

## SUMMARY

# A Review of the SC Education Lottery and the State's Use of Lottery Proceeds

### INTRODUCTION

Members of the General Assembly requested the Legislative Audit Council to conduct an audit of the South Carolina Education Lottery (SCEL). We reviewed general management controls, and issues relating to lottery retailers and their compensation. Finally, we reviewed controls to ensure that lottery proceeds for education are spent as the General Assembly intended. This is not the responsibility of the SCEL, but of other agencies designated by the General Assembly.

Created by the South Carolina Education Lottery Act, the lottery began selling tickets in January 2002. The lottery is governed by a board of nine members appointed for three-year terms. SCEL is a quasi-state agency; it does not receive appropriations from the General Assembly but generates its own funds through the sale of lottery products, including online games and instant tickets. Game sales for FY 02-03 were \$724.3 million. As of June 30, 2003, the lottery had 129 employees and 3,545 retailers selling tickets.

December 2003



### ADMINISTRATIVE MANAGEMENT

We found that overall the SCEL has instituted adequate management controls and has taken steps to limit administrative costs.

The lottery's administrative costs (including commissions to retailers) have been less than the 15% allowed by law (see chart). The SCEL could further cut costs by reducing the number of cell phones provided to employees and re-evaluating its use of vehicles, resulting in more revenue for education.

We reviewed the lottery's management of its contracts, including its advertising and gaming contracts. The SCEL spent more than \$47 million on these contracts from August 2001 to March 2003. Generally we found that the lottery has adequate controls. However, in one case, the South Carolina Law Enforcement Division (SLED) has provided services to the lottery without a written contract.

The SCEL does not have a formal system of measuring results throughout the organization. The lottery measures its performance by meeting or exceeding its revenue goal. While revenue is a key indicator of the lottery's performance, it is not the only area in the organization that should be monitored for results.

We reviewed the Education Lottery Act and lottery operations and found that some advertising restrictions could be changed to reduce costs and increase lottery sales. Also, the lottery is restricted from competitively procuring communication services, which could prevent the selection of providers that are cost-effective and high-quality.



### LOTTERY OPERATIONS

We found that the SCEL has appropriate controls over the retailer licensing process; however, the policies and procedures should be updated regularly. As of March 2003, the SCEL had more than 3,400 licensed retailer locations and had denied licensure to 211 retailers — 98% for failure to pay taxes. We found that the lottery has experienced a low percentage (4/100 of 1% of gross lottery earnings) of retailer debt.

Compared to other states, South Carolina's 7% retailer commission is higher than average, ranking 7<sup>th</sup> out of 39 lotteries. We did not find problems in the area of retailer recruitment and retention. Most retailer terminations were because the retailer was not making anticipated profits.

The lottery has a good system of controls over prize payments; however, an independent review of policy compliance would strengthen these controls. Also, the General Assembly should consider lowering the threshold (currently \$5,000) at which the lottery must withhold debts owed to the state.

# THE STATE'S USE OF LOTTERY PROCEEDS

## FOR MORE INFORMATION

Our full report, including comments from SCEL, and this document are published on the Internet at

[www.state.sc.us/sclac](http://www.state.sc.us/sclac)

Copies can also be obtained by calling

(803) 253-7612

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We reviewed the use of lottery funds by various state agencies and found that generally the funds were used as required by law; however, the General Assembly released some agencies from the statutory requirements due to the state's budget situation. In 2003, the General Assembly passed joint resolutions lifting the restrictions on use of lottery funds for SDE and South Carolina State University. The local school districts and SCSU were able to use lottery funds for general operating expenses.

Higher education has been the primary recipient of lottery funds. The Commission on Higher Education (CHE) administers the LIFE, HOPE, and Palmetto Fellows scholarships (\$50.8 million), which accounted for 39% of CHE's lottery funds in FY 02-03.

Other uses of lottery funds for higher education include:

- G Tuition assistance for residents attending two-year institutions – \$34 million.
- G Endowed chairs program for research universities – \$30 million.
- G Funding for technology at the state's four-year teaching institutions and the two-year and technical colleges – \$21.7 million.

K-12 education has received about one-third of the lottery funds; most of these funds are distributed by the State Department of Education. The majority of these funds (76%) is distributed directly to school districts. K-12 lottery funding went in large part to programs designed to improve reading, math, science, and social studies, the purchase and maintenance of school buses, and for teacher specialists — teachers who are paid approximately \$20,000 annually in supplements to teach at low performing schools. Other lottery funds were appropriated to SCETV and the S.C. State Library for technology-related projects.

## Controls Not Yet Implemented

We found that controls over the use of lottery funds are uneven and still being established. For example, lottery-funded scholarships are subject to a system of audits and controls that are already established. In other areas, agencies have not yet instituted appropriate controls. The State Auditor's Office is directed by the FY 03-04 appropriations act to ensure that agencies receiving lottery funds have appropriate controls.

## Unused Lottery Funds

Some lottery funds have not been used in a timely manner. For example, using the first \$1 million in unclaimed prize funds, the Budget and Control Board was required by state law to contract for services assisting in the prevention and treatment of gambling disorders. However, although funds have been available since November 2002, as of August 2003, these contracts had not yet been awarded.

Other funds that were not used as of August 2003, were \$2 million for grants to teachers to pay for courses to upgrade their skills or obtain masters' degrees and \$1.5 million for the National Guard Student Loan Repayment Program. The General Assembly should consider whether previously appropriated lottery funds have been spent when deciding on future appropriations.

DISTRIBUTION OF LOTTERY PROCEEDS  
FY 01-02 AND FY 02-03

