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STATEMENT OF LOTTERY REVENUES,  
PRIZE DISBURSEMENTS AND OTHER EXPENSES

(UNAUDITED)

FOR THE FISCAL YEAR ENDED

JUNE 30, 2004

**COLORADO LOTTERY  
FINANCIAL STATEMENTS  
(UNAUDITED)**

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# STATE OF COLORADO

## DEPARTMENT OF REVENUE

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Bill Owens  
Governor

M. Michael Cooke  
Executive Director

Peggy Gordon  
Lottery Director

August 2, 2004

State Treasurer and Members of the Colorado Lottery Commission:

Pursuant to CRS 24-35-204, the Colorado Lottery is required to furnish monthly, "a complete statement of lottery revenues, prize disbursements and other expenses."

The financial performance for the fiscal year ended June 30, 2004 depicts total revenues of \$401.4 million, gross ticket sales of \$401.3 million, net income before proceeds distributions of \$102.8 million, and a net decrease in net assets of \$1.3 million. Accordingly, a total of \$104.1 million distribution will have been made by September 1, 2004 in the following manner; \$49.7 million to the Great Outdoors Colorado Fund, \$10.4 million to the State Parks, Recreation, \$41.6 million to the Conservation Trust Fund, for distribution to cities and other local government agencies and \$2.4 million to the State School Fund.

The attached financial statements for June 30, 2004 have not been audited. They have been prepared in accordance with generally accepted accounting principles, using established accounting and internal control procedures. These procedures include, but are not limited to, documentation and accounting estimates, which support the production of reliable financial statements. As with any system of accounting and internal control procedures, there are inherent limitations, and the procedures cannot be relied upon to completely eliminate the occurrence of discrepancies, error or omissions, but should reduce that risk to a relatively low tolerable level.

Respectfully submitted,

A handwritten signature in cursive script that reads "Barb Aggson".

Barb Aggson  
Controller  
Colorado Lottery

**COLORADO LOTTERY  
FINANCIAL STATEMENTS  
(UNAUDITED)**

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## MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE FISCAL YEAR ENDED JUNE 30, 2004

This discussion and analysis of the Lottery's financial performance provides an overview of financial activities for the Fiscal Year ended June 30, 2004. Please read it in conjunction with the Lottery's financial statements, which begin on page 9. These financial statements reflect only activities of the Colorado Lottery, a proprietary fund of the State of Colorado.

### ***FISCAL YEAR 2004 FINANCIAL HIGHLIGHTS***

- The Lottery's overall sales performance of \$401.3 million reflected a \$9.8 million increase from last year and replaced Fiscal Year 2003 as the second largest sales year since the Lottery's start up in 1983. Our highest overall sales year was Fiscal Year 2002 with sales totaling \$407 million.

Scratch sales totaled \$260.9 million to capture the highest year of scratch sales ever, with the second highest honors going to Fiscal Year 2002 with scratch sales of \$257.2 million. An increase in marketing efforts including offering a broader range of price points, additional games and an overall upgrade to the look of our scratch tickets, contributed to this increase in scratch sales.

Lotto sales continue to decline since the introduction of Powerball in Fiscal Year 2002. Odds were also not in the game's favor this year. Statistically, the Lotto jackpot should have been won only 9 times when in fact lucky Colorado players hit the Lotto jackpot 13 times. Fiscal Year 2004 Lotto sales reflect a decrease of \$7.5 million from the previous year for a total of \$40.8 million in sales.

On the other hand, large Powerball jackpots helped Powerball sales for Fiscal Year 2004 increase by \$9.3 million over the prior fiscal year. Powerball sales for Fiscal Year 2004 totaled \$85 million.

Cash 5 sales for Fiscal Year 2004 showed an unexpected increase. Sales increased nearly 9% to a total of \$14.5 million, with little effort made in the marketing area.

- Proceeds distributions fell slightly totaling \$104.1 million as compared to \$104.8 million in Fiscal Year 2003. This included, for the third time, a spillover into the State Public School Fund Contingency Reserve of \$2.4 million. A spillover occurs when the distributions cap for GoCo is reached in any one year. The cap for GoCo is set by taking the 1992 base year and adjusting it for the annual change in the cost of living increase for the Denver-Boulder area.
- For the fifth year in a row, the Lottery received a Certificate of Achievement from the Government Finance Officers Association. This Certificate is the highest honor awarded for governmental accounting and financial reporting

- Gross profit as a percent of sales decreased by .8 percent, a reflection of the increase in the prize costs from 58% to 59% of sales. Fiscal Year 2003 prize expense was slightly lower due to a decrease in powerball prize expense from the absorption of an unclaimed powerball jackpot.

### ***GAMES OFFERED BY THE COLORADO LOTTERY***

Currently, the Lottery offers two different ways to play: Scratch games and On-Line games (Powerball, Lotto, and Cash 5). Scratch games consist of pre-printed tickets that may be purchased for various prices (\$1, \$2, \$3, \$5, and \$10) at any Lottery retailer. When scratched, they provide immediate knowledge if the ticket is a winner and can be cashed immediately at the retailer level if the amount of the winnings are \$599 or less.

On-Line games, however, require a longer playing time. Tickets are also purchased at Lottery retailers and are printed on ticket stock as the purchase is made. Each ticket contains one or more playing boards. Each board consists of a set of numbers, the combination of numbers required for play varying by game. The winning numbers for each game are posted after their respective draw nights with drawings held on every night of the week excluding Sunday. The player must check their numbers against the numbers drawn for each respective game to determine if they have a winning ticket. They may also be cashed at the retailer level if the amount of the winnings are \$599 or less.

### ***USING THIS ANNUAL REPORT***

This annual report consists of a series of financial statements. The statement of net assets provides information about the Lottery's assets and liabilities and reflects the Lottery's financial position as of June 30, 2004 and 2003. The statement of revenues, expenses, and changes in net assets reports the activity of selling Lottery products and the expenses related to such activity for the years ended June 30, 2004 and 2003. And finally, the statement of cash flows outlines the cash inflows and outflows related to the activity of selling Lottery products for the years ended June 30, 2004 and 2003.

### ***STATEMENT OF NET ASSETS***

The statement of net assets is a financial snapshot of the Colorado Lottery at June 30, 2004 and 2003. It presents the fiscal resources of the Lottery (assets), the claims against those resources (liabilities) and the residual available for future operations (net assets). Assets and liabilities are classified by liquidity as either current or non-current. Net assets are classified by the ways in which they may be used for future operations.

COLORADO LOTTERY  
CONDENSED STATEMENT OF NET ASSETS  
JUNE 30, 2004 AND 2003

|                              | <u>2004</u>          | <u>2003</u>          |
|------------------------------|----------------------|----------------------|
| <b>ASSETS</b>                |                      |                      |
| Current Assets               | \$ 39,951,270        | \$ 46,057,987        |
| Restricted Assets            | 5,024,418            | 4,430,844            |
| Capital Assets               | <u>1,029,114</u>     | <u>1,427,326</u>     |
| Total Assets                 | \$ <u>46,004,802</u> | \$ <u>51,916,157</u> |
| <b>LIABILITIES</b>           |                      |                      |
| Current Liabilities          | \$ 43,576,343        | \$ 48,061,451        |
| Long-Term Liabilities        | <u>782,863</u>       | <u>958,754</u>       |
| Total Liabilities            | \$ <u>44,359,206</u> | \$ <u>49,020,205</u> |
| <b>NET ASSETS</b>            |                      |                      |
| Investment in Capital Assets | \$ 1,029,114         | \$ 1,427,326         |
| Restricted-Licensed Agent    |                      |                      |
| Recovery Reserve             | 469,424              | 460,638              |
| Unrestricted                 | <u>147,057</u>       | <u>1,007,988</u>     |
| Total Net Assets             | \$ <u>1,645,595</u>  | \$ <u>2,895,952</u>  |

The Lottery's total assets at June 30, 2004, were \$46 million. Assets consisted primarily of cash and investments with the State Treasury of \$25.4 million, Prepaid Prize Expense with MUSL of \$3.5 million, receivables from Lottery retailers for the sale of Lottery products of \$14.7 million, and a net investment in fixed assets of \$1 million.

Comparable figures at June 30, 2003, were \$51.9 million in total assets, including \$31.5 million in cash and investments with the State Treasury, Prepaid Prize Expense with MUSL of \$2.5 million, receivable from retailers of \$15.3 million, and a net investment in fixed assets of \$1.4 million.

The Lottery's total liabilities at June 30, 2004, totaled \$44.4 million consisting primarily of proceeds distributions due to recipients of \$25.8 million and prize liability on all Lottery products of \$14 million.

The Lottery's total liabilities at June 30, 2003, totaled \$49 million, which consisted primarily of proceeds distributions due of \$25.4 million and prize liability on all Lottery products of \$18.6 million.

Components of the Lottery's net assets are: 1) an amount approved by the Lottery Commission to represent the Lottery's net investment in capital assets as required by the reporting model under GASB 34, (See "Total Capital Assets" on the Statement of Net

Assets); 2) a Licensed Agent Recovery Reserve (bonding reserve) funded by retailers to cover any uncollectible receivable accounts and; 3) an adjustment made by the Lottery to reflect its share of unrealized gains or losses on investments held by the State Treasurer. The change in net assets from June 30, 2003 to June 30, 2004, consisted of a decrease in investment in capital assets from \$1.4 million to \$1 million, a minor increase in the bonding reserve from \$460,638 to \$469,424, and a net decrease in unrestricted net assets of \$860,931 resulting from a net decrease in the adjustments on State Treasury investments.

Following is a schedule of net assets:

|                                | <u>2004</u>        | <u>2003</u>        | <u>Change</u>        |
|--------------------------------|--------------------|--------------------|----------------------|
| Investment in Capital Assets   | \$1,029,114        | \$1,427,326        | (\$398,212)          |
| Bonding Reserve                | 469,424            | 460,638            | 8,786                |
| Unrealized gain on investments | <u>147,057</u>     | <u>1,007,998</u>   | <u>860,931</u>       |
| Total Net Assets               | <u>\$1,645,595</u> | <u>\$2,895,952</u> | <u>(\$1,250,357)</u> |

### ***SALES ACTIVITIES***

Revenues from the sale of Lottery products for the Fiscal Year ended June 30, 2004, were the second highest in the Lottery's twenty-two year history. As shown in the financial statements, overall sales increased slightly by 2.5% from the prior year, from \$391.5 million in Fiscal Year ended June 30, 2003, to \$401.2 million in the current year. The increase in Scratch sales from \$254.3 million to \$260.9 represented a slightly larger percentage increase of 2.6%. Powerball finished its second full year of sales with more than a 12.3% increase in sales from the prior year, a result of large Powerball jackpots. Lotto sales suffered a statistically off year, as addressed on page 1, resulting in a 15.5% reduction in sales. This was the second consecutive year that Lotto experienced a large percentage reduction in sales with, the other being Fiscal Year 2003, when sales reflected a 16.2% decrease from Fiscal Year 2002.

