



**NEW YORK STATE LOTTERY**

Basic Financial Statements

March 31, 2010 and 2009

(With Independent Auditors' Report Thereon)

**NEW YORK STATE LOTTERY**

Basic Financial Statements

March 31, 2010 and 2009

**Table of Contents**

	<b>Page</b>
Independent Auditors' Report	1
Management's Discussion and Analysis (Unaudited)	2
Statements of Net Assets	10
Statements of Revenue, Expenses, and Changes in Net Assets	11
Statements of Cash Flows	12
Notes to Basic Financial Statements	13



**KPMG LLP**  
515 Broadway  
Albany, NY 12207

## **Independent Auditors' Report**

New York State Lottery:

We have audited the accompanying statements of net assets of the New York State Lottery (Lottery) as of March 31, 2010 and 2009, and the related statements of revenue, expenses, and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Lottery's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Lottery's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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.

As discussed in note 1, the financial statements of the New York State Lottery are intended to present the financial position, and changes in financial position and cash flows, of only that portion of the financial reporting entity of the State of New York that is attributable to the transactions of the Lottery. They do not purport to, and do not, present fairly the financial position of the State of New York as of March 31, 2010 and 2009, the changes in financial position or its cash flows, where applicable, for the years then ended in conformity with U.S. generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net assets of the New York State Lottery as of March 31, 2010 and 2009, and changes in net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

The Management's Discussion and Analysis on pages 2 through 9 is not a required part of the basic financial statements but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

**KPMG LLP**

June 30, 2010

## NEW YORK STATE LOTTERY

### Management's Discussion and Analysis (Unaudited)

March 31, 2010 and 2009

The management of the New York State Lottery (New York Lottery or Lottery) offers readers the following general overview and analysis of the New York Lottery's financial position and activities for the fiscal year ending March 31, 2010 and 2009. We encourage readers to consider this information in conjunction with the detailed financial statements and explanatory notes that follow. The New York Lottery's basic financial statements for the fiscal years ending March 31, 2010 and 2009 have been prepared in accordance with U.S. generally accepted accounting principles.

#### Financial Highlights

- New York Lottery revenues totaled \$7.818 billion, the largest total ever for the Lottery, while net proceeds earned for Lottery Aid to Education reached \$2.666 billion for fiscal year 2010, also an all-time record.
- New York Lottery revenues in fiscal year 2010 surpassed the revenues of 2009 by \$158.2 million or 2.1%. In fiscal year 2009, the annual revenue increase was \$111.7 million or 1.5%.
- Net proceeds earned for Lottery Aid to Education in fiscal year 2010 were more than the net proceeds of 2009 by \$122.3 million or 4.8%. Comparatively, the annual earnings for education in fiscal year 2009 were less than 2008 by \$12.2 million or 0.5%.
- Prize expense decreased by \$52.0 million or 1.3% during fiscal year 2010. Prize expense increased by \$50.5 million or 1.3% during fiscal year 2009. Prize expense decreased in fiscal year 2010 due to a sales shift from higher payout instant games to draw games with lower prize payouts. Prize expense also declined due to transactions in the investment portfolio whereby the Lottery sold a significant portion of U.S. Treasury strip holdings and purchased similarly rated, higher-yielding municipal bonds. The resulting savings reduced prize expense during fiscal year 2010 since less cash was required to fulfill prize obligations.
- Operating income increased by \$172.1 million or 6.9% during fiscal year 2010. Operating income decreased by \$79.4 million or 3.1% during fiscal year 2009.
- Nonoperating income decreased by \$162.7 million during fiscal year 2010. This decrease follows a \$12.0 million decrease in fiscal year 2009. The decreases are primarily the result of a decline in unrealized gains on investments.
- Working Capital (current assets minus current liabilities) decreased to \$109.4 million at the end of fiscal year 2010. This was a decrease of \$26.4 million or 19.5% compared to fiscal year 2009, primarily due to reduced receivables on ticket sales. At the end of fiscal year 2009, working capital was \$135.8 million. This was a decrease of \$0.4 million or 0.3% compared to fiscal year 2008.

# NEW YORK STATE LOTTERY

## Management's Discussion and Analysis (Unaudited)

March 31, 2010 and 2009

### **Overview of Financial Statements**

The New York Lottery presents its financial statements using the accrual basis of accounting, which is comparable to the method used by many private sector businesses. The accrual basis recognizes revenues when earned, not when received. Likewise, expenses are recognized when incurred, not when paid. The Lottery prepares the following three financial statements for fiscal years 2010 and 2009:

#### *Statements of Net Assets*

The statement on page 10 provides information on the nature and amount of the Lottery's assets, liabilities and net assets at the close of fiscal years 2010 and 2009. The relationship of assets to liabilities and resulting net assets is one indicator of the financial condition of the Lottery and can also be a reflection of changes within the Lottery.

#### *Statements of Revenue, Expenses, and Changes in Net Assets*

The statement on page 11 reflects the Lottery's operating and nonoperating revenues and expenses and the change in net assets for the year.

#### *Statements of Cash Flows*

The comparative statement on page 12 is presented on the direct method of reporting and reflects cash flows from operating activities as well as capital and noncapital financing and investing activities. Cash collections and payments are reflected in this statement to arrive at the net increase or decrease in cash and cash equivalents for the year.

The above mentioned financial statements, the notes and this management discussion and analysis provide information about the Lottery's overall financial condition.

This management discussion and analysis is meant to be an introduction to the financial statements and to assist readers in understanding the results of the operation and the financial condition of the New York Lottery. The notes to the financial statements are an integral part of the statements and include additional data and explanations which are to be used in concert with the financial statements.

The New York Lottery deposits its net proceeds into six accounts held in joint custody by the Commissioner of Taxation and Finance and the State Comptroller. These six accounts and the purpose of the funds are as follows:

- Lottery Education Account – Accumulates the required deposits for Aid to Education from revenues, not including video gaming revenues.
- Prize Pending Account – Consists of Lottery prizes that have not yet been paid from revenues, excluding video gaming revenues.
- Administration Account – Utilized to pay for the Lottery's administrative costs that are not related to or funded by video gaming revenues.
- Video Gaming Education Account – Accumulates the required deposits for Aid to Education from video gaming operations.

## NEW YORK STATE LOTTERY

### Management's Discussion and Analysis (Unaudited)

March 31, 2010 and 2009

- Video Gaming Prize Pending Account – Consists of video gaming prizes awarded that have not yet been claimed.
- Video Gaming Administration Account – Utilized to pay the administrative costs of video gaming.

