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June 22, 1995

Mr. Hank Scott  
Director of Administration and Finance  
New York State Lottery  
One Broadway Center  
P.O. Box 7500  
Schenectady, NY 12301

Dear Hank:

Enclosed are fifteen (15) copies of the draft Audited Financial Statements and Other Financial Information for New York State Lottery for the year ended March 31, 1995.

We wish to extend our thanks and appreciation for the opportunity to perform this service. If you have any questions or comments, please call Rick Hannmann or me.

Very truly yours,


KPMG Peat Marwick LLP



Robert F. Audi  
Partner

Enclosures



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The Global Leader

NEW YORK STATE LOTTERY

Financial Statements  
and Other Financial Information

Years Ended March 31, 1995 and 1994

(With Independent Auditors' Report Thereon)

NEW YORK STATE LOTTERY

Financial Statements  
and Other Financial Information

Years Ended March 31, 1995 and 1994

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Independent Auditors' Report

## New York State Lottery

We have audited the accompanying statement of assets and liabilities of the New York State Lottery as of March 31, 1995, and the related statements of revenue and expenses, and cash flows for the year then ended. These financial statements are the responsibility of the New York State Lottery's management. Our responsibility is to express an opinion on these financial statements based on our audit. The accompanying financial statements of the New York State Lottery as of March 31, 1994, were audited by other auditors whose report thereon dated May 25, 1994, expressed an unqualified opinion on those statements.

We conducted our audit 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 audit provides a reasonable basis for our opinion.

In our opinion, the 1995 financial statements referred to above present fairly, in all material respects, the financial position of the New York State Lottery at March 31, 1995, and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles.



May 26, 1995

NEW YORK STATE LOTTERY

Statements of Assets and Liabilities

March 31, 1995 and 1994

(In Thousands)

<u>Assets</u>	<u>1995</u>	<u>1994</u>
Current assets:		
Cash and cash equivalents (Note 2)	\$ 157,657	94,365
Accounts receivable	102,422	36,743
Investments, at amortized cost (Note 3)	173,749	156,541
Instant game ticket inventory	<u>4,565</u>	<u>-</u>
Total current assets	438,393	287,649
Long-term investments, at amortized cost (Note 3)	1,320,572	1,202,000
Equipment and leasehold improvements, net of accumulated depreciation and amortization (Note 4)	<u>4,847</u>	<u>6,494</u>
Total assets	\$ <u><u>1,763,812</u></u>	<u><u>1,496,143</u></u>
<u>Liabilities</u>		
Current liabilities:		
Prizes payable (Note 5)	173,231	156,451
Unclaimed and future prizes	110,128	72,876
Due to education (Note 7)	107,882	25,914
Due to administration	7,108	6,825
Deferred revenue	10,709	9,934
Other payables	<u>18,053</u>	<u>8,394</u>
Total current liabilities	427,111	280,394
Long-term prizes payable (Note 5)	<u>1,336,701</u>	<u>1,215,749</u>
Commitments and contingencies (Note 11)		
Total liabilities	\$ <u><u>1,763,812</u></u>	<u><u>1,496,143</u></u>

See accompanying notes to financial statements.

NEW YORK STATE LOTTERY  
 Statements of Revenue and Expenses  
 Years Ended March 31, 1995 and 1994  
 (In Thousands)

	<u>1995</u>	<u>1994</u>
Ticket sales	\$ 3,028,585	2,369,080
Less:		
Prizes	(1,470,635)	(1,107,476)
Agent commissions	(181,725)	(142,145)
Contractor fees	(64,948)	(50,579)
Instant game ticket printing expense	(7,915)	-
Gross profit on ticket sales	<u>1,303,362</u>	<u>1,068,880</u>
General and administrative expenses	<u>(68,198)</u>	<u>(64,001)</u>
Income from operations	1,235,164	1,004,879
Nonoperating revenue (expenses):		
Interest income	121,877	115,636
Interest expense - amortization of discount on prizes payable	(117,314)	(110,893)
Other, net	<u>4,090</u>	<u>1,536</u>
Total nonoperating revenue	<u>8,653</u>	<u>6,279</u>
Income earned and required allocation to education, net	\$ <u>1,243,817</u>	<u>1,011,158</u>
Components of income earned (loss incurred) and required allocation to education, net:		
New York State	1,243,815	1,014,976
New York City (Note 1)	<u>2</u>	<u>(3,818)</u>
	\$ <u>1,243,817</u>	<u>1,011,158</u>

See accompanying notes to financial statements.

