

FISCAL YEAR

2016

ANNUAL REPORT



**SOUTH DAKOTA
LOTTERY™**

A DIVISION OF THE SOUTH DAKOTA
DEPARTMENT OF REVENUE

LOTTERY STAFF ORGANIZATIONAL CHART

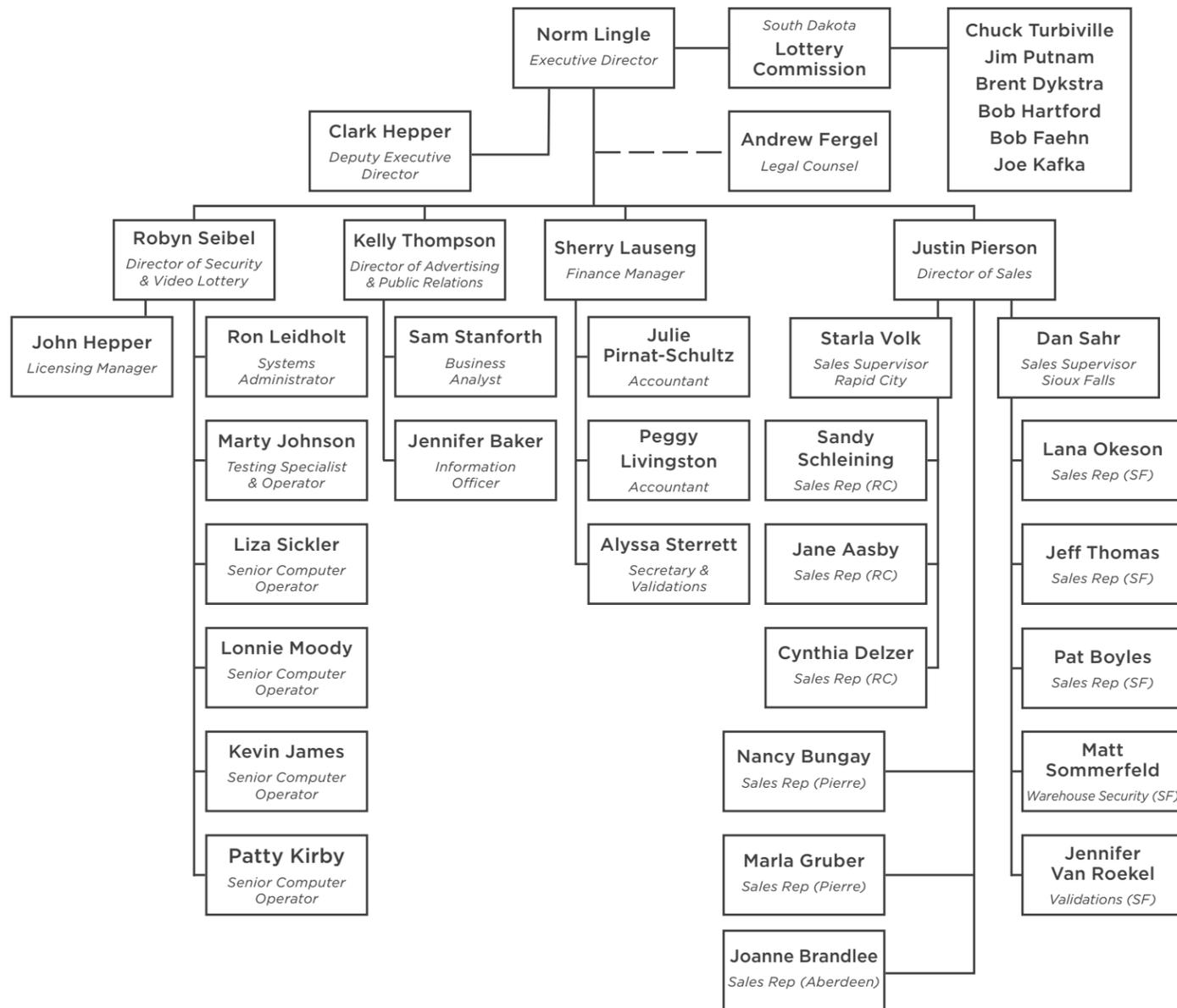


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VALIDATION CENTERS & MAILING ADDRESS

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South Dakota Lottery, 711 E. Wells Ave., Pierre, SD 57501 | lottery.sd.gov

MISSION STATEMENT

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

FROM THE DIRECTOR

To the Governor, Legislature and People of South Dakota:

Fiscal year 2016 was a busy one for the South Dakota Lottery staff and Commission and I'm pleased to share our accomplishments with you in our Annual Report. As a division of the Department of Revenue, we worked hard to bring changes and improvements to our lotto, scratch, and video lottery programs to ensure that the Lottery remains a viable and sustainable source of revenue for the State of South Dakota.

Thanks to our loyal players and retail partners, the South Dakota Lottery provided \$117.7 million to funds that improve the quality of life in South Dakota. \$7.7 million was added to the Capital Construction Fund which is used to pay for rural water systems, community drinking water and wastewater improvement projects, and recycling and waste disposal programs. We also provided \$109.8 million to the General Fund which funds local K-12 schools and state universities and technical institutes. In total, we have distributed an impressive \$2.58 billion to our beneficiaries since our start in 1987.

The Lottery is committed to promoting responsible play of all our products. In fiscal year 2016, we were pleased to participate once again in National Problem Gambling Month during March and in the National Council on Problem Gambling's holiday campaign against providing lottery tickets as gifts to minors. We're also a member in good standing of the South Dakota Council on Responsible Gambling.

I invite you to take some time to read more about our highlights and improvements from Fiscal Year 2016; I also encourage you to stay up-to-date on the South Dakota Lottery through our website (lottery.sd.gov) and social media platforms (Facebook, Twitter and YouTube).

We look forward to continuing our service to the State of South Dakota and its residents in fiscal year 2017.

Sincerely,



Norm Lingle
Executive Director
South Dakota Lottery



“Thanks to our loyal players and retail partners, the South Dakota Lottery provided \$117.7 million to funds that improve the quality of life in South Dakota.”

