



**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
LOTTERY AND CHARITABLE GAMES CONTROL BOARD**

Financial Statements and Management's Discussion and Analysis

September 30, 2004 and 2003

(With Independent Auditors' Report Thereon)

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
LOTTERY AND CHARITABLE GAMES CONTROL BOARD**

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**KPMG LLP**  
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## **Independent Auditors' Report**

To the Mayor and Members of  
The Council of the Government of the District of Columbia, and  
The Lottery and Charitable Games Control Board  
Washington, D.C.:

We have audited the accompanying financial statements of the District of Columbia Lottery and Charitable Games Control Board, an enterprise fund of the Government of the District of Columbia, as of and for the years ended September 30, 2004 and 2003, as listed in the Table of Contents. These financial statements are the responsibility of the District of Columbia Lottery and Charitable Games Control Board management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in note 2, the financial statements only present the District of Columbia Lottery and Charitable Games Control Board and do not purport to, and do not, present fairly the financial position of the Government of the District of Columbia as of September 30, 2004 and 2003, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the District of Columbia Lottery and Charitable Games Control Board, as of September 30, 2004 and 2003, and the changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated January 24, 2005 on our consideration of District of Columbia Lottery and Charitable Games Control Board's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our 2004 audit.



The Management's Discussion and Analysis on pages 3 through 10 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

January 24, 2005

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
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Management's Discussion and Analysis

September 30, 2004 and 2003

(Dollar amounts in thousands)

This discussion and analysis of the D.C. Lottery and Charitable Games Control Board's (the Lottery) financial performance provides an overview of its financial activities for the fiscal years ended September 30, 2004 and 2003. This discussion and analysis should be read in conjunction with the accompanying financial statements.

**Background and Other Significant Information**

The Lottery was established by Public Law 3-172 as an agency of the Government of the District of Columbia (District). In accordance with law, the Lottery is responsible for generating revenues through the sales of lottery products and required to remit monthly gaming revenues (less prizes, operating expenses, and a reserve not to exceed 2% of annual prize payments) to the General Fund of the District.

The Lottery's financial transactions are accounted for as an enterprise fund in the District's basic financial statements.

**Financial Highlights**

- Gross revenue from lottery gaming activities increased by \$3,243 or 1.36% from prior year amounts;
- Aggregate ticket sales for all games, excluding Powerball, increased by \$6,879 or 3.57% for the year;
- Total operating expenses increased \$1,753 or 1.05% as a result of an overall increase in ticket sales; and
- Transfers to the District's General Fund increased \$1,450 equivalent to 2.01% over the prior year's total.

To effectively understand the Lottery's operations and to assess its financial activities, the reader must pay attention to individual game sales, related prize expenses and payout percentages, and the resulting impact on change in net assets or amounts transferred to the District's General Fund. Prize payouts and Powerball sales have the most dramatic effect on transfer levels but are beyond the control of management.

**Using this Financial Report**

This financial report consists of a series of financial statements, prepared in accordance with Government Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. These statements focus on the financial condition, the results of operations, and cash flows of the Lottery as a whole.

One of the most important questions asked about the Lottery's finances is whether or not they have improved as a result of the year's activities. The key to understanding this core question is the Statements of Net Assets; the Statements of Revenues, Expenses, and Changes in Net Assets; and the Statements of Cash Flows. These statements present financial information in a form that is similar to that used by commercial entities.

The Lottery's net assets, the difference between assets and liabilities, are one indicator of the improvement or erosion of financial health. The Statements of Net Assets include all assets and liabilities. It is prepared under the economic resources measurement focus and the accrual basis of accounting, whereby revenues are recognized when earned and expenses are recognized when the related liability is incurred.

The Statements of Revenues, Expenses, and Changes in Net Assets present the revenues earned and the expenses incurred during each year. Activities are reported as either operating or nonoperating.

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Another important factor to consider when evaluating financial viability is the Lottery's ability to meet financial obligations as they come due. The Statements of Cash Flows present information related to cash inflows and outflows summarized by operating, capital and noncapital financing and investing activities.

**Financial Analysis**

The Lottery's net assets increased by \$14 and \$77 for the years ended September 30, 2004 and 2003, respectively. The following tables present a summary of the Lottery's financial information as of and for the years ended September 30, 2004, 2003, and 2002.

**Table 1: Summary of Net Assets**

	September 30		
	2004	2003	2002
Assets:			
Current unrestricted assets	\$ 14,562	14,497	13,574
Capital assets (net of accumulated depreciation)	1,030	1,354	1,495
Restricted investments	66,481	73,537	78,789
Total assets	<u>82,073</u>	<u>89,388</u>	<u>93,858</u>
Liabilities:			
Accounts payable and accrued expenses	3,852	3,704	4,084
Deferred revenues	306	271	131
Accrued prizes and commissions	7,858	8,314	7,369
Obligations for unpaid prizes	66,481	73,537	78,789
Total liabilities	<u>78,497</u>	<u>85,826</u>	<u>90,373</u>
Net assets:			
Invested in capital assets	1,030	1,354	1,495
Unrestricted	2,546	2,208	1,990
Total net assets	<u>\$ 3,576</u>	<u>3,562</u>	<u>3,485</u>

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**Table 2: Summary of Revenues, Expenses,  
 and Changes in Net Assets**

	Years ended September 30		
	2004	2003	2002
Operating revenues:			
Gaming revenues	\$ 241,133	237,890	211,151
Operating expenses:			
Prizes	122,318	123,564	110,741
Other	45,620	42,621	37,930
Total operating expenses	167,938	166,185	148,671
Operating income	73,195	71,705	62,480
Nonoperating revenues – interest and dividends	319	422	630
Income before transfers	73,514	72,127	63,110
Transfers to the District's General Fund	(73,500)	(72,050)	(63,000)
Change in net assets	\$ 14	77	110

Unrestricted net assets were \$2,546, \$2,208, and \$1,990 at September 30, 2004, 2003, and 2002, respectively, which represents an increase of \$338 in 2004 and an increase of \$218 in 2003. Current assets increased by \$65 in 2004 and increased by \$923 in 2003. Total liabilities decreased by \$7,329, or 8.54% for the year ended September 30, 2004 and \$4,547, or 5.03% for the year ended September 30, 2003 primarily due to the decrease in the Lottery's obligations for unpaid prizes.

