

**AUDIT REPORT
OF THE
NEBRASKA LOTTERY**

FOR THE FISCAL YEAR ENDED JUNE 30, 2018

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the Auditor of Public Accounts.**

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Issued on October 19, 2018

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 37th 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®, Lucky for Life®, 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) (Supp. 2017) 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

NEBRASKA LOTTERY

BACKGROUND

(Concluded)

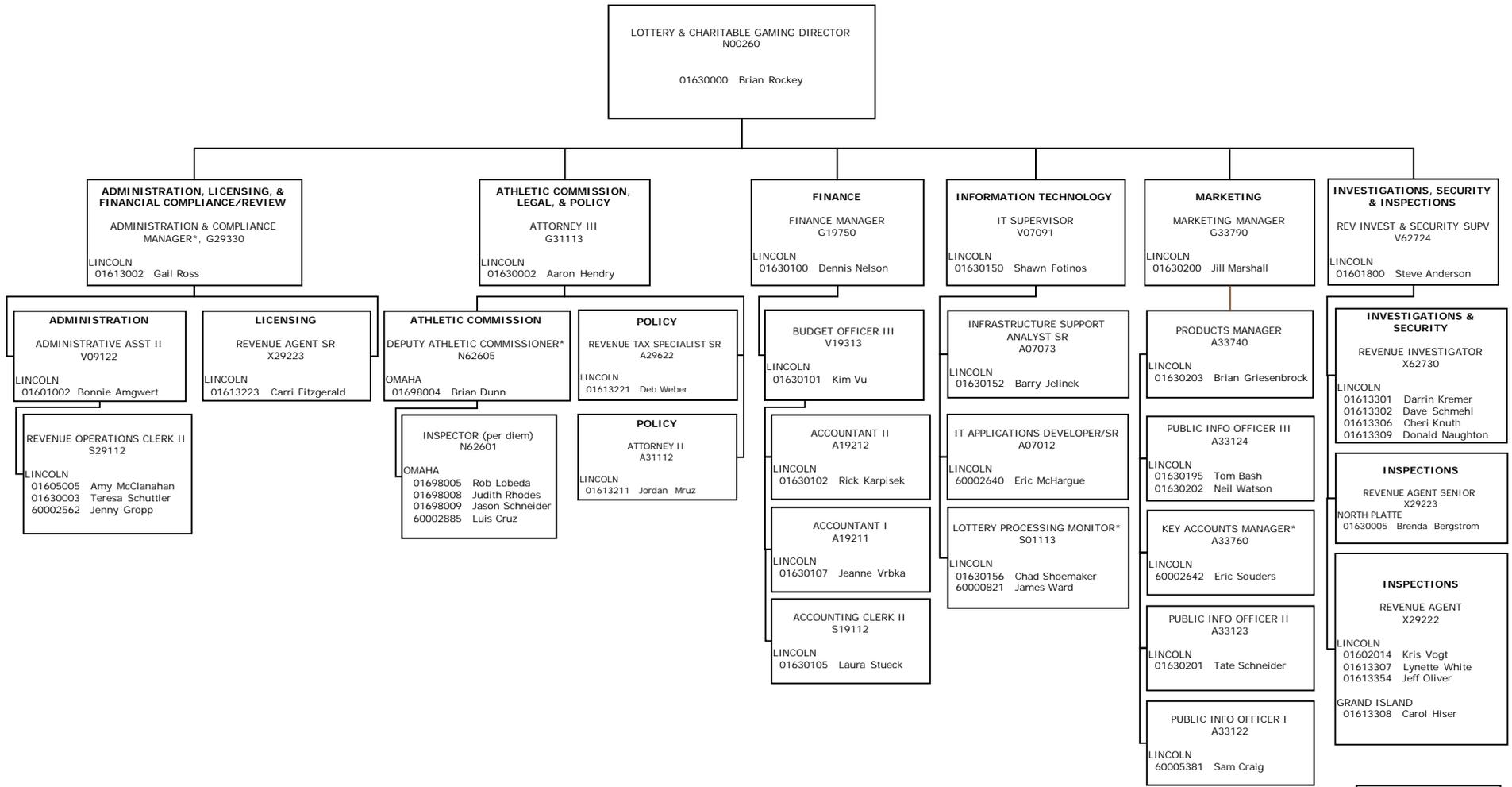
(e) One percent of the money remaining after the payment of prizes and operating expenses and the initial transfer to the Compulsive Gamblers Assistance Fund shall be transferred to the Compulsive Gamblers Assistance Fund to be used as provided in section 9-1006.

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 2018



38 Total Positions
38 Filled
0 Vacant

4 Per Diem Employees

Updated 8/22/2018

*Working Title

NEBRASKA LOTTERY

KEY OFFICIALS AND AGENCY CONTACT INFORMATION

Nebraska Lottery Executive Management

Name	Title
Tony Fulton	Tax Commissioner
Brian Rockey	Lottery Director
Dennis Nelson	Lottery Finance Manager

The Nebraska Lottery
137 N.W. 17th Street
P.O. Box 98901
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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, 2018, 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, 2018, and the respective changes in financial position and, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

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, 2018, 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 Matter

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 7-10 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 11, 2018, 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 solely 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 effectiveness of the Nebraska Lottery's 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, CISA
Audit Manager
Lincoln, Nebraska

October 11, 2018

NEBRASKA LOTTERY

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the Nebraska Lottery annual audit presents management's discussion and analysis of the financial performance of the Nebraska Lottery for the fiscal period ended June 30, 2018. 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, 2018. 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 increased about \$970,000. This cash was produced by a large increase in Prizes Payable (cash for prizes that will be paid later) of \$2.3 million and was reduced by lower Account Payables (cash used to pay down amounts owed) of \$270,000. The other portion was cash that was not collected as Accounts Receivables/Reserves went up \$890,000 (essentially this is more money that was not collected at the end of this fiscal year). Several items caused this increase; 1) there were only six days of revenue that had not been collected last year whereas seven days were uncollected in this year; 2) weekly sales were higher at this year-end, \$3.1 million versus \$2.5 million; and 3) instead of the Lottery owing money to the Multi-State Lottery Association for prizes, funds were actually owed to the Lottery, which created an accounts receivable.

NEBRASKA LOTTERY

MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

The largest liability change was the Prizes Payable classification this year. There was an increase of \$2.3 million as mentioned above. This is due to higher sales this year, \$183.4 million versus \$173.8 million, which increased the prizes accrued costs.

