

Annual Report • Fiscal Year 2001



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It is our pleasure to present the annual report on the activities of the Vermont Lottery Commission for Fiscal Year 2001. This fiscal year (FY) saw an increase in lottery sales, an even stronger “Play Responsibly” message presented to the public, the major conversion of the entire Lottery terminal system and the first year of operation with the new vendor for our online and instant game systems.

Vermont Lottery revenues increased to just over \$81 million, up 8.2% from the previous year. From profits and unclaimed prizes, \$17.5 million was sent to the state’s Education Fund (decrease of 9.8%), as \$52.2 million was returned to players in the form of prizes (increase of 11.6%) and \$4.7 million went to lottery agents as commissions on sales (increase of 8.2%). The decrease in contribution to the State Education Fund was due primarily to the needed replacement of our terminal system, and the increase in vendor fees.

The replacement of the entire Lottery terminal system started on July 2, 2000, as approximately 735 old terminals were shut down and new replacement terminals installed. While the conversion did not go as smoothly as planned, the results at year-end were positive.

The Vermont Lottery continued to make internal changes during this fiscal year, with some employees doing new and different jobs. This made the Lottery more efficient and better able to serve the public and its agents. The Lottery initiated a major change in the instant ticket delivery system, moving from sales rep delivery of tickets to a courier system. The Lottery set up a warehousing system/process, and started using an outside vendor (UPS) to deliver tickets, allowing the Lottery’s marketing and sales reps to work closer with agents on the marketing of tickets.

Public awareness of the Lottery’s “Play Responsibly” program was increased during the fiscal year through a comprehensive, coordinated and focused advertising campaign. The campaign was well received by Vermonters, and received national and international recognition for its “Play Responsibly” message and “reality-based” marketing message.

When the General Assembly established the Lottery in 1977, after a statewide referendum, the Lottery’s stated purpose was to “produce the maximum amount of net revenue consonant with the dignity of the state and the general welfare of the people.” Thus the balance between providing funds to the state’s Education Fund, and a strong “Play Responsibly” program.

Over the past 23 years, the Vermont Lottery has produced over \$838 million in sales. From those sales, over \$495 million has been returned to players in the form of prizes, and over \$228 million has gone to the state’s General or Education Funds.

The staff and Commissioners of the Vermont Lottery Commission are proud of their contribution to the State of Vermont, and will work to increase that contribution in the next fiscal year.

Martha H. O’Connor, Chair

Alan R. Yandow, Executive Director

Vermont Lottery Commission

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our history

1976

In a 1976 referendum regarding the establishment of a state lottery, 66% of those casting ballots voted in favor of the proposal. Based on those results, Public Act No. 82 was enacted by the 1977 General Assembly establishing the Vermont Lottery Commission. The Act also provided for termination of the Lottery on June 30, 1980, unless the 1979 Assembly authorized continuation.

1978

The Vermont Lottery Commission was granted \$250,000 in seed money, which was subsequently paid back in full to the state eighteen months later. It took the Lottery seven months from the inception of the Commission to produce its first ticket, Green Mountain Game, which went on sale to the public on February 14, 1978. The game was based on a weekly drawing of numbers matched to preprinted numbers on game tickets. The Lottery's first instant ticket, Scratch 'N Match, went on sale to the public on June 20, 1978.

1979

A steady rise in lottery ticket sales resulted in approval by the 1979 legislature to continue the mission of the Vermont Lottery. Authorization providing for indefinite continuation of the Vermont Lottery was subsequently passed by the 1981 General Assembly.

1998

Since its inception, all profits generated by the Vermont Lottery were dedicated for use by the state's General Fund. In July 1998, the Vermont legislature mandated that all profits from the lottery go to the state Education Fund.

2001

The Vermont Lottery continues to be run by a small, efficient staff of professionals consisting of twenty full-time employees and five commissioners. It is still one of the smallest staffs of any lottery in the United States, yet it generated \$81.2 million in ticket revenue during FY2001 or \$4.06 million per employee.

The Vermont Lottery Commission consists of five members appointed by the governor with the advice and consent of the senate. The members are appointed for a three-year term and may not have any pecuniary interest in any contract awarded pursuant to Chapter 14 of Title 31V.S.A. The Commission is responsible for the public oversight and policies of the state lottery, and no more than three Commission members may belong to the same political party.

products summary

Instant Games

In Fiscal Year 2001, the Vermont Lottery offered four products to customers:

Instant Tickets, Tri-State Megabucks, Tri-State WinCash and the Tri-State Daily Numbers Games (Pick 3 and Pick 4). Each game provides fun and entertainment to a broad customer base by offering different odds, play styles, prize levels and top prizes.



Instant Games are sold at all Vermont Lottery agent locations. This product is a paper ticket with a latex-covered play area that, when scratched, instantly reveals if a player has won. In FY01, instant tickets accounted for 83% of total lottery product sales. Instant games continue to grow in popularity and create the largest revenue for the Vermont Lottery. Multiple games are on the market at any given time offering players a variety of play styles, prize levels, top prizes and themes. In FY01, instant ticket prizes ranged from \$1 to \$100,000; other top prizes included campers, snow machines and cruises.

The prize payout, which is the percentage of money that goes back to the player in the form of prizes, ranged from 65% to 75%, with an overall payout of 67%. This translates to approximately \$45 million won in prizes for the instant product in FY01.

The Vermont Lottery released 49 instant games in FY01. Of those games, 24 were \$1 games, 15 were \$2 games, five were \$3 games, four were \$5 games and one was a \$10 holiday game. Eighteen to 22 instant games were on the market simultaneously throughout FY01. A broad mix of price points, themes and play styles were offered to provide fun and entertainment to a broad consumer base.

Tri-State Megabucks

Vermont, New Hampshire and Maine formed Tri-State Megabucks in 1985.



Megabucks has transformed many times since 1985 to create the game that customers enjoyed in FY01. When the first draw was held on September 3, 1985, Megabucks was a six number out of 30 number matrix with jackpot odds of one in 593,775. A jackpot winner was paid in 20 annual installments. There was one draw per

week which was held on Saturday night. The draw was shown on live television.

In January 1986, the Megabucks game was changed to a six number out of 36 number matrix. The odds of winning the jackpot increased to one in 1.9 million. The draw was still held on Saturday night. In January 1988, the matrix was increased to six numbers out of 40 numbers, which increased the jackpot odds to one in 3.8 million. One draw was held weekly on Saturday night. In May, 1990, the number of draws increased to twice a week, Wednesday and Saturday. The draws continued to be aired on live television. In June, 1996, Megabucks was enhanced to include a one-time-only, lump sum cash payment option. This allowed jackpot winners to take their share of the money available in the jackpot prize pool in a one-time-only, lump sum payment. The cash option was about half of the estimated annuitized jackpot amount.

In March 1997, Megabucks changed again. This is the format that was available to players in FY01. The matrix changed to six numbers out of 42 numbers and included a seventh number, called the bonus number. The bonus number was drawn after the first six numbers were drawn. This seventh number offered four more prize levels by creating another way for players to match their numbers to the numbers drawn. The odds of winning the jackpot changed to one in 5.2 million. The number of jackpot payments increased from 20 to 25 annual installments. The cash option remained as a jackpot payment option at approximately half of the estimated annuitized jackpot amount. Either payment option had to be determined by the player at the time of purchase. In FY01 Megabucks draws were held at New Hampshire Lottery headquarters on Wednesday and Saturday at 7:59 PM. Draws were not aired on television. Jackpot levels started at a guaranteed annuitized \$500,000 and went as high as \$6.7 million.

