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Joint Committee on Finance

Paper #675

Lottery Fund Condition and Lottery Credit (DOR – Lottery Administration)

[LFB 2023-25 Budget Summary: Page 548, #1, Page 549, #2,
Page 550, #3, #4, & #5, and Page 585, #3]

CURRENT LAW

Operation of the state lottery is the responsibility of the Lottery Division within the Department of Revenue (DOR). The state lottery is the one form of legal gambling in Wisconsin that is operated by the state, utilizing both state employees and contracted services, including private sector retailer outlets for lottery ticket sales.

Funding for the Lottery Division, including prizes, is primarily provided from the segregated (SEG) lottery fund. Additionally, 2021 Act 58 provided \$72.9 million GPR annually in 2021-23 for retailer compensation and vendor fees. The Division is budgeted \$99,320,400 in 2022-23, including \$20,203,400 for general operations, \$57,304,600 for retailer compensation, and \$21,812,400 for vendor fees.

The Lottery Division is authorized 69.7 full-time equivalent (FTE) SEG positions in 2022-23, including one unclassified division administrator. Currently, 29.8 positions are allocated for retailer relations and sales, 16.0 positions for product development and marketing, and the remaining 23.9 positions for other administrative and operational functions. The total revenue available for tax relief is the remaining revenue available after SEG lottery expenditures, minus a statutory reserve (2% of gross revenue). Net revenue available for tax relief depends on actual lottery fund revenues and expenditures and will change with any change in revenue or expenditures.

DISCUSSION POINTS

1. Since the introduction of Assembly Bill 43/Senate Bill 70 (AB 43/SB 70), DOR has reestimated both projected sales and the Lottery Fund condition under current law. Lottery sales have been strong in 2022-23, in large part due to three significant lotto jackpots in the first half of 2022-23. However, revenues in the 2023-25 biennium are not expected to be higher than the estimates included in AB 43/SB 70. Under current law, expenditures from the Lottery fund would equal adjusted base level appropriations, as modified by the Committee under Motion #12. These modifications included standard budget adjustments, including an adjustment to overtime, as well as sum sufficient reestimates of late claim applications for the lottery and gaming credit. In addition, SEG expenditures for prizes, retailer compensation, and vendor fees would be increased to reflect the reestimate of lottery sales. Finally, the amount of SEG revenues available for distribution as the lottery and gaming tax credit would also increase.

2. The amount available for the lottery and gaming tax credit depends on many factors, including lottery sales trends and the opening balance of the lottery fund. Additionally, GPR funding has been provided to pay for certain lottery expenses, in order to increase the amount of lottery and gaming revenues available for the credit. In the previous budget, GPR funding was provided for retailer compensation and vendor fee expenses. Base level GPR funding for these lottery expenses totals \$72.9 million.

3. Table 1 below indicates lottery sales under AB 43/SB 70. These sales amounts are identical to those certified by the Committee in October, 2022.

TABLE 1

**Lottery Sales under AB 43/SB 70
(\$ in Millions)**

<u>Game Type</u>	<u>Actual 2021-22</u>	<u>Estimated 2022-23</u>	<u>Estimated 2023-24</u>	<u>% Change from 2022-23</u>	<u>Estimated 2024-25</u>	<u>% Change from 2023-24</u>
Scratch	\$637.8	\$643.5	\$643.5	0.0%	\$643.5	0.0%
Pull-tab	1.1	1.3	1.3	0.0	1.3	0.0
Lotto	<u>248.9</u>	<u>267.3</u>	<u>267.3</u>	<u>0.0</u>	<u>267.3</u>	<u>0.0</u>
Total	\$887.8	\$912.1	\$912.1	0.0%	\$912.1	0.0%

4. Due to strong sales and the large lotto jackpots mentioned earlier, lottery sales revenues are expected to be higher than earlier estimates for 2022-23. However, for the 2023-25 biennium, current sales estimates are unchanged compared to AB 43/SB 70. As a result, prize payouts and lottery expenditures are also expected to be largely unchanged in the biennium. Table 2 provides current law estimates of lottery sales for 2022-23 and the 2023-25 biennium.