### Financial Analysis

#### *Summary of Net Assets*

The comparative summary of net assets represents the Lottery's financial position as of the fiscal years ended for 2010, 2009, and 2008 (in millions):

	FY 2010	FY 2009	FY 2008	FY 2010 vs. FY 2009		FY 2009 vs. FY 2008	
				Dollar change	Percent change	Dollar change	Percent change
Capital assets	\$ 4	7	11	(3)	(42.9)%	\$ (4)	(36.4)%
Other assets	2,064	2,098	2,081	(34)	(1.6)	17	0.8
Total assets	2,068	2,105	2,092	(37)	(1.8)	13	0.6
Current liabilities	631	586	637	45	7.7	(51)	(8.0)
Noncurrent liabilities	1,268	1,241	1,182	27	2.2	59	5.0
Total liabilities	1,899	1,827	1,819	72	3.9	8	0.4
Restricted net assets	79	72	110	7	9.7	(38)	(34.5)
Invested in capital assets, net	—	—	—	—	—	—	—
Unrestricted net assets	90	206	163	(116)	(56.3)	43	26.4
Total net assets	\$ 169	278	273	(109)	(39.2)	\$ 5	1.8

#### *Capital Assets*

Capital assets consist of equipment and leasehold improvements. During fiscal year 2010 and 2009, there were no significant changes in capital assets. Activity was primarily limited to yearly depreciation. Additional information about the Lottery's capital assets can be found in note 1h of the notes to the basic financial statements.

#### *Other Assets*

Other assets consist of cash and cash equivalents, accounts receivable, instant ticket inventory, and investments. During fiscal year 2010, other assets decreased by \$34.0 million which represented a change of (1.6)% from the previous year. This was in contrast to fiscal year 2009 when other assets increased by \$17.4 million, or 0.8%.

#### *Current Liabilities*

Current liabilities consist of prizes awarded in the past year that remain unclaimed, amounts due to education, accrued expenses, accounts payable, the value of Lottery tickets purchased in advance of game drawings (deferred ticket sales), and the short-term portion of long-term prizes payable, capitalized leases, and amounts due to employees for unused vacation leave. In total, these accounts increased by \$45.1 million during fiscal year 2010 due primarily to an increase in unclaimed prizes. These changes can be contrasted to the fiscal year ended

## NEW YORK STATE LOTTERY

### Management's Discussion and Analysis (Unaudited)

March 31, 2010 and 2009

March 31, 2009 when there was a \$50.3 million annual decrease in total current liabilities due in large part to payment of a \$32.8 million Lotto jackpot that had been outstanding at the close of the prior year.

#### *Noncurrent Liabilities*

Noncurrent liabilities consist of amounts due to be paid more than one year after the close of the fiscal year for installment prizes, unused employee vacation leave, and capitalized leases. During fiscal year 2010 and 2009, this category of liabilities increased by \$26.8 million and \$59.1 million respectively, with the increases occurring primarily in long-term prizes payable. The increases were caused mainly by the steady addition each year of new instant game top prize winners to be paid over an extended period of time and in some cases for the rest of their lives.

#### *Net Assets*

Restricted net assets for future prizes consist of prize funds that are in excess of prizes actually claimed at the fiscal year end, but which are necessary to ensure future prize payments. For example, prize funds from past sales are utilized to pay an accumulating or future New York Lotto, Powerball, or Mega Millions jackpot or contribute toward a created but unclaimed instant ticket prize. These amounts are available by statute for this purpose.

Net assets invested in capital assets are the amounts recorded as capital assets less the amounts of related debt. During fiscal years 2010, 2009, and 2008, capital assets were \$4.0 million, \$6.8 million and \$11.3 million, respectively, while related debt was \$3.9 million, \$6.9 million and \$11.4 million.

Unrestricted net assets listed on the statement of net assets are largely the cumulative result of increased fair market value of United States guaranteed marketable securities held by the Lottery to pay prize winners on an annuity basis. Since the full maturity value of the investments is needed to pay the annuity prizes, the Lottery does not expect to realize any permanent gain on these investments.

## NEW YORK STATE LOTTERY

### Management's Discussion and Analysis (Unaudited)

March 31, 2010 and 2009

#### *Summary of Revenue, Expenses, and Changes in Net Assets*

The following summary compares the Lottery's operating revenues, expenses and changes in net assets for the fiscal years 2010, 2009 and 2008 (in millions).

	FY 2010	FY 2009	FY 2008	FY 2010 vs. FY 2009		FY 2009 vs. FY 2008	
				Dollar change	Percent change	Dollar change	Percent change
Operating revenue:							
Lottery revenue, net	\$ 7,818	7,660	7,548	158	2.1%	\$ 112	1.5%
Operating expenses:							
Direct expenses	(5,013)	(5,030)	(4,838)	17	(0.3)	(192)	4.0
Indirect expenses	(133)	(130)	(131)	(3)	2.3	1	(0.8)
Total operating expenses	(5,146)	(5,160)	(4,969)	14	(0.3)	(191)	3.8
Operating income	2,672	2,500	2,579	172	6.9	(79)	(3.1)
Nonoperating income (expenses)							
Nonoperating income	(40)	124	175	(164)	(132.3)	(51)	(29.1)
Nonoperating expenses	(75)	(76)	(115)	1	(1.3)	39	(33.9)
Total nonoperating income (expenses)	(115)	48	60	(163)	(339.6)	(12)	(20.0)
Income before required allocation	2,557	2,548	2,639	9	0.4	(91)	(3.4)
Required allocation – contribution for aid to education	(2,666)	(2,544)	(2,556)	(122)	4.8	12	(0.5)
Change in net assets	\$ (109)	4	83	(113)	(2,825.0)	\$ (79)	(95.2)

#### *Revenues*

The New York Lottery exists for the sole purpose of raising revenue to help support Aid to Education. The Lottery achieves its mission through the sale of Lottery tickets at approximately 17,000 licensed retail locations across the state. The Lottery also achieves its mission through eight licensed video lottery gaming facilities located in Saratoga, Monticello, Farmington, Hamburg, Batavia, Tioga, Vernon, and Yonkers, New York.

During the fiscal year 2010, the Lottery achieved \$3.170 billion in draw sales, \$3.611 billion in instant sales, and \$1.037 billion in video lottery gaming net machine income for a total of \$7.818 billion, a 2.1% (\$158.2 million) increase over the previous fiscal year. This record year eclipses the record set the previous year when 2009 revenues reached \$7.660 billion, a \$111.7 million or 1.5% increase. Significant growth was generated in video gaming during both fiscal years and in draw games during 2010.

## NEW YORK STATE LOTTERY

### Management's Discussion and Analysis (Unaudited)

March 31, 2010 and 2009

The following compares the Lottery's revenues by game and the percentage of total revenues by game for the fiscal years 2010, 2009, and 2008 (in millions).

