

**AUDIT REPORT  
OF THE  
NEBRASKA LOTTERY**

**FOR THE FISCAL YEAR ENDED JUNE 30, 2017**

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**Issued on October 11, 2017**

# NEBRASKA LOTTERY

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# NEBRASKA LOTTERY

## BACKGROUND

The Legislature created the Lottery Division of the Nebraska Department of Revenue (Nebraska Lottery) in 1991. Nebraska voters passed a constitutional amendment allowing the creation of a State lottery in November 1992, and the Legislature established the State lottery in 1993. As the 37<sup>th</sup> lottery in the nation, the Nebraska Lottery began scratch ticket sales on September 11, 1993. Sales of on-line products began on July 21, 1994.

The Nebraska Lottery is responsible for contracting for scratch ticket production, on-line equipment, advertising, security, and related services. In addition, the Nebraska Lottery recruits and screens Nebraska Lottery retailers, develops Nebraska Lottery products, and collects Nebraska Lottery revenues.

Currently, the Nebraska Lottery offers Powerball®, Nebraska Pick 5®, Nebraska Pick 3®, 2by2®, MyDaY®, Mega Millions®, and instant games.

Article III, § 24, of the Nebraska Constitution sets out the basic requirements for the transfer of lottery proceeds to certain beneficiary funds, specifying that a portion of those revenues are to “be used for education as the Legislature may direct.”

Neb. Rev. Stat. § 9-812(2) (2017 Neb. Laws, LB 512, § 5) offers the following legislative directive for the transfer of lottery proceeds:

*A portion of the dollar amount of the lottery tickets which have been sold on an annualized basis shall be transferred from the State Lottery Operation Trust Fund to the Education Innovation Fund, the Nebraska Opportunity Grant Fund, the Nebraska Education Improvement Fund, the Nebraska Environmental Trust Fund, the Nebraska State Fair Board, and the Compulsive Gamblers Assistance Fund as provided in subsection (3) of this section. The dollar amount transferred pursuant to this subsection shall equal the greater of (a) the dollar amount transferred to the funds in fiscal year 2002-03 or (b) any amount which constitutes at least twenty-two percent and no more than twenty-five percent of the dollar amount of the lottery tickets which have been sold on an annualized basis. To the extent that funds are available, the Tax Commissioner and director may authorize a transfer exceeding twenty-five percent of the dollar amount of the lottery tickets sold on an annualized basis.*

Additionally, § 9-812(3) provides these further instructions:

*Of the money available to be transferred to the Education Innovation Fund, the Nebraska Opportunity Grant Fund, the Nebraska Education Improvement Fund, the Nebraska Environmental Trust Fund, the Nebraska State Fair Board, and the Compulsive Gamblers Assistance Fund:*

*(a) The first five hundred thousand dollars shall be transferred to the Compulsive Gamblers Assistance Fund to be used as provided in section 9-1006;*

*(b) Beginning July 1, 2016, forty-four and one-half percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the Nebraska Education Improvement Fund;*

*(c) Forty-four and one-half percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the Nebraska Environmental Trust Fund to be used as provided in the Nebraska Environmental Trust Act;*

## NEBRASKA LOTTERY

### **BACKGROUND**

(Concluded)

*(d) Ten percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the Nebraska State Fair Board if the most populous city within the county in which the fair is located provides matching funds equivalent to ten percent of the funds available for transfer. Such matching funds may be obtained from the city and any other private or public entity, except that no portion of such matching funds shall be provided by the state. If the Nebraska State Fair ceases operations, ten percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the General Fund; and*

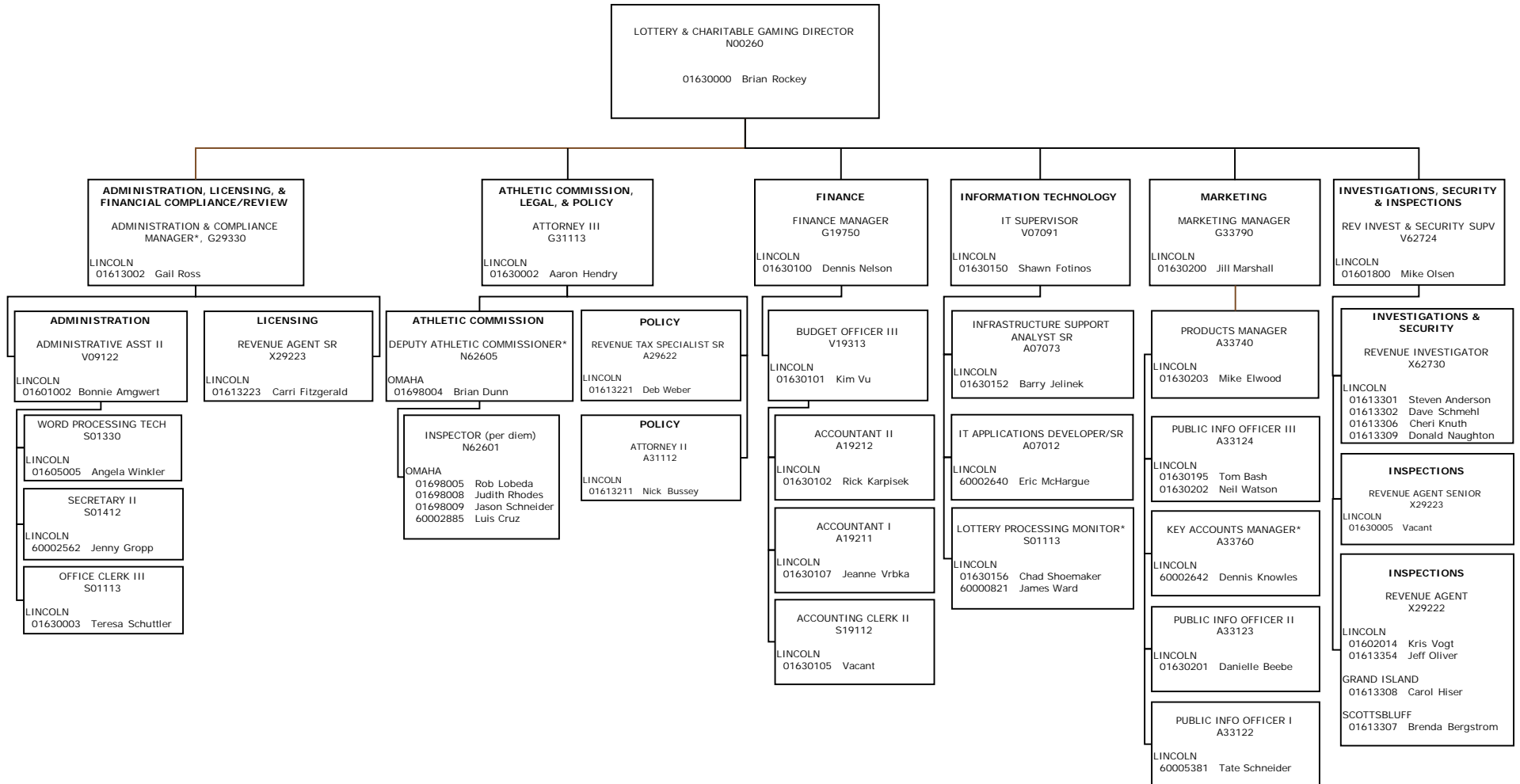
*(e) One percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the Compulsive Gamblers Assistance Fund to be used as provided in section 9-1006.*

### **MISSION STATEMENT**

The mission of the Nebraska Lottery is to generate proceeds for good causes while providing quality entertainment options to Nebraskans.

# NEBRASKA LOTTERY ORGANIZATIONAL CHART

## NEBRASKA DEPARTMENT OF REVENUE LOTTERY & CHARITABLE GAMING DIVISIONS ATHLETIC COMMISSION July - September 2017



38 Total Positions  
36 Filled  
2 Vacant  
4 Per Diem Employees

Updated 8/28/2017

\*Working Title

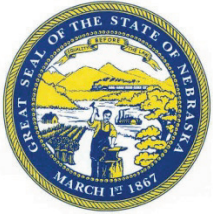
# NEBRASKA LOTTERY

## KEY OFFICIALS AND AGENCY CONTACT INFORMATION

### The Nebraska Lottery Executive Management

<b>Name</b>	<b>Title</b>
Tony Fulton	Tax Commissioner
Brian Rockey	Director
Dennis Nelson	Finance Manager

The Nebraska Lottery  
137 N.W. 17th Street  
P.O. Box 98901  
Lincoln, NE 68509-8901  
(402) 471-6100  
lottery@nelottery.com



## NEBRASKA AUDITOR OF PUBLIC ACCOUNTS

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### NEBRASKA LOTTERY

### INDEPENDENT AUDITOR'S REPORT

State Tax Commissioner  
Nebraska Department of Revenue, Lottery Division  
Lincoln, Nebraska

#### **Report on the Financial Statements**

We have audited the accompanying financial statements of the business-type activities of the Nebraska Department of Revenue, Lottery Division, (Nebraska Lottery) as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the Nebraska Lottery's basic financial statements, as listed in the Table of Contents.

#### ***Management's Responsibility for the Financial Statements***

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

#### ***Auditor's Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 Nebraska Lottery'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 previously present fairly, in all material respects, the respective financial position of the business-type activities of the Nebraska Lottery, as of June 30, 2017, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

### ***Emphasis of Matter***

As discussed in Note 1, the financial statements of the Nebraska Lottery are intended to present the financial position and the changes in financial position of only that portion of the business activities of the State that is attributable to the transactions of the Nebraska Lottery. They do not purport to, and do not, present fairly the financial position of the State of Nebraska as of June 30, 2017, and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

### ***Other Matters***

#### ***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis, on pages 8-11 herein, 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, which 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 Information***

The statistical section has 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 it.



***Other Reporting Required by Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated October 3, 2017, on our consideration of the Nebraska 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, 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 the Nebraska Lottery's internal control over financial reporting and compliance.



Zachary Wells, CPA  
Audit Manager  
Lincoln, Nebraska

October 3, 2017

## NEBRASKA LOTTERY

### MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the annual audit for the Nebraska Department of Revenue, Lottery Division, (Nebraska Lottery) presents management's discussion and analysis of the financial performance of the Nebraska Lottery for the fiscal period ended June 30, 2017. This discussion should be read in conjunction with the accompanying financial statements and related notes. The financial statements, notes, and this discussion are the responsibility of the Nebraska Lottery's management.

