

COMMISSION AGENDA ITEM

Item 8(k) – Fiscal Year 2025-26 Budget



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To: California State Lottery Commission

From: Harjinder K. Shergill Chima *HKC*
Director

Prepared By: Nicholas Buchen
Deputy Director, Finance Division

Subject: **Item 8(k) – Fiscal Year 2025-26 Budget**

ISSUE

Pursuant to California State Lottery (Lottery) policy, the Lottery is required to present the California State Lottery Commission (Commission) with a proposed annual budget for the upcoming fiscal year, typically in June.

BACKGROUND

The Lottery's budget prepared for Fiscal Year (FY) 2025-26 presents a sales goal of \$9.10 billion and is estimated to provide approximately \$2.08 billion to public education. This proposed budget includes resources to responsibly maintain operational growth as well as the resources necessary to implement the Lottery's FY 2025-26 Business Plan. The budget represents the financial plan to deploy strategies to further the Lottery's current multi-year strategic plan to drive bottom-line contributions to education.

DISCUSSION

Development of the Lottery's FY 2025-26 budget began by zero-basing divisional operating expense budgets. A preliminary sales projection was used to determine the availability of resources to fund proposed business plan initiatives and address operational improvements to drive increased sales and contributions to public education.

This comprehensive assessment of sales goals, the funding needed to deliver those goals, and the resulting contribution to education culminates in the proposed FY 2025-26 budget presented for approval. A summary of the elements of the proposed FY 2025-26 budget is presented below:

Sales

Total sales for all Lottery products are projected to be \$9.10 billion for FY 2025-26; this represents an increase of \$72 million, or 0.8 percent from the estimated year-end sales levels for FY 2024-25. The primary driver of this projected year-over-year increase in sales is that the multi-state jackpot games (Mega Millions® and Powerball®) experienced lower than expected

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performance in the current year where we anticipate more typical expected jackpot performance in the coming year, combined with a full year of the new \$5 Mega Millions game.

The following chart compares the FY 2024-25 year-end estimate (rounded to the nearest million) with proposed sales goals for the FY 2025-26 budget.

Fiscal Years Comparison Chart

Comparison of Revenues FY 2024-25 Estimated Sales and Proposed FY 2025-26 Sales Goals (Dollars in Thousands)			
Sales:	Year-End Estimate FY 2024-25	Proposed Budget FY 2025-26	Difference
Scratchers®	\$6,908,000	\$6,820,000	(\$88,000)
Multi-State Jackpot Games	1,038,000	1,180,000	142,000
SuperLotto Plus®	237,000	240,000	3,000
Hot Spot®	421,000	440,000	19,000
Daily Games	424,000	420,000	(4,000)
Total Sales	\$9,028,000	\$9,100,000	\$72,000

Expenses

The following section describes costs associated with the FY 2025-26 budget.

Prize Expense

Prize expense is estimated to total \$6.0 billion in FY 2025-26. This is an increase of \$42.4 million (0.7 percent) from the estimated FY 2024-25 prize expense mainly due to the increased sales projection.

Pursuant to Lottery policy, the Director is required to make a determination that prize payout levels across all games have been optimized for the coming fiscal year to ensure that funding for education is maximized annually. Since Scratchers sales account for more than 70 percent of total revenues and the Lottery has more direct influence on the sale of these tickets, the Lottery ran several product plan scenarios for Scratchers to identify the optimal mix yielding the highest contribution to education. The resulting estimated prize expense totals 66.2 percent of projected sales for FY 2025-26, which is within the range of 65 percent to 67 percent that was recommended as being ideal in an analysis that was conducted for the Lottery to determine the optimal prize payout rate.

Administrative Expenses

Administrative expenses include retailer compensation, gaming costs, and operating costs. The Lottery Act caps administrative expenses at 13.0 percent of total annual sales revenues.

Excluding the reserve for insurable risk and administrative spending reserve (described below),

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total administrative expenses for FY 2025-26 are estimated to be \$1.08 billion, a slight increase of \$4.3 million (0.4 percent) from estimated administrative expenses for FY 2024-25. This year-over-year change primarily reflects the increased sales projection partially offset by strategic investment in FY 2025-26–Business Plan initiatives and operational improvements to help achieve and sustain future growth.

Retailer compensation costs are estimated to total approximately \$617.0 million for FY 2025-26, which represents a decrease of \$405 thousand (0.1 percent) from the FY 2024-25 year-end projection. This budget category includes the cost to pay the Lottery's more than 23,000 retail partners incentives to sell Lottery tickets and cash the associated eligible winning tickets. Retailers also earn bonuses for selling eligible winning jackpot/top prize tickets and certain winning tickets worth \$1.0 million or more. The year-over-year decrease in this item is primarily associated with a higher-than-expected payout of incentive bonuses in the current fiscal year.

Gaming costs are budgeted at \$157.3 million for FY 2025-26, which is a decrease of \$4.1 million (2.5 percent) from the FY 2024-25 year-end projection. This budget category includes the cost of operating the gaming system, gaming equipment installation and maintenance, and production and distribution of Scratchers tickets. This year-over-year decrease is due primarily to the decreased sales projection for Scratchers in FY 2025-26.

Excluding the reserves, retailer compensation and gaming costs account for 71.5 percent of the Lottery's administrative expenses for FY 2025-26. The remaining administrative expenditures are the Lottery's operating costs, which include personnel costs, advertising/marketing costs, and other overhead costs. Operating costs also contain the funding and resources required to execute the FY 2025-26 Business Plan initiatives and funding for operational improvements which, combined, account for the vast majority of the projected year-over-year increase in this budget category.

Personal services costs increases are mainly due to a previously-negotiated general salary increase that becomes effective on July 1, the assumption that the Lottery will be more effective in filling positions in the upcoming fiscal year, the addition of several temporary help positions to meet operational needs, and the proposed addition of 15 new positions for FY 2025-26.

Also included within administrative expenses for FY 2025-26 is a \$5.0 million reserve for insurable risk to cover fiscal exposures for the areas of our organization that we are continuing to self-insure, as well as a \$95.0 million administrative spending reserve to act as a safeguard against future uncertainties. The administrative spending reserve also provides the Commission and the Lottery with the flexibility to take advantage of opportunities to increase funding for education that may emerge over the upcoming year. The administrative spending reserve is an element of the 13 percent of total revenues specified for administrative expenses. Pursuant to provisions of the Lottery Act, the entire unspent amount within both the administrative spending reserve and the reserve for insurable risk will be transferred directly to public education.

Summary

The proposed FY 2025-26 budget contains sales goals of \$9.10 billion, which, combined with the other elements in the budget and assuming the reserves remain unspent, is estimated to

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result in approximately \$2.08 billion in contributions to California public schools. The Lottery takes pride in this being its second consecutive budget that projects more than \$2 billion in supplemental funding being generated for education.

The \$9.10 billion sales goal and the approximately \$2.08 billion estimated contribution to education for FY 2025-26 are based on executing the annual Business Plan which is designed to result in the sustainable growth of future revenues. The proposed budget includes a balanced approach between funding resources to drive gains in FY 2025-26, as well as investing in longer-term initiatives to enable the Lottery to increase sales and contributions to public education in years to come.

Note that the FY 2025-26 budget is based on less refined revenue and expenditure projections due to the budget being presented for Commission approval in May rather than June. Therefore, the Lottery anticipates presenting a revised FY 2025-26 budget to the Commission during the course of the coming fiscal year.

RECOMMENDATION

Staff recommends that the Commission approve the Lottery's budget for FY 2025-26.

Attachment