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FISCAL IMPACT REPORT

SPONSOR Smith/McCamley **ORIGINAL DATE** 2/8/17
LAST UPDATED 3/16/17 **HB** _____

SHORT TITLE Transfer of Lottery Funds **SB** 192/aSFC/aHAFC

ANALYST Dulany

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Nonrecurring	Fund Affected
FY17	FY18	FY19		
	See Fiscal Implications			Lottery Tuition Fund

(Parenthesis () Indicate Revenue Decreases)

Relates to HB 237/HTRCS/HF15/aHF1#1 & HB 250/HBICS/aHF1#1

SOURCES OF INFORMATION

LFC Files
 Think New Mexico
 North American Association of State and Provincial Lotteries (NASPL)

Responses Received From

New Mexico Lottery Authority (NMLA)
 Higher Education Department (HED)

Other Responses

Think New Mexico
 North American Association of State and Provincial Lotteries (NASPL)

SUMMARY

Synopsis of House Appropriations and Finance Committee Amendments

The House Appropriations and Finance Committee amendment would require net transfers of revenue “upon the effective date of [SB 192] through June 30, 2022, or until the end of a fiscal year in which the total net revenue transfers to the lottery tuition fund are less than [\$38 million], whichever occurs first...”

Synopsis of Senate Floor Action

SB 192 as passed by the Senate no longer contains an emergency clause.

Synopsis of Senate Finance Committee Amendments

The Senate Finance Committee amendments require NMLA to transmit all net revenue to the lottery tuition fund between the time the bill is enacted through June 30, 2022. After June 30, 2022, the current 30 percent transfer requirement of gross lottery revenues to the lottery tuition fund would again apply. The amendments also add an emergency clause to the bill.

Synopsis of Original Bill

Senate Bill 192 amends the New Mexico Lottery Act to the 30 percent gross revenue transfer requirement to the lottery tuition fund and replaces it with a requirement that NMLA transmit all net revenue to the lottery tuition fund. Estimated net revenue is to be transmitted monthly, provided that the total amount of annual net revenue for a fiscal year shall be transmitted no later than August 1 following the end of that fiscal year.

FISCAL IMPLICATIONS

HED states, “The change to an annual distribution of net revenue cannot ensure additional revenue from year-to-year. A decrease in net revenue resulting from increased operating expenses would reduce revenues to the Lottery Tuition Fund.” In FY17, the Legislative Lottery Tuition Scholarship pays 90 percent of average tuition rates. Scholarship amounts are expected to decline to 60-70 percent of average tuition rates in FY18 due to the loss of Liquor Excise Tax revenues supporting scholarships.

NMLA Analysis of Scratcher Sales

NMLA suggests removal of the mandatory 30 percent gross revenue requirement may result in increased prizes in scratcher games, “which will ultimately increase the actual dollars returned for deposit in the lottery tuition fund.” NMLA further suggests this would align the lottery’s business operations with industry best practices across the U.S.

NMLA has advocated for the removal of the mandatory 30 percent transfer requirement in recent years, suggesting higher prize payouts translate to increases in sales and transfers to the lottery tuition fund for scholarships. NMLA cites historical scratcher sales figures as evidence, noting between FY04 and FY07, New Mexico Lottery scratcher sales grew by approximately 4.6 percent per year. In FY07, according to NMLA, scratcher sales peaked at \$91.4 million. NMLA asserts passage of legislation in 2007 requiring a specified percentage of gross lottery revenues be transferred for scholarships contributed to a slide in scratcher sales between FY08 and FY14. To meet the monthly transfer requirement, NMLA states, the authority cut budgets, operations, and expenses to identify \$6.5 million in reductions. NMLA further states the bulk of budget cuts resulted from reduced scratcher prize payouts. Between FY07 and FY14, according to the authority, scratcher annual sales decreased approximately 24 percent:

- \$86.6 million in FY08
- \$80.6 million in FY09
- \$78.4 million in FY10
- \$75.8 million in FY11
- \$68.7 million in FY12
- \$69.9 million in FY13
- \$69.8 million in FY14

NMLA attributes a recovery in gross revenues in scratcher sales in FY15 and FY16 to increased prize payouts accomplished through reduced administrative costs. NMLA has also reported it uses the unclaimed prize pool to enhance scratcher prize payouts. The two prior year scratcher sales total:

- \$80.0 million in FY15
- \$83.1 million in FY16.

