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Directory

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Fiscal Year 2010 Highlights

Successful conversions

The South Dakota Lottery's new **on-line system** successfully went live on August 2, 2009. The system, supplied by GTECH, features a touchscreen retailer terminal with expanded back-office capabilities. Players have quickly caught on to validating their own tickets on the self-service ticket checkers. Each retail location now sports a flat screen LCD monitor that flashes timely information about jackpots, new games and winners as well as messages regarding players' transpiring validations and sales transactions.



Executive Director Norm Lingle credited retailers with contributing to the success of the conversion by promoting the system to their customers and ensuring that employees were well-versed in the

operation of the new terminals.

A new **video lottery central system** also launched in FY2010. The Scientific Games International system includes a perpetual license of proprietary communication protocol, provides an updated system, and allows for multiple communication protocols to be used. The new protocol allows manufacturers to introduce new games more quickly.



Weather Eye Radio Network An eye on advertising

The Weather Eye Radio Network branding campaign introduced in FY2010 features sponsorship tags for select weathercasts on participating radio stations. The ads are easily modified to spotlight various games. They receive high listenership and help to display the Lottery's concern for the public's welfare.

Problem gambling efforts

Each year the South Dakota Lottery provides up to \$214,000 to the Department of Health and Human Services to pay for problem gambling treatment services. South Dakota also participates in the National Association of Problem Gambling's annual Problem Gambling Awareness Week. The goal of this campaign is to educate the public and health care professionals about the warning signs of problem gambling and raise awareness about the help that is available.

Mega Millions offers more ways to win

The introduction of Mega Millions in May rounded out FY2010 events for the South Dakota Lottery. The game piqued players' interest with drawings on Tuesdays and Fridays and a richer second level prize of \$250,000. "Adding Mega Millions increases the possibility of players winning big jackpots," Director Lingle said. "With dozens of states cross-selling Mega Millions and Powerball we see the jackpots of both games grow faster."



Fiscal Year 2010 Sales and Revenue

Instant tickets

The Lottery launched 24 new instant ticket games during FY2010. At the close of the year, there were 617 licensed instant ticket retailers across the state. Sales were down fractionally from the previous year.



Lotto tickets

South Dakota currently offers five lotto games. Powerball, Mega Millions, Wild Card 2 and Hot Lotto are multi-state games. Dakota Cash is played only in South Dakota.

At the end of the fiscal year, there were 586 licensed lotto retailers. Lotto games reported an overall increase in sales of 21.7 percent from the previous fiscal year.

Video Lottery

The Lottery regulates and controls the video lottery game activities through licensing procedures for the machines, machine owners, and establishments as well as a comprehensive secure central computer system.

Video lottery sales (cash in) decreased 1.6 percent in FY2010. The average number of active video lottery machines during the year was 9,114, and the average number of licensed establishments was 1,476.

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

Sales and Revenues

Total fiscal year 2010 Lottery revenue distributed to state funds was nearly \$120 million.

	Sales	Prizes	Retailer Commissions	Revenue Distributed
Instant Tickets	\$20,151,392	\$12,667,200	\$1,129,283	\$4,697,123
Lotto Tickets	\$25,392,506	\$12,841,729	\$1,402,704	\$8,172,583
Video Lottery**	\$642,214,243	\$426,757,417	\$107,728,413	\$106,910,129
			Total:	\$119,779,835

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

Revenue Distribution

	General Fund	Cap. Construct. Fund	Property Tax Reduction Fund	Dept. of Human Services
Instant Tickets	\$4,697,123			
Lotto Tickets	\$1,400,000	\$6,772,583		
Video Lottery	\$45,000		\$106,651,129	\$214,000
Totals:	\$6,142,123	\$6,772,583	\$106,651,129	\$214,000



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MARTIN L. GUINDON, CPA
AUDITOR GENERAL

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

The Honorable Dennis Daugaard
Governor of South Dakota

and

South Dakota Lottery Commission
State of South Dakota

We have audited the financial statements of the South Dakota Lottery Fund of the State of South Dakota as of and for the fiscal years ended June 30, 2010 and 2009 and have issued our report thereon dated February 25, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the South Dakota Lottery Fund's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of South Dakota Lottery in a separate letter dated February 25, 2011.