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The Multi-State Lottery Association (MUSL) purchases U.S. government securities in the name of the Lottery for Lotto America and Powerball jackpot winners from the District of Columbia. Jackpot winners have the option of accepting the cash value of the jackpot amount or annuity payments for 25 years. The restricted investments balance of \$66,481, \$73,537, and \$78,789 in 2004, 2003, and 2002, respectively, represents the net present value of securities totaling \$80,137, \$88,794, and \$97,425 in 2004, 2003, and 2002, respectively, to fund future annuity installment payments. The account decreased \$7,056 and \$5,252 in value during 2004 and 2003, respectively, as the result of payments of \$8,631, net of unrealized losses of \$3,975, and \$3,215 in 2004 and 2003, respectively, and accretion of investments totaling \$5,550 and \$4,111 in 2004 and 2003, respectively. Corresponding amounts are recorded as obligations for unpaid prizes.

**Table 3: Gaming Revenue, Prizes, Commissions, and Transfers**

2004											
	Lucky Numbers	D.C. Four	Powerball	Quick Cash	Hot Five	Extra Games	Keno	Hot Lotto	Instant Games	Others	Total
Gaming revenue	\$ 69,512	71,588	40,871	4,161	4,345	143	9,711	1,356	38,940	506	\$ 241,133
Prizes	(32,955)	(33,190)	(19,142)	(2,715)	(2,008)	(77)	(5,892)	(682)	(25,657)	—	(122,318)
Agent's commissions	(4,545)	(4,115)	(2,235)	(232)	(274)	(9)	(656)	(73)	(2,869)	—	(15,008)
Gross margin	\$ 32,012	34,283	19,494	1,214	2,063	57	3,163	601	10,414	506	\$ 103,807
Transfers	\$ 24,175	26,275	14,150	720	1,620	23	1,950	—	4,587	—	\$ 73,500

  

2003											
	Lucky Numbers	D.C. Four	Powerball	Quick Cash	Hot Five	Lucky Numbers Extra	D.C. Four-Extra	Keno	Instant Games	Others	Total
Gaming revenue	\$ 70,268	71,894	44,360	4,217	4,841	360	600	3,791	36,904	655	\$ 237,890
Prizes	(35,848)	(35,413)	(21,415)	(755)	(2,473)	(226)	(380)	(2,312)	(24,742)	—	(123,564)
Agent's commissions	(4,597)	(4,082)	(2,400)	(212)	(300)	(25)	(41)	(254)	(2,781)	—	(14,692)
Gross margin	\$ 29,823	32,399	20,545	3,250	2,068	109	179	1,225	9,381	655	\$ 99,634
Transfers	\$ 22,325	24,535	16,238	2,810	1,385	—	125	585	4,047	—	\$ 72,050

  

2002											
	Lucky Numbers	D.C. Four	Powerball	Quick Cash	Hot Five	Lucky Numbers Extra	D.C. Four-Extra	Instant Games	Others	Total	
Gaming revenue	\$ 72,194	68,453	27,723	4,200	5,067	234	328	32,924	28	\$ 211,151	
Prizes	(34,692)	(36,146)	(12,039)	(3,215)	(2,635)	(151)	(211)	(21,652)	—	(110,741)	
Agent's commissions	(4,491)	(3,822)	(1,519)	(243)	(309)	(16)	(22)	(2,385)	—	(12,807)	
Gross margin	\$ 33,011	28,485	14,165	742	2,123	67	95	8,887	28	\$ 87,603	
Transfers	\$ 25,475	21,075	10,225	235	1,515	—	—	4,475	—	\$ 63,000	

Table 3 provides a comparison of sales, prizes, agent commissions, gross margin, and transfers to the District's General Fund generated by each lottery product offered in fiscal years 2004, 2003, and 2002. Overall gaming revenue sales totaled \$241,133, \$237,890, and \$211,151 in fiscal years 2004, 2003, and 2002, respectively. Prize expenses decreased by \$1,246 in 2004 and increased by \$12,823 in 2003. Total prize payouts as a percentage of sales decreased to 50.73% in 2004 for the year in comparison to 51.94% in 2003. Agent commissions increased by \$316 and \$1,885 in 2004 and 2003, respectively, due to the related increase in ticket sales.



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**Lucky Numbers**

Lucky Numbers is a daily three-digit game in which players may wager 50 cents or one dollar with nine ways to win prizes ranging from 25 to 500 dollars. Sales totaled \$69,512 in 2004 for a \$756 or 1.07% decrease over the prior year's sales level of \$70,268.

Prizes decreased to \$32,955 in 2004, a decrease of \$2,895 or 8.07% from the \$35,848 expensed in 2003. Agents/retailers commissions decreased \$52 due to reduced ticket sales and prize payouts in 2004. Net proceeds to the District's General Fund totaled \$24,175, a \$1,850 increase from the \$22,325 generated in 2003. The increase in transfer amount can be primarily attributed to the decrease in prize payouts and commissions offset by the reduction in ticket sales.

In 2003, sales totaled \$70,268 for a \$1,926 or 2.67% decrease over the 2002 sales level of \$72,194. The decrease represented a continuance of the game's declining sales trend for several years. The Lucky Numbers game accounted for 29.54% of total gaming revenue and 29.93% of the overall gross margin.

Prizes increased to \$35,848 in 2003, an increase of \$1,156 or 3.33% from the \$34,692 expensed in 2002. Agents/retailers commissions increased \$106 primarily as a result of increased prizes. The reduction in sales and increase in related expenses translated into net proceeds to the District's General Fund of \$22,325, a \$3,150 decrease from the \$25,475 generated the prior year.

