

NEW MEXICO LOTTERY AUTHORITY

FINANCIAL STATEMENTS

JUNE 30, 2017 and 2016

CliftonLarsonAllen LLP



WEALTH ADVISORY | OUTSOURCING | AUDIT, TAX, AND CONSULTING



New Mexico Lottery Authority

OFFICIAL ROSTER

June 30, 2017

BOARD OF DIRECTORS

Dr. Dan Salzwedel	Chairman
Mark Koson	Vice Chairman
John Kubiak, CPA	Secretary/Treasurer
Amy Bailey, Esq.	Asst. Secretary/Treasurer
Claude Austin	Member
Salvatore Baragiola	Member
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OFFICIALS OF THE NEW MEXICO LOTTERY AUTHORITY

David M. Barden, Esq.	Chief Executive Officer
Sylvia A. Jaramillo, CPA	Chief of Staff/Director of Administration
J. Vince Torrez	Executive Vice President for Security
Wendy Ahlm	Director of Advertising and Marketing
Karla Wilkinson	Director of Gaming Products
Evelyn McKnight	Director of Human Resources
Pam Poteat	Director of Sales

ORGANIZATIONAL DIVISIONS OF THE NEW MEXICO LOTTERY AUTHORITY

As per the New Mexico Lottery Act, Chapter 6, Article 24 NMSA 1978, the New Mexico Lottery Authority (the Lottery) is governed by a seven-member Board of Directors (Board or Directors), who provide the Lottery with the private-sector perspective of a large marketing and sales enterprise in order to maximize revenues for the Legislative Lottery Scholarship.

The Directors are residents of New Mexico appointed by the Governor with the advice and consent of the Senate. The Directors are prominent persons in their businesses or professions and geographically represent the State of New Mexico. No more than four Directors are from any one political party. The Directors receive no compensation for their services, but are reimbursed for approved expenses incurred in the conduct of the Lottery's business. Each Director is subject to a background check and investigation to determine his/her fitness for the office. At least one Director has five years of experience as a law enforcement officer, one Director is an attorney admitted to practice in New Mexico, and one Director is a Certified Public Accountant certified in New Mexico. The Directors are appointed for a five-year term, but can be reappointed by the Governor. The Board selects a Chairman, a Vice-Chairman, a Secretary/Treasurer, and an Assistant-Secretary/Treasurer each fiscal year. The Chairman also appoints a Chairman and two Directors for each of the three standing committees of the Board; the Finance/Audit Committee, the Security/Operations Committee, and the Personnel Committee. The Directors appoint the Chief Executive Officer (CEO) and prescribe his qualifications, duties and salary, and with the recommendation and assistance of the CEO, employ an Executive Vice President for Security and an Internal Auditor. The Directors meet at least once each quarter, and more often as needed. At their meetings, the Directors:

- adopt, amend, or repeal rules, policies and procedures necessary for the operation of the Lottery;
- approve, disapprove, amend, or modify the original budget for the succeeding fiscal year and any revised budget during a fiscal year;
- review and discuss current financial information and the Lottery's performance to the approved budget for the fiscal year;
- approve or disapprove all procurements over seventy-five thousand dollars and the resulting award of contracts;
- approve the financial audit contract after (or pending) Office of the State Auditor (State Auditor) approval, hold audit entrance and exit conferences with the independent public accountants (IPA) at an executive session of the Board or in the Finance/Audit Committee, and at an open meeting accept the fiscal year audit following release by the State Auditor and presentation by the IPA;
- listen to and discuss Lottery updates on sales, games, issues, etc.;
- review, discuss, and accept internal audit reports; and
- discuss, and when necessary, approve or disapprove other matters that should properly come before the Directors in their fiduciary duty for the efficient and effective operation, profitability, integrity, and security of the Lottery.

ORGANIZATIONAL DIVISIONS OF THE NEW MEXICO LOTTERY AUTHORITY - CONTINUED

The Executive Division, under the direction of the Chief Executive Officer, provides leadership for all activities of the Lottery to carry out its objectives and overall statutory mission to maximize net revenues for the Lottery's beneficiaries. The division establishes and directs the organization's day-to-day operating strategy and plan. In addition, the division performs as a liaison among the Board, the Governor, the Legislature, governmental entities, external providers of goods and services, retailers, the public, and Lottery divisions and employees.

The Administration Division, under the direction of the Chief of Staff/Director of Administration, performs all the activities associated with the financial and accounting functions of the Lottery, including the general ledger; cash management; retailer accounts receivable and debt collection; capital asset accounting; game accounting; payroll and benefit preparation, accounting, payment, and review; and tax reporting and payment. In addition, the division provides financial reporting, disclosure, and compliance with generally accepted accounting practices and budget compilation, including the quarterly and annual financial reporting of revenues, expenses, and net revenues to the State of New Mexico; the financial audit and related compilation of financial statements, related notes, and the Management's Discussion and Analysis (MDA) for the fiscal year; the statutorily required annual proposed operating budget for the Lottery for the succeeding fiscal year and the final (revised) proposed budget by division for Board of Directors' approval. Furthermore, the division is responsible for the procurement of materials and services; claims center payment of prizes and sales of tickets; and accounts payable. The warehouse component of the Administration Division is responsible for the packing and shipment of the Lottery's instant scratcher tickets and for the maintenance and shipping of Lottery premium and point of sale items. The division is also responsible for the management of building and grounds maintenance and vehicle fleet operations and maintenance.

The Advertising and Marketing Division, under the direction of the Director of Advertising and Marketing, is responsible for implementing, managing and administering the activities associated with marketing the Lottery and its products, including advertising, drawings, promotions and special events. This entails creating and producing multi-media advertising campaigns, in-store point of sale materials and player and retailer publications; as well as negotiating and overseeing the Lottery's participation in many statewide promotions and special events. In addition, within the Advertising and Marketing Division is communications, which is responsible for all aspects of corporate communications including creating news releases and responding to requests for information by the public and the media.

Gaming Products, under the direction of the Director of Gaming Products, manages and monitors the instant and on-line products, including such areas as game launches, game endings, and performance analysis using several key performance measures. In addition, instant ticket printing and on-line services contracts are managed by the Director of Gaming Products.

**ORGANIZATIONAL DIVISIONS
OF THE NEW MEXICO LOTTERY AUTHORITY - CONTINUED**

The Human Resources Division, under the direction of the Director of Human Resources, oversees the development and implementation of human resources policies, programs and services, including recruitment, selection, retention, legal compliance, employee benefits, employee insurance reconciliation, employee relations, employment practices and procedures, employee communications and employee events.

The Sales Division, under the direction of the Director of Sales, is responsible for developing and implementing all sales activities and programs for the Lottery, including customer relationship management, ticket sales, inventory management, point of sales material distribution, retailer recruitment, arranging for retailer installations, promotional and event participation and preparation, as well as maximizing sales initiatives.

The Security Division, under the direction of the Executive Vice President for Security, statutorily as a law enforcement agency is responsible for administering, enforcing and ensuring compliance with the security provisions of the New Mexico Lottery Act. The division conducts backgrounds of all prospective employees, lottery retailers, lottery vendors and lottery contractors. It also supervises ticket verification and conducts/oversees second chance drawings when the prize amount is more than \$5,000. The division functions as liaison among the Attorney General's Office, District Attorney Offices and law enforcement agencies in general. It is also responsible for building and employee security and safety.

The Information Technology (IT) Department, under the direction of the Information Technology Administrator, oversees all the activities associated with the systems and data processing functions of the Lottery, including financial applications, testing of new games, products, functions, and related reporting, monitoring of game activities and providing data and analysis to divisions. In addition, the management of the lottery's network is overseen by the IT Department.

The Internal Audit Department, under the direction of the Internal Auditor, conducts and coordinates comprehensive audits for all aspects of the Lottery as spelled out in the New Mexico Lottery Act. Audits are carried out pursuant to an annual audit plan that is approved by the Board of Directors and as may be requested by the CEO.

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INDEPENDENT AUDITORS' REPORT

Board of Directors
New Mexico Lottery Authority and
Mr. Tim Keller
New Mexico State Auditor
Albuquerque, New Mexico

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities, and the aggregate remaining fund information of the New Mexico Lottery Authority, a component unit of the State of New Mexico, as of and for the years ended June 30, 2017 and 2016, and the related notes to the financial statements, which collectively comprise the entity's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

Board of Directors
New Mexico Lottery Authority and
Mr. Tim Keller
New Mexico State Auditor

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities, and the aggregate remaining fund information of the New Mexico Lottery Authority as of June 30, 2017 and 2016, and the respective changes in financial position and, where applicable, cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 through 25 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the New Mexico Lottery Authority's basic financial statements. The Schedule of Percentage Return to the State of New Mexico is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The Schedule of Percentage Return to the State of New Mexico is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Schedule of Percentage Return to the State of New Mexico is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Board of Directors
New Mexico Lottery Authority and
Mr. Tim Keller
New Mexico State Auditor

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 10, 2017, on our consideration of the New Mexico Lottery Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the New Mexico Lottery Authority's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the New Mexico Lottery Authority's internal control over financial reporting and compliance.

A handwritten signature in cursive script that reads "CliftonLarsonAllen LLP".

CliftonLarsonAllen LLP

Albuquerque, New Mexico
October 10, 2017

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)

This Management's Discussion and Analysis of the New Mexico Lottery Authority (Lottery), offers readers of the Lottery's financial statements a narrative overview and analysis of the financial activities of the Lottery for the fiscal years ended June 30, 2017 and 2016 with comparative numbers for the fiscal year ended June 30, 2015. Please read it in conjunction with the financial statements, which begin on page 26.

FINANCIAL HIGHLIGHTS

- At the end of fiscal years 2017 and 2016, the Lottery's total current assets decreased by \$1,808,427, or (16.8)%, and \$70,330, or (0.6)%, respectively, in comparison to June 30th of each previous fiscal year.
- Compared to the end of the two preceding fiscal years, the Lottery's total current liabilities decreased by \$2,752,050, or (23.4)%, and \$1,161,463, or (9.0)%.
- In fiscal year 2017, total net ticket sales were \$126,041,264, a decrease of \$28,303,504, or (18.3)%, compared to the previous fiscal year. In fiscal year 2016, total net ticket sales were \$154,344,768, an increase of \$17,328,045, or 12.6%, compared to net ticket sales of \$137,016,723 in fiscal year 2015.
- From the prior fiscal years, total game expenses decreased by \$19,195,673, or (18.6)%, in fiscal year 2017 and increased by \$12,260,378, or 13.5%, in fiscal year 2016.
- Total operating expenses decreased by \$520,273, or (14.2)%, in fiscal year 2017 and decreased by \$1,404,972, or (27.8)%, in fiscal year 2016, each in comparison to the previous fiscal year.
- Non-operating income (expense) decreased by \$2,100, (8.7)%, and \$2,443, (9.2)%, in fiscal year 2017 and 2016, respectively, compared to each preceding fiscal year.
- In fiscal year 2017, net income was \$38,998,459, a decrease of \$8,566,698, or (18.0)% over fiscal year 2016's net income. Whereas, in fiscal year 2016, net income was \$47,565,157, an increase of \$6,443,936, or 15.7%, compared to the previous fiscal year's net income of \$41,121,221.
- Beginning July 1, 2007, the Lottery was required by the New Mexico Lottery Act to transmit at least twenty-seven percent of its gross revenues to the State of New Mexico and then at least 30% beginning in January 2009. In each fiscal year of 2017 and 2016, the Lottery transmitted 30.00% in net return to the State. In addition, in each of the last two fiscal years, the Lottery met the 30% required gross revenue return each month.
- Including the final transfer on July 31, 2017 of June 2017's net return; the Lottery has transferred \$738,715,914 to the State of New Mexico since the commencement of sales in April 1996.