Game	FY 2010		FY 2009		FY 2008	
	Revenue	Percent of total revenues	Revenue	Percent of total revenues	Revenue	Percent of total revenues
Mega Millions	\$ 558	7.1%	\$ 467	6.1%	\$ 482	6.4%
Lotto	178	2.3	178	2.3	208	2.8
Take 5	306	3.9	329	4.3	320	4.2
Numbers	846	10.8	850	11.1	857	11.4
Win 4	766	9.8	740	9.7	718	9.5
Quick Draw	412	5.3	425	5.5	444	5.9
Pick 10	32	0.4	32	0.4	32	0.4
Promotion Raffle Game	—	—	8	0.1	18	0.2
Sweet Million	36	0.5	—	—	—	—
Powerball	36	0.5	—	—	—	—
Instant	3,611	46.1	3,666	47.9	3,594	47.6
Subtotal traditional lottery	6,781	86.7	6,695	87.4	6,673	88.4
Video Gaming, net *	1,037	13.3	965	12.6	875	11.6
Total revenues	\$ 7,818	100.0%	\$ 7,660	100.0%	\$ 7,548	100.0%

\* Video gaming revenue represents net machine income after awarding prizes. Video gaming credits played and won were as follows:

	FY 2010	FY 2009	FY 2008
Credits played	\$ 12,328	11,664	10,683
Credits won	(11,291)	(10,699)	(9,808)
Net machine income	\$ 1,037	965	875

### **Direct Expenses**

Direct expenses consist of prize expense for traditional Lottery games, commissions to Lottery retailers and video lottery gaming facilities, fees to gaming contractors, expenses of providing instant tickets to players, and telecommunications. The largest expenditure in this category is prize expense which made up roughly 80% of direct expenses during each of the three years being discussed. This expense decreased by \$52.0 million to \$3.951 billion in fiscal year 2010. At the same time, traditional retailer commissions increased by \$5.2 million to \$405.9 million and gaming contractor fees increased by \$7.1 million to \$133.6 million. Video lottery gaming commissions to facilities increased by \$30.9 million to \$469.5 million.

During fiscal year 2009, prize expense increased by \$50.5 million to \$4.003 billion, traditional retailer commissions decreased by \$0.1 million to \$400.7 million, and gaming contractor fees increased by \$5.6 million to \$126.5 million. As a result of legislated changes to net video gaming revenue allocation, commissions to video lottery gaming facilities reached \$438.7 million, an increase of \$130.9 million, which was the majority of the increase in direct expenses.

### **Other Operating Expenses**

Other operating expenses include marketing, state agency charges, personal services, fringe benefits and other administrative costs. These costs were \$132.8 million during fiscal year 2010 which was 2.1% higher than

## NEW YORK STATE LOTTERY

### Management's Discussion and Analysis (Unaudited)

March 31, 2010 and 2009

\$130.2 million in the prior year. By contrast, fiscal year 2009 had remained relatively unchanged from the \$130.7 million for these costs in 2008.

#### ***Nonoperating Revenues (Expenses)***

Nonoperating revenues and expenses consist of miscellaneous income plus the net growth or decline in the fair market value of investments used to fund long-term prizes. Investment income of \$(40.0) million in 2010, \$123.9 million in 2009 and \$175.0 million in 2008 consists of both the fair value adjustments of investments plus the normal growth of the value of Lottery investments as the securities move closer to maturity. The market driven, fair value adjustment is the primary factor in the fluctuation in this amount from year to year. Investment expense is a reflection of the Lottery expending the investment income to increase the valuation of the long-term prizes payable to winners. The annual fair value adjustment of investments (shown here as income) flows to the unrestricted net assets balance on the statement of net assets.

#### ***Income Before Required Allocation and Change in Net Assets***

The revenues and expenses for fiscal year 2010 resulted in income before required allocation totaling \$2.558 billion. This amount consists of a required allocation for Aid to Education of \$2.666 billion that transfers out as a contribution for Aid to Education and a \$108.7 million decrease in net assets for the year. The \$108.7 million decrease in net assets is a combination of a \$7.1 million increase in net assets restricted for prizes, a \$0.2 million increase in net assets invested in capital assets, and a \$116.0 million decrease in unrestricted net assets. The revenues and expenses for fiscal year 2009 resulted in income before required allocation totaling \$2.548 billion. This amount consists of a required allocation for Aid to Education of \$2.544 billion that transfers out as a contribution for Aid to Education and a \$4.2 million increase in net assets for the year. The \$4.2 million increase in net assets is a combination of a \$38.0 million decrease in net assets restricted for prizes, a \$0.1 million increase in net assets invested in capital assets, and a \$42.1 million increase in unrestricted net assets.

#### **Summary and Outlook**

The revenues reported here include those from eight video lottery gaming facilities. One more facility is expected to open in Queens, NY, at the Aqueduct Racetrack but the date of its opening has yet to be determined. During fiscal year 2010, the Lottery began offering two more draw games; Sweet Million held its first drawing in September 2009 and Powerball held its first drawing in February 2010. Their sales in fiscal year 2010 were limited by the portion of the year when they were available but in future periods they will be producing sales during the entire year.

## **NEW YORK STATE LOTTERY**

Management's Discussion and Analysis (Unaudited)

March 31, 2010 and 2009

### **Contacting New York Lottery's Financial Management**

This financial report is designed to provide the State of New York, the public, and other interested parties with an overview of the financial results of the New York State Lottery and an explanation of the Lottery's financial condition. If you have any questions about this report or require additional information, email [Questions@Lottery.state.ny.us](mailto:Questions@Lottery.state.ny.us) or write to The New York Lottery Communications Office, One Broadway Center, P.O. Box 7500, Schenectady, NY 12301-7500.

## NEW YORK STATE LOTTERY

### Statements of Net Assets

March 31, 2010 and 2009

(In thousands)

<b>Assets</b>	<b>2010</b>	<b>2009</b>
Current assets:		
Cash and cash equivalents	\$ 153,220	43,947
Accounts receivable	417,233	480,213
Instant ticket inventory	9,796	12,430
Investments	160,852	185,859
Total current assets	741,101	722,449
Noncurrent assets:		
Long-term investments, net	1,323,051	1,375,670
Capital assets	3,967	6,818
Total noncurrent assets	1,327,018	1,382,488
Total assets	2,068,119	2,104,937
<b>Liabilities</b>		
Current liabilities:		
Prizes payable	\$ 183,472	184,703
Unclaimed prizes	281,482	189,248
Due to education	139,385	175,714
Accounts payable and accrued liabilities	12,800	20,718
Capital lease obligations	2,062	2,673
Deferred ticket sales	11,239	12,301
Compensated absences	1,284	1,283
Total current liabilities	631,724	586,640
Noncurrent liabilities:		
Compensated absences	562	305
Long-term capital lease obligations	1,810	4,222
Long-term prizes payable	1,265,176	1,236,198
Total noncurrent liabilities	1,267,548	1,240,725
Total liabilities	1,899,272	1,827,365
<b>Net Assets</b>		
Restricted for future prizes	79,119	72,026
Invested in capital assets, net of related debt	95	(77)
Unrestricted	89,633	205,623
Total net assets	\$ 168,847	277,572

See accompanying notes to basic financial statements.