**D.C. Four**

D.C. Four is a daily four-digit game with a fixed payout. Players may wager 50 cents or one dollar for a chance to win seven different ways. Sales totaled \$71,588 in 2004 for a \$306 or 0.43% decrease over the \$71,894 in the prior year.

Prizes totaled \$33,190 in 2004, a decrease of \$2,223 or 6.28% over the \$35,413 in prizes reported in 2003. Other operating costs, less prizes and commissions, increased by \$167 over the prior year's amount primarily due to contractual and other miscellaneous expenses. The decrease in sales and related prizes contributed to a \$1,883 increase in the gross margin when compared to the prior year. Net proceeds to the District's General Fund totaled \$26,275, an increase of \$1,740 or 7.09% from the \$24,535 transferred in 2003. The D.C. Four game accounted for 29.69% of total gaming revenue and 33.03% of the overall gross margin.

In 2003, sales totaled \$71,894 for a \$3,441 or 5.03% increase over the \$68,453 in the prior year. Prizes totaled \$35,413 in 2003, a decrease of \$733 or 2.03% over the \$36,146 in prizes reported in 2002. Other operating costs, less prizes and commissions, increased by \$636 over the prior year's amount primarily due to contractual and advertising expenses. The increase in sales, offset by related prizes and commissions resulted in a \$3,914 increase in the gross margin when compared to the prior year. Net proceeds to the District's General Fund totaled \$24,535, an increase of \$3,460 or 16.42% from the \$21,075 transferred in 2002. The game's activities accounted for 30.22% of total gaming revenue and 32.52% of the overall gross margin.

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**Powerball**

The Powerball game is a five out of fifty-three plus one out of forty-two online lottery game that pays a grand prize on an annuitized pari-mutuel basis and all other prizes on a fixed basis. The Powerball game is sponsored by the Multi-State Lottery Association (MUSL), a conglomerate of twenty-six states and the District of Columbia, that combines resources and sales to offer larger jackpots. Party lotteries pool their sales and other resources, but otherwise account for operations separately. Powerball sales of \$40,871 in 2004 represented a \$3,489 or 7.86% decrease from the \$44,360 generated in 2003. The decrease in sales can be attributed to four jackpots in 2004 ranging from \$100 million to \$222 million compared to four jackpots in the range of \$100 million to \$315 million during 2003.

Prizes amounted to \$19,142 for the year, representing a decrease of \$2,274 or 10.62% in relation to the \$21,415 expensed in 2003. Powerball prizes are expensed at the rate of 50.0% of sales intake offset by lapsed prizes. Other expenses, less prizes and commissions, increased by \$850 as a result of higher advertising costs. The decrease in sales partially offset by the related decrease in overall expenses account for the \$2,088 or a 12.86% reduction in net proceeds and transfers to the General Fund of \$14,150 from the \$16,238 transferred in 2003.

Powerball sales of \$44,360 in 2003 represented a \$16,637 or 60.01% increase from the \$27,723 generated in 2002. Powerball game sales are jackpot driven and the lack of medium to high jackpots severely hampered sales in 2002. There were four jackpots over \$100 million in 2003, with one eclipsing the \$314 million mark. This was in comparison to no jackpots in excess of \$100 million in 2002, which essentially accounted for the low sales volume. Another contributing factor to the decline in 2002 sales was the downturn in the economy, which impacted interest rates, causing jackpots to increase at a slower pace.

Prizes amounted to \$21,415 for the year representing an increase of \$9,376 or a 77.88% in relation to the \$12,039 expensed in 2002. Other expenses, less prizes and commissions, increased by \$955 in relation to the higher sales level. Higher sales partially offset by the related increases in expenses account for the \$6,013 or a 58.81% increase in net proceeds and transfers to the District's General Fund of \$16,238 from the \$10,225 transferred in 2002.

**Quick Cash**

The Quick Cash game is a six out of thirty-nine numbers daily online lotto type game that pays fixed prize payouts ranging from 10 to 250,000 dollars. Players receive three boards (set of six numbers) for one dollar. Quick Cash sales amounted to \$4,161 in fiscal year 2004 and reflected a marginal decrease over the \$4,217 sold in 2003.

Prizes in 2004 totaled \$2,715. This amount represented a \$1,959 or 259.44% increase over prize payments of \$755 in 2003. The increase was a result of the payout of nine prizes of \$250 that occurred in 2004. Net proceeds and transfers to the District's General Fund reflected a decrease from \$2,810 in 2003 to \$720 in 2004 as a result of the increase in prize payouts.

Quick Cash sales amounted to \$4,217 in fiscal year 2003 and reflected a marginal increase over the \$4,200 sold in 2002. Prizes in 2003 totaled \$755. This amount represented a \$2,460 or 76.52% decrease in prize payments from \$3,215 in 2002. The decline was a result of nine prizes of \$250 that occurred in 2002. Net proceeds and transfers to the District's General Fund reflected an increase to \$2,810 from \$235 in 2002.

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**Hot Five**

The Hot Five game is a five out of thirty-three numbers online lotto type game that pays fixed prize payouts ranging from one to 25,000 dollars. Players receive one wager (set of five numbers) for the sum of one dollar. Hot Five sales decreased by \$496 or 10.23% from a total of \$4,841 in 2003 to \$4,345 in 2004. Overall operating expenses decreased by \$730 from prior year levels. The decline in sales offset by the decline in operating expenses primarily account for the increase in the 2004 transfer amount of \$1,620 from \$1,385 transferred in 2003.

Hot Five sales decreased by \$226 or 4.46% from a total of \$5,067 in 2002 to \$4,841 in 2003. Overall operating expenses decreased by \$83 from prior year levels. The decline in sales primarily account for the reduced 2003 transfer amount of \$1,385 in comparison to \$1,515 transferred in 2002.

