



## BUREAU OF STATE LOTTERY

An Enterprise Fund of the State of Michigan

# COMPREHENSIVE ANNUAL FINANCIAL REPORT

For the Fiscal Year Ended September 30, 2005

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Prepared by Accounting Department

Bureau of State Lottery, State of Michigan  
Comprehensive Annual Financial Report  
For the fiscal year ended September 30, 2005

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## **INTRODUCTORY SECTION**



JENNIFER M. GRANHOLM  
GOVERNOR

STATE OF MICHIGAN  
BUREAU OF STATE LOTTERY  
LANSING



GARY C. PETERS  
COMMISSIONER

December 5, 2005

To the Honorable Jennifer M. Granholm, Governor  
Members of the Legislature  
Citizens of the State of Michigan

We are pleased to present to you the Comprehensive Annual Financial Report (CAFR) of the Bureau of State Lottery (Lottery) for the fiscal years ending September 30, 2005 and 2004. Lottery management is responsible for the accuracy of the financial data and the completeness of the contents of this report.

The Lottery is an enterprise fund within the State of Michigan and its financial statements are included in the State's Comprehensive Annual Financial Report. This report presents only the activity of the Lottery as a single enterprise fund and is an overview of the Lottery's operations.

The mission statement of the Lottery is as follows:

- To maximize net revenues to supplement state education programs.
- To provide fun and entertaining games of chance.
- To operate all games and bureau functions with nothing less than total integrity.

Within the financial section of this CAFR, the Lottery's Management Discussion and Analysis (MD&A) provides a detailed narrative of activities that occurred over this time period. This letter of transmittal is intended to complement the MD&A and should be read in combination with the MD&A.

The report is organized into three sections. The Introductory Section includes this letter of transmittal and an organizational chart with principal officials. The Financial Section includes the independent auditors' report, management's discussion and analysis, audited financial statements with accompanying notes, supplementary information schedules and the auditors' report on compliance and internal control. Demographic, historical and industry comparative information are presented in the Statistical Section of this report.

## **History of the Lottery**

The Lottery was created in 1972 to generate funds to support Michigan's public school system. The first lottery tickets were the Green Ticket which went on sale on November 13, 1972. On October 7, 1975, the first instant game ticket was sold. On-line sales began June 6, 1977 with the introduction of the Daily 3 game. The first multi-state ticket sales for the Lottery were on August 31, 1996 for The Big Game (now called Mega Millions). Over the 32 years since the Lottery was created, a total of \$12.2 billion has been contributed to the School Aid Fund.

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## **Economic Condition and Outlook**

Michigan's economy continues to struggle. Michigan's employment forecasts show a decline in overall employment in 2005 and 2006. Although there is growth in many job sectors, the manufacturing sector continues to decline. Michigan's economy relies heavily on the performance of the manufacturing sector in general and the auto industry specifically. Even with job growth in other sectors, Michigan's unemployment rate is forecast to rise to 7.2% in 2005 and 7.4% in 2006, well above the national average forecast of 5.1%.

In addition, high unemployment, reductions in income, interest rate increases and the expected increases in gasoline and home heating costs cause further concern. These changes in the economy will impact personal disposable incomes and spending patterns and could impact Lottery sales.

## **Lottery Products**

The Lottery offers a variety of games in several styles of play, instant, also known as "scratch" games; on-line games, where daily or more frequent drawings are conducted to select winning numbers; and pull tab, played similar to instant where a perforated tab is pulled on the ticket. These games are made available to the playing public through more than 11,000 licensed Lottery retailers.



Instant Games

Instant games are played by scratching latex covering on each ticket to reveal prize symbols. A variety of games with different themes, play styles, price points and prize structures are available with an on-going product offering of over 70 new games a year. The games offered are priced between \$1 and \$20 and prizes range from \$1 to \$2 million.

## **On-line Games**

On-line game tickets are generated by a terminal connected to a central system and drawings are conducted to determine the winning numbers. Drawings are every five minutes, twice a day, daily or twice a week depending on the game. On-line games currently offered are Mega Millions, Classic Lotto 47, Fantasy 5, Daily 3, Daily 4, Keno and Club Keno and are played as follows:



### Mega Millions

Mega Millions is a multi-state on-line game, formerly known as The Big Game. Players select from two pools of numbers: five numbers between 1 and 56 and one number between 1 and 46 for a chance to win a multi-million dollar jackpot prize. The jackpot starts at \$12 million. This game offers nine ways to win with guaranteed prize amounts on lower tier prizes. Drawings are conducted twice a week. A total of 12 states participate in the Mega Millions game with Michigan including California, Georgia, Illinois, Maryland, Massachusetts, New Jersey, New York, Ohio, Texas, Virginia, and Washington.



### Classic Lotto 47

Classic Lotto 47 is an in-state Lotto game. It was introduced May 15, 2005 and replaced the Winfall game. Players select 6 of 47 numbers in twice a week drawings. Jackpots start at \$1 million. Classic Lotto 47 offers four ways to win, with guaranteed prize amounts at the lower prize levels.



### Fantasy 5

Fantasy 5 was introduced September 12, 2004, replacing the Rolldown game. Players pick 5 of 39 numbers with rolling jackpots starting at \$100,000, with daily drawings. Jackpots increase a minimum of \$5,000 per draw and roll until a player matches all five numbers in a drawing. This game offers four ways to win with guaranteed prize amounts at the lower prize levels.



and



### Daily 3 & 4 Games

The Daily 3 & 4 games are the Lottery's longest running and most consistently popular games, representing 34 percent of total sales. Drawings are conducted twice a day, seven days a week. These games offer a wide variety of winning combinations and fixed prizes. The top prize for Daily 3 is \$500; and for Daily 4, \$5,000.



Keno!

Keno! is another long-running game which started in 1990. Although the sales are less than 1 percent of total sales, it has a very strong and loyal player base. In this game, players chose 10 numbers from a pool of 80. The Lottery draws 22 numbers and if the player matches 10 of those 22 numbers, they win the jackpot prize of \$250,000. There are also five other ways to win by matching combinations of the numbers drawn. Drawings are conducted daily.



Club Games

Club Games were introduced in October 2003. Club Games are played by patrons of bars, restaurants and bowling centers, a new retailer base. Club Games consist of an on-line Club Keno game and Pull Tab games. To play Club Keno, players select up to 10 numbers from a pool of 80. The Lottery draws 20 numbers, the more numbers the player matches, the more they win. Results of the drawings, which are conducted every five minutes, are displayed on TV monitors located in the retailers' establishments. Club Keno can be played every day from 6:05 am to 1:45 am. Wagers can be placed from \$1 to \$20 and the top prize is \$2 million.

Pull Tab games are similar to instant tickets but players pull a perforated tab instead of scratching off the ticket. A variety of different Pull Tab games are offered at one time. Ticket prices are 50 cents, \$1 and \$2 and top prizes range from \$50 to \$500. Pull Tab winning tickets must be redeemed by the selling retailer.

## **Highlights of Fiscal Year 2005**

### **Record Contribution to the School Aid Fund**

The Lottery had yet another outstanding year in fiscal 2005 with a record \$667.6 million being transferred to the School Aid Fund. This marks the second consecutive year of record contributions to the School Aid Fund.

### **Sales**

Sales for 2005 surpassed \$2 billion for the first time in the history of the Lottery and were at a record high for the second consecutive year.

### **Retailers Win Big with Record Commissions**

Not only did the Lottery have record School Aid Fund transfers and sales in both 2004 and 2005, but retailer commissions were also at an all-time high in both years. Retailer commissions totaled \$152.7 million in 2005 and \$145.4 million in 2004.



### **Largest Single Ticket Mega Millions Winner in Michigan**

In April 2005 a single ticket purchased in Michigan won a total of \$208 million in the Mega Millions game. This was the largest single ticket winner in the history of Mega Millions.

### **Instant Game \$2 Million Dollar Drawings**

The Lottery conducted four separate instant game \$2 million grand prize drawings in November, March, June and September of fiscal 2005. Players are entered in the drawings automatically by winning \$1,000 in any \$20 game. The first two drawings were held at the Palace of Auburn Hills during halftime at Detroit Pistons games. The third drawing was held at the International Freedom Festival in Detroit. The final drawing was held at the Arts Beats and Eats Festival in Pontiac.

### **New Player City Internet Club**

In June the Lottery introduced a new Internet-based VIP club for players called Player City. Player City offers a variety of on-site activities in which players can participate. Points are earned for participation in surveys and other activities and these points are redeemable for entry into drawings for event tickets and other prizes. In addition, players who become members receive many benefits such as special prize drawings, exclusive offers only for Player City members, anniversary rewards redeemable for exclusive members-only rewards, and email alerts for jackpots and winning numbers. Membership in Player City is free.

## **Financial Information**

The sale of Lottery tickets provides all funding for operations and the net income is transferred to the School Aid Fund for K-12 education. The operations involve sale of tickets, determination of winning tickets, payment of prizes, compensation to retailers, and administrative functions. The Lottery also provides \$1 million a year to the Department of Community Health for gambling addiction programs. The Lottery's Commissioner is responsible to the Governor, Legislature and the citizens of the State for Lottery operations.

The Lottery's goals and objectives ensure there is an ongoing effort to achieve operational efficiencies to not only maximize revenues but maximize profits for the School Aid Fund. Operational results are included in the financial and statistical sections.

Charitable Gaming division activities net proceeds are dedicated to the State's General Fund. These activities are discussed in the MD&A.

## **Accounting Systems and Policies**

As an enterprise fund of the State of Michigan, the Lottery operates like a business within state government structure. The Lottery uses the accrual basis of accounting, following generally accepted accounting principles (GAAP) and governmental accounting standards board (GASB) pronouncements.

## **Budgetary System and Controls**

The Lottery works with the Department of Management and Budget, Office of the Budget and the Legislature to create an annual appropriated budget for the administrative costs for the Lottery. The proposed budget is approved by the Legislature annually. This approved budget becomes a spending cap for administrative expenses and ticket revenues provide funding for operations. Revenue and net income forecasts are prepared throughout the fiscal year comparing estimates and forecasts to actual sales and expenses. This information is provided to the Office of the Budget with appropriate action plans taken as needed.

## **Internal Controls**

The Michigan Lottery and the State of Michigan policies and procedures tightly control assets, inventory, computer systems, drawing studios and accounting. Separation of duties, internal controls, ongoing monitoring and evaluation of information as well as stringent employee, retailer and contractor standards all minimize risk of loss or theft. All employees, retailers and contractor employees must pass a security background check.

## **Debt Administration**

Long term liabilities for the Lottery are for payments owed to Lotto, Mega Millions and Instant Game grand prize installment winners. These prize liabilities are funded by investments in United States Government Zero Coupon Bonds which are held to maturity.

## **Cash Management**

Cash due from retailers for Lottery transactions is collected weekly by automated clearing house (ACH) electronic funds transfer. Monthly net income from Lottery operations is transferred to the School Aid Fund. Any excess cash is maintained in an account managed by the Michigan Department of Treasury. Any short term investing in the common cash fund is done by Treasury following its policies and guidelines.

## **Risk Management**

The Michigan Department of Management and Budget (DMB) controls risk management through two internal service funds administratively established during fiscal year 1989-1990. These funds are self-insured for most general liability, property losses, portions of employee insurance benefit, employee bonding programs, employee theft, workers compensation and unemployment compensation claims. The Lottery is assessed annual premiums by DMB for risk management.

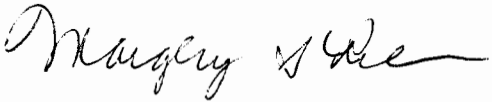
## **Independent Audit**

The enabling legislation of the Lottery requires biannual and special post audits of all accounts and transactions of the Lottery by the Auditor General or by an independent public accounting firm appointed by the Auditor General. The Auditor General has contracted with an independent public accounting firm for these audits. The financial statements have been 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.

## **Acknowledgements**

Preparation of this report would not be possible without the efficient and dedicated efforts of the Accounting Division of the Lottery. Their teamwork has greatly contributed to the success of this informative document.

Respectfully submitted,



Margery S. Reh  
Deputy Commissioner for Administration

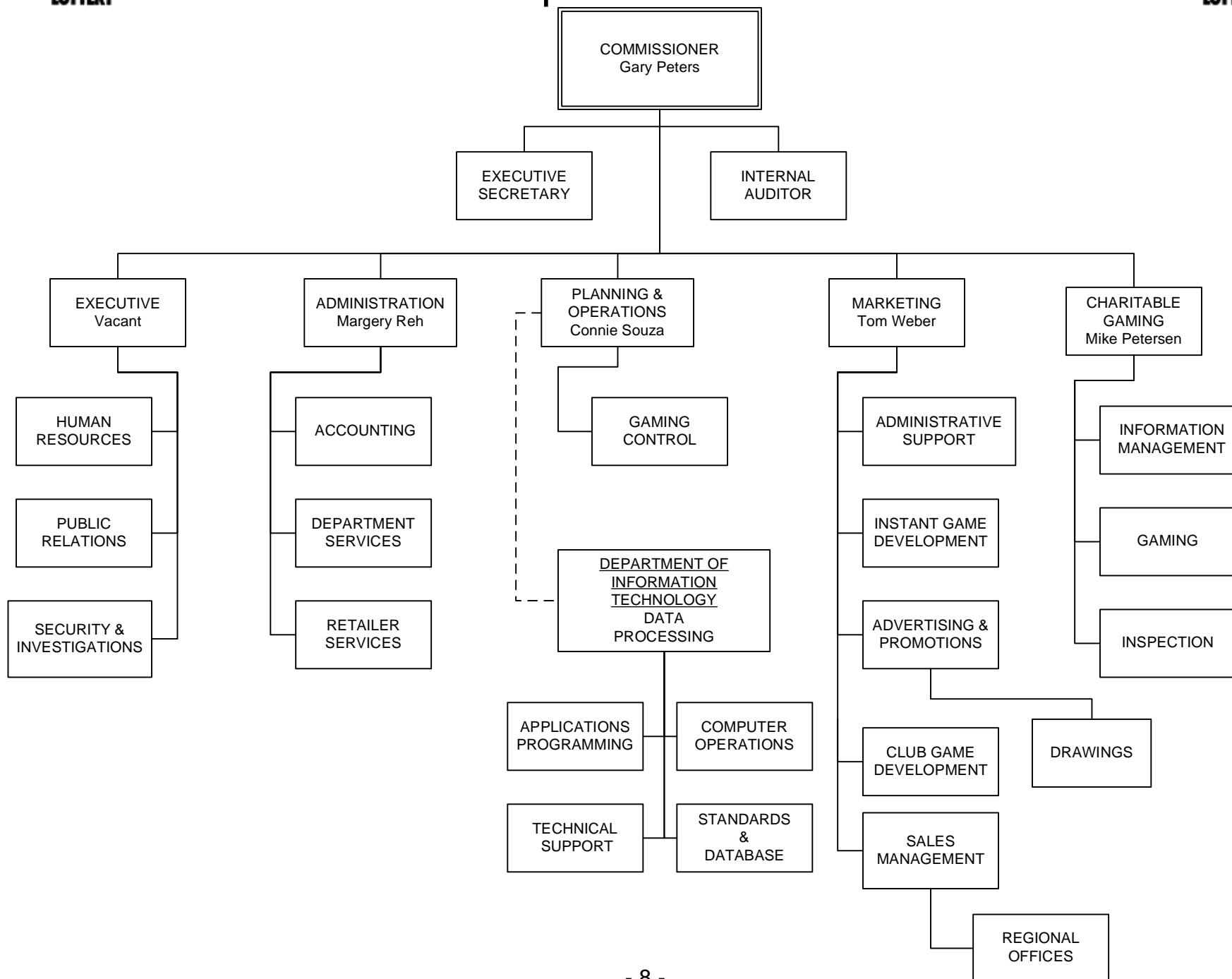


Gary Peters  
Commissioner



# BUREAU OF STATE LOTTERY

## September 2005



## **FINANCIAL SECTION**

## **Independent Auditors' Report**

Mr. Gary C. Peters, Commissioner  
Bureau of State Lottery, State of Michigan  
and  
Mr. Thomas H. McTavish, Auditor General  
State of Michigan

We have audited the accompanying financial statements of the Bureau of State Lottery, State of Michigan (the "Lottery"), a proprietary fund of the State of Michigan, as of and for the six month periods and years ended, September 30, 2005 and 2004, which collectively comprise the Lottery's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Lottery's management. Our responsibility is to express opinions 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 1, the financial statements present only the Bureau of State Lottery, State of Michigan, and are not intended to present the financial position of the State of Michigan and the results of its operations and cash flows of its proprietary fund types 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 Lottery, as of September 30, 2005 and 2004, and the changes in its net assets and its cash flows for the six month periods and years 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 November 18, 2005, on our consideration of the Lottery's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, not to provide an opinion on 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 conjunction with this report in considering the results of our audit.

The management's discussion and analysis presented on pages 11 through 20 is not a required part of the basic financial statements but is supplementary information required by 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 required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Lottery's basic financial statements. The accompanying supplementary schedules, as listed in the foregoing table of contents, are presented for the purpose of additional analysis and are not a required part of the basic financial statements. The supplementary schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements, and in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

*Yeo & Yeo, P.C.*

Lansing, Michigan  
November 18, 2005

## **Management's Discussion and Analysis**

The following discussion of the Michigan Bureau of State Lottery's (the Lottery) financial performance provides an overview of the Lottery's financial activities for the fiscal year ended September 30, 2005. Please read it in conjunction with the financial statements, which begin on page 21.

