

**NEW MEXICO LOTTERY AUTHORITY**

**FINANCIAL STATEMENTS**

**JUNE 30, 2016 and 2015**



Wealth Advisory

Outsourcing

Audit, Tax, and Consulting

New Mexico Lottery Authority

**OFFICIAL ROSTER**

June 30, 2016

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**OFFICIALS OF THE NEW MEXICO LOTTERY AUTHORITY**

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Karla Wilkinson	Director of Gaming Products
Evelyn McKnight	Director of Human Resources
Pam Poteat	Director of Sales

## **ORGANIZATIONAL DIVISIONS OF THE NEW MEXICO LOTTERY AUTHORITY**

As per the New Mexico Lottery Act, Chapter 6, Article 24 NMSA 1978, the New Mexico Lottery Authority (the Lottery) is governed by a seven-member Board of Directors (Board or Directors), who provide the Lottery with the private-sector perspective of a large marketing and sales enterprise in order to maximize revenues for the Legislative Lottery Scholarship.

The Directors are residents of New Mexico appointed by the Governor with the advice and consent of the Senate. The Directors are prominent persons in their businesses or professions and geographically represent the State of New Mexico. No more than four Directors are from any one political party. The Directors receive no compensation for their services, but are reimbursed for approved expenses incurred in the conduct of the Lottery's business. Each Director is subject to a background check and investigation to determine his/her fitness for the office. At least one Director has five years of experience as a law enforcement officer, one Director is an attorney admitted to practice in New Mexico, and one Director is a Certified Public Accountant certified in New Mexico. The Directors serve for a five-year term, but can be reappointed by the Governor. The Board selects a Chairman, a Vice-Chairman, a Secretary/Treasurer, and an Assistant-Secretary/Treasurer each fiscal year. The Chairman also appoints a Chairman and two Directors for each of the three standing committees of the Board; the Finance/Audit Committee, the Security/Operations Committee, and the Personnel Committee. The Directors appoint the Chief Executive Officer (CEO) and prescribe his qualifications, duties and salary, and with the recommendation and assistance of the CEO, employ an Executive Vice President for Security and an Internal Auditor. The Directors meet at least once each quarter, and more often as needed. At their meetings the Directors:

- adopt, amend, or repeal rules, policies and procedures necessary for the operation of the Lottery;
- approve, disapprove, amend, or modify the original budget for the succeeding fiscal year and any revised budget during a fiscal year;
- review and discuss current financial information and the Lottery's performance to the approved budget for the fiscal year;
- approve or disapprove all procurements over seventy-five thousand dollars and the resulting award of contracts;
- approve the financial audit contract after (or pending) Office of the State Auditor (State Auditor) approval, hold an audit exit conference with the independent public accountants (IPA) at an executive session of the Board or in the Finance/Audit Committee, and at an open meeting accept the fiscal year audit following release by the State Auditor and presentation by the IPA;
- listen to and discuss Lottery updates on sales, games, issues, etc.;
- review, discuss, and accept internal audit reports; and
- discuss, and when necessary, approve or disapprove other matters that should properly come before the Directors in their fiduciary duty for the efficient and effective operation, profitability, integrity, and security of the Lottery.

## **ORGANIZATIONAL DIVISIONS OF THE NEW MEXICO LOTTERY AUTHORITY - CONTINUED**

The Executive Division, under the direction of the Chief Executive Officer, provides leadership for all activities of the Lottery to carry out its objectives and overall statutory mission to maximize net revenues for the Lottery's beneficiaries. The division establishes and directs the organization's day-to-day operating strategy and plan. In addition, the division performs as a liaison among the Board, the Governor, the Legislature, governmental entities, external providers of goods and services, retailers, the public, and Lottery divisions and employees.

The Administration Division, under the direction of the Chief of Staff/Director of Administration, performs all the activities associated with the financial and accounting functions of the Lottery, including the general ledger; cash management; retailer accounts receivable and debt collection; capital asset accounting; game accounting; payroll and benefit preparation, accounting, payment, and review; and tax reporting and payment. In addition, the division provides financial reporting, disclosure, and compliance with generally accepted accounting practices and budget compilation, including the quarterly and annual financial reporting of revenues, expenses, and net revenues to the State of New Mexico; the financial audit and related compilation of financial statements, related notes, and the Management's Discussion and Analysis (MDA) for the fiscal year; the statutorily required annual proposed operating budget for the Lottery for the succeeding fiscal year and the final (revised) proposed budget by division for Board of Directors' approval. Furthermore, the division is responsible for the procurement of materials and services; claims center payment of prizes and sales of tickets; and accounts payable. The warehouse component of the Administration Division is responsible for the packing and shipment of the Lottery's instant scratcher tickets and for the maintenance and shipping of Lottery premium and point of sale items. The division is also responsible for the management of building and grounds maintenance and vehicle fleet operations and maintenance.

The Advertising and Marketing Division, under the direction of the Director of Advertising and Marketing, is responsible for implementing, managing and administering the activities associated with marketing the Lottery and its products, including advertising, television drawings, promotions and special events. This entails creating and producing multi-media advertising campaigns, in-store point of sale materials and player and retailer publications; as well as negotiating and overseeing the Lottery's participation in a number of statewide promotions and special events. In addition, within the Advertising and Marketing Division is communications, which is responsible for all aspects of corporate communications including creating news releases and responding to requests for information by the public and the media.

Gaming Products, under the direction of the Director of Gaming Products, manages and monitors the instant and on-line products, including such areas as game launches, game endings, and performance analysis using several key performance measures. In addition, Instant ticket printing and on-line services contracts are managed by the Director of Gaming Products.

**ORGANIZATIONAL DIVISIONS  
OF THE NEW MEXICO LOTTERY AUTHORITY - CONTINUED**

The Human Resources Division, under the direction of the Director of Human Resources, oversees the development and implementation of human resources policies, programs and services, including recruitment, selection, retention, legal compliance, employee benefits, employee insurance reconciliation, employee relations, employment practices and procedures, employee communications and employee events.

The Sales Division, under the direction of the Director of Sales, is responsible for developing and implementing all sales activities and programs for the Lottery, including customer relationship management, ticket sales, inventory management, point of sales material distribution, retailer recruitment, arranging for retailer installations, promotional and event participation and preparation, as well as maximizing sales initiatives.

The Security Division, under the direction of the Executive Vice President for Security, statutorily as a law enforcement agency is responsible for administering, enforcing and ensuring compliance with the security provisions of the New Mexico Lottery Act. The division conducts backgrounds of all prospective employees, lottery retailers, lottery vendors and lottery contractors. It also supervises ticket verification and conducts second chance drawings when the prize amount is more than \$5,000. The division functions as liaison among the Attorney General's Office, District Attorney Offices and law enforcement agencies in general. It is also responsible for building and employee security and safety.

The Information Technology (IT) Department, under the direction of the Information Technology Administrator, oversees all the activities associated with the systems and data processing functions of the Lottery, including financial applications, testing of new games, products, functions, and related reporting, monitoring of game activities and providing data and analysis to divisions. In addition, the management of the lottery's network is overseen by the IT Department.

The Internal Audit Department, under the direction of the Internal Auditor, conducts and coordinates comprehensive audits for all aspects of the Lottery as spelled out in the New Mexico Lottery Act. Audits are carried out pursuant to an annual audit plan that is approved by the Board of Directors and as may be requested by the CEO.

# **TABLE OF CONTENTS**

## **NEW MEXICO LOTTERY AUTHORITY**

<b>REPORT OF INDEPENDENT AUDITORS .....</b>	<b>1-3</b>
<b>MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) .....</b>	<b>4-26</b>
<b>BASIC FINANCIAL STATEMENTS</b>	
Statements of Net Position.....	27
Statements of Revenues, Expenses and Changes in Net Position.....	28
Statements of Cash Flows.....	29-30
Statements of Fiduciary Net Position.....	31
Statements of Changes in Fiduciary Net Position .....	32
Notes to Financial Statements .....	33-54
<b>SUPPLEMENTARY INFORMATION</b>	
Budgetary Comparison Statements .....	55
Schedules of Percentage Return to the State of New Mexico .....	56
<b>OTHER INFORMATION</b>	
Report of Independent Auditors on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With <i>Government Auditing Standards</i> .....	57-58
Schedule of Findings and Responses.....	59-60
Summary Schedule of Prior Audit Findings .....	61
Schedule of Vendor Information .....	62
Exit Conference.....	63

## INDEPENDENT AUDITORS' REPORT

Board of Directors  
New Mexico Lottery Authority and  
Mr. Tim Keller  
New Mexico State Auditor  
Albuquerque, New Mexico

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the business-type activities and the aggregate remaining fund information of the New Mexico Lottery Authority (Lottery), a component unit of the State of New Mexico, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Lottery's basic financial statements as listed in the table of contents. We have also audited the Lottery's budgetary comparison statement presented as supplementary information, as defined by the Government Accounting Standards Board for the year ended June 30, 2016 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.

### ***Auditors' Responsibility***

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

Board of Directors  
New Mexico Lottery Authority and  
Mr. Tim Keller  
New Mexico State Auditor

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 business-type activities and the aggregate remaining fund information of the Lottery as of June 30, 2016, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statements referred to above present fairly, in all material respects, the respective budgetary comparison statement of the Lottery for the year ended June 30, 2016, in accordance with accounting principles generally accepted in the United States of America.

### ***Other Matters***

#### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 through 26 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 Information*

Our audit for the year ended June 30, 2016 was conducted for the purpose of forming opinions on the basic financial statements and the budgetary comparison statement of the Lottery. The schedule of percentage return to the State of New Mexico for the year ended June 30, 2016, and the schedule of vendor information as required by Section 2.2.2.10 (A)(2)(g) NMAC are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The schedule of percentage return to the State of New Mexico is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements for the year ended June 30, 2016, and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of percentage return to the State of New Mexico is fairly stated in all material respects in relation to the basic financial statements as a whole for the year ended June 30, 2016.



Board of Directors  
New Mexico Lottery Authority and  
Mr. Tim Keller  
New Mexico State Auditor

The schedule of vendor information as required by Section 2.2.2.10 (A)(2)(g) NMAC has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

The Lottery's basic financial statements and budgetary comparison statement for the year ended June 30, 2015 were audited by other auditors, whose report thereon dated October 20, 2015, expressed unmodified opinions on the respective financial statements of the business-type activities, and the aggregate remaining fund information and the budgetary comparison statement. The report of the other auditors dated October 20, 2015, stated that the Lottery's schedule of percentage return to the State of New Mexico for the year ended June 30, 2015 was subjected to the auditing procedures applied in the audit of the 2015 basic financial statements and certain additional auditing procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare those basic financial statements or the those basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America and, in their opinion, was fairly stated in all material respects in relation to the basic financial statements as a whole for the year ended June 30, 2015.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated October 4, 2016, on our consideration of the Lottery's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the result of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Lottery's internal control over financial reporting and compliance.



**CliftonLarsonAllen LLP**

Albuquerque, New Mexico  
October 4, 2016

## New Mexico Lottery Authority

### MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)

This Management's Discussion and Analysis of the New Mexico Lottery Authority (Lottery), offers readers of the Lottery's financial statements a narrative overview and analysis of the financial activities of the Lottery for the fiscal years ended June 30, 2016 and 2015 with comparative numbers for the fiscal year ended June 30, 2014. Please read it in conjunction with the financial statements, which begin on page 27.

#### FINANCIAL HIGHLIGHTS

- At the end of fiscal years 2016 and 2015, the Lottery's total current assets decreased by \$70,330, a 0.6% decrease, and \$4,430,614, a 29% decrease, respectively, in comparison to June 30<sup>th</sup> of each previous fiscal year.
- Compared to the end of the two preceding fiscal years, the Lottery's total current liabilities decreased by \$1,161,463, a 9% decrease, and \$2,842,226, an 18% decrease.
- In fiscal year 2016, total net ticket sales were \$154,344,768, an increase of \$17,328,045, a 12.6% increase, compared to the previous fiscal year. In fiscal year 2015, total net ticket sales were \$137,016,723, an increase of \$1,014,119, a 0.7% increase, compared to total net sales of \$136,002,604 in fiscal year 2014.
- From the prior fiscal years, total game expenses increased by \$12,260,378, or 13.5%, in fiscal year 2016 and \$1,276,204, or 1.4%, in fiscal year 2015.
- Total operating expenses decreased by \$1,404,972, or (27.8)%, in fiscal year 2016 and \$182,933 or (3.5)%, in fiscal year 2015, each in comparison to the previous fiscal year.
- Non-operating income (expense) decreased by \$2,443, (9.2)% and by \$5,704, (17.6)%, in fiscal year 2016 and 2015, respectively, compared to each preceding fiscal year.
- In fiscal year 2016, net income was \$47,565,157, an increase of \$6,443,936 or a 15.7% increase over fiscal year 2015's net income. Whereas, net income in fiscal year 2015 was \$41,121,221, a decrease of \$87,329, or a 0.2% decrease, compared to the previous fiscal year's net income of \$41,208,550.

Beginning July 1, 2007, the Lottery was required by the New Mexico Lottery Act to transmit at least twenty-seven percent of its gross revenues to the State of New Mexico and then at least 30% beginning in January 2009. In each fiscal year of 2016 and 2015, the Lottery transmitted 30.00% in net return to the State. In addition, in each of the last two fiscal years, the Lottery met the 30% required gross revenue return each month.

- Including the final transfer on July 29, 2016 of June 2016's net revenues (net income); the Lottery has transferred \$700,880,455 to the State of New Mexico since the commencement of sales in April 1996.

## MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED

### OVERVIEW OF THE FINANCIAL STATEMENTS

The Lottery was established in 1995 as a public body, politic and corporate, separate and apart from the State of New Mexico and constituting a governmental instrumentality and, therefore, is accounted for as such, reporting all of the Lottery's assets and liabilities using the accrual basis of accounting, much like any private-sector business entity. Since the Lottery is a component unit of the State, the Lottery's financial statements are incorporated into the State of New Mexico's Comprehensive Annual Financial Reports.

This report consists of three parts—the Management's Discussion and Analysis (this section), the basic financial statements, including the notes to the financial statements; supplementary information, the Budgetary Comparison Statements, and supplementary information, the Schedules of Percentage Return to the State of New Mexico.

**Financial Statements.** The Statements of Net Position on Page 27 and the Statements of Revenues, Expenses, and Changes in Net Position on page 28 report the Lottery's assets, liabilities, revenues and expenses in comparative format for fiscal year 2016 and fiscal year 2015. The Statements of Cash Flows on pages 29 and 30 report the sources and uses of cash for fiscal years 2016 and 2015. The Statements of Fiduciary Net Position on page 31 and Statements of Changes in Fiduciary Net Position on page 32 report the balances and activity of the Lottery's Retirement Plans for fiscal years 2016 and 2015.

**Notes to Financial Statements.** The Notes to Financial Statements on pages 33 to 54 provide additional information that is essential for a full understanding of the financial statements and provide more detailed data.

**Budgetary Comparison Statements.** The Budgetary Comparison Statements on page 55 show the variances between the budgets and actual Lottery performance.

**Schedules of Percentage Return to the State of New Mexico.** The Schedules of Percentage Return to the State of New Mexico on page 56 reports the percentages of gross revenues that were returned to the State of New Mexico for fiscal years 2016 and 2015 in compliance with the New Mexico Lottery Act.

To assess the Lottery's financial position and financial health, the reader of these statements should pay particular attention to changes in the components of assets and liabilities as set forth in the Statements of Net Position; in changes in total revenues, game expenses, operating expenses, non-operating income (expense) and net income as set forth in the Statements of Revenues, Expenses, and Changes in Net Position; and in the sources and uses of cash as set forth in the Statements of Cash Flows.

New Mexico Lottery Authority

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED**

**FINANCIAL ANALYSIS**

**Total Net Position**

At the end of fiscal years 2016 and 2015, the Lottery's net position was \$1,508,000 and \$267,000, respectively.

