

THE OKLAHOMA EDUCATION LOTTERY

The Oklahoma Education Lottery was created by voter approval of SQ 705 and SQ 706 in 2004. Under the terms of these two measures, at least 35 percent of gross revenues are dedicated as net proceeds to the Oklahoma Education Lottery Trust Fund for appropriation by the Legislature. The distribution of lottery net proceeds was specified as follows:

K - 12 funding, including early childhood programs	45%
Higher Education Tuition Assistance	
Capital projects (all levels of education)	
Technology improvement (all levels of education)	45%
Endowed Chair Professorships for Higher Education	
Schools for the Deaf and Blind	
School Consolidation Fund	5%
Teacher's Retirement Fund	5%

The Lottery Trust Fund is a certified fund, meaning that the Legislature can appropriate up to 95 percent of estimated collections for the upcoming fiscal year. If collections exceed the appropriated amount, the surplus is carried over and is available to be appropriated in subsequent years. If lottery revenues come in below the appropriated amount, agencies must either absorb the difference or the Legislature must identify additional funds.

Table 1 presents the revenue and expenditure history of the lottery for its seven years of operation, along with projections for FY '12. For the most part, lottery sales have remained remarkably consistent, regardless of the up and downs of the economy, the addition of new games, and growing competition from tribal casinos and the new state lottery in Arkansas. Total revenue in the lottery's first year, FY '06, was \$191.0 million and grew modestly, by 6.5

percent, to 203.5 million in FY '07, with the addition of Powerball. However, revenues flattened in FY '08 and then declined by 5.5 percent to \$193.3 million in FY '09 before growing by 3.4 percent in FY '10 and dipping by 0.8 percent in FY '11. Revenues in FY '12 are projected to decrease by 6.0 percent.

Net proceeds from lottery revenues to the Oklahoma Education Lottery Trust Fund have totaled \$68.9 million in FY '06, \$69.4 million in FY '07, \$78.4 million in FY '08 (which included carryover funds), \$69.2 million in FY '09, \$70.0 million in FY '10, and \$69.4 million in FY '11. Revenues in FY '07 and FY '08 fell considerably below the certified estimate, creating a shortfall in appropriations to the agencies and programs supported by lottery funds. In FY '11, revenues exceeded projections by \$3.4 million. Net proceeds in FY '12 are projected at \$65.1 million.

Lottery net proceeds are divided between several education agencies as set out by the statutes. For the most part, lottery revenues have been blended with other revenues to support general operating expenses, rather than being dedicated to any distinct, ongoing, and identifiable purpose. Current year (FY '12) appropriations includes \$63.1 million of lottery revenues out of total state appropriations of \$6.5 billion, or 1.0 percent.

Over the past several years, the Lottery Commission has advocated forcefully but unsuccessfully for the Legislature to eliminate or reduce the mandated 35 percent profit percentage and allow for higher prize payouts. The Commission contends this change is needed to boost lottery sales and ultimately generate increased revenue to fund education.

TABLE 1: Education Lottery Trust Fund Revenues and Appropriations. FY '06 - FY '12 (in \$ millions)

	FY '06 Actual	FY '07 Actual	FY '08 Actual	FY '09 Actual	FY '10 Actual	FY '11 Actual	FY '12 Estimated
Total Revenues	\$ 191.0	\$ 203.5	\$ 204.6	\$ 193.3	\$ 199.9	\$ 198.3	\$ 186.1
Share of net proceeds/profit	36.1%	34.1%	35.0%	35.8%	35.0%	33.5%	35.0%
Net Proceeds	\$ 68.9	\$ 69.4	\$ 71.6	\$ 69.2	\$ 70.0	\$ 66.5	\$ 65.1
Available Prior-Year Carryover	\$ -	\$ -	\$ 6.8	\$ -	\$ -	\$ -	\$ 6.3
Total Net Proceeds plus Carryover	\$ 68.9	\$ 69.4	\$ 78.4	\$ 69.2	\$ 70.0	\$ 66.5	\$ 71.4
APPROPRIATIONS OF LOTTERY FUNDS							
Common Education	\$ 34.2	\$ 64.8	\$ 48.7	\$ 38.2	\$ 34.9	\$ 33.9	\$ 35.3
Higher Education	\$ 28.0	\$ 46.7	\$ 35.4	\$ 27.3	\$ 25.0	\$ 24.3	\$ 24.3
Career Tech		\$ 6.0	\$ 4.5	\$ 3.8	\$ 3.5	\$ 3.4	\$ 3.5
Rehab Services		\$ 0.3					
Total Appropriations	\$ 62.2	\$ 117.8	\$ 88.6	\$ 69.3	\$ 63.4	\$ 61.6	\$ 63.1
Surplus/Shortfall	\$ 6.7	\$ (48.4)	\$ (10.2)	\$ (0.1)	\$ 6.6	\$ 4.9	-

