

2013 ANNUAL REPORT

NORTH CAROLINA EDUCATION LOTTERY



Financial Highlights

In fiscal year 2013, the N.C. Education Lottery ...

- Achieved seventh year of record sales and earnings
- Recorded highest sales ever, \$1.69 billion
- Set new record in instant games sales, exceeding \$1 billion in instant sales for first time ever
- Exceeded \$9.6 billion in sales since inception
- Recorded highest earnings ever, \$478 million
- Surpassed \$2.9 billion in earnings since inception
- Received a clean opinion, for the seventh year in a row, during its annual independent financial audit
- Credited with “exceptional performance” and cited for “prudent cost-benefit approach” for increasing sales and earnings in biennial performance audit
- Increased number of lottery retailers to 6,839, up 1 percent from year before
- Paid \$118 million in sales commission to retailers
- Awarded a prize of \$1 million or more for the 129th time since inception
- Collected \$14.2 million in state income taxes from prize winnings
- Collected from prize winnings \$1.3 million in debts owed to state and local governments
- Supported minority-owned businesses with \$11.2 million in contracts either from the NCEL or its vendors
- Provided \$1 million to the N.C. Department of Health and Human Services for gambling addiction, education and treatment programs
- Received awards, for the fourth year in a row, for its efforts to clearly communicate its financial information to the public from the Government Finance Officers Association of the United States and Canada.



"I would like to say thank you, to you and the North Carolina Education Lottery, for the grant scholarship. I know the money that was awarded to me was not "free money", and that someone was responsible for helping me achieve my educational goals. To not thank you and your foundation would be very ungrateful of me. I truly value every educational opportunity I receive. Thank you again."

*Erica J. Woodington
Fayetteville
May 2013 graduate, Fayetteville Technical Community College*

table of contents

chairman's report	4
commission	5
executive director's report	6
organization	7
beneficiaries	8
record sales	10
\$1 billion in instant sales	12
games	13
marketing	14
winners	16
responsible gaming	18
management's discussion & analysis	21
financial statements	27

EDUCATION LOTTERY ACHIEVES RECORD SALES AND EARNINGS FOR SEVENTH YEAR IN A ROW



Keith Ballentine
Chairman
Rocky Mount

Vice President of Daughtridge Gas & Oil Company

Appointed by Speaker of the House Thom Tillis. Named chairman by Gov. Pat McCrory

Term: Aug. 2013 - Aug. 31, 2017

I'm pleased to report that the N.C. Education Lottery completed its year by setting, for the seventh year in a row, another year of record sales and another year of record profits for one of the state's most important causes, education.

Revenues hit \$1.69 billion in fiscal year 2013 and our earnings for education topped \$478 million. If you're investing money these days, most of us would agree that a return of 28 percent on every dollar you invest is a great dividend to get back. That's the kind of return the state is getting from the operations of the Education Lottery.

Here's another record that I, as a businessman, am pleased to share. For the seventh year in a row, independent auditors, hired by North Carolina's State Auditor Beth Wood, audited the lottery's financial records and again gave the lottery a clean opinion, the highest standard that can be achieved.

So when you take the measure of the Education Lottery, thanks to the good guidance provided by my fellow commissioners and the work of Executive Director Alice Garland and her professional staff, the results you see are: integrity, efficiency and exceptional performance. We know that's the kind of performance citizens across our state expect and deserve from their government. Our goal is to see that it continues.

As we ended our latest fiscal year, the total amount raised by the lottery to support education programs exceeded \$2.9 billion. Every county gets lottery dollars to help build and repair schools, keep teachers teaching in grades K-3, provide for four-year-olds to attend a good pre-k program, and help young people pay for the costs of going to college.

In my hometown, I don't have to go far to see a concrete example of the benefits. This fall, a 60-year-old school building that once was the home of Rocky Mount High School was restored and brought back to use, with the help of lottery dollars, as Rocky Mount Middle School. Education programs in every county in the state have seen similar benefits. Please visit a section of our website called "Where The Money Goes" to see how your county has benefited from the state lottery.

Seven years of record sales and earnings don't just happen. They occur because, like any successful business, we stay committed to providing quality customer service, work closely with our business partners, and keep a close eye on the bottom line. Every dollar we raise is a dollar the state has available to make an important investment in its future.

A handwritten signature in black ink that reads "W. Keith Ballentine". The signature is written in a cursive, flowing style.

NORTH CAROLINA EDUCATION LOTTERY COMMISSION



The Education Lottery Commission consists of nine members. Five members are appointed by the governor and four by the N.C. General Assembly, of which two are recommended by the speaker of the N.C. House of Representatives, and two by the president pro tem of the N.C. Senate. Commissioners serve five-year terms and can only serve two successive terms. One member must have five years experience in law enforcement, one must be a certified public accountant, and one must have retail sales experience as an owner or manager of a sales company. Commission meetings are held once a quarter.

Courtney A. Crowder
Raleigh
Owner, Crowder Consulting Co.
Appointed by: Gov. Beverly Perdue
Term: Nov. 6, 2012 – Aug. 31, 2017

A.J. Daoud
Pilot Mountain
President and CEO,
American Funeral Partners
Appointed by: Gov. Pat McCrory
Term: Oct. 22, 2013 – Aug. 31, 2018

Barry Z. Dodson
Stoneville
Certified Public Accountant
Appointed by: Senate President
Pro Tem Phil Berger
Term: Feb. 15, 2011 – Aug. 31, 2013

David F. Kirby
Raleigh
Attorney
Appointed by: Gov. Beverly Perdue
Term: June 28, 2012 – Aug. 31, 2016

Chris L. Shew
Wilkesboro
Sheriff, Wilkes County
Appointed by: Gov. Pat McCrory
Term: Oct. 22, 2013 – Aug. 31, 2016

Jody Tyson
Snow Hill
Managing Partner, Taylor-Tyson
Funeral Service
Appointed by: Senate President
Pro Tem Phil Berger
Term: July 2, 2012 – Aug. 31, 2017

Alice Underhill
New Bern
Retired law librarian and
former member, N.C. House
of Representatives.
Appointed by: Gov. Beverly Perdue
Term: Jan. 4, 2013 – Aug. 31, 2016

Doug Baker
Chapel Hill
CEO, OfficeMeds of Durham
Appointed by: Speaker of the House
Thom Tillis
Term: Sept. 1, 2013 – Aug. 31, 2018

Commissioners who left the commission as their terms expired included Carla Archie of Charlotte, Robert Farris Jr. of Wilson, and J. Marlene Hyatt of Waynesville. Commissioner Ray Warren of Hiddenite resigned in FY13.

PERFORMANCE AUDIT CALLED EDUCATION LOTTERY'S OPERATIONS "EXCEPTIONAL"



Alice Garland
Executive Director, North Carolina Education Lottery

Every two years, the N.C. Education Lottery gets put to the test as independent auditors conduct a performance audit comparing our operations in key areas to those of our peers. I'm pleased to report that in the latest test, completed in February 2013, the auditors described the lottery's ongoing overall performance as exceptional.

In fact, the audit reported that the N.C. Education Lottery was one of only three U.S. lotteries to achieve growth in earnings every year from 2007 through 2012. It also cited the lottery's "prudent cost-benefit approach" to increasing sales and earnings for the state.

Here are three achievements cited by the performance audit that I believe any head of a \$1.7 billion business in North Carolina could be proud of:

- Growing sales 60 percent from fiscal year 2008 through fiscal year 2012
- Seeing a 48 percent increase in sales per retailer from 2008 to 2012
- Achieving a 27 percent increase in productivity of lottery employees

The performance audit also underscored the importance of advertising to the lottery's mission of raising money for good causes. It found that the Education Lottery had the lowest per capita spending on advertising of its peers but the second highest return of investment in advertising. To me those findings say we are getting a good bang for our buck with our advertising dollars.

As you read our Annual Report this year, I hope it conveys to you a sense of what a complicated undertaking a lottery can be.

We are a sales organization with over 6,800 retailers that need to be serviced by our sales staff either in the field or on the phone. We are a technology company that tests new games and programs before tickets go on sale. We are a collections agency, collecting about \$30 million a week in revenues from our retailers through a sweep of their bank accounts. We pursue insufficient fund accounts and have a 99.97% collection rate.

We are a prize award agency, paying out on average \$2.6 million a day. We are a regulatory body, licensing new retailers and administering retail contracts. We are a security firm, protecting our games and drawings from fraud.

We are a gaming venture, launching 45 new instant games a year, adding features to our draw games and studying players to determine what new games to offer. We are an advertising and marketing firm reaching consumers statewide, year-round, through strategic advertising and marketing campaigns. Our marketing efforts include fairs, festivals, and sporting events from the Dixie Classic Fair to NASCAR races.

I'm glad to share such positive results from the performance audit with you. It shows that North Carolina has the efficient, well-run lottery it deserves.

Alice Garland

MORE THAN 110 YEARS OF EXPERIENCE LEADS EDUCATION LOTTERY

Senior leaders of the N.C. Education Lottery have a combined total of 113 years of experience in the lottery business. Top executives have worked in some of the most successful lotteries in the United States – the New York, the New Jersey and Georgia lotteries.

ALICE GARLAND

*Executive Director
North Carolina Education Lottery*

Has seven years of experience with the N.C. Education Lottery. She was named to the lottery's top post in January 2011, serving previously as deputy executive director for legislative and corporate communications. She has a combined 32 years of experience in executive posts handling government affairs and communications.



QUAN KIRK
General Counsel

JAMIE KING FUQUAY
Director of Government Affairs

CAROL JAMES
Director of Human Resources

NIKKI HOWARD
Director of Internal Audit

SALES



SAM HAMMETT

*Deputy Executive Director,
Sales*

Has 19 years of experience with lotteries in Georgia and North Carolina. Responsible for all lottery ticket distribution and sales, including the management of lottery relationships with its retail and corporate partners who sell lottery tickets in 6,800 locations, and the operations of the lottery's six regional claims centers and warehouse.

FINANCE, ADMINISTRATION & SECURITY



BILL JOURDAIN

*Deputy Executive Director,
Finance, Administration
and Security*

Has 36 years of experience with lotteries in New Jersey and North Carolina. Is responsible for oversight of all lottery finances, the administration of contracts, the payout of prizes to winners, the management of lottery facilities, and oversight of lottery security to protect the integrity of its games.

ADVERTISING, MARKETING & COMMUNICATIONS



LOU ANN RUSSELL

*Deputy Executive Director,
Advertising, Marketing
and Communications*

Has 20 years of experience with lotteries in Georgia and North Carolina. Responsible for the development of the lottery's brand and image as well as the promotion of its games through advertising, marketing, product design and public relations.

MANAGEMENT INFORMATION & GAMING SYSTEMS



DEBORAH DOTY

*Deputy Executive Director,
Management Information
and Gaming Systems*

Has 31 years of experience with lotteries in New York and North Carolina. Is responsible for all technology at the lottery and for contract compliance with the lottery's gaming vendors.

TERRI AVERY FOWLER
Director of Field Sales

WALTER INGRAM
Director of Sales Development

MOE McKNIGHT
Director of Security

MICHELLE LASSITER
Director of Finance

STACY ASKEW
Director of Administration

TAMI WIGGS
Director of Marketing

VAN DENTON
Director of Communications

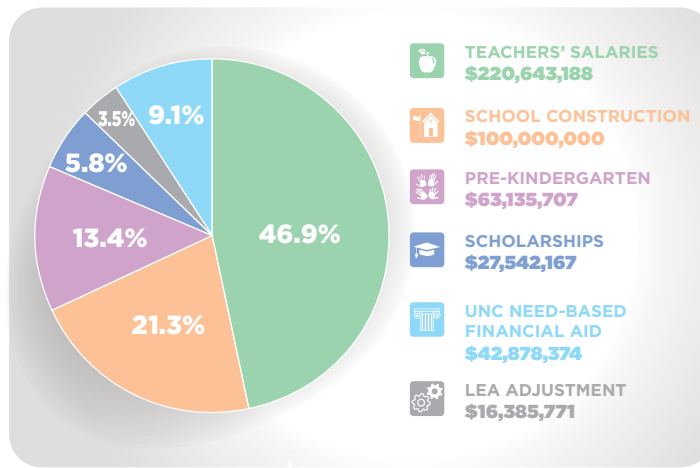
SUSAN SINGLEY
Director of Advertising

RANDY SPIELMAN
Director of Product Development

JOE NORMAN
Director of Gaming Systems

TONY CHUNG
Director of MIS

County	FY13 Total	Seven Year Total
Alamance	7,146,893	40,540,044
Alexander	1,647,859	10,022,780
Alleghany	507,787	3,384,865
Anson	1,304,840	8,881,548
Ashe	1,197,397	7,802,847
Avery	779,733	5,106,421
Beaufort	2,169,891	13,460,921
Bertie	1,033,215	7,167,372
Bladen	1,793,932	12,834,731
Brunswick	4,061,271	23,988,094
Buncombe	9,146,023	49,653,374
Burke	4,228,900	28,400,176
Cabarrus	10,065,945	59,863,661
Caldwell	3,533,530	21,370,420
Camden	550,105	3,513,608
Carteret	2,768,426	15,335,661
Caswell	856,130	5,834,926
Catawba	7,429,838	42,762,379
Chatham	2,653,597	16,401,671
Cherokee	1,177,588	7,156,471
Chowan	737,376	4,626,473
Clay	468,181	2,849,153
Cleveland	5,140,418	34,744,925
Columbus	2,938,801	21,298,934
Craven	4,676,541	25,967,862
Cumberland	17,876,550	115,858,197
Currituck	1,095,170	6,203,951
Dare	1,577,224	8,884,026
Davidson	7,390,799	44,565,077
Davie	2,077,102	13,261,825
Duplin	2,993,413	18,429,348
Durham	10,633,151	61,257,205
Edgecombe	2,749,429	18,244,661
Forsyth	16,559,297	97,075,988
Franklin	2,552,055	15,029,108
Gaston	10,414,068	65,645,732
Gates	538,557	3,653,769
Graham	447,704	2,705,278
Granville	2,492,029	15,839,694
Greene	995,193	7,013,424
Guilford	26,040,826	153,697,541
Halifax	2,669,733	17,431,063
Harnett	5,624,766	34,377,655
Haywood	2,364,227	13,630,278
Henderson	4,060,059	23,023,594
Hertford	1,213,122	7,969,583
Hoke	2,990,042	18,842,351
Hyde	222,238	1,400,557
Iredell	7,880,669	44,325,262
Jackson	1,149,776	7,153,297
Johnston	9,311,772	56,781,741



LOTTERY BENEFITS EDUCATION ALL ACROSS STATE

Nothing is more important than the lottery's mission to maximize the funds available to support specific education programs statewide. Thanks to players, retailers and support from the entire organization, the lottery's performance in fiscal year 2013 resulted in the largest amount of money transferred to education programs in lottery history. Here are highlights of the lottery's beneficiary programs last year:

- Made largest transfer ever in a single year, \$461.3 million to the state to benefit education
- Reached a new overall total of more than \$2.9 billion in transfers since inception
- Increased the amount transferred to the state for the 7th year in a row

The transfers are made quarterly from the lottery to the state. The state then distributes lottery dollars to education programs that the lottery serves. Transfers are not the same as lottery earnings because the final transfer each year occurs before the end of the fiscal year. Additional earnings from sales in the last days of the month are carried over and become part of the transfer in the first quarter of the next fiscal year.

