

**STATE OF NEW JERSEY,
DEPARTMENT OF THE TREASURY,
DIVISION OF STATE LOTTERY**

Financial Statements
and Supplementary Information

June 30, 2016

**STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE
LOTTERY**

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**STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)**

INTRODUCTION

The following discussion and analysis provides an analytical overview of the financial position and activities of the State of New Jersey, Department of the Treasury, Division of State Lottery (the "Division of State Lottery") for the years ended June 30, 2016 and 2015. This statement was prepared by management and should be read in conjunction with the financial statements and notes hereto, which follow this section.

The Division of State Lottery was established in 1970 pursuant to the "State Lottery Law," N.J.S.A. 5:9-1 et seq. The Division of State Lottery operates within the Department of the Treasury of the State of New Jersey. The New Jersey Lottery Commission is a seven-member board, appointed by the Governor, authorized and empowered to promulgate rules and regulations in the operation of the Lottery. The "State Lottery Law" also mandates that a minimum of 30% of gross revenues from ticket sales be allocated for contributions to state aid for education and state institutions N.J.S.A. 5:9-7a (11).

As of June 30, 2016, the Division of State Lottery licensed more than 7,600 retailers throughout the State of New Jersey to act as retailers in the sale of New Jersey Lottery tickets. Lottery retailers receive compensation in the form of commissions on each ticket sold or validated, bonuses and various retailer incentive programs.

On June 20, 2013, a competitively bid 15-year (plus Fiscal Year 2014 stub year) contract was awarded to Northstar New Jersey, LLC (Northstar NJ) to provide sales and marketing services to the Division of State Lottery for the purpose of increasing lottery sales and net income (net proceeds for state aid for education and state institutions). If contracted net income targets for a given Fiscal Year are met or exceeded, Northstar NJ will earn incentive compensation. Conversely, if net income targets for a given Fiscal Year are not met it could result in reduced incentive or a contribution shortfall payment to the Division of State Lottery. In addition to compensation for its sales and marketing efforts, Northstar NJ is reimbursed for certain direct costs it incurs on behalf of the Division of State Lottery.

For the purposes of the incentive compensation calculation, the Division of State Lottery's net income is predicated on income targets contained in the amended Northstar NJ contract (see Schedule of Northstar NJ Net Income Targets). The Division of Lottery's actual net income for a Fiscal Year is decreased when Northstar NJ earns an incentive payment and is increased if Northstar NJ is obligated to pay a shortfall payment.

During Fiscal 2015, the Northstar NJ in accordance with the terms of the contract filed an adverse action due to the State of New Jersey's refusal to allow monitor games at retailers. The Division of State Lottery agreed that the refusal was an adverse action and provided relief to Northstar in the form of amended (reduced) net income targets. The amended contract provided for an allowance of \$2.5 million from Northstar NJ to the Division of State Lottery as an additional consideration for the terms contained therein.

Northstar NJ's first operational year, the year ending June 30, 2014, was a stub year October 1, 2013 through June 30, 2014. The remaining fifteen years (Fiscal Years 2015 – 2029) of the contract coincide with the Lottery's Fiscal Year, starting on July 1 and ending on June 30 through the year ending June 30, 2029. The year ended June 30, 2016, was the second full operational year of the contract.

**STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)**

INTRODUCTION (CONTINUED)

Under the terms of the agreement, Northstar NJ is responsible for subcontracting on behalf of the Lottery for service for which the Division of State Lottery previously contracted. Such services include the online terminal network for ticket sales, the warehousing and distribution of instant tickets, printing contracts for instant tickets, and marketing and advertising services.

The Division of State Lottery offers various products for sale with prize awards ranging from \$1.00 to annuity prizes well in excess of \$100 million. The various products sold are:

- Instant Games
- FastPlay (launched in August 2015)
- 5 Card Cash (launched in May 2016)
- Pick 3 (Including Pick 3 Instant Match)
- Pick 4 (Including Pick 4 Instant Match)
- Jersey Cash 5 (Including Jersey Cash 5 Instant Match)
- Pick 6 Xtra Lotto
- Mega Millions
- Powerball
- CASH4LIFE

FINANCIAL HIGHLIGHTS

The Division of State Lottery's financial position at June 30, 2016 and 2015, consisted of total assets of \$553 million and \$511 million, respectively, and total liabilities of \$542 million and \$509 million, respectively. A substantial portion of the asset and liability amounts is due to the Division of State Lottery's annuity investment in prize awards. The total amounts invested and due to Division of State Lottery winners as future installment payments at June 30, 2016 and 2015, were \$253 million and \$269 million, respectively. Net position increased from \$1.80 million in Fiscal Year 2015 to \$11.4 million for Fiscal Year 2016.

FINANCIAL STATEMENTS

The Division of State Lottery's financial statements include statement of net position as of June 30, 2016 and 2015, statement of revenues, expenses and changes in net position for years ended June 30, 2016 and 2015, and statement of cash flows for years ended June 30, 2016 and 2015. The financial statements are prepared in accordance with the accounting principles established by the Governmental Accounting Standards Board.

Statement of Net Position

The statement of net position presents the Division of State Lottery's financial position as of the last day of the Fiscal Year. The Division of State Lottery's assets, liabilities and net position are summarized (in millions) as follows:

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) (CONTINUED)

FINANCIAL STATEMENTS (CONTINUED)

Statements of Net Position (Continued)

	Years Ended June 30,		
	2016	2015	2014
Current Assets	\$ 326	\$ 283	\$ 272
Deposit Fund Contracts	227	228	245
Total Assets	<u>553</u>	<u>511</u>	<u>517</u>
Current Liabilities	314	280	270
Non-Current Liabilities	228	229	246
Total Liabilities	<u>542</u>	<u>509</u>	<u>516</u>
Restricted Net Position	3.9	1.5	.5
Unrestricted Net Position	7.5	.3	.3
Total Net Position	<u>\$ 11.4</u>	<u>\$ 1.8</u>	<u>\$.8</u>

Current assets consist of cash and investment in the State of New Jersey Cash Management Fund (the NJCMF), accounts receivable, current year annuity investments and deferred expenses. The investment in the NJCMF totaled \$251 million and \$207 million at June 30, 2016 and 2015, respectively.

The Division of State Lottery funds long-term installment prizes with insurance company annuities and United States Treasury securities. The total value of these investments was \$253 million and \$269 million as of June 30, 2016 and 2015, respectively. The Division of State Lottery has annuity investments with ten (10) insurance companies. The total market value of the United States Treasury securities was \$45 million at June 30, 2016 and 2015, respectively. The annuities due beyond Fiscal Year 2017 and Fiscal Year 2016 total \$228 million and \$229 million respectively. These represent the non-current assets reported on the Division of State Lottery's statements of net position. Although categorized as an asset, annuities represent an obligation that the Division of State Lottery has to the annuitants to fund the monies due to them over a fixed period of time based on the amount of the annuitized jackpot at the time of the "win." The duration of an annuity varies from twenty years to life. Because of the true nature of these annuities, the Division of State Lottery has a fiduciary responsibility to continue to administer these instruments in a responsible and prudent manner. The current amounts due to annuity winners totaled \$25 million and \$40 million as of June 30, 2016 and 2015, respectively.

Non-current liabilities represent annuity prize awards due beyond 2017 and also include the total due for unused vacation and sick leave (compensated absences).

Net position represents the excess of the Division of State Lottery's assets over its liabilities and are summarized as follows (in millions):

	Years Ended June 30,		
	2016	2015	2014
Restricted (Unclaimed Prize Reserves)	\$ 3.9	\$ 1.5	\$ 0.5
Unrestricted	7.5	0.3	0.3
Total Net Position	<u>\$ 11.4</u>	<u>\$ 1.8</u>	<u>\$ 0.8</u>

Expired prizes, or unclaimed prize reserves, are restricted to fund either future prizes or state contributions.

**STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) (CONTINUED)**

FINANCIAL STATEMENTS (CONTINUED)

Statements of Revenues, Expenses and Changes in Net Assets

The results of the Division of State Lottery's operations are presented in the statements of revenues, expenses and changes in net position, which are summarized (in millions) as follows:

	Years Ended June 30,		
	2016	2015	2014
Operating revenues			
Ticket sales	\$ 3,290	\$ 3,001	\$ 2,901
Forfeited prizes	34	48	39
Miscellaneous income	2	1	2
Total operating revenue	<u>3,326</u>	<u>3,050</u>	<u>2,942</u>
Operating expenses			
Prize expenses	2,002	1,825	1,732
Retailer commissions	186	170	162
Northstar NJ fees & expenses	44	42	29
Vendor fees	60	54	46
Administrative expense	10	10	16
Bad debt expense	0	1	1
Total operating expenses	<u>2,302</u>	<u>2,102</u>	<u>1,986</u>
Operating income	<u>1,024</u>	<u>948</u>	<u>956</u>
Non-Operating revenue (expenses)	<u>(28)</u>	<u>13</u>	<u>1</u>
Income before transfers out	997	961	957
Operating transfers – State contributions	987	960	965
Increase (decrease) in net position	<u>\$ 10</u>	<u>\$ 1</u>	<u>\$ (8)</u>

The Division of State Lottery awarded approximately \$2.002 billion in prize awards in Fiscal Year 2016 and approximately \$1.825 billion in Fiscal Year 2015. Nearly 113 million winning tickets were validated and paid in Fiscal Year 2016. This amount is a slight increase above the 111 million winning tickets which were validated and paid in Fiscal Year 2015.

The Division of State Lottery's vendors provided critical services to the Division of State Lottery, including the production, warehousing, distribution and accounting for all lottery tickets. The total compensation paid for the Division of State Lottery's vendors and network fees was \$104 million in Fiscal Year 2016. This amount was paid directly to Northstar NJ for the services it provided or procured on behalf of the Division of State Lottery. Included in the \$104 million paid to Northstar NJ was \$25 million for advertising and marketing costs, \$35 million for gaming system vendor fees, and \$24 million for instant ticket printing vendor fees. In Fiscal Year 2015, the total compensation paid for the Division of Lottery's vendors and network fees was \$97 million. Of this amount \$96 million was paid to Northstar NJ including \$23 million for advertising and marketing costs, \$32 million for gaming system vendor fees, and \$22 million for instant ticket printing vendor fees.

**STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) (CONTINUED)**

FINANCIAL STATEMENTS (CONTINUED)

Statements of Revenues, Expenses and Changes in Net Assets (Continued)

The Division of State Lottery's administrative expenses for the Fiscal Years 2016 and 2015 were \$10 million, respectively for each year. These administrative expenses include salaries, auditing services, rent, security, data processing services, office supplies and attorney general fees. The management services contract has shifted advertising and other expenses from the Division of State Lottery to Northstar NJ.

The Division of State Lottery is required by the State of New Jersey Lottery law to contribute a minimum of 30% of net revenues from ticket sales to the State of New Jersey, Department of the Treasury for state aid for education and state institutions. As a result of various sales initiatives, game enhancements and efficient operations, the Division of State Lottery contributed \$987 million, 30% of net revenues, in Fiscal Year 2016 and \$960 million, 32% of net revenues, in Fiscal Year 2015.

During the term of the contract, Northstar NJ's incentive compensation is reduced in the event the annual contractual net income target is not met or if the 30% minimum contribution threshold is not achieved. Conversely, incentive compensation is increased in the event that the net income target is exceeded. Furthermore, in the event that actual net income is significantly below the contracted net income target, then the contribution shortfall payment provisions are invoked. Northstar's (amended) net income target for the Fiscal Year ended June 30, 2016, was \$963,478,103.

The operating income for Fiscal Year 2016 totaled \$1,024.7 million. In accordance with the amended Northstar contract, a separate calculation is performed to determine the operating income for the purposes of establishing the incentive/shortfall payment. The calculation deducts a portion of the unclaimed prizes for use of the Division of State Lottery, and also subtracts the cost of the Million Dollar Replay program. The calculation determined that Northstar NJ's incentive/shortfall payment is based on operating income of \$1,024.7 million. The calculation is shown below.

Operating Income	\$ 1,024.7 million
Division of State Lottery Portion of Unclaimed Prizes	(2.6) million
Cost of Million Dollar Replay Program	(1.4) million
Total Deduction	<u>\$ 1,020.8 million</u>

The amended contract does establish bottom and top caps on Northstar NJ's compensation. In the event of a particularly lucrative contract year (Upper Income Levels are surpassed) total compensation to Northstar NJ cannot exceed 3% of Operating Income for the entire contract year. Conversely, in a subpar contract year, the contribution shortfall payment cannot exceed 2% of net income.

In Fiscal Year 2016, the former scenario was utilized to calculate the Incentive Compensation Payment as outlined below.

**STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) (CONTINUED)**

FINANCIAL STATEMENTS (CONTINUED)

Statements of Revenues, Expenses and Changes in Net Assets (Continued)

Net Income Target	\$ 963.5 million
Fiscal Year 2016 Operating Income (adjusted)	1,020.8 million
3% Calculation for Incentive Compensation	30.6 million
Less Penalty for Failure to Achieve 30% Contribution Mandate	<u>0.0 million</u>
Total Incentive Compensation for Fiscal Year 2016	<u>\$ 30.6 million</u>

Statement of Cash Flows

The statements of cash flows are summarized (in millions) as follows:

	Years Ended June 30,		
	2016	2015	2014
Cash flows provided by operating activities	\$ 1,042	\$ 936	\$ 916
Cash flows used in non-capital financing activities	(1,017)	(943)	(950)
Cash flows (used in) provided by investing activities	(28)	10	34
Net increase (decrease) in cash	<u>\$ (3)</u>	<u>\$ 3</u>	<u>\$ -</u>

SUMMARY

Division of State Lottery management has been working closely with Northstar NJ throughout Fiscal Year 2016, and looks forward to continuing this innovative partnership going into the third full year of the contract.

Prior to the end of Fiscal Year 2014 the Division of State Lottery along with the New York State Lottery launched the new multi-state draw game, CASH4LIFE in which players can win \$1,000 a day for life, \$1,000 a week for life or seven other fixed prize levels. Through Fiscal Year 2015 "CASH4LIFE" exceeded expectations and proved to be both very popular with players and attractive to other lottery jurisdictions with Virginia and Pennsylvania joining the game in the spring of 2015. In Fiscal Year 2016, CASH4LIFE expanded to a total of six states with Tennessee and Maryland joining. In Fiscal Year 2017, CASH4LIFE is expected to increase to a total of nine states with Georgia joining in August, Indiana joining in September, and Florida joining later in the year.

In August 2015, the Division of State Lottery launched FastPlay, a new terminal game. Unlike traditional draw games, the FastPlay product line comprises a series of quick play style games generated through the lottery terminal that offer multiple price points and multiple themes. Similar to an instant game, players will know immediately if they have won rather than wait until later in the day or the week for a drawing to take place to learn the outcome. This new "easy to play and win" game category has proven successful with attracting new players in other lottery jurisdictions. During Fiscal Year 2016, the game generated nearly \$48 million in net revenues. By attracting additional players to the entire New Jersey Lottery gaming portfolio, the game proved to be a key building block in the Division of State Lottery's efforts to obtain record sales during the year.

**STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) (CONTINUED)**

SUMMARY (CONTINUED)

Before the close of Fiscal 2016, the Division of State Lottery launched 5 Card Cash, a new daily terminal game which is based on the rules of poker. The player receives a ticket containing the images of five playing cards from a traditional fifty-two card deck. If any combination of those five cards contains a winning hand, the player instantly wins a prize ranging in size from \$2.00 to \$5,000.00. For an additional wager, the player may opt to participate in the game's "All In" feature and have a chance to win the progressive jackpot that pays a minimum of \$10,000.00. Every player also has a chance to win at the evening draw when the images of five playing cards will be drawn from a draw machine. Similar to FastPlay, 5 Card Cash contains the attributes of both an instant and a draw game.