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED

OVERVIEW OF THE FINANCIAL STATEMENTS

The Lottery was established in 1995 as a public body, politic and corporate, separate and apart from the State of New Mexico and constituting a governmental instrumentality and, therefore, is accounted for as such, reporting all the Lottery's assets and liabilities using the accrual basis of accounting, much like any private-sector business entity. Since the Lottery is a component unit of the State, the Lottery's financial statements are incorporated into the State of New Mexico's Comprehensive Annual Financial Reports.

This report consists of three parts—the Management's Discussion and Analysis (this section), the basic financial statements, including the notes to the financial statements; and supplementary information, the Schedules of Percentage Return to the State of New Mexico.

Financial Statements. The Statements of Net Position on Page 26 and the Statements of Revenues, Expenses, and Changes in Net Position on page 27 report the Lottery's assets, liabilities, revenues and expenses in comparative format for fiscal year 2017 and fiscal year 2016. The Statements of Cash Flows on pages 28 and 29 report the sources and uses of cash for fiscal years 2017 and 2016. The Statements of Fiduciary Net Position on page 30 and Statements of Changes in Fiduciary Net Position on page 31 report the balances and activity of the Lottery's Retirement Plans for fiscal years 2017 and 2016.

Notes to Financial Statements. The Notes to Financial Statements on pages 32 to 53 provide additional information that is essential for a full understanding of the financial statements and provide more detailed data.

Schedules of Percentage Return to the State of New Mexico. The Schedules of Percentage Return to the State of New Mexico on page 54 reports the percentages of gross revenues that were returned to the State of New Mexico for fiscal years 2017 and 2016 in compliance with the New Mexico Lottery Act.

To assess the Lottery's financial position and financial health, the reader of these statements should pay particular attention to changes in the components of assets and liabilities as set forth in the Statements of Net Position; in changes in total revenues, game expenses, operating expenses, non-operating income (expense) and net income as set forth in the Statements of Revenues, Expenses, and Changes in Net Position; and in the sources and uses of cash as set forth in the Statements of Cash Flows.

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED

FINANCIAL ANALYSIS

Total Net Position

At the end of fiscal years 2017 and 2016, the Lottery's net position was \$2,671,000 and \$1,508,000, respectively.

Total Assets

	2017	2016	2015	Increase (Decrease) \$ Change 2016 to 2017	Increase (Decrease) % Change 2016 to 2017	Increase (Decrease) \$ Change 2015 to 2016	Increase (Decrease) % Change 2015 to 2016
Cash and cash							
equivalents	\$4,660,713	\$6,381,875	\$5,515,045	\$(1,721,162)	(27.0)%	\$ 866,830	15.7%
Accounts receivable, (net of allowance for doubtful accounts)	736,905	742,846	1,586,110	(5,941)	(0.8)	(843,264)	(53.2)
Reserves on							
deposit	3,217,539	3,308,537	3,420,292	(90,998)	(2.8)	(111,755)	(3.3)
Inventory	188,110	156,721	162,024	31,389	20.0	(5,303)	(3.3)
Prepaid expenses	157,802	179,517	156,355	(21,715)	(12.1)	23,162	14.8
Total current							
assets	8,961,069	10,769,496	10,839,826	(1,808,427)	(16.8)	(70,330)	(0.6)
Capital assets, net	3,228,247	3,248,070	3,329,832	(19,823)	(0.6)	(81,762)	(2.5)
Total assets	<u>\$12,189,316</u>	<u>\$14,017,566</u>	<u>\$14,169,658</u>	<u>\$(1,828,250)</u>	(13.0)%	<u>\$(152,092)</u>	(1.1)%

Compared to each prior fiscal year, the Lottery's cash and cash equivalents decreased by \$1,721,162, a 27.0% decrease, at the end of fiscal year 2017, while at the end of fiscal year 2016 cash and cash equivalents increased by \$866,830, a 15.7% increase. The changes in cash and cash equivalents relate mainly to changes in accounts receivable, accounts payable and prizes payable at the end of each fiscal year compared to the prior fiscal year. At the end of fiscal year 2017, cash had decreased due to prizes payable also decreasing. During the fiscal year, much of the balance of unclaimed prizes was transferred to meet the 30% return mandate, reducing the balance of unclaimed prizes from \$2,553,494 down to \$1,307,897. At the end of fiscal year 2016, accounts receivable were collected on the last day of the year, which helped to increase the cash balance.

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED

FINANCIAL ANALYSIS – CONTINUED

Total Assets - Continued

Accounts receivable from the Lottery's retailers are collected each Thursday through electronic bank transfers. Receivables are equal to sales by retailers net of any prizes paid by the retailers and any commissions earned; less the allowance for bad debts plus any miscellaneous receivables from any other source. The accounts receivable balances at the end of fiscal year 2017 and the end of fiscal year 2016 are comparable with less than a \$6,000 difference between the two years. At the end of fiscal year 2016, Accounts receivables decreased by \$843,264, a 53.2% decrease. The change in fiscal year 2016 is due to collecting the amount owed for the prior week on the last day of the year.

The Lottery has amounts on deposit with the Multi-State Lottery Association (MUSL) called reserves on deposit, as required by the Powerball® (Powerball), Hot Lotto® (Hot Lotto), Mega Millions® (Mega Millions), and Monopoly Millionaires' Club® game rules and an unreserved account for payment of expenses and to record receipts of interest and other income on the deposits. The changes in these accounts in both fiscal years 2017 and 2016 of decreases of \$90,998 and \$111,755, respectively were caused by the receipts of interest earned and other income on the deposits with MUSL; payments of game expenses; changes to the Mega Millions, Hot Lotto, and Monopoly Millionaires' Club reserve accounts, as required by the Mega Millions, Hot Lotto, and Monopoly Millionaires' Club game rules; and the re-balancing of the reserve accounts.

The inventory balance at the end of fiscal year 2017 increased by \$31,389, a 20.0% increase, while in 2016 it decreased by \$5,303, a 3.3% decrease. The Lottery has agreements signed in March 2010 and amended in March 2014, with its primary instant ticket printer, whereby the tickets printed are owned by the vendor with the Lottery having an obligation to pay for the tickets when the tickets are sold. Therefore, these tickets are not included in the Lottery's inventory. But, under an agreement signed with a secondary instant ticket printer in March 2010 and amended in March 2014, the Lottery began purchasing the instant tickets printed by this vendor. The Lottery has accounted for games printed under this agreement as ticket inventory using the specific identification method at the lower of cost or market. At the end of each of the two fiscal years 2017 and 2016, the Lottery had remaining inventory purchased under this agreement of \$184,189 and \$152,219 for eleven and fourteen games, respectively in each year. In addition, at the end of fiscal years 2017 and 2016, the Lottery had inventory of \$3,921 and \$4,502, respectively, for two promotional instant games purchased.

The changes in capital assets in fiscal years 2017 and 2016 are primarily attributable to \$168,055 and \$181,700 in capital asset purchases and \$186,593 and \$225,958 in depreciation, for the two fiscal years, respectively.

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED

FINANCIAL ANALYSIS – CONTINUED

Total Liabilities

Table 2
Total Liabilities

	2017	2016	2015	Increase (Decrease) \$ Change 2016 to 2017	Increase (Decrease) % Change 2016 to 2017	Increase (Decrease) \$ Change 2015 to 2016	Increase (Decrease) % Change 2015 to 2016
Current Liabilities							
Accounts payable and other current liabilities	\$1,979,997	\$1,760,948	\$1,537,100	\$219,049	12.4%	\$223,848	14.6%
Current portion of note payable	239,717	231,644	223,123	8,073	3.5	8,521	3.8
Current portion of capital lease obligation	-	-	2,595	-	-	(2,595)	(100.0)
Prizes payable	3,748,021	6,331,639	8,110,042	(2,583,618)	(40.8)	(1,778,403)	(21.9)
Due to Lottery Tuition Fund	3,044,533	3,440,087	3,052,921	(395,554)	(11.5)	387,166	12.7
Total current liabilities	9,012,268	11,764,318	12,925,781	(2,752,050)	(23.4)	(1,161,463)	(9.0)
Long-term Liabilities							
Noncurrent portion of note payable	506,048	745,248	976,877	(239,200)	(32.1)	(231,629)	(23.7)
Total liabilities	\$9,518,316	\$12,509,566	\$13,902,658	\$(2,991,250)	(23.9)%	\$(1,393,092)	(10.0)%

Accounts payable and other current liabilities increased by \$219,049, a 12.4% increase, and \$223,848, a 14.6% increase at the end of fiscal years 2017 and 2016, respectively. In both fiscal years, the changes compared to the prior fiscal year were mainly due to amounts owed to five vendors for advertising, the on-line gaming system, instant ticket printing fees, and the lottery's share of prizes payable to MUSL for Powerball, Hot Lotto, and Mega Millions. Sales during the last weeks of each fiscal year and advertising incurred, but not billed, will generally determine the amounts owed at the end of each fiscal year to these vendors and whether that amount is higher or lower than in the prior fiscal year.

Prizes payable is essentially comprised of amounts accrued based on the Lottery's game designs and prize structures for draw game and instant game prizes, the related unremitted federal and state taxes withheld on prizes claimed, and any unclaimed prizes in the prize fund. At the end of fiscal years 2017 and 2016, prizes payable decreased by \$2,583,618, (40.8)%, and \$1,778,403,

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED

FINANCIAL ANALYSIS – CONTINUED

Total Liabilities - Continued

(21.9)%. These differences relate to the changes of prizes payable on individual Lottery games between the fiscal years as a result of sales in each fiscal year and prizes not yet claimed. In addition, in both fiscal years 2017 and 2016, the Lottery had to use unclaimed prizes to enable it to meet the 30% return to the Legislative Lottery Scholarship Fund and to supplement the prizes in scratcher (instant ticket) games to maximize sales in eleven of the twelve months in each fiscal year. The unclaimed prize fund balance was \$1,307,897 and \$2,553,494 at the end of fiscal years 2017 and 2016, respectively.

At the end of fiscal years 2017 and 2016, \$3,044,533 and \$3,440,087, respectively, of net revenues for the month of June were due to the Lottery Tuition Fund. These funds were transferred to the New Mexico State Treasurer by the end of July of each year.

At the end of both fiscal year 2017 and 2016, the Lottery reflected a current portion of a note payable of \$239,717 and \$231,644, respectively, and a noncurrent portion of a note payable of \$506,048 and \$745,248, respectively for each year. These amounts represented the amounts owed to a local bank for financing the purchase of the Lottery's corporate offices and warehouse, which the Lottery purchased at the end of fiscal year 2015. At the end of fiscal years 2017 and 2016, the note payable totaled \$745,765 and \$976,892, respectively.