This report is intended solely for the information and use of management and members of the South Dakota Legislature and is not intended to be and should not be used by anyone other than those specified. However, this report is a matter of public record and its distribution is not limited.

A handwritten signature in black ink, appearing to read "Martin L. Guindon". The signature is fluid and cursive, with a large initial "M" and "G".

Martin L. Guindon, CPA
Auditor General

February 25, 2011



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MARTIN L. GUINDON, CPA
AUDITOR GENERAL

INDEPENDENT AUDITOR'S REPORT

The Honorable Dennis Daugaard
Governor of South Dakota

and

South Dakota Lottery Commission
State of South Dakota

We have audited the accompanying financial statements of the South Dakota Lottery Fund, as of and for the fiscal years ended June 30, 2010 and 2009, as listed in the Table of Contents. These financial statements are the responsibility of the South Dakota Lottery Fund's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

The financial statements present only the financial position and changes in financial position and cash flows of the South Dakota Lottery Fund. They do not purport to, and do not, present fairly the financial position of the State of South Dakota as of June 30, 2010 and 2009, and the changes in its financial position and its cash flows, where applicable, for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the South Dakota Lottery Fund as of June 30, 2010 and 2009, and the respective changes in financial position and cash flows thereof for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 25, 2011, on our consideration of the South Dakota Lottery's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Martin L. Guindon, CPA
Auditor General

February 25, 2011

South Dakota Lottery
STATEMENT OF NET ASSETS

June 30, 2010 and 2009

Assets	2010	2009
		(As Restated)
Current Assets:		
Cash	\$8,026,410	\$8,645,779
Restricted Cash	42,500	34,800
Total Cash	8,068,910	8,680,579
Accounts Receivable	4,836,486	5,203,921
Restricted Other Receivable	808,223	792,684
Interest Receivable	81,032	118,544
Restricted Certificates of Deposit	461,705	387,053
Total Current Assets	14,256,356	15,182,781
Noncurrent Assets:		
Capital Assets less Accumulated Depreciation/Amortization	2,746,139	32,157
Total Assets	17,002,495	15,214,938
Liabilities		
Current Liabilities:		
Accounts Payable	291,162	237,111
Prizes Payable	1,447,429	1,175,118
Due to the Property Tax Reduction Fund	4,196,376	4,045,717
Due to the Capital Construction Fund	1,772,583	728,086
Due to the General Fund	1,097,123	934,831
Due to Other Funds	89,289	89,008
Due to Other Governments	10,828	10,000
Operator Security Deposits	504,205	421,853
Escrows Payable – Reservation Sales	70,930	48,591
Accrued Liabilities	222,996	232,963
Deferred Revenue	157,890	235,348
Total Current Liabilities	9,860,811	8,158,626
Noncurrent Liabilities:		
Accrued Liabilities	113,302	119,444
Total Liabilities	9,974,113	8,278,070
Net Assets		
Invested in Capital Assets, Net of Related Debt	2,746,139	32,157
Restricted for MUSL Permitted Uses	808,223	792,684
Unrestricted	3,474,020	6,112,027
Total Net Assets	\$7,028,382	\$6,936,868

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

South Dakota Lottery
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
For the Fiscal Years Ended June 30, 2010 and 2009