Vermont had one Megabucks jackpot winner in FY01 – 20% of the five jackpot winners in the Tri-State region. The total Megabucks jackpot dollars won by Vermont players in FY01 came to \$1,384,212 or 10% of the total Megabucks jackpot dollars won in the Tri-State region. Vermont's percentage of Megabucks sales in FY01 was 19%. The total number of Megabucks jackpot winners in Vermont since the game's inception is 72 or 19% of the total

winners in the Tri-State region. Megabucks jackpot dollars won in Vermont since the game began in 1985 is \$120,424,635 or 16% of total Megabucks jackpot dollars won in the Tri-State region.

Tri-State WinCash

WinCash is the Tri-State secondary cash lotto game. It replaced Tri-State 5 Card Cash in September 1997. WinCash has a matrix of six numbers out of 36 numbers.



The top prize is a rolling jackpot that starts at a guaranteed \$50,000. The odds of winning the jackpot are one in 1.9 million. The first draw was held on September 12, 1997. Draws were held on Tuesday and Friday night at 6:46 PM. This was the first Tri-State game in which draws were not aired on television.

In FY01, there were five WinCash winners in the Tri-State region. Twenty percent or one of those five was a Vermont winner. FY01 WinCash jackpot dollars won in Vermont for this game totaled \$968,515 or 33% of total WinCash jackpot dollars won in the Tri-State region. Vermont's percentage of WinCash sales in FY01 was 20%. The total number of WinCash jackpot winners in Vermont since the game began in 1997 is six or 33% of the total WinCash jackpot winners in the Tri-State region. Since the game's inception, WinCash jackpot dollars won in Vermont totals \$7,655,764 or 57% of total WinCash jackpot dollars won in the Tri-State region.

Tri-State Daily Numbers

Pick 3 was Vermont's first online game. It began on November 10, 1980. Pick 4 began on September 3, 1985. The Daily Numbers games became Tri-State games on June 25, 1995. These games were drawn every night from Monday through Saturday at 6:59 PM. On June 7, 1998, a Sunday draw was added. In September 1998, front pair/back pair was added to the game. In FY01, the draws were not aired on live television.



Pick 3 is played by selecting a combination of three numbers from zero to nine. Pick 4 is played by selecting four numbers from zero to nine. The amount won depends on the amount played. Prizes range from \$25 to \$25,000.

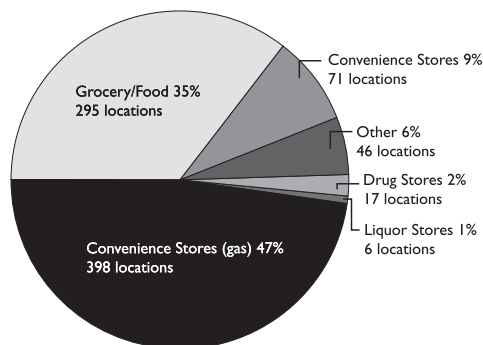
Tri-State Drawings

In 1997, Tri-State draws were no longer aired on live television. All drawing equipment was moved from WMUR TV in Manchester, NH (where the draws were previously held) to the New Hampshire Lottery's draw room in Concord, NH. The New Hampshire Lottery draw room was built specifically for conducting drawings. When Tri-State draws were conducted in FY01 the following Tri-State employees were present: draw supervisor, draw monitor, independent auditor and law enforcement official. All draws were recorded utilizing the following recording devices: 8 mm camera, VHS recorder and 24-hour surveillance camera. After each drawing, the 8 mm footage was stored in a secure off-site facility, where it remains for 14 months.

In FY01 the Vermont Lottery provided Tri-State winning numbers on the following television stations: WVNY 22 (ABC) and WNNE 31 (NBC).

Sales by Agent Summary

Through June 30, 2001 there were 833 lottery sales agents in Vermont. Of those agents, 562 (total throughout the fiscal year) sold Tri-State products, which included Tri-State Megabucks, Tri-State WinCash and Tri-State Daily Numbers Games. Total agents by category were:



Agents received 5.75% of their lottery ticket sales plus a 1% bonus for selling winning tickets of \$500 and up (agent bonus capped at \$30,000). In FY01, the commission and bonuses paid to agents totaled \$4.7 million.

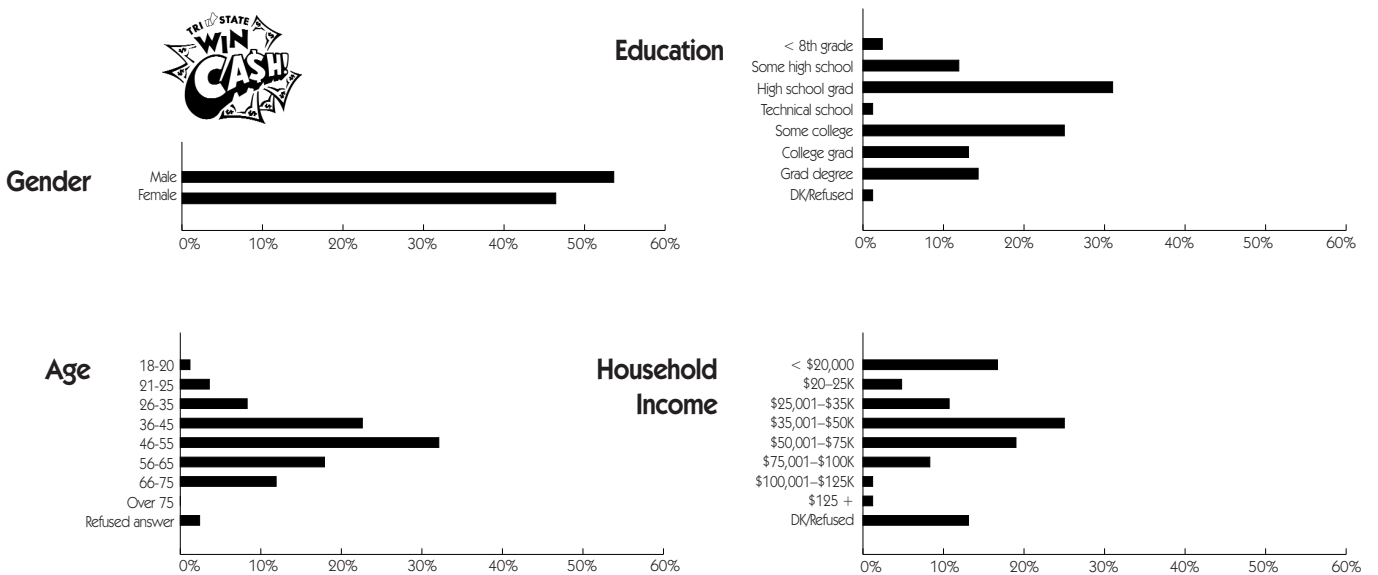
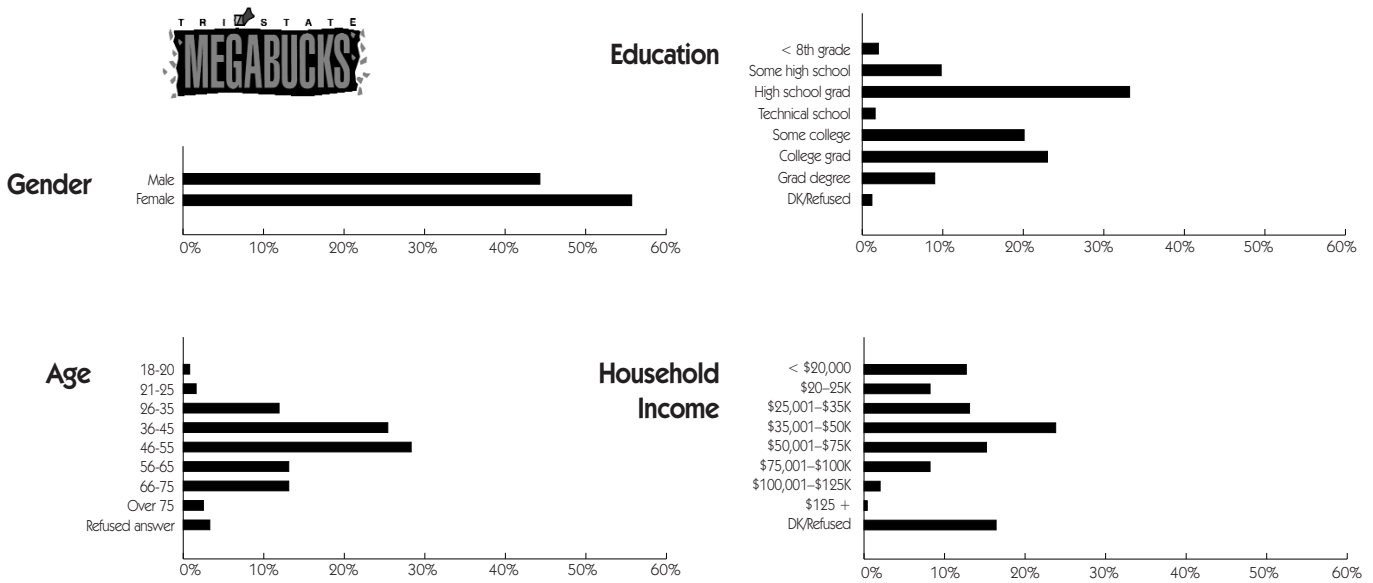
Top Five Agents in FY01 Commission Earned

