

# **CALIFORNIA LOTTERY**

Report of Analysis

## **QUARTERLY TRANSFER OF FUNDS TO PUBLIC EDUCATION**

*For the Quarter Ended March 31, 2013*



**JOHN CHIANG**  
California State Controller

November 2013



**JOHN CHIANG**  
**California State Controller**

November 15, 2013

California Lottery Commission  
700 North Tenth Street  
Sacramento, California 95811

Dear Commissioners:

The State Controller's Office analyzed the financial documentation supporting the California Lottery's (Lottery) transfer of funds to the public education community for the quarter ended March 31, 2013. Our analysis found that the transfer amount of \$327,581,533 appears to be supported by the Lottery's accounting records, and that the Lottery is on target to comply with the annual statutory percentages for prizes, education, and administration.

If you have any questions, please call Andrew Finlayson, Chief, State Agency Audits Bureau, at (916) 324-6310.

Sincerely,

*Original signed by*

**JEFFREY V. BROWNFIELD, CPA**  
Chief, Division of Audits

JVB/nh

cc: Nathaniel Kirtman III, Commissioner  
California Lottery Commission  
John Smolin, Commissioner  
California Lottery Commission  
Connie M. Perez, Commissioner  
California Lottery Commission  
Gregory Ahern, Commissioner  
California Lottery Commission  
Paula D. LaBrie, Acting Director  
California Lottery  
Nicholas Buchen, Deputy Director, Finance  
California Lottery  
Roberto Zavala, Chief Internal Auditor  
California Lottery

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# Report of Analysis

## Summary

In a letter dated May 16, 2013, the California Lottery (Lottery) requested that the State Controller's Office (SCO) transfer \$327,581,533 to the Lottery Education Fund for disbursement to the public education community. Our analysis found that the transfer amount appears to be supported by the Lottery's accounting records and that the Lottery is on target to comply with the annual statutory percentages for prizes, education, and administration.

On June 25, 2013, the SCO transferred \$327,581,533 to the Lottery Education Fund. Due to the SCO's apportionment process, all funds except \$23.73 were disbursed to the public education community. This balance will remain in the Lottery Education Fund to be apportioned during the next quarterly transfer.

## Introduction

This report presents the results of our analysis of the Lottery's quarterly request that the SCO transfer funds to the public education community. This analysis is part of our responsibility under the California State Lottery Act (Lottery Act). We performed this analysis to determine if the transfer of funds to the public education community was supported by amounts recorded in the Lottery's accounting records and to determine if the Lottery is on target to comply with the annual Lottery Education Fund allocation requirements contained in the Lottery Act.

## Background

In 1984, California voters passed an initiative which, by amending the State Constitution, authorized a state-operated lottery. The initiative created the Lottery Act, which requires the quarterly transfer of net revenues to the public education community and established the allocation percentages for lottery funds. The Lottery Act also requires the SCO to conduct quarterly and annual post-audits of all accounts and transactions of the California Lottery Commission and other special post-audits as the State Controller deems necessary.

The Lottery Act was amended by Assembly Bill 142 on April 8, 2010. The bill was an urgency statute that went into effect immediately. Assembly Bill 142 requires revenues from the Lottery to be allocated to maximize the amount of funding allocated to the public education community. The bill requires that not less than 87% of the total annual revenues from Lottery ticket sales be returned to the public in the form of prizes and funds to education and not more than 13% be allocated for Lottery expenses. The bill specified that not less than 50% of the total annual Lottery revenues, in an amount to be determined by the Lottery Commission, be returned to the public in the form of prizes. In addition, the bill requires the Lottery Commission to establish the percentages to be allocated to the benefit of public education.

Each quarter, the Lottery requests that the SCO transfer net revenues to the public education community (see Attachment). The Lottery request usually occurs eight to ten weeks after the close of the quarter.

## Objectives, Scope, and Methodology

We performed this analysis of the quarterly transfer of funds to the public education community in order to determine if:

- The Lottery's requested transfer amount of \$327,581,533 for the quarter ended March 31, 2013 is supported by accounting records; and
- The Lottery is on target to meet the annual allocation requirements specified in the Lottery Act.

We traced the transfer amount to Lottery financial statements and accounting records and applied analytical review procedures to the Lottery fund accounts by comparing them with those from the prior year.

## Results

On June 25, 2013, the SCO transferred \$327,581,533 to the Lottery Education Fund. Due to the SCO's apportionment process, all funds except \$23.73 were disbursed to the public education community. This balance will remain in the Lottery Education Fund to be apportioned during the next quarterly transfer.

After analyzing the Lottery's unaudited financial statements and supporting records for the quarter ended March 31, 2013, we determined that the Lottery's request to transfer \$327,581,533 to the Lottery Education Fund appears to be supported by formal accounting records.

For the quarter ended March 31, 2013, of the total revenues from ticket sales:

- 60.25% was returned to the public in the form of prizes;
- 28.03% was transferred to the public education community; and
- 11.72% was used for administrative expenses.

The Lottery returned 88.28% of the total revenues from the sales of tickets to the public in the form of prizes and funds to education. The Lottery is on target to meet the annual allocation requirements specified in the Lottery Act. See Schedule 1 for a summary of Lottery transfers and allocation percentages.