NORM LINGLE

SALES & REVENUES

Total fiscal year 2016 Lottery revenue generated for state funds was more than \$117 million. These revenues come from three main sources, as evidenced in the chart below.

	Sales	Prizes	Commission	Revenue Distributed
Instant Tickets	\$26,299,493	\$17,132,245	\$1,479,346	\$5,517,739
Lotto Tickets	\$28,992,932	\$14,584,767	\$1,515,613	\$9,137,710
Video Lottery*	\$678,898,195	\$471,295,651	\$103,801,272	\$102,997,813
			Total	\$117,653,262

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

REVENUE APPROPRIATIONS

Revenue from each of the three types of lottery products is designated for specific purposes.

	General Fund	Capital Construction Fund	Department of Social Services*
Instant Tickets	\$5,517,739		
Lotto Tickets	\$1,400,000	\$7,737,710	
Video Lottery	\$102,763,259		\$159,554
Video Lottery License Fees	\$75,000		
Totals	\$109,755,998	\$7,737,710	\$159,554



All monies from the sale of scratch tickets are transferred to the state General Fund, nearly half of which supports local K-12 schools, state universities and technical institutes.

The first \$1.4 million in revenue from lotto tickets is put into the General Fund. Anything beyond that amount is transferred to the Capital Construction Fund which filters money to the following areas:

- **Water and Environment Fund** - used for a variety of projects from drinking water and wastewater improvement to recycling to natural resource development.
- **Ethanol Fuel Fund** - provides annual production payments to qualified South Dakota ethanol producers.

- **State Highway Fund** - used for state highways and bridges.

Revenue generated from video lottery terminals, or Net Machine Income (NMI), is calculated by taking the cash put into the machines minus the prizes paid out. The NMI for each machine is split between the State of South Dakota and the licensed operator who owns the machine, each earning half of the total. Of the state's share, 49.5% is transferred to the General Fund which supports public and higher education, programs like Medicaid and Temporary Assistance to Needy Families, human services facilities, and the corrections and court systems. A small amount (0.5% of NMI) is kept by the Lottery for operation costs.

The South Dakota Lottery prides itself on using every dollar earned as an investment in the future of South Dakota.

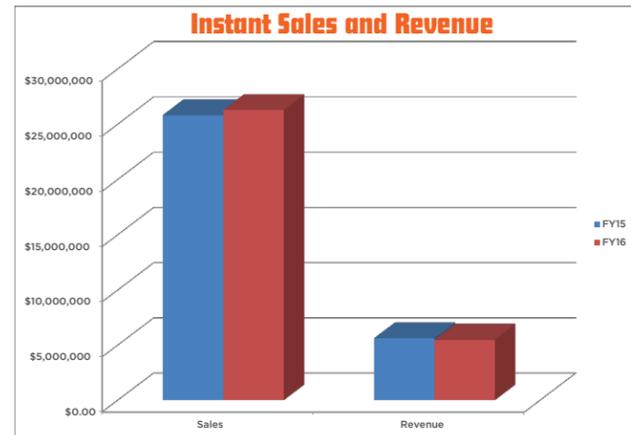
*The Lottery annually provides the S.D. Department of Social Services with funding for problem gambling services. Funding comes from the Lottery's 0.5% of net machine income for administration.

FISCAL YEAR 2016 HIGHLIGHTS

The South Dakota Lottery markets instant tickets and lotto games, and regulates, maintains and markets video lottery to raise revenue for state programs and projects. Since its inception in 1987, the Lottery has distributed over \$2.58 billion in revenue.

INSTANT TICKETS

The Lottery launched 25 new instant ticket games during fiscal year 2016. Prices for instant tickets ranged from \$1 to \$20, and prizes ranged from \$1 to \$500,000 as well as merchandise prizes.

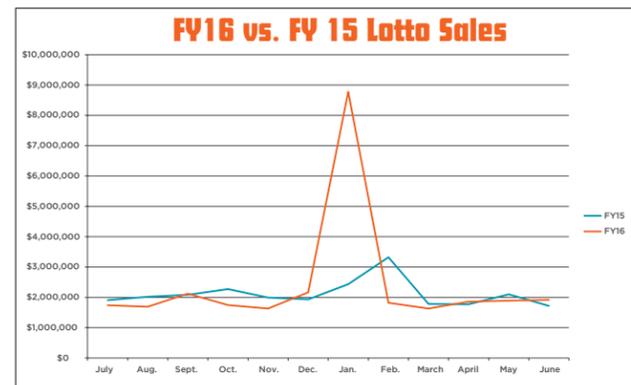


At the close of fiscal year 2016, there were 623 licensed instant ticket retailers across the state. Retailers receive a 5% commission for selling tickets, a 1% commission for cashing winning tickets with prizes up to \$100, and a 1% commission for selling tickets with prizes of more than \$100.

Fiscal year 2016 instant ticket sales were up 1.8% from the previous year but revenues were down 2.3%. Revenue from the sale of instant tickets is distributed to the General Fund.

LOTTO TICKETS

South Dakota currently offers four lotto games. Powerball, Mega Millions, and Hot Lotto are multi-state games. Dakota Cash with EZ Match is played only in South Dakota.

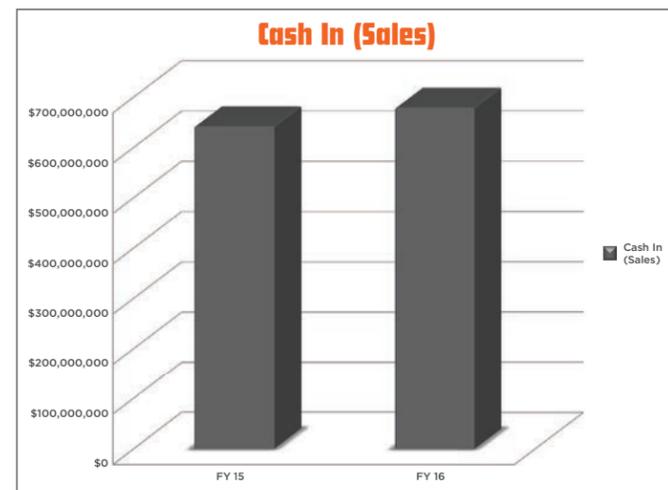


At the end of fiscal year 2016, there were 610 licensed lotto retailers. Lotto retailers receive a 5% commission for selling tickets, plus varying bonuses for selling larger winning tickets.

