

*South Dakota*  
**LOTTERY**

**25**  
YEARS

# Annual Report



## Fiscal Year 2013

A Division of the South Dakota Department of Revenue



## FY2013 Annual Report Table of Contents

Fiscal Year 2013 Highlights.....	1
Fiscal Year 2013 Sales and Revenues.....	2
Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards.....	3
Independent Auditor's Report.....	5
Statement of Net Position.....	7
Statement of Revenues, Expenses, and Changes in Fund Net Position.....	8
Statement of Cash Flows.....	9
Notes to the Financial Statements.....	10

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# Fiscal Year 2013 Highlights

## 25th Anniversary recognizes retailers

It was time to celebrate and thank our retail partners on the occasion of the the Lottery's 25th Anniversary. One-hundred and six of our current retailers "stepped up to the challenge when the first ticket was sold in 1987," according to Executive Director Norm Lingle. Commemorative anniversary clocks were presented to each of them as a gesture of appreciation.

Two anniversary-themed scratch tickets were launched, one of which replicated the Lottery's first scratch game, Match 3. Players could also register for 25th Anniversary premium items and \$500 cash prizes.

The celebration culminated with the taking of a 25th Anniversary photo in which Lottery officials presented Governor Dennis Daugaard with a ceremonial check for \$2.13 billion, the amount of the revenue provided by the Lottery since 1987.



## Signs of success

Electronic billboards located in Sioux Falls and Rapid City were implemented to attract players' attention when lotto jackpots climb to record amounts.

New digital jackpot signs were deployed at all retailers in Fiscal Year 2013. The new signs are lighter and brighter than the previous models, are wireless and include all

five lotto games.



## Fun and games

Hot Lotto and Wild Card 2 underwent changes in their matrices, odds and prizes. The changes were implemented to drive jackpots higher, faster and increase player interest. Increased sales for both games reflected player approval of the changes.

May 18, 2013 saw the largest Powerball jackpot in history, generating nearly \$4 million in sales during the six-week run.

The \$20 instant game 50X the Money game was re-launched midway through the year with radio and television ads, web banners, posters, pennants and 4' x 8' standees. The marketing boost paid off, sparking a 40 percent sales jump in the first month of the campaign. The game offered a \$350,000 top prize, the largest in South Dakota Lottery history.



## Fiscal Year 2013 events

❑ The Lottery staff and commissioners crafted a mission statement and achieved all short-term objectives of the 2012 Strategic Plan. A second Strategic Planning meeting in May of 2013 focused on the instant and on-line products. Vendors presented information on successful product and marketing trends used in other jurisdictions for instant and on-line products. Lottery staff reported on player loyalty and marketing programs.

❑ The Lottery hired Union Gaming Analytics to conduct a review of the video lottery program and make recommendations to ensure the long term viability and sustainability of the net machine income.

## Mission Statement:

To work cooperatively with our partner licensees to promote and ensure the integrity, fairness, security and honesty of lottery games, to maximize revenues for state programs and initiatives, and to ensure the Lottery remains a viable and sustainable source of revenue and entertainment for the State of South Dakota.

Adopted on August 15, 2013

# Fiscal Year 2013 Sales and Revenues

## Instant tickets

The Lottery launched 28 new scratch tickets during Fiscal Year 2013 with price points ranging from \$1 to \$20. Top prizes ranged from \$500 to \$350,000.

Of the 605 retailers statewide, 76 percent were convenience stores, 17 percent were grocery stores, and the remaining 7 percent were restaurants, bars, liquor and drug stores.

Sales were up 2.1 percent from the previous fiscal year.

## Lotto games

South Dakota offers five lotto games. Powerball, Hot Lotto, Wild Card 2, and Mega Millions are played in multiple jurisdictions. Dakota Cash is South Dakota's very own game.

There were 593 lotto retailers operating throughout the year. Overall lotto sales were up 13 percent from the previous year. Powerball sales were up 29 percent, Mega Millions were down 34 percent. Dakota Cash sales were down 5 percent. Hot Lotto sales were up 6 percent. Wild Card 2 sales were up 21 percent.

## Video Lottery

The Lottery regulates and controls video lottery game activities through licensing procedures for the machines, machine owners, establishments, distributors, and manufacturers. The Lottery also oversees the secure central computer system and tests new terminal hardware and software.

Video lottery net revenue was up 4.5 percent from the previous year. The average number of active video lottery machines during the year was 9,133. The average number of establishments was 1,426.

Revenue from video lottery net machine income is distributed to the Property Tax Reduction Fund. A portion of machine manufacturer license fees is distributed to the General Fund.

## Sales and Revenues

Total fiscal year 2013 Lottery revenue distributed to state funds was nearly \$108 million.

