



FY12 Annual Report



2012 Annual Report

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Dear Readers:

The Minnesota State Lottery continued its record-setting pace in fiscal year 2012. For the fifth consecutive year, ticket sales set a record, coming in at \$520 million. The money raised for the state beneficiaries also set a new record of \$123.6 million.

The sales mark of \$520 million is an increase of \$15.6 million from FY11. Scratch game sales set a new record of \$355.3 million. Sales of lotto games totaled \$164.8 million, which is up \$15.2 million over the previous year. The record \$656 million Mega Millions® jackpot that was won on March 30 contributed to this increase.

Prize payments to players were a record \$320.6 million, while the Lottery's hard-working retail partners earned a record \$31.6 million in commissions and incentives for selling lottery products. This is an average of \$10,100 per business.

Strong increases in our lotto-style games, especially \$2 Powerball® and Mega Millions, as well as continued success with scratch game sales, were the main drivers toward the sales record. These games also helped to make up the \$32 million in sales lost during the state shutdown in July 2011. We have seen sales increase each of the last five years, a feat that only a handful of U.S. lotteries can claim. This has helped us to meet our important mission of raising revenue for the state of Minnesota. The Lottery's retail partners and staff have worked tirelessly to pull off this monumental feat.

Important state programs and projects gained \$123.6 million from lottery ticket sales. Among the beneficiaries, the Environment and Natural Resources Trust Fund earned \$31 million for critical environmental projects, while the Game & Fish Fund and Natural Resources Fund each received \$12.2 million. Programs supported by the state's General Fund netted \$68.2 million.

We will continue to work hard to grow sales and maximize the contributions to state programs that benefit all Minnesotans.

Sincerely,



Ed Van Petten
Executive Director



HOW LOTTERY DOLLARS BENEFIT MINNESOTA

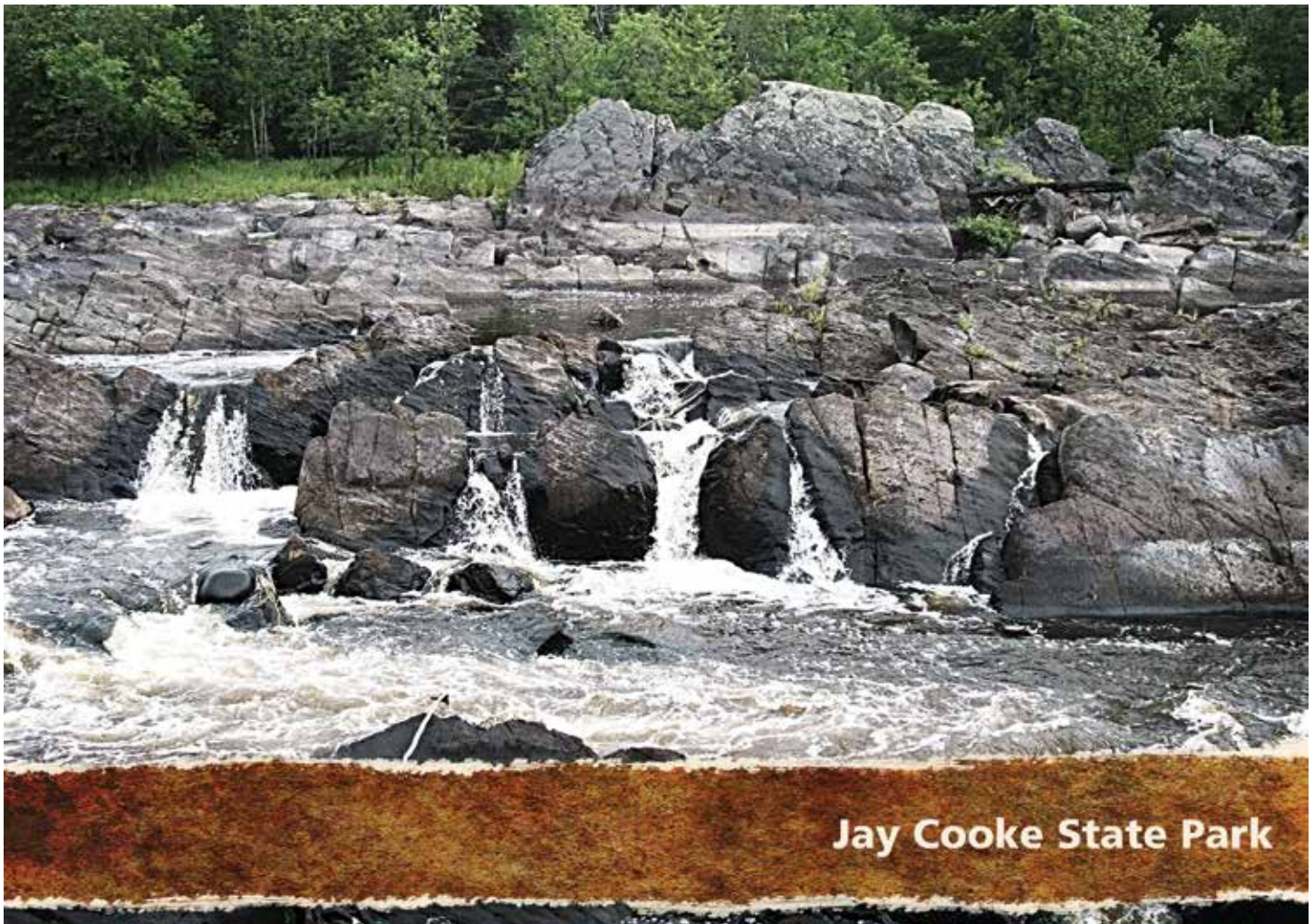
Sales of lottery products reached a record \$520 million in fiscal year 2012. This is the fifth consecutive year of record-setting sales and the second year in a row sales exceeded \$500 million.

The money raised for the state beneficiaries also set a new record of \$123.6 million.

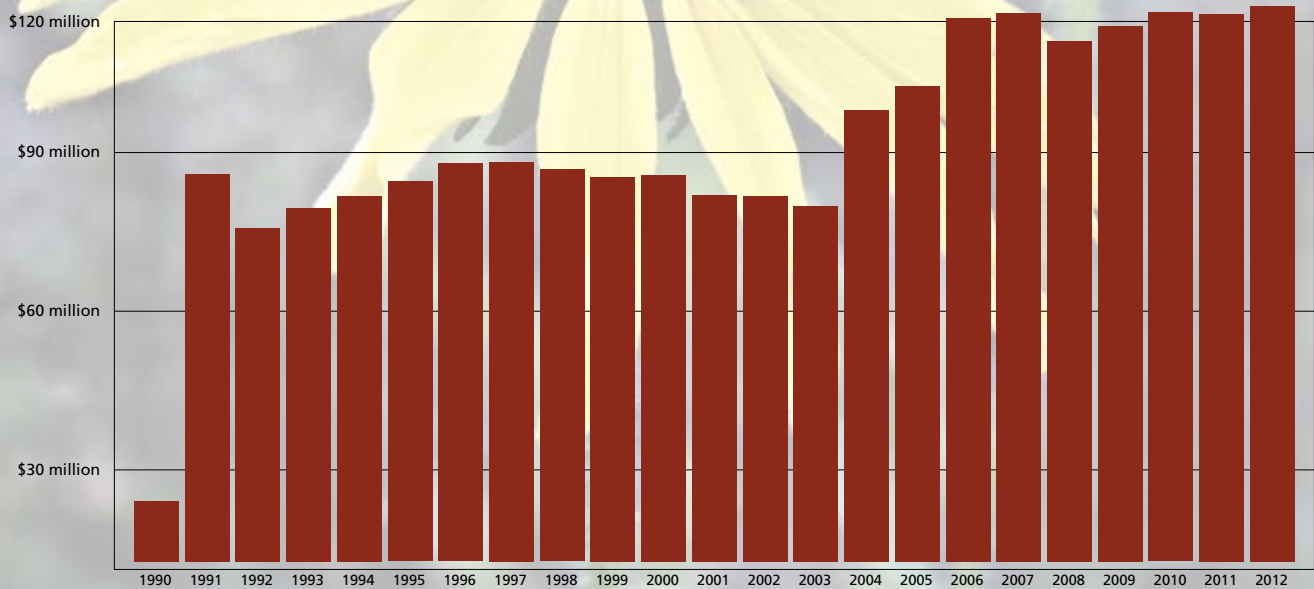
Revenues from the Lottery are divided between the state's General Fund and several environmental programs. The Minnesota Constitution requires that 40 percent of net proceeds — the amount remaining after all expenses have been paid — go to the Environment and Natural Resources Trust Fund through the year 2024. The remaining 60 percent is appropriated at the discretion of the legislature and is currently dedicated to the General Fund, including a specific appropriation to problem gambling programs.

In addition, a 6.5 percent in-lieu-of-sales tax (collected by the Lottery rather than individual retailers) on lottery tickets is also available for legislative appropriation. Under current law, these proceeds are divided between the Game and Fish Fund (36.2 percent), the Natural Resources Fund (36.2 percent) and the General Fund (27.8 percent). The Natural Resources Fund appropriation is further divided between state parks and trails (16.3 percent), metropolitan parks and trails (16.3 percent), local parks (2.2 percent), and the state's three zoos (1.4 percent).