TABLE 2

**Current Law Lottery Sales Projections
(\$ in Millions)**

<u>Game Type</u>	<u>Actual 2021-22</u>	<u>Estimated 2022-23</u>	<u>Estimated 2023-24</u>	<u>% Change from 2022-23</u>	<u>Estimated 2024-25</u>	<u>% Change from 2023-24</u>
Scratch	\$637.8	\$655.6	\$643.5	-1.8%	\$643.5	0.0%
Pull-tab	1.1	1.3	1.3	0.0	1.3	0.0
Lotto	<u>248.9</u>	<u>322.8</u>	<u>267.3</u>	<u>-17.2</u>	<u>267.3</u>	<u>0.0</u>
Total	\$887.8	\$979.7	\$912.1	-6.9%	\$912.1	0.0%

5. In recent years, total lottery sales have generally been increasing. This increase may be attributable to a number of factors, including the COVID-19 pandemic and other economic pressures. A portion of the increase in sales is likely also attributable to higher advertised jackpots for games such as Mega Millions and Powerball. While higher jackpots are unpredictable by nature and can result in fluctuations in annual lotto revenues, a number of factors in recent years have made them more likely. An increase in the price of tickets from \$1 to \$2 (which occurred in 2012 for Powerball and 2017 for Mega Millions) results in more funds going into a jackpot. Changes to the structure of jackpot games have also resulted in a lower probability of winning the jackpot on any individual ticket. As a result, jackpots are more likely to roll over, resulting in further growth. Finally, advertised jackpots are based on the sum of annuity payments that are provided over 30 years. As interest rates have risen across the economy, the value of these annuities has risen accordingly. This results in a higher advertised jackpot, which in turn has led to increased sales. All of these factors may continue to contribute to higher advertised jackpots, and therefore a trend toward higher lottery ticket sales, in the future, although fluctuations will continue to exist.

6. In 2021-22, the amount distributed under the lottery and gaming credit totaled \$340.2 million, including funding for late claims, which provided an average credit of \$230. In October, 2022, the Joint Committee on Finance certified the distribution of \$320.7 million in 2022-23 for the 2022(23) lottery and gaming credit, which would provide an estimated average credit of \$216. This credit amount, which has since been distributed, was based on projected lottery sales for 2022-23 at that time. Currently, 2022-23 sales are projected to exceed the October, 2022, projections. These additional net sales revenues for 2022-23 will lead to a higher opening balance for the Lottery Fund for 2023-24. That opening balance is estimated to be \$43.9 million, an increase of \$25.7 million over the previous estimate. Further, 2023-24 revenues, prize payouts, retailer compensation, and vendor fees will not be changed, as the estimated sales are not expected to increase in the biennium relative to earlier estimates. As a result, the amount available for distribution of the 2023(24) lottery and gaming tax credit will be higher than previously estimated. Table 3 shows the current law lottery fund condition, as well as the amount available for property tax relief.

TABLE 3**Current Law Lottery Fund Condition**

	<u>2023-24</u>	<u>2024-25</u>
Fiscal Year Opening Balance	\$43,939,100	\$18,247,600
Operating Revenues		
Total Ticket Sales	\$912,117,200	\$912,117,200
Retailer Fees and Miscellaneous	<u>262,800</u>	<u>262,800</u>
Gross Revenues	\$912,380,000	\$912,380,000
Expenditures (SEG)		
Prizes	\$578,481,400	\$578,481,400
Retailer Compensation	12,366,800	12,366,800
Vendor Fees	3,483,000	3,483,000
General Program Operations	20,603,700	20,603,700
Gaming Law Enforcement	464,500	464,500
Lottery Credit Administration	337,600	337,600
Program and Other Reserves	<u>235,300</u>	<u>528,700</u>
Total SEG Expenditures	\$615,972,300	\$616,265,700
Expenditures (GPR)		
Retailer Compensation	\$51,999,600	\$51,999,600
Vendor Fees	<u>20,875,400</u>	<u>20,875,400</u>
Total GPR Expenditures	\$72,875,000	\$72,875,000
Net SEG Proceeds	\$296,407,700	\$296,114,300
Interest Earnings	\$1,052,000	\$841,000
Total Available for Tax Relief *	\$341,398,800	\$315,202,900
Appropriations For Tax Relief		
Lottery and Gaming Credit	\$322,301,200	\$296,105,300
Late Lottery and Gaming Credit Applications	<u>850,000</u>	<u>850,000</u>
Total Appropriations for Tax Relief	\$323,151,200	\$296,955,300
Gross Closing Balance	\$18,247,600	\$18,247,600
Reserve (2% of Gross Revenues)	\$18,247,600	\$18,247,600
Net Closing Balance	\$0	\$0

*Opening balance, net SEG proceeds, and interest earnings.