Legislators allocate lottery dollars in the state budget. Here is a review of how lottery dollars were allocated in fiscal year 2013.



TEACHERS' SALARIES

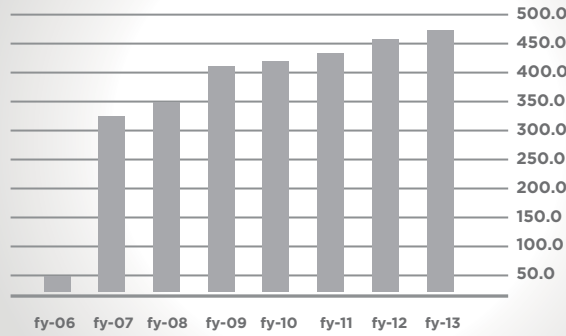
School systems and charter schools across the state received a share of \$220.6 million for teachers' salaries in grades K-3. The money was enough to pay the salaries of 3,784 teachers.

“I love teaching and have been blessed to be able to do it for 28 years. The parents' support and recognition bolstered my spirits and gave me new vigor to continue to do my best.”

- Rebecca Schuit

Third-grade teacher Rebecca Schuit of Black Mountain Primary School in Buncombe County, one of 32 teachers featured in “Thanks to Teachers” segments on WLOS-TV, sponsored by the lottery.

TRANSFERS TO EDUCATION



SCHOOL CONSTRUCTION

Each county in the state received its share of \$100 million allocated for school construction and repairs. County commissioners decide how the money should be used. Lottery dollars are the only source of state funding for school's capital needs and their availability helps to keep property taxes from rising.

“We are thankful to have the lottery funds. It would have been very difficult to achieve this project if we didn't have those dollars available to us.”

- Ronna Gore



Ronna Gore, principal of Old Dock Elementary School in Whiteville in Columbus County, which used \$930,000 in lottery dollars to build a new addition.

N.C. PRE-K

About \$63.1 million went to the Pre-K program, formerly known as More at Four. The program, available in each of the state's 100 counties, serves four-year-olds who are considered to be at risk of falling behind their peers. It provides a year in an academic prekindergarten class to those children with the goal of preparing them for success in kindergarten.



Shani Nelson of Raleigh, who received a lottery scholarship to help her pursue a degree in social work from N.C. Central University.

COLLEGE SCHOLARSHIPS AND FINANCIAL AID

Lottery dollars help North Carolina students cover the costs of going to college. Some \$27.5 million went to provide N.C. Education Lottery Scholarships. The scholarships, awarded to students who qualify for federal Pell Grants, can be used for tuition, fees, room and board, books or supplies. Last year, 27,144 scholarships were awarded.

Another \$42.8 million provided grants to students attending a UNC system school through the UNC Need-Based Grant Program. Lottery dollars provided about 29 percent of the \$144 million provided for UNC need-based financial aid.

“I'm just really appreciative. It makes me want to do my best because I'm so thankful that I was able to receive that scholarship.”

- Shani Nelson

LOCAL EDUCATION AGENCY ADJUSTMENT

For fiscal year 2013, \$16.3 million in lottery funds were allocated to partially offset how much state funding a school system had to return to the state.

County	FY13 Total	Seven Year Total
Jones	494,998	3,427,414
Lee	3,327,485	20,691,754
Lenoir	2,917,160	19,191,299
Lincoln	3,479,084	20,597,340
Macon	1,515,853	9,075,864
Madison	794,418	4,767,060
Martin	1,161,434	7,748,068
Mcdowell	1,940,973	11,893,251
Mecklenburg	43,657,664	254,558,328
Mitchell	580,288	3,869,824
Montgomery	1,424,017	10,005,253
Moore	3,384,455	18,581,208
Nash	4,915,301	31,349,482
New Hanover	8,941,272	50,240,784
Northampton	948,210	6,642,977
Onslow	8,931,618	46,505,958
Orange	5,856,959	33,328,965
Pamlico	495,508	3,190,363
Pasquotank	1,933,402	11,344,006
Pender	2,564,516	14,714,900
Perquimans	568,398	3,578,368
Person	1,635,667	10,753,996
Pitt	8,192,681	48,016,742
Polk	777,523	5,279,890
Randolph	6,634,527	39,162,550
Richmond	2,370,446	16,693,763
Robeson	8,412,180	55,353,202
Rockingham	4,085,699	26,522,722
Rowan	6,035,009	38,558,853
Rutherford	3,032,667	19,386,919
Sampson	3,788,515	24,393,154
Scotland	2,234,994	15,219,805
Stanly	3,114,886	20,638,676
Stokes	2,106,739	14,635,822
Surry	3,460,664	22,842,689
Swain	720,554	4,294,193
Transylvania	1,023,308	6,253,249
Tyrrell	203,202	1,290,603
Union	11,437,619	66,769,724
Vance	2,169,594	14,256,735
Wake	44,206,235	233,641,526
Warren	823,428	5,318,060
Washington	628,619	4,541,354
Watauga	1,710,528	9,235,689
Wayne	6,493,121	42,743,237
Wilkes	3,543,392	23,241,572
Wilson	3,645,814	22,995,246
Yadkin	1,820,954	12,105,487
Yancey	676,824	4,351,598

TOP 20 RETAILER FOR FY 13

RETAILER NAME	RETAILER CITY
Reilly Road BP Amoco	Fayetteville
Rose Mart # 14	Wilson
Winners Food Mart	Roxboro
Carlton's Tanglewood	Clemmons
C Mini Mart # 3	Raleigh
Bobby Taylor Oil # 2	Fayetteville
Raceway	Tarboro
Catamount Travel Center	Whittier
Circus Food Store #6	Durham
Eagles Express	Knightdale
Church Street Convenience Mart	Rocky Mount
Short Stop	Carrboro
Fairway One Stop #21	Greensboro
Ethco Service Station	Engelhard
N & R Convenience Marts Inc	Lumberton
Sunrise Food & Gas	Siler City
Ponderosa Exxon	Fayetteville
Raceway #6743	Charlotte
CJ Food Store	Jacksonville
The Border Station	Moyock

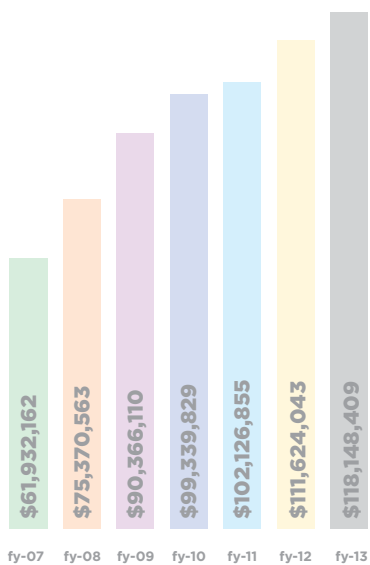
LOTTERY SALES SET RECORD FOR SEVENTH YEAR IN A ROW

Ticket sales are the engine that powers the lottery's performance as a significant and growing fixture of the North Carolina economy. A sales force of more than 100 people service the lottery's retail partners, operating out of headquarters and five regional offices. Retail locations selling lottery tickets include convenience stores, grocery stores, pharmacies and other community-based commercial enterprises. Highlights of lottery sales in FY13 include:

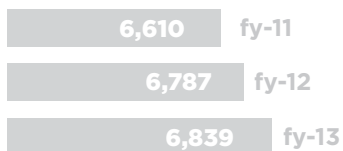
- \$1.69 billion in sales, an increase of 5.8 percent
- \$9.6 billion in total sales since inception
- \$4.6 million in ticket sales per day on average
- \$118 million in retail commissions, \$7 million more than FY12
- Single-day instant ticket activation record of \$6.7 million
- Single-day Powerball ticket sales record of \$12.8 million
- Retail base grew to 6,839 locations, up 1 percent
- New record sales quarter, \$463.6 million, from April 1, 2013 to June 30, 2013

According to an external review conducted by independent auditors, the N.C. Education Lottery is one of just three across the nation to achieve growth in sales every year from 2007 through 2012.

COMMISSIONS



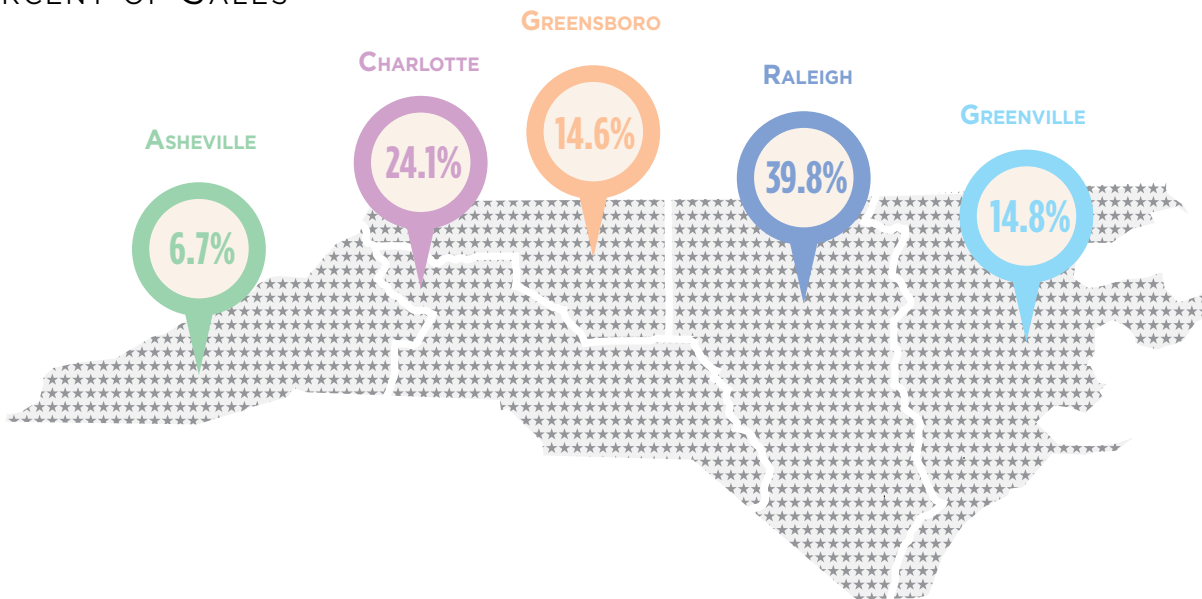
NUMBER OF RETAILERS



FY 2013 SALES BY REGION

	Asheville	Greensboro	Charlotte	Raleigh	Greenville
Instant	\$83,705,569.00	\$156,874,323.00	\$266,348,740.00	\$379,173,624.00	\$125,840,933.00
Powerball	\$14,773,964.00	\$29,264,762.00	\$58,041,336.00	\$73,865,042.00	\$20,997,686.00
Mega Millions	\$4,330,659.00	\$8,535,577.00	\$14,270,968.00	\$20,488,566.00	\$6,039,940.00
Pick 3	\$3,731,969.00	\$29,160,493.50	\$36,506,872.00	\$126,167,530.00	\$63,301,383.00
Pick 4	\$1,610,627.50	\$13,264,975.50	\$16,190,034.50	\$47,714,310.50	\$25,122,167.50
Cash 5	\$4,664,429.00	\$10,437,805.00	\$16,101,176.00	\$25,215,782.00	\$8,061,371.00
TOTAL	\$112,817,217.50	\$247,537,936.00	\$407,459,126.50	\$672,624,854.50	\$249,363,480.50

PERCENT OF SALES



LIFE TO DATE SALES BY FISCAL YEAR

	Instant Games	Powerball	Mega Millions	Pick 3	Pick 4	Cash 5	Raffle	Total
FY 2013 (7/1-6/30)	\$1,011,943,189.00	\$196,942,790.00	\$53,665,710.00	\$258,868,247.50	\$103,902,115.50	\$64,480,563.00		\$1,689,802,615.00
FY 2012 (7/1-6/30)	\$959,955,361.00	\$153,921,894.00	\$85,564,057.00	\$247,751,644.00	\$91,528,197.00	\$57,971,905.00		\$1,596,693,058.00
FY 2011 (7/1-6/30)	\$862,090,476.00	\$138,670,659.00	\$72,847,709.00	\$258,443,414.00	\$65,309,804.00	\$57,757,944.00	\$5,986,380.00	\$1,461,106,386.00
FY 2010 (7/1-6/30)	\$855,582,267.00	\$198,756,717.00	\$25,969,303.00	\$222,777,592.00	\$57,370,252.00	\$60,873,168.00		\$1,421,329,299.00
FY 2009 (7/1-6/30)	\$798,676,404.00	\$209,746,679.00		\$208,883,766.00	\$15,793,159.00	\$60,011,218.00		\$1,293,111,226.00
FY 2008 (7/1-6/30)	\$635,880,115.00	\$229,255,174.00		\$147,158,304.00		\$58,516,249.00	\$7,369,240.00	\$1,078,179,082.00
FY 2007 (7/1-6/30)	\$494,314,534.00	\$258,967,883.00		\$89,541,216.50		\$36,501,699.00	\$10,000,000.00	\$889,325,332.50
FY 2006 (03/30-06/30)	\$198,454,677.00	\$27,317,594.00						\$225,772,271.00
Life to Date	\$5,816,897,023.00	\$1,413,579,390.00	\$238,046,779.00	\$1,433,424,184.00	\$333,903,527.50	\$396,112,746.00	\$23,355,620.00	\$9,655,319,269.50

DAILY AVERAGE

	Instant Games	Powerball	Mega Millions	Pick 3	Pick 4	Cash 5	Raffle	Total
FY 2013 (7/1-6/30)	\$2,772,447.09	\$539,569.29	\$147,029.34	\$709,228.08	\$284,663.34	\$176,659.08		\$4,629,596.22
FY 2012 (7/1-6/30)	\$2,622,828.86	\$420,551.62	\$233,781.58	\$676,917.06	\$250,077.04	\$158,393.18		\$4,362,549.34
FY 2011 (7/1-6/30)	\$2,361,891.72	\$379,919.61	\$199,582.76	\$708,064.15	\$178,930.97	\$158,240.94	\$16,401.04	\$4,003,031.19

FEELING LUCKY?