*Original signed by*

JEFFREY V. BROWNFIELD, CPA  
Chief, Division of Audits

November 15, 2013

## Schedule 1— Summary of Lottery Transfers and Allocation Percentages

Fiscal Year 2012-13	Quarter Ended <sup>1</sup>							
	09/30/2012	%	12/31/2012	%	03/31/2013	%	06/30/2013	%
Sales	\$ 1,008,382,162	100.00%	\$ 2,051,515,833	100.00%	\$ 3,153,730,899	100.00%	\$	%
Prizes	\$ 611,579,884	60.65%	\$ 1,245,909,894	60.73%	\$ 1,900,093,870	60.25%	\$	%
Administration	\$ 119,232,009	11.82%	\$ 244,601,506	11.92%	\$ 369,679,624	11.72%	\$	%
Available for Education	\$ 277,570,269	27.53%	\$ 561,004,433	27.35%	\$ 883,957,395	28.03%	\$	%
Prizes and Available for Education	\$ 889,150,153	88.18%	1,806,914,327	88.08%	\$ 2,784,051,275	88.28%		
Other Income <sup>2</sup>	10,591,621		15,064,526		\$ 19,693,087			
Adjustment	4,715,142 <sup>4</sup>		—					
Transfer to Education	\$ 292,877,032		\$ 576,068,959		\$ 903,650,492		\$	

Fiscal Year 2011-12	Quarter Ended <sup>1</sup>							
	09/30/2011	%	12/31/2011	%	03/31/2012	%	06/30/2012	%
Sales	\$ 869,113,412	100.00%	\$ 1,971,252,588	100.00%	\$ 3,330,793,946	100.00%	\$ 4,371,491,746	100.00%
Prizes	\$ 494,773,562	56.93%	\$ 1,146,667,271	58.17%	\$ 1,936,723,462	58.15%	\$ 2,560,306,587	58.57%
Administration	\$ 105,050,044	12.09%	\$ 224,397,328	11.38%	\$ 374,310,153	11.24%	\$ 512,935,953	11.73%
Available for Education	\$ 269,289,806	30.98%	\$ 600,187,989	30.45%	\$ 1,019,760,331	30.61%	\$ 1,298,249,204	29.70%
Prizes and Available for Education	764,063,368	87.91%	1,746,855,260	88.62%	2,956,483,793	88.76%	\$ 3,858,555,793	88.27%
Other Income <sup>2</sup>	7,960,834		12,916,600		17,251,082		22,477,351	
Adjustment	4,999,206 <sup>3</sup>		—		—		(4,715,142) <sup>4</sup>	
Transfer to Education	\$ 282,249,846		\$ 613,104,589		\$ 1,037,011,413		\$ 1,316,011,413	

### Annual Statutory Requirements After AB 142 (enacted April 8, 2010)

Prizes = Not less than 50% of sales

Administration = No more than 13% of sales

Prizes and available for education = Not less than 87% of sales

Other income = 100% due education

Note: The actual percentage allocation is computed on an annual basis when determining whether the Lottery has met the allocation requirements. The percentages shown above indicate the Lottery's year-to-date progress toward meeting these requirements.

<sup>1</sup> Quarterly amounts represent fiscal year-to-date totals.

<sup>2</sup> Includes interest income, other income, and unclaimed prizes.

<sup>3</sup> This represents the amount withheld in the fourth quarter of FY 2009-10, pending the financial audit and resolution of accounting issues.

<sup>4</sup> This represents the amount withheld in FY 2011-12, pending the financial audit and resolution of accounting issues.

**Attachment—  
California Lottery's  
Transfer Request of May 16, 2013**

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700 North Tenth Street  
Sacramento, CA 95811  
calottery.com



May 16, 2013

Mr. George Lolas, Chief  
Division of Accounting and Reporting  
State Controller's Office  
3301 C Street, Suite 700  
Sacramento, CA 95816

Dear Mr. Lolas:

The California State Lottery requests that you transfer to the Lottery Education Fund for disbursement to the education community \$327,581,533. This figure represents:

Operating income for the nine months ended March 31, 2013	\$ 883,957,405
SMIF interest earned	943,206
Other income	44,686
Unclaimed prizes	<u>18,705,195</u>
	<u>\$ 903,650,492</u>
Less: Transfer for the six months ended December 31, 2012	\$ 576,068,959
	<u>\$ 327,581,533</u>

We have attached a copy of the Statement of Revenues, Expenses, and Changes in Net Assets for the nine months ended March 31, 2013, prepared from books without audit, for your files.

Sincerely,

Nicholas Buchen, Deputy Director  
Finance Division

Attachment  
cc: Robert O'Neill, Director

**CALIFORNIA STATE LOTTERY FUND**  
Statement of Revenues, Expenses, and Changes in Net Assets  
For the Nine Months Ending March 31, 2013

Lottery sales	\$3,153,730,899
Prizes	1,900,093,870
	-----
Sales after prizes	\$1,253,637,029
	-----
Less game costs:	
Retailer costs	\$216,857,092
On-line game costs	34,773,947
Off-line game costs	21,239,349
	-----
Total game costs	\$272,870,388
	-----
Income before operating expenses	\$980,766,641
	-----
Operating expenses:	
Salaries, wages and benefits	\$36,106,253
Advertising	32,091,056
Promotion, public relations and point of sale	4,239,443
Other professional services	10,130,165
Depreciation and amortization	4,496,575
Other general and administrative expenses	9,745,744
	-----
Total operating expenses	\$96,809,236
	-----
Operating income	\$883,957,405
Non-operating (expenses) revenues:	
Investment earnings	(\$10,360,629)
Other Income	44,686
Allocation to Education Fund	(884,945,297)
	-----
Total non-operating (expenses) revenues	(\$895,261,240)
Changes in net assets	(\$11,303,835)
Total net assets-beginning of year	155,597,555
	-----
Total net assets-end of year	\$144,293,720
	=====

**State Controller's Office  
Division of Audits  
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**<http://www.sco.ca.gov>**