# NEW YORK STATE LOTTERY

## Statements of Cash Flows

Years Ended March 31, 1995 and 1994

(In Thousands)

	<u>1995</u>	<u>1994</u>
Cash flows from operating activities:		
Cash received from ticket sales	\$ 2,963,875	2,380,526
Cash payments for prizes	(1,413,235)	(1,132,308)
Cash payments for commissions and fees	(246,788)	(192,634)
Cash payments for ticket printing	(10,613)	-
Cash payments for general and administrative expenses	<u>(63,209)</u>	<u>(60,673)</u>
Net cash provided by operating activities	1,230,030	994,911
Cash flows from investing activities:		
Proceeds from investment maturities	162,822	149,247
Proceeds from sale of investments	-	5,106
Purchases of investments	(174,643)	(147,321)
Interest on cash and cash equivalents	4,202	4,403
Net proceeds from swaps of investment securities	2,513	60
Other cash payments and receipts, net	<u>1,374</u>	<u>1,200</u>
Net cash provided (used) by investing activities	(3,732)	12,695
Cash flows from noncapital financing activities:		
Cash transfer to education	(1,161,849)	(1,053,999)
Cash flows from capital financing activities:		
Cash payments for equipment and leasehold improvements	(31)	-
Principal payments on capital leases	<u>(1,126)</u>	<u>(1,008)</u>
Net cash used by capital financing activities	<u>(1,157)</u>	<u>(1,008)</u>
Net increase (decrease) in cash and cash equivalents	63,292	(47,401)
Cash and cash equivalents, beginning of year	<u>94,365</u>	<u>141,766</u>
Cash and cash equivalents, end of year	\$ <u>157,657</u>	<u>94,365</u>
Reconciliation of income from operations to net cash provided by operating activities:		
Income from operations	1,235,164	1,004,879
Adjustments to reconcile income from operations to net cash provided by operating activities:		
Depreciation and amortization	1,688	1,655
Change in operating assets and liabilities:		
Accounts receivable	(65,505)	10,295
Prizes payable	20,418	(7,208)
Unclaimed and future prizes	37,252	(17,648)
Ticket inventory	(4,565)	-
Due to administration	283	(1,010)
Deferred revenue	775	1,133
Other payables	<u>4,520</u>	<u>2,815</u>
Net cash provided by operating activities	\$ <u>1,230,030</u>	<u>994,911</u>

See accompanying notes to financial statements.

# NEW YORK STATE LOTTERY

## Notes to Financial Statements

March 31, 1995 and 1994

(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 revenue and expenses 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.

During fiscal year 1992, Chapter 6 of the Laws of 1991 created a special anti-crime instant cash game (the City games) for sale only within the City of New York. The purpose was to generate revenue for educational purposes, including security at educational facilities, within New York City. The City games began in September 1991 and are authorized by the legislation to continue through June 1996. The New York State Lottery administers the City games and is reimbursed for administrative costs (including agent commissions and contractors' fees) of the games up to a maximum of 15% of game sales. The law also has a hold harmless provision which requires the City games to reimburse the Lottery for shortfalls in net revenue, as defined, resulting from other instant cash games administered by the Lottery in the City of New York not increasing at an annual rate of 5%. Shortfalls approximated \$0 and \$4,012,000 in fiscal years 1995 and 1994, respectively.

(a) Revenue Recognition

(i) On-line Games

Revenue from ticket sales for Lotto, Take Five, Pick 10, New York Numbers and Win-4 games (on-line games) is recognized when the related drawing takes place. Revenue from subscription sales and other ticket sales for future drawings is recorded as deferred revenue.

(ii) Instant Cash Games

Revenue from instant cash games is recognized based on the dollar value of the total number of tickets available for sale. Tickets are available for sale upon being activated on the Lottery Validation System at the agent locations.

(b) Commissions and Fees

Agents receive a commission of 6% based on the total tickets sold. The on-line game contractor receives a fee equal to a contractual percentage of the revenue generated through the respective network maintained by the contractor. All other gaming contractors are paid fees based on the units of service provided (see note 11).

