



ANNUAL REPORT

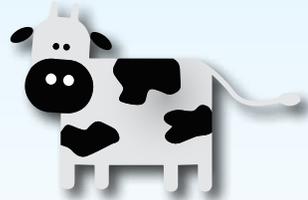
Fiscal Year 2014



All Profits Benefit the Vermont Education Fund



vtlottery.com





Greg Smith,
Executive Director

The Vermont Lottery connects with our customers in various ways, using our marketing and promotion methods and tracking how our customers respond to us. What had been accomplished in prior years by Instant tickets and jackpot signs in stores has expanded into television and radio ads, websites and social media communication, player accounts and 2nd Chance drawings.

All of this is done with the intent of attracting new players, and keeping current players who play for fun and the hope of winning some money. Getting and staying engaged with your customers is easy to say, but quite a multi-tasking challenge to do well.

In a year that saw only one large jackpot run (\$600 million) and a few medium sized ones (\$300 million), we used good advertisements played on TV, radio and YouTube, supported by social media postings and 2nd Chance contests, to help increase the sales of Instant ticket games. We were spoiled in the prior year with three record-breaking jackpots, so a normal year like this one caused us to shift our focus back to our strongest product line – Instant tickets. We have seen, and players have told us, that reliable wins that improve their month or their year are much more realistic than hoping to win many millions of dollars. But remember, somebody always wins.

I am always surprised when someone asks me where Lottery profits go, or “Do we really send all of our profits to the Education Fund?” Yes, 100% of all Vermont Lottery profits go to the Education Fund. The Lottery staff is focused on responsible growth of revenues through our marketing and sales efforts coupled with accuracy and integrity applied to each transaction. Through these efforts, we work to maintain and grow the sales of Lottery products and the resulting profits.

We will continue to explore new games, new places to play lottery games, and new ways to engage with customers. And while we do this, we will remain mindful that some Vermonters have trouble controlling their gambling habits or addiction. The Vermont Lottery is the sole source of funding for the problem gambling services offered in the state and we monitor the quality of those services to ensure help is available to those who need it.

Martha H. O'Connor, Chair

Greg Smith, Executive Director

Commissioners



Martha O'Connor
Chair
Brattleboro
Term Expires
02/17



Karen O'Hagan
Winooski
Term Expires
02/17



Ed Flanagan
Tri-State
Commissioner
11/14
Montpelier
Term Expires
02/16



Virginia Barry
Vice Chair
Barre
Term Expires
02/15



Tom Scala
Tri-State
Commissioner
Brattleboro
Resigned
10/14

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 FY14.

Products

In FY14, the Vermont Lottery offered ten games for sale: Instant tickets, Powerball, Mega Millions, Hot Lotto, Lucky For Life; the Tri-State games Megabucks, Fast Play, Pick 3, Pick 4, and 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 FY14, 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 FY14, the commissions and bonuses paid to agents totaled \$6 million.

Responsible Gaming

The Vermont Lottery continued its close partnership with the Vermont Council on Problem Gambling (VCPG) so we can provide assistance to Vermonters who need help managing their focus on gambling. We also provided training to the counselors who offer these services throughout Vermont.

The funding provided by the Lottery pays for staffing the 24-hour helpline, website maintenance, training for counselors, literature and event sponsorships. We also create, produce and air TV and radio advertisements all year long. And we will continue to list the helpline number and website address on over 20 million lottery tickets sold each year.

We encourage everyone who knows somebody struggling with a gambling problem to have them call the toll free number or visit the website so they can get on the road to recovery.

Results of Operations

FY14 ended with overall revenue of \$102,311,700. The total profit contributed to the state's Education Fund was \$22.6 million. In addition to the profits to the Education Fund, \$65 million was returned to players in the form of prizes, and \$6.1 million was paid to Lottery agents as commissions and bonuses on sales.

Sales

Total FY14 sales equaled \$102,309,458. Sales by game were as follows:

| | 2014 | 2013 |
|----------------------|------------------------------|------------------------------|
| Instant games | \$ 75,972,763 | \$ 74,214,288 |
| <i>Online games:</i> | | |
| Powerball | 9,498,896 | 12,034,883 |
| Mega Millions | 3,986,661 | 2,796,901 |
| Hot Lotto | 781,827 | 991,188 |
| Lucky for Life | 2,054,307 | 2,588,726 |
| Megabucks | 3,923,082 | 4,889,349 |
| Pick 3 | 1,354,018 | 1,365,930 |
| Pick 4 | 1,198,851 | 1,254,733 |
| Raffle | 140,860 | — |
| Gimme 5 | 868,628 | 141,737 |
| Fast Play | <u>2,529,565</u> | <u>1,809,653</u> |
| Total Sales | <u>\$ 102,309,458</u> | <u>\$ 102,087,388</u> |

Operating Expenses

Administrative costs for the Lottery were \$2,985,065, a decrease of \$43,830 from FY13. Administrative costs include salaries and benefits, contracted services, equipment, and supplies that were components of the Lottery's annual operating budget appropriation from the Legislature. The budget appropriation came from Lottery revenues.