CONTACTING THE DIVISION'S FINANCIAL MANAGEMENT

This financial report is designed to provide citizens with a general overview of the Division of State Lottery's finances. If you have any questions about this report or need additional financial information, contact the Division of State Lottery's Deputy Director of Finance at One Lawrence Park Complex, 1333 Brunswick Avenue, PO Box 041, Lawrenceville, New Jersey 08625-0041.

INDEPENDENT AUDITORS' REPORT

INDEPENDENT AUDITORS' REPORT

State of New Jersey
Department of the treasury
Division of State Lottery

Report on the Financial Statements

We have audited the accompanying financial statements of the State of New Jersey, Department of the Treasury, Division of State Lottery (the "Division of State Lottery") as of and for the years ended June 30, 2016 and 2015, and the related notes to financial statements, which collectively comprise the Division of State Lottery's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the 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 Division of State Lottery'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.

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INDEPENDENT AUDITORS' REPORT (CONTINUED)

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Division of State Lottery as of June 30, 2016 and 2015, and the respective changes in its financial position and cash flows thereof for the years then ended, 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 one through seven 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 Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Division of State Lottery's basic financial statements. The accompanying schedules of revenues, expenses and changes in net position budget and actual, instant game revenues, and administrative expenses are presented for the purposes of additional analysis and are not a required part of the basic financial statements. Such information 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. The information except for the portion marked "unaudited," has been subjected to the auditing procedures applied in the audit of the basic financial statements 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, except for the portion marked "unaudited," the schedules of revenues, expenses and changes in net position budget and actual, instant game revenues, and administrative expenses are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

The schedule of Northstar NJ net income targets as listed in the table of contents 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.

INDEPENDENT AUDITORS' REPORT (CONTINUED)

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated December 1, 2016, on our consideration of Division of State 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 the Division of State Lottery's internal control over financial reporting and compliance.

Mercadien, P.C.

Certified Public Accountants

December 1, 2016

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY

STATEMENTS OF NET POSITION

	June 30,	
	2016	2015
ASSETS		
Current Assets		
Cash	\$ 84,665	\$ 3,301,670
Accounts receivable, net of allowance for doubtful accounts of \$2,224,000 in 2016 and \$2,724,000 in 2015	46,188,335	16,412,649
Northstar NJ shortfall receivable	-	12,910,236
Deferred expenses	2,690,563	2,724,776
Investments:		
Deposit Fund Contracts	25,352,704	40,211,749
State of New Jersey Cash Management Fund	251,134,998	207,229,895
Total current assets	<u>325,451,266</u>	<u>282,790,974</u>
Non-Current Assets		
Investments - deposit fund contracts	<u>227,170,016</u>	<u>228,525,068</u>
Total non-current assets	<u>227,170,016</u>	<u>228,525,068</u>
 Total Assets	 <u>\$ 552,621,282</u>	 <u>\$ 511,316,042</u>
LIABILITIES		
Current Liabilities		
Accounts payable and accrued expenses	\$ 64,235,894	\$ 30,956,803
Obligation for unpaid prize awards	120,682,044	76,100,675
Installment prize awards	25,352,704	40,211,749
Due To State Of New Jersey - education & State institutions	103,000,000	133,000,000
Total current liabilities	<u>313,270,643</u>	<u>280,269,226</u>
Non-Current Liabilities		
Compensated absences	733,631	723,069
Installment prize awards	<u>227,170,016</u>	<u>228,525,068</u>
Total non current liabilities	<u>227,903,647</u>	<u>229,248,137</u>
Total Liabilities	<u>541,174,289</u>	<u>509,517,363</u>
NET POSITION		
Restricted for prize awards or contributions for aid to education and State institutions	3,881,442	1,479,398
Unrestricted	<u>7,565,551</u>	<u>319,282</u>
Total Net Position	<u>\$ 11,446,993</u>	<u>\$ 1,798,680</u>

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

	Years ended June 30,	
	2016	2015
Operating revenues		
Ticket Sales		
Pick 3	\$ 439,627,708	\$ 437,774,537
Pick 4	275,200,494	271,765,815
Jersey Cash 5	151,636,143	148,424,382
Pick 6 Lotto	54,632,415	57,613,947
CASH4LIFE	45,760,158	71,417,890
Mega Millions	144,424,092	162,460,731
Powerball	286,003,472	165,435,126
Fastplay	48,388,770	-
Niche Games (5 Card Cash)	3,064,919	-
Monopoly Millionaires' Club	-	3,265,580
Instant Games	1,872,915,471	1,709,143,246
Sales discounts/tickets provided as prizes	(31,806,927)	(26,772,618)
Total ticket sales	<u>3,289,846,714</u>	<u>3,000,528,636</u>
Other revenues		
Forfeited Prizes	33,931,475	48,069,961
Miscellaneous	1,983,565	1,391,732
Total operating revenues	<u>3,325,761,753</u>	<u>3,049,990,329</u>
Operating expenses		
Prize expenses	2,001,693,206	1,825,233,183
Retailer commissions	185,980,265	169,445,854
Instant ticket vendor printing fees	24,467,215	22,316,078
Gaming system vendor fees	35,080,631	31,786,934
Northstar NJ management fee	4,952,335	4,850,004
Northstar NJ manager expenses	13,979,117	14,186,014
Northstar NJ advertising & marketing expenses	24,779,320	23,320,008
Administration expenses	10,134,156	9,967,207
Multi-State fees	61,239	81,538
Drawing broadcast fees	407,093	334,957
Bad debt expense	110,000	625,000
Total operating expenses	<u>2,301,644,578</u>	<u>2,102,146,779</u>
Operating income	1,024,117,175	947,843,550
Non-operating revenue		
Northstar NJ	2,500,000	-
Interest	655,103	225,611
	<u>1,027,272,279</u>	<u>948,069,161</u>
Northstar NJ incentive/(shortfall) payment	30,623,965	(12,910,236)
Income available for transfer	<u>996,648,314</u>	<u>960,979,397</u>
Contributions for State aid to education and State institutions	987,000,000	960,000,000
Change in net position	9,648,314	979,397
Net position, beginning of year	1,798,679	819,282
Net position - end of year	<u>\$ 11,446,993</u>	<u>\$ 1,798,679</u>

See accompanying notes to financial statements.

**STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY
STATEMENTS OF CASH FLOWS**

	Years ended June 30,	
	2016	2015
Cash Flows from Operating Activities		
Sales to customers	\$ 1,523,781,082	\$ 1,400,922,317
Payments for prize awards	(383,423,271)	(376,612,147)
Payments for vendor commissions and fees	(96,561,724)	(95,987,279)
Administrative payments	(10,002,023)	(2,628,159)
Other payments	-	(27,741)
Cash flows from annuity operations		
Annuity receipts	36,079,204	48,049,662
Purchases of annuities	(2,307,648)	(2,862,726)
Payments of annuity prizes	(25,942,860)	(35,297,300)
Net cash provided by operating activities	<u>1,041,622,759</u>	<u>935,556,627</u>
Cash Flows used in Non-Capital Financing Activities		
Contributions for aid to education and state institutions	<u>(1,017,000,000)</u>	<u>(943,010,000)</u>
Cash Flows from Investment Activities		
Cash Management Fund proceeds	1,299,200,000	1,251,147,625
Cash Management Fund purchases	(1,342,450,000)	(1,240,800,000)
Proceeds from Northstar NJ	15,410,236	-
Net cash (used) provided by investment activities	<u>(27,839,764)</u>	<u>10,347,625</u>
Net (Decrease) Increase in cash	(3,217,005)	2,894,252
Cash, beginning of year	3,301,670	407,418
Cash, end of year	<u>\$ 84,665</u>	<u>\$ 3,301,670</u>
Reconciliation of operating income to net cash provided by operating activities		
Operating Income	\$ 1,024,117,175	\$ 947,843,550
Changes in assets and liabilities		
Accounts receivable	(29,775,686)	(16,129,858)
Investments - deposit fund contracts	16,214,097	27,533,956
Other assets	34,213	302,278
Accounts payable and accrued expenses	2,655,126	17,184,339
Obligation for unpaid prize awards	28,367,272	(41,213,808)
Compensating absences	10,562	36,170
Net cash provided by operating activities	<u>\$ 1,041,622,759</u>	<u>\$ 935,556,627</u>

See accompanying notes to financial statements.