Lotto games reported an overall sales increase of 14.4%; transfers were up 20.6% from fiscal year 2015. The first \$1.4 million of revenue from the sale of lotto tickets is distributed to the General Fund, and the balance is distributed to the Capital Construction Fund.

VIDEO LOTTERY

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



Video lottery sales (cash in) increased by 5.8% in fiscal year 2016. The average number of active video lottery machines during fiscal year 2016 was 9,002 and the average number of licensed establishments was 1,331. The revenue from video lottery is calculated on net machine income, which is cash-in (sales) minus cash-out (prizes). Net machine income is divided between the state and machine operators on a 50/50 split. One-half of one percent (0.5%) of the state's share is retained by the Lottery for administration.

Revenue from video lottery net machine income during fiscal year 2016 was distributed to the General Fund.

The Lottery's website, lottery.sd.gov, offers winning numbers, prize claim forms, retailer forms, licensing and accounting information, recent winners' stories and other general information about the Lottery. The Lottery also maintains a Facebook page (facebook.com/sdlottery), a Twitter feed (@sdlottery), and its own YouTube channel.

FISCAL YEAR 2016 HIGHLIGHTS

FY2016 JACKPOT WINNERS

SEPTEMBER 2, 2015

Josh Johnson, Sioux Falls, won the **\$178,607 Dakota Cash jackpot**



NOVEMBER 11, 2015

David DeJong, Sioux Falls, won the **\$270,000 Wild Card 2 jackpot**



NOVEMBER 23, 2015

Everett Felix Sr., Sisseton, won the **\$215,000 Wild Card 2 jackpot**

DECEMBER 9, 2015

Susan Nickle, Deadwood, won the **\$6.7 million Hot Lotto jackpot**

DECEMBER 12, 2015

Roger Van Twisk, Sioux Falls, won the **\$149,512 Dakota Cash jackpot**



APRIL 6, 2016

Kathy King, Lesterville, won the **\$223,707 Dakota Cash jackpot**

MAY 4, 2016

Travis Carrico, Watertown, won the **\$35,658 Dakota Cash jackpot**

MAY 25, 2016

James Hamler, Canton, won the **\$25,146 Dakota Cash jackpot**

GOODBYE WILD CARD 2

The Wild Card 2 lotto game held its final drawing on Feb. 24, 2016. The only game in South Dakota to offer two plays for \$1 got its start in 1994 as Tri-West Lotto and was offered only in Idaho, Montana and South Dakota. In 1998, it was changed to Wild Card and was finally revised to Wild Card 2 a year later. When the game ended after 22 years, it was played in Idaho, Montana, North Dakota and South Dakota and had produced 21 jackpot winners in South Dakota.

\$1.6 BILLION POWERBALL JACKPOT



The Powerball run that ended on Jan. 13, 2016, with a final jackpot of \$1.6 billion set the record for the largest lottery prize ever offered in the world that could be won with a single ticket. Sales for the Jan. 13 draw were \$3.45 million and sales for that day were \$1.79 million. Sales for the entire run, which began Nov. 5 and took 20 draws and 11 weeks, were \$5.85 million. Revenue was \$1.46 million for the run that broke South Dakota Powerball records in sales for the final draw, sales for the day (Jan. 13), and sales for the run.

SOUTH DAKOTA POWERBALL RECORDS SET

\$5.85 million
SALES FOR THE ENTIRE JACKPOT RUN

\$3.45 million
SALES FOR THE JAN. 13, 2016 DRAW

\$1.79 million
SALES THE DAY OF JAN. 13, 2016 DRAW

FISCAL YEAR 2016 HIGHLIGHTS

MARKET RESEARCH RESULTS

In FY2016, the South Dakota Lottery realized that to find better ways to reach its players, current and potential, it first needed to learn more about them. So the Lottery, in collaboration with its advertising agency, Lawrence & Schiller (L&S), conducted a research study in the fall of 2015 to learn more about the variety and frequency of play, and understand people's current perceptions of the Lottery.

The study found that some of the challenges facing Lottery included competition from tribal casinos, Deadwood casinos, and sports betting, as well as the operational costs of video lottery. And while the majority of South Dakota residents were familiar with the games and had played them in the past, many of those who did play did so infrequently. This provided an opportunity to increase the number of times residents played each game, if given an incentive or reason to do so.

A Behavior and Motivations Survey found most participants had a neutral opinion of the Lottery and positive impressions of both scratch tickets and lotto games. First impressions of scratch tickets were 40% positive, with an image of them being fun and social, offering variety, and making good gifts. Lotto games left

SUMMARY OF FIRST IMPRESSIONS

	POSITIVE	NEUTRAL	NEGATIVE
NATIVE AMERICAN CASINOS	+ 46%	= 25%	- 29%
DEADWOOD CASINOS	+ 40%	= 44%	- 16%
SPORTS BETTING	+ 20%	= 49%	- 31%
SCRATCH TICKETS	+ 40%	= 27%	- 33%
LOTTO GAMES	+ 37%	= 32%	- 31%
VIDEO LOTTERY	+ 15%	= 31%	- 54%

37% of participants with a positive impression, noting big money, big odds, and jackpot buzz as their first impressions. Video Lottery didn't fare as well, with only 15% of impressions being positive. Despite its negative image, the potential exists to refocus attention on beneficiary awareness and how video lottery revenues support South Dakota.

To influence behavior moving forward, L&S recommended reinforcing that Lottery is fun, entertaining, social, responsible, full of big winners, and benefits the state.

NEW BRAND IMAGE, LOGO

In FY2016, the South Dakota Lottery's logo got a new look...and a new attitude.

On Feb. 16, 2016, the Lottery officially launched their "Good Fun" brand campaign aimed at improving the public's perception of the agency and its products. A study conducted by Lawrence & Schiller, the Lottery's advertising agency, showed many South Dakotans had a neutral, unfavorable or unfamiliar view of the Lottery.