#### **OVERVIEW OF THE FINANCIAL STATEMENTS**

The Nebraska Legislature established the Nebraska Lottery (Lottery) on February 24, 1993. The Lottery is to provide instant win games and on-line random number selection games. The Lottery began selling instant (scratch) tickets on September 11, 1993, and began selling on-line (lotto) tickets on July 21, 1994. The Lottery is a division of the Nebraska Department of Revenue and as such, the financial summaries presented here and the related comments are for the Lottery's activities only and do not include the Department of Revenue's activities or statements.

The Lottery accounts for its financial transactions as an enterprise fund. Enterprise funds are used to account for governmental operations that are financed and operated in a manner similar to private business. The Lottery uses the accrual basis of accounting. In the annual report issued by the Lottery, there are three financial reports.

**1) Statement of Net Position**

This report will show the assets, liabilities, and net position ("equity") of the Lottery as of June 30, 2017. This report is basically the balance sheet for a private business.

**2) Statement of Revenues, Expenses, and Changes in Net Position**

This report will show the revenue, expenses, transfers to other funds, and changes in net position for the Lottery for the fiscal year. This report would be similar to an income statement or a profit-loss statement for a private business.

**3) Statement of Cash Flows**

This report is an analysis of the sources of cash flows into the Lottery and out of the Lottery for the fiscal year.

#### **DISCUSSION OF NET POSITION**

While reviewing the Summary of Net Position, it must be compared to the prior year's Summary to see the changes in the various classifications (see Table A below). The largest asset change was Cash and Cash Equivalents, which decreased about \$800,000. This cash was used to reduce Account Payables, which went down \$1.1 million. The other portion was cash that was not collected as Accounts Receivables/Reserves went up \$200,000 (essentially this is more money that was not collected at the end of this fiscal year as there were only five days of revenue that had not been collected last year whereas six days were uncollected in this year).

The largest liability change was the Accounts Payable classification this year. There was a decrease of \$1.1 million mentioned above. The amounts owed to our contractual services vendor, IGT, decreased as did the payable to our advertising vendor, SKAR Advertising. Another \$200,000 decrease was in the amount owed to the Multi-State Lottery Association

NEBRASKA LOTTERY

**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
(Continued)

(MUSL), which operates our multi-jurisdiction lotto games. A lot of these changes are due to the timing of sales, billings, and the timing of advertising projects.

In the Net Position section, the Unrestricted Assets went up about \$400,000, which is the result of transferring less money to the beneficiary trust funds than the profit that had been generated this year.

Table A  
**Summary of Net Position**

	FY 2017	FY 2016	Change
<b>CURRENT ASSETS</b>			
Cash and Cash Equivalents	\$ 7,439,920	\$ 8,263,811	\$ (823,891)
Accounts Receivable and Reserves on Deposit	6,029,226	5,822,814	206,412
Prepaid Prizes and Costs	68,474	9,600	58,874
<b>TOTAL CURRENT ASSETS</b>	<u>13,537,620</u>	<u>14,096,225</u>	<u>(558,605)</u>
<b>NONCURRENT ASSETS</b>			
Reserves on Deposit	2,410,743	2,349,961	60,782
Furniture, Fixtures, Equipment (Net)	70,272	86,759	(16,487)
<b>TOTAL NONCURRENT ASSETS</b>	<u>2,481,015</u>	<u>2,436,720</u>	<u>44,295</u>
<b>TOTAL ASSETS</b>	<u>\$ 16,018,635</u>	<u>\$ 16,532,945</u>	<u>\$ (514,310)</u>
<b>CURRENT LIABILITIES</b>			
Accounts Payable	\$ 1,448,415	\$ 2,593,648	\$ (1,145,233)
Compensated Absences and Accrued Payroll Payable	108,687	94,138	14,549
Prizes Payable	6,459,861	6,421,263	38,598
Other Accrued Liabilities	395,052	293,606	101,446
<b>TOTAL CURRENT LIABILITIES</b>	<u>8,412,015</u>	<u>9,402,655</u>	<u>(990,640)</u>
<b>NONCURRENT LIABILITIES</b>			
Compensated Absences Payable	267,080	245,860	21,220
<b>TOTAL NONCURRENT LIABILITIES</b>	<u>267,080</u>	<u>245,860</u>	<u>21,220</u>
<b>TOTAL LIABILITIES</b>	<u>\$ 8,679,095</u>	<u>\$ 9,648,515</u>	<u>\$ (969,420)</u>
<b>NET POSITION</b>			
Invested in Capital Assets	\$70,272	\$86,759	\$(16,487)
Restricted for Future Prizes	2,410,743	2,349,961	60,782
Unrestricted Assets	4,858,525	4,447,710	410,815
<b>TOTAL NET POSITION</b>	<u>\$ 7,339,540</u>	<u>\$ 6,884,430</u>	<u>\$ 455,110</u>

## NEBRASKA LOTTERY

### MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

#### **DISCUSSION OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION**

After a record-setting sales year last year, the Lottery had decreased sales this year of \$5.6 million (see Table B below). The Lottery had an upswing in sales for scratch of about 4.5% (roughly \$4.4 million in sales) but lotto suffered a 12% decrease (about \$10 million in sales). On the lotto side, sales decreased mainly in Powerball. In 2016, Powerball had a record jackpot of \$1.5 billion, which led to historical sales for the Lottery in that year. For 2017, the largest Powerball jackpot was less than \$500 million. The number of large jackpot runs and the size of the jackpots materially affect weekly lotto sales.

On the scratch side, sales increased about \$4.4 million. The largest increase was in the \$10 price point (\$6.3 million) most of which was due to the discontinuation of the \$15 price point. While the \$1, \$3, and of course the \$15 price points saw decreased sales, the \$2, \$5, \$10, and \$20 price points saw increases.

The Prize Expense went down about \$2.7 million. This can be attributed to lower sales than last year. The lower sales also affected the Contractual Services Expense (costs related to IGT which are based on a percentage of sales) as it was about \$200,000 less than last year as was the Retailer Commissions which was about \$300,000 less too.

The Transfers to Other Funds had a decrease of almost \$1.5 million. With lower lotto sales, which has a higher profit margin, the Lottery had decreased profits and was not able to transfer as much to the beneficiary trust funds this year.

(Continued on Next Page)

# NEBRASKA LOTTERY

## MANAGEMENT'S DISCUSSION AND ANALYSIS (Concluded)

Table B

### Summary of Revenues, Expenses, and Changes in Net Position

	FY 2017	FY 2016	Change
<b>REVENUES</b>			
Sales	\$ 175,967,645	\$ 181,909,582	\$ (5,941,937)
Sales Returns	(2,148,539)	(2,436,827)	288,288
<b>OPERATING REVENUE</b>	173,819,106	179,472,755	(5,653,649)
Interest Income	299,317	299,512	(195)
Other Income	8,752	13,670	(4,918)
Multi-State Lottery Assoc. Income	23,421	17,961	5,460
<b>NON-OPERATING REVENUE</b>	331,490	331,143	347
<b>TOTAL REVENUES</b>	\$ 174,150,596	\$ 179,803,898	\$ (5,653,302)
<b>EXPENSES</b>			
Prize Expense	\$ 101,901,594	\$ 104,644,944	\$ (2,743,350)
Retailer Commissions	11,127,474	11,400,607	(273,133)
Contractual Services	11,971,020	12,148,324	(177,304)
Marketing Expense	5,426,184	5,758,466	(332,282)
Lottery Operating Expense	1,991,557	1,866,887	124,670
<b>TOTAL EXPENSES</b>	\$ 132,417,829	\$ 135,819,228	\$ (3,401,399)
<b>NET INCOME BEFORE TRANSFERS</b>	\$ 41,732,767	\$ 43,984,670	\$ (2,251,903)
<b>TRANSFERS TO OTHER FUNDS</b>	\$ 41,277,657	\$ 42,782,923	\$ (1,505,266)
<b>CHANGE IN NET POSITION</b>	<u>\$ 455,110</u>	<u>\$ 1,201,747</u>	<u>\$ (746,637)</u>

### **OTHER ITEMS OF NOTE**

The unpredictability of the Powerball, Mega Millions, and Pick 5 jackpots along with external forces that affect player purchases (fuel prices, economic situations, international tensions, other entertainment options, etc.) could have a material effect on future sales and future transfers to the beneficiary trust funds.

### **CONTACTING LOTTERY MANAGEMENT**

This financial report is required as part of Governmental Accounting Standards Board (GASB) Statement 34 and is prepared to provide the readers such as the Legislature, the public, and other interested parties with an overview of the financial results of the Nebraska Lottery's activities. If you have any questions about this report, please contact the Nebraska Lottery at PO Box 98901, Lincoln, NE 68509-8901.

NEBRASKA LOTTERY  
STATEMENT OF NET POSITION  
AS OF JUNE 30, 2017

**ASSETS**

**CURRENT ASSETS:**

Cash and Cash Equivalents	\$ 7,439,920
Accounts Receivable, Net of Allowance (Note 4)	5,670,069
Prepaid Prizes	68,474
Reserves on Deposit (Note 6)	359,157
<b>TOTAL CURRENT ASSETS</b>	<b>13,537,620</b>

**NONCURRENT ASSETS:**

Reserves on Deposit (Note 6)	2,410,743
Capital Assets:	
Furniture, Fixtures, and Equipment (Note 5)	276,651
Less: Accumulated Depreciation	206,379
Total Capital Assets, Net	70,272
<b>TOTAL NONCURRENT ASSETS</b>	<b>2,481,015</b>

<b>TOTAL ASSETS</b>	<b>\$ 16,018,635</b>
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**LIABILITIES**

**CURRENT LIABILITIES:**

Accounts Payable	\$ 544,277
Vendors Payable	904,138
Compensated Absences Payable (Note 7)	26,415
Accrued Payroll Payable	82,272
Withheld Taxes on Prizes Paid	29,200
Prize Payable	6,459,861
Due to Other Funds	15,901
Other Accrued Liabilities	349,951
<b>TOTAL CURRENT LIABILITIES</b>	<b>8,412,015</b>

**NONCURRENT LIABILITIES:**

Compensated Absences Payable (Note 7)	267,080
<b>TOTAL NONCURRENT LIABILITIES</b>	<b>267,080</b>

<b>TOTAL LIABILITIES</b>	<b>8,679,095</b>
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**NET POSITION**

Invested in Capital Assets	70,272
Restricted for Future Prizes (Note 6)	2,410,743
Unrestricted (Note 10)	4,858,525
<b>TOTAL NET POSITION</b>	<b>7,339,540</b>

<b>TOTAL LIABILITIES AND NET POSITION</b>	<b>\$ 16,018,635</b>
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The accompanying Notes to the Financial Statements are an integral part of this statement.

