

Report No. 2016-080
January 2016

STATE OF FLORIDA AUDITOR GENERAL

Financial Audit

DEPARTMENT OF THE LOTTERY

For the Fiscal Years Ended
June 30, 2015, and 2014



Sherrill F. Norman, CPA
Auditor General

Secretary of the Department of the Lottery

The State of Florida, Department of the Lottery (Lottery) was established as a State agency with the enactment of the Florida Public Education Lottery Act, Chapter 24, Florida Statutes, in 1987. The head of the Lottery is the Secretary, who, pursuant to Section 20.317, Florida Statutes, is appointed by the Governor subject to the confirmation of the Senate. During the period of our audit, Cynthia F. O'Connell served as Department Secretary. Effective November 23, 2015, Thomas R. Delacenserie was appointed Department Secretary.

The Auditor General conducts audits of governmental entities to provide the Legislature, Florida's citizens, public entity management, and other stakeholders unbiased, timely, and relevant information for use in promoting government accountability and stewardship and improving government operations.

The team leader was Jon M. Bardin, CPA, and the audit was supervised by Allen G. Weiner, CPA.

For the information technology portion of this audit, the team leader was Earl M. Butler, CISA, CFE, and the supervisor was Arthur Hart, CPA.

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SUMMARY

SUMMARY OF REPORT ON FINANCIAL STATEMENTS

Our audit disclosed that the basic financial statements prepared by the Department of the Lottery (Lottery) present fairly, in all material respects, the net position of the Lottery as of June 30, 2015, and 2014, and the changes in the financial position and cash flows thereof for the years then ended in accordance with prescribed financial reporting standards.

SUMMARY OF REPORT ON INTERNAL CONTROL AND COMPLIANCE

In our opinion, Lottery management maintained, in all material respects, effective internal control over financial reporting.

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* issued by the Comptroller General of the United States; however, we noted certain additional matters as summarized below.

ADDITIONAL MATTERS

Information Technology Controls

Finding 1: During our audit, we identified the need for an enhancement to the Lottery's information technology control practices. Specific details of this issue are not disclosed in this report to avoid the possibility of compromising Lottery information. However, the appropriate Lottery personnel have been notified of this issue.

Minority Retailer Participation

Finding 2: Section 24.113, Florida Statutes, requires that 15 percent of the Lottery's retailers be minority business enterprises, as defined in Section 288.703(3), Florida Statutes; however, no more than 35 percent of such retailers shall be owned by the same type of minority person, as defined by Section 288.703(4), Florida Statutes. Our audit disclosed that as of July 1, 2015, retailers comprising one minority type totaled 67 percent of the total number of minority retailers. A similar finding has been included in prior reports.

AUDIT OBJECTIVES AND SCOPE

Our audit objectives were to determine whether the Lottery had:

- Presented the Lottery's basic financial statements in accordance with generally accepted accounting principles;
- Established and implemented internal control over financial reporting and compliance with requirements that could have a direct and material effect on the financial statements;
- Complied with the various provisions of laws, rules, regulations, and contracts that are material to the financial statements; and
- Taken corrective actions for findings included in our report No. 2015-092.

The scope of this audit included an examination of the Lottery’s basic financial statements as of and for the fiscal years ended June 30, 2015, and 2014, and an examination of the effectiveness of the Lottery’s internal control over financial reporting. With respect to internal control over financial reporting, our examination included obtaining an understanding of the internal control over financial reporting, testing and evaluating the design and operating effectiveness of the internal control, and performing such other procedures as we considered necessary in the circumstances. We also examined various transactions to determine whether they were executed, both in manner and in substance, in accordance with governing provisions of laws, rules, regulations, and contracts.

AUDIT METHODOLOGY

The audit methodology used to develop the findings in this report included the examination of pertinent Lottery records in connection with the application of procedures required by auditing standards generally accepted in the United States of America and applicable standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.



Sherrill F. Norman, CPA
Auditor General

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The President of the Senate, the Speaker of the
House of Representatives, and the
Legislative Auditing Committee

INDEPENDENT AUDITOR'S REPORT

Report on the Financial Statements

We have audited the accompanying financial statements of the Department of the Lottery (Lottery), an enterprise fund of the State of Florida, as of and for the fiscal years ended June 30, 2015, and 2014, and the related notes to the financial statements which collectively comprise the Lottery's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audits. We conducted our audits 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 audits 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 error or fraud. 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. 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 opinions.

Opinions

In our opinion, the financial statements referred to above, present fairly, in all material respects, the respective financial position of the Lottery as of June 30, 2015, and 2014, and the respective changes in financial position and cash flows, for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

As discussed in Note I. to the financial statements, the financial statements of the Lottery are intended to present the financial position, the changes in financial position, and cash flows of only that portion of the business-type activities and major funds of the State that is attributable to the transactions of the Lottery. They do not purport to, and do not, present fairly the operations of the State of Florida as of June 30, 2015, and 2014, or the changes in its financial position and its cash flows for the 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.

As discussed in Notes I.U. and IX. to the financial statements, the Lottery implemented Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions, an amendment of GASB Statement No. 27*, which is a change in accounting principle that requires an employer participating in a cost-sharing multiple-employer defined benefit pension plan to report the employer's proportionate share of the net pension liability of the defined benefit pension plan. This affects the comparability of amounts reported in the 2014-15 fiscal year with the amounts reported for the 2013-14 fiscal year. Our opinion is also not modified with respect to this matter.

Other Matters

Required Supplementary Information

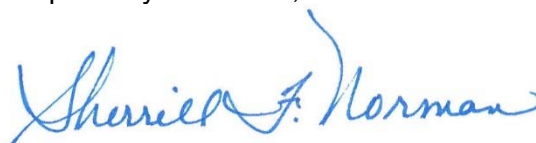
Accounting principles generally accepted in the United States of America require that **MANAGEMENT'S DISCUSSION AND ANALYSIS** (pages 4 through 12) and the other required supplementary schedules of the Lottery's proportionate share of the net pension liability and contributions (pages 43 through 44) be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with attestation standards established by the American Institute of Certified Public Accountants and applicable *Government Auditing Standards*, we have also issued a report on our examination of the Lottery's internal control over financial reporting, and on our tests of the Lottery's

compliance with certain provisions of laws, rules, regulations, contracts, and other matters included under the heading **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**. As noted by that report dated January 29, 2016, we have examined, in accordance with attestation standards established by the American Institute of Certified Public Accountants and the standards applicable to attestation engagements in *Government Auditing Standards*, the Lottery's internal control over financial reporting as of June 30, 2015, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and expressed an unqualified opinion. With respect to compliance, the purpose of that report is not to provide an opinion on compliance, but rather to describe the scope of our testing of compliance and the results of that testing. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Lottery's internal control over financial reporting and compliance.

Respectfully submitted,



Sherrill F. Norman, CPA
Tallahassee, Florida
January 29, 2016

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEARS ENDED JUNE 30, 2015, AND JUNE 30, 2014

The information presented in the Management's Discussion and Analysis (MD&A) introduces the Florida Lottery's (Lottery) financial statements and provides readers an analytical overview of the Lottery's financial activities and performance for the fiscal years ended June 30, 2015, and 2014. We encourage readers to consider the information presented here in conjunction with the financial statements and notes to the financial statements, which begin on page 14.

FINANCIAL HIGHLIGHTS

The Lottery has as its mission the maximization of revenues for the benefit of education in a manner consistent with the dignity of the State of Florida and the welfare of its citizens. The Lottery is considered a mature lottery and offers its players a full range of both Scratch-Off and Terminal products. The Lottery has been successful in sustaining ticket sales in excess of \$2 billion for the twenty-sixth consecutive fiscal year, with the past three fiscal years exceeding \$5 billion. During the same twenty-six year period, the transfer to the Educational Enhancement Trust Fund (EETF) has been a minimum of \$800 million annually, with the fiscal year 2015 transfer exceeding \$1 billion for the thirteenth consecutive year.

For the fiscal year ended June 30, 2015:

- Transfers to the EETF were approximately \$1.5 billion this fiscal year, as well as the prior fiscal year.
- The Lottery's ticket sales increased by 4.01 percent over the prior fiscal year from approximately \$5.37 billion to \$5.58 billion.
- Approximately 66.7 percent of total sales were provided by the Scratch-Off product line. This shift in product mix from the higher profit-margin Terminal product to the lower profit-margin Scratch-Off product directly impacts the amount transferred to the EETF.
- Prize expense increased \$196.8 million, which represents a 5.74 percent increase during fiscal year 2015. The Lottery has the authority to vary the prize expense in order to maximize transfers. This expense typically increases or decreases in proportion to ticket sales and represented approximately 64.98 percent of ticket sales.
- The gaming vendors' fees and retailer commissions are based on sales and therefore fluctuate in direct correlation with sales revenue. Fiscal year 2015 expenses for these items increased 4.77 percent over the prior fiscal year expenses in conjunction with the increase in sales.
- Administrative operating expenses, which include advertising, salaries and benefits, rent, utilities and maintenance, professional fees, depreciation, and other administrative expenses, experienced an increase of \$1.17 million. Administrative operating expenses for fiscal years 2015 and 2014 were \$75.70 million and \$74.53 million, respectively.
- Nonoperating income increased \$4.40 million over the prior fiscal year. The increase was primarily due to a decrease of \$3.76 million in amortization of grand prizes.
- EETF transfers from unclaimed prize money decreased \$9.75 million over the prior fiscal year. Transfers from unclaimed Terminal games increased \$3.27 million while transfers from unclaimed Scratch-Off games decreased \$13.02 million compared to fiscal year 2014. This decrease can be attributed to the fact that during fiscal year 2015 the Lottery closed 18 games compared to 46 games closed during fiscal year 2014.

OVERVIEW OF THE FINANCIAL STATEMENTS

The Lottery is accounted for as an enterprise fund, reporting transactions using the accrual basis of accounting similar to the method used by business entities. This MD&A is intended to serve as an introduction to the Lottery's basic financial statements, including the notes to the financial statements. The Statements of Net Position on page 14, the Statements of Revenues, Expenses, and Changes in Net Position on page 16, and the Statements of Cash Flows on page 17 report the Lottery's net position and changes therein. The notes to the financial statements provide additional information that is essential to a reader's understanding of the data provided in the financial statements.

The Lottery transfers its net profits each fiscal year to the EETF. As a result, the Lottery's net position consists of funds invested in capital assets, unrestricted net position, and restricted net position. Unrestricted net position consists of liabilities for which no cash payments will be made. The restricted net position consists of the investments being held by the Lottery to fund deferred prize payouts, 20 percent of unclaimed prizes designated for future prize payouts or promotions, and the Multi-State Lottery Association (MUSL) deposit amounts. The financial statements do include the cumulative effect of periodic adjustments to recognize the fair value of the grand prize investments despite the fact that the Lottery purchased the investments with the intention of holding the investments until maturity in order to meet the future obligations and, therefore, would not realize any gains or losses related to these investments for distribution as net proceeds.

SUMMARY OF NET POSITION

Table 1 presents a comparative summary of the Lottery's Statements of Net Position for fiscal years 2015, 2014, and 2013.

Table 1
Condensed Statements of Net Position
As of June 30, 2015, 2014, and 2013
(In Thousands)

	2015	2014	2013
Current Assets	\$ 205,746	\$ 175,627	\$ 195,874
Restricted Assets	732,727	841,406	1,053,576
Capital Assets, Net of Depreciation	5,820	4,243	3,215
Total Assets	944,293	1,021,276	1,252,665
Total Deferred Outflows of Resources	3,969	-	-
Current Liabilities	206,321	167,804	190,498
Current Liabilities Payable from Restricted Assets	383,503	450,147	607,554
Noncurrent Liabilities	271,186	305,664	349,312
Total Liabilities	861,010	923,615	1,147,364
Total Deferred Inflows of Resources	5,709	-	-
Net Position:			
Net Investment in Capital Assets	5,820	4,243	3,215
Restricted Net Position	95,094	93,418	102,086
Unrestricted Net Position	(19,371)	-	-
Total Net Position	\$ 81,543	\$ 97,661	\$ 105,301

Assets

Total assets at the end of fiscal year 2015 decreased \$76.98 million from \$1.02 billion at June 30, 2014, to \$944.29 million at June 30, 2015. At the end of fiscal year 2014, total assets were \$231.39 million less than the \$1.25 billion at the end of fiscal year 2013.

- Current assets increased from \$175.63 million in 2014 to \$205.75 million in 2015, representing an increase of \$30.12 million. The increase was primarily due to an increase of \$18.64 million in accounts receivable for fiscal year 2015, which was related to timing in the weekly sweeps at June 30, 2015.
- Restricted assets decreased \$108.68 million from \$841.41 million in 2014 to \$732.73 million in 2015. This decrease was predominately due to the continued decrease in the deferred payment investment portfolio as the preference in payout options for jackpot prizewinners progressively shifted toward the cash option instead of the alternative annuity option. There were \$86.15 million in payouts of annuities and \$5.9 million in purchases of new investments in fiscal year 2015 in comparison to fiscal year 2014, which had annuity payouts of \$112.60 million, and purchases of new investments of \$18.12 million. The amount of invested collateral and time deposits from the lending of those securities also continues to decline. The Lottery held \$317.06 million in invested collateral and time deposits at June 30, 2015, \$363.98 million at June 30, 2014, and \$494.32 million at June 30, 2013.