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED

FINANCIAL ANALYSIS – CONTINUED

Net Ticket Sales and Prize Expense

Table 3
Net Ticket Sales and Prize Expense

2017	Net Ticket Sales	Prize Expense
Instant tickets	\$ 72,398,832	\$ 38,861,016
Powerball	26,329,419	13,164,850
Mega Millions	9,655,935	4,886,749
Roadrunner Cash	7,141,187	4,362,676
Pick 3	5,364,936	3,151,910
Hot Lotto	4,294,146	2,195,738
Quicksters	741,067	488,009
Lucky Numbers Bingo	115,742	73,202
Total	<u>\$ 126,041,264</u>	<u>\$ 67,184,150</u>
2016	Net Ticket Sales	Prize Expense
Instant tickets	\$ 83,105,873	\$ 47,531,599
Powerball	43,321,879	21,660,960
Mega Millions	10,509,262	5,270,102
Roadrunner Cash	7,394,565	4,695,036
Pick 3	4,891,153	2,853,765
Hot Lotto	4,283,277	2,202,208
Quicksters	691,531	446,528
Lucky Numbers Bingo	147,228	94,185
Total	<u>\$ 154,344,768</u>	<u>\$ 84,754,383</u>
2015	Net Ticket Sales	Prize Expense
Instant tickets	\$ 79,956,236	\$ 45,678,174
Powerball	27,722,571	13,861,367
Mega Millions	11,161,262	5,580,632
Roadrunner Cash	6,240,297	3,737,198
Pick 3	4,621,530	2,742,610
Hot Lotto	5,997,386	2,998,693
Quicksters	742,509	473,980
Lucky Numbers Bingo	153,912	93,665
Monopoly Millionaires' Club	421,020	426,006
Total	<u>\$ 137,016,723</u>	<u>\$ 75,592,325</u>
\$ (Decrease) from FY 2016 to FY 2017	<u>\$ (28,303,504)</u>	<u>\$ (17,570,233)</u>
% (Decrease) from FY 2016 to FY 2017	<u>(18.3)%</u>	<u>(20.7)%</u>
\$ Increase from FY 2015 to FY 2016	<u>\$ 17,328,045</u>	<u>\$ 9,162,058</u>
% Increase from FY 2015 to FY 2016	<u>12.6%</u>	<u>12.1%</u>

Note: Instant ticket sales are net of tickets provided as prizes, stolen, and promotion tickets; Powerball, Mega Millions, Roadrunner Cash, Hot Lotto, Pick 3, Quickster, Monopoly Millionaires' Club and Lucky Numbers Bingo sales are net of spoiled and promotional tickets.

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS – CONTINUED

Net Ticket Sales and Prize Expense – Continued

Table 3 provides net ticket sales and prize expense for each lottery game for fiscal years 2017, 2016, and 2015. In fiscal year 2017 net sales and the related prize expense increased for Pick 3, Hot Lotto and Quicksters, while net sales and the related prize expense decreased for instant tickets, Powerball, Mega Millions, Roadrunner Cash and Lucky Numbers Bingo. In fiscal year 2016 net sales and the related prize expense increased for instant tickets, Powerball, Roadrunner Cash, and Pick 3, while Mega Millions, Hot Lotto and Quickster net sales and the related prize expense decreased. The Lucky Numbers Bingo game net sales went down in fiscal year 2016, but produced more lucky winners than in the previous fiscal year. In fiscal year 2015 net sales and the related prize expense increased for instant tickets, Hot Lotto, Pick 3, and Quicksters, while Powerball, Mega Millions and Roadrunner Cash net sales and the related prize expense decreased. The new games Monopoly Millionaires' Club and Lucky Numbers Bingo were added in fiscal year 2015 and produced sales of \$575,000.

Net Ticket Sales

In fiscal year 2017, drawing game net sales were \$53.6 million compared to \$71.2 million in fiscal year 2016, a decrease of \$17.6 million, (24.7)%, while in fiscal year 2016 net drawing game sales increased by \$14.2 million, 24.9%, over fiscal year 2015's net drawing game sales of \$57.1 million. In fiscal year 2017, net sales for instant tickets were \$72.4 million compared to \$83.1 million in fiscal year 2016, a decrease of \$10.7 million, (12.9)%, while in fiscal year 2016 net instant ticket sales increased by \$3.1 million, 3.9%, over fiscal year 2015's net instant ticket sales of \$80.0 million. Overall, net sales decreased by \$28.3 million, (18.3)%, in fiscal year 2017, while net sales increased by \$17.3 million, 12.7%, in fiscal year 2016.

Higher drawing game sales may occur when the jackpots start climbing. Unfortunately, the Lottery has no influence over the amount that jackpots will grow and cannot predict when jackpot run-ups will happen. In some fiscal years, the jackpots will roll to extremely high jackpots, such as in fiscal year 2016 where the jackpot climbed to nearly \$1.6 billion, and in those fiscal years, the net drawing game sales will be extremely high and the return to the Legislative Lottery Scholarship will be much higher. But in other years, even with multi-hundred million dollar jackpots, net drawing game sales don't grow even with these jackpots, as was the case in fiscal year 2017.

The Lottery can achieve higher year-over-year instant ticket sales by implementing higher prize payouts in instant games. This is a business model followed by virtually all successful lotteries in the United States. But, due to the 30% return mandate and a dwindling unclaimed prize fund balance, prizes in instant games have been reduced causing instant ticket sales to fall in fiscal year 2017, as well as, causing the return to the Legislative Lottery Scholarship to decrease. Whereas, instant ticket sales should be the foundation for year-over-year sales growth for the Lottery with high jackpots for drawing games adding incremental sales, with the instability of

MANAGEMENT’S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

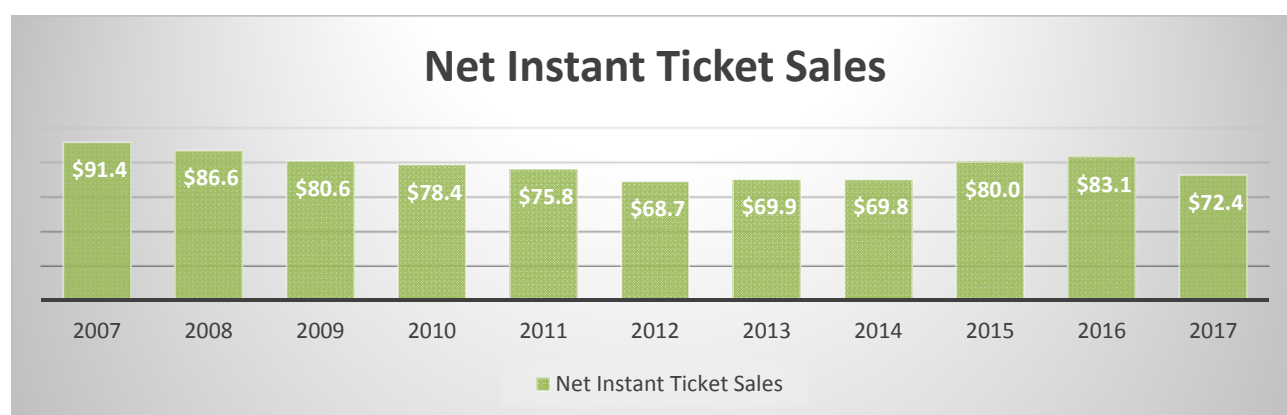
FINANCIAL ANALYSIS - CONTINUED

Net Ticket Sales and Prize Expense – Continued

Net Ticket Sales – Continued

growth for instant ticket sales caused by low prize structures due to the 30% return, this is not the case in New Mexico.

NET INSTANT TICKET SALES – FYs 2007 Through 2017



As reflected in this graph, sales begin rebounding in fiscal year 2015 and fiscal year 2016 toward the \$91.4 million net instant ticket sales of ten years ago. Net instant sales increased in fiscal year 2016 by \$3,150,000, a 3.9% increase, and by \$10,151,000, a 14.5% increase in fiscal year 2015. Fiscal year 2016 ended the year with over \$83.1 million dollars in net instant ticket sales, still \$8.3 million less than the fiscal year 2007 record-setting net instant ticket sales of \$91.4 million. Fiscal year 2015 ended the year with nearly \$80 million in net instant ticket sales, nearly \$10.2 million more than the previous year. Without this \$10.2 million increase in instant ticket sales in fiscal year 2015, the Lottery would have returned over three million dollars less to the Legislative Lottery Scholarship fund for the fiscal year.

During the last quarter of fiscal year 2014, the Lottery began using a comprehensively planned instant ticket sales strategy, including using unclaimed prizes to supplement the prizes in instant ticket games, launching instant games on the first Tuesday of the month, providing diagrams for retailers to follow in placing instant tickets into the dispensers and self-service lottery terminals, and increasing the visibility of instant tickets by using on-counter dispensers.

Unfortunately, in fiscal year 2017, the Lottery was forced to substantially reduce supplemental funding of instant ticket prize payouts to meet the statutory mandated return of 30%. (During fiscal year 2016, the Lottery used both unclaimed prize funds and administrative savings to fund higher instant ticket payouts.) The Lottery reduced the prizes in instant ticket games and could not afford to launch a \$20 instant ticket game causing net instant sales in fiscal year 2017 to fall by \$10.7 million or 12.9%. This reduction in net instant ticket sales caused the return to the Legislative Lottery Scholarship Fund to decrease by over \$3.2 million in fiscal year 2017.