	Sales	Prizes	Retailer Commissions	Revenue Distributed
Instant Tickets	\$25,298,065	\$16,213,494	\$1,421,847	\$5,621,600
Lotto Tickets	\$32,048,317	\$16,205,052	\$1,709,358	\$10,387,780
Video Lottery**	\$580,092,145	\$395,451,581	\$92,320,282	\$91,693,935
			<b>Total:</b>	<b>\$107,703,315</b>

\*\*Video lottery sales are cash in; prizes are cash out; private share of net machine income is retailer commission

	General Fund	Capitol Construction Fund	Property Tax Reduction Fund	Department of Social Services
Instant Tickets	\$5,621,600			
Lotto Tickets	\$1,400,000			
Video Lottery	\$135,000	\$8,987,780	\$91,397,079	\$161,856
<b>Totals:</b>	<b>\$7,156,600</b>	<b>\$8,987,780</b>	<b>\$91,397,079</b>	<b>\$161,856</b>



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MARTIN L. GUINDON, CPA  
AUDITOR GENERAL

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

The Honorable Dennis Daugaard  
Governor of South Dakota

and

South Dakota Lottery Commission  
State of South Dakota

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the South Dakota Lottery Fund, which comprise the statement of net position as of June 30, 2013 and 2012, and the related statements of revenues, expenses and changes in net position, and cash flows for the years then ended, and the related notes to the financial statements, and have issued our report thereon dated December 6, 2013.

Internal Control Over Financial Reporting

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

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

or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

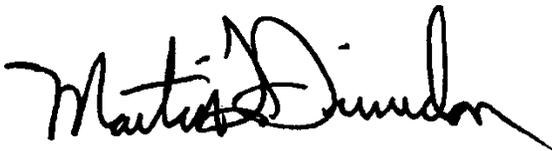
Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

#### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the South Dakota Lottery's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

#### Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. As required by South Dakota Codified Law 4-11-11, this report is a matter of public record and its distribution is not limited.



Martin L. Guindon, CPA  
Auditor General

December 6, 2013



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MARTIN L. GUINDON, CPA  
AUDITOR GENERAL

## INDEPENDENT AUDITOR'S REPORT

The Honorable Dennis Daugaard  
Governor of South Dakota

and

South Dakota Lottery Commission  
State of South Dakota

### Report on the Financial Statements

We have audited the accompanying financial statements and the related notes to the financial statements of the South Dakota Lottery Fund, an enterprise fund of the State of South Dakota, as of and for the years ended June 30, 2013 and 2012, which collectively comprise the Fund's basic financial statements as listed in the table of contents.

### Management's Responsibility for the Financial Statements

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

### Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the South Dakota Lottery as of June 30, 2013 and 2012, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As described in Note 1, the financial statements present only the financial position and changes in financial position and cash flows of the South Dakota Lottery. They do not purport to, and do not, present fairly the financial position of the State of South Dakota as of June 30, 2013 and 2012, and the changes in its financial position and its cash flows, where applicable, for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

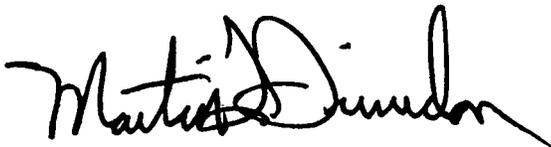
*Supplementary and Other Information*

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the South Dakota Lottery's basic financial statements. The FY2013 Highlights and FY2013 Sales and Revenues sections are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The FY2013 Highlights and FY2013 Sales and Revenues sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated December 6, 2013 on our consideration of the South Dakota Lottery's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering South Dakota Lottery's internal control over financial reporting and compliance.



Martin L. Guindon, CPA  
Auditor General

December 6, 2013

**SOUTH DAKOTA LOTTERY**  
**STATEMENT OF NET POSITION**  
*June 30, 2013 and 2012*

<b>Assets</b>	<b>2013</b>	<b>2012</b>
Current Assets:		
Cash	\$9,612,150	\$9,109,791
Restricted Cash	21,582	16,982
Total Cash	9,633,732	9,126,773
Accounts Receivable	4,403,348	4,302,225
Restricted Other Receivable	817,117	791,852
Interest Receivable	44,732	50,534
Restricted Certificates of Deposit	472,199	503,021
Total Current Assets	15,371,128	14,774,405
Noncurrent Assets:		
Capital Assets less Accumulated Depreciation/Amortization	2,549,011	2,036,471
<b>Total Assets</b>	<b>17,920,139</b>	<b>16,810,876</b>
<b>Liabilities</b>		
Current Liabilities:		
Accounts Payable	456,395	455,790
Prizes Payable	1,597,316	1,451,396
Due to the Property Tax Reduction Fund	3,460,463	3,472,901
Due to the Capital Construction Fund	2,387,780	1,905,577
Due to the General Fund	821,600	1,400,976
Due to Other Funds	66,881	81,751
Due to Other Governments		2,814
Operator Security Deposits	493,781	520,003
Escrows Payable-Reservation Sales	68,085	76,919
Accrued Liabilities	287,578	230,464
Unearned Revenue	286,082	288,771
Total Current Liabilities	9,925,961	9,887,362
Noncurrent Liabilities:		
Accrued Liabilities	144,880	121,192
<b>Total Liabilities</b>	<b>10,070,841</b>	<b>10,008,554</b>
<b>Net Position</b>		
Net Investment in Capital Assets	2,549,011	2,036,471
Restricted for MUSL Permitted Uses	817,117	791,852
Unrestricted	4,483,170	3,973,999
<b>Total Net Position</b>	<b>\$7,849,298</b>	<b>\$6,802,322</b>

The accompanying notes are an integral part of the financial statements.