Deferred Outflows of Resources

Total deferred outflows of resources as of June 30, 2015, were \$3.97 million for pension related items (Refer to Note IX. to the financial statements for additional details).

Liabilities

Total liabilities at June 30, 2015, were \$861.01 million, which was approximately \$62.61 million lower than the total liabilities of \$923.62 million at June 30, 2014. The total liabilities at June 30, 2014, were \$223.75 million lower than the June 30, 2013, amount of \$1.15 billion.

- Current liabilities increased from \$167.80 million on June 30, 2014, to \$206.32 million on June 30, 2015. This increase can be attributed to a Powerball® jackpot that was won at the end of June 2015 and paid in July 2015. As expected, current liabilities payable from restricted assets decreased \$66.65 million from \$450.15 million at June 30, 2014, to \$383.50 million at June 30, 2015. The amount of grand prizes payable due within one year and the obligations under securities lending, which are the two primary components of this liability class, are associated with the amounts payable to jackpot winners, who have chosen the deferred payment option. The obligations under securities lending decreased by \$46.91 million and the current portion of grand prizes payable decreased by \$19.74 million. At June 30, 2014, current liabilities payable from restricted assets balance of \$450.15 million was \$157.40 million less than the balance of \$607.55 million at June 30, 2013.
- Noncurrent liabilities principally consist of the long-term portion of grand prizes payable, which represents the amount to be paid to grand prizewinners in future years. Correlative to current grand prizes payable, the long-term grand prizes payable decreased \$44.31 million from June 30, 2014, to June 30, 2015, and decreased \$44.98 million from June 30, 2013, to June 30, 2014.

Deferred Inflows of Resources

Total deferred inflows of resources as of June 30, 2015, were \$5.71 million for pension related items (Refer to Note IX. to the financial statements for additional details).

Net Position

Net position decreased \$16.12 million from June 30, 2014, to June 30, 2015. Net position at June 30, 2015, 2014, and 2013 were \$81.54 million, \$97.66 million, and \$105.30 million, respectively. The decline at June 30, 2015, can be attributed to a \$6.21 million decrease in the amount restricted for undistributed appreciation on restricted investments and the \$19.4 million impact of recording a new net pension liability with the implementation of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions, an amendment of GASB Statement No. 27*, for the fiscal year ended June 30, 2015. Refer to Note I.U. for further details.

The Lottery joined MUSL six years ago in order to participate in the Powerball® with Powerplay® game and on May 15, 2013, the Lottery began participating in Mega Millions® with Megaplier®. In accordance with MUSL's rules, the Lottery must contribute to various prize reserve funds maintained by MUSL for unforeseen prize payouts related to the Powerball with Powerplay and Mega Millions with Megaplier games. The Lottery's deposits in reserve funds with MUSL totaled \$21.77 million and \$19.82 million as of June 30, 2015, and June 30, 2014, respectively. Refer to Note VI., Multi-State Lottery Association, for further details.

SUMMARY OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

The most important element demonstrated with the Lottery's financial statements is the transfer to the EETF. Accordingly, the primary focus of these financial statements is determining net income available for transfer, rather than the change in net position of the Lottery, which primarily reflects the changes in fair value of restricted investments.

Table 2 presents the condensed Statements of Revenues, Expenses, and Changes in Net Position for the fiscal year ended June 30, 2015, and the prior fiscal years ended June 30, 2014, and June 30, 2013, as derived from the Lottery's Statements of Revenues, Expenses, and Changes in Net Position.

Table 2
Condensed Statements of Revenues, Expenses, and Changes in Net Position
As of June 30, 2015, 2014, and 2013
(In Thousands)

	<u>2015</u>	<u>2014</u>	<u>2013</u>
Operating Revenues:			
Ticket Sales	\$ 5,583,331	\$ 5,368,230	\$ 5,012,996
Bad Debt Expense	(1,263)	(1,337)	(912)
Terminal & Retailer Fees and Miscellaneous	7,652	7,817	7,979
Total Operating Revenues	<u>5,589,720</u>	<u>5,374,710</u>	<u>5,020,063</u>
Operating Expenses:			
Prizes	3,627,939	3,431,092	3,162,889
Retailer Commissions	311,981	298,651	278,493
Vendor Commissions	81,635	77,052	75,205
Other Expenses	75,696	74,528	72,653
Total Operating Expenses	<u>4,097,251</u>	<u>3,881,323</u>	<u>3,589,240</u>
Income from Operations	<u>1,492,469</u>	<u>1,493,387</u>	<u>1,430,823</u>
Nonoperating Revenue, Net of Expenses	<u>(1,218)</u>	<u>(5,618)</u>	<u>(37,816)</u>
Income Before Operating Transfers	1,491,251	1,487,769	1,393,007
Total Transfers to EETF	<u>(1,496,371)</u>	<u>(1,495,409)</u>	<u>(1,424,307)</u>
Change in Net Position	(5,120)	(7,640)	(31,300)
Net Position, Beginning Restated	86,663	105,301	136,601
Net Position, End of Year	<u>\$ 81,543</u>	<u>\$ 97,661</u>	<u>\$ 105,301</u>

FINANCIAL ANALYSIS

Sales

For the fiscal year ended June 30, 2015, ticket sales increased by \$215.10 million over fiscal year 2014, which experienced a sales increase of \$355.23 million over fiscal year 2013. The Terminal game ticket sales decreased 4.70 percent from the prior year. To offset the impact of the slow economic recovery on sales, the Lottery not only continued to utilize proven techniques, but also created new promotions for players.

- The daily games, CASH 3™ and Play 4™, reflect increases over the prior year. The total sales from these two games reached \$639.47 million making up 34.39 percent of total Terminal game ticket sales.
- On July 2, 2014, Lucky Money replaced Mega Money. The game provided a 29.83 percent (\$23.7 million) increase in sales over the prior year.
- A total of 500 Full Service Vending Machines (FSVMs) were installed at the Lottery's top Instant Ticket Vending Machine (ITVM) locations during fiscal years 2013 and 2014. The FSVM allows players to purchase both Terminal and Scratch-Off tickets. Total sales from FSVMs reached \$257.31 million during fiscal year 2015.

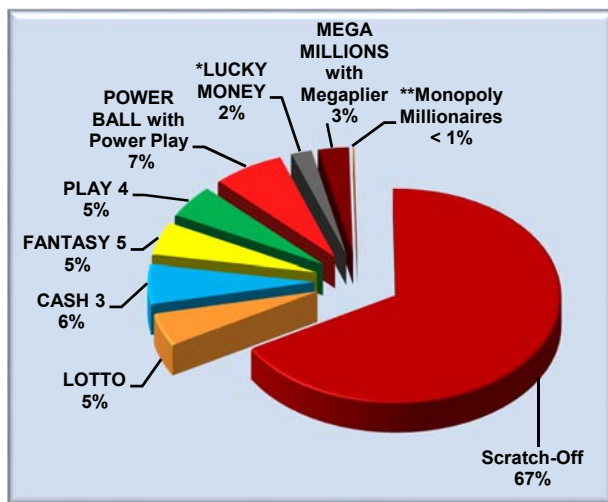
Sales of Scratch-Off tickets increased from \$3.42 billion or 63.65 percent of total sales in fiscal year 2014 to \$3.72 billion, or 66.70 percent of total sales in fiscal year 2015.

- Scratch-Off ticket sales experienced an increase of 8.98 percent over prior year sales with increases being reflected in most price points. The largest increases were seen in the \$10 and \$25 price points. The \$25 price point was dominated by the 100X THE CASH ticket with sales totaling \$374.68 million.
- ITVMs have proven successful in increasing the visibility of Scratch-Off ticket products and offering a convenience to players. There were 1,500 machines in use during the year. Total sales from the ITVMs accounted for \$311.63 million of the Scratch-Off sales.

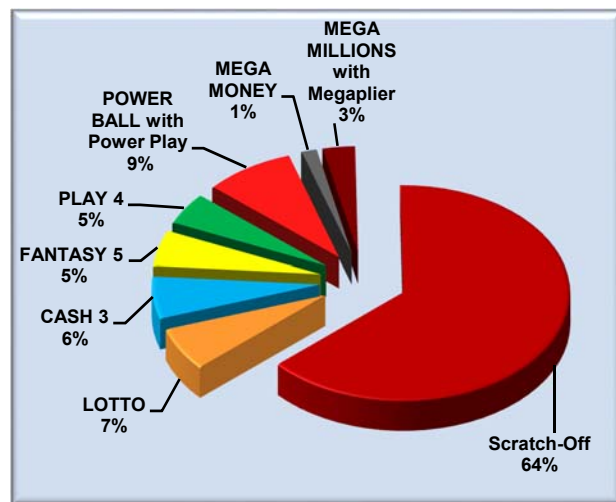
Bad debt expense is reported as a reduction in gross revenue in accordance with Governmental Accounting Standards Board requirements. The amount of bad debt expense for the fiscal years ended June 30, 2015, and 2014, was \$1.26 million and \$1.34 million, respectively.

The following charts show sales by product for the various Lottery games during the fiscal years 2015 and 2014:

Sales by Product for Fiscal Year 2014-15



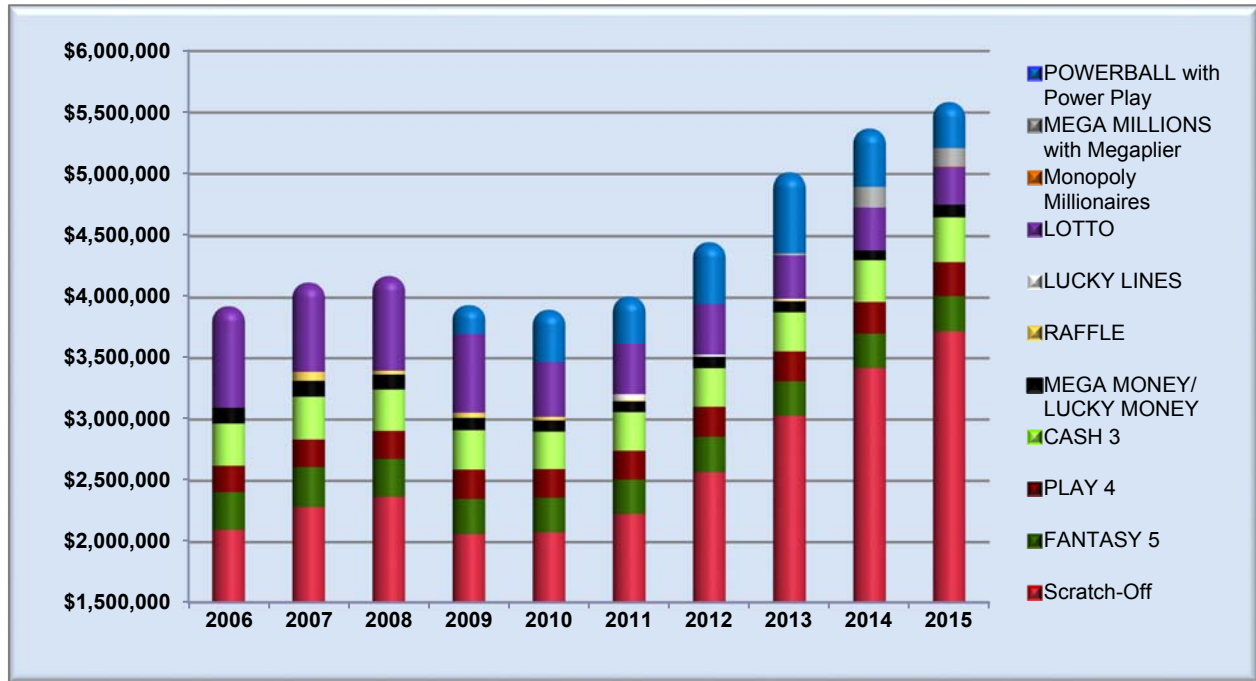
Sales by Product for Fiscal Year 2013-14



* Mega Money was replaced by Lucky Money on July 2, 2014.
 ** Monopoly Millionaires' Club launched October 19, 2014, but was discontinued December 26, 2014.