## NEW YORK STATE LOTTERY

### Statements of Revenue, Expenses, and Changes in Net Assets

Years ended March 31, 2010 and 2009

(In thousands)

	<b>2010</b>	<b>2009</b>
Operating revenue:		
Lottery revenue, net	\$ 7,818,316	7,660,145
Operating expenses:		
Prize expense	(3,951,226)	(4,003,267)
Retailer commissions	(875,430)	(839,312)
Gaming contractor fees	(133,587)	(126,479)
Instant ticket direct expenses	(28,575)	(32,755)
Telecommunications	(24,485)	(28,109)
Total direct expenses	(5,013,303)	(5,029,922)
Online games/jackpot marketing	(49,443)	(39,758)
Personal service and fringe benefits	(30,663)	(31,227)
Instant games marketing	(25,988)	(27,676)
All games marketing	(10,983)	(13,513)
Other administrative costs	(11,362)	(11,678)
State agency charges	(1,540)	(1,710)
Depreciation	(2,851)	(4,599)
Total indirect expenses	(132,830)	(130,161)
Total operating expenses	(5,146,133)	(5,160,083)
Operating income	2,672,183	2,500,062
Nonoperating revenue (expenses):		
Investment income	(40,024)	123,909
Other expense, net	(298)	(271)
Investment expense, net	(74,205)	(75,512)
Total nonoperating revenue	(114,527)	48,126
Income before required allocation	2,557,656	2,548,188
Required allocation for aid to education	(2,666,381)	(2,543,950)
Change in net assets	(108,725)	4,238
Net assets beginning of year	277,572	273,334
Net assets end of year	\$ 168,847	277,572

See accompanying notes to basic financial statements.

**NEW YORK STATE LOTTERY**  
Statements of Cash Flows  
Years ended March 31, 2010 and 2009  
(In thousands)

	<u>2010</u>	<u>2009</u>
Operating activities:		
Cash received from net lottery revenue	\$ 7,880,043	7,650,432
Cash payments for prizes	(3,903,871)	(4,056,857)
Cash payments for commissions	(875,410)	(839,184)
Cash payments for contractor fees	(133,112)	(126,947)
Cash payments for telecommunications	(24,485)	(28,109)
Cash payments for instant ticket direct expenses	(24,262)	(36,426)
Cash payments for other operating expenses	(139,648)	(130,743)
Net cash provided by operating activities	<u>2,779,255</u>	<u>2,432,166</u>
Investing activities:		
Proceeds from investment maturities	186,244	189,451
Purchases of investments	(554,937)	(140,099)
Interest on cash and cash equivalents	1,430	4,318
Net proceeds from swaps of investment securities	—	1,683
Net proceeds from sales of investment securities	403,312	—
Net cash provided by investing activities	<u>36,049</u>	<u>55,353</u>
Noncapital financing activities:		
Cash transfer to State for Aid to Education	(2,825,995)	(2,954,095)
Cash received from State General Fund for Lottery Aid Guarantee	123,285	410,124
Other cash payments	(298)	(271)
Net cash used by noncapital financing activities	<u>(2,703,008)</u>	<u>(2,544,242)</u>
Capital financing activities:		
Cash payments for equipment and capital leases	(3,023)	(4,691)
Net cash used by capital financing activities	<u>(3,023)</u>	<u>(4,691)</u>
Net increase (decrease) in cash and cash equivalents	109,273	(61,414)
Cash and cash equivalents, beginning of year	43,947	105,361
Cash and cash equivalents, end of year	\$ <u>153,220</u>	<u>43,947</u>
Reconciliation of operating income to cash provided by operating activities:		
Operating income	\$ 2,672,183	2,500,062
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	2,851	4,599
Change in operating assets and liabilities:		
(Increase) decrease in accounts receivable, net	64,533	(7,846)
(Increase) decrease in ticket inventory	2,634	(2,441)
Decrease in prizes payable	(46,458)	(18,886)
Increase (decrease) in unclaimed prizes	92,234	(34,730)
Increase in compensated absences	258	81
Decrease in accounts payable and accrued liabilities	(7,918)	(6,286)
Decrease in deferred ticket sales	(1,062)	(2,387)
Net cash provided by operating activities	<u>\$ 2,779,255</u>	<u>2,432,166</u>
Noncash investing activities:		
Increase (decrease) in unrealized gains on investments	\$ (130,954)	42,220
Amortization of investment discount	72,811	75,688

See accompanying notes to basic financial statements.

# NEW YORK STATE LOTTERY

## Notes to Basic Financial Statements

March 31, 2010 and 2009

### (1) Summary of Significant Accounting Policies

The New York State Lottery (Lottery) was established in 1967. The Lottery is currently administered by the Division of the Lottery, an independent unit of the New York State Department of Taxation and Finance, which 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.

These financial statements present only the Lottery and do not present the financial position of the State nor changes in the State's financial position and cash flows. However, the Lottery is included in the State of New York's Basic Financial Statements as an enterprise fund.

The Lottery prepares its financial statements under the economic resources measurement focus whereby all inflows, outflows and balances affecting net assets are reported, and uses the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized when incurred. The primary operating revenue of the Lottery is ticket sales from games. Nonoperating income consists mostly of investment income and unrealized gains on investments. Operating expenses consist of direct expenses for prizes, commissions to Lottery retailers, fees to gaming contractors, expenses for providing instant tickets to players, and telecommunications. Other operating expenses that are indirect to the results of each game include marketing, state agency charges, personal services, and fringe benefits. Nonoperating expense includes the amortization of the discount on long-term prizes payable. The Lottery applies all applicable Governmental Accounting Standards Board (GASB) pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements: Statements and Interpretations of the Financial Accounting Standards Board (FASB), Accounting Principles Board (APB) Opinions, and Accounting Research Bulletins (ARB's) of the Committee on Accounting Procedure. The Lottery has elected the option, under GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Government Entities that Use Proprietary Funds*, not to apply all FASB Statements and Interpretations issued after November 30, 1989.

The more significant accounting policies of the Lottery are described below:

#### (a) Revenue Recognition

##### (i) Draw Games

Revenue from ticket sales for Lotto, Sweet Million, Quick Draw, Take 5, Pick 10, Mega Millions, PowerBall, Numbers and Win-4 games, and promotional games (draw games) is recognized when the related drawing takes place. Receipts from subscription sales and other ticket sales for future drawings are recorded as deferred revenue and recognized when the related drawings take place.

