

REVENUE ESTIMATING CONFERENCE

TAX: Lottery Revenues/Educational Enhancement Trust Fund

ISSUE: Impact of New Machine Authority

BILL NUMBER(S): SB 674

SPONSOR(S):

MONTH/YEAR COLLECTION IMPACT BEGINS:

DATE OF ANALYSIS: April 21, 2010

SECTION 1: NARRATIVE

a. Current Situation:

Florida Statutes Chapter 24.105 outlines the powers and duty of the department of Lottery. At the present time, the department is authorized to use only one type of player-activated machine. The machine described can only dispense instant tickets. Chapter 24 has authorized this type of vending machine since 1996. At that time, the lottery industry had not envisioned the utilization of other types of vending machines. Beginning in August 2009, the department began deploying the current inventory of 1,000 Instant Ticket Vending Machines (ITVM) on a statewide basis as outlined in the chapter.

Benefits of Current Authority

At this time, the department has 1,000 ITVMs deployed at its highest selling retailers around the state. The vast majority of the ITVMs are being used in the large corporate grocery store locations. The department calculates that as of this date, there has been an incremental increase in instant ticket sales of \$72.9 million which results in an additional \$13.8 million in EETF transfers as a result of the deployment of the machines in fiscal year 2009-2010.

Mission Fulfillment: The mission of the Florida Lottery is to maximize revenues for the enhancement of public education in Florida. In order to achieve its mission, the department has deployed various product distribution methods over its twenty two years. As technology has improved over time the department has modernized its distribution methods accordingly to seek new and more cost effective opportunities as they have presented themselves.

Operational Efficiencies: The current ITVM program is extremely cost efficient. It is designed to provide legislatively compliant equipment for use by retailers in high volume locations. Retailers agree to follow an instant ticket plan-o-gram provided by the Lottery. The plan-o-gram is intended to maximize sales by ensuring stores carry the best selling games and the plan-o-gram is updated monthly to coincide with the introduction of new games being launched. The ITVMs also receive expeditious equipment support from the on-line gaming vendor. The assigned retailer is responsible for ensuring the machine is kept full at all times and being used by only above age players. Sales data from each machine is automatically relayed to the retailer's Altura terminal and then into the department's central gaming system. Location sales data is analyzed by local sales staff and headquarters staff to ensure the optimized placement of the limited number of machines.

b. Proposed Change:

CS for SB 674 proposes to add authority for the department to utilize two additional types of vending machines as well as continues to authorize the currently deployed ITVMs.

The first of the two new types of machines described will dispense a pre-determined electronic instant lottery ticket. The device will utilize a video screen and require the player to touch the image of the ticket on the screen to reveal the outcome of the ticket. The machine may not disburse winnings and may not use video or mechanical reels or simulate the play of any casino game. Retailers utilizing such machines will be compensated in the same manner as retailers selling paper instant tickets. These devices may not be deployed at any licensed pari-mutual facility.

The second type of device authorized is a machine that can provide the department's on-line products through a self-service machine much like the current version of the ITVM. This device can dispense paper on-line tickets with numbers selected by the player or randomly selected by the machine. The machine may not reveal the winning numbers to the player and winning numbers must be selected at a subsequent time and different location through a drawing by the department. This machine or any machine linked to it may not make use of video or mechanical reels or other video depictions of slot machines or casino-game themes or titles for game play. The machine may not be used to redeem winning tickets.

SECTION 2: DESCRIPTION OF DATA AND SOURCES

The department has reviewed data obtained from LaFleurs and its on-line gaming vendor in order to ascertain sales experiences of other states utilizing similar types of equipment. In addition, the department has analyzed the current fiscal

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year impact to the instant ticket revenues from its own implementation of the current model of ITVM to assess potential sales impact for the on-line products if deployment of the similar type of self-service equipment is implemented.

SECTION 3: METHODOLOGY (INCLUDE ASSUMPTIONS AND ATTACH DETAILS)

The methodology used in this analysis contains various underlying assumptions. As the department does not have current authority for the various types of machines being proposed, the department has not undertaken the necessary steps to obtain competitive pricing for the lease or purchase of the described equipment. The department will assume that the pricing of this equipment will not result in the department increasing the operating expense as a percentage of revenue to a level higher than 10%. The department's recent history for operating expense as a percentage of revenue has been approximately 9%. This will allow for the use of a slightly lower transfer rate for new revenues generated from these types of machines. In addition, the department will assume that all other facets of the department's operations will remain unchanged for the purposes of this analysis.