1. \$32,649
2. \$23,901
3. \$22,998
4. \$22,967
5. \$22,681

players profiles

During 1999 the Vermont Lottery participated in a Public Attitudes Awareness Study to gain an understanding of who is playing Vermont Lottery games and why. The study analyzed the playing habits of over 300 lottery players and 300 non-lottery players.

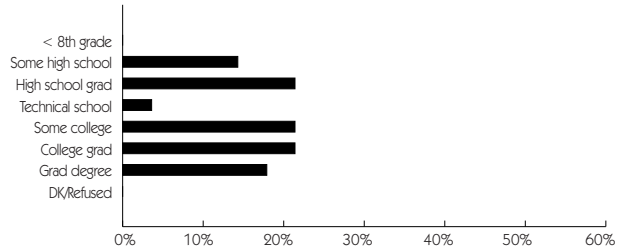
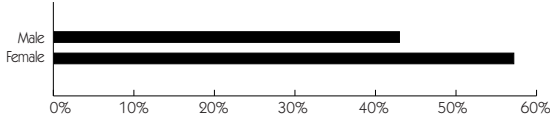
Player profiles by game type are detailed on the following charts:



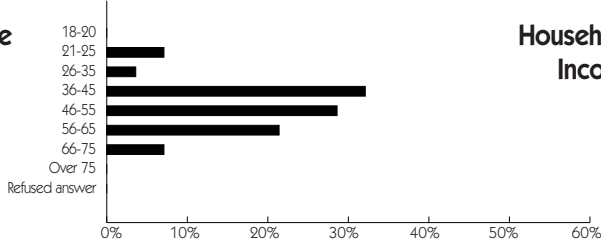


Education

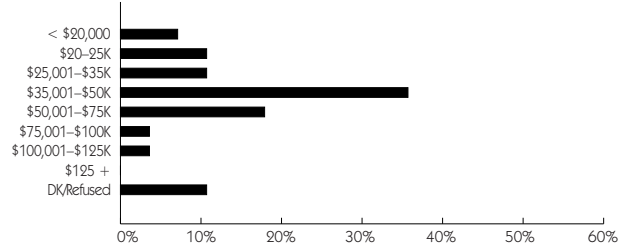
Gender



Age

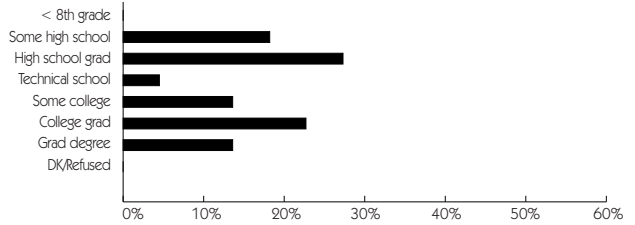
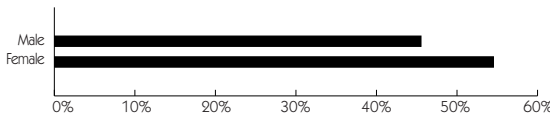


Household Income

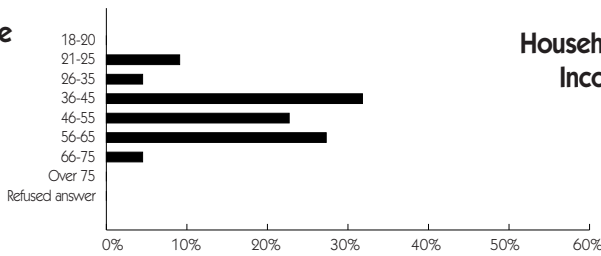


Education

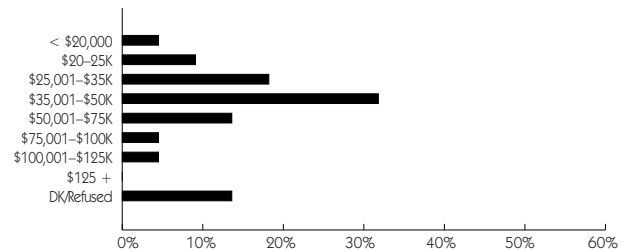
Gender



Age



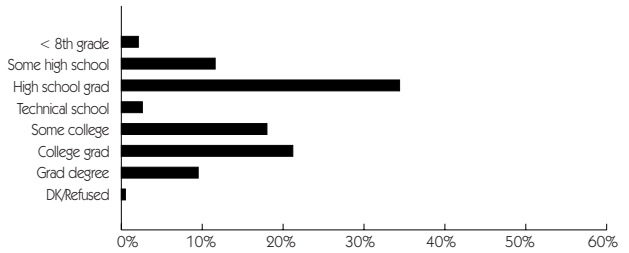
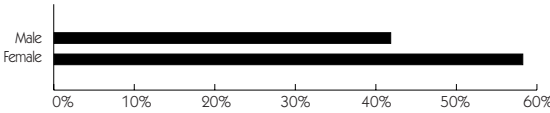
Household Income