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The State of New Jersey, Department of the Treasury, Division of State Lottery (the "Division of State Lottery") and the State Lottery Commission (the "Commission") were concurrently established in 1970, pursuant to the "State Lottery Law" (N.J.S.A. 5:9-1 et seq.). The Division of State Lottery operates within the Department of the Treasury of the State of New Jersey. The Commission consists of the State Treasurer and six public members and is authorized and empowered to promulgate rules and regulations regarding the conduct of lottery games, including the price or prices of tickets, the number and size of prizes on winning tickets, the licensing of retailers, and the apportionment of ticket revenues. The Division of State Lottery's financial statements are presented as those of an enterprise fund and include the operations for which the Division of State Lottery is financially accountable and exercises oversight responsibility.

Basis of Accounting

The Division of State Lottery prepares its financial statements using the accrual basis of accounting. Revenues are recognized when earned, and expenses are recognized when incurred.

In its accounting and financial reporting, the Division follows the pronouncements of the Governmental Accounting Standards Board ("GASB") and other entities that promulgate accounting principles. GASB Statement 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, establishes the order of priority of pronouncements and other sources of accounting and financial reporting guidance that a governmental entity should apply. Per the Statement, the sources of authoritative generally accepted accounting principles ("GAAP") are categorized in descending order of authority as follows: GASB Statements and Interpretations, GASB Technical Bulletins, GASB Implementation Guides, and literature of the American Institute of Certified Public Accountants ("AICPA") cleared by the GASB. Authoritative GAAP is incorporated periodically into the *Codification of Governmental Accounting and Financial Reporting Standards* (Codification), and when presented in the Codification, it retains its authoritative status. If the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP described above, a governmental entity should first consider accounting principles for similar transactions or other events within a source of authoritative GAAP described above and then may consider nonauthoritative accounting literature from other sources. These include GASB Concepts Statements; pronouncements and other literature of the Financial Accounting Standards Board ("FASB"), Federal Accounting Standards Advisory Board, International Public Sector Accounting Standards Board, and International Accounting Standards Board, and AICPA literature not cleared by the GASB; practices that are widely recognized and prevalent in state and local government; literature of other professional associations or regulatory agencies; and accounting textbooks, handbooks, and articles.

Use of Estimates

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 amounts and disclosures. Accordingly, actual results could differ from those estimates.

State of New Jersey Cash Management Fund

Investments in the State of New Jersey Cash Management Fund are valued at cost, which approximates fair value.

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Accounts Receivable

Accounts receivable is comprised primarily of amounts due from retailers. The allowance for uncollectible accounts is funded by a \$100 per year license renewal fee paid by the Division's retailers. Operating expense is charged with an allowance for estimated uncollectible accounts based on past experience and an analysis of current accounts receivable collectibility. Accounts deemed uncollectible are charged to the allowance in the year they are deemed uncollectible.

Installment Prize Awards and Prize Expenses

Installment prize awards are recorded based upon the present value of an annuity at terms to yield a series of future payments needed to meet the obligations of the Division of State Lottery for prize disbursements. For each lottery winner that chooses to receive their prize in installments, the Division of State Lottery purchases annuity contracts from insurance companies and U.S. government securities to fund its liability for installment prize awards. An annuity contract represents an obligation by an insurance company to provide a fixed series of payments over a specified period. Annuity contracts are subject to credit risk. The Division of State Lottery seeks to control its exposure to such credit risk by purchasing annuity contracts only from insurance companies that meet certain minimum standards.

Due to the long-term nature of these contracts, the credit quality of the issuer is subject to change. Amounts recorded as prize expense reflect the cost of annuity contracts and U.S. government securities necessary to satisfy stated prize awards plus any single payment awards. These annuities are presented on the statements of net position as deposit fund contracts, carried at contract value which approximates fair value.

Equipment

The Division follows the state's threshold for capitalizing equipment as follows: machinery and equipment over \$20,000 and motor vehicles over \$30,000. Purchases that do not meet the threshold for capitalization are recognized as expenses in the statements of revenues, expenses and changes in net assets in the period during which they are acquired and are included in administrative expenses. As of June 30, 2016 and 2015, leasehold improvements included in deferred expenses were \$734,362. For the years ended June 30, 2016 and 2015, amortization expense was \$75,378 and \$68,408, respectively.

Net Position

Restricted

Amounts restricted for prize awards or contributions for aid to education and state institutions consist of prizes that are not claimed within one year from the date of the drawing for machine games and within one year from the date of game's closing for instant games.

Unrestricted

The unrestricted net position represents resources available for current operating expenses in compliance with legal and budgetary restrictions.

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Revenue Recognition

Revenues from the sale of lottery tickets are recognized as follows:

- “Pick-3”, “Pick-4”, “Jersey Cash 5”, “Pick-6 Lotto”, “Mega Millions”, “Megaplier”, “Powerball”, “Power Play”, “CASH4LIFE”, and “5 Card Cash” games on the drawing date.
- Instant games are recognized daily, based upon the settlement of instant game inventory packs by selling retailers. Sales adjustments are recorded based upon final reconciliations prepared after the termination of a lottery instant game.
- Fastplay games upon the sale of each ticket.
- Sales discounts are recorded for the sales value of tickets provided to retailers at no cost, to be used for promotional purposes. Tickets provided as prizes are recorded as sales at the face value of each ticket, then backed out as discounts and are not included in prize expense.

Forfeited Prizes

The State Lottery Law requires that prizes not claimed within one year from the date of the drawing for machine games and within one year from the date of the game’s closing for instant games be forfeited. Effective November 21, 1991, the Commission authorized that 70% of forfeited prizes are to be maintained restricted for prize awards and are available to augment future prize awards or, at the discretion of the executive director, to augment the Division of State Lottery’s contribution for state aid for education and state institutions. The remaining 30% goes directly to contributions to aid education and institutions to be consistent with the 30% minimum contribution requirement of the State Lottery Law. Forfeited prizes are recognized as “Other Revenues” during the period forfeited. For the years ended June 30, 2016 and 2015, forfeited prizes were \$33,931,475 and \$48,069,961, respectively.

Contributions and Prize Awards

The State Lottery Law requires no less than 30% of total revenues accruing from ticket sales to be paid to the State Treasury for state aid for education and state institutions. Contributions for the years ended June 30, 2016 and 2015, aggregated \$987,000,000 and \$960,000,000, respectively, of which \$103,000,000 and \$133,000,000 was due to the State Treasury at June 30, 2016 and 2015, respectively.

For machine games, the Division of State Lottery has designated that a minimum of 45% of gross revenues be allocated for prize awards, including retailer bonuses. Prize expense is recorded when the winning ticket number is selected for the respective lottery game based on eligible winning tickets sold. For instant games, the percentage of gross revenues to be allocated for prize awards varies by game.

Commissions and Fees

Retailers receive a commission of 5% based on the total tickets sold, a commission of 1.25% of terminal validations and top tier selling bonuses. The online game contractor receives a fee equal to a contractual percentage of the revenue generated through the respective network maintained by the contractor. All other gaming contractors are paid fees based on the units of service provided.

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY

NOTES TO FINANCIAL STATEMENTS

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Commissions and Fees (Continued)

Northstar NJ has had numerous retailer incentive programs for the purpose of boosting sales, these include temporary commission increases and bonuses. Both of these incentives are recorded as prize expense.

