

Losing Odds

**How New York Lottery
Retailers Are Losing Ground
Due to Rising Costs and
Stagnant Commissions**

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PREPARED BY THE

NEW YORK ASSOCIATION OF CONVENIENCE STORES

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Seven days a week, 52 weeks a year, including holidays, neighborhood mini-marts have provided adult New Yorkers with quick, convenient access to lottery tickets for the past 40 years.

By dedicating prime counter and window space, accepting new games and procedures, and tending to the needs of customers, they have helped build New York Lottery sales from \$53.6 million in 1967 to \$6.8 billion in 2006.

Our trusted partner in this 100-fold growth has been the state Division of the Lottery. A dynamic force in our industry, the Division has shown energy and initiative in helping retail lottery agents improve sales, inventory management and customer service.

Yet, as retailers' operating costs have risen dramatically – 377% in some expense categories – the Lottery Division has refused to fairly compensate them in the form of a higher commission.

The commission rate for mom-and-pop stores that have been selling instant lottery tickets one at a time for 40 years has languished at 6% since 1967. Meanwhile, racetracks are receiving commissions as high as 32% on the video lottery terminals they began operating just two or three years ago.

The New York Association of Convenience Stores is a private, not-for-profit trade association representing nearly 5,000 neighborhood mini marts and convenience stores licensed to sell New York Lottery tickets.

What's the issue?

The commission paid to New York Lottery retailers by the state Division of the Lottery doesn't cover the retailer's sharply higher costs and risks associated with selling lottery tickets.

What is the commission rate?

Retailers receive 6% of the face value of each ticket sold. It was 6 cents on the dollar when the Lottery began in 1967, when Lyndon B. Johnson was President. Forty years later, it's still 6 cents on the dollar.

What's wrong with that?

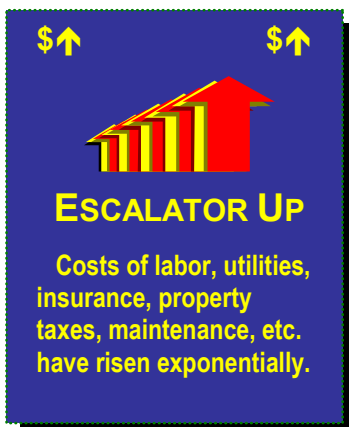
The costs and risks associated with selling lottery tickets have increased exponentially since 1967. Cost for labor, insurance, utilities, maintenance, property taxes, regulatory compliance, professional services etc. all have multiplied. And new risks of license suspension and ticket theft have emerged. Six percent is no longer sufficient to cover these costs and risks.

What are retailers complaining about – doesn't the lottery bring customers into your stores?

Absolutely. Lottery is a strong traffic builder. But in any business, when your gross profit doesn't cover your costs, no matter how many customers come through your door, you're losing ground financially.

If the Lottery paid retailers higher commissions, wouldn't that take money away from education?

No. As parents, citizens and taxpayers, we would **never, ever** ask that funding for education be diverted to agent commissions. Rather, the commission increase can be achieved by simply **reallocating a portion of the administrative resources** currently spent on broadcast advertising, prizes, and point-of-sale materials – *without* hurting sales. In order to fairly compensate the sales force that helped build New York Lottery into a \$6 billion-a-year enterprise, couldn't the state make do with a few less TV commercials showing a dog buying a lottery ticket?



The Issue

Do lottery retailers receive a percentage of winnings?

The Lottery offers a bonus of \$10,000 to stores selling Mega Millions jackpot tickets (odds: 175 million to one). For other winning tickets, stores receive only publicity. Paying retailers bonuses for winning tickets would not solve the problem, because the store incurs the higher costs and risks on every ticket it sells, not just on the small percentage of winning ones.

Who sets retail lottery commission rates?

The state Division of the Lottery. It fixed the rate at 6% in 1967 and has refused to increase it ever since, ignoring the exponentially higher costs and risks incurred by lottery retailers. Therefore, as an alternative, NYACS is seeking legislation to statutorily boost commissions to a fair level.

How much of an increase do convenience stores propose?

From the current 6.00% to 8.00%.

How much would that cost?

Approximately \$170 million a year, or 3% of the Lottery's operating budget. Again, the cost would be covered by reallocating existing administrative resources, *not* by reducing net proceeds to education.

	Commission Rate	Annual Expense	% of Lottery Budget
Current Commission	6.00%	511,059,000	10.7%
Proposed Commission	8.00%	681,241,647	13.8%
Difference	2.00%	170,182,647	3.1%

If it's a losing proposition for stores to sell lottery tickets, why not just quit selling them?

In today's competitive retail environment, that's not a realistic option for the typical mom-and-pop store. Lottery does bring a certain percentage of customers to the store. If you were to drop lottery but your competitor down the street still offered it, you would lose customers. A more sensible solution is to increase the rate of commission.

