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## FISCAL IMPACT REPORT

**SPONSOR** Harper/McQueen/  
Montoya      **ORIGINAL DATE** 2/19/19      **LAST UPDATED** 3/04/19      **HB** 441/aHF1#1

**SHORT TITLE** Lottery Changes      **SB** \_\_\_\_\_

**ANALYST** Glenn

### REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Nonrecurring	Fund Affected
FY19	FY20	FY21		
Indeterminate/See Fiscal Implications	Indeterminate/See Fiscal Implications	Indeterminate/See Fiscal Implications	Recurring	Lottery Tuition Fund

(Parenthesis ( ) Indicate Revenue Decreases)

Relates to SB 80, SB 179, SB 283, SB 407, SB 397, HB 146, HB 350, HB 363

Conflicts with SB 80, SB 283

### SOURCES OF INFORMATION

LFC Files

#### Responses Received From

New Mexico Attorney General (NMAG)

Higher Education Department (HED)

Lottery Authority (NMLA)

### SUMMARY

#### Synopsis of HF1#1 Amendment

The House Floor #1 Amendment to House Bill 441:

- removes language in Section 1’s amendment to Section 6-24-6(A)(13) NMSA 1978 that ties the amount of any bonuses paid to lottery contractors and vendors to the increase in ticket sales revenue deposited in the lottery tuition fund in the state treasury, and makes a corresponding change in the bill’s title.

- amends Section 4(A)(3), which prohibits the Lottery Authority from sports betting or betting on real events, to state that “real events” covered by the prohibition do not include live drawings or other live events ancillary to lottery games.

Synopsis of Original Bill

House Bill 441 modifies the New Mexico Lottery Act to:

- Tie the amount of any bonuses paid to lottery employees and vendors to the increase in ticket sales revenue deposited in the lottery tuition fund in the state treasury;
- Change the dispensation of unclaimed lottery prizes, specifically that forfeited prizes be paid into the tuition fund instead of being paid into the NMLA prize fund;
- Provide for semiannual deposits to the tuition fund instead of monthly deposits; and
- Add a new section of the Act prohibiting certain technology and types of lottery games including video lottery games, as defined in the bill, mobile phone games, sports betting, and self-service machines tied to gas pumps or ATMs.

**FISCAL IMPLICATIONS**

**New Mexico Lottery Authority**

NMLA states that HB 441's provisions pertaining to unclaimed prizes and prohibiting certain types of lottery games have significant fiscal implications for the lottery tuition fund.

Unclaimed Prizes

NMLA explains that, under current law, when lottery prizes are not claimed within the required time, NMLA uses those prize amounts for three important purposes:

1. to meet the monthly statutory 30 percent return mandate in Section 6-24-24 of the New Mexico Lottery Act;
2. to enhance Scratchier (instant-win) game prizes for players, thereby increasing sales and generating more revenue dollars for the tuition fund; and
3. to support cash flow for paying expenses, including prizes for winners.

Section 2 of HB 441 requires NMLA to pay unclaimed prizes into the lottery tuition fund and prohibits them from inclusion in the calculation of gross revenues required for transmission to the lottery tuition fund under Section 6-24-24. NMLA states that HB 441 would negatively affect its use of unclaimed prize money in several respects.

First, NMLA notes that, because it is included in gross revenues, unclaimed prize money is already being transferred to the tuition scholarship fund, and is not a source of new or additional funding for tuition scholarships. NMLA's ability under current law to use unclaimed prizes to increase Scratchier prizes results in higher sales and tuition fund dollars than would be available without the use of unclaimed prizes. Without the use of the unclaimed prize fund, NMLA's total fiscal year transfer to the tuition fund would be reduced by \$6,000,000 or more. Since fiscal year 2008, the tuition fund has received nearly \$40,000,000 of unclaimed prize money to meet the mandatory return requirement.

NMLA reports that, as of June 30, 2018 and 2017, it had unclaimed prizes in the amount of

\$1,651,204 and \$1,307,897, respectively, reported as prizes payable that had not yet been applied against prize expense. Those amounts were deposited in the unclaimed prize fund and continue to supplement the prizes on Scratchers games that have been printed and offered for sale.

Second, NMLA states that it currently relies on the unclaimed prize fund to supplement net revenues used to meet the monthly statutory obligation to return 30 percent (since 2009) of net revenues to the tuition fund. NMLA has needed unclaimed prize money in approximately 83 percent of the months (114 out of 137) since the return mandates began in 2007. Without unclaimed prizes to supplement net revenue, as would be the case under HB 441, NMLA would have been returning only 27.5 percent to 28 percent each month.