Administrative Expenses

The Division of State Lottery follows the state's threshold for capitalizing equipment, which is as follows: machinery and equipment over \$20,000 and motor vehicles over \$30,000. Purchases that do not meet the threshold for capitalization are recognized as expenses in the statement of revenues, expenses and changes in net position during the period in which they are acquired and are included in administrative expenses.

The Division records vacation and sick time incurred during the period in "administrative expenses" in the accompanying statements of revenues, expenses and changes in net assets. Payments for accumulated sick leave balances are made to retiring employees upon regular retirement from the State of New Jersey's General Fund. Such payment is based on 50% of the employee's sick leave accumulation at the pay rate in effect at the time of retirement, up to a maximum of \$15,000. Employees separating from service prior to retirement are not entitled to payments for accumulated sick leave.

B. CASH AND INVESTMENTS

The Division of State Lottery adopted GASB Statement No. 40, "Deposits and Investment Risk Disclosures," which requires uncollateralized deposits exposed to custodial credit risk to be disclosed. The custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits that are in possession of an outside party. The following is a summary of the Division's cash deposits by financial institution and the amount exposed to custodial credit risk at June 30, 2016 and 2015. The Division's deposits with Wells Fargo are insured by the Federal Deposit Insurance Corporation up to \$250,000.

	<u>June 30,</u>	
	<u>2015</u>	<u>2015</u>
Wells Fargo	\$ 84,416	\$ 3,301,420
New Jersey Cash Management Fund	<u>251,134,998</u>	<u>207,229,895</u>
Total	<u>\$ 251,219,414</u>	<u>\$ 210,531,565</u>

The New Jersey Cash Management Fund ("NJCMF") is a common trust fund administered by the Department of the Treasury, Division of Investment. NJCMF is considered to be an investment trust fund as defined in Governmental Accounting Standards Board (GASB) Statement No. 31. NJCMF funds are not subject to custodial credit risk due to the fact that the funds are held by and in the name of the NJCMF in a segregated trust account with the third party custodian rather than in the possession of the third party custodian. Additionally, though the underlying assets and investments of the NJCMF pool are subject to credit risk, the risk is limited by the mix of the credit quality ratings of the assets in the portfolio maintained by NJCMF.

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY

NOTES TO FINANCIAL STATEMENTS

B. CASH AND INVESTMENTS (CONTINUED)

Fair Value Measurements

The Division of State Lottery follows the Fair Value Measurements Topic of the FASB Accounting Standards Codification, which provides a framework for measuring fair value under accounting principles generally accepted in the United States of America.

Fair Value on a Recurring Basis

The table below presents the balances of investments - deposit fund contracts measured at fair value on the statement of net position as of June 30, 2016 and 2015:

	June 30, 2016			
	Total	Level 1	Level 2	Level 3
Annuity Investment Deposit Fund Contracts	\$ 252,522,720	\$ 45,382,269	\$ 207,140,451	\$ -
Total	<u>\$ 252,522,720</u>	<u>\$ 45,382,269</u>	<u>\$ 207,140,451</u>	<u>\$ -</u>
	June 30, 2015			
Annuity Investment Deposit Fund Contracts	\$ 268,736,817	\$ 45,496,949	\$ 223,239,868	\$ -
Total	<u>\$ 268,736,817</u>	<u>\$ 45,496,949</u>	<u>\$ 223,239,868</u>	<u>\$ -</u>

C. FUTURE INSTALLMENT PRIZE AMOUNTS

The Division of State Lottery purchases annuity, or deposit fund contracts, from insurance companies and U.S. government securities to fund its liability for future installment prize awards. Generally, insurance company annuity contracts fund life annuities for games such as the CASH4LIFE draw game and Win for Life instant games. U.S. government securities fund term annuity prizes for games such as Pick 6 Xtra Lotto, Mega Millions, Powerball and instant games. An annuity contract represents an obligation by an insurance company to provide a fixed series of payments over a specified period.

Annuity contracts are carried at their current contract values, which are based upon their original purchase prices adjusted for credited interest and amounts already received by Lottery and disbursed to annuitants. Annuity contracts are subject to credit risk. The Division of State Lottery seeks to control its exposure to such credit risk by purchasing annuity contracts only from insurance companies that meet certain minimum standards. Such standards include the following requirements:

1. Combined capital and surplus of at least \$1 billion;
2. Admitted assets of at least \$10 billion;
3. Risk based capital ratio of at least 300%; and
4. Must have ratings equal to or better than at least two of the three private rating agencies:
 - Standard & Poor's long term insurer financial strength rating of AA- or higher
 - AM Best financial strength rating of "A" or higher
 - Moody's long term insurance financial strength rating of "Aa3" or higher.

According to the Division of State Lottery's calculation, only one company does not meet the criteria, that of Delaware Life, formerly Sun Life Assurance; as of June 30, 2016 and 2015, Delaware Life had annuity contracts totaling approximately \$24,657,743 and \$28,936,804, respectively. However, due to the long-term nature of these contracts, the credit quality of the issuer is subject to change.

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY

NOTES TO FINANCIAL STATEMENTS

C. FUTURE INSTALLMENT PRIZE AMOUNTS (Continued)

At June 30, 2016 and 2015, the Division of State Lottery held insurance company annuity contracts totaling \$207,140,451 and \$223,239,868, respectively, issued through ten insurance companies, which are due in installments ranging from twenty-five years to the lifetime of the recipient. The estimated fair value of annuity contracts approximates the carrying value reflected in the accompanying statement of net position at June 30, 2016 and 2015.

U.S. government securities are carried at fair value. At June 30, 2016 and 2015, the Division of State Lottery had \$45,382,268 and \$45,496,949, respectively, in U.S. treasuries (see Note B).

Concentrations of Credit Risk

“Concentration of Credit Risk” is the risk that relates to the amount of investment at any one entity. The disclosure requirement of this risk factor is limited to investments in excess of 5% of the total. Guaranteed annuity contracts, as stated above, are the only category subject to concentration of credit risk disclosure.

A significant portion (in excess of 5% of total) of the Division of State Lottery's investment in annuity contracts at such date is invested with each of the following five companies:

- Ohio National Life
- New York Life Insurance Co.
- Protective Life
- Metropolitan Life
- Delaware Life (formerly Sun Life Assurance)

D. LITIGATION

The Division of State Lottery is a party to a number of lawsuits arising out of the conduct of its business. While the ultimate results of the lawsuits or other proceedings against the Division of State Lottery cannot be predicted with certainty, management of the Division of State Lottery does not expect that these matters will have a material adverse effect on the financial position or results of operations of the Division of State Lottery.

E. COMMITMENTS

Contractual Arrangements

The Division of State Lottery maintains a gaming network of over 7,600 retailer locations where all games are sold. IGT Corporation, formerly GTECH Corporation is responsible for operating the network games and providing courier services under a contract that was assigned to Northstar NJ on October 1, 2013, and expires concurrent with Northstar NJ's contract.

On June 20, 2013, a competitively bid 15-year contract was awarded to Northstar New Jersey Lottery Group, LLC to provide sales and marketing services to the Division of State Lottery. Northstar New Jersey Lottery Group, LLC is owned directly by two members: (1) Scientific Games New Jersey, LLC, and (2) Northstar New Jersey Holding Company, LLC, and indirectly by three companies: (1) IGT Corporation and (2) OSI LTT NJ Holdings Inc., which are the Members of Northstar New Jersey Holding Company, LLC, and (3) Scientific Games International, Inc., which is the owner of Scientific Games New Jersey, LLC. The base services commenced on October 1, 2013. The contract required NSNJ to bid net income targets for each Fiscal Year of the 15-year contract. An amendment signed on December 31, 2015, revised the income level and targets downward for contract years 3 through 15. The amended contract provided for an allowance of \$2.5 million from Northstar NJ to the Division of State Lottery (PTO) as an additional consideration for the terms contained therein. If NSNJ meets or exceeds the net income target for a given Fiscal Year, they can earn an incentive pay or alternatively, if they don't meet the net income target, they are assessed a penalty.