The "Good Fun" slogan highlights that Lottery products are designed to be FUN and entertaining for players and that playing them is GOOD for the beneficiaries of Lottery revenues.

The updated logo, which replaced the 10-year-old sunset-South-Dakota-and "L" image, features a simpler, contemporary design in orange, black and white. The new logo and slogan was featured in TV and radio ads, billboards, social media and digital marketing, and was added to scratch and lotto tickets, video lottery machines, the Lottery's vehicles, and point of sale items.



**SOUTH DAKOTA
LOTTERY**



#GoodFunSD

FISCAL YEAR 2016 HIGHLIGHTS

SIoux FALLS OFFICE RELOCATION

After nearly 30 years in the same location, on March 18, 2016, the Sioux Falls lottery office moved to a new building at 3605 S. Western Avenue in the parking lot of the Western Mall. The new location is more convenient for both players and Lottery staff, with a bigger lobby area to accommodate players, a better office layout for staff, and more warehouse space with easier access for deliveries.



VIDEO LOTTERY SECURITY REQUEST FOR PROPOSAL (RFP)



Making video lottery casinos more secure for businesses and their players became a Lottery priority in FY2016. In December 2015, the Lottery Commission asked Lottery staff to look into a security assessment for video lottery establishments. The concept of the video lottery security request for proposal (RFP) was brought on by a rash of burglaries at casinos and the results of a Lawrence & Schiller (L&S) study that found 54% of respondents had a negative opinion of South Dakota's video lottery industry.

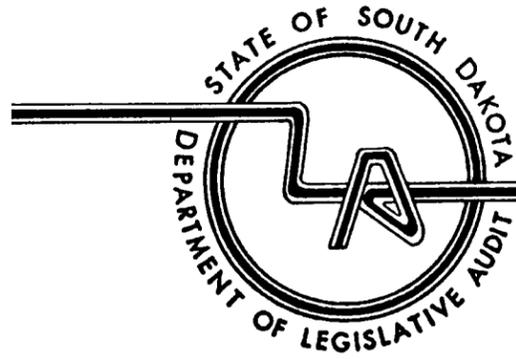
In early 2016, an RFP was written for a study to examine, evaluate, and assess areas of security vulnerability for video lottery establishments; look at the premises from the interior and exterior; and review security processes and procedures already in place at establishments, like employee training and interaction with local law enforcement. The RFP would also identify other security aspects where Lottery may be exposed to threats, such as how products are received, stored, and transferred by the Lottery and its partners. The security assessment RFP was scheduled to be awarded in FY2017.

PLAY IT AGAIN

The Lottery's second chance drawing program for players continued to make winners during FY2016. The Play It Again Lucky Leap grand prize drawing was held Feb. 29, 2016, and had 233,142 entries of non-winning \$2 and \$3 tickets. The \$30,000 winner was Penny Wallingford of Gillette, WY.

The Play It Again Summer Sizzle promotion launched March 1, 2016, and included monthly mini-drawings, in which five winners had their choice of \$100 in scratch tickets or \$100 gift card from a participating retailer. The \$30,000 grand prize drawing was set for Aug. 26, 2016.





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MARTIN L. GUINDON, CPA
AUDITOR GENERAL

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

The Honorable Dennis Daugaard
Governor of South Dakota

and

The South Dakota Lottery Commission
State of South Dakota

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the South Dakota Lottery Fund, an enterprise fund of the State of South Dakota, as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, which collectively comprise the South Dakota Lottery Fund's basic financial statements and have issued our report thereon dated October 25, 2016.

Internal Control Over Financial Reporting

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or 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. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

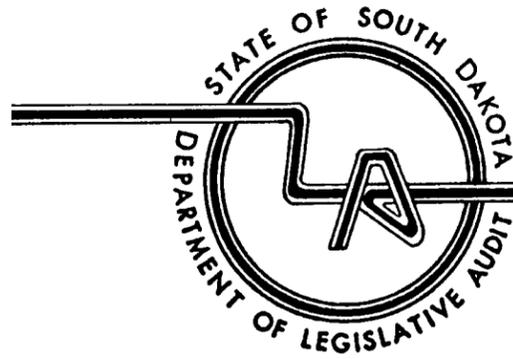
As part of obtaining reasonable assurance about whether South Dakota Lottery's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on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

Purpose of this Report

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

Martin L. Guindon, CPA
Auditor General

October 25, 2016



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MARTIN L. GUINDON, CPA
AUDITOR GENERAL

INDEPENDENT AUDITOR'S REPORT

The Honorable Dennis Daugaard
Governor of South Dakota

and

The South Dakota Lottery Commission
State of South Dakota

Report on the Financial Statements

We have audited the accompanying financial statements of the South Dakota Lottery Fund, an enterprise fund of the State of South Dakota, as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the South Dakota Lottery Fund, an enterprise fund of the State of South Dakota, as of June 30, 2016 and 2015, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the South Dakota Lottery Fund and do not purport to, and do not, present fairly the financial position of the State of South Dakota, as of June 30, 2016 and 2015, the changes in its financial position, or, where applicable, its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the South Dakota Lottery's basic financial statements. The *Message from the Director, Sales and Revenues, Revenue Appropriations, and Fiscal Year 2016 Highlights* sections are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The *Message from the Director, Sales and Revenues, Revenue Appropriations, and Fiscal Year 2016 Highlights* sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on them.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 25, 2016 on our consideration of the South Dakota Lottery's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering South Dakota Lottery's internal control over financial reporting and compliance.