### **Using this Report**

The Lottery is accounted for as an enterprise activity/proprietary fund, reporting on all of the activity's assets and liabilities using the accrual basis of accounting much like a private business entity. As such, this semi-annual report consists of a series of financial statements, along with explanatory notes to the financial statements and supplementary schedules. The Statement of Net Assets on page 21 and the Statement of Revenues, Expenses and Changes in Fund Net Assets on page 22, report the Lottery's net assets and changes in them.

By law, the Lottery is required to transfer all of its net income each fiscal year to either the State School Aid Fund (for income related to lottery gaming activities) or the General Fund (for income related to charitable gaming activities). As a result, the net assets of the Lottery consist largely of capital assets (leasehold improvements and equipment) and restricted income related to unrealized gain on investments held to fund future payments due on lottery prizes that are annuities. To assess the Lottery's financial position and financial health, the reader of these statements should pay particular attention to changes in the components of assets and liabilities as set forth in the Statement of Net Assets, and in changes in operating revenues, expenses, and transfers to other funds as set forth in the Statement of Revenues, Expenses, and Changes in Fund Net Assets. In addition the reader should also refer to the accompanying notes to the financial statements.

### **Financial Highlights 2004 to 2005**

- Gross revenues for lottery gaming activities set a record for the second consecutive year and surpassed the \$2 billion mark for the first time in the Lottery's history. These revenues increased by \$94.8 million, or 4.8%.
- Total revenues for all activities (including non-operating) increased \$96.8 million or 4.8%.
- Net non-operating expenses decreased by \$5.3 million. There was an unrealized loss of \$24.6 million in 2005, and an unrealized loss of \$28.1 million in 2004. Therefore, the decrease in net non-operating expenses is attributable to a smaller reduction of the fair market valuation of investments from 2004 to 2005. These investments are held to fund future payments that are due to annuity prizes winners.
- Total operating expenses for 2005 increased \$74.5 million, or 5.6%. Of this increase, prize awards (net of unclaimed prizes) related to operating revenues from gaming activities increased by \$62.3 million, or 5.7%, agent and vendor commissions increased \$8.9 million, or 4.9%, while other operating expenses increased by \$2.1 million, or 5.1%.
- Total expenses (including non-operating) for all activities increased \$71.3 million or 5.2%.



- Back-to-back record setting transfers were made to the School Aid Fund in fiscal year 2004 and 2005. Transfers to the School Aid Fund were \$644.8 million in 2004 and \$667.6 million in 2005. Net income before transfers increased by \$25.7 million, or 4.1%. Net income transferred to the General Fund related to Charitable Gaming activities decreased by \$.5 million or 4.1%.

## Net Assets

A summary of the Lottery's net assets is presented below:

Table 1 - Net Assets  
(in millions)

	September 30,		
	2005	2004	2003
Current and other assets	\$ 567.7	\$ 471.6	\$ 491.5
Investments	420.9	496.8	588.2
Capital assets (net of accumulated depreciation)	0.5	0.5	0.6
Total assets	<u>989.1</u>	<u>968.9</u>	<u>1,080.3</u>
Current liabilities	562.8	459.8	482.8
Long-term liabilities	373.9	432.0	492.3
Total liabilities	<u>936.7</u>	<u>891.8</u>	<u>975.1</u>
Net assets			
Invested in capital assets	0.5	0.5	0.6
Restricted for unrealized gains on investments	52.4	77.1	105.2
Unrestricted (deficit)	(0.5)	(0.5)	(0.6)
Total net assets	<u>\$ 52.4</u>	<u>\$ 77.1</u>	<u>\$ 105.2</u>

As shown in Table 1 above, the Lottery's net assets decreased from \$105.2 million in September 2003 to \$52.4 million in September 2005. The steady decrease is attributable to the decrease in holdings as well as a decrease in market value of investments the Lottery holds to fund future payments due on annuitized lottery prizes. Capital assets consist of equipment and leasehold improvements.

Accounting principles dictate that the Lottery record in the financial records, the gain or loss related to the change in market value of these investments. Zero-coupon U.S. government bonds have been purchased for the payment of installment prize awards and are generally held to maturity. Therefore, the difference between the market value of these investments and the amortized book value is recorded as a restriction for unrealized gains on investments. The unrealized gain on investments is not available for transfer to the School Aid Fund.

A detail of the Lottery's liabilities is presented in Table 2 below:

Table 2 - Liabilities  
(in millions)

	September 30,		
	2005	2004	2003
Current:			
Prize awards payable (net of discount)	\$ 131.7	\$ 135.7	\$ 142.0
Obligation for security lending	409.2	301.9	306.1
Warrants authorized and warrants outstanding	8.1	9.4	6.9
Accounts payable and other liabilities	3.2	2.9	2.7
Due to School Aid Fund	10.6	9.9	25.0
Total current	<u>562.8</u>	<u>459.8</u>	<u>482.7</u>
Long-term:			
Prize awards payable (net of discount)	371.9	430.2	490.9
Compensated absences	2.0	1.8	1.4
Total long-term	<u>373.9</u>	<u>432.0</u>	<u>492.3</u>
Total liabilities	<u>\$ 936.7</u>	<u>\$ 891.8</u>	<u>\$ 975.0</u>

Current liabilities in 2005 include an adjustment of \$13.2 million in increased prize liability. This adjustment is also reflected in a decrease in unclaimed prize revenue. The adjustment is a change in estimate and is the result of improved information technology which provided the resources necessary for the lottery to reconcile the general ledger prize liability with the actual gaming system prize liability. This reconciliation provides additional assurance of the accuracy of the financial statements and adjusts prize liability balances carried forward in the general ledger since the inception of the Lottery. Refer to note 1 in the accompanying financial statements for more information.

Long-term liabilities consist principally of prize liability for prizes paid in installments over several years. Long-term prize liability decreased by \$58.3 million from 2004 to 2005 and decreased \$119 million from 2003 to 2005. The decrease is attributable to the maturing of some long term prize liabilities as well as minimal additions to the pool of annuitized installment prizes in all three years. Most prize winners eligible for annuity payments chose to have their payment in a lump sum rather than paid in installments. Refer to note 6 in the accompanying financial statements for more information.

Security lending liability is identical to and directly related to security lending collateral listed in current assets. These represent short-term lending of the Lottery's securities managed by the Department of Treasury. The amount due other state agencies has increased slightly from 2004 to 2005 and represents a timing issue of cash available at the end of the fiscal year.

A summary of the Lottery's change in net assets is presented in Table 3 below:

Table 3 - Changes in Net Assets  
(in millions)

	September 30,		
	2005	2004	2003
Operating revenues	\$ 2,090.1	\$ 1,995.3	\$ 1,701.8
Operating expenses:			
Prizes and direct game expenses			
Prizes less unclaimed prize/adjustments	1,162.0	1,099.7	899.7
Commissions and game related expenses	209.5	199.5	166.9
Total prizes and direct game expenses	1,371.5	1,299.2	1,066.6
Income before other operating expenses	718.6	696.1	635.2
Other operating expenses	43.4	41.3	40.3
Operating income	675.2	654.8	594.9
Non-operating revenues (expenses)	(19.6)	(24.9)	(19.6)
Income before transfers out	655.6	629.9	575.3
Transfers out			
Transfer to School Aid Fund	667.6	644.8	586.0
Transfer to General Fund	11.7	12.2	11.2
Transfer to Community Health	1.0	1.0	1.0
Total transfers out	680.3	658.0	598.2
Change in net assets	(24.7)	(28.1)	(22.9)
Total net assets beginning of period	77.1	105.2	128.1
Total net assets end of period	\$ 52.4	\$ 77.1	\$ 105.2

Because the Lottery is required by law to transfer all of its net income (excluding the unrealized gain or loss on investments discussed above) to the School Aid Fund or General Fund, change in net assets does not reflect the result of the Lottery's operating activities. The \$667.6 million transferred to the School Aid Fund reflects the Lottery's operating activities for the fiscal year 2005. Both 2004 and 2005 fiscal years were record years for the Lottery's transfers to the School Aid Fund, with an increase of \$22.8 million or 3.5% from 2004 and an increase of \$81.6 million or 13.9% over 2003. The transfer to the General Fund reflects Charitable Gaming activities. Charitable Gaming activities experienced a slight decline in net revenue and the 2005 transfer is a slight decrease from 2004. Charitable Gaming net income is transferred annually to the General Fund.

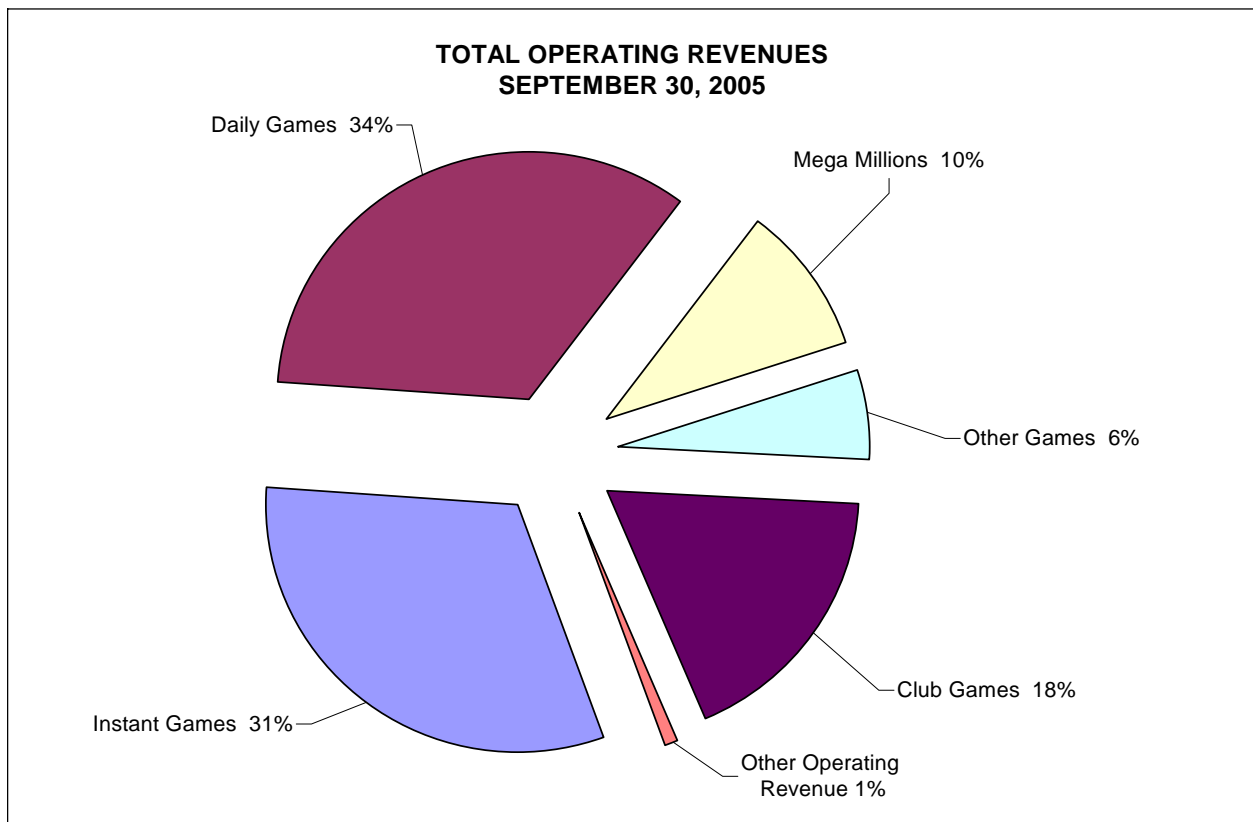
Transfers are detailed in Table 4 below:

**Table 4 - Transfers**  
(in millions)

	September 30,		
	2005	2004	2003
Transfer to School Aid Fund	\$ 667.6	\$ 644.8	\$ 586.0
Transfer to General Fund	11.7	12.2	11.2
Transfer to Community Health	1.0	1.0	1.0
Total Transfers	<u>\$ 680.3</u>	<u>\$ 658.0</u>	<u>\$ 598.2</u>

## Revenues

The following chart shows the major sources and the percentages of revenues for the fiscal year ended September 30, 2005:



A detail of the Lottery's revenues is presented in Table 5 below:

Table 5 - Revenues  
(in millions)

	September 30,		
	2005	2004	2003
Operating revenues			
Instant tickets	\$ 662.5	\$ 690.2	\$ 682.7
Daily games	712.6	733.4	720.5
Mega Millions	203.9	206.6	147.5
Club games	371.4	229.6	-
Other games	119.1	114.1	130.8
Other operating revenue	20.6	21.4	20.3
Total operating revenues	<u>2,090.1</u>	<u>1,995.3</u>	<u>1,701.8</u>
Non-operating revenues:			
Unrealized (loss) on investments	(24.6)	(28.1)	(22.9)
Amortization on bonds	35.9	41.1	46.1
Other income	9.4	5.7	4.6
Total non-operating revenue	<u>20.7</u>	<u>18.7</u>	<u>27.8</u>
Total revenues	<u>\$ 2,110.8</u>	<u>\$ 2,014.0</u>	<u>\$ 1,729.6</u>

Operating revenues for the fiscal year 2005, primarily Lottery ticket sales, increased overall from both 2003 and 2004. The overall sales increase in fiscal year 2005 over 2004 was by \$94.8 million or 4.8%. Classic Lotto 47 replaced Winfall and was introduced in May 2005. New on-line games are introduced periodically to keep player interest and maintain sales.

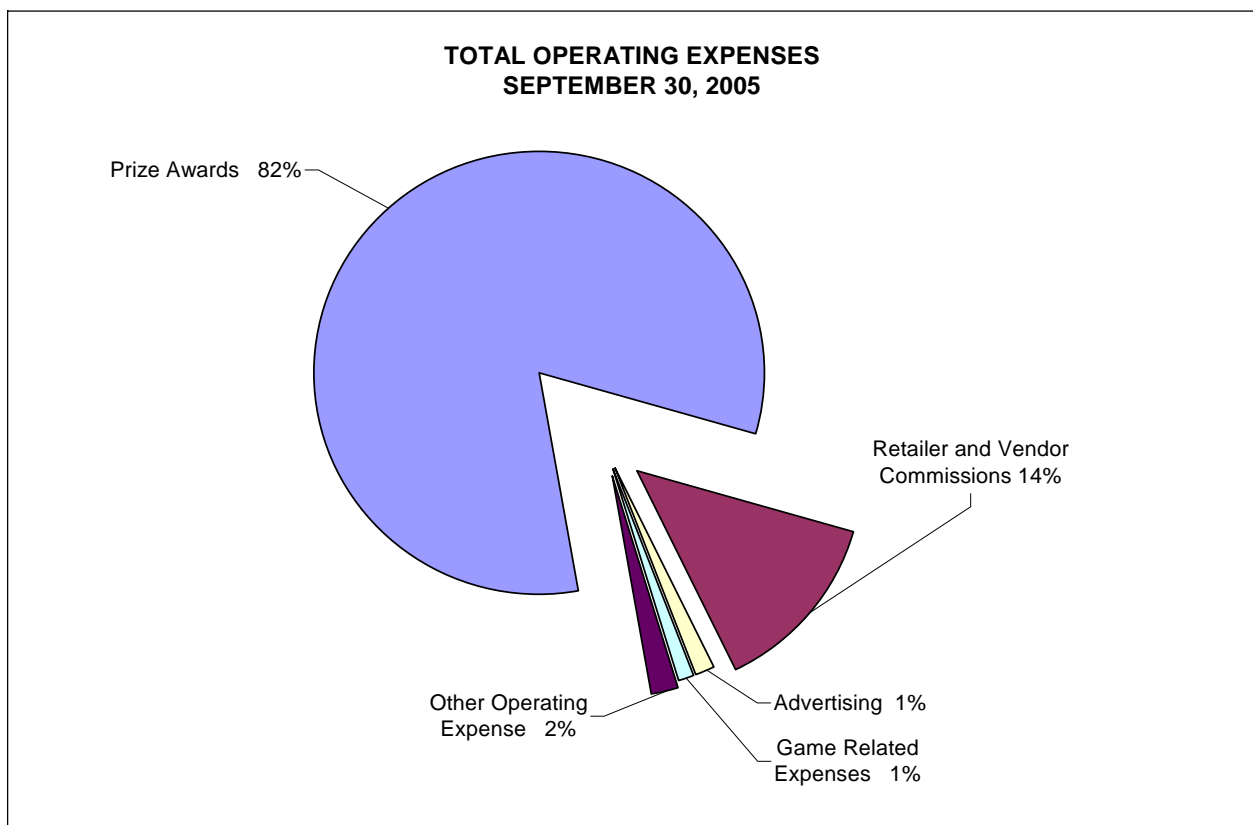
Mega Millions sales remain strong although there was a slight decrease in sales from 2004 to 2005. The sales for this game are very dependent on large jackpot rolls (i.e. greater than \$100 million). Mega Millions, which is a multi-state lotto game, had a 1.3% decrease in sales. This slight decrease is due to fewer large jackpot rolls in 2005 over 2004. Sales in 2005 were \$56.4 million more than in 2003. The states participating in Mega Millions with Michigan are California, Georgia, Illinois, Maryland, Massachusetts, New Jersey, New York, Ohio, Texas, Virginia and Washington. California joined the Mega Millions group in June 2005. With the addition of California more frequent large jackpot rolls are anticipated.

