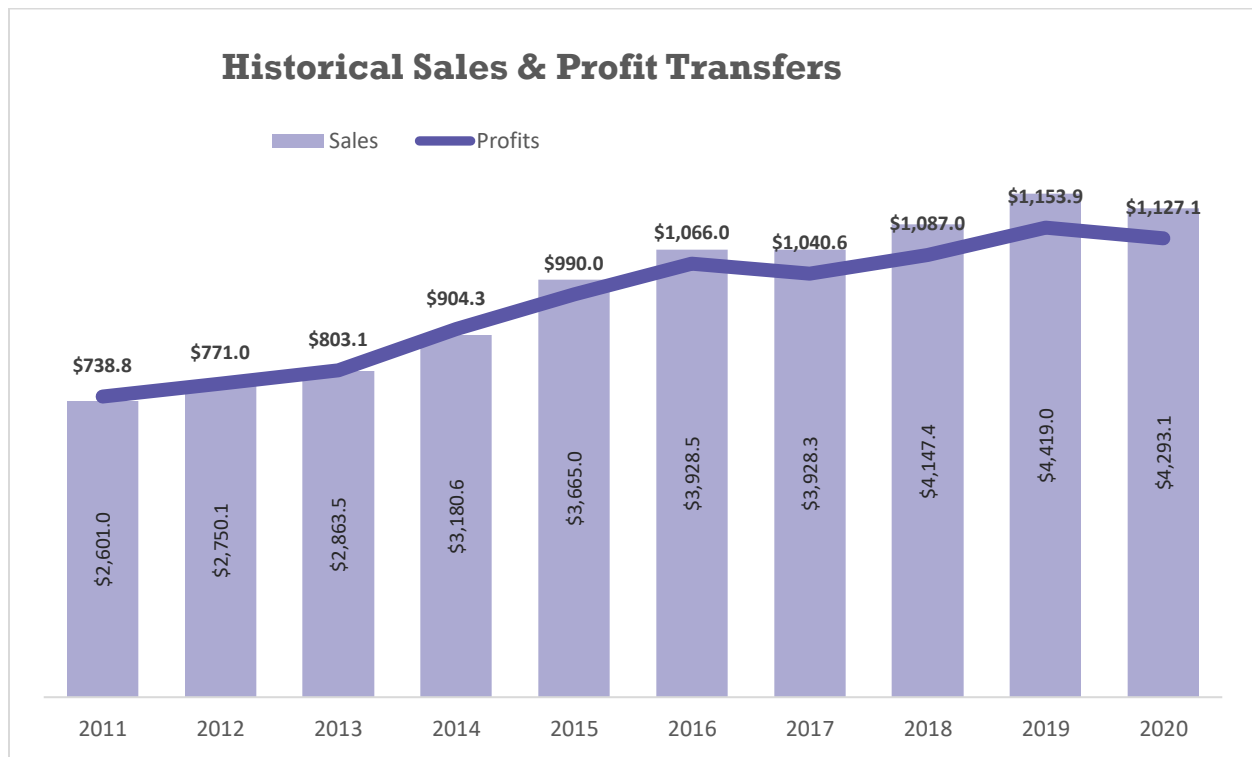
Despite encountering various challenges throughout fiscal year 2020, the Lottery was still able to meet and exceed its annual LPEF commitment of \$1.126 billion. Initial sales trends were negative primarily due to an upgrade of lottery point of sale units that required retraining all 9,800+ retailers; a transition to a new vendor for the agency’s warehousing and distribution of scratch-off tickets; and low jackpot levels for multistate games like Mega Millions® and Powerball®. By the end of October 2019, traditional sales of scratch-off tickets and draw games were down almost \$83 million, or over 7%, behind the previous year’s pace.

However, a record-setting holiday campaign marked the start of a strong turnaround in which sales for the month of December were the second highest recorded for any month in Lottery history. By leveraging predictive modeling to optimize inventory levels at retail and deploying a diversified game portfolio and strategic launch schedule, scratch-off sales were up by double digits in both January and February compared to the previous year. Draw games—led by KENO

and the Numbers games —also posted double-digit gains in those months, with the Daily Numbers games specifically having benefitted from a successful marketing campaign.

Beginning in March, however, the COVID-19 pandemic began to impact lottery revenues. Net win from video lottery terminals, which was up by almost \$20 million or nearly 9% at the end of February, finished the year down by approximately \$238 million or 22.5% compared to the prior year. This was a direct impact of the pandemic, as non-essential businesses were closed for nearly three months. Additionally, games like KENO that are popular in bars and restaurants finished the year down by 2.4% after pacing almost 10% ahead of the prior year’s sales.

In spite of the challenges the pandemic presented, positive growth in sales demonstrated the resiliency of the Lottery’s scratch-off product line. By working closely with vendors to ensure retailers had the right type and quantity of games, scratch-off sales growth in May and June was double industry growth trends and hovered around 50% ahead of sales from the previous May and June. These gains, along with a strong finish in the Numbers game category and a rigorous focus on fiscal accountability and cost containment, were able to offset much of the profit loss experienced elsewhere due to the pandemic and were key to allowing the Lottery to meet its LPEF commitment for fiscal year 2020.