Prizes not claimed after one year also benefit the General Fund. In fiscal year 2012, the General Fund received \$68.3 million from the Lottery (including \$2.1 million for problem gambling programs), the Environment and Natural Resources Trust Fund received \$31 million and the Game and Fish Fund and Natural Resources Fund received \$12.2 million each.



Visit mnlottery.com to learn about projects funded by the Environment & Natural Resources Trust Fund.



YEARLY LOTTERY CONTRIBUTIONS TO THE STATE OF MINNESOTA SINCE INCEPTION

GAMES & WINNERS

**MILLION
\$\$
MATCH**

Scratch games continue to be popular in Minnesota. The Lottery introduced 75 new scratch games in FY12, including Million \$\$ Match, the first \$30 ticket with a \$1 million top prize.

Rodney Hegna of Hayfield, pictured with his wife Jen, bought gasoline and a Million \$\$ Match scratch ticket. He thought "that's not possible" after he uncovered the \$1 million prize.



The artwork of Jim Hansel, one of Minnesota's premier wildlife, nature and landscape artists, was featured on the Wildlife Winnings game book. Players could also enter non-winning tickets into a drawing to win a Jim Hansel print.

Wade Kutzera of St. Joseph won \$300,000 on a Wildlife Winnings ticket.

Players had the opportunity to win one of four trips to Hollywood for the chance to play a Lottery-only edition of Wheel of Fortune® with Pat Sajak and Vanna White through the Wheel of Fortune scratch game and second-chance promotion.

Edith Bodie of Gilbert, a huge fan of Wheel of Fortune, won the opportunity to play the game with Pat Sajak. She won \$6,100 on the show.

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WHEEL of FORTUNE®

The Lottery teamed up with three Minnesota-based companies and Explore Minnesota Tourism to promote fishing within the state of Minnesota. The fishing family of games offered second-chance prizes that included two 1875 Pro-V Lund boats with a Mercury motor and trailer; \$2,500 Gander Mountain gift cards; \$500 Rapala gift cards; and Minnesota vacations.

Scratch game winners Narda Bates of St. Paul, Cathy Paquette & Valerie Weaver of Coon Rapids, Abraham Wolf of Cohasset and Julie Munson of Montrose.



Minnesota saw its jackpot winner counts increase in FY12!

Thomas and Kathleen Morris of Burnsville made Minnesota State Lottery history on Aug. 10, 2011 when they became Minnesota's 21st Powerball jackpot winners and the winners of Minnesota's largest jackpot when they won the \$228.9 million Powerball jackpot. The couple selected the cash option of \$123.6 million.

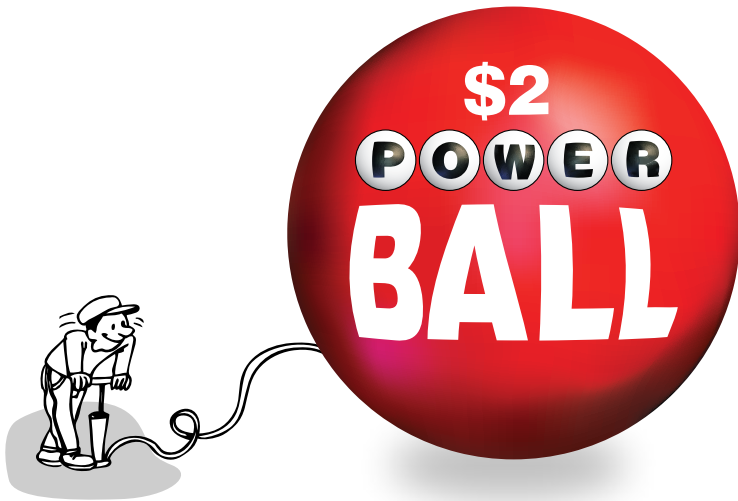
SuperAmerica, 16161 Cedar Ave. in Lakeville, received a \$50,000 bonus for selling the winning ticket. Acting Lottery Director Jenny Canfield (back row, left) presented a ceremonial check to Kirk Ellis, regional manager for SuperAmerica (front row, 2nd from left). Nick Green (back row, 4th from left) sold the winning ticket.



Two Hot Lotto® jackpots were also won in Minnesota. Don Conrad of Grand Rapids won a \$2.61 million jackpot on Jan. 14, 2012. He selected the \$1.98 million cash option. Two months to the day later, a family from North Mankato became Minnesota's tenth Hot Lotto jackpot winners when they won the \$2.99 million jackpot on March 14. They opted for the \$2.21 million cash option payment.

Minnesota's 9th and 10th Hot Lotto jackpot winners: Don Conrad and his wife Sandy and Thomas H. Browne, his son Lee Browne and his daughter Elaine Pleiss.





Mega Millions, which is a relatively new game in Minnesota, got a huge boost in March when the jackpot grew to a record \$656 million. As a result of the jackpot run (January 24, 2012 through March 30, 2012), \$5.2 million was generated for the state of Minnesota. This run, in part, helped set a new monthly sales record of \$61.6 million in March.

Russicha Deloach of New Hope won \$250,000 when the first five numbers on her ticket matched the numbers drawn!

David Froats of Vadnais Heights added the Megaplier® option to his ticket for an extra \$1; his \$10,000 prize became \$40,000!

Some enhancements were made to Powerball, the Lottery's most well-known game, in January 2012. The changes resulted in more \$1 million winners, bigger starting jackpots and better overall odds of winning a prize. The Match 5 prize was increased to \$1 million (from \$200,000); Match 5 winners who add Power Play® to their ticket automatically win \$2 million. The starting jackpot is now \$40 million, up from \$20 million. The pool of numbers the Powerball number is drawn from decreased from 39 to 35, resulting in better odds of winning the jackpot (now 1 in 175.2 million, down from 1 in 195.2 million) and better overall odds of winning a prize (from 1 in 35.1 to 1 in 31.8). The ticket price went from \$1 to \$2 to fund these bigger prizes.



Minnesota Millionaire Raffle continues to be a favorite game among Minnesota State Lottery players. All 600,000 tickets were sold in 49 days this year, a new record. Mike Snyder of Wadena was one of two lucky players to win the \$1 million top prize. He claimed the prize with his wife, Lea, at his side.

\$1 million Raffle winner Mike Snyder of Wadena, with his wife Lea, is introduced to the media at Holiday in Wadena, where he bought his winning ticket.

The Lottery's other lotto games continued to produce winners throughout the fiscal year.

Lotto game winners Sharon Strle of Britt, Benjamin Ramos of Wells, Robert "Gerb" Bruce of Sauk Centre, Gloria Banks of St. Paul and Hau Doan of New Brighton.

