



ANNUAL REPORT

Fiscal Year 2013



Profits benefit the Vermont Education Fund



Greg Smith,
Executive Director

The Vermont Lottery continues to offer a variety of games for Vermonters to play and enjoy. Our instant ticket games have the most visual appeal and are favorites among most of our core players. They also provide us the best opportunity to catch the attention of potential customers with themes that may resonate with them. This year we offered a game show ticket for "The

Price Is Right", another one modeled after the popular board game, "Battleship", and other games with Vermont themes and general lottery themes. You can expect to see more of these special tickets.

And what a year for our draw games! In March of 2012, Mega Millions set the record with a jackpot reaching \$656 million. Powerball followed that with jackpots of \$580+ million in November, and then another for \$590+ million in May of 2013. These three astronomical amounts caught the attention of everyone in the USA, and many around the world. We wonder if we will see the first \$1 billion jackpot in the near future, and what does winning that kind of money mean? A few lucky Vermonters became millionaires this year playing lottery games, and many others added to their nest eggs with wins ranging from \$50,000 - \$100,000.

Our 2nd Chance games experienced significant growth this year. We transitioned from a mail-in entry to an online entry in June of 2012, and saw approximately 1.5 million entries. These savvy players got a 2nd Chance to win a top prize from most of our instant ticket games, and also chances to win quarterly prizes of cash, grocery gift cards, fuel gift cards and passes for outdoor sports. We awarded over 400 2nd Chance prizes this year and look forward to increasing that next year with even more top prizes.

After we paid for all the prizes, and paid for the services to deliver lottery games, we contributed all of our profits to the Education Fund. This year's profits totaled just under \$23 million, or over 22% of total sales. The staff of the Vermont Lottery is very proud of the work we do, the integrity of the lottery games that we offer to Vermonters, and our collaboration with almost 700 lottery agents around the state.

The Vermont Lottery celebrated our 35th anniversary this year. In that time we have contributed over \$500 million back to the state – money that did not have to be raised by taxes. That's right, over \$500 million. So, go ahead, Play A Little.

Martha H. O'Connor, Chair

Greg Smith, Executive Director

Commissioners



Martha O'Connor
Chair
Brattleboro
Term Expires
02/14



Karen O'Hagan
Winooski
Term Expires
02/14



Arthur Ristau
Vice Chair
Barre
Term Expired
02/13



Virginia Barry
Vice Chair 03/13
Barre
Term Expires
02/15



Tom Scala
Tri-State
Commissioner
Brattleboro
Term Expires
02/15



Ed Flanagan
Montpelier
Term Expires
02/16

History

Public Act No. 82 was enacted by the 1977 General Assembly establishing the Vermont Lottery Commission. The first Lottery ticket, Green Mountain Game, went on sale to the public February 14, 1978. Since the Lottery's inception, all profits generated by the Vermont Lottery were dedicated for use by the state's General Fund. In July 1998, the Vermont Legislature mandated that all profits from the Lottery go to the state's Education Fund. The Vermont Lottery is run by a small, efficient staff of 21 full-time employees and five Commissioners. It is still one of the smallest staffs of any lottery in the United States, yet generated over \$102 million in revenue during FY13.

Vermont Lottery Commission

1311 U.S. Route 302, Suite 100, Barre, VT 05641

(802) 479-5686 • Fax (802) 479-4294

Email: staff@vtlottery.com

Products

In FY13, the Vermont Lottery offered ten games for sale: Instant tickets, Powerball, Mega Millions, Hot Lotto, Lucky For Life; the Tri-State games Megabucks Plus, Fast Play, Pick 3, Pick 4; and the newest game, Gimme 5. A few of these had changes to their prizes, odds and rules implemented this year, and more of them have changes planned for next year. We believe that making periodic changes to games causes them to be more appealing to current and potential players. These changes are thoroughly reviewed by mathematicians, lottery game technicians, market research groups and each state lottery that offers the games to ensure integrity and ease of play. The variety of games, prices, prize levels, odds of winning, and themes allows us to provide games that appeal to a broad demographic mix.

Lottery Agents

In FY13, there were approximately 685 Lottery agents in Vermont who sold our online games and instant tickets. Agents received 6% of their total Powerball, Hot Lotto, Mega Millions and Lucky for Life sales and 5.75% of all other Lottery product sales. In addition, agents received a 1% bonus for selling winning tickets of \$500 and up (agent bonus capped at \$30,000). In FY13, the commissions and bonuses paid to agents totaled \$6 million.

Top Five Agents in FY13 Commission Earned:

1) \$35,013 2) \$34,265 3) \$31,637 4) \$30,012 5) \$27,442

Responsible Gaming

The Vermont Lottery continues its close partnership with The Vermont Council on Problem Gambling (VCPG) so we can assist any Vermonter who may have difficulty with any type of gambling.

The Vermont Lottery's funding of VCPG covers the staffing, phone lines and website, training for staff and addiction counselors, literature, event sponsorships and much more. We also include the VCPG hotline number, web address and a message about responsible play on all Lottery tickets and advertising.

This year we increased the frequency of VCPG television and radio ads so that they run almost every day on Vermont stations. If you know someone who has a gambling problem, the Vermont Lottery encourages you to provide them the toll free number or web address for VCPG so they can get on the road to recovery.

Results of Operations

FY13 ended with overall revenue of \$102,088,644. The total contribution to the state's Education Fund was \$22.9 million. In addition to the Education Fund contribution, \$64.5 million was returned to players in the form of prizes, and \$6.0 million went to local Lottery agents as commissions on sales.