**SOUTH DAKOTA LOTTERY**  
**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION**  
*For the Fiscal Years Ended June 30, 2013 and 2012*

	<b>FY2013</b>	<b>FY2012</b>
<b>Operating Revenues:</b>		
Video Lottery Revenue	\$92,320,281	\$88,322,065
Instant Ticket Sales	25,298,065	24,772,392
On-Line Ticket Sales	32,048,317	28,365,084
Terminal License Fees	1,094,600	1,105,200
Retailer License Fees	520,350	474,250
<b>Total Operating Revenue</b>	<b><u>151,281,613</u></b>	<b><u>143,038,991</u></b>
<b>Direct Game Costs:</b>		
Instant Prizes	16,213,494	14,888,496
On-Line Prizes	16,205,052	14,351,483
Instant Retail Commissions	1,421,847	1,386,613
On-Line Retail Commissions	1,709,358	1,501,390
Instant Ticket Print Costs	725,523	603,677
<b>Total Direct Costs</b>	<b><u>36,275,274</u></b>	<b><u>32,731,659</u></b>
<b>Gross Profit</b>	<b><u>115,006,339</u></b>	<b><u>110,307,332</u></b>
<b>Operating Expenses:</b>		
Personal Services and Benefits	1,627,461	1,505,032
Travel	136,859	127,024
Advertising	659,924	506,551
Contractual Services	4,396,929	4,040,991
Supplies and Materials	149,758	526,934
Depreciation/Amortization	784,060	357,426
Bad Debt Expense	1,981	3,773
Payments to Reservations	68,085	76,919
<b>Total Operating Expenses</b>	<b><u>7,825,057</u></b>	<b><u>7,144,650</u></b>
<b>Operating Income</b>	<b><u>107,181,282</u></b>	<b><u>103,162,682</u></b>
<b>Non-operating Revenues (Expenses):</b>		
Pooled Investment Income	151,658	258,364
Investment Costs	(11,232)	
Non-operating Revenue from MUSL	110,298	17,164
Miscellaneous Revenue	21,685	18,373
<b>Total Non-operating Revenue (Expenses)</b>	<b><u>272,409</u></b>	<b><u>293,901</u></b>
<b>Income Before Transfers</b>	<b><u>107,453,691</u></b>	<b><u>103,456,583</u></b>
<b>Transfers:</b>		
Transfers to the Property Tax Reduction Fund	91,397,079	87,438,844
Transfers to the General Fund	7,156,600	8,225,976
Transfers to the Capital Construction Fund	8,987,780	7,905,577
Transfers to the Department of Social Services	161,856	131,399
<b>Total Transfers</b>	<b><u>107,703,315</u></b>	<b><u>103,701,796</u></b>
<b>Special Items:</b>		
Lotto Signs Provided by Contract Extension	1,296,600	
<b>Total Special Items</b>	<b><u>1,296,600</u></b>	<b><u>0</u></b>
<b>Change in Net Position</b>	<b><u>1,046,976</u></b>	<b><u>(245,213)</u></b>
Net Position Beginning of Year	6,802,322	7,047,535
<b>Net Position End of Year</b>	<b><u>\$7,849,298</u></b>	<b><u>\$6,802,322</u></b>

The accompanying notes are an integral part of the financial statements.

