

NEW YORK STATE LOTTERY

**FINANCIAL STATEMENTS
(AND REPORT OF INDEPENDENT ACCOUNTANTS)**

For the Years Ended March 31, 1991 and 1990

**Coopers
& Lybrand**

Certified Public Accountants

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REPORT OF INDEPENDENT ACCOUNTANTS

New York State Lottery

We have audited the accompanying statements of assets and liabilities of the New York State Lottery as of March 31, 1991 and 1990, and the related statements of revenues and expenses and cash flows for the years then ended. These financial statements are the responsibility of the management of the New York State Lottery. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the assets and liabilities of the New York State Lottery as of March 31, 1991 and 1990, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

Coopers & Lybrand

Albany, New York
May 31, 1991

NEW YORK STATE LOTTERY
 STATEMENTS OF ASSETS AND LIABILITIES
 March 31, 1991 and 1990
 (In Thousands)

<u>ASSETS</u>	<u>1991</u>	<u>1990</u>
Current assets:		
Cash and cash equivalents	\$ 104,781	\$ 105,377
Accounts receivable	35,797	28,495
Investments, at amortized cost	<u>119,047</u>	<u>99,911</u>
Total current assets	259,625	233,783
Long-term investments, at amortized cost	924,592	782,771
Equipment, principally capital leases, net of accumulated depreciation and amortization	<u>4,597</u>	<u> </u>
Total assets	<u>\$1,188,814</u>	<u>\$1,016,554</u>
 <u>LIABILITIES</u>		
Current liabilities:		
Prizes payable	\$ 117,111	\$ 99,769
Unclaimed and future prizes	96,958	123,333
Due to education	8,137	(9,430)
Due to administration	4,622	8,558
Other payables	<u>21,997</u>	<u>4,045</u>
Total current liabilities	248,825	226,275
Long-term prizes payable	939,989	790,279
Commitments and contingencies (Note 10)	<u> </u>	<u> </u>
Total liabilities	<u>\$1,188,814</u>	<u>\$1,016,554</u>

The accompanying notes are an integral
part of the financial statements.

NEW YORK STATE LOTTERY

STATEMENTS OF REVENUES AND EXPENSES
 For the Years Ended March 31, 1991 and 1990
 (In Thousands)

	<u>1991</u>	<u>1990</u>
Ticket sales	\$2,134,644	\$2,058,139
Less:		
Prizes	(949,816)	(909,341)
Agent commissions	(128,104)	(123,488)
Contractor fees	<u>(57,122)</u>	<u>(50,393)</u>
Gross profit on ticket sales	999,602	974,917
General and administrative expenses	<u>55,044</u>	<u>63,637</u>
Income from operations	<u>944,558</u>	<u>911,280</u>
Nonoperating revenues (expenses):		
Interest income	105,924	84,305
Interest expense - amortization of discount on prizes payable	(94,648)	(70,197)
Other, net	<u>1,744</u>	<u>1,721</u>
Total nonoperating revenues (expenses)	<u>13,020</u>	<u>15,829</u>
Income earned and required allocation to education	<u>\$ 957,578</u>	<u>\$ 927,109</u>

The accompanying notes are an integral part of the financial statements.

NEW YORK STATE LOTTERY

STATEMENTS OF CASH FLOWS
 For the Years Ended March 31, 1991 and 1990
 Increase (Decrease) in Cash and Cash Equivalents
 (In Thousands)