##### (ii) Instant Games

Revenue from Instant 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 retailer locations.

## NEW YORK STATE LOTTERY

### Notes to Basic Financial Statements

March 31, 2010 and 2009

#### (iii) Video Gaming

Revenue from video lottery gaming is recognized based on net machine income, which is defined as amounts played less prizes won.

#### (b) Commissions and Fees

Retailers selling draw and Instant Game tickets receive a commission of 6% based on the total tickets sold. For video gaming facilities receive a varying percent of incremental annual net machine income according to provisions of Section 1612 of the Tax Law. The particular percent applied to a range of net machine income can vary depending on the facility's number of video gaming machines, geographical area of the state, population level, or proximity to Native American gaming facilities. The draw game contractor and the video gaming central processing contractor receive fees equal to a contractual percentage of the sales generated through the network maintained by the respective contractor. The instant game contractor is paid a fee equal to a contractual percentage of instant sales. Video lottery terminal contractors receive a fee equal to a contractual percentage of revenue, adjusted for the units of service provided. All other gaming contractors are paid fees based on the units of service provided (see note 13).

#### (c) Accounts Receivable

Accounts receivable represents amounts due from retailers through a Lottery gaming contractor and amounts due from video lottery gaming facilities, net of commissions and fees, as well as amounts due from agents for Instant Game tickets which have been activated, but not yet settled. Instant ticket settlements occur within 45 days after a book of tickets is activated. Video lottery gaming receivables are received two business days after each sales day and draw games are collected within four business days after the close of each sales week.

#### (d) 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 for educational purposes to be at least 20% for the New York State Lottery Instant Games, 35% for Take 5, Numbers, Win-4, Mega Millions, Powerball, and Pick 10, 45% for Lotto, Sweet Million, and promotional games, and 25% for Quick Draw. In addition, the Lottery has legislative authority to issue up to three Instant Games per year with at least 10% for educational purposes. For video lottery, the required allocation to education is a varying percent of each facility's annual incremental net machine income, depending on factors such as the facility's number of video gaming machines, geographical area of the state, population level, and proximity to Native American gaming facilities.

## NEW YORK STATE LOTTERY

### Notes to Basic Financial Statements

March 31, 2010 and 2009

- Allocations of ticket sales revenue for the payment of lottery prizes are not to exceed 65% for the New York State Lottery Instant Games, 50% for Take 5, New York's Numbers, Win-4, Mega Millions, Powerball, and Pick 10, 40% for Lotto, Sweet Million, and promotional games, and 60% for Quick Draw. In addition, the Lottery has legislative authority to issue up to three Instant Games per year with up to 75% allocated to prizes. Video lottery is required to pay prizes that average no less than 90% of gross sales.
- Allocations of ticket sales revenue from all traditional games for the payment of Lottery administrative expenses (including agent commissions and contractor fees) are not to exceed 15%. For video lottery, 10% of net revenue (the total revenue wagered after payout for prizes) is allocated for Lottery Administration. Unlike traditional games, video lottery administrative expenses do not include commissions and fees which are described separately in note 1b. Any excess of the maximum allocation over actual administrative expenses is allocated to education. Such allocations amounted to approximately \$395,540,000 and \$382,605,000 for fiscal years 2010 and 2009, respectively. Administrative expenses incurred by the Lottery represent telecommunications, advertising, salary and other operating costs.

**(e) Cash and 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 Commissioner of Taxation and Finance and the 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.

**(f) Investments**

Investments, consisting of U.S. Government-backed obligations (zero coupon bonds and stripped Government securities) and New York City municipal bonds, are carried at fair value. Investment income represents accretion of bond discount, interest on bonds and deposits, and the change in fair value of investments.

**(g) Inventory**

Instant Game tickets are purchased from printing vendors. Tickets not activated for sale are held in inventory and are valued at cost by game. Tickets are charged to instant ticket direct expense under the first-in, first-out (FIFO) accounting method when activated for sale by the lottery retailers. At the conclusion of an Instant Game, unused inventory is charged to instant ticket direct expense.

**NEW YORK STATE LOTTERY**

Notes to Basic Financial Statements

March 31, 2010 and 2009

**(h) Capital Assets**

Capital assets consist of equipment and leasehold improvements which are carried at historical cost. Equipment is capitalized when it has cost in excess of \$40,000 and a useful life of two years or more. Leasehold improvements are capitalized when they have a cost of \$100,000 or more. Depreciation of equipment is computed using the straight-line method over five years, the estimated useful lives of the assets. 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. Changes in capital assets and related accumulated depreciation are shown below, by major class of asset, for the years ended March 31, 2010 and 2009 (in thousands).

	<u>2008</u>	<u>Additions</u>	<u>Deletions</u>	<u>2009</u>	<u>Additions</u>	<u>Deletions</u>	<u>2010</u>
Leasehold improvements:							
Cost	\$ 4,526	—	—	4,526	—	—	4,526
Accumulated depreciation	(4,526)	—	—	(4,526)	—	—	(4,526)
Net value	—	—	—	—	—	—	—
Equipment:							
Cost	25,858	160	—	26,018	—	—	26,018
Accumulated depreciation	(14,601)	(4,599)	—	(19,200)	(2,851)	—	(22,051)
Net value	11,257	(4,439)	—	6,818	(2,851)	—	3,967
Total	\$ 11,257	(4,439)	—	6,818	(2,851)	—	3,967

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 other revenues, net in the period of disposal.

**(i) Prizes Payable**

Lotto, Powerball, and Mega Millions jackpot players have the option at the time of ticket purchase of selecting a lump sum payment or a long-term annuity payment. Some Instant Games also have jackpot prizes that are long-term annuity payments. Prizes payable represents the liability for those prizes which are payable in annual installments. Such prize payments are funded by the Lottery's investments. The amortization of the long-term annuity payment discount is recorded as investment expense in these financial statements. Any excess of investment maturities over related annuity prize payments are recorded in restricted net assets and made available for future prizes.

**(j) Unclaimed Prizes**

Unclaimed prizes at March 31, 2010 and 2009 were \$281,482,000 and \$189,248,000, respectively. Prizes unclaimed for one year after the drawing date (lapsed) are forfeited by the ticket holder. Total prizes lapsed amounted to approximately \$46,160,000 and \$41,727,000 for fiscal years 2010 and 2009, respectively. These forfeited prizes are netted against prize expense in the statement of Revenues, Expenses, and Changes in Net Assets.