	FY2010	FY2009
Operating Revenues:		
Video Lottery Revenue	\$107,728,412	\$110,062,616
Instant Ticket Sales	20,151,392	20,180,554
On-Line Ticket Sales	25,392,506	20,864,968
Terminal License Fees	1,034,000	1,031,200
Retailer License Fees	325,650	318,950
Total Operating Revenue	<u>154,631,960</u>	<u>152,458,288</u>
Direct Game Costs:		
Instant Prizes	12,677,200	12,790,933
On-Line Prizes	12,841,729	10,527,701
Instant Retail Commissions	1,129,283	1,134,612
On-Line Retail Commissions	1,402,704	1,220,383
Instant Ticket Print Costs	412,879	508,995
Total Direct Costs	<u>28,463,795</u>	<u>26,182,624</u>
Gross Profit	<u>126,168,165</u>	<u>126,275,664</u>
Operating Expenses:		
Personal Services and Benefits	1,459,070	1,471,838
Travel	144,231	144,709
Advertising	532,256	653,886
Contractual Services	4,487,690	4,175,752
Supplies and Materials	66,378	66,564
Depreciation/Amortization	186,018	10,562
Bad Debt Expense	896	4,894
Payments to Reservations	70,930	48,591
Total Operating Expenses	<u>6,947,469</u>	<u>6,576,796</u>
Operating Income	<u>119,220,696</u>	<u>119,698,868</u>
Non-operating Revenues (Expenses):		
Pooled Investment Income	612,719	805,815
Broker Rebate Expense		(5,141)
Non-operating Revenue from MUSL	22,643	101,792
Miscellaneous Revenue	15,291	29,976
Total Non-operating Revenue (Expenses)	<u>650,653</u>	<u>932,442</u>
Income Before Transfers	<u>119,871,349</u>	<u>120,631,310</u>
Transfers:		
Transfers to the Property Tax Reduction Fund	106,651,129	108,961,990
Transfers to the General Fund	6,142,123	6,179,831
Transfers to the Capital Construction Fund	6,772,583	4,528,086
Transfers to the Department of Human Services	214,000	214,000
Total Transfers	<u>119,779,835</u>	<u>119,883,907</u>
Change in Net Assets	<u>91,514</u>	<u>747,403</u>
Total Net Assets – Beginning	<u>6,936,868</u>	<u>6,189,465</u>
Total Net Assets – Ending	<u>\$7,028,382</u>	<u>\$6,936,868</u>

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

South Dakota Lottery
STATEMENT OF CASH FLOWS
For the Fiscal Years Ended June 30, 2010 and 2009

	FY2010	FY2009
Cash Flows from Operating Activities		
Receipts from Customers and Users	\$155,178,944	\$152,711,292
Payments for Lottery Prizes	(25,457,407)	(23,374,487)
Payments to Suppliers	(7,327,537)	(7,215,452)
Payments for Interfund Services Used	(838,645)	(751,139)
Payments for Employee Services	(1,475,179)	(1,446,898)
Other Receipts (Payments)	(19,689)	247,719
Net Cash Provided (Used) by Operating Activities	<u>120,060,487</u>	<u>120,171,035</u>
Cash Flows from Capital and Related Financing Activities		
Purchase of Capital Assets	(2,900,000)	(27,588)
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>(2,900,000)</u>	<u>(27,588)</u>
Cash Flows from Noncapital Financing Activities		
Transfers to Other Funds	(118,422,387)	(119,639,046)
Net Cash Provided (Used) by Noncapital Financing Activities	<u>(118,422,387)</u>	<u>(119,639,046)</u>
Cash Flows from Investing Activities		
Pooled Investment Income	650,231	824,133
Security Lending Rebate Fees	(5,141)	(5,141)
Net Cash Provided (Used) by Investing Activities	<u>650,231</u>	<u>818,992</u>
Net Increase (Decrease) in Cash during the Fiscal Year	(611,669)	1,323,393
Cash at Beginning of Year	8,680,579	7,357,186
Cash at End of Year	<u>\$8,068,910</u>	<u>\$8,680,579</u>
Reconciliation of Operating Income to Net Cash Provided (Used) by Operating Activities		
Operating Income	\$119,220,696	\$119,698,868
Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided by Operating Activities:		
Depreciation/Amortization Expense	186,018	10,562
Other Revenue	15,291	29,976
Non-operating Revenue from MUSL	22,643	101,792
Decrease/(Increase) in Assets:		
Accounts Receivable	366,539	249,732
Restricted Other Receivable	(15,539)	145,008
Restricted Certificates of Deposit	(74,652)	163,436
Increase/(Decrease) in Liabilities:		
Accounts Payable	54,051	(105,924)
Prizes Payable	272,311	(90,970)
Due to Other Funds	281	16,315
Due to Other Governments	828	10,000
Operator Security Deposits	82,352	(143,436)
Escrows Payable	22,339	4,685
Allowance for Doubtful Accounts	896	4,894
Accrued Liabilities	(16,109)	24,940
Deferred Revenue	(77,458)	51,157
Total Adjustments	<u>839,791</u>	<u>472,167</u>
Net Cash Provided by Operating Activities	<u>\$120,060,487</u>	<u>\$120,171,035</u>