Club games experienced solid growth due to strong per terminal sales as well as continued retailer expansion into this market. Sales increased in 2005 \$141.8 million or 61.8% over 2004. Club games were introduced October 27, 2003. Currently there are approximately 2,077 active Club game retailers. Club games are primarily sold in bars and restaurants licensed for on premise alcohol consumption. Recruitment is ongoing with a goal for fiscal 2006 of 2,350 total Club games retailers.

The increase in non-operating revenues from 2004 to 2005 resulted from a smaller unrealized loss on investments. As previously discussed, the unrealized loss on investments is a reflection of the market value of the investments and does not impact the transfer to the School Aid Fund. The reduction in bond amortization is due to a decreasing bond portfolio from maturing investments as well as the fact that prize winners have elected the cash option, instead of installment payments. Other income increased from 2004 to 2005 due to higher interest rates which resulted in greater interest on common cash and also because of increased security lending revenue.

## Expenses

The following chart shows prizes, games costs and other operating expenses as a percentage of total operating expenses for the fiscal year ended September 30, 2005:



A detail of the Lottery's expenditures is presented in Table 6 below:

Table 6 - Expenses  
(in millions)

	September 30,		
	2005	2004	2003
Prizes:			
Instant prizes	\$ 417.8	\$ 435.6	\$ 428.2
Online prizes	519.5	543.6	491.0
Club game prizes	242.3	151.6	-
Total prizes	1,179.6	1,130.8	919.2
Less: unclaimed prizes/adjustments	17.6	31.1	19.6
Net prize awards	1,162.0	1,099.7	899.6
Direct game expenses:			
Retailer commissions	152.7	145.4	121.8
Vendor commissions	38.5	36.9	29.5
Game related expenses	18.4	17.2	15.7
Total direct game expenses	209.6	199.5	167.0
Other operating expenses:			
Salaries, wages and benefits	13.0	11.3	10.6
Other professional services	5.3	5.1	5.1
Printing and supplies	2.3	2.5	2.7
Other general and administrative	5.1	4.8	4.5
Advertising	17.6	17.5	17.4
Total other operating expenses	43.3	41.2	40.3
Total operating expenses	1,414.9	1,340.4	1,106.9
Non-operating expenses:			
Security lending expenses	6.0	4.3	3.3
Amortization of prize discount	34.3	39.2	44.1
Total non-operating expenses	40.3	43.5	47.4
Total expenses	\$ 1,455.2	\$ 1,383.9	\$ 1,154.3

The Daily games prize payout decreased overall in 2005 compared to 2004. Daily 3 prize payout was 47.2% in 2005, compared to 50.4% in 2004. Daily 4 prize payout was 51.9% in 2005, compared to 53.3% in 2004.

The Club Games prize payout percentage for 2005 of 65.2% was slightly lower than the 2004 pay out of 66.2%. The higher Club Games payout is an important part of the appeal of this latest style of game in this new market. The other on-line games have a 50%-55% anticipated payout.

Instant games had an overall payout of 63.1% in 2005, 63.2% in 2004 and 62.8% in 2003. The games vary in payout percentage depending on selling price of a ticket for a game. Instant game prize payouts range from 50% for a \$1 game to 70% for a \$20 game. The decrease in instant game prize expense from 2004 to 2005 of 4.1% is directly related to the 4% reduction in instant game sales.

Retailer, vendor commissions and game related expenses have increased commensurate with higher overall on-line sales.

Salaries, wages and benefits increased from 2004 to 2005 due to a 4% salary increase for employees effective October 1, 2004 as well as temporary suspension from October through December 2004 of the banked leave program which was in effect for the entire 2003-2004 fiscal year. The four hours in banked leave can be used as leave time or paid into an employee's 401K plan at employment termination. Under the banked leave program employees work 80 hours each bi-weekly pay period but are paid for 76 hours.

### **Unclaimed Prizes**

By law, lottery prizes not claimed within one year of their drawing date are to be transferred to the State School Aid Fund.

The Lottery recognizes the value of unclaimed prizes using an allowance methodology. Under the method, historical averages are utilized to estimate the amount of prizes awarded during the current year that will not be paid out due to claims not being filed for those prizes. The amounts estimated under the allowance method are recorded as a reduction of current year prize expense to match true prize expense to related sales.

Unclaimed prizes and adjustments decreased by \$13.5 million from 2004 to 2005. Of the decrease \$13.2 million is due to the liability estimate adjustment, as previously discussed. Again, this is a one-time adjustment that reflects activity since the inception of the lottery.

### **Charitable Gaming**

Table 7 - Charitable Gaming Revenue, Expense, and Net Income  
(in millions)

	September 30,		
	2005	2004	2003
Gross revenue	\$ 19.6	\$ 20.0	\$ 19.2
Operating expenses	7.9	7.8	7.9
Net income	<u>\$ 11.7</u>	<u>\$ 12.2</u>	<u>\$ 11.3</u>



Charitable gaming activities overseen by the Lottery include the licensing and regulation of charitable and certain other not-for-profit organizations that conduct bingo games, millionaire parties, and raffles for fund-raising purposes. The Lottery also oversees the distribution and sale of break-open tickets to these same organizations, also for fund-raising purposes. The mission of the Lottery with respect to charitable gaming activities is to ensure that only qualified organizations are licensed to conduct fund-raising activities, and that said activities are conducted in accordance with existing laws, rules and regulations. Revenues received through the issuance of licenses and from the distribution of break-open tickets are intended to cover the costs of overseeing the program activities, and are not intended as a primary goal to generate revenue for the State. Any revenue in excess of program costs is transferred annually to the State's General Fund.

### **Other Potentially Significant Factors Impacting Next Year**

The Lottery had a record sales year in 2004 and again in 2005 due to the large success of Club Games as well as strong Mega Millions sales. Management anticipates continued growth of the Club Games as the retailer base continues to expand. Management is also anticipating more large jackpots with the addition of California to the Mega Millions game which should equate to growth in Mega Millions sales in 2006. In November of 2004, a proposal limiting gambling expansion in the state was passed by a vote of the people. This proposal amended the constitution requiring a vote of the people for any future expansion of gambling. The language in the proposal was very broad and has the potential to negatively impact the Lottery's ability to generate revenue in the form of new games. This creates uncertainty in the continued growth of lottery revenues.

### **Contacting the Lottery's Financial Management**

This financial report is designed to provide the legislature and the executive branch of government, the public, and other interested parties with an overview of the financial results of the Lottery's activities, and to show the Lottery's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Deputy Commissioner for Administration at the Michigan Lottery, P.O. Box 30023, Lansing, Michigan, 48909.

**Bureau of State Lottery, State of Michigan**  
**Statement of Net Assets**  
**September 30, 2005 and 2004**

	2005	2004
<b>Assets</b>		
Current assets		
Equity in State Treasurer's Common Cash Fund	\$ 6,201,864	\$ 6,738,077
Investments, at fair value	93,378,340	103,861,541
Security lending collateral	409,169,719	301,949,675
Receivables from retailers - net	55,584,934	55,332,391
Inventory	3,358,586	3,752,075
Other current assets	29,779	9,820
Total current assets	<u>567,723,222</u>	<u>471,643,579</u>
Noncurrent assets		
Investments, at fair value	420,884,559	496,824,201
Capital assets		
Leasehold improvements and equipment	4,018,994	4,111,967
Accumulated depreciation	<u>(3,475,300)</u>	<u>(3,599,132)</u>
Total capital assets	<u>543,694</u>	<u>512,835</u>
Total noncurrent assets	<u>421,428,253</u>	<u>497,337,036</u>
Total assets	<u>989,151,475</u>	<u>968,980,615</u>
<b>Liabilities</b>		
Current liabilities		
Warrants outstanding	790,299	1,756,671
Warrants authorized	7,351,788	7,686,787
Accounts payable and other liabilities	3,234,779	2,866,006
Due to School Aid Fund	10,579,438	9,882,841
Obligations under security lending	409,169,719	301,949,675
Prize awards payable - net of discount	<u>131,682,198</u>	<u>135,696,751</u>
Total current liabilities	<u>562,808,221</u>	<u>459,838,731</u>
Noncurrent liabilities		
Prize awards payable - net of discount	371,916,697	430,228,031
Accrual for compensated absences	<u>1,975,191</u>	<u>1,816,321</u>
Total noncurrent liabilities	<u>373,891,888</u>	<u>432,044,352</u>
Total liabilities	<u>936,700,109</u>	<u>891,883,083</u>
<b>Net assets</b>		
Invested in capital assets	543,694	512,835
Restricted for unrealized gains on investments	52,451,366	77,097,532
Unrestricted (deficit)	<u>(543,694)</u>	<u>(512,835)</u>
Total net assets	<u>\$ 52,451,366</u>	<u>\$ 77,097,532</u>

See Accompanying Notes to Financial Statements

**Bureau of State Lottery, State of Michigan**  
**Statement of Revenues, Expenses and Changes in Fund Net Assets**  
**For the Six Months and Years Ended September 30, 2005 and 2004**

	Six Months Ended		Years Ended	
	2005	2004	2005	2004
<b>Operating revenues</b>				
Ticket sales	\$ 1,031,146,502	\$ 998,597,234	\$ 2,069,493,348	\$ 1,973,900,234
Charitable gaming and other	10,108,683	10,822,591	20,638,899	21,410,947
Total operating revenues	1,041,255,185	1,009,419,825	2,090,132,247	1,995,311,181
<b>Operating expenses</b>				
Prize awards	580,474,986	589,439,479	1,179,642,069	1,130,843,804
Less - unclaimed prizes	(17,516,337)	(15,303,088)	(17,634,462)	(31,171,242)
Net prize awards	562,958,649	574,136,391	1,162,007,607	1,099,672,562
Agent and vendor commissions	94,801,190	92,548,856	191,174,540	182,304,941
Game related expenses	8,933,753	8,651,187	18,369,818	17,207,801
Depreciation expense	67,575	75,042	136,651	149,416
Other operating expenses	20,484,214	19,866,495	43,233,420	41,102,852
Total operating expenses	687,245,381	695,277,971	1,414,922,036	1,340,437,572
<b>Operating income</b>	354,009,804	314,141,854	675,210,211	654,873,609
<b>Non-operating revenues (expenses)</b>				
Investment revenue	12,898,794	(1,091,154)	11,803,031	13,029,258
Interest on equity in State Treasurer's Common Cash Fund	1,723,699	616,259	2,540,807	959,770
Revenue from security lending	3,628,907	2,629,169	6,363,685	4,704,821
Security lending expenses	(3,446,371)	(2,471,743)	(6,013,676)	(4,347,073)
Amortization of prize award obligation discount	(16,512,669)	(19,008,946)	(34,251,841)	(39,223,183)
Total non-operating revenues (expenses)	(1,707,640)	(19,326,415)	(19,557,994)	(24,876,407)
<b>Income before transfers out</b>	352,302,164	294,815,439	655,652,217	629,997,202
<b>Transfers out</b>				
Transfer to School Aid Fund	(351,201,017)	(308,900,496)	(667,579,438)	(644,882,842)
Transfer to General Fund	(5,530,674)	(6,260,256)	(11,728,945)	(12,203,298)
Transfer to Community Health	(495,000)	(495,000)	(990,000)	(990,000)
Total transfers out	(357,226,691)	(315,655,752)	(680,298,383)	(658,076,140)
<b>Change in net assets</b>	(4,924,527)	(20,840,313)	(24,646,166)	(28,078,938)
<b>Total net assets at beginning of period</b>	57,375,893	97,937,845	77,097,532	105,176,470
<b>Total net assets at end of period</b>	\$ 52,451,366	\$ 77,097,532	\$ 52,451,366	\$ 77,097,532

See Accompanying Notes to Financial Statements

**Bureau of State Lottery, State of Michigan**  
**Statement of Cash Flows**  
**For the Six Months and Years Ended September 30, 2005 and 2004**

	Six Months Ended		Years Ended	
	2005	2004	2005	2004
<b>Cash Flows From Operating Activities</b>				
Cash collections from customers	\$ 1,041,573,345	\$ 1,007,617,250	\$ 2,089,744,974	\$ 2,008,217,935
Payments to employees	(6,192,515)	(5,418,831)	(12,522,503)	(10,977,867)
Payments to suppliers	(28,151,484)	(25,996,438)	(48,359,870)	(46,409,186)
Payments to prize winners	(621,463,859)	(620,774,361)	(1,258,585,335)	(1,205,945,290)
Payments for retailer commissions	(94,801,190)	(92,548,856)	(191,174,540)	(182,304,941)
Net cash provided by operating activities	290,964,297	262,878,764	579,102,726	562,580,651
<b>Cash Flows From Noncapital Financing Activities</b>				
Transfer to other funds	(414,718,946)	(383,193,299)	(679,601,787)	(673,240,929)
<b>Cash Flows From Capital and Related Financing Activities</b>				
Acquisition and construction of capital assets	(167,510)	(81,606)	(167,510)	(81,606)
<b>Cash Flows From Investing Activities</b>				
Proceeds from the sale and maturity of investment securities	171,025,936	54,418,000	222,098,936	108,890,000
Purchase of investments	(116,773,232)	-	(123,873,062)	-
Interest received	2,245,336	805,234	2,540,807	959,770
Security lending proceeds	3,630,822	2,656,624	6,343,725	4,722,956
Security lending payments	(3,446,371)	(2,471,743)	(6,013,676)	(4,347,073)
Net cash provided by investing activities	56,682,491	55,408,115	101,096,730	110,225,653
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>(67,239,668)</b>	<b>(64,988,026)</b>	<b>430,159</b>	<b>(516,231)</b>
<b>Cash and cash equivalents at beginning of period</b>	<b>72,651,233</b>	<b>69,969,432</b>	<b>4,981,406</b>	<b>5,497,637</b>
<b>Cash and cash equivalents at end of period</b>	<b>\$ 5,411,565</b>	<b>\$ 4,981,406</b>	<b>\$ 5,411,565</b>	<b>\$ 4,981,406</b>

**Bureau of State Lottery, State of Michigan**  
**Statement of Cash Flows**  
**For the Six Months and Years Ended September 30, 2005 and 2004**

	Six Months Ended		Years Ended	
	2005	2004	2005	2004
<b>Reconciliation of net operating income to net cash provided by operating activities</b>				
Operating income	\$ 354,009,804	\$ 314,141,854	\$ 675,210,211	\$ 654,873,609
Adjustments to reconcile operating income to net cash provided by operating activities				
Depreciation expense	67,575	75,042	136,651	149,416
Bad debt expense	54,389	73,149	134,729	130,725
Amortization of prize award obligation discount	(16,512,669)	(19,008,946)	(34,251,841)	(39,223,183)
Net changes in assets and liabilities:				
Inventory	1,641,416	(635,673)	393,488	(1,585,173)
Receivables from retailers	318,160	(1,802,575)	(387,272)	12,906,755
Warrants authorized, compensated absences, accounts payable, other liabilities	(6,621,837)	(2,335,064)	192,647	2,378,047
Prize awards payable	(41,992,541)	(27,629,023)	(62,325,887)	(67,049,545)
<b>Net cash provided by operating activities</b>	<b>\$ 290,964,297</b>	<b>\$ 262,878,764</b>	<b>\$ 579,102,726</b>	<b>\$ 562,580,651</b>
<b>Reconciliation of cash and cash equivalents</b>				
Cash at beginning of period				
Equity in State Treasurer's Common Cash Fund	\$ 74,232,824	\$ 71,747,185	\$ 6,738,077	\$ 6,494,160
Warrants outstanding	(1,581,591)	(1,777,753)	(1,756,671)	(996,523)
<b>Net cash and cash equivalents at beginning of period</b>	<b>\$ 72,651,233</b>	<b>\$ 69,969,432</b>	<b>\$ 4,981,406</b>	<b>\$ 5,497,637</b>
Cash at end of period				
Equity in State Treasurer's Common Cash Fund	\$ 6,201,864	\$ 6,738,077	\$ 6,201,864	\$ 6,738,077
Warrants outstanding	(790,299)	(1,756,671)	(790,299)	(1,756,671)
<b>Net cash and cash equivalents at end of period</b>	<b>\$ 5,411,565</b>	<b>\$ 4,981,406</b>	<b>\$ 5,411,565</b>	<b>\$ 4,981,406</b>
<b>Schedule of noncash investing, capital, and financing activities</b>				
Decrease in fair value of investments	\$ (4,924,527)	\$ (20,840,313)	\$ (24,646,166)	\$ (28,078,938)
Transfers to other funds (accrual)	(10,579,438)	(9,882,841)	(10,579,438)	(9,882,841)
<b>Total noncash investing, capital, and financing activities</b>	<b>\$ (15,503,965)</b>	<b>\$ (30,723,154)</b>	<b>\$ (35,225,604)</b>	<b>\$ (37,961,779)</b>

Concluded  
See Accompanying Notes to Financial Statements

## **Bureau of State Lottery, State of Michigan**

### **Notes to Financial Statements**

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#### **NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

##### **REPORTING ENTITY**

The Bureau of State Lottery (the "Lottery") was established by Public Act No. 239, Public Acts of 1972, as amended.