The following table compares Lottery product sales between fiscal years. All sales are presented in millions of dollars:

| <u>Product Sales</u> | <u>2004</u> | <u>2003</u> | <u>Difference</u> | <u>Percentage</u> |
|----------------------|-------------|-------------|-------------------|-------------------|
| Scratch              | \$260.9     | \$254.3     | \$6.6             | 2.6%              |
| Powerball            | 85.0        | 75.7        | 9.3               | 12.3%             |
| Lotto                | 40.8        | 48.3        | -7.5              | -15.5%            |
| Cash 5               | 14.5        | 13.2        | 1.3               | 9.8%              |
| Total                | \$401.2     | \$391.5     | \$9.7             | 2.5%              |



## ***TOTAL REVENUES***

Non-operating revenues for the year ended June 30, 2004 totaled \$.1 million as compared with \$2.3 million for the year ended June 30, 2003. Two major factors contributed to the decrease from Fiscal Year 2003 to Fiscal Year 2004. First, investment income for Fiscal Year 2004 was decreased by \$860,931 to record the net, of the reversal in the Lottery's share of unrealized gains on investments as mandated by GASB 31 from Fiscal Year 2003, and the entry of unrealized gains on investments in Fiscal Year 2004. In contrast, a \$398,543 net increase in investment income for the same adjustments was made in Fiscal Year 2003. Second, interest received from the treasury and other sources was down by nearly \$700,000 due to lower interest rates in a sluggish economy and a statutory requirement for Fiscal Year 2004, requiring 15% of the lottery's treasury interest to be sent to the General Fund.

Total revenues were \$401.4 million and \$393.7 million for the years ended June 30, 2004 and 2003, respectively. As mentioned elsewhere, the two major contributors to the increase of approximately \$7.7 million was an increase in Lottery sales of \$9.8 million offset by a decrease in non-operating revenues of \$2.1 million.

## ***MAJOR EXPENSES***

Approximately \$276.5 million of the Lottery's total expenses of \$298.6 million for the Fiscal Year ended June 30, 2004, were incurred in direct support of Lottery games. These included prize expense, retailer compensation, money spent to purchase Scratch tickets, and compensation to the vendor who maintains and supports the On-Line gaming system.

In comparison, \$266.4 million of the Lottery's total expenses of \$288.7 million for the fiscal year ended June 30, 2003, were game-related expenses.

Following is a table comparing the game-related expenses between Fiscal Years. All expenses are presented in millions of dollars.

| <u>Game Related Expenses</u>         | <u>2004</u>    | <u>2003</u>    | <u>Difference</u> | <u>Percentage</u> |
|--------------------------------------|----------------|----------------|-------------------|-------------------|
| Prize Expense/Powerball Prz Variance | \$236.6        | \$226.9        | \$9.7             | 4.3%              |
| Retailer Compensation:               |                |                |                   |                   |
| Commissions                          | 26.6           | 26.0           | 0.6               | 2.3%              |
| Bonuses                              | 3.6            | 3.5            | 0.1               | 2.9%              |
| Ticket Costs                         | 3.0            | 3.2            | -0.2              | -6.3%             |
| Vendor Fees                          | 6.7            | 6.8            | -0.1              | -1.5%             |
| <b>Total</b>                         | <b>\$276.5</b> | <b>\$266.4</b> | <b>\$10.1</b>     | <b>3.8%</b>       |

**STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS**

The statement of revenues, expenses and changes in net assets presents the financial activity of the Colorado Lottery over the fiscal year. The focus is on operating revenues and expenses that have a significant effect on the distributions paid to the proceeds recipients.

COLORADO LOTTERY  
CONDENSED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET  
ASSETS  
FOR THE FISCAL YEARS ENDED JUNE 30, 2004 AND 2003

|                                   | <u>2004</u>           | <u>2003</u>           |
|-----------------------------------|-----------------------|-----------------------|
| OPERATING REVENUES                | \$ 401,250,971        | \$ 391,473,640        |
| DIRECT OPERATING EXPENSES         | <u>276,512,227</u>    | <u>266,444,993</u>    |
| GROSS PROFIT ON SALE OF TICKETS   | \$ <u>124,738,744</u> | \$ <u>125,028,647</u> |
| OTHER OPERATING EXPENSES          |                       |                       |
| Marketing and Communications      | 8,643,422             | 9,093,013             |
| Wages and Benefits                | 8,129,740             | 7,976,826             |
| Other operating expenses          | <u>5,301,655</u>      | <u>5,221,953</u>      |
| Total Operating Expenses          | <u>22,074,817</u>     | <u>22,291,792</u>     |
| OPERATING INCOME                  | \$ <u>102,663,927</u> | \$ <u>102,736,855</u> |
| NONOPERATING REVENUES (EXPENSES)  |                       |                       |
| Other Revenue                     | \$ 156,990            | \$ 303,134            |
| Interest Income                   | 184                   | 1,958,747             |
| Proceeds Distributions            | <u>(104,071,458)</u>  | <u>(104,779,061)</u>  |
| Total Non-operating Rev (Exp)     | <u>(103,914,284)</u>  | <u>(102,517,180)</u>  |
| INCREASE (DECREASE) IN NET ASSETS | \$ (1,250,357)        | \$ 219,675            |
| NET ASSETS - BEGINNING OF YEAR    | <u>2,895,952</u>      | <u>2,676,277</u>      |
| NET ASSETS - END OF YEAR          | \$ <u>1,645,595</u>   | \$ <u>2,895,952</u>   |

The increase in the game-related expenses, including prize expense, commission expense and bonus expense, is reflective of the increase in product sales. See the product sales schedule above. In addition, the prize expense percentage was further increased in Fiscal

Year 2004 over the prize expense percentage in Fiscal Year 2003, as the prize expense percentage in Fiscal Year 2003 had been reduced by the expiration of an unclaimed Powerball jackpot. The small percentage decrease in ticket costs is a result of alternate printing options exercised in Fiscal Year 2003.

Of the \$22.1 million in Fiscal Year 2004 expenses that were not game-related, more than \$8.6 million was for promotions and institutional and product advertising, and \$8.1 million to compensate Lottery employees. In comparison, of the Fiscal Year 2003 non game related expenses of \$22.3 million, just under \$9.1 million was for promotions and institutional and product advertising, and \$8.0 million compensatd Lottery employees.

### ***DISTRIBUTIONS TO PROCEEDS RECIPIENTS***

The Lottery's efforts generated proceeds distributions of \$104.1 million in the current Fiscal Year, the third highest year ever. Of these total proceeds, nearly \$49.7 million was allocated to the Great Outdoors Colorado Trust Fund, \$41.6 million to the Conservation Trust Fund, and \$10.4 million to the Division of State Parks and Recreation per the distribution formula stated in Colorado Revised Statutes (C.R.S.) 24-35-210. The maximum distribution to Great Outdoors Colorado of \$49.7 million pursuant to C.R.S. 33-60-104 (1) (c) and 33-60-104 (2) was reached, thus creating a spill over into the State's Public School Fund Contingency Reserve of \$2.4 million pursuant to C.R.S.22-54-117 (1.6) (a).

The Lottery's proceeds distributions for the prior year was the second highest year on record totaling \$104.8 million. Approximately, \$48.7 million was distributed to Great Outdoors Colorado, \$41.9 million to the Conservation Trust Fund, \$10.5 million to the Division of State Parks and Recreation and a spillover into the State's Public School Fund Contingency Reserve of nearly \$3.7 million.

### ***BUDGETARY HIGHLIGHTS***

The Lottery's budget is determined by a variety of methods. The majority of the budget is set by the annual appropriations bill (called the Long Bill), which determines budgets for every agency within the State. The Long Bill and department level allocations are approved shortly before the start of each Fiscal Year. Agencies may also request a supplemental appropriation during the Fiscal Year to cover unexpected expenses (or a negative supplemental for less than expected expenses) as well as year-end transfers of spending authority if needed. In the third quarter of Fiscal Year 2004, the Legislature approved supplemental appropriations to adjust for changes in estimated sales levels and other unforeseen needs/adjustments. Supplemental appropriations were approved in operating expenses, MNT payments, legal services, ticket costs, and retailer compensation lines, offset by reductions in the vehicle lease payments, telecommunications, risk management, indirect costs, vendor fees, prizes, and Powerball prize variance. In Fiscal Year 2004, there was a year-end transfer from operating to

vehicle lease payments of \$1,182. The final method of funding is special legislation. There was no special legislation affecting the Lottery's budget in Fiscal Year 2004.

The approved Lottery budget at the beginning of the year was \$355.4 million. Department level allocations approved at the beginning of the Fiscal Year increased the budget by \$0.4 million. Supplemental appropriations and adjustments made in the third quarter decreased the budget by \$6.9 million to a total of \$348.9 million. Total expenditures and roll-forwards for Fiscal Year 2004 came to \$304.4 million, resulting in excess appropriations (or savings) of more than \$44.5 million

### ***ECONOMIC FACTORS AND NEXT YEAR'S BUDGET***

The Lottery considered several factors when setting the revenue estimates and the Fiscal Year 2005 budget. On-Line sales (Powerball, Lotto, and Cash 5) are expected to decrease slightly overall as sales for On-Line games naturally decrease over the life cycle of each game.

Scratch sales for Fiscal Year 2004 were up approximately \$6.6 million from projections, finishing at \$260.9 million as the best Scratch sales ever. Therefore, the Lottery is projecting that Fiscal Year 2005 sales will be comparable or slightly higher than Fiscal Year 2004.

Fiscal Year 2005 revenue estimates total \$392.5 million, an \$8.7 million decrease from Fiscal Year 2004 actual sales due to a projected decrease in Powerball sales as the game matures.

In addition to normal increases in costs, there will be one other major change in costs in Fiscal Year 2005, which will decrease on-line system related costs due to a new on-line contract

### ***CONTACTING THE LOTTERY'S FINANCIAL MANAGEMENT***

This management discussion and analysis report is designed to provide Colorado citizens, Colorado government officials, our players, retailers and other interested parties with a general overview of the Lottery's financial activity for Fiscal Year 2004 and to demonstrate the Lottery's accountability for the money generated from the sale of Lottery products. If you have questions about this report or need additional information, contact Barbara Aggson, the Colorado Lottery's Controller, 201 West 8<sup>th</sup> Street, Suite 600, Pueblo, CO 81003.

COLORADO LOTTERY  
FINANCIAL HIGHLIGHTS  
\$ IN MILLIONS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2004 AND 2003

The table included below and the graphs included on page 2 present certain summarized operating results of the Colorado Lottery for the fiscal year ended June 30, 2004 and 2003, and should be read in conjunction with the financial statements presented herein. The graphs included on page 2 are presented for the purpose of demonstrating the Colorado Lottery's compliance with certain statutes that pertain to its operations.

|  | For the fiscal year ended June 30, |                   |                 |                   |
|--|------------------------------------|-------------------|-----------------|-------------------|
|  | 2004                               |                   | 2003            |                   |
|  | Total                              | Actual<br>Percent | Total           | Actual<br>Percent |
| <b>INCOME</b>                              |                                    |                   |                 |                   |
| Gross Ticket Sales                         | \$401.25                           |                   | \$391.47        |                   |
| Nonoperating revenue                       | 0.16                               |                   | 2.26            |                   |
| <b>TOTAL INCOME</b>                        | <b>401.41</b>                      |                   | <b>393.73</b>   |                   |
| <b>LESS:</b>                               |                                    |                   |                 |                   |
| PRIZES                                     | \$236.60                           | 59.0% (1)         | \$226.91        | 58.0% (1)         |
| RETAILER COMMISSIONS AND BONUSES           | \$30.26                            | 7.5% (1)          | \$29.53         | 7.5% (1)          |
| <b>ADMINISTRATIVE COSTS</b>                |                                    |                   |                 |                   |
| Ticket Costs and Vendor Fees               | 9.65                               |                   | 10.00           |                   |
| Other Operating Expenses                   | 22.08                              |                   | 22.29           |                   |
| <b>TOTAL ADMINISTRATIVE COSTS (Note 3)</b> | <b>31.73</b>                       | <b>7.9% (2)</b>   | <b>32.29</b>    | <b>8.2% (2)</b>   |
| <b>NET INCOME BEFORE DISTRIBUTIONS</b>     | <b>102.82</b>                      |                   | <b>105.00</b>   |                   |
| <b>NET CHANGE IN NET ASSETS</b>            | <b>-1.25</b>                       |                   | <b>0.22</b>     |                   |
| <b>PROCEEDS DISTRIBUTION</b>               | <b>\$104.07</b>                    | <b>25.9% (2)</b>  | <b>\$104.78</b> | <b>26.6% (2)</b>  |

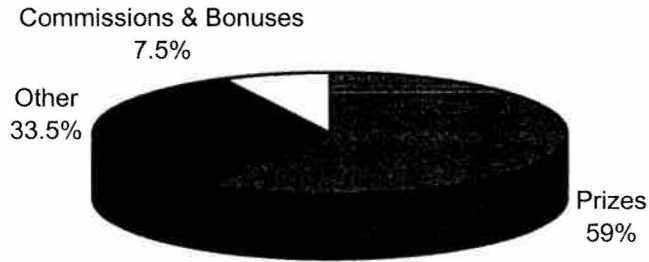
Note 1: Percent of gross ticket sales.