LFC staff cannot verify with certainty that the mandatory distributions to the lottery tuition fund was the cause of the decline in scratcher sales between FY07 and FY14.

NMLA indicates the increased prize payouts in FY15 and FY16 cannot be sustained in FY17 due to increased online vendor cost coupled with a mandated percentage return. “Thus,” according to NMLA, “Scratcher sales have once again decreased in FY17 to \$35.7 [million year-to-date] as of December 2016.” Scratcher sales for the same time period in FY16 totaled \$38.4 million. NMLA projects FY17 year-end scratcher sales to be \$70 million for FY17, compared with \$83.1 million in FY16.

NMLA asserts, “Since 2007, the falling Scratcher sales have resulted in a projected loss of approximately \$35-50 million in revenue to the Legislative Lottery Scholarship.”

HED points out gross revenues for all lottery games in the first two quarters of FY17 (\$64.6 million) have increased slightly over revenues in the first two quarters of FY16 (\$63.3 million).

NMLA cites data from International Gaming Technology (IGT), a vendor of lottery and gaming products and services, suggesting the state could anticipate increases in scratcher profitability between FY17 and FY22 if NMLA were able to set higher prize payout levels for the each scratcher ticket price point:

New Mexico Lottery Payout Levels							
Price	\$1	\$2	\$3	\$5	\$10	\$20	Aggregate Payout
2007 Payout at Peak	60.0%	62.0%	63.0%	64.0%	70.0%	75.0%	64.1%
FY14 Payout Levels	56.0%	57.8%	57.6%	60.7%	65.3%	68.1%	60.1%
Recommended Payout Levels	58.0%	63.0%	64.0%	68.0%	72.0%	75.0%	68.0%

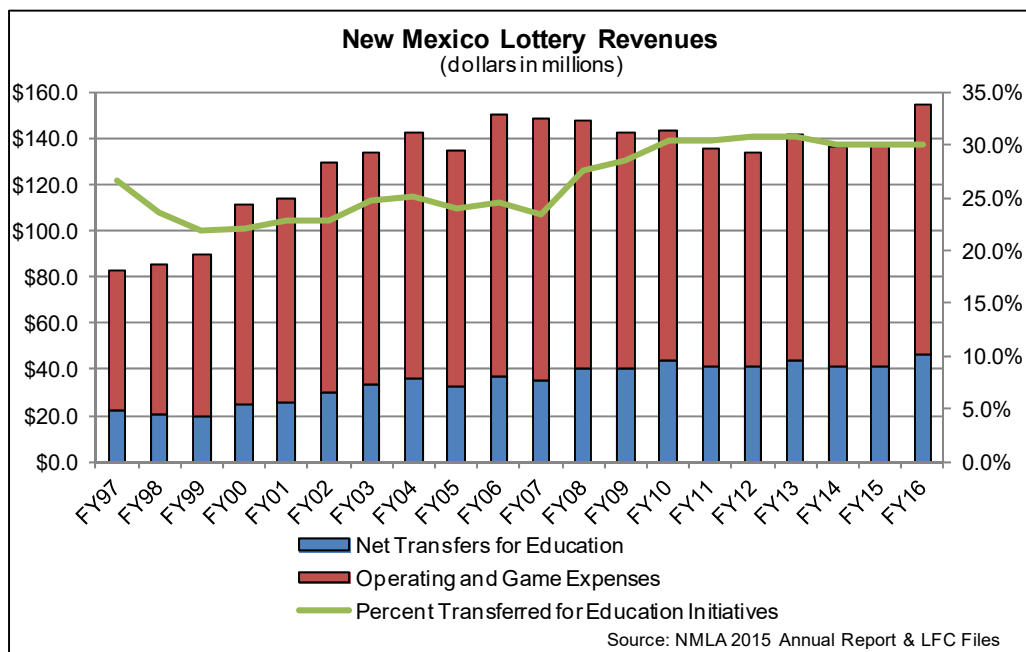
Source: IGT analysis provided to NMLA

According to the data from IGT cited by NMLA, based on the payout increases suggested above “a level increase in overall scratcher profitability of an additional \$11.1 million (40.7 percent increase) by FY22 is expected versus FY17 performance.” The analysis indicates a total profit increase between FY18 and FY22 of \$27.7 million.