Through January of 2021, traditional sales for fiscal year 2021 are up from last year by \$495.7 million. The multi-state jackpot game category is trending higher due to the January 2021 Mega Millions jackpot of \$1.05 billion along with the Powerball jackpot of \$730.1 million. Daily draw, monitor, and terminal-based games have all grown compared to the previous fiscal year. Scratch-off tickets are up once again, an increase of \$292.5 million compared to fiscal year 2020. Overall, lottery trends for the first seven months of fiscal year 2021 have been positive. Therefore, the Lottery is optimistic that the agency will meet its FY 2021 profit commitment of \$1.177 billion.

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.

This budget factors in an increase in our Responsible Gambling funding to \$4 million in each year of the next biennium. In addition to funding our annual responsible gambling efforts like the problem gambling prevention campaign, employee trainings, and work with Ohio Mental Health and Addiction Services, this increase will help expand the Ohio for Responsible Gambling collaborative’s prevention campaign to reach the “at-risk” population and increase treatment programs throughout Ohio.

Biennium Budget Request

This budget request for the next biennium represents the resources necessary to fulfill the Lottery’s commitment to Ohio’s education system via the LPEF. The Lottery is confident that this funding level can result in transfers to the LPEF of at least \$1.234 billion in fiscal year 2022 and \$1.263 billion in fiscal year 2023.

This commitment is contingent on the fulfillment of an operating budget of \$388.4 million in 2022 and \$402.0 million in 2023, which will support sales growth and fund new products and initiatives for the upcoming biennium. The Lottery’s budget can be categorized into three distinct parts: Operating Expenses for traditional lottery products, Video Lottery Operations, and Vouchered Prizes paid via state warrants.

Budget Request	FY 2022	FY 2023
Operating Expenses	\$ 164,478,238	\$ 174,206,257
Video Lottery Operations	11,873,414	12,050,075
Vouchered Prizes	212,011,419	215,746,013
	<u>\$ 388,363,071</u>	<u>\$ 402,002,345</u>

The Ohio Lottery’s overall budget request for the next biennium represents a minor increase in comparison to the fiscal year 2021 budget. Much of this increase is related to increases in sales-based or revenue sharing contracts—including the Lottery’s gaming system, scratch-off ticket printing, and product warehousing and distribution—and are based on projected sales growth. These payment arrangements represent contractual obligations resulting from competitive bids.

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 budget request also includes sufficient funding for top agency priorities and initiatives for the biennium that will further promote revenue growth. These priorities and initiatives include:

- **Retail Recruitment:** As the Lottery continues to recruit additional retailers, profits rise for Ohio’s education system. Currently, the Lottery is in the process of adding a new retail chain, Walmart, that will significantly expand its retailer distribution network but also require customized self-service vending equipment.
- **Adding New Trade Channels for Scratch-Offs:** The Lottery anticipates adding new trade channels for its scratch-off product line by introducing customized self-service vending equipment into the bar and

restaurant retailer channels. While these channels have proven successful with monitor games like KENO and Lucky One, most have been unwilling to sell scratch-off tickets over the counter or install standard self-service scratch-off vending machines onsite due to their large footprint.

- **Expanding Digital Presence:** The Lottery’s MyLotto Rewards mobile app currently has over 1.2 million active registered users and has experienced significant user growth over the past few years. This digital platform is key to reaching new and existing customers and gathering key consumer insights that can be leveraged for promotional campaigns and product research and development. Plans to add or expand features (such as mobile prize cashing) and offer additional second-chance and cross-promotional opportunities will ensure continued growth of this important digital tool. Additionally, marketing resources will continue to target digital platforms such as social media and streaming services.
- **Promoting “In Lane” Sales:** While lottery products are traditionally purchased on a lottery-specific point-of-sale (POS) terminal, a growing trend within the lottery industry is to transition to “in-lane” sales by integrating with existing retailer POS systems. This would allow lottery games—particularly scratch-offs—to be sold at checkout lanes, thereby increasing visibility and accessibility to new and existing customers.
- **Revamping Legacy Draw Games:** Sales for legacy draw games such as Classic Lotto and Rolling Cash 5 have stagnated over the past several years. Led by the Office of Product Innovation, the Lottery is currently evaluating potential ways to revamp these games and stimulate sales. Changes are currently being planned and implementation may take place at or around the start of the biennium.

The requested budget provides the Lottery with the flexibility and opportunity to overcome industry challenges. Ultimately, this will generate over \$2.5 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 by Appropriation Line Item (ALI)

The Lottery has made concerted efforts to minimize costs and evaluate operating expenses solely on the basis of their contribution to producing profits for education and has made every effort to evaluate and improve operational efficiency. These appropriation requests reflect the Lottery’s continued emphasis on effective management and good stewardship of Lottery funds. The requested funding levels are required to sustain Lottery operations and allow the Lottery to remain a viable contributor towards the State’s education budget.