**Total Assets**

Table 1  
Total Assets

	2016	2015	2014	Increase (Decrease) \$ Change 2015 to 2016	Increase (Decrease) % Change 2015 to 2016	Increase (Decrease) \$ Change 2014 to 2015	Increase (Decrease) % Change 2014 to 2015
Cash and cash equivalents	\$ 6,381,875	\$ 5,515,045	\$ 10,280,672	\$ 866,830	15.7%	\$ (4,765,627)	(46.4)%
Accounts receivable, (net of allowance for doubtful accounts)	742,846	1,586,110	1,326,831	(843,264)	(53.2)	259,279	19.5
Reserves on deposit	3,308,537	3,420,292	3,431,968	(111,755)	(3.3)	(11,676)	(0.3)
Inventory	156,721	162,024	122,891	(5,303)	(3.3)	39,133	31.8
Prepaid expenses	179,517	156,355	108,078	23,162	14.8	48,277	44.7
<b>Total current assets</b>	<b>10,769,496</b>	<b>10,839,826</b>	<b>15,270,440</b>	<b>(70,330)</b>	<b>(0.6)</b>	<b>(4,430,614)</b>	<b>(29.0)</b>
Capital assets, net	3,248,070	3,329,832	827,886	(81,762)	(2.5)	2,501,946	302.2
<b>Total assets</b>	<b>\$ 14,017,566</b>	<b>\$ 14,169,658</b>	<b>\$ 16,098,326</b>	<b>\$ (152,092)</b>	<b>(1.1)%</b>	<b>\$ (1,928,668)</b>	<b>(12.0)%</b>

Compared to each prior fiscal year, the Lottery's cash and cash equivalents increased by \$866,830, a 15.7% increase at the end of fiscal year 2016, while in fiscal 2015 cash and cash equivalents decreased by \$4,765,627, a 46.4% drop. The changes in cash and cash equivalents relate mainly to changes in accounts receivable, accounts payable and prizes payable at the end of each fiscal year compared to the prior fiscal year. At the end of fiscal year 2016, accounts receivable were collected on the last day of the year, which helped to increase the cash balance. In fiscal year 2015, the purchase of the Lottery's corporate offices and warehouse was finalized on June 26, 2016 with part of the purchase being paid with cash.

Accounts receivable from the Lottery's retailers are collected each Thursday through electronic bank transfers. Receivables are equal to sales by retailers net of any prizes paid by the retailers and any commissions earned; less the allowance for bad debts plus any miscellaneous

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED**

**FINANCIAL ANALYSIS – CONTINUED**

**Total Assets - Continued**

receivables from any other source. At the end of fiscal year 2016, Accounts receivables decreased by \$843,264, a 53.2% decrease, while at the end of fiscal year 2015, accounts receivable increased by \$259,279, a 19.5% increase. The change in fiscal year 2016 is due to collecting the amount owed for the prior week on the last day of the year. Accounts receivable for fiscal year 2015 compared to the previous fiscal year 2014 are due to the difference in sales and related prize payments and commissions that had not yet been collected since the last bank EFT sweep in the respective fiscal year and due to having significantly higher multi-draw sales at the end of the fiscal year that were for drawings included in fiscal year 2015 sales compared to the multi-draw sales included in fiscal year 2014 sales. These multi-draw sales were adjusted into the fiscal year in which the drawings were held.

The Lottery has amounts on deposit with the Multi-State Lottery Association (MUSL) called reserves on deposit, as required by the Powerball® (Powerball), Hot Lotto® (Hot Lotto), Mega Millions® (Mega Millions), and Monopoly Millionaires' Club® game rules and an unreserved account for payment of expenses and to record receipts of interest and other income on the deposits. The changes in these accounts in both fiscal years 2016 and 2015 of decreases of \$111,755 and \$11,676, respectively were caused by the receipts of interest earned and other income on the deposits with MUSL; payments of game expenses; changes to the Mega Millions, Hot Lotto, and Monopoly Millionaires' Club reserve accounts, as required by the Mega Millions, Hot Lotto, and Monopoly Millionaires' Club game rules; and the re-balancing of the reserve accounts.

The inventory balance at the end of fiscal year 2016 decreased by \$5,303, a 3.3% decrease, while in 2015 it increased by \$39,133, a 31.8% increase. The Lottery has agreements signed in March 2010 and amended in March 2014, with its primary instant ticket printer, whereby the tickets printed are owned by the vendor with the Lottery having an obligation to pay for the tickets when the tickets are sold. Therefore, these tickets are not included in the Lottery's inventory. But, under an agreement signed with a secondary instant ticket printer in March 2010 and amended in March 2014, the Lottery began purchasing the instant tickets printed by this vendor. The Lottery has accounted for games printed under this agreement as ticket inventory using the specific identification method at the lower of cost or market. At the end of each of the two fiscal years 2016 and 2015, the Lottery had remaining inventory purchased under this agreement of \$155,771 and \$112,102 for fifteen and thirteen games, respectively in each year. In addition, at the end of fiscal years 2016 and 2015, the Lottery had inventory of \$950 and \$1,732, respectively, for a promotional instant game purchased. Included in inventory, the Lottery also had merchandise prizes at the end of fiscal year 2015 of \$48,190 for a summer second chance drawing promotion.

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED**

**FINANCIAL ANALYSIS – CONTINUED**

**Total Assets – Continued**

The changes in capital assets in fiscal years 2016 and 2015 are attributable to \$181,700 and \$2,847,624 in capital asset purchases and \$225,958 and \$298,547 in depreciation, for the two fiscal years, respectively. At the end of fiscal year 2015, the Lottery purchased its corporate offices and warehouse. The facility had been advertised for sale in December 2013 at \$3,900,000. After many months, the Lottery was able to purchase the building for \$2,700,000 or approximately two-thirds of the original asking price and at a price under the appraised market value of the facility. The purchase of the facility will provide substantial cost savings to the Lottery in comparison to the previous lease costs.

As part of the facility lease agreements signed in 2002 and 2012, the landlord paid for \$29,975 and \$51,858 in tenant improvements for the Lottery's corporate offices and warehouse in fiscal years 2013 and 2012, respectively. The Lottery had capitalized \$72,543 as tenant improvements with a related deferred liability, while the remaining purchases of tenant improvements totaling \$9,290 were expensed because the items purchased did not meet the \$5,000 threshold for capitalization. When the Lottery purchased its corporate offices and warehouse, the remaining capital lease obligation of \$60,724 for tenant improvements was retired as part of the purchase transaction. Therefore, at the end of fiscal year 2015, both the current and long-term obligation for the tenant improvements became zero on the books of the Lottery.

New Mexico Lottery Authority

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED**

**FINANCIAL ANALYSIS – CONTINUED**

**Total Liabilities**

Table 2  
Total Liabilities

	2016	2015	2014	Increase (Decrease) \$ Change 2015 to 2016	Increase (Decrease) % Change 2015 to 2016	Increase (Decrease) \$ Change 2014 to 2015	Increase (Decrease) % Change 2014 to 2015
<b>Current Liabilities</b>							
Accounts payable and other current liabilities	\$ 1,760,948	\$ 1,537,100	\$ 2,145,418	\$ 223,848	14.6%	\$ (608,318)	(28.4)%
Current portion of note payable	231,644	223,123	-	8,521	3.8	223,123	-
Current portion of capital lease obligation	-	2,595	14,064	(2,595)	(100.0)	(11,469)	(81.5)
Prizes payable	6,331,639	8,110,042	10,552,075	(1,778,403)	(21.9)	(2,442,033)	(23.1)
Due to Lottery Tuition Fund	3,440,087	3,052,921	3,056,450	387,166	12.7	(3,529)	(0.1)
<b>Total current liabilities</b>	<b>11,764,318</b>	<b>12,925,781</b>	<b>15,768,007</b>	<b>(1,161,463)</b>	<b>(9.0)</b>	<b>(2,842,226)</b>	<b>(18.0)</b>
<b>Long-term Liabilities</b>							
Noncurrent portion of note payable	745,248	976,877	-	(231,629)	(23.7)	976,877	-
Noncurrent portion of capital lease obligation	-	-	63,319	-	-	(63,319)	(100.0)
<b>Total long-term liabilities</b>	<b>745,248</b>	<b>976,877</b>	<b>63,319</b>	<b>(231,629)</b>	<b>(23.7)</b>	<b>913,558</b>	<b>1,442.8</b>
<b>Total liabilities</b>	<b>\$ 12,509,566</b>	<b>\$ 13,902,658</b>	<b>\$ 15,831,326</b>	<b>\$ (1,393,092)</b>	<b>(10.0)%</b>	<b>\$ (1,928,668)</b>	<b>(12.2)%</b>

Accounts payable and other current liabilities increased by \$223,848 at the end of fiscal year 2016, while in fiscal year 2015 accounts payable and other current liabilities decreased by \$608,318 or (28.4)%. In both fiscal years, the changes compared to the prior fiscal year were mainly due to amounts owed to five vendors for advertising, the on-line gaming system, instant ticket printing fees, and the lottery's share of prizes payable to MUSL for Powerball, Hot Lotto, and Mega Millions. Sales amounts and advertising during the last weeks of each fiscal year will generally determine the amounts owed at the end of each fiscal year to these vendors and whether that amount is higher or lower than in the prior fiscal year.

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED**

**FINANCIAL ANALYSIS – CONTINUED**

**Total Liabilities - Continued**

Prizes payable is essentially comprised of amounts accrued based on the Lottery's game designs and prize structures for draw game and instant game prizes, the related unremitted federal and state taxes withheld on prizes claimed, and any unclaimed prizes in the prize fund. At the end of fiscal years 2016 and 2015, prizes payable decreased by \$1,778,403, (21.9)%, and \$2,442,033, (23.1)%. These differences relate to the changes of prizes payable on individual Lottery games between the fiscal years as a result of sales in each fiscal year and prizes not yet claimed. In addition, in both fiscal years 2016 and 2015, the Lottery had to use unclaimed prizes to supplement the prizes in scratcher (instant ticket) games in order to sustain the growing scratcher sales and to enable it to meet the 30% return to the Legislative Lottery Scholarship Fund each month.

At the end of fiscal years 2016 and 2015, \$3,440,087 and \$3,052,921, respectively, of net revenues for the month of June were due to the Lottery Tuition Fund. These funds were transferred to the New Mexico State Treasurer by the end of July of each year.

At the end of both fiscal year 2016 and 2015, the Lottery reflected a current portion of a note payable of \$231,644 and \$223,123, respectively, and a noncurrent portion of a note payable of \$745,248 and 976,877, respectively for each year. These amounts represented the amounts owed to a local bank for financing the purchase of the Lottery's corporate offices and warehouse. At the end of fiscal years 2016 and 2015, the note payable totaled \$976,892 and \$1,200,000, respectively.



New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED

FINANCIAL ANALYSIS – CONTINUED

Net Ticket Sales and Prize Expense

Table 3  
Net Ticket Sales and  
Prize Expense

2016	Net Ticket Sales	Prize Expense
Instant tickets	\$ 83,105,873	\$ 47,531,599
Powerball	43,321,879	21,660,960
Mega Millions	10,509,262	5,270,102
Roadrunner Cash	7,394,565	4,695,036
Pick 3	4,891,153	2,853,765
Hot Lotto	4,283,277	2,202,208
Quicksters	691,531	446,528
Lucky Numbers Bingo	147,228	94,185
Total	\$ 154,344,768	\$ 84,754,383
2015	Net Ticket Sales	Prize Expense
Instant tickets	\$ 79,956,236	\$ 45,678,174
Powerball	27,722,571	13,861,367
Mega Millions	11,161,262	5,580,632
Roadrunner Cash	6,240,297	3,737,198
Pick 3	4,621,530	2,742,610
Hot Lotto	5,997,386	2,998,693
Quicksters	742,509	473,980
Lucky Numbers Bingo	153,912	93,665
Monopoly Millionaires' Club	421,020	426,006
Total	\$ 137,016,723	\$ 75,592,325
2014	Net Ticket Sales	Prize Expense
Instant tickets	\$ 69,804,813	\$ 39,624,564
Powerball	34,027,555	16,983,374
Mega Millions	13,410,732	6,704,090
Roadrunner Cash	8,592,684	5,266,316
Pick 3	3,828,187	2,208,335
Hot Lotto	5,700,311	2,907,024
Quicksters	638,322	366,543
Total	\$ 136,002,604	\$ 74,060,246
\$ Increase from FY 2015 to FY 2016	\$ 17,328,045	\$ 9,162,058
% Increase from FY 2015 to FY 2016	12.6%	12.1%
\$ Increase from FY 2014 to FY 2015	\$ 1,014,119	\$ 1,532,079
% Increase from FY 2014 to FY 2015	0.7%	2.1%

**MANAGEMENT’S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED**

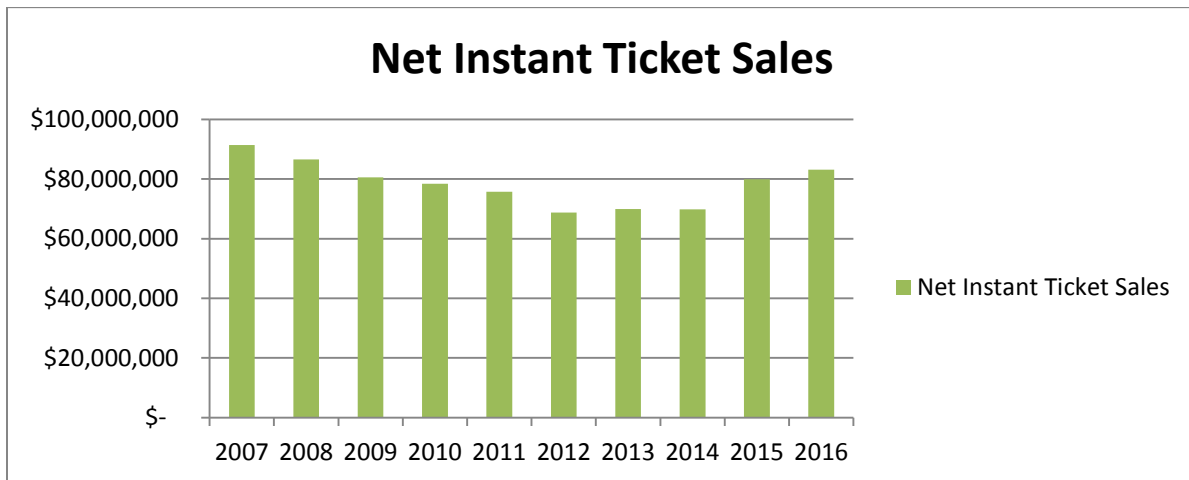
**FINANCIAL ANALYSIS – CONTINUED**

**Net Ticket Sales and Prize Expense – Continued**

Table 3 provides net ticket sales and prize expense for each lottery game for fiscal years 2016, 2015, and 2014. In fiscal year 2016 net sales and the related prize expense increased for instant tickets, Powerball, Roadrunner Cash, and Pick 3, while Mega Millions, Hot Lotto and Quickster and the related prize expense decreased. The Lucky Numbers Bingo game net sales went down in fiscal year 2016, but produced more lucky winners than in the previous fiscal year. In fiscal year 2015 net sales and the related prize expense increased for instant tickets, Hot Lotto, Pick 3, and Quicksters, while Powerball, Mega Millions and Roadrunner Cash net sales and the related prize expense decreased. The new games Monopoly Millionaires’ Club and Lucky Numbers Bingo were added in fiscal year 2015 and produced sales of \$575,000.

***Net Ticket Sales***

***NET INSTANT TICKET SALES – FYs 2007 Through 2016***



Since the last quarter of fiscal year 2014, net instant sales continue to grow with instant sales increasing in fiscal year 2016 by \$3,150,000, a 3.9% increase, and by \$10,151,000, a 14.5% increase in fiscal year 2015. This growth has occurred due to a comprehensively planned instant ticket sales strategy, including using unclaimed prizes to supplement the prizes in instant ticket games, launching instant games on the first Tuesday of the month, providing diagrams for retailers to follow in placing instant tickets into the dispensers and self-service lottery terminals, and increasing the visibility of instant tickets by using on-counter dispensers.

In addition, in both fiscal years 2016 and 2015, the Lottery has continued to use the customer relationship management (CRM) system for placing instant game tickets at retailer locations. The Lottery’s customer service representatives have continued placing calls each week to

New Mexico Lottery Authority

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED**

**FINANCIAL ANALYSIS - CONTINUED**

**Net Ticket Sales and Prize Expense – Continued**

***Net Ticket Sales – Continued***

each retailer location, reviewing the inventory at each location with the retailer, and placing orders as needed based on the inventory turnover at each location. In fiscal year 2016, fifty new instant ticket games were launched – 14 - \$1, 11 - \$2, 9 - \$3, 11 - \$5, 4 - \$10, and 1 - \$20 price point games – 1 more \$1, 1 more \$2, 2 more \$3, and 2 more \$10 games than in fiscal year 2015. In fiscal year 2015, forty-four new instant ticket games were launched – 13 - \$1, 10 - \$2, 7 - \$3, 11 - \$5, 2 - \$10 and 1 - \$20 price point games—3 less \$3 games, 1 more \$5, and 3 less \$10 game than in fiscal year 2014. In fiscal year 2016, the Lottery launched 25 games with free (prize) tickets and 25 games without prize tickets, while in fiscal year 2015, the Lottery launched 19 games with free (prize) tickets and 25 games without prize tickets.