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY

NOTES TO FINANCIAL STATEMENTS

E. COMMITMENTS (CONTINUED)

Contractual Arrangements (Continued)

The Northstar NJ contract provides for an allowance of \$20 million to offset any potential contribution shortfall payments over the life of the contract. For Fiscal Year 2015, the calculated contribution shortfall amounted to \$18,799,399 which was offset by \$5,889,163 remaining of the \$20 million shortfall allowance, resulting in a net shortfall payment of \$12,910,236. For Fiscal Year 2016, NSNJ met its amended contractual net income target resulting in an incentive contribution due to NSNJ of \$30,623,965.

Prior to the beginning of each Fiscal Year the Division of State Lottery and Northstar NJ agree to an annual business plan that includes the projected operating expenses of Northstar NJ for the Fiscal Year. Each month NSNJ may invoice the Division of State Lottery one twelfth (1/12) of the total operating expenses for the Fiscal Year. Each monthly invoice is accompanied by detailed backup data and information supporting expenses incurred. At the end of the Fiscal Year Northstar NJ operating expenses are aggregated and reconciled with any excess returned to the Division of State Lottery. The Northstar NJ expenses for services to the Division of State Lottery amounted to \$43,710,772 and \$42,356,026 for the years ended June 30, 2016 and 2015, respectively.

In addition to the budgeted monthly expenditures, NSNJ receives a system provider vendor fee based on 1.05% of ticket sales and an instant ticket printing fee based on 1.216% of ticket sales as part of its subcontractor agreements. All other gaming contractors are paid fees based on the units of service provided.

Operating Leases

The Division of State Lottery leases certain office facilities and equipment under non-cancelable operating lease agreements expiring through Fiscal Year 2024. Future minimum lease payments for office facilities are as follows:

<u>Year Ending June 30,</u>	<u>Amount</u>
2017	\$ 767,619
2018	638,550
2019	648,583
2020	655,750
2021	655,750
2022-2024	<u>1,584,729</u>
	<u>\$ 4,950,982</u>

Rent expense for office facilities and equipment for the years ended June 30, 2016 and 2015, was \$1,261,056 and \$1,130,524, respectively.

F. GASB STATEMENT NUMBER 45 - ACCOUNTING AND FINANCIAL REPORTING BY EMPLOYERS FOR POST-RETIREMENT BENEFITS OTHER THAN PENSION

The Division of State Lottery is a member of the State of New Jersey's cost sharing multiple-employer plan for health and post-retirement medical benefits. Thus, the Division of State Lottery's portion of this liability and cost is included in the State of New Jersey's Comprehensive Annual Financial Report, as such, the Liability of Division of State Lottery's employees is covered under the State plan on an annual basis. Please refer to State website www.state.nj.us for more information regarding the plan.

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY

NOTES TO FINANCIAL STATEMENTS

G. PENSION PLAN

The Division of State Lottery's employees which are part of the Department of the Treasury, participate in the Public Employees Retirement System of New Jersey ("PERS"), a cost sharing multiple-employer defined benefit plan. The Division of State Lottery's contribution is determined by State statute and is based upon an actuarial computation performed by the PERS.

The Division of State Lottery's total and covered payroll for the years ended June 30, 2016, 2015 and 2014, was, \$6,315,443, \$6,306,627 and \$6,421,066, respectively. The State of New Jersey's (the "State") contribution is based on the employer contribution rate developed by the system's actuary. The rate is then applied against the pension eligible salary for all State employees. The State does not keep track of contributions made to PERS for each separate state agency. For Fiscal Year ended June 30, 2016 and 2015, the contribution rate was 3.06%. For Fiscal Year ended June 30, 2014, the contribution rate was 3.06%.

The State of New Jersey, Division of Pension and Benefits, issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the State of New Jersey, Division of Pension and Benefits, P.O. Box 295, Trenton, NJ 08625-0295 or by visiting their website at: www.state.nj.us/treasury/pensions.

H. ROUNDING

Some schedules in the financial statements may have dollar differences due to rounding adjustments.

SUPPLEMENTARY INFORMATION

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY

SCHEDULE OF REVENUES, EXPENSES AND CHANGES IN NET POSITION - BUDGET AND ACTUAL

Year ended June 30, 2016

	Budget (unaudited)	Actual	Variance (unfavorable) favorable
Operating revenues			
Ticket sales			
Pick 3	\$ 447,756,647	\$ 439,627,708	\$ (8,128,939)
Pick 4	277,962,903	275,200,494	(2,762,409)
Jersey Cash 5	151,582,690	151,636,143	53,453
Pick 6 Lotto	59,822,647	54,632,415	(5,190,232)
Cash 4 Life	50,072,204	45,760,158	(4,312,046)
Fastplay (Started August 2015)	40,214,769	48,388,770	8,174,001
Niche Games (5 Card Cash started May 2016)	9,574,740	3,064,919	(6,509,821)
Monitor Games	-	-	-
Mega Millions	172,177,424	144,424,092	(27,753,332)
Powerball	192,596,342	286,003,472	93,407,130
Instant Games	1,836,338,814	1,872,915,471	36,576,657
Sales discounts/Tickets Provided as Prizes	<u>(51,919,500)</u>	<u>(31,806,927)</u>	<u>20,112,573</u>
	3,186,179,679	3,289,846,714	103,667,035
Other Revenues			
Forfeited prizes	36,540,000	33,931,475	(2,608,525)
Miscellaneous	<u>1,500,000</u>	<u>1,983,565</u>	<u>483,565</u>
Total operating revenues	3,224,219,679	3,325,761,753	101,542,074
Operating expenses			
Prize expenses	1,942,102,328	2,001,693,206	(59,590,878)
Retailer commissions	180,362,124	185,980,265	(5,618,141)
Instant ticket vendor printing fees	22,329,880	24,467,215	(2,137,335)
Instant Enhancement/License Fee	2,472,600	-	2,472,600
Gaming system vendor fees	34,000,041	35,080,631	(1,080,590)
Northstar NJ management fee	4,952,000	4,952,335	(335)
Northstar NJ manager expenses	18,200,000	13,979,117	4,220,883
Northstar NJ advertising & marketing expenses	24,950,000	24,779,320	170,680
Administration expenses	13,658,125	10,134,156	3,523,969
Multi-State fees	150,000	61,239	88,761
Drawing broadcast fees	250,000	407,093	(157,093)
Bad debt expense	<u>600,000</u>	<u>110,000</u>	<u>490,000</u>
Total operating expenses	<u>2,244,027,098</u>	<u>2,301,644,578</u>	<u>(57,617,480)</u>
Operating income	980,192,581	1,024,117,175	43,924,594
Non-operating revenue			
Northstar NJ	-	2,500,000	2,500,000
Interest	<u>200,000</u>	<u>655,103</u>	<u>455,103</u>
	980,392,581	1,027,272,279	46,879,698
Northstar NJ (shortfall)/incentive payment	<u>(19,607,852)</u>	<u>30,623,965</u>	<u>(50,231,817)</u>
Income available for transfer	1,000,000,433	996,648,314	(3,352,119)
Contributions for State aid to education and State institutions	<u>1,000,000,000</u>	<u>987,000,000</u>	<u>(13,000,000)</u>
Change in net position	433	9,648,314	9,647,881
Net position, beginning of year	<u>1,798,679</u>	<u>1,798,679</u>	<u>-</u>
Net position, end of year	<u>\$ 1,799,112</u>	<u>\$ 11,446,993</u>	<u>\$ 9,647,881</u>