MANAGEMENT’S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

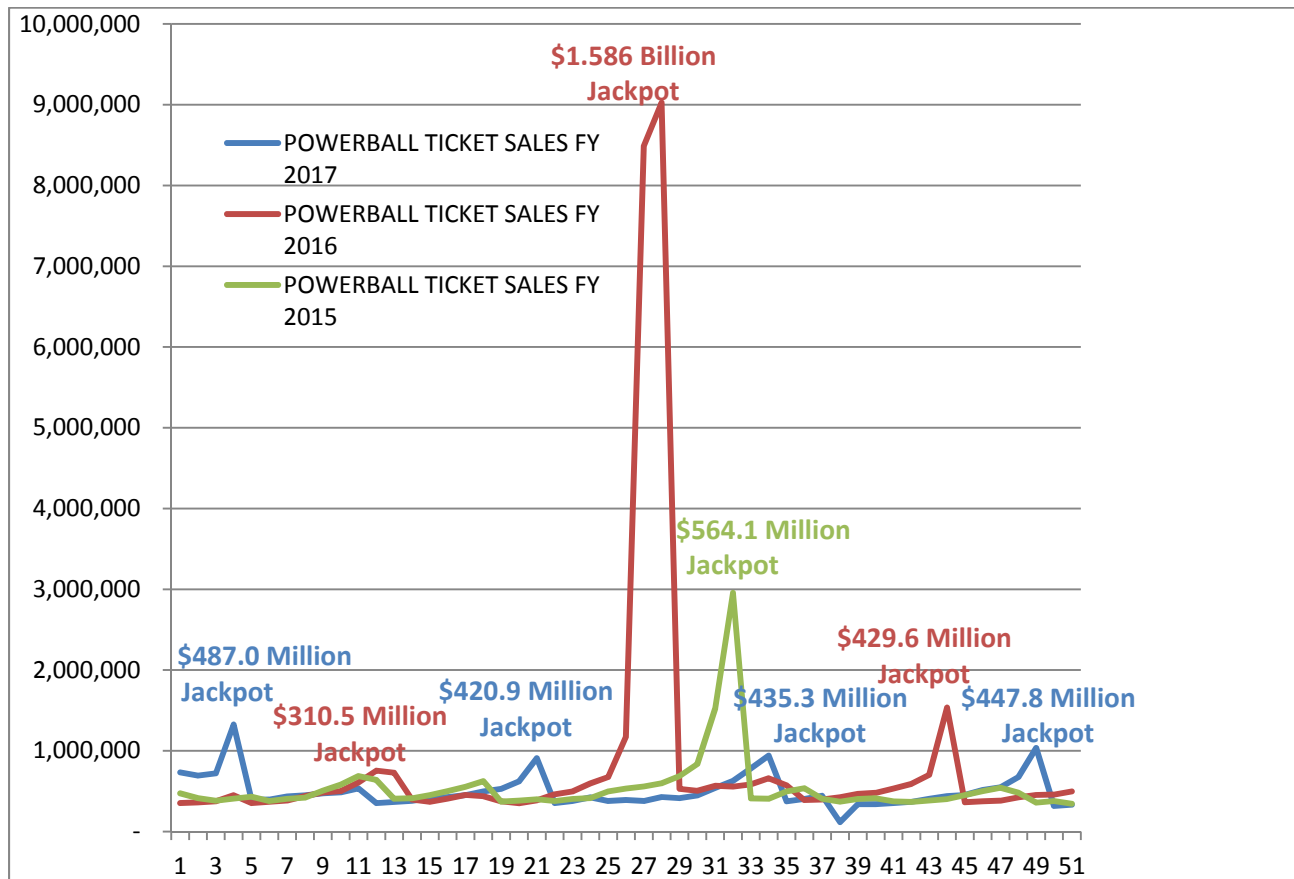
FINANCIAL ANALYSIS - CONTINUED

Net Ticket Sales and Prize Expense – Continued

Net Ticket Sales – Continued

The Lottery has continued to use the customer relationship management (CRM) system for placing instant game tickets at retailer locations. The Lottery’s customer service representatives have continued placing calls each week to each retailer location, reviewing the inventory at each location with the retailer, and placing orders as needed based on the inventory turnover at each location. In fiscal year 2017, forty-three new instant ticket games were launched – 10 - \$1, 9 - \$2, 6 - \$3, 11 - \$5, 7 - \$10, and 0 - \$20 price point games – 4 less \$1, 2 less \$2, 3 less \$3, the same number of \$5, 3 more \$10 and 1 less \$20 game than in fiscal year 2016. In fiscal year 2016, fifty new instant ticket games were launched – 14 - \$1, 11 - \$2, 9 - \$3, 11 - \$5, 4 - \$10, and 1 - \$20 price point games – 1 more \$1, 1 more \$2, 2 more \$3, and 2 more \$10 games than in fiscal year 2015. In fiscal year 2017, the Lottery launched 17 games with free (prize) tickets and 26 games without prize tickets, while in fiscal year 2016, the Lottery launched 25 games with free (prize) tickets and 25 games without prize tickets.

POWERBALL TICKET SALES – FYs 2017, 2016, & 2015



MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS - CONTINUED

Net Ticket Sales and Prize Expense – Continued

Net Ticket Sales – Continued

Powerball sales are driven by the advertised jackpot. As time passes, the jackpot that will influence the casual players into buying a jackpot ticket keeps growing. To tackle Powerball jackpots not growing to “super jackpots” and sales decreasing, Powerball was changed starting on October 4, 2015. The game is now a five (5) out of sixty-nine (69) plus one (1) out of twenty-six (26) lottery game instead of a five (5) out of fifty-nine (59) plus one (1) out of thirty-five (35) lottery game. In addition, a 10X multiplier was added when the Grand Prize Jackpot is \$150 million or less, the Match 4 plus one prize was increased to \$50,000 from \$10,000, and the overall odds of winning a prize are better at 1:24.87 compared to 1:31.85 previously.

For fiscal year 2017, except for the first month of sales, which had a jackpot run-up to \$487 million, the first eight months of the year were approximately 74% to 96% of the projected year-to-date budget with jackpots during those months also growing to \$87, \$246.8, \$420.9, \$121.6 and \$435.3 million. In March 2017, the Powerball sales budget was revised downward from \$36 million to \$28 million. During the rest of the year the jackpots were \$156.2, \$60, and \$447.8 million. Powerball sales ended the fiscal year \$17 million less than in fiscal year 2016 or 39.2% less.

For the first six months of fiscal year 2016, Powerball sales each month were approximately 67% to 85% of the year-to-date sales budget with four jackpots during those months growing to \$70, \$110, \$310.5, and \$144.1 million. In January 2016 after 20 jackpot rolls, the Powerball jackpot grew to a record setting \$1.586 billion jackpot that brought in approximately \$18 million in additional sales and helped Powerball finally reach and surpass its year-to-date sales budget. Two more jackpots followed in the fiscal year, growing to \$291.4 after 14 jackpot rolls and to \$429.6 after 19 jackpot rolls – this last jackpot not growing anywhere near the \$1.586 billion jackpot created in January after 20 jackpot rolls. Powerball sales culminated the fiscal year at \$43.3 million, a \$15.6 million increase over fiscal year 2015, or a 56.3% increase.

In fiscal year 2015, there were 14 jackpot run-ups with a February 2015 jackpot of \$564.1 million being the largest jackpot of the fiscal year. Other jackpots that grew to over one-hundred million during the year before being won were \$228.5, \$202.6, \$188.9, \$136.0, and \$124.9 million. There were eight other jackpots that were less than \$90 million when won. Having only one note-worthy jackpot in fiscal year 2015 caused sales to be \$6.3 million less than in fiscal year 2014, (18.5)% less. Nationally, Powerball sales were 17.2% less in fiscal year 2015 than in fiscal year 2014.

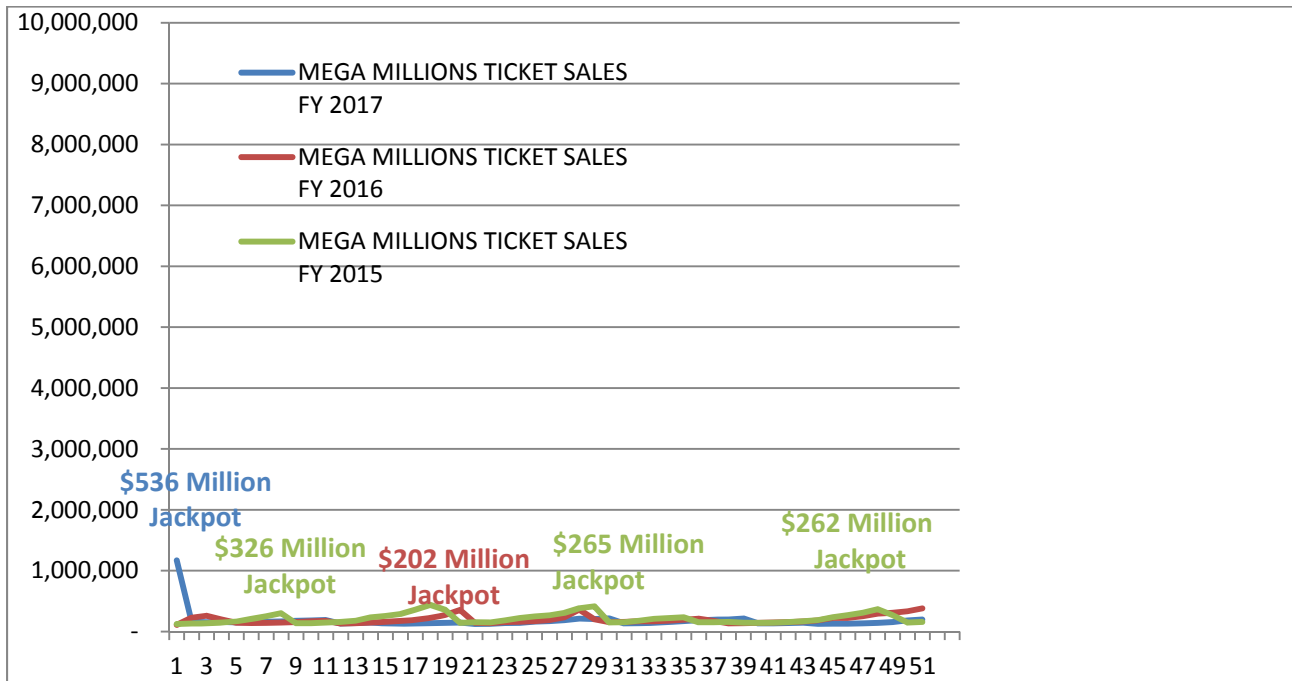
MANAGEMENT’S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS - CONTINUED

Net Ticket Sales and Prize Expense – Continued

Net Ticket Sales – Continued

MEGA MILLIONS TICKET SALES – FYs 2017, 2016, & 2015



Mega Millions sales are also driven by the jackpot amount and the game has also been experiencing jackpot fatigue, where players keep looking for bigger and bigger jackpots before they buy a ticket. Fiscal Year 2017 started the year with the one and only large jackpot run-up of \$536 million. July gave the Lottery a good head start for Mega Millions sales because the rest of the year’s jackpots were smaller at \$25, \$15, \$134, \$49, \$83, \$191, \$177, and \$61 million. The annual budget for Mega Millions sales was increased by half a million dollars to \$9.5 million due to the sales in July. Sales for the year grew to nearly \$9.7 million; \$853,000 less than in fiscal year 2016, or 8.1% less.

In fiscal year 2016, the largest jackpot roll-up was only \$202 million with the five other jackpots in the fiscal year being \$25, \$106, \$153, \$157, and \$169 million. Therefore, Mega Million sales were only \$10.5 million for the year; \$652,000, or (5.8)%, less than the prior fiscal year.

In fiscal year 2015, there were 6 jackpots that were won by players; the largest jackpot was \$326 million, followed by a \$265 million, a \$262 million, a \$180 million, a \$126 million and a \$58 million jackpot. Again, due to the lack of huge jackpots, fiscal year 2015 closed with sales being nearly \$11.2 million, which were \$2.25 million, (16.8)%, less than the previous fiscal year.

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS - CONTINUED

Net Ticket Sales and Prize Expense – Continued

Net Ticket Sales – Continued

Like Powerball and Mega Millions games, Roadrunner Cash sales are driven by the jackpot (top) prize amount. In fiscal year 2017 there was one jackpot that grew to \$420,000, one that grew to \$407,000, followed by one that grew to \$350,000, 4 that were over \$222,000, two that were over \$160,000 and six that were less than \$100,000. Sales for the fiscal year of \$7.1 million were \$253,000, (3.4%), less than in fiscal year 2016. In fiscal year 2016 there was one jackpot that grew to \$705,000, one that grew to \$355,000 followed by two over \$200,000, two over \$100,000 and thirteen jackpots that were less than \$100,000. With these jackpots, sales for Roadrunner Cash surpassed the sales for the previous fiscal year by nearly \$1.2 million, or 18.5%. In fiscal year 2015 there were four jackpot run-ups that exceeded \$200,000 with the largest being \$275,000; six jackpots exceeded \$100,000 and seven jackpots were \$67,000 or less. With so few jackpots growing to over \$200,000, Roadrunner Cash net sales ended the year \$2.35 million, (27.4)%, less than the previous fiscal year.