GAMING REVENUES

SQ 712, which Oklahoma voters approved in the fall of 2004, had two principal components:

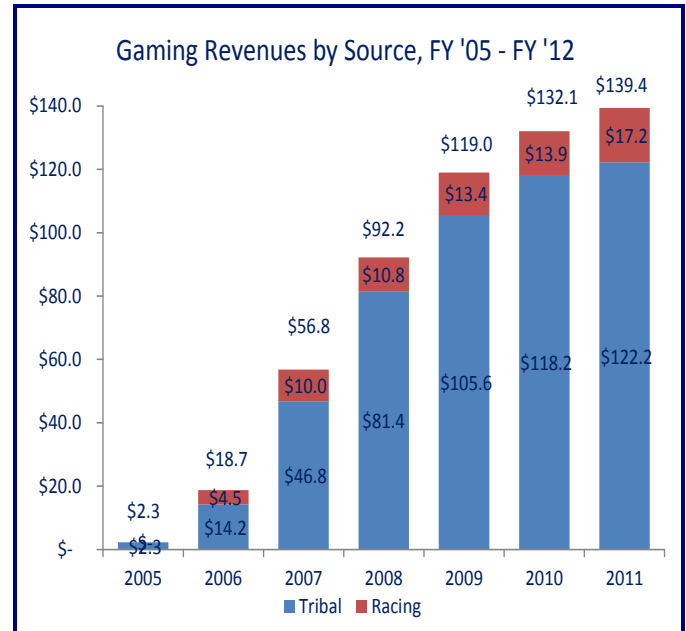
- It authorized a set number of gaming terminals at each of three racetracks (Remington Park, Blue Ribbon Downs and Will Rogers), and authorized or prohibited specific categories of games;
- It set up a model compact between the state and Native American tribes to regulate Class III tribal gaming operations. Under the compact, tribes were authorized to operate specified Class III games in return for making exclusivity payments to the state.

The state receives a share of gaming revenues generated by the compacting tribes and racetracks. The state's share of adjusted gross revenues begins at 4 percent of tribal games subject to the compact (10 percent for card games), and at 10 percent of revenues from racetrack gaming. The state share rises if revenues from particular tribes and racetracks exceed certain thresholds.

- After an initial \$250,000 is allocated to the Department of Mental Health and Substance Abuse Services for gambling education and treatment, 87.5 percent of gaming revenues are deposited in the 1017 Education Reform Fund, with the remaining 12.5 percent allocated to the General Revenue Fund.

State revenues from gaming have grown from \$2.3 million in FY '05 to \$18.7 million in FY '06, \$56.8 million in FY '07, \$92.2 million in FY '08, \$119.0 million in FY '09, \$132.1 million in FY '10, and \$139.4 million in FY '11. While gaming revenues continued to climb by a solid 5.5 percent in FY '11, the rate of annual growth has clearly begun to slow. Tribal gaming and racetrack gaming contributed equally to the growth in gaming revenue in FY '11.

Of the \$139.4 million collected in FY '11, \$122.2 million (87.7 percent) came from tribal gaming and \$17.2 million (12.3 percent) from the racetracks. These revenues can be further broken down as follows:



- Almost two-thirds (65.0 percent) of the \$122.2 million in tribal gaming revenues in FY '10 came from four tribes – the Chickasha (\$35.2 million), Choctaw (\$22.1 million), Cherokee (\$12.6 million) and Muskogee (Creek) (\$9.6 million). Revenue growth was greatest in FY '11 for the Choctaws, Muskogee (Creek) and Cheyenne–Arapahoes, while fifteen tribes saw slight declines in gaming fees this past year. In total, 31 tribes paid exclusivity fees to the state under the compact.
- Revenue from *electronic games* made up 87 percent of tribal gaming revenues, while *card games* made up the remaining 13 percent of gaming revenue. Both revenue streams grew modestly (about 3 percent) in FY '11. There were almost 60,000 machines in tribal casinos in Oklahoma in 2009, trailing only California.
- About 89 percent of racetrack gaming revenue is from machines at Remington Park (\$15.3 million) and 11 percent from Will Rogers Downs (\$1.9 million). Revenue from Remington Park grew by \$3.6 million in FY '11, while Will Rogers Down was largely unchanged. Blue Ribbon Downs ceased operations in November 2009.

