

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
OFFICE OF THE INSPECTOR GENERAL**

**DISTRICT OF COLUMBIA**

**LOTTERY AND CHARITABLE  
GAMES CONTROL BOARD**

**Financial Statements and  
Management's Discussion and Analysis  
(with Independent Auditors' Report Thereon)  
Fiscal Year Ended September 30, 2010**



**CHARLES J. WILLOUGHBY  
INSPECTOR GENERAL**

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**Office of the Inspector General**

Inspector General



June 9, 2011

The Honorable Vincent C. Gray  
Mayor  
District of Columbia  
Mayor's Correspondence Unit, Suite 316  
1350 Pennsylvania Avenue, N.W.  
Washington, D.C. 20004

The Honorable Kwame R. Brown  
Chairman  
Council of the District of Columbia  
John A. Wilson Building, Suite 504  
1350 Pennsylvania Avenue, N.W.  
Washington, D.C. 20004

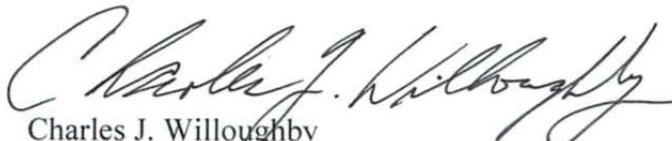
Dear Mayor Gray and Chairman Brown:

As part of our contract for the audit of the District of Columbia's general purpose financial statements for fiscal year (FY) 2010, Bert Smith and Company (BS&C) submitted the enclosed final report on the District of Columbia Lottery and Charitable Games Control Board (Board).

BS&C opined that the financial statements present fairly, in all material respects, the financial position of the Board for the year ended September 30, 2010, and the changes in financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. In accordance with *Government Accounting Standards*, BS&C also has issued its report on consideration of the Board's internal control over financial reporting and on its tests of the Board's compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters.

If you have questions or need additional information, please contact me or Ronald W. King, Assistant Inspector General for Audits, at (202) 727-2540.

Sincerely,



Charles J. Willoughby  
Inspector General

Enclosure

CJW/ws

cc: See Distribution List

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**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
LOTTERY AND CHARITABLE GAMES CONTROL BOARD**

**FINANCIAL STATEMENTS AND MANAGEMENT'S DISCUSSION AND ANALYSIS  
(WITH INDEPENDENT AUDITOR'S REPORT THEREON)**

**YEAR ENDED SEPTEMBER 30, 2010**

**BERTSMITH  
& Co.**

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**Certified Public Accountants and Management Consultants**

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
LOTTERY AND CHARITABLE GAMES CONTROL BOARD**

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## INDEPENDENT AUDITOR'S REPORT

To the Mayor and Members of  
The Council of the Government of the District of Columbia, and  
The Lottery and Charitable Games Control Board  
Washington, D.C.

We have audited the accompanying financial statements of the District of Columbia Lottery and Charitable Games Control Board, an enterprise fund of the Government of the District of Columbia, as of and for the year ended September 30, 2010, as listed in the table of contents. These financial statements are the responsibility of the District of Columbia Lottery and Charitable Games Control Board management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year's summarized comparative information has been derived from the District of Columbia Lottery and Charitable Games Control Board's 2009 financial statements. Those statements were audited by other auditors whose report dated March 18, 2010, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District of Columbia Lottery and Charitable Games Control Board's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in note 2, the financial statements only present the District of Columbia Lottery and Charitable Games Control Board and do not purport to, and do not, present fairly the financial position of the Government of the District of Columbia as of September 30, 2010, 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.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the District of Columbia Lottery and Charitable Games Control Board, as of September 30, 2010, and the changes in financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 24, 2011 on our consideration of the District of Columbia Lottery and Charitable Games Control Board's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The accompanying management's discussion and analysis on pages 3 through 13, is not a required part of the basic financial statements but is supplementary information required by the accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Bert Smith & Co.

Washington, D.C.  
January 24, 2011

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**LOTTERY AND CHARITABLE GAMES CONTROL BOARD**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**SEPTEMBER 30, 2010**  
*(Dollar Amounts in Thousands)*

The discussion and analysis of the D.C. Lottery and Charitable Games Control Board's (the Lottery) financial performance provides an overview of its financial activities for the fiscal year ended September 30, 2010. This discussion and analysis should be read in conjunction with the attached financial statements.

**Background and Other Significant Information**

The Lottery was established by Public Law 3-172 as an independent agency of the Government of the District of Columbia (District). In accordance with law, the Lottery is responsible for generating revenues through the sale of lottery products and required to remit monthly gaming revenues less prizes, operating expenses and a reserve not to exceed 2% of annual prize payments to the General Fund of the District.

The Lottery's financial transactions are accounted for as an enterprise fund in the District's basic financial statements.

**Financial Highlights**

- Gross revenues from lottery gaming activities decreased \$15,211 or 6.20% from prior year amount.
- The Agency generated ticket sales of \$229,705 for an aggregate decrease of \$15,277 or 6.24% less than the prior year total of \$244,982.
- Total operating expenses decreased by \$13,232 or 7.49% primarily the result of prizes payout reduction to 51.78% of ticket sales versus the prior year rate of 52.27%.
- The DC Four game's prize payout percentage rate decreased to 41.63% of sales from the prior year's payout rate of 52.42%.
- Overall prize payouts decreased \$9,126 or 7.13% from the prior year total.
- Transfers to the District's General Fund decreased \$2,025 equivalent to 2.94% of the prior year's total.

To effectively understand the Lottery's operations and to assess its financial activities, the reader must pay attention to individual game sales, related prize expenses and payout percentages, and the resulting impact on change in net assets or amounts transferred to the District's General Fund. Prize payouts and the volume of Powerball and Mega Millions sales have the most dramatic effect on transfer levels but are beyond the control of management.

**Using This Financial Report**

This financial report consists of a series of financial statements, prepared in accordance with GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. These statements focus on the financial condition, the results of operations, and cash flows of the Lottery as a whole.

One of the most important questions asked about the Lottery's finances is whether or not they have improved as a result of the year's activities. The key to understanding this core question is the Statements of Net Assets; the Statements of Revenues, Expenses, and Changes in Net Assets; and the Statements of Cash Flows. These statements present financial information in a form that is similar to that used by commercial entities.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
 LOTTERY AND CHARITABLE GAMES CONTROL BOARD  
 MANAGEMENT'S DISCUSSION AND ANALYSIS  
 SEPTEMBER 30, 2010  
 (Dollar Amounts in Thousands)**

The Lottery's net assets (the difference between assets and liabilities) are one indicator of the improvement or erosion of financial health. The Statements of Net Assets include all assets and liabilities. It is prepared under the economic resources measurement focus and the accrual basis of accounting, whereby revenues are recognized when earned and expenses are recognized when the related liability is incurred.

The Statements of Revenues, Expenses and Changes in Net Assets present the revenues earned and the expenses incurred during each year. Activities are reported as either operating or non-operating. Another important factor to consider when evaluating financial viability is the Lottery's ability to meet financial obligations as they come due. The Statements of Cash Flows present information related to cash inflows and outflows summarized by operating, capital and non-capital financing and investing activities.

**Financial Analysis**

The Lottery's net assets increased by \$41, \$49 and \$68 for the years ended September 30, 2010, 2009, and 2008, respectively. The following is a summary of the Lottery's financial information as of and for the years ended September 30, 2010, 2009, and 2008.