Note 2: Percent of total income.

Note 3: Total operating expenses per the statement of revenues, expenses and changes in fund net assets includes unappropriated expenses such as depreciation and accrued annual and sick leave. The actual administrative costs percentage would be slightly lower if they were removed from the calculation.

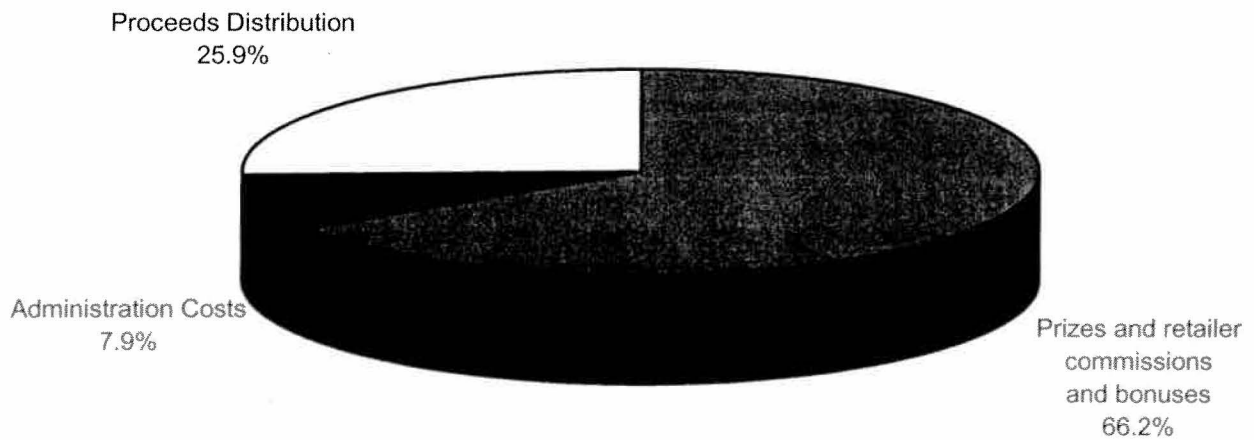
COLORADO LOTTERY  
SUPPLEMENT OF FINANCIAL HIGHLIGHTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

**PERCENT OF GROSS TICKET SALES**



To depict compliance with the 50% prize payment statute and the commission/bonus rules.

**PERCENT OF TOTAL INCOME**



To depict status of administrative expenditures to date.

COLORADO LOTTERY  
STATEMENT OF NET ASSETS  
JUNE 30, 2004 AND 2003  
(UNAUDITED)

| ASSETS   | 2004          | 2003          |
|--|---------------|---------------|
| Current Assets:  |               |               |
| Cash and Investments   | \$ 23,920,655 | \$ 29,602,733 |
| Accounts Receivable, net of the allowance for doubtful accounts of \$70,846 in 2004 and \$77,833 in 2003 | 14,671,184    | 15,261,679    |
| Game Prizes Inventory, at Cost   | 120,323       | 0             |
| Consignment Inventory, at Cost   | 157,705       | 131,703       |
| Warehouse Inventory, at Cost   | 1,043,264     | 917,029       |
| Prepaid Expenses   | 38,139        | 144,843       |
| Total Current Assets   | 39,951,270    | 46,057,987    |
| Restricted Assets:   |               |               |
| Cash and Investments-Operating Reserve   | 1,029,114     | 1,427,326     |
| Cash and Investments-Licensed Agent Recovery Reserve Receipts  | 469,424       | 460,638       |
| Prepaid Prize Expense with MUSL  | 3,525,880     | 2,542,880     |
| Total Restricted Assets  | 5,024,418     | 4,430,844     |
| Capital Assets:  |               |               |
| Equipment  | 4,455,227     | 5,559,322     |
| Leasehold Improvements   | 327,287       | 330,936       |
| Less Accumulated Depreciation and Amortization   | (3,753,400)   | (4,462,932)   |
| Total Capital Assets   | 1,029,114     | 1,427,326     |
| TOTAL ASSETS   | 46,004,802    | 51,916,157    |
| LIABILITIES  |               |               |
| Current Liabilities:   |               |               |
| Accounts Payable   | 1,987,161     | 1,590,977     |
| Prize Liability  | 13,975,136    | 18,565,011    |
| Payable to MUSL  | 129,377       | 678,159       |
| Wages and Benefits   | 725,844       | 671,966       |
| Accrued Annual and Sick Leave  | 78,211        | 142,254       |
| Retailer Bonus Liability   | 576,370       | 574,247       |
| Funds Available for Distribution   | 25,805,521    | 25,412,933    |
| Deferred Revenue   | 298,723       | 425,904       |
| Total Current Liabilities  | 43,576,343    | 48,061,451    |
| Long-Term Liabilities:   |               |               |
| Accrued Annual and Sick Leave  | 653,670       | 829,541       |
| Expired Warrants Liability   | 129,193       | 129,213       |
| Total Long-Term Liabilities  | 782,863       | 958,754       |
| TOTAL LIABILITIES  | 44,359,206    | 49,020,205    |
| NET ASSETS   |               |               |
| Investment in Capital Assets   | 1,029,114     | 1,427,326     |
| Restricted-Licensed Agent Recovery Reserve   | 469,424       | 460,638       |
| Unrestricted   | 147,057       | 1,007,988     |
| TOTAL NET ASSETS   | \$ 1,645,595  | \$ 2,895,952  |

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

COLORADO LOTTERY  
STATEMENTS OF REVENUES, EXPENSES AND  
CHANGES IN FUND NET ASSETS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2004 AND 2003  
(UNAUDITED)

|   | <u>2004</u>           | <u>2003</u>          |
|---|-----------------------|----------------------|
| OPERATING REVENUES                                |                       |                      |
| Gross Ticket Sales                                | \$ 401,250,971        | \$ 391,473,640       |
| DIRECT OPERATING EXPENSES                         |                       |                      |
| Prize Expense                                     | 238,427,919           | 227,514,771          |
| Powerball Prize Variance                          | (1,824,959)           | (597,361)            |
| Retailer Commissions and Bonuses                  | 30,255,251            | 29,528,971           |
| Cost of Tickets and Vendor Fees                   | <u>9,654,016</u>      | <u>9,998,612</u>     |
| GROSS PROFIT ON SALE OF TICKETS                   | <u>124,738,744</u>    | <u>125,028,647</u>   |
| OTHER OPERATING EXPENSES                          |                       |                      |
| Marketing and Communications                      | 8,643,422             | 9,093,013            |
| Administration Fees Paid to MUSL                  | 134,839               | 114,766              |
| Wages and Benefits                                | 8,129,740             | 7,976,826            |
| Professional Services                             | 559,685               | 314,768              |
| State Agencies Services                           | 405,910               | 257,947              |
| Department of Revenue Services                    | 330,926               | 372,155              |
| Travel  | 111,983               | 104,985              |
| Equipment   | 99,455                | 108,330              |
| Depreciation                                      | 489,609               | 463,741              |
| Accrued Annual and Sick Leave                     | (248,377)             | 79,075               |
| Space Rental                                      | 746,806               | 718,649              |
| Rents for Equipment                               | 690,126               | 689,546              |
| Motorpool Leasing                                 | 276,191               | 284,947              |
| Materials and Supplies                            | 141,202               | 89,984               |
| Telephone   | 190,334               | 148,466              |
| On-Line Telecommunications                        | 725,728               | 801,383              |
| Data Processing Supplies and Services             | 55,413                | 65,850               |
| Equipment Maintenance                             | 280,227               | 264,729              |
| Postage   | 73,219                | 74,468               |
| Printing  | 34,796                | 69,513               |
| Other   | 203,583               | 198,651              |
| Total Other Operating Expenses                    | <u>22,074,817</u>     | <u>22,291,792</u>    |
| OPERATING INCOME                                  | <u>102,663,927</u>    | <u>102,736,855</u>   |
| NONOPERATING REVENUES (EXPENSES)                  |                       |                      |
| Other Revenue                                     | 156,990               | 303,134              |
| Investment Income                                 | 184                   | 1,958,747            |
| Funds Distributed for Current Year                | (78,265,937)          | (79,366,128)         |
| Funds Available for Distribution for Current Year | (25,805,521)          | (25,412,933)         |
| Total Nonoperating Revenues (Expenses)            | <u>(103,914,284)</u>  | <u>(102,517,180)</u> |
| NET INCOME (LOSS)                                 | <u>\$ (1,250,357)</u> | <u>\$ 219,675</u>    |
| NET ASSETS, BEGINNING OF YEAR                     | 2,895,952             | 2,676,277            |
| Net Change in Net Assets                          | <u>(1,250,357)</u>    | <u>219,675</u>       |
| NET ASSETS, END OF YEAR                           | <u>\$ 1,645,595</u>   | <u>\$ 2,895,952</u>  |