In the Net Position section, the Restricted for Future Prizes went up about \$55,000, which is the result of increase reserves for future prizes that is held by the Multi-State Lottery Association for the Lottery.

Table A
Summary of Net Position

	FY 2018	FY 2017	Change
CURRENT ASSETS			
Cash and Cash Equivalents	\$ 8,408,369	\$ 7,439,920	\$ 968,449
Accounts Receivable and Reserves on Deposit	6,915,349	6,029,226	886,123
Prepaid Prizes and Costs	110,994	68,474	42,520
TOTAL CURRENT ASSETS	<u>15,434,712</u>	<u>13,537,620</u>	<u>1,897,092</u>
NONCURRENT ASSETS			
Reserves on Deposit	2,465,976	2,410,743	55,233
Furniture, Fixtures, Equipment (Net)	49,654	70,272	(20,618)
TOTAL NONCURRENT ASSETS	<u>2,515,630</u>	<u>2,481,015</u>	<u>34,615</u>
TOTAL ASSETS	<u>\$ 17,950,342</u>	<u>\$ 16,018,635</u>	<u>\$ 1,931,707</u>
CURRENT LIABILITIES			
Accounts Payable	\$ 1,181,675	\$ 1,448,415	\$ (266,740)
Compensated Absences and Accrued Payroll Payable	108,151	108,687	(536)
Prizes Payable	8,776,064	6,459,861	2,316,203
Other Accrued Liabilities	295,848	395,052	(99,204)
TOTAL CURRENT LIABILITIES	<u>10,361,738</u>	<u>8,412,015</u>	<u>1,949,723</u>
NONCURRENT LIABILITIES			
Compensated Absences Payable	248,417	267,080	(18,663)
TOTAL NONCURRENT LIABILITIES	<u>248,417</u>	<u>267,080</u>	<u>(18,663)</u>
TOTAL LIABILITIES	<u>\$ 10,610,155</u>	<u>\$ 8,679,095</u>	<u>\$ 1,931,060</u>
NET POSITION			
Invested in Capital Assets	\$ 49,654	\$ 70,272	\$ (20,618)
Restricted for Future Prizes	2,465,976	2,410,743	55,233
Unrestricted	4,824,557	4,858,525	(33,968)
TOTAL NET POSITION	<u>\$ 7,340,187</u>	<u>\$ 7,339,540</u>	<u>\$ 647</u>

NEBRASKA LOTTERY

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

DISCUSSION OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

After setting a record for sales two years ago, the Lottery set a new record this year with sales of \$183.4 million, which was an increase over last year of \$9.5 million (see Table B below). The Lottery had an upswing in sales for lotto of about 14.3% (roughly \$10.3 million in sales) but scratch remained steady and suffered a small .8% decrease. On the lotto side, \$4.3 million of the increase was due to the August introduction of Lottery's seventh lotto game, Lucky for Life. Mega Millions sales went up \$3.8 million and Powerball sales went up \$1.7 million. The number of large jackpot runs and the size of the jackpots materially affect weekly lotto sales for those two games.

On the scratch side, sales decreased about \$750,000. The largest increase was in the \$20 price point (\$1.7 million), which can be attributed to the introduction of another \$20 game offering, Lottery's 25th anniversary game. The largest decrease was in the \$3 price point (\$1.7 million). At this time, we do not know the specific reason for the decline in the \$3 price point but suspect price point migration and less successful secondary games that support the core \$3 games. While the \$2, \$3, and \$10 price points saw decreased sales, the \$1, \$5, and \$20 price points saw increases.

The Prize Expense went up about \$4.7 million. This can be attributed to higher sales than last year. The higher sales also affected the Contractual Services Expense (costs related to the lottery services provider which are based on a percentage of sales) as it was about \$350,000 more than last year. The Retailer Commissions were higher too, about \$700,000 more.

The Transfers to Other Funds had an increase of almost \$4.0 million. With the higher lotto sales, which has a higher profit margin, the Lottery had increased profits and was able to transfer more 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 2018	FY 2017	Change
REVENUES			
Sales	\$ 185,242,484	\$ 175,967,645	\$ 9,274,839
Sales Returns	(1,874,392)	(2,148,539)	274,147
OPERATING REVENUE	<u>183,368,092</u>	<u>173,819,106</u>	<u>9,548,986</u>
Interest Income	303,920	299,317	4,603
Other Income	3,229	8,752	(5,523)
Multi-State Lottery Assoc. Income	58,796	23,421	35,375
NON-OPERATING REVENUE	<u>365,945</u>	<u>331,490</u>	<u>34,455</u>
TOTAL REVENUES	<u>\$ 183,734,037</u>	<u>\$ 174,150,596</u>	<u>\$ 9,583,441</u>
OPERATING EXPENSES			
Prize Expense	\$ 106,634,524	\$ 101,901,594	\$ 4,732,930
Retailer Commissions	11,838,749	11,127,474	711,275
Contractual Services	12,319,559	11,971,020	348,539
Marketing Expense	5,715,880	5,426,184	289,696
Lottery Operating Expense	1,974,564	1,991,557	(16,993)
TOTAL EXPENSES	<u>\$ 138,483,276</u>	<u>\$ 132,417,829</u>	<u>\$ 6,065,447</u>
NET INCOME BEFORE TRANSFERS	<u>\$ 45,250,761</u>	<u>\$ 41,732,767</u>	<u>\$ 3,517,994</u>
TRANSFERS TO OTHER FUNDS	<u>\$ 45,250,114</u>	<u>\$ 41,277,657</u>	<u>\$ 3,972,457</u>
CHANGE IN NET POSITION	<u>\$ 647</u>	<u>\$ 455,110</u>	<u>\$ (454,463)</u>
BEGINNING NET POSITION	<u>\$ 7,339,540</u>	<u>\$ 6,884,430</u>	<u>\$ 455,110</u>
ENDING NET POSITION	<u>\$ 7,340,187</u>	<u>\$ 7,339,540</u>	<u>\$ 647</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, 2018

ASSETS

CURRENT ASSETS:

Cash and Cash Equivalents	\$ 8,408,369
Accounts Receivable, Net of Allowance (Note 5)	6,568,404
Prepaid Prizes	110,994
Reserves on Deposit (Note 7)	346,945
TOTAL CURRENT ASSETS	15,434,712

NONCURRENT ASSETS:

Reserves on Deposit (Note 7)	2,465,976
Capital Assets:	
Furniture, Fixtures, and Equipment (Note 6)	295,423
Less: Accumulated Depreciation	245,769
Total Capital Assets, Net	49,654
TOTAL NONCURRENT ASSETS	2,515,630

TOTAL ASSETS	\$ 17,950,342
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LIABILITIES

CURRENT LIABILITIES:

Accounts Payable	\$ 220,736
Vendors Payable	960,939
Compensated Absences Payable (Note 8)	24,569
Accrued Payroll Payable	83,582
Withheld Taxes on Prizes Paid	20,250
Prize Payable	8,776,064
Due to Other Funds	13,503
Other Accrued Liabilities	262,095
TOTAL CURRENT LIABILITIES	10,361,738

NONCURRENT LIABILITIES:

Compensated Absences Payable (Note 8)	248,417
TOTAL NONCURRENT LIABILITIES	248,417

TOTAL LIABILITIES	10,610,155
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NET POSITION

Invested in Capital Assets	49,654
Restricted for Future Prizes (Note 7)	2,465,976
Unrestricted (Note 11)	4,824,557
TOTAL NET POSITION	7,340,187

TOTAL LIABILITIES AND NET POSITION	\$ 17,950,342
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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, 2018

OPERATING REVENUE:	
Sales	\$ 185,242,484
Less: Sales Returns	1,874,392
TOTAL OPERATING REVENUE	<u>183,368,092</u>
OPERATING EXPENSES:	
Prize Expense, Net of Unclaimed Prizes (Note 1c)	106,634,524
Retailer Commissions	11,838,749
Contractual Services Expense	12,319,559
Marketing	5,715,880
Lottery Operating	1,974,564
TOTAL OPERATING EXPENSES	<u>138,483,276</u>
OPERATING INCOME	44,884,816
NONOPERATING REVENUE:	
Interest Income	303,920
Other Income	3,229
Multi-State Lottery Association Income	58,796
TOTAL NONOPERATING REVENUE	<u>365,945</u>
INCOME BEFORE OPERATING TRANSFERS	45,250,761
TRANSFERS TO OTHER FUNDS (Note 10)	<u>(45,250,114)</u>
CHANGE IN NET POSITION	647
TOTAL NET POSITION, BEGINNING OF YEAR	<u>7,339,540</u>
TOTAL NET POSITION, END OF YEAR	<u><u>\$ 7,340,187</u></u>

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, 2018

CASH FLOWS FROM OPERATING ACTIVITIES:	
Ticket Sales	\$ 182,765,966
Prizes Paid to Winners	(105,088,604)
Commissions Paid to Retailers	(11,833,636)
Paid to Contractors for Goods and Services	(18,030,175)
Paid to Employees	(1,563,497)
Other Operating Expenses	(372,982)
Net Cash Provided by Operating Activities	<u>45,877,072</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:	
Paid to Nebraska Education Improvement Fund	(19,913,801)
Paid to Nebraska State Fair Support and Improvement Cash Fund	(4,475,011)
Paid to Nebraska Environmental Trust Fund	(19,913,801)
Paid to Compulsive Gamblers Assistance Fund	(947,501)
Net Cash Used in NonCapital Financing Activities	<u>(45,250,114)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:	
Purchase of Property and Equipment	(21,225)
CASH FLOWS FROM INVESTING ACTIVITIES:	
Interest on Cash	303,920
Multi-State Lottery Association Income	58,796
Net Cash Provided by Investing Activities	<u>362,716</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	968,449
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>7,439,920</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 8,408,369</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:	
Operating Income	\$ 44,884,816
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:	
Depreciation Expense	45,072
Changes in Assets (Increase) Decrease in:	
Reserves on Deposit	(43,021)
Prepaid Prizes	(42,520)
Accounts Receivable (Net)	(898,335)
Changes in Liabilities Increase (Decrease) in:	
Other Accrued Liabilities	(87,856)
Accounts Payable and Due to Other Funds	(325,939)
Prizes Payable	2,316,203
Compensated Absences and Accrued Payroll Payable	(19,199)
Withheld Taxes on Prizes Paid	(8,950)
Vendors Payable	56,801
Total Adjustments	<u>992,256</u>
Net Cash Provided by Operating Activities	<u>\$ 45,877,072</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, 2018

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 (Supp. 2017), 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 Nebraska 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 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.

NEBRASKA LOTTERY

NOTES TO THE FINANCIAL STATEMENTS

(Continued)

1. Summary of Significant Accounting Policies (Continued)

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 Nebraska 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 Nebraska 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.

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, 2018, totaled \$3,179,584.

NEBRASKA LOTTERY

NOTES TO THE FINANCIAL STATEMENTS

(Continued)

1. Summary of Significant Accounting Policies (Continued)

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, 2018, 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.

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.

NEBRASKA LOTTERY

NOTES TO THE FINANCIAL STATEMENTS
(Continued)

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

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.

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.

NEBRASKA LOTTERY

NOTES TO THE FINANCIAL STATEMENTS (Continued)

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

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, 2018, and revenues and expenditures during the reporting period. Actual results could differ from those estimates.

2. **Deposits and Investments**

Investment of all available cash is made by the State Investment Officer on a daily basis, based on total bank balances. These funds are held in the State of Nebraska Operating Investment Pool (OIP), an internal investment pool. Additional information on the deposits and investments portfolio, including investment policies, risks, and types of investments, can be found in the State of Nebraska's Comprehensive Annual Financial Report (CAFR).

3. **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 \$1 million of exposure per accident with a self-insured retention of \$300,000 and \$300,000 corridor retention. Motor vehicle liability has excess coverage of \$4 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 \$500 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.
- 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.

NEBRASKA LOTTERY

NOTES TO THE FINANCIAL STATEMENTS (Continued)

3. **Contingencies and Commitments** (Concluded)

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.

4. **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.

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.

NEBRASKA LOTTERY

NOTES TO THE FINANCIAL STATEMENTS

(Continued)

4. **State Employees Retirement Plan (Plan)** (Concluded)

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, 2018, employees contributed \$56,792, and the Nebraska Lottery contributed \$88,595. 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.

5. **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 \$29,095.