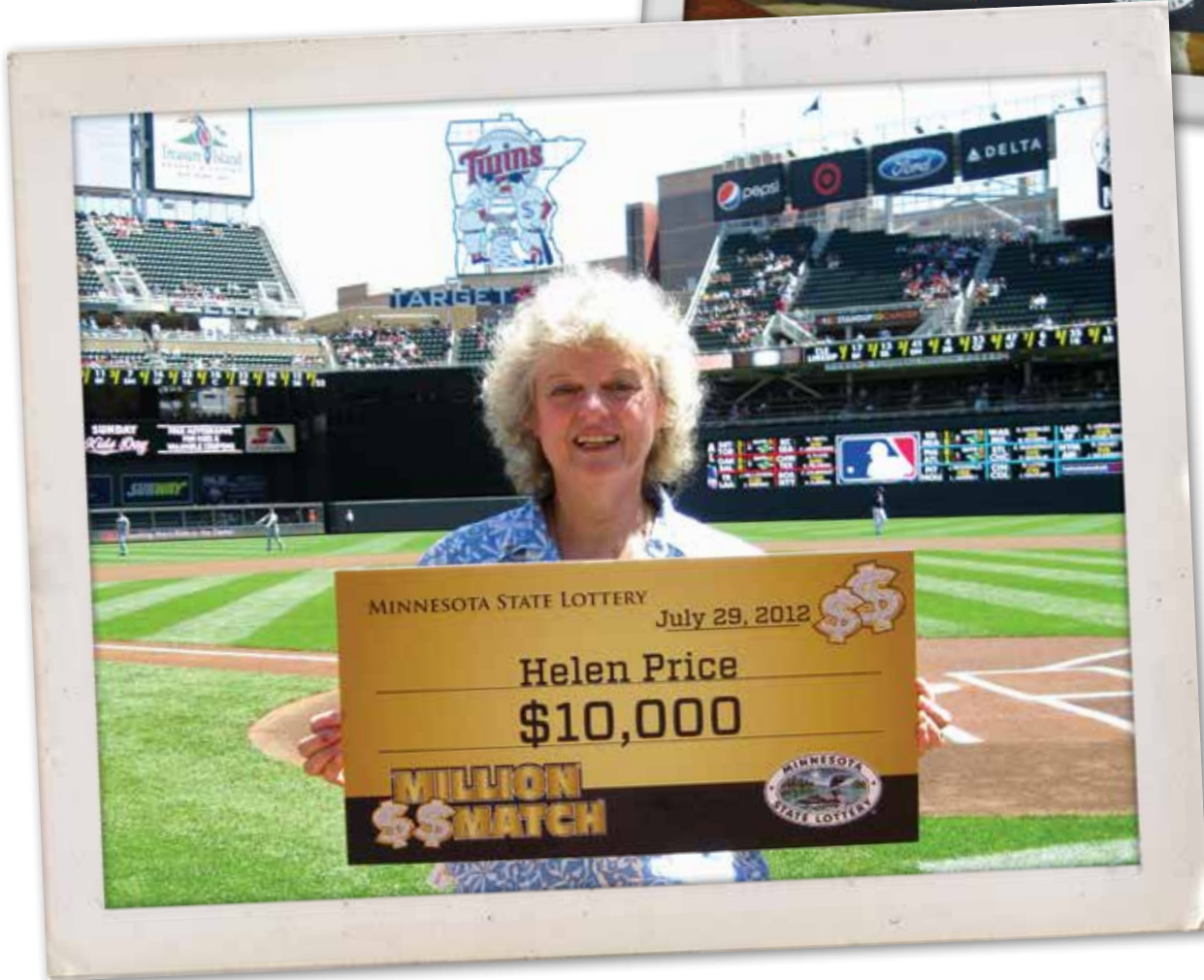
GOPHER 5



Lottery players can win cash and prizes throughout the year by entering second-chance contests. During FY12, ten players who entered non-winning Million \$\$ Match tickets on LuckyMN.com played Match 3 for the chance to win \$10,000, \$15,000, \$20,000 or \$100,000. These events were held on Twin Cities Live, at a Minnesota Twins game and during halftime at a Minnesota Timberwolves game.

Clayton Bleske of South St. Paul won \$10,000 playing Match 3 on Twin Cities Live!

Helen Price of Elk River played Match 3 at a Minnesota Twins game at Target Field and won \$10,000!





RETAILERS

More than 3,100 authorized lottery retailers, located throughout Minnesota, play a crucial role in the success of the Lottery.

Retailers receive 5.5 cents for each \$1 of ticket sales at their business, as well as 1 percent of the amount of each winning ticket cashed at their store (retailers pay prizes up to \$599). Retailers also receive a bonus for selling qualifying top prizes or jackpot-winning tickets after the prize has been claimed. Winning ticket bonuses were paid to retailers during the fiscal year ranging from \$130 to \$50,000.

In fiscal year 2012, lottery retailers earned a record \$31.6 million in commission and incentives — an average of \$10,100 per store.

TOP 10 RETAILERS IN FISCAL YEAR 2012

1. Airport Foundation, MSP Airport, St. Paul
2. M & H Gas, Moorhead
3. Orton's Moorhead Food Mart, Moorhead
4. Holiday, St. Paul (Rice St.)
5. East Grand Station, East Grand Forks
6. Rainbow Foods, Minneapolis (26th Ave. S.)
7. Cub Foods, Brooklyn Center
8. M & H Gas, St. Paul
9. Cub Foods, Maple Grove
10. Cub Foods, Crystal



COMMITMENT TO SOCIAL RESPONSIBILITY

As an agency of the state of Minnesota, the Lottery is held to a high standard. It is not only expected to raise money for good causes, but to do so with integrity and regard to the best interest of its customers and the citizens of Minnesota. The goal is to be recognized as a leader in the United States and throughout the world in the area of social responsibility.

The social responsibility programs are wide ranging, covering all aspects of the Lottery's operations. It includes the commitment to business, player protection policies and programs to help understand, prevent and treat problem gambling.

BUSINESS INTEGRITY

The Lottery strives to conduct its operations in a manner that is open, transparent and accountable. An annual independent financial audit and periodic outside audits of the Lottery's security and technology systems are completed. Lottery staff regularly communicates with the office of the governor, the legislature and other government agencies about lottery finances and operations. The Lottery's security department works closely with law enforcement agencies to vigorously investigate any allegations of wrongdoing relating to the Lottery. All lottery products are extensively tested before putting them on sale and the drawing systems are tested daily to ensure that every ticket stands an equal chance of winning.

PLAYER COMMITMENT

Lottery customers are entitled to lottery games that can be purchased with complete confidence regarding their security and integrity. To this end the Lottery has adopted a Player Commitment Statement that outlines the policies for achieving these aims. The Lottery has also initiated a retailer compliance program that ensures retailers follow the rules and regulations outlined in their contract when interacting with players and when paying winners. Additional efforts have been made to encourage players to sign tickets and self-service terminals have been introduced at many retail locations that allow players to check their own tickets.

FRAUD PROTECTION

Too many Minnesotans have been victimized by scam artists seeking to convince the vulnerable that they have won a prize in a lottery that they have not entered. To combat these fraudulent activities, the Lottery has joined with many other public agencies, non-profit organizations and private businesses in a cooperative effort to combat lottery and sweepstakes fraud.

RESPONSIBLE GAMBLING AND PROBLEM GAMBLING

For most people, playing the lottery is nothing more than an enjoyable diversion. For a few, however, lottery play can become excessive. They may play beyond their means or even develop an addiction to gambling. The Minnesota State Lottery is committed to maintaining its status as a world leader in the promotion of responsible gambling and the prevention of problem gambling. To this end the Lottery will continue to make responsible choices, including providing complete information about the odds of winning, the process of selecting winners and information about problem gambling services should the need arise.

The Minnesota State Lottery will also continue its partnerships with organizations that work to treat and prevent problem gambling, including the National Council on Problem Gambling, Northstar Problem Gambling Alliance and the Minnesota Department of Human Services. Lottery staff is also working with the World Lottery Association on the development of worldwide standards for lottery responsible gambling programs and plans to seek certification at the highest level once this program is in place. Minnesota State Lottery staff were asked to participate in several problem gambling conferences throughout North America and the Lottery has donated the resources of its advertising agency to help develop materials that aid in this effort.

In fiscal year 2012, \$2.1 million was appropriated to the Department of Human Services for problem gambling treatment and prevention, bringing the Lottery's contributions for these efforts to more than \$35 million since 1990. Lottery contributions to problem gambling are determined by the Legislature.

Visit mnlottery.com for information on problem gambling treatment and prevention.



INDEPENDENT AUDITOR'S REPORT



Schechter Dokken Kanter
Andrews & Selcer Ltd

The Director
Minnesota State Lottery
Roseville, Minnesota

Suite 1600

We have audited the accompanying balance sheets of the Minnesota State Lottery as of and for the years ended June 30, 2012 and 2011, as listed in the table of contents. These financial statements are the responsibility of the Minnesota State Lottery's management. Our responsibility is to express an opinion on these financial statements based on our audits.

100 Washington Avenue South

We conducted our audits 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

Minneapolis, MN

As discussed in Note 1, the financial statements present only the Minnesota State Lottery, an Enterprise Fund of the State of Minnesota, and do not purport to, and do not, present the financial statements of the State of Minnesota.

55401-2192

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Minnesota State Lottery as of June 30, 2012 and 2011, and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Phone 612-332-5500

In accordance with Government Auditing Standards, we have also issued separately our report dated October 9, 2012, on our consideration of the Minnesota State Lottery'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 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 and should be considered in assessing the results of our audits.

Fax 612-332-1529

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 2 through 6 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 of the limited procedures do not provides us with sufficient evidence to express an opinion or provide any assurance.

E-mail info@sdkcpc.com

www.sdkcpc.com

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The introductory section and statistical section are presented for purposes of additional analysis and are not a required part of the financial statements. The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

*Schechter Dokken Kanter
Andrews & Selcer Ltd.*

October 9, 2012

MANAGEMENT DISCUSSION AND ANALYSIS

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis includes an overview of financial activities regarding the financial performance of the Minnesota State Lottery for the fiscal year ended June 30, 2012 and should be read in conjunction with the transmittal letter and supplementary information included in this report. This report consists of three parts: management's discussion and analysis, the basic financial statements and the notes to the financial statements. Included below and on the following pages are the financial highlights, summary of contributions to the State, summary results of operations for years ended June 30, 2012, 2011 and 2010 and a condensed version of the balance sheets as of June 30, 2012, 2011 and 2010.

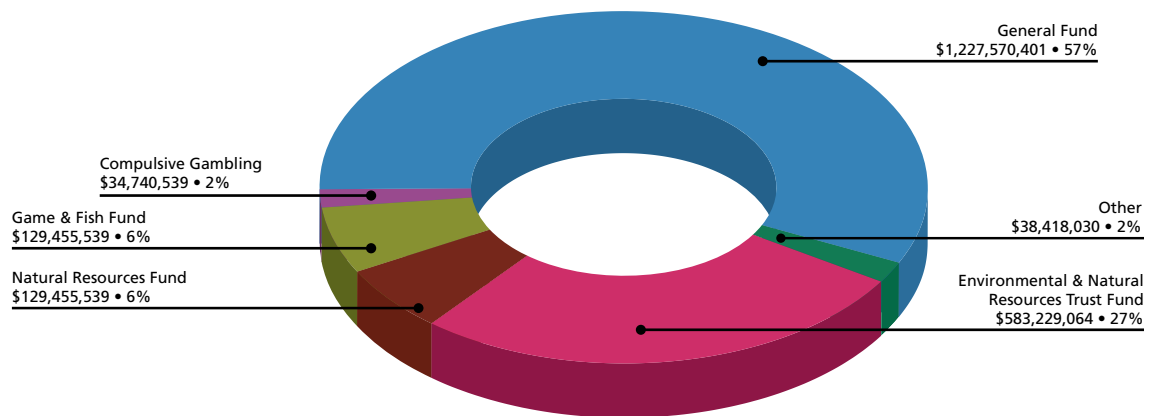
FINANCIAL HIGHLIGHTS

The Minnesota State Lottery achieved record operating revenue of \$520.1 million in fiscal year 2012. Lotto ticket sales led the way increasing \$15.1 million over the previous year while scratch ticket sales were mostly unchanged. Lottery Powerball sales were a significant factor in the increased sales in fiscal year 2012 contributing \$11.5 million over fiscal year 2011. Much of the increase in Powerball revenue was the result of the change in price point from \$1 to \$2 as well as the consistently high jackpots: a direct result of the new Powerball game structure. Gopher 5 and Mega Millions sales also contributed significantly in the Lottery's record sales together providing an increase \$9.8 million in sales.