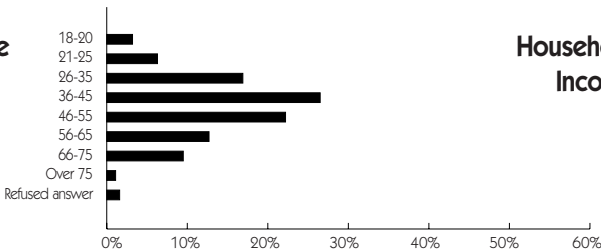
\$1 Game

Education

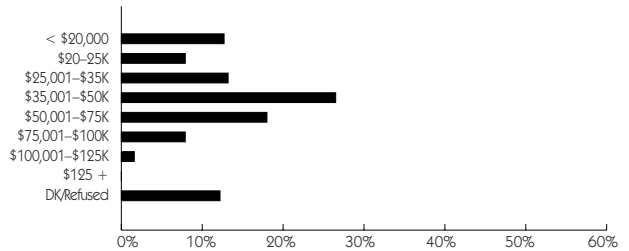
Gender



Age



Household Income

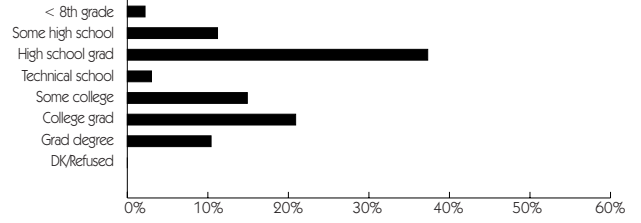
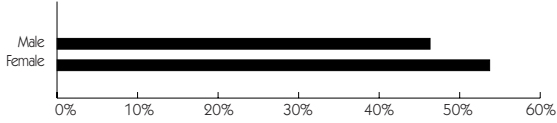




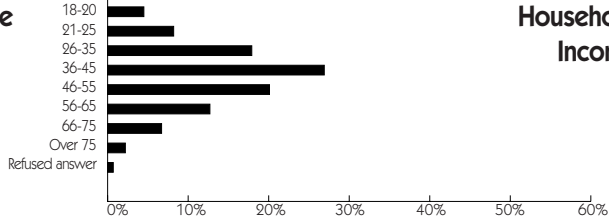
\$2 Game

Education

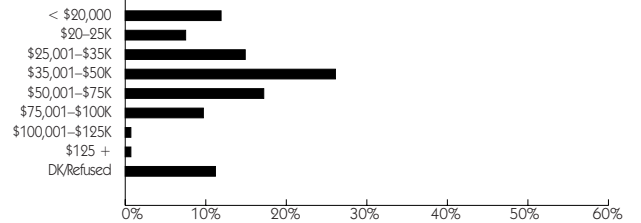
Gender



Age



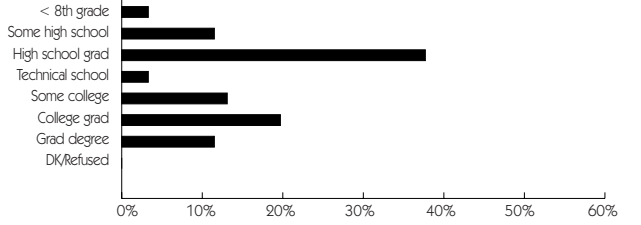
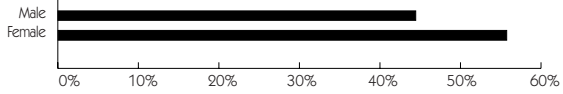
Household Income



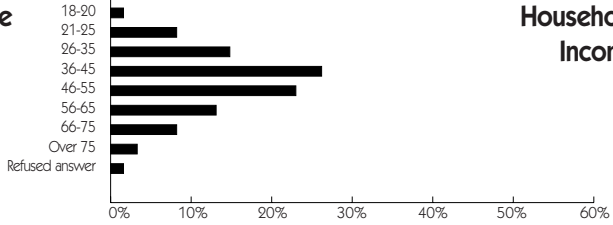
\$3 Game

Education

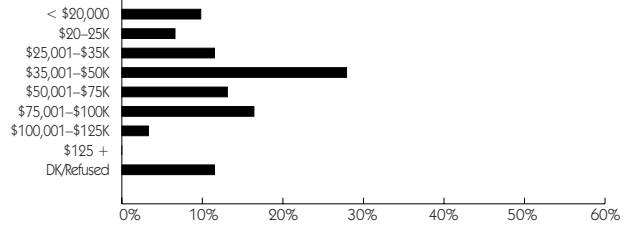
Gender



Age



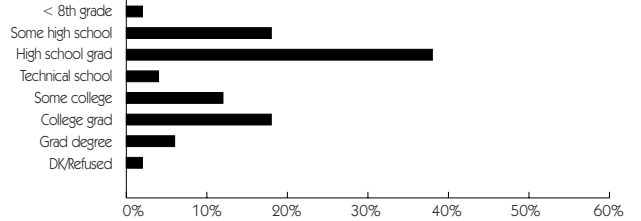
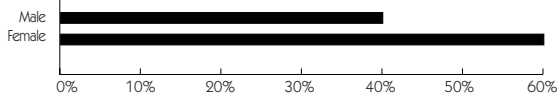
Household Income



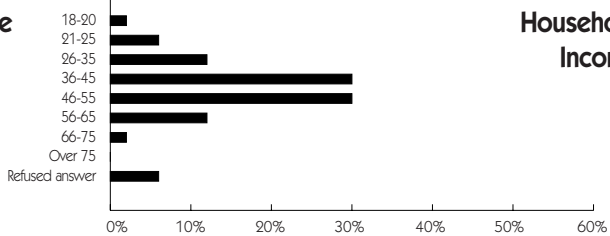
\$5 Game

Education

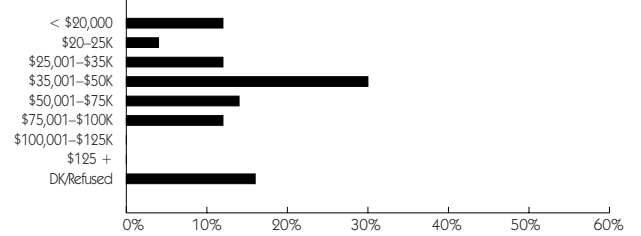
Gender



Age



Household Income



responsible gaming

Fiscal 2001

In FY97, the Vermont Lottery Commission began working with Joy Mitchell of the Brattleboro Retreat, the only Vermont-based gambling treatment program. Cooperatively, the Vermont Lottery and Ms. Mitchell developed a print campaign that received limited statewide advertising support. Stickers with the National Council on Problem Gambling's toll free number were placed on all Vermont Lottery instant ticket dispensers and/or lottery terminals.

In August 1998, Ms. Mitchell received a two-year grant that enabled her to create the Vermont Council on Problem Gambling. This organization provides 24-hour crisis intervention and referrals. The Vermont Lottery and the Vermont Council on Problem Gambling have worked together since then to build awareness of the Council and encourage responsible gambling.

The first "official" Responsible Gambling plan was developed and implemented in FY99. According to a survey done on behalf of the lottery in 1999, 27.4% of lottery players and 13.5% of non-players were aware that the Vermont Lottery Commission addressed problem gambling. Research conducted again the following year demonstrated that 74% of respondents recalled the "Play lottery games responsibly" message. The same research, conducted in 2001, showed that 85% of all respondents recalled the responsible play message. This is strong indication that the Responsible Gaming message is reaching Vermonters at a significant level.

The FY01 Responsible Gaming message was included in all advertising communications produced by the Vermont Lottery. Other notable efforts included the following:

"Straight Talk" Campaign: This campaign was designed to reach friends and family members of persons who may have problems with gambling. The schedule was supported with a one-week campaign of statewide newspaper advertising, a two-week campaign of statewide radio advertising and a poster which was prominently displayed at all lottery agent locations. Many radio stations partnered with the efforts of the Vermont Lottery and the Vermont Council by contributing additional radio time at no charge. In addition, several radio stations interviewed Alan Yandow and Joy Mitchell regarding the joint effort.