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



COLORADO LOTTERY  
STATEMENTS OF CASH FLOWS  
FOR THE FISCAL YEARS ENDED JUNE 30, 2004 & 2003  
(UNAUDITED)

|   | 2004                  | 2003                  |
|---|-----------------------|-----------------------|
| Cash flows from operating activities:   |                       |                       |
| Cash received from retailers  | \$ 400,528,775        | \$ 390,853,822        |
| Cash paid in prizes   | (242,453,240)         | (227,822,348)         |
| Cash paid in retailer commissions   | (26,620,204)          | (25,965,985)          |
| Cash payments to suppliers  | (22,597,775)          | (21,858,289)          |
| Cash payments to employees for services   | (7,990,304)           | (7,319,796)           |
| Cash received from Lotto subscription sales   | 463,239               | 654,617               |
| Cash paid in retailer bonus   | (3,640,176)           | (3,625,433)           |
| Cash received (used) - other  | 29,380                | 17,128                |
|   | 97,719,695            | 104,933,716           |
| Cash flows from non-capital financing activities:   |                       |                       |
| Distribution of net proceeds  | (103,678,870)         | (101,305,142)         |
|   | (103,678,870)         | (101,305,142)         |
| Cash flows from capital and related financing activities:   |                       |                       |
| Acquisition of capital assets   | (112,513)             | (311,456)             |
| Cash flows from investing activities:   |                       |                       |
| Investment income received  | 861,115               | 1,560,204             |
| Unrealized gains (losses) on investments  | (860,931)             | 398,543               |
|   | 184                   | 1,958,747             |
| Net increase (decrease) in cash and investments   | (6,071,504)           | 5,275,865             |
| Cash and investments, Beginning of Year (including \$464,096 and \$411,629, respectively, in restricted accounts) | 31,490,697            | 26,214,832            |
| Cash and investments, End of Year, (including \$460,638 and \$464,096, respectively, in restricted accounts)      | \$ 25,419,193         | \$ 31,490,697         |
| <br><i>Reconciliation of operating income to net cash provided by operating activities:</i>                       |                       |                       |
| <i>Operating income</i>   | <i>\$ 102,663,927</i> | <i>\$ 102,736,855</i> |
| <i>Adjustments to reconcile operating income to net cash provided by operating activities</i>                     |                       |                       |
| <i>Depreciation</i>   | <i>489,609</i>        | <i>463,741</i>        |
| <i>Loss on disposition of equipment</i>   | <i>21,117</i>         | <i>23,125</i>         |
| <i>Other revenue</i>  | <i>156,990</i>        | <i>303,134</i>        |
| <i>Increase in Prepaid Prize Expense with MUSL</i>  | <i>(983,000)</i>      | <i>(1,084,753)</i>    |
| <i>Change in:</i>   |                       |                       |
| <i>Accounts Receivable</i>  | <i>590,495</i>        | <i>(1,551,606)</i>    |
| <i>Ticket Inventory</i>   | <i>(152,237)</i>      | <i>377,246</i>        |
| <i>Other Assets</i>   | <i>(13,619)</i>       | <i>475,315</i>        |
| <i>Liabilities(excluding funds available for distribution)</i>  | <i>(5,053,587)</i>    | <i>3,190,659</i>      |
|   | <i>\$ 97,719,695</i>  | <i>\$ 104,933,716</i> |

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

**COLORADO LOTTERY  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2004 AND 2003  
(UNAUDITED)**

**1. NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

***Nature of Operations***

The Colorado Lottery was incorporated April 30, 1982, under the provisions of Section 24-35-202, C.R.S. The Colorado Lottery operates under a Commission and provides operation and service of lottery games as authorized by the statute. The Colorado Lottery's revenues are predominately earned from the sale of lottery products including scratch, Lotto, Powerball, and Cash 5.

The financial statements reflect activities of the Colorado Lottery, an enterprise fund of the State of Colorado, for the Fiscal Years Ended June 30, 2004 and 2003. The Colorado Lottery is an agency of the State of Colorado. The financial statements present only the Colorado Lottery, an enterprise fund of the State of Colorado. The financial statements are intended to present the financial position and results of operations and cash flows of only that portion of the State of Colorado that is attributable to the transactions of the Colorado Lottery in accordance with accounting principles generally accepted in the United States of America.

The accounting policies of the Colorado Lottery conform to accounting principles generally accepted in the United States of America as applicable to governments. The following is a summary of the more significant policies:

***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 at the date of the financial statements and the reported amounts of revenues, expenses, gains, losses and other changes in net assets during the reporting period. Actual results could differ from those estimates.

***Fund Accounting***

Government resources are allocated to and accounted for in separate sub-entities, called funds, based upon the purposes for which the resources are to be spent and the means by which spending activities are controlled. A fund is a fiscal and accounting entity with a self-balancing set of accounts that comprise its assets, liabilities, net assets, revenues, and expenditures.

## ***Enterprise Fund***

The Colorado Lottery accounts for its operations as an enterprise fund. The intent of the State of Colorado Legislature is that the cost (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges. As permitted by Governmental Accounting Standards Board Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Colorado Lottery has elected to apply only those applicable Financial Accounting Standards Board Statements and interpretations issued prior to November 30, 1989.

The Colorado Lottery defines operating revenues as those earned as a direct result of the fund's principal ongoing operation, i.e. the sale of lottery products. Operating expenses include expenses incurred in earning those revenues such as the cost of tickets, vendor fees, retailer commissions and bonuses, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting these definitions are reported as nonoperating revenues and expenses.

## ***Basis of Accounting***

Basis of accounting refers to when revenues, expenditures or expenses are recognized in the accounts and reported in the financial statements. The Colorado Lottery accounts for funds using the accrual basis of accounting. Revenues from scratch ticket sales are recognized at the point of ticket pack activation. Revenues from Lotto ticket, Powerball ticket, Cash 5 ticket, and subscription sales are recognized using the specific performance method whereby sales are recognized at the point that the play becomes active for the next drawing. Expenses are recognized when they are incurred.

## ***Budget***

By October 24th of each year, the Department of Revenue Executive Director submits to the Office of State Planning and Budgeting a proposed legislative budget for the Fiscal Year commencing the following July 1. The legislative budget includes proposed expenditures and the means of financing them.

Public hearings are conducted by the Joint Budget Committee to obtain clarification and taxpayer comments. Prior to June 30, the budget is legally enacted through passage of a statute referred to as the Long Bill.

During the Fiscal Year, the approved legislative budget may be modified due to roll-forward authorization, supplemental budget approval or line item transfer authorization. All modifications must be approved by the State Controller and the Office of State Planning and/or Budgeting and the Legislature.

### ***Accounts Receivable and Allowance for Doubtful Accounts***

Accounts receivable consist of amounts due from retailers for activated ticket packs. The accounts receivable are stated at the amount billed to retailers. Accounts receivable are ordinarily due seven days after the issuance of the invoice and are electronically transferred from the retailers accounts into the Lottery's account.

Allowance for Doubtful Accounts represents a provision for receivables that will probably not be collected in the future. Consideration of the economic climate, credit-worthiness of individual account debtors, bankruptcy of debtor, discontinuance of debtor's business, failure of repeated attempts to collect, and barring of collection by statute of limitations are factors used in considering when an account becomes uncollectible. The accrual of a loss contingency is required when a loss is probable and can be reasonably estimated.

The Colorado Lottery uses the specific identification method to determine expected uncollectibles. Under the provisions of Section 24-35-219, C.R.S., licensed agent recovery reserve receipts are collected from the retailers to cover uncollectible accounts. The accounts receivable and the licensed agent recovery reserve are shown net of estimated uncollectible receivables of \$70,846 and \$77,833 as of June 30, 2004 and June 30, 2003, respectively.

### ***Game Prizes Inventory***

Game Prizes Inventory represents merchandize prizes connected to certain scratch games that, as of the statement of net assets date, have not been claimed.

### ***Consignment Inventory***

Inventory on consignment represents non-activated ticket inventory in the possession of retailers who act as agents of the Colorado Lottery. The Colorado Lottery retains title to these tickets since retailers have the right to return non-activated tickets; therefore, the tickets are included in the inventory and reported on the statement of net assets. Consignment inventory is stated at cost using the specific identification method.

### ***Warehouse Inventory***

Warehouse inventory represents unsold tickets in possession of the Colorado Lottery and is stated at cost using the specific identification method.

### ***Supplies Inventory***

The State of Colorado's threshold for recording supplies inventories is \$100,000 per location. The supplies inventory of the Colorado Lottery consistently falls below the \$100,000 threshold per location. Accordingly, no supplies inventory appears on the statement of net assets.

### ***Fixed Assets***

Equipment and leasehold improvements are stated at cost. Beginning September 1, 1996, equipment may be capitalized if the cost exceeds \$5,000 and has a useful life of more than one year, however, a state agency could select a minimum acquisition cost or useful life which was less than the stated criteria for capitalization. Accordingly, the Colorado Lottery adopted a capitalization policy, which capitalized equipment with a cost of \$1,000 or more that had a useful life of more than one year. In addition, the Colorado Lottery capitalized all personal computers regardless of their cost. Beginning January 1, 2004, the Colorado Lottery now capitalizes equipment only if the cost exceeds \$5,000 and has a useful life of more than one year. Depreciation for equipment is computed on the straight-line method over estimated useful lives ranging from three to ten years. Leasehold improvements are depreciated over the shorter of the lease term or the estimated useful lives of the improvements. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and resulting gains or losses are recognized in current operations.

The Colorado Lottery made the decision in May of 2003 to remove the Player Express Terminals (PES) from all retailers by the end of January 31, 2004. In accordance with GAAP the monthly depreciation on these PES terminals was adjusted (accelerated) to insure that they were fully depreciated by the end of their useful life or January 31, 2004. This accelerated depreciation increased the regular monthly depreciation on these PES terminals from \$30,000 per month to by \$52,061 per month for the effected months - May 2003 through January 2004. For Fiscal Year 2004, an additional \$154,427 of depreciation related to the PES terminals has been recorded and presented on the Lottery's financial statements.

### ***Prize Liability and Prize Expense***

Under the provisions of Section 24-35-210 (9),C.R.S., the Colorado Lottery must pay no less than fifty percent (50%) of total ticket sales as prizes. In the aggregate, all games to date are planned to pay 50% or more of total ticket sales in prizes. Additional prize expense and corresponding liability may be incurred as a result of market fluctuations in the cost of annuities used to pay Lotto jackpots (see Note 11).

All scratch, on-line, and special drawing prizes are accounted for using the accrual basis of accounting. The liability for scratch prizes and on-line prizes is recognized at the point of retail sale. The liability for special drawing prizes is accrued on the first day of sales.

Payments of scratch prize amounts of \$150 or less may be done at the Lottery or at the retail outlet; payment of scratch prize amounts of \$151 to \$600 may be done at the retailer level at the option of the retailer, or at the Lottery. Scratch prizes of \$600 or more are paid by the Lottery. Retailers are given credit for prize payments they make on a daily basis. Prizes may be claimed up to 180 days after game-end. After the final claim date, any unclaimed scratch prizes will result in a decrease to prize expense, and any prizes claimed in excess of the liability accrued will result in an increase to prize expense. Net unclaimed

scratch prizes resulted in a decrease to prize expense of \$4,867,069 through the Fiscal Year Ended June 30, 2004 and \$4,857,072 through the Fiscal Year Ended June 30, 2003.

Payments of cumulative on-line prize amounts of \$150 or less on a single ticket may be done at the Lottery or at the retail outlet; payment of cumulative prize amounts of \$151 to \$600 on a single ticket may be done at the retailer level at the option of the retailer, or at the Lottery. Payment of cumulative prize amounts of \$600 or more on a single ticket must be done at the Lottery. Retailers are given credit for prize payments they make on a daily basis. On-line prizes may be claimed up to 180 days after the date of the drawing. After the final claim date, unclaimed on-line prizes will result in a decrease to prize expense so long as the aggregate prize expense of all games exceeds or equals the statutory fifty percent of sales. In the event that the expiration of an unclaimed prize would result in the aggregate prize expense of all games to fall below the statutory fifty percent level, the unclaimed prize amount would remain in prize expense and be paid out to players as a guaranteed additional prize. Unclaimed on-line prizes resulted in a decrease to prize expense of \$10,313,756 through the Fiscal Year Ended June 30, 2004 and \$9,433,114 through the Fiscal Year Ended June 30, 2003.

Powerball Prize Variance expense(revenue) represents a portion of the Powerball 50% prize expense accrual (as mandated by game rule) that is transferred to or received from the Multi-State Lottery Association (MUSL). Powerball Prize Variance expense occurs when Colorado's liability for any draw, which consists of the low-tier prizes won by Colorado players plus Colorado's contribution to the jackpot, is less than the 50% accrual. Powerball Prize Variance revenue occurs when Colorado's liability for any draw is greater than the 50% accrual. In the event the liability in any week exceeds the 50% accrual, MUSL will reimburse the excess to the lottery.