NEBRASKA LOTTERY  
**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION**  
 FOR THE YEAR ENDED JUNE 30, 2017

**OPERATING REVENUE:**

Sales	\$ 175,967,645
Less: Sales Returns	2,148,539
<b>TOTAL OPERATING REVENUE</b>	<u>173,819,106</u>

**OPERATING EXPENSES:**

Prize Expense, Net of Unclaimed Prizes (Note 1c)	101,901,594
Retailer Commissions	11,127,474
Contractual Services Expense	11,971,020
Marketing	5,426,184
Lottery Operating	1,991,557
<b>TOTAL OPERATING EXPENSES</b>	<u>132,417,829</u>

<b>OPERATING INCOME</b>	41,401,277
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**NONOPERATING REVENUE:**

Interest Income	299,317
Other Income	8,752
Multi-State Lottery Association Income	23,421
<b>TOTAL NONOPERATING REVENUE</b>	<u>331,490</u>

<b>INCOME BEFORE OPERATING TRANSFERS</b>	41,732,767
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<b>TRANSFERS TO OTHER FUNDS</b> (Note 9)	<u>(41,277,657)</u>
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<b>CHANGE IN NET POSITION</b>	455,110
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<b>TOTAL NET POSITION, BEGINNING OF YEAR</b>	<u>6,884,430</u>
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<b>TOTAL NET POSITION, END OF YEAR</b>	<u><u>\$ 7,339,540</u></u>
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The accompanying Notes to the Financial Statements are an integral part of this statement.

**NEBRASKA LOTTERY**  
**STATEMENT OF CASH FLOWS**  
**FOR THE YEAR ENDED JUNE 30, 2017**

**CASH FLOWS FROM OPERATING ACTIVITIES:**

Ticket Sales	\$ 173,452,276
Prizes Paid to Winners	(102,009,565)
Commissions Paid to Retailers	(11,122,583)
Paid to Contractors for Goods and Services	(18,316,238)
Paid to Employees	(1,523,455)
Other Operating Expenses	(335,426)
Net Cash Provided by Operating Activities	<u>40,145,009</u>

**CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:**

Paid to Nebraska Education Improvement Fund	(18,146,057)
Paid to Nebraska State Fair Support and Improvement Cash Fund	(4,077,766)
Paid to Nebraska Environmental Trust Fund	(18,146,057)
Paid to Compulsive Gamblers Assistance Fund	(907,777)
Net Cash Used in NonCapital Financing Activities	<u>(41,277,657)</u>

**CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:**

Purchase of Property and Equipment	(13,981)
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**CASH FLOWS FROM INVESTING ACTIVITIES:**

Interest on Cash	299,317
Multi-State Lottery Association Income	23,421
Net Cash Provided by Investing Activities	<u>322,738</u>

**NET DECREASE IN CASH AND CASH EQUIVALENTS** (823,891)

**CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR** 8,263,811

**CASH AND CASH EQUIVALENTS AT END OF YEAR** \$ 7,439,920

**RECONCILIATION OF OPERATING INCOME TO  
NET CASH PROVIDED BY OPERATING ACTIVITIES:**

Operating Income	\$ 41,401,277
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:	
Depreciation Expense	39,220
Changes in Assets (Increase) Decrease in:	
Reserves on Deposit	(3,095)
Prepaid Prizes	(58,874)
Accounts Receivable (Net)	(264,099)
Changes in Liabilities Increase (Decrease) in:	
Other Accrued Liabilities	147,292
Accounts Payable and Due to Other Funds	(186,533)
Prizes Payable	38,598
Compensated Absences and Accrued Payroll Payable	35,769
Withheld Taxes on Prizes Paid	(39,196)
Vendors Payable	(965,350)
Total Adjustments	<u>(1,256,268)</u>
Net Cash Provided by Operating Activities	<u><u>\$ 40,145,009</u></u>

The accompanying Notes to the Financial Statements are an integral part of this statement.



# NEBRASKA LOTTERY

## NOTES TO THE FINANCIAL STATEMENTS

For the Fiscal Year Ended June 30, 2017

### 1. **Summary of Significant Accounting Policies**

#### **A. Basis of Presentation**

The accompanying basic financial statements of the Nebraska Department of Revenue, Lottery Division, (Nebraska Lottery) have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP), as applied to governmental units. As the Nebraska Lottery is a business-type activity, the financial statements presented are the financial statements required by Governmental Accounting Standards Board (GASB) Statement Number 34 for an enterprise fund. GASB is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

The basic financial statements have been prepared primarily from data maintained by the Nebraska Lottery on computer systems provided by the lottery-services vendor and from accounts maintained by the State Accounting Administrator of the Department of Administrative Services.

#### **B. Reporting Entity**

The Nebraska Lottery was created on February 24, 1993, by the Nebraska Legislature as a division of the Nebraska Department of Revenue, established under and governed by the laws of the State of Nebraska. As such, the Nebraska Lottery is exempt from State and Federal income taxes. The financial statements include all funds of the Nebraska Lottery. The Nebraska Lottery is to provide an instant win and a random number selection on-line lottery. The net proceeds, as outlined in Neb. Rev. Stat. § 9-812 (Neb. Laws 2017, LB 512, § 5), are to be transferred to the Compulsive Gamblers Assistance Fund, the Nebraska Education Improvement Fund, the Nebraska Environmental Trust Fund, and the Nebraska State Fair Support and Improvement Cash Fund, a fund of the State Fair Board. The financial statements include only the Nebraska Lottery and are not intended to present the financial position of the Nebraska Department of Revenue (Department) or the results of operations and changes in net positions of the Department as a whole. The Department is part of the primary government for the State of Nebraska's reporting entity.

The Nebraska Lottery has also considered all potential component units for which it is financially accountable, including other organizations that are fiscally dependent on the Lottery or whose relationship with the Nebraska Lottery is so significant that exclusion would be misleading or incomplete. GASB has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Nebraska Lottery to impose its will on that organization, or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the Nebraska Lottery. The Nebraska Lottery is also considered financially accountable if an organization is fiscally dependent on it, and there is potential for the organization to

# NEBRASKA LOTTERY

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 1. Summary of Significant Accounting Policies (Continued)

provide specific financial benefits to, or impose specific financial burdens on, the Nebraska Lottery, regardless of whether the organization has (1) a separately elected governing board, (2) a governing board appointed by a higher level of government, or (3) a jointly appointed board.

These financial statements present the Nebraska Lottery. No component units were identified. The Nebraska Lottery is part of the primary government for the State of Nebraska's reporting entity.

#### C. **Measurement Focus, Basis of Accounting**

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus and basis of accounting. Basis of accounting refers to when revenues and expenses are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied.

The Nebraska Lottery's financial statements were reported using the economic resources measurement focus and the accrual basis of accounting. With the economic resources measurement focus, all assets and all liabilities associated with the operations are included on the Statement of Net Position. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Net Position is segregated into restricted and unrestricted. The Lottery's operating statements present increases (e.g., revenues) and decreases (e.g., expenses) in net position.

It is the policy of the State to spend restricted resources only when unrestricted resources are insufficient or unavailable. When both restricted and unrestricted resources are available for use, it is the Lottery's policy to use unrestricted resources first, then restricted resources, as they are needed.

Revenues generated from the sale of lottery tickets are reported as operating revenues. Transactions that are capital financing, non-capital financing, or investing related are reported as non-operating revenues. All expenses related to operating the Nebraska Lottery are reported as operating expenses. All other expenses are reported as non-operating expenses.

Instant ticket revenue is recognized when tickets are sold to the retailer, and on-line revenue is recognized after the drawing is completed for the respective wagers. A 5.5% - 6.0% retailer commission and a prize expense are recognized at the same time. Revenues from the sale of on-line tickets for future drawings and the related agent commission and prize expense are deferred until the drawings are held.

# NEBRASKA LOTTERY

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 1. **Summary of Significant Accounting Policies** (Continued)

Prize expense is recognized in the same period ticket revenue is recognized based on the predetermined prize structure for each game. Because the instant prize-winning tickets are randomly distributed throughout the tickets, and some winning tickets will be lost, destroyed, or unredeemed for other reasons, there will be differences between amounts accrued and the amounts actually paid. These differences, denoted as unclaimed prizes, are recognized as a reduction of prize expense 181 days after the close of each instant game and 181 days after each draw for on-line games as prizes unclaimed for 180 days expire. Unclaimed prizes for the fiscal year ended June 30, 2017, totaled \$3,302,135.

The activities of the Nebraska Lottery are accounted for as an enterprise fund. Enterprise funds are used to account for governmental operations that are financed and operated in a manner similar to private business enterprises and where the governing body has decided that periodic determination of revenues earned, expenses incurred, and net position is appropriate.

#### **D. Cash and Cash Equivalents**

In addition to bank accounts and petty cash, this classification includes all short-term investments, such as certificates of deposit, repurchase agreements, and U.S. treasury bills. These short-term investments may have original maturities (remaining time to maturity at acquisition) greater than three months; however, cash is available and is considered cash and cash equivalents for reporting purposes. These investments are stated at cost, which at June 30, 2017, approximates market. Banks pledge collateral, as required by law, to guarantee State funds held in time and demand deposits.

Cash and cash equivalents are under the control of the State Treasurer or other administrative bodies, as determined by law. All cash deposited with the State Treasurer is initially maintained in a pooled cash account. On a daily basis, the State Treasurer invests cash not needed for current operations with the State's Investment Council, which maintains an operating investment pool for such investments. Interest earned on these investments is allocated to funds based on their percentage of the investment pool.

#### **E. Budgetary Process**

The State's biennial budget cycle ends on June 30 of the odd-numbered years. By September 15, prior to a biennium, the Nebraska Lottery and all other State agencies must submit their budget requests for the biennium beginning the following July 1. The requests are submitted on forms that show estimated funding requirements by programs, sub-programs, and activities. The Executive Branch reviews the requests, establishes priorities, and balances the budget within the estimated resources available during the upcoming biennium.