Sales

Total FY13 sales equaled \$102,087,388. Game sales were as follows:

	2013	2012
Instant scratch off games	\$ 74,214,288	\$ 74,537,161
<i>Online games:</i>		
Pick 3	1,365,930	1,383,792
Pick 4	1,254,733	1,297,613
Fast Play	1,809,653	951,643
Mega Millions	2,796,901	4,682,208
Hot Lotto	991,188	1,060,724
Powerball	12,034,883	9,649,154
Weekly Grand Extra	—	1,004,506
Lucky for Life	2,588,726	999,668
Megabucks Plus	4,889,349	5,360,610
Gimme 5	141,737	—
Total Sales	\$ 102,087,388	\$ 100,927,079

Operating Expenses

Administrative costs for the Lottery were \$3,028,895, an increase of \$121,487 from FY12. Administrative costs included salaries, benefits, contracted services, depreciation, equipment, and supplies that were included in the Lottery's annual operating budget appropriation from the Legislature. This budget appropriation came from Lottery revenues.

Other operating expenses, dependent on Lottery sales, included Lottery tickets, courier system, agent network expenses and facilities management fees to our online vendor, Intralot, and instant ticket gaming system vendor, Scientific Games, International. The total cost of other operations for FY13 was \$7,401,922, an increase of \$88,740 from FY12, which includes the administrative costs of \$3,208,895 mentioned above.

Tri-State Expenses

The Tri-State operating, communications, and facilities management costs totaled \$1,182,997, an increase of \$70,312 from FY12.

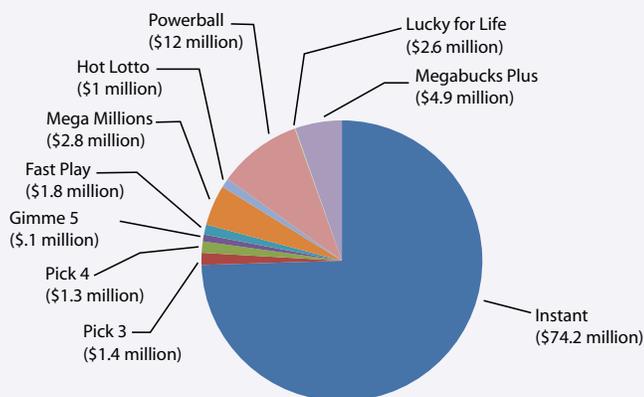
Prizes and Commissions

The total prizes paid to players in FY13 were \$64,556,404 and the total commissions paid to agents were \$6,020,216.

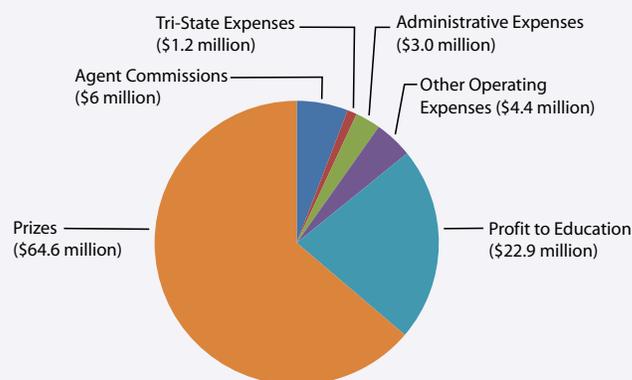
Contribution to Vermont Education Fund

The total contribution to the Vermont Education Fund in FY13 was \$22,927,105.

Where the sales were:



Where the money went:



STATEMENTS OF NET POSITION*

JUNE 30, 2013 AND 2012

ASSETS

	2013	2012
Current Assets:		
Cash and cash equivalents	\$ 3,784,668	\$ 3,480,721
Accounts receivable	1,843,443	1,821,371
Due from State Education Fund	8,680	—
Prepaid expenses	6,569	5,819
Inventory	491,788	497,831
Total current assets	<u>6,135,148</u>	<u>5,805,742</u>
Restricted and noncurrent assets:		
Investments	1,757,232	2,045,324
Property and equipment, less accumulated depreciation	11,132	17,917
Total restricted and noncurrent assets	<u>1,768,364</u>	<u>2,063,241</u>
Total assets	<u>7,903,512</u>	<u>7,868,983</u>
LIABILITIES:		
Current liabilities:		
Accounts payable	542,971	905,682
Accrued leave	75,189	93,202
Accrued payroll	59,214	56,151
Current - Due to winners	254,537	249,057
Reserve for future and unclaimed prizes	4,487,653	3,791,589
Deferred revenue	178,832	162,537
Total current liabilities	<u>5,598,396</u>	<u>5,258,218</u>
Liabilities payable from restricted assets:		
Noncurrent - Due to winners	1,250,154	1,435,101
Cash advances by State Treasurer	300,000	300,000
Total long-term liabilities	<u>1,550,154</u>	<u>1,735,101</u>
Total liabilities	<u>7,148,550</u>	<u>6,993,319</u>
NET POSITION:		
Invested in capital assets	11,132	17,917
Unrestricted	743,830	857,747
Total net position	<u>\$ 754,962</u>	<u>\$ 875,664</u>

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION*

FOR THE YEARS ENDED JUNE 30, 2013 AND 2012

	2013	2012
OPERATING REVENUES:		
Ticket sales	\$ 102,087,388	\$ 100,927,079
Agents' license fees and other receipts	1,256	3,441
Total operating revenues	<u>102,088,644</u>	<u>100,930,520</u>
OPERATING EXPENSES:		
Prize expense	64,556,404	64,409,376
Commissions - agents	6,020,216	5,914,952
Lottery tickets	1,186,633	1,158,847
Instant ticket dispensers	46,232	46,491
Courier system	220,746	218,610
Facilities management fee - instant	2,398,108	2,238,913
Facilities management fee - online	548,331	495,636
Tri-State expenses	1,182,997	1,112,685
MUSL expenses	93,679	32,405
Other costs of sales and services	—	37,046
Personal services	1,475,351	1,480,387
Advertising	769,222	687,950
Other operating expenses	540,019	575,931
Depreciation	6,785	13,140
Department of Health	150,000	150,000
Total operating expenses	<u>79,194,723</u>	<u>78,572,369</u>
OPERATING INCOME	<u>22,893,921</u>	<u>22,358,151</u>
NONOPERATING REVENUES (EXPENSES):		
Investment income (loss)	(87,518)	147,771
Total nonoperating revenues (expenses)	<u>(87,518)</u>	<u>147,771</u>
INCOME BEFORE OPERATING TRANSFERS	22,806,403	22,505,922
NET PROFIT TRANSFERRED TO THE STATE OF VERMONT		
Education Fund	(22,927,105)	(22,328,096)
INCREASE (DECREASE) IN NET POSITION	(120,702)	177,826
NET POSITION, beginning of year	<u>875,664</u>	<u>697,838</u>
NET POSITION, end of year	<u>\$ 754,962</u>	<u>\$ 875,664</u>

*A copy of the complete financial statements with the Independent Auditor's Reports is available upon request.