### ***Retailer Bonus Liability***

Under provisions 5.10 and 10.10 of the Colorado Lottery Commission Rules and Regulations effective as of July 1, 1997:

*". .the Director may provide such additional compensation to licensees as is deemed appropriate by the Director to further the sale of lottery tickets, so long as such additional compensation is made equally available to all licensees and does not exceed a total of One and Thirteen Hundredths Percent (1.13%) for scratch, Seven Tenths Percent (.7%) for Lotto, Sixty Five Hundredths Percent (.65%) for Powerball, and Ninety-six Hundredths Percent (.96%) for Cash 5."*

A portion of the additional compensation shall be used to pay each licensee, as a bonus, an amount (cashing bonus) equal to one percent (1%) of each prize paid by the licensee up to and including \$599.99.

At the Director's discretion, the residual resulting after paying the cashing bonuses may be used to provide additional compensation to licensees and/or to decrease the bonus expense by reverting the excess amount. The cashing bonus is accrued as tickets are sold and paid as winning tickets are redeemed. Any cashing bonuses unclaimed at the end of the claim period result in a reduction of bonus expense.

### ***Licensed Agent Recovery Reserve***

Under the provisions Section 24-35-219, C.R.S., a Licensed Agent Recovery Reserve was established on January 1, 1988 to maintain surety bond receipts collected from Colorado Lottery retailers. Billing rates are established by the Colorado Lottery Commission and are reviewed on an annual basis. Retailers have the option to obtain private surety bond coverage at a rate of \$2,000 surety coverage per outlet at their discretion.

### ***Compensated Leave***

All permanent employees of the Colorado Lottery may accrue annual and sick leave based on length of service subject to certain limitations on the amount that will be paid on termination. In addition, employees who are classified as non-exempt from overtime pay have accumulated overtime which must be taken as compensatory time or paid. The estimated cost of compensated absence for which employees are vested is as follows:

| <b>Increase</b>           | <b><u>June 30, 2004</u></b> | <b><u>June 30, 2003</u></b> | <b><u>(Decrease)</u></b> |
|---------------------------|-----------------------------|-----------------------------|--------------------------|
| Annual Leave              | \$ 593,571                  | \$ 776,768                  | \$ (183,197)             |
| Sick Leave                | <u>135,078</u>              | <u>192,701</u>              | <u>(57,623)</u>          |
| Total Annual & Sick Leave | 728,649                     | 969,469                     | (240,820)                |
| Compensatory Time         | <u>3,233</u>                | <u>2,326</u>                | <u>907</u>               |
| Total Compensated Leave   | <u>\$ 731,882</u>           | <u>\$ 971,795</u>           | <u>\$ (239,913)</u>      |

### ***Expired Warrants Liability***

Expired Warrants Liability represents the expiration of aged uncashed warrants and imprest checks over one (1) year old which expired on or before June 30, 2003. In accordance with Section 15-12-914 (2), C.R.S., recipients are entitled to claim payment up to 21 years after original date of issue. Pursuant to Section 24-35-212 (2), C.R.S., the amount of these uncashed warrants remained in the Lottery fund. Pursuant to the Unclaimed Property Act 38-13-113, the funds to cover the liability for any uncashed warrants, which expire after June 30, 2003 are transferred to the Unclaimed Property Fund. The Lottery must request reimbursement from the Unclaimed Property Fund for any warrants presented for payment, which have expired after June 30, 2003.

### ***Deferred Revenue***

The Colorado Lottery offers two methods of purchasing on-line tickets for future draws. One is purchased through the terminal, referred to as Advance Play, and allows the player to purchase on-line tickets good for up to 10 draws. The second method is restricted to Lotto tickets only and is purchased through the mail via a pre-printed form, referred to as subscription, and allows the player to purchase Lotto tickets good for up to 104 draws. The revenues generated from

both methods are recognized as the draws occur. Revenues for future draws are classified as a liability.

A detail of Deferred Revenue at June 30, 2004 and 2003, is as follows:

|                        | <u>2004</u>       | <u>2003</u>       |
|------------------------|-------------------|-------------------|
| Subscription           | \$ 114,843        | \$ 238,160        |
| Advance play-Lotto     | 97,477            | 84,643            |
| Advance play-Powerball | 56,042            | 68,889            |
| Advance play-Powerplay | 13,283            | 15,918            |
| Advance play-Cash 5    | <u>17,078</u>     | <u>18,294</u>     |
| Total Deferred Revenue | <u>\$ 298,723</u> | <u>\$ 425,904</u> |

### ***Promotional Activity***

The Colorado Lottery engages in two types of promotional activities in an attempt to enhance sales and to increase the player base. Specific promotional coupons and Lottery Bucks coupons are distributed to players through special promotions and can be redeemed at any retailer for a lottery product. Through the Fiscal Years Ended June 30, 2004 and 2003, 51,375 and 16,285 coupons were redeemed, respectively. Scratch tickets for specific games are given away as a more direct approach to introduce players to lottery games. Through the Fiscal Years Ended June 30, 2004 and 2003, 70,168 and 63,008 dollars worth of free scratch tickets were given away, respectively. Scratch tickets and coupons are valued at cost. Through the Fiscal Years Ended June 30, 2004 and 2003, \$80,591 and \$51,453, respectively, in promotional ticket expense was recorded as Marketing and Communications expense in the statements of revenues, expenses, and changes in fund net assets for coupons redeemed and scratch tickets given away.

## **2. CASH AND INVESTMENTS**

### ***Cash***

Cash includes petty cash, change funds, an imprest fund, a depository account, and cash on deposit with the State Treasurer. A detail of cash at June 30, 2004 and 2003 is as follows:

|                                      | <u>2004</u>       | <u>2003</u>       |
|--------------------------------------|-------------------|-------------------|
| Petty Cash                           | \$ 800            | \$ 1,950          |
| Change Funds                         | 70,300            | 50,300            |
| Imprest Fund                         | 350,000           | 350,000           |
| Depository Account                   | 30,000            | 15,000            |
| Cash on Deposit with State Treasurer | <u>23,469,555</u> | <u>29,230,225</u> |
| TOTAL UNRESTRICTED CASH              | 23,920,655        | 29,602,733        |



|  |                      |                      |
|--|----------------------|----------------------|
| Cash and Investments-Operating Reserve                     | 1,029,114            | 1,427,326            |
| Cash Restricted - Licensed Agent Recovery Reserve Receipts | <u>469,424</u>       | <u>460,638</u>       |
| TOTAL RESTRICTED CASH                                      | <u>1,498,538</u>     | <u>1,887,964</u>     |
| TOTAL CASH   | <u>\$ 25,419,193</u> | <u>\$ 31,490,697</u> |

***Cash on Deposit with State Treasurer***

Under the provisions of Section 24-35-210 (6), C.R.S., the State Treasurer shall invest the moneys of the Colorado Lottery in excess of operating and prize payment expenses and all authorized transfers. Interest or any other return on investments is paid to the Lottery Fund Account on a monthly basis. Actual interest payments are determined by the State Treasurer. The actual allocated interest annual yield for interest received from the State Treasurer during Fiscal Years 2004 and 2003 was approximately 3.17 percent and 4.52 percent respectively.

In addition, the State Treasurer pools these deposits and invests them in securities approved by Section 24-75-601.1, C.R.S. The Colorado Lottery reports its share of the Treasurer's unrealized gains and losses based on its participation in the State Treasurer's pool only at fiscal year end. Effective July 1, 1997, with the Lottery's initial adoption of Governmental Accounting Standards Board Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, all of the Treasurer's investments, which include the net Licensed Agent Recovery Reserve Receipts, are reported at fair value, which is determined based on quoted market prices. The State Treasurer does not invest any of the pool resources in any external investment pool, and there is no assignment of income related to participation in the pool. Additional information on the Treasurer's pool may be obtained in the State of Colorado's Comprehensive Annual Financial Report.

***Insured and Collateralized Deposits***

The Colorado Lottery has one imprest and one depository account with banking institutions. The depository account is used for the purpose of depositing daily collections throughout the State and transferring the collections to the State Treasurer in a timely manner.

The Public Deposit Protection Act requires financial institutions to collateralize any uninsured public deposits. At June 30, 2004 the Colorado Lottery had cash with a carrying value of \$380,000, and a bank balance of \$365,936 on deposit with banking institutions. Of the bank balance, \$100,000 is insured by federal insurance (FDIC); the amount not insured is covered by collateral held in the pledging institution's trust department in the State's name.

### **Statement of Cash Flows**

The statement of cash flows is prepared under the direct method then adjusted for prize payments and commission and bonus payments to retailers, which are netted from cash received from retailers and applied against account receivable balances. For cash flow purposes, cash and investments include restricted cash and investments held by the State Treasurer in its cash and investment pool.

### **Categorization of Deposits and Investments**

The Colorado Lottery's total bank balances are classified in the following three categories of credit risk:

Category 1 – Insured or collateralized with securities held by the Colorado Lottery or by its agent in the Colorado Lottery's name

Category 2 – Collateralized with securities held by the pledging financial institution's trust department or agent in the Colorado Lottery's name

Category 3 – Uncollateralized, including any bank balance that is collateralized with securities held by the pledging financial institution, or by its trust department or agent but not in the Colorado Lottery's name

Additionally, the Colorado Lottery classifies its investments in the following three categories of credit risk:

Category 1 – Insured or registered, or securities held by the Colorado Lottery or its agent in the Colorado Lottery's name

Category 2 – Uninsured and unregistered, with securities held by the counterparty's trust department or agent in the Colorado Lottery's name

Category 3 – Uninsured and unregistered, with securities held by the counterparty; or by its trust department or agent but not in the Colorado Lottery's name, including the portion of the carrying amount of any repurchase agreement that exceeds the market value of the underlying securities, if any

The cash deposits bank balance of \$365,936 (see C. above) is categorized as follows as of June 30, 2004:

|            |           |
|------------|-----------|
| Category 1 | \$100,000 |
| Category 2 | 265,936   |

For Cash on Deposit with State Treasurer, the State Treasurer's investments as of June 30, 2004 are Category 1 investments and its cash deposits are principally Category 2 deposits.

### 3. SCHEDULE OF CAPITAL ASSET ACTIVITY

| Capital Assets being depreciated:            | <u>June 30, 2003</u> | <u>Increases</u>    | <u>Decreases</u>    | <u>June 30, 2004</u> |
|--|----------------------|---------------------|---------------------|----------------------|
| Equipment                                    | \$ 5,559,322         | \$ 112,513          | \$(1,216,608)       | \$ 4,455,227         |
| Leasehold Improvements                       | <u>330,936</u>       | <u>0</u>            | <u>( 3,649)</u>     | <u>327,287</u>       |
| Total capital assets being depreciated       | 5,890,258            | 112,513             | (1,220,257)         | 4,782,514            |
| Less: accumulated depreciation for Equipment | (4,237,420)          | (475,046)           | 1,195,542           | (3,516,924)          |
| Leasehold Improvements                       | <u>(225,512)</u>     | <u>(14,563)</u>     | <u>3,599</u>        | <u>(236,476)</u>     |
| Total accumulated depreciation               | <u>(4,462,932)</u>   | <u>(489,609)</u>    | <u>1,199,141</u>    | <u>(3,753,400)</u>   |
| Total capital assets, being depreciated, net | <u>\$ 1,427,326</u>  | <u>\$ (377,096)</u> | <u>\$ ( 21,116)</u> | <u>\$ 1,029,114</u>  |

|  | <u>June 30, 2002</u> | <u>Increases</u>    | <u>Decreases</u>   | <u>June 30, 2003</u> |
|--|----------------------|---------------------|--------------------|----------------------|
| Equipment                                    | \$ 5,356,715         | \$ 311,456          | \$ (108,849)       | \$ 5,559,322         |
| Leasehold Improvements                       | <u>330,936</u>       | <u>0</u>            | <u>0</u>           | <u>330,936</u>       |
| Total capital assets being depreciated       | 5,687,651            | 311,456             | (108,849)          | 5,890,258            |
| Less: accumulated depreciation for Equipment | (3,873,966)          | (449,179)           | 85,725             | (4,237,420)          |
| Leasehold Improvements                       | <u>(210,949)</u>     | <u>(14,563)</u>     | <u>0</u>           | <u>(225,512)</u>     |
| Total accumulated depreciation               | <u>(4,084,915)</u>   | <u>(463,742)</u>    | <u>85,725</u>      | <u>(4,462,932)</u>   |
| Total capital assets, being depreciated, net | <u>\$ 1,602,736</u>  | <u>\$ (152,286)</u> | <u>\$ (23,124)</u> | <u>\$ 1,427,326</u>  |

### 4. OPERATING LEASES

The Colorado Lottery occupies office and warehouse space in Pueblo, Denver, Colorado Springs, Grand Junction, and Fort Collins. Rental payments are contingent upon the continuing availability of funds. Specific lease information follows:

#### ***Pueblo***

*Office* - The Colorado Lottery occupies office space in the Wells Fargo Bank Building in Pueblo. The lease agreement with 200 South Broadway Limited Partnership began on July 1, 1995 and expires on June 30, 2005. There is no provision for renewal.