The Governor's budget bill is submitted to the Legislature in January. The Legislature considers revisions to the bill and presents the appropriations bill to the Governor for signature. The Governor may: a) approve the appropriations bill in its entirety; b) veto the bill; or c) line item veto certain sections of the bill. Any vetoed bill or line item can be overridden by a three-fifths vote of the Legislature.

# NEBRASKA LOTTERY

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 1. **Summary of Significant Accounting Policies** (Continued)

The approved appropriations will generally set spending limits for a particular program within the agency. Within the agency or program, the Legislature may provide funding from one to five budgetary fund types. Thus, the control is by fund type, within a program, within an agency.

Appropriations are usually made for each year of the biennium, with unexpended balances being reappropriated at the end of the first year of the biennium. For most appropriations, balances lapse at the end of the biennium.

All State budgetary expenditures for the enterprise fund type are made pursuant to the appropriations, which may be amended by the Legislature, upon approval by the Governor. State agencies may reallocate the appropriations between major objects of expenditure accounts, except that the Legislature's approval is required to exceed the personal service limitations contained in the appropriations bill. Increases in total appropriations must also be approved by the Legislature as a deficit appropriations bill.

Revenues are not budgeted.

#### **F. Receivables**

Receivables are reported net of estimated allowances for uncollectible amounts, which are estimated based upon past collection experience and current economic conditions.

#### **G. Capital Assets**

Capital assets include equipment that is valued at cost when historical records are available and at estimated historical cost when no historical records exist. Donated capital assets are valued at their estimated fair market value on the date received. Generally, equipment that has a cost in excess of \$1,500 at the date of acquisition and has an expected useful life of more than one year is capitalized. All computer towers, laptops, notebook computers, and tablet computers purchased after July 1, 2015, are also required to be capitalized regardless of cost.

Equipment is depreciated using the straight line method over the estimated useful life of three to seven years.

#### **H. Compensated Absences**

All permanent employees working for the Nebraska Lottery earn sick and annual leave and are allowed to accumulate compensatory leave rather than being paid overtime. Temporary and intermittent employees are not eligible for paid leave. The liability has been calculated using the vesting method, in which leave amounts, for both employees currently eligible to receive termination payments and other employees expected to become eligible in the future to receive such payments upon termination, are included.

Nebraska Lottery employees accrue vested annual leave at a variable rate based on years of service. Generally, accrued annual leave cannot exceed 35 days at the end of a calendar year.

# NEBRASKA LOTTERY

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 1. **Summary of Significant Accounting Policies** (Concluded)

Employees accrue sick leave at a variable rate based on years of service. In general, accrued sick leave cannot exceed 180 days. There is no maximum limit on the accumulation of sick leave days for employees under certain labor contracts. Sick leave is not vested except upon either death or reaching the retirement eligibility age of 55, at which time the State is liable for 25 percent of the employee's accumulated sick leave. Employees under certain labor contracts can only be paid a maximum of 50 or 60 days.

The Nebraska Lottery's financial statements recognize the expense and accrued liability when vacation and compensatory leave is earned or when sick leave is expected to be paid as termination payments.

#### **I. Use of Estimates**

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 at June 30, 2017, and revenues and expenditures during the reporting period. Actual results could differ from those estimates.

### 2. **Contingencies and Commitments**

**Risk Management.** The Nebraska Lottery is exposed to various risks of loss related to torts, theft of, damage to, or destruction of assets, errors or omissions, injuries to employees, and natural disasters. The Nebraska Lottery, as part of the primary government for the State, participates in the State's risk management program. The Nebraska Department of Administrative Services is responsible for maintaining the insurance and self-insurance programs for the State. The State generally self-insures for general liability, employee health care, employee indemnification, and workers' compensation. The State has chosen to purchase insurance for the following:

- A. Motor vehicle liability with vehicular pursuit, which is insured for the first \$5 million of exposure per accident with a self-insured retention of \$300,000 and \$300,000 corridor retention. Motor vehicle liability is insured for \$1 million with a self-insured retention of \$200,000, and with excess coverage of \$400 million. Insurance is also purchased, with various limits and deductibles, for physical damage and uninsured and underinsured motorists. State agencies have the option to purchase coverage for physical damage to vehicles. There is a \$5,000 deductible for this coverage.
- B. Life insurance for eligible employees.
- C. Crime coverage, with a limit of \$31 million for each loss and a \$25,000 self-insured retention per incident subject to specific conditions, limits, and exclusions.

## NEBRASKA LOTTERY

### NOTES TO THE FINANCIAL STATEMENTS (Continued)

#### 2. **Contingencies and Commitments** (Concluded)

- D. Real and personal property on a blanket basis for losses up to \$401 million, with a self-insured retention of \$200,000 per loss occurrence. Newly acquired properties are covered up to \$10 million for 120 days, and after 120 days, if the property has not been reported, the limit decreases to \$5 million. The perils of flood, earthquake, and acts of terrorism have various coverage, sub-limits, and self insurance. State agencies have the option to purchase building contents and inland marine coverage.

Details of the various insurance coverages are available from the Nebraska Department of Administrative Services – Risk Management Division.

No settlements exceeded commercial insurance coverage in any of the past three fiscal years. Workers' compensation is funded in the Workers' Compensation Internal Service Fund through assessments on each agency based on total agency payroll and past experience. Tort claims, theft of, damage to, or destruction of assets, errors or omissions, and natural disasters would be funded through the State General Fund or by individual agency assessments, as directed by the Legislature, unless covered by purchased insurance. No amounts for estimated claims have been reported in the Nebraska Lottery's financial statements. Health care insurance is funded in the Insurance Trust Funds through a combination of employee and State contributions.

**Litigation.** The potential amount of liability involved in litigation pending against the Nebraska Lottery, if any, could not be determined at this time. However, it is the Nebraska Lottery's opinion that final settlement of those matters should not have an adverse effect on the Nebraska Lottery's ability to administer current programs. Any judgment against the Nebraska Lottery would have to be processed through the State Claims Board and be approved by the Legislature.

#### 3. **State Employees Retirement Plan (Plan)**

The single-employer Plan became effective by statute on January 1, 1964. The Plan consists of a defined contribution option and a cash balance benefit. The cash balance benefit is a type of defined benefit plan. Each member employed and participating in the retirement system prior to January 1, 2003, elected either to continue participation in the defined contribution option or to begin participation in the cash balance benefit. The defined contribution option is closed to new entrants. All new members of the Plan on and after January 1, 2003, become members of the cash balance benefit. The benefits and funding policy of the Plan is established and can only be amended by the Nebraska Legislature.

All permanent full-time employees are required to begin participation in the retirement system upon employment. All permanent part-time employees, who have attained the age of eighteen years, may exercise the option to begin participation in the retirement system.

# NEBRASKA LOTTERY

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 3. State Employees Retirement Plan (Plan) (Concluded)

**Contribution.** Per statute, each member contributes 4.8% of his or her monthly compensation. The Nebraska Lottery matches the member's contribution at a rate of 156%. The employee's and employer's contributions are kept in separate accounts.

The employee's account is fully vested. The employer's account is fully vested after a total of three years of participation in the system, including credit for participation in another Nebraska governmental plan prior to actual contribution to the Plan.

**Defined Contribution Option.** Upon attainment of age 55, regardless of service, the retirement allowance is to be equal to the sum of the employee and employer accounts. Members have several forms of payment available, including withdrawals, deferrals, annuities, or a combination of these.

**Cash Balance Benefit.** Upon attainment of age 55, regardless of service, the retirement allowance shall be equal to the accumulated employee and employer cash balance accounts, including interest credits, annuitized for payment in the normal form. The normal form of payment is single life annuity with five year certain, payable monthly. Members will have the option to convert their member cash balance account to a monthly annuity with built in cost-of-living adjustments of 2.5% annually. Also available are additional forms of payment allowed under the Plan that are actuarially equivalent to the normal form, including the option of lump-sum or partial lump-sum.

For the fiscal year ended June 30, 2017, employees contributed \$58,085, and the Nebraska Lottery contributed \$90,612. A separate plan report is issued by and can be obtained from the Nebraska Public Employees Retirement System. This report contains full pension-related disclosures.

The State of Nebraska Comprehensive Annual Financial Report (CAFR) also includes pension-related disclosures. The CAFR report is available from the Nebraska Department of Administrative Services – Accounting Division or on the Nebraska Auditor of Public Accounts' website at [www.auditors.nebraska.gov](http://www.auditors.nebraska.gov).

### 4. Receivables

Retailers comprised principally of grocery stores, convenience stores, and off-sale liquor stores serve as the primary distribution channel for lottery sales to the general public. No one retailer accounts for a significant amount of the Nebraska Lottery's sales or accounts receivable. Retailers must pay for instant lottery tickets 45 days after activation or when the pack is 70% validated, whichever comes first. Retailers pay for on-line tickets each Wednesday for balances due through the previous Saturday. The retailers' accounts receivable is net of allowance for uncollectible in the amount of \$36,181.

Accounts Receivable	
Retailers (net)	\$ 5,670,069
Other	-
Total	<u>\$ 5,670,069</u>

# NEBRASKA LOTTERY

## NOTES TO THE FINANCIAL STATEMENTS (Continued)

### 5. Capital Assets

Capital asset activity for the year ended June 30, 2017, was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital Assets: Furniture, Fixtures, and Equipment	\$ 268,878	\$ 22,733	\$ 14,960	\$ 276,651
Less: Accumulated Depreciation	182,119	39,220	14,960	206,379
Total Capital Assets, Net	<u>\$ 86,759</u>	<u>\$ (16,487)</u>	<u>\$ -</u>	<u>\$ 70,272</u>

### 6. On-Line Games

During the fiscal year ended June 30, 2017, the Nebraska Lottery offered a variety of on-line games, as described in the following table.

Game Name	Operated by	Nebraska's Share of Prize Reserves
Powerball®	MUSL	\$ 1,759,128
Nebraska Pick 5®	Nebraska Lottery	N/A
Nebraska Pick 3®	Nebraska Lottery	N/A
MyDaY®	Nebraska Lottery	N/A
Mega Millions®	MUSL	523,933
2by2®	MUSL	127,682
		<u>\$ 2,410,743</u>

The Nebraska Lottery is a member of the Multi-State Lottery Association (MUSL), which operates games on behalf of participating state lotteries. Each MUSL member sells on-line game tickets through its agents and makes weekly payments to MUSL in an amount equal to each game's prize structure, less amounts retained for prizes paid directly to the winners by each member lottery. MUSL maintains prize reserve funds on each game to serve as a contingency reserve to protect from unforeseen prize liabilities. The money in these reserve funds is to be used at the discretion of the MUSL Board of Directors. The prize reserve funds are refundable to MUSL members if MUSL disbands or if a member leaves MUSL. Members leaving MUSL must wait one year before receiving their remaining share of the prize reserve funds.