Martin L. Guindon, CPA
Auditor General

October 25, 2016

FINANCIAL STATEMENTS

South Dakota Lottery
STATEMENT OF NET POSITION
June 30, 2016 and 2015

ASSETS	2016	2015
Current Assets:		
Cash	\$9,494,706	\$8,749,183
Restricted Cash	18,200	28,300
Total Cash	<u>9,512,906</u>	<u>8,777,483</u>
Accounts Receivable	4,580,059	4,847,771
Restricted Other Receivable	633,133	700,807
Interest Receivable	42,271	39,377
Restricted Certificates of Deposit	451,581	456,245
Prepaid Expenses	16,000	16,000
Total Current Assets	<u>15,235,950</u>	<u>14,837,683</u>
Noncurrent Assets:		
Capital Assets less Accumulated Depreciation/Amortization	837,179	1,060,681
Restricted Net Pension Asset	319,851	543,598
Total Noncurrent Assets	<u>1,157,030</u>	<u>1,604,279</u>
Total Assets	<u>16,392,980</u>	<u>16,441,962</u>
DEFERRED OUTFLOWS OF RESOURCES		
Deferred Outflows of Resources-Related to Pensions	600,067	483,438
Total Deferred Outflows of Resources	<u>600,067</u>	<u>483,438</u>
LIABILITIES		
Current Liabilities:		
Accounts Payable	395,568	277,067
Prizes Payable	1,513,895	1,599,555
Due to the Capital Construction Fund	1,137,710	577,367
Due to the General Fund	5,072,571	5,373,842
Due to Other Funds	116,718	91,667
Due to Other Governments	17,194	39,000
Operator Security Deposits	469,781	484,545
Escrows Payable-Reservation Sales	64,366	69,178
Accrued Liabilities	305,844	298,563
Unearned Revenue	263,702	271,528
Total Current Liabilities	<u>9,357,349</u>	<u>9,082,312</u>
Noncurrent Liabilities:		
Accrued Liabilities	164,302	160,454
Total Liabilities	<u>9,521,651</u>	<u>9,242,766</u>
DEFERRED INFLOWS OF RESOURCES		
Deferred Inflows of Resources-Related to Pensions	476,085	629,579
Total Deferred Inflows of Resources	<u>476,085</u>	<u>629,579</u>
NET POSITION		
Net Investment in Capital Assets	837,179	1,060,681
Restricted For:		
Pension Obligations	443,833	397,457
MUSL Permitted Uses	633,134	700,807
Unrestricted	5,081,165	4,894,110
Total Net Position	<u>\$6,995,311</u>	<u>\$7,053,055</u>

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

FINANCIAL STATEMENTS

South Dakota Lottery
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION
For the Fiscal Years Ended June 30, 2016 and 2015

OPERATING REVENUES:	FY2016	FY2015
Video Lottery Revenue	\$103,801,272	\$99,564,998
Instant Ticket Sales	26,299,493	25,839,734
On-Line Ticket Sales	28,992,932	25,340,133
Terminal License Fees	1,117,700	1,112,200
Retailer License Fees	401,810	410,425
Total Operating Revenue	<u>160,613,207</u>	<u>152,267,490</u>
DIRECT GAME COSTS:		
Instant Prizes	17,132,245	16,929,551
On-Line Prizes	14,584,767	12,814,156
Instant Retail Commissions	1,479,346	1,453,501
On-Line Retail Commissions	1,515,613	1,358,225
Instant Ticket Print Costs	550,853	417,172
Total Direct Costs	<u>35,262,824</u>	<u>32,972,605</u>
Gross Profit	<u>125,350,383</u>	<u>119,294,885</u>
OPERATING EXPENSES:		
Personal Services and Benefits	1,769,797	1,767,388
Travel	135,908	130,068
Advertising	901,000	767,331
Contractual Services	4,814,694	4,361,251
Supplies and Materials	264,920	237,751
Depreciation/Amortization	237,002	725,720
Bad Debt Expense		3,615
Payments to Reservations	64,366	69,178
Total Operating Expenses	<u>8,187,687</u>	<u>8,062,302</u>
Operating Income	<u>117,162,696</u>	<u>111,232,583</u>
NON-OPERATING REVENUES (EXPENSES):		
Pooled Investment Income	321,921	138,496
Investment Costs	(3,057)	(16,608)
Non-operating Revenue from MUSL	72,632	33,758
Miscellaneous Revenue	41,326	59,956
Total Non-operating Revenue (Expenses)	<u>432,822</u>	<u>215,602</u>
Income Before Transfers	<u>117,595,518</u>	<u>111,448,185</u>
TRANSFERS:		
Transfers to the Property Tax Reduction Fund		94,744,636
Transfers to the General Fund	109,755,998	10,963,842
Transfers to the Capital Construction Fund	7,737,710	6,177,367
Transfers to the Department of Social Services	159,554	188,374
Total Transfers	<u>117,653,262</u>	<u>112,074,219</u>
Change in Net Position	<u>(57,744)</u>	<u>(626,034)</u>
Net Position Beginning of Year	7,053,055	7,387,190
Restatement Due to New Standard (see Note 1)		291,899
Adjusted Net Position Beginning of Year	<u>7,053,055</u>	<u>7,679,089</u>
NET POSITION END OF YEAR	<u>\$6,995,311</u>	<u>\$7,053,055</u>