**Table 1: Summary of Net Assets  
 (In Thousands)**

	<b>September 30</b>		
	<b>2010</b>	<b>2009</b>	<b>2008</b>
<b>Assets:</b>			
Current and other assets	\$ 15,834	\$ 14,981	\$ 14,675
Capital assets (net of accumulated depreciation)	579	478	364
Restricted investments	29,218	35,153	41,379
Total assets	<u>45,631</u>	<u>50,612</u>	<u>56,418</u>
<b>Liabilities:</b>			
Accounts payable and accrued expenses	4,298	3,974	3,682
Deferred revenues	152	180	303
Accrued prizes and commissions	8,052	7,435	7,233
Obligations for unpaid prizes - short term	6,873	7,406	7,681
Obligations for unpaid prizes - long term	22,345	27,747	33,698
Total liabilities	<u>41,720</u>	<u>46,742</u>	<u>52,597</u>
<b>Net assets:</b>			
Invested in capital assets	579	478	364
Unrestricted	3,332	3,392	3,457
Total net assets	<u>\$ 3,911</u>	<u>\$ 3,870</u>	<u>\$ 3,821</u>

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
 LOTTERY AND CHARITABLE GAMES CONTROL BOARD  
 MANAGEMENT'S DISCUSSION AND ANALYSIS  
 SEPTEMBER 30, 2010  
 (Dollar Amounts in Thousands)**

**Table 2: Summary of Revenues, Expenses,  
 and Changes in Net Assets  
 (In Thousands)**

	<b>Years Ended September 30</b>		
	<b>2010</b>	<b>2009</b>	<b>2008</b>
Operating revenues:			
Gaming revenues	\$ 230,159	\$ 245,370	\$ 252,721
Operating expenses:			
Prizes	118,932	128,058	135,060
Other	44,461	48,567	47,921
Total operating expenses	163,393	176,625	182,981
Operating income	66,766	68,745	69,740
Nonoperating revenues – interest and dividends	25	79	628
Income before transfers	66,791	68,824	70,368
Transfers to the District's General Fund	(66,750)	(68,775)	(70,300)
Change in net assets	\$ 41	\$ 49	\$ 68

Unrestricted net assets were \$3,332, \$3,392 and \$3,457 at September 30, 2010, 2009 and 2008, which represent decreases of \$60 and \$65 and increase of \$15, respectively. Current assets increased by \$853, \$306 and \$116 in 2010, 2009, and 2008, respectively. Total liabilities decreased \$5,022 or 10.74%, \$5,855 or 11.13%, and \$5,245 or 9.07%, for the years ended September 30, 2010, 2009 and 2008, respectively, primarily the result of decreases in the Lottery's obligations for unpaid prizes. The Multi-State Lottery Association (MUSL) purchases U.S. government securities in the name of the Lottery for Lotto America and Powerball jackpot winners from the District of Columbia. Jackpot winners have the option of accepting the cash value of the jackpot amount or annuity payments for 25 years. The restricted investments balance of \$29,218, \$35,153 and \$41,379 in 2010, 2009 and 2008, respectively, represents the net present value of securities totaling \$30,526, \$37,932, and \$45,613 in 2010, 2009 and 2008, respectively, to fund future annuity installment payments. The restricted investments value decreased by \$5,935, \$6,226 and \$5,346 during 2010, 2009 and 2008, respectively, due to payments of \$7,406, \$7,681 and \$8,631 net of unrealized gains of \$908 and \$249 in 2010 and 2009 and net unrealized losses of \$356 in 2008. Accretion of investments totaled \$563, \$1,206 and \$3,641 in 2010, 2009 and 2008, respectively. Corresponding amounts are recorded as obligations for unpaid prizes.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
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 MANAGEMENT'S DISCUSSION AND ANALYSIS  
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Table 3: Gaming Revenues, Prizes, Commissions and Transfers

2010													
	Lucky			Hot			Rolling		Mega		Instant		Total
	Numbers	D.C. Four	Powerball	Keno	Lotto	Daily 6	Cash 5	DC Five	Millions	Raffle	Games	Others	Total
Gaming revenues	\$ 56,361	\$ 68,619	\$ 20,175	\$ 12,582	\$ 2,871	\$ 3,382	\$ -	\$ 11,392	\$ 4,313	\$ 39	\$ 49,972	\$ 453	\$ 230,159
Prizes	(29,166)	(28,563)	(9,321)	(7,983)	(1,378)	(1,325)	246	(5,270)	(2,230)	(60)	(33,882)	-	(118,932)
Agent's commissions	(3,696)	(3,844)	(1,072)	(848)	(164)	(202)	12	(624)	(231)	(2)	(3,907)	-	(14,478)
Gross margin	\$ 23,499	\$ 36,212	\$ 9,782	\$ 3,751	\$ 1,329	\$ 1,855	\$ 258	\$ 5,498	\$ 1,852	\$ (23)	\$ 12,283	\$ 453	\$ 96,749
Transfers	\$ 16,450	\$ 27,625	\$ 7,025	\$ 2,500	\$ 1,000	\$ 1,525	\$ 255	\$ 4,325	\$ 1,200	\$ -	\$ 4,845	\$ -	\$ 66,750

2009												
	Lucky			Hot			Rolling		Instant		Total	
	Numbers	D.C. Four	Powerball	Keno	Lotto	Daily 6	Cash 5	DC Five	Raffle	Games	Others	Total
Gaming revenues	\$ 60,831	\$ 79,908	\$ 33,003	\$ 12,578	\$ 3,831	\$ 3,957	\$ 2,713	\$ 2,908	\$ -	\$ 45,253	\$ 388	\$ 245,370
Prizes	(27,504)	(41,890)	(15,557)	(7,762)	(1,872)	(1,596)	(1,351)	(1,212)	-	(29,314)	-	(128,058)
Agent's commissions	(3,869)	(4,558)	(1,899)	(840)	(219)	(238)	(168)	(160)	-	(3,365)	-	(15,316)
Gross margin	\$ 29,458	\$ 33,460	\$ 15,547	\$ 3,976	\$ 1,740	\$ 2,123	\$ 1,194	\$ 1,536	\$ -	\$ 12,574	\$ 388	\$ 101,996
Transfers	\$ 21,770	\$ 23,145	\$ 11,025	\$ 2,625	\$ 1,200	\$ 1,610	\$ 860	\$ 805	\$ -	\$ 5,735	\$ -	\$ 68,775

2008												
	Lucky			Hot			Rolling		Instant		Total	
	Numbers	D.C. Four	Powerball	Hot Fire	Keno	Lotto	Daily 6	Cash 5	Raffle	Games	Others	Total
Gaming revenues	\$ 66,409	\$ 84,156	\$ 32,774	\$ -	\$ 13,640	\$ 2,945	\$ 4,270	\$ 3,111	\$ -	\$ 45,020	\$ 396	\$ 252,721
Prizes	(33,387)	(43,436)	(15,698)	-	(8,425)	(1,445)	(1,777)	(1,708)	19	(29,153)	-	(135,060)
Agent's commissions	(4,323)	(4,786)	(1,813)	-	(936)	(166)	(257)	(190)	-	(3,321)	-	(15,782)
Gross margin	\$ 28,699	\$ 35,934	\$ 15,263	\$ -	\$ 4,289	\$ 1,334	\$ 2,236	\$ 1,213	\$ 19	\$ 12,546	\$ 396	\$ 101,879
Transfers	\$ 21,150	\$ 26,210	\$ 11,065	\$ -	\$ 2,765	\$ 900	\$ 1,635	\$ 765	\$ 18	\$ 5,792	\$ -	\$ 70,300

Table 3 provides a comparison of sales, prizes, agent commissions, gross margin, and transfers to the District's General Fund generated by each lottery product offered. Overall gaming revenues totaled \$230,159, \$245,370 and \$252,721 in fiscal years 2010, 2009 and 2008, respectively. Prize expenses decreased \$9,126 or 7.13% in 2010, \$7,002 or 5.18% in 2009 and \$10,278 or 7.07% in 2008. Total prize payouts as a percentage of gaming revenue were 51.67%, 52.19%, and 53.44% in 2010, 2009 and 2008, respectively. Agent commissions decreased \$838, \$466 and \$209 in 2010, 2009 and 2008, respectively, due to the related declines in ticket sales and prize payouts.

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LOTTERY AND CHARITABLE GAMES CONTROL BOARD  
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(Dollar Amounts in Thousands)**

**Lucky Numbers**

Lucky Numbers is a daily three-digit game in which players may wager 50 cents or one dollar with nine ways to win prizes ranging from 25 to 500 dollars. Sales totaled \$56,361 in 2010 for a \$4,470 or 7.35% decline from the 2009 sales level of \$60,831. The game continues to be impacted by the economic downturn, demographic changes in the District's population and some cannibalization of sales by the DC Five game. The Lottery Board continues to strategically implement marketing and promotional campaigns in an attempt to stabilize and enhance sales for the game.