**SOUTH DAKOTA LOTTERY**  
**STATEMENT OF CASH FLOWS**  
*For the Fiscal Years Ended June 30, 2013 and 2012*

	<b>FY2013</b>	<b>FY2012</b>
<b>Cash Flows from Operating Activities</b>		
Receipts from Customers and Users	\$151,168,369	\$142,791,165
Payments for Lottery Prizes	(32,228,926)	(28,917,977)
Payments to Suppliers	(8,557,799)	(7,985,404)
Payments for Interfund Services Used	(676,156)	(624,573)
Payments for Employee Services	(1,546,659)	(1,485,838)
Other Receipts (Payments)	14,828	(49,360)
Net Cash Provided (Used) by Operating Activities	<u>108,173,657</u>	<u>103,728,013</u>
<b>Cash Flows from Capital and Related Financing Activities</b>		
Purchase of Capital Assets		(6,701)
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>0</u>	<u>(6,701)</u>
<b>Cash Flows from Noncapital Financing Activities</b>		
Transfers to Other Funds	(107,812,926)	(103,020,410)
Net Cash Provided (Used) by Noncapital Financing Activities	<u>(107,812,926)</u>	<u>(103,020,410)</u>
<b>Cash Flows from Investing Activities</b>		
Pooled Investment Income	157,460	278,305
Investment Costs	(11,232)	
Net Cash Provided (Used) by Investing Activities	<u>146,228</u>	<u>278,305</u>
Net Increase (Decrease) in Cash during the Fiscal Year	506,959	979,207
Cash at Beginning of Year	9,126,773	8,147,566
Cash at End of Year	<u>\$9,633,732</u>	<u>\$9,126,773</u>
<b>Reconciliation of Operating Income to Net Cash Provided (Used) by Operating Activities</b>		
Operating Income	\$107,181,282	\$103,162,682
<b>Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided by Operating Activities:</b>		
Depreciation/Amortization Expense	784,060	357,426
Other Revenue	21,685	18,373
Non-operating Revenue from MUSL	110,298	17,164
<b>Decrease/(Increase) in Assets:</b>		
Accounts Receivable	(103,104)	(315,048)
Restricted Other Receivable	(25,265)	68
Restricted Certificates of Deposit	30,822	(46,643)
<b>Increase/(Decrease) in Liabilities:</b>		
Accounts Payable	605	66,764
Prizes Payable	145,920	241,041
Due to Other Funds	(14,870)	8,937
Due to Other Governments	(2,814)	2,814
Operator Security Deposits	(26,222)	46,925
Escrows Payable	(8,834)	7,350
Allowance for Doubtful Accounts	1,981	3,773
Accrued Liabilities	80,802	19,194
Unearned Revenue	(2,689)	137,193
Total Adjustments	<u>992,375</u>	<u>565,331</u>
Net Cash Provided by Operating Activities	<u>\$108,173,657</u>	<u>\$103,728,013</u>

The accompanying notes are an integral part of the financial statements.

**SOUTH DAKOTA LOTTERY**  
**NOTES TO THE FINANCIAL STATEMENTS**  
*For the Fiscal Years Ended June 30, 2013 and 2012*

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**ORGANIZATION.** The South Dakota Lottery markets instant tickets and lotto games, and regulates video lottery to raise revenue for State programs and projects.

The South Dakota Lottery was created during the 1987 Legislative Session by the passage of Senate Bill 254. The legislation authorized the Lottery to market instant games, with sales commencing on Sept. 30, 1987.

Video Lottery was created by the passage of Senate Bill 129 during the 1989 Legislative Session. It gave the Lottery authority to license and regulate a video lottery game with play commencing on Oct. 16, 1989.

Lotto games were approved by the 1990 Legislature through the passage of Senate Bill 86. South Dakota was accepted as a member of the Multi-State Lottery Association (MUSL) in April of 1990 and began selling tickets on Nov. 15, 1990. The current lotto games offered by the Lottery are Powerball, Power Play, Mega Millions, Megaplier, Hot Lotto, Sizzler, Wild Card 2 and Dakota Cash.

**BASIS OF PRESENTATION.** The South Dakota Lottery Fund is accounted for as a proprietary type enterprise fund for the State of South Dakota. Proprietary funds are accounted for using the accrual basis of accounting. The accompanying financial statements are prepared in accordance with generally accepted accounting principles (GAAP) for governments as prescribed by the Governmental Accounting Standards Board (GASB). The South Dakota Lottery is considered part of the primary government as reported by the State of South Dakota. Revenues are recognized when they are earned, and expenses are recognized when they are incurred.

**CASH.** Cash includes cash on hand, demand deposits, and a participating interest in the State's internal investment pool held by the State Treasurer. The amount held in the State's internal investment pool is reported at fair value.

Management of the State's internal investment pool is the statutory responsibility of the South Dakota Investment Council (SDIC). The investment policy and required risk disclosures for the State's internal investment pool are presented in the SDIC's audit report which can be obtained by contacting the Department of Legislative Audit, 427 South Chapelle, C/O 500 East Capital, Pierre, South Dakota 57501.

**RESTRICTED CASH.** Restricted cash is the amount of operator security deposits in the form of cash on deposit with the Lottery.

**ACCOUNTS RECEIVABLE.** Accounts receivable (net) represents the following at June 30:

	<u>2013</u>	<u>2012</u>
<i>Uncollected instant/on-line ticket revenues</i>	\$ 876,797	\$ 785,991
<i>Allowance for doubtful instant/on-line accounts</i>	(14,457)	(12,476)
<i>Uncollected video lottery revenues and fees</i>	3,541,008	3,528,710
	<u>\$4,403,348</u>	<u>\$4,302,225</u>

**RESTRICTED OTHER RECEIVABLE.** The Restricted Other Receivable account represents the South Dakota Lottery's share of funds held by the Multi-State Lottery Association (MUSL) in an Unreserved Account. The earnings from MUSL operations are deposited into this account and considered to be distributions to the member lotteries. This money may be used by a member lottery only for the purposes approved by the MUSL Board.