The strategy behind the “Feeling Lucky” advertising campaign was to promote the overall playing of the lottery’s instant games rather than sales of a single game.



INSTANT TICKET SALES EXCEED \$1 BILLION MARK FOR FIRST TIME

For the first time in its history, the N.C. Education Lottery achieved a key milestone of instant ticket sales exceeding \$1 billion. Instant games are the most popular with North Carolina lottery players, accounting for about 60 percent of all sales. Highlights of instant ticket sales in fiscal year 13 included:

- Increasing instant ticket sales by 5.4 percent
- Becoming only the 12th U.S. lottery to achieve \$1 billion in instant tickets sales in a year
- Launching 49 new instant games, ranging in price from \$1 to \$20, during the year

The \$1 billion goal was part of a plan created two years ago by the Education Lottery as it sought to improve instant ticket sales. The central strategy of the plan aligned sales, advertising, marketing and game design behind the shared \$1 billion sales goal. The plan took steps to improve the overall portfolio of instant games and their prizes, to create more effective sales practices, including how instant tickets are allocated and then sold in stores, and to strengthen the advertising and marketing programs supporting instant games.

“The North Carolina Education Lottery recently announced results for fiscal year 2013. The real-attention getter was rocketing up to \$1 billion instant ticket sales in less time than any other state except for Texas and California, and those are states with triple the population base of North Carolina.”

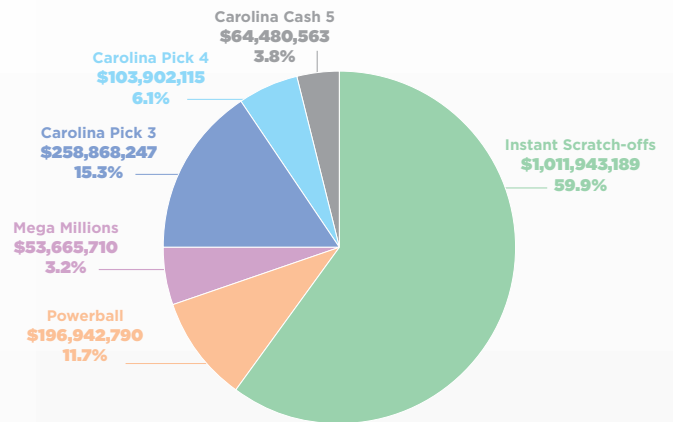
- Public Gaming International



The \$10 game headlined a series of four new instant games, launched in August 2012, which offered players the chance to win as much as \$5,000 a week for life. The Week for Life games provided the highest prizes ever offered for instant games at those price points.



In March 2013, four instant scratch-off games based on the popular board game MONOPOLY went on sale. Players could also enter non-winning tickets into monthly second-chance drawings for cash prizes.



NEW AND IMPROVED GAMES HELP BOOST SALES

The lottery's products are prizes. Our prizes come from games ranging from the two big multi-state jackpot games, Powerball and Mega Millions, to North Carolina draw games including Carolina Cash 5, Carolina Pick 4, and Carolina Pick 3, to a portfolio of instant scratch-off games with prices from \$1 to \$20. Lottery tickets provide inexpensive fun that can pay off big for players.

GAME LAUNCHES

- Released 49 new instant scratch-off games into the marketplace
- Launched fourth \$20 instant game, \$4,000,000 Gold Bullion, with three top prizes of \$4 million and seven prizes of \$1 million
- Launched four new instant games that offered players the chance to win as much as \$5,000 a week for life. The guaranteed value of the prizes represent the largest ever offered on instant tickets at \$1, \$2, \$5, and \$10 per play
- Released new licensed games. One was an officially licensed Star Trek scratch-off ticket that gave players five chances to win \$20,000 instantly and offered a second-chance drawing for a trip to the annual Star Trek convention in Las Vegas. A suite of four MONOPOLY games offered prizes up to \$1 million and multiple second-chance drawings for cash prizes

RECORD POWERBALL JACKPOT

- Powerball ticket sales and returns to the state were helped by two major jackpots including a \$590.5 million jackpot in May, the largest of the game's history. During the May jackpot's roll, sales exceeded \$38 million in the state, generating \$14.6 million for education. More than 556,000 tickets won prizes totaling more than \$8 million, including four \$40,000 prizes and 17 \$10,000 prizes. Retailers across the state earned more than \$2.6 million in commissions from Powerball sales.

SUM IT UP

- The NCEL added the "Sum It Up" feature to Pick 3 and Pick 4 in February. This feature allows players to win if the sum of their three/four numbers matches the sum of the numbers drawn, even if the numbers themselves do not match. For an extra .50 or \$1, Pick 3 players can win as much as \$500 and Pick 4 players can win as much as \$5,000 in addition to their regular ticket winnings.





ADVERTISING AND MARKETING DESIGNED TO SHARE THE FUN WITH EVERYONE

WINNING CAMPAIGNS

Advertising continued to play a central role in generating ticket sales that enabled the lottery to raise money for education. Ads are how many North Carolinians are introduced to new games and become informed about the lottery's mission. Strategic planning of game messages, media schedules and production services translated into cohesive campaigns integrated with marketing efforts throughout the lottery. Highlights include:

- Summer-long tourism program along the coast intended to reach vacationers
- Creating awareness for the \$1 and \$2 instant scratch-off games
- Instant scratch-off branding campaign called "Feeling Lucky"
- Updated corporate redesign to include fresh, new colors for sales reps' vans and point of sale
- Boosting the profile of Carolina Cash 5 with "Tonight Could be Your Day" TV and radio spots
- Channels for the lottery's beneficiary message included TV, radio and print advertising



Executive Director Alice Garland with two-time NCEL 200 winner Kyle Busch.

BIG PROMOTIONS

The lottery's marketing promotions program is designed to connect with the public at live events. By supporting fairs and festivals and being a part of the fun at both local and professional sporting events, the lottery has the opportunity to reach a broader audience.

- Marketing staff on-site for 35 events in FY13, up 25%
- Nine university sponsorships added, bringing total to 11
- For a sixth straight year, title sponsor of the NCEL 200 NASCAR Camping World Truck Series Race
- For the first time, brought the action of the NCEL 200 to the Rockingham Speedway
- High-profile partnerships with Carolina Hurricanes, Charlotte Bobcats and Carolina Panthers



REWARDING EXPERIENCES

Today, customers expect opportunities to get more value from the brands they like the most. That's why, with the addition of a player loyalty program on Oct. 1, 2012, the NCEL reached an important milestone. The program, called Lucke-Rewards, allows players to earn points by entering non-winning instant-scratch-off tickets and all winning and non-winning draw game tickets online. Players can use the points they accrue to enter weekly and monthly drawings for as much as \$25,000 and other prizes, such as iPads or tailgating gear.

- 352,769 - membership at close of FY13
- 138,997 - average entries made per monthly drawing

BONUS OPPORTUNITIES

A series of Green Ball Bonus Draws gave Pick 3 players the chance to win bonus cash during a four-week span in July 2012. The Green Ball appeared 4 times, boosting the prize payout to the lucky winners. A special promotion called Cash 5 Bonus Bucks also started in FY13. It gave Carolina Cash 5 players extra chances to win as much as \$50,000.



A new Toyota Tundra was added to the \$50,000 grand prize for one of the drawings. Esther Hall, a home healthcare professional from Salisbury, was the winner.

SOCIAL STATS






25,992 - Total "Likes" on Facebook
4,462 - Total followers on Facebook



297,319 - Total page views on Lucke-Zone blog

SPOTLIGHTING TEACHERS

Each week of the school year, three television stations in North Carolina do a weekly feature spotlighting the work great teachers do in their communities. The programs producing the weekly stories on teachers are sponsored by the lottery. The stations and their programs are:

"Teacher of the Week"	"Thanks to Teachers"	"Teacher of the Week"
		
(Triangle Region) 39 stories last school year	(Western North Carolina) 32 stories last school year	(Eastern North Carolina) 40 stories last school year

SPORTING EVENTS

- Carolina Panthers
- Charlotte Bobcats
- Carolina Hurricanes
- Charlotte Checkers

MINOR LEAGUE BASEBALL

- Durham Bulls
- Kannapolis Intimidators
- Hickory Crawdads
- Asheville Tourists
- Carolina Mudcats
- Greensboro Grasshoppers

RACING EVENTS

- Bank of America 500
- Dollar General 300
- NHRA Four-Wide Nationals
- NCEL 200 NASCAR Camping World Truck Series Race
- NASCAR Sprint All-Star Race
- World of Outlaws Finals and Spring Car Showdown at the Dirt Track
- NASCAR History 300
- NASCAR Coca-Cola 600

COLLEGIATE EVENTS

- Duke University
- Wake Forest University
- North Carolina State University
- University of North Carolina at Chapel Hill
- Appalachian State University
- East Carolina University
- Western Carolina University
- University of North Carolina at Wilmington
- University of North Carolina at Charlotte
- North Carolina A&T State University
- Fayetteville State University
- ACC Basketball Tournament
- Southern Conference Tournament
- CIAA Basketball Tournament

FAIRS & FESTIVALS

- Cabarrus County Fair, Concord
- Cleveland County Fair, Shelby
- Dixie Classic Fair, Winston-Salem
- Historic Morganton Festival, Morganton
- N.C. Seafood Festival, Morehead City
- Ray Price Capital City Bikefest, Raleigh
- Mumfest, New Bern
- Riverfest, Wilmington
- Barbecue Festival, Lexington
- BBQ & Blues, Charlotte
- Azalea Festival, Wilmington
- Dogwood Festival, Fayetteville
- Speed Street and Taste of Charlotte, Charlotte
- Food Lion Auto Fair, Charlotte



"I'm a little more retired now," said Rusty Hunter of Pfafftown. To win it - what I won - is like 'Whoa.'"

FORTY-NINE PLAYERS WIN \$1 MILLION OR MORE

Our players like that the lottery raises money for education, but they buy a lottery ticket hoping to win a prize. In interviews with winners, most say they plan to use their winnings to pay bills, save for retirement or college for their kids, to donate to a favorite charity, to buy houses or cars, or to take a vacation. Prize money seems in many cases to be flowing right back into the state's economy.

- Allocated 60% of lottery revenues to prizes
- Twenty-six players won \$1 million or more playing instant games; 17 won playing Powerball; four won playing Mega Millions; one won playing Carolina Cash 5; and one came with a second-chance drawing in the Holiday Millions instant game. Those winners lived in 27 North Carolina counties
- Paid out on average \$2.6 million a day in prizes

WINNING EXPERIENCES

- Rusty Hunter of Pfafftown won \$4 million, the largest guaranteed instant prize in NCEL history and the biggest of 2013 playing the \$4,000,000 Gold Bullion game. The self-employed handyman purchased a new Chevy Silverado pick-up truck and plans to buy an Airstream trailer. Hunter added that he would like to buy a vacation home in the mountains where he can go hunting and fishing and spend time with his dad.
- Emily Stone of Denver won the largest second-chance prize ever, \$3 million, in a second-chance drawing. The drawing was open to those entering their non-winning Holiday Millions instant tickets into the drawing.

*"These winners chose to take a chance, and won big. The opportunity to win big prizes is a huge reason why many North Carolinians enjoy playing the lottery."
- Alice Garland, executive director of the Education Lottery.*



- Homer Buffaloe, a farmer from Zebulon, won a \$1,144,821 Carolina Cash 5 jackpot, the largest ever won by a single ticket. This was the second time he'd matched all five numbers in a Cash 5 drawing. The first occurred in Nov. 2010 when he claimed half of a \$408,066 jackpot.
- Esther Hall, a home healthcare professional from Salisbury, won a \$50,000 prize and a new 2013 Toyota Tundra in the lottery's Carolina Cash 5 Bonus Bucks drawing.

BIG WINS WITH DRAWINGS

Players of Carolina Pick 3 and Carolina Pick 4 won big in FY13 when the popular combinations of "Trips" and "Quads" were drawn.

TRIPS			
Date	Day/Evening	Winning Numbers	Prize Amount
Aug. 11, 2012	Day	777	\$1,675,000
Sept. 5, 2012	Evening	444	\$2,164,500
Sept. 15, 2012	Day	999	\$1,383,000
Oct. 23, 2012	Evening	999	\$714,250
Oct. 30, 2012	Day	222	\$1,619,000
Dec. 9, 2012	Evening	888	\$3,754,500
Dec 19, 2012	Evening	111	\$2,530,500
May 13, 2013	Day	777	\$1,809,267
June 14, 2013	Day	444	\$2,153,945
QUADS			
Date	Day/Evening	Winning Numbers	Prize Amount
Aug. 11, 2012	Evening	1111	\$7,500,000
Nov. 21, 2012	Evening	3333	\$6,602,500
April 20, 2013	Evening	2222	\$7,463,450



Each March, during National Problem Gambling Awareness Week, the Education Lottery suspends advertising on games and uses instead a responsible play message.



GROWING LOTTERY RESPONSIBLY IS ONE OF LOTTERY'S TOP GOALS

The N.C. Education Lottery is committed to meeting the lottery industry's best practices in the area of responsible gaming. For guidance, it follows standards outlined by the National Association of State and Provincial Lotteries and the World Lottery Association's Responsible Gaming Framework. Highlights in fiscal year 2013 included:

- Provided \$1 million to the N.C. Department of Health and Human Services for gambling addiction, education and treatment programs
- Created a new responsible play advertisement. The ad plays each March during National Problem Gambling Awareness Week in lieu of advertising supporting sales and games
- Sponsored the National Conference on Problem Gambling and participated in the council's campaign during the 2012 holiday season to raise public awareness that lottery tickets should not be given as gifts to children

KEY ELEMENTS OF LOTTERY'S RESPONSIBLE GAMING PROGRAM

At retail locations: All marketing materials carry a play responsibly message with the toll-free number for the N.C. Problem Gambling Helpline. Play centers are stocked with problem gambling brochures. Pencils used by lottery players at the play centers carry the name of the program and its toll-free numbers. Slide shows on video monitors at 4,200 retail locations include slides with a play responsibly message and a "No Sales To Minors" message.

