

# **CALIFORNIA STATE LOTTERY**

Review Report

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

*For the Quarter Ended March 31, 2020*



**BETTY T. YEE**  
California State Controller

June 2021



**BETTY T. YEE**  
California State Controller

June 2, 2021

Alva Vernon Johnson, Director  
California State Lottery  
700 North Tenth Street  
Sacramento, CA 95811

Dear Mr. Johnson:

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 March 31, 2020. Our review found that the transfer amount of \$383,828,694 is supported by the Lottery's accounting records, and that the Lottery was on target to meet 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, 2020.

If you have any questions, please contact Andrew Finlayson, Chief, State Agency Audits Bureau, by telephone at (916) 324-6310, or by email at [afinlayson@sco.ca.gov](mailto:afinlayson@sco.ca.gov).

Sincerely,

*Original signed by*

KIMBERLY TARVIN, CPA  
Chief, Division of Audits

KT/as

cc: Gregory Ahern, Chair  
California State Lottery Commission  
Nathaniel Kirtman III, Commissioner  
California State Lottery Commission  
Keetha Mills, Commissioner  
California State Lottery Commission  
Peter Stern, Commissioner  
California State Lottery Commission  
Nicholas Buchen, Deputy Director, Finance Division  
California State Lottery  
James Shannon, Audit Manager, Internal Audits  
California State Lottery

# Contents

## Review Report

<b>Summary .....</b>	<b>1</b>
<b>Background .....</b>	<b>1</b>
<b>Objectives, Scope, and Methodology .....</b>	<b>1</b>
<b>Results.....</b>	<b>2</b>
<b>Views of Responsible Officials.....</b>	<b>3</b>
<b>Restricted Use .....</b>	<b>3</b>
<b>Schedule—FY 2019-20 and FY 2018-19 Year-to-Date Lottery Revenue Allocations.....</b>	<b>4</b>
<b>Attachment—California State Lottery’s Transfer Request Dated June 5, 2020</b>	

# Review Report

## Summary

The California State Lottery (Lottery) requested that the State Controller's Office (SCO) transfer \$383,828,694 to the Lottery Education Fund for disbursement to the public education community for the quarter ended March 31, 2020. 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 was on target to meet 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, 2020.

## Background

On November 6, 1984, California voters passed Proposition 37, the Lottery Act, which authorized the creation of a state-operated lottery. The Lottery Act is found in Government Code Chapter 12.5, section 8880 et seq.

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.

Government Code section 8880.46.6 states that the SCO shall conduct quarterly and annual audits of all accounts and transactions of the Commission and other special audits as the State Controller deems necessary. The Controller has the authority to examine any and all records of the Commission, its distributing agencies, Lottery contractors, and Lottery retailers.

Each quarter, the Lottery requests that the SCO transfer funds to the Lottery Education Fund (Attachment). The Lottery's request usually occurs eight to 10 weeks after the close of each quarter.

## Objectives, Scope, and Methodology

The objectives of our analysis were to determine whether:

- The requested transfer amount was supported by accounting records; and
- The Lottery was on target to meet the annual allocation requirements specified in the Lottery Act.

We performed this analysis for the third quarter ended March 31, 2020. To achieve our objectives, we:

- Compared current fiscal year audited income statement balances with prior fiscal year audited income statement balances and performed analytical procedures for variances over 15%;
- Traced amounts reported in the income statement to the Lottery's accounting records;
- Judgmentally selected sales and expense items, based on dollar amount and type, and traced them to supporting documentation;<sup>1</sup>
- Determined whether the Lottery met the annual revenue allocation requirements specified in the Lottery Act;
- Determined whether the requested transfer amount to the Lottery Education Fund occurred; and
- Verified that the funds were transferred from the Lottery Education Fund to the public education community for the current quarter.

## Results

Based on the work performed, we determined that the requested transfer amount of \$383,828,694 for the third quarter ended March 31, 2020 was supported by the Lottery's accounting records. In addition, we determined that the Lottery was on target to meet annual revenue allocation requirements for prize payouts, funds to education, and administrative expenses as specified in the Lottery Act for the quarter ended March 31, 2020.