**SOUTH DAKOTA LOTTERY**  
**NOTES TO THE FINANCIAL STATEMENTS**  
*For the Fiscal Years Ended June 30, 2013 and 2012*

**OPERATOR SECURITY DEPOSITS.** ARSD 48:02:05:04(18) requires video lottery operators to furnish to the Lottery by July 1 of each year, security equal to one-eighteenth of the State's share of estimated annual net machine income derived from the operator's video lottery machines. Security may be in the form of a surety bond, deposit in cash, an irrevocable letter of credit, or a certificate of deposit issued by a South Dakota financial institution with the Lottery endorsed on it as a payee. As of June 30, 2013 and 2012, the amount of cash on deposit with the Lottery was \$21,582 and \$16,982 and the amount of certificates of deposit being held by the Lottery was \$472,199 and \$503,021, respectively. The amount of \$4,939,000 and \$5,011,900, respectively, was in the form of surety bond or irrevocable letter of credit and are not reported on the Statement of Net Position. The total Security Deposits on June 30, 2013 and 2012 were \$5,432,781 and \$5,531,903, respectively.

**CAPITAL ASSETS.** Assets are capitalized based on policies established by the South Dakota Bureau of Finance and Management. Capital assets are capitalized at cost or estimated historical cost, if the original cost is unavailable. Equipment is capitalized when the cost of individual items is \$5,000 or more. Intangible assets are capitalized when the cost of individual items is more than \$250,000. Depreciation or amortization on capital assets is computed using the straight line method over the estimated useful lives of the assets, which is 3 to 10 years for all equipment and 3 to 25 years for intangible assets. When assets are disposed of, the costs and related accumulated depreciation are removed from the accounts and any gain or loss is reflected in the results from operations in the period of disposal.

Capital Assets consisted of the following for fiscal years 2013 and 2012:

	<u>2013</u>				<u>2012</u>			
	Beginning Balance	Additions	Deletions	Ending Balance	Beginning Balance	Additions	Deletions	Ending Balance
<i>Equipment</i>	\$ 656,267	\$1,296,600	\$ 10,518	\$1,942,349	\$ 662,649	\$ 6,701	\$ 13,083	\$ 656,267
<i>Intangible Assets-Software</i>	2,313,097	-	-	2,313,097	2,313,097	-	-	2,313,097
<i>Total Capital Assets</i>	<u>2,969,364</u>	<u>\$1,296,600</u>	<u>10,518</u>	<u>4,255,446</u>	<u>2,975,746</u>	<u>6,701</u>	<u>13,083</u>	<u>2,969,364</u>
<i>Less Accumulated Depreciation/Amortization for:</i>								
<i>Equipment</i>	(354,619)	(552,750)	10,518	(896,851)	(241,586)	(126,116)	13,083	(354,619)
<i>Intangible Assets-Software</i>	(578,274)	(231,310)	-	(809,584)	(346,964)	(231,310)	-	(578,274)
<i>Total Accumulated Depreciation/Amortization</i>	<u>(932,893)</u>	<u>(784,060)</u>	<u>10,518</u>	<u>(1,706,435)</u>	<u>(588,550)</u>	<u>(357,426)</u>	<u>16,083</u>	<u>(932,893)</u>
<i>Total Capital Assets, Net</i>	<u>\$2,036,471</u>	<u>\$512,540</u>	<u>\$ -</u>	<u>\$2,549,011</u>	<u>\$2,387,196</u>	<u>(\$350,725)</u>	<u>\$ -</u>	<u>\$2,036,471</u>

**PRIZES.** Prize expense for instant games is recorded as prizes are paid. Adjustments are made based on the predetermined prize structure for each instant game as necessary. Prizes payable represents the difference between the amount of prize expense recognized and actual prizes paid.

Prize expense and prizes payable for on-line games are recorded based on actual drawing results. Prizes payable represents unpaid prizes not yet claimed or reverted.

A minimum of 50 percent of the projected revenue from the sale of lottery tickets, computed on a year-round basis, is allocated for payment of prizes. Prizes may be claimed up to 180 days after the official end of the game. Unclaimed prizes are added to the prize pools of subsequent lottery games. Reverted prizes during the fiscal years ended June 30, 2013 and 2012 were \$420,199 for on-line prizes and \$617,993 for instant prizes, and \$1,065,978 for on-line prizes and \$438,051 for instant prizes, respectively.

**SOUTH DAKOTA LOTTERY**  
**NOTES TO THE FINANCIAL STATEMENTS**  
*For the Fiscal Years Ended June 30, 2013 and 2012*

**DUE TO THE PROPERTY TAX REDUCTION FUND.** SDCL 42-7A-63 sets the State's percentage of net machine income at 50 percent of which all but 0.5 percent is deposited into the Property Tax Reduction Fund. At June 30, 2013 and 2012, there was a liability to the Property Tax Reduction Fund of \$3,460,463 and \$3,472,901, respectively.