Prizes amounted to \$29,166 in 2010, for a \$1,662 or 6.04% increase over the \$27,504 expensed in 2009. Agents/retailers commission expense decreased \$173 primarily the result of noted decrease in sales offset by increase in prize validation commissions over prior year amount. Net proceeds to the District's General Fund totaled \$16,450 and represented a \$5,320 or 24.44% decline from the \$21,770 generated in 2009. The decrease in transfer amount can be attributed to lower sales, interest and other income, and increase in prize payouts offset by a decrease in other operating expenses allocated to the game from prior year totals. The Lucky Numbers game accounted for 24.49% of total gaming revenue and 24.29% of the overall gross margin. The game reflected essentially the same gaming revenue percentage contribution and a 4.59% decline in gross margin percentage contribution in comparison to prior year amounts.

In 2009, sales totaled \$60,831 for a \$5,578 or 8.40% decrease from the prior year's sales level of \$66,409. Prizes decreased \$5,883 or 17.62% to \$27,504 in 2009 from the \$33,387 expensed in 2008. Agents/retailers commission expense decreased \$454 as a result of corresponding decreases in sales and prize amounts from the prior year. Net proceeds to the District's General Fund totaled \$21,770 for a \$620 increase from the \$21,150 generated in 2008. The increase in transfer amount can be attributed to the decreases in sales, interest and other income, prize payouts, agents/retailer commissions, and other operating expenses in comparison to prior year totals. The Lucky Numbers game accounted for 24.79% of total gaming revenue and 28.88% of the overall gross margin reflecting a marginal decline in percentage of gaming revenue and slight increase in gross margin percentage contribution over the prior year.

**DC Four**

DC Four is a daily four-digit game with a fixed payout. Players may wager 50 cents or one dollar for a chance to win seven different ways. Ticket sales totaled \$68,619 in 2010 for an \$11,289 or 14.13% decrease from the \$79,908 generated in 2009. The game was impacted by economic conditions and suffered sales erosion due to the DC Five game.

Prizes in 2010 totaled \$28,563 representing a \$13,327 or 31.81% decrease from the \$41,890 prize payout in 2009. Other operating costs decreased \$2,447 from the prior year's total primarily due to decreased agents/retailer commissions, direct costs, and administrative cost allocations to the game. Transfers to the District's General Fund totaled \$27,625 for a \$4,480 or 19.36% increase over the \$23,145 transferred in 2009. The decrease in ticket sales offset by lower prize expense and net decrease in other costs account for the decline in transfer amount. The DC Four game provided 29.81% of total gaming revenue and 37.43% of the overall gross margin. The decrease in gaming revenue and increase in gross margin contribution percentages from prior year amounts can be directly associated to lower ticket sales, prizes, and agents/retailer commissions.

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In 2009, sales totaled \$79,908 for a \$4,248 or 5.05% decrease from the \$84,156 recorded in 2008. Prizes totaled \$41,890 in 2009 for a \$1,596 or 3.67% decline from the \$43,486 amount expensed in 2008. Other operating costs increased \$422 over 2008 as a result of lower other direct and administrative cost allocations to the game. Net proceeds to the District's General Fund totaled \$23,145 for a \$3,065 decrease from the \$26,210 transferred in 2008. The decrease in sales offset by lower prize expense and net increase in other operating costs account for the decline in transfer amount. The DC Four game accounted for 32.57% of total gaming revenue and 32.81% of the overall gross margin. The decrease in contribution percentages for gaming revenue and gross margin from prior year amounts can be directly associated to lower ticket sales.

#### **DC Five**

DC Five is a daily five-digit game with a fixed payout. Players may wager 50 cents or one dollar for a chance to win thirteen different ways. Players select a number within the range 00000 to 99999. Tickets may be purchased for the next draw only or for next draw and up to seven consecutive draws for the mid-day and nightly drawings. Players also have the option for advance day play. This feature allows a player to place a bet for a specific day in the future. The DC Five game was launched effective July 19, 2009.

Ticket sales totaled \$11,392 in 2010. Prizes and agents/retailer commissions amounted to \$5,894. Other operating expenses inclusive of gaming fees, advertising, other direct costs, and administrative costs accounted for an additional \$1,166 in expenses. The game generated \$4,325 in transfer to the District's General.

In 2009, ticket sales amounted to \$2,908 due to slightly over two full months of operations. Overall operating expenses amounted to \$2,101 resulting in transfers to the District's General Fund of \$805.

#### **Powerball**

The Powerball game is a five out of fifty-nine plus one out of thirty-nine online lottery game that pays a grand prize on an annuitized para-mutuel basis or as a cash lump sum payment and all other prizes on a fixed basis. All annuitized prizes are paid in thirty annual graduated installments. The Powerball game is sponsored by the Multi-State Lottery Association (MUSL), a conglomerate of thirty states, the District of Columbia and Virgin Islands, that combines resources and sales to offer larger jackpots. Party lotteries pool their sales and other resources, but otherwise account for operations separately. The prize structure matrix for the game was changed effective January 4, 2009.

Powerball sales totaled \$20,175 in 2010 representing a \$12,828 or 38.87% decrease from the \$33,003 generated in 2009. The Multi-State Lottery Association and Mega Millions conglomerates agreed to allow respective member states to cross sale tickets in January 2010. The decrease in ticket sales can be attributed to offsetting of sales to the Mega Millions game, lost sales to surrounding jurisdictions, and the Powerball game's inability to generate jackpots to levels necessary to increase player participation and sales volume. Powerball sales are jackpot driven and high jackpots impact sales levels.

Prizes amounted to \$9,321 in 2010 representing a \$6,236 decrease from the \$15,557 expensed in 2009. Powerball prizes are expensed at the rate of 50.0% of sales intake offset by lapsed prizes. Prize expense decreased proportionate to sales intake in 2010 offset by lapsed prizes totaling \$805. Operating expenses excluding prizes decreased \$2,224 primarily due to lower sales volume. Other income charged to the game increased \$357. The decrease in ticket sales offset by lower operating costs accounts for the \$4,000 reduction in transfer to the District's General Fund to \$7,025 from the \$11,025 transferred in 2009.

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Powerball sales amounted to \$33,003 in 2009 and represented a \$229 increase over the \$32,774 sold in 2008. Prizes totaled \$15,557 for a \$141 decrease from the \$15,698 expensed in 2008. Prize expense increased proportionate to sales in 2009, but was offset by more lapsed prizes. Operating expenses excluding prizes increased \$192 as a result of higher agents/retailers commissions and allocated administrative costs. Other income charged to the game decreased \$197 as a result of change in method of computing MUSL dividends income. The increase in ticket sales offset by decreases in other income and prizes, and increased other operating expenses accounts for the reduction in transfer to the District's General Fund to \$11,025 from \$11,065 transferred in 2008.

### **Mega Millions**

The Mega Millions game is a five out of fifty-six plus one out of forty-six online lottery game that pays a grand prize or a cash lump sum payment and all other prizes on a fixed basis. All annuity prizes are paid in twenty-six annual installments. Some states offer a megaplier feature to increase non-jackpot prizes by 2, 3, or 4 times. The Mega Millions game is sponsored by the Mega Millions Group, a conglomerate of twelve states, and participating MUSL members that combine resources and sales to offer larger jackpots. All Mega Millions transactions of the Lottery are handled through the Multi-State Lottery Association. Party lotteries pool their sales and other resources, but otherwise account for operations separately. The Lottery began selling Mega Millions tickets effective January 31, 2010.

Mega Millions sales totaled \$4,313 for the approximate eight months of operations in 2010. Prizes expense and other operating costs amounted to \$2,230 and \$860 in 2010, respectively. Mega Millions prizes are expensed at the rate of 51.0% of regular sales and 50% of megaplier sales offset by lapsed prizes. Ticket sales offset by overall operating costs resulted in a transfer to the District's General Fund of \$1,200.