In a letter dated June 5, 2020, the Lottery requested that the SCO transfer \$383,828,694 to the Lottery Education Fund for disbursement to the public education community. On June 23, 2020, the SCO's Government Programs and Services Division (LGPSD) transferred \$383,828,694 from the State Lottery Fund to the Lottery Education Fund.

In our prior quarterly reports, we disclosed the following issue, which we also disclose in this report because it remained uncorrected during this review period.

During the fiscal year (FY) 2018-19 first-quarter allocation calculations, while updating the average daily attendance (ADA) figures for approximately 2,500 educational entities, LGPSD transposed ADA numbers for some schools in two counties. LGPSD collected the overpayments from the two counties as soon as the errors were discovered. The ADA errors resulted in misallocations, totaling \$5,196,819, to all educational entities that receive Lottery funding. LGPSD staff indicated that process changes are being implemented to minimize the potential for future ADA transposition errors.

---

<sup>1</sup> As non-statistical sampling methods were used, the results were not projected to the intended population.

For the nine months ended March 31, 2020, of the total revenues from ticket sales:

- 66.25% was returned to the public in the form of prize payouts;
- 21.74% was transferred to the public education community; and
- 12.01% was used for administrative expenses.

The Lottery returned 87.99% of total revenues from ticket sales in the form of prize payouts and funds to education. The Lottery was on target to meet 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 February 10, 2021. 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.

*Original signed by*

KIMBERLY TARVIN, CPA  
Chief, Division of Audits

June 2, 2021

**Schedule—**  
**FY 2019-20 and FY 2018-19**  
**Year-to-Date Lottery Revenue Allocations**

Fiscal Year 2019/2020	Three Months Ended 9/30/2019	% of Sales <sup>1</sup>	Six Months Ended 12/31/2019	% of Sales <sup>1</sup>	Nine Months Ended 3/31/2020	% of Sales <sup>1</sup>	Twelve Months Ended 6/30/2020	% of Sales <sup>1</sup>
Sales	\$ 1,663,239,267	100.00%	\$ 3,355,739,201		\$ 4,981,760,628	100.00%		
Prizes	\$ 1,106,200,805	66.51%	\$ 2,223,100,423	66.25%	\$ 3,300,388,515	66.25%		
Operating income to education	\$ 359,504,052	21.61%	\$ 728,641,946	21.71%	\$ 1,083,119,336	21.74%		
Revenues returned to public	\$ 1,465,704,857	88.12%	\$ 2,951,742,369	87.96%	\$ 4,383,507,851	87.99%		
Administrative expenses	\$ 197,534,410	11.88%	\$ 403,996,832	12.04%	\$ 598,252,777	12.01%		
Miscellaneous income <sup>2</sup>	\$ 58,157,980		\$ 74,538,873		\$ 80,410,080			
Adjustment	\$ -		\$ -		\$ 23,480,097 <sup>5</sup>			
<b>Allocation to Education Fund <sup>4</sup></b>	<b>\$ 417,662,032</b>		<b>\$ 803,180,819</b>		<b>\$ 1,187,009,513</b>			

Fiscal Year 2018/2019	Three Months Ended 9/30/2018	% of Sales <sup>1</sup>	Six Months Ended 12/31/2018	% of Sales <sup>1</sup>	Nine Months Ended 3/31/2019	% of Sales <sup>1</sup>	Twelve Months Ended 6/30/2019	% of Sales <sup>1</sup>
Sales	\$ 1,632,006,024	100.00%	\$ 3,717,330,531	100.00%	\$ 5,562,239,364	100.00%	\$ 7,388,050,316	100.00%
Prizes	\$ 1,046,074,342	64.10%	\$ 2,340,130,361	62.95%	\$ 3,526,400,829	63.40%	\$ 4,715,592,673	63.83%
Operating income to education	\$ 393,824,838	24.13%	\$ 945,471,555	25.43%	\$ 1,390,758,881	25.00%	\$ 1,809,721,391	24.50%
Revenues returned to public	\$ 1,439,899,180	88.23%	\$ 3,285,601,916	88.39%	\$ 4,917,159,710	88.40%	\$ 6,525,314,064	88.32%
Administrative expenses	\$ 192,106,844	11.77%	\$ 431,728,615	11.61%	\$ 645,079,654	11.60%	\$ 862,736,252	11.68%
Miscellaneous income <sup>2</sup>	\$ 15,409,724		\$ 30,919,170		\$ 41,508,306		\$ 61,025,893	
Adjustment	\$ -		\$ -		\$ 2,803,132 <sup>3</sup>		\$ (23,480,097) <sup>5</sup>	
<b>Allocation to Education Fund <sup>4</sup></b>	<b>\$ 409,234,562</b>		<b>\$ 976,390,725</b>		<b>\$ 1,435,070,319</b>		<b>\$ 1,847,267,187</b>	