Other operating expenses, dependent on Lottery sales, included Lottery tickets, courier system, and agent network expenses and facilities management fees to our gaming vendor (Intralot, Inc.). The total cost of other operations for FY14 was \$7,498,682, an increase of \$96,760 over FY13. This includes the administrative costs of \$2,985,065 mentioned above.

Tri-State Expenses

The Tri-State operating, communications and facilities management costs totaled \$1,155,084, a decrease of \$27,913 from FY13.

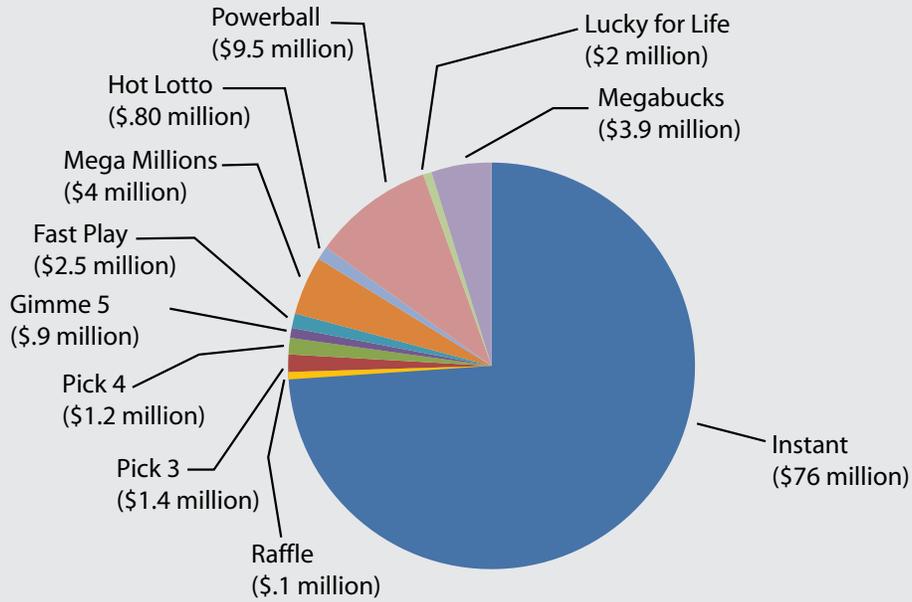
Prizes and Commissions

The total prizes paid to players in FY14 were \$65,029,356 and the total commissions and bonuses paid to agents were \$6,082,393.

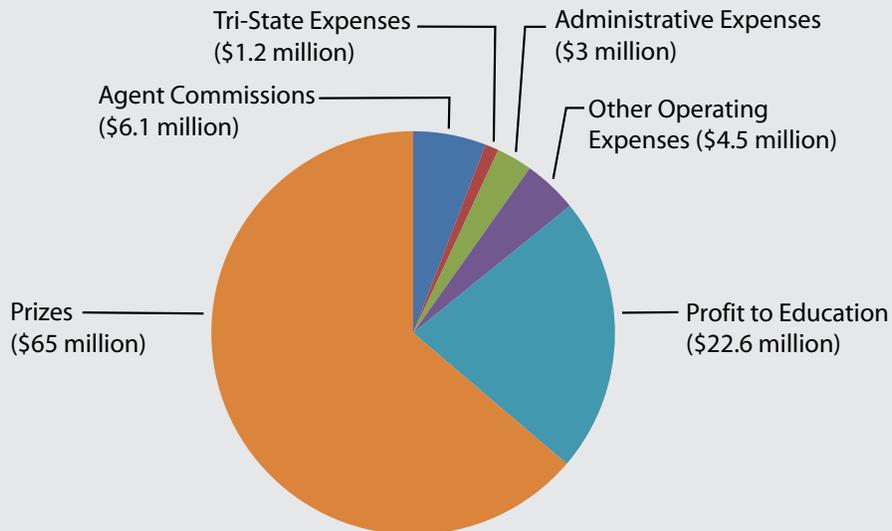
Contribution to Vermont Education Fund

Total profits contributed to the Vermont Education Fund were \$22,560,467.

Where the sales were:



Where the money went:



Vermont Lottery Commission

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

(802) 479-5686 • Fax (802) 479-4294

Email: staff@vtlottery.com

STATEMENTS OF
NET POSITION*
JUNE 30, 2014 AND 2013

| ASSETS | 2014 | 2013 |
|--|---------------------|---------------------|
| CURRENT ASSETS | | |
| Cash and cash equivalents | \$ 4,203,934 | \$ 3,784,668 |
| Accounts receivable, net | 2,070,088 | 1,843,443 |
| Due from State Education Fund | 18,567 | 8,680 |
| Inventory | 466,455 | 491,788 |
| Prepaid expenses | 4,067 | 6,569 |
| Total current assets | <u>6,763,111</u> | <u>6,135,148</u> |
| | | |
| PROPERTY AND EQUIPMENT, net | <u>5,138</u> | <u>11,132</u> |
| | | |
| OTHER ASSETS | | |
| Investments | <u>1,532,327</u> | <u>1,757,232</u> |
| Total other assets | <u>1,532,327</u> | <u>1,757,232</u> |
| Total assets | \$ <u>8,300,576</u> | \$ <u>7,903,512</u> |
| | | |
| LIABILITIES AND NET POSITION | | |
| CURRENT LIABILITIES: | | |
| Accounts payable | \$ 703,568 | \$ 542,971 |
| Accrued payroll and compensated absences | 151,577 | 134,403 |
| Reserve for future and unclaimed prizes | 4,962,633 | 4,487,653 |
| Due to winners, current | 260,362 | 254,537 |
| Deferred revenue | <u>178,876</u> | <u>178,832</u> |
| Total current liabilities | <u>6,257,016</u> | <u>5,598,396</u> |
| | | |
| NONCURRENT LIABILITIES | | |
| Due to winners, net of current portion | 1,054,567 | 1,250,154 |
| Due to State Treasurer | <u>300,000</u> | <u>300,000</u> |
| Total non-current liabilities | <u>1,354,567</u> | <u>1,550,154</u> |
| Total liabilities | <u>7,611,583</u> | <u>7,148,550</u> |
| | | |
| NET POSITION, unrestricted | <u>688,993</u> | <u>754,962</u> |
| | | |
| Total liabilities and net position | \$ <u>8,300,576</u> | \$ <u>7,903,512</u> |

STATEMENTS OF
REVENUES, EXPENSES AND CHANGES IN NET POSITION*
FOR THE YEARS ENDED JUNE 30, 2014 AND 2013

| | 2014 | 2013 |
|--|--------------------|--------------------|
| OPERATING REVENUES: | | |
| Ticket sales | \$ 102,309,458 | \$ 102,087,388 |
| Agents' license fees and other receipts | <u>2,242</u> | <u>1,256</u> |
| Total revenues | <u>102,311,700</u> | <u>102,088,644</u> |
| | | |
| OPERATING EXPENSES: | | |
| Prize expense | 65,029,357 | 64,556,404 |
| Agents commissions | 6,082,393 | 6,020,216 |
| Lottery tickets | 1,186,603 | 1,186,633 |
| Ticket dispensers | 89,954 | 46,232 |
| Courier system | 213,551 | 220,746 |
| Facilities management fee - instant | 2,494,537 | 2,398,108 |
| Facilities management fee - online | 489,978 | 548,331 |
| Tri-State expenses | 1,155,086 | 1,182,997 |
| MUSL expenses | 26,278 | 93,679 |
| Personal services | 1,537,664 | 1,475,351 |
| Advertising | 750,656 | 769,222 |
| Other operating expenses | 590,143 | 540,019 |
| Depreciation | 5,994 | 6,785 |
| Department of Health | 150,000 | 150,000 |
| Total operating expenses | <u>79,802,194</u> | <u>79,194,723</u> |
| | | |
| OPERATING INCOME | <u>22,509,506</u> | <u>22,893,921</u> |
| | | |
| NON-OPERATING EXPENSES | | |
| Investment income (loss) | (15,008) | (87,518) |
| Total non-operating (expenses) | <u>(15,008)</u> | <u>(87,518)</u> |
| | | |
| INCOME BEFORE OPERATING TRANSFERS | <u>22,494,498</u> | <u>22,806,403</u> |
| | | |
| NET PROFIT TRANSFERRED TO THE EDUCATION FUND | 22,560,467 | 22,927,105 |
| Change in net position | (65,969) | (120,702) |
| NET POSITION, beginning of year | <u>754,962</u> | <u>875,664</u> |
| NET POSITION, end of year | \$ <u>688,993</u> | \$ <u>754,962</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, 2014 and 2013

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INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS' AUDIT REPORT

To the Commissioners' of the
Vermont Lottery Commission
Barre, Vermont

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, 2014, 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 statement 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 from 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, 2014, and the changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

To the Commissioners' of the
Vermont Lottery Commission
Barre, Vermont
Page 2

Emphasis of 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, 2014, the changes in its financial position, or, where applicable, its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Other Information

The comparative information of Vermont Lottery Commission as of and for the year ended June 30, 2013 was audited by other auditors whose report dated October 8, 2013 expressed an unmodified opinion.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3–5 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 November 13, 2014, on our consideration of the Vermont Lottery Commission's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and 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 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.

Williston, Vermont
November 13, 2014

VERMONT LOTTERY COMMISSION
MANAGEMENT DISCUSSION AND ANALYSIS
June 30, 2014

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, 2014. Please read it in conjunction with the financial statements.