Public Act 95 of 1996 allows the Lottery to participate in joint enterprises with other sovereignties, such as multi-state lotteries. Michigan participates in Mega Millions, a jointly operated multi-state lottery comprised of twelve states: California, Georgia, Illinois, Maryland, Massachusetts, Michigan, New Jersey, New York, Ohio, Texas, Virginia, and Washington. Net income from Mega Millions is transferred to the School Aid Fund.

##### **BASIS OF PRESENTATION**

The Lottery is classified as an enterprise fund of the State of Michigan. Accordingly, the Lottery's financial statements are included in the State's Comprehensive Annual Financial Report. The accompanying financial statements are not intended to present the financial position and results of operations of the State of Michigan or its enterprise funds.

##### **BASIS OF ACCOUNTING**

The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. The Lottery distinguishes operating revenue and expenses from non-operating items. The principal operating revenue of the Lottery is primarily comprised of sales from instant and on-line tickets. Operating expenses mainly consist of payments to instant and on-line prize winners and commissions to retailer agents and vendors. Excess revenue over expenses is designated for payment to the State School Aid Fund, except for the excess of revenue over expenses from charitable gaming activities, which is designated for payment to the State General Fund. All other revenues and expenses are reported as non-operating.

In accordance with Governmental Accounting Standards Board Statement 20, the Lottery has elected not to apply Financial Accounting Standards Board statements and interpretations issued after November 30, 1989, to its financial statements.

##### **STATEMENT OF CASH FLOWS**

For the purposes of the statement of cash flows, the Lottery considers equity in the State Treasurer's Common Cash pool net of warrants outstanding to be cash equivalents.

##### **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 and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. During the year ended September 30, 2005, the Lottery improved its methods of estimating current prize liability for instant and on-line games. The net effect was an additional prize expense of \$ 13,212,140.

## **Bureau of State Lottery, State of Michigan**

### **Notes to Financial Statements**

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#### EQUITY IN STATE TREASURER'S COMMON CASH FUND

The State Treasurer manages the State's Common Cash pool, which is used by the Lottery. The pooling of cash allows the Treasurer to invest monies not needed to pay immediate obligations so that investment earnings on available cash are maximized. Investments of the pool are not segregated by fund; rather, each contributing fund's balance is treated as equity in the pool, and presented in this report as "Equity in State Treasurer's Common Cash."

Investment policies and risk categorization are included in the State of Michigan's comprehensive annual financial report.

#### INVESTMENTS

Investments are reported at fair value. Investments are in U.S. Treasury stripped deep discount bonds and are purchased to meet future installment payments to prize winners. There are generally no available realized gains or losses on investments, as it is the State Treasurer's policy to hold the Lottery's investments to maturity or liquidated. The difference between the fair value and the amortized cost is reflected as a restriction of Net Assets for unrealized gains on investments.

#### INVENTORY

Inventory consists of instant game tickets, pull-tab game tickets, and charity game tickets on hand and for sale at year end as well as merchandize prizes for games that have not started as of September 30, 2005. The inventory is valued at cost, primarily using the weighted average method.

#### PROVISION FOR DOUBTFUL ACCOUNTS

The Lottery establishes an allowance for bad debt for any retailer accounts receivable greater than 90 days old. A bad debt expense is recorded when the allowance is set up for these receivables. The amount of the allowance for doubtful accounts totaled \$ 1,500,811 for the year ended September 30, 2005 and \$ 1,494,572 for the year ended September 30, 2004.

#### CAPITAL ASSETS

The Lottery has established a \$ 5,000 threshold for capitalization of purchases of assets, which include equipment and leasehold improvements, and are reported in the Statement of Net Assets. Such assets are recorded at historical cost. Depreciation of equipment is computed using the straight-line method over five years, the estimated useful life of the assets. Information technology equipment is depreciated over three years, the estimated useful life of the assets. Building leasehold improvements are depreciated over eight years, the estimated useful life of the improvements. The costs of normal maintenance and repairs that do not add to the value of assets or materially extend asset lives are not capitalized.

#### ADVANCE WAGERS

All on-line games may be played on an advance wager basis. An associated liability is recognized for all wagers received for drawings to be held after the end of the reporting period.

## **Bureau of State Lottery, State of Michigan**

### **Notes to Financial Statements**

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#### WARRANTS AUTHORIZED AND WARRANTS OUTSTANDING

Most of the Lottery's disbursements are made through warrants issued by the State. Warrants requested by the Lottery are charged to the Lottery's equity in the State Treasurer's Common Cash Fund as they clear the State Treasurer's account. Therefore, warrants outstanding represent drafts issued against the State Treasurer's account, which have not cleared. Warrants requested by the Lottery, but not yet issued by the State, are reported as warrants authorized.

#### UNCLAIMED PRIZES

Prizes not claimed within one year after the drawing date or after the expiration date indicated on the back of the instant game tickets, are forfeited by the ticket holder. The Lottery estimates the amount of winning on-line and instant tickets, which will not be claimed within one year after the drawing date for on-line tickets or after the expiration date for instant tickets. All unclaimed prizes are transferred to the State School Aid Fund as provided by State Statute.

#### NOTE 2 - EQUITY IN STATE TREASURER'S COMMON CASH

The Lottery participates in the State Treasurer's Common Cash pool. The investment authority for the pool is found in P.A. 105 of 1855, as amended. The pool functions as both a cash management pool and a demand deposit account. The State Treasurer may invest surplus funds belonging to the State in the bonds, notes, and other evidences of indebtedness of the United States Government, and its agencies, and in prime commercial paper. The Treasurer invests excess cash in short-term investments, mostly prime commercial paper.

The following paragraphs provide disclosures about deposits and investments of the State Treasurer's Common Cash Fund:

#### COMMON CASH DEPOSITS

##### Custodial Credit Risk

The custodial credit risk for deposits is the risk that in the event of a bank failure, the State may recover its deposits.

Deposits are exposed to custodial credit risk if they are not covered by depository insurance and the deposits are:

- a. Uncollateralized
- b. Collateralized with securities held by the pledging financial institution, or
- c. Collateralized with securities held by the pledging financial institution's trust department or agent but not in the depositor-government's name.



## **Bureau of State Lottery, State of Michigan**

### **Notes to Financial Statements**

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The State Treasurer's policy requires the following criteria to lessen the custodial credit risk: All financial institutions holding the State's money must pledge collateral equal to the amount of the account balance for all demand and time deposits, to secure the State funds. A bank, savings and loan association or credit union holding State funds must be organized under the law of Michigan or federal law and maintain a principal office or branch office in the state of Michigan. No deposit in any financial organization may be in excess of 50 percent of the net worth of the organization.

#### Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of a deposit.

Act 35 of 1997 requires State deposits to be held in a financial institution which maintains a principal office or branch office located in the state of Michigan.

No deposits were exposed to foreign currency risk, as is precluded by State policy.

#### COMMON CASH INVESTMENTS

##### Risk

In accordance with GASB Statement No. 40, investments require certain disclosures regarding policies and practices with respect to the risks associated with them. The custodial credit risk, the credit risk, and the interest rate risk are discussed in the following paragraphs:

##### Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty, the State will not be able to recover the value of the investment or collateral securities that are in the possession of the outside party.

Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the government and are held by either:

The counterparty or

The counterparty's trust department or agent but not in the government name.

The State Treasurer does not have a policy for custodial credit risk for common cash investments.

##### Credit Risk

Credit risk is the risk that an issuer will not fulfill its obligations.

## Bureau of State Lottery, State of Michigan

### Notes to Financial Statements

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Prime commercial paper investments must be rated A-1 or P-1 at the time of purchase as rated by the two major rating services Standard and Poor (A-1); and Moody's (P-1). Borrowers must have at least \$ 400 million in commercial paper outstanding, and the State Treasurer may not invest in more than 10% of the borrower's outstanding debt. The investments are further limited to \$ 200 million in any borrower, unless the borrower has an A-1+ rating in which case the investment is not to exceed \$ 300 million.

#### Interest Rate Risk

Interest rate risk is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment.

The State Treasurer's policy states that cash equivalents are invested in short term fixed income securities with an average weighted maturity of less than one year to provide liquidity and safety of principal from capital market and default risk.

#### NOTE 3 - INVESTMENTS

Investments totaling \$ 514,262,899 at September 30, 2005, and \$ 600,685,742 at September 30, 2004, are in the form of United States Treasury zero coupon bonds. These investments were purchased to fund future payments due to annuity prize winners. The zero coupon bonds are reported at fair value. The corresponding liability to the prize winners is recorded in prizes payable and is disclosed in note 6. Cash receipts from the maturity of investments in prize annuities totaled \$ 104,833,000 in the year ended September 30, 2005 and \$ 108,890,000 in the year ended September 30, 2004.

Investments at September 30, consist of the following:

As reported on the Statement of Net Assets:	2005	2004
Current investments	\$ 93,378,340	\$ 103,861,541
Noncurrent investments	420,884,559	496,824,201
Total Investments	<u>\$ 514,262,899</u>	<u>\$ 600,685,742</u>

#### Policy Disclosures

Investment authority with regard to the State Lottery Fund is delegated to the State Treasurer per the McCauley-Traxler-Law-Bowman-McNeely Lottery Act 239 of 1972 section 432.41 paragraph 2. This authority is the same investment authority with regard to retirement system funds which is the Public Employee Retirement System Investment Act 314 of 1965, as amended by Act 55 of 1982. The Act incorporates the prudent person rule and requires that investment fiduciaries act solely in the interest of the entities' participants and beneficiaries. Investments in common stock are limited to 60% of the system's assets and must be in companies paying dividends in three of the last five years. Investments in fixed debt securities are limited to issuing entities graded within the top four grades by the two national rating services.

## Bureau of State Lottery, State of Michigan

### Notes to Financial Statements

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The Act also permits investments in real estate and certain other assets not exceeding 20% of the portfolio, however the Lottery had no such investments at September 30, 2005 and 2004, respectively. The Lottery has no policy, but the procedure is to invest solely in United States Treasury Zero Coupon bonds and hold them to maturity.

#### Interest Rate Risk

Investments at September 30, 2005 consist of the following:

<u>Maturities In years</u>	<u>Investments in United States Treasury Zero Coupon Bonds</u>	<u>Interest Rate Low to High</u>
Less than 1	\$ 93,378,340	5.54% to 11.04%
1-5	261,083,606	5.58% to 11.10%
6-10	126,844,343	5.68% to 11.02%
11-15	19,981,285	5.74% to 7.38%
16-20	6,781,042	5.14% to 6.54%
21-26	<u>6,194,283</u>	5.00% to 5.13%
Fair Market Value	<u><u>\$ 514,262,899</u></u>	

Interest rate risk is the risk that an investment's fair value decreases as market interest rates increase. Typically, this risk is higher in debt securities with longer maturities. The State does not have a policy regarding interest rate risk. The investments are subject to fluctuations in fair value due to interest rate risk, but these bonds are held to maturity to satisfy the annual installment obligations to the prize winners. The fair value at maturity is the face value of the bonds regardless of the fluctuations in value during the time period that the investments are outstanding, thus minimizing the interest rate risk, if held to maturity.

#### Credit Risk

U. S. Treasury zero coupon bonds are explicitly guaranteed by the U. S. government and credit quality ratings are therefore not required. The Lottery procedure to invest in this type of bond does not require a specific credit rating, but credit quality is inherently high as the bonds are explicitly guaranteed by the U. S. government.

#### Concentration of Credit Risk

Investments are in United States Treasury zero coupon bonds which are guaranteed by the United States government. Therefore, there is no concentration of credit risk.

#### Custodial Credit Risk

In accordance with GASB Statement No. 40, for an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Lottery will not be able to recover the value of its investments that are in the possession of an outside party. These are uninsured and unregistered, with securities held by the counterparty or by its trust department or agent but not in the entity's name. The Lottery does not have any of these types of investments.

## Bureau of State Lottery, State of Michigan

### Notes to Financial Statements

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The Lottery does participate in a security lending program. However the investments remain in the name of the Lottery and 102% collateral is required as explained below.

State Statues do not prohibit the Lottery from participating in securities lending transactions; and the Lottery has, via a Securities Lending Authorization Agreement, authorized the agent bank to lend its securities to broker dealers and banks pursuant to a form of loan agreement.

The following represents the balances relating to the securities lending transactions as of September 30, 2005:

Securities Lent	Underlying Securities	Collateral Received	Collateral Investment Value	Type of Collateral
U.S. Government securities	\$ 400,127,292	\$ 409,169,719	\$ 409,169,719	Custodian's short-term invesment pool

During the year, the agent bank lent, at the direction of the State Treasurer, the Lottery's securities and received cash (United States and foreign currency), securities issued or guaranteed by the United States Government, sovereign debt rated A or better, convertible bonds, and irrevocable bank letters of credit as collateral. The agent bank did not have the ability to pledge or sell collateral securities delivered absent a borrower default. The agent bank borrowers were required to deliver collateral for each loan equal to: (i) in the case of loaned securities denominated in United States dollars or whose primary trading market was located in the United States or sovereign debt issued by foreign governments, 102% of market value of the loaned securities; and (ii) in the case of loaned securities not denominated in United States dollars or whose primary trading market was not located in the United States, 105% of the market value of loaned securities.

The Lottery did not impose any restrictions during the year on the amount of the loans that the agent bank made on its behalf and the agent bank indemnified the Lottery by agreeing to purchase replacement securities, or return cash collateral in the event borrower failed to return the loaned security or pay distributions thereon. There were no failures by any borrowers during the fiscal year. Moreover, there were no losses during the fiscal year resulting from a default of the borrowers or the agent bank.

During the year, the Lottery and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested in a collective investment pool. Because the loans were terminable at will, their duration did not generally match the duration of the investments made with cash collateral. On September 30, 2005, the Lottery had no custodial credit risk exposure to borrowers.

Gross income from securities lending for the six months and year ended September 30, 2005, was \$ 3,628,907 and \$ 6,363,685, respectively. Expenses associated with this income for the six months and year ended September 30, 2005, were \$ 3,376,423 and \$ 5,883,506, respectively, for the borrower's rebates and \$ 69,948 and \$ 130,170, respectively, for bank fees and fees paid to the agent.

#### Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. The Lottery had no short-term external collateral investment pool deposits subject to foreign currency risk at September 30, 2005.

**Bureau of State Lottery, State of Michigan**  
**Notes to Financial Statements**

**NOTE 4 - CAPITAL ASSETS**

A summary of capital asset activity for the years ended September 30, 2005 and 2004 was as follows:

Period Ending	Beginning Balance	Additions	Deletions	Ending Balance
<u>September 30, 2005</u>				
Capital assets, being depreciated:				
Leasehold improvements	\$ 1,917,979	\$ -	\$ -	\$ 1,917,979
Equipment	2,193,988	167,510	260,483	2,101,015
Total capital assets, being depreciated	4,111,967	167,510	260,483	4,018,994
Less: accumulated depreciation				
Leasehold improvements	1,655,971	49,735	-	1,705,706
Equipment	1,943,161	86,916	260,483	1,769,594
Total accumulated depreciation	3,599,132	136,651	260,483	3,475,300
Total capital assets, being depreciated, net	<u>\$ 512,835</u>	<u>\$ 30,859</u>	<u>\$ -</u>	<u>\$ 543,694</u>
<u>September 30, 2004</u>				
Capital assets, being depreciated:				
Leasehold improvements	\$ 1,917,979	\$ -	\$ -	\$ 1,917,979
Equipment	2,112,382	81,606	-	2,193,988
Total capital assets, being depreciated	4,030,361	81,606	-	4,111,967
Less: accumulated depreciation				
Leasehold improvements	1,603,825	52,146	-	1,655,971
Equipment	1,845,891	97,270	-	1,943,161
Total accumulated depreciation	3,449,716	149,416	-	3,599,132
Total capital assets, being depreciated, net	<u>\$ 580,645</u>	<u>\$ (67,810)</u>	<u>\$ -</u>	<u>\$ 512,835</u>

**NOTE 5 - DISAGGREGATION OF PAYABLE BALANCE**

Accounts payable and other liabilities at September 30, were as follows:

	2005	2004
Accounts payable	\$ 1,211,383	\$ 1,269,801
Retailer security deposits	1,155,000	1,008,500
Accrued salaries	673,542	416,069
Compensated absences	194,854	171,636
Total	<u>\$ 3,234,779</u>	<u>\$ 2,866,006</u>

**Bureau of State Lottery, State of Michigan**  
**Notes to Financial Statements**

**NOTE 6 - PRIZE AWARDS**

Installment prize awards are recorded at their present value using discount rates ranging from 5.0% to 8.5%. U.S. Treasury stripped deep discount bonds have been purchased to provide for the payment of installment prize awards in addition to cash maintained in the State's common cash fund. Prize awards payable as of September 30, were as follows:

	2005	2004
Current - at face amount	\$ 134,965,339	\$ 139,299,103
Less - unamortized discount	(3,283,141)	(3,602,352)
Current - at present value	131,682,198	135,696,751
Long-term - at face amount	527,301,740	617,282,543
Less - unamortized discount	(155,385,043)	(187,054,512)
Long-term - at present value	371,916,697	430,228,031
Total	<u>\$ 503,598,895</u>	<u>\$ 565,924,782</u>

Installment prize awards payable for the twelve-month period ending September 30,

2006	\$ 94,716,502
2007	86,266,945
2008	75,509,570
2009	68,324,070
2010	56,550,595
2011-2015	168,513,261
2016-2020	37,046,700
2021-2025	17,811,100
2026-2030	7,320,500
2031-2035	5,055,000
Later years	4,904,000
Total	622,018,243
Less - unamortized discount	(158,668,184)
Total installment prize awards payable at present value	463,350,059
Non-installment prize awards payable	40,248,836
Total prize awards payable	<u>\$ 503,598,895</u>

Long-term liability activity of installment prize awards payable for the years ended September 30, was as follows:

Period Ending	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year at Present Value
2005	\$ 530,013,607	\$ 36,888,678	\$ 103,552,226	\$ 463,350,059	\$ 91,433,362
2004	\$ 596,670,328	\$ 43,160,136	\$ 109,816,857	\$ 530,013,607	\$ 99,785,577

**Bureau of State Lottery, State of Michigan**  
**Notes to Financial Statements**

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**NOTE 7 - COMPENSATED ABSENCES**

The Lottery records as a liability estimated vested vacation, sick pay and longevity. Employees are granted vacation pay in varying amounts based on length of service. Accumulated unused vacation pay is paid to employees or their beneficiaries upon death, retirement or resignation. Sick leave accrues for all employees at the rate of four hours for each two week period worked. Up to 50% of accumulated, unused sick leave of employees hired prior to October 1, 1980, is paid to the employees or their beneficiaries upon death, retirement or resignation. For employees hired after September 30, 1980, unused sick leave is forfeited upon termination of employment. In accordance with state Civil Service Rules, longevity compensation payments, which are separate from regular compensation, are paid based on employee years of service. The Lottery accrues for vacation, vested sick leave and longevity to be paid upon death, retirement or resignation during the period of active employment.