The following chart and table show sales by game for the last ten fiscal years:

**Department of the Lottery
Historical Lottery Sales by Game
(In Thousands)**



**Table 3
Department of the Lottery
Historical Lottery Sales by Game
Last Ten Fiscal Years
(In Thousands)**

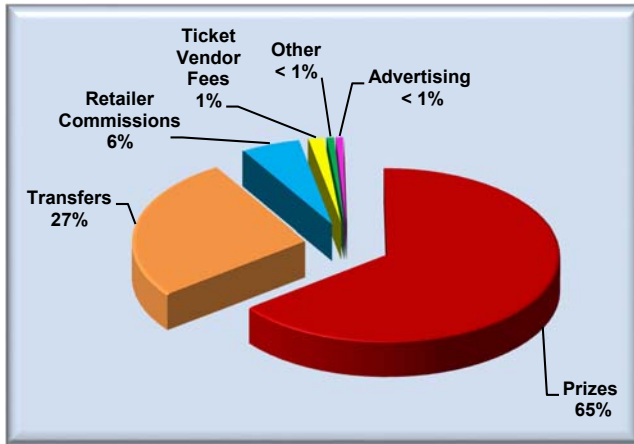
Fiscal Year Ended June 30	LOTTO	FANTASY 5	PLAY 4	CASH 3	LUCKY MONEY / MEGA MONEY	RAFFLE	LUCKY LINES	POWERBALL with Power Play	MEGA MILLIONS with Megaplier	Monopoly Millionaires	Scratch-Off	Combined Sales
2006	\$ 835,028	\$ 306,679	\$ 215,529	\$ 343,174	\$ 128,502	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 2,100,118	\$ 3,929,030
2007	735,585	326,241	225,285	348,694	130,142	72,549	-	-	-	-	2,283,620	4,122,116
2008	778,954	309,445	227,940	336,096	122,742	30,818	-	-	-	-	2,368,781	4,174,776
2009	650,603	287,285	238,957	320,157	102,190	41,314	-	233,396	-	-	2,064,135	3,938,037
2010	445,881	281,963	235,027	304,039	92,060	29,334	-	434,062	-	-	2,078,133	3,900,499
2011	411,389	282,777	235,692	313,270	88,971	12,603	45,369	392,969	-	-	2,225,676	4,008,716
2012	419,040	290,672	244,711	314,747	92,346	-	17,692	503,697	-	-	2,566,991	4,449,896
2013	352,375	281,492	244,141	324,539	89,500	12,879	8,582	654,263	16,698	-	3,028,527	5,012,996
2014	349,114	288,237	257,752	339,636	79,483	-	-	469,292	167,573	-	3,417,143	5,368,230
2015	300,961	287,803	276,217	363,251	103,196	-	-	375,057	147,370	5,481	3,723,995	5,583,331

Expenses

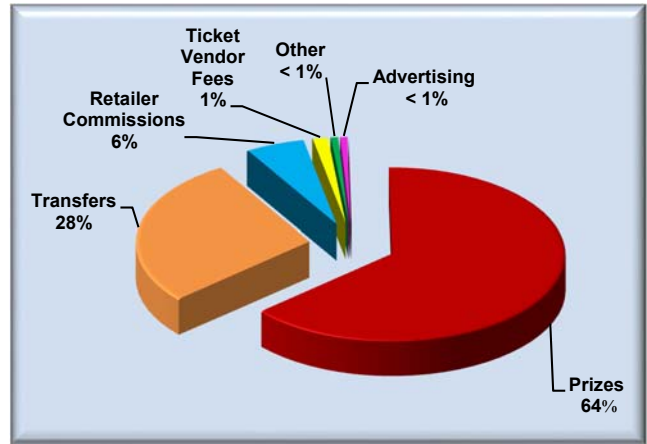
Section 24.121, Florida Statutes, stipulates that funds remaining in the Operating Trust Fund after the transfer to the EETF shall be used for the payment of administrative expenses of the Lottery. These expenses include Terminal game expenses, Scratch-Off ticket expenses, advertising, and other expenses required for the day-to-day operations of the Lottery.

The following charts show the major components of Lottery operating expenses and transfers as a percentage of ticket sales for the 2015 and 2014 fiscal years:

**Operating Expenses and Transfers
Fiscal Year 2014-15**



**Operating Expenses and Transfers
Fiscal Year 2013-14**



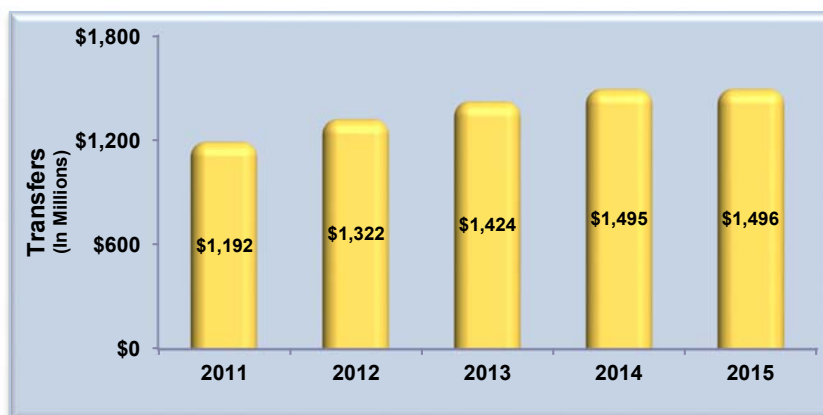
Prizes, commissions, and gaming vendor fees are directly related to sales and fluctuate accordingly. In fiscal year 2015, these expenses changed proportionally; yet as a percentage of total expenses they remained constant. The other expenses, which consisted of advertising, salary and benefits, professional fees, rent, maintenance, and depreciation, increased slightly. Fiscal year 2015 and 2014 administrative expenses were \$75.70 million and \$74.53 million, respectively.

Transfers

Since its inception, the Lottery has transferred \$28.4 billion to the EETF. The Lottery’s contribution to the EETF for fiscal year ended June 30, 2015, was \$1.50 billion. The Lottery has contributed over \$1 billion for the thirteenth consecutive year.

The following chart shows the total transfers to the EETF for the past five years:

**Department of the Lottery
Transfers to the EETF
(In Millions)**



ECONOMIC FACTORS AND FUTURE IMPACTS

The main economic factors affecting lottery sales are population growth, personal income changes, tourism, and competition for discretionary consumer spending. Florida's unemployment rate dropped from 6.2 percent in fiscal year 2014 to 5.6 percent during fiscal year 2015. In fiscal year 2015, Lottery sales exceeded \$5.58 billion, setting new sales records for Scratch-Off and total game sales. The Lottery's strategies have revolved around enhancing Terminal and Scratch-Off games, increasing retailer penetration in the State, and refreshing the Lottery's brand.

FINANCIAL CONTACT

The Lottery's financial statements and this MD&A are designed to give a general overview to the reader. If you have any questions regarding this report or require additional information, please contact the State of Florida, Department of the Lottery, Chief Financial Officer, 250 Marriott Drive, Capitol Complex, Tallahassee, Florida 32399.

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BASIC FINANCIAL STATEMENTS

**Department of the Lottery
Statements of Net Position
As of June 30, 2015, and June 30, 2014
(In Thousands)**

	<u>June 30, 2015</u>	<u>June 30, 2014</u>
Assets		
Current Assets:		
Cash and cash equivalents	\$ 136,697	\$ 124,629
Interest receivable	62	35
Accounts receivable, net	65,645	47,003
Prepaid expenses	148	8
Inventories	1,090	1,735
Security deposits	2,104	2,217
Total Current Assets	<u>205,746</u>	<u>175,627</u>
Noncurrent Assets:		
Restricted Assets		
Cash and cash equivalents	35,159	30,609
Securities lending income receivable	76	496
Deposit with MUSL	21,766	19,817
Investments, grand prize	372,266	441,503
Investments, security lending collateral	303,460	348,981
Total Restricted Assets	<u>732,727</u>	<u>841,406</u>
Capital assets, net	5,820	4,243
Total Noncurrent Assets	<u>738,547</u>	<u>845,649</u>
Total Assets	<u>944,293</u>	<u>1,021,276</u>
Deferred Outflows of Resources		
Pension related items	3,969	-
Total Deferred Outflows of Resources	<u>3,969</u>	<u>-</u>
Total Assets and Deferred Outflows of Resources	<u>\$ 948,262</u>	<u>\$ 1,021,276</u>

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

(Continued)

Department of the Lottery
Statements of Net Position
As of June 30, 2015, and June 30, 2014
(In Thousands)

	<u>June 30, 2015</u>	<u>June 30, 2014</u>
Liabilities		
Current Liabilities:		
Accounts payable and accrued liabilities	\$ 7,729	\$ 5,513
Prizes payable	128,514	104,078
Due to Educational Enhancement Trust Fund	67,371	55,409
Deposits payable	2,106	2,219
Compensated absences payable	409	585
Net pension liability	192	-
Total Current Liabilities	<u>206,321</u>	<u>167,804</u>
Current Liabilities Payable from Restricted Assets:		
Securities lending fees payable	47	40
Obligations under securities lending	317,044	363,953
Grand prizes payable	66,412	86,154
Total Current Liabilities Payable from Restricted Assets	<u>383,503</u>	<u>450,147</u>
Noncurrent Liabilities:		
Grand prizes payable from restricted assets	254,154	298,466
Compensated absences payable	3,455	3,189
Net pension liability	8,492	-
Other long-term liabilities	5,085	4,009
Total Noncurrent Liabilities	<u>271,186</u>	<u>305,664</u>
Total Liabilities	<u>861,010</u>	<u>923,615</u>
Deferred Inflows of Resources		
Pension related items	5,709	-
Total Deferred Inflows of Resources	<u>5,709</u>	<u>-</u>
Net Position		
Invested in capital assets	5,820	4,243
Restricted for undistributed appreciation on restricted investments	51,800	58,009
Restricted for MUSL	21,766	19,817
Restricted for future prizes or special prize promotions	21,528	15,592
Unrestricted	(19,371)	-
Total Net Position	<u>81,543</u>	<u>97,661</u>
Total Liabilities, Deferred Inflows of Resources, and Net Position	<u>\$ 948,262</u>	<u>\$ 1,021,276</u>

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

Department of the Lottery
Statements of Revenues, Expenses, and Changes in Net Position
Years Ended June 30, 2015, and June 30, 2014
(In Thousands)

	<u>June 30, 2015</u>	<u>June 30, 2014</u>
Operating Revenues		
Ticket sales	\$ 5,583,331	\$ 5,368,230
Bad debt expense	(1,263)	(1,337)
Terminal fees and miscellaneous	7,456	7,611
Retailer fees	196	206
Total Operating Revenues	<u>5,589,720</u>	<u>5,374,710</u>
Operating Expenses		
Prizes	3,627,939	3,431,092
Retailer commissions	311,981	298,651
Scratch-Off tickets	51,665	48,157
Terminal games	29,970	28,895
Advertising	37,513	37,486
Personal services	27,320	27,614
Other contractual services	8,344	7,656
Materials and supplies	2,078	1,057
Depreciation	441	715
Total Operating Expenses	<u>4,097,251</u>	<u>3,881,323</u>
Operating Income	<u>1,492,469</u>	<u>1,493,387</u>
Nonoperating Revenues (Expenses)		
Interest	4,032	2,776
Securities lending income	997	1,534
Securities lending fees	(505)	(327)
Investment management fees	(370)	(532)
Net appreciation (depreciation) in fair value of investments	12,604	13,718
Property disposition (loss)	64	124
Amortization of grand prizes payable	(18,040)	(22,911)
Total Nonoperating Revenues (Expenses), Net	<u>(1,218)</u>	<u>(5,618)</u>
Income Before Operating Transfers	<u>1,491,251</u>	<u>1,487,769</u>
Transfers to Educational Enhancement Trust Fund	<u>(1,496,371)</u>	<u>(1,495,409)</u>
Change in Net Position	<u>(5,120)</u>	<u>(7,640)</u>
Net Position, Beginning of Year, as originally reported	97,661	105,301
Implementation effect of GASB Statement No. 68	(10,998)	-
Net Position, Beginning Restated	<u>86,663</u>	<u>105,301</u>
Net Position, End of Year	<u>\$ 81,543</u>	<u>\$ 97,661</u>

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

Department of the Lottery
Statements of Cash Flows
Years Ended June 30, 2015, and June 30, 2014
(In Thousands)

	<u>June 30, 2015</u>	<u>June 30, 2014</u>
Operating Activities		
Ticket sales	\$ 5,563,425	\$ 5,366,452
Prizes paid to winners	(3,605,452)	(3,432,073)
Commissions paid and payments to retailers	(311,981)	(298,651)
Paid to vendors for goods and services	(126,956)	(125,973)
Paid to employees	(26,622)	(26,307)
Other operating revenue	7,652	7,817
Net Cash Provided by Operating Activities	<u>1,500,066</u>	<u>1,491,265</u>
Noncapital Financing Activities		
Payments to Educational Enhancement Trust Fund	(1,484,409)	(1,516,111)
Net Cash Used in Noncapital Financing Activities	<u>(1,484,409)</u>	<u>(1,516,111)</u>
Capital and Related Financing Activities		
Purchase of capital assets	(1,954)	(1,619)
Net Cash Used in Capital and Related Financing Activities	<u>(1,954)</u>	<u>(1,619)</u>
Investing Activities		
Cash received from maturity of grand prize investments	86,154	112,603
Cash paid to grand prizewinners upon maturity of grand prize investments	(86,154)	(112,603)
Security lending	(1,400)	(46,209)
Investment income, net of fees	4,315	4,712
Net Cash Provided by Investing Activities	<u>2,915</u>	<u>(41,497)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	<u>16,618</u>	<u>(67,962)</u>
Cash and Cash Equivalents, Beginning of Year	155,238	223,200
Cash and Cash Equivalents, End of Year	<u>\$ 171,856</u>	<u>\$ 155,238</u>
Reconciliation of Income from Operations to Net Cash Provided by Operating Activities:		
Income from operations	\$ 1,492,469	\$ 1,493,387
Adjustments to reconcile income from operations to net cash provided by operating activities:		
Depreciation	441	715
Changes in assets and liabilities		
(Increase) decrease in:		
Accounts receivable	(21,258)	(762)
Inventories	645	(872)
Prepaid expenses	(140)	(4)
Increase (decrease) in:		
Allowance for uncollectible accounts	779	(535)
Accounts payable and accrued liabilities	2,103	(1,607)
Prizes payable	24,436	(201)
Compensated absences payable	90	97
Net pension liability and related deferred outflows and inflows	(575)	-
Postemployment healthcare benefits payable	1,076	1,047
Net Cash Provided by Operating Activities	<u>\$ 1,500,066</u>	<u>\$ 1,491,265</u>
Noncash Investing, Capital and Financing Activities:		
Increase/(decrease) in fair value of investments	\$ (42,047)	\$ (57,946)

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

NOTES TO FINANCIAL STATEMENTS

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The State of Florida, Department of the Lottery (the Lottery) was established as a State agency with the enactment of the Florida Public Education Lottery Act (the Act) in 1987. The purpose of the Act is “to implement Section 15, Article X of the State Constitution in a manner that enables the people of the State to benefit from significant additional moneys for education and also enables the people of the State to play the best lottery games available.”

