

CALIFORNIA STATE LOTTERY

Review Report

QUARTERLY TRANSFER OF FUNDS TO PUBLIC EDUCATION

For the Quarter Ended June 30, 2021



MALIA M. COHEN
California State Controller

March 2024



MALIA M. COHEN
CALIFORNIA STATE CONTROLLER

March 21, 2024

Harjinder K. Shergill-Chima, Director
California State Lottery
700 North Tenth Street
Sacramento, CA 95811

Dear Ms. Shergill-Chima:

The State Controller's Office reviewed the financial documentation supporting the California State Lottery's (Lottery) transfer of funds to the public education community for the quarter ended June 30, 2021. Our review found that the transfer amount of \$461,000,000 is supported by the Lottery's accounting records, and that the Lottery complied with annual revenue allocation requirements for prize payouts, funds to education, and administrative expenses, as specified in the California State Lottery Act of 1984, for the fiscal year ended June 30, 2021.

If you have any questions, please contact Roochel Espilla, Chief, State Agency Audits Bureau, by telephone at (916) 323-5744, or by email at respilla@sco.ca.gov

Sincerely,

Original signed by

KIMBERLY TARVIN, CPA
Chief, Division of Audits

KT/ac

Ms. Harjinder K. Shergill-Chima

March 21, 2023

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cc: Gregory Ahern, Chair

California State Lottery Commission

Tiffani Alvidrez, Commissioner

California State Lottery Commission

Anthony Garrison-Engbrecht, Commissioner

California State Lottery Commission

Keetha Mills, Commissioner

California State Lottery Commission

Alexandre Rasouli, M.D., Commissioner

California State Lottery Commission

Nicholas Buchen, Deputy Director, Finance Division

California State Lottery

Sara Sheikholislam, Deputy Director, Internal Audits

California State Lottery

Emily Nguyen, Audit Manager, Internal Audits

California State Lottery

Mimi Alemu, External Audits Liaison, Internal Audits

California State Lottery

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**Attachment A—California State Lottery’s Revised Transfer Request
Dated September 7, 2022**

Attachment B—California State Lottery’s Transfer Request Dated September 8, 2021

Review Report

Summary

The California State Lottery (Lottery) requested that the State Controller's Office (SCO) transfer \$461,000,000 to the Lottery Education Fund for disbursement to the public education community for the quarter ended June 30, 2021. Based on the work performed, we determined that the requested transfer amount was supported by the Lottery's accounting records. In addition, we determined that the Lottery complied with annual revenue allocation requirements for prize payouts, funds to education, and administrative expenses as specified in the California State Lottery Act of 1984 (Lottery Act) for the fiscal year ended June 30, 2021.

Background

In 1984, California voters passed an initiative, Proposition 37, to authorize the creation of a state-operated lottery. The initiative created the Lottery Act, which is found in Chapter 12.5 of Government Code.

The Lottery Act requires revenues from the Lottery to be allocated to maximize the amount of funding allocated to the public education community. The Lottery Act requires that not less than 87% of the total annual revenues from Lottery ticket sales be returned to the public in the form of prize payouts and funds to education and not more than 13% be allocated for administrative expenses. Furthermore, the Lottery Act requires that not less than 50% of the total annual Lottery revenues, in an amount to be determined by the California State Lottery Commission (Commission), be returned to the public in the form of prize payouts. In addition, the Commission must establish the percentages to be allocated to the benefit of public education.

Each quarter, the Lottery requests that the SCO transfer funds to the Lottery Education Fund. The Lottery's request usually occurs eight to 10 weeks after the close of each quarter. The transfer request for the quarter ended June 30, 2021, is included as Attachment A.

Review Authority

We conducted this review in accordance with Government Code section 8880.46.6, which authorizes the SCO to conduct quarterly and annual audits of all accounts and transactions of the Commission and other special audits as necessary. The SCO has the authority to examine any and all records of the Commission, its distributing agencies, Lottery contractors, and Lottery retailers.