Revenues Prior to FY08

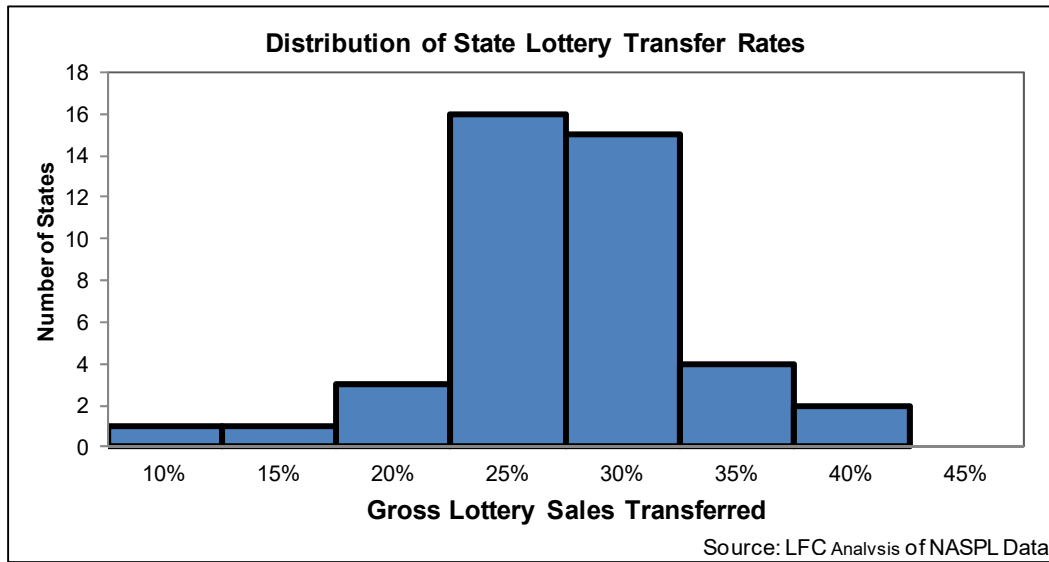
Effective in FY08, a mandatory return of gross revenues was enacted in New Mexico statute. The mandatory transfer to the lottery tuition fund was initially 27 percent and eventually increased to 30 percent of gross revenues. Prior to FY08, statute mandated the “authority shall transmit all net revenues to the state treasurer, who shall deposit them in the lottery tuition fund,” which is identical to the language contained in SB 192.

Between FY97 and FY07, under the language requiring a transfer of all net revenues, NMLA transmitted an aggregate of 23.8 percent of gross revenues for scholarships and other education initiatives. This excludes FY96 because lottery revenues were only received for part of that fiscal year. The graph below shows overall lottery revenues and the percent of gross revenue transferred for each fiscal year since the FY97:



SIGNIFICANT ISSUES

Analysis of North American Association of State and Provincial Lotteries (NASPL) data from FY14 by LFC staff indicates New Mexico’s current transfer rate of 30 percent is in line with other states in the nation:



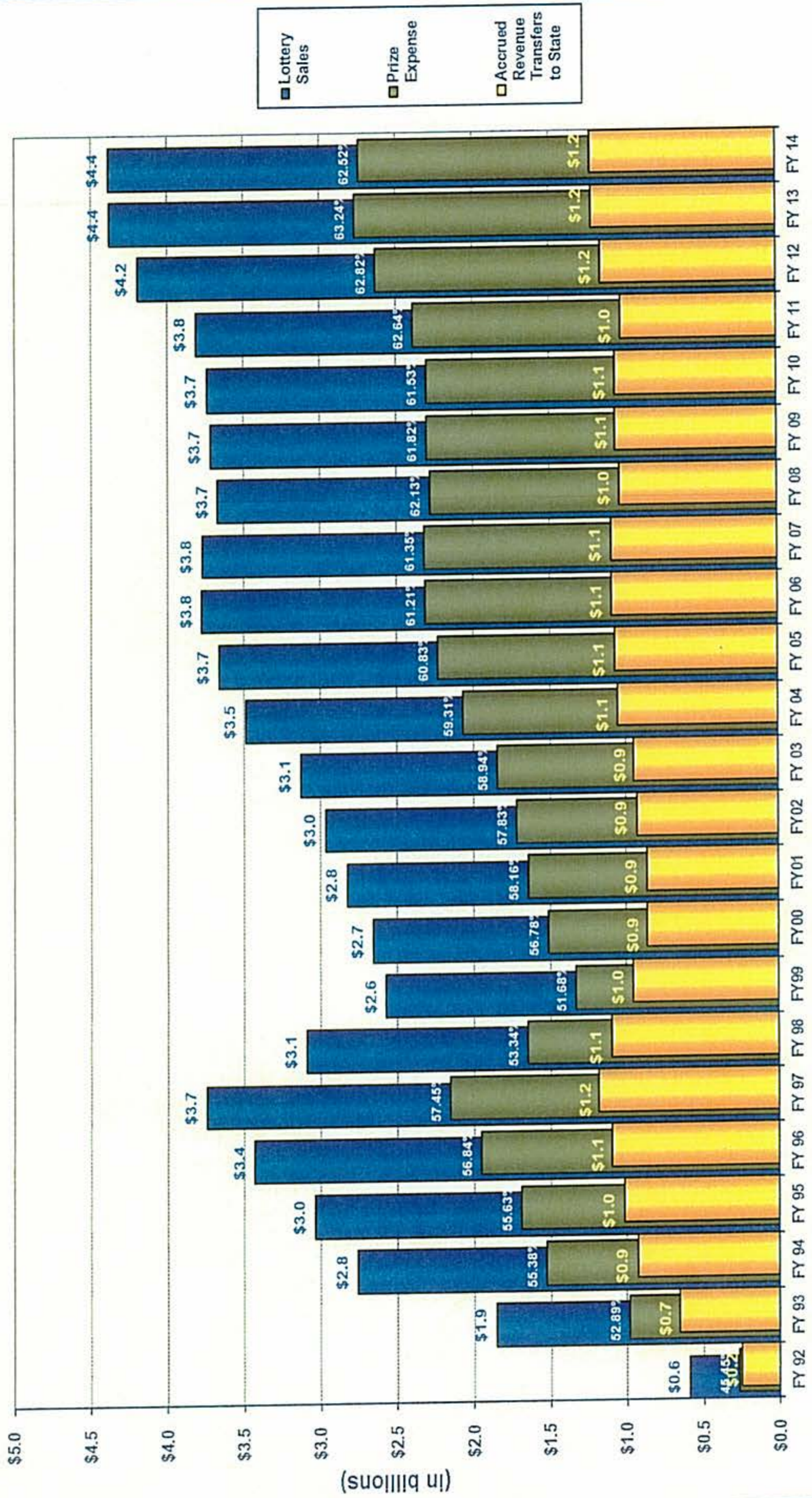
RELATIONSHIP

HB 237 extends the distribution of Liquor Excise Tax revenues to the lottery tuition fund through FY20.

HB 250 ties bonuses or incentive compensation paid to officers of NMLA, vendors, and retailers to the increase in lottery ticket sales revenue transmitted to the lottery tuition fund. HB 250 also requires money from unclaimed prizes be transmitted to the lottery tuition fund and prohibits any style of video lottery game.

TD/jle/al/jle

Texas Lottery Commission Sales, Prize Expense, and Transfer FY 1992-2014



Note: Prize Expense as a % of Sales is net of reduction for unclaimed prizes; Prize Payout capped at 52% for FY 98-99 Biennium; Prize Payout Cap was repealed in FY 2000, but a provision linking the Advertising Budget to the Prize Payout % was adopted as outlined in Section 466.015(d) of the State Lottery Account; The Advertising provision was repealed by the 81st Legislature.