	<u>1991</u>	<u>1990</u>
Cash flows from operating activities:		
Cash received from ticket sales	\$2,113,851	\$2,043,911
Cash payments for prizes	(893,236)	(829,070)
Cash payments for commissions and fees	(182,091)	(171,600)
Cash payments for general and administrative expenses	(58,763)	(72,962)
Net cash provided by operating activities	<u>979,761</u>	<u>970,279</u>
Cash flows from noncapital financing activities:		
Cash transfer to education	(940,011)	(927,986)
Cash flows from investing activities:		
Proceeds from investment maturities	106,675	90,894
Proceeds from sale of investments	2,160	4,598
Purchases of investments	(162,418)	(158,400)
Interest on cash and cash equivalents	11,449	14,086
Other cash payments and receipts, net	<u>1,788</u>	(325)
Net cash used in investing activities	<u>(40,346)</u>	<u>(49,147)</u>
Net decrease in cash and cash equivalents	(596)	(6,854)
Cash and cash equivalents, beginning of year	<u>105,377</u>	<u>112,231</u>
Cash and cash equivalents, end of year	<u>\$ 104,781</u>	<u>\$ 105,377</u>
Reconciliation of income from operations to net cash provided by operating activities:		
Income from operations	\$ 944,558	\$ 911,280
Adjustments to reconcile income from operations to net cash provided by operating activities:		
Depreciation and amortization	217	
Changes in assets and liabilities affecting income from operations:		
Accounts receivable	(7,341)	(11,012)
Prizes payable	72,404	57,561
Unclaimed and future prizes	(26,375)	21,516
Due to administration	(3,936)	(9,325)
Other payables	<u>234</u>	<u>259</u>
Net cash provided by operating activities	<u>\$ 979,761</u>	<u>\$ 970,279</u>

The accompanying notes are an integral part of the financial statements.

NEW YORK STATE LOTTERY
NOTES TO FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

The New York State Lottery (the "Lottery") was established in 1967. The Lottery is currently administered by the Division of the Lottery, an independent unit of the Department of Taxation and Finance, which was created in 1976 and operates in accordance with the provisions of the New York State Lottery for Education Law (Tax Law Article 34). The purpose of the Lottery is to raise revenue for education in the State of New York ("State") through the administration of lottery games.

The Lottery is included within the financial reporting entity of the State of New York. Within the General Purpose Financial Statements of the State of New York, the Lottery is accounted for within two funds. The revenues and expenditures for administration, aid to education and prizes are reported in a Special Revenue Fund. Monies for prizes are transferred to a Lottery Agency Fund for payment of prizes as claims are filed. The accompanying financial statements include the accounts of both funds and are presented as an enterprise fund. The accounting policies of the Lottery conform in all material respects to generally accepted accounting principles whereby revenue is recognized when earned and expenses are recognized when incurred.

Revenue Recognition

Revenue from completed Instant Games is reported based on the dollar value of lottery ticket sales. Ticket sales are determined based on the total number of tickets available for sale for each game less unsold tickets at the conclusion of each game.

Revenue from Instant Games in progress is reported based on the dollar value of the total number of tickets available for sale for each game less ticket inventories on hand at the Instant Game ticket contractor.

Revenue from Lotto, Cash 40, Daily Numbers, Pick 10, Keno and Win-Four games is reported at the dollar value of all tickets sold. Revenue from ticket sales includes subscription sales and other ticket sales for future drawings of approximately \$8,952,000 and \$8,913,000 for fiscal years 1991 and 1990, respectively.

On April 1, 1990, the Lottery replaced Keno with Pick 10, a game with similar features.

Commissions and Fees

Agents receive a commission of six percent based on the total tickets sold. Contractors receive a fee equal to a contractual percentage of the revenues generated through the respective network maintained by each contractor (see Note 10).

NEW YORK STATE LOTTERY

NOTES TO FINANCIAL STATEMENTS, Continued

1. Summary of Significant Accounting Policies, Continued

Allocation of Revenue from Ticket Sales

The allocation of ticket sales is made in accordance with the provisions of the New York State Lottery for Education Law which requires:

- allocations of ticket sales revenue to New York State for educational purposes to be at least 35 percent for the Daily Numbers, Win-Four and Instant games and 45 percent for Lotto, Cash 40, Pick 10 and Keno.
- allocations of ticket sales revenue for the payment of lottery prizes not to exceed 50 percent for the Daily Numbers, Win-Four and Instant games and 40 percent for Lotto, Cash 40, Pick 10 and Keno.
- allocations of ticket sales revenue from all games for the payment of lottery administration expenses (including agent commissions and contractors' fees) not to exceed 15 percent. Any excess of the maximum allocation over administration expenses is allocated to education. Such allocations amounted to approximately \$84,971,000 and \$75,297,000 for fiscal years 1991 and 1990, respectively. Administration expenses incurred by the Lottery represent the cost of developing and printing lottery tickets, advertising, salary and other operating costs and include an accrual for expenses to be paid after the fiscal year-end.