As reflected in the graph on the previous page, sales are rebounding in the last few years toward the \$91.3 million net instant ticket sales of ten years ago. Fiscal year 2016 ended the year with over \$83.1 million dollars in net instant ticket sales, still \$8.2 million less than the fiscal year 2007 record setting net instant ticket sales of \$91.3 million. Fiscal year 2015 ended the year with nearly \$80 million in net instant ticket sales, nearly \$10.2 million more than the previous year. Without this \$10.2 million increase in instant ticket sales in fiscal year 2015, the Lottery would have returned over three million dollars less to the Legislative Lottery Scholarship fund in the fiscal year.

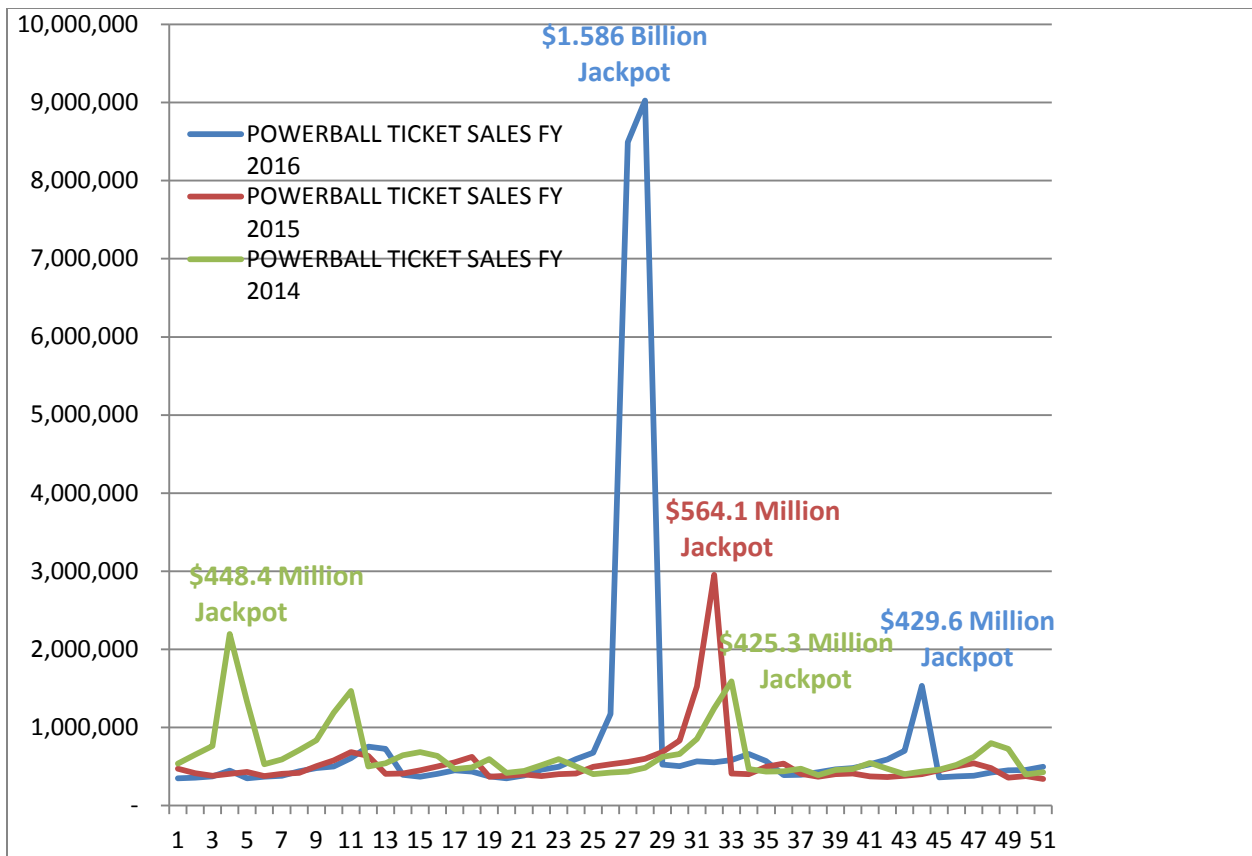
**MANAGEMENT’S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED**

**FINANCIAL ANALYSIS - CONTINUED**

**Net Ticket Sales and Prize Expense – Continued**

***Net Ticket Sales – Continued***

**POWERBALL TICKET SALES – FYs 2016, 2015, & 2014**



Powerball sales are driven by the advertised jackpot. As time passes, the jackpot that will influence the casual players into buying a jackpot ticket keeps growing. To tackle Powerball jackpots not growing to “super jackpots” and sales decreasing in the last two fiscal years, Powerball was changed starting on October 4, 2015. The game is now a five (5) out of sixty-nine (69) plus one (1) out of twenty-six (26) lottery game instead of a five (5) out of fifty-nine (59) plus one (1) out of thirty-five (35) lottery game. In addition, a 10X multiplier was added when the Grand Prize Jackpot is \$150 million or less, the Match 4 plus one prize was increased to \$50,000 from \$10,000, and the overall odds of winning a prize are better at 1:24.87 compared to 1:31.85 previously.

For the first six months of fiscal year 2016, Powerball sales each month were approximately 67% to 85% of the year-to-date sales budget with four jackpots during those months growing to \$70, \$110, \$310.5, and \$144.1 million. In January 2016 after 20 jackpot rolls, the Powerball

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED**

**FINANCIAL ANALYSIS - CONTINUED**

**Net Ticket Sales and Prize Expense – Continued**

***Net Ticket Sales – Continued***

jackpot grew to a record setting \$1.586 billion jackpot that brought in approximately \$18 million in additional sales and helped Powerball finally reach and surpass its year-to-date sales budget. Two more jackpots followed in the fiscal year, growing to \$291.4 after 14 jackpot rolls and to \$429.6 after 19 jackpot rolls – this last jackpot not growing anywhere near the \$1.586 jackpot created in January after 20 jackpot rolls. Powerball sales culminated the fiscal year at \$43.3 million, a \$15.6 million increase over fiscal year 2015, or a 56.3% increase.

In fiscal year 2015, there were 14 jackpot run-ups with a February 2015 jackpot of \$564.1 million being the largest jackpot of the fiscal year. Other jackpots that grew to over one-hundred million during the year before being won were \$228.5, \$202.6, \$188.9, \$136.0, and \$124.9 million. There were eight other jackpots that were less than \$90 million when won. Having only one note-worthy jackpot in fiscal year 2015 caused sales to be \$6.3 million less than in fiscal year 2014, (18.5)% less. Nationally, Powerball sales were 17.2% less in fiscal year 2015 than in fiscal year 2014.

In fiscal year 2014, there were 11 jackpot run-ups with an August 2013 jackpot of \$448.4 million being the largest of the fiscal year followed by another jackpot of \$425.3 million in February 2014. Other jackpots reached \$399.4, \$259.8, \$213.4, \$148.8, \$130.3, and \$122.9 million with three other jackpots that were less than \$100 million when won. While three jackpots surpassed or were nearly \$400 million when won, not having the “super jackpots” of nearly \$600 million dollars as in the prior fiscal year caused sales in fiscal year 2014 to be more than \$12.7 million less than in fiscal year 2013.

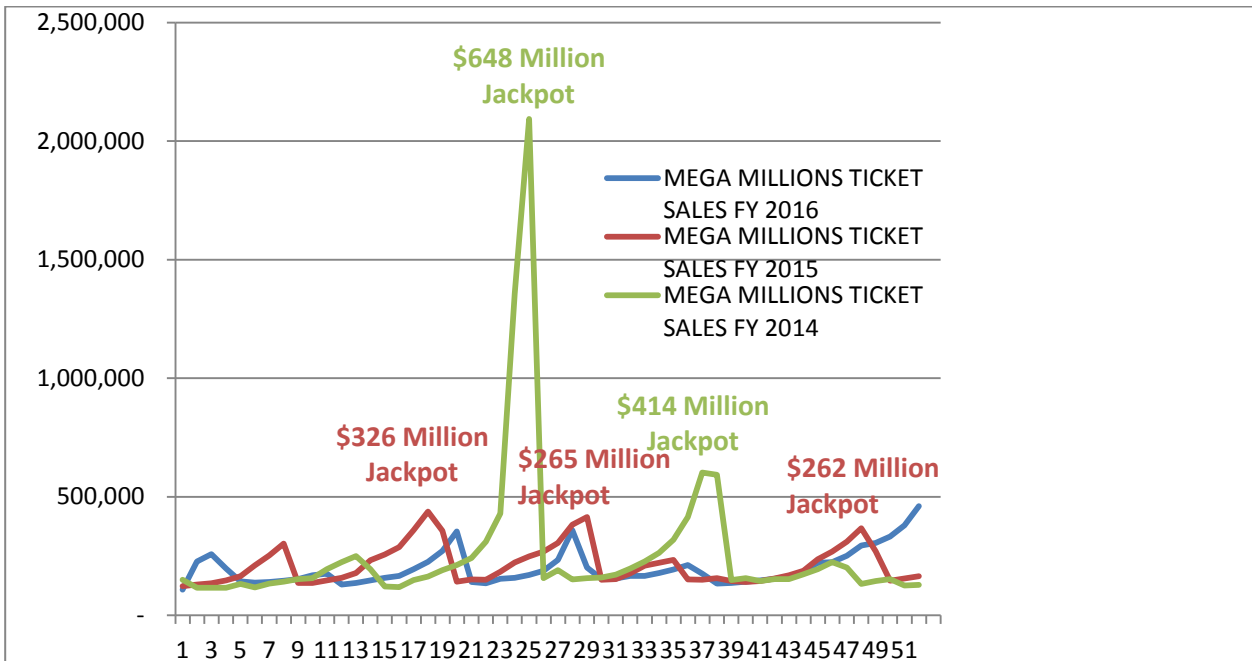
**MANAGEMENT’S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED**

**FINANCIAL ANALYSIS - CONTINUED**

**Net Ticket Sales and Prize Expense – Continued**

***Net Ticket Sales – Continued***

**MEGA MILLIONS TICKET SALES – FYs 2016, 2015, & 2014**



Mega Millions’ sales are also driven by the jackpot amount. In fiscal year 2016, the largest jackpot roll-up was only \$202 million with the five other jackpots in the fiscal year being \$25, \$106, \$153, \$157, and \$169 million. Therefore, Mega Million sales were only \$10.5 million for the year; \$652,000, or (5.84)% less than the prior fiscal year.

In fiscal year 2015, there were 6 jackpots that were won by players; the largest jackpot was \$326 million, followed by a \$265 million, a \$262 million, a \$180 million, a \$125 million and a \$58 million jackpot. Again, due to the lack of huge jackpots, fiscal year 2015 closed with sales being nearly \$11.2 million, which were \$2.25 million, (16.8)% less than the previous fiscal year.

In fiscal year 2014, the highest jackpot for Mega Millions was \$648 million in December 2013 followed by a \$414 million jackpot in March 2014. There were also two jackpots of \$189 million and \$149 million and 8 jackpots of less than \$80 million. The December 2013 jackpot brought in approximately four million dollars of incremental sales during the last few drawings while the jackpot was growing. Due to the large jackpots, Mega Millions closed the year with \$5.3 million in net sales over the prior fiscal year; a 66% increase in net sales.

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED**

**FINANCIAL ANALYSIS - CONTINUED**

**Net Ticket Sales and Prize Expense – Continued**

***Net Ticket Sales – Continued***

Similar to the Powerball and Mega Millions games, Roadrunner Cash sales are driven by the jackpot (top) prize amount. In fiscal year 2016 there was one jackpot that grew to \$705,000, one that grew to \$355,000 followed by two over \$200,000, two over \$100,000 and thirteen jackpots that were less than \$100,000. With these jackpots, sales for Roadrunner Cash surpassed the sales for the previous fiscal year by nearly \$1.2 million, or 18.5%. In fiscal year 2015 there were four jackpot run-ups that exceeded \$200,000 with the largest being \$275,000; six jackpots exceeded \$100,000 and seven jackpots were \$67,000 or less. With so few jackpots growing to over \$200,000, Roadrunner cash net sales ended the year \$2.35 million, (27.4)%, less than the previous fiscal year. In fiscal year 2014, Roadrunner Cash had a record setting jackpot of \$890,000. During that month, Roadrunner Cash sales grew by approximately \$1.5 million. There was also one jackpot that rose to \$385,000 and another jackpot that rose to \$307,000 with two other jackpots growing to \$265,000 and \$220,000 before being won; twelve other jackpots were \$160,000 or less. Fiscal year 2014 ended with Roadrunner Cash net sales being \$1.8 million dollars more than the prior fiscal year.

The MUSL game, Hot Lotto, is another smaller national jackpot game offered by the Lottery. Sales for this game also track with the jackpot. In fiscal year 2016, the Hot Lotto jackpot was won on July 1<sup>st</sup> when it was \$9.85 million; on that day it started again at \$1 million and grew until December when it was won at \$4.46 million. It then started again at \$1 and grew the rest of the year, ending the year at \$3.6 million. Therefore, fiscal year 2016 sales were only \$4.3 million, a decrease of \$1.7 million or (28.6)%. In fiscal year 2015, the Hot Lotto jackpot started the year at \$8.56 million and was won in September 2014. It started again at \$1 million dollars and grew all year until it was won on July 1, 2015. Fiscal year 2015's net sales ended the year \$297,000, 5.2%, ahead of the previous fiscal year. Fiscal year 2014 started with the Hot Lotto jackpot at approximately \$6.9 million. The jackpot grew until it was won by a New Mexico Lottery player on August 3, 2013 when it was \$7.3 million. Following this win, the jackpot climbed to nearly \$2 million when it was won in October and then began climbing again at that time, ending the year at just over \$8.1 million. These changing jackpots reflect on net sales during each fiscal year.

Pick 3 sales continued to grow in fiscal year 2016, ending the year at nearly \$4.9 million, \$270,000 or 5.8% ahead of the previous fiscal year. In early June 2014, the Lottery added a mid-day drawing. With a mid-day drawing adding additional sales for the full fiscal year, Pick 3 ended fiscal year 2015 more than \$793,000, 20.7%, ahead of fiscal year 2014. For the month of June 2014, when mid-day drawings started, sales of approximately \$4,700 for each mid-day draw occurred and provided nearly \$90,000 in additional sales for the month. Pick 3 net sales increased in fiscal year 2014 by \$335,271. Pick 3 has remained a core game for the Lottery bringing in steady monthly average net sales; in fiscal year 2016 of more than \$400,000 each month and in fiscal year 2015 of nearly \$400,000 each month.

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED**

**FINANCIAL ANALYSIS – CONTINUED**

**Net Ticket Sales and Prize Expense – Continued**

***Net Ticket Sales – Continued***

A new game, Quicksters, was started on March 25, 2012. Quicksters are instant-win games, similar to instant ticket games, but produced by the same lottery sales terminals as draw game tickets and with no scratching needed to reveal the prizes. In fiscal year 2016, net quickster sales were \$692,000, a drop of approximately \$51,000, (6.9)%, compared to the previous fiscal year. In fiscal year 2015, Quicksters net sales were \$742,509, a 16.3% increase over fiscal year 2014 Quickster net sales of \$638,000.

On November 9, 2014, the Lottery introduced a new game, Lucky Numbers Bingo. Lucky Numbers Bingo is a draw game that offers two ways to play and two ways to win either through the Bingo numbers or through the Lucky Numbers. Lucky Numbers Bingo produced \$154,000 in net sales in fiscal year 2015, but dropped to approximately \$147,000 in fiscal year 2016, a 4.4% drop.

The Lottery also started a national game, Monopoly Millionaires' Club, on October 19, 2014, which was a five dollar draw game with a weekly drawing, promotional drawings for a trip to Las Vegas, NV to be on an associated TV game show. This national game was played until December 26, 2014, when it was ended nationally due to its overall performance.

***Prize Expense***

Prize expense for the draw games of Powerball, Mega Millions and Hot Lotto is based on the overall prize payout per the game design, while prize expense for Roadrunner Cash, Pick 3, Quicksters and Lucky Numbers Bingo is determined by the prizes won each month for each drawing or game. The prize expense for the Monopoly Millionaires' Club game was based on the actual cost of the prizes for the period that it was played. The prizes included in the prize structure for each instant game printed determine prize expense for instant games. In general, prize expense increases or decreases from year-to-year relative to the increases or decreases in sales for each Lottery product and the prize structures of the games.