Television: A significant portion (33%) of the FY01 television budget was dedicated to creating awareness of the Vermont Lottery's "Responsible Play" campaign. A commercial spot encouraging responsible play and featuring the Vermont Council's toll free number was aired during the Lottery's FY01 television campaign. The campaign was successful in terms of increased call volume to the Vermont Council on Problem Gambling.

Media Plan: The Vermont Lottery's media plan was intended to reach individuals who have the discretionary dollars to afford participation in lottery games. The media plan for FY01 was developed recognizing two factors: 1) county per capita income; and 2) county per capita sales. This information was then weighted to distribute media weight in a manner that delivered advertising to counties best suited for lottery participation.

Print Advertising Campaign: The print campaign, "Name a product you should not buy if you need it," continued to appear in statewide publications.

"Please Play Responsibly" Message on all Advertising Media: All television and print advertising contained the "Please Play Responsibly" logo and all radio advertisements included a "Please Play Responsibly" tag or statement.

Responsible Gaming on the Web Site: Information regarding Gamblers Anonymous and other resources could be found at the Lottery's website www.vtlottery.com.

"Please Play Responsibly" Sticker: A sticker incorporating the logo and the Vermont Council's toll free number appeared in a visible location at all lottery agent locations.

Logo and Toll free Number on Lottery Tickets: The "Please Play Responsibly" logo and the Vermont Council's toll free number were printed on the back of all Vermont Lottery tickets.

18+ Message: Agents prominently displayed stickers stating, "You must be 18 or older to purchase lottery tickets."

Advertising Guidelines: Advertising guidelines developed by the Vermont Lottery were observed for all Lottery advertising.

advertising

Fiscal 2001

In FY01, the Vermont Lottery further extended its “Good. Clean. Fun.” advertising campaign, which was launched in 1999. The campaign’s central theme was crafted around a creative strategy which positioned all Vermont Lottery games as enjoyable entertainment when played in a responsible manner.

The campaign contributed to a second year of sales growth. Its consistent message was reinforced across multiple media, including network and cable television, radio and newspapers serving all 13 Vermont counties.

The Vermont Lottery’s campaign was developed in association with Communicators Group of Brattleboro.

Vermont Lottery Executive Director Alan Yandow continued in his role as campaign spokesperson, using his talents to communicate the Vermont Lottery’s spirit of responsible fun in a friendly yet serious manner.

As before, all advertising was written to avoid making unrealistic promises of winning. In fact, the commercials demonstrated in amusing ways that getting rich is quite unlikely. One TV spot compared winning Tri-State Megabucks to finding a needle in a haystack.

Advertisements for instant tickets explained that they’re not designed to make players rich, even though they do offer a “pretty good chance of winning something.” Virtually all communications materials noted the Vermont Lottery’s contribution of all profits to the Vermont Education Fund.

Once again, a special TV spot was created solely to promote responsible play, referring viewers to the Vermont Council on Problem Gambling and providing a toll free telephone number for assistance.

Responsibility isn’t just a creative message; it pervades all aspects of media planning. Vermont Lottery staff and its advertising agency have worked together to craft a media strategy that is balanced in its approach to geographic and demographic opportunities.

All indications point to a further expansion of the “Good. Clean. Fun” effort during fiscal 2002.

Executive Director

Alan Yandow continues to promote responsible play and “Good. Clean. Fun” as the Vermont Lottery’s campaign spokesperson.



results of operations from the Business Office

Fiscal Year 2001 ended with sales totaling just over \$81 million. This was an increase of 8.2% from Fiscal Year 2000. This year's operations resulted in a net profit of \$16.9 million sent to the state's Education Fund. This net profit was a decrease of 12.7% from the previous fiscal year. Adding in unclaimed prizes, the total Lottery contribution to the Education Fund was \$17.5 million (decrease of 9.8%). In addition, \$52.2 million (increase of 11.6%) was returned to players in the form of prizes, and \$4.7 million (increase of 8.2%) went to lottery agents as commissions on sales.

Sales and Operating Expenses

The overall result of sales this year shows an increase of 8.2%.

Total sales equal \$81,198,198. Ticket sales are as follows:

	2001	2000
Instant	\$67,428,182	\$60,749,467
Pick 3	\$ 1,369,058	\$ 1,326,824
Pick 4	\$ 1,113,560	\$ 978,813
Megabucks	\$ 9,479,230	\$ 9,884,948
WinCash	\$ 1,808,168	\$ 2,090,794
Total Sales	\$81,198,198	\$75,030,846

Instant ticket sales were \$67,428,182. This is an 11.0% increase over FY00. Instant ticket sales represent 83% of total sales.

Pick 3 and Pick 4 combined sales were \$2,482,618, a 7.6% increase from FY00. These games represent 3% of total sales.

Megabucks sales were \$9,479,230 this year. This is a 4.1% decrease over FY00. Megabucks sales represent 12% of total sales.

WinCash sales were \$1,808,168, a 13.5% decrease from FY00.

WinCash represents 2% of total sales.

Operating Expenses

The total cost of operations for FY01 was \$3,944,971, an increase of 31.9% or \$955,106 from last fiscal year, while administrative costs were \$1,603,943, an increase of 5% from FY00.

Overall operating expenses include personal services, lottery tickets, ticket dispensers, depreciation, supplies, equipment and facilities management fees for instant sales and all miscellaneous costs to the lottery.

Broken out from the overall operating expenses are the administra-

tive costs for the Lottery. These costs include salaries, benefits, contracted services, supplies, vehicle costs and all other costs included in the Lottery's annual budget appropriation from the Legislature. This budget appropriation comes from Lottery revenues.

Tri-State Expenses

Although Tri-State operating expenses actually declined in FY01, the facilities management fee and communication costs saw an expected increase, due to the installation and operation of a completely new terminal system. The combination of operating expenses, communication costs and facilities management fees increased the Tri-State expenses by \$2,307,893 or 132%, as anticipated. The facilities management fee will actually decline, as a percentage of sales, in years three through six of the new contract.

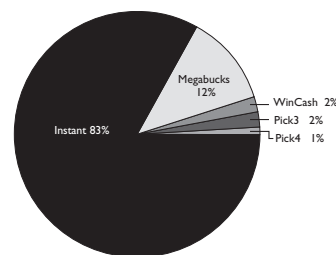
Prizes and Commissions

Overall prize expense showed an increase of 11.6%. The increase is due to an increase in sales and a slightly higher prize payout on the instant games. Our instant games were designed to pay an average of 67% of instant ticket sales. Overall commissions increased 8.2% due to the related sales increase.

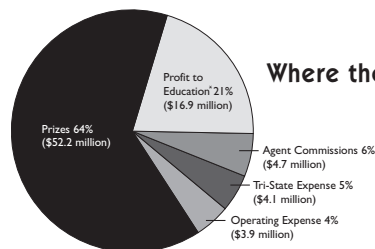
Net Profit

The net profit of \$16.9 million was a 12.7% decrease from the FY00 figure of \$19.4 million. Adding unclaimed prizes, the total Lottery contribution to the Education Fund was \$17.5 million (9.8% decrease).

Where the sales were



Where the money went



*An additional contribution of approximately \$600,000 from unclaimed prizes increased the total Profit to Education to \$17.5 million.

auditreportcontents

June 30, 2001 and 2000

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independent auditors report

Mudgett Jennett & Krogh-Wisner, P.C.

Certified Public Accountants #435

INDEPENDENT AUDITOR'S REPORT

To the Commissioners of the
Vermont Lottery Commission:

We have audited the financial statements of the Vermont Lottery Commission, an enterprise fund of the State of Vermont, as of and for the year ended June 30, 2001, as listed in the accompanying table of contents. These financial statements are the responsibility of the Vermont Lottery Commission's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Vermont Lottery Commission for the year ended June 30, 2000 were audited by other auditors whose report, dated December 8, 2000, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in "Government Auditing Standards" issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes 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 opinion.