Cash Equivalents

For purposes of the statements of cash flows, the Lottery considers cash equivalents to be amounts held with banks and amounts held under the joint custody of the Lottery and the Office of the State Comptroller of the State of New York through the Short-term Investment Pool, which is used for the temporary investment of funds not required for immediate payments.

Investments

Investments, consisting of U.S. Government-backed obligations (zero coupon bonds and stripped Government securities), are carried at amortized cost. The periodic amortization of discount is recorded as interest income in these financial statements.

Equipment

Equipment is recorded at cost and is depreciated using the straight line method over five years, the estimated useful life of the assets.

Equipment acquired under capital leases are amortized using the straight-line method over five years, which is the lesser of the useful life of the asset or the term of the lease.

NEW YORK STATE LOTTERY

NOTES TO FINANCIAL STATEMENTS, Continued

1. Summary of Significant Accounting Policies, Continued

Prizes Payable

Prizes payable represents the liability for those prizes which are payable in annual installments. Such prize payments are funded by the Lottery's investment in U.S. Government-backed securities. The periodic amortization of discount is recorded as interest expense in these financial statements. Any excess of investment maturities over prize payments is made available for prizes.

Unclaimed and Future Prizes

Prizes unclaimed for one year after the drawing date are forfeited by the ticket holders and are allocated to education. Such allocations amounted to approximately \$28,663,000 and \$31,896,000 for fiscal years 1991 and 1990, respectively.

Legislation passed during fiscal year 1990 requires the Lottery to transfer unclaimed prizes to education six months after a drawing in anticipation of a possible forfeiture. Such transfer is in addition to the allocation to education and amounted to \$14,843,000 and \$14,852,000 for fiscal years 1991 and 1990, respectively. Funds for prizes claimed and paid between six and twelve months after a drawing are reimbursed by reducing subsequent transfers to the education account. All prizes can still be claimed for twelve months after a drawing.

Future prizes represent the difference between the statutory allocation to prizes and the amount allocated to the winning pools of Lottery games. Such amounts are disbursed, as determined by management, for the sole benefit of Lottery game winners.

Statements of Cash Flows

In September 1989, the Governmental Accounting Standards Board issued Statement No. 9, "Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting". The provisions of this statement are effective for fiscal years ending after December 15, 1990. Accordingly, the Lottery has adopted the provisions of Statement No. 9 in its 1991 financial statements and restated the previously reported statement of changes in assets and liabilities for 1990.

Reclassifications

Certain 1990 amounts have been reclassified to conform to the 1991 presentation.

NEW YORK STATE LOTTERY

NOTES TO FINANCIAL STATEMENTS, Continued

2. Cash and Cash Equivalents

Lottery deposits and investments are made in accordance with New York State statutes.

Lottery sales receipts are allocated and deposited in investment fund accounts for prizes, education and administration under the joint custody of the Lottery and the Office of the State Comptroller of the State of New York. The accounts for prizes and administration earn interest through participation in a short-term investment pool administered by the State Comptroller. The carrying and market value of the accounts included in cash and cash equivalents were \$92,200,000 and \$107,145,000 at March 31, 1991 and 1990, respectively. Interest income earned in each investment account is used for the specific purpose and benefit of that account.

The Lottery also maintains sole custody accounts which are used for daily cash management purposes. Amounts of cash balances (book overdraft) included in cash and cash equivalents related to sole custody accounts were \$12,581,000 and (\$1,768,000) for fiscal years 1991 and 1990, respectively.