TOBACCO TAXES

Oklahoma voters in 2004 approved SQ 713, which increased the excise tax on cigarettes and other tobacco products, while eliminating the state and local sales tax on these products.

The amount of the tax increase approved by SQ 713 differed for tribal and non-tribal retailers. For non-tribal retailers, the cigarette tax was increased by 80 cents per pack of cigarettes to \$1.03 per pack, with an offsetting elimination of twenty-five cents per pack in state and local sales taxes. For tribal retailers, the situation was more complicated, with retailers subject to one of six different rates depending on their geographic location and status of their compact with the state. The tribal tax rate ranges from a maximum of 85.75 cents per pack for a tribe that has negotiated a revised compact with the state, to a minimum of 5.75 cents for tribes under a “proximity exemption”. Taxes were also increased on other tobacco products.

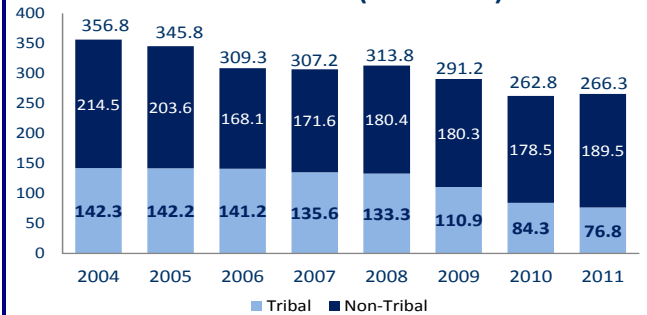
Eight health care projects were selected to receive a portion of new revenues generated by the tobacco tax increases, as follows:

- Oklahoma Health Care Authority for Medicaid provider payments and services for children with developmental disabilities (40.1 percent);
- Health Employee and Economy Improvement Act Fund to assist low-income employees buy into employer or public health insurance coverage—the Insure Oklahoma program (33.5 percent);
- Trauma Care Assistance Fund to support emergency trauma care (11.4 percent);
 - The share of revenue going to this Fund was decreased in to 10.4 percent in FY '11, with 0.9 percent now going to the Emergence Response System Fund;
- Comprehensive Cancer Center Debt Service Fund for bond payments on a new OU cancer center (4.7 percent);
- OSU College of Medicine Fund for telemedicine and indigent care (4.7 percent);
- Department of Mental Health and Substance Abuse Services for adolescent substance abuse centers and services (4.0 percent);

Revenue from Increased Cigarette and Tobacco Taxes, FY '05 - FY '11 (in millions)



Cigarette Stamps Sold, FY'04- FY '11; Tribal vs. Non-Tribal (in millions)



- Tobacco Prevention and Cessation Fund for anti-tobacco efforts (1.0 percent);
- Breast and Cervical Cancer Treatment Fund to fund Medicaid coverage of cancer treatment (0.7 percent).

Since passage of SQ 713, total cigarette sales have declined in Oklahoma. In FY '11, a total of 266.3 million cigarette stamps were sold, a 25.4 percent decrease compared to FY '04, the last full year under the old tax rate, but a slight increase over FY '10. Tribal sales have fallen sharply the past three years while non-tribal sales rose in FY '11 to their highest level since FY '05.

The tax increase, which took effect mid-way through FY '05 (Jan. 1, 2005), generated \$107.1 million in FY '06, the first full year under the new rates. Revenues rose for the next three years before declining slightly in FY '10 and then rising again in FY '11 to \$137.4 million.

When the tobacco tax increase was proposed, it was projected to generate \$104 million from non-tribal retailers and \$46 million from tribal retailers. In FY '11, net revenue collections from non-tribal retailers came in at \$111 million, slightly above the state's original projections. Tribal tax collections for health care projects totaled \$26.5 million in FY '10. This is below initial projections, but significantly above collections in the first years under the new law. In FY '06, tribal sales yielded only \$11.6 million.

Most of the initial shortfall in tribal tobacco tax collections was the result of a shift in sales to retailers selling cigarettes with the lowest 5.75 cent 'proximity exception' tax rate. As a result of various measures aimed at curtailing tribal retailers from purchasing and reselling cigarettes stamped with the lowest rate, its prevalence declined from over two-thirds of all tribal sales in FY '07 to just 6 percent in FY '11. The state negotiated a new “unity rate” of 51.5 cents per pack with several tribes which took effect in 2008 and accounted for 52 percent of tribal sales in FY '11. One-third of tribal sales in FY '11 took place under the highest compact rate of 85.75 cents per pack.