Accounts Receivable	
Retailers (net)	\$ 6,179,227
Other	389,177
Total	<u>\$ 6,568,404</u>

6. **Capital Assets**

Capital asset activity for the year ended June 30, 2018, was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital Assets: Furniture, Fixtures, and Equipment	\$ 276,651	\$ 24,454	\$ 5,682	\$ 295,423
Less: Accumulated Depreciation	206,379	45,072	5,682	245,769
Total Capital Assets, Net	<u>\$ 70,272</u>	<u>\$ (20,618)</u>	<u>\$ -</u>	<u>\$ 49,654</u>

NEBRASKA LOTTERY

NOTES TO THE FINANCIAL STATEMENTS

(Continued)

7. On-Line Games

During the fiscal year ended June 30, 2018, the Nebraska Lottery offered a variety of on-line games, as described in the following table.

Game Name	Administered by	Nebraska's Share of Prize Reserves
Powerball®	MUSL	\$ 1,616,242
Nebraska Pick 5®	Nebraska Lottery	N/A
Nebraska Pick 3®	Nebraska Lottery	N/A
MyDaY®	Nebraska Lottery	N/A
Mega Millions®	MUSL	722,052
2by2®	MUSL	127,682
Lucky for Life®	MUSL	N/A
		\$ 2,465,976

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 some of the games 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 \$346,945 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.

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.

The Lucky for Life® top two prize levels can be paid either through annuity payments for the life of the winner or as a lump sum cash payment, depending on the selection of the winner when claiming the prize. If a Nebraska winner selects the annuity, the Nebraska Lottery has a contract with MUSL so that MUSL will secure bids from financial services companies to provide the annual payments directly to the winner. Each participating jurisdiction contributes a proportionate share to fund the annuity or lump sum payment. There were no Lucky for Life® top prize winners in Nebraska this fiscal year.

NEBRASKA LOTTERY

NOTES TO THE FINANCIAL STATEMENTS
(Continued)

8. Noncurrent Liabilities

Changes in noncurrent liabilities for the year ended June 30, 2018, are summarized as follows:

	Beginning Balance	Increases	Decreases	Ending Balance	Amounts Due Within One Year
Compensated Absences	\$ 293,495	\$ 5,906	\$ 26,415	\$ 272,986	\$ 24,569

9. Lease Commitments

The Nebraska Lottery leases office space under an operating lease. The following schedule for operating leases includes all leases for the Nebraska Lottery. Although the lease terms may vary, all leases are subject to annual appropriation by the Legislature.

The minimum annual lease payments for operating leases as of June 30, 2018, are as follows:

Year	Activities
2019	\$ 77,923
2020	\$ 77,923
2021	\$ 77,923
2022	\$ 77,923
2023	\$ 77,923
2024-2027	\$ 311,691
Total	\$ 701,306

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, 2018, were \$75,018.

10. 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.”

Neb. Rev. Stat. § 9-812(2) (Supp. 2017) 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.

NEBRASKA LOTTERY

NOTES TO THE FINANCIAL STATEMENTS
(Continued)

10. **Significant Compliance Requirements** (Concluded)

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.

As required under its enabling legislation, transfers of \$45,250,114 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 \$46,442 in delinquent State taxes and \$56,055 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 Nebraska Lottery represents only part of the State's primary government.

NEBRASKA LOTTERY

NOTES TO THE FINANCIAL STATEMENTS
(Concluded)

11. 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.



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, 2018, 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 October 11, 2018. 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

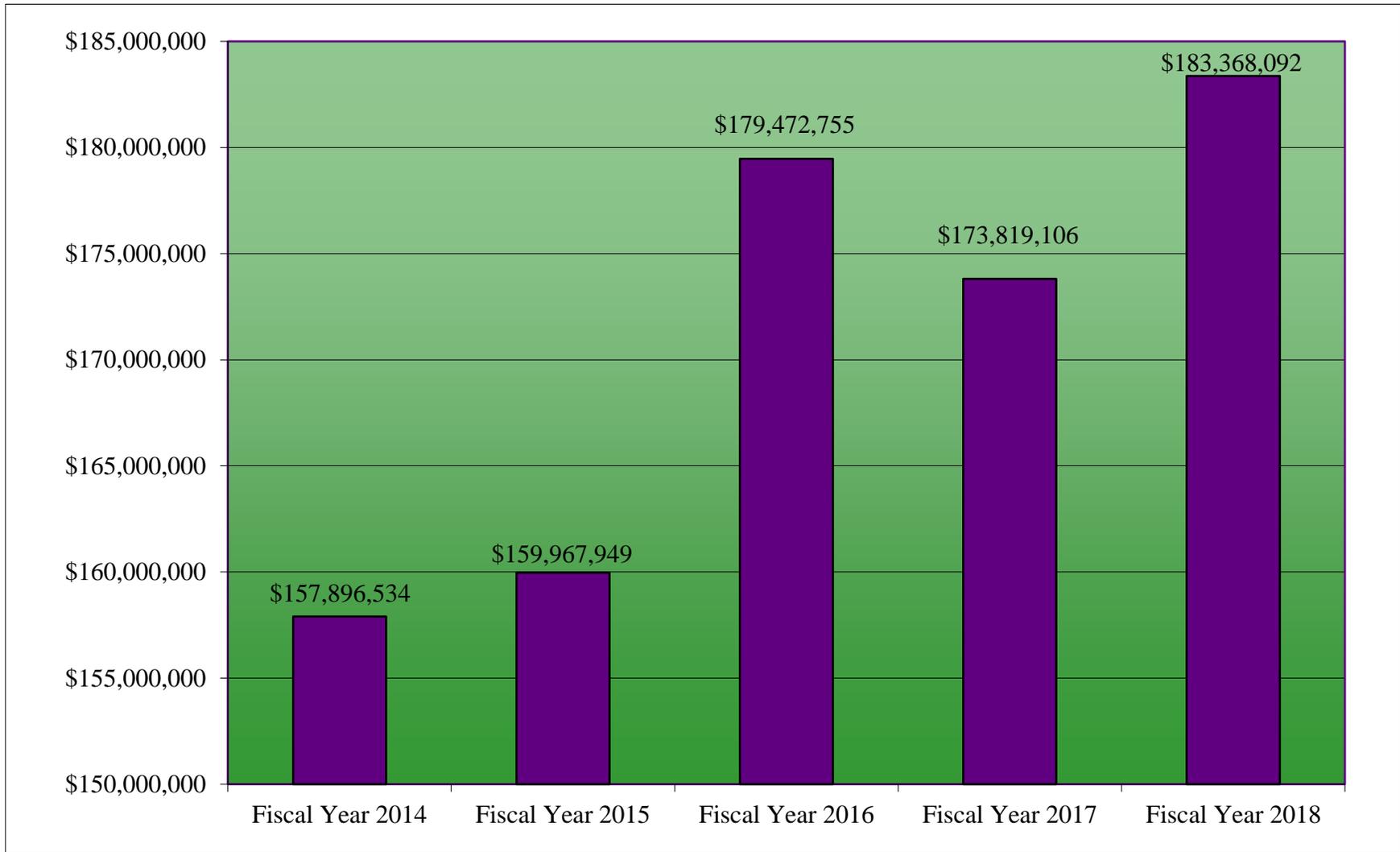
The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, not to provide an opinion on the effectiveness of the Nebraska Lottery's internal control or on compliance. This report is an integral part of an audit performed 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 11, 2018