The Vermont Lottery Commission (the Lottery) 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 \$223,056 or 0.22%.
- Total operating expenses for the year increased by \$607,471 or 0.77%. Of this increase, prize expense increased by \$472,953 facilities management fees increased by \$38,076, agent commissions increased by \$62,177, and Tri-State expenses decreased by \$27,911.
- Nonoperating revenue in FY 2014 included an unrealized loss on investments of \$35,143. The total investment loss of \$15,008 resulted in an overall increase of \$72,510 from the non-operating loss in FY 2013.
- Income before operating transfers (net revenue) decreased by \$311,905.

Assets and Net Position

The assets of the Lottery are primarily cash and investments held for operating purposes. Total assets at June 30, 2014, of \$8,300,576 include net capital assets of \$5,138, restricted investments of \$1,532,327 and current operating assets such as cash and cash equivalents, accounts receivable, prepaid expenses and inventory of \$6,763,111. Net position retained by the Lottery was \$688,993.

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 Lottery was \$754,962.

Liabilities

The Lottery's liabilities consist of operating liabilities and obligations for payment of prizes to lottery winners. Total liabilities at June 30, 2014, of \$7,611,583 include long-term liabilities for prize obligations of \$1,054,567, cash advances from the State of \$300,000 and current operating liabilities of \$6,257,016.

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.

VERMONT LOTTERY COMMISSION
MANAGEMENT DISCUSSION AND ANALYSIS
June 30, 2014

Sales

The following shows ticket sales by game:

| | <u>2014</u> | <u>2013</u> |
|---------------------------|-----------------------|-----------------------|
| Instant scratch off games | \$ 75,972,763 | \$ 74,214,288 |
| Online Games: | | |
| Powerball | 9,498,896 | 12,034,883 |
| Mega Millions | 3,986,661 | 2,796,901 |
| Hot Lotto | 781,827 | 991,188 |
| Lucky for Life | 2,054,307 | 2,588,726 |
| Megabucks Plus | 3,923,082 | 4,889,349 |
| Pick 3 | 1,354,018 | 1,365,930 |
| Pick 4 | 1,198,851 | 1,254,733 |
| Raffle | 140,860 | - |
| Gimme 5 | 868,628 | 141,737 |
| Fast Play | <u>2,529,565</u> | <u>1,809,653</u> |
| Total sales | <u>\$ 102,309,458</u> | <u>\$ 102,087,388</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 Lottery 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>2014</u> | <u>2013</u> |
|---|----------------------|----------------------|
| Prize expense - Instant scratch off games | \$ 51,345,395 | \$ 50,157,540 |
| Prize expense - Online games | <u>13,683,962</u> | <u>14,398,864</u> |
| | <u>\$ 65,029,357</u> | <u>\$ 64,556,404</u> |

VERMONT LOTTERY COMMISSION

MANAGEMENT DISCUSSION AND ANALYSIS

June 30, 2014

Other Potentially Significant Factors

Operating results for 2014 were not improved over 2013. The overall improvement in sales was offset by the increased cost of sales. Much of the increased sales were in Instant Scratch games and the Fast Play games which had prize payouts that were higher than online games. The increased sales in these games were the result of strategic planning and the offering of new progressive style Fast Play. Other games that had increased sales were Mega Millions, the result of large jackpot rolls, and a full year this year of the newest Tri-State game, Gimme 5, were all factors in the improved sales for fiscal year 2014.

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, 2014 and 2013

| | <u>2014</u> | <u>2013</u> |
|--|---------------------|---------------------|
| ASSETS | | |
| CURRENT ASSETS | | |
| Cash and cash equivalents | \$ 4,203,934 | \$ 3,784,668 |
| Accounts receivable, net | 2,070,088 | 1,843,443 |
| Due from the State Education Fund | 18,567 | 8,680 |
| Inventory | 466,455 | 491,788 |
| Prepaid expenses | <u>4,067</u> | <u>6,569</u> |
| Total current assets | <u>6,763,111</u> | <u>6,135,148</u> |
| PROPERTY AND EQUIPMENT, net | <u>5,138</u> | <u>11,132</u> |
| OTHER ASSETS | | |
| Investments | <u>1,532,327</u> | <u>1,757,232</u> |
| Total other assets | <u>1,532,327</u> | <u>1,757,232</u> |
| Total assets | <u>\$ 8,300,576</u> | <u>\$ 7,903,512</u> |
| LIABILITIES AND NET POSITION | | |
| CURRENT LIABILITIES | | |
| Accounts payable | \$ 703,568 | \$ 542,971 |
| Accrued payroll and compensated absences | 151,577 | 134,403 |
| Reserve for future and unclaimed prizes | 4,962,633 | 4,487,653 |
| Due to winners, current | 260,362 | 254,537 |
| Deferred revenue | <u>178,876</u> | <u>178,832</u> |
| Total current liabilities | <u>6,257,016</u> | <u>5,598,396</u> |
| NONCURRENT LIABILITIES | | |
| Due to winners, net of current portion | 1,054,567 | 1,250,154 |
| Due to state treasurer | <u>300,000</u> | <u>300,000</u> |
| Total noncurrent liabilities | <u>1,354,567</u> | <u>1,550,154</u> |
| Total liabilities | 7,611,583 | 7,148,550 |
| NET POSITION, unrestricted | <u>688,993</u> | <u>754,962</u> |
| Total liabilities and net position | <u>\$ 8,300,576</u> | <u>\$ 7,903,512</u> |

See Independent Certified Public Accountants' Audit Report and Notes to Financial Statements.