Long-term liability activity of these benefits for the years ended September 30 was as follows:

<u>Fiscal Year</u> <u>Ending</u>	<u>Beginning</u> <u>Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending</u> <u>Balance</u>	<u>Due Within</u> <u>One Year</u>
2005	\$ 1,987,957	\$ 1,095,017	\$ 912,929	\$ 2,170,045	\$ 194,854
2004	\$ 1,679,494	\$ 1,040,835	\$ 732,372	\$ 1,987,957	\$ 171,636

**NOTE 8 - PENSION**

The Lottery's employees hired prior to March 31, 1997, are enrolled in a noncontributory defined benefit plan through the State Employees' Retirement System ("Plan 1") upon meeting certain eligibility requirements. The Plan provides for pension, dental, vision, and major medical coverage. A member may retire with an age and service allowance after completing: (1) at least 10 years of credited service and (2) attaining the minimum retirement age of 60, or at least age 55 with 30 years of service credit. Pension benefits are determined using 1.5% times a member's final average compensation, calculated as the average of a member's monthly pay during the period of 36 consecutive months of credited service producing the highest monthly average multiplied by length of service.

The Lottery's employees hired after March 31, 1997, are enrolled in a defined contribution plan through the State Employee's Retirement System ("Plan 2") upon meeting certain eligibility requirements. Qualified participants are generally eligible to retire at age 55, with 30 years of service or at age 60 with 10 years of service. The Lottery contributes a mandatory four percent of the employees' salary and matches up to an additional three percent of the employees' contributions.

Participants in Plan 2 are 100% vested for any employee contributions. Participants become vested for 50% of the employer contributions after 2 years of service, 75% after 3 years of service and 100% after 4 years of service. Employees become vested for retiree health insurance benefits with 10 or more years of service.

**Bureau of State Lottery, State of Michigan**  
**Notes to Financial Statements**

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The cost of these benefits is allocated to the Lottery as a percentage of gross payroll. The payroll for the Lottery employees covered by the Plan 1 and Plan 2 was approximately \$ 4,196,769, \$ 3,670,803, and \$ 3,674,940 for the six months ended September 30, 2005, 2004, and 2003, respectively and approximately \$ 8,569,264, \$ 7,414,633, and \$ 7,452,739 for the years ended September 30, 2005, 2004, and 2003, respectively. The Lottery's actuary determined contribution requirements and contributions actually made were approximately \$ 1,277,796, \$ 903,453, and \$ 895,199 for the six month periods ended September 30, 2005, 2004, and 2003, respectively and approximately \$ 2,598,929, \$ 2,011,560, and \$ 1,835,898 for the years ended September 30, 2005, 2004, and 2003, respectively. Contributions represent approximately 30.3%, 27.1%, and 24.6% of annual covered payroll during 2005, 2004, and 2003, respectively.

Additional detail and data regarding Plan 1 and Plan 2 descriptions, vesting and eligibility requirements, actuarial cost methods and assumptions, funding requirements, accounting policies and 10-year historical trend information is provided in the State of Michigan Comprehensive Annual Financial Report and the detailed financial report issued by the Lottery of Retirement Systems.

**NOTE 9 - LEASE AND RENTAL COMMITMENTS**

The total operating lease payments for years ended September 30, 2005 and 2004 were \$ 68,939 and \$ 74,473, respectively. These leases represent leases for buildings. There were no capital lease obligations.

A summary of operating lease commitments to maturity follows:

<u>Year Ended September 30</u>	<u>Operating Leases</u>
2006	\$ 102,111
2007	103,049
2008	103,049
2009	75,486
2010	55,799
	<u>\$ 439,494</u>



**Bureau of State Lottery, State of Michigan**  
**Notes to Financial Statements**

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**NOTE 10 - TRANSACTIONS WITH OTHER STATE AGENCIES**

As a State agency, the Lottery is required to utilize services, supplies and equipment provided by other State agencies. Following is a summarization of these charges for the year ended September 30, 2005:

Department of Management and Budget		
Support services	\$ 127,300	
Space rental - Lottery Central, Detroit, Saginaw offices	2,123,509	
Vehicle and Travel Services	722,819	
Other - Telephone, mailing and other offices services	<u>317,650</u>	
Total Department of Management and Budget		\$ 3,291,278
Civil Service		125,898
Department of Treasury		96,605
Attorney General		212,948
Department of Information Technology (DIT)		
Direct costs	2,971,368	
Michigan Administrative Information Network (MAIN), Lansing		
Metropolitan Area Network (LMAN), Unisys Platform Charges	119,069	
Michigan Gov Portal Web Charges	381,593	
Overhead	<u>112,845</u>	
Total DIT Charges		3,584,875
History, Arts, & Library		25,200
Other Agencies		<u>37,479</u>
 Total all State agencies		 <u><u>\$ 7,374,283</u></u>

**NOTE 11 - RISK MANAGEMENT**

The Lottery is exposed to various risks related to torts; property damage and destruction, errors and omissions, workers' compensation and unemployment compensation. The State of Michigan has elected not to purchase commercial insurance for many of the risks of losses to which the Lottery is exposed, but to self-insure for such risks. More detailed information on risk management is available in the State of Michigan's comprehensive annual financial report.

**NOTE 12 - COMMITMENTS AND CONTINGENCIES**

From time to time, the Lottery is party to lawsuits and claims arising in the normal course of business. The Lottery has defended and intends to continue to defend these actions vigorously and believes, based on currently available information, that adverse settlements, if any, will not be material to its financial position or results of operation.

**Bureau of State Lottery, State of Michigan**  
**Supplementary Schedule of Revenues, Expenses and Transfers**  
**For the Six Months and Year Ended September 30, 2005**

		Six Months Ended		Year Ended	
		Amount	Percent of Sales	Amount	Percent of Sales
Lottery ticket sales:	Daily 3	\$ 194,353,643	18.8%	\$ 401,071,740	19.5%
	Daily 3 Double	860,384	0.1%	1,827,075	0.1%
	Daily 4	150,427,470	14.5%	308,845,176	14.9%
	Daily 4 Double	392,076	0.0%	833,898	0.0%
	Winfall	7,945,640	0.8%	37,179,827	1.8%
	Classic Lotto 47	18,463,251	1.8%	18,463,251	0.9%
	Mega Millions	117,263,887	11.4%	203,902,214	9.8%
	Keno	6,824,025	0.7%	13,520,419	0.7%
	Michigan Rolldown	(1,136)	0.0%	(6,443)	0.0%
	Fantasy Five	24,385,432	2.4%	49,899,126	2.4%
	Club Keno	168,122,562	16.3%	332,356,189	16.1%
	Pull-Tab tickets	16,173,528	1.6%	39,066,984	1.9%
	Instant tickets	325,935,740	31.6%	662,533,892	31.9%
Total lottery ticket sales		1,031,146,502	100.0%	2,069,493,348	100.0%
Prize awards:	Daily 3	92,330,083	9.0%	189,245,384	9.1%
	Daily 3 Double	486,500	0.0%	1,061,150	0.1%
	Daily 4	74,003,016	7.2%	160,256,378	7.7%
	Daily 4 Double	237,500	0.0%	522,000	0.0%
	Winfall	3,454,460	0.4%	23,785,095	1.1%
	Classic Lotto 47	10,435,121	1.0%	10,435,121	0.5%
	Mega Millions	58,223,350	5.6%	101,554,158	4.9%
	Keno	3,036,394	0.3%	6,549,239	0.3%
	Fantasy Five	12,673,156	1.2%	26,195,281	1.3%
	Club Keno	109,800,262	10.6%	216,752,935	10.5%
	Pull-Tab tickets	10,543,789	1.0%	25,521,544	1.2%
	Instant tickets	205,251,355	19.9%	417,763,784	20.3%
Total prize awards		580,474,986	56.2%	1,179,642,069	57.0%
Less: unclaimed prizes		(17,516,337)	-1.7%	(17,634,462)	-0.9%
Net prize awards		562,958,649	54.5%	1,162,007,607	56.1%
Gross margin		468,187,853	45.5%	907,485,741	43.9%
Agent and vendor commission expense		94,801,190	9.2%	191,174,540	9.2%
Game related expense		8,933,753	1.0%	18,369,818	1.0%
Net ticket revenue		364,452,910	35.3%	697,941,383	33.7%
Other operating expense		16,507,386	1.6%	35,459,978	1.6%
Other miscellaneous revenue		533,606	0.2%	999,861	0.0%
Net lottery operating income		348,479,130	33.9%	663,481,266	32.1%
Charitable gaming					
Charitable gaming revenue		9,575,077	0.9%	19,639,038	1.0%
Charitable gaming expense		4,044,403	0.4%	7,910,093	0.4%
Net charitable gaming income		5,530,674	0.5%	11,728,945	0.6%

Continued

**Bureau of State Lottery, State of Michigan**  
**Supplementary Schedule of Revenues, Expenses and Transfers**  
**For the Six Months and Year Ended September 30, 2005**

	Six Months Ended		Year Ended	
	Amount	Percent of Sales	Amount	Percent of Sales
Non-operating revenues (expenses)				
Amortization expense - prize discount	(16,512,669)	-1.6%	(34,251,841)	-1.7%
Amortization revenue - investment discount	17,330,617	1.7%	35,956,493	1.7%
Realized gain on investment	492,704	0.0%	492,704	0.0%
Unrealized (loss) on investments	(4,924,527)	-0.5%	(24,646,166)	-1.1%
Interest revenue - common cash fund	1,723,699	0.2%	2,540,807	0.1%
Net security lending income	182,536	0.0%	350,009	0.0%
Net non-operating revenues (expenses)	<u>(1,707,640)</u>	<u>-0.2%</u>	<u>(19,557,994)</u>	<u>-1.0%</u>
Net income before transfers	352,302,164	34.2%	655,652,217	31.7%
Unrealized loss on investments	<u>4,924,527</u>	<u>0.5%</u>	<u>24,646,166</u>	<u>1.2%</u>
Net income available for transfer	<u>\$ 357,226,691</u>	<u>34.7%</u>	<u>\$ 680,298,383</u>	<u>32.9%</u>
Amount transferred to:				
School Aid Fund	\$ 351,201,017	34.1%	\$ 667,579,438	32.3%
General Fund	5,530,674	0.6%	11,728,945	0.6%
Community Health	<u>495,000</u>	<u>0.0%</u>	<u>990,000</u>	<u>0.0%</u>
Total amount transferred out	<u>\$ 357,226,691</u>	<u>34.7%</u>	<u>\$ 680,298,383</u>	<u>32.9%</u>

**Bureau of State Lottery, State of Michigan**  
**Supplementary Schedule of Revenues, Expenses and Transfers**  
**For the Six Months and Year Ended September 30, 2004**

		Six Months Ended		Year Ended	
		Amount	Percent of Sales	Amount	Percent of Sales
Lottery ticket sales:	Daily 3	\$ 209,000,256	20.9%	\$ 420,453,878	21.3%
	Daily 3 Extra	139,539	0.0%	1,273,614	0.1%
	Daily 3 Double	1,534,641	0.2%	1,534,641	0.1%
	Daily 4	153,928,751	15.4%	308,163,027	15.6%
	Daily 4 Extra	132,229	0.0%	1,163,558	0.1%
	Daily 4 Double	855,148	0.1%	855,148	0.0%
	Winfall	31,074,442	3.1%	66,569,830	3.4%
	Mega Millions	103,295,984	10.3%	206,620,985	10.4%
	Keno	7,280,468	0.7%	14,855,678	0.8%
	Michigan Rolldown	13,542,409	1.4%	29,862,687	1.5%
	Fantasy Five	2,702,623	0.3%	2,702,623	0.1%
	Change Play	-	0.0%	88,159	0.0%
	Club Keno	125,718,726	12.6%	204,519,031	10.4%
	Pull-Tab tickets	13,037,599	1.3%	25,079,647	1.3%
	Instant tickets	336,354,419	33.7%	690,157,728	34.9%
Total lottery ticket sales		998,597,234	100.0%	1,973,900,234	100.0%
Prize awards:	Daily 3	106,339,965	10.6%	211,990,865	10.7%
	Daily 3 Extra	89,500	0.0%	796,150	0.0%
	Daily 3 Double	939,500	0.1%	939,500	0.0%
	Daily 4	93,541,364	9.4%	163,286,182	8.3%
	Daily 4 Extra	84,050	0.0%	727,750	0.0%
	Daily 4 Double	447,625	0.0%	447,625	0.0%
	Winfall	18,613,696	1.9%	37,927,309	1.9%
	Mega Millions	51,936,198	5.2%	103,628,825	5.2%
	Keno	3,174,462	0.3%	7,874,977	0.4%
	Michigan Rolldown	6,647,937	0.7%	14,677,166	0.7%
	Fantasy Five	1,376,664	0.1%	1,376,664	0.1%
	Change Play	-	0.0%	34,618	0.0%
	Club Keno	83,802,754	8.4%	135,246,232	6.9%
	Pull-Tab tickets	8,480,864	0.8%	16,317,094	0.8%
	Instant tickets	213,964,900	21.4%	435,572,847	22.1%
Total prize awards		589,439,479	58.9%	1,130,843,804	57.1%
Less: unclaimed prizes		(15,303,088)	-1.5%	(31,171,242)	-1.6%
Net prize awards		574,136,391	57.4%	1,099,672,562	55.5%
Gross margin		424,460,843	42.6%	874,227,672	44.5%
Agent and vendor commission expense		92,548,856	9.3%	182,304,941	9.2%
Game related expense		8,651,187	0.9%	17,207,801	0.9%
Net ticket revenue		323,260,800	32.4%	674,714,930	34.4%
Other operating expense		16,027,954	1.6%	33,474,872	1.7%
Other miscellaneous revenue		648,751	0.1%	1,430,253	0.1%
Net lottery operating income		307,881,597	30.9%	642,670,311	32.8%
Charitable gaming					
Charitable gaming revenue		10,173,840	1.0%	19,980,694	1.0%
Charitable gaming expense		3,913,583	0.4%	7,777,396	0.4%
Net charitable gaming income		6,260,257	0.6%	12,203,298	0.6%

Continued

**Bureau of State Lottery, State of Michigan**  
**Supplementary Schedule of Revenues, Expenses and Transfers**  
**For the Six Months and Year Ended September 30, 2004**

	Six Months Ended		Year Ended	
	Amount	Percent of Sales	Amount	Percent of Sales
Non-operating revenues (expenses)				
Amortization expense - prize discount	(19,008,946)	-1.9%	(39,223,183)	-2.0%
Amortization revenue - investment discount	19,749,159	2.0%	41,108,196	2.1%
Unrealized (loss) on investments	(20,840,313)	-2.1%	(28,078,938)	-1.4%
Interest revenue - common cash fund	616,259	0.1%	959,770	0.0%
Net security lending income	157,426	0.0%	357,748	0.0%
Net non-operating revenues (expenses)	<u>(19,326,415)</u>	<u>-1.9%</u>	<u>(24,876,407)</u>	<u>-1.3%</u>
Net income before transfers	294,815,439	29.6%	629,997,202	32.1%
Unrealized loss on investments	<u>20,840,313</u>	<u>2.0%</u>	<u>28,078,938</u>	<u>1.3%</u>
Net income available for transfer	<u>\$ 315,655,752</u>	<u>31.6%</u>	<u>\$ 658,076,140</u>	<u>33.4%</u>
Amount transferred to:				
School Aid Fund	\$ 308,900,496	31.0%	\$ 644,882,842	32.7%
General Fund	6,260,256	0.6%	12,203,298	0.6%
Community Health	<u>495,000</u>	<u>0.0%</u>	<u>990,000</u>	<u>0.1%</u>
Total amount transferred out	<u>\$ 315,655,752</u>	<u>31.6%</u>	<u>\$ 658,076,140</u>	<u>33.4%</u>

Concluded

**Bureau of State Lottery, State of Michigan**  
**Supplementary Schedule of Other Operating Expenses**  
**For the Six Months and Years Ended September 30, 2005 and 2004**

	Six Months Ended		Years Ended	
	2005	2004	2005	2004
Salaries and wages	\$ 4,196,769	\$ 3,670,803	\$ 8,569,264	\$ 7,414,633
Employee benefits and taxes	2,038,119	1,648,989	4,408,372	3,892,685
Advertising	7,789,653	8,416,737	17,597,101	17,534,439
Talent	138,609	139,284	272,978	266,188
Printing and supplies, including purchase of charitable gaming tickets	1,123,894	1,223,069	2,325,458	2,535,094
Other contractual services	2,634,115	2,375,291	4,976,168	4,778,746
Building rent	898,286	807,381	1,797,491	1,707,545
Travel	486,846	452,676	913,590	845,003
Utilities	196,811	275,221	412,561	618,683
Postage	177,394	202,040	362,558	388,006
Equipment maintenance and rental	738,056	577,928	1,447,068	980,812
Bad debt expense	54,389	73,149	134,729	130,725
Interest paid on security deposits	11,273	3,927	16,082	10,293
Total	<u>\$ 20,484,214</u>	<u>\$ 19,866,495</u>	<u>\$ 43,233,420</u>	<u>\$ 41,102,852</u>

**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***

Mr. Gary C. Peters, Commissioner  
Bureau of State Lottery, State of Michigan  
and  
Mr. Thomas H. McTavish, Auditor General  
State of Michigan

We have audited the financial statements of the Bureau of State Lottery, State of Michigan (the "Lottery"), as of and for the six month period and year ended September 30, 2005, and have issued our report thereon dated November 18, 2005. 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 in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

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 no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

We noted a certain matter that we reported to the management of the Lottery in a separate letter dated November 18, 2005.