With lottery tickets: All lottery tickets, both instant and draw, carry the play responsibly message and the toll-free numbers for the problem gambling helpline. The odds of winning a breakeven prize are printed on the back of every instant ticket.

On advertising: All NCEL advertising carry a play responsibly message and provide to viewers the toll-free number for the problem gambling helpline.



On the NCEL website: The odds of winning lottery prizes are provided for every instant game and on How-To-Play pages for draw games. Information about prizes remaining at all levels of all instant games is updated daily. Resources about problem gambling and responsible play are provided on a dedicated Play Responsibly page. A collection of Play Responsibly advertisements are displayed on the website's Video Center.

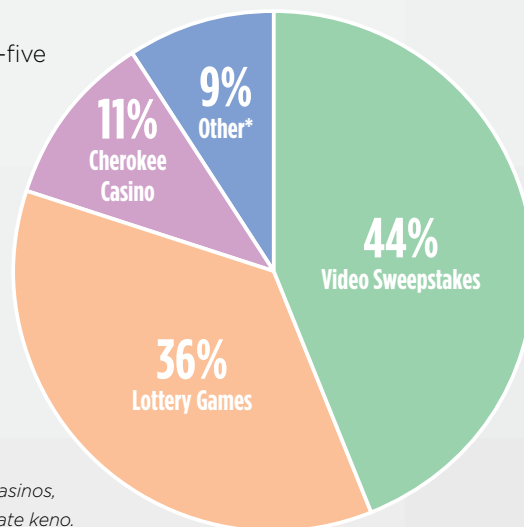
In education: The NCEL's support of the N.C. Problem Gambling Program gives it the financial means to offer an evidence-based curriculum, "Stacked Deck," at middle schools and high schools for the prevention of problem gambling among students and young adults.

KEY FACTS ON PROBLEM GAMBLING IN NORTH CAROLINA

In an annual report to the N.C. Education Lottery Commission, the N.C. Problem Gambling Program reported:

- Problem gambling affects nearly 2.1 percent of adult population, based on the 2010 North Carolina Behavioral Risk Factors Surveillance Survey.
- Of 5,754 callers to the North Carolina Problem Gambling helpline, 721 problem gamblers and family members received services. Seventy-five percent of callers reported they were problem gamblers and 25 percent were family members or friends of a problem gambler.
- Breakdown of callers showed gender as 51 percent male and 49 percent female and race as 52 percent Caucasian, 42 percent African-American, and 6 percent Asian and Hispanic.

WHAT CALLERS REPORTED AS PRIMARY PROBLEM GAMBLING ACTIVITY.



**Online gaming, sports betting, out-of-state casinos, private card games, or out-of-state keno.*

Report of Independent Auditor

To the Commissioners
North Carolina Education Lottery
Raleigh, North Carolina

Report on the Financial Statements

We have audited the accompanying statements of net position of the North Carolina Education Lottery ("NCEL"), a major enterprise fund of the state of North Carolina, as of and for the years ended June 30, 2013 and 2012, and the related statements of revenues, expenses and changes in net position and cash flows, and notes to the financial statements which collectively comprise the NCEL's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit 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 financial statement presentation of the financial statements.

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the NCEL as of June 30, 2013 and 2012, and the respective changes in financial position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 2, the financial statements present only the NCEL and do not purport to and do not present fairly the financial position of the state of North Carolina as of and for the years ended June 30, 2013 and 2012, and the changes in its financial position and its cash flows thereof for the years then ended in conformity 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 as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not a required part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated September 27, 2013, on our consideration the NCEL's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants agreements, and other matters. The purpose of the 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 NCEL's internal control over financial reporting and compliance.



Raleigh, North Carolina
September 27, 2013

NORTH CAROLINA EDUCATION LOTTERY

Management's Discussion & Analysis - June 30, 2013 & 2012

The following is a discussion and analysis of the financial performance of the North Carolina Lottery Commission [aka, North Carolina Education Lottery (NCEL)] for the fiscal years ended June 30, 2013, 2012 and 2011 and should be read in conjunction with the financial statements, including the footnotes. This report consists of three parts: management's discussion and analysis, the basic financial statements and the notes to the financial statements. Included below and on the following pages are the financial highlights, summary of contributions to the state, and summary results of operations for the fiscal years ended June 30, 2013, 2012 and 2011.

Financial Highlights

For fiscal year 2013, gross ticket sales totaled \$1.69 billion representing a \$93.1 million increase over fiscal year 2012. Total operating income was \$480 million, which represented an increase of \$19.2 million over fiscal year 2012. Other significant financial highlights included the following:

- North Carolina General Statute Section 18C-164 (a) requires the NCEL to transfer net proceeds from operations and any prior year surplus to the State of North Carolina at least four times a year. In fiscal year 2013, the sum total of these cash transfers was \$461.4 million, the largest annual total for cash transfers in NCEL's history. Total cash transfers for fiscal years 2012 and 2011 were \$456.8 million and \$446.9 million, respectively.
- Awarded \$1 million or more to an NCEL player for the 129th time.
- Increased the number of retailers to 6,839, representing a 1% increase over the prior year, and provided service to our retailers on a regular basis.
- Released 49 new instant scratch-off games into the marketplace generating gross instant ticket sales of \$1.01 billion.

Overview of the Financial Statements

This financial report is designed to inform the public and other interested parties of the financial results of the NCEL and show its accountability in meeting the legislated mandate to generate funds to further the goal of providing enhanced educational opportunities. Accordingly, the focus of the financial statements is to determine funds available for payment to the State's Education Lottery Fund. It is important to note that most financial statement balances have a direct or indirect relationship to revenue. As lottery sales increase, the amount paid to the State's Education Lottery Fund also increases. Similarly, increases in revenues generally result in direct increases to cost of sales including, but not limited to, prize expense, retailer commission expense and gaming system vendor charges.

The NCEL is a major enterprise fund of the primary government of the State of North Carolina. The financial statements were prepared on the accrual basis of accounting in a manner similar to a private business entity. The principal operating revenues of the NCEL are sales of lottery products, by contracted retailers, to the general playing public. Operating expenses include the cost of prizes, retailer commissions, gaming system vendor charges, personnel, and other administrative expenses.

Included in this report are the Statements of Net Position as of June 30, 2013 and 2012, the Statements of Revenues, Expenses, and Changes in Net Position for the periods ended June 30, 2013 and 2012, and the Statements of Cash Flows for the periods ended June 30, 2013 and 2012.

The NCEL transfers its net revenues to the Office of State Budget and Management (OSBM) for credit to the Education Lottery Fund. Education Lottery funds are distributed by OSBM based on the budgeted distribution of lottery net revenue as recommended by the General Assembly.

Total Assets

Total assets at the end of fiscal year 2013 were \$111 million compared to \$96 million at the end of fiscal year 2012, representing an increase of \$15 million.

Current assets increased from \$48 million in 2012 to \$60 million in 2013, representing an increase of \$12 million. This growth resulted from an increase in Pooled Cash due to fiscal year 2013 and 2012 surplus earnings held to be dispersed in the subsequent fiscal year. In addition, there was an increase in the State Treasurer's Securities Lending Collateral. More detailed information can be found in Note 2D in the financial statements. The increase was also partially caused by an increase in accounts receivable in 2013 from 2012. This primarily represents amounts due from retailers for ticket sales less commissions and prizes paid by the retailers. The increase is essentially due to the timing of the end of the accounting week for billing and collections from our retailers at fiscal year end. Electronic Funds Transfer is used to collect receivables weekly from retailer bank accounts that are set up in trust for the NCEL.

Current assets were also affected by a \$404 thousand increase in investments in annuity contracts.

The Short Term Investment portfolio has the general characteristics of a demand deposit account in that participants may deposit additional cash at any time and may withdraw cash at any time without prior notice or penalty. All deposits are combined with other State agencies and invested by the State Treasurer until needed to cover disbursements. Investments are limited to those authorized for the State's General Fund, pursuant to NC

Management's Discussion & Analysis - June 30, 2013 & 2012

General Statute 147-69.1. Interest earned of \$417 thousand on these balances is recorded as non-operating revenue. Earnings on the accounts are credited on a monthly basis. The allocable share of the revenues arising from State Treasurer's Securities Lending Collateral program transactions are also included as non-operating revenue.

The NCEL's investment in capital assets, net of accumulated depreciation in 2013 was \$897 thousand which is approximately \$225 thousand higher than 2012. The investment in capital assets includes game equipment, data processing equipment, telephone equipment, software and fixtures. The capitalization of all items including equipment, computers, and furniture follows the Office of the State Controller's (OSC) policy. The NCEL defines capital assets as assets with an initial unit cost of \$5,000 or greater and an estimated useful life of two or more years. Capital assets are carried at cost less accumulated depreciation.

Additional information on the NCEL's capital assets can be found in Notes 2F and 5E to the financial statements.

The activity for capital assets for the year ended June 30, 2013 was (in thousands):

<u>Category</u>	<u>Balance July 1, 2012</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance June 30, 2013</u>
Capital assets, depreciable				
Furniture	\$ 29	\$ 17	\$ -	\$ 46
Equipment	3,076	553	-	3,629
Motorized equipment	67	-	-	67
Total capital assets, depreciable	<u>3,172</u>	<u>570</u>	<u>-</u>	<u>3,742</u>
Less accumulated depreciation for:				
Furniture	29	2	-	31
Equipment	2,403	343	-	2,746
Motorized equipment	68	-	-	68
Total accumulated depreciation	<u>2,500</u>	<u>345</u>	<u>-</u>	<u>2,845</u>
Total capital assets, depreciable, net	<u>672</u>	<u>225</u>	<u>-</u>	<u>897</u>
Capital assets, net	<u>\$ 672</u>	<u>\$ 225</u>	<u>\$ -</u>	<u>\$ 897</u>

Total Liabilities

Total current liabilities for the NCEL were \$61 million in 2013 increasing by \$12 million from 2012. The growth in current liabilities mainly resulted from increases in due to other funds and the obligations under State Treasurer's security lending collateral agreements. The increase in due to other funds can be attributed to the timing of transactions encountered in the normal course of business. The increase in the obligations under State Treasurer's security lending collateral is directly related to the NCEL having more cash on hand at year-end. Current liabilities also consist of prize awards payable, and other payables.

Noncurrent liabilities are Accrued Paid Time Off or Compensated Absences. A liability is recorded to reflect the balances for unpaid Paid Time Off (PTO) earned, which is provided to employees for use whenever vacation, sick leave, personal leave or bereavement leave is requested and approved. Current and noncurrent liability for Accrued Paid Time Off is shown below in thousands.

<u>Beginning</u>	<u>Earned</u>	<u>Used</u>	<u>Ending</u>	<u>Current Liabilit</u>	<u>Long Term Portion</u>
<u>\$ 1,228</u>	<u>\$ 1,666</u>	<u>\$ 1,546</u>	<u>\$ 1,348</u>	<u>\$ 291</u>	<u>\$ 1,057</u>

Noncurrent liabilities also includes the present value of the annuity contracts that fund the long term installment prizes that are due to NCEL annuity prize winners that will be paid after June 30, 2014.

Net Position and Changes in Net Position

As required in the North Carolina State Lottery Act, net revenues of the NCEL are transferred quarterly to the NC Education Lottery Fund at the Office of State Budget and Management. At year end, Net Revenues/Position are zero for the NCEL. There are no changes in the Net Position from year to year.

Condensed Statement of Net Position (in thousands)

	2013	2012	2011
ASSETS			
Total Current Assets	\$ 59,643	\$ 48,484	\$ 30,345
Noncurrent Assets	51,605	47,337	36,586
Total Assets	<u>111,248</u>	<u>95,821</u>	<u>66,931</u>
LIABILITIES			
Total Current Liabilities	60,525	49,338	30,217
Noncurrent Liabilities	50,723	46,483	36,714
Total Liabilities	<u>111,248</u>	<u>95,821</u>	<u>66,931</u>
NET POSITION			
Net Investment in Capital Assets	897	672	819
Unrestricted	<u>(897)</u>	<u>(672)</u>	<u>(819)</u>
Total Net Position	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

Current liabilities consist of "Due to Other Funds" in the amount of \$27.317 million. Of this amount, \$27.253 million represents the remaining amount of the "Net Revenues" and "50% of Unclaimed Prizes" for Fiscal Year 2013 not yet transferred to the State of North Carolina as of June 30, 2013. These funds will be transferred to the state during Fiscal Year 2014. The remainder is due to other state agencies for services provided to the NCEL. Additional information on "Due to Other Funds" is found in Note 6D to the financial statements.

Revenues

Operating revenues consist of gross sales, fees and licenses net of prize tickets.

Sales

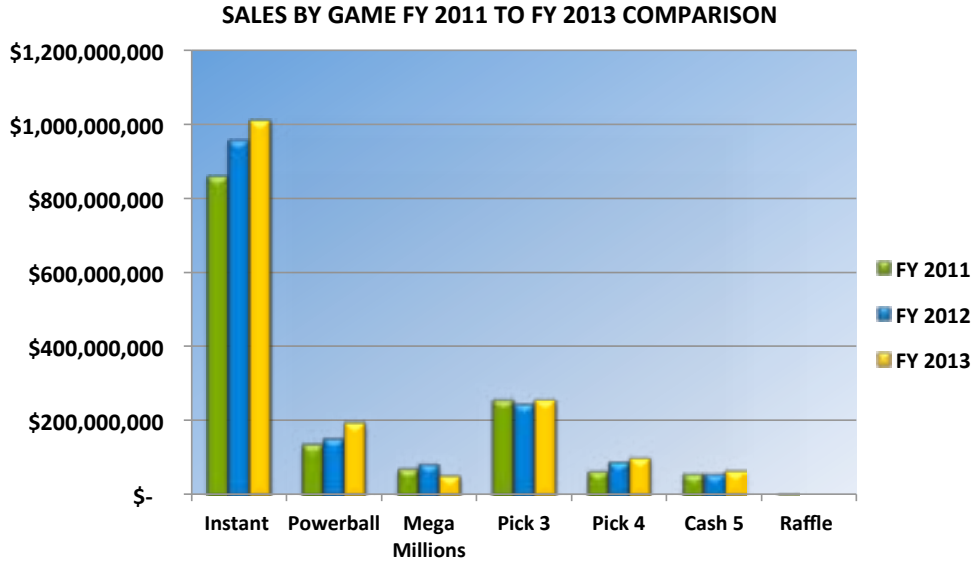
The gross lottery ticket sales for fiscal year 2013 totaled \$1.69 billion as compared to \$1.597 billion for fiscal year 2012 and \$1.461 billion in fiscal year 2011. This represents an increase of \$93 million from 2012 and \$229 million from 2011.