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

<sup>1</sup> 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 meeting annual statutory requirements.

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

<sup>3</sup> This amount was withheld from the FY 2017-18 fourth-quarter transfer and was adjusted in the FY 2018-19 third-quarter transfer after the completion of the financial statement audit and resolution of accounting issues.

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

<sup>5</sup> 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.

**Attachment—  
California State Lottery's  
Transfer Request Dated June 5, 2020**

---





June 5, 2020

Natalie Sidarous, Chief  
Local Government Programs and Services Division  
State Controller's Office  
3301 C Street, Suite 700  
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 \$383,828,694. This figure represents:

Operating income for the nine months ended	
March 31, 2020	\$ 1,083,119,336
SMIF interest earned	10,043,651
Other income	213,222
Unclaimed prizes	<u>70,153,207</u>
	\$ 1,163,529,416
Less: Transfer for the six months ended	
December 31, 2019	<u>803,180,819</u>
	\$ 360,348,597
Add: Amount withheld from 2018-19 fiscal year	
pending audit	<u>23,480,097</u>
	<u>\$ 383,828,694</u>

We have attached a copy of the Statement of Revenues, Expenses, and Changes in Net Position for the nine months ended March 31, 2020, prepared from books without audit, for your files.

Please note, the above amount includes the funds withheld from the 2018-19 transfer pending audit. While the 2018-19 audit report has not yet been issued, we do not believe this amount will change.

Sincerely,

A digital signature block showing a stylized signature in black ink over a white background. Above the signature is the text 'DocuSigned by:' and below it is a long alphanumeric string '78B135F3ECC14F6...'.

DocuSigned by:  
78B135F3ECC14F6...

Nicholas Buchen, Deputy Director  
Finance Division

Attachment

cc: Alva V. Johnson, Director

**California State Lottery Fund**  
**Statement of Revenues, Expenses, and Changes in Net Fund Position**  
**For the Nine Months Ended March 31, 2020**

Operating revenues: Lottery sales	\$ 4,981,760,628
Prizes	<u>\$ 3,300,388,515</u>
Sales after prizes	<u>\$ 1,681,372,113</u>
Less game costs:	
Retailer costs	\$ 346,798,043
Gaming System costs	\$ 62,707,882
Scratchers® game costs	<u>\$ 31,364,035</u>
Total game costs	<u>\$ 440,869,960</u>
Income before operating expenses	<u>\$ 1,240,502,153</u>
Operating expenses:	
Salaries, wages and benefits	\$ 68,102,402
Advertising	\$ 42,980,302
Promotion, public relations and point of sale	\$ 6,645,116
Other professional services	\$ 11,928,671
Depreciation and amortization	\$ 14,005,237
Other general and administrative expenses	<u>\$ 13,721,089</u>
Total operating expenses	<u>\$ 157,382,817</u>
Operating income	<u>\$ 1,083,119,336</u>
Non-operating (expenses) revenues:	
Investment earnings (Note 9)	\$ 78,576,228
Other Income	\$ 213,222
Allocation to Education Fund (Note 7)	<u>\$ (1,093,376,210)</u>
<b>Total non-operating (expenses) revenues</b>	<u><b>\$ (1,014,586,760)</b></u>
Changes in net position	\$ 68,532,576
Total net position - beginning of year	<u>\$ (151,715,806)</u>
Total net position - ending balance	<u><u>\$ (83,183,230)</u></u>

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

**<http://www.sco.ca.gov>**