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

FINANCIAL STATEMENTS

South Dakota Lottery

STATEMENT OF CASH FLOWS

For the Fiscal Years Ended June 30, 2016 and 2015

	FY2016	FY2015
Cash Flows from Operating Activities		
Receipts from Customers and Users	\$161,141,947	\$152,206,765
Payments for Lottery Prizes	(32,008,938)	(29,333,900)
Payments to Suppliers	(8,642,875)	(7,746,814)
Payments for Interfund Services Used	(923,764)	(933,356)
Payments for Employee Services	(1,805,044)	(1,838,419)
Other Receipts (Payments)	65,817	107,653
Net Cash Provided (Used) by Operating Activities	<u>117,827,143</u>	<u>112,461,929</u>
Cash Flows from Capital and Related Financing Activities		
Purchase of Capital Assets	(13,500)	
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>(13,500)</u>	<u>0</u>
Cash Flows from Noncapital Financing Activities		
Transfers to Other Funds	(117,394,190)	(112,447,724)
Net Cash Provided (Used) by Noncapital Financing Activities	<u>(117,394,190)</u>	<u>(112,447,724)</u>
Cash Flows from Investing Activities		
Pooled Investment Income	319,027	147,038
Investment Costs	(3,057)	(16,608)
Net Cash Provided (Used) by Investing Activities	<u>315,970</u>	<u>130,430</u>
Net Increase (Decrease) in Cash during the Fiscal Year	735,423	144,635
Cash at Beginning of Year	8,777,483	8,632,848
Cash at End of Year	<u>\$9,512,906</u>	<u>\$8,777,483</u>
Reconciliation of Operating Income to Net Cash Provided (Used) by Operating Activities		
Operating Income	\$117,162,696	\$111,232,583
Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided by Operating Activities:		
Depreciation/Amortization Expense	237,002	725,720
Other Revenue	41,326	59,956
Non-operating Revenue from MUSL	72,632	33,758
Decrease/(Increase) in Assets:		
Accounts Receivable	267,712	(6,870)
Allowance for Doubtful Accounts		3,615
Restricted Other Receivable	67,674	112,196
Restricted Certificates of Deposit	4,664	6,454
Prepaid Expense		(16,000)
Restricted Net Pension Asset	223,747	(330,866)
Decrease/(Increase) in Deferred Outflows of Resources:		
Deferred Outflows of Resources - Related to Pensions	(116,629)	(404,271)
Increase/(Decrease) in Liabilities:		
Accounts Payable	118,501	14,767
Prizes Payable	(85,660)	363,609
Due to Other Funds	25,051	(4,737)
Due to Other Governments	(21,806)	21,360
Operator Security Deposits	(14,764)	(2,336)
Escrows Payable	(4,812)	4,181
Accrued Liabilities	11,129	34,527
Unearned Revenue	(7,826)	(15,296)
Increase/(Decrease) in Deferred Inflows of Resources:		
Deferred Inflows of Resources - Related to Pensions	(153,494)	629,579
Total Adjustments	<u>664,447</u>	<u>1,229,346</u>
Net Cash Provided by Operating Activities	<u>\$117,827,143</u>	<u>\$112,461,929</u>

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

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

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

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

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

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

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

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

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

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

	2016	2015
Uncollected instant/on-line ticket revenues	\$486,764	\$974,302
Allowance for doubtful instant/on-line accounts	(18,072)	(18,072)
Uncollected video lottery revenues and fees	4,111,367	3,891,541
	<u>\$4,580,059</u>	<u>\$4,847,771</u>

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

OPERATOR SECURITY DEPOSITS. ARSD 48:02:05:04(18) requires video lottery operators to furnish to the Lottery by July 1 of each year, security equal to one-eighteenth of the State's share of estimated annual net machine income derived from the operator's video lottery machines. Security may be in the form of a surety bond, deposit in cash, an irrevocable letter of credit, or a certificate of deposit issued by a South Dakota financial institution with the Lottery endorsed on it as a payee. As of June 30, 2016 and 2015, the amount of cash on deposit with the Lottery was \$18,200 and \$28,300 and the amount of certificates of deposit being held by the Lottery was \$451,581 and \$456,245, respectively. The amount of \$5,115,700 and \$4,753,400, respectively, was in the form of surety bond or irrevocable letter of credit and are not reported on the Statement of Net Position. The total security deposits on June 30, 2016 and 2015 were \$5,585,481 and \$5,237,945, respectively.

NOTES TO THE FINANCIAL STATEMENTS

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

Capital Assets consisted of the following for fiscal years 2016 and 2015:

	2016				2015			
	Beginning Balance	Additions	Deletions	Ending Balance	Beginning Balance	Additions	Deletions	Ending Balance
Equipment	\$1,958,659	\$13,500	\$ —	\$1,972,159	\$1,958,659	\$ —	\$ —	\$1,958,659
Intangible Assets-Software	2,313,097	—	—	2,313,097	2,313,097	—	—	2,313,097
Total Capital Assets	4,271,756	13,500	—	4,285,256	4,271,756	—	—	4,271,756
Less Accumulated Depreciation/Amortization for:								
Equipment	(1,938,871)	(5,692)	—	(1,944,563)	(1,444,461)	(494,410)	—	(1,938,871)
Intangible Assets-Software	(1,272,204)	(231,310)	—	(1,503,514)	(1,040,894)	(231,310)	—	(1,272,204)
Total Accumulated Depreciation/Amortization	(3,211,075)	(237,002)	—	(3,448,077)	(2,485,355)	(725,720)	—	(3,211,075)
Total Capital Assets, Net	\$1,060,681	(\$223,502)	\$ —	\$ 837,179	\$1,786,401	(\$725,720)	\$ —	\$1,060,681

PENSIONS. In June 2012, the GASB issued Statement No. 68, Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27 and in November 2013 GASB issued Statement No. 71, Pension Transition for Contributions Made Subsequent to the Measurement Date – An Amendment of GASB Statement No. 68. The requirements of this statement are effective for financial statements for fiscal years beginning after June 15, 2014. The primary objective of this statement is to improve accounting and financial reporting by state and local governments for pensions.

Accounting changes adopted to conform to the provisions of this Statement were applied retroactively by restating beginning net position for the period ended June 30, 2015. For purposes of measuring the restricted net pension asset, deferred outflows of resources and deferred inflows of resources related to pensions, and pension revenue, information about the fiduciary net position of the South Dakota Retirement System (SDRS) and additions to/deletions from SDRS's fiduciary net position have been determined on the same basis as they are reported by SDRS. South Dakota Lottery contributions and restricted net pension asset are recognized on an accrual basis of accounting.

Beginning net position has been restated to reflect the related restricted net pension asset and deferred outflows of resources as of July 1, 2014 as follows:

Net position June 30, 2014 as previously reported	\$ 7,387,190
Restatement for pension accounting:	
Restricted net pension asset	212,732
Pension related deferred outflows of resources	79,167
Net position July 1, 2014, as restated	<u>\$7,679,089</u>

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

NOTES TO THE FINANCIAL STATEMENTS

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

A minimum of 50 percent of the projected revenue from the sale of lottery tickets, computed on a year-round basis, is allocated for payment of prizes. Prizes may be claimed up to 180 days after the official end of the game. Unclaimed prizes are added to the prize pools of subsequent lottery games. Reverted prizes during the fiscal years ended June 30, 2016 and 2015 were \$300,781 for on-line prizes and \$707,636 for instant prizes, and \$333,668 for on-line prizes and \$655,677 for instant prizes, respectively.