SUMMARY OF CONTRIBUTIONS TO STATE

The Lottery contributed \$123.8 million to the State in fiscal year 2012. This was a slight increase from the \$121.9 million contributed in 2011 and the \$122.2 million contributed in fiscal year 2010. The following table provides detail on the total amounts transferred to the State as well as the source of the transfers provided to the state in the last three fiscal years.

The Lottery has contributed over \$2 billion to the State since inception



| CONTRIBUTIONS TO THE STATE | 2012 | 2011 | 2010 |
|----------------------------------|----------------------|----------------------|----------------------|
| Net proceeds to the State | \$77,524,634 | \$77,110,501 | \$78,374,378 |
| In-lieu-of-sales tax | \$33,802,180 | \$32,778,367 | \$32,432,967 |
| Compulsive gambling contribution | \$2,230,000 | \$2,230,000 | \$2,230,000 |
| Unclaimed prizes to the State | \$10,250,589 | \$9,759,269 | \$9,211,142 |
| Total paid to State | \$123,807,403 | \$121,888,137 | \$122,248,487 |

SUMMARY RESULTS OF OPERATIONS

| | 2012 | 2011 | 2010 |
|---|-----------------------|-----------------------|-----------------------|
| Gross receipts | \$486,284,810 | \$471,736,178 | \$466,575,526 |
| Prizes, commissions and ticket costs | \$370,218,586 | \$357,892,568 | \$351,471,062 |
| Gross profit | \$116,066,224 | \$113,843,610 | \$115,104,464 |
| Operating expenses | \$26,371,872 | \$24,865,261 | \$25,554,707 |
| <i>Operating income</i> | <u>\$89,694,352</u> | <u>\$88,978,349</u> | <u>\$89,549,757</u> |
| Non-operating revenues (expense): | | | |
| Interest earned on investments | \$155,819 | \$121,421 | \$265,763 |
| Unused Compulsive Gambling | \$155,052 | 0 | 0 |
| Payments to State (not including sales tax) | (\$90,005,223) | (\$89,099,770) | (\$89,815,520) |
| Total non-operating revenue (expense) | <u>(\$89,694,352)</u> | <u>(\$88,978,349)</u> | <u>(\$89,549,757)</u> |
| <i>Net Income</i> | <u>\$0</u> | <u>\$0</u> | <u>\$0</u> |

OPERATING INCOME

A steady increase in operating revenue in the last three years is largely due to the emphasis on marketing scratch games as well as changes in the price of a Powerball ticket increasing from one to two dollars. Other factors contributing to the increase in revenue include the Lottery's concentrated efforts on increasing the number of retail locations as well as improving web based exposure through our Luckymn web site and Facebook. Operating revenue increased \$15.6 million or 3.1 percent in fiscal year 2012 over fiscal year 2011 and increased \$5.5 million or 1.1 percent in fiscal year 2011 over fiscal year 2010.

OPERATING EXPENSES

Operating expenses increased in fiscal year 2012 by \$1.5 million or 6.1 percent from fiscal year 2011 largely due to an increase in marketing and promotion expenses. Operating expenses decreased in fiscal year 2011 by \$689 thousand or 2.7 percent over fiscal year 2010 due to a decrease in marketing, promotion and salary expenses.

| GROSS RECEIPTS BY GAME | 2012 | 2011 | 2010 |
|-------------------------------|----------------------|----------------------|----------------------|
| Scratch ticket sales | \$355,260,670 | \$354,813,430 | \$338,114,154 |
| Lotto ticket sales: | | | |
| Daily 3® | \$12,844,327 | \$13,258,715 | \$12,939,238 |
| Gopher 5® | \$19,611,685 | \$16,457,217 | \$15,451,880 |
| Powerball® | \$70,516,182 | \$59,028,789 | \$82,252,717 |
| Power Play® | \$3,141,464 | \$3,816,815 | \$4,997,806 |
| Mega Millions® | \$24,678,710 | \$17,995,480 | \$5,900,573 |
| Megaplier® | \$1,563,907 | \$1,545,180 | \$582,425 |
| Hot Lotto® | \$8,604,488 | \$12,250,143 | \$13,805,414 |
| Sizzler® | \$823,377 | \$1,065,828 | \$1,096,382 |
| Northstar Cash® | \$9,941,086 | \$10,872,164 | \$11,899,536 |
| Minnesota Millionaire Raffle | \$5,993,670 | \$5,999,710 | \$4,998,520 |
| Progressive Print-N-Play® | \$7,053,971 | \$7,332,938 | \$6,930,076 |
| Total Lotto Ticket Sales | \$164,772,867 | \$149,622,979 | \$160,854,567 |
| Operating revenue | \$520,033,537 | \$504,436,409 | \$498,968,721 |
| Other income | \$53,453 | \$88,136 | \$39,772 |
| Total operating revenue | \$520,086,990 | \$504,524,545 | \$499,008,493 |
| Less in-lieu-of-sales tax | \$33,802,180 | \$32,788,367 | \$32,432,967 |
| <i>Gross Receipts</i> | <i>\$486,284,810</i> | <i>\$471,736,178</i> | <i>\$466,575,526</i> |

SCRATCH GAMES

Scratch game sales accounted for 68.3 percent, 70.3 percent and 67.8 percent of sales respectively for fiscal years 2012, 2011 and 2010. Scratch sales remain mostly unchanged in fiscal year 2012 over fiscal year 2011. Fiscal year 2011 scratch sales were up 4.9 percent over fiscal year 2010. Total scratch sales were \$355.3 million in fiscal year 2012, \$354.8 million in fiscal year 2011 and \$338.1 million in fiscal year 2010.

LOTTO GAMES

Total Lotto Game sales increased in fiscal year 2012 largely due to the \$11.5 million increase in Powerball sales. Other contributing factors include the increased price of a Powerball ticket as well as the \$640 million Mega Millions jackpot run in fiscal year 2012. All other Lotto games in the aggregate have remained very consistent with sales of \$69.6 million, \$72.6 million and \$72.7 million in the last three fiscal years 2012, 2011 and 2010.

BALANCE SHEET SUMMARY

| CONDENSED BALANCE SHEETS | 2012 | 2011 | 2010 |
|---|---------------------|---------------------|---------------------|
| Assets: | | | |
| Cash and cash equivalents | \$21,756,782 | \$16,539,449 | \$13,981,238 |
| Receivables | \$4,720,077 | \$4,957,153 | \$7,569,329 |
| Inventory and prepaid expenses | \$1,164,238 | \$1,112,825 | \$1,827,037 |
| Capital assets | \$1,535,356 | \$2,151,282 | \$2,265,672 |
| Total assets | \$29,176,453 | \$24,760,709 | \$25,643,276 |
| Liabilities and net assets: | | | |
| Due to State and State Agencies | \$16,043,053 | \$15,624,368 | \$14,132,066 |
| Accounts payable & current accrued expenses | \$8,089,692 | \$7,480,960 | \$5,309,656 |
| Current accrued prizes | \$4,348,289 | \$896,399 | \$5,471,136 |
| Long-term accrued expenses | \$695,419 | \$758,982 | \$730,418 |
| Unrestricted net assets | (\$1,535,356) | (\$2,151,282) | (\$2,265,672) |
| Net assets invested in capital assets | \$1,535,356 | \$2,151,282 | \$2,265,672 |
| Net assets | 0 | 0 | 0 |
| Total liabilities and net assets | \$29,176,453 | \$24,760,709 | \$25,643,276 |

The Lottery is required to advance net proceeds to the State of Minnesota and therefore, net assets remains unchanged from year to year. In general, short term assets and liabilities will fluctuate with the activity of games being played and the timing of the year end cut-off related to our business cycle.

CASH AND CASH EQUIVALENTS AND RECEIVABLES

Cash and cash equivalents and receivables have increased with a \$5.0 million variance from fiscal year 2012 to 2011. This is a direct result of the higher sales at the end of the year relative to the prior year.

CAPITAL ASSETS AND OTHER ASSETS

Net capital assets decreased by over \$615 thousand in fiscal year 2012 due mainly to less purchases in 2012 compared to 2011 when \$500 thousand of express point machines were purchased. Purchases of capital assets included office equipment and vehicles which accounted for \$226 thousand of the \$277 thousand in total purchases of capital assets. Net of depreciation, total retirements were \$0.