In evaluating the Lottery as a reporting entity, management has addressed all potential component units for which the Lottery may be financially accountable and, as such, be includable in the Lottery’s financial statements. The Lottery is financially accountable if it appoints a voting majority of the organization’s governing board and (1) it is able to impose its will on the organization or (2) there is a potential for the organization to provide specific financial benefit to or impose specific financial burden on the Lottery. Additionally, the primary government is required to consider other organizations for which the nature and significance of their relationship with the primary government is such that exclusion would cause the reporting entity’s financial statements to be misleading or incomplete. Management’s analysis has disclosed no component units that should be included in the Lottery’s financial statements.

B. Basis of Presentation

The Lottery is accounted for as a proprietary type enterprise fund. Enterprise funds are used to account for activities that are financed and operated in a manner similar to private business enterprises: (1) where the costs of providing goods and services to the general public on a continuing basis are to be financed through user charges; or (2) where the periodic determination of net income is considered appropriate. The Lottery is reported as an enterprise fund within the State of Florida’s Comprehensive Annual Financial Report.

C. Basis of Accounting

Basis of accounting refers to when the revenues, expenses, and related assets and liabilities are recognized in the accounts and reported in the financial statements. The financial statements are prepared on the accrual basis of accounting in accordance with generally accepted accounting principles. Under this method, revenues are recognized when they are earned and expenses are recognized when they are incurred.

The measurement focus of proprietary fund types is on a flow of economic resources method, which emphasizes the determination of net income, financial position, and cash flows. All fund assets and liabilities, current and noncurrent, are accounted for on the Statements of Net Position.

The Lottery’s operating revenues and expenses generally result from the sale and marketing of lottery tickets and the payment of related prizes. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

D. Cash and Cash Equivalents

The Lottery considers all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents. This includes cash in banks, repurchase agreements with financial institutions, petty cash, balances held by the State Board of Administration (SBA), and pooled investments in the State Treasury.

E. Investments

Florida Statutes authorize the Lottery to invest in certain instruments. The Lottery reports investments at fair value. Investments that are not publicly quoted are priced by a third party through a discounted cash flow method. Details of investments are included in Note II.

F. Allowance for Doubtful Accounts

The allowance for doubtful accounts is based on an analysis of collectability of accounts receivable, which considers the age of the accounts.

G. Inventories

Supply inventory and promotional items are valued at cost, using the first-in, first-out method. Supply inventory comprised game merchandise, prepaid postage, and prepaid tolls.

H. Prepaid Expenses

Prepaid expenses represent warranty agreements paid for during the current year but will not be consumed or used up until a future period.

I. Capital Assets

Capital assets are stated at cost less accumulated depreciation. As required by Chapter 273, Florida Statutes, a capitalization threshold of \$1,000 and useful life extending beyond one year are employed for tangible personal property. The Lottery's capitalization threshold for intangible assets is \$100,000. Depreciation on all capital assets is computed using the straight-line method over the following estimated useful lives:

Data processing equipment	3 to 5 years
Office furniture and fixtures	3 to 15 years
Vehicles and other equipment	3 to 20 years
Software	3 to 15 years

When capital assets are retired or otherwise disposed of, the costs and related accumulated depreciation are removed from the accounts and any resulting gain or loss is reflected in the Statements of Revenues, Expenses, and Changes in Net Position in the period of disposal. See Note V for more detailed information on capital assets.

J. Deferred Outflows of Resources

A consumption of net assets by the government that is applicable to a future reporting period is presented as a deferred outflow of resources.

K. Long-term Liabilities

Refer to Note VII. for information on grand prizes payable, compensated absences payable, postemployment healthcare benefits payable, and net pension liability, along with changes in long-term liabilities. Also, refer to Note IX. for additional information on net pension liability and postemployment healthcare benefits payable.

L. Compensated Absences

Employees earn the right to be compensated during absences for vacation, illness, and unused special compensatory leave earned for hours worked on legal holidays. Compensated absences for annual leave are recorded as a liability when the benefits are earned. Compensated absences for sick leave are calculated based on the vesting method. Within the limits established by law or rule, unused leave benefits are paid to employees upon separation from State service. The cost of vacation and calculated sick leave benefits is accrued in the period in which the benefits are earned. The compensated absences are based on current fiscal year-end salary rates and include employer social security and pension contributions at current rates.

M. Deferred Inflows of Resources

A deferred inflow of resources is an acquisition of net assets by the government that is applicable to a future reporting period.

N. Net Position

Net position includes categories for invested in capital assets, restricted for undistributed appreciation on restricted investments, restricted for future prizes or special prize promotions, restricted for the Multi-State Lottery Association (MUSL), and unrestricted net position resulting from liabilities for which no cash payments will be made. See Note I.V. for more information on unrestricted net position.

The invested in capital assets category represents the investment in capital assets, recorded at cost less accumulated depreciation.

The restricted for undistributed appreciation on restricted investments category represents the undistributed appreciation for all restricted asset accounts.

The restricted for future prizes or special prize promotions category represents the portion of unclaimed prize obligations legally reverted back to the Lottery and restricted for use in the payment of future prize pools or special prize promotions in accordance with Section 24.115(2), Florida Statutes.

The restricted for MUSL category represents the amount placed into reserve for the Florida Lottery by the MUSL in accordance with Rule 53ER12-6, Florida Administrative Code. See Note VI. for more information on MUSL.

O. Revenue Recognition

Lottery games are sold to the public by contracted retailers. Revenue is recognized when Terminal game tickets are sold to players and when books of Scratch-Off tickets are settled. Certain games

include tickets that entitle the holder to exchange one ticket for another (free tickets). Such tickets are deemed to be replacements and, therefore, are not included in ticket sales.

P. Commissions

Retailers receive a commission of 5 percent on ticket sales. The commission on ticket sales for games is based upon total tickets distributed to the players (including free tickets) which, when compared to revenue, causes the percentage to be slightly higher or lower than 5 percent at any given time. Additionally, retailers are paid commissions through a 1 percent cashing bonus on redemption of tickets (including free tickets).

Q. Prizes

In accordance with the Act, variable percentages of the gross revenue from the sale of Terminal and Scratch-Off lottery tickets shall be returned to the public in the form of prizes paid by the Lottery or retailers as authorized.

Prize expense for Terminal games is recorded based on prizes won by the players, as revenue is recognized. Any prize that remains unclaimed at the end of a 180-day period following a draw is considered unclaimed.

Prize expense for Scratch-Off games is recorded based on the predetermined prize structure for each game, as revenue is recognized. Any prize that remains unclaimed 60 days after a Scratch-Off game is closed is considered unclaimed.

Effective July 1, 2005, 80 percent of all unclaimed prize money is deposited in the Educational Enhancement Trust Fund (EETF). The remaining 20 percent of unclaimed prize money is added to the pool from which future prizes are to be awarded or used for special prize promotions and is reported as restricted for future prizes or special prize promotions.

All prizes are recorded at the actual amount except for the annuity-funded prizes, which are paid out on a deferred basis. The actual prize expense for these types of prizes is based on the present value of an annuity using the interest yield on the investments acquired to fund the annuity.

R. Self-Insurance

The Lottery participates in the various self-insurance programs established by the State of Florida for property and casualty losses and employee health insurance. Coverage includes property, general liability, automobile liability, workers' compensation, court-awarded attorney fees, and Federal civil rights actions. The property insurance program self-insures the first \$2 million per occurrence for all perils except named windstorm and flood. For named windstorm and flood, the property insurance program self-insures the first \$2 million per occurrence but with an annual aggregate retention of \$40 million. Commercial excess insurance is purchased for losses over the self-insured retention up to \$54 million per occurrence for named windstorm and flood losses and \$200 million per occurrence for all other perils. Workers' compensation is provided to comply with the applicable law. The employee health and dental insurance program provides for payment of medical claims of employees and covered dependents.

S. Use of 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, liabilities, restricted net position, revenues, and expenses, and disclosures of contingent assets and liabilities. Actual results could differ from those estimates.

T. Bad Debt Expense

Bad debt expense is reported as a reduction in gross revenue. Bad debt expense is recognized when a Lottery retailer's uncollected revenue is past due. The amount of expense is based on an accounts receivable age analysis. The bad debt expense for the fiscal years ended June 30, 2015, and June 30, 2014, was \$1,263,000 and \$1,337,000, respectively.

U. Accounting Changes

The Lottery implemented GASB Statement No. 68, *Accounting and Financial Reporting for Pensions, an amendment of GASB Statement No. 27*, and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date, an amendment of GASB Statement No. 68*. These standards require participants of cost-sharing multiple-employer defined benefit pension plans to recognize their proportionate share of plans' net pension liability and related deferred outflows of resources and deferred inflows of resources. As a participant of the Florida Retirement System and Retiree Health Insurance Subsidy Program defined benefit plans, implementation of these standards required the Lottery to recognize its portion of the plans' net pension liabilities and related deferred outflows of resources and deferred inflows of resources on the Statements of Net Position. Also, refer to Note IX. to the Notes to Financial Statements for further detail on the impact of the implementation.

V. Unrestricted Net Position Deficit

The unrestricted net position deficit of \$19,371,000 includes the cumulative effect of the Lottery's postemployment healthcare benefits, compensated absences, and net pension liabilities, along with the deferred outflows of resources and deferred inflows of resources for pension related items. As a result of these items being recorded for reporting purposes only and being excluded from the calculation of transfers to the EETF, the effect is a deficit balance in unrestricted net position.

W. Net Position Restatement

Net position, June 30, 2014, as previously reported (in thousands)	\$97,661
Implementation effect of GASB Statement No. 68 (Refer to Note IX.)	<u>(10,998)</u>
Net Position, June 30, 2014, as restated	<u>\$86,663</u>

II. CASH AND INVESTMENTS

A. Cash and Cash Equivalents

Cash is held in demand deposits at various financial institutions. These deposits, with a book value of approximately \$514,000 at June 30, 2015, and \$370,000 at June 30, 2014, were insured by either

the State's collateral for public deposits in accordance with Section 280.04, Florida Statutes, or Federal depository insurance. Cash held in time deposits for the security lending program with a book value of \$13,600,000 were exposed to custodial credit risk as these balances were uncollateralized and uninsured.

Chapter 280, Florida Statutes, generally requires public funds to be deposited in a Qualified Public Depository, which is a bank or savings association that is designated by the State of Florida Chief Financial Officer (State CFO) as authorized to receive deposits in the State and that meets the collateral requirements. The State CFO determines the collateral requirements and collateral pledging level for each Qualified Public Depository following guidelines outlined in Section 280.04, Florida Statutes, and Chapter 69C-2, Florida Administrative Code. Collateral pledging levels include 25, 50, 110, and 150 percent of a Qualified Public Depository's average daily deposit balance or, if needed, an amount as prescribed by the State CFO. Collateral may be held by another custodian with approval of the State CFO if conditions are met that protect the State's interest. Eligible collateral includes federal, federally-guaranteed, state and local government obligations, corporate bonds, and other securities designated allowable under conditions set by the State CFO.

Florida Statutes provides that if a loss to public depositors is not covered by deposit insurance and the proceeds from the sale of securities pledged by the defaulting depository, the difference will be provided by an assessment levied against other Qualified Public Depositories of the same type as the depository in default.

Due to the investing policy of the Lottery, book overdrafts were approximately \$1,019,000 at June 30, 2015, and \$3,178,000 at June 30, 2014, representing outstanding prize payment checks and retailer payment checks. These outstanding checks are included as a component of prizes payable and accounts payable. The Lottery has an agreement with a financial institution to honor prize payments and retailer payments, as they are presented to the bank, up to \$75 million.

Surplus cash is maintained in the State Treasury's general pool of investments. The State CFO pools funds from all State agencies. Included in the pool are primarily time deposits, U.S. Government securities, federal agency securities, commercial paper, corporate bonds and notes, and repurchase agreements. The Lottery's share of this investment pool was approximately \$157,742,000 and \$139,868,000 at June 30, 2015, and 2014, respectively. No allocation will be made as to the Lottery's share of the types of investments or their risk categories. The Lottery's share of the assets and liabilities arising from the securities lending agreements administered by the State Treasury will likewise not be carried on the Statements of Net Position since the State Treasury operates on a pooled basis and to do so may give the misleading impression that the Lottery itself has entered into such agreements. For further information, refer to the State of Florida's Comprehensive Annual Financial Report or publications of the State of Florida Department of Financial Services, Office of the Chief Financial Officer.