Zachary Wells, CPA, CISA
Audit Manager
Lincoln, Nebraska

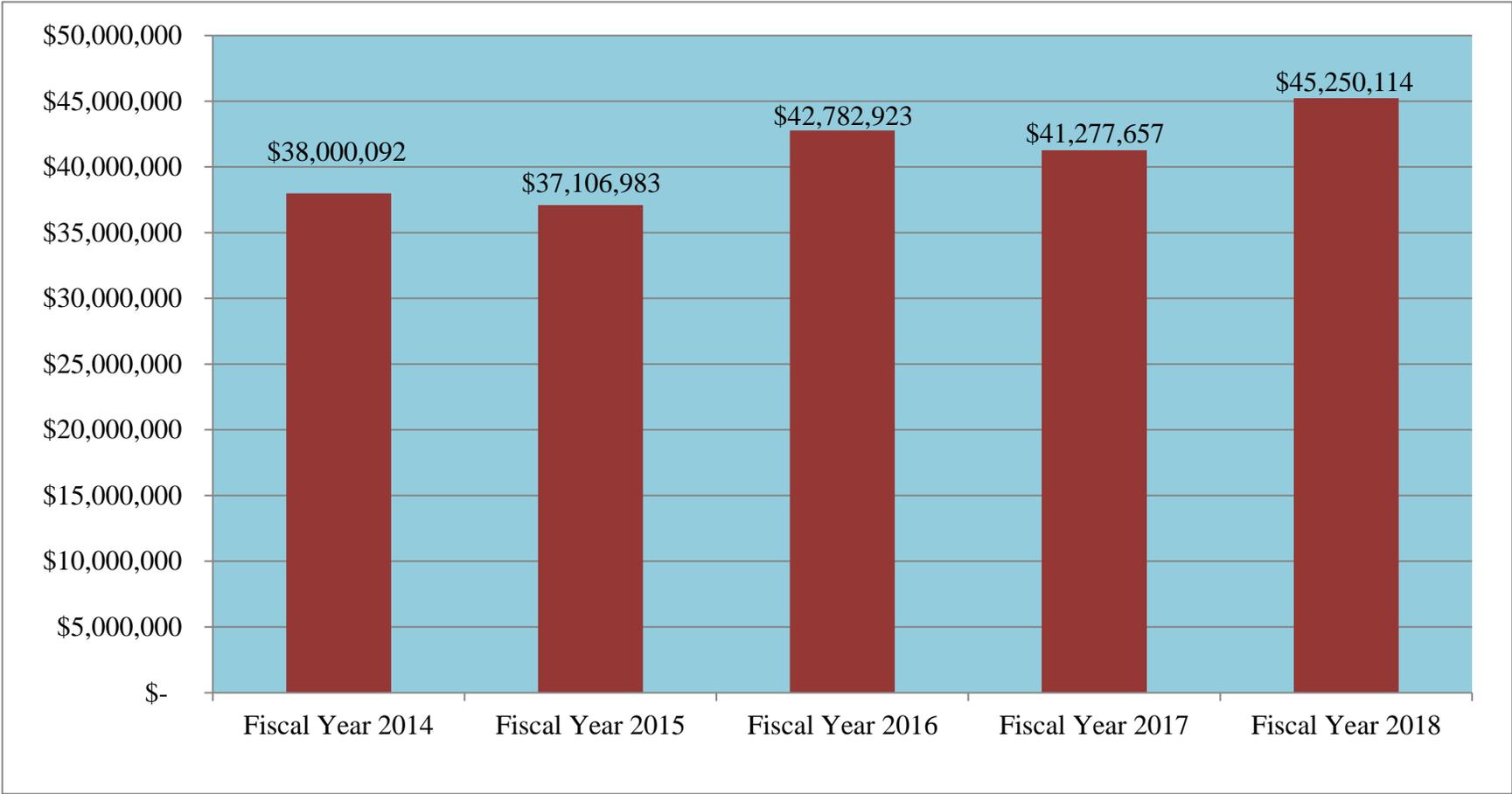
NEBRASKA LOTTERY
LOTTERY TICKET SALES
For the Fiscal Years 2014 through 2018



Note: These sales are shown on an accrual basis.

NEBRASKA LOTTERY
TOTAL OPERATING TRANSFERS TO BENEFICIARY FUNDS

For the Fiscal Years 2014 through 2018



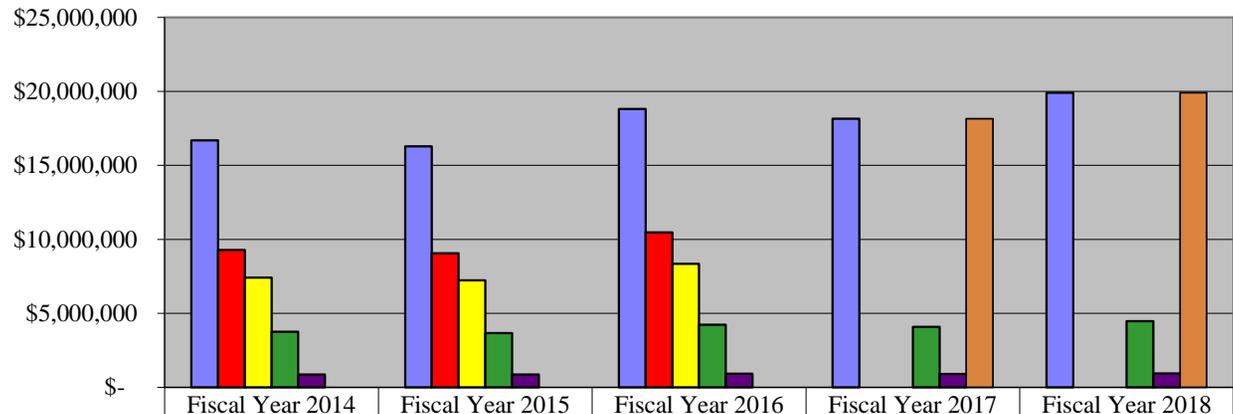
Note: The Total Operating Transfers include transfers to the Nebraska Environmental Trust Fund, the Education Innovation Fund, the Nebraska Opportunity Grant Fund, the Compulsive Gamblers Assistance Fund, Nebraska Education Improvement Fund, and the Nebraska State Fair Support and Improvement Cash Fund.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