In addition, the Nebraska Lottery has \$359,157 held by MUSL, reported on the Statement of Net Position as Reserves on Deposit (Current), which can be used to pay the Nebraska Lottery's portion of MUSL's operating budget, any MUSL legal expenses, and other expenses incurred by MUSL. These funds are not tied directly to any MUSL game.



# NEBRASKA LOTTERY

## NOTES TO THE FINANCIAL STATEMENTS

(Continued)

### 6. On-Line Games (Concluded)

The Powerball® and Mega Millions® grand prizes can be paid either as annual installments or a lump sum cash payment, depending on the selection of the winner when claiming the prize. If the winner selects annual installments, MUSL purchases bonds, which are held in trust to fund the future installments. Maturities are staggered in order to provide adequate cash flow for each installment. MUSL is responsible for paying amounts owed to the grand prize winners. The assets and related liabilities are reflected in MUSL's financial statements and, therefore, are not reflected in the Nebraska Lottery's financial statements.

### 7. Noncurrent Liabilities

Changes in noncurrent liabilities for the year ended June 30, 2017, are summarized as follows:

	Beginning Balance	Increases	Decreases	Ending Balance	Amounts Due Within One Year
Compensated Absences	\$ 270,176	\$ 32,359	\$ 9,040	\$ 293,495	\$ 26,415

### 8. Lease Commitments

The minimum annual lease payments for operating leases as of June 30, 2017, are as follows:

Year	Activities
2018	\$ 73,801
2019	\$ 73,801
2020	\$ 73,801
2021	\$ 73,801
2022	\$ 73,801
2023-2027	\$ 369,005
Total	\$ 738,010

The Nebraska Lottery has the option to extend the lease agreement by two 5-year periods for a total additional period of 10 years. Total operating lease payments for the year ended June 30, 2017, were \$61,681.

### 9. Significant Compliance Requirements

Article III, § 24, of the Nebraska Constitution sets out the basic requirements for the transfer of lottery proceeds to certain beneficiary funds, specifying that a portion of those revenues are to "be used for education as the Legislature may direct."

## NEBRASKA LOTTERY

### NOTES TO THE FINANCIAL STATEMENTS (Continued)

#### 9. **Significant Compliance Requirements** (Continued)

Neb. Rev. Stat. § 9-812(2) (Neb. Laws 2017, LB 512, § 5) offers the following legislative directive for the transfer of lottery proceeds:

*A portion of the dollar amount of the lottery tickets which have been sold on an annualized basis shall be transferred from the State Lottery Operation Trust Fund to the Education Innovation Fund, the Nebraska Opportunity Grant Fund, the Nebraska Education Improvement Fund, the Nebraska Environmental Trust Fund, the Nebraska State Fair Board, and the Compulsive Gamblers Assistance Fund as provided in subsection (3) of this section. The dollar amount transferred pursuant to this subsection shall equal the greater of (a) the dollar amount transferred to the funds in fiscal year 2002-03 or (b) any amount which constitutes at least twenty-two percent and no more than twenty-five percent of the dollar amount of the lottery tickets which have been sold on an annualized basis. To the extent that funds are available, the Tax Commissioner and director may authorize a transfer exceeding twenty-five percent of the dollar amount of the lottery tickets sold on an annualized basis.*

Additionally, § 9-812(3) provides these further instructions:

*Of the money available to be transferred to the Education Innovation Fund, the Nebraska Opportunity Grant Fund, the Nebraska Education Improvement Fund, the Nebraska Environmental Trust Fund, the Nebraska State Fair Board, and the Compulsive Gamblers Assistance Fund:*

*(a) The first five hundred thousand dollars shall be transferred to the Compulsive Gamblers Assistance Fund to be used as provided in section 9-1006;*

*(b) Beginning July 1, 2016, forty-four and one-half percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the Nebraska Education Improvement Fund;*

*(c) Forty-four and one-half percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the Nebraska Environmental Trust Fund to be used as provided in the Nebraska Environmental Trust Act;*

*(d) Ten percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the Nebraska State Fair Board if the most populous city within the county in which the fair is located provides matching funds equivalent to ten percent of the funds available for transfer. Such matching funds may be obtained from the city and any other private or public entity, except that no portion of such matching funds shall be provided by the state. If the Nebraska State Fair ceases operations, ten percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the General Fund; and*

*(e) One percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the Compulsive Gamblers Assistance Fund to be used as provided in section 9-1006.*

## NEBRASKA LOTTERY

### NOTES TO THE FINANCIAL STATEMENTS (Concluded)

#### 9. **Significant Compliance Requirements** (Concluded)

As required under its enabling legislation, transfers of \$41,277,657 were made to other funds during the fiscal year.

The Nebraska Lottery develops game structures to comply with the minimum prize provision of its enabling legislation, which requires a minimum of 40 percent to be paid in prizes.

The Nebraska Lottery compares the social security number of each winner who has a per-wager prize in excess of \$500 against a list of social security numbers having an outstanding State tax liability or delinquent child support payments. Any delinquent payments are withheld from winnings and forwarded to the appropriate State agency. During the fiscal year, the Nebraska Lottery collected \$26,919 in delinquent State taxes and \$15,201 in delinquent child support payments.

Operating Transfers In/Out will not balance, and Due To/From Other Funds will not balance, within the Nebraska Lottery's financial statements, as the Lottery represents only part of the State's primary government.

#### 10. **Net Position**

The Nebraska Lottery's unrestricted net position represents funds not legally restricted for any specific purpose; however, the funds may be used only to fund additional prize pay-outs, transfers to the beneficiary funds, or additional operating expenses of the Nebraska Lottery. Management's intention is to use the unrestricted net position to fund additional prize pay-outs, retailer incentives, and other game enhancements.

#### 11. **Subsequent Events**

Beginning August 20, 2017, the Nebraska Lottery began offering the "Lucky for Life" game. "Lucky for Life" is a multi-state \$2 Lotto game with a top prize of \$1,000 per day for life. Other prizes include \$25,000 per year for life, and single prizes range from \$5,000 to \$3. Lifetime prizes can be paid as an annuity for the length of the winner's life or as a lump-sum payment. A minimum of 20 years' worth of payments is guaranteed with the annuity option. Additional information on the "Lucky for Life" game can be found on the "Lucky for Life" website at <http://www.luckyforlife.us/>.



## NEBRASKA AUDITOR OF PUBLIC ACCOUNTS

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

State Tax Commissioner  
Nebraska Department of Revenue, Lottery Division  
Lincoln, Nebraska

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the business-type activities of the Nebraska Department of Revenue, Lottery Division, (Nebraska Lottery) as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the Nebraska Lottery's basic financial statements, and have issued our report thereon dated June 30, 2017. The report was modified to emphasize that the financial statements present only the funds of the Nebraska Lottery.

### **Internal Control Over Financial Reporting**

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

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Nebraska Lottery'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 Nebraska Lottery's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

### **Purpose of this Report**

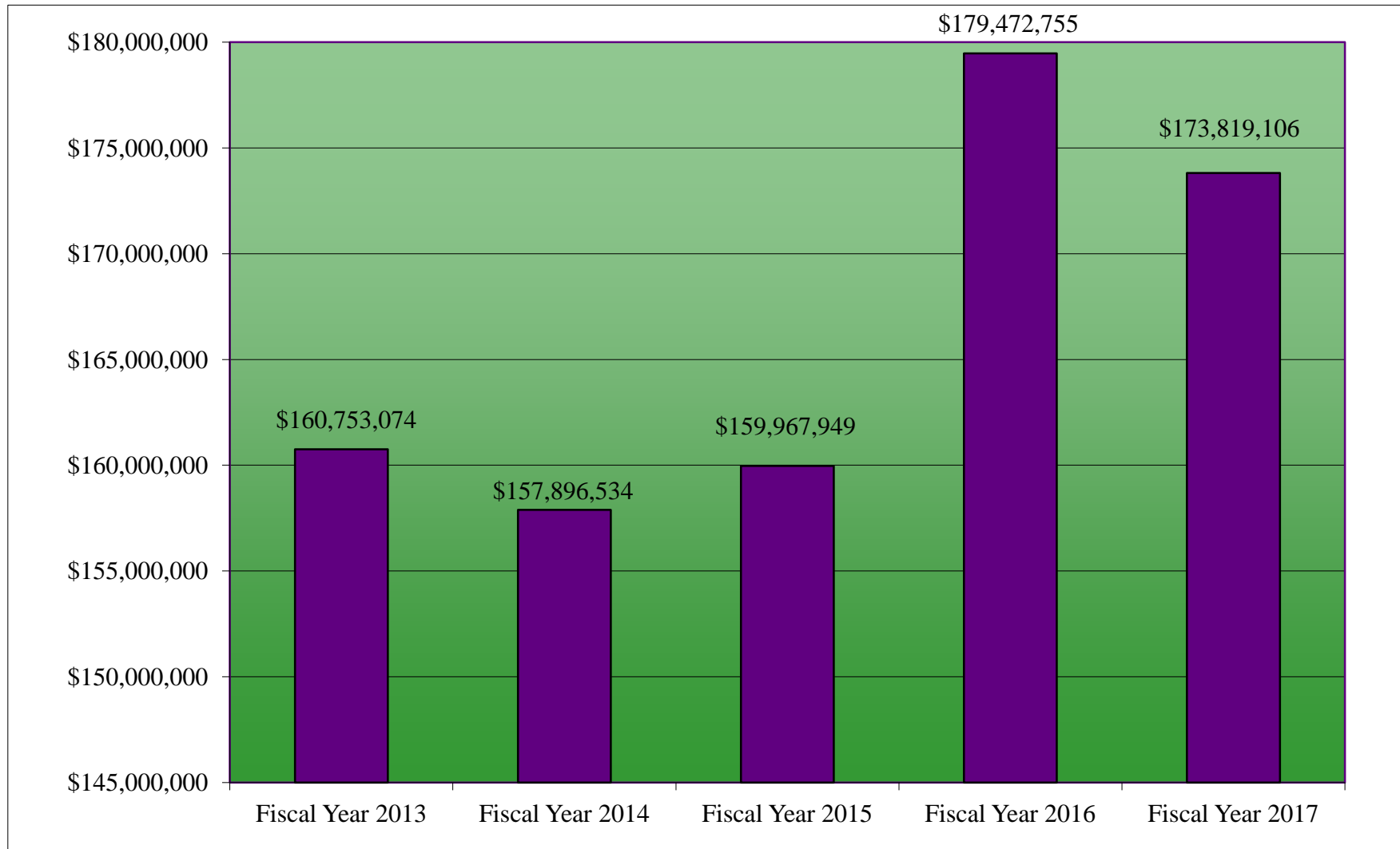
The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, not to provide an opinion on the effectiveness of the Nebraska Lottery's internal control or on compliance. This report is an integral part of an audit performed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