In fiscal year 2016, the prize payout decreased by approximately .71%, while in fiscal years 2015 and 2014, the prize payout increased by approximately 2.74% and 1.09%, respectively, prior to the application of unclaimed prizes. The decrease in fiscal year 2016 was mainly due to a lower prize payout on instant games.

At the end of the claim period for each game, unclaimed prizes for the Lottery's instant games and draw games are paid into the "Prize Fund," in accordance with the New Mexico Lottery Act. These unclaimed prizes from the Lottery's prize fund have been used to supplement the prizes in instant and draw games and for second chance drawings and, therefore, reduce the prize expense for Lottery products and help the Lottery to maximize its sales and its return to education. Unclaimed prizes were used to supplement prizes in order to meet the 30% return in eleven months in fiscal year 2016 and in each month in fiscal year 2015.



New Mexico Lottery Authority

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED**

**FINANCIAL ANALYSIS – CONTINUED**

**Net Ticket Sales and Prize Expense – Continued**

***Prize Tickets***

In fiscal years 2016 and 2015, tickets provided as prizes (prize or free tickets) claimed for instant games increased by nearly \$431,000, a 18.4% increase, and nearly \$245,000, a 11.7%, increase, respectively while in fiscal year 2014 tickets provided as prizes decreased by \$383,000 or (15.5)%. Prize tickets are placed in the prize structure of the game in lieu of the breakeven prizes. Prize tickets give a player a prize of another instant game ticket of the same price point as the instant ticket that had the winning prize ticket. Each fiscal year, the Lottery continues to study the market to determine the optimum quantity of prize tickets to place in its instant ticket games in order to optimize its instant ticket sales.

**Game Expenses**

Table 4  
Game Expenses

	2016	2015	2014	Increase (Decrease) \$ Change 2015 to 2016	Increase (Decrease) % Change 2015 to 2016	Increase (Decrease) \$ Change 2014 to 2015	Increase (Decrease) % Change 2014 to 2015
Prize expense	\$ 84,754,383	\$ 75,592,325	\$ 74,060,246	\$ 9,162,058	12.1%	\$ 1,532,079	2.1%
Retailer							
commissions	10,035,060	8,941,265	8,782,855	1,093,795	12.2	158,410	1.8
On-line vendor							
fees	4,284,035	2,193,183	2,177,205	2,090,852	95.3	15,978	0.7
Advertising	2,053,906	2,174,697	2,267,772	(120,791)	(5.6)	(93,075)	(4.1)
Ticket vendor							
fees	1,314,494	1,265,885	1,188,107	48,609	3.8	77,778	6.5
Other game							
expenses	703,038	717,183	1,132,149	(14,145)	(2.0)	(414,966)	(36.7)
Total game							
expenses	\$ 103,144,916	\$ 90,884,538	\$ 89,608,334	\$ 12,260,378	13.5%	\$ 1,276,204	1.4%

The changes in retailer commissions for fiscal years 2016 and 2015 are consistent with the changes in gross ticket sales for the two years and are equivalent to 6.50% and 6.52% of gross revenues for the two years, respectively. Retailer commissions are paid to the Lottery's retailers for selling Lottery tickets, cashing Lottery prizes and for selling a jackpot/grand prize

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED**

**FINANCIAL ANALYSIS – CONTINUED**

**Game Expenses – Continued**

for Powerball, Mega Millions or Hot Lotto, for selling a match 5 prize for Powerball or Mega Millions, and for selling a jackpot prize of more than \$100,000 for Roadrunner Cash.

Since November 21, 2008, the on-line vendor fee has been a fixed percentage of net sales, plus applicable gross receipts taxes, with no additional terminal fees as in previous agreements. The on-line fee increases or decreases as draw game and instant ticket net sales increase or decrease. Effective November 22, 2015, the Lottery entered into an agreement for on-line vendor services following the issuance of a Request for Proposals in May 2015. Only one of the three on-line vendors provided a proposal for these services. The system includes the supply, installation, maintenance, service, and operation of a communication network, a new back office accounting system, new lottery terminals and peripheral equipment for the Lottery's existing and future retailers, ticket scanners to enable players to check their tickets for prizes, self-service ticket vending machines that sell both instant and draw game tickets, disaster recovery services, and various employees to operate the system and provide sales and marketing support to the Lottery. For fiscal years 2016 and 2015, the changes in the on-line vendor fees for the two fiscal years are consistent with the changes in draw game and instant ticket net sales in the fiscal years and the change in rate in fiscal year 2016 and are equivalent to 2.77% and 1.60% of gross revenues for the two years, respectively.

Advertising money is expended to market the Lottery and its products to the public and to inform the public about the games that are available, the jackpot and top prize amounts for the draw games, to provide security tips and gambling awareness for our players and benefit messages to New Mexico students and their families, and to keep the lottery products fresh in the public's minds, all in order to maximize sales. Advertising expense was approximately 1.33% and 1.59% of gross revenues, respectively, for fiscal years 2016 and 2015 and stayed within the Lottery Board approved budgets of \$2,200,000 and \$2,400,000, respectively, for each fiscal year. In fiscal year 2016 and 2015, the advertising dollars were maximized by purchasing advertising for the entire year at the beginning of the year. In fiscal years 2016 and 2015, the annual buys provided \$1.2 million and \$900,000, respectively, of additional advertising without any added cost.

In fiscal years 2010 the Lottery signed a new contract with its primary ticket printer effective in March of that year. Under this contract, the instant tickets are owned by the vendor with the Lottery expensing the cost to ticket vendor fees and paying for the tickets as a percentage of net instant sales when the tickets are sold. In addition, in March 2010, the Lottery signed a contract with a secondary printer, whereby the Lottery would be purchasing the tickets printed. These tickets are included in inventory with the cost of the tickets being recorded as ticket vendor fees as the tickets are consigned to retailers. Both of these contracts were extended for four additional years in March 2014. In addition, in both fiscal year 2016 and 2015, the cost for any licensing fees or special printing costs are also included in ticket vendor fees. The ticket vendor fees for both fiscal year 2016 and 2015 are .85% and .92% of gross revenues and are consistent with net instant ticket sales for each fiscal year.

New Mexico Lottery Authority

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED**

**FINANCIAL ANALYSIS – CONTINUED**

**Game Expenses - Continued**

Included in other game expenses are shipping and postage, retailer equipment, promotions, responsible gaming, game membership, and drawing game expenses. Fiscal year 2016 reflects a decrease of \$14,145, or (2.0)% and fiscal year 2015 reflects a decrease of \$414,966 or (36.7)%. In fiscal year 2014, the Lottery had purchased electronic jackpots for its retailers, in fiscal year 2016 and 2015 there were no further purchases of these products. In addition, in fiscal year 2015, the in-house lottery drawings for Roadrunner Cash and Pick 3 were automated at the end of October, thus, saving nearly \$66,000 during the rest of the fiscal year in this line item expense and nearly \$103,000 in fiscal year 2016. Further, in fiscal year 2016 and 2015, promotions were reduced by \$17,000 and \$87,000, respectively, and shipping and postage was reduced by \$35,000 and \$23,500, respectively. In fiscal year 2016, MUSL game membership fees were decreased by \$10,000, while in fiscal year 2015 game membership fees increased by \$23,000 mainly due to the new game, Monopoly Millionaires' Club.

**Operating Expenses**

Table 5  
Operating Expenses

	2016	2015	2014	(Decrease) \$ Change 2015 to 2016	(Decrease) % Change 2015 to 2016	Increase (Decrease) \$ Change 2014 to 2015	Increase (Decrease) % Change 2014 to 2015
Salaries, wages, and benefits	\$ 2,609,094	\$ 3,485,280	\$ 3,726,941	\$ (876,186)	(25.1)%	\$ (241,661)	(6.5)%
Utilities and maintenance	313,846	410,518	448,166	(96,672)	(23.5)	(37,648)	(8.4)
Leases, property taxes, and insurance	145,591	435,550	423,932	(289,959)	(66.6)	11,618	2.7
Other operating expenses	584,094	726,249	641,491	(142,155)	(19.6)	84,758	13.2
Total operating expenses	<u>\$ 3,652,625</u>	<u>\$ 5,057,597</u>	<u>\$ 5,240,530</u>	<u>\$ (1,404,972)</u>	(27.8)%	<u>\$ (182,933)</u>	(3.5)%

Operating expenses are made up of salaries, wages and benefits, utilities and maintenance, leases, property taxes, and insurance, and other operating expenses, which include professional fees, depreciation and amortization, materials and supplies, travel, and other expenses. In fiscal year 2016, operating expenses were reduced by \$1.4 million or (27.8)% and in fiscal year 2015, operating expenses were reduced by nearly 183,000 or 3.5%. Salaries, wages and benefits were reduced by more than \$876,000 in fiscal year 2016. The Lottery

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED**

**FINANCIAL ANALYSIS – CONTINUED**

**Operating Expenses – Continued**

started the year with 51 full-time and part-time employees and ended the year with 34 full-time and part-time employees; a reduction of force occurred during the year involving 15 full-time employee positions. In fiscal year 2016, the Lottery was also able to save approximately \$160,000 in expense for its corporate offices and warehouse through the purchase of the building in June 2015. In addition, with the reduction in its work force and fleet, the Lottery was able to save approximately \$80,000 in additional expenses.

In fiscal year 2015, salaries, wages, and benefits were reduced by nearly \$242,000 or 6.5%. At the end of fiscal year 2014, the Lottery employed 57 individuals, while at the end of fiscal year 2015, the Lottery employed 51 individuals. During fiscal year 2015, a restructuring of departments took place where jobs were combined and positions were changed or eliminated through attrition. In addition, during open enrollment in December 2014, the benefits offered for health insurance coverage were changed by increasing the co-pays and out-of-pocket amounts paid by employees to bring the premiums to a more reasonable level and the percentage amounts of the premiums that the Lottery paid for employee and dependent coverage were decreased; for the employer portion for employees the Lottery increased the portion paid to 90% of the premium instead of 75% of the premium, but decreased the amount paid for dependents to approximately 50% of the premium instead of the 75% of the premium that it had always paid. In a full year, this change in the percentages paid for employee and dependent premiums was projected to save over \$48,000 a year. There were also other cost savings in utilities and maintenance and in materials and supplies, which were offset by increases for depreciation and for professional fees.

**Non-Operating Income**

Non-operating income decreased in both fiscal years 2016 and 2015. Interest rates paid on deposits continue to be low during both fiscal years. No significant other income was received in either fiscal year 2016 or 2015.

**Non-Operating Expense**

Due to the purchase of the Lottery's corporate offices and warehouse at the end of fiscal year 2015, a small amount of interest expense was accrued on the Lottery's books. The Lottery paid \$40,000 in interest on the note in fiscal year 2016.

New Mexico Lottery Authority

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED**

**FINANCIAL ANALYSIS – CONTINUED**

**Net Income**

Table 6  
Net Income

	<u>Total Operating Revenues</u>	<u>Net Income</u>
Fiscal Year 2016	<u>\$ 154,338,488</u>	<u>\$ 47,565,157</u>
Fiscal Year 2015	<u>\$ 137,036,703</u>	<u>\$ 41,121,221</u>
Fiscal Year 2014	<u>\$ 136,025,057</u>	<u>\$ 41,208,550</u>
Increase from FY 2015 to FY 2016	<u>\$ 17,301,785</u>	<u>\$ 6,443,936</u>
% Increase from FY 2015 to FY 2016	<u>12.6%</u>	<u>15.7%</u>
Increase (Decrease) from FY 2014 to FY 2015	<u>\$ 1,011,646</u>	<u>\$ (87,329)</u>
% Increase (Decrease) from FY 2014 to FY 2015	<u>0.7%</u>	<u>(0.2)%</u>

Effective July 1, 2007, the New Mexico Lottery Act, Chapter 6, Article 24 NMSA 1978, was changed to require the Lottery to transmit at least twenty-seven percent of its gross revenues to the State Treasurer until December 31, 2008 and at least thirty percent of its gross revenues thereafter. In fiscal years 2016 and 2015, the Lottery transmitted its net income each month, totaling \$46,324,157 and \$41,121,221, respectively. The gross revenue percentage return for fiscal year 2016 and 2015 was 30.00% each month in both fiscal years.

The changes in net income for fiscal years 2016 and 2015 were related to the changes in sales for the Lottery's games during the two years netted against savings in the cost of the product and operating expenses during the two fiscal years, which is reviewed in the previous pages of this Management's Discussion and Analysis.

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED

FINANCIAL ANALYSIS – CONTINUED

**Budgetary Comparison**

Table 7  
Budgetary Comparison

	2016				
	Original Budget	Final Budget	Actual	Variance with Final Budget	% Variance with Final Budget
Total operating revenues	\$ 141,438,000	\$ 151,188,000	\$ 154,338,488	\$ 3,150,488	2.1%
Total game expenses	93,775,000	101,759,000	103,144,916	1,385,916	1.4
Total operating expenses	<u>5,207,000</u>	<u>4,044,000</u>	<u>3,652,625</u>	<u>(391,375)</u>	(9.7)
Operating income	42,456,000	45,385,000	47,540,947	2,155,947	4.8
Total non-operating income (expense)	<u>(17,000)</u>	<u>(22,000)</u>	<u>24,210</u>	<u>46,210</u>	(210.0)
Net income before transfers to Lottery Tuition Fund	<u>\$ 42,439,000</u>	<u>\$ 45,363,000</u>	<u>\$ 47,565,157</u>	<u>\$ 2,202,157</u>	4.9%
	2015				
	Original Budget	Final Budget	Actual	Variance with Final Budget	% Variance with Final Budget
Total operating revenues	\$ 142,800,000	\$ 138,037,000	\$ 137,036,703	\$ (1,000,297)	(0.7)%
Total game expenses	94,130,000	91,244,000	90,884,538	(359,462)	(0.4)
Total operating expenses	<u>5,846,000</u>	<u>5,399,000</u>	<u>5,057,597</u>	<u>(341,403)</u>	(6.3)
Operating income	42,824,000	41,394,000	41,094,568	(299,432)	(0.7)
Total non-operating income (expense)	<u>24,000</u>	<u>24,000</u>	<u>26,653</u>	<u>2,653</u>	11.1
Net income before transfers to Lottery Tuition Fund	<u>\$ 42,848,000</u>	<u>\$ 41,418,000</u>	<u>\$ 41,121,221</u>	<u>\$ (296,779)</u>	(0.7)%

In fiscal year 2016, the original budget was revised to reflect the better performance in sales for instant tickets, Powerball, and Roadrunner Cash and to reduce the sales for Mega Millions, Hot Lotto, Quicksters, and Lucky Numbers Bingo. Net sales were increased by more than \$9.7

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED**

**FINANCIAL ANALYSIS - CONTINUED**

**Budgetary Comparison - Continued**

million, made up of a \$1 million increase for instant sales, a \$12 million increase for Powerball, a \$700,000 increase for Roadrunner Cash, a \$2.4 million decrease for Mega Millions, a \$1.7 million decrease for Hot Lotto, a \$50,000 decrease for Quicksters, and a \$75,000 decrease for Lucky Numbers Bingo, as well as a \$200,000 decrease for tickets provided as prizes and a \$75,000 decrease for spoiled, stolen, and promotional tickets. Game expenses were increased by nearly \$8.0 million and operating expenses were reduced by nearly \$1.2 million. The net income return was increased by more than \$2.9 million. The final return remained at 30% with these changes.

Fiscal year 2016 culminated with net sales out-performing the final (revised) budget by more than \$3.1 million or 102% of the budget. Net sales exceeded the budget for instant sales by more than \$700,000, for Powerball sales by more than \$1.3 million, for Mega Millions by more than \$900,000, for Roadrunner Cash by nearly \$200,000 and for Pick 3 by nearly \$100,000, but for Hot Lotto, Quicksters, and Lucky Numbers Bingo, sales didn't reach the budget by approximately \$17,000, \$58,000 and \$28,000, respectively. Game expenses were 101% of the final budget and operating expenses were 90% of the final budget. Net income ended the year at 102% of the final (revised) budget with nearly \$2.2 in additional revenue.