VERMONT LOTTERY COMMISSION

FINANCIAL STATEMENTS
JUNE 30, 2013
WITH COMPARATIVE TOTALS FOR JUNE 30, 2012
AND
INDEPENDENT AUDITOR'S REPORTS

VERMONT LOTTERY COMMISSION

JUNE 30, 2013 AND 2012

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INDEPENDENT AUDITOR'S REPORT

The Commissioners
Vermont Lottery Commission

Report on the Financial Statements

We have audited the accompanying financial statements of the Vermont Lottery Commission, an enterprise fund of the State of Vermont, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Vermont Lottery Commission as of June 30, 2013, and the changes in its financial position and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Emphasis of a Matter

As discussed in note 1, the financial statements present only the Vermont Lottery Commission and do not purport to, and do not, present fairly the financial position of the State of Vermont as of June 30, 2013, the changes in its financial position, or where applicable, its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Information

Report on Summarized Comparative Information

We have previously audited the Vermont Lottery Commission's financial statements for the year ended June 30, 2012, and we expressed an unmodified audit opinion on those financial statements in our report dated September 5, 2012. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2012 is consistent, in all material respects, with the audited financial statements from which it has been derived.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 8, 2013, on our consideration of the Vermont Lottery Commission's internal control over financial reporting, on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, and on other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Vermont Lottery Commission's internal control over financial reporting and compliance.

Montpelier, Vermont
October 8, 2013

*Mudgett, Jennett &
Krogh-Wisner, P.C.*

**VERMONT LOTTERY COMMISSION
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2013**

This discussion of the Vermont Lottery Commission's financial performance provides an overview of the Commission's financial activities for the fiscal year ended June 30, 2013. Please read it in conjunction with the financial statements.

The Vermont Lottery Commission (the Commission) is an enterprise fund of the State of Vermont. The Commission's operations are classified as business-type activities and reported in a manner similar to commercial entities.

Financial Highlights

- Gross revenues for lottery gaming activities increased by \$1,158,124 or 1.15%.
- Total operating expenses for the year increased by \$622,354 or 0.79%. Of this increase, prize expense increased by \$147,028, facilities management fees increased by \$211,890, agent commissions increased by \$105,264, and Tri-State expenses increased by \$70,312.
- Nonoperating revenue in FY 2013 included an unrealized loss on investments of \$108,625. The total investment loss of \$87,518 resulted in an overall decrease of \$235,289 from the nonoperating revenue in FY 2012.
- Income before operating transfers (net revenue) increased by \$300,481.

Assets and Net Position

The assets of the Commission are primarily cash and investments held for operating purposes. Total assets at June 30, 2013, of \$7,903,512 include net capital assets of \$11,132, restricted investments of \$1,757,232 and current operating assets such as cash and cash equivalents, accounts receivable, prepaid expenses and inventory of \$6,135,148. Net position retained by the Commission is \$754,962.

Total assets at June 30, 2012, of \$7,868,983 included net capital assets of \$17,917, restricted investments of \$2,045,324 and current operating assets such as cash and cash equivalents, accounts receivable, prepaid expenses and inventory of \$5,805,742. Net position retained by the Commission was \$875,664.

Liabilities

The Commission's liabilities consist of operating liabilities and obligations for payment of prizes to lottery winners. Total liabilities at June 30, 2013, of \$7,148,550 include long-term liabilities for prize obligations of \$1,250,154, cash advances from the State of \$300,000 and current operating liabilities of \$5,598,396.

Total liabilities at June 30, 2012, of \$6,993,319 included long-term liabilities for prize obligations of \$1,435,101, cash advances from the State of \$300,000 and current operating liabilities of \$5,258,218.

Sales

The following shows ticket sales by game:

	<u>2013</u>	<u>2012</u>
Instant scratch off games	\$ 74,214,288	\$ 74,537,161
Online games:		
Powerball	12,034,883	9,649,154
Mega Millions	2,796,901	4,682,208
Hot Lotto	991,188	1,060,724
Lucky for Life	2,588,726	999,668
Megabucks Plus	4,889,349	5,360,610
Pick 3	1,365,930	1,383,792
Pick 4	1,254,733	1,297,613
Weekly Grand Extra	-	1,004,506
Gimme 5	141,737	-
Fast Play	<u>1,809,653</u>	<u>951,643</u>
Total sales	\$ <u>102,087,388</u>	\$ <u>100,927,079</u>

Prizes

In general, prize expense by game will increase or decrease from year to year in proportion to the increase or decrease in sales for a particular game. Prize expense for the instant games product category is controllable, to a large degree, by printing a predetermined number and value of winning tickets in the production of each instant game. Prize expense for online games is predetermined by design to yield a certain ratio of prizes to sales over a large number of drawings. Currently for online games the Commission has designated that at least 50% of online sales revenue be reserved for prize awards. Each of these lottery products' actual prize payout is determined by lottery players' luck in matching the particular set of numbers randomly selected in each drawing for each game. If the value of prizes for the winning tickets selected is not at least the 50% of sales revenue, the difference between the designated prize pool and the value of the winning tickets is contributed to either a jackpot pool in the case of Tri-State Megabucks, the Powerball game, Mega Millions game and Hot Lotto game, or is reported as prize contingencies by the Tri-State Lotto Commission in the case of Pick 3, Pick 4, Weekly Grand Extra and Fast Play or by the Vermont Lottery Commission in the case of Lucky for Life.

