

The Arizona Republic

Arizona Lottery revenue has grown, but tracking how funds are used proves difficult

By Alia Beard Rau The Republic | azcentral.com Dec. 1, 2013

Every week, thousands of Arizonans fork over a few dollars, and often more, for a handful of Lottery tickets and a head full of dreams.

For the players, it's about buying hope — a chance at a lifestyle they would likely not otherwise obtain. But the real winner in this game is the state, and it seems it has become addicted to the revenue.

The Arizona Lottery's sales revenue over the past 30 years totals more than \$9.8 billion, with \$1.3 billion of that going to the state general fund. In fiscal 2013 alone, \$117 million, or 17 percent, of the Lottery's \$694 million in annual revenue landed in the general fund.

That wasn't the deal sold to voters when they approved the Lottery in 1980 — and several more times since then.

Since its inception, the Lottery has marketed itself as a way to help the people and places of Arizona. Its advertising focuses on how revenue goes to education, health and public welfare, the environment and economic development.

But its marketing can be misleading.

An *Arizona Republic* analysis of 30 years of Arizona Lottery revenue and disbursements found that the Lottery has met at least the minimum requirements set by voters and lawmakers for allocations to those key areas over the years. Yet as Lottery revenue has grown, particularly in recent years, less money has gone to those promised areas of focus, while more has gone toward prizes and retailer bonuses — and into the state's general fund, where it is impossible to track how specific general-fund dollars are spent. That revenue might have gone to schools and public-welfare programs as promised, or it might have gone to prisons and lawmaker pensions.

The Lottery, overseen by a five-member, governor-appointed commission and an executive director, controls the marketing. But it's the Legislature that has taken control of where the revenue is allocated.

In fiscal 2013, \$59.6 million — 8.6 percent of the Lottery’s \$694 million in annual revenue — went directly to programs touted to voters. Despite popular belief, no Lottery money has gone directly to K-12 education.

During tight budget years, particularly 2010, the Arizona Legislature used Lottery revenue as an emergency fund. Money normally directed by lawmakers toward advertised programs like public transportation and forest health was diverted into the general fund to balance the state budget.

“In Arizona, where the Lottery has been in place for so long, it is now seen as an absolutely indispensable source of revenue — particularly in times when state budgets are very, very tight,” said Patrick Pierce, political-science professor at St. Mary’s College in Indiana and author of “Gambling Politics: State Government and the Business of Betting.”

Though the state Legislature’s Republican body once decried the creation of a Lottery as a sinful vice, there is no longer mention of eliminating it — especially as Lottery proceeds have risen while other revenue has faltered.

“The current Arizona Legislature would never approve the Lottery, in my opinion,” said House Appropriations Chairman John Kavanagh, R-Fountain Hills. “But it won’t be repealed because there’s no way we could replace the money.”

The Lottery website boasts it has generated a lifetime total of more than \$1 billion for economic development, \$833million for education, \$415 million for the environment and \$732 million for health and public welfare.

But those numbers are deceiving.

No Lottery revenue has ever been given directly to K-12 education, according to state budget documents. In its education total, the Lottery counts \$752 million given to the general fund, \$32 million to pregnancy prevention, \$21 million to disease-control research and \$27 million to repay university bonding for building construction.