Objectives, Scope, and Methodology

The objectives of our review were to determine whether:

- The requested transfer amount was supported by accounting records; and
- The Lottery complied with the annual allocation requirements specified in the Lottery Act.

We performed this review for the fourth quarter ended June 30, 2021. To achieve our objectives, we performed the following procedures:

- We compared fiscal year (FY) 2020-21 audited income statement balances with FY 2019-20 audited income statement balances and performed analytical procedures for variances over 15%.
- We traced amounts reported in the income statement to the Lottery's accounting records.
- We judgmentally selected sales and expense items, based on dollar amount and type, and traced to supporting documentation. Results were not projected to the intended (total) population.
- We determined whether the Lottery met the annual revenue allocation requirements specified in the Lottery Act.
- We reviewed a selection of accruals and determined whether they were adequately supported, accurately calculated, and correctly recorded.
- We determined whether the requested amount was transferred to the Lottery Education Fund.
- We verified that the funds were transferred from the Lottery Education Fund to the public education community for the quarter ended June 30, 2021.

Results

Based on the work performed, we determined that the requested transfer amount of \$461,000,000 for the fourth quarter ended June 30, 2021, was supported by the Lottery's accounting records. In addition, we verified that the Lottery complied with annual revenue allocation requirements for prize payouts, funds to education, and administrative expenses, as specified in the Lottery Act, for the fiscal year ended June 30, 2021.

In a letter dated September 8, 2021 (Attachment B), the Lottery requested that the SCO transfer \$461,000,000 to the Lottery Education Fund for disbursement to the public education community. On September 29, 2021, the SCO's Local Government Programs and Services Division transferred \$461,000,000 from the State Lottery Fund to the Lottery Education Fund. On September 30, 2021, \$460,999,999 was disbursed from the Lottery Education Fund to the public education community. The difference of \$1 between the requested transfer amount and the disbursement to the public education community is due to rounding. The remainder was apportioned during the subsequent quarterly transfer.

On September 7, 2022, the Lottery submitted a revision to its original transfer request dated September 8, 2021. The revision reported a decrease in the Lottery's operating income for the fiscal year ended June 30, 2021, but did not change the requested transfer amount of \$461,000,000. Despite the revisions, the Lottery complied with annual revenue allocation requirements specified in the Lottery Act.

For the 12 months ended June 30, 2021, of the total revenues from ticket sales:

- 66.65% was returned to the public in the form of prize payouts;
- 22.07% was transferred to the public education community; and
- 11.28% was used for administrative expenses.

The Lottery returned 88.72% of total revenues from ticket sales in the form of prize payouts and funds to education. The Lottery complied with annual allocation requirements specified in the Lottery Act. See the Schedule for a summary of Lottery revenue allocations and allocation percentages.

**Views of
Responsible
Officials**

We discussed our results with Lottery representatives via email on May 10, 2023. As there are no findings, the Lottery waived the exit conference and draft report. We agreed the report would be issued as final.

Restricted Use

This report is intended for the information and use of the Lottery, the Commission, and the SCO; it is not intended to be, and should not be, used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record and is available on the SCO website at www.sco.ca.gov.

Original signed by

KIMBERLY TARVIN, CPA
Chief, Division of Audits

March 21, 2024

Schedule—
Fiscal Year 2020-21 and Fiscal Year 2019-20
Year-to-Date Lottery Revenue Allocations