This report is intended solely for the information and use of the Commissioners, management and the Office of Auditor General, State of Michigan and is not intended to be and should not be used by anyone other than these specified parties.

*Yeo & Yeo, P.C.*

Lansing, Michigan  
November 18, 2005



## **STATISTICAL SECTION**



**Bureau of State Lottery, State of Michigan**  
**Net Assets**  
**Fiscal Years 2000 through 2005**

	2000	2001	2002	2003	2004	2005
<b>Net assets</b>						
Invested in capital assets	\$ 450,412	\$ 287,335	\$ 442,720	\$ 580,645	\$ 512,835	\$ 543,694
Restricted for unrealized gains on investments	50,876,628	95,705,521	128,060,961	105,176,470	77,097,532	52,451,366
Unrestricted (deficit)	<u>(450,412)</u>	<u>(287,335)</u>	<u>(442,720)</u>	<u>(580,645)</u>	<u>(512,835)</u>	<u>(543,694)</u>
<b>Total net assets</b>	<u>\$ 50,876,628</u>	<u>\$ 95,705,521</u>	<u>\$ 128,060,961</u>	<u>\$ 105,176,470</u>	<u>\$ 77,097,532</u>	<u>\$ 52,451,366</u>

Note: The Lottery implemented GASB Statement 34 in 2001; schedules include information beginning in the preceding year.



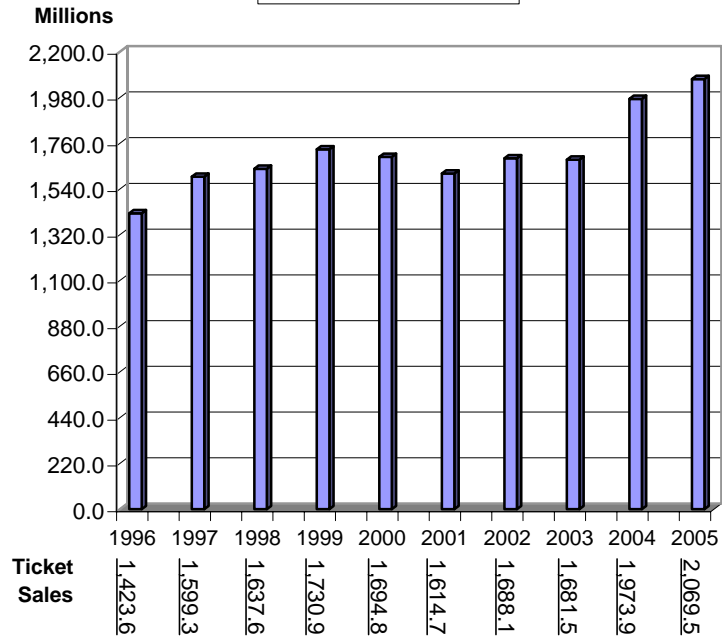
**Bureau of State Lottery, State of Michigan**  
**Changes in Net Assets**  
**Fiscal Years 2000 through 2005**

	2000	2001	2002	2003	2004	2005
<b>Operating revenues</b>						
Ticket sales	\$ 1,694,750,658	\$ 1,614,667,908	\$ 1,688,057,837	\$ 1,681,548,440	\$ 1,973,900,234	\$ 2,069,493,348
Charitable gaming and other	15,211,428	17,726,699	20,627,608	20,281,993	21,410,947	20,638,899
Total operating revenues	1,709,962,086	1,632,394,607	1,708,685,445	1,701,830,433	1,995,311,181	2,090,132,247
<b>Operating expenses</b>						
Prize awards	920,800,127	873,324,730	918,104,561	919,221,954	1,130,843,804	1,179,642,069
Less - unclaimed prizes	(26,524,711)	(23,288,590)	(44,402,717)	(19,568,089)	(31,171,242)	(17,634,462)
Net prize awards	894,275,416	850,036,140	873,701,844	899,653,865	1,099,672,562	1,162,007,607
Retailer commissions	120,376,589	114,928,153	120,717,665	121,787,454	145,367,020	152,630,718
Game related expenses	43,063,956	41,763,462	44,090,452	45,108,711	54,145,722	56,913,640
Other operating expenses	38,394,497	38,992,302	40,035,192	40,324,410	41,252,268	43,370,071
Total operating expenses	1,096,110,458	1,045,720,057	1,078,545,153	1,106,874,440	1,340,437,572	1,414,922,036
Operating income	613,851,628	586,674,550	630,140,292	594,955,993	654,873,609	675,210,211
<b>Nonoperating revenues (expenses)</b>						
Investment revenue	58,586,644	103,651,197	75,069,369	23,248,419	13,029,258	11,803,031
Interest on equity in State Treasurer's Common Cash Fund	8,219,213	4,184,421	1,620,574	904,718	959,770	2,540,807
Revenue from security lending	15,160,137	11,461,593	5,593,655	3,680,001	4,704,821	6,363,685
Security lending expenses	(14,220,245)	(10,647,631)	(4,756,404)	(3,314,402)	(4,347,073)	(6,013,676)
Net gain (loss) on sale of assets	-	(29,375)	-	-	-	-
Amortization of prize obligation discount	(67,060,630)	(53,079,522)	(48,725,693)	(44,088,295)	(39,223,183)	(34,251,841)
Total non-operating revenue	685,119	55,540,683	28,801,501	(19,569,559)	(24,876,407)	(19,557,994)
<b>Transfers out</b>						
Transfer to School Aid Fund	(618,513,554)	(587,009,374)	(613,530,186)	(586,047,631)	(644,882,842)	(667,579,438)
Transfer to General Fund	(7,018,771)	(9,392,966)	(12,066,167)	(11,233,294)	(12,203,298)	(11,728,945)
Transfer to Community Health	(983,000)	(984,000)	(990,000)	(990,000)	(990,000)	(990,000)
Total transfers out	(626,515,325)	(597,386,340)	(626,586,353)	(598,270,925)	(658,076,140)	(680,298,383)
Increase (Decrease) in net assets	\$ (11,978,578)	\$ 44,828,893	\$ 32,355,440	\$ (22,884,491)	\$ (28,078,938)	\$ (24,646,166)

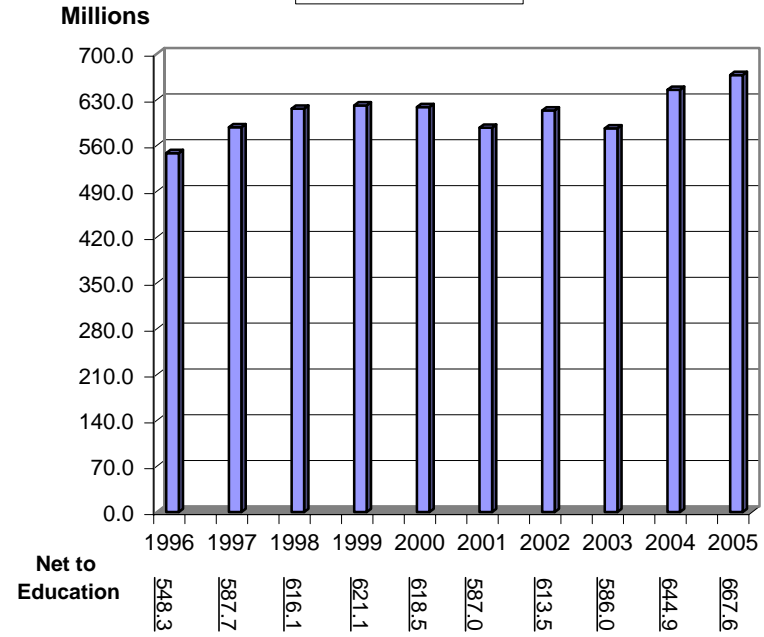
Source: Bureau of State Lottery, State of Michigan

**BUREAU OF STATE LOTTERY  
STATE OF MICHIGAN  
2005 FINANCIALS**

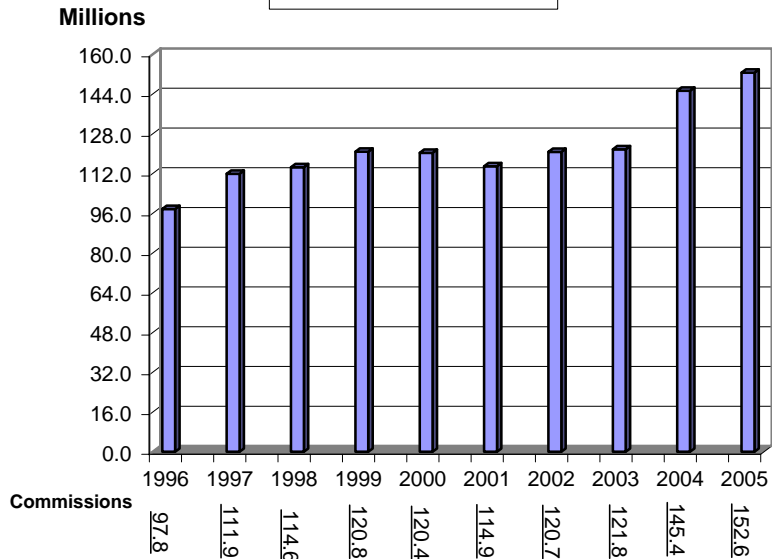
**Ticket Sales History**



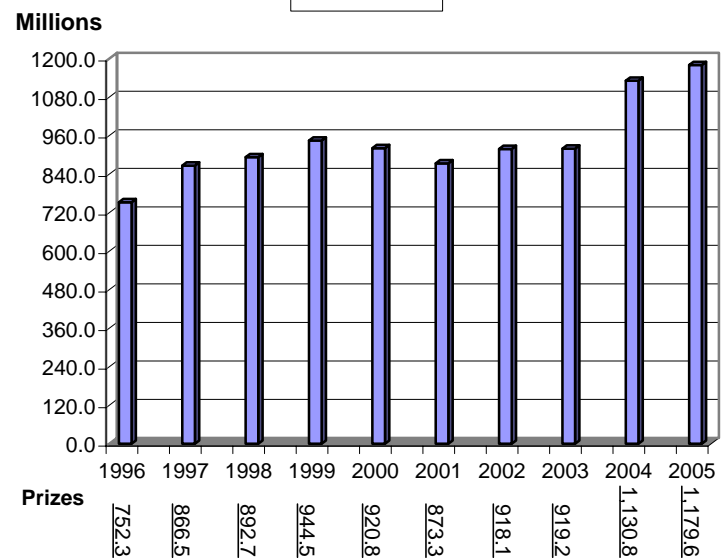
**Net To Education**



**Retailer Commissions**



**Prizes Won**



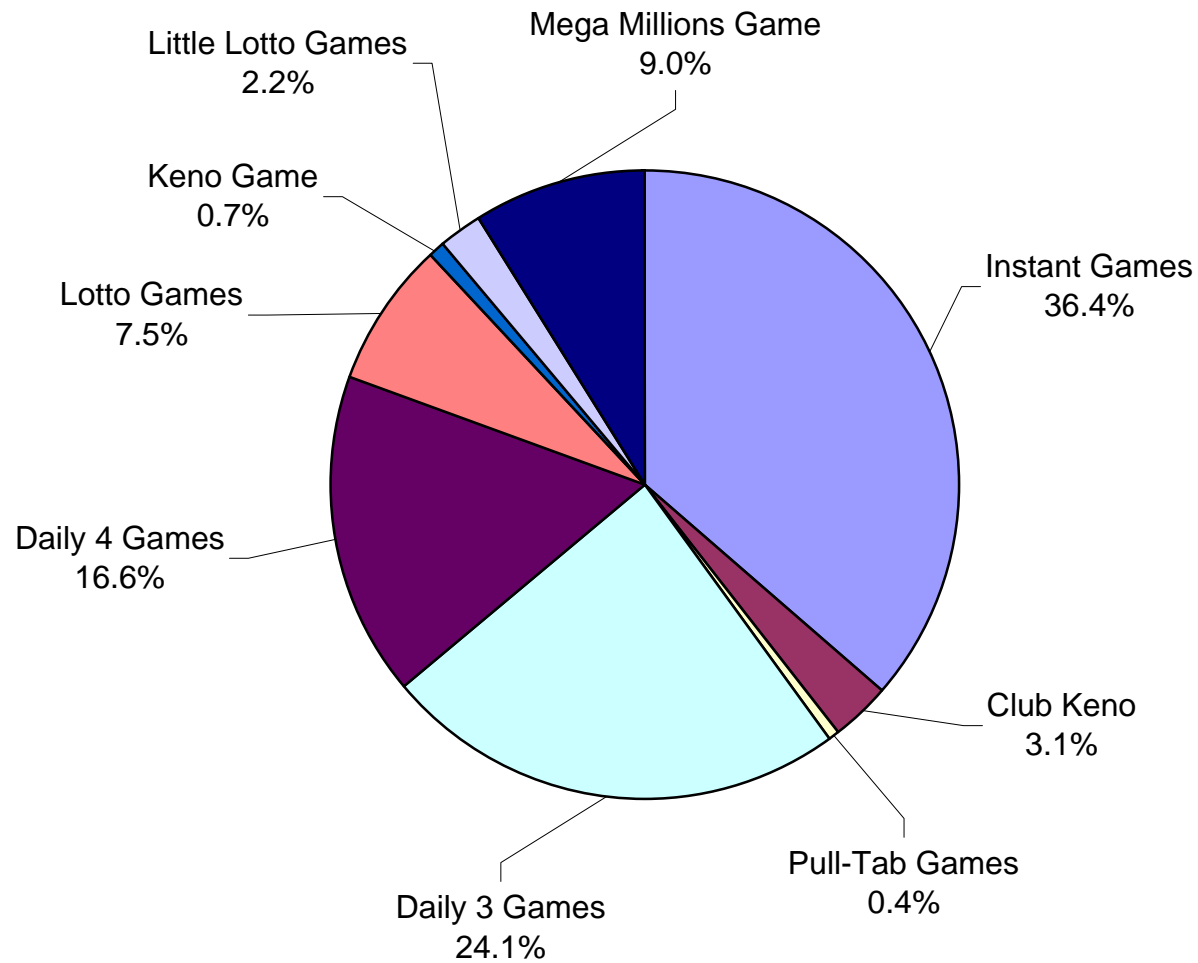


**Bureau of State Lottery, State of Michigan**  
**Revenues from Ticket Sales**  
**Fiscal Years 1996 through 2005**

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
<b>TICKET SALES</b>										
<b><i>Instant Games</i></b>										
Instant Tickets	\$ 472,292,640	\$ 563,851,942	\$ 605,901,617	\$ 629,941,090	\$ 643,266,961	\$ 626,680,348	\$ 655,415,025	\$ 682,703,482	\$ 690,157,728	\$ 662,533,892
<b><i>Club Games</i></b>										
Club Keno									204,519,031	332,356,189
Pull-Tab Tickets									25,079,647	39,066,984
Total Club Games									229,598,678	371,423,173
<b><i>On-Line Games</i></b>										
Daily 3, Extra 3, Double 3	381,967,674	400,801,313	410,104,556	424,471,395	416,774,485	404,194,582	418,261,372	423,338,204	423,262,133	402,898,815
Daily 4, Extra 4, Double 4	235,789,381	262,175,539	280,524,867	293,921,172	284,721,995	280,640,145	289,152,434	297,155,103	310,181,733	309,679,074
Michigan Lotto, Michigan Millions, Winfall, Classic Lotto 47	264,826,661	202,288,866	167,244,802	161,464,448	106,212,831	99,995,145	71,668,228	79,288,683	66,569,830	55,643,078
Keno	16,689,999	13,966,754	12,614,409	11,595,608	10,744,189	10,061,887	10,323,523	13,470,547	14,855,678	13,520,419
Little Lotto: Cash Five, Michigan Rolldown, Fantasy 5 and Change Play	44,174,558	36,222,802	32,110,584	28,551,780	44,430,655	41,102,363	37,254,044	38,058,135	32,653,469	49,892,683
Mega Millions	7,908,511	120,014,344	129,092,062	180,971,893	188,599,542	151,993,438	205,983,211	147,534,286	206,620,985	203,902,214
Total On-line	951,356,784	1,035,469,618	1,031,691,280	1,100,976,296	1,051,483,697	987,987,560	1,032,642,812	998,844,958	1,054,143,828	1,035,536,283
<b>TOTAL TICKET SALES</b>	<b>1,423,649,424</b>	<b>1,599,321,560</b>	<b>1,637,592,897</b>	<b>1,730,917,386</b>	<b>1,694,750,658</b>	<b>1,614,667,908</b>	<b>1,688,057,837</b>	<b>1,681,548,440</b>	<b>1,973,900,234</b>	<b>2,069,493,348</b>