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

South Dakota Lottery
NOTES TO THE FINANCIAL STATEMENTS
For the Fiscal Years Ended June 30, 2010 and 2009

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

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

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

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

BASIS OF PRESENTATION. The South Dakota Lottery Fund is accounted for as a proprietary type enterprise fund for the State of South Dakota. Proprietary funds are accounted for using the accrual basis of accounting. The South Dakota Lottery Fund follows all Governmental Accounting Standards Board (GASB) pronouncements and those Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins that were issued on or before Nov. 30, 1989, except for those that conflict with a GASB pronouncement. The South Dakota Lottery is considered part of the primary government as reported by the State of South Dakota. Revenues are recognized when they are earned, and expenses are recognized when they are incurred. The financial statements are prepared in accordance with generally accepted accounting principles for proprietary (enterprise) funds.

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

Management of the State's internal investment pool is the statutory responsibility of the South Dakota Investment Council (SDIC). The investment policy and required risk disclosures for the State's internal investment pool are presented in the South Dakota Investment Council Audit Report.

RESTRICTED CASH. Restricted cash is the amount of operator security deposits in the form of cash on deposit with the Lottery. This restricted cash was restated for June 30, 2009.

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

	<u>2010</u>	<u>2009</u>
Uncollected instant/on-line ticket revenues	\$ 596,298	\$ 1,133,159
Allowance for doubtful instant/on-line accounts	(18,890)	(17,994)
Uncollected video lottery revenues and fees	4,259,078	4,088,756
	<u>\$4,836,486</u>	<u>\$5,203,921</u>

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

OPERATOR SECURITY DEPOSITS. ARSD 48:02:05:04(18) requires video lottery operators to furnish to the Lottery by July 1 of each year, security equal to one-eighteenth of the State's share of estimated annual net machine income derived from the operator's video lottery machines. Security may be in the form of a surety bond, deposit in cash, an irrevocable letter of credit, or a certificate of deposit issued by a South Dakota financial institution with the

South Dakota Lottery
NOTES TO THE FINANCIAL STATEMENTS
For the Fiscal Years Ended June 30, 2010 and 2009

Lottery endorsed on it as a payee. As of June 30, 2010 and 2009, the amount of cash on deposit with the Lottery was \$42,500 and \$34,800 and the amount of certificates of deposit being held by the Lottery was \$461,705 and \$387,053, respectively. The amount of \$5,828,100 and \$6,218,300, respectively, was in the form of surety bond or irrevocable letter of credit and are not reported on the Statement of Net Assets. The total Security Deposits on June 30, 2010 and 2009 were \$6,332,305 and \$6,640,153, respectively.

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

The South Dakota Lottery obtained a new Video Lottery Central Monitoring and Control System (VLCS) from Scientific Games on December 24, 2010. The Lottery made an upfront payment to Scientific Games of \$2,900,000. This included the hardware for a primary, back-up and test system, a perpetual license to use the VLCS communications protocol and a license to use Scientific Games system software.