October 3, 2017

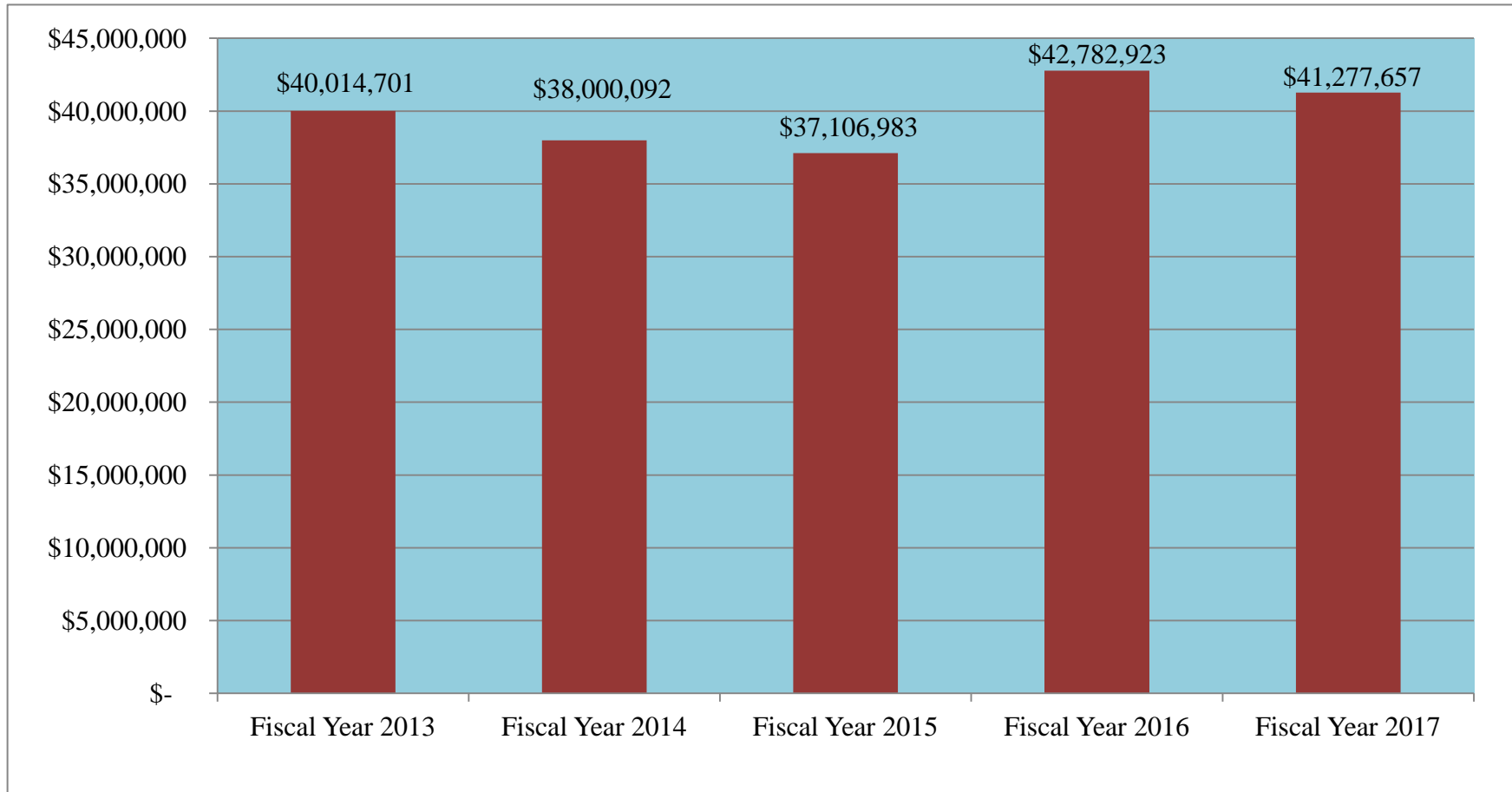
Zachary Wells, CPA  
Audit Manager  
Lincoln, Nebraska

**NEBRASKA LOTTERY**  
**LOTTERY TICKET SALES**  
For the Fiscal Years 2013 through 2017



Note: These sales are shown on an accrual basis.

**NEBRASKA LOTTERY**  
**TOTAL OPERATING TRANSFERS TO BENEFICIARY FUNDS**  
For the Fiscal Years 2013 through 2017



Note: The Total Operating Transfers include transfers to the Nebraska Environmental Trust Fund, the Education Innovation Fund, the Nebraska Opportunity Grant Fund, the Compulsive Gamblers Assistance Fund, Nebraska Education Improvement Fund, and the Nebraska State Fair Support and Improvement Cash Fund. These transfers are shown on a cash basis.

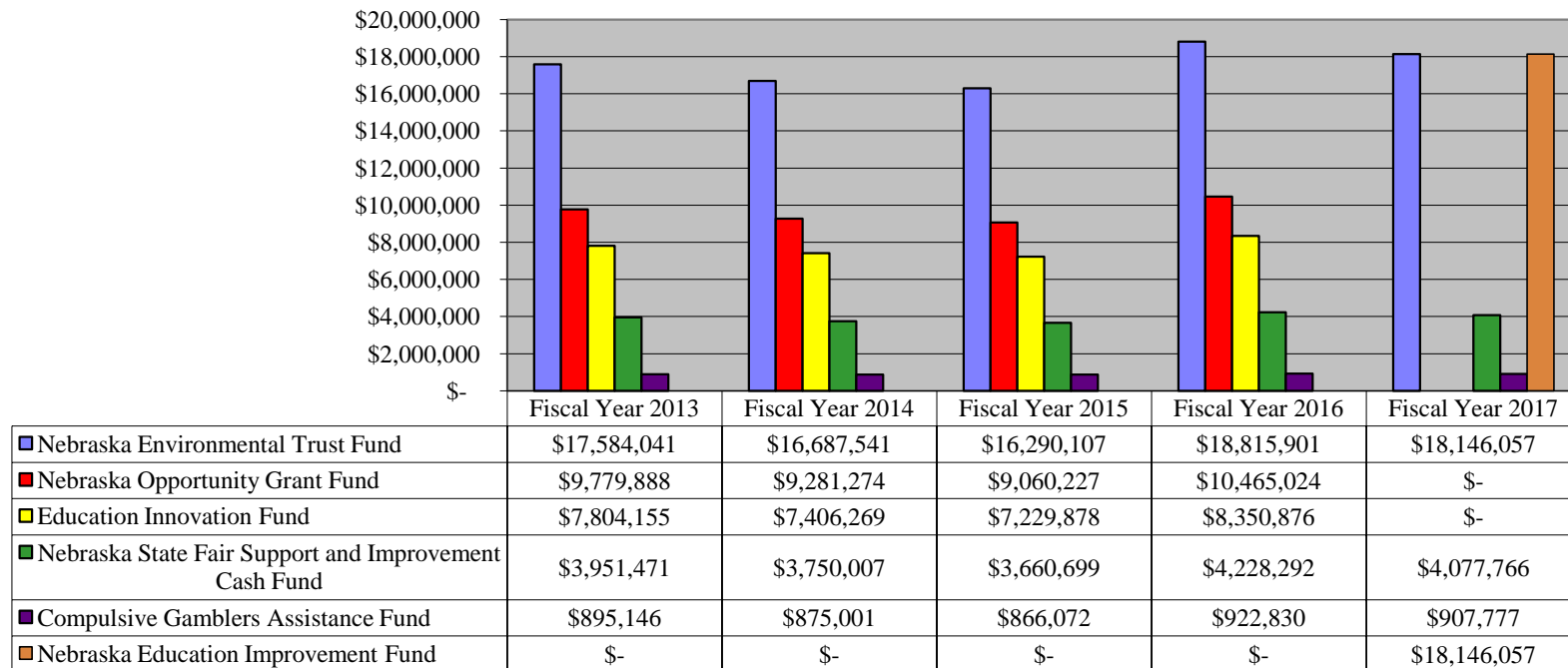
**NEBRASKA LOTTERY  
SCHEDULE OF CUMULATIVE OPERATING TRANSFERS  
TO BENEFICIARY FUNDS**

<u>Fiscal Year</u>	<u>Transfer Amount</u>
1994	\$ 10,931,811
1995	19,308,170
1996	20,486,304
1997	23,363,387
1998	18,740,463
1999	17,581,026
2000	17,887,538
2001	16,596,397
2002	18,235,952
2003	20,098,664
2004	20,807,945
2005	27,195,478
2006	27,601,895
2007	29,266,219
2008	31,008,281
2009	30,245,118
2010	32,000,274
2011	32,055,328
2012	36,075,064
2013	40,014,701
2014	38,000,092
2015	37,106,983
2016	42,782,923
2017	41,277,657
Total Cumulative Transfers	<u>\$ 648,667,670</u>

Note: Total Cumulative Transfers includes transfers to the Solid Waste Landfill Closure Fund (final allocation made in July 1997), the Nebraska Environmental Trust Fund, the Education Innovation Fund, the Nebraska Opportunity Grant Fund (beginning October 1, 2003) (LB 956 (2010) changed the Nebraska Scholarship Fund to the Nebraska Opportunity Grant Fund as of July 1, 2010), the Compulsive Gamblers Assistance Fund, and the Nebraska State Fair Support and Improvement Cash Fund (beginning January 1, 2005). These transfers are shown on a cash basis except for an adjustment of \$2,342,407 increasing the Fiscal Year 2000 transfer amount and decreasing the Fiscal Year 2001 transfer amount to better reflect the transfer in the year it relates to. The 2005 transfer amount includes a \$5,000,000 transfer from the State Lottery Operation Trust Fund to the General Fund in July 2004, as required by LB 1091 (2004). Effective July 1, 2016, the Nebraska Lottery no longer transferred funds to the Education Innovation Fund and the Nebraska Opportunity Grant Fund. Instead, the Nebraska Lottery was to transfer 44.5% of funds available to be transferred to the Nebraska Education Improvement Fund (LB 497 (2013)).