Source: Bureau of State Lottery, State of Michigan

**BUREAU OF STATE LOTTERY  
STATE OF MICHIGAN  
REVENUES  
FISCAL YEARS 1996 THROUGH 2005**



Source: Bureau of State Lottery, State of Michigan

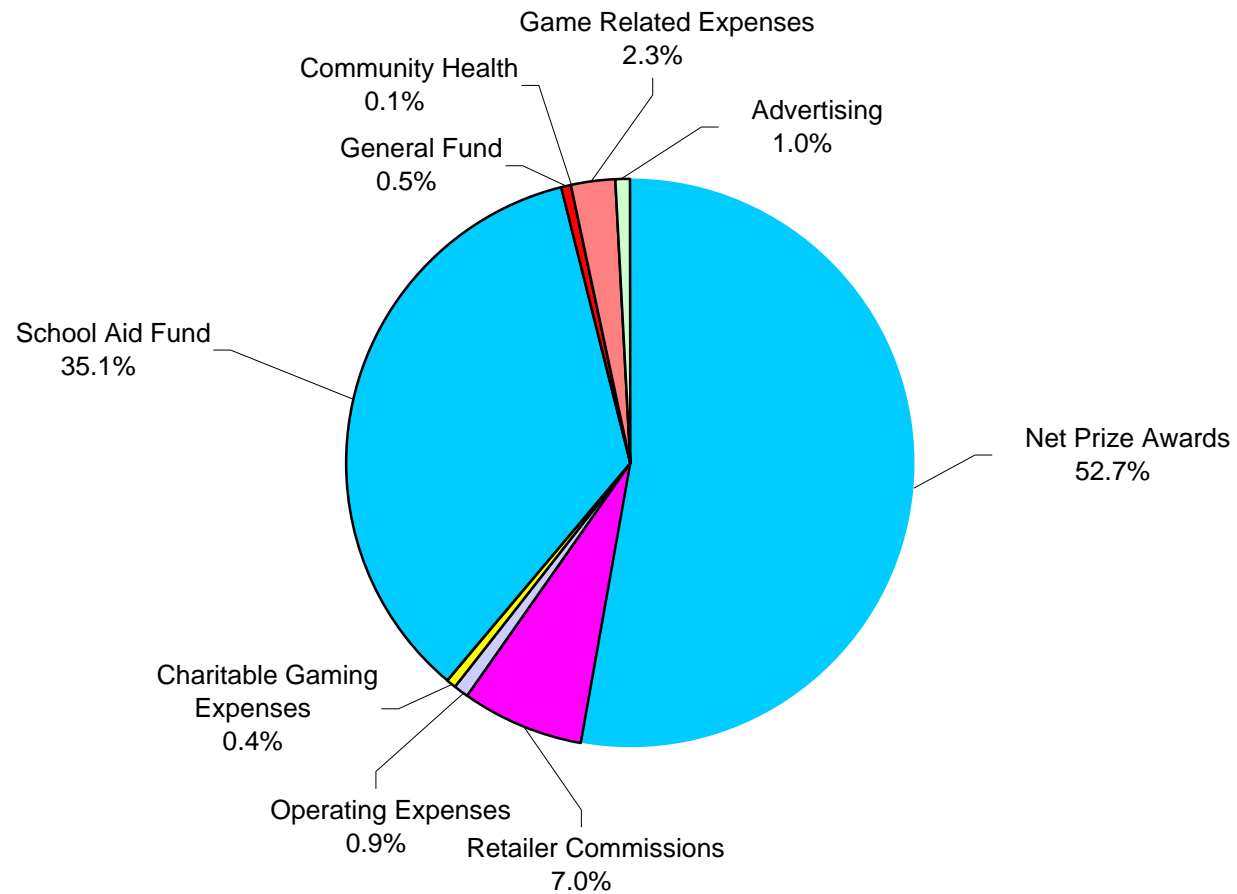


**Bureau of State Lottery, State of Michigan**  
**Expenses and Transfers to the State's School Aid Fund, General Fund, and Department of Community Health**  
**Fiscal Years 1996 through 2005**

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
<b>EXPENSES</b>										
Prize Awards	\$ 752,256,691	\$ 866,458,148	\$ 892,673,699	\$ 944,507,720	\$ 920,800,127	\$ 873,324,730	\$ 918,104,561	\$ 919,221,954	\$ 1,130,843,804	\$ 1,179,642,069
Unclaimed Prizes	<u>(16,183,286)</u>	<u>(14,496,433)</u>	<u>(42,039,541)</u>	<u>(20,347,948)</u>	<u>(26,524,711)</u>	<u>(23,288,590)</u>	<u>(44,402,717)</u>	<u>(19,568,089)</u>	<u>(31,171,242)</u>	<u>(17,634,462)</u>
Net Prize Awards	736,073,405	851,961,715	850,634,158	924,159,772	894,275,416	850,036,140	873,701,844	899,653,865	1,099,672,562	1,162,007,607
Advertising	14,947,096	15,613,541	16,662,631	15,040,342	17,277,883	16,960,287	17,097,428	17,121,905	17,534,439	17,597,101
Game Related Expenses	25,053,202	26,083,697	32,308,798	44,293,754	43,063,956	41,763,462	44,090,452	45,108,711	54,145,722	56,913,640
Retailer Commissions	97,764,715	111,893,673	114,562,213	120,819,152	120,376,589	114,928,153	120,717,665	121,787,454	145,367,020	152,630,718
Operating Expenses	14,884,939	15,891,408	16,056,613	16,027,467	14,487,141	14,668,440	15,366,848	15,280,493	15,940,433	17,862,878
Charitable Gaming Expenses	<u>9,729,962</u>	<u>5,519,360</u>	<u>6,696,821</u>	<u>6,448,849</u>	<u>6,629,473</u>	<u>7,363,575</u>	<u>7,570,916</u>	<u>7,922,012</u>	<u>7,777,396</u>	<u>7,910,092</u>
<b>TOTAL EXPENSES</b>	<b><u>\$ 898,453,319</u></b>	<b><u>\$ 1,026,963,394</u></b>	<b><u>\$ 1,036,921,234</u></b>	<b><u>\$ 1,126,789,336</u></b>	<b><u>\$ 1,096,110,458</u></b>	<b><u>\$ 1,045,720,057</u></b>	<b><u>\$ 1,078,545,153</u></b>	<b><u>\$ 1,106,874,440</u></b>	<b><u>\$ 1,340,437,572</u></b>	<b><u>\$ 1,414,922,036</u></b>
<b>TRANSFERS TO THE STATE</b>										
School Aid Fund	548,319,432	587,732,972	616,109,991	621,131,480	618,513,554	587,009,374	613,530,186	586,047,631	644,882,842	667,579,438
General Fund	1,226,633	7,374,895	7,025,865	7,342,332	7,018,771	9,392,966	12,066,167	11,233,294	12,203,298	11,728,945
Community Health	<u></u>	<u></u>	<u>950,000</u>	<u>983,000</u>	<u>983,000</u>	<u>984,000</u>	<u>990,000</u>	<u>990,000</u>	<u>990,000</u>	<u>990,000</u>
<b>TOTAL TRANSFERS</b>	<b><u>\$ 549,546,065</u></b>	<b><u>\$ 595,107,867</u></b>	<b><u>\$ 624,085,856</u></b>	<b><u>\$ 629,456,812</u></b>	<b><u>\$ 626,515,325</u></b>	<b><u>\$ 597,386,340</u></b>	<b><u>\$ 626,586,353</u></b>	<b><u>\$ 598,270,925</u></b>	<b><u>\$ 658,076,140</u></b>	<b><u>\$ 680,298,383</u></b>

Transfers to Community Health began in fiscal year 1998.

**BUREAU OF STATE LOTTERY  
STATE OF MICHIGAN  
EXPENSES AND TRANSFERS  
FISCAL YEARS 1996 THROUGH 2005**



Source: Bureau of State Lottery, State of Michigan





**Bureau of State Lottery, State of Michigan**  
**Ratio of Installment Prize Awards Liability**  
**Fiscal Years 1996 through 2005**

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
<b><u>INSTALLMENT PRIZE AWARDS LIABILITY</u></b>										
Current - at face amount	\$ 121,119,575	\$ 130,913,375	\$ 132,857,975	\$ 133,239,975	\$ 110,418,093	\$ 110,074,593	\$ 109,824,593	\$ 109,581,493	\$ 103,387,928	\$ 94,716,503
Long-term - at face amount	<u>1,501,397,300</u>	<u>1,570,604,125</u>	<u>1,490,366,550</u>	<u>1,373,350,575</u>	<u>1,039,651,949</u>	<u>929,797,357</u>	<u>819,972,764</u>	<u>713,964,671</u>	<u>617,282,543</u>	<u>527,301,740</u>
Total installment prize awards	<u>\$ 1,622,516,875</u>	<u>\$ 1,701,517,500</u>	<u>\$ 1,623,224,525</u>	<u>\$ 1,506,590,550</u>	<u>\$ 1,150,070,042</u>	<u>\$ 1,039,871,950</u>	<u>\$ 929,797,357</u>	<u>\$ 823,546,164</u>	<u>\$ 720,670,471</u>	<u>\$ 622,018,243</u>
<b><u>INVESTMENTS</u></b>										
<b><u>United States Treasury zero coupon bonds: purchased to provide for the payment of future installment payments to prize winners</u></b>										
Face amount	<u>\$ 1,603,898,000</u>	<u>\$ 1,689,042,000</u>	<u>\$ 1,600,216,000</u>	<u>\$ 1,467,645,000</u>	<u>\$ 1,148,897,000</u>	<u>\$ 1,038,439,000</u>	<u>\$ 928,332,000</u>	<u>\$ 818,303,000</u>	<u>\$ 709,413,000</u>	<u>\$ 626,745,000</u>
Installment prize awards payable as a percentage of investments:	101.16%	100.74%	101.44%	102.65%	100.10%	100.14%	100.16%	100.64%	101.59%	99.25%

**Note:** Details regarding the Bureau's prize awards and investments can be found in the notes to the financial statements.



**Bureau of State Lottery, State of Michigan**  
**Demographic and Economic Information**  
**Fiscal Years 1997 through 2005**

These are the results of the Lottery's demographic general tracking study prepared biennially.

	1997	1999	2001	2003	2005
<b>Gender</b>					
Male	40%	40%	39%	50%	50%
Female	60%	60%	61%	50%	50%
<b>Education</b>					
Some high school	8%	5%	9%	7%	9%
Completed high school	39%	35%	41%	44%	36%
Some college	25%	26%	22%	18%	23%
Completed college	23%	29%	24%	26%	29%
Technical or vocation school	4%	4%	3%	3%	2%
Refused	1%	1%	1%	2%	1%
<b>Age</b>					
18 - 24 Yrs	9%	10%	5%	5%	5%
25 - 34 Yrs	21%	20%	13%	8%	8%
35 - 44 Yrs	23%	20%	21%	21%	14%
45 - 54 Yrs	23%	18%	21%	20%	19%
55 - 64 Yrs	13%	14%	18%	21%	22%
65 Yrs & over	11%	17%	20%	22%	31%
Refused	0%	1%	2%	3%	1%
<b>Marital Status</b>					
Married	57%	60%	53%	56%	59%
Single	43%	40%	47%	44%	41%
<b>Income</b>					
Under \$25,000	20%	17%	18%	21%	22%
\$25,000 - \$50,000	31%	29%	26%	25%	22%
\$50,000 - \$100,000	17%	24%	20%	25%	21%
\$100,000 or more	3%	6%	5%	4%	6%
Refused	29%	24%	31%	25%	29%
<b>Ethnicity</b>					
White	80%	81%	71%	73%	83%
Black/African-American	13%	11%	24%	17%	9%
Hispanic/Latino	1%	1%	1%	3%	1%
Other	2%	7%	3%	3%	1%
Refused	4%	3%	1%	4%	6%



**Bureau of State Lottery, State of Michigan**  
**Operating Information and Employees**  
**Fiscal Years 1996 through 2005**

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
<b>Number of Employees</b>	194	175	189	189	184	175	175	159	161	166
<b>Number of Retailers</b>										
Instant only	3,185	3,006	2,827	2,891	2,630	2,141	1,869	1,760	1,600	1,497
Club Games	-	-	-	-	-	-	-	-	1,829	2,077
On-line	5,892	6,151	6,410	6,415	6,641	7,076	7,291	7,288	7,377	7,502
Total retailers	9,077	9,157	9,237	9,306	9,271	9,217	9,160	9,048	10,806	11,076
<b>Retailer Commissions</b>	97,764,715	111,893,673	114,562,213	120,819,152	120,376,589	114,928,153	120,717,665	121,787,454	145,367,020	152,630,718
<b>Sales</b>										
Instant Tickets	472,292,640	563,851,942	605,901,617	629,941,090	643,266,961	626,680,348	655,415,025	682,703,482	690,157,728	662,533,892
Club Game Tickets									229,598,678	371,423,173
On-line Tickets	951,356,784	1,035,469,618	1,031,691,280	1,100,976,296	1,051,483,697	987,987,560	1,032,642,812	998,844,958	1,054,143,828	1,035,536,283
Total sales	1,423,649,424	1,599,321,560	1,637,592,897	1,730,917,386	1,694,750,658	1,614,667,908	1,688,057,837	1,681,548,440	1,973,900,234	2,069,493,348
<b>Prize Awards</b>										
Instant Tickets	272,957,041	338,154,272	366,006,104	379,220,060	398,201,122	392,423,315	413,526,776	428,203,637	435,572,847	417,763,784
Club Game Tickets	-	-	-	-	-	-	-	-	151,563,326	242,274,479
On-line Tickets	479,299,650	528,303,876	526,667,595	565,287,660	522,599,005	480,901,415	504,577,785	491,018,317	543,707,631	519,603,806
Total prize awards	752,256,691	866,458,148	892,673,699	944,507,720	920,800,127	873,324,730	918,104,561	919,221,954	1,130,843,804	1,179,642,069
<b>Prize Payout Percentage</b>										
Instant Tickets	57.79%	59.97%	60.41%	60.20%	61.90%	62.62%	63.09%	62.72%	63.11%	63.06%
Club Game Tickets									66.01%	65.23%
On-line Tickets	50.38%	51.02%	51.05%	51.34%	49.70%	48.67%	48.86%	49.16%	51.58%	50.18%
<b>Total Revenues</b>	1,544,265,759	1,742,124,497	1,846,837,604	1,737,283,386	1,791,928,080	1,751,691,818	1,790,969,043	1,729,663,571	2,014,005,030	2,110,839,770
<b>Total Lottery Revenues</b>	1,533,309,163	1,729,230,242	1,833,114,918	1,723,492,205	1,778,279,836	1,734,935,277	1,771,331,960	1,710,508,265	1,994,024,336	2,091,200,732
<b>Transfers to the State</b>										
School Aid Fund	548,319,432	587,732,972	616,109,991	621,131,480	618,513,554	587,009,374	613,530,186	586,047,631	644,882,842	667,579,438
<b>Percentage of total Lottery revenues transferred to the State School Aid Fund</b>	35.76%	33.99%	33.61%	36.04%	34.78%	33.83%	34.64%	34.26%	32.34%	31.92%