As discussed in Note 1, the financial statements present only the Vermont State Lottery and are not intended to present the financial position of the State of Vermont and the results of its operations and cash flows of its proprietary fund types and non-expendable trust funds in conformity with generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Vermont Lottery Commission as of June 30, 2001 and the results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with "Government Auditing Standards", we have also issued our report dated September 27, 2001 on our consideration of the Vermont Lottery Commission's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with "Government Auditing Standards" and should be read in conjunction with this report in considering the results of our audit.

Montpelier, Vermont
September 27, 2001

*Mudgett, Jennett &
Krogh-Wisner, P.C.*

141 Main Street • P.O. Box 937, Montpelier, Vermont 05601 • Phone (802) 229-9193

balancesheets

vermont lottery commission
June 30, 2001 and 2000

	<u>2001</u>	<u>2000</u>
ASSETS		
Cash and cash equivalents - Note 2	\$ 6,053,183	\$ 2,767,194
Cash with State of Vermont Treasurer - Note 3	(4,877,739)	(1,533,009)
Investments - Note 4	4,646,719	3,175,536
Accounts receivable - Note 5	757,674	61,333
Inventory - Note 6	563,075	705,409
Property and equipment, less accumulated depreciation - Note 7	<u>157,228</u>	<u>199,468</u>
 Total assets	 <u>\$ 7,300,140</u>	 <u>\$ 5,375,931</u>

LIABILITIES AND RETAINED EARNINGS

LIABILITIES

Accounts payable - Note 8	\$ 987,392	\$ 711,130
Accrued unpaid leave	80,551	70,292
Accrued payroll	28,876	28,432
Due to State of Vermont Treasurer	300,000	300,000
Due to State Education Fund	958,039	535,078
Due to winners - Note 4	4,104,549	3,063,760
Reserve for future and unclaimed prizes - Note 9	255,456	105,327
Deferred revenue - Note 10	<u>187,746</u>	<u>176,158</u>
Total liabilities	<u>6,902,609</u>	<u>4,990,177</u>

Retained Earnings:

Reserve for encumbrances - Note 11	46,344	41,637
Unreserved	<u>351,187</u>	<u>344,117</u>
Total retained earnings	<u>397,531</u>	<u>385,754</u>

Total liabilities and retained earnings	<u>\$ 7,300,140</u>	<u>\$ 5,375,931</u>
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The accompanying notes to financial statements are an integral part of these statements.

statements of
revenues, expenses &
changes in retained earnings

vermont lottery commission
for the years ended
June 30, 2001 and 2000

	<u>2001</u>	<u>2000</u>
REVENUES:		
Ticket sales	\$ 81,198,198	\$ 75,030,846
Investment income	653,033	222,370
Agents' license fees and other receipts	42,222	7,820
Total revenues	<u>81,893,453</u>	<u>75,261,036</u>
PRIZES:		
Cash prizes	<u>52,230,445</u>	<u>46,791,511</u>
EXCESS OF REVENUE OVER PRIZES	<u>29,663,008</u>	<u>28,469,525</u>
COMMISSIONS, OPERATING EXPENSES AND TRI-STATE EXPENSES:		
COMMISSIONS - AGENTS	<u>4,696,864</u>	<u>4,339,199</u>
OPERATING EXPENSES:		
Personal services	985,126	899,296
Lottery tickets	1,403,850	722,686
Other operating expenses	560,379	496,259
Depreciation	56,472	73,148
Supplies	31,100	29,498
Instant ticket dispensers	42,068	41,735
Provision for bad debts	17,572	(10,719)
Courier system	79,142	-
Facilities management fee - instant	<u>769,262</u>	<u>737,962</u>
Total operating expenses	<u>3,944,971</u>	<u>2,989,865</u>
TRI-STATE EXPENSES:	<u>4,059,312</u>	<u>1,751,419</u>
Total commissions, operating expenses and Tri-State expenses	<u>12,701,147</u>	<u>9,080,483</u>
NET INCOME	16,961,861	19,389,042
NET PROFIT TRANSFERRED TO THE STATE OF VERMONT EDUCATION FUND - NOTE 16	(16,950,084)	(19,426,594)
RETAINED EARNINGS, beginning of year	<u>385,754</u>	<u>423,306</u>
RETAINED EARNINGS, end of year	<u>\$ 397,531</u>	<u>\$ 385,754</u>

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

statements of

cashflows

vermont lottery commission
for the years ended June 30, 2001 and 2000

	<u>2001</u>	<u>2000</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash received from sale of tickets	\$80,490,269	\$75,050,011
Cash paid for management fees, operations and other	(7,520,679)	(4,798,650)
Cash paid for prizes and agents' commissions	(55,734,561)	(50,158,995)
Cash paid to State from Lottery Fund	(16,388,385)	(18,933,759)
Cash paid to purchase investments (net)	(1,059,335)	(1,030,216)
Cash on deposit with State Treasurer	3,344,730	932,852
Cash received from other sources	9,061	7,820
Net cash provided by operating activities	<u>3,141,100</u>	<u>1,069,063</u>
 CASH FLOWS FROM INVESTING ACTIVITIES:		
Investment income	208,456	102,307
Proceeds from sale of vehicles and equipment	33,161	-
Acquisition of property and equipment	(96,728)	(82,258)
Net cash provided by investing activities	<u>144,889</u>	<u>20,049</u>
 NET INCREASE IN CASH AND CASH EQUIVALENTS		
	3,285,989	1,089,112
 CASH AND CASH EQUIVALENTS, beginning of year		
	<u>2,767,194</u>	<u>1,678,082</u>
 CASH AND CASH EQUIVALENTS, end of year		
	<u><u>\$6,053,183</u></u>	<u><u>\$2,767,194</u></u>

(page 1 of 2)

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

statements of

cashflows

vermont lottery commission
for the years ended June 30, 2001 and 2000

	<u>2001</u>	<u>2000</u>
RECONCILIATION OF NET INCOME TO NET CASH		
 PROVIDED BY OPERATING ACTIVITIES:		
Net income	\$16,961,861	\$19,389,042
Adjustments to reconcile net income to net cash provided by operating activities -		
Transfer to State of Vermont Education Fund	(16,950,084)	(19,426,594)
Depreciation	56,472	73,148
Bad debts expense	17,572	-
Loss on disposal of equipment	83,799	7,953
Investment income	(260,492)	(102,306)
(Increase) decrease in the following assets:		
Cash with State of Vermont Treasurer	3,344,730	932,852
Investments	(1,471,183)	(1,150,281)
Accounts receivable	(696,341)	6,563
Inventory	142,334	(48,742)
Increase (decrease) in the following liabilities:		
Accounts payable	276,262	94,095
Accrued unpaid leave	10,259	10,195
Accrued salaries	444	(17,383)
Due to winners	1,040,789	1,030,216
Reserve for future and unclaimed prizes	150,129	(235,132)
Deferred revenue	11,588	12,602
Due to State of Vermont Education Fund	422,961	492,835
 Net cash provided by operating activities	 <u>\$3,141,100</u>	 <u>\$1,069,063</u>

(page 2 of 2)

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



1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The Vermont Lottery Commission (the Lottery) was created by an enactment of the Vermont State Legislature and signed into law by the Governor on April 27, 1977. Title 31, Chapter 14 of the Vermont Statutes is the law under which the Lottery operates. The Lottery is an enterprise fund of the State of Vermont and is managed by a five-member Commission appointed by the Governor for three-year terms. The Commission, by law, has the authority to operate the State lottery, determine the type and forms of lottery games, set the price of lottery tickets, determine the number and size of prizes, select the ticket sales locations and may enter into agreements with another state or states to provide for the operation of the lottery. Approval of the joint fiscal committee and the Governor shall be required for such contractual agreements with other states.