The Lottery's deposits are collateralized under a program administered by the Office of the State Comptroller of the State of New York. The State requires that its depository banks pledge collateral based on available bank balances. All securities pledged as collateral are held by the State's fiscal agent in the name of the State. The Lottery's deposits with financial institutions were fully collateralized at fiscal year-end. The State uses average daily available balances adjusted for experience to determine collateral requirements. This method could result in the available balances being undercollateralized at certain times during the fiscal year.

3. Investments

The Lottery is authorized to invest in U.S. Government-backed obligations (zero coupon bonds and stripped Government securities), which will provide for the payment of prizes payable (see Note 5). During fiscal years 1991 and 1990, approximately \$94,923,000 and \$70,456,000, respectively, of amortized discount was included in interest income.

These investments consisted of the following at March 31 (in thousands):

	<u>1991</u>	<u>1990</u>
Maturity value	\$2,043,222	\$1,779,896
Less unamortized discount	<u>999,583</u>	<u>897,214</u>
Total carrying value	1,043,639	882,682
Less: investments, maturing within one year	<u>119,047</u>	<u>99,911</u>
Long-term investments	<u>\$ 924,592</u>	<u>\$ 782,771</u>
Total market value	<u>\$1,115,751</u>	<u>\$ 926,943</u>

NEW YORK STATE LOTTERY
 NOTES TO FINANCIAL STATEMENTS, Continued

3. Investments, Continued

Maturities of the investments in each of the five fiscal years following March 31, 1991, and the total thereafter, are as follows (in thousands):

1992	\$ 123,890
1993	122,921
1994	122,438
1995	123,186
1996	123,190
1997 and thereafter	<u>1,427,597</u>
	<u>\$2,043,222</u>

The Lottery's investments are categorized to give an indication of the level of risk assumed by the Lottery at year-end. All of the Lottery's investments are included in category "A", the lowest risk, as defined by the Governmental Accounting Standards Board to include investments that are "insured or registered or securities held by the Lottery or its agent in the Lottery's name".

Disclosures relating to risk and type of investments as presented above are indicative of activity and positions held during the year.

4. Equipment

Equipment as of March 31, 1991 and 1990 is as follows:

	<u>1991</u>	<u>1990</u>
Equipment	\$4,914,495	\$ 100,000
Less accumulated depreciation and amortization	<u>317,200</u>	<u>100,000</u>
Equipment, net	<u>\$4,597,295</u>	<u>\$ -0-</u>

During fiscal 1991, the Lottery entered into a \$4,700,000 capital lease for new computer equipment. The lease is for a five-year term and requires ten semi-annual payments approximating \$573,000 each, through March 1996.

Accumulated amortization for the equipment recorded under this capital lease approximated \$217,000 at March 31, 1991.

NEW YORK STATE LOTTERY

NOTES TO FINANCIAL STATEMENTS, Continued

5. Prize Payable

Prizes payable consisted of the following at March 31 (in thousands):

	<u>1991</u>	<u>1990</u>
Total obligation	\$2,052,572	\$1,783,194
Less unamortized discount	<u>995,472</u>	<u>893,146</u>
Total carrying amount	\$1,057,100	\$ 890,048
Less: prize payable within one year	<u>117,111</u>	<u>99,769</u>
Long-term prizes payable	<u>\$ 939,989</u>	<u>\$ 790,279</u>

The amortized discount on the prizes payable is based on interest rates which range from 6.37 percent to 13.55 percent and reflect the interest rates earned by the investments held to fund the related liabilities. The amortization of discount is recorded as interest expense in the statements of revenues and expenses and amounted to \$94,648,000 and \$70,197,000 for the fiscal year 1991 and 1990, respectively.