	<u>2013</u>	<u>2012</u>
Prize expense - Instant scratch off games	\$ 50,157,540	\$ 50,393,672
Prize expense - Online games	<u>14,398,864</u>	<u>14,015,704</u>
	\$ <u>64,556,404</u>	\$ <u>64,409,376</u>

Other Potentially Significant Factors

Operating results for FY 2013 were improved over FY 2012. The overall improvement in sales was offset by the increased cost of sales as would be expected as most of these expenses are paid as a percentage of sales. The robust Powerball sales, the result of several large jackpot rolls, Fast Play offering multiple games at multiple price points, the addition of New England game Lucky for Life, and the addition of the new Tri-State game, Gimme 5, were all factors in the improved sales for FY 2013.

The Lottery is a highly visible governmental activity. Its mission is to operate a State Lottery that will produce the maximum amount of net revenue consonant with the dignity of the State and general welfare of the people. There are a number of revenue-enhancing opportunities generally available to the lottery industry. These options, if deemed to be consonant with the general welfare of the people by those in the executive branch and/or legislature, may be considered in future years.

VERMONT LOTTERY COMMISSION
STATEMENTS OF NET POSITION
JUNE 30, 2013
WITH COMPARATIVE TOTALS FOR JUNE 30, 2012

ASSETS:	<u>2013</u>	<u>2012</u>
Current assets:		
Cash and cash equivalents	\$ 3,784,668	\$ 3,480,721
Accounts receivable	1,843,443	1,821,371
Due from the State Education Fund	8,680	-
Prepaid expenses	6,569	5,819
Inventory	491,788	497,831
Total current assets	<u>6,135,148</u>	<u>5,805,742</u>
Restricted and noncurrent assets:		
Investments	1,757,232	2,045,324
Property and equipment, less accumulated depreciation	<u>11,132</u>	<u>17,917</u>
Total restricted and noncurrent assets	<u>1,768,364</u>	<u>2,063,241</u>
Total assets	<u>7,903,512</u>	<u>7,868,983</u>
 LIABILITIES:		
Current liabilities:		
Accounts payable	542,971	905,682
Accrued leave	75,189	93,202
Accrued payroll	59,214	56,151
Current - Due to winners	254,537	249,057
Reserve for future and unclaimed prizes	4,487,653	3,791,589
Deferred revenue	<u>178,832</u>	<u>162,537</u>
Total current liabilities	<u>5,598,396</u>	<u>5,258,218</u>
Liabilities payable from restricted assets:		
Non-current - Due to winners	1,250,154	1,435,101
Cash advances by State Treasurer	<u>300,000</u>	<u>300,000</u>
Total long-term liabilities	<u>1,550,154</u>	<u>1,735,101</u>
Total liabilities	<u>7,148,550</u>	<u>6,993,319</u>
 NET POSITION:		
Invested in capital assets	11,132	17,917
Unrestricted	<u>743,830</u>	<u>857,747</u>
Total net position	<u>\$ 754,962</u>	<u>\$ 875,664</u>

The notes to financial statements are an integral part of these statements.

**VERMONT LOTTERY COMMISSION
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN NET POSITION
FOR THE YEAR ENDED JUNE 30, 2013
WITH COMPARATIVE TOTALS FOR THE YEAR ENDED JUNE 30, 2012**

	<u>2013</u>	<u>2012</u>
OPERATING REVENUES:		
Ticket sales	\$ 102,087,388	\$ 100,927,079
Agents' license fees and other receipts	<u>1,256</u>	<u>3,441</u>
Total operating revenues	<u>102,088,644</u>	<u>100,930,520</u>
OPERATING EXPENSES:		
Prize expense	64,556,404	64,409,376
Commissions - agents	6,020,216	5,914,952
Lottery tickets	1,186,633	1,158,847
Instant ticket dispensers	46,232	46,491
Courier system	220,746	218,610
Facilities management fee - instant	2,398,108	2,238,913
Facilities management fee - online	548,331	495,636
Tri-State expenses	1,182,997	1,112,685
MUSL expenses	93,679	32,405
Other costs of sales and services	-	37,046
Personal services	1,475,351	1,480,387
Advertising	769,222	687,950
Other operating expenses	540,019	575,931
Depreciation	6,785	13,140
Department of Health	<u>150,000</u>	<u>150,000</u>
Total operating expenses	<u>79,194,723</u>	<u>78,572,369</u>
OPERATING INCOME	<u>22,893,921</u>	<u>22,358,151</u>
NONOPERATING REVENUES (EXPENSES):		
Investment income (loss)	<u>(87,518)</u>	<u>147,771</u>
Total nonoperating revenues (expenses)	<u>(87,518)</u>	<u>147,771</u>
INCOME BEFORE OPERATING TRANSFERS	22,806,403	22,505,922
NET PROFIT TRANSFERRED TO THE STATE OF VERMONT:		
Education Fund	<u>(22,927,105)</u>	<u>(22,328,096)</u>
INCREASE (DECREASE) IN NET POSITION	(120,702)	177,826
NET POSITION, beginning of year	<u>875,664</u>	<u>697,838</u>
NET POSITION, end of year	\$ <u>754,962</u>	\$ <u>875,664</u>

The notes to financial statements are an integral part of these statements.