In fiscal year 2015, the original budget was revised to reflect better performance in sales for instant tickets, Mega Millions, Hot Lotto, and Pick 3 and to reduce Powerball, Roadrunner Cash, Monopoly Millionaires' Club, Lucky Numbers Bingo and Quicksters sales. The net sales budget was reduced by \$4,766,000, which was made up of a \$5.0 million increase for instant tickets, a \$3.0 million increase for Mega Millions, a \$1.0 million increase for Hot Lotto, and \$400,000 increase for Pick 3 sales, but was reduced by \$8.0 million for Powerball, \$500,000 for Roadrunner Cash, \$2,579,000 for Monopoly Millionaires' Club, \$3,250,000 for Lucky Numbers Bingo, and \$725,000 for Quicksters, as well as a reduction for tickets provided as prizes of \$700,000 and for spoiled stolen and promotional tickets of \$188,000. Game expenses were reduced by nearly \$2.9 million and operating expenses were reduced by \$447,000. The final return remained at 30% with these changes.

Fiscal year 2015 ended with net instant ticket sales out-performing the revised budget by nearly \$2.3 million and net Pick 3 sales exceeding the revised budget by \$22,000. All the other games did not meet the revised budget; Powerball was short of the revised budget by over \$2.2 million and Mega Millions by over \$838,000. Once again not having any significant jackpot run-ups during the year kept Powerball from meeting either the original budget or the revised budget. Without the increased performance for instant tickets sales, this would have been a dismal fiscal year for sales and the return to the Legislative Lottery Scholarship Fund would have been approximately \$3 million less. All in all, because of the instant ticket sales performance, gross revenues ended the fiscal year at 99.28% of the revised budget, game expenses at 99.61% of the revised budget, operating expenses at 93.68% of the revised budget, and net income at 99.28% of the revised budget.

New Mexico Lottery Authority

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED**

**FINANCIAL ANALYSIS - CONTINUED**

**Requests for Additional Financial Information**

This financial report is designed to provide the executive and legislative branches of the State of New Mexico, the public, the Lottery's retailers, vendors, creditors, and other interested parties with a general overview of the financial position of the Lottery as of June 30, 2016 and 2015, and results of its operations, cash flows, variances from budgets, and percentage return to the state for the years then ended and to demonstrate the Lottery's accountability for the revenues it receives. If you have any questions about this report or need additional information, contact the Director of Administration at the New Mexico Lottery Authority, P.O. Box 93130, Albuquerque, New Mexico 87199.



New Mexico Lottery Authority

**STATEMENTS OF NET POSITION**

June 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 6,381,875	\$ 5,515,045
Accounts receivable (net of allowance for doubtful accounts)	742,846	1,586,110
Reserves on deposit	3,308,537	3,420,292
Inventory	156,721	162,024
Prepaid expenses	<u>179,517</u>	<u>156,355</u>
Total current assets	10,769,496	10,839,826
<b>CAPITAL ASSETS, NET</b>	<u>3,248,070</u>	<u>3,329,832</u>
Total assets	<u>\$ 14,017,566</u>	<u>\$ 14,169,658</u>
<b>CURRENT LIABILITIES</b>		
Accounts payable and other current liabilities	\$ 1,760,948	\$ 1,537,100
Current portion of note payable	231,644	223,123
Current portion of capital lease obligation	-	2,595
Prizes payable	6,331,639	8,110,042
Due to Lottery Tuition Fund	<u>3,440,087</u>	<u>3,052,921</u>
Total current liabilities	<u>11,764,318</u>	<u>12,925,781</u>
<b>LONG-TERM LIABILITIES</b>		
Noncurrent portion of note payable	<u>745,248</u>	<u>976,877</u>
Total long-term liabilities	<u>745,248</u>	<u>976,877</u>
Total liabilities	<u>\$ 12,509,566</u>	<u>\$ 13,902,658</u>
<b>NET POSITION</b>		
Net investment in capital assets	\$ 2,271,178	\$ 2,129,832
Unrestricted (deficit)	<u>(763,178)</u>	<u>(1,862,832)</u>
Total net position	<u>\$ 1,508,000</u>	<u>\$ 267,000</u>

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

New Mexico Lottery Authority

**STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION**

Years ended June 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
<b>OPERATING REVENUES</b>		
Instant ticket sales	\$ 83,105,873	\$ 79,956,236
Powerball sales	43,321,879	27,722,571
Mega Millions sales	10,509,262	11,161,262
Roadrunner Cash sales	7,394,565	6,240,297
Pick 3 sales	4,891,153	4,621,530
Hot Lotto sales	4,283,277	5,997,386
Quickster sales	691,531	742,509
Lucky Numbers Bingo sales	147,228	153,912
Monopoly Millionaires' Club sales	-	421,020
Net ticket sales	<u>154,344,768</u>	<u>137,016,723</u>
Retailer fees	14,720	19,980
Bad debts	<u>(21,000)</u>	-
Total operating revenues	<u>154,338,488</u>	<u>137,036,703</u>
<b>GAME EXPENSES</b>		
Prize expense	84,754,383	75,592,325
Retailer commissions	10,035,060	8,941,265
On-line vendor fees	4,284,035	2,193,183
Advertising	2,053,906	2,174,697
Ticket vendor fees	1,314,494	1,265,885
Shipping and postage	276,853	312,134
Retailer equipment	182,538	96,816
Promotions	116,770	134,190
Responsible gaming	69,999	69,998
Game membership	56,878	66,895
Drawing game	-	37,150
Total game expenses	<u>103,144,916</u>	<u>90,884,538</u>
<b>OPERATING EXPENSES</b>		
Salaries, wages, and benefits	2,609,094	3,485,280
Utilities and maintenance	313,846	410,518
Professional fees	229,908	232,028
Depreciation and amortization	225,958	298,547
Leases, property taxes, and insurance	145,591	435,550
Other	54,878	52,281
Materials and supplies	48,743	77,233
Travel	24,607	66,160
Total operating expenses	<u>3,652,625</u>	<u>5,057,597</u>
<b>OPERATING INCOME</b>	<u>47,540,947</u>	<u>41,094,568</u>
<b>NON-OPERATING INCOME (EXPENSE)</b>		
Interest expense	(40,104)	(236)
Other income	47,173	10,516
Interest income	17,141	16,373
Total non-operating income	<u>24,210</u>	<u>26,653</u>
Net income before transfers	47,565,157	41,121,221
Transfers to Lottery Tuition Fund	<u>46,324,157</u>	<u>41,121,221</u>
Change in net position	1,241,000	-
Net position at beginning of year	<u>267,000</u>	<u>267,000</u>
Net position at end of year	<u>\$ 1,508,000</u>	<u>\$ 267,000</u>

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

New Mexico Lottery Authority

**STATEMENTS OF CASH FLOWS**

Years ended June 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Cash flows from operating activities		
Cash received:		
From retailers-sales net of commissions, incentives, and prize, spoiled, and stolen ticket credits	\$ 145,142,254	\$ 127,841,627
Cash payments:		
To prize winners and related taxes	(69,215,424)	(67,726,913)
To MUSL	(17,317,362)	(10,307,445)
To suppliers of goods or services	(9,135,798)	(8,767,859)
To employees for services and related taxes	(2,259,228)	(2,844,830)
Net cash provided by operating activities	<u>47,214,442</u>	<u>38,194,580</u>
Cash flows from noncapital financing activities		
Transfers to Lottery Tuition Fund	<u>(45,936,991)</u>	<u>(41,124,750)</u>
Cash flows from capital and related financing activities		
Purchases of capital assets	(167,517)	(1,819,538)
Principal paid on capital debt	(223,108)	-
Interest paid on capital debt	(39,853)	-
Principal payments under capital lease	(2,595)	(27,657)
Net cash used by capital and related financing Activities	<u>(433,073)</u>	<u>(1,847,195)</u>
Cash flows from investing activities		
Receipts of interest	8,277	11,464
Other	14,175	274
Net cash provided by investing activities	<u>22,452</u>	<u>11,738</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	866,830	(4,765,627)
Cash and cash equivalents at beginning of year	<u>5,515,045</u>	<u>10,280,672</u>
Cash and cash equivalents at end of year	<u>\$ 6,381,875</u>	<u>\$ 5,515,045</u>

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

New Mexico Lottery Authority

**STATEMENTS OF CASH FLOWS - CONTINUED**

Years ended June 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Reconciliation of operating income to net cash provided by operating activities		
Operating income	\$ 47,540,947	\$ 41,094,568
Adjustments to reconcile operating income to net cash provided by operating activities		
Depreciation	225,958	298,547
Vendor's non-cash transactions	52,866	163,353
Interest on MUSL unreserved account	4,335	2,353
Net changes in assets and liabilities:		
Accounts receivable	838,826	(253,811)
Reserves on deposit	123,924	27,331
Inventory	5,303	(39,133)
Prepaid expenses	(23,162)	(48,277)
Accounts payable and other liabilities	223,848	(608,318)
Prizes payable	(1,778,403)	(2,442,033)
	<u>(1,778,403)</u>	<u>(2,442,033)</u>
Net cash provided by operating activities	<u>\$ 47,214,442</u>	<u>\$ 38,194,580</u>

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

New Mexico Lottery Authority

**STATEMENTS OF FIDUCIARY NET POSITION**

Years ended June 30, 2016 and 2015

	2016			2015		
	Money Purchase Pension Plan	Section 457(b) Plan	Total	Money Purchase Pension Plan	Section 457(b) Plan	Total
<b>ASSETS</b>						
Cash and cash equivalents	\$ 319,830	\$ -	\$ 319,830	\$ 377,891	\$ 1,606	\$ 379,497
Marketable securities and other investments	4,379,720	252,556	4,632,276	4,806,858	101,743	4,908,601
Contribution receivable	10,820	-	10,820	9,611	-	9,611
Total assets	<u>\$ 4,710,370</u>	<u>\$ 252,556</u>	<u>\$ 4,962,926</u>	<u>\$ 5,194,360</u>	<u>\$ 103,349</u>	<u>\$ 5,297,709</u>
<b>NET POSITION</b>						
Held in Trust for Pension plan participants' benefits	<u>\$ 4,710,370</u>	<u>\$ 252,556</u>	<u>\$ 4,962,926</u>	<u>\$ 5,194,360</u>	<u>\$ 103,349</u>	<u>\$ 5,297,709</u>

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

New Mexico Lottery Authority

**STATEMENTS OF CHANGES IN FIDUCIARY NET POSITION**

Years ended June 30, 2016 and 2015

	2016			2015		
	Money Purchase Pension Plan	Section 457(b) Plan	Total	Money Purchase Pension Plan	Section 457(b) Plan	Total
<b>ADDITIONS</b>						
Net Gain in fair value of investments	\$ -	\$ -	\$ -	\$ 32,071	\$ 15	\$ 32,086
Dividends	205,072	6,181	211,253	166,979	1,417	168,396
Employer contributions	263,884	-	263,884	342,629	-	342,629
Employee contributions	-	87,723	87,723	-	101,917	101,917
Employee rollovers	-	92,844	92,844	-	-	-
Total additions	<u>468,956</u>	<u>186,748</u>	<u>655,704</u>	<u>541,679</u>	<u>103,349</u>	<u>645,028</u>
<b>DEDUCTIONS</b>						
Net Loss in fair value of investments	323,107	5,693	328,800	-	-	-
Distributions to participants	627,349	31,188	658,537	707,122	-	707,122
Other activity	2,490	660	3,150	1,411	-	1,411
Total deductions	<u>952,946</u>	<u>37,541</u>	<u>990,487</u>	<u>708,533</u>	<u>-</u>	<u>708,533</u>
Change in net position	(483,990)	149,207	(334,783)	(166,854)	103,349	(63,505)
Net position - beginning	<u>5,194,360</u>	<u>103,349</u>	<u>5,297,709</u>	<u>5,361,214</u>	<u>-</u>	<u>5,361,214</u>
Net position - ending	<u>\$ 4,710,370</u>	<u>\$ 252,556</u>	<u>\$ 4,962,926</u>	<u>\$ 5,194,360</u>	<u>\$ 103,349</u>	<u>\$ 5,297,709</u>

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

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS**

June 30, 2016 and 2015

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

1. Reporting Entity

The financial reporting entity as defined by Governmental Accounting Standards Board (GASB) Statement 14 (as amended by GASB *Statement 61*) consists of the primary government, organizations for which the primary government is financially accountable, and other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading. This definition of the reporting entity is based primarily on the notion of financial accountability as the "cornerstone of all financial reporting in government."

With the enactment of the New Mexico Lottery Act (the Act) on July 1, 1995, the New Mexico Lottery Authority (the Lottery) was created as a public body, politic and corporate, separate and apart from the State of New Mexico and constituting a governmental instrumentality of the state. The Lottery was created and organized for the purpose of establishing and conducting the Lottery to provide revenues for the public purposes designated by the Act. The New Mexico Lottery was organized as an independent business enterprise separate from state government, self-sustaining and self-funded, without need for state revenues or resources and subject to oversight, audit, and accountability by public officials and agencies. However, since there is a financial benefit to the State's institutions of higher education, which are part of the State, the Lottery is considered a component unit of the State of New Mexico. The Lottery has no component units.

The Lottery commenced sales of instant tickets on April 27, 1996, and sales of draw game tickets on October 20, 1996.

2. Basis of Presentation

The financial statements are prepared on the economic resources measurement focus and the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

2. Basis of Presentation – Continued

Two Fiduciary Funds are used to account for assets held in a trustee capacity for Lottery employees. The Lottery's two fiduciary funds are a money purchase pension plan trust fund, the "New Mexico Lottery Authority Retirement Plan" and a section 457(b) pension plan trust fund, the "New Mexico Lottery Authority 457(b) Plan".

The pension trust funds per Statements of Fiduciary Net Position and Statements of Changes in Fiduciary Net Position and Note D reflect the activities of the New Mexico Lottery Authority Retirement Plans pursuant to a trust agreement with Verisight Trust Company in fiscal year 2015 and formerly with Wells Fargo bank prior to August 2014. The trustee holds, invests and distributes the assets of the Plan for the benefit of the Plan participants, subject to the overall direction of the Lottery in its capacity as plan administrator.

The Lottery distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing goods and services in connection with the Lottery's principal ongoing operations. The principal operating revenues of the Lottery are sales of instant and draw game tickets. The Lottery also recognizes retailer fees for connecting new retailers to the system as operating revenues. Operating expenses include the costs related to sales, administrative expenses required to manage and operate the Lottery, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

When an expense is incurred that can be paid using either restricted or unrestricted resources, the Lottery's policy is to first apply the expense toward unrestricted resources and then toward restricted resources. At the end of fiscal years 2016 and 2015 there were no restricted resources.

3. Budgets and Budgetary Accounting

Each year, Lottery management prepares a budget in conformity with GAAP for the succeeding fiscal year. The Lottery's budget is not legally binding. The budget is presented by management to the Lottery's board of directors for review, amendment, and approval prior to the beginning of the next fiscal year. Any revisions to this budget during the fiscal year are also approved by the Lottery's board of directors. The Lottery's financial statements are reviewed at each regular board of directors' meeting. Performance in relation to the budget is presented and discussed during these meetings.



New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

4. Cash and Cash Equivalents

For the purposes of the Statements of Cash Flows, the Lottery considers cash and cash equivalents to be cash on hand, demand deposits, time deposits with an original maturity of ninety days or less, and overnight repurchase agreements.

5. Accounts Receivable

Accounts receivable represent the unremitted receipts on ticket sales, net of retailer commissions and prizes paid by the retailers. Receipts are transferred weekly from retailer bank accounts to the Lottery. Credit losses relating to contracted retailers have been within management expectations. Generally, collateral is not required on receivables. At June 30, 2016 and 2015, an allowance for doubtful accounts of \$32,883 and \$31,540, respectively, has been provided to recognize future uncollectible billings. In fiscal years 2016 and 2015, ten retail customers (569 and 513 retailers) represented 62% and 61% of sales for each year, respectively, and 90% and 65% of accounts receivable for each year, respectively.

6. Reserves on Deposit

The Lottery is a member of the Multi-State Lottery Association (MUSL), which operates games on behalf of participating lotteries. MUSL currently operates the POWERBALL® (Powerball), Hot Lotto® (Hot Lotto) and Mega Millions® (Mega Millions) games for the Lottery. The Lottery sells Powerball, Hot Lotto and Mega Millions game tickets through its retailers and makes weekly wire transfers to MUSL in an amount equivalent to the member lottery's share of the estimated grand prize liability for each game. Lesser prizes are paid directly to the winners by each member lottery. The prize pools for Powerball and Hot Lotto are 50% of each game's drawing period's sales after the prize pool accounts and prize reserve accounts are funded to the amounts set by the MUSL product group. The prize pool for Mega Millions is up to 55% of each drawing period's sales after the prize reserve accounts are funded to the amounts set by the MUSL product group, but may be higher or lower based upon the number of winners at each prize level, as well as the funding required to meet a guaranteed Annuity Grand Prize. In fiscal year 2015, MUSL also operated Monopoly Millionaires' Club Game from October 19, 2014 to December 26, 2014 when the game was ended.