NMLA notes that, to meet the mandated return, it had to reduce the prize payouts on Scratchers games in the spring of 2007. That action reduced Scratchers sales by 24 percent between 2007 and 2014, which, in turn, is estimated to have reduced the amount returned to the tuition fund by \$35 million to \$50 million during those seven fiscal years. NMLA anticipates that further reduction of Scratchers prize payouts due to the bill would aggravate the declines in Scratchers game sales and dramatically reduce the dollar amount returned to the tuition fund each year.

Third, NMLA states that, without unclaimed prizes, NMLA's cash flow and cash in the bank would decrease. Having cash available allows NMLA to pay prizes won early in a game before the game has achieved the requisite sales to fund those prizes. Money would have to be continually borrowed to pay expenses, such as prizes to winners, retailer commissions, vendor and supplier costs, and other operating expenses. The interest paid on money borrowed would be another reduction in the amount transmitted to the tuition fund.

Finally, NMLA notes that it has nine to twelve months of Scratchers ticket inventory available for sale at retailer locations. The prizes in these Scratchers games have been partially funded from unclaimed prizes. If HB 441 passes and is applicable to NMLA's current Scratchers ticket inventory, NMLA would have to pull games from the marketplace and shred millions of tickets. NMLA states, as an example, that it would be forced to pull or significantly reduce the \$10 Scratchers price point from the game portfolio, resulting in the loss of approximately \$22,000,000 in annual sales. NMLA also states that it would likely incur costs from removing the inventory of Scratchers games and that the cash flow disruption would likely result in interest costs from borrowing money to pay expenses.

### Technology Prohibitions

NMLA states that, as a sales organization, NMLA endeavors to use new technology and game types to keep its products relevant to consumers. NMLA must be able to keep up with an environment where technology changes often and consumers are looking for more convenient purchase methods, including being able to purchase items where they are. Not changing with new technology would affect NMLA's ability to sell tickets, which would reduce the amount available to transfer to the tuition fund.

NMLA describes two instances where NMLA has approved the use of technology or games that would be precluded by HB 441. First, the Lottery Board of Directors approved a policy in 2015 that included mobile phone technology to add convenience to lottery purchases. For example, introducing a simple voucher program where a player would purchase a voucher at a retailer store and then apply the amount of that voucher to a mobile app for lottery purchases, would allow players to purchase draw game plays at their convenience. NMLA states that prohibiting

any sort of gaming on a mobile phone diminishes the lottery’s relevance to millennials and other groups who use mobile technology heavily for their consumer decisions.

Second, in 2018, the Lottery Board of Directors approved moving forward with a lottery game with a sports theme. The sports lottery game would be very similar to existing games like Pick 3. A player would use a simple play slip to select numbers that correspond to sports elements, such as teams. The sports lottery game would use a parlay play type where a player must select the winners of at least three games to win. The processes to select numbers, purchase a ticket, and claim prizes would follow existing draw games. NMLA states that the prohibition of such a game would reduce NMLA’s ability to reach new players. Eliminating any sports lottery game also eliminates the new contributions that would be made to the tuition fund.

NMLA notes that it does not sell from ATMs at present and that a program to sell tickets at gas pumps is being discontinued. Nevertheless, NMLA is concerned that the bill’s ATM and gas pump prohibitions would prevent NMLA from reaching consumers where they are and in a convenient way in the future.

### **Higher Education Department**

HED states that, for purposes of the discussion below, it estimated revenue to the lottery tuition fund from NMLA’s report of unclaimed prize pool funds in the FY17 audited financial statement. See

[https://www.saonm.org/media/audits/811\\_New\\_Mexico\\_Lottery\\_Authority\\_FY2017.pdf](https://www.saonm.org/media/audits/811_New_Mexico_Lottery_Authority_FY2017.pdf)

NMLA’s audited financial statements indicate that during fiscal year 2017, much of the balance of unclaimed prizes was used to meet Section 6-24-24’s 30 percent return mandate, reducing the balance of unclaimed prizes from \$2,553,494 down to \$1,307,897. According to HED, a \$1.3 million increase in the lottery tuition fund would increase the per-student scholarship award by approximately 3 percent.

## **SIGNIFICANT ISSUES**

### **Lottery Authority**

According to NMLA, HB 441, if enacted, would not lead to any net increase in funding for tuition scholarships. By decreasing money available to supplement prizes on Scratcher games and suppressing new game innovation, NMLA states that the bill would have a negative impact on funding for tuition scholarships. See discussion under Fiscal Implications.