**Lucky Numbers Extra and D.C. Four-Extra**

The Lucky Numbers and D.C. Four-Extra games were launched on August 12, 2002. The games, introduced as online instant games, must be played in conjunction with the Lucky Numbers (three-digit) and D.C. Four (four-digit) games. For one dollar, a player can purchase a chance to win 3 to 500 dollars instantly on a three or four digit ticket prior to the midday or nightly drawing. The player requests an extra ticket when purchasing a three or four-digit ticket. The three or four-digit ticket is printed with an extra number for the extra game. If numerical digits of the extra ticket correspond diagonally to the Lucky Numbers or D.C. Four digits, the player is an instant winner for the sum displayed. Ticket sales for the two games totaled \$143 in fiscal year 2004 compared to a total of \$960 in 2003. This represents a \$817 or 85.11% decrease over prior years. Ticket sales totaled \$562 for approximately two months of operations in 2002. The games were discontinued effective February 2004.

Prizes in 2004 totaled \$77. This amount represented a \$529 or a 87.30% decrease from prize payments of \$606 in 2003. Net proceeds and transfers to the District's General Fund of \$23 reflected a \$102 decrease from the \$125 transferred in 2003. Prizes, commissions, start-up costs, and other expenses amounted to \$893 in 2002, resulting in a net operating loss of \$331 for the year.

**Keno**

Keno was launched on May 5, 2003. Keno is a 10/20/80 game with fixed prizes. Players choose to play from 1 to 10 spots, with each spot having a different prize structure. Players select twenty numbers from a field of 80 numbers. Draws are held every four minutes during valid game times. Payouts range from five dollars to 100,000 dollars.

Ticket sales totaled \$9,711 in 2004 compared to \$3,791 for the approximate five (5) months of operations in 2003. The increase of \$5,920 or 156.11% was primarily the result of a full year's operations and more Keno locations. The Keno Multiplier was also introduced as a supplement to the regular Keno game in May 2004, which also helped to enhance sales. Prize payments increased \$3,580 to \$5,892 in 2004 from \$2,312 for the partial year's operations in 2003. Increased sales in 2004 offset by additional operating expenses culminated into net proceeds and transfers to the District's General Fund of \$1,950 for an increase of \$1,365 over the transferred amount of \$585 in 2003. Ticket sales in 2003 of \$3,791 less prizes, commissions, start-up costs, and other expenses totaling \$3,162, resulted in net income of \$45.

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**Hot Lotto**

Hot Lotto was launched on April 5, 2004. The Hot Lotto game is a five out of thirty-nine plus one out of nineteen online lottery game that pays a grand prize, at the election of the player at time of ticket purchase, either on an annuitized pari-mutuel or cash option basis. All other prizes are paid on a fixed basis. The Hot Lotto game is sponsored by the Multi-State Lottery Association (MUSL), a conglomerate of seven states and the District of Columbia, that combined resources and sales to offer larger jackpots. The initial jackpot starts at \$1 million and drawings are held every Wednesday and Saturday. Party lotteries pool their sales and other resources, but otherwise account for operations separately. Ticket sales of \$1,356 in 2004 less operating expenses of \$1,489 resulted in net loss of \$133.

**Instant Games**

Instant or scratch games are designed to allow a player the opportunity to determine if he/she is a winner at the time of purchase. The price of tickets and prize structure are determined before the production of tickets. Instant ticket sales of \$38,940 in 2004 were \$2,036 or 5.52% greater than sales in 2003 of \$36,904.

Prizes in 2004 totaled \$25,657 and resulted in a prize expense increase of \$915 or 3.70% over \$24,742 in 2003. Other operating costs, less prizes and commissions, increased by \$475 over the prior year's amount primarily due to contractual and administrative expenses. Transfers to the General Fund of \$4,587 represent an increase of \$540 over the transfers amount of \$4,047 reported in 2003.

Instant ticket sales of \$36,904 in 2003 were \$3,980 or 12.09% greater than sales in 2002 of \$32,924. Prizes in 2003 totaled \$24,742 and represented an increase of \$3,090 or 14.27% over \$21,652 in 2002. Other operating costs, less prizes and commissions, increased by \$873 over the prior year's amount primarily due to contractual and administrative expenses. Transfers to the District's General Fund of \$4,047 represented a decrease of \$428 over the transfers of \$4,475 reported in 2002.

The Lottery has been able to stimulate sales over the past two years through games designed with higher prize payouts and the introduction of games with various price points up to 20 dollars. The average prize payout rate in 2004 was 65.89% versus 67.04% in 2003.

**Interest**

All idle cash of the Lottery is invested through the District's General Fund Pooled Investments Account. Powerball receipts transferred to MUSL to fund major jackpots are invested in securities prior to related jackpots being hit, and earnings are allocated quarterly to party lotteries. Interest income shown separately in the financial statements decreased by \$103 and \$208 in 2004 and 2003, respectively due to lower interest rates and the slow down in the economy.

**Contacting the Lottery**

Interested parties can contact the D.C. Lottery at D.C. Lottery and Charitable Games Control Board, 2101 Martin Luther King Jr. Avenue, S.E. Washington, D.C. 20020.

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Statements of Net Assets

September 30, 2004 and 2003

(Dollar amounts in thousands)

<b>Assets</b>	<b>2004</b>	<b>2003</b>
Current assets:		
Cash and cash equivalents	\$ 9,701	10,617
Accounts receivable, net	4,362	3,221
Inventory	485	647
Prepaid expenses and other	14	12
Restricted investments	8,631	8,631
Total current assets	23,193	23,128
Noncurrent assets:		
Capital assets, net	1,030	1,354
Restricted investments	57,850	64,906
Total noncurrent assets	58,880	66,260
Total assets	82,073	89,388
<b>Liabilities</b>		
Current liabilities:		
Accounts payable	2,950	2,752
Compensation liabilities	894	517
Deferred revenue	306	271
Accrued prizes and commissions	7,858	8,314
Other accrued liabilities	8	435
Obligations for unpaid prizes – current portion	8,631	8,631
Total current liabilities	20,647	20,920
Obligations for unpaid prizes – noncurrent portion	57,850	64,906
Total liabilities	78,497	85,826
<b>Net Assets</b>		
Invested in capital assets, net of related debt	1,030	1,354
Unrestricted	2,546	2,208
Total net assets	\$ 3,576	3,562