The MUSL game, Hot Lotto, is another smaller national jackpot game offered by the Lottery. Sales for this game also track with the jackpot. The jackpot for Hot Lotto started the year at \$3.7 million and grew to \$4.9 million before being won in August. It grew to \$1.2 million and was hit again at the end of August. It started rolling again at \$1 million and grew until the end of the year to nearly \$7.8 without being won. Sales for the year were nearly \$4.3 million, only \$11,000 more than in fiscal year 2016, a .25% increase. In fiscal year 2016, the Hot Lotto jackpot was won on July 1st when it was \$9.85 million; on that day, it started again at \$1 million and grew until December when it was won at \$4.46 million. During the rest of the fiscal year, it grew to a \$1.1 million jackpot and a \$1.55 million jackpot and then grew the rest of the year, ending the year at \$3.7 million. Therefore, fiscal year 2016 sales were only \$4.3 million, a decrease of \$1.7 million or (28.6)%. In fiscal year 2015, the Hot Lotto jackpot started the year at \$8.56 million and was won in September 2014. It started again at \$1 million dollars and grew all year until it was won on July 1, 2015. Fiscal year 2015's net sales ended the year \$297,000, 5.2%, ahead of the previous fiscal year.

Pick 3 sales continued to grow by nearly \$474,000, a 9.7% increase, to nearly \$5.4 million in fiscal year 2017. On June 12, 2016, Sunday sales for Pick 3 were started. Pick 3 sales ended fiscal year 2016 at nearly \$4.9 million, \$270,000 or 5.8% ahead of the previous fiscal year. In early June 2014, the Lottery had added a mid-day drawing. With a mid-day drawing adding additional sales for the full fiscal year, Pick 3 ended fiscal year 2015 more than \$793,000, 20.7%, ahead of fiscal year 2014. Pick 3 has remained a core game for the Lottery bringing in steady monthly average net sales; in fiscal year 2017 ranging from \$408,000 to \$503,000 each month, in fiscal year 2016 of more than \$400,000 each month and in fiscal year 2015 of nearly \$400,000 each month.

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS – CONTINUED

Net Ticket Sales and Prize Expense – Continued

Net Ticket Sales – Continued

A new game, Quicksters, was started on March 25, 2012. Quicksters are instant-win games, similar to instant ticket games, but produced by the same lottery sales terminals as draw game tickets and with no scratching needed to reveal the prizes. In fiscal year 2017, Quickster net sales increased by nearly \$50,000 to \$741,000, an increase of 7.2%. In fiscal year 2016, net Quickster sales were \$692,000, a drop of approximately \$51,000, (6.9)%, compared to the previous fiscal year. In fiscal year 2015, Quicksters net sales were nearly \$743,000, a 16.3% increase over fiscal year 2014 Quickster net sales of \$638,000.

On November 9, 2014, the Lottery introduced a new game, Lucky Numbers Bingo. Lucky Numbers Bingo is a draw game that offers two ways to play and two ways to win either through the Bingo numbers or through the Lucky Numbers. Lucky Numbers Bingo produced \$154,000 in net sales in fiscal year 2015, but dropped to approximately \$147,000 in fiscal year 2016, a 4.3% drop. In fiscal year 2017, Lucky Numbers Bingo sales again dropped by nearly \$31,000, (21.4)%, to \$116,000.

The Lottery also started a national game, Monopoly Millionaires' Club, on October 19, 2014. This national game was played until December 26, 2014, when it was ended nationally due to its overall performance.

Prize Expense

Prize expense for the draw games of Powerball, Mega Millions and Hot Lotto is based on the overall prize payout per the game design, while prize expense for Roadrunner Cash, Pick 3, Quicksters and Lucky Numbers Bingo is determined by the prizes won each month for each drawing or game. The prize expense for the Monopoly Millionaires' Club game was based on the actual cost of the prizes for the period that it was played. The prizes included in the prize structure for each instant game printed determine prize expense for instant games. In general, prize expense increases or decreases from year-to-year relative to the increases or decreases in sales for each Lottery product and the prize structures of the games.

In fiscal years 2017 and 2016, the prize payout decreased by approximately .87% and .71%, while in fiscal year 2015, the prize payout increased by approximately 2.74%, prior to the application of unclaimed prizes. The decreases in fiscal years 2017 and 2016 were mainly due to a lowering of prize payout on instant games by 2.54% and .46%, respectively, in each year, which inversely affected the growth of net instant game sales for each year.

At the end of the claim period for each game, unclaimed prizes for the Lottery's instant games and draw games are paid into the "Prize Fund," in accordance with the New Mexico Lottery Act.

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS – CONTINUED

Net Ticket Sales and Prize Expense – Continued

Prize Expense – Continued

These unclaimed prizes from the Lottery's prize fund have been used to meet the 30% return most months by supplementing the prizes in instant and draw games and for second chance drawings and, thereby, reducing the prize expense for Lottery products, which in turn has helped the Lottery maximize its sales and its return to education. Unclaimed prizes were used to supplement prizes in order to meet the 30% return in fiscal year 2017 and 2016 for eleven months in each fiscal year, respectively.

Prize Tickets

In fiscal years 2017, tickets provided as prizes (prize or free tickets) claimed for instant games decreased by \$515,000, an 18.6% decrease, while in fiscal years 2016 and 2015, prize tickets increased by nearly \$431,000, a 18.4% increase, and nearly \$245,000, a 11.7%, increase, respectively. Prize tickets are generally placed in the prize structure of the game in lieu of the breakeven prizes. Prize tickets give a player a prize of another instant game ticket of the same price point as the instant ticket that had the winning prize ticket. Each fiscal year, the Lottery continues to study the market to determine the optimum quantity of prize tickets to place in its instant ticket games in order to optimize its instant ticket sales.

Game Expenses

Table 4
Game Expenses

	2017	2016	2015	Increase (Decrease) \$ Change 2016 to 2017	Increase (Decrease) % Change 2016 to 2017	Increase (Decrease) \$ Change 2015 to 2016	Increase (Decrease) % Change 2015 to 2016
Prize expense	\$ 67,184,150	\$ 84,754,383	\$ 75,592,325	\$ (17,570,233)	(20.7)%	\$ 9,162,058	12.1%
Retailer							
commissions	8,196,191	10,035,060	8,941,265	(1,838,869)	(18.3)	1,093,795	12.2
On-line vendor							
fees	4,612,157	4,284,035	2,193,183	328,122	7.7	2,090,852	95.3
Advertising	2,126,939	2,053,906	2,174,697	73,033	3.6	(120,791)	(5.6)
Ticket vendor							
fees	1,172,844	1,314,494	1,265,885	(141,650)	(10.8)	48,609	3.8
Other game							
expenses	656,962	703,038	717,183	(46,076)	(6.6)	(14,145)	(2.0)
Total game							
expenses	\$ 83,949,243	\$ 103,144,916	\$ 90,884,538	\$ (19,195,673)	(18.6)%	\$ 12,260,378	13.5%

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS – CONTINUED

Game Expenses – Continued

The changes in retailer commissions for fiscal years 2017 and 2016 are consistent with the changes in gross ticket sales for the two years and are equivalent to 6.50% of gross revenues for the two years, respectively. Retailer commissions are paid to the Lottery's retailers for selling Lottery tickets, cashing Lottery prizes and for selling a jackpot/grand prize for Powerball, Mega Millions or Hot Lotto, for selling a match 5 prize for Powerball or Mega Millions, and for selling a jackpot prize of more than \$100,000 for Roadrunner Cash.

Since November 21, 2008, the on-line vendor fee has been a fixed percentage of net sales, plus applicable gross receipts taxes, with no additional terminal fees as in previous agreements. The on-line fee increases or decreases as draw game and instant ticket net sales increase or decrease. Effective November 22, 2015, the Lottery entered into an agreement for on-line vendor services following the issuance of a Request for Proposals in May 2015. Only one of the three on-line vendors provided a proposal for these services. The system includes the supply, installation, maintenance, service, and operation of a communication network, a new back office accounting system, new lottery terminals and peripheral equipment for the Lottery's existing and future retailers, ticket scanners to enable players to check their tickets for prizes, self-service ticket vending machines that sell both instant and draw game tickets, disaster recovery services, and various employees to operate the system and provide sales and marketing support to the Lottery. For fiscal years 2017 and 2016, the changes in the on-line vendor fees for the two fiscal years are consistent with the changes in draw game and instant ticket net sales for the fiscal years along with the increase in the vendor contract pricing as of November 2015 and are equivalent to 3.66% and 2.77% of gross revenues for the two years, respectively.

Advertising money is expended to market the Lottery and its products to the public and to inform the public about the games that are available, the jackpot and top prize amounts for the draw games, to provide security tips and gambling awareness for our players, and benefit messages to New Mexico students and their families, and to keep the lottery products fresh in the public's minds, all in order to maximize sales. Advertising expense was approximately 1.69% and 1.33% of gross revenues, respectively, for fiscal years 2017 and 2016 and stayed within the Lottery Board approved budgets of \$2,261,000 and \$2,200,000, respectively, for each fiscal year. In fiscal year 2017 and 2016, the advertising dollars were again maximized by purchasing advertising for the entire year at the beginning of the year. In fiscal years 2017 and 2016, the annual buys provided \$2.3 million and \$1.2 million, respectively, of additional advertising without any added cost, more than doubling the advertising budget in fiscal year 2017.

In fiscal years 2010 the Lottery signed a new contract with its primary ticket printer effective in March of that year. Under this contract, the instant tickets are owned by the vendor with the Lottery expensing the cost to ticket vendor fees and paying for the tickets as a percentage of net

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED

FINANCIAL ANALYSIS – CONTINUED

Game Expenses - Continued

instant sales when the tickets are sold. In addition, in March 2010, the Lottery signed a contract with a secondary printer, whereby the Lottery would be purchasing the tickets printed. These tickets are included in inventory with the cost of the tickets being recorded as ticket vendor fees as the tickets are consigned to retailers. Both contracts were extended for four additional years in March 2014. In addition, in both fiscal year 2017 and 2016, the cost for any licensing fees or special printing costs are also included in ticket vendor fees. The ticket vendor fees for both fiscal year 2017 and 2016 are .93% and .85% of gross revenues and are consistent with net instant ticket sales for each fiscal year.

Included in other game expenses are shipping and postage, promotions, retailer equipment, responsible gaming, and game membership expenses. Fiscal year 2017 reflects a decrease of \$46,076, or (6.6)%, and fiscal year 2016 reflects a decrease of \$14,145, or (2.0)%. In fiscal year 2016, the Lottery purchased player stations to replace 20-year old equipment at lottery retailer locations. In fiscal year 2017 additional player stations were purchased for new retailers, but a lesser quantity was purchased, therefore, reducing the cost of retailer equipment. In fiscal year 2015, the in-house lottery drawings for Roadrunner Cash and Pick 3 were automated at the end of October 2014, thus, saving nearly \$66,000 during the rest of the fiscal year and nearly \$103,000 in fiscal years 2017 and 2016. Further, in fiscal year 2016, promotions were reduced by \$17,000 and shipping and postage was reduced by \$35,000.