**NEBRASKA LOTTERY
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
2018	45,250,114
Total Cumulative Transfers	<u>\$ 693,917,784</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)).

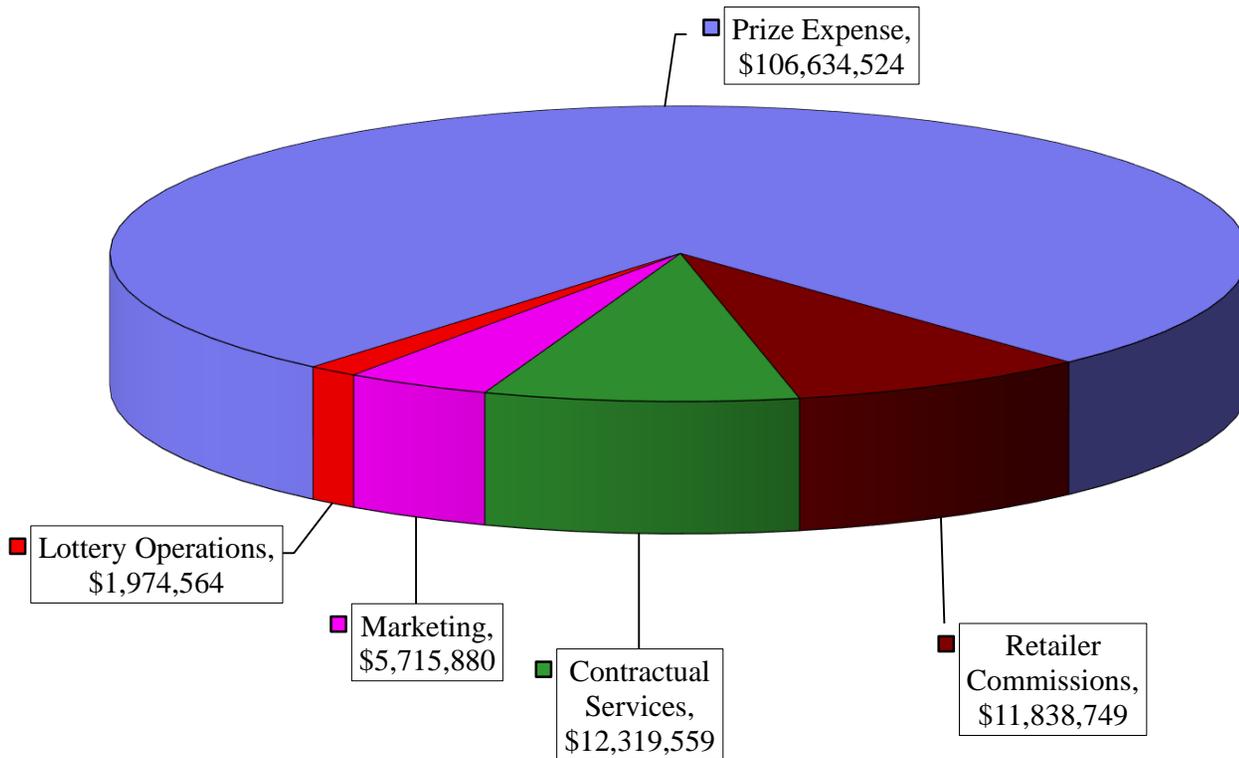
NEBRASKA LOTTERY
OPERATING TRANSFERS TO BENEFICIARY FUNDS
For the Fiscal Years 2014 through 2018



	Fiscal Year 2014	Fiscal Year 2015	Fiscal Year 2016	Fiscal Year 2017	Fiscal Year 2018
■ Nebraska Environmental Trust Fund	\$16,687,541	\$16,290,107	\$18,815,901	\$18,146,057	\$19,913,801
■ Nebraska Opportunity Grant Fund	\$9,281,274	\$9,060,227	\$10,465,024	\$-	\$-
■ Education Innovation Fund	\$7,406,269	\$7,229,878	\$8,350,876	\$-	\$-
■ Nebraska State Fair Support and Improvement Cash Fund	\$3,750,007	\$3,660,699	\$4,228,292	\$4,077,766	\$4,475,011
■ Compulsive Gamblers Assistance Fund	\$875,001	\$866,072	\$922,830	\$907,777	\$947,501
■ Nebraska Education Improvement Fund	\$-	\$-	\$-	\$18,146,057	\$19,913,801

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) (Supp. 2017) 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, 2018



Total Operating Expenses \$138,483,276

Breakdown of Expenses

Prize Expense:

Instant Prize Expense	\$67,199,314
On-Line Prize Expense	\$42,614,794
Unclaimed Prizes	(\$3,179,584)
Total	\$106,634,524

Retailer Commissions:

Instant Commissions	\$7,003,370
On-line Commissions	\$4,798,875
Misc. Retailer Expense	\$36,504
Total	\$11,838,749

Contractual Services:

IGT	\$11,820,916
Other Contractors	\$498,643
Total	\$12,319,559

Marketing Expense:

Advertising Expense	\$5,218,796
Promotions Expense	\$497,084
Total	\$5,715,880

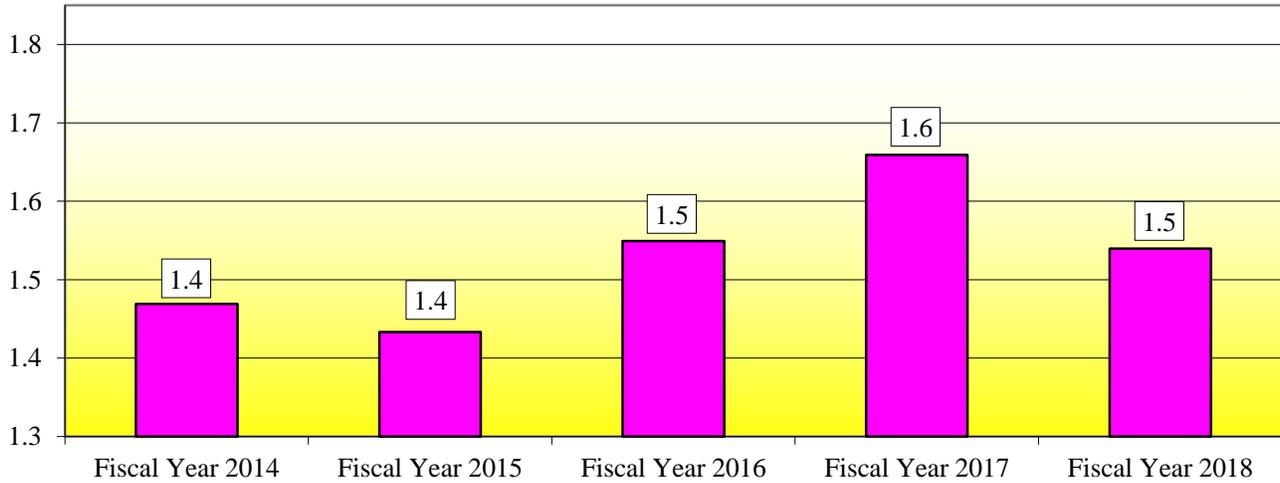
Lottery Operations:

Payroll Expense	\$1,544,298
Other Operating Expense	\$430,266
Total	\$1,974,564

NEBRASKA LOTTERY

CURRENT RATIO

For the Fiscal Years 2014 through 2018

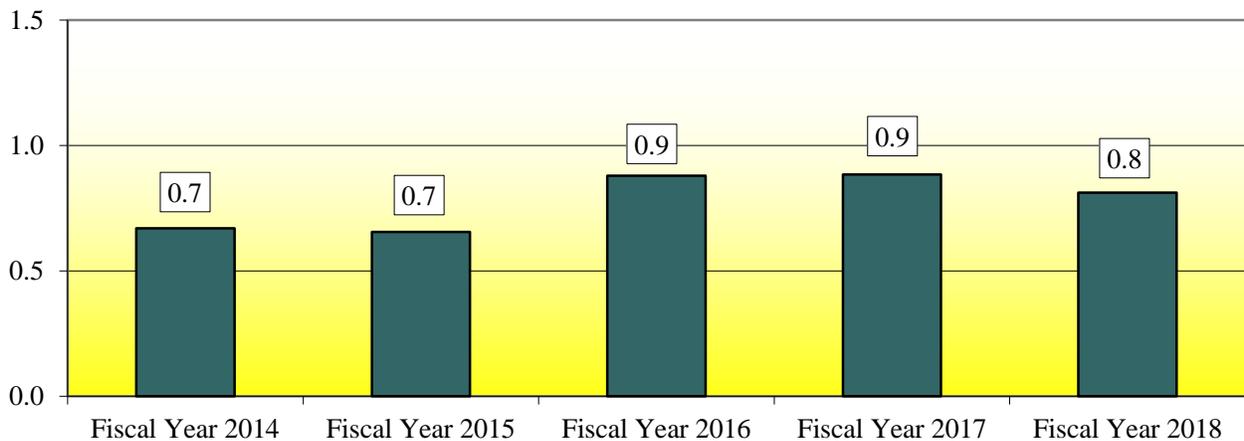


	Fiscal Year 2014	Fiscal Year 2015	Fiscal Year 2016	Fiscal Year 2017	Fiscal Year 2018
Current Assets	\$ 12,295,363	\$ 12,473,367	\$ 14,096,225	\$ 13,537,620	\$ 15,434,712
Current Liabilities	<u>\$ 8,663,425</u>	<u>\$ 9,018,207</u>	<u>\$ 9,402,655</u>	<u>\$ 8,412,015</u>	<u>\$ 10,361,738</u>

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 2014 through 2018

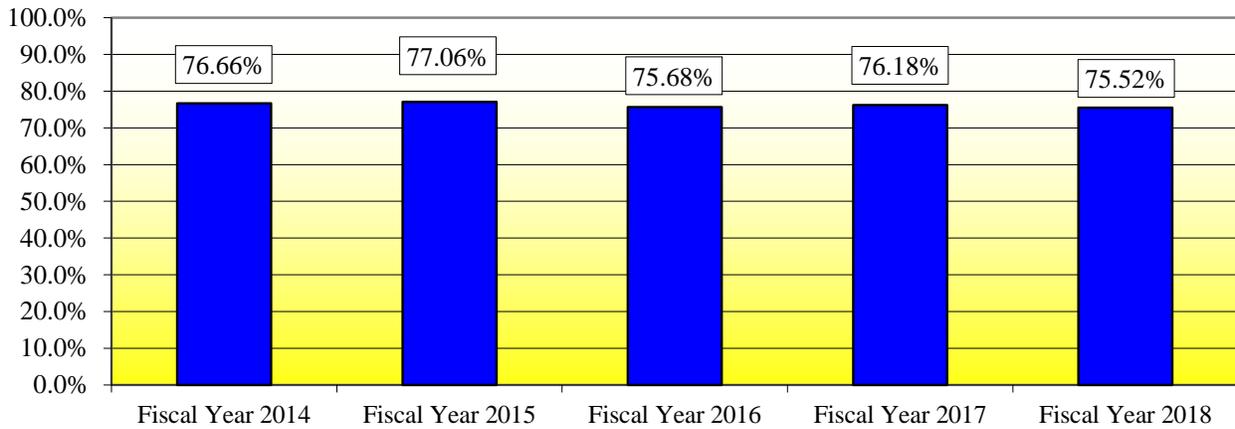


	Fiscal Year 2014	Fiscal Year 2015	Fiscal Year 2016	Fiscal Year 2017	Fiscal Year 2018
Cash & Cash Equivalents	\$ 5,803,806	\$ 5,910,974	\$ 8,263,811	\$ 7,439,920	\$ 8,408,369
Current Liabilities	<u>\$ 8,663,425</u>	<u>\$ 9,018,207</u>	<u>\$ 9,402,655</u>	<u>\$ 8,412,015</u>	<u>\$ 10,361,738</u>