7. Under the current law estimate of the lottery fund condition, \$323,151,200 would be available for property tax relief in 2023-24, and \$296,955,300 would be available in 2024-25, including late claims. Included in this estimate, under Motion #12, is the Committee's earlier decision

to approve the sum sufficient reestimates for lottery late claims of \$850,000 for each year of the biennium. The reestimate of the Lottery Fund condition would establish the appropriation levels listed in Table 3 for lottery expenditures, and would result in reestimated lottery and gaming credits of \$322,301,200 in 2023-24 (a \$45,185,200 increase to base) and \$296,105,300 in 2024-25 (a \$18,989,300 increase to base). The estimated lottery and gaming credit associated with these funding levels would be \$218 in 2023-24 and \$200 in 2024-25. The amounts available for the credit would be higher by \$23,450,500 in 2023-24 and lower by \$971,600 in 2024-25 compared to AB 43/SB 70. [Alternative A1]

8. As mentioned earlier, in recent biennia significant amount of GPR funding has been provided for the lottery program operations. However, in the 2021-23 biennium, GPR funding was limited to just retailer compensation and vendor fees associated with the administration of the lottery. This GPR funding offsets SEG expenditures from the lottery, which in turn increases the amount of SEG available for property tax relief. GPR funding for retailer compensation and vendor fees is provided from two separate sum certain, annual appropriations. If GPR funding is insufficient to pay the full costs of annual retailer compensation and vendor fees, two separate SEG sum sufficient appropriations for these purposes are also available to cover those costs.

9. Under current law, basic retailer compensation is established by statute at 5.5% of the retail price of lotto lottery tickets and 6.25% of the retail price of instant tickets. In addition, the retailer performance program provides an amount of up to 1% of gross lottery sales as incentive payments to retailers. Vendor fees are paid under a major procurement contract for the provision of data processing services to both lotto and instant lottery games.

10. Under AB 43/SB 70, GPR funding for lottery expenditures would remain the same as the past biennium. Any increased funding needed to cover retailer compensation and vendor fees would be provided through the sum sufficient SEG appropriations, estimated at \$15,849,800 SEG annually. Providing additional GPR for these purposes would result in a corresponding increased amount of SEG available for the lottery and gaming credit. The lottery fund condition with these changes is shown in Table 4. Under this fund condition, an additional \$15,849,800 annually would be available for distribution under the lottery and gaming credit, which would result in a total funding level for the credit of \$338,151,000 in 2023-24 (a \$61,035,000 increase to base) and \$311,955,100 in 2024-25 (a \$34,839,100 increase to base). The estimated average lottery and gaming credit associated with these funding levels would be \$228 in 2023-24 and \$210 in 2024-25. Compared to AB 43/SB 70, the amounts available for the credit would be higher by \$39,300,300 in 2023-24 and by \$14,878,200 in 2024-25. [Alternative A2]

TABLE 4**Lottery Fund With Additional GPR for Retailer Compensation and Vendor Fees**

	<u>2023-24</u>	<u>2024-25</u>
Fiscal Year Opening Balance	\$43,939,100	\$18,247,600
Operating Revenues		
Total Ticket Sales	\$912,117,200	\$912,117,200
Retailer Fees and Miscellaneous	<u>262,800</u>	<u>262,800</u>
Gross Revenues	\$912,380,000	\$912,380,000
Expenditures (SEG)		
Prizes	\$578,481,400	\$578,481,400
Retailer Compensation	0	0
Vendor Fees	0	0
General Program Operations	20,603,700	20,603,700
Gaming Law Enforcement	464,500	464,500
Lottery Credit Administration	337,600	337,600
Program and Other Reserves	<u>235,300</u>	<u>528,700</u>
Total SEG Expenditures	\$600,122,500	\$600,415,900
Expenditures (GPR)		
Retailer Compensation	\$64,366,400	\$64,366,400
Vendor Fees	<u>24,358,400</u>	<u>24,358,400</u>
Total GPR Expenditures	\$88,724,800	\$88,724,800
Net SEG Proceeds	\$312,257,500	\$311,964,100
Interest Earnings	\$1,052,000	\$841,000
Total Available for Tax Relief *	\$357,248,600	\$331,052,700
Appropriations For Tax Relief		
Lottery and Gaming Credit	\$338,151,000	\$311,955,100
Late Lottery and Gaming Credit Applications	<u>850,000</u>	<u>850,000</u>
Total Appropriations for Tax Relief	\$339,001,000	\$312,805,100
Gross Closing Balance	\$18,247,600	\$18,247,600
Reserve (2% of Gross Revenues)	\$18,247,600	\$18,247,600
Net Closing Balance	\$0	\$0

*Opening balance, net SEG proceeds and interest earnings.