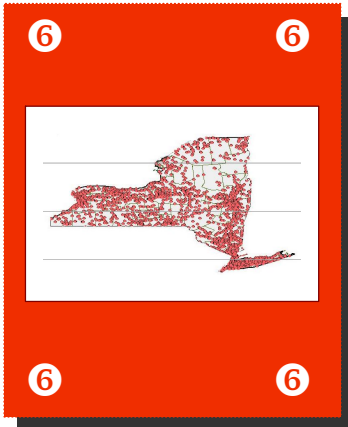
More Ways to Lose

Store's exposure to loss from theft of instant tickets grew as Lottery expanded number of games and introduced \$5, \$10 and \$20 denominations.

Comparison With Other States

How does New York compare with other states when it comes to commissions for lottery retailers?

Various other states pay commissions that are higher, lower or the same as New York. Here is a sample showing lottery commissions in 12 states, excluding any prize bonuses.



State	Lottery Since	Retailer Commission
North Carolina	2006	7.0%
Washington	1982	6.0%
Michigan	1972	6.0%
New York	1967	6.0%
Texas	1992	6.0%
Virginia	1988	6.0%
Ohio	1974	5.5%
Massachusetts	1972	5.0%
New Jersey	1970	5.0%
Maryland	1973	5.0%
Georgia	1993	5.0%
Illinois	1974	0.0%

How does New York compare with other states when it comes to the productivity of lottery retailers?

Among states in the sample, New York ranks third in per capita sales of lottery, higher than eight of the other 11 states in the comparison sample:

State	Retail Commission	Population U.S. Census	Per Capita Lottery Sales
Massachusetts	5.0%	6,349,097	\$ 710.42
Georgia	5.0%	8,186,453	388.14
New York	6.0%	18,976,457	358.49
Maryland	5.0%	5,296,486	294.70
New Jersey	5.0%	8,414,350	286.00
Michigan	6.0%	9,938,444	222.07
Virginia	6.0%	7,078,515	192.88
Texas	6.0%	20,851,820	182.22
Ohio	5.5%	11,353,140	195.91
Illinois	0.0%	12,419,293	160.16
Washington	6.0%	5,894,121	81.10
North Carolina	7.0%	8,049,313	28.05

Increased Costs for Retailers

Payroll Costs: While few convenience store employees are actually at the minimum wage, many receive hourly rates pegged to the minimum, i.e. \$2 above minimum. As illustrated by the chart below, since 1967, New York's minimum wage has gone up 377% – from \$1.50/hr to \$7.15/hr. Each hike automatically increases the store's expenses for FICA, unemployment taxes, workers comp insurance, etc.



Bigger Payday!

NYS minimum wage has increased from \$1.40/hr to \$7.15/hr, quintupling the retailer's costs of wages, FICA, unemployment taxes, and workers compensation insurance.

Year	NYS Non-Farm Min Hourly Wage	Commission on \$1 Lottery Ticket
1967	\$ 1.50	\$ 0.06
1968	1.60	0.06
1970	1.85	0.06
1974	2.00	0.06
1975	2.10	0.06
1976	2.30	0.06
1978	2.65	0.06
1979	2.90	0.06
1980	3.10	0.06
1981	3.35	0.06
1990	3.80	0.06
1991	4.25	0.06
2000	5.15	0.06
2005	6.00	0.06
2006	6.75	0.06
2007	7.15	0.06

Texas, like New York, has a 6% commission rate. But it also has a minimum wage \$2/hr lower than New York's. Thus the cost of selling lottery tickets is significantly greater in New York.

State	Retailer Commission	Minimum Wage
Georgia	5.0%	5.15
Texas	6.0%	5.15
Virginia	6.0%	5.15
Maryland	5.0%	6.15
North Carolina	7.0%	6.15
Ohio	5.5%	6.85
Michigan	6.0%	7.15
New Jersey	5.0%	7.15
New York	6.0%	7.15
Illinois	0.0%	7.50
Massachusetts	5.0%	7.50
Washington	6.0%	7.93

Increased Costs for Retailers

Property Taxes: Here are state and local property taxes per capita for fiscal year 2004, according to The Tax Foundation:

State	Retail Commission	Property Tax Per Capita
New Jersey	5.0%	\$ 2,099
New York	6.0%	1,677
Massachusetts	5.0%	1,532
Illinois	0.0%	1,407
Texas	6.0%	1,254
Michigan	6.0%	1,186
Maryland	5.0%	1,082
Virginia	6.0%	1,031
Washington	6.0%	1,029
Ohio	5.5%	981
Georgia	5.0%	880
North Carolina	7.0%	713

Cost of Doing Business: The Milken Institute's Cost of Doing Business Index examines wages, taxes, electricity and real estate. The higher the index, the greater the costs:

State	Retail Commission	Cost of Doing Business Index
New York	6.0%	130.7
Massachusetts	5.0%	125.5
New Jersey	5.0%	120.7
Michigan	6.0%	106.1
Illinois	0.0%	103.7
Washington	6.0%	103.5
Maryland	5.0%	101.8
Virginia	6.0%	94.7
Ohio	5.5%	93.3
Texas	6.0%	92.8
Georgia	5.0%	91.6
North Carolina	7.0%	91.6

Credit Card



BONANZA!