The aggregate amount of prizes payable due in each of the five fiscal years following March 31, 1991, and the total thereafter, is as follows (in thousands):

1992	\$ 123,046
1993	123,046
1994	122,946
1995	122,836
1996	122,836
1997 and thereafter	<u>1,437,862</u>
	<u>\$2,052,572</u>

NEW YORK STATE LOTTERY

NOTES TO FINANCIAL STATEMENTS, Continued

6. Operating Segment Information

Operating segment information for fiscal 1991 and 1990 by type of lottery game is as follows (in thousands):

	1991				Total
	Lotto and Cash 40	Pick 10	Daily Numbers and Win-Four	Instant Games	
Ticket sales	\$851,328	\$119,065	\$902,290	\$261,961	\$2,134,644
Prizes	(324,184)	(45,964)	(447,845)	(131,823)	(949,816)
Commissions and fees	(65,917)	(9,403)	(70,874)	(39,032)	(185,226)
Interest and other income, net	99,977	713	5,415	1,563	107,668
Interest expense	(94,648)				(94,648)
General and administrative expenses	(25,297)	(3,416)	(25,992)	(339)	(55,044)
Income earned and required allocation to education	<u>\$441,259</u>	<u>\$ 60,995</u>	<u>\$362,994</u>	<u>\$ 92,330</u>	<u>\$ 957,578</u>
	1990				Total
	Lotto and Cash 40	Keno	Daily Numbers and Win-Four	Instant Games	
Ticket sales	\$929,493	\$ 65,591	\$860,563	\$202,492	\$2,058,139
Prizes	(353,356)	(24,308)	(429,308)	(102,369)	(909,341)
Commissions and fees	(71,593)	(5,101)	(66,903)	(30,284)	(173,881)
Interest and other income, net	77,488	496	6,510	1,532	86,026
Interest expense	(70,197)				(70,197)
General and administrative expenses	(31,916)	(2,229)	(29,266)	(226)	(63,637)
Income earned and required allocation to education	<u>\$479,919</u>	<u>\$ 34,449</u>	<u>\$341,596</u>	<u>\$ 71,145</u>	<u>\$ 927,109</u>

General and administrative expenses are allocated to each game based on the relationship of the revenue allocated to administration, net of commissions and fees of each game to the total of all games.

NEW YORK STATE LOTTERY

NOTES TO FINANCIAL STATEMENTS, Continued

7. Education

Income earned and required allocation to education during the fiscal years ended March 31, 1991 and 1990 are as follows:

	<u>1991</u>	<u>1990</u>
Revenue transferred to education	\$ 940,011	\$ 927,986
Prior year overtransfer	9,430	8,752
Other adjustments		(199)
Amount transferred from current year revenue	<u>949,441</u>	<u>936,539</u>
Current year payable (overtransfer)	<u>8,137</u>	<u>(9,430)</u>
Income earned and required allocation to education	<u>\$ 957,578</u>	<u>\$ 927,109</u>

8. Defined Benefit Pension Plan

Substantially all Lottery employees participate in the New York State Employees' Retirement System ("the System"), a cost-sharing multiple-employer public employee retirement system. The payroll for Lottery employees covered by the system for the year ended March 31, 1991 was approximately \$7,382,000; the Lottery's total payroll was \$7,536,000.

The System provides retirement benefits as well as death and disability benefits. All benefits vest after 10 years of credited service. Retirement benefits that employees are entitled to are established by New York State law and are dependent upon the point in time at which the employee last joined the System. These retirement plans have both contributory and noncontributory requirements depending upon the point at which an employee last joined the System. Most members of the System who joined before July 27, 1976 are enrolled in a noncontributory plan and may retire at age 55. Employees who last joined the System on or after July 27, 1976 are enrolled in a contributory plan which requires a 3% contribution of their salary and may retire at age 62. A public employee who joined the System on or after July 27, 1976 and leaves covered employment before 10 years of credited service may obtain a refund including interest of the accumulated employee contributions. Members, benefits, and employer and employee obligations to contribute are described in the New York State Retirement and Social Security Law. The number of members and benefit recipients of the System as of March 31, 1990 (1991 plan data is not available) totaled approximately 829,000, including 245,000 retirees and beneficiaries currently receiving benefits and no longer working members entitled to benefits but not yet receiving them; 80,000 nonvested inactive members, and 504,000 current working members.

The contribution requirement for the year ended March 31, 1991 was \$640,839, which consisted of \$503,408 from the Lottery and \$137,431 from employees; these contributions represented 6.8% and 1.9% of covered payroll, respectively.