*Warehouse* -The Colorado Lottery leases primary warehouse space from Santa Fe 250 LLC. The Lottery entered into a lease extension agreement, which began September 1, 2002 and expires on June 30, 2007. There is no provision for renewal.

*Interlott(G-Tech)* - The Colorado Lottery entered into a rental agreement with International Lottery, Inc., subsequently purchased by G-Tech, to rent Scratch Ticket Vending Machines (STVMs). The agreement covers the period from July 1, 2000 through June 30, 2002. The Lottery had the option to exercise two twelve-month

extensions. On June 3, 2002 the Lottery entered into a contract with Interlott to exercise both twelve-month extensions plus an additional four month extension which will expire on October 31, 2004. There are no other provisions for extension or renewal.

**Denver**

*Office* - The Colorado Lottery occupies office and warehouse space in the Galleria Towers Building in Denver. The lease agreement, which began on October 30, 1990, was amended on May 14, 1999 and extended the ending date for the lease from June 30, 1999 to June 30, 2006. There is no provision for renewal.

*Warehouse* – The Colorado Lottery entered into a lease agreement with Yukon Denver Valley, Inc. to occupy warehouse space. The lease agreement began on September 1, 1999 and expires on August 31, 2004. The Lottery has the option to extend the lease through August 31, 2009.

**Fort Collins**

The Colorado Lottery occupies space leased by the Department of Revenue and is responsible for reimbursing the Department of Revenue for lease payments.

**Grand Junction**

The Colorado Lottery occupies space in the Grand Junction State Services Building and is responsible for reimbursing the Capital Complex Division for lease payments.

**Colorado Springs**

The Colorado Lottery occupies warehouse space in a building located at 2818 Janitell Rd. in Colorado Springs, Colorado. The lease agreement, which began on August 1, 2003, expires on June 30, 2006. The Lottery has the option to exercise two twelve-month extensions under the new lease, extending the lease through June 30, 2008. There are no other provisions for renewal.

Operating lease expense incurred for the Fiscal Years Ended June 30, 2004 and 2003 and future minimum lease payments are as follows:

| Location          | Expense            |                    | Future Minimum Lease Payments |                  |                  |             |             | LATER YEARS |
|-------------------|--------------------|--------------------|-------------------------------|------------------|------------------|-------------|-------------|-------------|
|                   | 2003               | 2004               | FY 2005                       | FY 2006          | FY 2007          | FY 2008     | FY 2009     |             |
| Pueblo Office     | \$262,692          | \$275,900          | \$289,773                     | \$ 0             | \$ 0             | \$ 0        | \$ 0        | \$ 0        |
| Pueblo Warehouse  | 74,654             | 85,885             | 88,398                        | 91,052           | 78,623           | 0           | 0           | 0           |
| Interlott         | 651,273            | 652,389            | 217,800                       | 0                | 0                | 0           | 0           | 0           |
| CoSprgs Warehouse | 13,812             | 11,728             | 12,000                        | 12,466           | 0                | 0           | 0           | 0           |
| Denver            | 197,373            | 203,354            | 209,335                       | 215,316          | 0                | 0           | 0           | 0           |
| Denver Warehouse  | 103,622            | 107,039            | 16,844                        | 0                | 0                | 0           | 0           | 0           |
| Fort Collins      | 36,720             | 36,720             | 0                             | 0                | 0                | 0           | 0           | 0           |
| Grand Junction    | 4,063              | 4,557              | 0                             | 0                | 0                | 0           | 0           | 0           |
|                   | <u>\$1,344,209</u> | <u>\$1,377,572</u> | <u>\$ 834,150</u>             | <u>\$318,834</u> | <u>\$ 78,623</u> | <u>\$ 0</u> | <u>\$ 0</u> | <u>\$ 0</u> |

## 5. OTHER REVENUE

A schedule of other revenue for the Fiscal Years Ended June 30, 2004 and 2003 follows:

|  | <u>2004</u>       | <u>2003</u>       |
|--|-------------------|-------------------|
| License Fees                                 | \$ 61,047         | \$ 56,376         |
| Fines & Penalties                            | 24,600            | 16,250            |
| Assignment Fees                              | 7,012             | 10,803            |
| Net Licensed Agent Recovery Reserve Receipts | 8,786             | (3,458)           |
| Other  | <u>55,545</u>     | <u>223,163</u>    |
| Total  | <u>\$ 156,990</u> | <u>\$ 303,134</u> |

## 6. LOTTERY FUND NET ASSETS

In accordance with Section 24-35-210(4.1) (a), C.R.S., the Lottery Commission shall, reserve "...sufficient moneys to ensure the operation of the Lottery for the ensuing year." Under the provision, the Lottery Commission approved a reserve of \$1 million of net assets for Fiscal Year 1989. This remained in effect until the implementation of GASB 34 required a net asset balance sufficient to cover the net value of an agency's capital assets. Accordingly, at the June 2002 commission meeting, the Lottery Commission approved a balance in net assets "equal to the net value of the Lottery's capital assets". The net asset balances for the Fiscal Years Ended June 30, 2004 and June 30, 2003 are composed of the following:

|  | <u>2004</u>         | <u>2003</u>         |
|--|---------------------|---------------------|
| Investment in Capital Assets - GASB 34     | \$ 1,029,114        | \$ 1,427,326        |
| Restricted-Licensed Agent Recovery Reserve | 469,424             | 460,638             |
| Unrealized Gain on Investments-GASB 31     | 147,057             | 1,007,988           |
|  | <u>\$ 1,645,595</u> | <u>\$ 2,895,952</u> |

## 7. DISTRIBUTION OF NET PROCEEDS

Under the provisions of Section 33-60-104, C.R.S., distributions of net proceeds shall be made on a quarterly basis. The State Treasurer shall distribute net lottery proceeds as follows: forty percent (40%) to the Conservation Trust Fund, ten percent (10%) to the Division of Parks and Outdoor Recreation and all the remaining net lottery proceeds in trust to the trust fund board to be split between the Great Outdoors Colorado Trust Fund, and any excess to the General Fund of the State of Colorado as set forth in Section 33-60-104 (1) (c), C.R.S., and Section 33-60-104 (2), C.R.S. For each quarter including and after the first quarter of the State's Fiscal Year 2002, all moneys that would otherwise be transferred to the General Fund shall be transferred to the State Public School Fund as a contingency reserve as set forth in Section 22-54-117 (1.6), C.R.S.

Income available for distribution at June 30:

|  | <u>2004</u>          | <u>2003</u>          |
|--|----------------------|----------------------|
| Income before distributions                | \$ 102,821,101       | \$ 104,998,736       |
| Change in licensed agent recovery reserve  | (8,786)              | 3,458                |
| Change in fair market value of investments | 860,931              | (398,543)            |
| Other changes in net assets                | <u>398,212</u>       | <u>176,410</u>       |
| Income Available for Distribution          | \$ 104,071,458       | \$ 104,779,061       |
| Less distributions prior to year end       | <u>(78,265,937)</u>  | <u>(79,366,128)</u>  |
| Income Available for Distribution          | <u>\$ 25,805,521</u> | <u>\$ 25,412,933</u> |

The following is a schedule of funds available for distribution for the fiscal year end, the proceeds distributions by fund for the fiscal year end, and distributions paid by fund for the fiscal year end:

|   | <u>Accrued at<br/>June 30, 2003</u> | <u>Proceeds<br/>Distributions<br/>Expense</u> | <u>Distributions<br/>Paid</u> | <u>Accrued at<br/>June 30, 2004</u> |
|---|-------------------------------------|---|-------------------------------|-------------------------------------|
| Great Outdoors Colorado                   | \$ 9,016,090                        | \$ 49,639,294                                 | \$(48,149,060)                | \$ 10,506,324                       |
| State Public School Fund                  | 3,690,377                           | 2,396,438                                     | (3,690,377)                   | 2,396,438                           |
| Conservation Trust Fund                   | 10,165,173                          | 41,628,583                                    | (41,471,547)                  | 10,322,209                          |
| Division of Parks & Outdoor<br>Recreation | <u>2,541,293</u>                    | <u>10,407,143</u>                             | <u>(10,367,886)</u>           | <u>2,580,550</u>                    |
|   | <u>\$ 25,412,933</u>                | <u>\$ 104,071,458</u>                         | <u>\$(103,678,870)</u>        | <u>\$ 25,805,521</u>                |

|   | <u>Accrued at<br/>June 30, 2002</u> | <u>Proceeds<br/>Distributions<br/>Expense</u> | <u>Distributions<br/>Paid</u> | <u>Accrued at<br/>June 30, 2003</u> |
|---|-------------------------------------|---|-------------------------------|-------------------------------------|
| Great Outdoors Colorado                   | \$ 2,469,568                        | \$ 48,699,156                                 | \$ (42,152,634)               | \$ 9,016,090                        |
| General Fund                              | 8,499,940                           | 3,690,377                                     | (8,499,940)                   | 3,690,377                           |
| Conservation Trust Fund                   | 8,775,605                           | 41,911,625                                    | (40,522,057)                  | 10,165,173                          |
| Division of Parks & Outdoor<br>Recreation | <u>2,193,901</u>                    | <u>10,477,903</u>                             | <u>(10,130,511)</u>           | <u>2,541,293</u>                    |
|   | <u>\$ 21,939,014</u>                | <u>\$ 104,779,061</u>                         | <u>\$(101,305,142)</u>        | <u>\$ 25,412,933</u>                |

## 8. PENSION PLAN

### *Plan Description*

Virtually all of the Colorado Lottery's employees participate in a defined benefit pension plan. The plan's purpose is to provide income to members and their families at retirement or in case of death or disability. The plan is a cost-sharing multiple-employer plan administered by the Public Employees' Retirement Association (PERA). PERA was established by State statute in 1931. Responsibility for the organization and administration of the plan is placed with the Board of Trustees of PERA. Changes to the plan require legislation by the General Assembly. The State plan and other divisions' plans are included in PERA's financial statements which may be obtained by writing PERA at 1300

Logan Street, Denver, Colorado 80203, or by calling PERA at 303-832-9550 or 1-800-729-PERA (7372) or by visiting [www.copera.org](http://www.copera.org).