**VERMONT LOTTERY COMMISSION
STATEMENTS OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2013
WITH COMPARATIVE TOTALS FOR THE YEAR ENDED JUNE 30, 2012**
(Page 1 of 2)

	<u>2013</u>	<u>2012</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash received from customers	\$ 102,080,861	\$ 100,509,754
Cash paid for prizes and agents' commissions	(70,053,980)	(69,375,094)
Cash paid for management fees, operations and other	(7,498,678)	(6,298,142)
Cash paid to employees for services	(1,490,301)	(1,467,809)
Other operating revenue	<u>1,256</u>	<u>3,441</u>
Net cash provided by operating activities	<u>23,039,158</u>	<u>23,372,150</u>
 CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:		
Operating transfers	<u>(22,935,785)</u>	<u>(22,328,096)</u>
Net cash used in noncapital financing activities	<u>(22,935,785)</u>	<u>(22,328,096)</u>
 CASH FLOWS FROM INVESTING ACTIVITIES:		
Unrealized gains on investments	(51,687)	(64,660)
Proceeds from maturities of investments, net	<u>252,261</u>	<u>247,077</u>
Net cash provided (used) by investing activities	<u>200,574</u>	<u>182,417</u>
 NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		
	303,947	1,226,471
 CASH AND CASH EQUIVALENTS, beginning of year		
	<u>3,480,721</u>	<u>2,254,250</u>
 CASH AND CASH EQUIVALENTS, end of year		
	\$ <u>3,784,668</u>	\$ <u>3,480,721</u>

The notes to financial statements are an integral part of these statements.

**VERMONT LOTTERY COMMISSION
STATEMENTS OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2013
WITH COMPARATIVE TOTALS FOR THE YEAR ENDED JUNE 30, 2012**
(Page 2 of 2)

	<u>2013</u>	<u>2012</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating income	\$ <u>22,893,921</u>	\$ <u>22,358,151</u>
Adjustments to reconcile operating income to net cash provided by operating activities -		
Depreciation	6,785	13,140
(Increase) decrease in the following assets:		
Accounts receivable	(22,072)	(414,506)
Prepaid expenses	(750)	(5,819)
Inventory	6,043	(12,695)
Increase (decrease) in the following liabilities:		
Accounts payable	(362,711)	456,372
Accrued salaries and benefits	(14,950)	12,578
Due to winners	(179,467)	(170,017)
Reserve for future and unclaimed prizes	696,064	1,131,946
Deferred revenue	<u>16,295</u>	<u>3,000</u>
Total adjustments	<u>145,237</u>	<u>1,013,999</u>
Net cash provided by operating activities	\$ <u>23,039,158</u>	\$ <u>23,372,150</u>

The notes to financial statements are an integral part of these statements.

**VERMONT LOTTERY COMMISSION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013 AND 2012**

1. Summary of significant accounting policies:

The Vermont Lottery Commission (the Lottery) was created by an enactment of the Vermont State Legislature and signed into law by the Governor on April 27, 1977. Title 31, Chapter 14 of the Vermont Statutes is the law under which the Lottery operates. The Lottery is an enterprise fund of the State of Vermont and is managed by a five-member Commission appointed by the Governor for three-year terms. The Commission, by law, has the authority to operate the State lottery, determine the type and forms of lottery games, set the price of lottery tickets, determine the number and size of prizes, select the ticket sales locations and may enter into agreements with another state or states to provide for the operation of the Lottery.

Fiscal operations of the Lottery commenced in October, 1977. The Lottery's net revenue was transferred to the State of Vermont's General Fund through June 30, 1998. Beginning July 1, 1998, the Lottery's revenue is committed to funding public education, and Lottery net revenue is transferred to the State of Vermont Education Fund on a monthly basis.

The Lottery entered into a compact with the states of Maine and New Hampshire known as the Tri-State Lotto. The compact was enacted to implement the operation of Tri-State Lotto for the purpose of raising additional revenue for each of the party states. Vermont's portion of the Tri-State Lotto operations is accounted for by the Lottery.

In July 2003, the Lottery entered into an agreement with the Multi-State Lottery Association (MUSL) for the inclusion of the Powerball game.

In March 2012, the Lottery entered into an agreement with the Connecticut Lottery Corporation, the Maine State Liquor & Lottery Commission, the Massachusetts State Lottery Commission, the New Hampshire Lottery Commission, and the Rhode Island Division of State Lottery to offer Lucky for Life, a New England regional lotto game.

- A. Reporting entity - The Lottery is included in the State of Vermont's financial statements as an enterprise fund. In accordance with governmental accounting and financial reporting standards, there are no component units to be included within the Lottery's financial statements as a reporting agency.
- B. Measurement focus and basis of accounting - The financial statement presentation follows the recommendations of the Governmental Accounting Standards Board (GASB) in its Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*. The Lottery uses the economic resources measurement focus and the accrual basis of accounting whereby revenues are recorded when earned and expenses are recorded when the obligation for payment is incurred. The Lottery is classified as an enterprise fund of the governmental proprietary fund type. Enterprise funds account for operations similar to private business enterprises where the intent of the Legislature is that costs are to be financed or recovered primarily through user charges, or where the Legislature has decided that periodic determination of revenue earned, expenses incurred or net income is appropriate.

**VERMONT LOTTERY COMMISSION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013 AND 2012**

1. Summary of significant accounting policies (continued):

- C. Revenue recognition - Sales of instant lottery tickets are made to licensed retailers who market the tickets to the public on a commission basis. Revenue is recognized when the books of tickets are settled with the retailers. Tickets activated, but not sold by retailers, may be returned for credit. Sales of online lottery tickets are made to licensed retailers who market the tickets through the use of computerized terminals on a commission basis. Ticket revenue is recognized weekly. Tickets sold in advance of future drawing dates are recorded as deferred revenue until the ticket becomes valid for a drawing.
- D. Expenses - Commissions and fees for the instant and online games are recognized weekly. Administrative expenses, such as salaries, benefits, contracted services, depreciation, equipment and supplies are included in the Lottery's annual operating budget appropriation from the Legislature. This budget appropriation came from Lottery revenues. Other Lottery operating expenses, which will vary with product sales volume, such as lottery tickets, courier system, agent network expenses and facilities management fees for the gaming systems vendor are considered "cost of goods", are part of an authorized amount approved by Finance and Management, and are derived from Lottery revenues. In addition, Vermont State Statute Title 31, Chapter 14, §658 provides that agent commissions may not exceed 6.25% of gross receipts and bank commissions may not exceed 1% of gross receipts. The statutes also provide that the Lottery must pay out no less than 50% of gross receipts as prizes.
- E. Cash and cash equivalents - Cash includes demand deposits and short-term investments with a maturity date within three (3) months of the date acquired by the Lottery except for amounts included in the investment account.
- F. Investments - Investments with readily determinable fair market values are reported at their fair market values on the balance sheet. The Lottery's policy is to retain in net position the unrealized gains and losses on long-term investments held for the purpose of paying long-term installment prizes due to winners. This policy is consistent with the provision for apportionment of Lottery revenues in Title 31, Chapter 14, §654 (11)(A).
- G. Property and equipment - Property and equipment are stated at cost, recorded as a capital asset based on the nature of the item and depreciated over the estimated useful life of the asset. Capital assets are defined by the Lottery as assets with an initial individual cost of more than \$5,000 and a useful life of more than two years. Capitalized costs include freight-in, licenses, title application and any other costs required to establish the initial operation of the asset. Improvements and additions to an asset are capitalized. Maintenance and repair costs are not capitalized. Depreciation expense is calculated using the straight-line method over the estimated lives of the assets which are:
- | | |
|--------------------------------|-------------|
| Office furniture and equipment | 3-7 years |
| Leasehold improvements | 10-15 years |
- H. Compensated absences - Lottery employees are entitled to certain compensated absences based on their length of employment. Generally, compensated absences either vest or accumulate and are accrued when they are earned. Sick leave does not accrue beyond annual use.