NEW YORK STATE LOTTERY

NOTES TO FINANCIAL STATEMENTS, Continued

8. Defined Benefit Pension Plan, Continued

The contribution requirement for the year ended March 31, 1990 was \$500,276, which consisted of \$394,187 from the Lottery and \$106,089 from employees; these contributions represented 6.4% and 1.7% of covered payroll, respectively.

The "pension benefit obligation" is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of employee service to date. The measure, which is the actuarial present value of credited projected benefits, is intended to help users assess the System's funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among public employee retirement systems and employers. The System does not make separate measurements of assets and pension benefit obligation for individual employers. The pension benefit obligation at March 31, 1990 for the System as a whole, determined through an actuarial valuation performed as of that date, was \$36,974,000,000. The System's net assets available for benefits on that date (valued at market) were \$40,078,000,000 resulting in assets in excess of pension benefit obligation of \$3,104,000,000. The Lottery's 1990 contribution represented .07 percent of total contributions required of all participating entities.

Ten-year historical trend information showing the System's progress in accumulating sufficient assets to pay benefits when due is presented in the System's March 31, 1990 annual financial report.

9. Deferred Compensation

New York State offers its employees, including lottery employees, a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all employees, permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency.

All amounts of compensation deferred under the plan, all property and rights purchased with those amounts, and all income attributable to those amounts, property, or rights are (until paid or made available to the employee or other beneficiary) solely the property and rights of the State (without being restricted to the provisions of benefits under the plan), subject only to the claims of the State's general creditors. Participants' rights under the plan are equal to those of general creditors of the State in an amount equal to the fair market value of the deferred account for each participant. The assets and liabilities related to this plan are recorded in the State's financial statements.

NEW YORK STATE LOTTERY

NOTES TO FINANCIAL STATEMENTS, Continued

10. Commitments and Contingencies

Contractual arrangements:

The New York State Lottery maintains two parallel on-line gaming networks, each comprised of several thousand agent terminals. The Lottery contracts the operations of such networks with two contractors, GTECH Corporation (GTECH) and Control Data Corporation (CDC). The GTECH contract is for a term of approximately five years expiring December 31, 1992, and the CDC contract is for a term of six years expiring September 1, 1993. The New York State Lottery also contracts the operations of the Instant games with Scientific Games, Inc. This contract is for a term of approximately six years expiring January 13, 1992. Contractor fees are based on a percentage of ticket sales as defined in the respective contracts.

Insurance Contracts:

Prior to 1983, the Lottery had entered into agreements with New York insurance companies under which the Lottery purchased annuities and funding agreements under contracts that provide payments corresponding to the Lottery's obligation to the prize winners. Because it is the intent of the Lottery that the insurance companies make future installment payments directly to each prize winner, neither the present value of the annuities and funding agreements nor the present value of the related future payments are reflected in the accompanying financial statements. The Lottery may be liable for such future payments if the insurance companies were to default on their payments. Unpaid amounts under these arrangements approximated \$138,000,000 at March 31, 1991.

Litigation:

The Lottery has been named as a defendant in several lawsuits. While the ultimate outcome of these lawsuits cannot be predicted at this time, it is the opinion of management and in-house counsel that the disposition of any litigation in which the Lottery is involved will not have a material adverse effect on the financial position of the Lottery.

Federal Communications Commission (FCC) ruling:

On February 21, 1990, the FCC ruled, in response to a request from New York Telephone Company, that the New York Telephone Company should be permitted to retroactively charge intrastate rates rather than interstate rates for data telecommunications lines supplied to American Telephone and Telegraph Company (AT&T) for use by the Lottery. The Lottery estimates the amount of retroactive adjustment to approximate \$10,108,000.

The Lottery and AT&T have petitioned the FCC to reconsider its ruling, and those petitions are currently pending.

The ultimate outcome of this ruling cannot be predicted at this time. Management and in-house counsel believe that the final ruling will have no material impact on the financial position of the Lottery. Accordingly, no adjustment has been made to the accompanying financial statements.