Annual Lottery Revenue

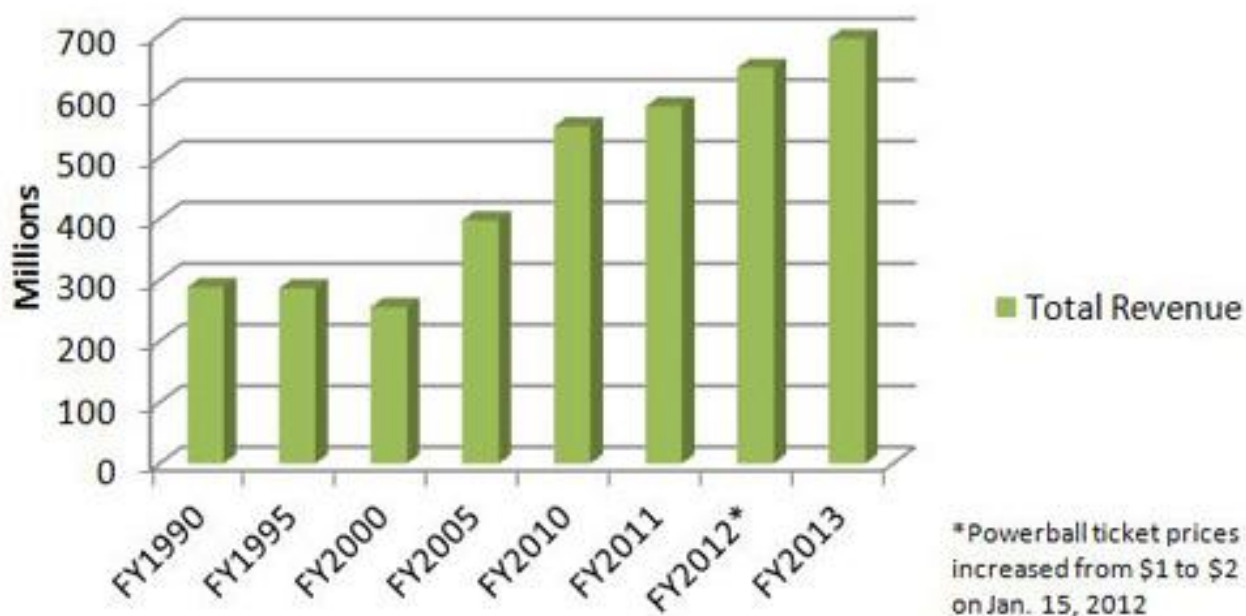


Illustration by: Ginger Rough/The Republic

Arizona Lottery revenue grew from \$551 million in fiscal 2010 to \$694 million in fiscal 2013.

The Lottery website advertises that “education receives 55.5 percent of the Lottery’s general fund total,” and states that was nearly \$65 million this past fiscal year. Lottery officials conceded in an e-mail that that’s how much the Legislature “should” allocate to education, and they admit that there is no way to know if it is actually happening. Nothing in state statute requires it.

However, Arizona Lottery Budget, Products and Communications Director Karen Bach said the Lottery is confident the spending from the general fund mirrors the directives of the Legislative Budget Process as specified in the Joint Legislative Budget Committee (JLBC) Appropriations Report.

However, she said the 2013 figures posted on the Lottery’s website are unaudited and will not be finalized until the end of the year.

No Lottery officials were available to discuss the discrepancy in marketing materials and allocations, and the e-mail did not elaborate on that topic.

Similarly, \$548 million counted under health and public welfare was also given directly to the general fund as opposed to a specific health or public-welfare program.

For the programs that were given money directly from the Lottery, many have seen the amount they get fall even as annual Lottery revenue has more than doubled since 1990.

For example, Arizona Lottery revenue grew from \$551 million in fiscal 2010 to \$694 million in fiscal 2013.

The economic-development fund got \$3.5 million in fiscal 2013, compared with \$5.7 million in fiscal 2010. The Heritage Fund, which benefits the environment, got \$10 million in fiscal 2013, compared with \$16 million in 2010.

And funding for transportation slipped from \$17.8 million in 2010 to \$11.2million in fiscal 2013.

Health and public-welfare program recipients, which include teen-pregnancy-prevention programs and food assistance for children and mothers, did see an increase from \$18.7 million in 2010 to \$19.6 million in 2013.

Arizona voters approved the creation of the Arizona Lottery in 1980 by a narrow margin.

Ballot literature promised proceeds would “pay for law enforcement, health services, education and other vital programs.” But the proposition wording required only that at least 30 percent of revenue go into the general fund. The governor and Legislature could distribute the general-fund revenue as they chose.

In 1990, voters required that \$20 million in Lottery revenue a year go into heritage funds for Arizona State Parks and the Arizona Game and Fish Department. The heritage funds were to be paid annually before the general fund landed its share.

Lawmakers in 1993 required up to \$23million a year in Lottery revenue to be put into a fund for local transit projects, and up to \$7.6 million a year to be divided among counties. The law required that the general fund get at least \$45 million before any other fund was paid, instead of the original 30 percent requirement.

In 1996, voters added yet another provision: that \$17 million in revenue be spent annually on specific health and social-service programs, including teen-pregnancy prevention, food assistance for infants and mothers, and disease research.

In 1998, as casinos opened and Lottery revenue fell, then-House Speaker Jeff Grosco led an effort asking voters to decide the Lottery’s fate. He fought to kill the Lottery, saying it had been fraught with mismanagement and fraud. Church leaders advocated against the Lottery, calling it moral poison.