### **Keno**

Keno is a 10/20/80 game with fixed prizes. Players choose to play from 1 to 10 spots, with each spot having a different prize structure. Players select twenty numbers from a field of 80 numbers. Draws are held every four minutes during valid game times. Payouts range from five dollars to 100,000 dollars. Tier 1 prizes start as a fixed payout and transitions to a para-mutuel payout when the number of winners per draw exceeds 10. The game is supplemented by Keno Spin which features a multiplier option to the game's prizes. The Keno game continues to be impacted by the changing demographics in the District of Columbia, inability to add new social settings and the economy. Keno sales totaled \$12,582 in 2010 are offered at all agent/retailers locations. The Lottery continues to market the game through targeted awareness and promotional campaigns.

Prizes expense in 2010 increased by \$221 to \$7,983 in comparison to the \$7,762 expensed in 2009. Overall operating expenses less prizes decreased \$111 primarily due to reduction in gaming fees cost. Transfers to the District's General Fund decreased \$125 to \$2,500 in 2010 from the \$2,625 transferred in 2009.

Ticket sales in 2009 totaled \$12,578 for a \$1,062 or 7.79% decrease from the \$13,640 generated in 2008. Prizes expense decreased \$663 to \$7,762 from the \$8,425 expensed in 2008. Overall operating expenses less prizes and agents/retailer commission expenses decreased \$175 primarily due to reductions in advertising and other direct costs. The decrease of \$140 in net proceeds and transfers to the District's General Fund to \$2,625 in 2009 from the \$2,765 transferred in 2008 can be attributed to lower sales offset by reduced operating costs.

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LOTTERY AND CHARITABLE GAMES CONTROL BOARD  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
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**Hot Lotto**

Hot Lotto is a five out of thirty-nine plus one out of nineteen online lottery game that pays a grand prize, at the election of the player at time of ticket purchase, either on an annuitized para-mutuel or cash option basis. All other prizes are paid on a fixed basis. Prizes are expensed at the rate of 50.0% of sales intake less lapsed prizes. The Hot Lotto game is sponsored by the Multi-State Lottery Association (MUSL), a conglomerate of thirteen states and the District of Columbia, which combines resources and sales to offer larger jackpots. The initial jackpot starts at \$1 million and drawings are held every Wednesday and Saturday. Party lotteries pool their sales and other resources, but otherwise account for operations separately.

Ticket sales amounted to \$2,871 in 2010, representing a \$960 or 25.06% decrease from the \$3,831 generated in 2009. The decrease in sales from the prior year's total is the result of lower jackpots during 2010.

Prizes and agents/retailer commission expenses totaled \$1,542 and reflected a \$549 or 26.26% decrease in 2010 from the \$2,091 expensed in 2009. Other operating expenses decreased \$223 primarily as a result of lower gaming fees, other direct and administrative cost allocations. The \$200 decrease in transfers to the District's General Fund to \$1,000 in 2010 from the \$1,200 transferred in 2009 can be attributed to decrease in sales offset by a proportionate decrease in other operating expenses.

Hot Lotto ticket sales increased \$886 or 30.08% to \$3,831 in 2009 in comparison to the \$2,945 sold in 2008. The increase in sales over the prior year was the direct result of higher jackpots in 2009. Prizes and agents/retailer commission expenses increased \$480 to \$2,091 or 29.79% over the \$1,611 expensed in 2008. Other operating expenses increased \$112 as a result of higher gaming fees, other direct costs, and administrative cost allocations. The \$300 increase in transfers to the District's General Fund to \$1,200 in 2009 over the \$900 transferred in 2008 can be directly attributed to increase in gross margin offset by increase in other operating expenses excluding prizes and agents/retailer commissions.

**DC Daily Six**

The DC Daily Six game is a six out of thirty-nine numbers online lotto type game that pays fixed prize payouts ranging from one dollar to 250,000 dollars. Players receive two boards (set of six numbers) for one dollar. Drawings are held nightly seven days a week and players can purchase tickets for the next draw only or the next draw and up to 42 consecutive drawings in predetermined increments. The Division 1 prize payout is fixed for the first four winners. If the number of winners exceeds four then all Division 1 winners share the maximum payout of \$1 million. Payouts for Divisions 2 through 6 are fixed. The DC Daily Six game launched effective August 28, 2005 and replaced the Quick Cash game in the Lottery Board's portfolio of games.

Ticket sales decreased \$575 or 14.53% to \$3,382 in 2010 from the \$3,957 sales amount in 2009.

Prizes and agents/retailers commission expense amounted to \$1,527 and reflected a \$307 decrease from the \$1,834 expensed in 2009. Other operating expenses reflected a decrease of \$191 from 2009 totals. The decrease of \$85 in transfer to the District's General Fund from \$1,610 in 2009 to \$1,525 in 2010 is the result of lower ticket sales offset by the net reduction in prizes, agents/retailers commissions and other operating costs.

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Sales totaled \$3,957 in 2009 for a \$313 or 7.33% decrease from the \$4,270 generated in 2008. Prizes and agents/retailer commission expense decreased \$200 to \$1,834 versus the \$2,034 incurred in 2008. Other operating expenses reflected a minor decrease of \$87 from the prior year total. Decreases in prizes and agents/retailer commissions and other operating costs offset by lower ticket sales account for the marginal decline of \$25 in transfer to the District's General Fund to \$1,610 in 2009 versus the \$1,635 produced in 2008.

#### **DC Rolling Cash Five**

The DC Rolling Cash Five game is a five out of thirty-five numbers online lotto type game that pays fixed prize payouts ranging from one dollar to the generated jackpot amount. Player received one wager (set of five numbers) for the sum of one dollar. Drawings are held nightly seven days a week and players could purchase tickets for the next draw only or the next draw and up to 42 consecutive drawings in predetermined increments. Division 1 grand prize winnings are para-mutuel and varied depending on number of players and winners. Prize payouts for Divisions 2 through Division 4 winners are fixed. The DC Rolling Cash Five game was launched November 20, 2005 and replaced by the Hot Five game. Lottery management decided to discontinue the game effective July 18, 2009 due to declining ticket sales year after year.

There were no ticket sales in 2010. The transfer to the District's General Fund totaling \$255 is the result of lapsed prizes and associated reduction in agents/retailer commissions.

Sales totaled \$2,713 in 2009 for a \$398 or 12.79% decrease from the \$3,111 generated in 2008. Operating expenses decreased \$490 to \$1,853 in 2009 compared to \$2,343 in 2008. The decrease in ticket sales offset by greater decline in operating expenses accounts for the \$95 increase in transfer to the District's General Fund to \$860 in 2009 compared to the \$765 transferred in 2008.

#### **DC Raffle**

The DC Raffle game is a promotional game designed to run for certain intervals of time and to generate a maximum number of tickets to be sold. Tickets are printed in sequential number order which serves as the bet. Each player wagers a set sum for a ticket and chance to win fixed prizes.

A small promotional campaign was initiated in 2010 resulting in minimal ticket sales of \$39. Operating costs totaling \$121 consisting primarily of prizes and agents/retailer commissions, gaming fees, and advertising costs resulted in a net operating loss of \$82.

There were no sales or other transactions for the game in 2009. The negative expense amount of \$19 reported in 2008 represented lapsed prizes which essentially accounts for the \$18 transferred to the District's General Fund.

#### **Instant Tickets**

Instant or scratch games are designed to allow a player the opportunity to determine if he/she is an instant winner at the time of ticket purchase. The price of tickets and prize structure are determined before the production of tickets. Instant ticket sales amounted to \$49,972 in 2010 representing a \$4,719 or 10.43% increase over sales of \$45,253 in 2009.

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Prizes in 2010 totaled \$33,882 for a \$4,568 increase over the \$29,314 expensed in 2009. Overall operating costs, less prizes and agents/retailer commissions totaled \$7,421 and represented a \$584 increase over the \$6,837 expensed in 2009. Transfers to the District's General Fund of \$4,845 in 2010 declined \$890 from the \$5,735 generated in 2009 primarily due to higher prize payouts, advertising, and allocated administrative costs.