Fiscal Year 2020-21	Three Months Ended 9/30/2020	% of Sales¹	Six Months Ended 12/31/2020	% of Sales¹	Nine Months Ended 3/31/2021	% of Sales¹	Twelve Months Ended 6/30/2021	% of Sales¹
Sales	\$ 2,025,442,485	100.00%	\$ 3,890,623,608	100.00%	\$ 6,228,285,642	100.00%	\$ 8,417,943,817	100.00%
Prizes	1,374,317,474	67.85%	2,619,737,310	67.33%	4,139,431,337	66.46%	5,610,605,541	66.65%
Operating income	424,642,033	20.97%	832,487,855	21.40%	1,388,741,332	22.30%	1,857,730,878	22.07%
Revenues returned to public	1,798,959,507	88.82%	3,452,225,165	88.73%	5,528,172,669	88.76%	7,468,336,419	88.72%
Administrative expenses	226,482,978	11.18%	438,398,443	11.27%	700,112,973	11.24%	949,607,397	11.28%
Miscellaneous income ²	10,151,995		14,534,351		18,532,272		24,823,527	
Adjustment	-		-		19,050,946 ⁵		(14,280,801) ⁶	
Allocation to Education Fund	\$ 434,794,028		\$ 847,022,206		\$ 1,426,324,550		\$ 1,868,273,605	
Fiscal Year 2019-20	Three Months Ended 9/30/2019	% of Sales¹	Six Months Ended 12/31/2019	% of Sales¹	Nine Months Ended 3/31/2020	% of Sales¹	Twelve Months Ended 6/30/2020	% of Sales¹
Sales	\$ 1,663,239,267	100.00%	\$ 3,355,739,201	100.00%	\$ 4,981,760,628	100.00%	\$ 6,622,003,405	100.00%
Prizes	1,106,200,805	66.51%	2,223,100,423	66.25%	3,300,388,515	66.25%	4,403,715,159	66.50%
Operating income	359,504,052	21.61%	728,641,946	21.71%	1,083,119,336	21.74%	1,425,154,855	21.52%
Revenues returned to public	1,465,704,857	88.12%	2,951,742,369	87.96%	4,383,507,851	87.99%	5,828,870,014	88.02%
Administrative expenses	197,534,410	11.88%	403,996,832	12.04%	598,252,777	12.01%	793,133,391	11.98%
Miscellaneous income ²	58,157,980		74,538,873		80,410,080		87,425,507	
Adjustment	-		-		23,480,097 ³		(19,050,946) ⁵	
Allocation to Education Fund ⁴	\$ 417,662,032		\$ 803,180,819		\$ 1,187,009,513		\$ 1,493,529,416	

Annual Statutory Revenue Allocation Percentage Requirements

Prize payouts – Not less than 50% of sales

Administrative expenses – Not more than 13% of sales

Prize payouts and funds to education – Not less than 87% of sales

Other income – 100% to education

¹ Statutory compliance is determined on an annual basis at fiscal year-end. The percentages displayed in the first three quarters are presented to show the Lottery's year-to-date progress toward complying with annual statutory requirements.

² Miscellaneous income includes Surplus Money Investment Fund interest earned, unclaimed prizes, and other income.

³ This amount was withheld from the FY 2018-19 fourth-quarter transfer and was adjusted in the FY 2019-20 third-quarter transfer after the completion of the financial statement audit and resolution of accounting issues.

⁴ The Lottery Education Fund allocation amount is sales plus miscellaneous income, plus the adjustment amount, less prizes, and less administrative expenses.

⁵ This amount was withheld from the FY 2019-20 fourth-quarter transfer and was included in the FY 2020-21 third-quarter transfer after the completion of the financial statement audit and resolution of accounting issues.

⁶ This amount was withheld from the FY 2020-21 fourth-quarter transfer and will be adjusted in a subsequent quarter transfer after the completion of the financial statement audit and resolution of accounting issues.

**Attachment A—
California State Lottery's
Revised Transfer Request Dated September 7, 2022**



September 7, 2022

Natalie Sidarous, Chief
Local Government Programs and Services Division
State Controller's Office
3301 C Street, Suite 740
Sacramento, CA 95816

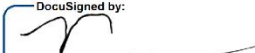
Dear Ms. Sidarous:

The California Lottery received pension and other postemployment benefits allocations, which impact the Lottery's operating income for the fiscal year ended June 30, 2021. Due to these and other adjustments, the Lottery is submitting this revision to the letter dated September 8, 2021, previously submitted.

