

# Arizona State Lottery Commission (Report Highlights)

June 2002

The Lottery was established by a vote of the people in 1980 and began operating in 1981. The Arizona State Lottery Commission’s purpose, as expressed in statute, is to “*oversee a state lottery to produce the maximum amount of net revenue consonant with the dignity of the State.*” Since 1981, the Lottery has:

- ✚ Received \$4.1 billion in revenues.
- ✚ Paid more than \$2.7 billion in prizes.
- ✚ Distributed \$1.4 billion to the State and its programs.

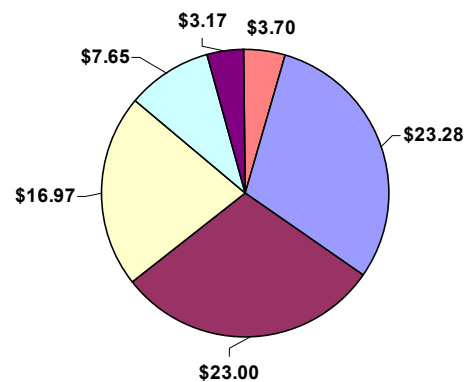
**Our Conclusions:** While the Lottery has made improvements to increase sales, it should explore several options—including greater use of instant-ticket vending machines and new types of games—for further increasing sales. The Lottery should also improve its compliance inspection and underage wagering enforcement programs. Finally, the Lottery has made many operational improvements since our 1997 audit, but needs to make a few more.

**The Lottery Should Do More To Maximize Sales**

**Programs benefited**—Approximately 28.4 percent of each Lottery dollar goes to several beneficiary funds that support state programs. The two biggest recipients of fiscal year 2001 revenues were the State General Fund and the Local Transportation Assistance Fund, which cities and towns use to support transportation and arts programs. (See Figure 1.) The Lottery also distributed \$1.5 million to the Court-Appointed Special Advocate Program from unclaimed prizes.

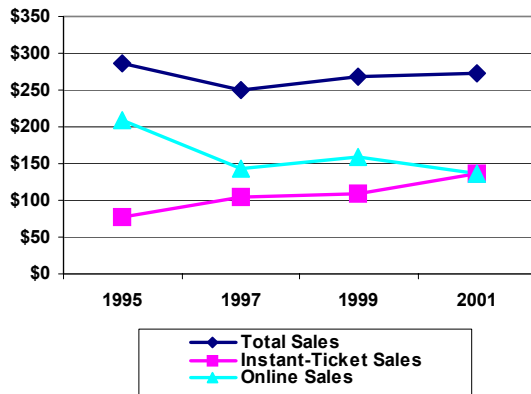
**Overall sales unchanged**—Although the Lottery is intended to produce revenue for the State, its sales have remained relatively unchanged since 1994. While instant-ticket sales have been increasing, online ticket sales have decreased. (See Figure 2, page 2.)

**Figure 1: Lottery Monies’ Distribution To Beneficiary Funds in 2001 (in Millions)**



- Mass Transit Fund
- State General Fund
- Local Transportation Assistance Fund
- State Heritage Fund
- County Assistance Fund
- Commerce and Economic Development Fund

**Figure 2:**  
**Lottery Sales Comparison**



**Increased prizes reduce funding**—In 1997, in an attempt to increase sales, the Legislature increased the prizes for the Lottery games by decreasing the State’s take of the revenue. Although instant game sales increased by 30 percent in the 4 years since this change, the monies distributed to the programs from instant-ticket games decreased 12 percent.

**Improving sales**—The Lottery can make several improvements to increase sales and produce more revenue for the State and its programs.

The Lottery can increase the use of instant-ticket vending machines. These vending machines have been shown to increase instant-ticket sales by up to 38 percent. When the Lottery added 100 of these vending machines in 2001, sales at those 100 locations increased from \$4.37 million the year before to \$6.04 million.

**Instant-Ticket Vending Machine**



However, instant-ticket vending machines were at only 8 percent of the Arizona Lottery retailers in fiscal year 2000, less than half the average of other state lotteries. The Lottery should determine how many additional retailers would benefit from these vending machines and seek the needed funding.