B. Investments, Grand Prize

The grand prize investments primarily consist of U.S. Government obligations held on the Lottery's behalf by the SBA. Grand prize investments and related grand prizes payable are not presented in current assets or liabilities. They are not part of current operations but instead are restricted assets

and liabilities that are held by the Lottery for grand prize winnings to be paid on a deferred basis if the cash payment option is not selected.

Grand prize investments are shown at fair value, and the related grand prizes payable are adjusted to the net present value using the yield on the investments. The difference between the fair value of the investments and the net present value of the grand prizes payable is reflected as restricted for undistributed appreciation on restricted investments in net position. This represents the unrealized gains on the investments. Because these investments are held restrictively for grand prizewinners, this balance is not available for transfer to the EETF.

Interest accreted on grand prize investments during the year is reflected as an increase in the carrying value of grand prizes payable on the Statements of Net Position, and as a nonoperating revenue (expense) on the Statements of Revenues, Expenses, and Changes in Net Position. Net appreciation (depreciation) in fair value of investments is reflected as a nonoperating revenue (expense) on the Statements of Revenues, Expenses, and Changes in Net Position, and takes into account all changes in fair value that occurred during the year, including purchases, maturities, and sales.

C. Investments, Security Lending Collateral

These investments consist of the fair value of investments made with cash collateral held by the SBA on the Lottery's behalf as part of a securities lending program.

The SBA, authorized by Section 215.47, Florida Statutes, participates in a security lending program involving grand prize investments. The Lottery, through the SBA, loans various securities to borrowers for collateral with a simultaneous agreement to return collateral for the same securities in the future. Collateral received from borrowers may be cash or U.S. Government securities. The SBA is contractually limited from pledging or selling collateral except in the event of borrower default. The contract with the lending agent requires it to indemnify the SBA if the borrowers fail to return the underlying securities or fail to pay income distributions on them. No significant violations of legal or contractual provisions occurred, and no losses resulted from borrower or lending agent defaults during fiscal years 2014 and 2015.

The Bank of New York Mellon (Mellon) is the agent for lending U.S. Treasury securities to various authorized brokers for cash or U.S. Government securities. Initially, collateral received shall be in the form of cash at 100 percent, or other securities valued at 102 percent, of the fair value of the securities loaned as required by the lending agreement. Borrowers must be approved for lending by Mellon's credit department. Mellon monitors the fair value of collateral provided and the securities on loan on a daily basis. Additional collateral is required if the fair value of the collateral for any loan is less than 100 percent of the fair value of the securities provided for such loan. The SBA had no credit risk exposure to borrowers at year-end.

The SBA had received \$317,044,000 of cash collateral for the lending program as of June 30, 2015, and \$363,953,000 as of June 30, 2014. At June 30, 2015, and June 30, 2014, the collateral that was held for the securities lending transactions exceeded the fair value of the securities underlying the agreements (including accrued interest). The cash was invested in securities authorized by the lending agreement. Authorized securities include primarily certificates of deposit, corporate and

medium term notes, asset-backed securities, and repurchase agreements. The invested cash collateral generally has a shorter maturity than the securities on loan.

A risk factor associated with this lending agreement is the potential for declines in the value of the invested holdings purchased with the cash collateral. If these investments must be liquidated, any shortfall between the value of the investments and the securities lending obligation becomes the responsibility of the Lottery. As of June 30, 2015, the unrealized shortfall was \$13,100 and as of June 30, 2014, the Lottery did not experience a shortfall.

Other risk factors associated with security lending include counterparty default and failure of the custodial bank to indemnify the Lottery.

Securities lending income and expenses for the year ended June 30, 2015, and 2014, consisted of (in thousands):

	<u>2015</u>	<u>2014</u>
Securities lending income	\$ 997	\$ 1,534
Less broker rebates	(447)	(313)
Less bank fees	(58)	(14)
Net securities lending revenue	<u>\$ 492</u>	<u>\$ 1,207</u>

D. Investment Credit Risk

Lottery grand prizewinner investments have been limited to U.S. Government guaranteed securities.

Listed below are Standard and Poor's (S&P) credit ratings for the lending program's invested cash collateral (in thousands):

As of June 30, 2015

Credit Ratings ⁽¹⁾	Total	Certificates of Deposit	Commercial Paper	Domestic Corporate Bonds & Notes	Domestic Non-Government		Repurchase Agreements ⁽²⁾
					Asset-backed Securities	International Corporate Bonds & Notes	
AAA	\$ 45,070	\$ -	\$ -	\$ 4,400	\$ 40,670	\$ -	\$ -
AA	54,457	8,099	-	25,130	-	18,306	2,922
A	14,308	-	-	14,308	-	-	-
A-1	3,099	-	3,099	-	-	-	-
Not Rated	75,232	24,000	-	-	26,479	-	24,753
	192,166	\$ 32,099	\$ 3,099	\$ 43,838	\$ 67,149	\$ 18,306	\$ 27,675
Not Rated ⁽²⁾	111,294	Repurchase agreements					
	<u>\$ 303,460</u>	Total					

Notes:

- (1) Ratings for investments are presented using S&P credit ratings. If S&P did not rate a security, including the collateral underlying repurchase agreements, the investments were presented as "Not Rated."
- (2) Collateral for repurchase agreements that are explicitly guaranteed by the U.S. Government do not require disclosure of credit quality.

As of June 30, 2014

Credit Ratings ⁽¹⁾	Total	Certificates of Deposit	Commercial Paper	Domestic Corporate Bonds & Notes	Domestic Non-Government Asset-backed Securities	International Corporate Bonds & Notes	International Non-Government Asset-backed Securities	Repurchase Agreements ⁽²⁾
AAA	\$ 25,390	\$ -	\$ -	\$ 9,044	\$ 16,346	\$ -	\$ -	\$ -
AA	89,593	11,212	-	52,241	-	24,112	-	2,028
A	40,537	5,406	-	26,219	-	8,912	-	-
A-1	25,803	-	25,803	-	-	-	-	-
Not Rated	121,351	97,734	8,802	8,101	5,129	-	1,222	363
	<u>302,674</u>	<u>\$ 114,352</u>	<u>\$ 34,605</u>	<u>\$ 95,605</u>	<u>\$ 21,475</u>	<u>\$ 33,024</u>	<u>\$ 1,222</u>	<u>\$ 2,391</u>
Not Rated ⁽²⁾	46,307	Repurchase agreements						
	<u>\$ 348,981</u>	Total						

- Notes:
- (1) Ratings for investments are presented using S&P credit ratings. If S&P did not rate a security, including the collateral underlying repurchase agreements, the investments were presented as "Not Rated."
 - (2) Collateral for repurchase agreements which are explicitly guaranteed by the U.S. Government do not require disclosure of credit quality.

The State Treasury Investment Pool's current rating by S&P is A+f as of June 30, 2015.

E. Investment Interest Rate Risk

The investment policy objective is to match maturities of investments with the maturities of the Lottery prizewinner annuities. Therefore, investments are held to maturity after they are purchased thereby eliminating interest rate risk. Listed below are the Lottery's investments in U.S. Treasury Strips (in thousands):

As of June 30, 2015		As of June 30, 2014	
Time to Maturity	Fair Value	Time to Maturity	Fair Value
< 1 year	\$ 66,412	< 1 year	\$ 86,115
> 1 year to 3 years	69,793	> 1 year to 3 years	109,955
> 3 years to 5 years	37,425	> 3 years to 5 years	42,903
> 5 years to 10 years	85,887	> 5 years to 10 years	85,612
> 10 years to 15 years	83,095	> 10 years to 15 years	70,014
> 15 years to 20 years	16,003	> 15 years to 20 years	32,927
> 20 years to 25 years	9,134	> 20 years to 25 years	8,618
> 25 years	4,517	> 25 years	5,359
Total	<u>\$ 372,266</u>	Total	<u>\$ 441,503</u>

The Lottery contracts with the SBA to execute the securities lending program. The securities lending authorization agreement between Mellon and the SBA requires that the maximum weighted average portfolio maturity not exceed 90 days. The lending program invests a significant amount of its assets in floating rate securities and limits the maximum reset period for interest rate changes to six months.

Next reset dates are used in the calculation of weighted average maturity. Listed below are the weighted average maturities for the lending program's invested cash collateral:

Investment Type	June 30, 2015		June 30, 2014	
	Fair Value (Thousands)	Weighted Average Maturity (Days)	Fair Value (Thousands)	Weighted Average Maturity (Days)
Certificates of Deposit	\$ 32,099	55	\$ 114,352	55
Commercial Paper	3,099	59	34,605	73
Domestic Corporate Bonds & Notes	43,838	46	95,605	48
Domestic Non-government Asset-backed Securities	67,149	19	21,475	23
International Corporate Bonds & Notes	18,306	60	33,024	57
International Non-government Asset-backed Securities	-	-	1,222	14
Repurchase Agreements	138,969	1	48,698	1
Total Fair Value	\$ 303,460		\$ 348,981	
Portfolio weighted average maturity		21		45

The effective duration of the State Treasury Investment Pool at June 30, 2015, and June 30, 2014, was approximately 2.67 years and 2.57 years, respectively.

F. Investment Concentration of Credit Risk

Since all long-term investments (other than in the securities lending program) are in U.S. Government guaranteed securities, the Lottery has not adopted a policy regarding concentration of credit risk. The securities lending program has established investment concentration of credit risk policies that limit the aggregate exposure to any one issuer or guarantor that is not the U.S. Government or guaranteed by the U.S. Government to 10 percent of the book value of the lending program's invested cash collateral. No invested cash collateral exceeded the 10 percent limitation.

G. Investment Custodial Credit Risk

Custodial credit risk is defined as the risk that an entity may not recover securities held by another party. The Lottery does not have a formal policy regarding custodial credit risk. The custodian for the SBA-administered lending program is also the counterparty to the investment transactions. Therefore, the amount of investments subject to investment custodial credit risk at June 30, 2015, and June 30, 2014, was \$303,460,000 and \$348,981,000, respectively.

At June 30, 2015, and June 30, 2014, all non-lending investments held were either insured or registered and held by the Lottery or its agents in the Lottery's name and thus were not subject to custodial credit risk.

H. Foreign Currency Risk

The Lottery had no exposure to foreign currency risk as of June 30, 2015, and June 30, 2014.

I. Investment Summary

The following schedule summarizes all investments and investments loaned under securities lending agreements at June 30 (in thousands):

Investment Type	June 30, 2015 Carrying Value	June 30, 2014 Carrying Value
Commercial Paper	\$ 3,099	\$ 34,605
Certificates of Deposit	32,099	114,352
Repurchase Agreements	138,969	48,698
U.S. Government Obligations & Federally Guaranteed Obligations	61,881	84,598
Domestic Corporate Bonds & Notes	43,838	95,605
Domestic Non-government Asset-backed Securities	67,149	21,475
International Corporate Bonds & Notes	18,306	33,024
International Non-government Asset-backed Securities	-	1,222
Investments Held by Others Under Securities Lending Agreements - U.S. Obligations	310,385	356,905
Pooled Investments with State Treasury	157,742	139,868
Total Investments	\$ 833,468	\$ 930,352

The following schedules reconcile cash and investments to the Statements of Net Position at June 30 (in thousands):

	June 30, 2015			
	Investments	Cash at Financial Institutions	Cash at State Treasury	Totals
Cash and cash equivalents	\$ 136,213	\$ 376	\$ 108	\$ 136,697
Restricted cash and cash equivalents	21,529	13,630	-	35,159
Investments, grand prize	372,266	-	-	372,266
Investments, security lending collateral	303,460	-	-	303,460
Totals	\$ 833,468	\$ 14,006	\$ 108	\$ 847,582

	June 30, 2014			
	Investments	Cash at Financial Institutions	Cash at State Treasury	Totals
Cash and cash equivalents	\$ 124,276	\$ 326	\$ 27	\$ 124,629
Restricted cash and cash equivalents	15,592	15,017	-	30,609
Investments, grand prize	441,503	-	-	441,503
Investments, security lending collateral	348,981	-	-	348,981
Totals	\$ 930,352	\$ 15,343	\$ 27	\$ 945,722

III. ACCOUNTS RECEIVABLE

Accounts receivable as of June 30, consisted of (in thousands):

	<u>2015</u>	<u>2014</u>
Ticket sales receivable	\$ 68,422	\$ 48,972
Other receivables	97	125
Total receivables	<u>68,519</u>	<u>49,097</u>
Less allowance for doubtful accounts	<u>(2,874)</u>	<u>(2,094)</u>
Accounts receivable, net	<u><u>\$ 65,645</u></u>	<u><u>\$ 47,003</u></u>

IV. SECURITY DEPOSITS AND DEPOSITS PAYABLE

The Lottery receives certificates of deposit and cashier's checks from certain vendors and retailers in order to secure contract performance. Certificates of deposit are held in trust by the State with any interest earnings being credited to the vendor or retailer. Cashier's checks are held as cash by the Lottery. These deposits are established to reduce the potential financial risk to the Lottery in the event of a breach of contract. The certificates appear on the Statements of Net Position, in assets as security deposits, and in liabilities, as deposits payable. The checks appear on the Statements of Net Position, in assets as cash, and in liabilities, as deposits payable.