Lottery Draw Staff

11. AB 43/SB 70 would provide \$42,600 SEG in 2023-24 and \$56,700 SEG in 2024-25 to

the Lottery Division's general operations appropriation to fund an additional full-time position to the lottery draw staff. A similar request was included in the Administration's 2021-23 budget recommendations, but was not included in 2021 Act 58. The additional funding and position are meant to assist with both the increased number of lotto games and the mid-day draws that have been implemented for several lotto games. The Lottery Division currently has three 0.5 full-time equivalent (FTE) positions, in addition to a supervisor.

12. Lottery draw staff are responsible for overseeing daily draws and ensuring the operation of the lottery. Coverage is needed 365 days per year, without exception, for both regular lotto game drawings and special drawings associated with seasonal games. Since the draw staff positions were initially created, the number of both games and draws have increased, which has in turn increased the workload of the staff. In addition, national lottery organizations have discussed potential future increases in draws, which would further increase the workload of the draw staff.

13. The Lottery Division indicates that certain responsibilities have had to be transferred to the Lottery's contracting specialist due to the limited number of positions authorized, and that the workload of the draw staff is currently being met by offering staff additional hours and by hiring limited term employees (LTEs). If the additional position and funding are provided, the Lottery Division indicates that this would allow for additional hours to be provided to two of the existing positions, as well as creating a new 0.5 FTE position. While one LTE position would still be required, two of the existing LTE positions would be able to be eliminated. The additional staffing and hours would also provide the Lottery Division with the ability to transfer responsibilities away from the contracting specialist and back to the draw staff. [Alternative B1]

14. The increased funding for the draw staff would not have an effect on lottery revenues, but would reduce the amounts available for property tax relief in each year in an amount equal to the costs of the position. The reduction to the estimated average credit would be minimal. [Alternative B2]

Lottery Investigators

15. AB 43/SB 70 would also provide \$214,200 in 2023-24 and \$280,500 in 2024-25 to the Lottery Division's general operations appropriation to fund 3.0 lottery investigator positions. The Lottery Division currently has three lottery investigators, overseen by a security director. These investigators are all currently based out of Madison. The Lottery Division indicates if the new lottery investigator positions were approved, one would be based in the northwestern region of the state, one would be based in the northeastern region of the state, and the third would be based in the Milwaukee area.

16. Lottery investigators are responsible for ensuring security for lottery drawings and conducting fraud investigations, as well as investigating and providing information to the public about current and potential scams. They also provide security assessments and training for lottery retailers and assist law enforcement in investigations related to the lottery. In certain cases, lottery investigators can also assist in the verification of lottery tickets.

17. The case load for lottery investigators has been increasing each year since 2019. The

Lottery Division indicates that the level of thefts and other security issues has been increasing as sales have increased, resulting in a greater workload for investigators. Additionally, law enforcement has a greater awareness of the assistance that lottery investigators can provide, resulting in increased requests for assistance.

18. While the existing lottery investigators are all based in Madison, they are responsible for providing services to retailers throughout the state. As of October, 2022, there were over 3,600 retailers statewide. Table 5 below shows the number of retailers in each region of the state. The Lottery Division indicates that lottery retailers outside of the Madison area may receive limited security assessments and in-person security training, due to lack of staffing.