DUE TO THE GENERAL FUND. SDCL 42-7A-63 sets the State's percentage of net machine income at 50 percent of which all but 0.5 percent is deposited into the General Fund. At June 30, 2016 and 2015, there was a liability to the General Fund of \$4,054,832 and of \$3,824,712, respectively.

DUE TO THE GENERAL FUND AND THE CAPITAL CONSTRUCTION FUND. The Lottery maximizes net proceeds to the State from the sale of instant and on-line tickets. These net proceeds are transferred to the General Fund and Capital Construction Fund on an annual basis on or about July 1. There was a liability for instant ticket sales to the General Fund of \$1,017,739 and \$1,549,130, and a liability for on-line ticket sales to the Capital Construction Fund of \$1,137,710 and \$577,367 as of June 30, 2016 and 2015, respectively.

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

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

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

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

NET POSITION. "Net Position" is the difference between assets and deferred outflows of resources and liabilities and deferred inflows of resources. Net position is reported in three categories:

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

Restricted net position consists of Pension Obligations which is the sum of the ending Restricted Net Pension Asset balance and the ending Deferred Outflows Related to Pension balance less the ending Deferred Inflows Related to Pension balance. Restricted net position also includes funds held by the Multi-State Lottery Association (MUSL) in an unreserved account. The earnings paid to this account are considered to be distributions to the member lotteries, but account funds may be used by a member lottery only for the purposes approved by the MUSL Board.

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

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

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

NOTES TO THE FINANCIAL STATEMENTS

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

On-line retailers selling a jackpot winning Powerball or Mega Millions ticket may receive a bonus of \$50,000. Selling bonuses of \$20,000 and \$1,000 may be paid to retailers selling Powerball tickets of \$1,000,000 and \$50,000, respectively. Selling bonuses of \$25,000 and \$500 may be paid to retailers selling Mega Millions tickets of \$1,000,000 and \$5,000, respectively. If a retailer sells a Power Play ticket winning \$2,000,000 or \$50,000 (times the multiplier), a bonus of \$25,000 or \$1,000 times the multiplier may be paid, respectively. If a retailer sells a Megaplier ticket hitting the second prize (automatically worth \$1,000,000 regardless of the multiplier) or the \$5,000 third prize (times the multiplier), a bonus of \$25,000 or \$500 times the multiplier may be paid, respectively. Retailers who sell a Dakota Cash jackpot winning ticket may receive a bonus equal to 5 percent of the value of the winning ticket not to exceed \$5,000. Retailers who sell a Hot Lotto jackpot, \$30,000 or \$3,000 winning ticket may receive a bonus of \$10,000, \$3,000 or \$300, respectively. Retailers who sell a Sizzler ticket winning \$90,000 or \$9,000 may receive a bonus of \$9,000 or \$900, respectively.

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

NOTE 2. COMPENSATED ABSENCES

All permanent full-time employees earn annual leave. Upon termination, employees are eligible to receive compensation for their accrued annual leave balances. At June 30, 2016 and 2015, a liability existed for accumulated annual leave calculated at the employee's June 30 pay rate in the amount of \$153,644 and \$147,487, respectively. Employees who have been continuously employed by the State of South Dakota for at least seven years prior to the date of their retirement, voluntary resignation, or death will receive payment for one-fourth of their accumulated sick leave balance. This payment is not to exceed the sum of 12 weeks of the employee's annual compensation. At June 30, 2016 and 2015, a liability existed for accumulated sick leave, calculated at each employee's June 30 pay rate, in the amount of \$197,504 and \$193,685, respectively. The following is a schedule of changes in compensated absences at June 30, 2016 and 2015.

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Compensated Absences Payable					
Fiscal Year 2016	\$ 341,172	\$ 179,354	\$ 169,378	\$ 351,148	\$ 186,846
Fiscal Year 2015	318,331	180,865	158,024	341,172	180,719

NOTE 3. PENSION PLAN

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

State law requires employees to contribute 6 percent of their salary to the plan and the employer to contribute an amount equal to the employee's contribution. The right to receive retirement benefits vests after three years of credited service. The South Dakota Lottery's contributions to the SDRS for the fiscal years ended June 30, 2016, 2015, and 2014 were \$85,562, \$82,597, and \$79,167, respectively, equal to the required contributions each year.

At June 30, 2015 and 2014, SDRS was 104.1% and 107% funded, respectively, and accordingly has a restricted net pension asset. At June 30, 2016 and 2015 respectively, the South Dakota Lottery reported an asset of \$319,851 and \$543,598 for its proportionate share of the restricted net pension asset. For the fiscal year ended June 30, 2016, pension expense of \$46,375 was recorded and for the fiscal year ended June 30, 2015, pension revenue of \$22,961 was recorded. Deferred outflows of resources and deferred inflows of resources related to pensions were reported from the following sources:

NOTES TO THE FINANCIAL STATEMENTS

	Deferred Outflows of Resources	Deferred Inflows of Resources
As of June 30, 2016:		
Difference between expected and actual experience	\$ 65,491	
Changes in assumption	253,622	
Net difference between projected and actual earnings on pension plan investments	195,392	\$ 471,947
Changes in Proportionate Share		4,138
Contributions after the measurement date	85,562	
Total	<u>\$ 600,067</u>	<u>\$ 476,085</u>

	Deferred Outflows of Resources	Deferred Inflows of Resources
As of June 30, 2015:		
Difference between expected and actual experience	\$ 45,996	
Changes in assumption	354,845	
Net difference between projected and actual earnings on pension plan investments		\$ 629,579
Changes in Proportionate Share		
Contributions after the measurement date	82,597	
Total	<u>\$ 483,438</u>	<u>\$ 629,579</u>

NOTE 4. OPERATING LEASES

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

The following schedule is a summary of future minimum rental payments by years required under operating leases with lease terms in excess of one year as of June 30, 2016:

<u>Period Ending June 30:</u>	
2017	\$ 130,776
2018	130,776
2019	130,776
2020	130,776
2021	130,776
Later years	540,042
Total Minimum Payments	<u>\$1,193,922</u>