**VERMONT LOTTERY COMMISSION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013 AND 2012**

1. Summary of significant accounting policies (continued):

- I. Advertising - Advertising costs are expensed as incurred.
- J. Annuities - The Lottery is the owner of two annuities that were purchased for grand prizes won by two individuals in 1995. The cost of the annuities was charged against the reserve for future prizes at the time of purchase. The annuities were purchased from the following insurance company and have the following expiration dates:

<u>Insurance Company</u>	<u>Annuity Expiration Date</u>
Keypoint Life Insurance Company	November 14, 2014
Keypoint Life Insurance Company	December 15, 2014

- K. Estimates - The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.
- L. Risk management - The Lottery is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; injuries to individuals; and natural disasters. These are managed by the State of Vermont on behalf of the Lottery.
- M. New accounting standard - The Lottery has implemented GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*. The impact on these financial statements was to change the term “Net Assets” to “Net Position.” In the future, deferred outflows of resources and deferred inflows of resources, if applicable, would be reported in the statement of net position.
- N. Prior year totals - The basic financial statements include certain prior year summarized comparative information in total but not at a level of detail required for a presentation in conformity with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the Lottery’s financial statements for the year ended June 30, 2012, from which the summarized information was derived.

2. Cash and cash equivalents:

Custodial credit risk - deposits - Custodial credit risk is the risk that in the event of a bank failure, the Lottery’s deposits may not be returned to it. The Lottery does not have a deposit policy for custodial credit risk. As of June 30, 2013, all of the Lottery’s bank balance of \$5,425,268 was insured or collateralized. As of June 30, 2012, all of the Lottery’s bank balance of \$2,375,305 was insured or collateralized. Collateralized amounts are held by the pledging bank’s trust department in the Lottery’s name.

**VERMONT LOTTERY COMMISSION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013 AND 2012**

3. Cash with State of Vermont Treasurer:

Cash with the State Treasurer represents cash held by the Vermont State Treasurer's Office for the purpose of funding expenditures of the Lottery and transfers to the State of Vermont Education Fund. The expenditures are provided for by an appropriation from the State of Vermont which is derived from Lottery revenues for the operation of the Lottery. The balance in this account is reduced by transfers of net revenue of the Lottery to the State of Vermont Education Fund.

4. Investments/due to winners:

Investments at June 30, 2013 and 2012 were as follows:

	<u>2013</u>	<u>2012</u>
U.S. Treasury Strips	\$ 1,575,740	\$ 1,781,572
Annuity contracts	<u>181,492</u>	<u>263,752</u>
	<u>\$ 1,757,232</u>	<u>\$ 2,045,324</u>

Interest rate risk - The Lottery purchases investments in government securities that will mature in future years to pay multi-year payment prizes won by certain instant ticket winners (see note 9). These are held by the Trust Department of the People's United Bank in Burlington, Vermont, and are reported at market value. The Lottery also owns two annuity contracts purchased for winners which are reported at amortized cost. Because these investments are scheduled to be paid to winners as they mature, the Lottery has an investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit and custodial credit risk - Investments in the two annuity contracts are both with Keyport Life Insurance Company (see note 1.J.). These contracts are unrated.

Investments and Due to winners as of June 30, 2013 are \$1,757,232 and \$1,504,691, respectively. Investments and Due to winners as of June 30, 2012 are \$2,045,324 and \$1,684,158, respectively.

5. Accounts receivable:

Accounts receivable at June 30, 2013 and 2012 consisted of the following:

	<u>2013</u>	<u>2012</u>
MUSL	\$ 901,692	\$ 885,305
Tri-State	58,718	129,037
Regular Agents	755,001	706,166
Chain Agents	<u>190,609</u>	<u>159,819</u>
Total	1,906,020	1,880,327
Less: Allowance for doubtful accounts	<u>(62,577)</u>	<u>(58,956)</u>
Net accounts receivable	<u>\$ 1,843,443</u>	<u>\$ 1,821,371</u>

**VERMONT LOTTERY COMMISSION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013 AND 2012**

6. Inventory:

The Lottery had inventory consisting of lottery tickets on hand and prizes valued at a cost of \$491,288 and \$500 at June 30, 2013 and \$496,581 and \$1,250 at June 30, 2012, respectively.

7. Property and equipment:

The following is a summary of changes in property and equipment during the fiscal years.