Instant ticket sales of \$45,253 in 2009 were \$233 or .52% greater than 2008 sales of \$45,020. Prizes expense in 2009 increased to \$29,314 and was \$161 over the \$29,153 expensed in 2008. Other operating costs totaled 6,837 for an increase of \$106 over the prior year's amount of \$6,731, primarily due to higher administrative cost allocations offset by lower other direct costs. Transfers to the District's General Fund of \$5,735 in 2009 represented a slight decline from the \$5,792 reported in 2008.

The Lottery has been able to stimulate sales through a combination of offering higher price point games, designing games with higher prize payouts to increase winning opportunities for players, and providing a full complement of available tickets at all agent locations. The prize payout rate averaged 67.80% and 64.78% as a percentage of tickets sold in 2010 and 2009, respectively.

#### **Interest, Dividends and Other Income**

All idle cash of the Lottery is invested through the District's General Fund Pooled Investments Account. Powerball receipts transferred to MUSL to fund major jackpots are invested in securities prior to jackpots being hit and earnings are allocated annually to party lotteries. Interest and dividend income, shown separately in the financial statements, has decreased by \$54, \$549, and \$312 in 2010, 2009 and 2008, respectively. Interest and dividend income is impacted by various market conditions, the national economy, and other factors beyond the control of individual entities.

Other Income increased \$65 in 2010 to \$453 and decreased \$8 in 2009 to \$388 from \$396 in 2008. Bonding fees receipts totaled \$28, \$192, and \$34 in 2010, 2009 and 2008, respectively. Refunds from MUSL as a result of rebalancing reserve funds and distributions of excess contributions by participating members amounted to \$375, \$18, and \$215, in 2010, 2009, and 2008, respectively.

#### **Charitable Gaming Activities**

The Lottery also oversees charitable gaming activities to include the licensing and regulation of charitable and other not-for-profit organizations conducting bingo, raffles, and other fund-raising activities within the District of Columbia. The mission of the Lottery with respect to charitable gaming is to insure that only qualified organizations are licensed to conduct fund-raising activities and that they are carried out in accordance with existing laws, rules and regulations. Revenues generated through the issuance of licenses, processing fees, etc. are not intended to cover costs associated with overseeing program activities.

#### **Contacting the Lottery**

Interested parties can contact the D.C. Lottery at D.C. Lottery and Charitable Games Control Board, 2101 Martin Luther King Jr. Avenue, S.E. Washington, D.C. 20020.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**LOTTERY AND CHARITABLE GAMES CONTROL BOARD**  
**STATEMENTS OF NET ASSETS**  
**SEPTEMBER 30, 2010**  
*(With Comparative Totals for 2009)*  
*(Dollar Amounts in Thousands)*

<b>Assets</b>	<u>2010</u>	<u>2009</u>
<b>Current assets:</b>		
Cash and cash equivalents	\$ 10,858	\$ 7,680
Accounts receivable	4,969	7,292
Prepaid expenses and other	7	9
Restricted investments	6,873	7,406
Total current assets	<u>22,707</u>	<u>22,387</u>
<b>Non-current assets:</b>		
Capital assets, net	579	478
Restricted investments	22,345	27,747
Total non-current assets	<u>22,924</u>	<u>28,225</u>
Total assets	<u>45,631</u>	<u>50,612</u>
<b>Liabilities</b>		
<b>Current liabilities:</b>		
Accounts payable	2,221	2,472
Compensation liabilities	838	764
Deferred revenues	152	180
Accrued prizes and commissions	8,052	7,435
Other accrued liabilities	1,239	738
Obligations for unpaid prizes - current portion	6,873	7,406
Total current liabilities	<u>19,375</u>	<u>18,995</u>
Obligations for unpaid prizes – noncurrent portion	<u>22,345</u>	<u>27,747</u>
Total liabilities	<u>41,720</u>	<u>46,742</u>
<b>Net Assets</b>		
Invested in capital assets, net of related debt	579	478
Unrestricted	3,332	3,392
Total net assets	<u>\$ 3,911</u>	<u>\$ 3,870</u>

*The accompanying notes are an integral part of these financial statements.*

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**LOTTERY AND CHARITABLE GAMES CONTROL BOARD**  
**STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS**  
**YEARS ENDED SEPTEMBER 30, 2010**  
*(With Comparative Totals for 2009)*  
*(Dollar Amounts in Thousands)*

	<u>2010</u>	<u>2009</u>
<b>Operating revenues:</b>		
Gaming revenues	\$ 230,159	\$ 245,370
<b>Operating expenses:</b>		
Prizes	118,932	128,058
Agent's commissions	14,478	15,316
Contractor fees	12,767	16,085
Advertising	5,148	4,900
Administration	11,918	12,132
Amortization and depreciation	150	134
Total operating expenses	<u>163,393</u>	<u>176,625</u>
Operating income	66,766	68,745
<b>Nonoperating revenues - interest and dividends</b>	<u>25</u>	<u>79</u>
Income before transfers	66,791	68,824
<b>Transfers to District General Fund</b>	<u>(66,750)</u>	<u>(68,775)</u>
Change in net assets	41	49
<b>Net assets, beginning of year</b>	<u>3,870</u>	<u>3,821</u>
<b>Net assets, end of year</b>	<u>\$ 3,911</u>	<u>\$ 3,870</u>

*The accompanying notes are an integral part of these financial statements.*

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**LOTTERY AND CHARITABLE GAMES CONTROL BOARD**  
**STATEMENTS OF CASH FLOWS**  
**YEARS ENDED SEPTEMBER 30, 2010**  
*(With Comparative Totals for 2009)*  
*(Dollar Amounts in Thousands)*

	<u>2010</u>	<u>2009</u>
Operating activities:		
Cash receipts from customers	\$ 232,001	\$ 244,665
Cash receipts from others	453	388
Cash payments to vendors	(22,494)	(26,360)
Cash payments to employees	(7,014)	(6,459)
Cash payments for prizes and commissions	(132,793)	(143,172)
Net cash provided by operating activities	<u>70,153</u>	<u>69,062</u>
Capital and related financing activities - acquisition of fixed assets	(250)	(248)
Non-capital financing activities - transfers out	(66,750)	(68,775)
Investing activities - interest and dividends	25	79
Net increase in cash	3,178	118
Cash and cash equivalents - beginning of year	7,680	7,562
Cash and cash equivalents - end of year	<u>\$ 10,858</u>	<u>\$ 7,680</u>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 66,766	\$ 68,745
Amortization and depreciation	150	134
Decrease (increase) in assets:		
Receivables	2,323	(194)
Prepaid expenses	1	6
Increase (decrease) in liabilities:		
Accounts payable	(251)	65
Compensation liabilities	74	166
Deferred revenue	(28)	(123)
Accrued prizes	617	202
Other current liabilities	501	61
Net cash provided by operating activities	<u>\$ 70,153</u>	<u>\$ 69,062</u>

*The accompanying notes are an integral part of these financial statements.*

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**LOTTERY AND CHARITABLE GAMES CONTROL BOARD**  
**NOTES TO FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2010 AND 2009**  
*(Dollar Amounts in Thousands)*

**NOTE 1 ORGANIZATION**

The Lottery and Charitable Games Control Board (the Lottery) was established by Public Law 3-172 as an independent agency of the Government of the District of Columbia (District). In accordance with the law, the Lottery must remit its monthly gaming revenues, less prizes, operating expenses and a reserve not to exceed 2% of projected annual prize payments to the General Fund of the District.

**NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**(a) *Basis of Presentation***

The Lottery's financial transactions are accounted for as an enterprise fund in the District's financial statements. The accompanying financial statements are only those of the Lottery and are not intended to present the financial position, changes in financial position, and cash flows of the District taken as a whole. The District provides certain legal, central accounting and other services to the Lottery. The costs and revenue associated with those services are not reflected in these financial statements.

**(b) *Basis of Accounting***

The accompanying financial statements are prepared on the accrual basis of accounting. Under this method, revenues are reported when earned and expenses are reported at the time the related liabilities are incurred. In accordance with Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Lottery has elected not to follow the Financial Accounting Standards Board (FASB) Statements and Interpretations, APB Opinions, and Accounting Research Bulletins issued after November 30, 1989.