Electronic Instant Lottery Ticket Machines

The department anticipates the most effective utilization of this type of machine would be in retailer types that would emulate bars, taverns and restaurants. The department currently has 63 of these types of retailers selling lottery products. The department understands that there are 2,697 establishments in Florida that could be potential locations for such a machine. At this time, the department does not have spending authority to obtain the described machine. The department has estimated an aggressive implementation period of 18 months to complete the program's concept design, complete the procurement process for the equipment, manufacture and coordinate the installation while also recruiting the new locations for deployment. This would establish a beginning sales period of mid-fiscal year 2011-12 and the first full year of sales fiscal year 2012-13. The department has established estimates for the potential revenue using current average weekly sales data from its existing 63 locations as well as looking at other states' sales data that have deployed similar machines. (Tables 3 and 4)

On-Line Ticket Machines

The department is presenting two options for the deployment of the proposed "full-service" vending machines. The current technology available in the industry is referred to as a "full-service" vending machine. The machine distributes both on-line and instant paper products. The department anticipates continuing to use the very successful "plan-o-gram" concept for the distribution of the instant tickets in these machines. Just as ITVMs currently operate, it is envisioned that these machines will feed real-time sales to the on-line gaming system so the department can assess efficient utilization and maximize sales potential.

The first option (Table 5) will result in the highest 500 current ITVM locations receiving the new "full-service" machines and relocation of the existing ITVMs to other retailers that do not currently have the machine. The estimates apply the current incremental sales increase realized for instant ticket sales to current average weekly sales for the proposed locations. The estimates include the impact of new incremental instant sales for the new locations that would benefit from the current ITVM equipment shift.

The department has estimated an aggressive implementation period of 18 months to complete the program's concept design, complete the procurement process for the equipment, manufacture and coordinate the installation while also recruiting the new locations for deployment. This would establish a beginning sales period of mid-fiscal year 2011-12 and the first full year of sales fiscal year 2012-13.

The second option (Table 6) will result in only new retailer locations that have previously not been willing to sell lottery products receiving the new equipment. The department's experience with large "box" retailers that have expressed interest in selling lottery products is that they are unwilling or unable to do so with the current option of only selling products from a customer service counter. This new technology would allow the department to provide an option to these retailer types that would be less labor intensive. These estimates do not include any shift from the current IVM sales. The department has identified 1,784 potential locations that are not currently Florida Lottery retailers. While some locations may not be viable, as a whole, they provide an opportunity to distribute product in a new trade style, increase sales, and grow brand. Data for this type of machine is somewhat limited, so the estimates presented are developed from data gathered from the on-line vendor and the experience of a pilot project in California.

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The department has estimated an aggressive implementation period of 24 months to complete the program's concept design, complete the procurement process for the equipment, manufacture and coordinate the installation while also recruiting the new locations for deployment. This would establish a beginning sales period of 2012-13.

The estimates do not have previously adopted growth rates built into the out years. The conference previously adopted growth rates of 1.27% and 1.60% for scratch-off and on-line growth in fiscal years 2012-13 and 2013-14 respectively.

SECTION 4: PROPOSED FISCAL IMPACT

State Impact: All Funds	FY 2010-2011 Cash	FY 2011-2012 Cash	FY 2011-12 Annualized	FY 2012-13 Cash	FY 2013-14 Cash
High	0	\$56.9	\$113.8	\$189.0	\$189.0
Middle	0	\$37.5	\$ 74.9	\$ 74.9	\$ 74.9
Low	0	\$16.4	\$ 32.9	\$ 44.0	\$ 44.0

SECTION 5: CONSENSUS ESTIMATE (ADOPTED)

	FY 2010-11 Cash	FY 2010-11 Annualized	FY 2011-12 Cash	FY 2012-13 Cash	FY 2013-14 Cash
General Revenue					
State Trust					
Total State Impact					
Total Local Impact					
Total Impact					

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Impact of SB 674 to EETF Summary

Table 1 (Millions)	FY 2011-2012	FY 2011-12	FY 2012-13	FY 2013-14
	Cash	Annualized	Cash	Cash
Low - Elec. IT (Table 4)	\$ 16.5	\$ 32.9	\$ 32.9	\$ 32.9
Low - OVM (Opt 1) (Table 5)	15.2	30.5	30.5	30.5
Low - OVM (Opt 2) (Table 6)	-	-	11.1	11.1

Mid - Elec. IT (Table 4)	\$ 17.8	\$ 35.6	\$ 35.6	\$ 35.6
Mid - OVM (Opt. 1) (Table 5)	19.6	39.3	39.3	39.3
Mid - OVM (Opt. 2) (Table 6)	-	-	46.9	46.9

High - Elec. IT (Table 4)	\$ 56.9	\$ 113.8	\$ 113.8	\$ 113.8
High - OVM (Opt. 1) (Table 5)	28.4	56.9	56.9	56.9
High - OVM (Opt. 2) (Table 6)	-	-	75.2	75.2

Table 2 (In Millions)	FY 2011-2012	FY 2011-12	FY 2012-13	FY 2013-14
	Cash	Annualized	Cash	Cash
Low (Elec. & Opt 1)	\$ 31.7	\$ 63.4	\$ 63.4	\$ 63.4
Low (Elec. & Opt 2)	16.5	32.9	44.0	44.0