V. CAPITAL ASSETS

Changes in capital assets are summarized as follows (in thousands):

	<u>Balance</u> <u>30-Jun-13</u>	<u>2013-14</u>		<u>Balance</u> <u>30-Jun-14</u>	<u>2014-15</u>		<u>Balance</u> <u>30-Jun-15</u>
		<u>Increase</u>	<u>Decrease</u>		<u>Increase</u>	<u>Decrease</u>	
Data processing equipment	\$ 3,407	\$ 494	\$ (95)	\$ 3,806	\$ 325	\$ (280)	\$ 3,851
Office equipment and fixtures	5,839	36	(1,570)	4,305	216	(190)	4,331
Vehicles and other equipment	3,541	325	(245)	3,621	1,249	(298)	4,572
Software and other intangibles	2,123	1,652	(920)	2,855	1,917	(1,772)	3,000
	<u>14,910</u>	<u>2,507</u>	<u>(2,830)</u>	<u>14,587</u>	<u>3,707</u>	<u>(2,540)</u>	<u>15,754</u>
Less accumulated depreciation	11,695	747	(2,098)	10,344	441	(851)	9,934
Total capital assets, net	<u><u>\$ 3,215</u></u>	<u><u>\$ 1,760</u></u>	<u><u>\$ (732)</u></u>	<u><u>\$ 4,243</u></u>	<u><u>\$ 3,266</u></u>	<u><u>\$ (1,689)</u></u>	<u><u>\$ 5,820</u></u>

VI. MULTI-STATE LOTTERY ASSOCIATION

MUSL is an unincorporated government-benefit voluntary association created for the purpose of administering joint lottery games. MUSL included 34 state lottery entities, the District of Columbia, Puerto Rico, and the Virgin Islands during fiscal year 2015. This association offers the Powerball with Powerplay, Mega Millions with Megaplier, and several other Terminal games in participating states. The chief executive officer of each member lottery serves on the MUSL board of directors.

As a member of MUSL, the Lottery is required to contribute to various prize reserve funds maintained by MUSL. The prize reserve funds serve as a contingency reserve to protect MUSL from unforeseen prize payments. MUSL periodically reallocates the prize reserve funds among the states based on relative Powerball with Powerplay and Mega Millions with Megaplier sales levels. All remaining funds remitted, and the related interest earnings (net of administrative costs), will be returned to the Lottery upon leaving MUSL, less any portion of unanticipated prize claims that may have been paid from the fund.

As of June 30, 2015, and June 30, 2014, the Lottery had deposits with MUSL of \$21,765,512, and \$19,817,102, respectively, representing the Lottery's deposits of reserve funds.

A copy of the MUSL financial statements may be obtained by submitting a written request to MUSL, 4400 N.W. Urbandale Drive, Urbandale, Iowa 50322.

VII. LONG-TERM LIABILITIES

A. Grand Prizes Payable

Grand prizes payable at June 30 consisted of (in thousands):

	2015	2014
FLORIDA LOTTO grand prizes (face value)	\$ 343,596	\$ 424,857
MEGA MONEY grand prizes (face value)	8,303	8,058
Win for Life grand prizes (face value)	7,752	11,202
Flamingo Fortune Game Show grand prizes (face value)	300	400
Win a Million grand prizes (face value)	150	200
Lucky for Life grand prizes (face value)	20,550	20,050
Set for Life grand prizes (face value)	1,560	1,740
Cash Spectacular grand prizes (face value)	400	450
Cash for Life grand prizes (face value)	180	190
Loaded for Life grand prizes (face value)	2,550	2,650
Billion Dollar Blockbuster grand prizes (face value)	7,350	7,900
Gas for Life grand prizes (face value)	168	174
2 Million Dollar Casino Action grand prizes (face value)	1,500	1,600
Million Dollar Holiday grand prizes (face value)	800	850
Week for Life grand prizes (face value)	37,674	38,818
Monopoly grand prizes (face value)	3,320	3,510
Million Wishes grand prizes (face value)	850	900
X's The Cash grand prizes (face value)	3,590	3,770
\$3 Million Flamingo grand prizes (face value)	2,700	2,850
Gold Rush grand prizes (face value)	8,460	2,850
Less imputed interest	<u>(131,187)</u>	<u>(148,399)</u>
Net present value of grand prizes payable	<u>\$ 320,566</u>	<u>\$ 384,620</u>
Current prizes payable from restricted assets	\$ 66,412	\$ 86,154
Noncurrent prizes payable from restricted assets	<u>254,154</u>	<u>298,466</u>
Total grand prizes payable	<u><u>\$ 320,566</u></u>	<u><u>\$ 384,620</u></u>

The following depicts by fiscal year the value (in thousands) of the grand prize annuities to pay prizewinners:

<u>Year Ending June 30</u>	<u>Amount</u>
2016	\$ 66,471
2017	44,909
2018	25,738
2019	19,833
2020	19,833
2021-2025	101,707
2026-2030	117,139
2031-2035	26,804
2036-2040	18,467
2041-2045	10,852
Grand prizes (face value)	451,753
Less imputed interest	(131,187)
Net present value of grand prizes payable	\$ 320,566

B. Compensated Absences Payable

Compensated absences payable at June 30 consisted of (in thousands):

	<u>2015</u>	<u>2014</u>
Current compensated absences	\$ 409	\$ 585
Noncurrent compensated absences	3,455	3,189
Total	\$ 3,864	\$ 3,774

C. Changes in Long-Term Liabilities

Changes in long-term liabilities are summarized as follows (in thousands):

	<u>2014-15</u>				
	<u>Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u>	<u>Amount Due Within One Year</u>
	<u>June 30, 2014</u>			<u>June 30, 2015</u>	
Grand prizes payable	\$ 384,620	\$ 23,897	\$ (87,951)	\$ 320,566	\$ 66,412
Compensated absences payable	3,774	1,124	(1,034)	3,864	409
Postemployment healthcare benefits payable	4,009	1,076	-	5,085	-
Net pension liability	-	12,758	(4,074)	8,684	192
Total long-term liabilities	\$ 392,403	\$ 38,855	\$ (93,059)	\$ 338,199	\$ 67,013

	<u>2013-14</u>				
	<u>Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u>	<u>Amount Due Within One Year</u>
	<u>June 30, 2013</u>			<u>June 30, 2014</u>	
Grand prizes payable	\$ 456,193	\$ 41,030	\$ (112,603)	\$ 384,620	\$ 86,154
Compensated absences payable	3,677	1,010	(913)	3,774	585
Postemployment healthcare benefits payable	2,962	1,047	-	4,009	-
Total long-term liabilities	\$ 462,832	\$ 43,087	\$ (113,516)	\$ 392,403	\$ 86,739

See Note IX. for additional information regarding the net pension liability and the postemployment healthcare benefits payable.

VIII. DUE TO EDUCATIONAL ENHANCEMENT TRUST FUND

In accordance with the Act, effective July 1, 2005, variable percentages of the gross revenue from the sale of Terminal games and Scratch-Off lottery tickets as determined by the Lottery, and other earned revenue, excluding application processing fees, shall be deposited in the EETF as provided in Section 24.121, Florida Statutes, as amended. The amount transferred to the EETF was \$1,496,371,000 for the fiscal year ended June 30, 2015, (26.8 percent of revenues), and \$1,495,409,000 (27.8 percent of revenues) for the fiscal year ended June 30, 2014.

Because the net appreciation in fair value of investments and amortization of grand prizes payable, included in nonoperating revenue and expenses, relate to valuations of the restricted grand prize investments and grand prizes payable, they are excluded from the determination of transfers to the EETF.

Effective July 1, 2005, provisions of the Act relating to the allocation of revenues for public education were revised. The changes in the provisions were designed to maximize the transfers of moneys to the EETF. These revisions resulted in changes in the methodology used to calculate the transfer based on a business model of revenue minus expenses rather than a percent of revenue.

The amount due to the EETF at June 30, 2015, and June 30, 2014, was as follows (in thousands):

	June 30, 2015	June 30, 2014
Terminal ticket sales	\$ 1,859,336	\$ 1,951,087
Average percent transferred	37%	38%
Transfer of Terminal ticket sales ¹	<u>688,241</u>	<u>744,066</u>
Unclaimed Terminal ticket prizes	32,933	28,848
Percent transferred	80%	80%
Transfer of unclaimed Terminal ticket prizes	<u>26,346</u>	<u>23,078</u>
Scratch-Off ticket sales	3,723,995	3,417,143
Average percent transferred	20%	20%
Transfer of Scratch-Off ticket sales ¹	<u>750,341</u>	<u>692,063</u>
Unclaimed Scratch-Off ticket prizes	14,737	31,012
Percent transferred	80%	80%
Transfer of unclaimed Scratch-Off ticket prizes	<u>11,790</u>	<u>24,810</u>
Nonoperating revenues (expenses), net	(1,218)	(5,618)
Add:		
Net (appreciation) depreciation in fair value of investments	(12,604)	(13,718)
Amortization of grand prizes payable	18,040	22,911
Total Nonoperating revenues, net	<u>4,218</u>	<u>3,575</u>
Change in methodology for addressing postemployment healthcare expenses and compensated absences expenses	7,783	-
Terminal fees and miscellaneous revenue	<u>7,652</u>	<u>7,817</u>
Due for the year	<u>1,496,371</u>	<u>1,495,409</u>
Balance due, beginning of year	55,409	76,111
Paid during the year	<u>(1,484,409)</u>	<u>(1,516,111)</u>
Due to Educational Enhancement Trust Fund, June 30	<u><u>\$ 67,371</u></u>	<u><u>\$ 55,409</u></u>

¹ Amounts do not foot due to rounding of average percent transferred.

IX. PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS

A. Retirement Programs

The Florida Department of Management Services (DMS) administers the State's pension plans referenced below. Financial statements and other required supplementary information for the plans are included in the Florida Department of Management Services' Florida Retirement System Pension Plan and Other State-Administered Systems Comprehensive Annual Financial Report (Pension CAFR). Copies of the Pension CAFR can be obtained from the DMS, Division of Retirement (Division), Bureau of Research and Member Communications, P.O. Box 9000, Tallahassee, Florida 32315-9000; by telephone at 877-377-1888 or 850-907-6500; by e-mail at rep@dms.myflorida.com; or at the Division's Web site (www.frs.myflorida.com).

Florida Retirement System. The Florida Retirement System (FRS) is a State-administered cost-sharing multiple-employer retirement plan administered by the DMS that offers members

(Regular Class, Special Risk Class, and Senior Management Service Class)¹ an initial choice between participating in a defined benefit plan (FRS Pension Plan) or a defined contribution plan (FRS Investment Plan) and one additional choice to change plans before retirement. FRS provisions are established by Chapters 121, 122, and 238, Florida Statutes; Chapter 112, Part IV, Florida Statutes; and Florida Retirement System Rules, Chapter 60S, Florida Administrative Code; wherein eligibility, required employer and employee contributions, and benefits are defined and described in detail. Essentially, all employees of participating employers in regularly established positions must be enrolled as members of the FRS or other non-integrated defined contribution plans in lieu of FRS membership.

Benefits in the FRS Pension Plan vest at six years of service for members initially enrolled before July 1, 2011, and at eight years for members initially enrolled on or after July 1, 2011. For members initially enrolled before July 1, 2011, Special Risk Class members are eligible for normal retirement benefits at age 55 and vested or after 25 years of service at any age. All other members initially enrolled before July 1, 2011, are eligible for normal retirement benefits at age 62 and vested or at any age after 30 years of service. For members initially enrolled on or after July 1, 2011, Special Risk Class members are eligible for normal retirement benefits at age 60 and vested or after 30 years of service at any age. All other members initially enrolled on or after July 1, 2011, are eligible for normal retirement benefits at age 65 and vested or at any age after 33 years of service.

Early retirement is available but imposes a penalty for each year a member retires before his or her normal retirement age. Retirement, disability, and death benefits are provided. Retirees with service prior to July 1, 2011, receive annual cost-of-living adjustments. Retirees only with service accrued on or after July 1, 2011, do not receive annual cost-of-living adjustments. Benefits are calculated at retirement based on the age, years of service, accrual value by membership class, and average final compensation (average of highest five fiscal years' salaries if initially enrolled before July 1, 2011, or the average of highest eight fiscal years' salaries if initially enrolled on or after July 1, 2011).

Members of the FRS Pension Plan who reach normal retirement may participate in the Deferred Retirement Option Program (DROP), subject to provisions of Section 121.091(13), Florida Statutes. DROP participants are technically retired, deferring termination and receipt of monthly retirement benefits for up to 60 months. During the period of DROP participation, deferred monthly benefits are held in the FRS Trust Fund and accrue interest.

FRS Investment Plan benefits are established in Part II, Chapter 121, Florida Statutes, and participation is available to all FRS members in lieu of the FRS Pension Plan. Members vest after one year of creditable service for Investment Plan contributions. If an accumulated benefit obligation for service credit originally earned under the FRS Pension Plan is transferred to the FRS Investment Plan, six years of service (including the service credit represented by the transferred funds) is required to be vested for these funds and the earnings on the funds. Benefits under the FRS Investment Plan are based on the account balance at retirement composed of contributions plus investment gains less investment losses and fees. Employer and employee contributions are a percentage of salary based

¹ Regular Class includes members of the FRS who do not qualify for membership in the other classes. Special Risk Class includes members who are employed as law enforcement officers and the Senior Management Service Class includes members in senior management level positions.

on membership class. Contributions are directed to individual member accounts and the individual members allocate contributions and account balances among various approved investment choices offered under the plan.