VERMONT LOTTERY COMMISSION

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
For the Years Ended June 30, 2014 and 2013

| | <u>2014</u> | <u>2013</u> |
|--|--------------------|--------------------|
| OPERATING REVENUES | | |
| Ticket sales | \$ 102,309,458 | \$ 102,087,388 |
| Agents' license fees and other receipts | <u>2,242</u> | <u>1,256</u> |
| Total revenues | <u>102,311,700</u> | <u>102,088,644</u> |
| OPERATING EXPENSES | | |
| Prize expenses | 65,029,357 | 64,556,404 |
| Agents commissions | 6,082,393 | 6,020,216 |
| Lottery tickets | 1,186,603 | 1,186,633 |
| Ticket dispensers | 89,954 | 46,232 |
| Courier system | 213,551 | 220,746 |
| Facilities management fee - instant | 2,494,537 | 2,398,108 |
| Facilities management fee - online | 489,978 | 548,331 |
| Tri-State expenses | 1,155,086 | 1,182,997 |
| MUSL expenses | 26,278 | 93,679 |
| Personal services | 1,537,664 | 1,475,351 |
| Advertising | 750,656 | 769,222 |
| Other operating expenses | 590,143 | 540,019 |
| Depreciation | 5,994 | 6,785 |
| Department of Health | <u>150,000</u> | <u>150,000</u> |
| Total operating expenses | <u>79,802,194</u> | <u>79,194,723</u> |
| OPERATING INCOME | <u>22,509,506</u> | <u>22,893,921</u> |
| NON-OPERATING EXPENSES | | |
| Investment income (loss) | <u>(15,008)</u> | <u>(87,518)</u> |
| Total non-operating expenses | <u>(15,008)</u> | <u>(87,518)</u> |
| INCOME BEFORE OPERATING TRANSFERS | <u>22,494,498</u> | <u>22,806,403</u> |
| NET PROFIT TRANSFERRED TO THE EDUCATION FUND | 22,560,467 | 22,927,105 |
| Change in net position | (65,969) | (120,702) |
| NET POSITION, beginning of year | <u>754,962</u> | <u>875,664</u> |
| NET POSITION, end of year | <u>\$ 688,993</u> | <u>\$ 754,962</u> |

See Independent Certified Public Accountants' Audit Report and Notes to Financial Statements.

VERMONT LOTTERY COMMISSION
STATEMENTS OF CASH FLOWS
For the Years Ended June 30, 2014 and 2013

| | <u>2014</u> | <u>2013</u> |
|--|----------------------|----------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Cash received from customers | \$ 102,085,360 | \$ 102,080,861 |
| Cash paid for prizes and agents' commissions | (70,801,199) | (70,053,980) |
| Cash paid for management fees, operations, and other | (6,986,189) | (7,498,678) |
| Cash paid to employees for services | (1,520,491) | (1,490,301) |
| Other operating revenue | <u>2,242</u> | <u>1,256</u> |
| Net cash provided by operating activities | <u>22,779,723</u> | <u>23,039,158</u> |
| CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES | | |
| Operating transfers | <u>(22,570,354)</u> | <u>(22,935,785)</u> |
| Net cash used by noncapital financing activities | <u>(22,570,354)</u> | <u>(22,935,785)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Unrealized gains (losses) on investments | 20,135 | (51,687) |
| Proceeds from maturities of investments, net | <u>189,762</u> | <u>252,261</u> |
| Net cash provided by investing activities | <u>209,897</u> | <u>200,574</u> |
| Net change in cash and cash equivalents | 419,266 | 303,947 |
| Cash and cash equivalents, beginning of year | <u>3,784,668</u> | <u>3,480,721</u> |
| Cash and cash equivalents, end of year | <u>\$ 4,203,934</u> | <u>\$ 3,784,668</u> |
| RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES | | |
| Operating income | \$ 22,509,506 | \$ 22,893,921 |
| Adjustments to reconcile changes in net assets to net cash provided by operating activities: | | |
| Depreciation | 5,994 | 6,785 |
| Changes in: | | |
| Accounts receivable | (226,645) | (22,072) |
| Inventory | 25,333 | 6,043 |
| Prepaid expenses | 2,502 | (750) |
| Accounts payable | 160,597 | (362,711) |
| Accrued payroll and other expenses | 17,173 | (14,950) |
| Due to winners | (189,762) | (179,467) |
| Reserve for future and unclaimed prizes | 474,980 | 696,064 |
| Deferred revenue | <u>45</u> | <u>16,295</u> |
| Total adjustments | <u>270,217</u> | <u>145,237</u> |
| Net cash provided by operating activities | <u>\$ 22,779,723</u> | <u>\$ 23,039,158</u> |

See Independent Certified Public Accountants' Audit Report and Notes to Financial Statements.