# NEW YORK STATE LOTTERY

## Notes to Financial Statements, Continued

### (c) 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 30% for the New York State Lottery instant cash games, 35% for New York Numbers, Win-4 and Pick 10, and 45% for Lotto. For Take Five, the allocation was changed to 35% in 1995 from 45% in 1994.
- Allocations of ticket sales revenue to New York City for educational purposes to be at least 35% for the New York City instant cash games, less any reimbursement to the Lottery for shortfalls in net revenue, as defined.
- Allocations of ticket sales revenue for the payment of lottery prizes not to exceed 55% for the New York State Lottery instant cash games, 50% for the New York Numbers, Win-4, Pick 10 and the New York City instant cash games, and 40% for Lotto. For Take Five, the allocation was changed to 50% in 1995 from 40% in 1994.
- Allocations of ticket sales revenue from all games for the payment of lottery administration expenses (including agent commissions and contractor fees) not to exceed 15%. Any excess of the maximum allocation over administration expenses is allocated to education as is any related interest or other income. Such allocations amounted to approximately \$133,182,000 and \$101,580,000 for fiscal years 1995 and 1994, respectively. Administration expenses incurred by the Lottery represent telecommunications, advertising, salary and other operating costs and include an accrual for expenses to be paid after the fiscal year-end.

### (d) 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.

### (e) 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.

### (f) Inventory

During 1995 the Lottery purchased instant game tickets directly from printers and have included tickets which have not been activated for resale in inventory. Inventories purchased for resale are valued at cost by game determined under the first-in, first-out (FIFO) accounting method. Tickets are charged to printing expense when activated for resale by the agents. At the conclusion of an instant cash ticket game unsold inventory is charged as a nonoperating expense.

NEW YORK STATE LOTTERY

Notes to Financial Statements, Continued

(g) Equipment and Leasehold Improvements  
Equipment and leasehold improvements are carried at cost. Depreciation of equipment is computed using the straight-line method over five years, the estimated useful lives of the assets. Amortization of leasehold improvements and equipment acquired under capital leases are amortized using the straight-line method over ten and five years, respectively, which is the lesser of their useful lives or the term of the leases.

When assets are retired or otherwise disposed of, the cost and related accumulated depreciation or amortization are removed from the accounts and any resulting gain or loss is reflected in nonoperating revenue (expenses) in the period of disposal.

(h) 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.

(i) Unclaimed and Future Prizes  
Prizes unclaimed for one year after the drawing date are forfeited by the ticket holder. Total prizes forfeited amounted to approximately \$27,916,000 and \$33,735,000 for fiscal years 1995 and 1994, respectively.

Legislation passed in June 1991, allows the Lottery to retain forfeited prizes and to use such amounts for payment of supplemental prizes in subsequent Lottery games. During fiscal year 1995, such supplemental prizes were paid for Lotto, New York Numbers, and Win-4; and during fiscal year 1994, such supplemental prizes were paid for Lotto and Take Five.

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.

(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 account for prizes earns interest through participation in a short-term investment pool administered by the State Comptroller. The account for administration earned such interest until June 1994 when the criteria for earning interest was changed by new legislation. The carrying and market value of the accounts included in cash and cash equivalents were \$158,104,000 and \$94,820,000 at March 31, 1995 and 1994, 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. The Lottery manages the investment of its cash balances to minimize its uninvested funds. At March 31, 1995 and 1994 the amount of outstanding checks in excess of bank balances included in cash and cash equivalents related to the sole custody accounts were (\$447,000) and (\$455,000), respectively.

NEW YORK STATE LOTTERY

Notes to Financial Statements. Continued

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.

(3) Investments

The Lottery is authorized to invest in U.S. Government-backed obligations (zero coupon bonds), which will provide for the payment of prizes payable (see note 5). During fiscal years 1995 and 1994, approximately \$117,696,000 and \$111,247,000, respectively, of amortized discount was included in interest income.

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

	<u>1995</u>	<u>1994</u>
Maturity value	\$ 2,622,184	2,416,404
Less: unamortized discount	<u>1,127,863</u>	<u>1,057,863</u>
Total carrying value	1,494,321	1,358,541
Less: investments, maturing within one year	<u>173,749</u>	<u>156,541</u>
Long-term investments	\$ <u>1,320,572</u>	<u>1,202,000</u>
 Total market value	 \$ <u>1,594,142</u>	 <u>1,505,498</u>

Maturities of the investments in each of the five fiscal years following March 31, 1995, and the total thereafter, are as follows (in thousands):

1996	\$ 180,328
1997	180,449
1998	180,620
1999	180,283
2000	180,391
Thereafter	<u>1,720,113</u>
	\$ <u>2,622,184</u>

The Lottery periodically enters into certain swap transactions whereby stripped government securities are swapped for other stripped government securities with substantially identical terms and characteristics. During fiscal years 1995 and 1994, the face value of the securities swapped amounted to \$859,881,000 and \$27,823,000 resulting in a gain of approximately \$2,513,000 and \$60,000, respectively. This gain is included in nonoperating revenue in the caption "other, net."