TABLE 5

Lottery Retailer by Region -- 2021-22

<u>Region</u>	<u>For-Profit Retailers</u>	<u>Pull-Tab Only Nonprofit Organizations</u>
Eau Claire	504	37
Green Bay	808	32
Madison	649	45
Milwaukee	1,310	72
Rhineland	<u>383</u>	<u>36</u>
Total	3,654	222

19. Under current staffing levels, and with all investigators based out of Madison, the Lottery Division estimates that it would take nearly five years to visit each retailer for a security assessment. Security assessments and investigations in some regions of the state, particularly those further from Madison, are more logistically complicated, and occasionally require overnight stays. With additional staff based across the state, the Lottery Division estimates that investigators would be able visit all retailers for a security assessment within a one year period. Additionally, the Lottery Division indicates that having an investigator based in the Milwaukee area would enable verification of tickets to a greater extent than what is currently possible at the Milwaukee Lottery offices. This in turn would reduce the amount of time required for the potential payout to be processed, and reduce the workload of investigators based out of the Madison area. [Alternative C1]

20. As shown in Table 5 above, a significant portion of lottery retailers are based in the Milwaukee area of the state. Rather than providing 3.0 FTE that would be spread throughout the state geographically, the Committee could instead provide 1.0 FTE that would be based in the Milwaukee area. In addition to this newly-created position for the Milwaukee region, the Committee could create a further 0.5 FTE, and require the Lottery Division to assign 0.5 FTE in Madison to assist the newly-created 0.5 position with work in the northern region of the state. [Alternative C2]

21. The increased funding for lottery investigators would not have an effect on lottery

revenues. The amount of funding available for property tax relief would be reduced in each year by the amount equal to the costs of the positions, though the reduction to the estimated average credit would likely be minimal. [Alternative C3]

ALTERNATIVES

A. Lottery Fund Condition Reestimate

1. Reestimate the lottery fund condition to reflect projected higher lottery sales under current law. Make the corresponding changes in base level funding for lottery general operations, retailer compensation, and vendor fees, as well as lottery credit expenditures, to reflect lottery sales as follows: (a) increase estimated funding by \$7,061,800 SEG annually to DOR's sum sufficient SEG appropriation for lottery retailer compensation; (b) increase estimated funding by \$2,546,000 SEG annually to DOR's sum sufficient SEG appropriation for vendor fees; and (c) increase estimated funding available for the shared revenue and tax relief (SRTR) sum sufficient lottery credit appropriation by \$45,185,200 SEG in 2023-24 and \$18,989,300 SEG in 2024-25.

ALT A1	Change to Base
SEG (DOR)	\$19,215,600
SEG (SRTR)	<u>64,174,500</u>
Total	\$83,390,100

2. Reestimate the lottery fund condition to reflect projected higher lottery sales under current law, but provide additional GPR funding for the increase in retailer compensation and vendor fees. Make the corresponding changes in base level funding for lottery general operations, retailer compensation, and vendor fees, as well as lottery credit expenditures, to reflect lottery sales as follows: (a) decrease estimated funding by \$5,305,000 SEG annually to DOR's sum sufficient SEG appropriation for lottery retailer compensation; (b) increase estimated funding by \$12,366,800 GPR annually to DOR's sum certain GPR appropriation for lottery retailer compensation; (c) decrease estimated funding by \$937,000 SEG annually to DOR's sum sufficient SEG appropriation for lottery vendor fees; (d) increase estimated funding by \$3,483,000 GPR annually to DOR's sum certain GPR appropriation for lottery vendor fees; and (e) increase estimated funding available for the SRTR sum sufficient lottery credit appropriation by \$61,035,000 SEG in 2023-24 and \$34,839,100 SEG in 2024-25.

ALT A2	Change to Base
GPR (DOR)	\$31,699,600
SEG (DOR)	-12,484,000
SEG (SRTR)	<u>95,874,100</u>
Total	\$115,089,700

B. Lottery Draw Staff

In addition to Alternative A1 or A2, do one of the following:

1. Provide \$42,600 SEG in 2023-24 and \$56,700 SEG in 2024-25 and 1.0 position to the Lottery Division's SEG general operations appropriation.

ALT B1	Change to Base	
	Funding	Positions
SEG	\$99,300	1.00

2. Take no action.

C. Lottery Investigators

In addition to Alternative A1 or A2, do one of the following:

1. Provide \$214,200 SEG in 2023-24 and \$280,500 SEG in 2024-25 and 3.0 positions to the Lottery Division's SEG general operations appropriation.

ALT C1	Change to Base	
	Funding	Positions
SEG	\$494,700	3.00

2. Provide \$107,100 SEG in 2023-24 and \$140,300 SEG in 2024-25 and 1.5 positions to the Lottery Division's SEG general operations appropriation.

ALT C2	Change to Base	
	Funding	Positions
SEG	\$247,400	1.50

3. Take no action.

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