Source: Bureau of State Lottery, State of Michigan

Bureau of State Lottery, State of Michigan  
Industry Comparative Information

**Fiscal 2004 U.S. Lottery Sales, Profit & Expense Analysis\***

Lottery	Pop. <sup>1</sup> (Mil)	Census 2004 Statewide Personal Income <sup>2</sup>	(Millions of dollars)							PC Sales	PC Net Income	Total Revenue as % of Personal Income	Net Income as % of Personal Income	Prizes as % of Total Rev.	Exp. as % of Total Rev.	Net Income as % of Total Rev.
			Ticket Sales	Other Income	Total Revenue	Prizes	Agent Comm.	Expense	Net Income							
Arizona	5.6	161,709	366.58	0.47	367.05	202.20	24.50	33.94	106.42	\$66	\$19	0.227%	0.066%	55.1%	9.2%	29.0%
California	35.5	1,259,549	2,973.97	-197.30	2,776.67	1,566.03	205.75	165.08	839.83	\$84	\$24	0.220%	0.067%	56.4%	5.9%	30.2%
Colorado	4.6	166,093	401.25	0.16	401.41	236.60	30.26	31.73	102.82	\$88	\$23	0.242%	0.062%	58.9%	7.9%	25.6%
Connecticut	3.5	159,030	907.66	0.56	908.22	538.33	50.50	38.48	280.91	\$261	\$81	0.571%	0.177%	59.3%	4.2%	30.9%
Delaware <sup>3</sup>	0.8	29,114	108.61		108.61	53.19	6.60	12.28	36.54	\$133	\$45	0.373%	0.126%	49.0%	11.3%	33.6%
D.C.	0.6	28,252	241.13	0.32	241.45	122.32	15.01	30.61	73.51	\$428	\$130	0.855%	0.260%	50.7%	12.7%	30.4%
Florida	17.0	541,273	3,070.96	-133.71	2,937.25	1,724.49	174.39	136.09	902.28	\$180	\$53	0.543%	0.167%	58.7%	4.6%	30.7%
Georgia	8.7	269,662	2,549.54	-10.78	2,538.76	1,480.30	177.99	113.53	766.93	\$294	\$88	0.941%	0.284%	58.3%	4.5%	30.2%
Idaho	1.4	37,385	109.32	0.12	109.44	64.73	6.31	14.01	24.39	\$80	\$18	0.293%	0.065%	59.1%	12.8%	22.3%
Illinois	12.7	441,255	1,687.58	25.51	1,713.09	973.83	85.39	85.72	568.15	\$133	\$45	0.388%	0.129%	56.8%	5.0%	33.2%
Indiana	6.2	189,487	734.87	1.04	735.91	436.53	50.33	49.73	199.32	\$119	\$32	0.388%	0.105%	59.3%	6.8%	27.1%
Iowa	2.9	89,970	208.53	1.94	210.47	114.46	13.30	27.30	55.41	\$71	\$19	0.234%	0.062%	54.4%	13.0%	26.3%
Kansas	2.7	84,716	224.46	1.00	225.45	120.78	12.93	21.08	70.68	\$82	\$26	0.266%	0.083%	53.6%	9.3%	31.3%
Kentucky	4.1	114,601	725.25	-17.65	707.61	439.19	45.13	48.02	175.28	\$176	\$43	0.617%	0.153%	62.1%	6.8%	24.8%
Louisiana	4.5	123,556	340.09	0.40	340.49	169.78	18.66	30.45	121.59	\$76	\$27	0.276%	0.098%	49.9%	8.9%	35.7%
Maine	1.3	39,947	185.87	2.44	188.32	114.89	13.61	17.29	42.53	\$142	\$33	0.471%	0.106%	61.0%	9.2%	22.6%
Maryland	5.5	218,614	1,395.41		1,395.41	795.17	91.30	50.56	458.37	\$253	\$83	0.638%	0.210%	57.0%	3.6%	32.8%
Massachusetts	6.4	268,122	4,368.39	13.39	4,381.78	3,148.46	248.08	73.23	912.01	\$679	\$142	1.634%	0.340%	71.9%	1.7%	20.8%
Michigan	10.1	326,168	1,973.90	-3.47	1,970.43	1,099.67	145.37	95.40	630.00	\$196	\$62	0.604%	0.193%	55.8%	4.8%	32.0%
Minnesota	5.1	181,793	386.92	0.46	387.38	225.53	22.81	38.33	100.71	\$76	\$20	0.213%	0.055%	58.2%	9.9%	26.0%
Missouri	5.7	174,256	791.15	6.58	797.73	484.83	49.32	40.96	222.63	\$139	\$39	0.458%	0.128%	60.8%	5.1%	27.9%
Montana	0.9	25,215	36.74	0.02	36.75	18.68	2.09	7.87	8.12	\$40	\$9	0.146%	0.032%	50.8%	21.4%	22.1%
Nebraska	1.7	55,418	92.61	0.45	93.06	52.61	5.63	15.02	19.80	\$53	\$11	0.168%	0.036%	56.5%	16.1%	21.3%
N. Hampshire	1.3	47,640	237.01	2.62	239.63	137.15	12.81	15.58	74.09	\$184	\$58	0.503%	0.156%	57.2%	6.5%	30.9%
New Jersey	8.6	362,430	2,188.40	43.77	2,232.16	1,239.74	121.00	73.06	798.36	\$253	\$92	0.616%	0.220%	55.5%	3.3%	35.8%
New Mexico	1.9	50,702	148.65	-6.05	142.60	78.88	10.13	17.65	35.94	\$79	\$19	0.281%	0.071%	55.3%	12.4%	25.2%
New York	19.2	732,681	5,847.50	-15.83	5,831.67	3,306.34	355.66	230.85	1,938.83	\$305	\$101	0.796%	0.265%	56.7%	4.0%	33.2%
N. Dakota	0.6	19,650	05.77	0.27	6.04	2.79	0.29	1.29	1.67	\$9	\$3	0.031%	0.008%	46.2%	21.4%	27.6%
Ohio	11.4	359,839	2,154.72	-69.97	2,084.75	1,275.99	132.77	97.67	578.32	\$188	\$51	0.579%	0.161%	61.2%	4.7%	27.7%
Oregon <sup>3</sup>	3.6	108,350	362.30	-0.59	361.71	232.12	31.88	27.62	70.08	\$102	\$20	0.334%	0.065%	64.2%	7.6%	19.4%
Pennsylvania	12.4	411,274	2,352.07	18.25	2,370.33	1,305.86	121.89	125.32	817.25	\$190	\$66	0.576%	0.199%	55.1%	5.3%	34.5%
R. Island <sup>3</sup>	1.1	36,147	249.40	1.31	250.71	148.40	30.54	7.56	64.21	\$232	\$60	0.694%	0.178%	59.2%	3.0%	25.6%
S. Carolina	4.1	114,270	950.01	2.78	952.79	552.29	66.95	43.42	290.13	\$229	\$70	0.834%	0.254%	58.0%	4.6%	30.5%
S. Dakota <sup>3</sup>	0.8	23,175	34.14	0.42	34.56	19.13	1.86	5.42	8.14	\$45	\$11	0.149%	0.035%	55.4%	15.7%	23.6%
Texas	22.1	680,409	3,487.92	1.02	3,488.94	2,068.64	176.56	180.82	1,062.92	\$158	\$48	0.513%	0.156%	59.3%	5.2%	30.5%
Vermont	0.6	20,106	92.38	-0.14	92.24	57.59	5.39	9.34	19.92	\$149	\$32	0.459%	0.099%	62.4%	10.1%	21.6%
Virginia	7.4	264,707	1,262.36	4.65	1,267.01	720.21	70.65	68.08	408.05	\$171	\$55	0.479%	0.154%	56.8%	5.4%	32.2%
Washington	6.1	215,260	481.44	-47.02	434.42	295.49	30.34	36.03	72.56	\$79	\$12	0.202%	0.034%	68.0%	8.3%	16.7%
W. Virginia <sup>3</sup>	1.8	47,339	206.87	-6.40	200.47	123.26	14.46	21.16	41.58	\$114	\$23	0.423%	0.088%	61.5%	10.6%	20.7%
Wisconsin	5.5	176,898	482.94	-9.85	473.09	275.18	33.88	33.35	130.68	\$88	\$24	0.267%	0.074%	58.2%	7.0%	27.6%
<b>Total</b>	<b>255.9</b>	<b>8,656,062</b>	<b>44,424.7</b>	<b>-388.83</b>	<b>44,035.8</b>	<b>26,021.6</b>	<b>2,712.3</b>	<b>2,170.9</b>	<b>13,130.9</b>	<b>\$174</b>	<b>\$51</b>	<b>0.509%</b>	<b>0.152%</b>	<b>59.1%</b>	<b>4.9%</b>	<b>29.8%</b>

<b>VLTs (only)</b>																
Delaware <sup>4</sup>	0.8	29,114	532.31		532.31		254.94	30.00	247.38	\$651	\$303	1.828%	0.850%		5.6%	46.5%
Oregon <sup>4</sup>	3.6	108,350	8,587.58		8,587.58	8,056.62	169.09	40.31	321.57	\$2,413	\$90	7.926%	0.297%	93.8%	0.5%	3.7%
R. Island <sup>4</sup>	1.1	36,147	1,231.23		1,231.23	872.28	141.39		217.56	\$1,144	\$202	3.406%	0.602%	70.8%		17.7%
S. Dakota <sup>4</sup>	0.8	23,175	630.33	1.19	631.51	413.57	108.38	1.55	108.01	\$825	\$141	2.725%	0.466%	65.5%	0.2%	17.1%
W. Virginia <sup>4</sup>	1.8	47,339	12,471.45		12,471.45	11,374.88	615.19	10.82	470.57	\$6,889	\$260	26.315%	0.994%	91.2%	0.1%	3.8%
<b>Total</b>	<b>7.2</b>	<b>244,125</b>	<b>23,452.90</b>	<b>1.19</b>	<b>23,454.08</b>	<b>20,717.35</b>	<b>1,288.97</b>	<b>82.67</b>	<b>1,365.09</b>	<b>\$3,253</b>	<b>\$189</b>	<b>9.607%</b>	<b>0.559%</b>	<b>88.3%</b>	<b>0.4%</b>	<b>5.8%</b>

<b>Total</b>	<b>255.94</b>	<b>8,656,062</b>	<b>67,877.56</b>	<b>-387.64</b>	<b>67,489.92</b>	<b>46,738.99</b>	<b>4,001.29</b>	<b>2,253.61</b>	<b>14,496.03</b>	<b>\$265</b>	<b>\$57</b>	<b>0.780%</b>	<b>0.167%</b>	<b>69.3%</b>	<b>3.3%</b>	<b>21.5%</b>
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\* Fiscal year ends June 30 except New York (March 31), Texas (August 31) and D.C. and Michigan (Sept. 30). <sup>1</sup> Source: U.S. Census Bureau; <sup>2</sup> Source: U.S. Department of Commerce

<sup>3</sup> This data represents only revenue from traditional lottery games. <sup>4</sup> This data represents revenue from VLT operations.

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See page 246 for definitions integral to the Lottery Sales, Profit & Expense Analysis

Source: LaFleur's 2005 World Lottery Almanac

Bureau of State Lottery, State of Michigan  
Industry Comparative Information

# U.S. lotteries' fiscal 2004 sales by game\*

(in \$millions)				Online Games								Total Sales	PC Sales	VLT (net)	Prizes <sup>1</sup>	Gov't Transfer
Lottery	Pop. (M)	Instant	Pulltab	3-digit	4-digit	Lotto	Cash Lotto	Bloc Lotto	Hot Lotto	Keno	Other					
Arizona	5.7	183.25		6.85		34.03	9.67	132.78				366.58	\$64		202.20	105.86
California	35.9	1,338.98		124.92		1,116.95	166.50			167.99	8.64	2,923.97	\$81		1,566.03	1,044.06
Colorado	4.6	260.90				40.81	14.51	85.03				401.25	\$88		236.60	104.07
Connecticut	3.5	558.01		105.29	73.02	34.20	41.28	95.86				907.66	\$259		538.33	280.76
Delaware <sup>1,2</sup>	0.8	25.01		27.97	16.71	8.89		30.03				108.61	\$131	532.31	53.19	283.92
D.C.	0.6	38.94		69.51	71.59		8.51	40.87	1.36	9.71	0.65	241.13	\$435		122.32	73.50
Florida	17.4	1,358.07		349.23	192.58	785.42	259.73				125.94	3,070.96	\$177		1,724.49	1,051.66
Georgia	8.8	1,556.71		596.92	171.85	76.11	74.70	186.03		47.18	0.97	2,710.46	\$307		1,480.30	782.72
Idaho	1.4	68.62	1.17	1.15		2.79		35.60				109.32	\$78		64.73	25.00
Illinois	12.7	759.60		308.86	166.75	117.23	99.64	226.50			9.00	1,687.58	\$133		973.83	576.06
Indiana	6.2	422.10	18.97	31.11	30.47	69.58	8.50	154.14				734.87	\$118		436.53	195.76
Iowa	3.0	95.26	25.53	6.33	1.66		4.43	65.97	7.72		1.64	208.53	\$71		114.46	55.79
Kansas	2.7	87.48	4.25	5.30		2.11	28.58	56.80		39.74	0.19	224.46	\$82		120.78	70.22
Kentucky	4.1	357.02	28.70	126.01	33.73	23.89	19.86	133.89			2.15	725.25	\$175		439.19	193.48
Louisiana	4.5	111.43		47.45	23.69	33.12	6.13	118.28				340.09	\$75		169.78	121.20
Maine	1.3	150.55		6.20	4.77		3.44	20.92				185.87	\$141		114.89	42.53
Maryland	5.6	355.02		290.75	209.21	36.18	21.24	90.31	389.80	2.90		1,395.41	\$251		795.17	458.37
Massachusetts	6.4	2,977.73	2.25		362.52	108.17	46.20	96.00	775.52			4,368.39	\$681		3,148.46	912.01
Michigan	10.1	690.16	25.08	423.26	310.18	66.57	32.57	206.62	219.37	0.09		1,973.90	\$195		1,099.67	644.88
Minnesota	5.1	215.70		13.30			24.60	117.50	10.40		5.40	386.90	\$76		225.53	100.71
Missouri	5.8	434.79	21.85	53.95	18.44	35.02	24.34	147.23	51.53	4.02		791.15	\$137		484.83	229.43
Montana	0.9	10.38				2.33	4.19	16.97	2.43		0.44	36.74	\$40		18.68	8.12
Nebraska	1.7	46.28				2.13	9.53	34.67				92.61	\$53		52.61	20.59
N. Hampshire	1.3	157.02		11.34		10.41	3.33	52.65	2.26			237.01	\$182		137.15	73.74
New Jersey	8.7	973.63		452.46	261.85	130.78	115.43	251.30		2.95		2,188.40	\$252		1,239.74	794.97
New Mexico	1.9	87.02		2.09			8.07	51.47				148.65	\$78		78.88	35.94
New York	19.3	2,733.94		757.53	592.76	356.43	363.11	474.43	534.31	13.20		5,825.71	\$302	22.00	3,306.34	1,907.40
N. Dakota <sup>3</sup>	0.6							5.66	0.11			5.77	\$9		2.79	1.57
Ohio	11.5	1,166.02		396.75	165.23	143.83	66.58	191.78		24.53		2,154.72	\$188		1,275.99	655.61
Oregon <sup>1,2</sup>	3.6	132.73	2.63		1.38	46.47		45.98	116.48	16.63		362.30	\$101	530.97	232.12	380.58
Pennsylvania	12.4	989.20		438.35	265.23	126.27	225.11	307.91				2,352.07	\$190		1,305.86	817.25
R. Island <sup>1,2</sup>	1.1	76.52		29.68			3.76	50.87	88.33	0.24		249.40	\$231	358.87	148.40	281.14
S. Carolina	4.2	537.34		109.10	48.59		22.79	232.19				950.01	\$226		552.29	286.75
S. Dakota <sup>1,2</sup>	0.8	15.26				1.67	1.54	14.50	1.16			34.14	\$44	216.76	19.13	115.77
Tennessee <sup>4</sup>	5.9	361.86		26.04				39.79				427.69	\$72		216.97	123.27
Texas	22.5	2,323.88		277.25		477.82	122.38	235.43		49.16		3,485.92	\$155		2,068.64	1,051.04
Vermont	0.6	68.80		1.62	1.29		1.37	19.30				92.38	\$149		57.59	19.62
Virginia	7.5	630.93		241.43	156.93	73.00	28.04	132.03				1,262.36	\$169		720.21	407.70
Washington	6.2	277.99		17.31		90.26	21.64	55.19	6.70	12.35		481.44	\$78		295.49	117.58
W. Virginia <sup>1,2</sup>	1.8	109.84		9.39	4.54		6.19	63.37	2.58	10.95		206.86	\$114	1,096.57	123.26	512.14
Wisconsin	5.5	266.63	3.66	23.92	10.11	20.22	50.45	107.96				482.94	\$88		275.18	131.60
Total	264.3	23,010.59	134.08	5,388.62	3,195.06	4,072.68	1,947.92	4,423.80	28.01	2,457.61	281.09	44,939.5	\$170	2,757.47	26,238.6	15,094.4
% of total		51.2%	0.3%	12.0%	7.1%	9.1%	4.3%	9.8%	0.1%	5.5%	0.6%	100.0%				

<sup>1</sup> Prizes do not include VLT prizes paid; <sup>2</sup> Denotes VLT net machine income; <sup>3</sup> Total sales period (3/20-6/30/04); <sup>4</sup> Total sales period (1/20-6/30/04)

\* Fiscal year ends June 30 for all U.S. states, except New York (March 31), Texas (August 31), D.C. and Michigan (Sept. 30)

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