Other assets slightly increased in fiscal year 2012 from fiscal year 2011 due mainly to scratch ticket inventory which increased from \$597 thousand in fiscal year 2011 to \$785 thousand in fiscal year 2012.

DUE TO STATE AND STATE AGENCIES

The fiscal year 2012 increase of \$419 thousand was due to the increase in unclaimed prizes due to the state.

CURRENT ACCRUED PRIZES

Current accrued prizes increased by \$3.5 million in fiscal year 2012 mainly due to high jackpots and winning tickets that remain uncashed at the end of the fiscal year. \$1 million winning Powerball tickets from the April 21st and June 30th drawings were still unclaimed at the end of the fiscal year. Also, a \$250 thousand winning Mega Millions ticket from February 7th and \$230 thousand in winning tickets from the \$640 million jackpot run remains unclaimed at the end of the fiscal year. Gopher 5 and Progressive Print-N-Play's jackpot at the end of the fiscal year was \$665 thousand and \$135 thousand, respectively. A Progressive Print-N-Play ticket sold on June 25th won the \$182 thousand jackpot and remains unclaimed at the end of the year.

ACCOUNTS PAYABLE AND CURRENT ACCRUED EXPENSES

Accounts payable and current accrued expenses are up \$609 thousand from 2011 to 2012 due to a \$1.2 million increase in payables for invoices received in June but not paid until the following fiscal year. The majority of the payables are invoices from our advertising and online vendors. This was offset by a \$704 thousand decrease in accrued salaries and deferred revenue. For salaries, the number of days accrued in fiscal year 2012 was 8 days compared to 17 days in fiscal year 2011. The decrease in deferred revenue is due to the fiscal year ending on a draw date for Powerball/Power Play and Hot Lotto/Sizzler.

| BALANCE SHEETS – JUNE 30, 2012 and 2011 | 2012 | 2011 |
|--|---------------------|---------------------|
| Assets | | |
| Current Assets: | | |
| Cash and Cash Equivalents (Note 3) | \$21,756,782 | \$16,539,449 |
| Accounts Receivable, Net (Note 4) | 4,709,064 | 4,950,167 |
| Interest Receivable | 11,013 | 6,986 |
| Scratch Ticket Inventory | 785,176 | 597,284 |
| Prepaid Expense | 379,063 | 515,541 |
| <i>Total Current Assets</i> | <u>27,641,098</u> | <u>22,609,427</u> |
| Capital Assets, Net (Note 5) | 1,535,356 | 2,151,282 |
| <i>Total Assets</i> | <u>\$29,176,454</u> | <u>\$24,760,709</u> |
| Liabilities and Net Assets | | |
| Current Liabilities: | | |
| Net Proceeds Due to State (Note 8) | \$5,792,465 | \$5,865,099 |
| Unclaimed Prizes Due to State (Note 6) | 10,250,589 | 9,759,269 |
| Accounts Payable | 3,546,476 | 2,339,773 |
| In-Lieu-of-Sales Tax Payable | 2,867,301 | 2,761,124 |
| Prize Liability | 4,348,289 | 896,399 |
| Accrued Salaries and Benefits, Current (Note 7) | 1,188,610 | 1,555,451 |
| Deferred Revenue | 487,305 | 824,612 |
| <i>Total Current Liabilities</i> | <u>28,481,035</u> | <u>24,001,727</u> |
| Accrued Salaries and Benefits, Net of Current Portion (Note 7) | 695,419 | 758,982 |
| <i>Total Liabilities</i> | <u>29,176,454</u> | <u>24,760,709</u> |
| Net Assets: | | |
| Unrestricted Net Assets | (1,535,356) | (2,151,282) |
| Net Assets Invested in Capital Assets (Note 8) | 1,535,356 | 2,151,282 |
| <i>Total Net Assets</i> | <u>0</u> | <u>0</u> |
| <i>Total Liabilities and Net Assets</i> | <u>\$29,176,454</u> | <u>\$24,760,709</u> |

See accompanying notes to Financial Statements.

**STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
YEARS ENDED JUNE 30, 2012 AND 2011**

| | 2012 | 2011 |
|--|---------------------|---------------------|
| Operating Revenues: | | |
| Scratch Ticket Sales | \$355,260,670 | \$354,813,430 |
| Lotto Ticket Sales | 164,772,867 | 149,622,979 |
| Other Income | 53,453 | 88,136 |
| Total Operating Revenues | 520,086,990 | 504,524,545 |
| Less: In-Lieu-of-Sales Tax | 33,802,180 | 32,788,367 |
| Gross Receipts | 486,284,810 | 471,736,178 |
| Direct Costs: | | |
| Scratch Ticket Prizes | 240,023,798 | 236,881,984 |
| Lotto Ticket Prizes | 80,584,939 | 73,977,591 |
| Online Vendor Expense | 9,505,892 | 9,077,683 |
| Ticket Costs | 8,635,277 | 7,608,118 |
| Retailer Commissions and Incentives (Note 11) | 31,468,680 | 30,347,192 |
| Total Direct Costs | 370,218,586 | 357,892,568 |
| Gross Profit | 116,066,224 | 113,843,610 |
| Operating Expenses (Note 12): | | |
| Advertising (Note 12) | 7,475,199 | 6,475,905 |
| Salaries and Benefits (Note 7, 13) | 10,264,453 | 10,649,595 |
| Promotion | 1,882,002 | 1,525,612 |
| Purchased Services | 1,750,921 | 1,442,811 |
| Communication | 552,099 | 472,423 |
| Occupancy Costs (Note 9) | 1,394,649 | 1,363,918 |
| Supplies and Materials | 947,940 | 1,164,920 |
| Computer and Omnipoint Maintenance | 422,769 | 321,110 |
| Depreciation | 892,802 | 913,304 |
| Other Expense | 789,038 | 535,663 |
| Total Operating Expenses | 26,371,872 | 24,865,261 |
| Operating Income | 89,694,352 | 88,978,349 |
| Nonoperating Revenue (Expense): | | |
| Interest Earned on Investments | 155,819 | 121,421 |
| Unused Compulsive Gambling Contribution | 155,052 | |
| Payments to State: | | |
| Compulsive Gambling Contribution from Prize Fund (Note 10) | (2,230,000) | (2,230,000) |
| Unclaimed Prizes to State (Note 6) | (10,250,589) | (9,759,269) |
| Net Proceeds to State (Note 8) | (77,524,634) | (77,110,501) |
| Total Nonoperating Expense | (89,694,352) | (88,978,349) |
| Net Income | 0 | 0 |
| Net Assets at Beginning of Year (Note 8) | 0 | 0 |
| Net Assets at End of Year (Note 8) | \$0 | \$0 |

See accompanying notes to Financial Statements.

| STATEMENTS OF CASH FLOWS – YEARS ENDED JUNE 30, 2012 AND 2011 | 2012 | 2011 |
|--|---------------------|---------------------|
| Cash Flows from Operating Activities: | | |
| Cash Received from Customers | \$519,937,333 | \$507,654,266 |
| Cash Received from Other Income | 53,453 | 92,196 |
| Payments to State (In-Lieu-of-Sales Tax) | (33,696,003) | (30,108,973) |
| Payments to Employees | (10,694,857) | (10,514,560) |
| Payments to Suppliers | (32,238,190) | (30,422,248) |
| Payments to Retailers | (31,468,680) | (30,439,388) |
| Payments to Prize Winners | (317,156,847) | (315,434,312) |
| <i>Net Cash Provided by Operating Activities</i> | <u>94,736,209</u> | <u>90,826,981</u> |
| Cash Flows from Capital and Non-Capital Financing Activities: | | |
| Net Proceeds Paid to State | (77,597,268) | (76,166,326) |
| Compulsive Gambling Contribution Transfer | (2,230,000) | (2,230,000) |
| Unused Compulsive Gambling Contribution | 155,052 | |
| Unclaimed Prizes Transfer | (9,759,269) | (9,211,142) |
| <i>Net Cash Used by Non-Capital Financing Activities</i> | <u>(89,431,485)</u> | <u>(87,607,468)</u> |
| Cash Flows from Capital and Related Financing Activities: | | |
| Purchases of Capital Assets | (276,876) | (800,378) |
| Proceeds on sale of Capital Assets | 37,693 | 11,478 |
| <i>Net Cash Used by Capital Financing Activities</i> | <u>(239,183)</u> | <u>(788,900)</u> |
| Cash Flows from Investing Activities: | | |
| Investment Income | 151,792 | 127,598 |
| <i>Net Cash Provided by Investing Activities</i> | <u>151,792</u> | <u>127,598</u> |
| Net Increase in Cash and Cash Equivalents | 5,217,333 | 2,558,211 |
| Beginning of Year Cash and Cash Equivalents | <u>16,539,449</u> | <u>13,981,238</u> |
| End of Year Cash and Cash Equivalents | <u>\$21,756,782</u> | <u>\$16,539,449</u> |
| Reconciliation of Operating Income to Net Cash Provided by Operating Activities: | | |
| Operating Income | \$89,694,352 | \$88,978,349 |
| Adjustments to Reconcile Operating Income to Net Cash provided by Operating Activities: | | |
| Depreciation | 892,802 | 913,304 |
| Gain on the disposal of capital assets | (37,693) | (10,014) |
| Net Change in Assets and Liabilities: | | |
| Scratch ticket inventory | (187,892) | 778,644 |
| Accounts receivable | 241,103 | 2,605,999 |
| Prepaid expenses | 136,478 | (64,432) |
| Other liabilities | 545,169 | 2,199,868 |
| Prize liability | 3,451,890 | (4,574,737) |
| <i>Net Cash Provided by Operating Activities</i> | <u>\$94,736,209</u> | <u>\$90,826,981</u> |

See accompanying notes to Financial Statements.