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

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
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Statements of Revenue, Expenses, and Changes in Net Assets

Years Ended September 30, 2004 and 2003

(Dollar amounts in thousands)

	2004	2003
Operating revenue:		
Gaming revenue	\$ 241,133	237,890
Operating expenses:		
Prizes	122,318	123,564
Agent's commissions	15,008	14,692
Contractor fees	14,342	12,639
Advertising	5,583	4,878
Administration	10,281	10,040
Amortization and depreciation	406	372
Total operating expenses	167,938	166,185
Operating income	73,195	71,705
Nonoperating revenues – interest income	319	422
Income before transfers	73,514	72,127
Transfers to District General Fund	(73,500)	(72,050)
Change in net assets	14	77
Net assets, beginning of year	3,562	3,485
Net assets, end of year	\$ 3,576	3,562

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

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
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Statements of Cash Flows

Years ended September 30, 2004 and 2003

(Dollar amounts in thousands)

	<b>2004</b>	<b>2003</b>
Operating activities:		
Cash receipts from customers	\$ 239,520	238,731
Cash receipts from others	506	655
Cash payments to vendors	(23,070)	(21,355)
Cash payments to employees	(6,826)	(6,553)
Cash payments for prizes and commissions	(137,783)	(137,311)
Net cash provided by operating activities	72,347	74,167
Capital and related financing activities – acquisition of fixed assets	(82)	(231)
Noncapital financing activities – transfers to District General Fund	(73,500)	(72,050)
Investing activities – interest income received	319	422
Net increase (decrease) in cash	(916)	2,308
Cash and cash equivalents – beginning of year	10,617	8,309
Cash and cash equivalents – end of year	\$ 9,701	10,617
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 73,195	71,705
Amortization and depreciation	406	372
Decrease (increase) in assets:		
Receivables	(1,141)	1,356
Inventory	162	36
Prepaid expenses and other	(2)	(7)
Increase (decrease) in liabilities:		
Accounts payable	198	(183)
Compensation liabilities	377	(209)
Deferred revenue	35	140
Accrued prizes and commissions	(456)	945
Other accrued liabilities	(427)	12
Net cash provided by operating activities	\$ 72,347	74,167

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

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
LOTTERY AND CHARITABLE GAMES CONTROL BOARD**

Notes to Financial Statements

September 30, 2004 and 2003

(Dollar amounts in thousands)

**(1) Organization**

The Lottery and Charitable Games Control Board (the Lottery) was established by Public Law 3-172 as an independent agency of the Government of the District of Columbia (District). In accordance with the law, the Lottery must remit its monthly gaming revenues, less prizes, operating expenses and a reserve not to exceed 2% of projected annual prize payments, to the General Fund of the District.

In addition to its responsibility for generating revenue through the sale of lottery products, the Lottery also oversees charitable gaming activities to include the licensing and regulation of charitable and other not-for-profit organizations conducting bingo, raffles, and other fund-raising activities within the District of Columbia. The mission of the Lottery with respect to charitable gaming is to insure that only qualified organizations are licensed to conduct fund-raising activities and that they are carried out in accordance with existing laws, rules, and regulations. Revenues generated through the issuance of licenses, processing fees, etc. are not intended to cover costs associated with overseeing program activities.

**(2) Summary of Significant Accounting Policies**

**(a) Basis of Presentation**

The Lottery's financial transactions are accounted for as an enterprise fund in the District's financial statements. The accompanying financial statements are only those of the Lottery and are not intended to present the financial position, changes in financial position, and cash flows of the District taken as a whole. The District provides certain legal, central accounting, and other services to the Lottery. The costs and revenue associated with these services are not reflected in these financial statements.

**(b) Basis of Accounting**

The accompanying financial statements are prepared on the accrual basis of accounting. Under this method, revenues are reported when earned and expenses are reported at the time the related liabilities are incurred. In accordance with Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Lottery has elected not to follow the Financial Accounting Standards Board (FASB) Statements and Interpretations, APB Opinions, and Accounting Research Bulletins issued after November 30, 1989.

**(c) Cash and Cash Equivalents**

The Lottery participates in the District's pooled cash program whereby cash that is not needed for immediate disbursement is pooled with that of the District and used to purchase current investments. In accordance with the law, the District may invest the pooled cash directly in, or through repurchase agreements, obligations of the United States or its agencies, which are fully guaranteed by the federal government, and in certificates of deposit, which are issued by federally insured banks. In accordance with District policies, substantially all deposits in the pooled cash program were insured or collateralized with securities held by the District or its agent in the District's name. Interest income from the investment of pooled cash is allocated to the Lottery based on the amount the



**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
 LOTTERY AND CHARITABLE GAMES CONTROL BOARD**

Notes to Financial Statements

September 30, 2004 and 2003

(Dollar amounts in thousands)

Lottery invests in the pool. The Lottery considers the pooled cash to be cash equivalents for the purpose of cash flows because the pool may not hold the securities for more than 91 days.

**(d) Inventory**

Inventory, consisting of instant lottery tickets, is valued at cost using the specific identification basis. The costs of the instant lottery tickets are recorded as an expense when the tickets are sold.

**(e) Capital Assets**

Capital assets are recorded at cost. The cost of major remodeling, betterments, and improvements of \$5 and greater are capitalized. Repairs and maintenance costs are expensed as incurred. When capital assets are retired or sold, the cost and related accumulated depreciation are removed from the appropriate property and equipment accounts, and resulting gains or losses are recorded.

Amortization and depreciation expense are calculated using the straight-line method over the following estimated useful lives:

Category	Estimated useful life
Machinery and equipment	5–8 years
Office furniture and fixtures	5–8 years
Leasehold improvements	5–15 years

**(f) Gaming Revenue**

Revenue from online tickets is recorded as gaming revenue when the drawings are held. Online tickets sold in advance are recorded as deferred revenue until the drawings are held. Revenue from instant tickets is recorded as gaming revenue when the tickets are activated.

