



Ohio Lottery Commission Budget Testimony for Fiscal Years 2024 and 2025

Delivered by Executive Director Pat McDonald to the Ohio House Primary and Secondary Education Subcommittee on Tuesday, February 21, 2023

Introduction

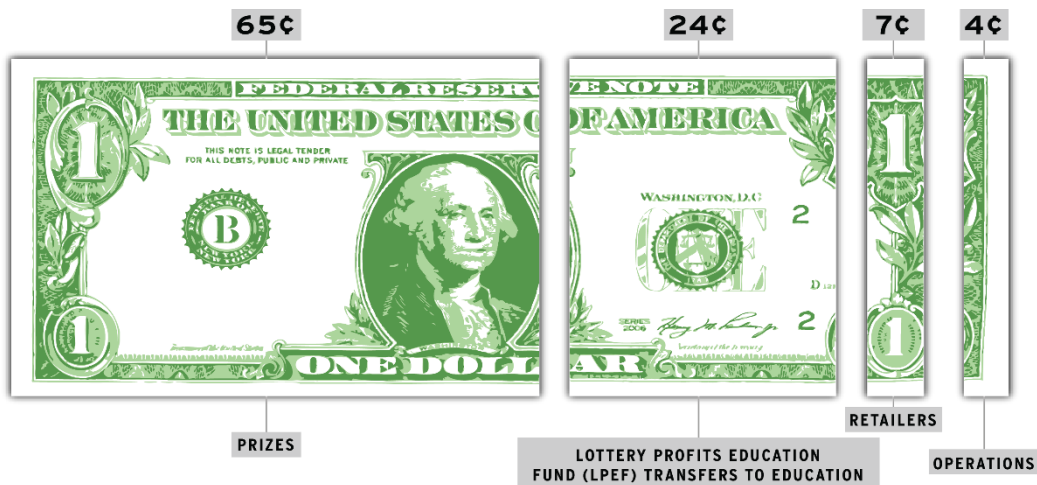
Chair Richardson, Ranking Member Isaacsohn, and Members of the Primary and Secondary Education Subcommittee: I'm Pat McDonald, Executive Director of the Ohio Lottery Commission, and I'm pleased to present you with the Lottery's budget request for fiscal years 2024 and 2025.

The mission of the Lottery is to support funding for education in Ohio by offering entertaining gaming experiences. Profits from the sale of lottery games are transferred to the Lottery Profits Education Fund (LPEF) to provide funding for primary, secondary, vocational, and special education programs for Ohio's students. Since our first ticket was sold in 1974, we have transferred more than \$29 billion to the LPEF. Our annual transfers have exceeded \$1 billion since 2016, and in the most recent fiscal year, we transferred a record \$1.4 billion.

On average, for every dollar spent on lottery products, approximately 65 cents are paid out in prizes to players; 24 cents are transferred to the LPEF; 7 cents go to retailers in the form of commissions and bonuses; and only 4 cents—or 4 percent of lottery sales—are required for our operating expenses. As such, the Lottery requires no General Revenue Fund dollars to operate, and instead relies solely on lottery sales revenue for our appropriations.

In addition to our revenue-generating mission, the Lottery plays an important regulatory role in Ohio's gaming landscape. Since 2012, we have regulated the video lottery terminals (VLT's) at the seven racinos in Ohio. This includes licensing of the properties, their employees, and the equipment providers; establishing and enforcing regulations, operating standards, and minimum internal controls; and collecting 33.5 percent of VLT net revenue

As of this year, the Lottery is also responsible for regulating "type C" lottery sports gaming, which is currently offered at over 800 retail locations across the State. I will discuss lottery sports gaming in more detail later in my testimony.



Budget Request

For the next biennium, the Lottery is requesting a total appropriation of \$427.4 million for FY 2024 and \$443.2 million for FY 2025. These amounts represent annual increases of 4.8 percent and 3.7 percent, respectively. The Lottery's budget consists of six line-items. I will provide a brief overview of the trends within each line item, and then discuss the major challenges and highlights of our budget submission.

Fund	ALI	ALI Name	Actual			Estimated	Recommended			
			FY 2020	FY 2021	FY 2022	FY 2023	FY 2024	% Change	FY 2025	% Change
7044	950321	Operating Expenses	49,313,420	49,465,623	55,178,324	60,053,317	61,967,164	3.2%	64,686,040	4.4%
7044	950402	Advertising Contracts	25,625,729	23,879,854	28,441,933	27,925,000	29,755,000	6.6%	29,955,000	0.7%
7044	950403	Gaming Contracts	70,245,686	77,820,535	91,924,068	94,157,570	109,197,677	16.0%	120,685,198	10.5%
7044	950601	Direct Prize Payments	403,100,846	220,830,191	195,690,873	162,809,344	179,366,000	10.2%	182,106,000	1.5%
7044	950605	Problem Gambling	3,055,119	3,348,096	3,977,694	4,652,104	4,850,000	4.3%	4,850,000	0.0%
8710	950602	Annuity Prizes	57,998,217	52,939,470	48,096,197	58,328,775	42,243,000	-27.6%	40,946,000	-3.1%
		Total State Lottery	609,339,016	428,283,769	423,309,089	407,926,110	427,378,841	4.8%	443,228,238	3.7%
		Grand Total - Lottery Commission	609,339,016	428,283,769	423,309,089	407,926,110	427,378,841	4.8%	443,228,238	3.7%

Operating Expenses: Our Operating Expenses line item includes funding for nearly 400 employees as well as facilities fees for our headquarters, warehouse, and nine regional offices. Increases of three and four percent in this line item are driven primarily by cost-of-living adjustments, inflation assumptions, and rising health care costs.