VERMONT LOTTERY COMMISSION

NOTES TO FINANCIAL STATEMENTS

June 30, 2014 and 2013

Note 1. Nature of Operations and Summary of Significant Accounting Policies

Nature of operations

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 summary of the Corporation's significant accounting policies follows:

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.

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.

VERMONT LOTTERY COMMISSION

NOTES TO FINANCIAL STATEMENTS

June 30, 2014 and 2013

Note 1. Nature of Operations and Summary of Significant Accounting Policies (continued)

Basis of accounting (continued)

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.

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.

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.

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.

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).

VERMONT LOTTERY COMMISSION

NOTES TO FINANCIAL STATEMENTS

June 30, 2014 and 2013

Note 1. Nature of Operations and Summary of Significant Accounting Policies (continued)

Fair value measurements

Professional literature defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The guidance states that fair value is a market-based measurement, not an entity-specific measurement.

Therefore, a fair value measurement should be determined based on the assumptions market participants would use in pricing the asset or liability under current market conditions at the measurement date. As a basis for considering market participant assumptions in fair value measurements, the guidance establishes a fair value hierarchy that is based on the subjectivity of inputs.

It distinguishes between observable inputs (Levels 1 and 2) which are either observable from market data or corroborated by observable market data and those that are unobservable (Level 3).

Three levels of inputs that may be used to measure fair value are as follows:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities. Level 1 assets and liabilities include debt and equity securities that are traded in an active exchange market.

Level 2 – Inputs other than quoted prices included in Level 1 that are observable, either directly or indirectly. Such inputs may include quoted prices for similar assets, observable inputs include quoted prices (interest rates, yield curves, etc.) or inputs derived principally from or corroborated by observable market data by correlation or other means. This category generally includes certain U.S. Government and agency mortgage-backed debt securities and alternative investments using net asset value (NAV) per share for which the Organization has the ability to redeem its investment at or close to the measurement date.

Level 3 – Inputs are unobservable data points for the asset or liability, and include situations where there is little, if any, market activity for the asset or liability. The inputs reflect the Organization's assumptions based on the best information available in the circumstances. This category generally includes certain private debt and equity instruments, alternative investments where the investee at NAV per share or the redemption date is not close to the measurement date. This category also includes investments held in trust where the Organization is not the trustee and the beneficial interest is in perpetual trust.

All long-term investments (see Note 4.) have been valued in accordance with the definition of Level 1 inputs as described above.

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair value.

Furthermore, although the Lottery's management believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

VERMONT LOTTERY COMMISSION

NOTES TO FINANCIAL STATEMENTS

June 30, 2014 and 2013

Note 1. Nature of Operations and Summary of Significant Accounting Policies (continued)

Allowance for doubtful accounts

It is the policy of management to review the outstanding receivables at year end, as well as the bad debt write off experienced in the past, and establish an allowance for doubtful accounts for uncollectable amounts. Based on management's estimates, \$63,414 and \$62,577 was recorded as an allowance for doubtful accounts at June 30, 2014 and 2013, respectively.

Inventory

Inventory consists of lottery tickets on hand and prizes. Inventory is valued at the lower of cost or market using the first-in, first-out method.

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 |

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.

Advertising

Advertising costs are expensed as incurred.

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> |
|--------------------------------|--------------------------------|
| Keyport Life Insurance Company | November 14, 2014 |
| Keyport Life Insurance Company | December 15, 2014 |

VERMONT LOTTERY COMMISSION
NOTES TO FINANCIAL STATEMENTS
June 30, 2014 and 2013

Note 1. Nature of Operations and Summary of Significant Accounting Policies (continued)

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.

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.

Reclassifications

Certain amounts for the year ended June 30, 2013, have been reclassified for comparative purposes to conform to the presentation used in the June 30, 2014 financial statements. The reclassifications have no effect on total net position for the year ended June 30, 2013.

Subsequent Events

Subsequent events have been evaluated through November 13, 2014, which is the date the financial statements were issued.

Note 2. Cash and cash equivalents

Custodial credit risk on 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, 2014, all of the Lottery's bank balance of \$2,194,113 was insured or collateralized. As of June 30, 2013, all of the Lottery's bank balance of \$5,425,268 was insured or collateralized. Collateralized amounts are held by the pledging bank's trust department in the Lottery's name.

Cash with the 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.