**(g) Prize Expense**

Instant tickets prize expense is based on the prize payout percentage for each instant lottery game and is accrued as the related gaming revenue is earned. Prize expenses for online games, excluding the Powerball and Hot Five Lotto games, are accrued based on the draw liability associated with drawings for the specific games. Powerball and Hot Five Lotto prize expenses are recorded at the rate of 50% of ticket sales. The accrued prize liability represents a payable for prize amounts that have not been claimed as of each fiscal year-end. Prize expense for all games is reduced by the sum of lapsed prizes not claimed during the required period of one year from the sales draw date for online games and the respective game closing date for instant games.

**(h) Compensated Absences**

The Lottery permits employees to accumulate earned but unused vacation and sick pay benefits depending on the employee's length of service. Employees may not accumulate more than 240 hours

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
 LOTTERY AND CHARITABLE GAMES CONTROL BOARD**

Notes to Financial Statements

September 30, 2004 and 2003

(Dollar amounts in thousands)

of vacation benefits. The Lottery accrues for accumulated vacation as the benefits are earned by employees.

There is not a maximum limitation on the amount of unused sick pay benefits that employees may accumulate. The Lottery does not accrue for nonvesting accumulating rights to receive sick pay benefits. At the time of retirement, unused sick pay benefits are added to the retirees' years of service in the retirement programs.

*(i) Use of Estimates*

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

**(3) Accounts Receivable**

The components of accounts receivable as of September 30, 2004 and 2003 are as follows:

<u>Description</u>	<u>2004</u>	<u>2003</u>
Due from agents:		
Online games	\$ 1,204	485
Instant games	3,405	3,157
Total due from agents	4,609	3,642
Other	8	35
Total accounts receivable	4,617	3,677
Less allowance for doubtful accounts	(255)	(456)
Total accounts receivable, net	\$ 4,362	3,221

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
LOTTERY AND CHARITABLE GAMES CONTROL BOARD**

Notes to Financial Statements

September 30, 2004 and 2003

(Dollar amounts in thousands)

**(4) Capital Assets**

A summary of capital assets as of September 30, 2004 and 2003 is as follows:

	Balance as of October 1, 2003	Additions	Reductions	Balance as of September 30, 2004
Cost:				
Machinery and equipment	\$ 2,861	82	—	2,943
Office furniture and fixtures	321	—	—	321
Leasehold improvements	774	—	—	774
Total cost	<u>3,956</u>	<u>82</u>	<u>—</u>	<u>4,038</u>
Less accumulated depreciation:				
Machinery and equipment	1,852	347	—	2,199
Office furniture and fixtures	308	5	—	313
Leasehold improvements	442	54	—	496
Total accumulated amortization and depreciation	<u>2,602</u>	<u>406</u>	<u>—</u>	<u>3,008</u>
Capital assets – net	<u>\$ 1,354</u>			<u>1,030</u>

	Balance as of October 1, 2002	Additions	Reductions	Balance as of September 30, 2003
Cost:				
Machinery and equipment	\$ 2,630	231	—	2,861
Office furniture and fixtures	321	—	—	321
Leasehold improvements	774	—	—	774
Total cost	<u>3,725</u>	<u>231</u>	<u>—</u>	<u>3,956</u>
Less accumulated depreciation:				
Machinery and equipment	1,480	372	—	1,852
Office furniture and fixtures	308	—	—	308
Leasehold improvements	442	—	—	442
Total accumulated amortization and depreciation	<u>2,230</u>	<u>372</u>	<u>—</u>	<u>2,602</u>
Capital assets – net	<u>\$ 1,495</u>			<u>1,354</u>

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
 LOTTERY AND CHARITABLE GAMES CONTROL BOARD**

Notes to Financial Statements

September 30, 2004 and 2003

(Dollar amounts in thousands)

**(5) Multi-State Lottery Association**

**(a) Background**

The Lottery is a member of the Multi-State Lottery Association (MUSL). MUSL has 26 members and administers a multi-state lottery game. Powerball, the current game, was initiated on April 20, 1992 and is a semiweekly pari-mutuel drawing with a minimum grand prize of \$10. MUSL previously administered the Lotto-America game which was terminated on April 18, 1992. All MUSL members remit a portion of their Powerball revenue to MUSL for the prize payments and administrative expenses of Powerball.

**(b) Restricted Investments and Obligations for Unpaid Prizes**

Lotto-America and Powerball prizes of \$250 or greater are payable to the winner in annual installments over 25 years. The Lottery is responsible for sending the annual payments to Lotto-America and Powerball winners who purchased their winning tickets from the Lottery. MUSL is responsible for providing the Lottery cash to fund these installment payments.

As of September 30, 2004 and 2003, the cost of U.S. Government and Agency securities purchased by MUSL for the Lottery, aggregating \$80,163 and \$88,794, respectively, to fund future installment payments for the Lottery's Lotto-America and Powerball winners.

The market value of these securities was \$66,481 and \$73,537 as of September 30, 2004 and 2003, respectively. The investments provide the Lottery cash payments corresponding to the Lottery's obligations to send the annual installments to the prize winners. The Lottery has reflected the market value of the securities as restricted investments and as corresponding obligations for unpaid prizes on the statements of net assets. All restricted investments are insured and registered or are held by the Lottery or its agent in the Lottery's name.

As of September 30, 2004, the Lottery had the following investments and maturities:

Investment type	Fair value	Investment maturities (in years)			
		Less than 1	1 - 5	6 - 10	More than 10
U.S. Government and Agency Securities	\$ 66,481	8,631	36,690	18,575	2,585

These investments are obligations explicitly guaranteed by the U.S. government and are held for prize annuities based on quoted market prices. The fair value of the liabilities are based on current interest rates of the related U.S. government security held to fund annuity obligations. MUSL's investment policy limits its exposure to credit risk by investing only in securities that are backed by the full faith and credit of the U.S. government or its agencies.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
LOTTERY AND CHARITABLE GAMES CONTROL BOARD**

Notes to Financial Statements

September 30, 2004 and 2003

(Dollar amounts in thousands)

**(c) MUSL Prize Reserves**

The prize pool for Powerball consists of 50% of each drawing period's sales. Two percent of the prize pool is placed in a prize reserve fund and a set prize reserve fund. These reserve funds serve as contingency funds to protect MUSL from unforeseen liabilities. As of September 30, 2004 and 2003, the total Powerball prize reserve fund was approximately \$70,000 and \$69,000, respectively, of which the Lottery's share was approximately \$1,733 and \$2,200, respectively. In addition, the total Powerball set prize reserve fund as of September 30, 2004 and 2003, was approximately \$26,000 and \$25,000, respectively, of which the Lottery's share was approximately \$510 and \$531, respectively.