	2013					
	Balance July 1, 2012	Additions	Retirements	Balance June 30, 2013	Accumulated Depreciation	Net Property and Equipment June 30, 2013
Computer equipment	\$ 5,583	\$ -	\$ -	\$ 5,583	\$ 5,583	\$ -
Furniture & fixtures	56,114	-	-	56,114	55,327	787
Other equipment	130,754	-	-	130,754	130,754	-
Leasehold improvements	<u>59,935</u>	<u>-</u>	<u>-</u>	<u>59,935</u>	<u>49,590</u>	<u>10,345</u>
	<u>\$ 252,386</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 252,386</u>	<u>\$ 241,254</u>	<u>\$ 11,132</u>
	2012					
	Balance July 1, 2011	Additions	Retirements	Balance June 30, 2012	Accumulated Depreciation	Net Property and Equipment June 30, 2012
Computer equipment	\$ 22,442	\$ -	\$ 16,859	\$ 5,583	\$ 5,583	\$ -
Furniture & fixtures	56,114	-	-	56,114	54,627	1,487
Other equipment	130,754	-	-	130,754	130,754	-
Leasehold improvements	<u>59,935</u>	<u>-</u>	<u>-</u>	<u>59,935</u>	<u>43,505</u>	<u>16,430</u>
	<u>\$ 269,245</u>	<u>\$ -</u>	<u>\$ 16,859</u>	<u>\$ 252,386</u>	<u>\$ 234,469</u>	<u>\$ 17,917</u>

**VERMONT LOTTERY COMMISSION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013 AND 2012**

8. Accounts payable:

The Lottery's accounts payable at June 30, 2013 and 2012 consisted of the following:

	<u>2013</u>	<u>2012</u>
Tri-State	\$ 58,447	\$ 42,578
MUSL	46,704	272,148
Vendors	<u>437,820</u>	<u>590,956</u>
	<u>\$ 542,971</u>	<u>\$ 905,682</u>

9. Due to winners:

Presented below is a summary of requirements to maturity for long-term installment prizes due to winners awarded as of June 30, 2013 and payable through the year 2033:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Current portion:			
Fiscal year -			
2014	\$ <u>254,537</u>	\$ <u>15,463</u>	\$ <u>270,000</u>
Long-term:			
Fiscal year -			
2015	251,771	18,229	270,000
2016	149,018	20,982	170,000
2017	140,456	29,544	170,000
2018	92,936	27,064	120,000
2019	87,680	32,320	120,000
2020-2024	347,505	212,495	560,000
2025-2029	109,065	90,935	200,000
2030-2034	<u>71,723</u>	<u>88,277</u>	<u>160,000</u>
Total long-term portion	<u>1,250,154</u>	<u>519,846</u>	<u>1,770,000</u>
Total requirements to maturity	<u>\$ 1,504,691</u>	<u>\$ 535,309</u>	<u>\$ 2,040,000</u>

Due to winners represents annual payments owed to jackpot winners and is fully funded by investments in U.S. Government Treasury Strips and annuities that mature on a schedule coinciding with the installments (see note 4).

10. Prize expense and reserve for future and unclaimed prizes:

By law, the Lottery must pay a minimum of 50% of gross revenue to participants in the form of prizes. Prize expense is calculated on the basis of total sales multiplied by an approved prize payout percentage. The reserve for future and unclaimed prizes is increased by the prize expense as calculated and reduced by the dollar value of prizes actually paid out. Unclaimed prizes from online games can be used for special prizes, to supplement regular prizes or in the case of instant games can be transferred to the State of Vermont Education Fund for State and local funding of public education.

For instant games, the Lottery calculated prize expense at varying percentages according to game design ranging from 61% to 75% for the years ended June 30, 2013 and 2012.

**VERMONT LOTTERY COMMISSION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013 AND 2012**

10. Prize expense and reserve for future and unclaimed prizes (continued):

In September 1985, the states of Vermont, Maine and New Hampshire instituted Tri-State Megabucks (now known as Tri-State Megabucks Plus), with a calculated prize expense of 50% of ticket sales. Megabucks Plus ticket sales in Vermont were approximately \$4.9 million for the year ended June 30, 2013 and \$5.4 million for the year ended June 30, 2012.

The Lottery began offering the Pick 3 and Pick 4 daily numbers games in November 1980 and September 1985, respectively, with calculated prize expense of 50% of ticket sales. Effective June 1995, the daily numbers games, Pick 3 and Pick 4, became Tri-State games. Pick 3 and Pick 4 sales in Vermont were approximately \$2.6 million for the year ended June 30, 2013 and \$2.7 million for the year ended June 30, 2012.

The Tri-State Lotto Commission's net position for the years ending June 30, 2013 and 2012 were \$11,152,660 and \$13,611,421, respectively. Of these amounts, \$4,345,585 represented designated prize reserves for each year and \$6,807,075 and \$9,265,836 represented unrealized gains on investments held for installment prize obligations for the years ended June 30, 2013 and 2012, respectively. The Tri-State Lotto Commission's annual financial report may be obtained by writing to the Tri-State Lotto Commission, 1311 US Route 302, Suite 100, Barre, Vermont 05641.

Effective July 1, 2003, the Lottery became a member of the Multi-State Lottery Association (MUSL) which operates online games on behalf of participating state lotteries. Each MUSL member sells game tickets through its agents and makes weekly wire transfers to the MUSL in an amount equivalent to the member's share of the estimated grand prize liability. Each MUSL member pays non-jackpot prizes directly to the winners. The MUSL operates the Powerball game as well as Hot Lotto and is a member of the Mega Millions group offering the Mega Millions game. Participating lotteries are required to maintain deposits with MUSL for contingency reserves to protect MUSL from unforeseen prize liabilities. The money in these reserve funds is refundable to MUSL members if the MUSL disbands or if a member leaves the MUSL Board. Vermont Powerball sales were approximately \$12.0 million for the year ended June 30, 2013 and approximately \$9.6 million for the year ended June 30, 2012. In July 2009, Vermont began offering Vermont Hot Lotto with the Sizzler feature, both with a calculated prize expense of 50% of ticket sales. Vermont Hot Lotto sales were approximately \$1.0 million for the year ended June 30, 2013 and \$1.1 million for the year ended June 30, 2012. In January 2010, Vermont began offering Vermont Mega Millions with the Megaplier feature, both with a calculated prize expense currently at no more than 51.5% of ticket sales. Vermont Mega Millions sales were approximately \$2.8 million for the year ended June 30, 2013 and \$4.7 million for the year ended June 30, 2012. On behalf of the Lottery, the MUSL held in trust prize reserve accounts for Powerball, Hot Lotto and Mega Millions totaling \$627,113 for the fiscal year ended June 30, 2013 and \$614,226 for the fiscal year ended June 30, 2012. The MUSL annual financial report may be obtained by writing to the Multi-State Lottery Association, 4400 N.W. Urbandale Drive, Urbandale, Iowa 50322-7919.