Fund	ALI	ALI Name	Actual			Estimated	Recommended			
			FY 2018	FY 2019	FY 2020	FY 2021	FY 2022	% Change	FY 2023	% Change
7044	950321	Operating Expenses	46,845,178	48,744,538	49,313,421	56,241,063	57,344,482	2.0%	58,581,656	2.2%
7044	950402	Advertising Contracts	24,395,404	25,272,893	25,625,729	26,700,000	27,925,000	4.6%	27,925,000	0.0%
7044	950403	Gaming Contracts	70,201,028	62,464,282	70,245,686	71,239,582	84,082,171	18.0%	90,357,570	7.5%
7044	950601	Direct Prize Payments	237,777,568	141,764,106	403,100,846	157,390,000	158,700,369	0.8%	162,809,344	2.6%
7044	950605	Problem Gambling	2,952,310	3,397,505	3,055,119	3,400,000	4,000,000	17.6%	4,000,000	0.0%
8710	950602	Annuity Prizes	71,906,369	64,663,059	57,998,217	52,723,717	56,311,050	6.8%	58,328,775	3.6%
Total State Lottery			454,077,857	346,306,383	609,339,018	367,694,362	388,363,072	5.6%	402,002,345	3.5%

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 and related maintenance for our sales force. The expenditures within this ALI allow the Lottery to invest in people, technology, and essential equipment to help support many of the services that it provides.

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, state printing & state purchasing expenses (Attorney General Office (AGO), Office of Budget & Management (OBM) and Auditor of State (AOS).

When compared to fiscal year 2021's original budget, the appropriation request for this ALI is to be less in each year of the next biennium. The Lottery has a keen focus on its day-to-day administrative expenses, and this focus continues to yield efficiencies over time. For instance, during the outbreak of the pandemic that followed with budget reductions, the agency was successful in renegotiating some services and also sought discounts on purchased equipment and merchandise. This approach has yielded positive results by reducing/eliminating unnecessary expenses.

ALI 950402: Cash Explosion, Drawings & Advertising Contracts

This ALI exists to support the Office of Marketing's objective to design, manage, and execute marketing campaigns and programs that reach a variety of player segments. As with any business, advertising plays an important role in the Lottery's ability to promote its full line of products. The Lottery believes the requested funding levels are necessary to meet its objectives of providing adequate media/marketing coverage throughout the State. These funding levels take into consideration the changing landscape of how consumers receive and absorb information and the fact that the Lottery must be in position to combat direct and indirect competitors. Advertising spending is usually expressed as a percentage of sales, a metric known as the ad/sales ratio. In the lottery industry, the average ad/sales ratio across all U.S. lotteries is 1.0%. The budget expenditure requested represents less than 0.75% of total traditional sales, which is lower than the industry standard.

A decade ago, lottery products consisted of only a few draw games and scratch-off tickets. 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. The goal of every program is to push out relevant content to new and existing customers. Services include, but are not limited to, the following areas – production, research, media planning and buying, digital development/optimization, graphic design, promotions, and partnerships. 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 consumers.

ALI 950403: Gaming Services Contracts

All gaming-related contracts are included within this line item. This includes the operation of the gaming system, gaming equipment, the vast network of retailers utilizing the gaming system, the printing & distribution of scratch-offs, paper stock for draw games and bet cards, the regulation 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 due to an anticipated increase in sales for all lottery products.

Many of the contracts within this ALI are sales-based contracts. For instance, as Lottery revenue increases, the contractual expenditures that are paid to vendors also increase. The Lottery prepared its budget with the flexibility to support this increased sales volume. The Lottery monitors sales throughout the year and adjusts its spending in these areas appropriately based on sales volume.

As such, this funding level requested will support an increase in sales over the current biennium. The Lottery expects to tap into new markets through retailer expansion and offering new or improved products. The Lottery believes that funding levels requested in this ALI are required to invest in technology and products necessary to generate the anticipated sales increases, which will lead to additional profits.

ALI 950601 & 950602: Direct Prize Payments & Annuity Prizes

Direct prize payments include all non-deferred 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 scratch games, and non-cash prize payouts to winners (Loyalty Program). Appropriations for direct prize payments are \$158.7 million in fiscal year 2022 and \$162.8 million in fiscal year 2023.

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 \$56.3 million in fiscal year 2022 and \$58.3 million in fiscal year 2023. The recent trends have shown a decrease within this line item, 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 (OMHAS), pursuant to Revised Code Sec. 3770.02(K). The Lottery's responsible gambling funds are used to support 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 \$4.0 million in each year of the biennium. Increased funding for responsible gambling outreach will allow for expanded promotion of the Lottery's problem gambling prevention campaign as well as combined efforts with the awareness campaigns of the Ohio Department of Mental Health and Addiction Services and Ohio for Responsible Gambling (ORG). Funding will also support the expansion of treatment programs, training of problem gambling treatment counselors, best practice treatment funds, and pilot in-patient treatment programs.

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 its goals and objectives.

By approving the budget respectfully submitted today, you will allow the Lottery to transfer nearly \$2.5 billion to the Lottery Profits Education Fund in the next biennium. Specifically, the Lottery has targeted a transfer commitment of \$1.234 billion in fiscal year 2022, and \$1.263 billion in fiscal year 2023.

Thank you for your time and consideration.