Advertising Contracts: The Lottery's Advertising Contracts line item includes modest increases to support and expand marketing efforts that drive sales growth and profits for the LPEF. These increases will ensure the Lottery remains competitive amid rising marketing costs, especially in the digital marketing arena.

Direct Prize Payments and Annuity Prizes: Appropriations for the Direct Prize Payments line item and the Annuity Prize Payments line item fluctuate across the biennium, and primarily reflect current trends in how lottery players are cashing their winnings.

Problem Gambling: The appropriation request of \$4.85 million for the Problem Gambling line item represents a four percent increase compared to FY 2023 projections. While I will highlight our responsible gambling efforts in more detail at the conclusion of my testimony, we have significantly expanded our funding for these programs over the past four years. In the next biennium, we will continue working closely with our partner agencies such as the Ohio Mental Health and Addiction Services Department (OMHAS), the Racing Commission, and the Casino Control Commission to effectively expand our responsible gambling services.

Gaming Contracts: Finally, our Gaming Contracts line item includes contracts for the Lottery's central gaming system, scratch-off ticket printing, and other gaming-related consumables, services, equipment, and maintenance. Historically, increases in this line item are generally driven by both investments in additional self-service terminals to generate profits as well as revenue-share agreements tied to sales growth. Revenue-share agreements are standard within the lottery industry and help incentivize vendor innovation and strategic alignment. While that is also true for this biennium, the majority of the increase within this line item stems from a new contract authorizing sports gaming on Lottery terminals.

Challenges

Sports Gaming: As you know, with the passage of House Bill 29 in 2021, the Lottery was tasked with the implementation and regulation of type C sports gaming at retail locations. The legislation allows for up to 20 sportsbooks—or “proprietors”—to sell limited sports gaming products with Lottery retailers who hold certain type D liquor permits. On January 1st, we successfully launched the type C sports gaming program with three proprietors at over 700 retail locations across 63 counties. Since then, we’ve added a fourth proprietor and have increased to more than 800 retail locations. In the weeks and months ahead, we anticipate another two proprietors will begin operating at additional locations.

The effort to launch this new sports gaming framework has required significant time and resources from the Lottery over the past year, and will continue to do so in the next biennium. Additionally, while net revenue from traditional lottery products averages approximately 24 percent of sales, net revenue from sports gaming is generally only 10 percent or less. Therefore, ongoing program costs combined with low profit margins and a new marketplace will result in minimal revenue compared to other major Lottery products and programs. Throughout the biennium, the Lottery will continue to face the unique challenge of ensuring the integrity and responsiveness of multiple systems and proprietors while also promoting profitability and competition.

Aging Gaming System and Infrastructure: FY 2024 will mark the fourteenth year of the Lottery’s central gaming system contract. Much of this system and related infrastructure, including a large portion of our self-service terminals, have been in place since the beginning of the original contract term in 2009. As the industry has advanced over the years, the Lottery and its vendor partners have added more components and features to the system to keep up with evolving consumer and industry trends and expectations. While our current contract has renewal options through FY 2027, system conversions in the lottery industry are generally a multi-year process involving procurement, design, testing, and implementation. Therefore, the Lottery has already begun that process by working with a consultant and issuing an RFI last October for information on a new comprehensive lottery gaming system. We anticipate releasing an RFP in the second half of calendar year 2023.

Revenue Forecast

The Lottery’s budget submission and LPEF commitment rely on revenue forecasts for FY 2024 and FY 2025. While we anticipate positive revenue growth over the next two years, we expect this growth will be modest.

From an industry perspective, lottery sales have largely cooled since the double-digit growth in 2020 and 2021, and we’ve seen the same trends in Ohio. For example, our FY 2022 sales—while the second highest in our history—ended slightly under prior year sales by less than one percent. At the midpoint of this fiscal year, VLT revenue was down by a half percent. And while overall sales were up by three percent, this was due in large part to an unprecedented streak of consecutive billion-dollar jackpots for Mega Millions and Powerball.