NOTES TO THE FINANCIAL STATEMENTS JUNE 30, 2012 AND 2011

1. ORGANIZATION OF THE MINNESOTA STATE LOTTERY

In 1988, Minnesotans voted to amend their Constitution to authorize a state-run lottery. In 1989, the Legislature approved and the Governor signed Minnesota Statutes Chapter 349A into law, officially creating the Minnesota State Lottery, the 33rd lottery in the country.

The Minnesota State Lottery (the Lottery), an Enterprise Fund of the State of Minnesota, is under the supervision and control of the Director of the Lottery, who is appointed by the Governor with the advice and consent of the Senate. The Lottery net proceeds and proceeds from the in-lieu-of-sales tax on tickets sales are dedicated to the General Fund, the Environment and Natural Resources Trust Fund, the Game and Fish Fund and the Natural Resources Fund. The funds are used to enhance the state's natural resources as well as public education, local government assistance and public safety.

The financial statements present only the Minnesota State Lottery, an Enterprise Fund of the State of Minnesota and do not purport to, and do not, present the financial statements of the State of Minnesota.

Lottery revenue is generated by sales of scratch games and lotto games that include: Daily 3^o, Northstar Cash^o, Progressive Print-N-Play^o, Gopher 5^o, Powerball^o, Power Play^o, Mega Millions^o, Megaplier^o, Hot Lotto^o, Sizzler^o and the Minnesota Millionaire Raffle game.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Lottery is an agency of the State of Minnesota using proprietary type enterprise accounting. The financial statements are prepared in accordance with generally accepted accounting principles as applicable to governmental units. Following are the significant accounting policies:

(a) Basis of Accounting

The financial statements of the Lottery have been prepared on the accrual basis of accounting. Revenues are recorded when they are earned and expenses are recognized as incurred.

Governmental Accounting Standards Board (GASB) Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting, provides that proprietary and similar trust funds should apply all GASB pronouncements, as well as the following pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB Pronouncements: Statements and Interpretations of the Financial Accounting Standards Board (FASB), Accounting Principles Board Opinions (APB), and Accounting Research Bulletins (ARB).

As permitted by GASB Statement No. 20, the Lottery has elected not to apply FASB statements or interpretations issued on or after November 30, 1989, unless the GASB specifically adopts such statements or interpretations.

(b) Accounting Standard: GASB No. 34

In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments. This Statement established updated financial reporting requirements for state and local governments. This statement also requires budgetary comparison schedules to be presented as supplementary information. The Lottery is not legally required to adopt a budget and therefore budgetary comparison schedules are not included as supplementary information.

(c) Measurement Focus

A proprietary fund is accounted for using the "economic resources" measurement focus. This means that all assets and liabilities associated with its activity are included on its balance sheet. The proprietary fund type operating statement presents increases (revenues) and decreases (expenses) in net total assets.

(d) Operating Revenue and Expenses

Operating revenue and expenses for a proprietary fund such as the Lottery are revenues and expenses that result from providing services and producing and delivering goods and/or services. Operating revenues are derived from providing various types of games. Operating expenses include commissions, prize costs, other direct costs of providing lottery games, and administrative expenses.

Packs of Scratch tickets are consigned to retail sales outlets and revenue is recognized upon settlement of ticket packs by retailers and are recorded at the sale price to the consumer. Sales of lotto tickets are recognized as operating revenue on the date of the draw for which the tickets were purchased. Revenues from future lotto ticket draw sales are deferred until the date of the draw for which the tickets were purchased.

(e) Cash and Cash Equivalents

Cash and cash equivalents include an amount in demand deposits as well as funds held in the State Treasury and invested by the State Board of Investment.

(f) Prizes and Reserves

Scratch ticket prize expense is recognized in accordance with the predetermined prize structure for each game and is accrued when revenue is recognized. High tier prizes for certain Scratch ticket games may also be structured and paid as an annuity.

Prize expense for Daily 3 is recorded based upon the actual winners on the date of the draw. Prize expense for Progressive Print-N-Play games are based on actual winners and are recorded at the time of sale. The prize expense for Northstar Cash is recorded at 53.3 percent of draw sales. The prize expense for Gopher 5 is recorded at 55 percent of draw sales.

Included in the Lottery Prize Liability at June 30, 2012 is a \$1,057,100 prize reserve which reflects funds due to the State Treasury that have been set aside in the Lottery prize fund by the Director in accordance with Minnesota Statutes, Section 349A.10, subdivision 2(b) to assure proper funding for future lottery prizes. The prize reserve at June 30, 2011 was \$986,802.

Prize expenses for Powerball, Power Play, Hot Lotto and Sizzler are recorded at 50 percent of draw sales; Mega Millions and Megaplier are recorded at 51.5 percent of draw sales. All Multi-State Lottery Association (MUSL) games are recorded in accordance with the MUSL prize structure. The Powerball, Power Play, Hot Lotto, Sizzler, Mega Millions and Megaplier prizes are paid with funds held by MUSL. MUSL has established separate prize pool reserves for Powerball, Power Play, Hot Lotto, Sizzler, Mega Millions and Megaplier to support payment of prizes in light of the remote possibility of claims greatly exceeding the expected amounts. In the event that the Lottery ceases to participate in one of these games, the Lottery may make claim to assets, if any, in the related prize pool reserve. The Lottery's share of these prize reserves as of June 30, 2012 was as follows:

| | |
|-------------------------|--------------------|
| Powerball/Power Play | \$4,211,582 |
| Mega Millions/Megaplier | 537,184 |
| Hot Lotto/Sizzler | 1,522,488 |
| Total | \$6,271,214 |

These reserves held by MUSL are not included in these financial statements.

The Lottery participates in joint marketing campaigns for various events in order to maximize its marketing dollar and the exposure to the Lottery. In doing so, other entities may donate various prizes which are given out by the Lottery to its players. The Lottery recognizes Other Income when the donated prize is received and records Prize Expense when the prize is given to the player. The Lottery received \$45,194 and \$19,134 in donated prizes in fiscal year 2012 and 2011 respectively which were subsequently given to players.

(g) Scratch Ticket Inventory

Scratch ticket inventories are carried at cost using the specific identification method. Tickets are charged to operating expense over the estimated life of each scratch game.

(h) Capital Assets

Assets costing \$5,000 or more are capitalized and are carried at cost less accumulated depreciation. Depreciation is computed on the straight-line basis using estimated useful lives from three to seven years. Computer equipment, printers, and software costs are depreciated over three years. Vehicles, other than the warehouse truck, are depreciated over four years. Office equipment, lotto drawing equipment and signs are depreciated over five years. Office furniture and the warehouse truck and equipment are depreciated over seven years. Leasehold improvements are depreciated on a straight-line basis over the shorter of the useful life or length of the lease. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is recognized.

(i) In-Lieu-of-Sales Tax

From every dollar in Lottery sales, the Lottery sets aside six and one-half cents as in-lieu-of-sales tax and remits that amount monthly to the Commissioner of Revenue as required by Minnesota Statutes, Section 297A.65. Minnesota Statutes, Section 297A.94(e), provides that 27.57% of the in-lieu-of-sales-tax is credited to the General Fund and the remaining 72.43% is credited equally between the Game and Fish Fund and the Natural Resources Fund to be used for natural resources projects as specified by law.

(j) Income Taxes

The Lottery, as an agency of the State of Minnesota, is exempt from federal and state income taxes. Accordingly, the Lottery makes no provision for income taxes.

(k) Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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.

3. CASH AND CASH EQUIVALENTS

Minnesota Statutes, Section 349A.10, subdivision 7(a), requires the Lottery transfer all funds to a Lottery cash flow account in the State Treasury. Funds necessary to cover cash needs are transferred as needed from State Treasury to the Lottery fund. Funds in this account earn interest, which is credited monthly to the Lottery's account. Cash on deposits in the State Treasury and with financial institutions are insured. Cash on deposit is covered up to \$250,000 per institution by the Federal Depository Insurance Corporation (FDIC). At times, cash balances may be in excess of the FDIC insurance limit. As a result, the financial institutions are required to pledge securities as collateral to the Lottery in an amount equal to the funds in excess of the FDIC insurance limit. The securities are held in the name of the Lottery.

Table 1 summarizes the Lottery's cash and cash equivalents at June 30, 2012 and 2011.

Available cash in the State Treasury is invested by the State Board of Investment. In accordance with Minnesota Statutes, Section 11A.24, the State Board of Investment must invest in obligations and stocks of U.S. and Canadian governments, their agencies and their registered corporations, short-term obligations of specified high quality, restricted participation as a limited partner in venture capital, real estate, or resource equity investments, and restricted participation in registered mutual funds. Lottery funds on deposit in the State Treasury cannot be tied to specific investment securities.