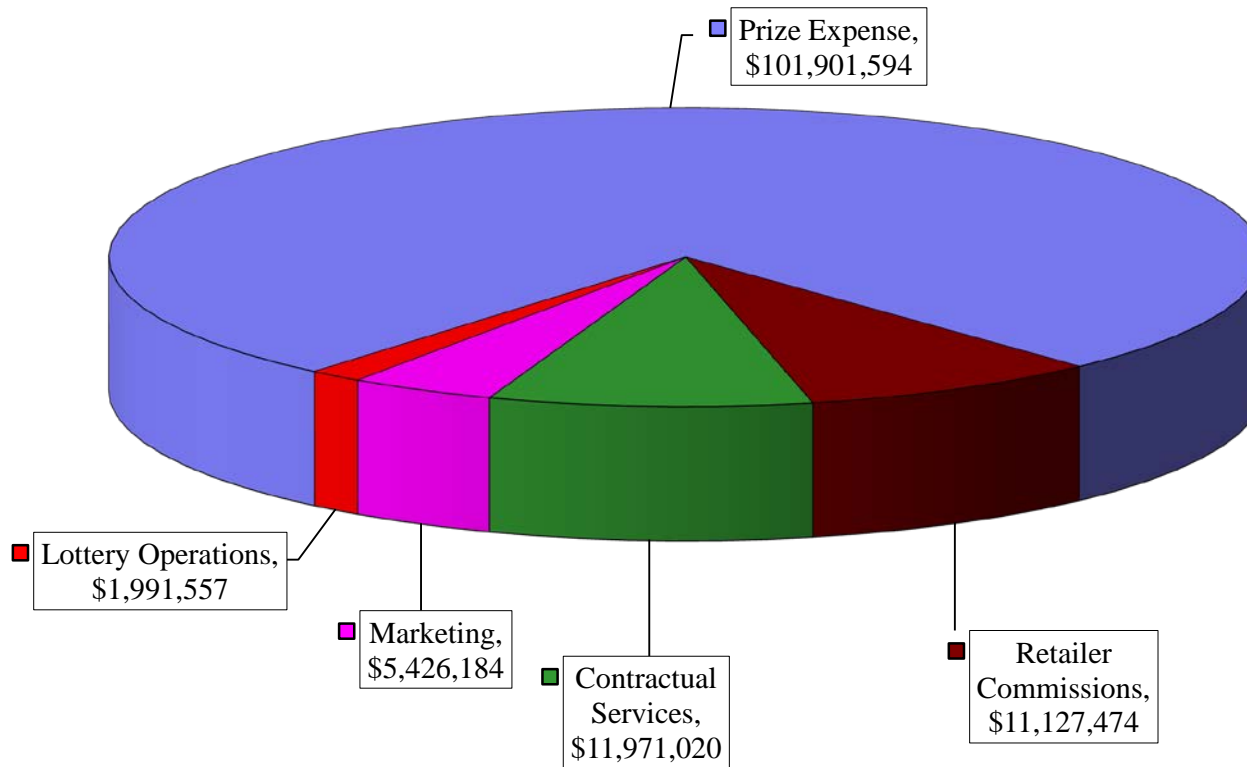


**NEBRASKA LOTTERY**  
**OPERATING TRANSFERS TO BENEFICIARY FUNDS**  
For the Fiscal Years 2013 through 2017



Note: Article III, § 24, of the Nebraska Constitution sets out the basic requirements for the transfer of lottery proceeds to certain beneficiary funds, specifying that a portion of those revenues are to “be used for education as the Legislature may direct.” Neb. Rev. Stat. § 9-812(2) (2017 Neb. Laws, LB 512, § 5) provides the following legislative directive for the transfer of lottery proceeds: “A portion of the dollar amount of the lottery tickets which have been sold on an annualized basis shall be transferred from the State Lottery Operation Trust Fund to the Education Innovation Fund, the Nebraska Opportunity Grant Fund, the Nebraska Education Improvement Fund, the Nebraska Environmental Trust Fund, the Nebraska State Fair Board, and the Compulsive Gamblers Assistance Fund as provided in subsection (3) of this section. The dollar amount transferred pursuant to this subsection shall equal the greater of (a) the dollar amount transferred to the funds in fiscal year 2002-03 or (b) any amount which constitutes at least twenty-two percent and no more than twenty-five percent of the dollar amount of the lottery tickets which have been sold on an annualized basis. To the extent that funds are available, the Tax Commissioner and director may authorize a transfer exceeding twenty-five percent of the dollar amount of the lottery tickets sold on an annualized basis.” Additionally, § 9-812(3) sets out these further instructions: “Of the money available to be transferred to the Education Innovation Fund, the Nebraska Opportunity Grant Fund, the Nebraska Education Improvement Fund, the Nebraska Environmental Trust Fund, the Nebraska State Fair Board, and the Compulsive Gamblers Assistance Fund: (a) The first five hundred thousand dollars shall be transferred to the Compulsive Gamblers Assistance Fund to be used as provided in section 9-1006; (b) Beginning July 1, 2016, forty-four and one-half percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the Nebraska Education Improvement Fund; (c) Forty-four and one-half percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the Nebraska Environmental Trust Fund to be used as provided in the Nebraska Environmental Trust Act; (d) Ten percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the Nebraska State Fair Board if the most populous city within the county in which the fair is located provides matching funds equivalent to ten percent of the funds available for transfer. Such matching funds may be obtained from the city and any other private or public entity, except that no portion of such matching funds shall be provided by the state. If the Nebraska State Fair ceases operations, ten percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the General Fund; and (e) One percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the Compulsive Gamblers Assistance Fund to be used as provided in section 9-1006.”

**NEBRASKA LOTTERY  
OPERATING EXPENSES**  
For the Fiscal Year Ended June 30, 2017



**Breakdown of Expenses**

**Prize Expense:**

Instant Prize Expense	\$68,622,460
On-Line Prize Expense	\$36,581,269
Unclaimed Prizes	(\$3,302,135)
<b>Total</b>	<b>\$101,901,594</b>

**Retailer Commissions:**

Instant Commissions	\$6,893,504
On-line Commissions	\$4,196,334
Misc. Retailer Expense	\$37,636
<b>Total</b>	<b>\$11,127,474</b>

**Contractual Services:**

IGT	\$11,448,589
Other Contractors	\$522,431
<b>Total</b>	<b>\$11,971,020</b>

**Marketing Expense:**

Advertising Expense	\$4,857,507
Promotions Expense	\$568,677
<b>Total</b>	<b>\$5,426,184</b>

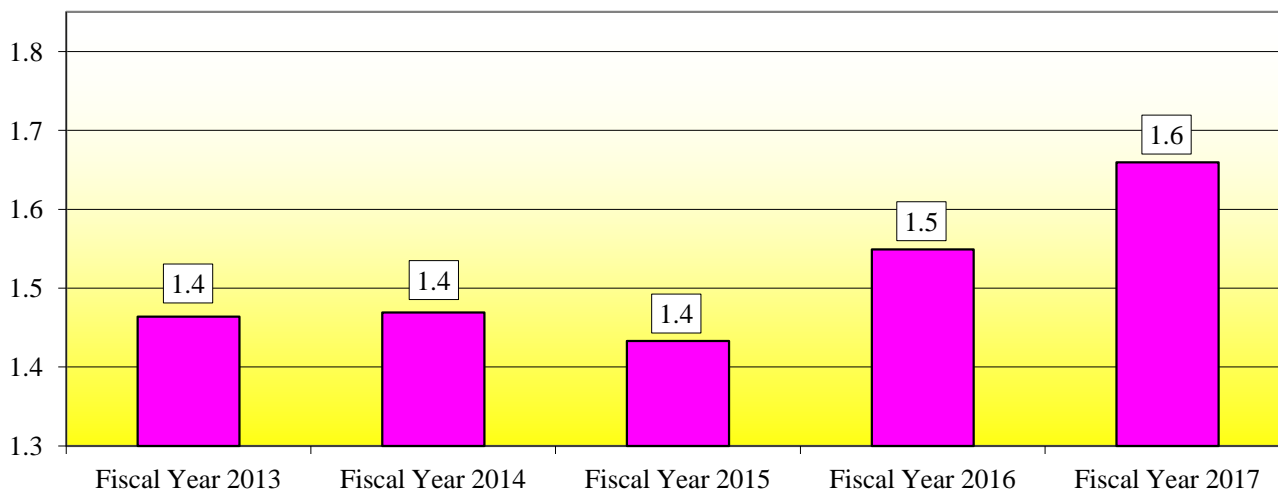
**Lottery Operations:**

Payroll Expense	\$1,559,224
Other Operating Expense	\$432,333
<b>Total</b>	<b>\$1,991,557</b>

# NEBRASKA LOTTERY

## CURRENT RATIO

For the Fiscal Years 2013 through 2017

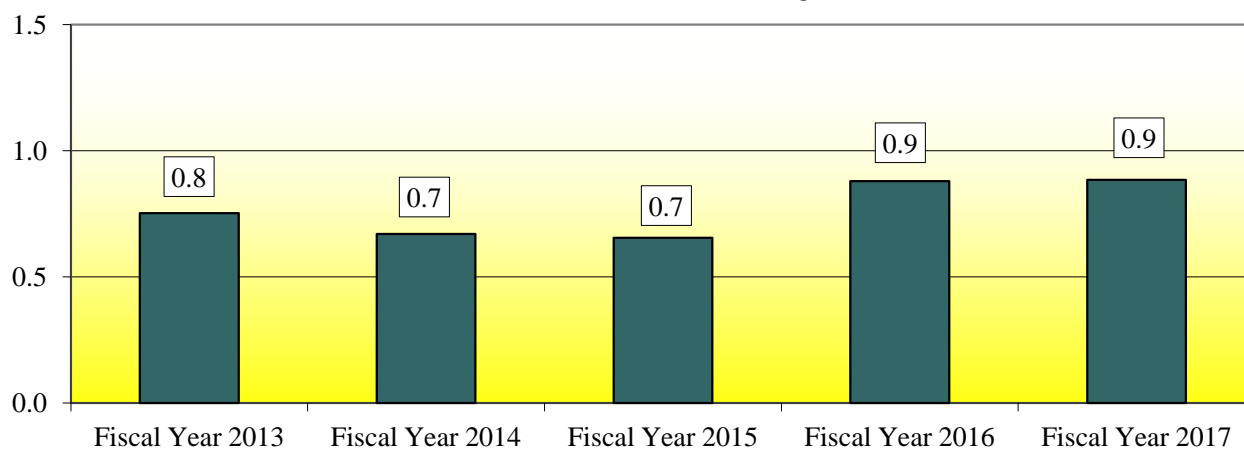


	Fiscal Year 2013	Fiscal Year 2014	Fiscal Year 2015	Fiscal Year 2016	Fiscal Year 2017
Current Assets	\$ 13,936,441	\$ 12,295,363	\$ 12,473,367	\$ 14,096,225	\$ 13,537,620
Current Liabilities	\$ 9,855,555	\$ 8,663,425	\$ 9,018,207	\$ 9,402,655	\$ 8,412,015

Note: The Current Ratio is an assessment of the Nebraska Lottery's current assets in excess of current liabilities.