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY

SCHEDULE OF INSTANT GAME REVENUES

	Years Ended June 30,	
	2016	2015
\$5,000,000 CASH EXTRAVAGANZA	\$ 152,973,829	\$ 111,664,860
100X THE CASH	80,048,840	-
\$5,000,000 CASH EXTRAVAGANZA	71,975,730	-
\$2,000,000 MEGA CASH	62,387,140	75,166,162
\$150,000,000 CASH SPECTACULAR	61,839,520	84,301,080
ALL CASH MILLIONS	45,125,300	-
CROSSWORD	41,816,993	-
CROSSWORD	40,177,386	-
50X THE CASH	37,808,775	-
BIG MONEY SPECTACULAR	34,369,344	-
DOUBLE DIAMOND SPECTACULAR	33,748,760	27,495,700
WILD CASH BONANZA	32,524,720	-
WIN FOR LIFE!	30,770,214	3,971,910
\$10,000 PAY DAY	29,926,883	-
LOTERIA	28,053,779	31,949,855
\$500,000 FORTUNE	27,869,818	9,253,540
SUPER CROSSWORD	27,763,089	-
CROSSWORD	27,672,013	14,166,273
SUPER CROSSWORD	27,669,390	-
\$500 FRENZY	27,313,609	24,061,710
WILD CASH	27,092,498	-
SUPER CROSSWORD	26,962,537	-
BIG MONEY SPECTACULAR	25,167,376	-
\$500,000 WINFALL	24,504,144	-
SUPER CASH SPECTACULAR	23,837,274	21,843,370
20X THE CASH	22,894,545	-
SEASON'S GOLD	22,448,258	-
\$20,000 PAY DAY	22,262,729	29,674,257
BIG MONEY SPECTACULAR	21,980,104	-
WORLD SERIES OF POKER	21,298,446	-
\$2,500 FRENZY	21,065,274	23,998,760
LUCKY CASH	19,894,503	-
\$1,000,000 JACKPOT	19,110,052	14,252,860
\$250,000 CROSSWORD	18,004,242	-
BIG MONEY SPECTACULAR	17,956,053	17,240,226
\$250,000 CROSSWORD	17,896,440	-
WIN \$2,500 A WEEK FOR LIFE	17,845,565	31,396,525
WILD 10S	17,840,691	-
\$10K BLOWOUT	17,695,390	-
\$250,000 CROSSWORD	17,587,300	-
CLASSIC BINGO	17,277,570	12,900
WILD CHERRY BINGO DOUBLER	17,243,956	-
SUPER CROSSWORD	16,846,035	-
HOLIDAY SPARKLE	16,730,190	-

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY

SCHEDULE OF INSTANT GAME REVENUES (CONTINUED)

	Years Ended June 30,	
	2016	2015
SUPER SLOTS	16,505,895	-
SUPER CROSSWORD	15,715,815	11,937,685
20X MONEY	15,369,604	28,588,614
SHIMMERING 7'S	15,129,670	-
BIG CASH SPECTACULAR	14,688,037	-
\$200,000 JACKPOT	14,405,823	10,905,280
CASINO ROYALE	13,883,807	-
GOLD BAR BINGO	13,542,234	7,311,098
10X THE CASH	13,313,526	-
CASH BLAST	13,170,700	-
50X MONEY	13,001,259	63,745,359
JOKER'S WILD	12,331,203	7,893,930
HOLIDAY LUCKY TIMES 10	11,851,996	-
BINGO MULTIPLIER	11,428,880	-
SUPER TIC TAC TOE	11,236,165	11,493,912
\$100 FRENZY	11,145,432	12,023,254
FROSTY FUN	10,473,178	-
DOUBLE MATCH	10,466,746	-
TRIPLE WINNING 7s	10,371,492	19,523,701
\$250,000 CROSSWORD	10,231,780	-
SUPER 7'S SLINGO	8,923,659	-
\$250,000 CROSSWORD	8,809,530	8,992,740
CASH EXPLOSION	7,707,106	2,775,210
MONOPOLY MILLIONAIRES' CLUB	7,567,270	6,285,180
\$30,000 JACKPOT	7,300,855	6,422,274
SPRING FLING TRIPLER	7,283,685	-
WIN IT ALL	7,215,581	19,064,177
\$100,000 WINNING STREAK	6,666,320	-
INSTANT BINGO	6,663,503	-
HOLIDAY CHEER	6,362,331	-
10X MONEY	6,289,054	17,686,749
QUICK \$50S	6,053,603	-
WIN \$500 A WEEK FOR LIFE	5,933,853	13,039,320
MASSIVE MONEY BINGO	5,747,990	12,443,930
BIG CASH SPECTACULAR	5,664,402	10,659,738
QUICK CHANGE	5,238,141	-
\$150,000 GOLD RUSH	5,112,310	-
CROSSWORD	5,061,708	-
DOUBLE DOUBLER	4,806,377	-
WILD DOUBLER	4,439,251	-
CASH BONUS BINGO	4,297,296	13,283,694
5X THE CASH	4,226,564	-
LUCKY LOOT	4,148,780	18,845,942
BIRTHDAY BUCKS	4,113,192	10,124,266

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY

SCHEDULE OF INSTANT GAME REVENUES (CONTINUED)

	Years Ended June 30,	
	2016	2015
BLOOMIN' BUCKS	3,944,436	3,139,139
\$50 FRENZY	3,724,657	5,770,157
BIRTHDAY BUCKS	3,692,622	-
RAPID REFUND	3,481,195	-
WIN FOR LIFE	3,116,103	-
WIN \$1,000 A WEEK FOR LIFE	3,101,703	26,223,224
LOOSE CHANGE	3,063,382	11,271,259
WORLD SERIES OF POKER	2,957,075	27,613,765
DOUBLE YOUR LUCK	2,791,141	1,415,108
CLASSIC BINGO	2,231,212	8,435,454
ESCAPE TO MARGARITAVILLE	2,126,790	6,753,319
\$5,000 JACKPOT	2,115,907	2,988,521
TIC TAC TOE	1,855,195	-
GEM 7s	1,849,902	17,701,631
LIFE IS GOOD	1,835,610	-
DIAMOND SPECTACULAR	1,519,218	43,949,560
MONOPOLY (\$2)	1,517,951	9,666,773
\$10,000 PAYDAY	1,159,276	34,971,900
AMC THE WALKING DEAD	1,140,714	8,232,414
BIG MONEY SPECTACULAR	1,101,600	-
5X MONEY	894,387	6,195,684
SUPER CROSSWORD	755,315	26,915,352
MONOPOLY (\$1)	717,605	5,222,539
CROSSWORD	671,278	41,271,814
RED WHITE & BLUE DOUBLER	631,096	-
TRIPLE DIAMONDS	484,350	14,399,291
MONEY MATCH	418,600	9,100,037
LUCKY IN LOVE	394,218	7,546,006
\$500 FRENZY	354,815	32,026,252
HOLIDAY LUCKY TIMES 10	345,048	14,841,073
CANDY CANE CROSSWORD	311,807	13,207,510
HOLIDAY GOLD	311,330	20,544,504
HOLIDAY MAGIC	182,194	15,068,247
BIG MONEY SPECTACULAR	175,769	34,999,477
QUARTER MILLION CROSSWORD	127,470	14,989,860
\$250,000 CROSSWORD	119,650	31,552,930
MONOPOLY (\$5)	116,176	14,054,943
2015 CASH SPECTACULAR	102,467	15,259,462
CHILLY BILLS	73,226	7,595,946
BINGO X10	73,010	20,817,258
HOLIDAY CASH	70,698	7,566,051
SILVER GOLD PLATINUM 7'S	19,395	11,156,650
CLASSIC BINGO	15,262	10,251,880
BINGO STAR TRIPLER	14,481	11,547,693

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY

SCHEDULE OF INSTANT GAME REVENUES (CONTINUED)