4. ACCOUNTS RECEIVABLE – ALLOWANCE FOR DOUBTFUL ACCOUNTS

Table 2 summarizes the Lottery's accounts receivable at June 30, 2012 and 2011.

5. CAPITAL ASSETS

Tables 3 and 4 (next page) show the summary of changes in capital assets for the years ended June 30, 2012 and 2011.

| TABLE 1 CASH AND CASH EQUIVALENTS AT JUNE 30, 2012 AND 2011 | 2012 | 2011 |
|--|---------------------|---------------------|
| Cash (checks issued but not yet presented for payment) | \$(399,509) | \$(2,062,144) |
| Cash on Deposit | 22,156,291 | 18,601,593 |
| Total Cash and Cash Equivalents | <u>\$21,756,782</u> | <u>\$16,539,449</u> |

| TABLE 2 ACCOUNTS RECEIVABLE AT JUNE 30, 2012 AND 2011 | 2012 | 2011 |
|--|--------------------|--------------------|
| Accounts Receivable | \$5,161,261 | \$5,383,724 |
| Allowance for Doubtful Accounts | (452,197) | (433,557) |
| Accounts Receivable, Net | <u>\$4,709,064</u> | <u>\$4,950,167</u> |

| TABLE 3 - CAPITAL ASSETS 2012 | JULY 1, 2011 | ADDITIONS | DELETIONS | TRANSFERS | JUNE 30, 2012 |
|---|---------------------------|---------------------------|-------------------|-------------------|---------------------------|
| Depreciable Capital Assets: | | | | | |
| Office Equipment & Furniture | \$1,869,415 | \$48,878 | (\$63,787) | | \$1,854,506 |
| Software Costs | 855,223 | 40,087 | | | 895,310 |
| Leasehold Improvements | 1,444,364 | | | | 1,444,364 |
| Vehicles | 956,488 | 177,201 | (130,912) | | 1,002,777 |
| Computer Equipment | 936,342 | 10,710 | | | 947,052 |
| Lotto Drawing Equipment | 775,528 | | | | 775,528 |
| Express Point Machines | 1,495,438 | | | | 1,495,438 |
| Signs | 79,151 | | | | 79,151 |
| Warehouse Equipment | 236,121 | | | | 236,121 |
| <i>Total</i> | <u>8,648,070</u> | <u>276,876</u> | <u>(194,699)</u> | <u>0</u> | <u>8,730,247</u> |
| Less - accumulated depreciation: | | | | | |
| Office Equipment & Furniture | (1,571,382) | (121,391) | 63,787 | | (1,628,986) |
| Software Costs | (488,544) | (228,411) | | | (716,955) |
| Leasehold Improvements | (1,361,510) | (13,728) | | | (1,375,238) |
| Vehicles | (657,126) | (129,922) | 130,912 | | (656,136) |
| Computer Equipment | (683,389) | (86,023) | | | (769,412) |
| Lotto Drawing Equipment | (710,221) | (24,941) | | | (735,162) |
| Express Point Machines | (749,366) | (272,827) | | | (1,022,193) |
| Signs | (69,579) | (9,574) | | | (79,153) |
| Warehouse Equipment | (205,671) | (5,985) | | | (211,656) |
| <i>Total accumulated depreciation</i> | <u>(6,496,788)</u> | <u>(892,802)</u> | <u>194,699</u> | <u>0</u> | <u>(7,194,891)</u> |
| Net Capital Assets | <u>\$2,151,282</u> | <u>(\$615,926)</u> | <u>\$0</u> | <u>\$0</u> | <u>\$1,535,356</u> |

| TABLE 4 - CAPITAL ASSETS 2011 | JULY 1, 2010 | ADDITIONS | DELETIONS | TRANSFERS | JUNE 30, 2011 |
|---|---------------------------|---------------------------|-------------------------|-------------------|---------------------------|
| Depreciable Capital Assets: | | | | | |
| Office Equipment & Furniture | \$1,786,438 | \$106,573 | \$(23,596) | | \$1,869,415 |
| Software Costs | 809,907 | 27,822 | | \$17,494 | 855,223 |
| Leasehold Improvements | 1,443,304 | 1,060 | | | 1,444,364 |
| Vehicles | 848,968 | 141,536 | (34,016) | | 956,488 |
| Computer Equipment | 941,036 | 12,800 | | (17,494) | 936,342 |
| Lotto Drawing Equipment | 775,528 | | | | 775,528 |
| Express Point Machines | 1,013,375 | 482,063 | | | 1,495,438 |
| Signs | 79,151 | | | | 79,151 |
| Warehouse Equipment | 207,597 | 28,524 | | | 236,121 |
| <i>Total</i> | <u>7,905,304</u> | <u>800,378</u> | <u>(57,612)</u> | <u>0</u> | <u>8,648,070</u> |
| Less - accumulated depreciation: | | | | | |
| Office Equipment & Furniture | (1,476,909) | (116,605) | 22,132 | | (1,571,382) |
| Software Costs | (250,040) | (237,335) | | (1,169) | (488,544) |
| Leasehold Improvements | (1,344,808) | (16,702) | | | (1,361,510) |
| Vehicles | (561,457) | (129,685) | 34,016 | | (657,126) |
| Computer Equipment | (595,539) | (89,019) | | 1,169 | (683,389) |
| Lotto Drawing Equipment | (684,924) | (25,297) | | | (710,221) |
| Express Point Machines | (471,938) | (277,428) | | | (749,366) |
| Signs | (59,148) | (10,431) | | | (69,579) |
| Warehouse Equipment | (194,869) | (10,802) | | | (205,671) |
| <i>Total accumulated depreciation</i> | <u>(5,639,632)</u> | <u>(913,304)</u> | <u>56,148</u> | <u>0</u> | <u>(6,496,788)</u> |
| Net Capital Assets | <u>\$2,265,672</u> | <u>(\$112,926)</u> | <u>(\$1,464)</u> | <u>\$0</u> | <u>\$2,151,282</u> |

6. UNCLAIMED PRIZES

Effective July 1, 2003 pursuant to Minnesota Statutes 349A.08, subdivision 5, all unclaimed prizes will be transferred to the General Fund at the end of the fiscal year. The unclaimed prizes due to the State are \$10,250,588 and \$9,759,269 on June 30, 2012 and June 30, 2011, respectively.

7. ACCRUED SALARIES AND BENEFITS

A liability is recognized for accrued salaries, post employment benefit obligations, unpaid vacation, compensatory hours, vested severance and anticipated severance pay when earned. Non-vested severance pay is estimated based upon historical trends and current demographics. A schedule of the accrued salaries and benefits is shown in **Tables 5 and 6**.

| TABLE 5 – ACCRUED SALARIES BENEFIT | 2012 | 2011 |
|--|--------------------|--------------------|
| Accrued Salary and Benefits: | | |
| Salaries Payable | \$350,875 | \$686,011 |
| Compensated Absences | 837,735 | 848,440 |
| Post Employee Obligations | 0 | 21,000 |
| <i>Total Current Accrued Salaries and Benefits</i> | <u>\$1,188,610</u> | <u>\$1,555,451</u> |
| Compensated Absences Payable | \$586,419 | \$649,982 |
| Post Employee Obligations | 109,000 | 109,000 |
| Total Non-Current Accrued Salaries and Benefits | <u>\$695,419</u> | <u>\$758,982</u> |

| TABLE 6 – COMPENSATED ABSENCES PAYABLE | BEGINNING | ADDITIONS | RETIREMENTS | ENDING |
|--|-------------|-------------|---------------|-------------|
| 2012 | \$1,498,422 | \$981,019 | \$(1,055,287) | \$1,424,154 |
| 2011 | \$1,433,090 | \$1,095,041 | \$(1,029,709) | \$1,498,422 |

8. NET ASSETS

Within 30 days after the end of each month, the Lottery is required by Minnesota Statutes, Section 349A.10, and subdivision 5 to deposit the net proceeds in the State Treasury. The monthly transfer of net proceeds leaves a zero balance in Net Assets. Net Proceeds Due to State on the accompanying balance sheets for the month ended June 30, 2012 and 2011 were \$5,792,465 and \$5,865,099, respectively. Net assets invested in capital assets consist of capital assets, net of accumulated depreciation.

9. COMMITMENTS AND CONTINGENCIES

(a) Risk Management

The Lottery is exposed to various risks of loss related to torts, checking, theft, damage to and destruction of assets, errors and omissions, injuries to employees and natural disasters.

The Lottery participates in the State's Risk Management Fund for property, liability, crime and automobile insurance coverage. The Lottery pays annual premiums for this coverage. The State's Risk Management Fund covers all claims above the deductible. The Lottery has not experienced any settlements in excess of coverage in the past three years.

The Lottery participates in the State's workers' compensation program. The Workers' Compensation Alternative Cost Allocation Account (WCACAA) funds

approximately 15% of the total workers' compensation costs annually. Funds are collected up-front through a premium based on each agency's unique exposure and experience. The Lottery paid a premium of \$32,014 in fiscal year 2012 and \$27,032 in fiscal year 2011.