The balance remaining in the reserve funds are refundable to MUSL members if a member leaves or if MUSL disbands. If a member leaves, the member must wait one year before their portion of the prize reserve funds is returned. The balance in the reserve funds may be used at the discretion of MUSL's board of directors. Accordingly, the Lottery's share of the reserve funds is not reflected in the accompanying financial statements.

The price pool for Hot Lotto consists of 50% of each drawing period's sales. The 50% contribution to the prize pool is distributed to grand prizes and a prize reserve fund based on the following jackpot levels:

- |                               |  |
|-------------------------------|--|
| • \$1,000,000 to \$2,000,000  | 52.5763% to grand prize                                  |
| • \$2,000,000 to \$5,000,000  | 52.5763% to grand prize plus 1.00% to prize reserve fund |
| • \$5,000,000 to \$10,000,000 | 52.5763% to grand prize plus 3.00% to prize reserve fund |

The prize reserve fund serves as a contingency fund to protect MUSL from unforeseen liabilities. As of September 30, 2004, the total Hot Lotto prize reserve fund was approximately \$617, of which the Lottery's share was approximately \$26. The balance in the prize reserve fund may be used at the discretion of the MUSL's Board of Directors. Accordingly, the Lottery's share of the prize reserve fund is not reflected in the accompanying financial statements.

**(6) Obligations for Unpaid Prizes**

Jackpot prizes are paid in 20 or 25 annual installments. The first installment is paid approximately two weeks after the prize is claimed. The subsequent annual payments are funded with U.S. Treasury obligations purchased by MUSL for the Lottery. Jackpot prizes payable represent the future annual prize payments valued at cost plus accrued interest (present value of securities held to maturity) of the investment securities funding the payments.

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
LOTTERY AND CHARITABLE GAMES CONTROL BOARD**

Notes to Financial Statements

September 30, 2004 and 2003

(Dollar amounts in thousands)

The Lottery's obligations for unpaid prizes are as follows:

	September 30	
	2004 Jackpot	2003 Jackpot
Jackpot prizes payable:		
Due within one year	\$ 8,631	8,631
Due in subsequent years	57,850	64,906
Total (present value)	66,481	73,537
Add interest to maturity	13,682	15,257
Jackpot prizes payable at maturity	\$ 80,163	88,794

The following schedule presents the changes in prizes payable:

Balance as of September 30, 2002	\$ 78,789
Increases	3,379
Decreases	(8,631)
Balance as of September 30, 2003	73,537
Increases	1,575
Decreases	(8,631)
Balance as of September 30, 2004	\$ 66,481

**(7) Gaming Revenue and Expenses**

Gaming revenue and expenses for the fiscal years ended September 30, 2004 and 2003 were as follows:

	2004										
	Lucky Numbers	D.C. Four	Powerball	Quick Cash	Hot Five	Extra Games	Keno	Hot Lotto	Instant Games	Others	Total
Gaming revenue	69,512	71,588	40,871	4,161	4,345	145	9,711	1,356	38,940	506	241,133
Prizes	(32,955)	(33,190)	(19,142)	(2,715)	(2,008)	(77)	(5,892)	(682)	(25,657)	—	(122,318)
Agent's commissions	(4,545)	(4,115)	(2,235)	(232)	(274)	(9)	(656)	(73)	(2,869)	—	(15,008)
Gross margin	32,012	34,283	19,494	1,214	2,063	57	3,163	601	10,414	506	103,807
	2003										
	Lucky Numbers	D.C. Four	Powerball	Quick Cash	Hot Five	Lucky Numbers Extra	D.C. Four- Extra	Keno	Instant Games	Others	Total
Gaming revenue	70,268	71,894	44,360	4,217	4,841	360	600	3,791	36,904	655	237,890
Prizes	(35,848)	(35,415)	(21,415)	(755)	(2,473)	(226)	(380)	(2,312)	(24,742)	—	(123,564)
Agent's commissions	(4,397)	(4,082)	(2,400)	(212)	(500)	(25)	(41)	(254)	(2,781)	—	(14,692)
Gross margin	29,823	32,399	20,545	3,250	2,068	109	179	1,225	9,381	655	99,634

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
LOTTERY AND CHARITABLE GAMES CONTROL BOARD**

Notes to Financial Statements

September 30, 2004 and 2003

(Dollar amounts in thousands)

**(8) Transfers to the General Fund of the District**

The District Budget Act (PL 4-162) (the Act) of 1983 requires the Lottery to transfer its revenues less expenses and less a reserve not to exceed 2% of annual prize payments to the General Fund of the District. The Mayor may approve a change in the reserve limit, as necessary, upon the request of the Lottery. During the fiscal years ended September 30, 2004 and 2003, the Lottery's net transfers to the General Fund of the District were \$73,500 and \$72,050, respectively. The Lottery was in compliance with the Act for the fiscal years ended September 30, 2004 and 2003.

**(9) Retirement Programs**

**(a) *Defined Benefit Pension Plan***

The majority of the full-time Lottery employees hired before October 1, 1987 are covered by the Federal Civil Service Retirement System (5 U.S.C. 833 1). The Federal Civil Service Retirement System is a cost-sharing multiple employer pension plan.

The U.S. Office of Personnel Management is responsible for administering the Federal Civil Service Retirement System, including collecting the contributions and disbursing the benefits.