NMLA notes that, since 1997, NMLA has been selling lottery tickets through self-service lottery terminals. There are approximately two hundred such machines throughout the state. NMLA does not believe the bill’s prohibition against selling “through a self-service device that is part of or shares a display with an automated teller machine” applies to ticket vending machines, but believes this language and the bill’s prohibition against selling “through a self-service device that is...adjacent to a retail petroleum dispenser” are unclear.

## Higher Education Department

HED states that the purpose of the New Mexico Lottery Act is to provide tuition assistance for qualified students at New Mexico post-secondary educational institutions. See Section 6-24-3 NMSA 1978. HED explains that since 2009, the cost of tuition scholarships has outpaced revenues from lottery ticket sales. As a result, the year-end fund balance of the lottery tuition fund has declined significantly in recent years.

Section 21-21N-4(B) of the Legislative Lottery Tuition Scholarship Act directs NMHED to distribute funds as follows:

- 1) one thousand five hundred dollars (\$1,500) per scholarship per program semester for a student enrolled at a research institution;
- 2) one thousand twenty dollars (\$1,020) per scholarship per program semester for a student enrolled at a comprehensive institution; and
- 3) three hundred eighty dollars (\$380) per scholarship per program semester for a student enrolled at a community college.

Depending on the total amount available for tuition scholarships, the Act directs HED to increase or decrease awards in a manner that maintains the ratio of the tuition distribution in Section 21-21N-4(B). Based upon projected enrollment, available fund balance, and statutory requirements, HED determined the following actual awards in FY19:

- \$2,294 per semester for students at research universities;
- \$1,560 per semester for students at comprehensive colleges; and
- \$581 per semester for students at community colleges.

The projected FY20 tuition sector average is predicted to be 70-75 percent of sector average tuition, depending on tuition rates, enrollment trends and actual revenues. HED will set the FY20 sector average on or before June 1, 2019.

## Bonuses – Potential Constitutional Issues

HB 441 requires that bonuses or incentive compensation committed or paid to NMLA's employees, agents, lottery contractors and vendors be based on the increase in lottery ticket sales revenues deposited in the lottery tuition fund and not on NMLA's gross revenues. NMLA states that it does not currently provide bonuses or incentives to officers, agents, employees, contractors, or vendors that are based on gross revenues.

The payment of bonuses contemplated by the bill raises issues under two provisions of the New Mexico Constitution. The first, often referred to as the "extra compensation clause," provides, in pertinent part:

No law shall be enacted giving any extra compensation to any public officer, servant, agent or contractor after services are rendered or contract made....

N.M. Const. art. IV, § 27.

The second provision is the "antidonation clause" of Article IX, Section 14, which generally

prohibits the state and specified local governments from “directly or indirectly ... mak[ing] any donation to or in aid of any person, association or public or private corporation....” A “donation” for purposes of the antidonation clause is "a ‘gift,’ an allocation or appropriation of something of value, without consideration." *Village of Deming v. Hosdreg Co.*, 62 N.M. 18, 28, 303 P.2d 920 (1956).

New Mexico courts have held that the extra-compensation clause and the antidonation clause prohibit retroactive salary increases and bonuses paid to employees and public contractors for services already performed. See *Nat’l Union of Hosp. & Health Care Employees v. Board of Regents of UNM*, 2010-NMCA-102, ¶ 40 (concluding that bonus to bargaining unit members included in an arbitrator’s award was “a retroactive wage” that violated Article IV, Section 27 and Article IX, Section 14). This means that, to pass constitutional muster, any bonus or incentive compensation contemplated by HB 441 would have to be paid in exchange for future services of an employee, vendor or contractor. See N.M. Att’y Gen. Advisory Letter (June 4, 2004) (available on New Mexico One Source) (discussing the constitutionality of retroactive pay increases, performance bonuses and bonuses in lieu of pay increases).

### **ADMINISTRATIVE IMPLICATIONS**

HED notes that its Financial Aid Division pays lottery tuition scholarship funds directly to higher education institutions on a reimbursement basis. HED states that a semi-annual distribution of lottery proceeds into the lottery tuition fund, as proposed by the bill, may affect the timing of reimbursements to the institutions.

### **CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP**

Relates to:

SB 80 Forfeited Lottery Prizes to Tuition Fund  
SB 179 Disabilities Students Lottery Scholarships  
SB 283 Limit Lottery Operational Expenses  
SB 407 Lottery Funds for Tribal Colleges  
SB 397 Anonymity of Lottery Winners  
HB 146 Full Lottery Scholarship Based on Need  
HB 350 Anonymity of Lottery Winners  
HB 363 Lottery Funds for Tribal Colleges

Conflicts with:

SB 80, which also amends Section 6-24-21 NMSA 1978  
SB 283, which also amends Section 6-24-24 NMSA 1978

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