Other states have increased sales by implementing pull-tab instant tickets. Pull-tabs have a paper tab that the player pulls off to reveal the prize. These tickets are generally sold in 25- and 50-cent denominations, often in bars and restaurants. In Missouri and Kentucky, pull-tabs accounted for 10 percent of their fiscal year 2000 sales. The Lottery’s statutes allow it to offer different game play-styles, which include pull-tab instant tickets. Pull-tab tickets might allow the Lottery to increase sales in restaurants and bars. Currently, there are only 35 restaurants and bars in Arizona that sell Lottery tickets.

**Instant Games—“Scratchers”**

- ✚ 29 different games in 2001
- ✚ \$1, \$2, \$3, and \$5 games
- ✚ 2001 revenues = \$136.9 million

**Online Games**

- ✚ The Pick, Fantasy 5, Pick3
- ✚ PowerBall (21 states participate)
- ✚ 2001 revenues = \$135.8 million

Some states also have higher denomination instant-tickets. Arizona’s highest-priced ticket is \$5, while some other states offer \$7 and \$10 tickets. These higher-priced tickets account for 16.5 percent to 27 percent of some of these states’ sales.

Lottery sales staff can also be used more effectively. The Lottery plans to contract the delivery of instant tickets. This will give the sales staff more time for sales activities, including informing retailers about new games, promoting incentive programs, discussing product displays, troubleshooting machines, recruiting new retailers, and addressing retailer concerns.

### The Lottery should:

- ✓ Identify retailers who might benefit from instant-ticket vending machines and seek funding for additional machines.
- ✓ Develop and submit to the Lottery Commission a plan to implement pull-tab instant tickets.
- ✓ Plan to offer higher-priced instant tickets.
- ✓ Proceed with plans to contract delivery of instant tickets and use its sales staff for sales activities.

### Lottery Should Improve Inspections and Underage Wagering Activities

In 2000, the Lottery adopted an ambitious goal to perform compliance inspections of every retailer every year. The inspections check retailers' compliance with regulations relating to terminal operation, prize payment limitations, employee training, and enforcement of underage wagering laws. However, higher priorities, such as investigating thefts and retailer and public

complaints, resulted in only 42 percent (1,122) of retailers receiving inspections. Further, the inspectors found only minor problems. The Lottery now plans to cut the inspections back to nearly 19 percent (500) of retailers a year. It should adopt a plan for identifying how many and which retailers to inspect.

Although reducing the number of inspections appears appropriate, the Lottery should track inspection results. The Lottery has an inspection database, but has not entered violation information. Such information would assist in identifying common problems and could then be used to enhance retailer training and education.

The Lottery also needs to take additional steps to monitor underage wagering. This is particularly important now because the legal age for purchasing Lottery tickets will increase from 18 to 21 in June 2003. The Lottery should develop a comprehensive program to deter underage wagering that includes:

- ✚ Revising the inspection checklist to address whether retailer staff know the minimum age requirements.
- ✚ Increasing the use of age limit signs in stores.
- ✚ Adopting training standards for retailers that will help remind them to check a player's age.

## The Lottery should:

- ✓ Develop a systematic plan for inspecting fewer retailers each year;
- ✓ Record the results of its inspections in its database to help identify common problems and enhance retailer training and education accordingly; and
- ✓ Improve monitoring of underage wagering.

### Recent Operational Improvements Can Be Enhanced

The Lottery has enhanced several management practices since our 1997 audit and should make some additional improvements.

For example, the Lottery has strengthened oversight of retailers through such things as collection policies and procedures and enforcement of minimum sales rules. It has also improved internal controls over cash handling and reduced cash balances on hand at claims stores. The Lottery has also hired an experienced procurement administrator and improved computer operations and security procedures.

Lottery claims store



The Lottery should improve in some other areas. The Lottery has been incorrectly paying revenues from two games to the Local Transportation Assistance Fund and the County Assistance Fund before making payments to the Heritage Fund. While this did not affect the amount ultimately distributed to the three funds, it delayed payments to the Heritage Fund until late in the fiscal year. The Lottery can also improve its accounting procedures by adopting additional written procedures to cover accounting functions that are unique to the Lottery, such as automated weekly revenue collections from retailers.

## The Lottery should:

- ✓ Follow statutory requirements for the distribution of game revenues.
- ✓ Adopt additional accounting procedures for Lottery-specific transactions.

### To Obtain More Information

- A copy of the full report can be obtained by calling (602) 553-0333 or by visiting our Web site at:

[www.auditor.gen.state.az.us](http://www.auditor.gen.state.az.us)

- The contact person for this report is *Shan Hays*.