MUSL has established prize reserve accounts for the games it operates. These prize reserve accounts are funded out of the prize pools for the games until the accounts reach amounts set by the MUSL product groups for each game. Once the prize reserve funds exceed these designated maximums, the excess becomes part of the grand prize pool. The prize reserve funds serve as contingency reserves to protect MUSL and the party lotteries from unforeseen

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

6. Reserves on Deposit – Continued

prize liabilities. The money in these reserve funds is used at the discretion of the MUSL Board of Directors. Any amounts remaining in the prize pool accounts or prize reserve account when the MUSL product group declares the end of a game shall be returned to the lotteries participating in the accounts after the end of all claim periods of all selling lotteries, carried forward to a replacement game, or otherwise expended in a manner at the election of the individual members of the Product Group in accordance with jurisdiction statute.

As of October 1, 2013, the Powerball prize reserve deduction was set to begin at two percent (2%) when the annuity jackpot, as determined after sales are known, exceeds \$120 million, and four percent (4%) when the annuity jackpot, as determined after sales are known, exceeds \$250 million. Prior to this time, MUSL included 2% of the Lottery's Powerball drawing period's sales in two prize reserve accounts, the Powerball Prize Reserve Account (PRA) and the Set Prize Reserve Account (SPRA), until the Lottery's share in both the PRA and SPRA were fully funded. The maximum amounts designated by the MUSL Powerball product group for the PRA is \$80 million and for the SPRA is \$40 million for all member lotteries. At June 30, 2016 and 2015, the Lottery's share in the Powerball PRA was \$1,007,923 and \$1,046,525, respectively, and in the SPRA was \$438,227 and \$455,011, respectively. Both Powerball reserve funds were fully funded at the end of June 2016 and 2015, respectively.

MUSL includes up to 3% of the Lottery's Hot Lotto drawing period's sales, depending on the annuitized value of the Grand Prize, into a Prize Reserve Account (PRA). The MUSL product group has set the maximum Hot Lotto PRA balance at nine million dollars for all party lotteries. At June 30, 2016 and 2015, the Lottery's share in the Hot Lotto PRA was \$560,781 and \$654,465, respectively. The Hot Lotto PRA was fully funded at the end of June 2016 and 2015, respectively.

MUSL may include an additional amount up to 5% of the Lottery's Mega Millions drawing period's sales into the Mega Millions Prize Reserve Account (PRA). The MUSL product group has set the maximum PRA balance at \$45 million for all party lotteries. At June 30, 2016 and 2015 the Lottery's share in the Mega Millions PRA was \$448,485 and \$463,953, respectively. The Lottery's Mega Millions prize reserve was fully funded at the end of June 2016 and 2015.

As of June 30, 2015, MUSL held \$4,257 in a reserve account for the Monopoly Millionaires' Club Game. This amount was refunded to the Lottery in March 2016.

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

6. Reserves on Deposit – Continued

The Lottery also has an unreserved fund with MUSL. Interest earned on the MUSL funds and any unclaimed grand prizes may be deposited into the unreserved fund and game membership fees and other MUSL costs may be paid from this fund. At June 30, 2016 and 2015, the Lottery's share of the unreserved fund was \$853,121 and \$796,081, respectively.

A winner of a Powerball grand prize or Mega Millions grand prize may select that the prize be paid at the cash value of the prize or as an annuity. For both, Powerball and Mega Millions, the grand prize annuity is paid out in 30 graduated annual installments over 29 years. Government securities at the discounted value of the grand prize annuity are purchased to fund all future installments and are held in trust. Maturities are staggered in order to provide adequate cash flow for each annual installment. These assets and related liabilities are reflected in MUSL's financial statements and therefore are not reflected in the Lottery's financial statements. MUSL is responsible for transferring the cash or the annuity installment amounts to the member lottery prior to the payment to any grand prize winner. Currently, the Lottery is not paying any prize winner any annuity prize payments.

As of May 12, 2013, the Hot Lotto advertised grand prize is paid as a withholdings taxes paid single, cash payment prize where the estimated advertised grand prize is grossed up to include federal and state tax withholdings and the prize winner receives the net prize after tax withholdings.

7. Inventory

The Lottery entered into an agreement with its primary instant ticket printer, whereby the printer retains title to the instant ticket inventory until the instant tickets are sold. Under this agreement, the Lottery pays the vendor a fee based on a fixed percentage of the net instant tickets sold; net instant tickets sold represents instant ticket sales less prize, spoiled, stolen, and promotional tickets. In addition, the Lottery signed an agreement with a secondary instant ticket printer, whereby the Lottery purchases and owns the tickets printed. These tickets are carried at the lower of cost or market using the specific identification method. At the end of fiscal years 2015 and 2016, the Lottery was distributing games printed under the two agreements. As of June 30, 2016 and 2015, \$156,721 and \$113,834, respectively, of instant tickets are included in inventory. For fiscal year 2015, \$48,190 of merchandise prizes for second chance drawings are also included in inventory.

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

8. Capital Assets

Capital assets, which include land, building, works of art, data processing software and hardware, building improvements, vehicles, furniture and fixtures, intellectual property, and equipment, are stated at cost net of any accumulated depreciation. The Lottery capitalizes all assets that have a cost greater than \$5,000 and an expected useful life of more than one year. Land and works of art, which have a perpetual or undeterminable life, are not depreciated. The building will be depreciated over its effective useful life of thirty-eight years with a residual value of ten percent. Significant building improvements are amortized over the remaining life of the building at the time of purchase of the improvement or if insignificant over 7 years; and intellectual property is amortized over the remaining life at the time of acquisition or at the time of development. For all other capital assets placed into service on or after July 1, 2013, depreciation and amortization are computed using the straight-line method over the estimated useful lives of 4 to 10 years. For any assets placed into service prior to July 1, 2013, depreciation and amortization are computed using the straight-line method over the estimated useful lives of 2 to 5 years. When assets are retired or otherwise disposed, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is reflected in the results from operations in the period of disposal.

9. Revenue and Accounts Receivable Recognition

Lottery games are sold to the public by contracted retailers and directly by the Lottery. Revenues and accounts receivable for instant tickets are recognized when packs are settled and retailers are billed for the tickets. Revenues and accounts receivable for all draw games are recognized when drawings are held, except for Quicksters and Lucky Numbers Bingo, where the revenues and accounts receivable are recognized at the time the tickets are sold. Accounts receivable are stated at their net realizable value and their past due status is based upon contractual terms.

The following is a summary of total operating revenues that are comprised of instant and draw game ticket sales and the related prize, spoiled, stolen, and promotional tickets, which are netted into the applicable game sales on the financial statements; plus any retailer fees and related bad debts that are shown as a contra revenue account in total operating revenues.

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

9. Revenue and Accounts Receivable Recognition – Continued

	2016	2015
OPERATING REVENUES		
Instant ticket sales	\$ 85,947,924	\$ 82,340,495
Powerball sales	43,321,920	27,722,733
Mega Millions sales	10,509,268	11,161,264
Roadrunner Cash sales	7,394,571	6,240,297
Pick 3 sales	4,891,175	4,673,406
Hot Lotto sales	4,283,277	5,997,386
Quickster sales	691,536	742,510
Lucky Numbers Bingo sales	147,228	153,912
Monopoly Millionaires' Club sales	-	421,020
Less tickets provided as prizes	(2,771,818)	(2,340,965)
Less spoiled, stolen, and promotional tickets	(70,313)	(95,335)
Net ticket sales	154,344,768	137,016,723
Retailer fees	14,720	19,980
Bad debts	(21,000)	-
Total operating revenues	\$ 154,338,488	\$ 137,036,703

10. Prizes

Prize expense for instant, Powerball, Mega Millions, and Hot Lotto games is recorded based on an estimate of the predetermined prize structure for each game. Prize expense for Roadrunner Cash, Pick 3, Quickster, and Lucky Numbers Bingo games is recorded based on the actual prizes won for each game. The prize expense for Monopoly Millionaires' Club was the actual cost of the prizes.

11. Commissions

Retailers receive a commission of 6% on gross ticket sales and a 1% cashing commission on winning ticket validations for prizes up to \$600.

12. Advertising Costs

Advertising costs are expensed as incurred.

13. Income Taxes

The Lottery is exempt from Federal and New Mexico income taxes. Accordingly, no provision for income taxes has been made.

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

14. Custodial Credit Risk and Interest Rate Risk

At June 30, 2016 and 2015, respectively, the Lottery maintained its cash balances in one financial institution. The balances for demand deposits were insured by the Federal Deposit Insurance Corporation up to \$250,000 at this financial institution.

Custodial credit risk – Deposits. In the case of deposits, this is the risk that in the event of a bank failure, the Lottery’s deposits may not be returned to it. The Lottery does not have a deposit policy for custodial credit risk. The Lottery limits its custodial risk for its cash and requires collateral in an amount greater than or equal to 50% of any deposit not insured by Federal Insuring Agencies. A greater amount of collateral is required when the Lottery determines it is prudent. Collateral must meet State of New Mexico “Security of Public Money” standards and be held in the third party safekeeping.

Custodial credit risk – Investments. For an investment, custodial credit risk is the risk that in the event of the failure of the counterparty, the Lottery will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. Mutual funds, external investment pools, and securities underlying reverse repurchase agreements are not exposed to custodial credit risk. The Lottery does not have an investment policy for custodial credit risk.

The Lottery’s custodial risk for investments is in accordance with Article 10, NMSA, 1978 Compilation. The Lottery’s investments are made in overnight repurchase agreements. Investments are made through a local financial institution and are held in safekeeping at the Federal Reserve Bank. Repurchase agreements are collateralized by Government Securities with a market value of at least 102% of the principal and are used for overnight investment only. Collateral must meet State of New Mexico “Security of Public Money” standards and be held in third party safekeeping. As of June 30, 2016 and 2015, the Lottery’s bank balances of \$6,426,835 and \$5,558,081, respectively, were exposed to custodial credit risk as follows:

	<u>2016</u>	<u>2015</u>
Uninsured and uncollateralized	\$ -	\$ -
Collateral held by the pledging bank’s trust department in the Banks’ name	-	-
Collateral held by the pledging bank’s trust department in the Lottery’s name	<u>6,426,835</u>	<u>5,558,081</u>
	<u>\$ 6,426,835</u>	<u>\$ 5,558,081</u>

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

14. Custodial Credit Risk and Interest Rate Risk – Continued

Interest Rate Risk – Investments. Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Lottery does not have a specific policy to limit its exposure to interest rate risk.

At June 30, 2016 and 2015, the Lottery had overnight yield repurchase agreements with one-day maturities.

15. Bank Accounts

At June 30, 2016:

Description	Bank	Balance per Bank
Operating account - overnight repurchase Agreement	Wells Fargo Bank, NA	\$ 6,426,783
Operating account – checking	Wells Fargo Bank, NA	<u>52</u>
Total amount deposited in bank		6,426,835
Less: FDIC coverage		<u>(52)</u>
*Total uninsured funds – deposits and overnight repurchase agreement		<u><u>\$ 6,426,783</u></u>
102% pledged collateral requirement per statute for repurchase agreement		\$ 6,555,319
* Total pledged security		<u>(6,555,319)</u>
Amount under (over) requirement at June 30, 2016		<u><u>\$ -</u></u>

\*Wells Fargo Bank, NA securities are held in safekeeping at the Federal Reserve Bank in San Francisco, CA. Presented at fair value, CUSIP Number 3128MJTQ3 (cost \$6,094,388), matures November 01, 2043. The repurchase agreement is collateralized with securities held in the name of the New Mexico Lottery.

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

15. Bank Accounts - Continued

Cash and cash equivalents per bank at June 30, 2016	\$ 6,426,835
Less reconciling items--outstanding checks	<u>( 54,735)</u>
Reconciled cash in bank at June 30, 2016	6,372,100
Cash in vault	<u>9,775</u>
Total cash and cash equivalents per Statements of Net Position	<u>\$ 6,381,875</u>

At June 30, 2015:

<u>Description</u>	<u>Bank</u>	<u>Balance per Bank</u>
Operating account - overnight repurchase Agreement	Wells Fargo Bank, NA	\$ 5,558,081
Operating account - checking	Wells Fargo Bank, NA	<u>-</u>
Total amount deposited in bank		5,558,081
Less: FDIC coverage		<u>-</u>
*Total uninsured funds - deposits and overnight repurchase agreement		<u>\$ 5,558,081</u>
102% pledged collateral requirement per statute for repurchase agreement		\$ 5,669,242
* Total pledged security		<u>(5,669,243)</u>
Amount under (over) requirement at June 30, 2015		<u>\$ (1)</u>

\*Wells Fargo Bank, NA securities are held in safekeeping at the Federal Reserve Bank in San Francisco, CA. Presented at fair value, CUSIP Number 3128MJTQ3 (cost \$5,343,685), matures November 01, 2043. The repurchase agreement is collateralized with securities held in the name of the New Mexico Lottery.



New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

15. Bank Accounts – Continued

Cash and cash equivalents per bank at June 30, 2015	\$ 5,558,081
Less reconciling items--outstanding checks	<u>( 50,986)</u>
Reconciled cash in bank at June 30, 2015	5,507,095
Cash in vault	<u>7,950</u>
Total cash and cash equivalents per Statements of Net Position	<u>\$ 5,515,045</u>

16. Risk Management

The Lottery is exposed to various risks of loss related to torts; theft of, damage to, and the destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Lottery purchases commercial insurance to cover these risks. The amount of coverage has not been exceeded by claims in the last three years.

17. Shipping and Handling Costs

Shipping and handling costs associated with inventory distribution are expensed as incurred and included in game expenses.

18. Net Position

Net position represents the difference between all other elements in a statement of financial position and should be displayed in the applicable components of net investment in capital assets, restricted and unrestricted.

*Net Investment in Capital Assets* – consists of capital assets, net of accumulated depreciation, reduced by outstanding balances of bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, constructions, or improvement of those assets.

*Restricted* – consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. The Lottery does not have a restricted component of net position.

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

18. Net Position – Continued

*Unrestricted* – consists of the net amount of assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position. In May 2014, the New Mexico Lottery Authority Board executed a resolution to establish contingency reserves from operating expenses for the sole purpose of allowing the New Mexico Lottery Authority to successfully carry out the provision of the New Mexico Lottery Act.

19. Unclaimed Prizes

The Act requires that prizes not claimed within the time period established by the Lottery are forfeited and shall be paid into the prize fund (unclaimed prize liability accounts). Unclaimed prizes have been applied against prize expense to supplement prizes in the Lottery's games and to promotions to increase sales. As of June 30, 2016, the Lottery had unclaimed prizes in the amount of \$2,553,494 reported as prizes payable that had not yet been applied against prize expense. The \$2,553,494 in the unclaimed prize fund has already been committed and continues to supplement the prizes on instant games that have been printed and are currently for sale. Any unclaimed prizes will continue to be a portion of the thirty percent return to the Legislative Lottery Scholarship Fund.

20. Use of Estimates in Preparation of Financial Statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

21. Compensated Absences Payable

Annual leave and sick leave are accrued at rates specified by the Lottery's Leave Policy. Annual leave is awarded based on the employee's years of lottery service, leave status, and employment status (full-time or part-time) and sick leave is awarded at 3.7 hours biweekly for full-time employees. The maximum number of annual leave hours that full-time employees may carry over and retain in their annual leave bank varies from 80 hours for an employee with less than 5 years of service up to a maximum of 320 hours for an employee with fifteen or more years of service. The maximum number of sick leave hours that a full-time employee may carry over from year-to-year is 480 hours. Part-time employees receive leave and carry-over and retain leave in their leave banks based on their percentage of employment. Upon

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

21. Compensated Absences Payable – Continued

separation from service, employees with at least one year of service will be compensated for their annual leave balance, not to exceed the maximum annual leave bank based on their years of service. Accrued sick leave hours will not be paid to an employee upon separation from service. During the years ended June 30, 2016 and 2015, the following changes occurred in the compensated absences liabilities:

<u>Balance July 1, 2015</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance June 30, 2016</u>
\$ 205,288	\$ 19,164	\$ (66,440)	\$ 158,012
<u>Balance July 1, 2014</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance June 30, 2015</u>
\$ 207,240	\$ 23,304	\$ (25,256)	\$ 205,288

The balances of compensated absences payable are reported on the Statements of Net Position in accounts payable and other current liabilities. The portion of accrued compensated absences due after one year is not material and, therefore is not presented separately.