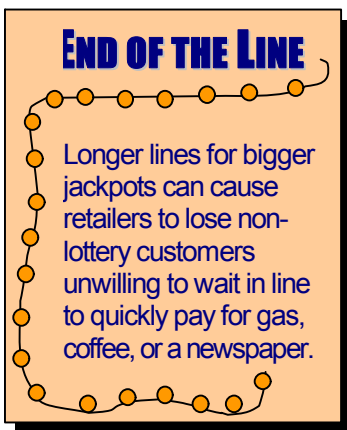
Over one-third of lottery sales are paid with credit or debit card. Acceptance fees to process those transactions eat up half the lottery commission!

Credit Card Fees: As the use of plastic as a form of payment, especially for smaller purchases, has exploded, so have the interchange fees that Visa and MasterCard charge retailers to process those transactions. When a lottery customer uses a credit card, the retailer incurs processing fees of 2% to 3% of the total sale, effectively cutting his or her 6% lottery commission in half.

Increased Risks for Retailers

In what way has the “risk” associated with selling lottery tickets increased?

Theft: First, the store's exposure to loss from theft of instant tickets multiplied as the Lottery Division introduced \$5, \$10 and \$20 instant games. If a customer or an unscrupulous employ steals a \$20 instant ticket, the retailer is out the full \$20. To make that back, at a 6% commission rate, the retailer would have to sell \$333 worth of additional lottery tickets.



Non-Lottery Customers: As Lotto and MegaMillions jackpots have grown, so have lines of lottery players at convenience store counters. This has increased the risk of losing *non-lottery* customers unwilling to wait in line to quickly pay for gas, coffee, or a newspaper. Some stores have tried adding a second register to handle just lottery customers, but doing so incurs additional labor costs, further eroding the 6% commission.

Licenses: In 2000, the lottery licenses of convenience stores were placed at risk under the state's tobacco enforcement program. If a clerk or cashier who has been properly trained in preventing underage sales sells tobacco to a minor anyway – even inadvertently – the store is punished. A second violation can result in the store's tobacco license *and* lottery license being suspended for six months. This pre-emptive suspension denies due process in that it penalizes the retailer based not on an act of selling lottery tickets to a minor, but a presumption that the store *might do so in the future* based on a separate proceeding. That's like saying if you get a speeding ticket, you should have your hunting license suspended, because if you violated the Vehicle and Traffic Law, you will probably violate the Conservation Law too. But that's another issue.

Vendor Reimbursement in NYS Law

Does New York State compensate retailers for performing other services besides selling lottery tickets?

Yes. The state pays retailers a sales tax “vendor allowance” to offset their cost of collecting, recording and remitting sales tax on taxable products they sell. This rate has been elevated periodically to reflect the retailer’s increased costs.

Year	NYS Sales Tax Vendor Allowance*	Lottery Commission
1994	1.5%	6.0%
1999	3.5%	6.0%
2006	5.0%	6.0%

* Quarterly \$ caps apply

Are there other parallels involving cost of doing business?

The state Cigarette Marketing Standards Act establishes state-minimum retail cigarette prices intended to reflect the convenience store’s “presumptive cost of doing business.” This minimum “markup” is periodically adjusted to keep pace with the retailer’s increasing costs.

Year	Minimum Retail Cigarette Markup	Lottery Commission
1986	6.0%	6.0%
1990	7.0%	6.0%

Do any other vendors receive commissions from the state Division of the Lottery?

Under another program administered by the Lottery Division, New York racetracks that operate video lottery terminals (VLTs) receive “lottery agent fees” based on their total revenue wagered minus prize payouts, as follows:

Annual Revenue	Commission
First \$50 million	32%
Next \$100 million	29%
Above that	26%

In addition to these generous commissions, the racetracks receive a “vendor marketing allowance” equal to 8% of the first \$100 million in revenue wagered minus prizes paid out and 5% on amounts exceeding that threshold.



Double Standard

Racetracks operating VLTs receive 32% commissions – plus an 8% marketing allowance – while lottery retailers get a commission of only 6%.

New York convenience stores aren't trying to make a "Fabulous Fortune" on lottery sales. They just want to attract customers, pay their bills, earn a living – and, in the process, help the state generate funds for education.

Since 1967, however, they have been asked by the State of New York to absorb rising costs and greater risks without any proportionate increase in lottery agent compensation. They are losing ground.

To date, the Division of the Lottery has declined to exercise its authority to administratively adjust retail commissions. Therefore, legislation is needed to establish a fair commission level that reflects the costs and risks associated with selling New York lottery tickets.

One excellent example is Senate bill 2998, introduced in February 2007 by Senator James Wright. Among other provisions, it would increase retail commissions to 8%. The bill has been referred to the Senate Committee on Racing, Gaming and Wagering.

The convenience store community welcomes the opportunity to continue the dialogue with the Legislature, the Division of the Lottery, and other interested parties on how to improve the odds for lottery retailers. And we look forward to building upon the partnership that has produced 40 years of success in generating revenue for education.



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