In April 2011, Tri-State replaced Weekly Grand with Weekly Grand Extra. In March 2012, Tri-State ended the Weekly Grand Extra game; it was not replaced with another Tri-State game until Gimme 5 was launched in May 2013. The sales of Gimme 5 in Vermont were approximately \$142,000 for the year ended June 30, 2013 with calculated prize expense of 53%. The sales of Weekly Grand Extra in Vermont were approximately \$1.0 million for the year ended June 30, 2012.

**VERMONT LOTTERY COMMISSION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013 AND 2012**

10. Prize expense and reserve for future and unclaimed prizes (continued):

In March 2012, the states of Vermont, Maine, New Hampshire, Connecticut, Massachusetts and Rhode Island instituted Lucky for Life, with a calculated prize expense of 60% of ticket sales. Lucky for Life ticket sales in Vermont were approximately \$2.6 million for the year ended June 30, 2013, and \$1.0 million for the year ended June 30, 2012.

11. Deferred revenue:

Deferred revenue consists of subscription receipts for Megabucks Plus, Powerball, Hot Lotto and Mega Millions games, advance tickets sold for the Powerball, Hot Lotto, Mega Millions, and Lucky for Life games and refundable terminal deposits for new agents. The sales revenue will be recognized as the drawings are held and the terminal deposits are refundable after one year.

12. Net position:

Net position invested in capital assets of \$11,132 includes furniture, equipment and leasehold improvements net of depreciation. Unrestricted net position at June 30, 2013 includes net position reserved for inventory of \$491,288 and for unrealized gains on investments held for the purpose of paying long-term installment prizes due to winners of \$252,542. These reserves are consistent with the provision for apportionment of Lottery revenues in Title 31, Chapter 14, §654(11)(A) & (B).

13. Appropriations:

The following are the cash basis appropriations compared to expenses at June 30, 2013 and 2012:

	<u>2013</u>	<u>2012</u>
Appropriation	\$ 3,084,193	\$ 2,892,961
Expenses	<u>2,927,445</u>	<u>2,869,970</u>
Variance	<u>\$ 156,748</u>	<u>\$ 22,991</u>

At June 30, 2013, \$156,597 was encumbered for personal services and advertising. At June 30, 2012, \$46,584 was encumbered for personal services.

14. Retirement plan:

The Vermont State Retirement System (VSRS), a defined benefit plan, covers substantially all Lottery employees except employees hired in a temporary capacity. Membership in the system is a condition of employment. The membership consists of employees who belong to the original contributory system with a contribution range of 6.4% to 8.28% of payroll (Groups A, C and D), vested members of the non-contributory system (Group E) as well as members of a new contributory system whose current contribution rate is 6.40% (Group F). All eligible employees of the Lottery are Group F members. The total amount of employer contributions was \$164,418 and \$153,767 for the fiscal years ended June 30, 2013 and June 30, 2012, respectively. The Lottery's payroll for all employees totaled \$998,799 and \$954,978 for the fiscal years ended June 30, 2013 and June 30, 2012, respectively, all of which is covered payroll for the plan. Funding and benefit information for this plan is maintained in the aggregate, not by Agency or Commission. Additional information regarding this plan is available upon request from the State of Vermont.

**VERMONT LOTTERY COMMISSION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013 AND 2012**

15. Deferred compensation:

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

In compliance with Federal mandates, the Vermont State Retirement Board adopted a Plan Trust Declaration for the State of Vermont's Deferred Compensation Plan effective January 1, 1999. The Federal mandate was established to protect the assets of deferred compensation plans by requiring the assets be placed in a trust to be used for the sole purpose of plan participants. After January 1, 1999, the plan assets are no longer considered assets of the State of Vermont.

16. Concentrations:

The Lottery utilized Intralot, Inc., a service organization, to process all of its online games and generate the accounting reports the Lottery used to record this activity in FY 2013. The Lottery also utilized Intralot to validate and settle its instant ticket lottery games. The Lottery utilized Scientific Games International (SGI) to print its instant games. Other service providers are available; however, an interruption in service by Intralot or SGI could have an adverse impact on the Lottery's revenues.

17. Commitments:

The State of Vermont entered into an agreement on behalf of the Lottery for office space. The lease commenced September 1, 2004 for ten years. The lease provides for annual rent of \$129,675 for the first five years and \$142,576 for the remaining five years through August 31, 2014. The annual rent was \$142,576 for the years ended June 30, 2013 and 2012.

The Lottery has a three-year agreement with Scientific Games International to print instant game tickets through January 16, 2014. The total cost of the contract is not to exceed \$7 million.

The Lottery is contracted with Intralot, Inc. to provide for the operation of an online gaming system through June 30, 2016. The estimated total contract price is approximately \$25 million over the six-year contract.

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL
REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN
AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE
WITH *GOVERNMENT AUDITING STANDARDS***

The Commissioners
Vermont Lottery Commission

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the Vermont Lottery Commission (the Lottery), an enterprise fund of the State of Vermont, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Lottery's basic financial statements, and have issued our report thereon dated October 8, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Lottery's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Lottery's internal control. Accordingly, we do not express an opinion on the effectiveness of the Lottery's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Lottery's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering for the entity's internal control and compliance. Accordingly, this report is not suitable for any other purpose.

Montpelier, Vermont
October 8, 2013

*Mudgett, Jennett &
Krogh-Wisner, P.C.*