22. Long-term Liabilities

During the years ended June 30, 2016 and 2015, the following changes occurred in long-term obligations:

	<u>Balance July 1, 2015</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance June 30, 2016</u>	<u>Amounts Due Within One Year</u>
Note payable	\$ 1,200,000	\$ -	\$ (223,108)	\$ 976,892	\$ 231,644
Capital leases	2,595	-	(2,595)	-	-
	<u>\$ 1,202,595</u>	<u>\$ -</u>	<u>\$ (225,703)</u>	<u>\$ 976,892</u>	<u>\$ 231,644</u>
	<u>Balance July 1, 2014</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance June 30, 2015</u>	<u>Amounts Due Within One Year</u>
Note payable	\$ -	\$ 1,200,000	\$ -	\$ 1,200,000	\$ 223,123
Capital leases	77,383	-	(74,788)	2,595	2,595
	<u>\$ 77,383</u>	<u>\$ 1,200,000</u>	<u>\$ (74,788)</u>	<u>\$ 1,202,595</u>	<u>\$ 225,718</u>

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

22. Long-term Liabilities – Continued

A promissory note payable to Wells Fargo Bank, NA for the purchase of the building used as the Lottery’s facility and warehouse was issued on June 26, 2015. Principal and interest payments are due monthly on the 26<sup>th</sup> day of the month. The note bears interest at 3.6% and matures on June 26, 2020. The outstanding balance at June 30, 2016 and 2015 is \$976,892 and \$1,200,000, of which \$231,644 and \$223,123 are due within one year, respectfully. Upon the purchase of the Lottery’s corporate offices and warehouse, the remaining capital lease obligation of \$60,724 was retired as part of the purchase transaction.

23. Debt Service Requirements for Note Payable

Debt service requirements on note payable as of June 30, 2016, are as follows:

<u>Year Ending June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2017	\$ 231,644	\$ 31,318	\$ 262,962
2018	239,736	23,225	262,961
2019	248,634	14,327	262,961
2020	256,878	5,107	261,985
	<u>\$ 976,892</u>	<u>\$ 73,977</u>	<u>\$ 1,050,869</u>

24. Accounts Payable and Other Current Liabilities

Accounts payable and other current liabilities are comprised of the following at June 30:

	<u>2016</u>	<u>2015</u>
Accounts payable	\$ 1,187,354	\$ 764,598
Accrued liabilities, vendors*	278,532	433,567
Accrued liabilities, retailers*	12,500	21,500
Accrued payroll and payroll taxes and benefits	124,550	112,147
Compensated absences	158,012	205,288
	<u>\$ 1,760,948</u>	<u>\$ 1,537,100</u>

\* The Lottery has accrued an estimated amount of services delivered by its vendors and deposits for its retailers as of June 30, 2016 and 2015, respectively.

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE B – CAPITAL ASSETS**

Capital assets at June 30, 2016 consisted of:

	Beginning Balance	Reclass- ification	Increases	Decreases	Ending Balance
Land	\$ 730,000	\$ -	\$ -	\$ -	\$ 730,000
Works of Art	6,850	-	6,850	-	13,700
Building	1,975,163	-	-	-	1,975,163
Data processing software	2,193,682	-	-	-	2,193,682
Data processing equipment	758,810	(76,251)	-	(6,008)	676,551
Equipment - Security and disaster recovery	635,622	(14,678)	-	-	620,944
Vehicles	452,284	(22,674)	75,943	(294,621)	210,932
Furniture and fixtures	230,767	(10,410)	11,908	-	232,265
Intellectual property	179,073	-	-	-	179,073
Equipment - communications	160,507	-	-	-	160,507
Equipment - warehouse	71,174	-	-	-	71,174
Equipment - office	49,508	-	10,632	(31,122)	29,018
Equipment - drawing	35,472	(35,472)	-	-	-
Building improvements	-	-	76,367	-	76,367
Obsolete capital assets	709,452	159,485	-	(23,287)	845,650
Capital assets	<u>8,188,364</u>	<u>-</u>	<u>181,700</u>	<u>(355,038)</u>	<u>8,015,026</u>
Building	-	-	(46,779)	-	(46,779)
Data processing software	(2,112,120)	-	(8,934)	-	(2,121,054)
Data processing equipment	(670,014)	76,251	(14,012)	6,008	(601,767)
Equipment - Security and disaster recovery	(557,397)	14,678	(30,790)	-	(573,509)
Vehicles	(357,697)	22,674	(52,164)	257,117	(130,070)
Furniture and fixtures	(230,767)	10,410	-	-	(220,357)
Intellectual property	(61,750)	-	(24,699)	-	(86,449)
Equipment - communications	(29,925)	-	(21,764)	-	(51,689)
Equipment - warehouse	(69,852)	-	(1,322)	-	(71,174)
Equipment - office	(49,508)	-	-	31,122	(18,386)
Equipment - drawing	(10,050)	35,472	(25,422)	-	-
Building improvements	-	-	(72)	-	(72)
Obsolete capital assets	<u>(709,452)</u>	<u>(159,485)</u>	<u>-</u>	<u>23,287</u>	<u>(845,650)</u>
Accumulated depreciation	<u>(4,858,532)</u>	<u>-</u>	<u>(225,958)</u>	<u>317,534</u>	<u>(4,766,956)</u>
Capital assets, net	<u>\$ 3,329,832</u>	<u>\$ -</u>	<u>\$ (44,258)</u>	<u>\$ (37,504)</u>	<u>\$ 3,248,070</u>

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE B - CAPITAL ASSETS - CONTINUED**

Capital assets at June 30, 2015 consisted of:

	Beginning Balance	Reclass- ification	Increases	Decreases	Ending Balance
Land	\$ -	\$ -	\$ 730,000	\$ -	\$ 730,000
Works of Art	-	-	6,850	-	6,850
Building	-	-	1,975,163	-	1,975,163
Data processing software	2,430,865	(307,183)	70,000	-	2,193,682
Data processing equipment	861,982	(134,027)	60,805	(29,950)	758,810
Equipment - Security and disaster recovery	638,837	(3,215)	-	-	635,622
Vehicles	452,284	-	-	-	452,284
Furniture and fixtures	230,767	-	-	-	230,767
Intellectual property	179,073	-	-	-	179,073
Equipment - communications	266,174	(110,473)	4,806	-	160,507
Equipment - warehouse	71,174	-	-	-	71,174
Equipment - office	49,508	-	-	-	49,508
Equipment - drawing	106,800	(71,328)	-	-	35,472
Tenant improvements	425,850	(845)	-	(425,005)	-
Obsolete capital assets	165,112	627,071	-	(82,731)	709,452
Capital assets	<u>5,878,426</u>	<u>-</u>	<u>2,847,624</u>	<u>(537,686)</u>	<u>8,188,364</u>
Building	-	-	-	-	-
Data processing software	(2,412,702)	307,183	(6,601)	-	(2,112,120)
Data processing equipment	(789,759)	134,027	(44,232)	29,950	(670,014)
Equipment - Security and disaster recovery	(529,822)	3,215	(30,790)	-	(557,397)
Vehicles	(276,184)	-	(81,513)	-	(357,697)
Furniture and fixtures	(230,767)	-	-	-	(230,767)
Intellectual property	(37,050)	-	(24,700)	-	(61,750)
Equipment - communications	(118,635)	110,473	(21,763)	-	(29,925)
Equipment - warehouse	(68,266)	-	(1,586)	-	(69,852)
Equipment - office	(49,508)	-	-	-	(49,508)
Equipment - drawing	(14,921)	71,328	(66,457)	-	(10,050)
Tenant improvements	(357,814)	845	(20,905)	377,874	-
Obsolete capital assets	<u>(165,112)</u>	<u>(627,071)</u>	<u>-</u>	<u>82,731</u>	<u>(709,452)</u>
Accumulated depreciation	<u>(5,050,540)</u>	<u>-</u>	<u>(298,547)</u>	<u>490,555</u>	<u>(4,858,532)</u>
Capital assets, net	<u>\$ 827,886</u>	<u>\$ -</u>	<u>\$ 2,549,077</u>	<u>\$ (47,131)</u>	<u>\$ 3,329,832</u>

Included in data processing software, data processing equipment and tenant improvements are \$0 and \$43,600 in assets reported as capital leases at June 30, 2016 and 2015, respectively. For fiscal year 2015, there was \$14,063 in related amortization on these assets. Upon the purchase of the Lottery's corporate offices and warehouse, the remaining capital lease obligation of \$60,724 for tenant improvements was retired as part of the purchase transaction.

Land and works of art are non-depreciable assets.

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE C - TRANSFERS TO LOTTERY TUITION FUND/THIRTY PERCENT RETURN**

	Due to Lottery Tuition Fund
	<hr/>
Balance at June 30, 2014	\$ 3,056,450
Prior year 30% return	41,121,221
Prior year transfers	<hr/> (41,124,750)
Balance at June 30, 2015	\$ 3,052,921
Current year 30% return	46,324,157
Current year transfers	<hr/> (45,936,991)
Balance at June 30, 2016	<hr/> <u>\$ 3,440,087</u>

In accordance with the Lottery Act, no later than the last business day of each month, the Lottery shall transmit at least thirty percent of the gross revenue of the previous month, to the New Mexico State Treasurer, who shall deposit it into state agency number 950, New Mexico Higher Education Department, the Lottery Tuition Fund, SHARE fund number 63700. As of July 31, 2016 and 2015, the Lottery has transferred \$46,324,157 and \$41,121,221, respectively, for the years ended June 30, 2016 and 2015 to the New Mexico State Treasurer.

**NOTE D - RETIREMENT PLANS**

Plan Descriptions and Funding

*Money Purchase Pension Plan*

All of the Lottery's eligible employees participate in a plan provided by the Lottery pursuant to the New Mexico Lottery Act (Chapter 6, Article 24 NMSA 1978). The Lottery is the administrator of the Plan, which is a defined contribution money purchase pension plan. Benefit terms, including contribution requirements are established and may be amended by the Lottery's Board of Directors. The plan provides for retirement benefits to plan members and their beneficiaries. The benefit that a plan member will receive when eligible will depend on the contributions to the member's individual account, actual earnings or losses on investments of those contributions, and any fees that are assessed to the member's account. Fifty-six and sixty-nine current and former employees of the Lottery were participants in the plan at the end of fiscal years 2016 and 2015, respectively.

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE D - RETIREMENT PLANS - CONTINUED**

Plan Descriptions and Funding- Continued

*Money Purchase Pension Plan - Continued*

Wells Fargo Bank was the trustee for the plan until August 15, 2014. At a Lottery Board of Directors' meeting on May 6, 2014, the Board by an adopted resolution removed Wells Fargo Bank as the trustee of the retirement plan and appointed Verisight Trust Company (c/o Verisight, Inc.) as the new trustee for the retirement plan (the "New Mexico Lottery Authority Retirement Plan") to be effective as of the date the money purchase pension plan retirement assets were transferred to or deposited at Verisight Trust Company. The retirement assets were liquidated by Wells Fargo Bank as of August 15, 2014 and transferred to Verisight Trust Company. With the appointment of Verisight Trust Company, the Lottery Board also elected to allow new employees to enter the retirement plan on their date of hire. Previously, employees became eligible to participate in the money purchase pension plan when they had completed six months of services. At that time, contributions started on the first day of the quarter coinciding with or next following the date in which the employee satisfied the eligibility requirement. The money purchase pension plan allows employees to self-direct their investments into any of the forty-one investment funds. Previously as trustee for the money purchase pension plan, Wells Fargo Bank had provided twenty-eight investment funds for employees to self-direct their funds.

The Lottery contributes 13.25% of compensation for each eligible employee to individual employee accounts for the money purchase pension plan. Employees are immediately 100% vested in the contributions and any earnings on those contributions. For the years ended June 30, 2016 and 2015, the Lottery recognized \$263,884 and \$342,629 of pension expense for the plan on eligible compensation of \$1,991,581 and \$2,585,879, respectively. There were no forfeitures of employee balances for the years ended June 30, 2016 and 2015, respectively. The entire pension amounts applicable to all compensation paid during the respective fiscal years have been paid to the plan by June 30, 2016 and 2015, respectively. For the years ended June 30, 2016 and 2015, the Lottery recognized a contribution liability of \$10,820 and \$9,611, respectively, for contributions owed on compensation earned, but not paid, for the last few days of each fiscal year.

*457(b) Plan*

At the May 6, 2014 Board of Directors' meeting, the Board adopted a Section 457(b) Plan, (the "New Mexico Lottery Authority 457(b) Plan") that allows both pre-tax and Roth (after tax) contributions by employees for their retirement up to applicable annual Internal Revenue Code limits. The 457(b) plan became effective with the payroll ended on August 2, 2014. Verisight Trust Company was also appointed the trustee for the 457(b) plan. This new plan, like the money purchase pension plan, allows employees to self-direct their investments into any of the forty-one investment funds. Thirty-four and thirty-nine current and former



New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE D - RETIREMENT PLANS- CONTINUED**

Fair Value Measurement of Retirement Plan Investments

*457(b) Plan - Continued*

employees were participants in the plan at the end of fiscal years 2016 and 2015. All amounts withheld from employee compensation for Section 457(b) contributions have been paid to the plan by June 30, 2016 and 2015, respectively.

In February 2015, GASB issued Statement No. 72, Fair Value Measurement and Application. This Statement establishes new requirements on how fair value should be measured, which assets and liabilities should be measured at fair value, and what information about fair value should be disclosed in the notes to the financial statements. The Lottery has implemented the standard for the fiscal year ending June 30, 2016.

The Lottery categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the investment. Level 1 investments reflect prices quoted in active markets; Level 2 investments reflect prices that are based on a similar observable asset either directly or indirectly; and Level 3 investments reflect prices based upon significant unobservable sources.

The Lottery has the following fair value measurements as of June 30, 2016 and 2015:

*Mutual funds* – Valued at the daily closing price as reported by the fund. These funds are required to publish their daily net asset value and to transact at that price. The mutual funds held by the Lottery are deemed to be actively traded and are registered with the Securities and Exchange Commission.

The Lottery had investments in various mutual funds that were comprised of bonds at June 30, 2016 and 2015, in the amount of \$713,679 and \$812,058, respectively with varying investment quality ratings and maturities. The average maturities averaged between 6-10 years with an average rating of primarily A on the underlying investments.

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE D - RETIREMENT PLANS - CONTINUED**

The plan has the following fair value measurements as of June 30:

	2016		2015	
	Money Purchase Pension Plan	457(b) Retirement Plan	Money Purchase Pension Plan	457(b) Retirement Plan
Total investments in the fair value measurement:				
Level 1 - Quoted prices in active markets				
<u>Mutual funds:</u>				
US Equity				
Value	\$ 864,850	\$ 102,452	\$ 939,318	\$ 15,594
Blend	271,782	30,486	264,834	5,093
Growth	530,815	2,137	544,505	11,728
Total US Equity	1,667,447	135,075	1,748,657	32,415
Bonds	200,397	704	200,806	798
Target Date	1,118,589	94,860	1,434,613	53,066
Balanced Asset Allocation	837,228	8,486	832,749	4,182
Foreign Equity	327,000	2,985	358,616	1,766
Specialty/Other	228,930	10,446	231,077	9,512
Total Level 1	4,379,591	252,556	4,806,518	101,739
Level 2 - Similar observable assets	-	-	-	-
Level 3 - Significant unobservable sources	-	-	-	-
Total investments in the fair value measurement	4,379,591	252,556	4,806,518	101,739
Total investments exempt from the fair value measurement:				
Money market/cash	319,959	-	378,231	1,610
Contribution receivable	10,820	-	9,611	-
Total Investments	\$ 4,710,370	\$ 252,556	\$ 5,194,360	\$ 103,349

The balances and activity of the Plan as of and for the years ended June 30, 2016 and 2015 are presented in the Statements of Fiduciary Net Position and Statements of Changes in Fiduciary Net Position. There are no separately issued financial statements available for the New Mexico Lottery Authority Retirement Plans.

**NOTE E - CREDIT AGREEMENT**

In July 2012, the Lottery entered into an agreement with Wells Fargo Bank effective May 15, 2012 for an automatic unsecured overdraft line of credit sweep in the amount of \$4,000,000 with a variable interest rate, which was 3.50% and 3.25% as of June 30, 2016 and 2015, respectively. This line matured on May 14, 2016, 2015, 2014, and 2013 and was renewed for another year under the same terms and conditions each year.