<u>Revised</u> Operating income for the year ended June 30, 2021	\$ 1,857,730,878
SMIF interest earned	3,592,599
<u>Revised</u> Other income	1,823,112
Unclaimed prizes	<u>19,407,816</u>
	\$ 1,882,554,405
Less: Transfer for the nine months ended March 31, 2021	1,407,273,604
<u>Revised</u> Amount withheld pending audit	<u>14,280,801</u>
	<u>\$ 461,000,000</u>

We have attached a revised copy of the Statement of Revenues, Expenses, and Changes in Net Position for the year ended June 30, 2021, for your files.

Sincerely,

DocuSigned by:

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Nicholas Buchen, Deputy Director
Finance Division

Attachment

cc: Alva Johnson, Director

California State Lottery
Statement of Revenues, Expenses, and Changes in Net Fund Position
For the Twelve Months Ended June 30, 2021

Operating revenues: Lottery Sales	\$ 8,417,943,816.91
Prizes	<u>\$ 5,610,605,541.27</u>
Sales after prizes	<u>\$ 2,807,338,275.64</u>
Less game costs:	
Retailer costs	\$ 585,861,905.77
Gaming system costs	\$ 97,963,147.72
Scratchers game costs	<u>\$ 44,601,523.87</u>
Total game costs	<u>\$ 728,426,577.36</u>
Income before operating expenses	<u>\$ 2,078,911,698.28</u>
Operating expenses:	
Salaries, wages, and benefits	\$ 104,757,919.03
Advertising	\$ 59,135,920.42
Promotion, public relations, and point of sale	\$ 7,490,495.79
Other professional services	\$ 17,728,391.05
Depreciation and amortization	\$ 16,765,127.49
Other general & administrative expenses	<u>\$ 15,302,966.13</u>
Total operating expenses	<u>\$ 221,180,819.91</u>
Operating Income	<u>\$ 1,857,730,878.37</u>
Non-operating (expenses) revenues:	
Investment Earnings	\$ (53,382,891.64)
Other Income	\$ 1,823,111.59
Allocation to Education Fund	<u>\$ (1,863,146,588.66)</u>
Total non-operating (expenses) revenues	<u>\$ (1,914,706,368.71)</u>
Changes in net position	\$ (56,975,490.34)
Total net position-beginning balance	<u>\$ (81,457,353.19)</u>
Total net position-ending balance	<u><u>\$ (138,432,843.53)</u></u>

See accompanying notes on the financial statements

**Attachment B—
California State Lottery's
Transfer Request Dated September 8, 2021**



September 8, 2021

Natalie Sidarous, Chief
Local Government Programs and Services Division
State Controller's Office
3301 C Street, Suite 740
Sacramento, CA 95816

Dear Ms. Sidarous:

The California State Lottery requests that you transfer to the Lottery Education Fund for disbursement to the education community \$461,000,000. This figure represents:

Operating income for the year ended June 30, 2021	\$ 1,867,146,141
SMIF interest earned	3,592,599
Other income	156,942
Unclaimed prizes	<u>19,407,816</u>
	\$ 1,890,303,498
Less: Transfer for the nine months ended March 31, 2021	1,407,273,604
Amount withheld pending audit	<u>22,029,894</u>
	<u>\$ 461,000,000</u>

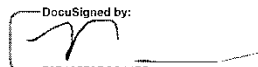
We have attached a copy of the Statement of Revenues, Expenses, and Changes in Net Position for the year ended June 30, 2021, prepared from books without audit, for your files.

Please note, as of the date of this letter, the State Controller's Office has not distributed the annual pension and other postemployment benefits reporting information needed to complete our GAAP financial statements. Once we receive the information, we will need to accrue our liability, and there may be an adjustment to our operating income. However, we anticipate that any adjustment will be funded by the amount withheld

pending audit, and that there will be no change to the requested transfer of \$461,000,000. If that is not the case, any adjustments to the funds transferred will be made in a future quarter.

We will send an updated letter for the quarter ended June 30, 2021, once the final pension and benefits information becomes available.

Sincerely,

DocuSigned by:

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Nicholas Buchen, Deputy Director
Finance Division

Attachment

cc: Alva Johnson, Director

**State Controller's Office
Division of Audits
Post Office Box 942850
Sacramento, CA 94250**

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