## NEW YORK STATE LOTTERY

### Notes to Basic Financial Statements

March 31, 2010 and 2009

Under the State Tax Law, the Lottery retains forfeited prizes for supplemental prizes in subsequent lottery games. During the fiscal years 2010 and 2009, these supplemental prizes were used for Lotto, Quick Draw, Take 5, promotional games, and various Instant Games.

**(k) *Restricted Net Assets***

Restricted net assets for prizes includes forfeited prizes and other prize assets that are restricted under State Tax Law Sections 1612 and 1614 for the purpose of meeting future prize expense.

**(l) *Use of Estimates***

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported and disclosed in the financial statements and related notes. Actual results could differ from those estimates.

**(2) *Cash and Cash Equivalents***

Lottery deposits of cash and cash equivalents are made in accordance with State Finance Law Sections 92c and 98a and State Tax Law Sections 1611 and 1612. Lottery sales receipts are allocated and deposited in separate fund accounts for prizes, education, and administration under the joint custody of the Commissioner of Taxation and Finance and the Comptroller of the State of New York. Per Section 98a of the State Finance Law, the accounts for prizes and administration earn interest through participation in a short-term investment pool administered by the Office of the State Comptroller of the State of New York. The prize account interest is used for future lottery prizes. The carrying amount of the accounts included in cash and cash equivalents were \$153,645,000 and \$48,696,000 at March 31, 2010 and 2009, respectively.

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, 2010 and 2009, the amount of accounts included in cash and cash equivalents related to the sole custody accounts were \$(425,000) and \$(4,749,000), respectively.

The Lottery's deposits are collateralized under a program administered by the Office of the State Comptroller of the State of New York. To manage custodial credit risk, 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 Lottery manages custodial credit risk by using several financial institutions and by minimizing balances in the sole custody accounts.

**(3) *Investments***

The Lottery is authorized by the Office of the State Comptroller per State statute to invest prize funds which will provide for the payment of prizes payable (see note 4). The Lottery invests these funds in U.S. Government-backed obligations and New York City municipal bonds, and Agency for International Development Bonds which are guaranteed by the full faith and credit of the United States. The fair value of these investments at March 31, 2010 and 2009 was \$1,483,903,000 and \$1,561,529,000, respectively. During fiscal years 2010 and 2009, approximately \$72,811,000 and \$75,688,000, respectively, of amortized discount was included in investment income.

**NEW YORK STATE LOTTERY**

Notes to Basic Financial Statements

March 31, 2010 and 2009

The amortized costs of these investments consisted of the following at March 31 (in thousands):

	<u>2010</u>	<u>2009</u>
Maturity value	\$ 1,860,316	2,088,715
Unamortized discount	<u>(451,005)</u>	<u>(732,732)</u>
Total at amortized cost	1,409,311	1,355,983
Less investments, maturing within one year, at amortized cost	<u>156,585</u>	<u>177,508</u>
Long-term investments, at amortized cost	\$ <u><u>1,252,726</u></u>	<u><u>1,178,475</u></u>

Proceeds of the investments in each of the five fiscal years following March 31, 2010, and five year incremental totals thereafter, are as follows (in thousands):

	<u>Maturities</u>	<u>Interest due</u>	<u>Total</u>
2011	\$ 161,364	18,187	179,551
2012	145,956	19,962	165,918
2013	130,619	19,854	150,473
2014	119,020	19,647	138,667
2015	108,041	19,363	127,404
2016 – 2020	404,383	93,183	497,566
2021 – 2025	362,655	73,663	436,318
2026 – 2030	149,426	50,870	200,296
2031 – 2035	78,572	39,390	117,962
2036 – 2040	<u>200,280</u>	<u>19,771</u>	<u>220,051</u>
	\$ <u><u>1,860,316</u></u>	<u><u>373,890</u></u>	<u><u>2,234,206</u></u>

The Lottery periodically enters into certain transactions whereby government securities are exchanged, through sales and purchases, for other government securities with substantially identical terms and characteristics. During 2010, no such transactions took place, however a change in investment policy resulted in the sale and purchase of certain securities of dissimilar terms and characteristics. During fiscal year 2009, the face value of the securities swapped amounted to \$51,481,000 resulting in gains of approximately \$1,683,000. The gains were included in investment income in the statements of revenue, expenses, and changes in net assets.

Credit risk is the risk that an issuer will not fulfill its obligations. The Lottery's policy is to follow State law which limits the investments that the Lottery can make and generally limit the Lottery's exposure to credit risk. The Lottery has generally limited its investments to obligations backed by the full faith of the U.S. Government. Beginning in 2010, the Lottery invested in similarly rated New York City Municipal bonds. The current credit ratings of the Lottery's investments as published by Standard & Poors are included on the next page.

**NEW YORK STATE LOTTERY**

Notes to Basic Financial Statements

March 31, 2010 and 2009

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Lottery's policy for managing this risk is to hold investment securities to maturity, at which time the fair value of the investment is equal to its stated maturity value.

As of March 31, 2010 and 2009, the Lottery had the following investments and maturities (amounts in thousands):

		<b>2010</b>			
		<b>Investment maturities</b>			
<b>Investment type</b>	<b>2010 Fair value</b>	<b>Credit rating</b>	<b>Less than five years</b>	<b>5 years to 10 years</b>	<b>More than 10 years</b>
U.S. Treasury Strips	\$ 422,157	AAA	\$ 196,723	137,033	302,996
New York City Municipal Bonds	393,103	AAA	29,955	61,360	303,685
Agency for International Development Bonds	<u>668,643</u>	AAA	<u>438,322</u>	<u>205,990</u>	<u>184,252</u>
Total	<u>\$ 1,483,903</u>		<u>\$ 665,000</u>	<u>404,383</u>	<u>790,933</u>
		<b>2009</b>			
		<b>Investment maturities</b>			
<b>Investment type</b>	<b>2009 Fair value</b>	<b>Credit rating</b>	<b>Less than five years</b>	<b>5 years to 10 years</b>	<b>More than 10 years</b>
U.S. Treasury Strips	\$ 778,987	AAA	\$ 282,269	203,752	662,115
Agency for International Development Bonds	<u>782,542</u>	AAA	<u>475,201</u>	<u>247,026</u>	<u>218,352</u>
Total	<u>\$ 1,561,529</u>		<u>\$ 757,470</u>	<u>450,778</u>	<u>880,467</u>

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to perform on a transaction, the Lottery will not be able to recover the value of investment securities that are in the possession of an outside party. In order to manage this risk, all of the Lottery's investments are insured or registered securities held by the Lottery or its agent in the Lottery's name.