Plan members vest after five years of service and most are eligible for retirement benefits at age 50 with 30 years of service, age 60 with 20 years of service, or at age 65 with 5 years of service. Members are also eligible for retirement benefits without a reduction for early retirement if they are at least 55 and have a minimum of 5 years of service credit, and their age plus years of service equals 80 or more. State troopers and judges comprise a small percentage of plan members but have higher contribution rates and are eligible for retirement benefits at different ages and years of service. Monthly benefits are calculated as a percentage of highest average salary (HAS). HAS is one-twelfth of the average of the highest salaries on which contributions were paid, associated with three periods of 12 consecutive months of service credit.

Members disabled, who have five or more years of service credit, six months of which has been earned since the most recent period of membership, may receive retirement benefits if determined to be permanently disabled. If a member dies before retirement, their spouse or their eligible children under the age of 18 (23 if a full time student) are entitled to monthly benefit payments. If there is no eligible spouse, financially dependent parents will receive a survivor's benefit.

### ***Funding Policy***

Most employees contribute 8.0% (10.0% for State Troopers) of their annual gross covered wages to an individual account in the plan. During Fiscal Year 2004, the State contributed 10.15% (12.85% for State Troopers and 12.66% for the Judicial Branch) of the employee's gross covered wages. Effective January 1, 2003, 1.1% of the total contribution was allocated to the Health Care Trust Fund. Through May 31, 2004, the amount needed to meet the match requirement established by the PERA Board was allocated to the Matchmaker Program (See Note 9). The balance remaining after allocations to the Matchmaker Program and the Health Care Trust Fund was allocated to the defined benefit plan.

The annual gross covered wages subject to PERA is the gross earnings less any reduction in pay to offset employer contributions to the State sponsored IRC 125 plan established under Section 125 of the Internal Revenue Code. The contribution requirements of plan members and their employers are established, and may be amended, by the General Assembly.

The Colorado Lottery's contributions to the three programs described above for the Fiscal Years Ended June 30, 2004, 2003 and 2002 were \$656,365, \$659,854 and \$623,072, respectively. These contributions met the contribution requirement for each year.

## **9. VOLUNTARY TAX-DEFERRED RETIREMENT PLANS**

Beginning on January 1, 2001, the Matchmaker Program established a State match for PERA members' voluntary contributions to tax-deferred retirement plans. For Calendar Years 2001 and 2002, the match was 100% of up to 3% of the employees' gross covered wages paid during the month (7% for judges in the Judicial Branch). For Calendar Year 2003, the match was 100% of up to 2% of employee's gross covered wages paid during the month (6% for judges in the Judicial Branch). For Calendar Year 2004 through May 31, 2004, the match was 100% of up to 1% of employee's gross covered wages paid during the month (5% for judges in the Judicial Branch). The PERA Board sets the level of the match annually based on the actuarial funding of the defined benefit pension plan. Two percent of gross salary plus 50% of any reduction in the overall contribution rate due to overfunding of the pension plan was available for the match. While the plan was not overfunded in the current year, the maximum one-year change in the match rate is statutorily limited to 1%, and therefore, the match changed from 2% to 1% on January 1, 2004. Legislation passed in the 2004 session of the General Assembly terminated the match for pay periods ending after May 31, 2004. The match will resume when the actuarial value of the defined benefit plan assets are 110% of actuarially accrued plan liabilities.

PERA offers a voluntary 401(k) plan entirely separate from the defined benefit pension plan. The State offers a 457 deferred compensation plan and certain agencies and institutions of the State offer a 403(b) plan. Members who contribute to any of these plans also receive the State match.

The Colorado Lottery's contributions to the Program described above for the Fiscal Years ended June 30, 2004, 2003 and 2002 were \$77,307, \$138,919 and \$156,897, respectively.

## **10. POST RETIREMENT HEALTH CARE AND LIFE INSURANCE BENEFITS**

### ***HEALTH CARE PROGRAM***

PERACare (formerly known as the PERA Health Care Program) began covering benefit recipients and qualified dependents on July 1, 1986. This benefit was developed after legislation in 1985 established the Program and the Health Care Trust Fund. Under this program, PERA subsidizes a portion of the monthly premium for health care coverage. The benefit recipient pays any remaining amount of that premium through an automatic deduction from the monthly retirement benefit. During the Fiscal Year Ended June 30, 2004, the premium subsidy was \$115.00 for those with 20 years of service credit (\$230.00 for members under age 65 and not eligible for Medicare), and it was reduced by 5% for each year of service fewer than 20. Medicare eligibility also affects the premium subsidy.

The Health Care Trust Fund is maintained by an employer's contribution as discussed above in Note 8.



Monthly premium costs for participants depend on the health care plan selected, the number of persons being covered, Medicare eligibility, and the number of years of service credit. PERA contracts with a major medical indemnity carrier to administer claims for self-insured medical and prescription benefit plans, and with several health maintenance organizations providing services within Colorado. As of December 31, 2002, there were 35,418 enrollees in the plan.

***Life Insurance Program***

PERA provides its members access to two group life insurance plans offered by Prudential and Anthem Life (formerly known as Rocky Mountain Life). Members may join one or both plans, and they may continue coverage into retirement. Premiums are collected monthly by payroll deduction or other means.

**11. CONTINGENCIES AND COMMITMENTS**

Prize Annuities – The Colorado Lottery purchases annuity contracts in the name of individual jackpot prize winners. Although the annuity contracts are in the name of the individual winners, the Colorado Lottery retains title to the annuity contracts. The Colorado Lottery remains liable for the payment of the guaranteed minimum prizes in the event the insurance companies issuing the annuity contracts default. The following guaranteed minimum prize payments for which annuity contracts have been purchased are due in varying amounts through October 27, 2027.

|   |                       |
|---|-----------------------|
| Specified prize payments                | \$ 575,114,261        |
| Lifetime prize payments                 | <u>45,723,000</u>     |
| Total guaranteed minimum prize payments | <u>\$ 620,837,261</u> |

Self Insurance - The State of Colorado currently self-insures its agencies, officials and employees for the risks of losses to which they are exposed. That includes general liability, motor vehicle liability, workers' compensation and medical claims. The State Risk Management Fund is a restricted General Fund used for claims adjustment, investigation, defense and authorization for the settlement and payment of claims or judgements against the State except for employee medical claims. The State Employees and Officials Insurance Fund is an Internal Service Fund established for the purpose of risk financing employees' and officials' medical claims. Property claims are not self-insured; rather the State has purchased insurance.

Colorado employers are liable for occupational injuries and diseases of their employees. Benefits are prescribed by the Worker's Compensation Act of Colorado for medical expenses and loss of wages resulting from job-related disabilities. The State utilizes the services of Pinnacol Assurance (formerly Colorado Compensation Insurance Authority), a related party, to administer its plan. The State reimburses Pinnacol Assurance for the current cost of claims paid and related administrative expenses.

The Colorado Lottery participates in the Risk Management Fund. State agency premiums are based on an assessment of risk exposure and historical experience. Liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. Liabilities include an amount for claims that have

been incurred but not reported. Because actual claims liabilities depend on such complex factors as inflation, changes in legal doctrines and damage awards, the process used in computing claims liability does not necessarily result in an exact amount. Claims liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims and other economic and social factors.

The limits of liability for which the State accepts responsibility pursuant to Section 24-10-114 (1), C.R.S., are as follows:

**Liability**

General & Automobile

**Limits of Liability**

Each person \$150,000  
Each occurrence \$600,000

***Medical and Disability Benefits***

The Group Benefit Plans Fund is a Pension and Other Employee Benefits Fund established for the purpose of risk financing employee and State-official medical claims. The fund includes several medical plan options ranging from provider of choice to managed care. Before January 1, 2000, the State offered a variety of medical plans; some of the plans were fully insured while others were self-insured using Anthem Blue Cross Blue Shield as the plan administrator. After January 1, 2000, self-insured plans were no longer offered, and the State and its employees paid premiums for insurance purchased to cover medical claims. Through Fiscal Year 2001-02, the Group Benefit Plans Fund continued to cover claims originating before January 1, 2000. The State's contribution to the premium is fixed in statute; State employees pay the difference between the statutory contribution and the premium set by the insurer.

Before January 1, 1999, the Group Benefit Plans Fund provided an employer-paid short-term disability plan for all employees. On January 1, 1999, the Public Employees Retirement Association (PERA) began covering short-term disability claims for State employees eligible under its retirement plan. The Group Benefit Plans Fund continues to provide short-term disability coverage for employees not yet qualified for the retirement plan and secondary benefits for employees also covered under the PERA short-term disability plan. The Group Benefit Plans program provides an employee with 60 percent of their pay beginning after 30 days of disability or the exhaustion of the employee's sick leave balance, whichever is later. This benefit expires six months after the beginning of the disability. Although fully insured, the Group Benefit Plans disability program includes a risk-sharing feature that provides experience rating refunds and a termination premium that is calculated as earned premium less the aggregate of incurred claims, claim reserve, retention charge and refunds paid previously over the term of the contract. Refunds, when applicable, are paid annually while deficits are carried forward.

Furniture and Equipment - The State of Colorado carries a \$15,000 deductible replacement policy on all State owned furniture and equipment. For each loss incurred, the Colorado Lottery is responsible for the first \$1,000 of the deductible and the State of Colorado is responsible for the next \$14,000. Any loss in excess of \$15,000 is covered by the insurance carrier up to replacement cost.

Gaming Operations Commitments – The Colorado Lottery has entered into long term contracts with certain significant vendors related to providing scratch tickets and on-line data processing services in support of the Colorado Lottery's gaming operations. The

on-line data processing extended contract expires October 31, 2004 and is not being renewed. The total amount to be paid on the on-line data contract shall not exceed \$51,800,000 over the period of the contract. The Colorado Lottery entered into a new on-line data processing contract with a new vendor on May 13, 2003. The contract period began on June 1, 2003 and will expire on October 31, 2010. Renewal options include two additional two year periods and two additional periods of ninety days for conversion and turnover purposes. The total cost of the initial contract period is not to exceed \$56,235,000. The scratch ticket contract expired June 30, 2004 with one annual renewal available. The renewal option was exercised extending the contract through June 30, 2005. Ticket rates are based upon ticket volume, physical size and design. The total costs of the extended contract shall not exceed \$14,445,184, and shall not exceed \$2,600,000 for the extension period.

The Colorado Lottery was approved for membership by the Multi-State Lottery Association (MUSL) on February 26, 2001 and thus entered into an agreement with MUSL on June 6, 2001 to become a member and participate in Powerball games. As a member, the Colorado Lottery agrees to abide by the terms of the Multi-State Agreement dated September 16, 1987 and to any amendments to that agreement duly made by the board. The Colorado Lottery will remain a member indefinitely. Pursuant to this agreement the Colorado Lottery will make payments to MUSL for administrative fees, weekly prize expenses, promotional purchases, miscellaneous reimbursements and assessments, and contributions to the prize reserves. The total amount to be contributed to the prize reserves as of June 30, 2004 is \$3,728,493. The total amount of the prize reserves funded as of June 30, 2004 was \$3,525,880 shown as prepaid prize expense with MUSL on the Statement of Net Assets.

Other Major Vendor Commitments – The Colorado Lottery entered into a long-term contract with an advertising agency to provide advertising services to promote the Colorado Lottery's products. The contract provided for expiration on June 30, 2002 with an option to renew up to three additional years through June 30, 2005. The total cost of the initial contract period was not to exceed \$16,320,000. On May 15, 2002, the Colorado Lottery exercised its option to renew the contract for a period of two years, extending it until June 30, 2004. The maximum cost shall not exceed \$8,500,000 in Fiscal Year 2003 and shall not exceed \$17,000,000 for the extended contract period. On June 10, 2004, the Colorado Lottery entered into a new long-term contract with the same agency. The contract period began on July 1, 2004 and expires on June 30, 2006 with an option to renew up to three additional one year periods through June 30, 2009. The total cost of the initial contract period is not to exceed \$9,000,000 for each year.