VERMONT LOTTERY COMMISSION

NOTES TO FINANCIAL STATEMENTS

June 30, 2014 and 2013

Note 3. Accounts Receivable

Accounts receivable consisted of the following at June 30:

| | <u>2014</u> | <u>2013</u> |
|--------------------------------------|---------------------|---------------------|
| MUSL | \$ 789,063 | \$ 901,692 |
| Tri-State | 164,606 | 58,718 |
| Intralot | 70,000 | -- |
| Regular Agents | 876,928 | 755,001 |
| Chain Agents | <u>232,905</u> | <u>190,609</u> |
| Total accounts receivable | 2,133,502 | 1,906,020 |
| Less allowance for doubtful accounts | <u>(63,414)</u> | <u>(62,577)</u> |
| Accounts receivable, net | <u>\$ 2,070,088</u> | <u>\$ 1,843,443</u> |

Note 4. Investments

Investments consisted of the following at June 30:

| | <u>2014</u> | <u>2013</u> |
|----------------------|---------------------|---------------------|
| U.S. Treasury Strips | \$ 1,438,629 | \$ 1,575,740 |
| Annuity Contracts | <u>93,698</u> | <u>181,492</u> |
| Total investments | <u>\$ 1,532,327</u> | <u>\$ 1,757,232</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.). These contracts are unrated.

Investments as of June 30, 2014 and 2013 were \$1,532,327 and \$1,757,232, respectively.

VERMONT LOTTERY COMMISSION

NOTES TO FINANCIAL STATEMENTS

June 30, 2014 and 2013

Note 5. Inventory

Inventory consisted of the following at June 30:

| | <u>2014</u> | <u>2013</u> |
|-----------------|-------------------|-------------------|
| Tickets on hand | \$ 466,455 | \$ 491,288 |
| Prizes | -- | 500 |
| | <u>\$ 466,455</u> | <u>\$ 490,788</u> |

Note 6. Property and Equipment

The following is a summary of the changes in property and equipment over the fiscal years:

| | <u>Balance July 1, 2013</u> | <u>Balance June 30, 2014</u> | <u>Accumulated Depreciation</u> | <u>Net Property & Equipment June 30, 2014</u> |
|----------------------|---------------------------------|----------------------------------|-------------------------------------|---|
| Computer equipment | \$ 5,584 | \$ 5,584 | \$ 5,584 | \$ -- |
| Furniture & fixtures | 56,114 | 56,114 | 56,027 | 87 |
| Other equipment | 130,754 | 130,754 | 130,754 | -- |
| Leasehold improv. | 59,935 | 59,935 | 54,884 | 5,051 |
| Total | <u>\$ 252,387</u> | <u>\$ 252,387</u> | <u>\$ 247,249</u> | <u>\$ 5,138</u> |
| | <u>Balance July 1, 2012</u> | <u>Balance June 30, 2013</u> | <u>Accumulated Depreciation</u> | <u>Net Property & Equipment June 30, 2013</u> |
| Computer equipment | \$ 5,584 | \$ 5,584 | \$ 5,584 | \$ -- |
| Furniture & fixtures | 56,114 | 56,114 | 55,327 | 787 |
| Other equipment | 130,754 | 130,754 | 130,754 | -- |
| Leasehold improv. | 59,935 | 59,935 | 49,590 | 10,345 |
| Total | <u>\$ 252,387</u> | <u>\$ 252,387</u> | <u>\$ 241,255</u> | <u>\$ 11,132</u> |

VERMONT LOTTERY COMMISSION
NOTES TO FINANCIAL STATEMENTS
June 30, 2014 and 2013

Note 7. Accounts Payable

Accounts payable consisted of the following at June 30:

| | <u>2014</u> | <u>2013</u> |
|------------------------|-------------------|-------------------|
| Tri-State | \$ 65,191 | \$ 58,447 |
| MUSL | 81,769 | 46,704 |
| Vendors | <u>556,608</u> | <u>437,820</u> |
| Total accounts payable | <u>\$ 703,568</u> | <u>\$ 542,971</u> |

Note 8. Due to Winners

The following is a summary of requirements to maturity for long-term installment prizes due to winners awarded as of June 30, 2014 and payable through the year 2033:

| | <u>Principal</u> | <u>Interest</u> | <u>Total</u> |
|--------------------------------|---------------------|-------------------|---------------------|
| Current Portion: | | | |
| For the year ending June 30, | | | |
| 2015 | <u>\$ 260,362</u> | <u>\$ 9,638</u> | <u>\$ 270,000</u> |
| Long-Term Portion: | | | |
| For the year ending June 30, | | | |
| 2016 | 157,509 | 12,491 | 170,000 |
| 2017 | 148,618 | 21,382 | 170,000 |
| 2018 | 98,380 | 21,620 | 120,000 |
| 2019 | 92,830 | 27,170 | 120,000 |
| 2020 | 87,397 | 32,603 | 120,000 |
| 2021 - 2025 | 305,987 | 174,013 | 480,000 |
| 2026 - 2030 | 108,572 | 91,428 | 200,000 |
| 2031 - 2033 | 55,274 | 64,726 | 120,000 |
| Total long-term portion | <u>1,054,567</u> | <u>445,433</u> | <u>1,500,000</u> |
| Total requirements to maturity | <u>\$ 1,314,929</u> | <u>\$ 455,071</u> | <u>\$ 1,770,000</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).

Note 9. 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.