Gross instant ticket sales were \$1.01 billion for fiscal year 2013 compared with \$960 million for fiscal year 2012 and \$862 million in fiscal year 2011, an increase of approximately \$50 million from fiscal year 2012 and approximately \$148 million from fiscal year 2011. The increase realized during fiscal year 2013 is attributable to several factors. The NCEL continued with its third \$20 instant scratch-off mega game, \$4 Million Cash Blowout, with a prize payout of 75%, which generated over \$63 million in sales during fiscal year 2013. In addition the NCEL launched its fourth \$20 instant scratch-off mega game, \$4 Million Gold Bullion, which generated over \$54 million in sales. The NCEL also launched its "A Week for Life" family of tickets, with games available at four price points from \$10 and below, which combined generated sales of over \$121 million. The NCEL released several very successful licensed games during the year. The Star Trek Instant Scratch-Off was introduced and provided players the chance to win a grand prize trip package, including VIP access to the Star Trek convention in Las Vegas. The NCEL launched its suite of Instant Monopoly Scratch-Off licensed games, with Monopoly games at four price points under \$10 resulting in over \$40 million in sales. In addition, other licensed instant games released such as "Bejeweled Money Multiplier" also proved to be very popular.

Draw game sales were \$678 million for fiscal year 2013 compared to \$637 million for fiscal year 2012 and \$599 for fiscal year 2011, representing a \$41 million increase from fiscal year 2012 and a \$79 million increase from fiscal year 2011. Draw game sales benefited from high jackpots in the multi-state game Powerball. The Powerball jackpot reached over \$500 million twice during the fiscal year, which helped increase Powerball sales to \$197 million, from \$153 million the previous year. The Carolina Cash 5 top prize exceeded half a million dollars eight times during the fiscal year and

reached over \$1 million once, resulting in increased draw sales. The Carolina Pick 4 game also had increased sales from the previous year. Carolina Pick 4 sales were over \$103.9 million compared to \$91.5 million the previous year.

The following chart depicts the distribution of sales by product for the fiscal years ended June 30, 2013, 2012 and 2011.



Non-operating Revenues mainly consist of investment earnings on Short Term Investment Fund (STIF) accounts and security lending transactions, and Multi-State Lottery Association (MUSL) dividends received.

Expenses

Section 18C-162, NC General Statute stipulates that no more than 8% of the total annual revenues shall be allocated for payment of expenses of the Lottery. Advertising expenses shall not exceed 1% of the total annual revenues.

The following charts show the major components of NCEL operating expenses and transfers as a percentage of total revenues for the fiscal years ended June 30, 2013, 2012 and 2011.



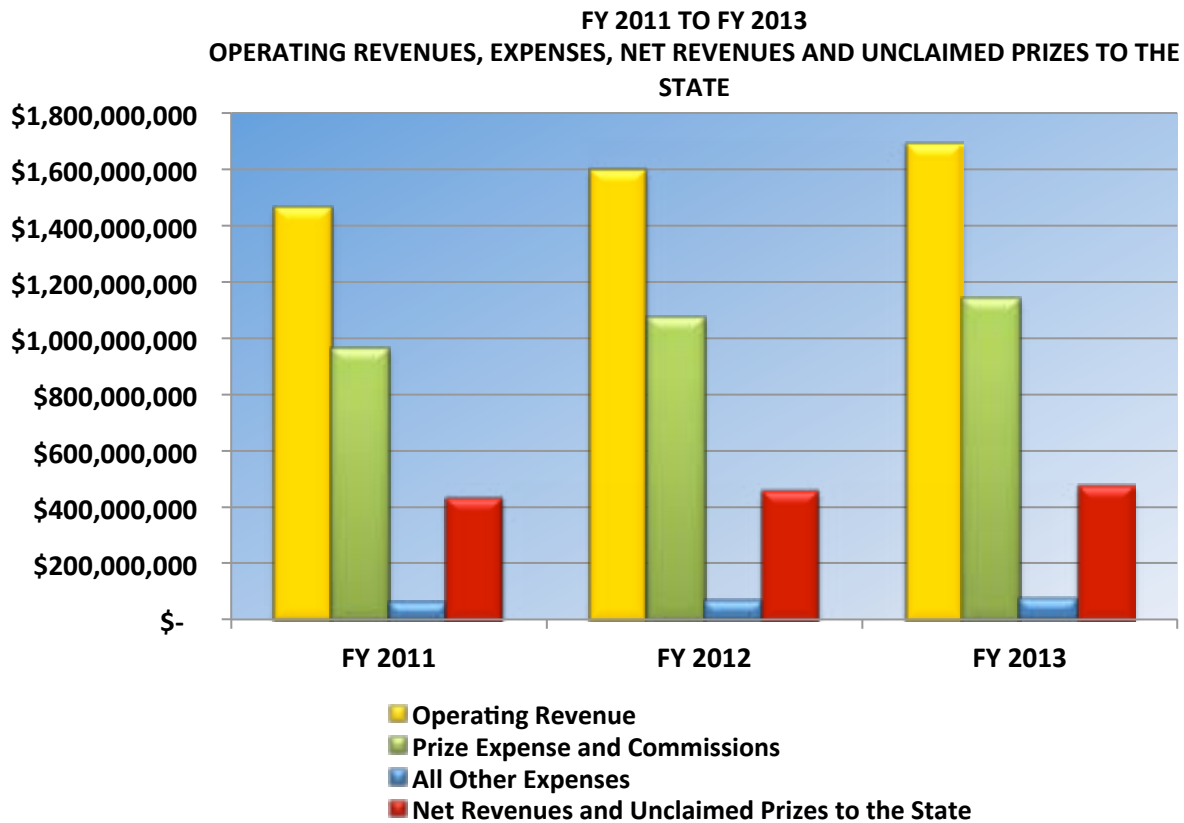
Prizes, commissions and gaming vendor charges all directly relate to sales. As expected, as sales have increased so have these expenses. In fiscal year 2013 total gaming expenses which consist of prizes, retailer commissions and gaming vendor charges (gaming system services), totaled \$1,170 million as compared to \$1,099 million and \$989 million for fiscal years 2012 and 2011, respectively. Other operating expenses, which consist of advertising and marketing, salary and benefits, professional fees, rent, maintenance, depreciation and general administrative expenses increased to \$46.1 million in fiscal year 2013, as compared with \$42.7 million and \$39.9 million for fiscal years 2012 and 2011, respectively. Other operating expenses represented 2.7%, 2.6% and 2.7% of total operating revenues in fiscal years 2013, 2012 and 2011, respectively.

NORTH CAROLINA EDUCATION LOTTERY
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2013 and 2012

Condensed Statement of Revenues, Expenses and Changes in Net Position (in thousands)

	2013	2012	2011
Operating Revenues:			
Gross Sales:	\$ 1,689,803	\$ 1,596,693	\$ 1,461,106
Less: Prize Tickets	-	(181)	(1,375)
Less: Sales/Service Bad Debt	(90)	(55)	(152)
Fees and Licenses	5,296	5,381	5,061
Total Operating Revenues	<u>1,695,009</u>	<u>1,601,838</u>	<u>1,464,640</u>
Operating Expenses:			
Gaming Expenses:			
Lottery Prizes	1,024,437	961,556	862,996
Retailer Commissions	118,148	111,624	102,127
Gaming Systems Services	27,262	26,031	23,482
Total Gaming Expenses	<u>1,169,847</u>	<u>1,099,211</u>	<u>988,605</u>
Other Operating Expenses	46,078	42,700	39,905
Total Operating Expenses	<u>1,215,925</u>	<u>1,141,911</u>	<u>1,028,510</u>
Operating Income	<u>479,084</u>	<u>459,927</u>	<u>436,130</u>
Nonoperating Revenues (Expenses):			
Investment Earnings, Nonoperating Revenue (Expense) and Compulsive Gambling Contribution	(576)	(458)	111
Net Revenues and Unclaimed prizes to the State	(478,508)	(459,469)	(436,241)
Total Nonoperating Revenue (Expenses)	<u>(479,084)</u>	<u>(459,927)</u>	<u>(436,130)</u>
Change in Net Position	<u>-</u>	<u>-</u>	<u>-</u>
Net Position Beginning July 1	<u>-</u>	<u>-</u>	<u>-</u>
Net Position Ending June 30	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

From fiscal year 2011 to fiscal year 2013, the NCEL has achieved annual increases in revenues and transfers to the State. The following graph depicts these trends.



Budget and Economic Outlook

On June 4, 2013, the NCEL Commission approved the Fiscal Year 2014 budget for the NCEL to provide a projected \$462 million to the State's Education Lottery Fund. This projected budget is a 4.5% increase over the fiscal year 2013 budget that reflected a \$442 million transfer to the State's Education Lottery Fund. The NCEL will continue to monitor the current economic conditions in the State, and its impact upon lottery ticket sales. As per the General Assembly Fiscal Research Division: "Since the economic slowdown last spring, the State's economy has steadily been gaining strength. While we do not anticipate the pace of economic growth to significantly quicken, we do expect it to stay on a steady upward trend." Also "The economy is on solid footing on most fronts, and improvements in the State's employment growth means the recovery will move along a sturdier track." Therefore, the NCEL has constructed an increasing but conservative budget and sales forecast for the upcoming fiscal year.

A focus of the NCEL Commission is to ensure sound operations. The existence of this focus is apparent in the opinions issued by external audit firms. For the seventh consecutive year, the State Auditor contracted with an outside CPA firm to conduct the fiscal year financial audit, which resulted in an unmodified opinion.

Requests for Information

Any request for information about this report should be sent to the Public Information Officer at the North Carolina Education Lottery, 2100 Yonkers Road, Raleigh, North Carolina 27604.

FINANCIAL STATEMENTS - JUNE 30, 2013 & 2012

NORTH CAROLINA EDUCATION LOTTERY

Statements of Net Position (in thousands)
June 30, 2013 and 2012

	2013	2012
ASSETS		
Current Assets:		
Cash and Cash Equivalents:		
Cash	\$ 99	\$ 119
Pooled Cash	32,386	26,381
Receivables:		
Accounts Receivable	17,774	14,797
Interest Receivable	18	39
Investment in Annuity Contracts	4,154	3,750
Inventory	-	4
Prepaid Items	381	335
State Treasurer's Security Lending Collateral	4,831	3,059
Total Current Assets	59,643	48,484
Noncurrent Assets:		
Investment in Annuity Contracts	49,666	45,417
Prepaid Items	1,042	1,248
Capital Assets, Depreciable (Net):		
Furniture and Equipment	3,742	3,172
Accumulated Depreciation	(2,845)	(2,500)
Total Capital Assets, Depreciable (Net)	897	672
Total Assets	111,248	95,821
LIABILITIES		
Current Liabilities:		
Accounts Payable	23,572	31,611
Accrued Payroll	431	412
Other Liabilities	-	263
Annuity Prize Award Payable - Current	4,154	3,750
Accrued Paid Time Off - Current	291	162
Due to Other Funds	27,317	10,175
Obligations Under State Treasurer's Security Lending Agreements	4,760	2,965
Total Current Liabilities	60,525	49,338
Noncurrent Liabilities:		
Annuity Prize Award Payable	49,666	45,417
Accrued Paid Time Off	1,057	1,066
Total Liabilities	111,248	95,821
NET POSITION		
Net Investment in Capital Assets	897	672
Unrestricted	(897)	(672)
Total Net Position	\$ -	\$ -

See Notes to the Financial Statements.

FINANCIAL STATEMENTS - JUNE 30, 2013 & 2012

NORTH CAROLINA EDUCATION LOTTERY

Statements of Revenues, Expenses and Changes in Net Position (in thousands)
Years Ended June 30, 2013 and 2012

	2013	2012
Operating Revenues:		
Gross Sales:	\$ 1,689,803	\$ 1,596,693
Less: Prize Tickets	-	(181)
Less: Sales/Service Bad Debt	(90)	(55)
Fees and Licenses	5,296	5,381
Total Operating Revenues	1,695,009	1,601,838
Operating Expenses:		
Salaries, Wages, and Benefits	17,540	16,639
Lottery Prizes	1,024,437	961,556
Retailer Commissions	118,148	111,624
Retailer Incentive	781	609
Gaming Systems Services	27,262	26,031
Advertising	15,278	14,696
Marketing	3,540	2,512
Other Services	4,802	4,634
Furniture, Fixtures, and Equipment	1,307	762
Depreciation	346	457
Other General and Administrative Expenses	2,484	2,391
Total Operating Expenses	1,215,925	1,141,911
Operating Income	479,084	459,927
Nonoperating Revenues (Expenses):		
Investment Earnings	417	523
Compulsive Gambling Contribution	(1,000)	(1,000)
Unclaimed Prizes to NC Education Lottery Fund	(11,381)	(11,083)
Net Revenues to the State of NC	(467,127)	(448,386)
Miscellaneous Nonoperating Revenues (Expenses)	7	19
Total Nonoperating Revenues (Expenses)	(479,084)	(459,927)
Change in Net Position	-	-
Net Position Beginning, July 1	-	-
Net Position Ending, June 30	\$ -	\$ -

See Notes to the Financial Statements.