Fiscal operations of the Lottery commenced in October, 1977. The Lottery's net revenue was transferred to the State of Vermont's General Fund through June 30, 1998. Beginning July 1, 1998, the Lottery's revenue is committed to funding Act 60, and its net revenue is transferred to the State of Vermont Education Fund on a monthly basis.

The Lottery entered into a compact with the states of Maine and New Hampshire known as the Tri-State Lotto. The compact was enacted to implement the operation of Tri-State Lotto, for the purpose of raising additional revenue for each of the party states. Vermont's portion of the Tri-State Lotto operations are accounted for by the Lottery.

A. Reporting entity - The Lottery is included in the State of Vermont's financial statements as an enterprise fund. In accordance with governmental accounting and financial reporting standards, there are no component units to be included within the Lottery's financial statements as a reporting agency.

B. Basis of accounting - The Lottery utilizes the accrual basis of accounting and is classified as an enterprise fund of the governmental proprietary fund type. Enterprise funds account for operations similar to private business enterprises where the intent of the Legislature is that costs are to be financed or recovered primarily through user charges, or where the Legislature has decided that periodic determination of revenue earned, expenses incurred or net income is appropriate. Under this basis of accounting and measurement focus, the Lottery applies all GASB pronouncements and FASB Statements and interpretations issued on or before November 30, 1989, except those that conflict with a GASB pronouncement.

C. Revenue recognition - Sales of instant lottery tickets are made to licensed retailers who market the tickets to the public on a commission basis. Revenue is recognized when tickets are activated by retailers. Tickets activated, but not sold by retailers, may be returned for credit.

Sales of online lottery tickets are made to licensed retailers who market the tickets through the use of computerized terminal on a commission basis. Ticket revenue is recognized weekly on drawing dates. Tickets sold in advance of future drawing dates are recorded as deferred revenue until the ticket becomes valid for a drawing.

D. Expenses - Commissions and fees for the instant and online games are recognized weekly on drawing dates. Expenses for administrative and overhead expenses of the operation of the Lottery, except agent and bank commissions, are paid from State appropriations. In addition, Vermont State Statute 658 provides that agency commissions may not exceed 5.75% of gross receipts and bank commissions may not exceed 1% of gross receipts. The statutes also provide that the Lottery must pay out no less than 50% of gross receipts as prizes.

E. Cash and cash equivalents - Cash includes amount in demand deposits as well as short-term investments with a maturity date within three (3) months of the date acquired by the Lottery except for amounts included in the investment account.

F. Investments - Investments with ready determinable fair values are reported at their fair values on the balance sheet. Unrealized gains and losses are included in investment income.

G. Property and equipment - Property and equipment are stated at cost and are recorded as a capital asset based on the nature of

financial statements

vermont lottery commission
June 30, 2001 and 2000

the item and are depreciated over the estimated useful life of the asset. Capitalized costs include freight-in, licenses, title application and any other costs required to establish the initial operation of the asset. Improvements and additions to an asset are capitalized. Maintenance and repair costs are not capitalized. Depreciation expense is calculated using the straight-line method over the estimated lives of the assets which are :

Automobile	3 years
Office furniture and equipment	3-7 years
Improvements	10-15 years

H. Compensated absences - Lottery employees are entitled to certain compensated absences based on their length of employment. Generally, compensated absences either vest or accumulate and are accrued when they are earned. Sick leave does not accrue beyond annual use.

I. Annuities - The Lottery is the owner of two annuities that were purchased for grand prizes won by two individuals in 1995. The cost of the annuities was charged against the reserve for future prizes at the time of purchase. The annuities were purchased from the following insurance company and have the following expiration dates:

Insurance Company	Annuity Expiration Date
Keyport Life Insurance Company	November 14, 2014
Keyport Life Insurance Company	December 15, 2014

J. Estimates - The preparation of financial statements in conformity with generally accepted accounting principles 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.

K. Risk management - The Lottery is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; injuries to individuals; and natural disasters. These are managed by the State of Vermont on behalf of the Lottery.

2. CASH AND CASH EQUIVALENTS:

The Lottery's cash deposits as of June 30, consisted of:

	2001		2000	
	Carrying Amount	Institutions' Balance	Carrying Amount	Institutions' Balance
Insured - FDIC	\$ 200,000	\$ 200,000	\$ 200,000	\$ 200,000
Uninsured, uncollateralized	5,853,183	5,988,440	2,567,194	2,404,744
	<u>\$ 6,053,183</u>	<u>\$ 6,188,440</u>	<u>\$ 2,767,194</u>	<u>\$ 2,604,744</u>

The difference between the balance per the bank and the balance per the books is due to deposits in transit and outstanding checks. The amount of uninsured cash varied significantly during the year due to the timing of various receipts and expenses.

financial statements

vermont lottery commission
June 30, 2001 and 2000

3. CASH WITH STATE OF VERMONT TREASURER:

Cash with the State Treasurer represents cash held by the Vermont State Treasurers' Office for the purpose of funding expenditures of the Lottery and transfers to the State of Vermont Education Fund. The expenditures are provided for by an appropriation from the State of Vermont for the operation of the Lottery. The balance in this account is reduced by transfers of net revenue of the Lottery to the State of Vermont Education Fund. There is a deficit in this account at June 30, 2001 and 2000, due to the timing of transfers out of the other cash accounts.

4. INVESTMENTS/DUE TO WINNERS:

The Lottery purchases investments in government securities that will mature in future years to pay multi-year payment prizes won by certain instant ticket winners. These are held by the Trust Department of the Chittenden Bank in Burlington, Vermont, and are reported at market value.

	<u>2001</u>	<u>2000</u>
Money Market Funds	\$ 152,000	\$ 353
U.S. Treasury Strips	3,605,788	2,248,603
	<u>\$ 3,757,788</u>	<u>\$ 2,248,956</u>

These investments are categorized to give an indication of the level of risk assumed. Category 1 includes investments that are insured or registered or for which the securities are held in the Lottery's name. Category 2 includes uninsured and unregistered investments for which securities are held by a counter party's trust department or agent in the Lottery's name. Category 3 includes uninsured and unregistered investments for which the securities are held by a counter party or by its trust department or agent, but not in the Lottery's name. All of the investments above are Category 1 investments.

The Treasury strips were purchased in the amount of the present value of payments as follows:

2002	\$ 393,459
2003	371,487
2004	349,717
2005	328,513
2006	309,637
Thereafter	<u>1,462,805</u>
	<u>\$ 3,215,618</u>

Also, included in Investments and Due to Winners is the present value of two (2) annuities purchased for the winners in the amount of \$888,931 and \$926,580 as of June 30, 2001 and 2000, respectively.