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 described above are indicative of activity and positions held during the year.

NEW YORK STATE LOTTERY

Notes to Financial Statements, Continued

(4) Equipment and Leasehold Improvements

Equipment and leasehold improvements as of March 31, are as follows (in thousands):

	<u>1995</u>	<u>1994</u>
Equipment (principally capital leases)	\$ 6,527	6,485
Leasehold improvements	<u>4,526</u>	<u>4,526</u>
	11,053	11,011
Less: accumulated depreciation and amortization	<u>(6,206)</u>	<u>(4,517)</u>
Equipment and leasehold improvements, net	<u>\$ 4,847</u>	<u>6,494</u>

The Lottery has entered into certain capital leases for computer equipment approximating \$5,378,000. Accumulated amortization for the capital leases approximated \$3,889,000 and \$2,906,000 for fiscal years 1995 and 1994, respectively.

(5) Prizes Payable

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

	<u>1995</u>	<u>1994</u>
Total obligation	\$ 2,635,786	2,425,352
Less: unamortized discount	<u>1,125,854</u>	<u>1,053,152</u>
Total carrying amount	1,509,932	1,372,200
Less: prizes payable within one year	<u>173,231</u>	<u>156,451</u>
Long-term prizes payable	<u>\$ 1,336,701</u>	<u>1,215,749</u>

The amortized discount on the prizes payable is based on interest rates which range from 3.01% to 13.55% 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 revenue and expenses and amounted to \$117,314,000 and \$110,893,000 for fiscal years 1995 and 1994, respectively.

The aggregate amount of prizes payable due in each of the five fiscal years following March 31, 1995, and the total thereafter, is as follows (in thousands):

1996	\$ 179,685
1997	179,685
1998	180,000
1999	180,000
2000	180,000
Thereafter	<u>1,736,416</u>
	<u>\$ 2,635,786</u>

NEW YORK STATE LOTTERY

Notes to Financial Statements, Continued

(6) Operating Segment Information

Operating segment information for fiscal 1995 and 1994 by type of lottery game is as follows (in thousands):

		1995					
	Ticket Sales	Prizes	Agent Commissions	Contractor Fees	Instant Cash Game Ticket Expense	Gross Profit on Ticket Sales	
Lotto	\$ 839,375	(339,777)	(50,372)	(12,543)	-	436,683	
Take Five	334,232	(167,565)	(20,054)	(5,097)	-	141,516	
Pick 10	83,608	(41,917)	(5,017)	(1,275)	-	35,399	
New York Numbers	689,374	(345,614)	(41,362)	(10,513)	-	291,885	
Win-4	415,847	(208,482)	(24,951)	(6,342)	-	176,072	
Instant Cash Games	666,145	(367,275)	(39,969)	(29,178)	(7,915)	221,808	
City Games	4	(5)	-	-	-	(1)	
	<u>\$ 3,028,585</u>	<u>(1,470,635)</u>	<u>(181,725)</u>	<u>(64,948)</u>	<u>(7,915)</u>	<u>1,303,362</u>	
General and administrative expenses						(68,198)	
Nonoperating revenue						<u>8,653</u>	
Income earned and required allocation to education, net						<u>\$ 1,243,817</u>	

		1994					
	Ticket Sales	Prizes	Agent Commissions	Contractor Fees	Gross Profit on Ticket Sales		
Lotto	\$ 645,718	(259,694)	(38,744)	(9,453)	337,827		
Take Five	307,475	(123,333)	(18,448)	(4,775)	160,919		
Pick 10	84,420	(42,304)	(5,065)	(1,307)	35,744		
New York Numbers	658,141	(329,805)	(39,488)	(10,268)	278,580		
Win-4	374,322	(187,579)	(22,459)	(5,817)	158,467		
Instant Cash Games	298,478	(164,496)	(17,909)	(18,927)	97,146		
City Games	526	(265)	(32)	(32)	197		
	<u>\$ 2,369,080</u>	<u>(1,107,476)</u>	<u>(142,145)</u>	<u>(50,579)</u>	<u>1,068,880</u>		
General and administrative expenses						(64,001)	
Nonoperating revenue						<u>6,279</u>	
Income earned and required allocation to education, net						<u>\$ 1,011,158</u>	