FINANCIAL STATEMENTS - JUNE 30, 2013 & 2012

NORTH CAROLINA EDUCATION LOTTERY

Statements of Cash Flows (in thousands)
Years Ended June 30, 2013 and 2012

	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from Customers	\$ 1,573,884	\$ 1,485,286
Payments to Employees and Fringe Benefits	(17,401)	(16,827)
Payments for Prizes, Benefits and Claims	(1,032,548)	(948,310)
Payments to Vendors and Suppliers	(55,480)	(51,955)
Other Receipts/Payments	25	-
	<u>468,480</u>	<u>468,194</u>
Net Cash Flows Provided from Operating Activities		
CASH USED FOR NONCAPITAL FINANCING ACTIVITIES		
Transfers to State	(461,367)	(456,765)
Transfers to Other State Agencies	(1,000)	(1,000)
	<u>(462,367)</u>	<u>(457,765)</u>
Total Cash Used for Noncapital Financing Activities		
CASH USED FOR CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition and Construction of Capital Assets	(570)	(311)
	<u>(570)</u>	<u>(311)</u>
Total Cash Used for Capital and Related Financing Activities		
CASH PROVIDED FROM INVESTING ACTIVITIES		
Investment Earnings	442	605
	<u>442</u>	<u>605</u>
Total Cash Provided from Investing Activities		
Net Increase/(Decrease) in Cash and Cash Equivalents	5,985	10,723
Cash and Cash Equivalents at Beginning of Year	26,500	15,777
Cash and Cash Equivalents at End of Year	<u>\$ 32,485</u>	<u>\$ 26,500</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating Income	\$ 479,084	\$ 459,927
Adjustments to Reconcile Operating Income to Cash Provided by Operating Activities:		
Depreciation Expense	345	457
Other Nonoperating Income	26	3
(Increase) Decrease in Assets:		
Accounts Receivable	(2,977)	(4,900)
Inventories	4	12
Prepaid Items	160	(1,404)
Increase (Decrease) in Liabilities:		
Accounts Payable	(8,039)	14,052
Accrued Payroll and Related Liabilities	19	(254)
Other Liabilities	(142)	301
	<u>\$ 468,480</u>	<u>\$ 468,194</u>
Total Cash Provided by Operating Activities		
NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES		
Assets Acquired through the Assumption of a Liability	\$ 6,425	\$ 12,013
Change in Fair Value of Investments	22	72

See Notes to the Financial Statements.

NOTE 1 - ORGANIZATION

The North Carolina State Lottery Commission [aka, North Carolina Education Lottery (NCEL)] was created with the enactment of House Bill 1023, effective August 31, 2005, as an independent, self-supporting, and revenue-raising agency of the State of North Carolina (the State). The NCEL commenced operations on March 30, 2006 with the sale of instant scratch-off tickets. In March 2006, the NCEL joined the Multi-State Lottery Association (MUSL) composed of a group of U.S. lotteries that combine jointly to sell POWERBALL lottery tickets. POWERBALL sales began on May 30, 2006. Additional draw games were introduced as follows:

- Carolina Pick 3 on October 6, 2006
- Carolina Cash 5 on October 27, 2006
- Carolina Pick 3 second daily draw (Monday through Saturday) on March 31, 2008
- Carolina Pick 4 on April 17, 2009
- Mega Millions on January 31, 2010
- Carolina Pick 4 second daily draw and Carolina Pick 3 second Sunday draw on February 27, 2011

The purpose of the NCEL is to generate funds to further the goal of providing enhanced educational opportunities, support school construction, and fund college and university scholarships. The operations of the NCEL are overseen by a nine member commission, five of whom are appointed by the Governor and four of whom are appointed by the General Assembly.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**A. Reporting Entity:**

For financial reporting purposes, the North Carolina Education Lottery is a major enterprise fund of the primary government of the State of North Carolina and is reported as such in the *Comprehensive Annual Financial Report* (CAFR) of the State. These financial statements for the NCEL are separate and apart from those of the State of North Carolina and do not present the financial position of the State nor changes in the State's financial position and cash flows.

B. Basis of Presentation:

The financial statements are prepared on the accrual basis of accounting in a manner similar to a private enterprise. The NCEL elected to apply all applicable Governmental Accounting Standards Board (GASB) pronouncements as well as Accounting Principles Board (APB) opinions. GASB Statement No. 62 incorporates into the GASB's authoritative literature the applicable guidance previously presented in the following pronouncements issued before November 30, 1989: 1) Financial Accounting Standards Board (FASB) Statements and Interpretations, 2) Accounting Principles Board Opinions, and 3) Accounting Research Bulletins of the American Institute of Certified Public Accountants' (AICPA) Committee on Accounting Procedure. The guidance generally has been taken "as-is" from the original FASB and AICPA pronouncements, except a few provisions that have been modified where necessary to relate specifically to the governmental environment.

As an enterprise fund, the NCEL is accounted for using the "economic resources" measurement focus. This means that all the assets and liabilities related to its operations are included on its statement of net position, and its operating statement includes all revenues (increases) and expenses (decreases) in net position. The NCEL distinguishes operating from non-operating revenues and expenses. Operating revenues and expenses generally relate to the NCEL's primary ongoing operations of selling lottery tickets and redeeming prizes; all revenues and expenses not meeting this definition are reported as non-operating. The principal operating revenues of the NCEL are for the sales of lottery products. The significant operating expenses include the cost of prizes, commissions, gaming system vendor charges, personnel, advertising and other administrative expenses.

C. Cash and Cash Equivalents:

Cash and cash equivalents include regional office deposited operating funds, imprest funds, and deposits held by the State Treasurer in the State Treasurer's Short Term Investment portfolio. The Short Term Investment portfolio maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit additional cash at any time and also may withdraw cash at any time without prior notice or penalty.

D. State Treasurer's Securities Lending Collateral:

While the NCEL does not directly engage in securities lending transactions, it deposits certain funds with the State Treasurer's Short Term Investment Fund which participates in securities lending activities. Based on the State Treasurer's allocation of these transactions, the NCEL recognizes its allocable share of the assets and liabilities related to these transactions on the accompanying financial statements as "State Treasurer's Securities Lending Collateral" and "Obligations Under State Treasurer's Securities Lending Agreements." The NCEL's allocable share of these assets and liabilities is based on the NCEL's year-end deposit balance per the State Treasurer's records.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Based on the authority provided in General Statute 147-69.3(e), the State Treasurer lends securities from its investment pool to brokers-dealers and other entities (borrowers) for collateral that will be returned for the same securities in the future. The Treasurer's securities custodian manages the securities lending program. The Treasurer's custodian lent U.S. government and agency securities, FNMA's, corporate bonds and notes for collateral. The Treasurer's custodian is permitted to receive cash, U.S. government and agency securities, or irrevocable letters of credit as collateral for the securities lent.

The collateral is initially pledged at 102 percent of the market value of the securities lent, and additional collateral is required if its value falls to less than 100 percent of the market value of the securities lent. There are no restrictions on the amount of loans that can be made. Substantially all security loans can be terminated on demand by either the State Treasurer or the borrower.

Additional details on the State Treasurer's securities lending program are included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.nc.gov/> and clicking on "Financial Reports," or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

E. Allowance for Doubtful Accounts:

An allowance for doubtful accounts has not been established because there are no indications of significant delinquencies from the collection of retailer accounts as of June 30, 2013 and 2012.

F. Capital Assets:

The NCEL defines capital assets as assets with an initial unit cost of \$5,000 or greater and an estimated useful life of two or more years. This definition conforms to the policy of the NC Office of State Controller. Depreciation is computed using the straight-line method over the estimated lives of the assets. The NCEL uses the half year convention. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation will be removed from the books and any resulting gain or loss reflected in operations of the period of disposal. Capital assets are carried at cost less accumulated depreciation. The estimated useful lives by general category are as follows:

Category	Years
Equipment	5-7
Furniture	5
Computers and Software	3-5

G. Game Revenue Recognition:

For the NCEL's draw games, POWERBALL, Mega Millions, Carolina Cash 5, Carolina Pick 4, Carolina Pick 3, and raffles offered, revenue is recognized at the time of sale on a daily basis. For instant games, revenue is recognized at the time a pack of tickets is settled (See Note 3A.1).

H. Lottery Prize Expense Recognition:

For POWERBALL, Mega Millions, Carolina Cash 5, Carolina Pick 4, Carolina Pick 3, and for raffles, prize expense is recorded at 50 percent of sales on a daily basis. For instant games, prize expense is accrued based on the final production prize structure percentage provided by the gaming vendor for each game and recorded daily on the value of packs settled. Certain games include free tickets (prize tickets) which entitle the holder to exchange one instant ticket for another of equal value. For the instant games with prize tickets, the final prize structure percentage used is adjusted to eliminate the value of the prize tickets. Prize expense for merchandise prizes is recognized as prizes are fulfilled.

I. 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 of assets and liabilities and disclosure of contingent assets and liabilities as of the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

NOTE 3 – REVENUE**A. Operating Revenue:****1. Game Revenue:**

Instant packs are settled using the following methodology:

- Manually by the retailer initiating a settlement transaction via the gaming terminal.
- Automatically by the gaming system - twenty one (21) days after pack activation.
- Automatically by the gaming system - once the fifth (5th) pack in a specific game is activated by a retailer, the oldest active pack is settled.

Operating revenues are reduced by the value of prize tickets validated during a period.

Game Revenue	2013	2012
Instant	\$ 1,011,943	\$ 959,955
Prize tickets	-	(181)
Draw	677,860	636,738
Bad debt write off	(83)	(51)
Damaged tickets, sales services	(7)	(4)
Total	<u>\$ 1,689,713</u>	<u>\$ 1,596,457</u>

2. Fees and Licenses:

The majority of Fees and Licenses represent a weekly retailer communication fee charged to active retailers for terminal satellite communications and an application fee for new retailers and changes in ownership. Total Fees and Licenses for fiscal year 2013 and 2012 were \$5,296 and \$5,381, respectively.

B. Non-operating Revenue:

The cash accounts of the NCEL are Short Term Investment Fund (STIF) Accounts which are interest bearing accounts held with the NC State Treasurer. Investments are limited to those authorized for the State's General Fund, pursuant to NC General Statute 147-69.1. The investment earnings earned on these accounts and the related security lending collateral transactions is \$417 and \$523 for the years ended June 30, 2013 and 2012, respectively.

The NCEL also has miscellaneous non-operating revenue related to dividends received from MUSL which were \$26 and \$50 for the years ended June 30, 2013 and 2012, respectively. The remaining miscellaneous non-operating revenue consists of sales and marketing materials to other lotteries and other miscellaneous items.

NOTE 4 – EXPENSES**A. Operating Expenses:****1. Lottery Prize Expense:**

Prize Expense	2013	2012
Instant	\$ 685,202	\$ 642,075
Draw	327,854	308,398
50% of unclaimed prizes	11,381	11,083
Total	<u>\$ 1,024,437</u>	<u>\$ 961,556</u>

NOTE 4 – EXPENSES (continued)

2. Retailer Commissions

Commissions	2013	2012
Instant	\$ 70,735	\$ 67,092
Draw	47,413	44,532
Total	<u>\$ 118,148</u>	<u>\$ 111,624</u>

3. Retailer Incentives:

In fiscal year 2010, the State Lottery Commission approved a retailer incentive program where retailers would receive compensation for selling a top/second tier prize in the Multi-State games POWERBALL and Mega Millions and a top tier prize in Carolina Cash 5. As of December 2011, the retailer incentive program was expanded to include instant ticket prizes of over \$1 million as well. The total payments issued for the retailer incentive program for fiscal years 2013 and 2012 were \$781 and \$609, respectively.

4. Other Services:

The principal expenses included are: security services, background checks, communications, legal services, travel, financial audit services, network support, and costs for temporary employees. The Other category under Other Services also includes payments issued to Alcohol and Law Enforcement (ALE) in the amount of \$948 in fiscal year 2013 and \$933 in fiscal year 2012.

	2013	2012
Security services	\$ 12	\$ 11
Background checks	1,016	977
Communications, including wiring	1,201	1,250
Legal services	158	94
Travel	149	133
Other	2,266	2,169
Total	<u>\$ 4,802</u>	<u>\$ 4,634</u>

5. Furniture, Fixtures, and Equipment:

To operate a lottery, numerous items of equipment, furniture, and ticket dispensers are required. Most of these items were one time purchases to be replaced as needed at various points in the future. These items were also below our threshold for capitalization (See Note 5E) and therefore expensed. The total expenses for fiscal years 2013 and 2012 were \$1,307 and \$762, respectively.

6. Leases – Buildings, Offices and Other Equipment:

The NCEL has entered into various operating leases through the North Carolina State Department of Administration for building and office facilities. These leases are for initial terms of seven to ten years.

Projected lease payments for these facilities are:

Year Ending	Amount
2014	\$ 1,145
2015	1,161
2016	1,150
2017	272
2018	227
2019-2023	429
Total	<u>\$ 4,384</u>

The total space rental costs for the fiscal years 2013 and 2012 were \$1,096 and \$1,091, respectively. The NCEL also has several contracts for various equipment leases including instant ticket vending machines (ITVM's).

NOTE 4 – EXPENSES (continued)**B. Non-operating Expenses:**

The allocable share of the expenses arising from State Treasurer's Securities Lending Collateral program transactions, totaling \$18 and \$31 for the years ended June 30, 2013 and 2012, respectively, are included as non-operating expense. For the years ended June 30, 2013 and 2012, the remaining non-operating expenses consist of other miscellaneous non-operating items.

C. Transfers Out:

There were three significant transfers from the NCEL. One million dollars was transferred to the NC Department of Health and Human Services for a gambling addiction education and treatment program as stipulated in the North Carolina State Lottery Act for the years ended June 30, 2013 and 2012 (See Note 7D).

The second transfer was \$11,381 and \$11,083 for the years ended June 30, 2013 and 2012, respectively, from unclaimed prizes during the year. The North Carolina State Lottery Act requires the NCEL to transfer "Fifty percent (50%)" of unclaimed prizes to the NC Education Lottery Fund each year (See Note 7C).

The third transfer was in compliance with the North Carolina State Lottery Act. This Act requires all "Net Revenues" of the NCEL to be transferred to the NC Education Lottery Fund for the educational purposes set forth in the legislation. "Net Revenues" were \$467,127 for fiscal year 2013 compared with \$448,386 for fiscal year 2012 (see Note 12). However, \$439,875 was transferred to the NC Education Lottery Fund for fiscal year 2013 compared with \$438,283 for fiscal year 2012. The balances remaining (\$27,253 and \$10,103 for fiscal years 2013 and 2012) were recorded as a payable to the State for both fiscal years and were transferred subsequent to fiscal year end. NC General Statute 18C-162 states: "The funds remaining in the North Carolina State Lottery Fund after receipt of all revenues to the Lottery Fund and after accrual of all obligations of the Commission for prizes and expenses shall be considered to be the net revenues of the North Carolina State Lottery Fund."