Investments and Due to Winners as of June 30, 2001 are \$4,646,719 and \$4,104,549, respectively. Investments and Due to Winners as of June 30, 2000 were \$3,175,536 and \$3,063,760, respectively.

financial statements

vermont lottery commission
June 30, 2001 and 2000

5. ACCOUNTS RECEIVABLE:

Accounts receivable at June 30 consisted of the following:

	2001	2000
Instant Agents	\$ 445,655	\$ 8,861
Instant Chains	36,162	39,067
Online Agents	265,849	347
Online Chains	27,580	13,058
Total	775,246	61,333
Less: Allowance for doubtful accounts	(17,572)	-
Net accounts receivable	\$ 757,674	\$ 61,333

6. INVENTORY:

The Lottery had inventory consisting of lottery tickets on hand and prizes valued at a cost of \$438,022 and \$125,053 at June 30, 2001, and \$602,988 and \$102,421 at June 30, 2000, respectively.

7. PROPERTY AND EQUIPMENT:

The following is a summary of changes in property and equipment during the fiscal years.

	2001					Net Property and Equipment June 30, 2001
	Balance July 1, 2000	Additions	Retirements	Balance June 30, 2001	Accumulated Depreciation	
Automobiles	\$ 231,347	\$ 69,383	\$ (119,275)	\$ 181,455	\$ (75,681)	\$ 105,774
Office furniture and equipment	249,284	27,345	(197,592)	79,037	(27,583)	51,454
	\$ 480,631	\$ 96,728	\$ (316,867)	\$ 260,492	\$ (103,264)	\$ 157,228

	2000					Net Property and Equipment June 30, 2000
	Balance July 1, 1999	Additions	Retirements	Balance June 30, 2000	Accumulated Depreciation	
Automobiles	\$ 184,728	\$ 46,619	\$ -	\$ 231,347	\$ (156,257)	\$ 75,090
Office furniture and equipment	291,384	35,639	(77,739)	249,284	(124,906)	124,378
	\$ 476,112	\$ 82,258	\$ (77,739)	\$ 480,631	\$ (281,163)	\$ 199,468

financial statements

vermont lottery commission
June 30, 2001 and 2000

8. ACCOUNTS PAYABLE:

The Lottery's accounts payable consisted of the following at June 30:

	2001	2000
Tri-State	\$ 802,582	\$ 281,376
Vendors	184,810	429,754
	<u>\$ 987,392</u>	<u>\$ 711,130</u>

9. PRIZE EXPENSE AND RESERVE FOR FUTURE AND UNCLAIMED PRIZES:

By law, the Lottery must pay a minimum of 50% of gross revenue to participants in the form of prizes. Prizes expense is calculated on the basis of total sales multiplied by an approved prize payout percentage. The reserve for future and unclaimed prizes is increased by the prize expense as calculated and reduced by the dollar value of prizes actually paid out. Unclaimed prizes can be used for special prizes, to supplement regular prizes or can be transferred to the State of Vermont Education Fund for state and local funding of public education.

For instant games, the Lottery calculated prize expense at varying percentages according to game design ranging from 64.00% to 75.22% for the year ended June 30, 2001 and 59.00% to 75.56% for the year ended June 30, 2000.

In September 1985, the states of Vermont, Maine and New Hampshire instituted Tri-State Megabucks, with a calculated prize expense of 50% of ticket sales. Megabucks ticket sales in Vermont were approximately \$9.5 million for the year ended June 30, 2001 and \$9.9 million for the year ended June 30, 2000.

In September 1997, the states of Vermont, Maine and New Hampshire began WIN Cash, replacing Tri-State 5 Card Cash, with an estimated payout of 50% of ticket sales. The sales in Vermont for the years ended June 30, 2001 and 2000 were approximately \$1.8 million and \$2.1 million, respectively.

10. DEFERRED REVENUE:

Deferred revenue consists of subscription receipts. The revenue will be recognized as the drawings are held.

11. RETAINED EARNINGS:

Encumbered retained earnings consists of monies earmarked for the following commitments at June 30:

	2001	2000
Equipment	<u>\$ 46,344</u>	<u>\$ 41,637</u>

12. APPROPRIATIONS:

The following are the cash basis appropriations compared to expenses at June 30:

	2001	2000
Appropriation	\$ 1,732,025	\$ 1,623,832
Expenditures	<u>1,685,681</u>	<u>1,549,178</u>
Variance	\$ 46,344	\$ 74,654

13. COMMITMENTS:

The Lottery is committed under a lease agreement for office space. The lease was rewritten as of July 1, 1997, for a term of five (5) years and may be renewed or extended for a further term of two (2) years at a rate which shall increase 4% each year of the renewal. The annual rent is \$79,848. The annual lease payment remaining is \$79,848 for July 1, 2002.

14. RETIREMENT PLAN:

The Vermont State Retirement System (VSRS), a defined benefit plan, covers substantially all Lottery employees except employees hired in a temporary capacity. Membership in the system is a condition of employment. The membership consists of employees who belong to the original contributory system with a contribution range of 5.1% to 6.28% of payroll (Groups A, B, C and D), vested members of the non-contributory system (Group E) as well as members of a new contributory system whose current contribution rate is 3.35% (Group F). All eligible employees of the Lottery are Group F members. The total amount of employee contributions was \$24,154. The Lottery's current year payroll for all employees totaled \$724,600 while its current year's covered payroll for the plan was \$721,017. Funding and benefit information for this plan is maintained in the aggregate, not by Agency or Commission. Additional information regarding this plan is available upon request from the State of Vermont.

15. DEFERRED COMPENSATION:

The State offers its employees a deferred compensation plan created in accordance with section 457 of the Internal Revenue Code. The plan, available to all Lottery employees, permits them to defer a portion of their current salary until future years. The deferred compensation is not available to the employees until termination, retirement, death or an unforeseeable emergency.

In compliance with Federal mandates, the Vermont State Retirement Board adopted a Plan Trust Declaration for the State of Vermont's Deferred Compensation Plan effective January 1, 1999. The Federal mandate was established to protect the assets of deferred compensation plans by requiring the assets be placed in a trust to be used for the sole purpose of plan participants. After January 1, 1999, the plan assets are no longer considered assets of the State of Vermont.

16. TRANSFER TO THE STATE OF VERMONT EDUCATION FUND:

The transfer to the State of Vermont Education Fund at June 30, 2001 consists of the amount due to the Fund for the current fiscal year only. Actual cash transfers during the year and subsequent to year end were \$17,442,919 and consist of amounts owed for June 30, 2000 (\$492,835) and 2001 (\$16,950,084).

17. CONCENTRATIONS:

The Lottery utilizes Scientific Games Corporation, a service organization, to process all its online games and generate accounting reports the Lottery uses to record this activity. The Lottery also utilizes Scientific Games Corporation to validate and settle its instant ticket lottery games. Other service providers are available; however, an interruption in service by Scientific Games Corporation could have an adverse impact on the Lottery's revenues.

18. RECLASSIFICATIONS:

Certain prior year account balances have been reclassified in these statements to be more comparable to the current year information.

independent auditors report

Mudgett Jennett & Krogh-Wisner, P.C.

Certified Public Accountants #435

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

To the Commissioners of the
Vermont Lottery Commission:

We have audited the financial statements of the Vermont Lottery Commission as of and for the year ended June 30, 2001, and have issued our report thereon dated September 27, 2001. 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.

Compliance

As part of obtaining reasonable assurance about whether the Vermont Lottery Commission's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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."

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Vermont Lottery Commission'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 assurance 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 over financial reporting that might be material weaknesses. A material weakness is a 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 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.

This report is intended solely for the information and use of management and the State of Vermont and is not intended to be and should not be used by anyone other than these specified parties.

Montpelier, Vermont
September 27, 2001

*Mudgett, Jennett &
Krogh-Wisner, P.C.*

141 Main Street • P.O. Box 937, Montpelier, Vermont 05601 • Phone (802) 229-9193