The Florida Legislature established uniform contribution rates for participating FRS employees. FRS employers pay the same contribution rate by membership class regardless of whether the members participate in the FRS Pension Plan or FRS Investment Plan. Contribution rates as a percentage of gross salary are as follows:

Class	Employee Rate	Employer Rate	Employee Rate	Employer Rate
	Fiscal Year Ended June 30, 2015	Fiscal Year Ended June 30, 2015 ⁽¹⁾	Fiscal Year Ended June 30, 2014	Fiscal Year Ended June 30, 2014 ⁽¹⁾
Senior Management Service	3.00 percent	21.14 percent	3.00 percent	18.31 percent
Regular	3.00 percent	7.37 percent	3.00 percent	6.95 percent
Special Risk	3.00 percent	19.82 percent	3.00 percent	19.06 percent
DROP - Applicable to members from all of the above classes	0.00 percent	12.28 percent	0.00 percent	12.84 percent

Note: (1) Total employer contribution rates above include 1.26 percent and 1.20 percent for the fiscal years ended June 30, 2015, and June 30, 2014, respectively, for the Retiree Health Insurance Subsidy Program. Also, employer rates, other than for DROP participants, include 0.04 percent and 0.03 percent for fiscal year ended June 30, 2015, and June 30, 2014, respectively, for administration costs of the financial education program and the FRS Investment Plan. Required employee contributions are deducted on a pre-tax basis.

FRS Contributions and Contributions as a Percentage of Covered Payroll. The Lottery's employer contributions and contribution as a percentage of covered payroll for the FRS Pension Plan and FRS Investment Plan for the fiscal years ended June 30, 2015, June 30, 2014, and June 30, 2013, are as follows:

Plan	Fiscal Year Ended		
	June 30, 2015	June 30, 2014	June 30, 2013
Employer Contributions:			
FRS Pension Plan	\$ 1,354,333	\$ 1,184,595	\$ 673,580
FRS Investment Plan	\$ 328,836	\$ 297,945	\$ 178,175
Contributions as a Percentage of Covered Payroll:			
FRS Pension Plan	8.47%	7.28%	4.26%
FRS Investment Plan	9.75%	8.67%	5.51%

Senior Management Service Optional Annuity Program. Some Lottery employees also participate in the Senior Management Service Optional Annuity Program (SMSOAP). Offered in lieu of FRS participation, the SMSOAP is a defined contribution plan that provides retirement and death benefits to the participant pursuant to Section 121.055, Florida Statutes. Participants have full and immediate vesting of all contributions paid on their behalf to the participating provider companies to invest as directed by the participants. Employees in eligible State positions may make an irrevocable

election to participate in the SMSOAP in lieu of the Senior Management Service Class. Employers contributed 6.27 percent of covered payroll for July 2012 through June 2015. This contribution rate includes a contribution that would otherwise be paid to the Retiree Health Insurance Subsidy Program (HIS) described below so the SMSOAP retiree is not eligible to receive monthly HIS benefits. A participant may contribute by salary reduction an amount not to exceed the percentage contributed by the employer. The Lottery's contributions for the fiscal years ended June 30, 2015, June 30, 2014, and June 30, 2013, totaled \$40,134, \$33,575, and \$13,103 respectively.

Retiree Health Insurance Subsidy Program. The HIS was created by the Florida Legislature in 1987 to assist FRS retirees in paying health insurance costs. HIS is a non-qualified, cost-sharing multiple-employer defined benefit pension plan established under Section 112.363, Florida Statutes. For the fiscal years ended June 30, 2015, 2014, and 2013, eligible retirees or beneficiaries received a monthly HIS payment equal to the number of years of creditable service completed at the time of retirement multiplied by \$5. The payments to individual retirees or beneficiaries were at least \$30 but not more than \$150 per month. To be eligible to receive HIS, an FRS retiree must apply for the benefit, certify health insurance coverage, which can include Medicare or TRICARE, and be approved.

HIS is funded by required contributions from FRS participating employers. For the fiscal years ended June 30, 2015, 2014, and 2013, required contributions were 1.26 percent, 1.20 percent, and 1.11 percent, respectively, of payroll for all active employees covered by the FRS, pursuant to Section 112.363, Florida Statutes. For the fiscal years ended June 30, 2015, 2014, and 2013, the Lottery contributed \$215,070, \$197,280, and \$173,089, respectively, in employer contributions to the HIS. HIS contributions are deposited in a DMS trust fund from which HIS payments are authorized. HIS benefits are not guaranteed and are subject to legislative appropriation. If these contributions or appropriation fail to provide full subsidy benefits to all participants, the Legislature may reduce or cancel the subsidy payments.

Deferred Compensation Plan. The Lottery, through the State of Florida, offers its employees a deferred compensation plan created in accordance with Section 457 of the Internal Revenue Code. The plan (refer to Section 112.215, Florida Statutes), available to all regular payroll State employees, permits them to defer a portion of their salaries until future years. The deferred compensation is not available to employees until termination, retirement, death, or an unforeseen emergency.

All amounts of compensation deferred under the plan, all property and rights purchased with those amounts, and all income attributable to those amounts, property, or rights are held in trust for the exclusive benefit of participants and their beneficiaries as mandated by 26 USC 457(g)(1).

The Lottery does not contribute to the plan. Participation under the plan is solely at the discretion of the employee.

The State has no liability for losses under the plan but does have the duty of due care that would be required of an ordinary and prudent investor. Pursuant to Section 112.215, Florida Statutes, the Deferred Compensation Trust Fund is created in the State Treasury.

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions. Effective July 1, 2014, the Lottery implemented the

provisions of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions, an amendment of GASB Statement No. 27*, which significantly changed the Lottery's accounting for pension amounts related to the two defined benefit plans it participates in, the FRS Pension Plan and the HIS (Plans).

For purposes of measuring the net pension liabilities, pension expense, and related deferred outflows/inflows of resources, information about the fiduciary net position of the Plans and additions to/deductions from the Plans' fiduciary net position have been determined on the same basis as they are reported by the DMS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when currently due and payable in accordance with the benefit terms. Investments are reported at fair value. Detailed information about the Plans' fiduciary net position is available in the Pension CAFR.

At June 30, 2015, the Lottery reported a net pension liability of \$3,299,714 for its proportionate share of the FRS Pension Plan's net pension liability and \$5,384,704 for its proportionate share of the HIS net pension liability, for a total net pension liability of \$8,684,418. The net pension liability was measured as of June 30, 2014, and the total pension liability used to calculate the net pension liability was based on an actuarial valuation as of July 1, 2014. The Lottery's proportionate share of the net pension liability was based on 2013-14 fiscal year contributions to the Plans relative to the total 2013-14 fiscal year contributions of all participating members. At June 30, 2014, the Lottery's proportionate share of the FRS Pension Plan net pension liability was 0.054080631 percent, which was a 26.3 percent increase from its proportionate share measured as of June 30, 2013, of 0.042831573 percent. The Lottery's proportionate share of the HIS net pension liability at June 30, 2014, was 0.057588909 percent, which was a 0.12 percent increase from its proportion as of June 30, 2013, of 0.057517866 percent. For the fiscal year ended June 30, 2015, the Lottery recognized pension expense of \$619,211 for the FRS Pension Plan and \$374,777 for the HIS, for pension expense totaling \$993,988. At June 30, 2015, the Lottery reported deferred outflows of resources and deferred inflows of resources related to the Plans from the following sources:

FRS Pension Plan

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual experience	\$ -	\$ 204,196
Changes in assumptions	571,456	-
Net difference between projected and actual earnings on pension plan investments	-	5,504,471
Changes in proportion and differences between employer contributions and proportionate share of contributions	1,629,089	-
Employer contributions subsequent to the measurement date	1,354,333	-
Totals	\$ 3,554,878	\$ 5,708,667

HIS

	Deferred Outflows of Resources
Difference between expected and actual experience	\$ -
Changes in assumptions	191,609
Net difference between projected and actual earnings on pension plan investments	2,585
Changes in proportion and differences between employer contributions and proportionate share of contributions	5,327
Employer contributions subsequent to the measurement date	215,070
Total	\$ 414,591

The Lottery's contributions subsequent to the measurement date of \$1,354,333 for the FRS Pension Plan and \$215,070 for the HIS are reported as deferred outflows of resources and will be recognized as a reduction of the total net pension liability in the fiscal year ended June 30, 2016. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year Ending June 30	FRS Pension Plan	HIS	Totals
2016	\$ (735,224)	\$ 27,989	\$ (707,235)
2017	(735,224)	27,989	(707,235)
2018	(735,224)	27,989	(707,235)
2019	(735,224)	27,989	(707,235)
2020	(735,224)	27,989	(707,235)
2021 - 2023	167,996	59,579	227,575
	\$ (3,508,124)	\$ 199,524	\$ (3,308,600)

Actuarial Methods and Assumptions. Actuarial assumptions for both defined benefit cost-sharing plans, the FRS Pension Plan and the HIS, are reviewed annually by the Florida Retirement System Actuarial Assumptions Conference. The most recent experience study for the FRS Pension Plan was completed in 2014 for the period July 1, 2008, through June 30, 2013. Because the HIS is funded on a pay as you go basis, no experience study has been completed for this program.

The total pension liability for each of the defined benefit plans was determined by an actuarial valuation as of July 1, 2014, using the entry age normal actuarial cost method. Inflation increases for both plans is assumed at 2.60 percent. Payroll growth for both Plans is assumed at 3.25 percent.

Both the discount rate and the long-term expected rate of return used for FRS Pension Plan investments are 7.65 percent. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the current contribution rate and that contributions from participating employers will be made at the statutorily required rates. Based on these assumptions, the FRS Pension Plan's fiduciary net position was projected to be available to make all projected future benefit payments to current active and inactive employees. Therefore, the

discount rate for calculating the total pension liability is equal to the long-term expected rate of return and was applied to all periods of projected benefit payments to determine the total pension liability.

Because the HIS uses a pay-as-you-go funding structure, a municipal bond rate of 4.29 percent was used to determine the total pension liability for the plan. Mortality assumptions for both plans were based on the Generational RP-2000 with Projection Scale BB tables (refer to the valuation reports at www.frs.myflorida.com for more information).

There were no changes in benefit terms for either the FRS Pension Plan or the HIS that affected the total pension liability since the prior measurement date. There were no changes between the measurement date and the reporting date which significantly impact the Lottery's proportionate share of the net pension liability, deferred outflows of resources, deferred inflows of resources, and pension expense for either the FRS Pension Plan or the HIS.

The following changes in actuarial assumptions occurred in 2014:

- FRS Pension Plan: As of June 30, 2014, the inflation rate assumption was decreased from 3.00 percent to 2.60 percent, the real payroll growth assumption was decreased from 1.00 percent to 0.65 percent, and the overall payroll growth rate assumption was decreased from 4.00 percent to 3.25 percent. The long-term expected rate of return decreased from 7.75 percent to 7.65 percent.
- HIS: The municipal rate used to determine total pension liability decreased from 4.63 percent to 4.29 percent.

The long-term expected rate of return on FRS Pension Plan investments was determined using a forward-looking capital market economic model, which includes an adjustment for the inflation assumption. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
Cash	1.00%	3.11%
Intermediate-term bonds	18.00%	4.18%
High yield bonds	3.00%	6.79%
Broad U.S. equities	26.50%	8.51%
Developed foreign equities	21.20%	8.66%
Emerging market equities	5.30%	11.58%
Private equity	6.00%	11.80%
Hedge funds / absolute return	7.00%	5.81%
Real estate (property)	12.00%	7.11%
	<u>100.00%</u>	

Sensitivity Analysis. The following tables demonstrate the sensitivity of the net pension liability to changes in the discount rate. The sensitivity analysis shows the impact to the Lottery's proportionate share of each plan's net pension liability if the discount rate was 1.00 percent higher or 1.00 percent lower than the current discount rate at June 30, 2014.

FRS Pension Plan			HIS		
Current			Current		
1% Decrease	Discount Rate	1% Increase	1% Decrease	Discount Rate	1% Increase
6.65%	7.65%	8.65%	3.29%	4.29%	5.29%
\$ 14,113,315	\$ 3,299,714	\$ (5,695,138)	\$ 6,124,664	\$ 5,384,704	\$ 4,767,048

B. Postemployment Healthcare Benefits

The Lottery participates in the State Employees' Health Insurance Program, a cost-sharing multiple-employer defined benefit postemployment healthcare plan administered by the DMS, Division of State Group Insurance, to provide group health benefits. Section 110.123, Florida Statutes, provides that retirees may participate in the State's group health insurance programs and assigns the authority to establish and amend benefit provisions to the DMS. Although premiums are paid by the retiree, the premium cost to the retiree is implicitly subsidized by the commingling of claims experience in a single risk pool with a single premium determination. An actuarial valuation has been performed for the plan and the Lottery's employees were included in the actuarial analysis. For more information on the plan regarding the funding policy and actuarial methods and assumptions, see the State of Florida's Comprehensive Annual Financial Report, which is available from the Department of Financial Services.