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE E - CREDIT AGREEMENT - CONTINUED**

For the years ended June 30, 2016 and 2015, the Lottery had no outstanding borrowings against the line-of-credit.

**NOTE F - LEASES**

In June 2012, the Lottery executed a new lease for its corporate office and warehouse space. The new lease commenced on July 1, 2012 and cancelled the remaining nine months of the 2002 lease extension. The new lease was for ten years and nine months, ending on March 31, 2023. The Lottery had the option to extend the new lease for five additional years until March 31, 2028.

As part of the 2002 lease extension with NMLB, LLC, the Lottery had received \$50,000 in 2012 to be used for improvements to the facility. In addition, as part of the 2012 lease, the Lottery had received \$1,858 in fiscal year 2012 and \$29,975 in fiscal year 2013 for improvements to the facility. The Lottery had recorded the \$81,833 as tenant improvements with a related deferred liability to be amortized over the life of the lease using the straight-line method.

On June 26, 2015, the Lottery purchased the building housing its corporate offices and warehouse from NMLB, LLC. With this purchase transaction, the June 2012 lease was terminated and the remaining capital lease obligation of \$60,724 was retired as part of the purchase transaction.

Rent expense on the building was \$284,132 for the year ended June 30, 2015.

Following is a schedule of the composition of net rental expense for all long-term operating leases for the years ended June 30:

	<u>2016</u>	<u>2015</u>
Minimum rentals	\$ -	\$ 276,965
Less: Subleases	-	-
	<u>\$ -</u>	<u>\$ 276,965</u>

New Mexico Lottery Authority

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2016 and 2015

**NOTE F - LEASES - CONTINUED**

As part of the agreement with INTRALOT, Inc., to provide an updated on-line gaming system, the Lottery installed and implemented a new internal control system (ICS) in fiscal year 2009. The cost for the ICS is included in the fixed fee paid to the vendor as a percentage of net sales. The Lottery has accounted for this transaction as a capital lease. The ICS cost was projected over the initial term of the contract of seven years and has been capitalized on the books of the Lottery at the present value of this cost, as determined with a discount rate of 4%. The initial term of the contract ended on November 20, 2015, at which time the cost had been amortized to zero.

**NOTE G - COMMITMENT**

Effective on November 15, 2007, the Lottery entered into an agreement with INTRALOT, Inc., a Georgia-based company, to provide an updated on-line gaming system for a total of seven years. The system includes the supply, installation, maintenance, service, and operation of a communication network, lottery terminals and peripheral equipment for the Lottery's existing and future retailers, ticket scanners to enable players to check their tickets for prizes, self-service ticket vending machines that sell both instant and draw game tickets, disaster recovery services, and various employees to operate the system and provide sales and marketing support to the Lottery. The transition to this new on-line gaming system took place on November 16, 2008.

Effective November 22, 2015, the Lottery entered into an agreement with INTRALOT, Inc. to provide an updated on-line gaming system for a total of eight years. The system shall include the provisions of the 2007 on-line system along with a new back office accounting system and new lottery terminals for the Lottery's retailers. Intralot shall also employ and manage a fifteen member lottery sales team.

**NOTE H - OTHER EXPENSES**

Other expenses at June 30 consisted of:

	2016	2015
Registrations and memberships	\$ 23,863	\$ 23,165
Other	17,301	19,274
Training	11,102	7,223
Publications and subscriptions	2,612	2,619
	\$ 54,878	\$ 52,281

New Mexico Lottery Authority

**SUPPLEMENTARY INFORMATION  
BUDGETARY COMPARISON STATEMENTS**

Years ended June 30,

2016

2015

	2016				2015			
	Original Budget	Final Budget	Actual	Variance with Final Budget	Original Budget	Final Budget	Actual	Variance with Final Budget
Operating revenues								
Instant ticket sales	\$ 81,227,000	\$ 82,376,000	\$ 83,105,873	\$ 729,873	\$ 71,893,000	\$ 77,664,500	\$ 79,956,236	\$ 2,291,736
Powerball sales	29,877,000	41,999,700	43,321,879	1,322,179	37,859,200	29,939,000	27,722,571	(2,216,429)
Mega Millions sales	11,999,000	9,599,800	10,509,262	909,462	8,994,900	11,999,500	11,161,262	(838,238)
Roadrunner Cash sales	6,499,000	7,199,900	7,394,565	194,665	6,992,800	6,499,000	6,240,297	(258,703)
Pick 3 sales	4,799,500	4,799,900	4,891,153	91,253	4,195,700	4,599,500	4,621,530	22,030
Hot Lotto sales	5,999,500	4,299,900	4,283,277	(16,623)	4,988,800	5,999,500	5,997,386	(2,114)
Quickster sales	799,500	749,900	691,531	(58,369)	1,498,500	774,500	742,509	(31,991)
Lucky Numbers Bingo sales	249,500	174,900	147,228	(27,672)	3,396,300	149,500	153,912	4,412
Monopoly Millionaires' Club sales	-	-	-	-	2,992,800	421,000	421,020	20
Net ticket sales	141,450,000	151,200,000	154,344,768	3,144,768	142,812,000	138,046,000	137,016,723	(1,029,277)
Retailer fees	12,000	12,000	14,720	2,720	12,000	15,000	19,980	4,980
Bad debts	(24,000)	(24,000)	(21,000)	3,000	(24,000)	(24,000)	-	24,000
Total operating revenues	141,438,000	151,188,000	154,338,488	3,150,488	142,800,000	138,037,000	137,036,703	(1,000,297)
Total game expenses	93,775,000	101,759,000	103,144,916	(1,385,916)	94,130,000	91,244,000	90,884,538	359,462
Total operating expenses	5,207,000	4,044,000	3,652,625	391,375	5,846,000	5,399,000	5,057,597	341,403
Operating income	42,456,000	45,385,000	47,540,947	2,155,947	42,824,000	41,394,000	41,094,568	(299,432)
Total non-operating income (expense)	(17,000)	(22,000)	24,210	46,210	24,000	24,000	26,653	2,653
Net income before transfers to Lottery Tuition Fund	\$ 42,439,000	\$ 45,363,000	\$ 47,565,157	\$ 2,202,157	\$ 42,848,000	\$ 41,418,000	\$ 41,121,221	\$ (296,779)

New Mexico Lottery Authority

**SUPPLEMENTARY INFORMATION**  
**SCHEDULES OF PERCENTAGE RETURN TO THE STATE OF NEW MEXICO**  
 Years ended June 30,

	2016	2015
<b>OPERATING REVENUES</b>		
Instant ticket sales	\$ 83,105,873	\$ 79,956,236
Powerball sales	43,321,879	27,722,571
Mega Millions sales	10,509,262	11,161,262
Roadrunner Cash sales	7,394,565	6,240,297
Pick 3 sales	4,891,153	4,621,530
Hot Lotto sales	4,283,277	5,997,386
Quickster sales	691,531	742,509
Lucky Numbers Bingo sales	147,228	153,912
Monopoly Millionaires' Club sales	-	421,020
Net ticket sales	<u>154,344,768</u>	<u>137,016,723</u>
Retailer fees	14,720	19,980
Bad debts	(21,000)	-
Total operating revenues	<u>154,338,488</u>	<u>137,036,703</u>
<b>NON-OPERATING INCOME</b>		
Other income	47,173	10,516
Interest income	17,141	16,373
Total non-operating income	<u>64,314</u>	<u>26,889</u>
<b>GROSS REVENUES</b>	<u>154,402,802</u>	<u>137,063,592</u>
<b>GAME EXPENSES</b>		
Prize expense	84,754,383	75,592,325
Retailer commissions	10,035,060	8,941,265
On-line vendor fees	4,284,035	2,193,183
Advertising	2,053,906	2,174,697
Ticket vendor fees	1,314,494	1,265,885
Shipping and postage	276,853	312,134
Retailer equipment	182,538	96,816
Promotions	116,770	134,190
Responsible gaming	69,999	69,998
Game membership	56,878	66,895
Drawing game	-	37,150
Total game expenses	<u>103,144,916</u>	<u>90,884,538</u>
<b>OPERATING EXPENSES</b>		
Salaries, wages, and benefits	2,609,094	3,485,280
Utilities and maintenance	313,846	410,518
Professional fees	229,908	232,028
Depreciation and amortization	225,958	298,547
Leases, property taxes, and insurance	145,591	435,550
Other	54,878	52,281
Materials and supplies	48,743	77,233
Travel	24,607	66,160
Operational Reserve Fund expense	1,241,000	-
Total operating expenses	<u>4,893,625</u>	<u>5,057,597</u>
<b>OPERATING INCOME</b>	<u>46,299,947</u>	<u>41,094,568</u>
<b>NON-OPERATING EXPENSE</b>		
Interest expense	40,104	236
Total nonoperating expense	<u>40,104</u>	<u>236</u>
<b>NET INCOME</b>	<u>\$ 46,324,157</u>	<u>\$ 41,121,221</u>
<b>GROSS REVENUE PERCENTAGE RETURN</b>	<u>30.00%</u>	<u>30.00%</u>

**INDEPENDENT AUDITORS' 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**

Board of Directors  
New Mexico Lottery Authority and  
Mr. Tim Keller  
New Mexico State Auditor  
Albuquerque, New Mexico

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the business-type activities and the aggregate remaining fund information of the New Mexico Lottery Authority (Lottery), as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise Lottery's basic financial statements, and the budgetary comparison statement of the Lottery, presented as supplementary information and have issued our report thereon dated October 4, 2016.

**Internal Control Over Financial Reporting**

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

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

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

Board of Directors  
New Mexico Lottery Authority and  
Mr. Tim Keller  
New Mexico State Auditor

### **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, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and responses as items 2016-001 and 2016-002.

### **The Lottery's Responses to Findings**

The Lottery's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. The Lottery's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

### **Purpose of this Report**

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



**CliftonLarsonAllen LLP**

Albuquerque, New Mexico  
October 4, 2016



## SCHEDULE OF FINDINGS AND RESPONSES

Year Ended June 30, 2016

### 2016-001 Network Access (Compliance and Other Matters)

**Condition:** During our review and testing of user account request process, the Lottery was unable to provide evidence for three out of three BOS user account requests as documentation is not maintained indicating approval of access.

**Criteria:** The Lottery should have effective controls and procedures in place to ensure documents are maintained for user account requests evidencing proper review and approval of access.

**Cause:** Lack of effective controls and procedures surrounding the documentation of user account requests.

**Effect:** Without appropriate documentation of user access request and approval of the request, unauthorized access may be granted to authorized or unauthorized users of BOS.

**Auditors' Recommendation:** We recommend management maintain documentation for any BOS access granted or changed.

**Management's Response:** The IT department is currently configuring a help desk solution and associated procedures that will allow us to assign tasks during the user creation process. The Director of HR will submit a request for new user creation, tasks will be assigned and notifications sent to the appropriate personnel. When the task has been completed and associated responses are received, the request will be updated. Once all related tasks are completed the request will be closed. Reports can be run to document the process.

The Executive Vice President for Security is responsible for ensuring that this new solution and associated procedures are implemented by the end of the second quarter of fiscal year 2017 and are functioning as designed.

### 2016-002 Disaster Recovery and Business Continuity Plans (Compliance and Other Matters)

**Condition:** The Lottery developed a disaster recovery plan. However, since the creation of the plan, there have been changes to the IT environment, vendors, and personnel that make the plan outdated. Also, the Lottery has not tested the disaster recovery plan at least annually.

**Criteria:** In accordance with ISACA's Control Objectives for Information and related Technology (COBIT) 4.1 framework (DS4), to ensure continuous service, a Disaster Recovery

**SCHEDULE OF FINDINGS AND RESPONSES – CONTINUED**

Year Ended June 30, 2016

**2016-002 Disaster Recovery and Business Continuity Plans (Compliance and Other Matters) (Continued)**

**Criteria (Continued):** and Business Continuity Plans need to be developed and tested to reduce impact of a major disruption on key business functions and processes. The plans should be based on risk understanding of potential business impacts and address requirements for resilience, alternative processing and recovery capability of all critical IT services. They should also cover usage guidelines, roles and responsibilities, procedures, communication processes, and the testing approach.

**Cause:** Lack of effective controls and procedures surrounding the updating of the disaster recovery plan for changes to the information and testing of the plan.

**Effect:** With the changes, some personnel may not know how to execute the plan in the event of a disaster. Without testing the disaster recovery plan, management is unable to assess whether the plan has any design flaws and whether it is still appropriate. Also, without testing the disaster recovery plan, management may not act as quickly or decisively in implementing the plan at the time of a disaster.

**Auditors' Recommendation:** We recommend management perform a review of the disaster recovery plan and update the plan for changes. We also recommend management test the disaster recovery plan annually to assess the plan for any design flaws and whether it is still appropriate and to ensure quick and decisive reactions in the event of a disaster.

**Management's Response:** The organization will continue to implement a fully functional disaster recovery plan and test the plan on an annual basis. The oversight of this function will be assigned to one specific staff member. During the last fiscal year, the organization migrated to a new vendor provided back office system to provide for more long term stability and functionality. The changeover process is virtually complete and now provides the opportunity to review and update and test all related procedural policies. As part of the back office migration, the organization now has two complete systems, a primary and a secondary system being physically located in two different states that mirrors all gaming transactions.

The Deputy Director of Administration will serve as the lead for the team that will provide the disaster recovery testing for all back office and financial systems. The goal is to complete the testing by the end of the third quarter of fiscal year 2017, but no later than the end of the fourth quarter of fiscal year 2017.

New Mexico Lottery Authority

**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS**

Year Ended June 30, 2016

There were no findings for the year ended June 30, 2015.

New Mexico Lottery Authority

**SCHEDULE OF VENDOR INFORMATION  
for Purchases Exceeding \$60,000 (excluding GRT)**

For the Year Ended June 30, 2016

Prepared by Agency Staff Name: Sylvia A. Jaramillo Title: Director of Administration Date: August 29, 2016

RFB#/ RFP#	Type of Procurement	Awarded Vendor	\$ Amount of Awarded Contract	\$ Amount of Amended Contract	Name and Physical Address per the Procurement Documentation, of <u>ALL</u> Vendor(s) that responded	In-State/Out-of-State Vendor (Y or N) (Based on Statutory Definition)	Was the Vendor In-State and Chose Veteran's Preference (Y or N) For Federal Funds Answer N/A	Brief Description of the Scope of Work
None	Lottery Gaming System and Associated Products and Services	Intralot, Inc.	Estimated \$5 Million Per Year over 8 Years	N/A	Intralot, Inc. 11360 Technology Circle Duluth, Georgia 30097	N	N/A	The vendor provides an on-line gaming system to the Lottery that includes the supply, installation, maintenance, service and operation of a communication network, a new back office accounting system, new lottery terminals and peripheral equipment for the Lottery's existing and future retailers, ticket scanners to enable players to check their tickets for prizes, self-service ticket vending machines that sell both instant and draw game tickets, disaster recovery services, and various employees to operate the system and provide sales and marketing support to the Lottery.

New Mexico Lottery Authority

**EXIT CONFERENCE**

For the Year Ended June 30, 2016

An exit conference was held at the New Mexico Lottery Authority on October 19, 2016. The following individuals participated:

<u>Name</u>	<u>Title</u>
<i><b>New Mexico Lottery Authority Finance/Audit Committee</b></i>	
<b>Dr. Dan Salzwedel</b>	<b>Board Chair</b>
<b>Mark Koson</b>	<b>Board Vice-Chair and Finance/Audit Committee Chairman</b>
<b>John Kubiak, CPA</b>	<b>Board Secretary/Treasurer</b>
<i><b>New Mexico Lottery Authority Employees</b></i>	
<b>David M. Barden, Esq.</b>	<b>Chief Executive Officer</b>
<b>Sylvia Ann Jaramillo, CPA</b>	<b>Chief of Staff/Director of Administration</b>
<b>Michael Boland, CPA</b>	<b>Internal Auditor</b>
<i><b>CliftonLarsonAllen LLP</b></i>	
<b>Matt Bone, CPA, CGFM, CGMA</b>	<b>Principal</b>
<b>Jane Tinker, CPA</b>	<b>Senior Associate</b>
<b>Elizabeth Nunez, CPA</b>	<b>Associate</b>

**Financial Statement Preparation**

The New Mexico Lottery Authority's financial statements, notes, and management's discussion and analysis have been prepared by the New Mexico Lottery Authority's accountants.