The Lottery purchased twenty lifetime annuities from various insurance companies. If these insurance companies were to default on those obligations these policies would be covered under a "Guaranty Fund Law" which is administered by the State of Minnesota. The amount guaranteed per annuity is \$300,000. The Lottery may be ultimately responsible for the lifetime annuities; however, management feels that the possibility of these insurance companies defaulting on its obligations in a material sum in excess of the \$300,000 guaranteed by the State is remote.

The areas of insurance coverage, limits and deductibles as of June 30, 2012 are shown in **Table 7** (next page).

| TABLE 7 - COVERAGE | LIMITS | DEDUCTIBLES |
|---|-----------------------|-------------|
| Property | \$8,583,126 | \$1,000 |
| Auto | | |
| Bodily Injury & Property Damage | \$500,000/\$1,500,000 | \$500 |
| Primary Crime | | |
| Employee Dishonesty, Money & Securities | \$25,000 | \$1,000 |
| General Liability | \$500,000/\$1,500,000 | None |
| Excess Crime | | |
| Employee Theft | \$1,000,000 | \$25,000 |
| Forgery or Alteration | \$1,000,000 | \$25,000 |
| Theft of Money & Securities | \$75,000 | \$25,000 |
| Robbery, Safe Burglary–Other Prop. | \$75,000 | \$25,000 |
| Outside Premises | \$75,000 | \$25,000 |
| Computer Fraud | \$1,000,000 | \$25,000 |
| Funds Transfer | \$1,000,000 | \$25,000 |
| Money Orders & Counterfeit Paper Currency | \$1,000,000 | \$25,000 |

| TABLE 8 - OPERATING LEASES YEAR ENDING JUNE 30 | LEASE AMOUNT | LESS SUB-LEASE AMOUNT | NET |
|--|--------------------|-----------------------|--------------------|
| 2013 | \$1,404,529 | \$205,227 | \$1,199,302 |
| 2014 | 370,508 | 0 | 370,508 |
| 2015 | 376,664 | 0 | 376,664 |
| 2016 | 372,722 | 0 | 372,722 |
| 2017 | 328,294 | 0 | 328,294 |
| Thereafter | 211,439 | 0 | 211,439 |
| Total | <u>\$3,064,156</u> | <u>\$205,227</u> | <u>\$2,858,929</u> |

(b) Operating Leases

The Lottery is committed under various operating leases for building and office space. For the years ended June 30, 2012 and 2011, the lease expense was \$1,159,137 and \$1,135,761, respectively. This is net of sublease rental income of \$336,371 and \$341,312 in 2012 and 2011, respectively. Sublease rental income is included within occupancy costs in the financial statements. Future minimum lease payments for existing lease agreements are shown in **Table 8** above.

10. COMPULSIVE GAMBLING TREATMENT CONTRIBUTION PROVIDED FROM PRIZE FUND

Minnesota Laws 1998, Chapter 407, Article 8, Section 11 directed the Lottery to pay \$340,000 annually from the prize fund to a special Indian Gaming account in the State Treasury. Funds in this account are transferred to the Department of Human Services for compulsive gambling treatment programs.

Minnesota Laws 2011, 1st Special Session, Chapter 9, Article 10, section 3, subdivision 1 appropriated \$1,665,000 for Fiscal Year 2012 from the prize fund

of the Department of Human Services for statewide compulsive gambling treatment programs.

Minnesota Laws 2009, Chapter 79, Article 13, section 3, 1st Special Session, Chapter 1, Article 25, section 3 appropriated \$1,586,000 for Fiscal Year 2011 from the prize fund to the Department of Human Services.

Minnesota Laws 2011, Chapter 101, Article 1, section 36 appropriated \$225,000 for Fiscal Year 2012 from the prize fund to the Gambling Control Board for a grant to the state affiliate recognized by the National Council of Problem Gambling to be used for public awareness, education, training of treatment providers, and research (of this appropriation \$50,000 each year is contingent on contribution of non-state matching funds).

Minnesota Laws 2009, Chapter 101, Article 1, section 31, appropriated \$225,000 for Fiscal Year 2011 from the prize fund to the Gambling Control Board.

11. RETAILER COMMISSIONS

Retailer commission is set by Minnesota Rule 7856.4030, subpart 1 as 5.5% of the price of each lottery ticket sold by a retailer and 1% of the amount of each winning lottery ticket cashed by a retailer.

12. STATUTORY LIMITATION ON OPERATING AND ADVERTISING EXPENSES

Gross revenue is defined in law as ticket sales and all other income less in-lieu-of-sales tax. Direct costs are expenses that are a direct function of lottery sales, which include all prize payouts, retailer commissions and incentives, amounts paid to produce and deliver scratch lottery tickets, and amounts paid to an outside vendor to operate and maintain an on-line gaming system. Operating costs include all other expenses of the Lottery.

Minnesota Statutes, Section 349A.10, subdivision 3 limits the Lottery’s advertising costs to 2.75 percent and operating costs to 9 percent of gross revenue. Minnesota Laws 2011 1st Special Session, Chapter 10, Article 1, section 33 and Minnesota Laws 2009, Chapter 101, Article 1, section 18 provides that notwithstanding Minnesota Statutes, section 349A.10, subdivision 3, the operating budget must not exceed \$29,000,000 in fiscal year 2012 and \$28,740,000 in fiscal year 2011, respectively.

The Lottery is in compliance with the statutory limits on advertising and operating costs. Advertising costs as a percentage of gross revenue were 1.54 percent and 1.37 percent for the years ended June 30, 2012 and 2011, respectively. Operating costs as a percentage of gross revenue were 5.42 percent and 5.27 percent for the years ended June 30, 2012 and 2011, respectively.

13. RETIREMENT PLANS AND POST RETIREMENT BENEFITS

The Lottery is involved in two pension programs as follows:

(a) General Plan – Defined Benefit Pension Plan – Statewide:

Plan Description

The Lottery contributes to the Minnesota State Retirement System (MSRS), which is a cost-sharing multiple-employer defined benefit pension plan administered by the MSRS. The plan provides retirement and disability benefits, annual cost of living adjustments, and death benefits to qualifying plan members and beneficiaries. Benefit provisions are established and may be amended by state statute and vest after three years of credited service. MSRS issues a publicly available financial report that includes financial statements and required supplementary information for MSRS. That report may be obtained by contacting MSRS at 651-296-2761 or www.msrs.state.mn.us.

Funding Policy

Plan members are required to contribute 5.0% of their annual covered salary and the Lottery is required to contribute at an actuarially-determined rate. The Lottery’s current rate is 5.0% of annual covered

payroll. The contribution requirements of plan members and the Lottery are established and may be amended by state statute. See **Table 9**.

(b) Unclassified Plan – Defined Contribution Plan – Statewide:

Plan Description

The Lottery contributes to the MSRS, which is a multiple-employer defined contribution plan administered by the MSRS. The plan provides retirement and disability benefits and death benefits to qualifying plan members and beneficiaries. Benefit provisions are established and may be amended by state statute and vest immediately. MSRS issues a publicly available financial report that includes financial statements and required supplementary information for MSRS. That report may be obtained by contacting MSRS at 651-296-2761 or www.msrs.state.mn.us.

Funding Policy

Plan members are required to contribute 5.0% of their annual covered salary and the Lottery is required to contribute 6.0% of the annual covered payroll. The contribution requirements of plan members and the Lottery are established and may be amended by state statute. See **Table 10**.

The Lottery provides other postemployment benefits (OPEB) as part of its total employee compensation package. GASB statement No. 45 “Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions” requires the Lottery to report OPEB on the face of its financial statements. The Lottery implemented GASB Statement No. 45 in Fiscal Year 2008. Total expenses related to OPEB for fiscal years 2012, 2011 and 2010 were \$21,000, \$24,000 and \$35,235, respectively.

| TABLE 9 – DEFINED BENEFIT PENSION PLAN CONTRIBUTIONS TO MSRS – YEAR ENDING JUNE 30 | | |
|--|-----------|-----------|
| 2012 | 2011 | 2010 |
| \$363,195 | \$376,714 | \$365,152 |

| TABLE 10 – DEFINED CONTRIBUTION PLAN CONTRIBUTIONS TO MSRS – YEAR ENDING JUNE 30 | | |
|--|----------|----------|
| 2012 | 2011 | 2010 |
| \$34,131 | \$35,403 | \$40,132 |

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Minnesota State Lottery

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2011

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



Christopher P. Morille

President

Jeffrey R. Emer

Executive Director



CERTIFICATION OF EXECUTIVE DIRECTOR AND CHIEF FINANCIAL OFFICER

I, Ed Van Petten, Executive Director of the Minnesota State Lottery and Joseph Pahl, Chief Financial Officer of the Minnesota State Lottery, certify that:

1. I have reviewed these Financial Statements for the fiscal year ended June 30, 2012 of the Minnesota State Lottery;
2. Based on my knowledge, these statements do not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by these statements;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Minnesota State Lottery as of, and for, the periods presented in these Financial Statements;
4. The Minnesota State Lottery's other certifying officer and I have disclosed, based on our most recent review of internal control over financial reporting, to the Minnesota State Lottery's auditors:
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Minnesota State Lottery's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Minnesota State Lottery's internal control over financial reporting.

Date: October 9, 2012

By:

Ed Van Petten, Executive Director

By:

Joseph Pahl, Chief Financial Officer





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