**DUE TO THE GENERAL FUND AND THE CAPITAL CONSTRUCTION FUND.** The Lottery maximizes net proceeds to the State from the sale of instant and on-line tickets. These net proceeds are transferred to the General Fund and Capital Construction Fund on an annual basis on or about July 1. There was a liability for instant ticket sales to the General Fund of \$821,600 and \$1,400,976, and a liability for on-line ticket sales to the Capital Construction Fund of \$2,387,780 and \$1,905,577 as of June 30, 2013 and 2012, respectively.

**DUE TO OTHER FUNDS.** A liability has been created for services provided by other components of state government but not yet paid as of June 30.

**ESCROWS PAYABLE.** The passage of House Bill 1344 by the 1989 Legislature authorized tribal governments to receive up to 50 percent of the State's revenue on lottery products sold on that reservation. Fifty percent of the State's share of revenue on the reservations has been escrowed for payment to the tribes.

**ACCRUED LIABILITIES.** Accrued liabilities that have been incurred but not yet paid as of June 30 include accrued wages, benefits, and retailer bonuses.

**UNEARNED REVENUE.** A liability has been recorded for on-line tickets sold for future drawings that were collected before June 30. A liability has also been recorded for video lottery distributor and manufacturer renewal fees owed July 1 but collected before June 30.

**NET POSITION.** "Net Position" is the difference between assets and liabilities. Net position is reported in three categories:

**Net investment in capital assets** consists of capital assets, net of accumulated depreciation/amortization and reduced by outstanding balances for bonds, notes, and other debt that is attributed to the acquisition, construction, or improvement of those assets.

**Restricted net position** consists of funds held by the Multi-State Lottery Association (MUSL) in an unreserved account. The earnings paid to this account are considered to be distributions to the member lotteries, but account funds may be used by a member lottery only for the purposes approved by the MUSL Board.

**Unrestricted net position** consists of assets that do not meet the definition of the two preceding categories.

When both restricted and unrestricted funds are eligible for use in payment of expenses, the type of expense to be incurred is analyzed to determine the best funding source based on available funds and plans for future projects.

**REVENUE RECOGNITION.** Sales of instant and on-line tickets are made to the public through licensed retailers. Instant ticket sales for games in progress are recorded as retailers settle (sell) the packs of tickets. Adjustments based upon the known relationship of the number of tickets sold to the number of winning tickets redeemed through the end of the accounting period are made as necessary. Instant ticket sales for

**SOUTH DAKOTA LOTTERY**  
**NOTES TO THE FINANCIAL STATEMENTS**  
*For the Fiscal Years Ended June 30, 2013 and 2012*

ended games and on-line ticket sales are reported as the actual ticket sales made to the public through the licensed retailers.

**RETAILER COMMISSIONS.** Lottery retailers selling instant and on-line tickets receive a 5 percent commission on each ticket sold or distributed to the public. Instant retailers receive a 1 percent selling commission for selling instant prize winning tickets over \$101 and a 1 percent cashing commission for cashing instant prize winning tickets of \$1 up to \$100.

On-line retailers selling a jackpot winning Powerball or Mega Millions ticket may receive a bonus of \$50,000. Selling bonuses of \$20,000 and \$1,000 may be paid to retailers selling Powerball tickets of \$1,000,000 and \$10,000, respectively. Selling bonuses of \$10,000 and \$1,000 may be paid to retailers selling Mega Millions tickets of \$250,000 and \$10,000, respectively. If a retailer sells a Power Play ticket winning \$2,000,000 or \$40,000, a bonus of \$20,000 or \$4,000 may be paid, respectively. If a retailer sells a Megaplier ticket hitting the second prize (automatically worth \$1,000,000 regardless of the multiplier) or the \$10,000 third prize (times the multiplier), a bonus of \$20,000 or \$1,000 times the multiplier may be paid, respectively. Retailers who sell a Dakota Cash jackpot winning ticket may receive a bonus equal to 5 percent of the value of the winning ticket not to exceed \$5,000. Retailers who sell a Wild Card 2 jackpot winning ticket may receive a bonus equal to 1 percent of the value of the winning ticket, not to exceed \$10,000; a retailer selling a \$6,000 winning ticket may receive a bonus of \$600. Retailers who sell a Hot Lotto jackpot, \$30,000 or \$3,000 winning ticket may receive a bonus of \$10,000, \$3,000 or \$1,000, respectively. Retailers who sell a Sizzler jackpot, \$90,000 or \$9,000 winning ticket may receive a bonus of \$10,000, \$9,000 or \$900, respectively.

**NON-OPERATING REVENUES AND EXPENSES.** Revenues and expenses that result from activities not associated with the sale of lottery tickets are classified as non-operating.