**(c) *Cash and Cash Equivalents***

The Lottery participates in the District's pooled cash program whereby cash that is not needed for immediate disbursement is pooled with that of the District and used to purchase current investments. In accordance with the law, the District may invest the pooled cash directly in, or through repurchase agreements, obligations of the United States or its agencies, which are fully guaranteed by the federal government, and in certificates of deposit, which are issued by federally insured banks. In accordance with District policies, substantially all deposits in the pooled cash program were insured or collateralized with securities held by the District or its agent in the District's name. Interest income from the investment of pooled cash is allocated to the Lottery based on the amount the Lottery invests in the pool. The Lottery considers the pooled cash to be cash equivalents for the purpose of cash flows because the pool may not hold the securities for more than 91 days. Cash and cash equivalents at September 30, 2010 and 2009 respectively, were \$10,858 and \$7,680; of which \$2,299 and \$960 was uninsured, respectively.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
 LOTTERY AND CHARITABLE GAMES CONTROL BOARD  
 NOTES TO FINANCIAL STATEMENTS  
 SEPTEMBER 30, 2010 AND 2009  
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**NOTE 2      SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**(d)    *Capital Assets***

Capital assets are recorded at cost. The cost of major remodeling, betterments, and improvements of \$5 and greater are capitalized. Repairs and maintenance costs are expensed as incurred. When capital assets are retired or sold, the cost and related accumulated depreciation are removed from the appropriate property and equipment accounts, and resulting gains or losses are recorded.

Amortization and depreciation expense are calculated using the straight-line method over the following estimated useful lives:

<u>Category</u>	<u>Estimated Useful Life</u>
Machinery and equipment	5-8 years
Office furniture and fixtures	5-8 years
Leasehold improvements	5-15 years

**(e)    *Gaming Revenue***

Gaming revenue consists of ticket sales and other related revenue including bonding and licensing fees. Revenue from online tickets is recorded as gaming revenue when the drawings are held. Online tickets sold in advance are recorded as deferred revenue until the drawings are held. Revenue from instant tickets is recorded as gaming revenue when the tickets are activated.

**(f)    *Prize Expense***

Instant tickets prize expense is based on the prize payout percentage for each instant lottery game and is accrued as the related gaming revenue is earned. Prize expenses for online games, excluding the Powerball, Hot Lotto, and DC Rolling Cash 5 games, are accrued based on the draw liability associated with drawings for the specific games. Powerball and Hot Lotto prize expenses are recorded at the rate of 50.0% of ticket sales. Mega Millions prize expenses are recorded at the rate of 51.0% of regular sales and 50.0% of megaplier prizes and any additional costs needed to fund jackpots. The accrued prize liability represents a payable for prize amounts that have not been claimed as of each fiscal year-end. Prize expense for all games is reduced by the sum of lapsed prizes not claimed during the required period of one year from the sales draw date for online games and the respective game closing date for instant games.

**(g)    *Compensated Absences***

The Lottery permits employees to accumulate earned but unused vacation and sick pay benefits depending on the employee's length of service. Employees may not accumulate more than 240 hours of vacation benefits. The Lottery accrues for accumulated vacation as the benefits are earned by employees.

There is not a maximum limitation on the amount of unused sick pay benefits that employees may accumulate. The Lottery does not accrue for non-vesting accumulating rights to receive sick pay benefits. Lottery employees participating in the Federal Civil Service Retirement System program may convert sick pay benefits to additional service time at the rate of one month for every 176 hours of sick leave not used at point of retirement.

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**NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**(h) 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, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**NOTE 3 ACCOUNTS RECEIVABLE**

The components of accounts receivable as of September 30, 2010 and 2009 are as follows:

	2010	2009
Due from agents:		
Online games	\$ 381	\$ 2,619
Instant games	4,152	4,556
Total due from agents	4,533	7,175
Other	436	117
Total accounts receivable	\$ 4,969	\$ 7,292

**NOTE 4 CAPITAL ASSETS**

A summary of capital assets as of September 30, 2010 and 2009 is as follows:

	Balance as of October 1, 2009	Additions	Reductions	Balance as of September 30, 2010
Cost:				
Machinery and equipment	\$ 2,474	\$ 250	\$ 109	\$ 2,615
Office furniture and fixtures	20	—	—	20
Lease hold improvements	758	—	—	758
Total cost	3,252	250	109	3,393
Less – accumulated depreciation:				
Machinery and equipment	2,004	141	109	2,036
Office furniture and fixtures	20	—	—	20
Lease hold improvements	750	8	—	758
Total accumulated depreciation	2,774	149	109	2,814
Capital assets – net	\$ 478			\$ 579

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**NOTE 4 CAPITAL ASSETS (CONTINUED)**

	<u>Balance as of October 1, 2008</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance as of September 30, 2009</u>
<b>Cost:</b>				
Machinery and equipment	\$ 2,786	\$ 248	\$ 560	\$ 2,474
Office furniture and fixtures	20	—	—	20
Lease hold improvements	758	—	—	758
Total cost	<u>3,564</u>	<u>248</u>	<u>560</u>	<u>3,252</u>
<b>Less – accumulated depreciation</b>				
Machinery and equipment	2,443	121	560	2,004
Office furniture and fixtures	20	—	—	20
Lease hold improvements	737	13	—	750
Total accumulated depreciation	<u>3,200</u>	<u>134</u>	<u>560</u>	<u>2,774</u>
Capital assets – net	<u>\$ 364</u>			<u>\$ 478</u>

**NOTE 5 MULTI-STATE LOTTERY ASSOCIATION**

**(a) Background**

The Lottery is a member of the Multi-State Lottery Association (MUSL). MUSL has thirty-one (31) members and administers multi-state lottery games. Powerball was initiated on April 20, 1992 and is a semi-weekly para-mutuel drawing with a minimum grand prize of \$20,000. MUSL previously administered the Lotto-America game, which was terminated on April 18, 1992. Hot Lotto was implemented on April 5, 2004 and is a semi-weekly para-mutuel drawing with a minimum grand prize of \$1,000. All MUSL members remit a portion of their Powerball and Hot Lotto revenue to MUSL for the prize payments and administrative expenses of the respective game.

**(b) Restricted Investments and Obligations for Unpaid Prizes**

Lotto-America and Powerball jackpot prizes are payable to winners in annual installments over 20 to 25 years. The Lottery is responsible for sending the annual payments to Lotto-America and Powerball winners who purchased their winning tickets from the Lottery. MUSL is responsible for providing the Lottery cash to fund these installment payments.

As of September 30, 2010 and 2009, MUSL had purchased for the Lottery, U.S. government securities aggregating \$30,526 and \$37,932, respectively to fund future installment payments for the Lottery's Lotto-America and Powerball winners.

The market value of these securities was \$29,218 and \$35,153 as of September 30, 2010 and 2009, respectively. The investments provide the Lottery cash payments corresponding to the Lottery's obligations for the annual installments to the prize winners. The Lottery has reflected the market value of the securities as restricted investments and as corresponding obligations for unpaid prizes on the statements of net assets. All restricted investments are insured and registered or are held by the Lottery or its agent in the Lottery's name.

During fiscal 2003, the Lottery adopted GASB Statement No. 40, *Deposits and Investment Risk Disclosures*. As of September 30, 2010, the Lottery had the following investments and maturities:

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
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**NOTE 5      MULTI-STATE LOTTERY ASSOCIATION (CONTINUED)**

Investment Type	Fair Value	Investment Maturities (in Years)			
		Less Than 1	1 - 5	6 - 10	More Than 10
U.S. Government and Agency Securities	29,218	7,909	18,760	2,280	269

These investments are obligations explicitly guaranteed by the U.S. government and are held for prize annuities based on quoted market prices. The fair value of the liabilities is based on current interest rates of the related U.S. government security held to fund annuity obligations. MUSL's investment policy limits its exposure to credit risk by investing only in securities that are backed by the full faith and credit of the U.S. government or its agencies.

As of September 30, 2010, the Lottery had an interest in a SEC 2a7 pooled government cash management fund of \$1,058 that is included in the less than one year maturity amount. This management fund is not rated.