Operating Expenses

Table 5
Operating Expenses

	2017	2016	2015	(Decrease) \$ Change 2016 to 2017	(Decrease) % Change 2016 to 2017	(Decrease) \$ Change 2015 to 2016	(Decrease) % Change 2015 to 2016
Salaries, wages, and benefits	\$ 2,350,058	\$ 2,609,094	\$ 3,485,280	\$ (259,036)	(9.9)%	\$ (876,186)	(25.1)%
Utilities and maintenance	223,841	313,846	410,518	(90,005)	(28.7)	(96,672)	(23.5)
Leases, property taxes, and insurance	113,646	145,591	435,550	(31,945)	(21.9)	(289,959)	(66.6)
Other operating expenses	444,807	584,094	726,249	(139,287)	(23.8)	(142,155)	(19.6)
Total operating expenses	<u>\$ 3,132,352</u>	<u>\$ 3,652,625</u>	<u>\$ 5,057,597</u>	<u>\$ (520,273)</u>	(14.2)%	<u>\$ (1,404,972)</u>	(27.8)%

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS - CONTINUED

Operating Expenses - Continued

Operating expenses are made up of salaries, wages and benefits, utilities and maintenance, leases, property taxes, and insurance, and other operating expenses, which include depreciation and amortization, professional fees, materials and supplies, travel, and other expenses. In fiscal year 2017, operating expenses were reduced by \$520,000, or (14.2)% and in fiscal year 2016, operating expenses were reduced by \$1.4 million or (27.8)%. Salaries, wages and benefits were reduced by more than \$259,000 in fiscal year 2017, (9.9)%, and by more than \$876,000, (25.1)%, in fiscal year 2016. In fiscal year 2016, the Lottery started the year with 50 full-time and part-time employees and ended the year with 34 full-time and part-time employees; a reduction of force occurred during the year involving 15 full-time employee positions along with having a few other vacancies during the fiscal year. The savings for these employees continued for the full year in fiscal year 2017. In fiscal years 2017 and 2016, the Lottery was also able to save approximately \$200,000 and \$160,000 in expenses for its corporate offices and warehouse through the purchase of the building in June 2015. In addition, in fiscal year 2017 with the replacement of light fixtures in the warehouse with LED lights, the Lottery saved over \$11,000 in utility costs. In both fiscal years, every expense line item in Operating Expenses, had a reduction in cost, except for Other Expenses in fiscal year 2016, which increased by \$2,600. The Lottery has a mantra "Is it nice or is it necessary?" With this catch phrase, evaluation of costs has been performed and costs have been reduced as much as is economically feasible without profoundly impacting our ability to perform our jobs and still having the ability to continue to maximize revenues for our beneficiaries.

Non-Operating Income

Non-operating income decreased in both fiscal years 2017 and 2016. Interest rates paid on deposits continue to be low during both fiscal years. No significant other income was received in either fiscal year 2017 or 2016.

Non-Operating Expense

Due to the purchase of the Lottery's corporate offices and warehouse at the end of fiscal year 2015, there was interest expense of nearly \$32,000 and \$40,000 on the note financing the facility in fiscal years 2017 and 2016, respectively.

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS - CONTINUED

Net Income

Table 6
Net Income

	<u>Total Operating Revenues</u>	<u>Net Income</u>
Fiscal Year 2017	<u>\$126,057,944</u>	<u>\$ 38,998,459</u>
Fiscal Year 2016	<u>\$154,338,488</u>	<u>\$ 47,565,157</u>
Fiscal Year 2015	<u>\$137,036,703</u>	<u>\$ 41,121,221</u>
(Decrease) from FY 2016 to FY 2017	<u>\$(28,280,544)</u>	<u>\$ (8,566,698)</u>
% (Decrease) from FY 2016 to FY 2017	<u>(18.3)%</u>	<u>(18.0)%</u>
Increase from FY 2015 to FY 2016	<u>\$ 17,301,785</u>	<u>\$ 6,443,936</u>
% Increase from FY 2015 to FY 2016	<u>12.6%</u>	<u>15.7%</u>

Effective July 1, 2007, the New Mexico Lottery Act, Chapter 6, Article 24 NMSA 1978, was changed to require the Lottery to transmit at least twenty-seven percent of its gross revenues to the State Treasurer until December 31, 2008 and at least thirty percent of its gross revenues thereafter. In fiscal years 2017 and 2016, the Lottery transmitted a 30 percent return each month, totaling \$37,835,459 and \$46,324,157, respectively.

The changes in net income for fiscal years 2017 and 2016 were related to the changes in sales for the Lottery's games during the two years netted against savings in the cost of the product and operating expenses during the two fiscal years, which has been reviewed in the previous pages of this Management's Discussion and Analysis.

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) – CONTINUED

FINANCIAL ANALYSIS – CONTINUED

Budgetary Comparison

Table 7
Budgetary Comparison

	2017				
	Original Budget	Final Budget	Actual	Variance with Final Budget Positive (Negative)	% Variance with Final Budget
Total operating revenues	\$ 143,988,000	\$ 125,148,000	\$ 126,057,944	\$ 909,944	0.7%
Total game expenses	96,780,000	84,129,000	83,949,243	(179,757)	(0.2)
Total operating expenses	<u>3,984,000</u>	<u>3,447,000</u>	<u>3,132,352</u>	<u>(314,648)</u>	(9.1)
Operating income	43,224,000	37,572,000	38,976,349	1,404,349	3.7
Total non-operating income (expense)	<u>(24,000)</u>	<u>(24,000)</u>	<u>22,110</u>	<u>46,110</u>	(192.1)
Net income before transfers to Lottery Tuition Fund	<u>\$ 43,200,000</u>	<u>\$ 37,548,000</u>	<u>\$ 38,998,459</u>	<u>\$ 1,450,459</u>	3.9%
	2016				
	Original Budget	Final Budget	Actual	Variance with Final Budget Positive (Negative)	% Variance with Final Budget
Total operating revenues	\$ 141,438,000	\$ 151,188,000	\$ 154,338,488	\$ 3,150,488	2.1%
Total game expenses	93,775,000	101,759,000	103,144,916	1,385,916	1.4
Total operating expenses	<u>5,207,000</u>	<u>4,044,000</u>	<u>3,652,625</u>	<u>(391,375)</u>	(9.7)
Operating income	42,456,000	45,385,000	47,540,947	2,155,947	4.8
Total non-operating income (expense)	<u>(17,000)</u>	<u>(22,000)</u>	<u>24,210</u>	<u>46,210</u>	(210.0)
Net income before transfers to Lottery Tuition Fund	<u>\$ 42,439,000</u>	<u>\$ 45,363,000</u>	<u>\$ 47,565,157</u>	<u>\$ 2,202,157</u>	4.9%

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS - CONTINUED

Budgetary Comparison - Continued

In fiscal year 2017, the original annual budget was revised to reflect the projected performance of sales for the fiscal year. Instant ticket sales were reduced by \$14.5 million, (16.6)%, Powerball sales were reduced by \$8 million, (22.2)%, Mega Millions sales were increased by \$500,000, Roadrunner Cash sales by \$300,000, Hot Lotto sales by \$1.95 million, Pick 3 by \$200,000, Lucky Numbers Bingo by \$10,000 and Quicksters by \$400,000 and the two new games were eliminated since neither would be launching in fiscal year 2017. Along with the reduction in instant sales, tickets provided as prizes were reduced by \$2.6 million and spoiled, stolen and promotional tickets were reduced by \$100,000. The overall reduction to net ticket sales was \$18.84 million, or 13.1%. Direct game expense line items were reduced due to the changes in sales, but remained close to the same percentages that they had been in the FY 17 original annual budget. Retailer equipment was reduced by \$270,000, promotions by \$47,000 and shipping and postage by \$19,000. The overall decrease to game expenses was 13.1%, which was the same as the change in net ticket sales of 13.1%. All operating expenses were reduced, including salaries, wages and benefits, which was reduced by \$323,000. The final return to the Legislative Lottery Scholarship remained at 30% with these changes, but was reduced by \$5,652,000, or (13.1)%.

Fiscal year 2017 ended with net instant ticket sales out-performing the final (revised) budget by approximately \$1.3 million, Mega Millions by \$156,450, Roadrunner Cash by \$441,700, Hot Lotto by \$344,650, Pick 3 by \$265,450, Lucky Numbers Bingo by \$6,450 and Quicksters by \$41,550, but Powerball missed its sales budget by nearly \$1.7 million. Altogether, net ticket sales exceeded the budget by approximately \$881,000. Once again jackpot fatigue may have played a part in players not being excited with the Powerball jackpots during the year and therefore, kept Powerball sales from meeting the original budget and the revised budget. Compared to last fiscal year, the ticket sales were \$28.3 million dollars less and produced nearly \$8.5 million less for the Legislative Lottery Scholarship program. All in all, because of the sales performance, gross revenues ended the fiscal year at 100.8% of the revised budget, game expenses at 99.8% of the revised budget, and operating expenses at 90.9% of the revised budget.

In fiscal year 2016, the original annual budget was revised to reflect the better performance in sales for instant tickets, Powerball, and Roadrunner Cash and to reduce the sales for Mega Millions, Hot Lotto, Quicksters, and Lucky Numbers Bingo. Net sales were increased by more than \$9.7 million, made up of a \$1 million increase for instant sales, a \$12 million increase for Powerball, a \$700,000 increase for Roadrunner Cash, a \$2.4 million decrease for Mega Millions, a \$1.7 million decrease for Hot Lotto, a \$50,000 decrease for Quicksters, and a \$75,000 decrease for Lucky Numbers Bingo, as well as a \$200,000 decrease for tickets provided as prizes and a \$75,000 decrease for spoiled, stolen, and promotional tickets. Game expenses were increased by nearly \$8.0 million and operating expenses were reduced by nearly \$1.2 million. The net income return was increased by more than \$2.9 million. The final return remained at 30% with these changes.

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS - CONTINUED

Budgetary Comparison - Continued

Fiscal year 2016 culminated with net sales out-performing the final (revised) budget by more than \$3.1 million or 102% of the budget. Net sales exceeded the budget for instant sales by more than \$700,000, for Powerball sales by more than \$1.3 million, for Mega Millions by more than \$900,000, for Roadrunner Cash by nearly \$200,000 and for Pick 3 by nearly \$100,000, but for Hot Lotto, Quicksters, and Lucky Numbers Bingo, sales didn't reach the budget by approximately \$17,000, \$58,000 and \$28,000, respectively. Game expenses were 101% of the final budget and operating expenses were 90% of the final budget.

Requests for Additional Financial Information

This financial report is designed to provide the executive and legislative branches of the State of New Mexico, the public, the Lottery's retailers, vendors, creditors, and other interested parties with a general overview of the financial position of the Lottery as of June 30, 2017 and 2016, and results of its operations, cash flows, and percentage return to the state for the years then ended and to demonstrate the Lottery's accountability for the revenues it receives. If you have any questions about this report or need additional information, contact the Director of Administration at the New Mexico Lottery Authority, P.O. Box 93130, Albuquerque, New Mexico 87199.