Litigation: In Fiscal Year 2001, a plaintiff filed a class action suit claiming that the Colorado Lottery breached its contract with players by continuing to sell tickets in games in which the top prize had already been claimed. Although litigation continues, it is the opinion of Lottery's management that the ultimate outcome of this matter will not have a material impact on the Lottery's financial statements.

## **12. TAX, SPENDING AND DEBT LIMITATIONS**

In November 1992, the Colorado voters passed Section 20, Article X of the Colorado Constitution, commonly known as the Taxpayer's Bill of Rights (TABOR). TABOR contains revenue, spending, tax and debt limitations that apply to the State of Colorado and all local governments. In the same general election, Article XXVII was passed

creating the State Board of the Great Outdoors Colorado Trust Fund. The simultaneous passage of these two constitutional amendments raised questions as to whether there are irreconcilable conflicts between the two amendments.

The General Assembly determined in Section 24-77-102 (17) (b) (IX), C.R.S., that the net proceeds from the Colorado Lottery are excluded from the scope of "State Fiscal Year spending" for purposes of TABOR. The Colorado Supreme Court, in response to an interrogatory from the General Assembly, approved that determination.

TABOR is complex and subject to further legislative and judicial interpretation. The Colorado Lottery believes it is in compliance with both of these constitutional amendments.

### **13. RELATED PARTY TRANSACTIONS**

The Colorado Lottery, as an agency of the State of Colorado, paid fees to other agencies of the State for auditing, legal and other services and vehicle and office rent. The Colorado Lottery also pays fees to the Department of Revenue for indirect costs. Interagency charges were \$985,613 and \$955,627 for the Fiscal Years Ended June 30, 2004 and June 30, 2003, respectively.

***SUPPLEMENTARY***

***INFORMATION***

COLORADO LOTTERY  
BUDGETARY COMPARISON  
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

|                                | FY04<br>Original<br>Budget | Supplementals<br>Pots Allocations<br>& Internal Transfers | FY04<br>Final<br>Budget | FY04<br>Actual<br>Expenditures | Under<br>Expended   | Percent<br>Under<br>Expended |
|--------------------------------|----------------------------|---|-------------------------|--------------------------------|---------------------|------------------------------|
| Personal Services              | \$7,999,032                | \$7,338   | \$8,006,370             | \$7,842,729                    | \$163,641           | 2.04%                        |
| Operating                      | 1,946,994                  | 90,470  | 2,037,464               | 1,953,800                      | 83,664              | 4.11%                        |
| Vehicle Lease Payments         | 181,492                    | (29,320)  | 152,172                 | 152,171                        | 1                   | 0.00%                        |
| Purch. Serv. Comp. Cen.        | 8,834                      | 0   | 8,834                   | 8,834                          | 0                   | 0.00%                        |
| Telecommunications             | 397,412                    | (80,000)  | 317,412                 | 252,725                        | 64,687              | 20.38%                       |
| MNT Payments                   | 0                          | 74,625  | 74,625                  | 74,625                         | 0                   | 0.00%                        |
| Payments to Other Agencies     | 340,488                    | 0   | 340,488                 | 340,488                        | 0                   | 0.00%                        |
| Legal Services                 | 40,425                     | 12,158  | 52,583                  | 33,513                         | 19,070              | 36.27%                       |
| Workmen's Compensation         | 0                          | 43,391  | 43,391                  | 43,391                         | 0                   | 0.00%                        |
| Unemployment Benefits          | 0                          | 1,867   | 1,867                   | 0                              | 1,867               | 100.00%                      |
| Health and Life                | 0                          | 275,346   | 275,346                 | 259,119                        | 16,227              | 5.89%                        |
| Short Term Disability          | 0                          | 13,482  | 13,482                  | 9,328                          | 4,154               | 30.81%                       |
| Leased Space                   | 774,513                    | 0   | 774,513                 | 766,482                        | 8,031               | 1.04%                        |
| Grand Junction - Leased Space  | 4,557                      | 0   | 4,557                   | 4,557                          | 0                   | 0.00%                        |
| Risk Management                | 0                          | 26,590  | 26,590                  | 26,590                         | 0                   | 0.00%                        |
| Capital Outlay                 | 0                          | 0   | 0                       | 0                              | 0                   | #DIV/0!                      |
| Info Tech Asset Maint (PC's)   | 0                          | 0   | 0                       | 0                              | 0                   | #DIV/0!                      |
| Travel Expenses                | 119,941                    | 0   | 119,941                 | 111,351                        | 8,590               | 7.16%                        |
| Marketing and Communications   | 9,097,225                  | 0   | 9,097,225               | 8,643,420                      | 453,805             | 4.99%                        |
| Indirect Costs                 | 384,804                    | (53,878)  | 330,926                 | 330,926                        | 0                   | 0.00%                        |
| Ticket Costs                   | 3,991,040                  | 98,640  | 4,089,680               | 2,987,133                      | 1,102,547           | 26.96%                       |
| Vendor Fees                    | 8,185,514                  | (78,666)  | 8,106,848               | 7,208,951                      | 897,897             | 11.08%                       |
| Prizes                         | 280,095,384                | (7,047,864)   | 273,047,520             | 238,427,918                    | 34,619,602          | 12.68%                       |
| Powerball Prize Variance       | 4,610,000                  | (45,000)  | 4,565,000               | 4,098,836                      | 466,164             | 10.21%                       |
| Retailer Compensation          | 35,566,840                 | 187,020   | 35,753,860              | 30,255,252                     | 5,498,608           | 15.38%                       |
| CMAC Project-Cap. Construction | 1,460,795                  | 0   | 1,460,795               | 371,865                        | 1,088,930           | 74.54%                       |
| Multi-State Lottery Fees       | 177,433                    | 0   | 177,433                 | 156,999                        | 20,434              | 11.52%                       |
| <b>TOTAL</b>                   | <b>\$355,382,723</b>       | <b>(\$6,503,801)</b>                                      | <b>\$348,878,922</b>    | <b>\$304,361,003</b>           | <b>\$44,517,919</b> | <b>12.76%</b>                |

FY03-04 Staffing (FTE) 128.00 (Appropriated) 120.014 (Actual)

Reconciliation of Expenses per "Statement of Revenues, Expenses and Changes in Net Assets" to Budgeted Expenditures:

Expenses Per Statement of Revenues, Expenses and Changes in Net Assets

|                               |                   |
|-------------------------------|-------------------|
| Prize Expense                 | 238,427,919       |
| Powerball Prize Variance      | (1,824,959)       |
| Commissions and Bonuses       | 30,255,251        |
| Cost of Tickets & Vendor Fees | 9,654,016         |
| Operating Expenses            | <u>22,074,817</u> |

Total Expenses per Statement of Revenues, Expenses and Changes in Net Assets 298,587,044

Plus: Powerball Variance classified as revenue 5,923,795

Less: Non-appropriated expenses

|                                  |                 |
|----------------------------------|-----------------|
| Depreciation                     | (489,609)       |
| Accrued Annual and Sick Leave    | 248,377         |
| Book Value of Assets Written-Off | <u>(21,117)</u> |

Sub-Total 304,248,490

Plus: Capitalized Fixed Assets

112,513  
304,361,003

COLORADO LOTTERY  
SCHEDULE OF REVENUE AND COSTS FOR SCRATCH AND ON-LINE GAMES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

|   | Games in Progress   |                     |                     |                    | FY 03-04             | FY 02-03             |
|---|---------------------|---------------------|---------------------|--------------------|----------------------|----------------------|
|   | Scratch             | Lotto               | Powerball           | Cash 5             | Total                | Scratch and On-Line  |
| TICKET SALES(Net of Coupons)                              | \$260,901,964       | \$40,811,438        | \$85,030,889        | \$14,506,680       | \$401,250,971        | \$391,473,640        |
| PRIZE EXPENSE   | (168,211,132)       | (22,403,120)        | (39,584,517)        | (8,229,150)        | (238,427,919)        | (227,514,771)        |
| POWERBALL PRIZE VARIANCE                                  | N/A                 | N/A                 | 1,824,959           | N/A                | 1,824,959            | 597,361              |
| NET REVENUE AFTER PRIZES                                  | <u>92,690,832</u>   | <u>18,408,318</u>   | <u>47,271,331</u>   | <u>6,277,530</u>   | <u>164,648,011</u>   | <u>164,556,230</u>   |
| COMMISSIONS, BONUSES, TICKET COSTS & VENDOR FEES (Note 1) |                     |                     |                     |                    |                      |                      |
| Retailer Commission                                       | (18,231,795)        | (2,416,392)         | (5,101,578)         | (870,439)          | (26,620,204)         | (25,965,985)         |
| Retailer Bonus  | (2,678,063)         | (263,910)           | (557,049)           | (136,025)          | (3,635,047)          | (3,562,986)          |
| Cost of Tickets Sold                                      | (2,987,133)         | N/A                 | N/A                 | N/A                | (2,987,133)          | (3,175,336)          |
| In-Lane Vendor Fees                                       | 0                   | (9,910)             | (20,646)            | (3,522)            | (34,078)             | (202,633)            |
| On-Line Vendor Fees                                       | (1,012,205)         | (1,677,512)         | (3,327,928)         | (615,160)          | (6,632,805)          | (6,620,643)          |
| TOTAL   | <u>(24,909,196)</u> | <u>(4,367,724)</u>  | <u>(9,007,201)</u>  | <u>(1,625,146)</u> | <u>(39,909,267)</u>  | <u>(39,527,583)</u>  |
| GROSS PROFIT ON SALE OF TICKETS                           | <u>\$67,781,636</u> | <u>\$14,040,594</u> | <u>\$38,264,130</u> | <u>\$4,652,384</u> | <u>\$124,738,744</u> | <u>\$125,028,647</u> |
| AVERAGE DAILY TICKET SALES                                | <u>\$712,847</u>    | <u>\$111,507</u>    | <u>\$232,325</u>    | <u>\$39,636</u>    | <u>\$1,096,314</u>   | <u>\$1,072,531</u>   |

Note 1: Administrative costs of Lottery operations, including wages, advertising and other expenses are not shown.

COLORADO LOTTERY  
SCHEDULE OF PERCENT OF PRIZE EXPENSE TO GROSS TICKET SALES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

|                                 | Games in Progress  |                   |                   |                   | Powerball Prize Variance | Coupons/ Free Plays | FY 03-04           |
|---------------------------------|--------------------|-------------------|-------------------|-------------------|--------------------------|---------------------|--------------------|
|                                 | Scratch            | Lotto             | Powerball         | Cash 5            |                          |                     | Total              |
| Prize Expense                   | \$168,242,838      | \$22,403,120      | \$39,584,517      | \$8,229,150       | -\$1,824,959             | (\$31,706)          | \$236,602,960      |
| (/)/Ticket Sales before coupons | <u>260,935,369</u> | <u>40,818,461</u> | <u>85,041,776</u> | <u>14,508,537</u> | N/A                      | <u>(53,172)</u>     | <u>401,250,971</u> |
| Prize %                         | <u>64.48%</u>      | <u>54.88%</u>     | <u>46.55%</u>     | <u>56.72%</u>     |                          | <u>59.63%</u>       | <u>58.97%</u>      |