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 2014 through 2018

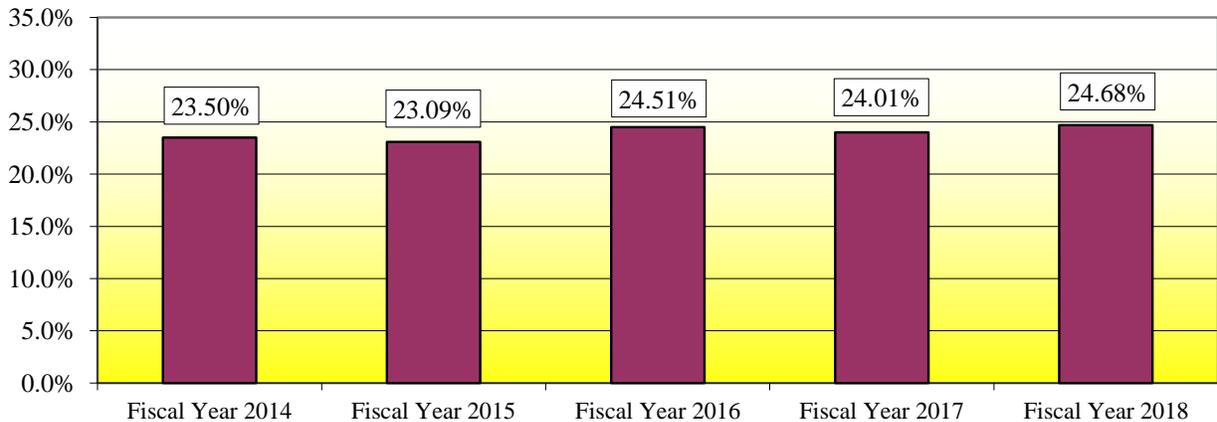


	Fiscal Year 2014	Fiscal Year 2015	Fiscal Year 2016	Fiscal Year 2017	Fiscal Year 2018
Total Operating Expense	\$121,046,318	\$123,277,591	\$135,819,228	\$132,417,829	\$138,483,276
Total Operating Revenue	\$157,896,534	\$159,967,949	\$179,472,755	\$173,819,106	\$183,368,092

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

NET INCOME BEFORE TRANSFERS COMPARED TO OPERATING REVENUE

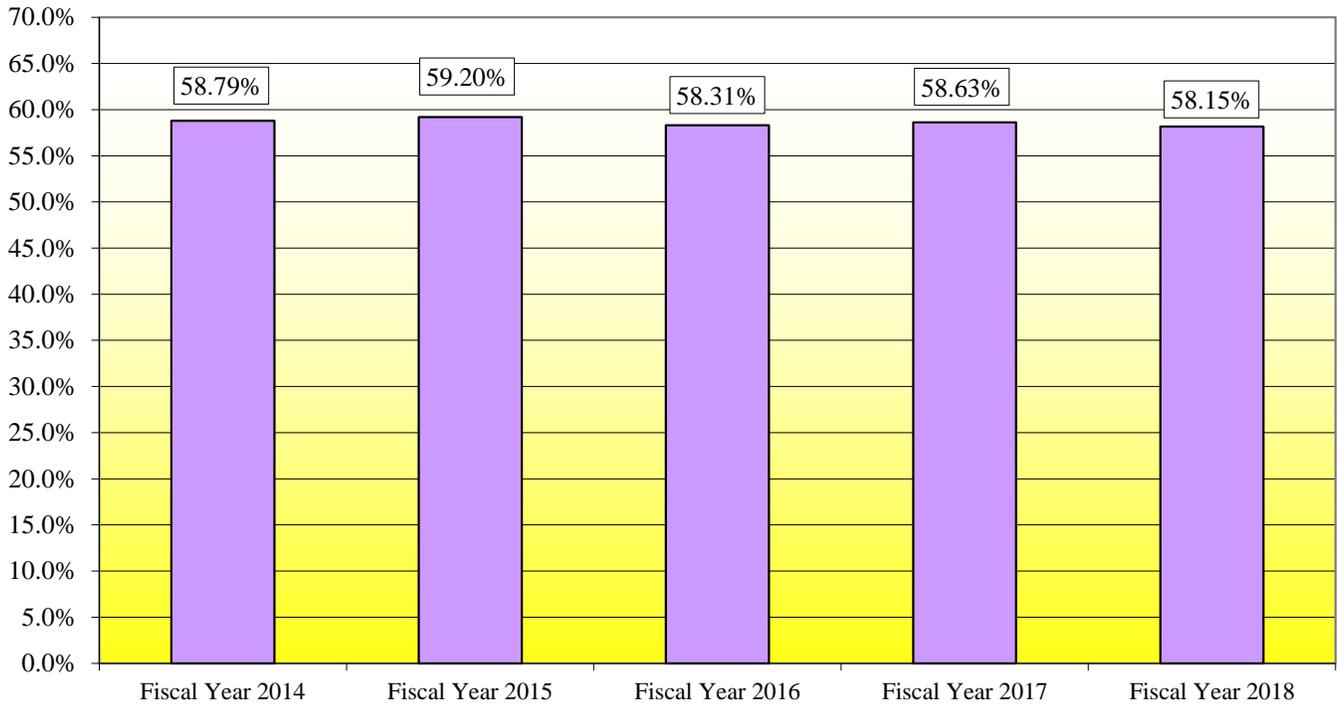
For the Fiscal Years 2014 through 2018



	Fiscal Year 2014	Fiscal Year 2015	Fiscal Year 2016	Fiscal Year 2017	Fiscal Year 2018
Net Income Before Transfers	\$ 37,107,758	\$ 36,940,611	\$ 43,984,670	\$ 41,732,767	\$ 45,250,761
Total Operating Revenue	\$157,896,534	\$159,967,949	\$179,472,755	\$173,819,106	\$183,368,092

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 2014 through 2018



	Fiscal Year 2014	Fiscal Year 2015	Fiscal Year 2016	Fiscal Year 2017	Fiscal Year 2018
Prize Expense	\$ 92,821,370	\$ 94,696,026	\$ 104,644,944	\$ 101,901,594	\$ 106,634,524
Total Operating Revenue	\$ 157,896,534	\$ 159,967,949	\$ 179,472,755	\$ 173,819,106	\$ 183,368,092

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