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, 1995 and 1994, are as follows (in thousands):

	<u>1995</u>	<u>1994</u>
Revenue transferred to education	\$ 1,161,849	1,053,999
Prior year payable	<u>(25,914)</u>	<u>(68,755)</u>
Amount transferred from current year revenue	1,135,935	985,244
Current year payable	<u>107,882</u>	<u>25,914</u>
Income earned and required allocation to education, net	\$ <u>1,243,817</u>	<u>1,011,158</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, 1995, was approximately \$9,059,000; the Lottery's total payroll was approximately \$9,278,000.

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. 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, 1994 totaled approximately 805,049, including 270,902 retirees and beneficiaries currently receiving benefits and members no longer working and entitled to benefits but not yet receiving them; 47,662 nonvested inactive members, and 486,485 current working members.

The contribution requirement for the year ended March 31, 1995, was \$566,000, which consisted of \$376,000 from the Lottery and \$190,000 from employees; these contributions represented 4.1% and 2.0% of covered payroll, respectively. The contribution requirement for the year ended March 31, 1994, was \$428,872, which consisted of \$260,630 from the Lottery and \$168,242 from employees; these contributions represented 3.1% and 2.0% 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, 1994, for the System as a whole, determined through an actuarial valuation performed as of that date, was \$49,879,000,000. The System's net assets available for benefits on that date (valued at market) were \$50,835,000,000 resulting in assets in excess of pension benefit obligation of \$956,000,000. The Lottery's 1994 contribution represented .1% of total contributions required of all participating entities.

# NEW YORK STATE LOTTERY

## Notes to Financial Statements, Continued

Ten-year historical trend information showing the System's progress in accumulating sufficient assets to pay benefits when due and other significant factors are presented in the System's March 31, 1994 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 the 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.

(10) Postretirement Benefits

In addition to the pension benefits described in Note 8, the State provides health insurance coverage and survivor benefits for retired employees and their survivors. Substantially all of the State's employees may become eligible for these benefits if they reach normal retirement age while working for the State. Health care benefits are provided through an insurance company whose premiums are based on the benefits paid during the year. The state recognizes the cost of providing health insurance by recording its share of insurance premiums as an expenditure in the general fund in the year paid. Additionally, the survivor's benefit program provides for a death benefit to be paid by the State to a retiree's designated beneficiary. The Lottery is not directly charged for these benefits to its former employees.

(11) Commitments and Contingencies

(a) Contractual Arrangements

The Lottery maintains a gaming network of over 8,300 on-line locations where all games are sold and over 3,000 off-line locations which sell only instant cash game tickets. GTECH Corporation (GTECH) is responsible for operating the on-line games under a contract expiring on February 28, 1999. Instant cash game sales are supported by the services of four contractors:

- (1) Under a contract expiring January 31, 1997, Scientific Games, Inc. is responsible for maintaining validating devices installed at each sales location.
- (2) Under a contract expiring July 14, 1996, Dittler Brothers, Inc. is responsible for production of instant cash tickets.
- (3) Under a contract expiring January 13, 1997, GTECH is responsible for various services related to the warehousing, sales, distribution of, and accounting for, instant cash tickets.
- (4) Instant cash tickets are also sold through vending machines at approximately 1,000 locations. A contract with Lottery Enterprises, Inc., expiring on July 14, 1996, provides for maintenance of the vending machines.

NEW YORK STATE LOTTERY

Notes to Financial Statements (continued)

(b) Capital and Operating Leases

The Lottery has entered into certain capital lease obligations with the State of New York which are included in other payables. The leases require semi-annual payments approximating \$638,000, including interest of 6.60% and 5.11% (imputed interest remaining under these leases is approximately \$97,000 at March 31, 1995; \$245,000 at March 31, 1994). The leases expire in March 1996 and August 1998.

In addition the Lottery has entered into operating leases for equipment and building space. Rental expense was \$3,973,000 and \$1,904,000 in 1995 and 1994, respectively.