	Years Ended June 30,	
	2016	2015
ELECTRIC 5s	13,148	8,932,939
SUPER CROSSWORD	12,690	27,543,845
FIRE & ICE	10,936	6,256,044
HIGH ROLLER	9,960	4,572,536
10X CASH	8,830	11,340,216
CROSSWORD	7,515	42,095,609
NEW JERSEY HOLD 'EM POKER	7,115	6,843,511
BIG MONEY SPECTACULAR	1,692	35,447,550
PRIOR YEAR GAME	-	(1,500)
MARTI - MONEY	-	(3,754)
GOLD MINE	-	(600)
BULLSEYE BINGO	-	(1,287)
BLACKJACK TRIPLER	-	(2,555)
CLASSIC BINGO	-	(528)
SKEE-BALL	-	(2,379)
DINER DOUBLER	-	(4,078)
STARRY NIGHT	-	(1,420)
BIRTHDAY WISHES	-	(712)
CASH COW	-	(2,004)
PACK MAN CASH	-	(1,024)
SUPER TIC TAC TOE	-	(2,529)
CASINO CASH	-	(1,195)
GOLD RUSH	-	(300)
LUCKY HORSESHOE BINGO	-	(573)
FOOTBALL BLITZ	-	(1,918)
\$50 FALL CLEANUP	-	(300)
THE GOLDEN TICKET	-	(5,375)
DOUBLE DOLLARS	-	(186)
WIN FOR LIFE	-	(2,472)
MASSIVE CASH	-	(2,910)
ZODIAC MATCH	-	(5,546)
FANTASY BLACK JACK	-	(6,430)
TIC TAC SNOW	-	(562)
BINGO TIMES 10	-	(625)
SUPER 7'S SLINGO	-	(4,758)
RED HOT HEARTS	-	(894)
FROGGER	-	(9,066)
SUPER CROSSWORD	-	(145)
\$1,000,000 LAS VEGAS GAME SHOW	-	(6,630)
\$50 SHADES OF GREEN	-	(296)
POKER SHOWDOWN	-	(2,880)
LUCKY LINES	-	(2,199)
MONEY MANIA	-	(2,690)
LUCKY TIMES 20	-	(1,905)
SPRING DOUBLER	-	(7,244)

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY
SCHEDULE OF INSTANT GAME REVENUES (CONTINUED)

	Years Ended June 30,	
	2016	2015
MONOPOLY MILLIONAIRE	-	(1,940)
MOTHER'S DAY	-	(7,573)
CASINO MULTIPLIER	-	(9,100)
TAKE ME OUT TO THE BALLGAME	-	(8,205)
DUBBLE BUBBLE BINGO	-	(19,113)
FATHER'S DAY	-	(13,007)
CLASSIC BINGO	-	(5,114)
CROSSWORD	-	(576)
WIN FOR LIFE	-	13,014
SUPER CROSSWORD	-	(300)
LUCKY DUCK DOUBLER	-	(5,957)
QUARTER MILLION CROSSWORD	-	(1,300)
CHAMPIONSHIP POKER	-	(4,735)
5X CASH	-	208,185
RED, WHITE & MOOLA	-	(10,742)
LUCKY 7'S DOUBLER	-	6,170
GOLD BAR BINGO	-	11,935
DIAMOND SPECTACULAR	-	(1,500)
CASH LINES	-	(2,667)
GOLDEN NUGGET	-	10,700
BIG MONEY SPECTACULAR	-	(600)
SUPER CROSSWORD	-	(1,500)
CROSSWORD	-	(3,276)
DIAMOND SPECTACULAR	-	453,900
SUNNY \$50'S	-	15,770
RUBY RED 7s	-	4,572
BIG MONEY SPECTACULAR	-	(600)
SUPER CROSSWORD	-	6,790
CROSSWORD	-	8,085
\$500,000 LUCKY STREAK	-	(2,464)
PLANTS VS. ZOMBIES	-	(8,780)
\$50,000 LUCKY STREAK	-	4,552
TRIPLE TRIPLER	-	238,224
BINGO BOXES	-	13,170
MERRY MILLIONAIRE	-	5,388
SEASON'S GOLD	-	10,145
HOLIDAY LUCKY TIMES 10	-	1,452
HOLIDAY GREETINGS	-	(24,760)
BIG MONEY SPECTACULAR	-	3,226
SUPER CROSSWORD	-	86,775
SNOW ME THE MONEY	-	479,394
QUARTER MILLION CROSSWORD	-	166,974
BIG MONEY SPECTACULAR	-	55,134
LOVE TO WIN!	-	241,353
BIG MONEY SPECTACULAR	-	1,735,454

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY
SCHEDULE OF INSTANT GAME REVENUES (CONTINUED)

	Years Ended June 30,	
	2016	2015
3X CASH	(35)	271,887
CLASSIC BINGO	(110)	198,482
ZUMA	(177)	581,593
HOLD 'EM POKER	(295)	3,539,220
SUPER CROSSWORD	(300)	12,034,250
\$100,000,000 SPECTACULAR	(600)	1,243,840
CROSSWORD	(606)	1,263,808
CROSSWORD	(663)	29,638,269
HIT \$50s	(694)	2,484,296
POWER PLAY CROSSWORD	(789)	822,504
BIG MONEY SPECTACULAR	(1,096)	28,156,743
SUPER CROSSWORD	(1,280)	27,831,472
7/11/2021	(1,761)	748,393
MASSIVE MONEY BINGO	(2,260)	4,354,801
CLASSIC BINGO	(2,294)	5,508,418
20X CASH	(3,140)	10,952,511
DOUBLE BLACKJACK	(6,700)	1,752,110
HOT DICE	(10,858)	3,414,591
	<u>\$ 1,872,915,471</u>	<u>\$ 1,709,143,246</u>

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY
SCHEDULE OF ADMINISTRATIVE EXPENSES

	Years Ended June 30,	
	2016	2015
Salaries	\$ 6,315,443	\$ 6,306,627
Printing & Office Supplies	65,801	66,921
Vehicular Supplies	489	583
Household & Clothing	2,898	2,032
Travel	40,177	36,783
Telephone	112,820	101,689
Postage	50,512	51,163
Data Processing	790,147	547,382
Household & Security	238,456	246,184
Professional Services	352,000	347,519
Other Professional Services	300,245	237,168
Data Processing-OIT	192,813	526,484
Maintenance - Building & Grounds	2,199	11,063
Maintenance - Office Equipment	6,150	10,702
Rent - Building & Grounds	1,261,056	1,130,524
Central Motor Pool	85,606	93,376
Vehicular Equipment	32,202	143,382
Other Equipment	178,709	29,300
Information Processing Equipment	31,056	9,919
Amortization	75,378	68,408
Total	<u>\$ 10,134,156</u>	<u>\$ 9,967,207</u>

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY
SCHEDULE OF NORTHSTAR NJ NET INCOME TARGETS (UNAUDITED)

Year	Fiscal Year	Net Income Target	
Year 1 (Stub Year)	2014	\$ 760,897,061	(Prorated)
Year 2	2015	1,047,000,000	
Year 3	2016	963,478,103	
Year 4	2017	990,513,343	
Year 5	2018	1,009,871,643	
Year 6	2019	1,023,544,636	
Year 7	2020	1,036,114,600	
Year 8	2021	1,045,300,757	
Year 9	2022	1,054,562,917	
Year 10	2023	1,063,906,791	
Year 11	2024	1,073,794,937	
Year 12	2025	1,083,757,077	
Year 13	2026	1,093,797,230	
Year 14	2027	1,103,903,546	
Year 15	2028	1,114,089,100	
Year 16	2029	1,124,348,918	

**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**

State of New Jersey
Department of the Treasury
Division of State Lottery

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 Division of State Lottery (the "Division of State Lottery") as of and for the year ended June 30, 2016 and 2015, and the related notes to financial statements, which collectively comprise the Division of State Lottery's basic financial statements, and have issued our report thereon dated December 1, 2016.

Internal Control over Financial Reporting

In planning and performing our audits of the basic financial statements, we considered the Division of State 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 the Division of State Lottery's internal control. Accordingly, we do not express an opinion on the effectiveness of the Division of State 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 Division of State Lottery'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.

**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
(CONTINUED)**

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Division of State 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.

Mercadien, P.C.
Certified Public Accountants

December 1, 2016