NOTE 5 – ASSETS**A. Cash:**

The cash and cash equivalents balances at June 30, 2013 and 2012 include no undeposited receipts on hand.

Unless specifically exempt, the NCEL is required by North Carolina General Statute 147-77 to deposit moneys received with the State Treasurer or with a depository institution in the name of the State Treasurer. Except as noted above, all NCEL funds are deposited with the State Treasurer. The NCEL has no deposit policy concerning credit risk, as all deposits are held by the State Treasurer.

At June 30, 2013 and 2012, respectively, \$32,386 and \$26,381 of the amounts shown on the Statement of Net Position as cash and cash equivalents represents the NCEL's equity position in the State Treasurer's Short Term Investment Fund. The Short Term Investment Fund (a portfolio within the State Treasurer's Investment Pool, an external investment pool that is not registered with the Securities and Exchange Commission and does not have a credit rating) had a weighted average maturity of 1.6 and 1.5 years, as of June 30, 2013 and 2012, respectively. Assets and shares of the Short Term Investment Fund are valued at amortized cost, which approximates fair value.

Deposit and investment risks associated with the State Treasurer's Investment Pool (which includes the State Treasurer's Short Term Investment Fund) are included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.nc.gov/> and clicking on "Financial Reports" or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

B. Accounts Receivable:

Accounts Receivable primarily represents amounts due from retailers ticket sales less commissions and prizes paid by the retailers. Electronic Funds Transfer is used to collect receivables weekly from retailer bank accounts that were set up in trust for the NCEL.

C. Inventory:

Inventory for the NCEL consists of all merchandise prizes that are paid for before distribution. Inventory is reduced as prizes are fulfilled. Inventory as of June 30, 2013 and 2012 was \$0 and \$4, respectively.

D. Investments in Annuity Contracts:

Investments in Annuity Contracts represent the present value of the contracts that fund the long term installment prizes contracted through insurance company annuities (See Note 7B). The current and long term balances are \$4,154 and \$49,666 for fiscal year 2013 and \$3,750 and \$45,417 for fiscal year 2012, respectively.

NOTE 5 – ASSETS (continued)

The policies of the NCEL only allow for direct purchase of annuity contracts from which the proceeds are used to fund long term installment prizes. As the NCEL is not pursuing other forms of investments, they are not currently anticipated under the policy. As a means of limiting exposure to interest rate risk, the policy only allows for direct purchase of annuity contracts which future value payments are pre-negotiated with the providers of the contracts. These contracts are not subject to foreign currency risk because the provider is required by contract to pay the full annuities. Accordingly, the NCEL does not have a policy regarding foreign currency risk since investments in products subject to this risk are not applicable to the NCEL.

The policy of the NCEL restricts direct purchase of annuity contracts to those with companies that hold minimum ratings as follows: AA by Fitch, Aa by Moody's or AA by Standard & Poor's. As of June 30, 2013, all annuities carried a rating of Aa/AA.

Maturities for investments in annuity contracts are as follows:

<u>Maturities</u>	<u>2013</u>	<u>2012</u>
Less than 1 year	\$ 4,154	\$ 3,750
1 to 5 years	20,640	18,750
6 to 10 years	20,640	18,750
More than 10 years	8,386	7,917
Total	<u>\$ 53,820</u>	<u>\$ 49,167</u>

E. Capital Assets:

The activity for capital assets for the year ended June 30, 2013 was:

<u>Category</u>	<u>Balance July 1, 2012</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance June 30, 2013</u>
Capital assets, depreciable				
Furniture	\$ 29	\$ 17	\$ -	\$ 46
Equipment	3,076	553	-	3,629
Motorized equipment	67	-	-	67
Total capital assets, depreciable	<u>3,172</u>	<u>570</u>	<u>-</u>	<u>3,742</u>
Less accumulated depreciation for:				
Furniture	29	2	-	31
Equipment	2,403	343	-	2,746
Motorized equipment	68	-	-	68
Total accumulated depreciation	<u>2,500</u>	<u>345</u>	<u>-</u>	<u>2,845</u>
Total capital assets, depreciable, net	<u>672</u>	<u>225</u>	<u>-</u>	<u>897</u>
Capital assets, net	<u>\$ 672</u>	<u>\$ 225</u>	<u>\$ -</u>	<u>\$ 897</u>

The activity for capital assets for the year ended June 30, 2012 was:

<u>Category</u>	<u>Balance July 1, 2011</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance June 30, 2012</u>
Capital assets, depreciable				
Furniture	\$ 29	\$ -	\$ -	\$ 29
Equipment	2,804	310	(38)	3,076
Motorized equipment	67	-	-	67
Total capital assets, depreciable	<u>2,900</u>	<u>310</u>	<u>(38)</u>	<u>3,172</u>
Less accumulated depreciation for:				
Furniture	27	2	-	29
Equipment	1,991	450	(38)	2,403
Motorized equipment	63	5	-	68
Total accumulated depreciation	<u>2,081</u>	<u>457</u>	<u>(38)</u>	<u>2,500</u>
Total capital assets, depreciable, net	<u>819</u>	<u>(147)</u>	<u>-</u>	<u>672</u>
Capital assets, net	<u>\$ 819</u>	<u>\$ (147)</u>	<u>\$ -</u>	<u>\$ 672</u>

Equipment expenditures for 2013 and 2012 included replacements of aged instant ticket dispensers and computer server equipment.

NOTE 6 – LIABILITIES**A. Accounts Payable:**

This primarily represents trade payables to vendors, prize liabilities, and multi-state game low-tier liability. At year end, June 30, 2013 and 2012, the balances were:

<u>Account Type</u>	<u>2013</u>	<u>2012</u>
Trade payables to vendors and other	\$ 4,074	\$ 3,926
Instant prize liability	8,518	8,889
Prize liability – unused unclaimed prizes	7,976	11,223
Multi state games low-tier liability	2,843	4,438
Prize liability – breakage	161	3,135
Total Accounts Payable	<u>\$ 23,572</u>	<u>\$ 31,611</u>

B. Other Liabilities:

Other liabilities of \$0 and \$263 for the years ended June 30, 2013 and 2012, respectively, primarily consist of federal and state withholding on prize payments, various clearing accounts, and deferred revenue.

C. Annuity Prize Awards Payable:

Annuity prize awards payable represents the present value of the contracts that fund the long term installment prizes that are due to NCEL annuity prize winners (See Note 7B). The current and long term balances are \$4,154 and \$49,666 for fiscal year 2013 and \$3,750 and \$45,417 for fiscal year 2012, respectively.

Annuity activity for both short and long term accounts during fiscal year 2013 are as follows:

	<u>Beginning Balance</u>	<u>Purchases</u>	<u>Annuity Appreciation</u>	<u>Annuity Disbursements</u>	<u>Reclass to Short Term</u>	<u>Ending Balance</u>
Short Term	\$ 3,750	\$ -	\$ -	\$ (3,750)	\$ 4,154	\$ 4,154
Long Term	45,417	7,188	1,215	-	(4,154)	49,666
Total	<u>\$ 49,167</u>	<u>\$ 7,188</u>	<u>\$ 1,215</u>	<u>\$ (3,750)</u>	<u>\$ -</u>	<u>\$ 53,820</u>

Annual activity for both short and long term accounts during fiscal year 2012 are as follows:

	<u>Beginning Balance</u>	<u>Purchases</u>	<u>Annuity Appreciation</u>	<u>Annuity Disbursements</u>	<u>Reclass to Short Term</u>	<u>Ending Balance</u>
Short Term	\$ 3,000	\$ -	\$ -	\$ (2,700)	\$ 3,450	\$ 3,750
Long Term	35,620	11,484	1,763	-	(3,450)	45,417
Total	<u>\$ 38,620</u>	<u>\$ 11,484</u>	<u>\$ 1,763</u>	<u>\$ (2,700)</u>	<u>\$ -</u>	<u>\$ 49,167</u>

D. Due to Other Funds:

As explained in Note 4C, \$27,253 and \$10,103 for the years ended June 30, 2013 and 2012, respectively, represent the amounts of the “Net Revenues” for the year not yet transferred to the State as of June 30, but will be transferred to the State subsequent to fiscal year-end. The remainder is due to other state agencies for services provided to the NCEL.

E. Accrued Paid Time Off:

Paid time off (PTO) is provided to employees for use whenever vacation, sick leave, personal leave or bereavement leave is requested and approved. Under this policy, every calendar year, on January 1st, a specific amount of PTO will be credited to Directors’ and above PTO accounts. All other employees’ PTO accounts will be credited on a monthly basis as earned. Employees must be employed at least one year to receive pay for accrued leave balances. Directors and above will be paid out accrued leave balances upon separation provided they have attained a minimum of six (6) months of service on the date of separation.

Activity for the year ended June 30, 2013:

<u>Beginning</u>	<u>Earned</u>	<u>Used</u>	<u>Ending</u>	<u>Current Liability</u>	<u>Long Term Portion</u>
<u>\$ 1,228</u>	<u>\$ 1,666</u>	<u>\$ 1,546</u>	<u>\$ 1,348</u>	<u>\$ 291</u>	<u>\$ 1,057</u>

NOTE 6 – LIABILITIES (continued)

E. Accrued Paid Time Off:

Activity for the year ended June 30, 2012:

<u>Beginning</u>	<u>Earned</u>	<u>Used</u>	<u>Ending</u>	<u>Current Liability</u>	<u>Long Term Portion</u>
\$ 1,162	\$ 1,323	\$ 1,257	\$ 1,228	\$ 162	\$ 1,066

NOTE 7 – OTHER IMPORTANT ITEMS

A. Deposits with Multi-State Lottery Association (MUSL):

MUSL is a voluntary association created for the purpose of administering joint, multi-jurisdictional lottery games, such as POWERBALL and Mega Millions. As of June 30, 2013, MUSL included 33 state lotteries, the District of Columbia and the U.S. Virgin Islands. The chief executive officer of each member lottery serves on the MUSL board of directors.

As a member of MUSL, the NCEL is required to contribute to various prize reserve funds maintained by MUSL. These contributions are included in the 50% prize expense calculated on POWERBALL and Mega Millions sales. The net amount of the 50% prize expense less the amount required to pay low-tier prizes within the State is paid to MUSL. This payment is to cover the NCEL's share of current jackpot prizes based on the NCEL's percent of sales for each drawing and the NCEL's share of the prize reserve fund. The prize reserve fund serves as a contingency reserve to protect all MUSL members including the NCEL from unforeseen prize liabilities. All prize reserve funds remitted, and the related interest earnings, will be returned to the NCEL upon leaving MUSL, less any portion of unanticipated prize claims which may have been paid from the fund. As of June 30, 2013 and 2012 the NCEL had been credited with \$9,992 and \$10,094, respectively, in the MUSL prize reserve funds.

B. Annuity Installment Prizes:

The NCEL funds long term installment prizes through the purchase of insurance company annuities. The contract holders will fund the future value of the installment prize awards over the life of the prize awarded to the player. The NCEL currently holds contracts with Met Life Insurance Company and Prudential Life Insurance Company to provide these future prize installment payments. The future value of the annuity prizes awarded as of June 30, 2013 and 2012 were \$67,982 and \$64,550, respectively.

C. Unclaimed Prizes:

As of June 30, 2013 and 2012, the NCEL had unclaimed prizes from both online and instant games. The first POWERBALL draw after the NCEL started selling tickets was on May 31, 2006, and therefore, the NCEL began recognizing unclaimed prizes on November 27, 2006 (180 days after the first draw). The first Carolina Pick 3 unclaimed prizes were recorded on April 4, 2007 and the first unclaimed prizes for Carolina Cash 5 were recorded on April 25, 2007. Unclaimed prizes for Carolina Pick 4 were recorded on November 14, 2009. Unclaimed prizes for Mega Millions were recorded on August 1, 2010. The NCEL closed forty-nine instant games during fiscal year 2013 resulting in \$11,435 in unclaimed prizes. In 2012, the NCEL closed forty-six instant games resulting in \$10,226 in unclaimed prizes.

<u>Game Type</u>	<u>2013</u>	<u>2012</u>
Instant	\$ 11,435	\$ 10,226
Powerball	5,025	5,998
Mega Millions	1,723	1,314
Carolina Cash 5	1,434	1,418
Carolina Pick 4	1,410	1,452
Carolina Pick 3	1,735	1,758
Total unclaimed prizes	\$ 22,762	\$ 22,166

D. Compulsive Gambling Contribution:

The North Carolina General Statute states that, the NCEL must make "a transfer of \$1,000 annually to the Department of Health and Human Services (DHHS) for gambling addiction education and treatment programs." (See Note 4C)

E. Limitations on Operating and Advertising Expenses:

As established in North Carolina General Statute 18C-162(a)(3); "No more than eight percent (8%) of the total annual revenues, as described in this Chapter, shall be allocated for payment of expenses of the Lottery. Advertising expenses shall not exceed one percent (1%) of the total annual revenues." The one percent for advertising expenses is included in the eight percent maximum for Lottery expenses. Total annual revenues include proceeds from the sale of lottery tickets, interest earned by the NCEL, and all other funds credited to the Lottery from any source.

NOTE 8 – RISK MANAGEMENT

The NCEL is exposed to various risks of loss related to torts; theft of, damage to, and the destruction of assets; errors and omissions; injuries to employees; and natural disasters. The NCEL participates in the State's Risk Management Program for property, liability, crime and automobile coverage, and pays an annual premium for this coverage. The Lottery has not experienced any losses during the year ended June 30, 2013.

The types of coverage, limits, and deductibles, as of June 30, 2013, are described below (the following chart is not shown in thousands).

Coverage Type	Limits (\$)	Deductible (\$)	Comments
Public officers and employee liability	1,000,000 /10,000,000	The first 150,000 /1,000,000 per person are paid by the Commission.	State is self-insured up to \$1,000,000; excess up to \$10,000,000 is with a private insurer.
All risk – property contents	4,697,880	5,000	
Auto – liability	1,000,000 per person/10,000,000 per accident		
Auto – comp/collision	29,470	50 100	Comp. deductible Collision deductible
Theft, disappearance, destruction	250,000	2,500	Inside premises
Theft, disappearance, destruction	50,000	2,500	Outside premises
Computer fraud	5,000,000	75,000	+10% over \$75,000
Employee dishonesty	5,000,000	75,000	+10% over \$75,000
Forgery and alteration	100,000	2,500	
Robbery and safe burglary – money/securities	500,000	1,000	

Employees and retirees are provided health care coverage by the State of North Carolina's Comprehensive Major Medical Plan. This employee benefit plan is funded by employer and employee contributions.