New Mexico Lottery Authority

STATEMENTS OF NET POSITION

June 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
CURRENT ASSETS		
Cash and cash equivalents	\$ 4,660,713	\$ 6,381,875
Accounts receivable (net of allowance for doubtful accounts)	736,905	742,846
Reserves on deposit	3,217,539	3,308,537
Inventory	188,110	156,721
Prepaid expenses	<u>157,802</u>	<u>179,517</u>
Total current assets	8,961,069	10,769,496
CAPITAL ASSETS, NET	<u>3,228,247</u>	<u>3,248,070</u>
Total assets	<u>\$ 12,189,316</u>	<u>\$ 14,017,566</u>
CURRENT LIABILITIES		
Accounts payable and other current liabilities	\$ 1,979,997	\$ 1,760,948
Current portion of note payable	239,717	231,644
Prizes payable	3,748,021	6,331,639
Due to Lottery Tuition Fund	<u>3,044,533</u>	<u>3,440,087</u>
Total current liabilities	9,012,268	11,764,318
LONG-TERM LIABILITIES		
Noncurrent portion of note payable	<u>506,048</u>	<u>745,248</u>
Total liabilities	<u>\$ 9,518,316</u>	<u>\$ 12,509,566</u>
NET POSITION		
Investment in capital assets	\$ 2,482,482	\$ 2,271,178
Unrestricted surplus (deficit)	<u>188,518</u>	<u>(763,178)</u>
Total net position	<u>\$ 2,671,000</u>	<u>\$ 1,508,000</u>

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

New Mexico Lottery Authority

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

Years ended June 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
OPERATING REVENUES		
Instant ticket sales	\$ 72,398,832	\$ 83,105,873
Powerball sales	26,329,419	43,321,879
Mega Millions sales	9,655,935	10,509,262
Roadrunner Cash sales	7,141,187	7,394,565
Pick 3 sales	5,364,936	4,891,153
Hot Lotto sales	4,294,146	4,283,277
Quickster sales	741,067	691,531
Lucky Numbers Bingo sales	115,742	147,228
Net ticket sales	<u>126,041,264</u>	<u>154,344,768</u>
Retailer fees	11,800	14,720
Instant game gift card commissions	4,880	-
Bad debts	-	<u>(21,000)</u>
Total operating revenues	<u>126,057,944</u>	<u>154,338,488</u>
GAME EXPENSES		
Prize expense	67,184,150	84,754,383
Retailer commissions	8,196,191	10,035,060
On-line vendor fees	4,612,157	4,284,035
Advertising	2,126,939	2,053,906
Ticket vendor fees	1,172,844	1,314,494
Shipping and postage	289,581	276,853
Promotions	122,588	116,770
Retailer equipment	114,539	182,538
Responsible gaming	70,250	69,999
Game membership	60,004	56,878
Total game expenses	<u>83,949,243</u>	<u>103,144,916</u>
OPERATING EXPENSES		
Salaries, wages, and benefits	2,350,058	2,609,094
Utilities and maintenance	223,841	313,846
Depreciation and amortization	186,593	225,958
Professional fees	154,181	229,908
Leases, property taxes, and insurance	113,646	145,591
Other	47,131	54,878
Materials and supplies	46,313	48,743
Travel	10,589	24,607
Total operating expenses	<u>3,132,352</u>	<u>3,652,625</u>
OPERATING INCOME	<u>38,976,349</u>	<u>47,540,947</u>
NON-OPERATING INCOME (EXPENSE)		
Interest expense	(31,719)	(40,104)
Interest income	33,641	17,141
Other income	20,188	47,173
Total non-operating income	<u>22,110</u>	<u>24,210</u>
Net income before transfers	38,998,459	47,565,157
Transfers to Lottery Tuition Fund	<u>37,835,459</u>	<u>46,324,157</u>
Change in net position	1,163,000	1,241,000
Net position at beginning of year	<u>1,508,000</u>	<u>267,000</u>
Net position at end of year	<u>\$ 2,671,000</u>	<u>\$ 1,508,000</u>

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

New Mexico Lottery Authority

STATEMENTS OF CASH FLOWS

Years ended June 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Cash flows from operating activities		
Cash received:		
From retailers-sales net of commissions, incentives, and prize, spoiled, and stolen ticket credits	\$ 117,839,738	\$ 145,142,254
Cash payments:		
To prize winners and related taxes	(55,530,784)	(69,215,424)
To MUSL	(14,236,984)	(17,317,362)
To suppliers of goods or services	(9,201,817)	(9,135,798)
To employees for services and related taxes	<u>(1,923,647)</u>	<u>(2,259,228)</u>
Net cash provided by operating activities	<u>36,946,506</u>	<u>47,214,442</u>
Cash flows from noncapital financing activities		
Transfers to Lottery Tuition Fund	<u>(38,231,013)</u>	<u>(45,936,991)</u>
Cash flows from capital and related financing activities		
Purchases of capital assets	(180,953)	(167,517)
Principal paid on capital debt	(231,127)	(223,108)
Interest paid on capital debt	(31,835)	(39,853)
Principal payments under capital lease	<u>-</u>	<u>(2,595)</u>
Net cash used by capital and related financing activities	<u>(443,915)</u>	<u>(433,073)</u>
Cash flows from investing activities		
Receipts of interest	6,878	8,277
Other	<u>382</u>	<u>14,175</u>
Net cash provided by investing activities	<u>7,260</u>	<u>22,452</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(1,721,162)	866,830
Cash and cash equivalents at beginning of year	<u>6,381,875</u>	<u>5,515,045</u>
Cash and cash equivalents at end of year	<u><u>\$ 4,660,713</u></u>	<u><u>\$ 6,381,875</u></u>

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

New Mexico Lottery Authority

STATEMENTS OF CASH FLOWS - CONTINUED

Years ended June 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Reconciliation of operating income to net cash provided by operating activities		
Operating income	\$ 38,976,349	\$ 47,540,947
Adjustments to reconcile operating income to net cash provided by operating activities		
Depreciation	186,593	225,958
Vendor's non-cash transactions	66,902	52,866
Interest on MUSL unreserved account	4,825	4,335
Net changes in assets and liabilities:		
Accounts receivable	(22,015)	838,826
Reserves on deposit	108,095	123,924
Inventory	(31,389)	5,303
Prepaid expenses	21,715	(23,162)
Accounts payable and other liabilities	219,049	223,848
Prizes payable	<u>(2,583,618)</u>	<u>(1,778,403)</u>
Net cash provided by operating activities	<u>\$ 36,946,506</u>	<u>\$ 47,214,442</u>

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

New Mexico Lottery Authority

STATEMENTS OF FIDUCIARY NET POSITION

Years ended June 30, 2017 and 2016

	2017			2016		
	Money Purchase Pension Plan	Section 457(b) Plan	Total	Money Purchase Pension Plan	Section 457(b) Plan	Total
ASSETS						
Cash and cash equivalents	\$ 200,835	\$ -	\$ 200,835	\$ 319,959	\$ -	\$ 319,830
Marketable securities and other investments	4,558,557	364,799	4,923,356	4,379,591	252,556	4,632,276
Contribution receivable	11,028	-	11,028	10,820	-	10,820
Total assets	<u>\$ 4,770,420</u>	<u>\$ 364,799</u>	<u>\$ 5,135,219</u>	<u>\$ 4,710,370</u>	<u>\$ 252,556</u>	<u>\$ 4,962,926</u>
NET POSITION						
Held in Trust for Pension plan participants' benefits	<u>\$ 4,770,420</u>	<u>\$ 364,799</u>	<u>\$ 5,135,219</u>	<u>\$ 4,710,370</u>	<u>\$ 252,556</u>	<u>\$ 4,962,926</u>

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

New Mexico Lottery Authority

STATEMENTS OF CHANGES IN FIDUCIARY NET POSITION

Years ended June 30, 2017 and 2016

	2017			2016		
	Money Purchase Pension Plan	Section 457(b) Plan	Total	Money Purchase Pension Plan	Section 457(b) Plan	Total
ADDITIONS						
Net Gain in fair value of investments	\$ 529,823	\$ 35,276	\$ 565,099	\$ -	\$ -	\$ -
Dividends	196,159	11,995	208,154	205,072	6,181	211,253
Employer contributions	233,876	-	233,876	263,884	-	263,884
Employee contributions	-	75,686	75,686	-	87,723	87,723
Employee rollovers	-	-	-	-	92,844	92,844
Total additions	<u>959,858</u>	<u>122,957</u>	<u>1,082,815</u>	<u>468,956</u>	<u>186,748</u>	<u>655,704</u>
DEDUCTIONS						
Net Loss in fair value of investments	-	-	-	323,107	5,693	328,800
Distributions to participants	898,998	10,564	909,562	627,349	31,188	658,537
Other activity	810	150	960	2,490	660	3,150
Total deductions	<u>899,808</u>	<u>10,714</u>	<u>910,522</u>	<u>952,946</u>	<u>37,541</u>	<u>990,487</u>
Change in net position	60,050	112,243	172,293	(483,990)	149,207	(334,783)
Net position - beginning	<u>4,710,370</u>	<u>252,556</u>	<u>4,962,926</u>	<u>5,194,360</u>	<u>103,349</u>	<u>5,297,709</u>
Net position - ending	<u>\$ 4,770,420</u>	<u>\$ 364,799</u>	<u>\$ 5,135,219</u>	<u>\$ 4,710,370</u>	<u>\$ 252,556</u>	<u>\$ 4,962,926</u>

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

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. Reporting Entity

The financial reporting entity as defined by Governmental Accounting Standards Board (GASB) Statement 14 (as amended by GASB *Statement 61*) consists of the primary government, organizations for which the primary government is financially accountable, and other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading. This definition of the reporting entity is based primarily on the notion of financial accountability as the "cornerstone of all financial reporting in government."

With the enactment of the New Mexico Lottery Act (the Act) on July 1, 1995, the New Mexico Lottery Authority (the Lottery) was created as a public body, politic and corporate, separate and apart from the State of New Mexico and constituting a governmental instrumentality of the state. The Lottery was created and organized for the purpose of establishing and conducting the Lottery to provide revenues for the public purposes designated by the Act. The New Mexico Lottery was organized as an independent business enterprise separate from state government, self-sustaining and self-funded, without need for state revenues or resources and subject to oversight, audit, and accountability by public officials and agencies. However, since there is a financial benefit to the State's institutions of higher education, which are part of the State, the Lottery is considered a component unit of the State of New Mexico. The Lottery has no component units.

The Lottery commenced sales of instant tickets on April 27, 1996, and sales of draw game tickets on October 20, 1996.

2. Basis of Presentation

The financial statements are prepared on the economic resources measurement focus and the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

Two Fiduciary Funds are used to account for assets held in a trustee capacity for Lottery employees. The Lottery's two fiduciary funds are a money purchase pension plan trust fund, the "New Mexico Lottery Authority Retirement Plan" and a section 457(b) pension plan trust fund, the "New Mexico Lottery Authority 457(b) Plan".

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

2. Basis of Presentation – Continued

The pension trust funds per Statements of Fiduciary Net Position and Statements of Changes in Fiduciary Net Position and Note D reflect the activities of the New Mexico Lottery Authority Retirement Plans pursuant to a trust agreement in fiscal year 2015 with Verisight Trust Company, which merged with Newport Group and is now known as the Newport Group. The trustee holds, invests and distributes the assets of the Plan for the benefit of the Plan participants, subject to the overall direction of the Lottery in its capacity as plan administrator.

The Lottery distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing goods and services in connection with the Lottery's principal ongoing operations. The principal operating revenues of the Lottery are sales of instant and draw game tickets. The Lottery also recognizes retailer fees for connecting new retailers to the system as operating revenues. Operating expenses include the costs related to sales, administrative expenses required to manage and operate the Lottery, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

When an expense is incurred that can be paid using either restricted or unrestricted resources, the Lottery's policy is to first apply the expense toward unrestricted resources and then toward restricted resources. At the end of fiscal years 2017 and 2016 there were no restricted resources.