**(c) MUSL Prize Reserves**

The prize pool for Powerball consists of 50% of each drawing period's sales. Two percent of the prize pool is placed in a prize reserve fund and a set prize reserve fund. These reserve funds serve as contingency funds to protect MUSL from unforeseen liabilities. As of September 30, 2010 and 2009, the total Powerball prize reserve fund was approximately \$85,812 and \$78,668, respectively, of which the Lottery's share was approximately \$1,211 for both years. In addition, the total Powerball set prize reserve fund as of September 30, 2010 and 2009 was approximately \$27,955 and \$28,650, respectively, of which the Lottery's share was approximately \$339 and \$356, respectively.

The balance remaining in the reserve funds are refundable to MUSL members if a member leaves or if MUSL disbands. If a member leaves, the member must wait one year before their portion of the prize reserve funds is returned. The balance in the reserve funds may be used at the discretion of MUSL's Board of Directors. Accordingly, the Lottery's share of the reserve funds is not reflected in the accompanying financial statements.

The prize pool for Hot Lotto consists of 50% of each drawing period's sales. The 50% contribution to the prize pool is distributed to grand prizes and a prize reserve fund based on the following jackpot levels:

- \$1,000,000 to \$2,000,000  
52.5763% to grand prize
- \$2,000,000 to \$5,000,000  
52.5763% to grand prize plus 1.00% to prize reserve fund
- \$5,000,000 to 10,000,000  
52.5763% to grand prize plus 3.00% to prize reserve fund

The prize reserve fund serves as a contingency fund to protect MUSL from unforeseen liabilities. As of September 30, 2010, the total Hot Lotto prize reserve fund was approximately \$6,827 of which the Lottery's share was approximately \$286. The balance in the prize reserve fund may be used at the discretion of the MUSL's Board of Directors. The Lottery's share of the prize reserve fund is not reflected in the accompanying financial statements.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
 LOTTERY AND CHARITABLE GAMES CONTROL BOARD  
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**NOTE 6 OBLIGATIONS FOR UNPAID PRIZES**

Powerball jackpot prizes are paid in 20 or 25 year installments. The first installment is paid approximately two weeks after the prize is claimed. The subsequent annual payments are funded with U.S. Treasury Strips purchased by MUSL for the Lottery. Jackpot prize payables represent the future annual prize payments valued at cost plus accrued interest (present value of securities held to maturity) of the investment securities funding the payments.

	<u>Year ended September 30, 2010 Jackpot</u>	<u>Year ended September 30, 2009 Jackpot</u>
Jackpot prizes payable:		
Due within one year	\$ 6,873	\$ 7,406
Due in subsequent years	<u>22,345</u>	<u>27,747</u>
Total (present value)	29,218	35,153
Add: Interest to maturity	<u>1,308</u>	<u>2,779</u>
Jackpot prizes payable at maturity	<u>\$ 30,526</u>	<u>\$ 37,932</u>

The unamortized discount on the prizes payable is based on interest rates which range from .7918% to 3.7947% and reflect the interest rates earned by the investments held to fund the related liabilities.

The aggregate amount of prizes payable due in each of the five years following September 30, 2010, and the five year incremental totals thereafter, is as follows:

2011	\$ 6,873
2012	6,878
2013	6,253
2014	4,019
2015	2,978
2016 - 2020	2,750
2021 - 2022	<u>775</u>
Total	<u>\$30,526</u>

The following schedule presents the changes in prizes payable:

<b>Balance as of October 1, 2008</b>	<b>\$ 41,379</b>
Increase	1,455
Decrease	<u>(7,681)</u>
<b>Balance as of September 30, 2009</b>	<b>35,153</b>
Increase	1,471
Decrease	<u>(7,406)</u>
<b>Balance as of September 30, 2010</b>	<b><u>\$ 29,218</u></b>

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**NOTE 7 GAMING REVENUES AND EXPENSES**

Gaming revenues and expenses for the fiscal years ended September 30, 2010 and 2009 were as follows:

**Gaming Revenues, Prizes, and Commissions**

	2010												
	Lucky Numbers	D.C. Four	Powerball	Keno	Hot Lotto	DC Daily 6	Rolling Cash 5	DC Five	Mega Millions	Raffle	Instant Games	Others	Total
Gaming revenues	\$ 56,361	\$ 68,619	\$ 20,175	\$ 12,582	\$ 2,871	\$ 3,382	\$ -	\$ 11,392	\$ 4,313	\$ 39	\$ 49,972	\$ 453	\$ 230,159
Prizes	(29,166)	(28,563)	(9,321)	(7,983)	(1,378)	(1,325)	246	(5,270)	(2,250)	(60)	(33,882)	-	(118,932)
Agent's commissions	(3,696)	(3,844)	(1,072)	(848)	(164)	(202)	12	(624)	(231)	(2)	(3,807)	-	(14,478)
<b>Gross margin</b>	<b>\$ 23,499</b>	<b>\$ 36,212</b>	<b>\$ 9,782</b>	<b>\$ 3,751</b>	<b>\$ 1,329</b>	<b>\$ 1,855</b>	<b>\$ 258</b>	<b>\$ 5,498</b>	<b>\$ 1,852</b>	<b>\$ (25)</b>	<b>\$ 12,283</b>	<b>\$ 453</b>	<b>\$ 96,749</b>

	2009											
	Lucky Numbers	D.C. Four	Powerball	Keno	Hot Lotto	DC Daily 6	Rolling Cash 5	DC Five	Raffle	Instant Games	Others	Total
Gaming revenues	\$ 60,831	\$ 79,908	\$ 33,003	\$ 12,578	\$ 3,831	\$ 3,957	\$ 2,713	\$ 2,908	\$ -	\$ 45,253	\$ 388	\$ 245,370
Prizes	(27,504)	(41,890)	(15,557)	(7,762)	(1,872)	(1,596)	(1,551)	(1,212)	-	(29,314)	-	(128,058)
Agent's commissions	(3,269)	(4,558)	(1,899)	(840)	(219)	(238)	(168)	(160)	-	(3,365)	-	(15,316)
<b>Gross margin</b>	<b>\$ 29,458</b>	<b>\$ 33,460</b>	<b>\$ 15,547</b>	<b>\$ 3,976</b>	<b>\$ 1,740</b>	<b>\$ 2,123</b>	<b>\$ 1,194</b>	<b>\$ 1,536</b>	<b>\$ -</b>	<b>\$ 12,574</b>	<b>\$ 388</b>	<b>\$ 101,996</b>

**NOTE 8 TRANSFERS TO THE GENERAL FUND OF THE DISTRICT**

The District Budget Act (PL 4-162) (the Act) of 1983 requires the Lottery to transfer its revenues less expenses and less a reserve not to exceed 2% of annual prize payments to the General Fund of the District. The Mayor may approve a change in the reserve limit, as necessary, upon the request of the Lottery. During the fiscal years ended September 30, 2010 and 2009, the Lottery's net transfers to the General Fund of the District totaled \$66,750 and \$68,775, respectively. The Lottery was in compliance with the Act for the fiscal years ended September 30, 2010 and 2009.

**NOTE 9 RETIREMENT PROGRAMS**

**(a) Defined Benefit Pension Plan**

The majority of the full-time Lottery employees hired before October 1, 1987 are covered by the Federal Civil Service Retirement System (5 U.S.C. 833 1). The Federal Civil Service Retirement System is a cost-sharing multiple employer pension plan.

The U.S. Office of Personnel Management is responsible for administering the Federal Civil Service Retirement System, including collecting the contributions and disbursing the benefits.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
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**NOTE 9 RETIREMENT PROGRAMS (CONTINUED)**

In accordance with the Balanced Budget Act of 1997 (Public Law 105-33), as amended, the Lottery contributes 7.00% and employees contribute 7.25% of employees' covered compensation to the Federal Civil Service Retirement System. Contributions by the Lottery amounted to \$90 and \$85 for the years ended September 30, 2010 and 2009, respectively. The number of Lottery employees covered under the Federal Civil Service Retirement System for fiscal year ended September 30, 2010 and 2009 were 15 and 14, respectively.

**(b) Defined Contribution Plan**

All full-time employees hired after September 30, 1987 are covered by the District-sponsored defined contribution plan. Employees do not contribute to this plan and are eligible to participate after one year of service. The Lottery contributes 5% of an eligible employee's base salary, which amounted to \$273 and \$243 for the fiscal years ended September 30, 2010 and 2009, respectively.