In accordance with the Balance Budget Act of 1997 (Public Law 105-33), the Lottery contributes 8.51% and employees contribute 7.25% of employees' covered compensation to the Federal Civil Service Retirement System. The Lottery's contribution decreased to 7.50% in October 2002 and to 7.00% in January 2003. Contributions by the Lottery amounted to \$205 and \$203 for the years ended September 30, 2004 and 2003, respectively. The number of Lottery employees covered under the Federal Civil Service Retirement System is 43.

**(b) *Defined Contribution Plan***

All full-time employees hired after September 30, 1987 are covered by the District-sponsored defined contribution plan. Employees do not contribute to this plan and are eligible to participate after one year of service. The Lottery contributes 5% of an eligible employee's base salary, which amounted to \$166 and \$149 for the fiscal years ended September 30, 2004 and 2003, respectively.

Contributions and earnings vest fully after four years of service following a one-year waiting period. Contributions and earnings are forfeited if separation occurs before five years of credited service. These contributions are not considered assets of the Lottery or the District, which have no further liability to this plan.

**(c) *Deferred Compensation Plan***

Lottery employees are eligible to participate in the District-sponsored deferred compensation plan (D.C. Code 47-3601) created in accordance with Internal Revenue Code Section 457. Employees may defer up to 25% of their compensation, not to exceed \$8. Compensation deferred and income earned are taxable when paid or made available to the participant or beneficiary upon retirement,

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
 LOTTERY AND CHARITABLE GAMES CONTROL BOARD**

Notes to Financial Statements

September 30, 2004 and 2003

(Dollar amounts in thousands)

death, termination, or unforeseeable emergency. Contributions are not assets of the Lottery or District, neither of which have any further liability to the plan.

**(10) Commitments and Contingencies**

**(a) Operating Leases**

The Lottery leases certain facilities under long-term, noncancelable, and operating leases. The total future minimum rental commitments as of September 30, 2004 are as follows:

Year ending September 30:		
2005	\$	1,241
2006		1,241
2007		413
	\$	<u>2,895</u>

The Lottery's future minimum rental commitments for the fiscal year ended September 30, 2004 is effective through February 5, 2007.

Rent expense for the fiscal years ended September 30, 2004 and 2003 was as follows:

	<u>2004</u>	<u>2003</u>
Gross rental expense	\$ 1,265	1,266
Less income from subleases	<u>(170)</u>	<u>(170)</u>
Net rent expense	<u>\$ 1,095</u>	<u>1,096</u>

**(b) Risk of Loss**

The Lottery is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Lottery or District covers all of the Lottery's claim settlements and judgments out of the Lottery revenues or the District's General Fund resources.



**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
LOTTERY AND CHARITABLE GAMES CONTROL BOARD**

Notes to Financial Statements

September 30, 2004 and 2003

(Dollar amounts in thousands)

**(c) Annuity Contracts**

Prizes awarded for the Lucky Lotto game, which ended effective May 1, 1989, are payable to the winners in annual installments over 10 or 20 years. The first installment payments were made by the Lottery at the time of the drawing. The Lottery had entered into agreements with insurance companies under which the Lottery purchased annuities contracts that provide the annual installment payments to the Lucky Lotto prize winners. As the insurance companies are responsible for the annual installments payments, neither the present value of the annuities nor the present value of the related future payments is reflected in the accompanying financial statements. The Lottery would be liable for such future installment payments if the insurance companies were to default on their payments. As of September 30, 2004 and 2003, future installment payments due to Lucky Lotto winners were approximately \$3,380 and \$5,233, respectively.

During 1991, Executive Life Insurance Company (ELIC), with whom the Lottery holds two annuities, was placed into conservancy with the Los Angeles, California Superior Court (Superior Court). In 1993, the Superior Court approved the terms of a rehabilitation plan and the purchase of ELIC by the Aurora National Life Insurance Company. As a result, the Lottery is required to fund a percentage of the annual installment payments for these annuities. The Lottery expensed \$138 during both years ended September 30, 2004 and 2003 for its share of the annual installment payments to these Lucky Lotto winners.

**(11) Related-Party Transactions**

The Lottery had related party transactions with the Office of Cable Television (OCT), another District of Columbia Government agency, during the fiscal years ended September 30, 2004 and 2003. OCT is responsible for the production of daily draws for the various lottery games. The annual contractual cost for the related services rendered were negotiated at arms length and amounted to \$510 and \$480 for the fiscal years ended September 30, 2004 and 2003, respectively.

During fiscal year 2004, the Lottery had related party transactions with the Office of the Chief Financial Officer (OCFO) to provide financial and managerial oversight. These services included, but were not limited to, internal audit and internal security, legal services, financial management, and executive management oversight. The annual contractual cost was \$110 and was negotiated at arms length.

Other services provided by District Government entities to the Lottery include central processing of payroll, accounting, computer technology services, and the handling of intra-district transactions for rent, telephone, security guard services, etc. Personnel costs for these services are budgeted and accounted for as part of the respective entity's regular operations.



**KPMG LLP**  
2001 M Street, NW  
Washington, DC 20036

**Independent Auditors' Report on Compliance and on Internal Control over  
Financial Reporting Based on an Audit of Financial Statements Performed  
in Accordance with *Government Auditing Standards***

To the Mayor and Members of  
The Council of the Government of District of Columbia, and  
The Lottery and Charitable Games Control Board  
Washington, D.C.

We have audited the financial statements of the Lottery and Charitable Games Control Board (the Lottery), an enterprise fund of the Government of the District of Columbia (District), as of and for the years ended September 30, 2004 and 2003, and have issued our report thereon dated January 24, 2005. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control over Financial Reporting**

In planning and performing our 2004 audit, we considered the Lottery's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

**Compliance and Other Matters**

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



This report is intended solely for the information and use of the Mayor, Council, the Inspector General of the Government of the District of Columbia, management of the Lottery, the U.S. General Accounting Office, and the U.S. Congress and is not intended to be, and should not be used by anyone other than these specified parties.

KPMG LLP

January 24, 2005