Capital Assets consisted of the following for fiscal years 2010 and 2009:

	<u>2010</u>				<u>2009</u>			
	Beginning Balance	Additions	Deletions	Ending Balance	Beginning Balance	Additions	Deletions	Ending Balance
<i>Equipment</i>	\$ 105,244	\$ 586,903	\$ 18,891	\$ 673,256	\$ 951,656	\$ 27,588	\$ 874,000	\$ 105,244
<i>Intangible Assets-Software</i>	-	2,313,097	-	2,313,097	-	-	-	-
<i>Total Capital Assets</i>	<u>105,244</u>	<u>2,900,000</u>	<u>18,891</u>	<u>2,986,353</u>	<u>951,656</u>	<u>27,588</u>	<u>874,000</u>	<u>105,244</u>
<i>Less Accumulated</i>								
<i>Depreciation/Amortization for:</i>								
<i>Equipment</i>	(73,087)	(70,364)	18,891	(124,560)	(936,525)	(10,562)	874,000	(73,087)
<i>Intangible Assets-Software</i>	-	(115,654)	-	(115,654)	-	-	-	-
<i>Total Accumulated</i>	<u>(73,087)</u>	<u>(186,018)</u>	<u>18,891</u>	<u>(240,214)</u>	<u>(936,525)</u>	<u>(10,562)</u>	<u>874,000</u>	<u>(73,087)</u>
<i>Depreciation/Amortization</i>	<u>(73,087)</u>	<u>(186,018)</u>	<u>18,891</u>	<u>(240,214)</u>	<u>(936,525)</u>	<u>(10,562)</u>	<u>874,000</u>	<u>(73,087)</u>
<i>Total Capital Assets, Net</i>	<u>\$ 32,157</u>	<u>\$ 2,713,982</u>	<u>\$ -</u>	<u>\$ 2,746,139</u>	<u>\$ 15,131</u>	<u>\$ 17,026</u>	<u>\$ -</u>	<u>\$ 32,157</u>

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

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

A minimum of 50 percent of the projected revenue from the sale of lottery tickets, computed on a year-round basis, is allocated for payment of prizes. Prizes may be claimed up to 180 days after the official end of the game. Unclaimed prizes are added to the prize pools of subsequent lottery games. Reverted prizes during the fiscal years ended June 30, 2010 and 2009 were \$464,039 for on-line prizes and \$462,607 for instant prizes, and \$426,211 for on-line prizes and \$464,646 for instant prizes, respectively.

DUE TO THE PROPERTY TAX REDUCTION FUND. SDCL 42-7A-63 sets the State's percentage of net machine income at 50 percent of which all but 0.5 percent is deposited into the Property Tax Reduction Fund. At June 30, 2010 and 2009, there was a liability to the Property Tax Reduction Fund of \$4,196,376 and \$4,045,717, respectively.

South Dakota Lottery
NOTES TO THE FINANCIAL STATEMENTS
For the Fiscal Years Ended June 30, 2010 and 2009

DUE TO THE GENERAL FUND AND THE CAPITAL CONSTRUCTION FUND. The Lottery maximizes net proceeds to the State from the sale of instant and on-line tickets. These net proceeds are transferred to the General Fund and Capital Construction Fund on an annual basis on or about July 1. There was a liability for instant ticket sales to the General Fund of \$1,097,123 and \$934,831, and a liability for on-line ticket sales to the Capital Construction Fund of \$1,772,583 and \$728,086 as of June 30, 2010 and 2009, respectively.

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

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

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

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

NET ASSETS. "Net Assets" are the difference between assets and liabilities. Net assets are reported in three categories:

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

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

Unrestricted net assets consist of assets that do not meet the definition of the two preceding categories.

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

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

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

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On-line retailers selling a jackpot winning Powerball or Mega Millions ticket may receive a bonus of \$50,000. Selling bonuses of \$10,000 and \$1,000 may be paid to retailers selling Powerball tickets of \$200,000 and \$10,000, respectively, or Mega Millions tickets of \$250,000 and \$10,000, respectively. If a retailer sells a Power Play ticket winning \$200,000 or \$10,000 (each times the multiplier) or a Megaplier ticket winning \$250,000 or \$10,000 (each times the multiplier), a bonus of \$20,000 or \$1,000 times the multiplier, respectively, may be paid. Retailers who sell a Dakota Cash jackpot winning ticket may receive a bonus equal to 5 percent of the value of the winning ticket not to exceed \$5,000. Retailers who sell a Wild Card 2 jackpot winning ticket may receive a bonus equal to 1 percent of the value of the winning ticket, not to exceed \$10,000; a retailer selling a \$5,000 winning ticket may receive a bonus of \$500. Retailers who sell a Hot Lotto jackpot winning ticket or a \$10,000 winning ticket may receive a bonus of \$10,000 and \$1,000, respectively. Retailers who sell a Sizzler jackpot winning ticket or a \$30,000 winning ticket may receive a bonus of \$10,000 or \$3,000, respectively.