In accordance with GASB Codification Section Po50, *Postemployment Benefit Plans Other Than Pension Plans - Defined Benefit*, the Lottery is required to record its portion of the implicit postemployment health benefit liability. Postemployment health benefits payable at June 30, 2015, June 30, 2014, and June 30, 2013, was \$5,085,000, \$4,009,000, and \$2,962,000, respectively.

X. OPERATING LEASES

The Lottery has entered into operating leases for the rental of office and warehouse space for the headquarters and district offices. Certain leases are renewable at the option of the Lottery.

Future minimum rental payments as of June 30, 2015, are scheduled as follows (in thousands):

<u>Year Ending June 30</u>	<u>Headquarters</u>	<u>Districts</u>	<u>Total</u>
2016	\$ 2,744	\$ 1,077	\$ 3,821
2017	2,772	1,115	3,887
2018	2,801	1,149	3,950
2019	234	1,187	1,421
2020	-	1,032	1,032
2021-2025	-	4,085	4,085
2026-2030	-	4,183	4,183
2031-2034	-	2,308	2,308
Total	\$ 8,551	\$ 16,136	\$ 24,687

Rental expense under all operating leases totaled approximately \$4,017,000 and \$4,075,000 for the fiscal years ended June 30, 2015, and 2014, respectively.

XI. VENDOR SUPPORT FUNDS

Each of the gaming vendor contracts requires the vendors to provide a fund for marketing support activities as directed by the Lottery. The vendors are required to make deposits into the designated accounts either weekly or monthly and distribute the funds as directed by the Lottery. The funds are used for market research and other expenses directly linked to product sales. Vendor balances committed for marketing research vary with timing of marketing initiatives, industry developments, and changes in technology. Actual cash balances for these funds at June 30, 2006, through June 30, 2015, ranged from \$1,058,000 to \$3,874,000. Each contract requires that any funds remaining in the accounts at the end of each contract's term will be returned to the Lottery for transfer to the EETF. Historically, no balances have reverted to the Lottery. The contract with IGT, formerly GTech, was extended in June 2015. The contract with Scientific Games was renewed in September 2013.

Vendor support fund activities are summarized as follows (in thousands):

	2014-15 Vendor Support Funds			
	Balance			Balance
	June 30, 2014	Additions	Deletions	June 30, 2015
GTech/IGT	\$ 155	\$ 360	\$ (286)	\$ 229
Scientific Games	903	5,201	(4,264)	1,840
Total Vendor Support	\$ 1,058	\$ 5,561	\$ (4,550)	\$ 2,069

	2013-14 Vendor Support Funds			
	Balance			Balance
	June 30, 2013	Additions	Deletions	June 30, 2014
GTech	\$ 340	\$ 360	\$ (545)	\$ 155
Scientific Games	2,155	4,290	(5,542)	903
Total Vendor Support	\$ 2,495	\$ 4,650	\$ (6,087)	\$ 1,058

XII. OTHER COMMITMENTS

The Lottery has contractual agreements under which Terminal and Scratch-Off lottery game vendors provide gaming systems, tickets, and related services. The Lottery's Terminal gaming vendor is compensated at a rate of 1.0699 percent of net Terminal game ticket sales. The vendor's compensation for Terminal games and for the provision of full service vending machines for the fiscal years ended June 30, 2015, and 2014, was \$29,970,000 and \$28,895,000, respectively.

The Lottery's Scratch-Off ticket vendor is currently compensated at rates that range from .09776 percent to 2.1997 percent based on ticket price points and total annual sales. Compensation under this agreement and the agreement for the provision of instant ticket vending machines amounted to \$51,665,000 for the fiscal year ended June 30, 2015, and \$48,157,000 for the fiscal year ended June 30, 2014.

XIII. LITIGATION

The Lottery is involved in litigation and other claims incidental to the ordinary course of its operations. In the opinion of Lottery management, based on the advice of legal counsel, the ultimate disposition of these lawsuits and claims will not have a material adverse effect on the financial position of the Lottery.

OTHER REQUIRED SUPPLEMENTARY INFORMATION

FLORIDA RETIREMENT SYSTEM
Schedule of the Lottery's Proportionate Share of the Net Pension Liability
and Related Ratios
Last Ten Fiscal Years ⁽¹⁾

	2014⁽²⁾
Lottery's proportion of the net pension liability	0.054080631%
Lottery's proportionate share of the net pension liability	\$ 3,299,714
Lottery's covered-employee payroll	\$ 16,266,000
Lottery's proportionate share of the net pension liability as a percentage of its covered-employee payroll	20.29%
Plan fiduciary net position as a percentage of the total pension liability	96.09%

(1) This schedule is intended to report information for ten years. Additional information will be displayed as it becomes available.

(2) The amounts presented for the fiscal year were determined as of 6/30.

Schedule of the Lottery's Contributions
Last Ten Fiscal Years ⁽¹⁾

	2015⁽²⁾	2014⁽²⁾
Contractually required contribution	\$ 1,354,333	\$ 1,184,595
Contributions in relation to the contractually required contribution	\$ (1,354,333)	\$ (1,184,595)
Contribution deficiency (excess)	\$ -	\$ -
Lottery's covered-employee payroll	\$ 15,985,814	\$ 16,266,000
Contributions as a percentage of covered-employee payroll	8.47%	7.28%

(1) This schedule is intended to report information for ten years. Additional information will be displayed as it becomes available.

(2) The amounts presented for the fiscal year were determined as of 6/30.

RETIREE HEALTH INSURANCE SUBSIDY PROGRAM
Schedule of the Lottery's Proportionate Share of Net Pension Liability
and Related Ratios
Last Ten Fiscal Years ⁽¹⁾

	<u>2014⁽²⁾</u>
Lottery's proportion of the net pension liability	0.057588909%
Lottery's proportionate share of the net pension liability	\$ 5,384,704
Lottery's covered-employee payroll	\$ 16,175,000
Lottery's proportionate share of the net pension liability as a percentage of its covered-employee payroll	33.29%
Plan fiduciary net position as a percentage of the total pension liability	0.99%

(1) This schedule is intended to report information for ten years. Additional information will be displayed as it becomes available.

(2) The amounts presented for the fiscal year were determined as of 6/30.

Schedule of the Lottery's Contributions
Last Ten Fiscal Years ⁽¹⁾

	<u>2015⁽²⁾</u>	<u>2014⁽²⁾</u>
Contractually required contribution	\$ 215,070	\$ 197,280
Contributions in relation to the contractually required contribution	\$ (215,070)	\$ (197,280)
Contribution deficiency (excess)	\$ -	\$ -
Lottery's covered-employee payroll	\$ 15,969,897	\$ 16,175,000
Contributions as a percentage of covered-employee payroll	1.35%	1.22%

(1) This schedule is intended to report information for ten years. Additional information will be displayed as it becomes available.

(2) The amounts presented for the fiscal year were determined as of 6/30.



Sherrill F. Norman, CPA
Auditor General

AUDITOR GENERAL STATE OF FLORIDA

Claude Denson Pepper Building, Suite G74
111 West Madison Street
Tallahassee, Florida 32399-1450



Phone: (850) 412-2722
Fax: (850) 488-6975

The President of the Senate, the Speaker of the
House of Representatives, and the
Legislative Auditing Committee

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*

Report on the Financial Statements

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Department of the Lottery (Lottery), as of and for the fiscal year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise the Lottery's basic financial statements, and have issued our report thereon dated January 29, 2016, included under the heading **INDEPENDENT AUDITOR'S REPORT**.

Internal Control over Financial Reporting

We have examined the effectiveness of the Lottery's internal control over financial reporting as of June 30, 2015, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Lottery's management is responsible for maintaining effective internal control over financial reporting and for its assertion of the effectiveness of internal control, included in the accompanying **MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING**. Our responsibility is to express an opinion on the effectiveness of internal control over financial reporting based on our examination.

We conducted our examination in accordance with attestation standards established by the American Institute of Certified Public Accountants, and the standards applicable to attestation engagements contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the examination to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our examination included obtaining an understanding of the internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating

effectiveness of internal control based on the assessed risk. Our examination also included performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

An entity's internal control over financial reporting is a process effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance regarding the preparation of reliable financial statements in accordance with accounting principles generally accepted in the United States of America. An entity's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the entity; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures of the entity are being made only in accordance with authorizations of management and those charged with governance; and (3) provide reasonable assurance regarding prevention, or timely detection and correction of unauthorized acquisition, use, or disposition of the entity's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control may not prevent, or detect and correct misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that the internal control may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Lottery maintained, in all material respects, effective internal control over financial reporting as of June 30, 2015, based on the criteria established in *Internal Control – Integrated Framework* issued by COSO. We did note an additional matter involving the internal control over financial reporting, which is discussed in the **SCHEDULE OF FINDINGS**.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Lottery's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, rules, 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*. However, we noted an additional matter, which is discussed in the accompanying **SCHEDULE OF FINDINGS**.

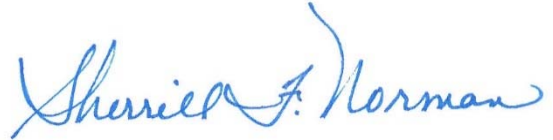
The Lottery's response to the findings described in the **SCHEDULE OF FINDINGS** section of this report is included in this report under the heading **MANAGEMENT'S RESPONSE**. We did not audit the Lottery's response, and accordingly, we express no opinion on it.

Purpose of the Report

The purpose of the **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 is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and to provide an opinion on the effectiveness of the Lottery's internal control. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Lottery's internal control and compliance. Accordingly, this report is not suitable for any other purpose.

Respectfully submitted,



Sherrill F. Norman, CPA
Tallahassee, Florida
January 29, 2016

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

RICK SCOTT
Governor



TOM DELACENSERIE
Secretary

Management's Report on Internal Control Over Financial Reporting

The Florida Lottery's internal control over financial reporting is a process effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance regarding the preparation of reliable financial statements in accordance with accounting principles generally accepted in the United States of America. An entity's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the entity; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures of the entity are being made only in accordance with authorizations of management and those charged with governance; and (3) provide reasonable assurance regarding prevention, or timely detection and correction of unauthorized acquisition, use, or disposition of the entity's assets that could have a material effect on the financial statements.

Management is responsible for establishing and maintaining effective internal control over financial reporting. Management assessed the effectiveness of the Florida Lottery's internal control over financial reporting as of June 30, 2015, based on the framework set forth by the Committee of Sponsoring Organizations of the Treadway Commission in *Internal Control – Integrated Framework (2013)*. Based on that assessment, management concluded that, as of June 30, 2015, the Florida Lottery's internal control over financial reporting is effective based on the criteria established in *Internal Control – Integrated Framework (2013)*.

The Florida Lottery

A handwritten signature in blue ink, appearing to be "Tom Delacenserie".

January 29, 2016

SCHEDULE OF FINDINGS

ADDITIONAL MATTERS

Finding 1: Information Technology Controls

Information technology (IT) controls are intended to protect the confidentiality, integrity, and availability of data and IT resources. During our audit, we identified the need for enhancements to the Lottery's IT control practices in one area which was also identified in the prior audit. To avoid the possibility of compromising Lottery information, specific details of this issue are not disclosed in this report. However, the appropriate Lottery personnel have been notified of this issue.

Recommendation: We recommend that Lottery management make the necessary IT control enhancements to address the issue identified.

Finding 2: Minority Retailer Participation

Section 24.113, Florida Statutes, requires that 15 percent of the Lottery's retailers be minority business enterprises, as defined in Section 288.703(3), Florida Statutes; however, no more than 35 percent of such retailers shall be owned by the same type of minority person, as defined by Section 288.703(4), Florida Statutes.

Our audit disclosed that as of July 1, 2015, retailers comprising one minority type totaled approximately 67 percent of the total number of minority retailers. A similar finding has been included in previous Auditor General reports.

The Lottery has developed an outreach program to increase retailer participation in under-represented minority groups; however, despite these efforts, the overall level of participation from these groups decreased slightly over the prior fiscal year.

Recommendation: We recommend that the Lottery continue its efforts to increase retailer participation in under-represented minority groups.

MANAGEMENT'S RESPONSE

RICK SCOTT
Governor



TOM DELACENSERIE
Secretary

January 29, 2016

Sherrill F. Norman, CPA
Auditor General
Claude Denson Pepper Building, Suite G74
111 West Madison Street
Tallahassee, Florida 32399-1450

Dear Ms. Norman:

The Lottery has received the list of preliminary and tentative audit findings and recommendations resulting from your audit of the Lottery's financial statements for the fiscal year ended June 30, 2015. Below is our response to each finding and recommendation:

Finding 1: Information Technology Controls

Recommendation: We recommend that Lottery management make the necessary IT control enhancements to address the issue identified.

Lottery's Response: We concur with the recommendation and will make the necessary IT control enhancements to address the issue identified.

Finding 2: Minority Retailer Participation

Recommendation: We recommend that the Lottery continue its efforts to increase retailer participation in under-represented minority groups.

Lottery's Response: We concur with the recommendation. Although the availability of certain minority retailer classifications is limited based on geographic location, the Lottery will continue its efforts to increase participation in under-represented minority groups through advertising and outreach.

Thank you for your audit efforts and recommendations. I look forward to receiving your final report.

Sincerely,

A handwritten signature in black ink, appearing to read "Tom Delacenserie".

Thomas R. Delacenserie
Secretary

TRD/twh