Revenue Forecast (\$ in billions)

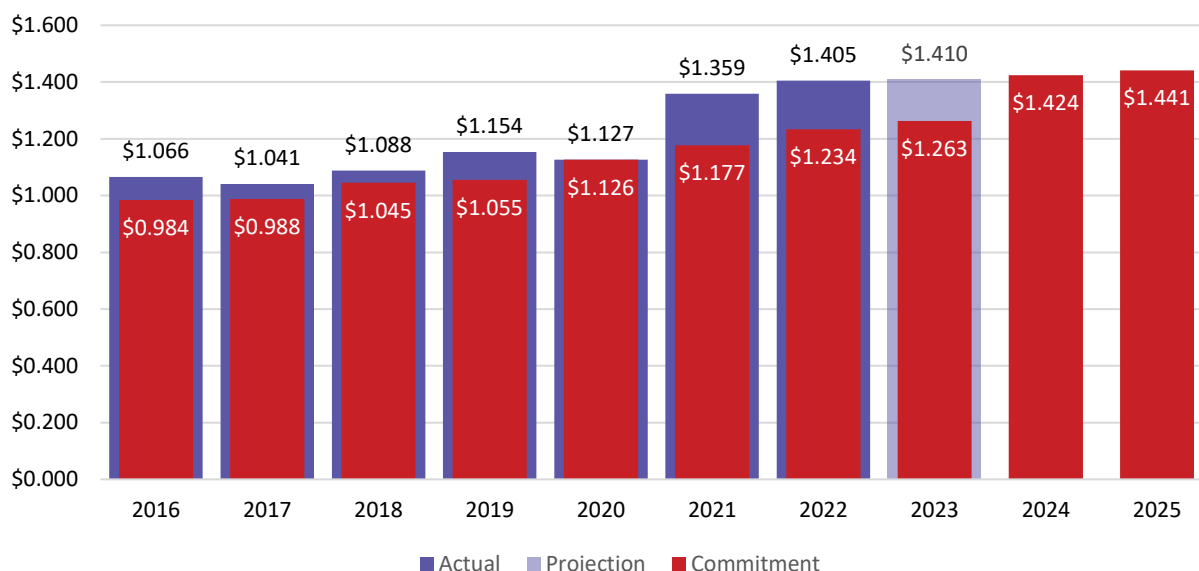
Type	FY 2024	FY 2025
Lottery Sales	\$4.303	\$4.349
VLT Net Revenue	\$1.343	\$1.374
Total Revenue	\$5.646	\$5.723

Over the past years, the Lottery has sought to minimize its reliance on unpredictable multistate game jackpots by diversifying its game portfolio. As such, multistate games now only account for approximately seven percent of annual sales revenue while scratch-off games and monitor games, such as KENO, account for nearly 70 percent of annual revenue. These product lines, along with modest projected increases in VLT revenue, will drive much of the revenue growth in the biennium.

LPEF Profit Transfers

With the aforementioned revenue forecast and budget appropriation request, the Lottery believes it can continue supporting increased profit transfers for education. We project total annual transfers of \$1.42 billion in FY 2024 and \$1.44 billion in FY 2025. These levels represent increases of 1.4 percent and 2.6 percent compared to our record FY 2022 transfer.

LPEF Transfers by Fiscal Year
(\$ in billions)



Since 2016, the Lottery has transferred at least \$1 billion annually to the LPEF and has met or exceeded its commitment each year.

Responsible Gambling

I’d like to conclude my testimony by highlighting several aspects of our responsible gambling program. The Lottery is very proud of its history and partnership with problem gambling stakeholders across the State and country. In 2021, we were the first lottery in the nation to receive an “exceeds standards” rating for our responsible gambling program from the National Council on Problem Gambling. Last October, we received two awards from the North American Association of State and Provincial Lotteries for best responsible gambling digital media campaign and best coordinated campaign. And in December, in partnership with Casino Control, we launched an online portal for our Voluntary Exclusion Program. This portal allows problem gamblers the ability to ban themselves from Ohio’s casinos, racinos, and sports gaming platforms for one year, five years, or for life. Additionally, this update coincided with rebranding the program as “Time Out Ohio” to help reach a broader audience.

Over the next biennium, the Lottery intends to build upon this success and expand its responsible gambling program as new forms of gambling enter the Ohio market. Our increased funding will allow the Lottery to support the establishment of telehealth services specifically to treat gambling disorder, pathological gambling, and co-occurring disorders. Funding will also support expansion of the Ohio for Responsible Gambling (ORG) consortium's new "Pause Before You Play" awareness campaign, which was created specifically to combat problem gambling caused by the recent launch of sports betting. Finally, our funding request will enable the Lottery to expand its own "Keep It Fun Ohio" campaign through the utilization of new marketing strategies to reach at-risk demographics. These efforts will complement our ongoing support of OMHAS, which utilizes our funds to operate gambling disorder treatment centers, hold an annual problem gambling conference, and provide training for gambling disorder counselors throughout Ohio.

Conclusion

The Ohio Lottery is recognized as an industry leader throughout the country, particularly for its responsible gambling programs, marketing efforts, cashless payment options, mobile cashing options, and data analytics. The budget request for fiscal years 2024 and 2025 leverages these and other strengths of the agency to address the challenges we will face. I am confident that our request will provide for the successful attainment of our goals and objectives, as well as continued growth in profits for education.

Thank you,



Pat McDonald
Executive Director