The following is a schedule of future minimum lease payments under noncancellable operating leases having initial or remaining terms in excess of one year as of March 31, 1995:

<u>Fiscal Year</u>	<u>Operating Leases</u>
1996	\$ 4,844,000
1997	4,373,000
1998	3,953,000
1999	3,939,000
2000	2,024,000
Thereafter	-
Total minimum lease payments	\$ <u>19,133,000</u>

(c) Insurance Contracts

Prior to 1983, the Lottery had entered into agreements with New York insurance companies under which the Lottery purchased contracts that provide payments corresponding to the Lottery's obligation to the prize winners. The types of contracts entered into include agreements that pay installments for a specific term (investment contracts) as well as agreements to make installment payments to prize winners over the winners' lifetime. Because it is the intent of the Lottery that the insurance companies make future installment payments directly to each prize winner, the present value of the future payments under these contracts are not 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 the investment contracts approximated \$73,000,000 at March 31, 1995, which have a fair value that approximates \$59,000,000. For contracts other than investment contracts, the insurance companies are making annual payments to approximately 65 individuals totaling approximately \$1,200,000 as of March 31, 1995.

(d) 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.



74 North Pearl Street  
Albany, NY 12207

Independent Auditors' Report  
on Other Financial Information

New York State Lottery

We have audited and reported separately herein on the financial statements of the New York State Lottery as of and for the year ended March 31, 1995.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements of the New York State Lottery taken as a whole. The following combining schedule of assets and liabilities and combining schedule of revenue and expenses is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

*KPMG Peat Marwick LLP*

May 26 1995

NEW YORK STATE LOTTERY

Combining Schedule of Assets and Liabilities

March 31, 1995  
(In Thousands)

<u>Assets</u>	<u>All Other Games</u>	<u>City Games</u>	<u>Eliminations</u>	<u>Combined Total</u>
Current assets:				
Cash and cash equivalents	\$ 157,618	39	-	157,657
Accounts receivable	108,748	-	(6,326)	102,422
Investments, at amortized cost	173,749	-	-	173,749
Instant game ticket inventory	4,565	-	-	4,565
Total current assets	<u>444,680</u>	<u>39</u>	<u>(6,326)</u>	<u>438,393</u>
Long-term investments, at amortized cost	1,320,572	-	-	1,320,572
Equipment and leasehold improvements, net of accumulated depreciation and amortization	<u>4,847</u>	<u>-</u>	<u>-</u>	<u>4,847</u>
Total assets	<u>\$ 1,770,099</u>	<u>39</u>	<u>(6,326)</u>	<u>1,763,812</u>
<u>Liabilities</u>				
Current liabilities:				
Prizes payable	173,231	-	-	173,231
Unclaimed and future prizes	110,089	39	-	110,128
Due to education	114,266	(6,384)	-	107,882
Due to administration	7,108	-	-	7,108
Deferred revenue	10,709	-	-	10,709
Hold harmless payable	-	6,326	(6,326)	-
Other payables	<u>17,995</u>	<u>58</u>	<u>-</u>	<u>18,053</u>
Total current liabilities	<u>433,398</u>	<u>39</u>	<u>(6,326)</u>	<u>427,111</u>
Long-term prizes payable	<u>1,336,701</u>	<u>-</u>	<u>-</u>	<u>1,336,701</u>
Total liabilities	<u>\$ 1,770,099</u>	<u>39</u>	<u>(6,326)</u>	<u>1,763,812</u>

NEW YORK STATE LOTTERY

Combining Schedule of Revenue and Expenses

March 31, 1995  
(In Thousands)

	All Other Games	City Games	Combined Total
Ticket sales	\$ 3,028,581	4	3,028,585
Less:			
Prizes	(1,470,630)	(5)	(1,470,635)
Agent commissions	(181,725)	-	(181,725)
Contractor fees	(64,948)	-	(64,948)
Instant Game ticket printing costs	(7,915)	-	(7,915)
Gross profit on ticket sales	<u>1,303,363</u>	<u>(1)</u>	<u>1,303,362</u>
General and administrative expenses	(68,198)	-	(68,198)
Income (loss) from operations	<u>1,235,165</u>	<u>(1)</u>	<u>1,235,164</u>
Nonoperating revenue (expenses):			
Interest income	121,874	3	121,877
Interest expense - amortization of discount on prizes payable	(117,314)	-	(117,314)
Hold harmless, City games	-	-	-
Other, net	4,090	-	4,090
Total nonoperating revenue	<u>8,650</u>	<u>3</u>	<u>8,653</u>
Income earned and required allocation to education, net	\$ <u>1,243,815</u>	<u>2</u>	<u>1,243,817</u>

Note: Hold harmless, City games represents the statutory shortfall in net revenue, as defined (see Note 1), based on the hold harmless calculation for the twelve-month period ended February 28, 1995.