Mid (Elec. & Opt 1)	\$ 37.5	\$ 74.9	\$ 74.9	\$ 74.9
Mid (Elec. & Opt 2)	17.8	35.6	82.5	82.5

High (Elec. & Opt 1)	\$ 85.4	\$ 170.7	\$ 170.7	\$ 170.7
High (Elec. & Opt 2)	56.9	113.8	189.0	189.0

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Electronic Instant Ticket Machines	Source- La Fleur's Fiscal 2008 Industry Report			
	New Mexico	Delaware	W. Virginia	Rhode Isl. Oregon
Installed Machines	3,183	7,884	18,956	5,874 12,230
Machines per 1,000 Residents	1.61	9.11	10.46	5.55 3.26
Daily Gross Sales per machine	\$ 802.04	\$ 772.89	\$ 678.06	\$ 769.96 \$ 717.85
Prizes to Players	577.47	556.03	488.63	546.53 516.85
Prize Payout	78.10%	78.00%	78.20%	77.50% 78.10%
Operating Expenses	166.81	140.58	103.89	85.37 61.46
Return to State	57.76	76.28	85.54	138.06 139.54
% of Return	7.2%	9.9%	12.6%	17.9% 19.4%
Florida's Experience (traditional sales)	63 locations			
Current Average Weekly SO Sales Fla. current 63 Bar Retailers	\$1,750.00			
Potential Locations	2,697			
Estimated Machines	2,000			
% of Potential	74%			
SO Transfer Rate (out years)	18.03%			

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Table 4 2,000 Machines	Rate of Return	Avg. Daily Sales	Total Daily Return	Total Annual Return to EETF (Millions)
Low Estimate				
Fla's Avg. Weekly Sales Experience	18.0%	250.00	90,150	\$ 32.9
Mid Estimate				
Lowest Daily Sales and ROR	7.2%	678.06	97,663	\$ 35.6
High Estimate				
Highest Daily Sales and ROR	19.4%	802.04	311,811	\$ 113.8

Table 5

Option 1 - Place "Full Service" Machines in Top 500 ITVM locations, shift ITVMs to new sites.

	Inc. OL Weekly Growth per unit	Avg. Inc. Weekly Sales per unit	Total Annual Sales (Millions)	EETF (Millions)
Low Estimate				
5% Incremental Growth in OL	\$ 869	\$ 4,972	\$ 129.3	\$ 28.0
% of Inc. OL sales	17.5%			21.7%
Shift of 500 ITVMs to new locations		\$ 500	\$ 13.0	\$ 2.5
Total			\$ 142.3	\$ 30.5
Mid Estimate				
10% Incremental Growth in OL	\$ 1,737	\$ 5,840	\$ 151.8	\$ 36.8
% of Inc. OL sales	29.7%			24.2%
Shift of 500 ITVMs to new locations		\$ 500	\$ 13.0	\$ 2.5
Total			\$ 164.8	\$ 39.3
High Estimate				
20% Incremental Growth in OL	\$ 3,475	\$ 7,578	\$ 197.0	\$ 54.4
	45.9%			27.6%
Shift of 500 ITVMs to new locations		\$ 500	\$ 13.0	\$ 2.5
Total			\$ 210.0	\$ 56.9
Other Relevant Information				
Avg Weekly OL Sales for Top 500 ITVM Retailers	\$ 17,374			

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Avg Incremental Weekly SO Sales for Top 500 ITVM Retailers (net of shift)	\$ 4,103	24% higher than Retailers without ITVMs
On-Line Sales as a percentage of sales for OVMs	10.0%	Provided by GTECH
Average Weekly SO Sales for non-ITVM retailers	\$ 2,500	

Table 6

Option 2 - Place "Full Service" Machines in New Retail Styles - not currently selling Lottery

	# of Units	Avg. Inc. Weekly Sales per unit	Total Annual Sales (Millions)	EETF (Millions)
Low Estimate				
Deploy with Walgreens - California Experience with "Box"	800	\$ 1,325	\$ 55.1	\$ 11.1 20.10%
Mid Estimate				
Deploy with Wal-Mart - Mirror Expected Performance for Publix	170	\$ 26,388	\$ 233.3	\$ 46.9 20.1%
High Estimate				
Deploy with Wal-Mart - GTECH Expected Performance	170	\$ 42,308	\$ 374.0	\$ 75.2 20.1%
<u>Other Relevant Information</u>				
Current Average Weekly Sales for Publix	\$ 22,913			
20% Incremental Growth in OL Sales for Publix	3,475			
California's Experience with 28 Pilot Stores (2 yrs) Average Weekly Sales	\$ 2,300			
% in OL Sales	8 - 10 %			
California's Experience with 363 Units (mostly in South Ca.) for 5 months				
Avg. Wkly Sales	\$ 1,325			
% in OL Sales	5 - 10 %			