**NEW YORK STATE LOTTERY**

Notes to Basic Financial Statements

March 31, 2010 and 2009

**(4) Prizes Payable**

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

		<u>2010</u>	<u>2009</u>
Total obligation	\$	2,316,901	2,153,007
Unamortized discount		<u>(868,253)</u>	<u>(732,106)</u>
Total carrying amount		1,448,648	1,420,901
Less prizes payable within one year		<u>183,472</u>	<u>184,703</u>
Long-term prizes payable	\$	<u><u>1,265,176</u></u>	<u><u>1,236,198</u></u>

The amortized discount on the prizes payable is based on interest rates which range from 0.18% to 9.40% and reflect the interest rates earned by the investments held to fund the related liabilities. The amortization of discount is recorded as investment expense in the statements of revenues, expenses, and changes in net assets and amounted to \$74,205,000 and \$75,512,000 for fiscal years 2010 and 2009, respectively.

The aggregate amount of prizes payable due in each of the five fiscal years following March 31, 2010, and the five year incremental totals thereafter, is as follows (in thousands):

2011	\$	183,544
2012		165,890
2013		153,375
2014		140,624
2015		128,243
2016 – 2020		504,768
2021 – 2025		434,590
2026 – 2030		232,651
2031 – 2035		129,532
Thereafter		<u>243,684</u>
	\$	<u><u>2,316,901</u></u>

**(5) Long-Term Liabilities**

The Lottery's long-term liabilities, as of March 31, 2010 and 2009 are comprised of the following, (in thousands):

	<u>Balance at March 31, 2009</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance at March 31, 2010</u>	<u>Current portion</u>
Capital lease obligations (note 12) \$	6,895	—	(3,023)	3,872	2,062
Compensated absences (note 11)	1,588	1,362	(1,104)	1,846	1,284
Prizes payable (note 4)	1,420,901	213,195	(185,448)	1,448,648	183,472

**NEW YORK STATE LOTTERY**

Notes to Basic Financial Statements

March 31, 2010 and 2009

	<u>Balance at March 31, 2008</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance at March 31, 2009</u>	<u>Current portion</u>
Capital lease obligations (note 12) \$	11,426	—	(4,531)	6,895	2,673
Compensated absences (note 11)	1,507	1,299	(1,218)	1,588	1,283
Prizes payable (note 4)	1,364,275	249,300	(192,674)	1,420,901	184,703

**(6) Aid to Education**

The required allocation and contribution transferred out for aid to education during the fiscal years ended March 31, 2010 and 2009, are as follows (in thousands):

	<u>2010</u>	<u>2009</u>
Cash transferred to education	\$ 2,825,995	2,954,095
Amount received from the State General Fund for Lottery Aid Guarantee	(123,285)	(410,124)
Net cash transferred to education	2,702,710	2,543,971
Prior year payable	(175,714)	(175,735)
Current year payable	139,385	175,714
Required allocation to education	\$ <u>2,666,381</u>	<u>2,543,950</u>

**(7) Pension Benefits**

Substantially all employees of the Lottery are members of the State and Local Employees' Retirement System (ERS) and the Public Employees' Group Life Insurance Plan (GLIP). The two programs are part of the State and Local Retirement System (System) which is a cost-sharing, multiple employer public employee retirement system. The Comptroller of the State of New York is sole trustee and administrative head of the System. The System issues a publicly available financial report that includes financial statements and required supplementary information which may be obtained by writing to New York State and Local Employees' Retirement Systems, 110 State Street, Albany, New York 12244.

The System provides retirement benefits as well as death and disability benefits. All benefits vest after five years of accredited service. Retirement benefits are established by the New York State Retirement and Social Security Law. Retirement benefits and contributory requirements depend upon the point in time 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; the Lottery contributes the entire amount determined to be payable to the System. Personnel who joined the System after July 27, 1976 are required by law to contribute 3% of their gross salary for their first ten years of employment; the Lottery withholds and contributes the balance payable to the System for these employees.

The Lottery paid to the Office of the State Comptroller of the State of New York \$1,861,000 for 2010, \$2,112,000 for 2009 and \$1,996,000 for 2008, to cover required employer contributions for retirement benefits and equaled 100% of the required contribution in each of the respective years. These payments made represent 8.82%, 10.50% and 10.84%, of covered payroll for each of the years, respectively.

**NEW YORK STATE LOTTERY**

Notes to Basic Financial Statements

March 31, 2010 and 2009

**(8) Operating Income**

Composition of operating income for fiscal 2010 and 2009 by type of lottery game is as follows (in thousands):

	<b>2010</b>					<b>Net</b>
	<b>Expenses</b>					
	<b>Revenue</b>	<b>Prizes**</b>	<b>Commissions</b>	<b>Fees</b>	<b>Instant direct expense</b>	
Mega Millions	\$ 558,167	(270,780)	(33,290)	(6,978)	—	247,119
Lotto	178,239	(73,291)	(9,897)	(2,056)	—	92,995
Take 5	306,332	(151,407)	(18,380)	(3,822)	—	132,723
Pick 10	32,234	(15,431)	(1,934)	(402)	—	14,467
Numbers	845,401	(410,194)	(50,724)	(10,513)	—	373,970
Win 4	765,848	(374,927)	(45,951)	(9,532)	—	335,438
Promotion Raffle Game	—	401	—	—	—	401
Sweet Million	35,583	(15,636)	(2,135)	(438)	—	17,374
Powerball	36,320	(14,638)	(2,179)	(366)	—	19,137
Instants	3,611,046	(2,369,845)	(216,664)	(27,505)	(28,575)	968,457
Quick Draw	411,898	(256,266)	(24,714)	(5,117)	—	125,801
Total traditional lottery	6,781,068	(3,952,014)	(405,868)	(66,729)	(28,575)	2,327,882
Video gaming	1,037,248*	788	(469,562)	(66,858)	—	501,616
	<u>\$ 7,818,316</u>	<u>(3,951,226)</u>	<u>(875,430)</u>	<u>(133,587)</u>	<u>(28,575)</u>	2,829,498
Telecommunications						(24,485)
Other operating expenses						(132,830)
Total operating income						<u>\$ 2,672,183</u>

\* Video gaming revenue represents net machine income after awarding prizes. Video gaming credits played and won were as follows:

Credits played	\$ 12,328,314
Credits won	<u>(11,291,066)</u>
Net machine income	<u>\$ 1,037,248</u>

\*\* Prizes unclaimed after one year are forfeited and are netted against prizes.