Contributions and earnings vest fully after four years of service following a one-year waiting period. Contributions and earnings are forfeited if separation occurs before five years of credited service. These contributions are not considered assets of the Lottery or the District, which have no further liability to this plan.

**(c) Deferred Compensation Plan**

Lottery employees are eligible to participate in the District-sponsored deferred compensation plan (D.C. Code 47-3601) created in accordance with Internal Revenue Code Section 457. Employees may defer an amount equal to the lesser of 100% of includible compensation or \$16.5 in 2010. Maximum annual contribution amounts are determined and set by the Internal Revenue Service (IRS). Compensation deferred and income earned is taxable when paid or made available to the participant or beneficiary upon retirement, death, termination, or unforeseeable emergency. Contributions are not assets of the Lottery or District, which have no further liability to the plan.

**NOTE 10 COMMITMENTS AND CONTINGENCIES**

**(a) Operating Leases**

The Lottery leased certain facilities under a ten (10) year long-term, non-cancelable, operating lease which began May 8, 2008. Future minimum rental commitments are as follows:

	<b>Amount</b>
September 30, 2011	\$ 2,119
September 30, 2012	2,172
September 30, 2013	2,321
September 30, 2014	2,379
September 30, 2015	2,438
Thereafter	5,061
Minimum Rental Commitment	<b>\$ 16,490</b>

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
 LOTTERY AND CHARITABLE GAMES CONTROL BOARD  
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**NOTE 10 COMMITMENTS AND CONTINGENCIES (CONTINUED)**

Rent expense for the fiscal years ended September 30, 2010 and 2009 was as follows:

	<u>2010</u>	<u>2009</u>
Gross rental expense	\$ 2,269	\$ 2,299
Less income from subleases	<u>(170)</u>	<u>(170)</u>
Net rent expense	<u>\$ 2,099</u>	<u>\$ 2,129</u>

**(b) Risk of Loss**

The Lottery is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Lottery or District covers all of the Lottery's claim settlements and judgments out of the Lottery revenues or the District's General Fund resources.

**(c) Liquidation Damages**

The Lottery issued a claim against Lottery Technology Enterprises (LTE) and GTECH Corporation for contract failure and security breach. The claim stated that LTE and GTECH supplied the Lottery with an online gaming system and telecommunication system that were vulnerable to fraud and theft, and hired subcontractors who exploited that vulnerability and failed to heed warnings that the systems had been compromised. The claim against LTE and GTECH totaled \$1,443. LTE filed an action with the District's Contracts Appeal Board seeking a reduction in damages assessed. The parties disposed of this matter by entering into a settlement agreement on October 14, 2009 to extend the LTE contract through November 22, 2010 at a reduced percentage rate of net sales.

**NOTE 11 RELATED PARTY TRANSACTIONS**

During 2010, The Lottery had related party transactions with the Office of the Chief Financial Officer (OCFO) to provide financial and managerial oversight. These services included, but were not limited to, internal audit and internal security, legal, human resources, procurement, financial management, and executive management oversight services. The annual contractual cost for these services was \$1,124 in both fiscal years 2010 and 2009.

Other services provided by District Government entities to the Lottery include central processing of payroll, accounting, computer technology services, and the handling of intra-district transactions for rent, telephone, security guard services, etc. Personnel costs for these services are budgeted and accounted for as part of the respective entity's regular operations.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**LOTTERY AND CHARITABLE GAMES CONTROL BOARD**  
**NOTES TO FINANCIAL STATEMENTS**  
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*(Dollar Amounts in Thousands)*

**NOTE 12      LITIGATION**

The Lottery is a defendant in a lawsuit brought by a former employee, alleging retaliation on the basis of protected speech, failure to due process before termination, and intentional infliction of emotional distress. The District Court ruled in favor of the Lottery. The Plaintiff appealed the case to the U.S. Court of Appeals. The appellate court affirmed the dismissal of all counts except for the due process claim, which was remanded to the District Court. The Lottery intends to defend this litigation and cannot, at this time, reasonably predict the outcome of the proceedings or sanctions, if any, that will be imposed.

The Lottery is a defendant in a lawsuit alleging violations of the Americans with Disabilities Act, the Rehabilitation Act and the District of Columbia Human Rights Act. The Plaintiffs and the Lottery are currently involved in settlement discussions. If the lawsuit goes to trial, the Lottery plans to vigorously defend this litigation and cannot, at this time, reasonably predict the outcome of the proceedings or sanctions, if any, that will be imposed.

While the ultimate outcome of these lawsuits cannot be predicted at the time, it is the opinion of management and in-house counsel that the disposition of any litigation in which the Lottery is involved will not have a material adverse effect on the financial position, results of operations, or cash flows of the 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**

To the Mayor and Members of  
The Council of the Government of District of Columbia, and  
The Lottery and Charitable Games Control Board  
Washington, D.C.

We have audited the financial statements of the Lottery and Charitable Games Control Board (the Lottery); an enterprise fund of the Government of the District of Columbia (District), as of and for the year ended September 30, 2010, and have issued our report thereon dated January 24, 2011. 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.

**Internal Control over Financial Reporting**

In planning and performing our audit, we considered the Lottery's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Lottery's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Lottery's internal control over financial reporting.

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, as described in the accompanying schedule of findings and responses, we identified a deficiency in internal control over financial reporting that we consider to be a significant deficiency in internal control over financial reporting (2010-1). 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 in governance.

### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the 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 an instance of noncompliance that is required to be reported under *Government Auditing Standards* and which is described in the accompany schedule of findings and responses as item 2010-1. We noted no other matters that are required to be reported to management of the Lottery.

The Lottery's response to the finding identified in our audit is described in the accompanying schedule of findings and responses. We did not audit the Lottery's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Mayor, the Council, and the Inspector General of the Government of the District of Columbia and management of the Lottery and is not intended to be, and should not be used by anyone other than these specified parties.

Bert Smith & Co.

Washington, D.C.  
January 24, 2011

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
LOTTERY AND CHARITABLE GAMES CONTROL BOARD  
SCHEDULE OF AUDIT FINDINGS & RESPONSES**

**2010-1**

***Remittance of Federal and State Taxes related to Winning Ticket***

- Condition:** During our testwork of internal controls over prize disbursements, we noted one instance in which the taxes withheld were not remitted to the necessary federal and state agencies.
- Criteria:** The Lottery is required to withhold a deposit of 25% of each lottery winning (28% if the winner has no SSN), and must remit this amount to the IRS within three business days. The Lottery is also required to withhold 8.5% of each District lottery winning and must remit this amount to the District by the 20<sup>th</sup> of the following month. The Lottery's accounting officer remits taxes to the federal and state agencies based on their receipt of a Federal Tax/Tax Deposit Request Form, which is faxed from the Claims Center and subsequently approved.
- Cause:** On September 30, 2010, federal taxes were withheld from a lottery winner's claim in the sum of \$2,500. It appears that Claims Center personnel followed the established procedure of faxing over a Federal Tax/Tax Deposit Request Form. Unfortunately, the tax deposit request form with supporting documentation did not print and/or for unknown reasons did not reach the parties responsible for making and confirming the deposit.
- Effect:** The Lottery was not in compliance with the tax remittance requirements. Without a process in place to determine the reasonableness of taxes remitted such as a recalculation of taxes due at a summary level compared to taxes remitted, there is a possibility that withholdings may be overlooked and not properly remitted.
- Recommendation:** The Lottery should implement a process that will ensure missed remittances can be identified and subsequently detected.
- Management's Response:** We consider the finding an isolated incident since most deposits are made on a timely basis. However, the Lottery will implement the following additional procedures to ensure that all federal and District tax deposits are made on a timely basis.
- Follow-up weekly with Claims Center personnel to verify that all Tax Deposit Request Forms submitted for processing have been confirmed.
  - Maintain log of all tax withholdings showing claimant's name, date withheld, amount withheld, and date of tax deposit. Reconcile log with cash disbursements records and general ledger monthly to determine accuracy of withholding entries and deposits.