VERMONT LOTTERY COMMISSION

NOTES TO FINANCIAL STATEMENTS

June 30, 2014 and 2013

Note 9. Prize Expense and Reserve for Future and Unclaimed Prizes (continued)

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, 2014 and 2013.

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 \$3.9 million for the year ended June 30, 2014 and \$4.9 million for the year ended June 30, 2013.

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 \$2.5 million for the year ended June 30, 2014 and \$2.6 million for the year ended June 30, 2013.

The Tri-State Lotto Commission's net position for the years ending June 30, 2014 and 2013 were \$9,771,309 and \$11,152,660, respectively. Of these amounts, \$4,345,585 represented designated prize reserves for each year and \$5,425,724 and \$6,807,075 represented unrealized gains on investments held for installment prize obligations for the years ended June 30, 2014 and 2013, 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 \$9.5 million for the year ended June 30, 2014 and approximately \$12.0 million for the year ended June 30, 2013. 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 \$0.78 million for the year ended June 30, 2014 and \$1.0 million for the year ended June 30, 2013. The Vermont Lottery discontinued its offering of the Hot Lotto game in May 2014. In January 2010, Vermont began offering Vermont Mega Millions with the Megaplier feature, both with a calculated prize expense currently at no more than 50% of ticket sales. Vermont Mega Millions sales were approximately \$3.9 million for the year ended June 30, 2014 and \$2.8 million for the year ended June 30, 2013. On behalf of the Lottery, the MUSL held in trust prize reserve accounts for Powerball, Hot Lotto and Mega Millions totaling \$566,462 for the fiscal year ended June 30, 2014 and \$627,113 for the fiscal year ended June 30, 2013. 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.

VERMONT LOTTERY COMMISSION

NOTES TO FINANCIAL STATEMENTS

June 30, 2014 and 2013

Note 9. Prize Expense and Reserve for Future and Unclaimed Prizes (continued)

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 with a calculated prize expense of 53%. Gimme 5 sales in Vermont were approximately \$868,000 for the year ended June 30, 2014 and \$142,000 for the year ended June 30, 2013.

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 \$2.1 million for the year ended June 30, 2014, and \$2.6 million for the year ended June 30, 2013.

Note 10. Deferred Revenue

Deferred revenue consists of subscription receipts for Megabucks Plus, Powerball and Mega Millions games, advance tickets sold for the Powerball, 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.

Note 11. Net Position

Net position invested in capital assets of \$5,138 includes furniture, equipment and leasehold improvements net of depreciation. Unrestricted net position at June 30, 2014 includes net position reserved for inventory of \$466,455 and for unrealized gains on investments held for the purpose of paying long-term installment prizes due to winners of \$217,399. These reserves are consistent with the provision for apportionment of Lottery revenues in Title 31, Chapter 14, §654(11)(A) & (B).

Note 12. Appropriations

The following are the cash basis appropriations compared to expenses at June 30:

| | <u>2014</u> | <u>2013</u> |
|---------------|-------------------|-------------------|
| Appropriation | \$ 3,188,165 | \$ 3,037,609 |
| Expenses | <u>2,947,081</u> | <u>2,927,455</u> |
| | <u>\$ 241,084</u> | <u>\$ 110,154</u> |

At June 30, 2014, \$42,485 was encumbered for personal services and equipment. At June 30, 2013, \$156,597 was encumbered for personal services and advertising.

Note 13. 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.

VERMONT LOTTERY COMMISSION

NOTES TO FINANCIAL STATEMENTS

June 30, 2014 and 2013

Note 13. Retirement Plan (continued)

The total amount of employer contributions was \$164,006 and \$164,418 for the fiscal years ended June 30, 2014 and June 30, 2013, respectively. The Lottery's payroll for all employees totaled \$1,007,852 and \$998,799 for the fiscal years ended June 30, 2014 and 2013, 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.

Note 14. 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.

Note 15. 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 2014. The Lottery also utilized Intralot to validate and settle its instant ticket lottery games. The Lottery utilized Scientific Games International (SGI) for most of fiscal year 2014 to print its instant games but has subsequently changed its printing vendor to Pollard Banknote. Other service providers are available; however, an interruption in service by Intralot or Pollard Banknote could have an adverse impact on the Lottery's revenues.

Note 16. 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, 2014 and 2013. The State has the option to renew the lease for an additional five years at an annual rate of \$156,834.

The Lottery has a three-year agreement with Pollard Banknote Limited to print instant game tickets through January 15, 2017. The total cost of the contract is not to exceed \$6.3 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.

SUPPLEMENTAL INFORMATION

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

To The Commissioners of
The Vermont Lottery Commission
Barre, Vermont

We have audited, in accordance with the 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, 2014, and the related notes to the financial statements, which collectively comprise the Lottery's basic financial statements, and have issued our report thereon dated November 13, 2014.

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 opinions 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 a 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*.

To the Board of Directors of
Vermont Lottery Commission
Barre, Vermont
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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 the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Williston, Vermont
November 13, 2014