Various non-profit organizations pushed to keep it. Their election literature criticized the Legislature for not spending the money as promised.

“Legislators argued that Powerball money was ‘not Lottery’ and endorsed the little rule they had made for themselves legislatively that the first 25 or so million (dollars) from Powerball was theirs to spend as they decide, leaving no money for projects as the voters have decided,” said an election argument from Healthy Arizona Coalition.

Voters that year, and again in 2002, chose to keep the Lottery.

In 2010, the Legislature didn’t bother with a public vote, electing itself to extend the Lottery through 2035. The same year, lawmakers borrowed against future Lottery revenue, eliminated allocations to the counties and essentially cut in half Lottery allocations to both the transportation fund and the heritage funds, sweeping nearly an extra \$30 million a year into the general fund.

Moral arguments against the Lottery have vanished with rising dependency on revenue.

“Opponents once argued that states should not be involved in running a service that preyed upon human weakness and led citizens to what they saw as an essential immoral behavior,” Pierce, the St. Mary’s political-science professor, said. “That just sounds silly now.”

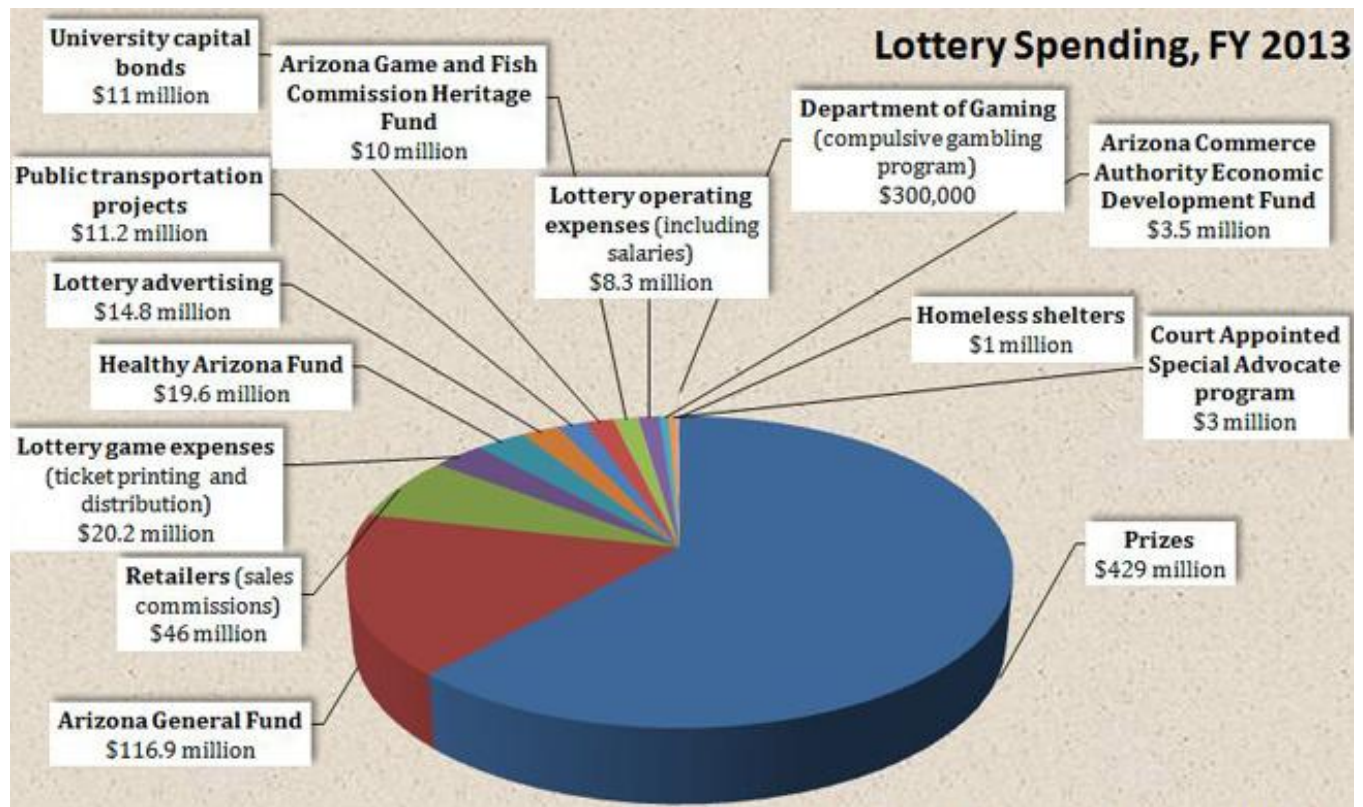


Illustration by Ginger Rough/The Republic

Many Lottery players, and some state lawmakers, concede they don't know where ticket revenues go.