The North Carolina Workers' Compensation Program provides benefits to workers injured on the job. All employees of the State are included in the program. When an employee is injured, the NCEL's primary responsibility is to arrange for and provide the necessary treatment for work related injury. The State is self-insured for workers' compensation. A third-party administrator processes workers' compensation claims. State agencies, including the NCEL, contribute to a fund administered by the Office of the State Controller to cover their workers' compensation claims. The third party administrator receives a per case administration fee and draws down State funds to make medical and indemnity payments on behalf of the State in accordance with the North Carolina Workers' Compensation Act.

Term life insurance of \$25 to \$50 is provided to eligible employees. This self-insured death benefit program is administered by the North Carolina Department of the State Treasurer and funded via employer contributions. The employer contribution rate was .16% of covered payroll for the current fiscal year.

Additional details on State-administered risk management programs are disclosed in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.nc.gov/> and clicking on "Financial Reports" or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

NOTE 9 – PENSION AND DEFERRED COMPENSATION PLANS**A. Retirement Plan:**

Each permanent full-time employee, as a condition of employment, is a member of the Teachers' and State Employees' Retirement System (TSERS) and is automatically enrolled in the Teachers' and State Employees' Retirement System.

The Teachers' and State Employees' Retirement System is a cost sharing multiple-employer defined benefit pension plan established by the State to provide pension benefits for employees of the State, its component units and local boards of education. The plan is administered by the NC Department of State Treasurer.

NOTE 9 – PENSION AND DEFERRED COMPENSATION PLANS (continued)

Benefit and contribution provisions for the Teachers' and State Employees' Retirement System are established by North Carolina General Statutes 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contribution rates are set each year by the North Carolina General Assembly based on annual actuarial valuations.

For the years ending June 30, 2013, 2012 and 2011, respectively, the NCEL had a total payroll of \$13,139, \$12,839, and \$12,018, of which \$13,139, \$12,839 and \$12,018 was covered under the Teachers' and State Employees' Retirement System. Total employer and employee contributions for pension benefits for the years ended June 30, 2013, 2012 and 2011, were \$1,883, \$1,725 and \$1,314, respectively. Required employer contribution rates for the years ended June 30, 2013, 2012 and 2011, were 8.33%, 7.44% and 4.93%, respectively, while employee contributions were 6% each year. The NCEL made 100% of its annual required contributions as mandated by Senate Bill 58. The contribution amounts for the years ended June 30, 2013, 2012, and 2011, were \$1,094, \$955 and \$592, respectively.

The Teachers' and State Employees' Retirement System's financial information is included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.nc.gov/> and clicking on "Financial Reports", or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

B. Supplemental Retirement Income Plan:

IRC Section 401(k) Plan – All full-time employees are eligible to enroll in the Supplemental Retirement Income Plan, a defined contribution plan, created under Internal Revenue Code Section 401(k). All costs of administering the plan are the responsibility of the plan participants. The Plan is provided by Prudential Retirement, administered by the NC Department of the State Treasurer and sponsored by the State of North Carolina. The effective date of participation was January 30, 2006. The voluntary contributions by employees amounted to \$138, \$170 and \$197 for the years ended June 30, 2013, 2012 and 2011, respectively.

C. Deferred Compensation Plan:

IRC Section 457 Plan – The State of North Carolina offers its permanent employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457 through the North Carolina Public Employee Deferred Compensation Plan (the Plan). The Plan permits each participating employee to defer a portion of his or her salary until future years. The deferred compensation is available to employees upon separation from service, death, disability, retirement or financial hardships if approved by the Plan's Board of Trustees. The Board, a part of the North Carolina Department of State Treasurer, maintains a separate fund for the exclusive benefit of the participating employees and their beneficiaries, the North Carolina Public Employee Deferred Compensation Trust Fund. The Board also contracts with an external third party to perform certain administrative requirements and to manage the trust fund's assets. All costs of administering and funding the Plan are the responsibility of the Plan participants. The effective date of participation was January 30, 2006. The voluntary contributions by employees amounted to \$58, \$85 and \$109, for the years ended June 30, 2013, 2012 and 2011, respectively.

NOTE 10 – OTHER POSTEMPLOYMENT BENEFITS

A. Health Care for Long Term Disability Beneficiaries and Retirees:

The NCEL participates in the Comprehensive Major Medical Plan (the Plan), a cost-sharing, multiple-employer defined benefit health care plan that provides post-employment health insurance to eligible former employees. Eligible former employees include long term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers' and State Employees' Retirement System. Coverage eligibility varies depending on years of contributory membership service in the retirement system prior to disability or retirement.

The Plan's benefit and contribution provisions are established by the State Treasurer and the Board of Trustees of the State Health Plan for Teachers and State Employees as authorized by Chapter 135, Article 3B, of the General Statutes. The Plan does not provide for automatic post-retirement benefit increases.

The General Statute states that a Retiree Health Benefit Fund (the Fund) has been established as a fund in which accumulated contributions from employers and any earnings on those contributions shall be used to provide health benefits to retired and disabled employees and applicable beneficiaries. The General Statute states that the Fund is administered by the Board of Trustees Teachers' and State Employees' Retirement System and contributions to the fund are irrevocable. Also by law, Fund assets are dedicated to providing benefits to retired and disabled employees and applicable beneficiaries and are not subject to the claims of creditors of the employers making contributions to the Fund. Contribution rates to the Fund, which are intended to finance benefits and administrative expenses on a pay-as-you-go basis, are determined by the State Treasurer and the Board of Trustees of the State Health Plan for Teachers and State Employees.

Notes to Financial Statements - June 30, 2013 & 2012 (in Thousands)

For the current fiscal year 2013, the NCEL contributed 5.3% of the covered payroll under the Teachers' and State Employees' Retirement System. Required contribution rates for the years ended June 30, 2012 and 2011, were 5.0% and 4.9%, respectively. The NCEL made 100% of its annual required contributions to the Plan for the years ended June 30, 2013, 2012, and 2011, which were \$696, \$642, and \$589, respectively.

The NCEL assumes no liability for retiree health care benefits provided by the programs other than its required contribution.

Additional detailed information about these programs can be located in the State of North Carolina's Comprehensive Annual Financial Report. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.nc.gov/> and clicking on "Financial Reports", or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

B. Long Term Disability:

The NCEL participates in the Disability Income Plan of North Carolina (DIPNC), a cost-sharing, multiple-employer defined benefit plan, to provide short term and long term disability benefits to eligible members of the Teachers' and State Employees' Retirement System. Benefit and contribution provisions are established by Chapter 135, Article 6, of the General Statute, and may be amended only by the North Carolina General Assembly. The plan does not provide for automatic post-retirement benefit increases.

Disability income benefits are funded by actuarially determined employer contributions that are established in the Appropriations Bill by the General Assembly. For the fiscal year ended June 30, 2013, the NCEL made a statutory contribution of .44% of covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the DIPNC. Required contribution rates for the years ended June 30, 2013, 2012 and 2011, were .44%, .52% and .52%, respectively. The NCEL made 100% of its annual required contributions to the DIPNC for the years ended June 30, 2013, 2012, and 2011, which were \$58, \$66, and \$62, respectively. The NCEL assumes no liability for long term disability benefits under the Plan other than its contribution.

Additional detailed information about the DIPNC is disclosed in the State of North Carolina's Comprehensive Annual Financial Report. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.nc.gov/> and clicking on "Financial Reports", or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

NOTE 11 – LITIGATION

As of June 30, 2013, the NCEL is not, nor anticipates being, a party to any litigation.

NOTE 12 – ALLOCATION OF TOTAL ANNUAL REVENUES/TRANSFERS TO NC EDUCATION LOTTERY FUND

	<u>2013</u>		
Lottery Ticket Sales	\$ 1,689,713		
Fees and Licenses	5,296		
Investment Earnings and Other Revenues	424		
Total Annual Revenue	1,695,453		
Less Prize Tickets	-	0%	Of Total Annual Revenue
Total Net Revenue	1,695,453		
Prize Expense	(1,024,437)	61%	Of Total Annual Revenue
Advertising	(15,278)	1%	Of Total Annual Revenue
All Other Expenses and Transfers	(59,062)		
Total Section 18C-162.a.3	(74,360)	4%	Of Total Annual Revenue
Commissions (per 18C-142)	(118,148)	7%	Of Lottery Ticket Sales
Unclaimed Prizes to The State of North Carolina	11,381		
Net Revenues to The State of North Carolina	467,127		
Total Revenues to The State of North Carolina	\$ 478,508	28%	Of Total Annual Revenue

NOTE 12 – ALLOCATION OF TOTAL ANNUAL REVENUES/TRANSFERS TO NC EDUCATION LOTTERY FUND (continued)

	<u>2012</u>		
Lottery Ticket Sales	\$ 1,596,638		
Fees and Licenses	5,381		
Investment Earnings and Other Revenues	<u>523</u>		
Total Annual Revenue	1,602,542		
Less Prize Tickets	<u>(181)</u>	0%	Of Total Annual Revenue
Total Net Revenue	<u>1,602,361</u>		
Prize Expense	(961,556)	60%	Of Total Annual Revenue
Advertising	(14,696)	1%	Of Total Annual Revenue
All Other Expenses and Transfers	<u>(55,016)</u>		
Total Section 18C-162.a.3	<u>(69,712)</u>	4%	Of Total Annual Revenue
Commissions (per 18C-142)	(111,624)	7%	Of Lottery Ticket Sales
Unclaimed Prizes to The State of North Carolina	11,083		
Net Revenues to The State of North Carolina	<u>448,386</u>		
Total Revenues to The State of North Carolina	<u>\$ 459,469</u>	29%	Of Total Annual Revenue

In accordance with Section § 18C-162 of the North Carolina State Lottery Act: Allocation of revenues.

- (a) The Commission shall allocate revenues to the North Carolina State Lottery Fund in order to increase and maximize the available revenues for education purposes, and to the extent practicable, shall adhere to the following guidelines:
 - (1) At least fifty percent (50%) of the total annual revenues, as described in this Chapter, shall be returned to the public in the form of prizes.
 - (2) At least thirty-five percent (35%) of the total annual revenues, as described in this Chapter, shall be transferred as provided in G.S. 18C-164.
 - (3) No more than eight percent (8%) of the total annual revenues, as described in this Chapter, shall be allocated for payment of expenses of the Lottery. Advertising expenses shall not exceed one percent (1%) of the total annual revenues.
 - (4) No more than seven percent (7%) of the face value of tickets or shares, as described in this Chapter shall be allocated for compensation paid to lottery game retailers.
- (b) To the extent that the expenses of the Commission are less than eight percent (8%) of total annual revenues, the Commission may allocate any surplus funds:
 - (1) To increase prize payments; or
 - (2) To the benefit of the public purposes as described in this chapter.
- (c) Unclaimed prize money shall be held separate and apart from the other revenues and allocated as follows:
 - (1) Fifty percent (50%) to enhance prizes under subdivision (a) (1) of this section.
 - (2) Fifty percent (50%) to the Education Lottery Fund to be allocated in accordance with G.S. 18C-164(c).(2005-344, s. 1; 2005-276, s. 31.1(r); 2007-323, s.5.2(c).)

NOTE 12 – ALLOCATION OF TOTAL ANNUAL REVENUES/TRANSFERS TO NC EDUCATION LOTTERY FUND (continued)

Additionally, in accordance with Section § 18C 142 of the North Carolina State Lottery Act, Compensation for lottery game retailers, “The amount of compensation paid to lottery game retailers for their sales of lottery tickets or shares shall be seven percent (7%) of the retail price of the tickets or shares sold for each lottery game.”

§ 18C-161. Types of income to the North Carolina State Lottery Fund.

- (1) All proceeds from the sale of lottery tickets or shares.
- (2) The funds for initial start-up costs provided by the State.
- (3) All other funds credited or appropriated to the Commission from any sources.
- (4) Interest earned by the North Carolina Lottery Fund.

The NCEL transferred \$461.4 million to the NC Education Lottery Fund for fiscal year 2013 compared with \$456.8 million for fiscal year 2012. As explained in Note 4C, \$27.3 million and \$10.1 million for fiscal years ended June 30, 2013 and 2012, respectively, were the amounts of the “Net Revenues” and “50% of Unclaimed Prizes” that were transferred to the State subsequent to the end of the respective fiscal year.

NOTE 13 – CHANGES IN FINANCIAL ACCOUNTING AND REPORTING

For the fiscal year ended June 30, 2013, the NCEL implemented the following pronouncement issued by the Governmental Accounting Standards Board (GASB):

GASB Statement No. 63, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position.

Statement No. 63 provides a new statement of net position format to report all assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position (which is the net residual amount of the other elements). The Statement requires that deferred outflows of resources and deferred inflows of resources be reported separately from assets and liabilities. Statement No. 63 also amends certain provisions of Statement No. 34, *Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments*, and related pronouncements to reflect the residual measure in the statement of financial position as net position, rather than net assets.

NOTE 14 – SUBSEQUENT EVENTS

The Commission of the NCEL has evaluated all subsequent events for potential recognition and disclosure through September 27, 2013, the date these financial statements will be available.

Report of Independent Auditor 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*

To the Commissioners
North Carolina Education Lottery
Raleigh, North Carolina

We have audited in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the North Carolina Education Lottery (“NCEL”), a major enterprise fund of the State of North Carolina, as of and for the years ended June 30, 2013 and 2012, which collectively comprise the NCEL’s basic financial statements as listed in the table of contents, and have issued our report thereon dated September 27, 2013.

The financial statements present only the NCEL and do not purport to and do not present fairly the financial position of the State of North Carolina, as of and for the years ended June 30, 2013 and 2012, and the changes in their financial position and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the NCEL’s internal control over financial reporting (“internal control”) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements but not for the purpose of expressing an opinion on the effectiveness of the NCEL’s internal control. Accordingly, we do not express an opinion on the effectiveness of the NCEL’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 NCEL’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 the NCEL’s financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed 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 NCEL’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 NCEL’s internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Raleigh, North Carolina
September 27, 2013

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