**NOTE 2. COMPENSATED ABSENCES**

All permanent full-time employees earn annual leave. Upon termination, employees are eligible to receive compensation for their accrued annual leave balances. At June 30, 2013 and 2012, a liability existed for accumulated annual leave calculated at the employee's June 30 pay rate in the amount of \$134,998 and \$113,470, respectively. Employees who have been continuously employed by the State of South Dakota for at least seven years prior to the date of their retirement, voluntary resignation, or death will receive payment for one-fourth of their accumulated sick leave balance. This payment is not to exceed the sum of 12 weeks of the employee's annual compensation. At June 30, 2013 and 2012, a liability existed for accumulated sick leave, calculated at each employee's June 30 pay rate, in the amount of \$175,635 and \$146,042, respectively. The following is a schedule of changes in compensated absences at June 30, 2013 and 2012.

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
<i>Compensated Absences Payable</i>					
<i>Fiscal Year 2013</i>	\$ 259,512	\$ 163,564	\$ 112,443	\$ 310,633	\$ 165,753
<i>Fiscal Year 2012</i>	243,895	144,878	129,261	259,512	138,320

**NOTE 3. RETIREMENT PLAN**

The South Dakota Lottery participates in the South Dakota Retirement System (SDRS), a cost-sharing, multiple-employer defined benefit pension plan established to provide retirement, disability, and survivor benefits for

**SOUTH DAKOTA LOTTERY**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**For the Fiscal Years Ended June 30, 2013 and 2012**

employees of the State and its political subdivisions. Authority for establishing, administering, and amending plan provisions is found in SDCL 3-12. The SDRS issues a publicly available financial report that includes financial statements, footnote disclosures, and required supplementary information. That report may be obtained by contacting the SDRS in writing at South Dakota Retirement System, P.O. Box 1098, Pierre, SD 57501-1098 or by calling (605) 773-3731.

State law requires employees to contribute 6 percent of their salary to the plan and the employer to contribute an amount equal to the employee's contribution. The right to receive retirement benefits vests after three years of credited service. The South Dakota Lottery's contributions to the SDRS for the fiscal years ended June 30, 2013, 2012, and 2011 were \$71,379, \$70,844, and \$66,335, respectively, equal to the required contributions each year.

**NOTE 4. OPERATING LEASES**

The South Dakota Lottery entered into agreements to lease buildings and certain equipment. Some of the operating leases contain the provision that the South Dakota Lottery may renew the operating leases at the expiration date of the lease on a year-to-year basis. In most cases, management expects that in the normal course of business, leases will be renewed or replaced by other leases of a similar nature.

The following schedule is a summary of future minimum rental payments by years required under operating leases with lease terms in excess of one year as of June 30, 2013:

<u>Period Ending June 30:</u>	
2014	\$ 63,909
2015	63,909
2016	24,846
2017	18,780
2018	18,780
Later years	97,030
Total Minimum Payments	<u><u>\$287,254</u></u>

Total rental expense for all operating leases for the fiscal years ended June 30, 2013 and 2012, was \$67,626 and \$67,456, respectively.

**NOTE 5. VIDEO LOTTERY**

Following is a summary of video lottery revenues for the fiscal years ended June 30, 2013 and 2012:

	<u>2013</u>	<u>2012</u>
Cash In	\$ 580,092,145	\$ 550,055,033
Less Cash Out	<u>395,451,581</u>	<u>373,410,903</u>
Video Lottery Net Machine Income	184,640,564	176,644,130
Less Operator and Establishment Share	<u>92,320,282</u>	<u>88,322,065</u>
Video Lottery Revenue Available to the State	92,320,282	88,322,065
Less Lottery Operating Share	<u>923,203</u>	<u>883,221</u>
Video Lottery Revenue to the Property Tax Reduction Fund	<u><u>\$ 91,397,079</u></u>	<u><u>\$ 87,438,844</u></u>

**SOUTH DAKOTA LOTTERY**  
**NOTES TO THE FINANCIAL STATEMENTS**  
*For the Fiscal Years Ended June 30, 2013 and 2012*

**NOTE 6. TRANSFERS**

Following is a summary of total transfers for the fiscal years ended June 30, 2013 and 2012:

Transfers Out:	<u>2013</u>	<u>2012</u>
General Fund Proceeds from Instant and On-Line	\$ 6,200,000	\$ 6,600,000
Capital Construction Fund Proceeds from On-Line	6,600,000	6,000,000
General Fund Proceeds from Instant and On-line not Yet Transferred	821,600	1,400,976
Capital Construction Fund Proceeds from On-Line not Yet Transferred	2,387,780	1,905,577
Video Lottery Proceeds Transferred to the Property Tax Reduction Fund	87,936,616	83,965,943
Video Lottery Proceeds to Prop. Tax Reduction Fund not Yet Transferred	3,460,463	3,472,901
Video Lottery Grant to Department of Social Services	161,856	131,399
Video Lottery Fees Transferred to the General Fund	135,000	225,000
Total Transfers Out	<u>\$107,703,315</u>	<u>\$103,701,796</u>

**NOTE 7. PARTICIPATION IN THE MULTI-STATE LOTTERY ASSOCIATION**

The South Dakota Lottery is a member of the Multi-State Lottery Association (MUSL), which operates the Powerball/Power Play, Wild Card 2, Hot Lotto, and Mega Millions/Megaplier games. Each MUSL member sells tickets through its licensed retailers and makes weekly wire transfers to MUSL in an amount equivalent to the member lottery's share of the prize liability less the actual low-tier prize liability.