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

NOTE 2. COMPENSATED ABSENCES

All permanent full-time employees earn annual leave. Upon termination, employees are eligible to receive compensation for their accrued annual leave balances. At June 30, 2010 and 2009, a liability existed for accumulated annual leave calculated at the employee's June 30 pay rate in the amount of \$106,766 and \$110,562, respectively. Employees who have been continuously employed by the State of South Dakota for at least seven years prior to the date of their retirement, voluntary resignation, or death will receive payment for one-fourth of their accumulated sick leave balance. This payment is not to exceed the sum of 12 weeks of the employee's annual compensation. At June 30, 2010 and 2009, a liability existed for accumulated sick leave, calculated at each employee's June 30 pay rate, in the amount of \$133,026 and \$143,033, respectively. The following is a schedule of changes in compensated absences at June 30, 2010 and 2009.

	<u>Beginning</u> <u>Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending</u> <u>Balance</u>	<u>Due Within</u> <u>One Year</u>
Compensated Absences Payable					
Fiscal Year 2010	\$ 253,595	\$ 131,637	\$ 145,440	\$ 239,792	\$ 126,490
Fiscal Year 2009	236,838	140,115	123,358	253,595	134,151

NOTE 3. RETIREMENT PLAN

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

State law requires employees to contribute 6 percent of their salary to the plan and the employer to contribute an amount equal to the employee's contribution. The right to receive retirement benefits vests after three years of credited service. The South Dakota Lottery's contributions to the SDRS for the fiscal years ended June 30, 2010, 2009, and 2008 were \$68,256, \$68,000, and \$64,194, respectively, equal to the required contributions each year.

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NOTE 4. OPERATING LEASES

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

The following schedule is a summary of future minimum rental payments by years required under operating leases with lease terms in excess of one year as of June 30, 2010:

<u>Period Ending June 30:</u>	
2011	\$ 63,724
2012	62,175
2013	7,521
2014	0
2015	0
Total Minimum Payments	<u>\$133,420</u>

Total rental expense for all operating leases for the fiscal years ended June 30, 2010 and 2009, was \$124,151 and \$120,638, respectively.

NOTE 5. VIDEO LOTTERY

Following is a summary of video lottery revenues for the fiscal years ended June 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Cash In	\$ 642,214,243	\$ 652,965,073
Less Cash Out	<u>426,757,417</u>	<u>432,839,841</u>
Video Lottery Net Machine Income	215,456,826	220,125,232
Less Operator and Establishment Share	<u>107,728,413</u>	<u>110,062,616</u>
Video Lottery Revenue Available to the State	107,728,413	110,062,616
Less Lottery Operating Share	<u>1,077,284</u>	<u>1,100,626</u>
Video Lottery Revenue to the Property Tax Reduction Fund	<u>\$ 106,651,129</u>	<u>\$ 108,961,990</u>

NOTE 6. TRANSFERS

Following is a summary of total transfers for the fiscal years ended June 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Transfers Out:		
General Fund Proceeds from Instant and On-Line	\$ 5,000,000	\$ 5,200,000
Capital Construction Fund Proceeds from On-Line	5,000,000	3,800,000
General Fund Proceeds from Instant and On-line not Yet Transferred	1,097,123	934,831
Capital Construction Fund Proceeds from On-Line not Yet Transferred	1,772,583	728,086
Video Lottery Proceeds Transferred to the Property Tax Reduction Fund	102,454,753	104,916,273
Video Lottery Proceeds to Prop. Tax Reduction Fund not Yet Transferred	4,196,376	4,045,717
Video Lottery Grant to Department of Human Services	214,000	214,000
Video Lottery Fees Transferred to the General Fund	45,000	45,000
Total Transfers Out	<u>\$119,779,835</u>	<u>\$119,883,907</u>