Officials continue to sell it as a public benefit.

“We need the Lottery to generate funds for good causes for Arizona like education, health and public welfare, economic and business development and the environment,” Bach said.

Of the \$694 million taken in the most recent fiscal year, \$11.2 million went to public-transportation projects and \$3.5million to the Arizona Commerce Authority. The Game and Fish Department Heritage Fund, which supports outdoor recreation and protects critical wildlife, got \$10 million; health and welfare programs, \$19.6 million. Homeless shelters took home \$1 million, and a state program for problem gamblers got \$300,000.

“Without the Lottery, many of these programs would not exist,” said Kerry Carmichael of Tempe, a Powerball regular who with his wife, Diane, won \$2.5million in 1995 and \$1 million in March.

That common public perception is cultivated by Lottery marketing. Designated programs have received hundreds of millions of dollars over the years, and Lottery officials tout those benefits.

Yet Pierce argued that there's no evidence to show that Lottery disbursements to even the designated programs truly improve services in any of those areas.

"Even when the revenue is dedicated for a particular purpose, you can't really trace them," Pierce said. "You don't know for sure that those are dollars added on top of what legislators would have appropriated."

Senate President Andy Biggs, R-Gilbert, who usually prides himself on his budget knowledge, concedes he has no idea where Lottery revenue goes — nor do players.

"I don't think people even think about where it goes," he said.

By statute, the Lottery is permitted to spend up to 18.5 percent of revenue on operating and game expenses, including ticket printing, distribution, online-vendor fees, advertising and retailer sales commissions. While revenue has risen, its operating budget hasn't changed dramatically in more than a decade.

Last fiscal year, its operating budget, which includes employing 98 people, totaled \$8.3 million plus \$20 million for game expenses — equaling 4 percent of revenue.

Its big boost in spending over the years has been in advertising, which grew from \$6 million in 2002 to more than \$14 million last fiscal year. That covers sponsoring events, paying public-relations company Lane Terralever and marketing new games, all with the goal of hooking Arizonans.

Commissions to retailers have also grown, particularly in recent years, as revenue has spiked. Retailers got \$46million last fiscal year compared with \$26.5 million in 2005.

With growth in those areas, the Lottery is nearing its 18.5 percent limit. Last fiscal year, those costs hit about 13 percent. According to the Lottery's strategic plan, it intends to ask the Legislature for an additional 10 percent in the marketing budget.

The bigger the pot, the more people play. Arizona Lottery announced in October that the multistate Mega Millions was boosting its jackpot from at least \$12 million to at least \$15 million and adding a \$1 million second prize. Record-breaking multistate Powerball games, and a \$587 million Arizona winner last November, helped attract Lottery players.

"Powerball is the gateway game for new players," Bach said.

And the Lottery isn't stingy with its winners: In fiscal 2013, 61.9 percent of revenue went to prize money. Statute requires at least 50 percent goes back to the players.

Bach said one goal is to introduce new games to attract new players while at the same time retaining core players.

According to the Lottery's analysis, the average state player is White, 52 years old, likely attended college and has a median annual income of \$53,630. A push is on to bring in younger buyers.

This year, the Lottery introduced Ghostbusters and Duck Dynasty Scratchers tickets, joined Instagram and gave away concert tickets.

Bach said the Lottery is in the process of finishing a study targeting 20-somethings.

As the Lottery works to fatten revenue, Arizona's counties plan to fight to restore their share of the winnings. Officials have begun talks with state lawmakers in the hopes of making that happen next session.

Until 2010, the state's 13 rural counties each landed \$550,000 a year in Lottery revenue, while Pima and Maricopa counties each got \$250,000. The counties would like to restore the funding at those levels again.

Some Democratic state lawmakers have mentioned an interest in trying to restore revenue for mass transit as well.

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