**NEW YORK STATE LOTTERY**

Notes to Basic Financial Statements

March 31, 2010 and 2009

2009						
Expenses						
	Revenue	Prizes**	Commissions	Fees	Instant direct expense	Net
Mega Millions	\$ 467,141	(227,948)	(27,835)	(5,961)	—	205,397
Lotto	178,075	(79,624)	(9,824)	(2,098)	—	86,529
Take 5	328,431	(163,080)	(19,706)	(4,220)	—	141,425
Pick 10	32,033	(15,290)	(1,922)	(412)	—	14,409
Numbers	850,331	(402,293)	(51,020)	(10,927)	—	386,091
Win 4	740,163	(388,478)	(44,410)	(9,511)	—	297,764
Promotion Raffle Game	8,388	(8,132)	(503)	(108)	—	(355)
Instants	3,666,087	(2,459,439)	(219,974)	(27,386)	(32,755)	926,533
Quick Draw	424,422	(259,496)	(25,465)	(5,454)	—	134,007
Total traditional lottery	6,695,071	(4,003,780)	(400,659)	(66,077)	(32,755)	2,191,800
Video gaming	965,074*	513	(438,653)	(60,402)	—	466,532
	\$ 7,660,145	(4,003,267)	(839,312)	(126,479)	(32,755)	2,658,332
Telecommunications						(28,109)
Other operating expenses						(130,161)
Total operating income						\$ 2,500,062

\* Video gaming revenue represents net machine income after awarding prizes. Video gaming credits played and won were as follows:

Credits played	\$ 11,663,674
Credits won	<u>(10,698,600)</u>
Net machine income \$	<u>965,074</u>

\*\* Prizes unclaimed after one year are forfeited and are netted against prizes.

**(9) Deferred Compensation**

The 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 are placed in trust for the participants and their beneficiaries.

**(10) Postretirement Benefits**

As a New York State (State) agency, the Lottery participates in the New York State Health Insurance Program (NYSHIP), which is administered by the State as an agent multiple employer defined benefit plan. Under the plan the State provides certain healthcare for eligible retired employees and their dependents under an employer noncontributory healthcare plan. The State's Plan states that employees and/or their dependents become eligible for these benefits at 55 years of age when the employee has 10 years of State service. In calculating the 10 year service requirement, all of the employee's service need not be with the State, but may be a composite of other government service elsewhere, with a minimum of 3 years with New York State. Employees with no prior State service must work a minimum of 10 years before they and

## NEW YORK STATE LOTTERY

### Notes to Basic Financial Statements

March 31, 2010 and 2009

their dependents are eligible for the retirement medical benefits. Generally retirees contribute 10% of the cost of single coverage and 25% of the cost of dependent coverage for health insurance benefits. The State generally covers 100% of the cost of single and dependent coverage for employees retired prior to January 1, 1983. NYSHIP does not issue a stand-alone financial report and NYSHIP's agent activities are included within the financial statements of the State.

During the fiscal year ended March 31, 2010, NYSHIP provided health insurance coverage through the Empire Plan, an indemnity health insurance plan with managed care components; 12 Health Maintenance Organizations (HMOs); and through the Student Employee Health Plan (SEHP). Generally, these include hospital, medical, mental health and substance abuse benefits, and prescription drug benefits

The Lottery's policy regarding retiree healthcare benefits is to pay the amounts billed through the State's fringe benefit rate on a pay-as-you-go basis. The Lottery has no obligation beyond the payment of the State's fringe benefit rate for retiree healthcare benefits. The State's policy is that the State is responsible for recording the annual required contribution and the actuarial accrued liability under GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions* for the Lottery's retiree health care benefits in the State's governmental-wide financial statements.

At March 31, 2010 and 2009, the Lottery had between 120 and 130 retired and/or spouses of retired employees receiving these benefits with an annual pay-as-you-go cost of approximately \$1,070,000 and \$800,000, respectively.

#### **(11) Employees' Compensated Absences**

Under the terms of the Lottery's personnel policies and its union agreements, vacation pay benefits may be paid upon termination up to a maximum of 225 hours. The Lottery recognizes employees' compensated absence benefits when earned. The liability for employees' compensated absences was approximately \$1,846,000 and \$1,588,000 as of March 31, 2010 and 2009, respectively, and is recorded as a liability in the statements of net assets.

#### **(12) Leases**

The Lottery leases surveillance equipment at its video lottery gaming facilities under capital leases with various companies. Amounts for capital leases, which are included in capital assets on the statements of net assets, were approximately \$22,672,000 at both March 31, 2010 and 2009. Accumulated depreciation on these capital assets was approximately \$18,902,000 and \$16,170,000 at March 31, 2010 and 2009, respectively.

The Lottery has entered into operating leases for equipment and building space. Rental expense was approximately \$2,358,000 and \$2,388,000 in 2010 and 2009, respectively.

**NEW YORK STATE LOTTERY**

Notes to Basic Financial Statements

March 31, 2010 and 2009

Future minimum lease payments under all noncancelable leases having initial or remaining terms in excess of one year as of March 31, 2010 are as follows (in thousands):

	<u>Operating leases</u>	<u>Capital leases</u>
2011	\$ 1,965	2,019
2012	1,695	1,994
2013	1,599	—
2014	1,546	—
2015	1,543	—
2016 and thereafter	<u>2,424</u>	<u>—</u>
Total minimum payments required	\$ <u>10,772</u>	4,013
Less amounts representing interest		<u>141</u>
Present value of minimum lease payments		3,872
Less current portion		<u>2,062</u>
Long-term capital lease obligations		\$ <u>1,810</u>

**(13) Commitments and Contingencies**

**(a) Contractual Arrangements**

The Lottery maintains a gaming network of approximately 17,000 on-line locations where all traditional lottery games are sold. GTECH Holdings Corporation (GTECH) is responsible for operating all traditional Lottery games under a contract expiring on August 31, 2010.

In March 2009, the Lottery awarded a seven year contract through August 5, 2017 to GTECH Corporation for a gaming network and vending machines including related communication services. A new gaming system will be operational under this contract in August 2010.

Instant Game sales are also supported by services provided under additional contracts:

- (1) Under a contract that expires July 23, 2011 Scientific Games, Inc. is the primary supplier of Instant Game tickets.
- (2) Under a contract expiring July 30, 2011 Pollard Banknote Limited is the secondary supplier of Instant Game tickets.
- (3) Under contracts that expire on July 27, 2011 Scientific Games, Inc. and GTECH Printing Corporation are tertiary suppliers of Instant Game tickets.

## **NEW YORK STATE LOTTERY**

### Notes to Basic Financial Statements

March 31, 2010 and 2009

- (4) Instant Game tickets are also sold through approximately 4,000 vending machines at approximately 3,000 locations. A contract with GTECH which expires on June 5, 2011 provides for maintenance of the vending machines.

Video lottery games are offered on approximately 12,500 video gaming machines spread over eight video lottery gaming facilities. Multimedia Games, Inc. provides a central processing system for the operation of video lottery games under a contract expiring on December 31, 2017. Video lottery gaming machines are provided under contracts expiring December 31, 2017 with three different companies (Bally Gaming, International Game Technology, and Spielo USA, Inc.).

**(b) *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.