The prize pool for Powerball is 50 percent of each drawing period's sales and up to 2 percent shall be placed into a prize reserve account. The Power Play prize pool is 49.96 percent of sales and .04 percent may be placed in a prize reserve account. The prize pool for Wild Card 2 is 57 percent of sales up from 55 percent on January 16, 2013, and 3 percent shall be placed in a prize reserve account. The prize pool for Hot Lotto is 50 percent of sales and up to 1 percent shall be placed in a prize reserve account. The Sizzler prize pool is 47.8813 percent of sales with 2.1187 percent may be placed in a prize reserve account. The prize pool for Mega Millions and Megaplier is up to 55 percent of sales and up to 5 percent of Mega Million sales shall be placed in a prize reserve account. A prize reserve fund serves as a contingency reserve to protect MUSL in cases of unforeseen liabilities. The money in a reserve fund is to be used at the discretion of the MUSL game group.

The prize reserve fund monies may be absorbed by a replacement game or are refundable to member states if MUSL or the MUSL game group disbands or if a member leaves MUSL or a game group. Members who leave must wait one year before receiving their remaining share, if any, of the prize reserve fund. The reserves are held by MUSL and are not included in these financial statements. At June 30, 2013 and 2012, the prize reserve account balances were:

	2013 MUSL <u>Balance</u>	2013 SD Lottery <u>Share</u>	2012 MUSL <u>Balance</u>	2012 SD Lottery <u>Share</u>
Powerball Prize Reserve Account	\$ 78,975,475	\$ 511,875	\$ 95,747,340	\$ 620,799
Powerball Set Prize Reserve Account	34,898,046	192,759	30,733,770	155,200
Wild Card Prize Reserve Account	693,336	130,214	793,033	157,561
Hot Lotto Prize Reserve Account	7,920,821	361,585	7,383,082	330,768
Mega Millions Prize Reserve Account	27,968,381	142,209	18,827,770	93,912
Total MUSL Prize Reserves	<u>\$150,456,059</u>	<u>\$1,338,642</u>	<u>\$153,484,995</u>	<u>\$1,358,240</u>

**SOUTH DAKOTA LOTTERY**  
**NOTES TO THE FINANCIAL STATEMENTS**  
***For the Fiscal Years Ended June 30, 2013 and 2012***

Also held by MUSL is the Unreserved Account into which is deposited the earnings from MUSL operations. The earnings paid to this account are considered to be distributions to the member lotteries. This money may be used by a member lottery for the purposes approved by the MUSL Board. This account balance is recorded as a Restricted Other Receivable.

Powerball and Mega Millions jackpot winners can choose a lump sum cash payment or receive the jackpot prize over 30 or 26 annual payments, respectively. Treasury zero coupon bonds that provide payments corresponding to the member lottery's obligation to these prize winners are purchased by MUSL in the name of the member lottery. MUSL holds these bonds and will cash the bonds when due and wire the money to the member lottery's account on or before the anniversary date of the win. The Wild Card 2 jackpot is paid in cash. The Hot Lotto jackpot will be paid in a single lump sum cash payment with all initial withholding taxes paid.

**NOTE 8. CONTRACTUAL ARRANGEMENTS**

- A. **Instant Tickets** - The South Dakota Lottery entered into a contract with Scientific Games to provide instant game tickets through August 29, 2016.
- B. **Video Lottery Vendor** - The South Dakota Lottery has contracted with Scientific Games to operate a video lottery system through December 24, 2019, with possible extension through December 24, 2024.
- C. **On-line Lottery Vendor** - The South Dakota Lottery has contracted with GTECH Corporation to operate an on-line lottery gaming system through August 2, 2019.

**NOTE 9. RISK MANAGEMENT**

The South Dakota Lottery is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Lottery is uninsured for property loss. The South Dakota Lottery participates in the various programs administered by the State of South Dakota. These risk management programs are funded through assessments charged to participating entities. The risk management programs include: 1) coverage for risks associated with automobile liability and general tort liability (including public officials' errors and omissions liability, medical malpractice liability, law enforcement liability, and products liability) through the State's Public Entity Pool for Liability Fund; 2) coverage of employee medical claims through the State's health insurance program; 3) coverage for unemployment benefits through the State's Unemployment Insurance Fund; and, 4) coverage for workers' compensation benefits through the State's Workers' Compensation Fund. Financial information relative to the self-insurance funds administered by the State is presented in the State of South Dakota Comprehensive Annual Financial Report.

**NOTE 10. SPECIAL ITEM**

In September 2012, the South Dakota Lottery received 600 new jackpot signs. The signs were obtained at no cost to the Lottery but were part of a 5 year contract extension with the on-line system vendor, GTECH Corporation.