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NOTE 7. PARTICIPATION IN THE MULTI-STATE LOTTERY ASSOCIATION

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

The prize pool for Powerball, Hot Lotto and Megaplier consists of 50 percent of each drawing period's sales. The prize pool for Power Play is 49.5 percent of sales, the prize pool for Mega Millions is 51 percent of sales, and the prize pool for Sizzler is 47.42 percent of sales. The prize pool for Wild Card 2 is 55 percent of each drawing period sales with all cash prizes. Two percent of sales for Powerball and Wild Card 2, 1.5 percent for Sizzler, 1 percent of Mega Millions, and 0.5 percent for Power Play are placed in a prize reserve fund. For Hot Lotto, up to 1 percent of sales is placed in a prize reserve fund after the annuitized jackpot exceeds \$2 million. An additional 2 percent of sales is placed in a prize reserve fund after the annuitized jackpot exceeds \$5 million. The prize reserve fund serves as a contingency reserve to protect MUSL in cases of unforeseen liabilities. The money in this reserve fund is to be used at the discretion of the MUSL Board of Directors.

The prize reserve fund monies may be absorbed by a replacement game or are refundable to member states if MUSL or the MUSL game group disbands or if a member leaves MUSL or a game group. Members who leave must wait one year before receiving their remaining share, if any, of the prize reserve fund. At June 30, 2010 and 2009, the MUSL Powerball prize reserve fund had a balance of \$84,281,999 and \$77,182,537, respectively, of which the South Dakota Lottery's share was \$449,601 and \$449,601, respectively. The set prize reserve fund had a balance of \$29,117,533 and \$27,790,601, respectively, of which the South Dakota Lottery's share was \$149,867 and \$148,585, respectively. The Wild Card 2 prize reserve fund had a balance of \$980,273 and \$955,598, respectively, of which the South Dakota Lottery's share was \$174,751 and \$176,486, respectively. The Hot Lotto prize reserve fund had a balance of \$6,491,541 and \$5,443,110, respectively, of which the South Dakota Lottery's share was \$265,150 and \$220,032, respectively. At June 30, 2010, the Mega Millions prize reserve had a balance of (\$629,706), of which the South Dakota Lottery's share was (\$4,362). These reserves are held by MUSL and are not included in these financial statements.

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

Prior to Nov. 5, 1997, the Powerball jackpot was payable to the winner(s) in annual installments over 20 years, with the first payment being made by the member lottery starting at the time of the drawing. Since that time, players can choose one lump-sum cash payment or receive the jackpot prize over 25 annual payments. Treasury zero coupon bonds that provide payments corresponding to the member lottery's obligation to these prize winners are purchased by MUSL in the name of the member lottery. MUSL holds these bonds and will cash the bonds when due and wire the money to the member lottery's account on or before the anniversary date of the win. The Wild Card 2 jackpot is paid in cash, and will be divided equally among all jackpot winners for a specific drawing. The Hot Lotto jackpot prize can be taken as cash or annuity and is divided equally among multiple winners.

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As of June 30, 2010 and 2009, MUSL had purchased zero coupon bonds to fund installment payments for the South Dakota Lottery aggregating \$0 and \$12,466,937, respectively. The total purchase price of these bonds was \$6,509,238 and the final installment payment was made on April 8, 2010.

NOTE 8. CONTRACTUAL ARRANGEMENTS

- A. Instant Tickets** - The South Dakota Lottery entered into a contract with Scientific Games to provide instant game tickets through August 30, 2010.
- B. Video Lottery Vendor** - The South Dakota Lottery has contracted with Scientific Games to operate a video lottery system through December 24, 2019, with possible extension through December 24, 2024.
- C. On-line Lottery Vendor** - The South Dakota Lottery has contracted with GTECH Corporation to operate an on-line lottery gaming system through August 2, 2014, with possible extension through August 2, 2019.

NOTE 9. RISK MANAGEMENT

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