Total rental expense for all operating leases for the fiscal years ended June 30, 2016 and 2015, was \$85,114 and \$72,967, respectively.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 5. VIDEO LOTTERY

Following is a summary of video lottery revenues for the fiscal years ended June 30, 2016 and 2015:

	2016	2015
Cash In	\$678,898,195	\$641,668,506
Less Cash Out	471,295,651	442,538,510
Video Lottery Net Machine Income	207,602,544	199,129,996
Less Operator and Establishment Share	103,801,272	99,564,998
Video Lottery Revenue Available to the State	103,801,272	99,564,998
Less Lottery Operating Share	1,038,013	995,650
Video Lottery Revenue to the Property Tax Reduction Fund/General Fund	<u>\$102,763,259</u>	<u>\$ 98,569,348</u>

NOTE 6. TRANSFERS

Following is a summary of total transfers for the fiscal years ended June 30, 2016 and 2015:

Transfers Out:	2016	2015
General Fund Proceeds from Instant and On-Line	\$ 5,900,000	\$ 5,500,000
Capital Construction Fund Proceeds from On-Line	6,600,000	5,600,000
General Fund Proceeds from Instant and On-line not Yet Transferred	1,017,739	1,549,130
Capital Construction Fund Proceeds from On-Line not Yet Transferred	1,137,710	577,367
Video Lottery Proceeds Transferred to the General Fund	98,708,427	
Video Lottery Proceeds Transferred to the Property Tax Reduction Fund		94,744,636
Video Lottery Proceeds to General Fund not Yet Transferred	4,054,832	3,824,712
Video Lottery Grant to Department of Social Services	159,554	188,374
Video Lottery Fees Transferred to the General Fund	75,000	90,000
Total Transfers Out	<u>\$117,653,262</u>	<u>\$112,074,219</u>

NOTE 7. PARTICIPATION IN THE MULTI-STATE LOTTERY ASSOCIATION

The South Dakota Lottery is a member of the Multi-State Lottery Association (MUSL), which operates the Powerball/Power Play, Hot Lotto, and the Mega Millions/Megaplier games. Each MUSL member sells tickets through its licensed retailers and makes weekly wire transfers to MUSL in an amount equivalent to the member lottery's share of the prize liability less the actual low-tier prize liability. Monopoly Millionaires Club sales began October 19, 2014, and were suspended on December 26, 2014. The Wild Card 2 game was ended on February 24, 2016.

The prize pool for Powerball is 50 percent of each drawing period's sales and up to 5 percent shall be placed into a prize reserve account. The Power Play prize pool is 45.934 percent of sales and 4.066 percent may be placed in a prize reserve account. In drawings where the ten (10X) multiplier is available, the Power Play prize pool is 49.969 percent of sales and .031 percent may be placed in a prize reserve account. The prize pool for Wild Card 2 was 57 percent of sales and 3 percent was placed in a prize reserve account. The prize pool for Hot Lotto is 50 percent of sales and up to 1 percent shall be placed in a prize reserve account. The Sizzler prize pool is 47.8813 percent of sales with 2.1187 percent may be placed in a prize reserve account. The prize pool for Mega Millions and Megaplier is up to 55 percent of sales and up to 5 percent of Mega Million sales shall be placed in a prize reserve account. The prize pool for Monopoly Millionaires Club was 50 percent of each drawing period's sales and up to 4 percent was placed in a prize reserve account. A prize reserve fund serves as a contingency reserve to protect MUSL in cases of unforeseen liabilities. The money in a reserve fund is to be used at the discretion of the MUSL game group.

The prize reserve fund monies may be absorbed by a replacement game or are refundable to member states if MUSL or the MUSL game group disbands or if a member leaves MUSL or a game group. Members who leave must wait one year before receiving their remaining share, if any, of the prize reserve fund. The reserves are held by MUSL and are not included in these financial statements. At June 30, 2016 and 2015, the prize reserve account balances were:

NOTES TO THE FINANCIAL STATEMENTS

	2016 MUSL Balance	2016 SD Lottery Share	2015 MUSL Balance	2015 SD Lottery Share
Powerball Prize Reserve Account	\$ 72,114,390	\$ 450,952	\$ 74,843,800	\$ 466,390
Powerball Set Prize Reserve Account	39,307,288	196,066	35,096,120	218,233
Wild Card Prize Reserve Account	(7,580)	(2,549)	128,321	(31,148)
Hot Lotto Prize Reserve Account	7,170,477	304,009	8,022,038	338,443
Monopoly Millionaires Club			361,844	1,744
Mega Millions Prize Reserve Account	38,541,036	153,759	37,271,793	159,356
Total MUSL Prize Reserves	<u>\$157,125,611</u>	<u>\$1,102,237</u>	<u>\$155,723,916</u>	<u>\$1,153,018</u>

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

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

NOTE 8. CONTRACTUAL ARRANGEMENTS

A. Instant Tickets - The South Dakota Lottery entered into contracts with Scientific Games and Pollard Banknote Limited to provide instant game tickets through August 29, 2019.

B. Video Lottery Vendor - The South Dakota Lottery has contracted with Scientific Games to operate a video lottery system through December 24, 2019, with possible extension through December 24, 2024.

C. On-line Lottery Vendor - The South Dakota Lottery has contracted with GTECH Corporation to operate an on-line lottery gaming system through August 2, 2019.

NOTE 9. RISK MANAGEMENT

The South Dakota Lottery is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The South Dakota Lottery participates in the various programs administered by the State of South Dakota. These risk management programs are funded through assessments charged to participating entities. The risk management programs include: 1) coverage for risks associated with automobile liability and general tort liability (including public officials' errors and omissions liability, medical malpractice liability, law enforcement liability, and products liability) through the State's Public Entity Pool for Liability Fund; 2) coverage of employee medical claims through the State's health insurance program; 3) coverage for unemployment benefits through the State's Unemployment Insurance Fund; 4) coverage for workers' compensation benefits through the State's Workers' Compensation Fund; and, 5) coverage for property loss through the South Dakota Property and Casualty Insurance Company, LLC. Financial information relative to the self-insurance funds administered by the State is presented in the State of South Dakota Comprehensive Annual Financial Report.



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