## QUICK RATIO

For the Fiscal Years 2013 through 2017



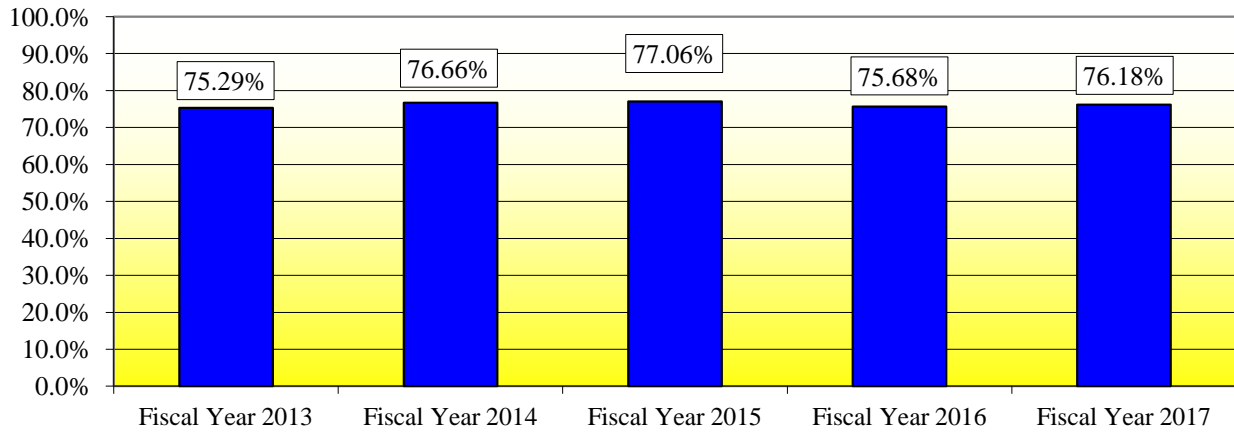
	Fiscal Year 2013	Fiscal Year 2014	Fiscal Year 2015	Fiscal Year 2016	Fiscal Year 2017
Cash & Cash Equivalents	\$ 7,422,584	\$ 5,803,806	\$ 5,910,974	\$ 8,263,811	\$ 7,439,920
Current Liabilities	\$ 9,855,555	\$ 8,663,425	\$ 9,018,207	\$ 9,402,655	\$ 8,412,015

Note: The Quick Ratio is an assessment of the Nebraska Lottery's cash in excess of current liabilities.

# NEBRASKA LOTTERY

## PERCENTAGE OF OPERATING EXPENSES TO REVENUES

For the Fiscal Year 2013 through 2017

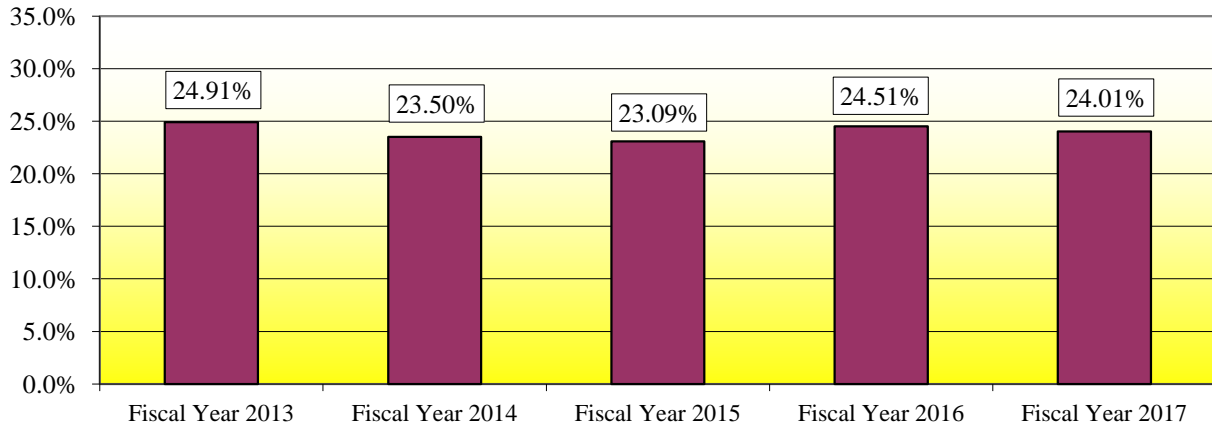


	Fiscal Year 2013	Fiscal Year 2014	Fiscal Year 2015	Fiscal Year 2016	Fiscal Year 2017
Total Operating Expense	\$ 121,035,830	\$ 121,046,318	\$ 123,277,591	\$ 135,819,228	\$ 132,417,829
Total Operating Revenue	\$ 160,753,074	\$ 157,896,534	\$ 159,967,949	\$ 179,472,755	\$ 173,819,106

Note: The graph represents the percentage of operating expenses to revenues.

## NET INCOME BEFORE TRANSFERS COMPARED TO OPERATING REVENUE

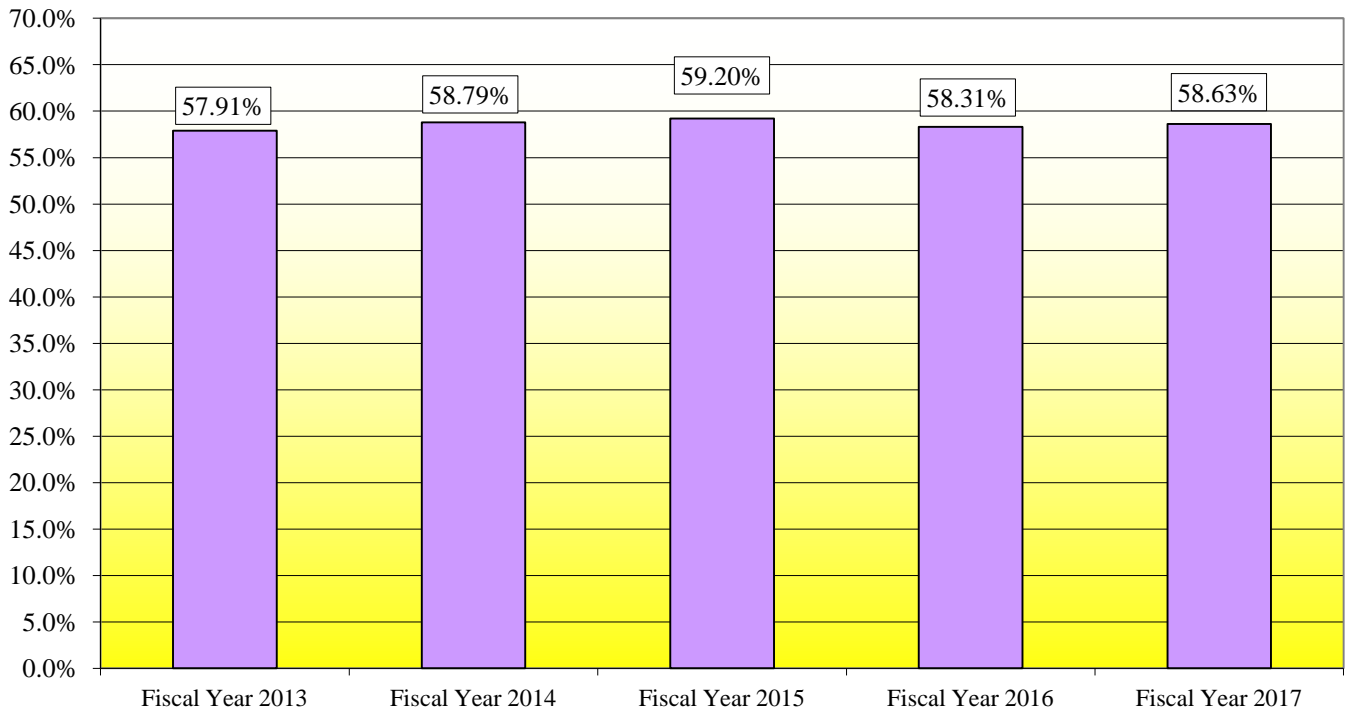
For the Fiscal Years 2013 through 2017



	Fiscal Year 2013	Fiscal Year 2014	Fiscal Year 2015	Fiscal Year 2016	Fiscal Year 2017
Net Income Before Transfers	\$ 40,045,381	\$ 37,107,758	\$ 36,940,611	\$ 43,984,670	\$ 41,732,767
Total Operating Revenue	\$ 160,753,074	\$ 157,896,534	\$ 159,967,949	\$ 179,472,755	\$ 173,819,106

Note: The graph represents the percentage of net income before operating transfers compared to total operating revenue.

**NEBRASKA LOTTERY**  
**PRIZE PERCENTAGE OF SALES**  
For the Fiscal Years 2013 through 2017



	Fiscal Year 2013	Fiscal Year 2014	Fiscal Year 2015	Fiscal Year 2016	Fiscal Year 2017
Prize Expense	\$ 93,092,437	\$ 92,821,370	\$ 94,696,026	\$ 104,644,944	\$ 101,901,594
Total Operating Revenue	\$ 160,753,074	\$ 157,896,534	\$ 159,967,949	\$ 179,472,755	\$ 173,819,106

Note: The graph represents the percentage of net sales paid out in prizes.