3. Budgets and Budgetary Accounting

Each year, Lottery management prepares a budget in conformity with GAAP for the succeeding fiscal year. The Lottery's budget is not legally binding. The budget is presented by management to the Lottery's Board of Directors for review, amendment, and approval prior to the beginning of the next fiscal year. Any revisions to this budget during the fiscal year are also approved by the Lottery's Board of Directors. The Lottery's financial statements are reviewed at each regular Board of Directors' meeting. Performance in relation to the budget is presented and discussed during these meetings.

4. Cash and Cash Equivalents

For the purposes of the Statements of Cash Flows, the Lottery considers cash and cash equivalents to be cash on hand, demand deposits, time deposits with an original maturity of ninety days or less, and overnight repurchase agreements.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

5. Accounts Receivable

Accounts receivable represent the unremitted receipts on ticket sales, net of retailer commissions and prizes paid by the retailers. Receipts are transferred weekly from retailer bank accounts to the Lottery. Credit losses relating to contracted retailers have been within management expectations. Generally, collateral is not required on receivables. At June 30, 2017 and 2016, an allowance for doubtful accounts of \$32,076 and \$32,883, respectively, has been provided to recognize future uncollectible billings. In fiscal years 2017 and 2016, ten retail customers (500 and 569 retailers) represented 62% and 63% of sales for each year, respectively, and 80% and 90% of accounts receivable for each year, respectively.

6. Reserves on Deposit

The Lottery is a member of the Multi-State Lottery Association (MUSL), which operates games on behalf of participating lotteries. MUSL currently operates the POWERBALL® (Powerball), Hot Lotto® (Hot Lotto) and Mega Millions® (Mega Millions) games for the Lottery. The Lottery sells Powerball, Hot Lotto and Mega Millions game tickets through its retailers and makes weekly wire transfers to MUSL in an amount equivalent to the member lottery's share of the estimated grand prize liability for each game. Lesser prizes are paid directly to the winners by each member lottery. The prize pools for Powerball and Hot Lotto are 50% of each game's drawing period's sales after the prize pool accounts and prize reserve accounts are funded to the amounts set by the MUSL product group. The prize pool for Mega Millions is up to 55% of each drawing period's sales after the prize reserve accounts are funded to the amounts set by the MUSL product group, but may be higher or lower based upon the number of winners at each prize level, as well as the funding required to meet a guaranteed Annuity Grand Prize.

MUSL has established prize reserve accounts for the games it operates. These prize reserve accounts are funded out of the prize pools for the games until the accounts reach amounts set by the MUSL product groups for each game. Once the prize reserve funds exceed these designated maximums, the excess becomes part of the grand prize pool. The prize reserve funds serve as contingency reserves to protect MUSL and the party lotteries from unforeseen prize liabilities. The money in these reserve funds is used at the discretion of the MUSL Board of Directors. Any amounts remaining in the prize pool accounts or prize reserve account when the MUSL product group declares the end of a game shall be returned to the lotteries participating in the accounts after the end of all claim periods of all selling lotteries, carried forward to a replacement game, or otherwise expended in a manner at the election of the individual members of the Product Group in accordance with jurisdiction statute.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

6. Reserves on Deposit – Continued

As of October 1, 2013, the Powerball prize reserve deduction was set to begin at two percent (2%) when the annuity jackpot, as determined after sales are known, exceeds \$120 million, and four percent (4%) when the annuity jackpot, as determined after sales are known, exceeds \$250 million. Prior to this time, MUSL included 2% of the Lottery's Powerball drawing period's sales in two prize reserve accounts, the Powerball Prize Reserve Account (PRA) and the Set Prize Reserve Account (SPRA), until the Lottery's share in both the PRA and SPRA were fully funded. The maximum amounts designated by the MUSL Powerball product group for the PRA is \$80 million and for the SPRA is \$40 million for all member lotteries. At June 30, 2017 and 2016, the Lottery's share in the Powerball PRA was \$942,823 and \$1,007,923, respectively, and in the SPRA was \$409,923 and \$438,227, respectively. Both Powerball reserve funds were fully funded at the end of June 2017 and 2016, respectively.

MUSL includes up to 3% of the Lottery's Hot Lotto drawing period's sales, depending on the annuitized value of the Grand Prize, into a Prize Reserve Account (PRA). The MUSL product group has set the maximum Hot Lotto PRA balance at \$9 million for all party lotteries. At June 30, 2017 and 2016, the Lottery's share in the Hot Lotto PRA was \$512,166 and \$560,781, respectively. The Hot Lotto PRA was fully funded at June 30, 2016, but had not met its requirement of \$553,815 as of June 30, 2017.

MUSL may include an additional amount up to 5% of the Lottery's Mega Millions drawing period's sales into the Mega Millions Prize Reserve Account (PRA). The MUSL product group has set the maximum PRA balance at \$45 million for all party lotteries. At June 30, 2017 and 2016 the Lottery's share in the Mega Millions PRA was \$447,493 and \$448,485, respectively. The Lottery's Mega Millions prize reserve was fully funded at the end of June 2017 and 2016.

The Lottery also has an unreserved fund with MUSL. Interest earned on the MUSL funds and any unclaimed grand prizes may be deposited into the unreserved fund and game membership fees and other MUSL costs may be paid from this fund. At June 30, 2017 and 2016, the Lottery's share of the unreserved fund was \$905,134 and \$853,121, respectively.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

6. Reserves on Deposit – Continued

A winner of a Powerball grand prize or Mega Millions grand prize may select that the prize be paid at the cash value of the prize or as an annuity. For both Powerball and Mega Millions, the grand prize annuity is paid out in 30 graduated annual installments over 29 years. Government securities at the discounted value of the grand prize annuity are purchased to fund all future installments and are held in trust. Maturities are staggered in order to provide adequate cash flow for each annual installment. These assets and related liabilities are reflected in MUSL's financial statements and therefore, are not reflected in the Lottery's financial statements. MUSL is responsible for transferring the cash or the annuity installment amounts to the member lottery prior to the payment to any grand prize winner. Currently, the Lottery is not paying any prize winner any annuity prize payments.

As of May 12, 2013, the Hot Lotto advertised grand prize is paid as a withholdings taxes paid single, cash payment prize where the estimated advertised grand prize is grossed up to include federal and state tax withholdings and the prize winner receives the net prize after tax withholdings.

7. Inventory

The Lottery entered into an agreement with its primary instant ticket printer, whereby the printer retains title to the instant ticket inventory until the instant tickets are sold. Under this agreement, the Lottery pays the vendor a fee based on a fixed percentage of the net instant tickets sold; net instant tickets sold represents instant ticket sales less prize, spoiled, stolen, and promotional tickets. In addition, the Lottery signed an agreement with a secondary instant ticket printer, whereby the Lottery purchases and owns the tickets printed. These tickets are carried at the lower of cost or market using the specific identification method. At the end of fiscal years 2017 and 2016, the Lottery was distributing games printed under the two agreements. As of June 30, 2017 and 2016, \$188,110 and \$156,721, respectively, of instant tickets are included in inventory.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

8. Capital Assets

Capital assets, which include land, building, works of art, data processing software and hardware, building improvements, vehicles, furniture and fixtures, intellectual property, and equipment, are stated at cost net of any accumulated depreciation. The Lottery capitalizes all assets that have a cost greater than \$5,000 and an expected useful life of more than one year. Land and works of art, which have a perpetual or undeterminable life, are not depreciated. The building will be depreciated over its effective useful life of thirty-eight years with a residual value of ten percent. Significant building improvements are amortized over the remaining life of the building at the time of purchase of the improvement or if insignificant over 7 years; and intellectual property is amortized over the remaining life at the time of acquisition or at the time of development. For all other capital assets placed into service on or after July 1, 2013, depreciation and amortization are computed using the straight-line method over the estimated useful lives of 4 to 10 years. For any assets placed into service prior to July 1, 2013, depreciation and amortization are computed using the straight-line method over the estimated useful lives of 2 to 5 years. When assets are retired or otherwise disposed, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is reflected in the results from operations in the period of disposal.

9. Revenue and Accounts Receivable Recognition

Lottery games are sold to the public by contracted retailers and directly by the Lottery. Revenues and accounts receivable for instant tickets are recognized when packs are settled and retailers are billed for the tickets. Revenues and accounts receivable for all draw games are recognized when drawings are held, except for Quicksters and Lucky Numbers Bingo, where the revenues and accounts receivable are recognized at the time the tickets are sold. Accounts receivable are stated at their net realizable value and their past due status is based upon contractual terms.

The following is a summary of total operating revenues that are comprised of instant and draw game ticket sales and the related prize, spoiled, stolen, and promotional tickets, which are netted into the applicable game sales on the financial statements; plus any retailer fees and related bad debts that are shown as a contra revenue account in total operating revenues.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

9. Revenue and Accounts Receivable Recognition – Continued

	2017	2016
OPERATING REVENUES		
Instant ticket sales	\$ 74,700,077	\$ 85,947,924
Powerball sales	26,329,700	43,321,920
Mega Millions sales	9,656,053	10,509,268
Roadrunner Cash sales	7,141,226	7,394,571
Pick 3 sales	5,364,976	4,891,175
Hot Lotto sales	4,294,247	4,283,277
Quickster sales	741,067	691,536
Lucky Numbers Bingo sales	115,742	147,228
Less tickets provided as prizes	(2,256,949)	(2,771,818)
Less spoiled, stolen, and promotional tickets	(44,875)	(70,313)
Net ticket sales	126,041,264	154,344,768
Retailer fees	11,800	14,720
Instant game gift card commissions	4,880	-
Bad debts	-	(21,000)
Total operating revenues	\$ 126,057,944	\$ 154,338,488

10. Prizes

Prize expense for instant, Powerball, Mega Millions, and Hot Lotto games is recorded based on an estimate of the predetermined prize structure for each game. Prize expense for Roadrunner Cash, Pick 3, Quickster, and Lucky Numbers Bingo games is recorded based on the actual prizes won for each game.

11. Commissions

Retailers receive a commission of 6% on gross ticket sales and a 1% cashing commission on winning ticket validations for prizes up to \$600.

12. Advertising Costs

Advertising costs are expensed as incurred.

13. Income Taxes

The Lottery is exempt from Federal and New Mexico income taxes. Accordingly, no provision for income taxes has been made.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

14. Custodial Credit Risk and Interest Rate Risk

At June 30, 2017 and 2016, respectively, the Lottery maintained its cash balances in one financial institution. The balances for demand deposits were insured by the Federal Deposit Insurance Corporation up to \$250,000 at this financial institution.

Custodial credit risk – Deposits. In the case of deposits, this is the risk that in the event of a bank failure, the Lottery’s deposits may not be returned to it. The Lottery does not have a deposit policy for custodial credit risk. The Lottery limits its custodial risk for its cash and requires collateral in an amount greater than or equal to 50% of any deposit not insured by Federal Insuring Agencies. A greater amount of collateral is required when the Lottery determines it is prudent. Collateral must meet State of New Mexico “Security of Public Money” standards and be held in the third-party safekeeping.

Custodial credit risk – Investments. For an investment, custodial credit risk is the risk that in the event of the failure of the counterparty, the Lottery will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. Mutual funds, external investment pools, and securities underlying reverse repurchase agreements are not exposed to custodial credit risk. The Lottery does not have an investment policy for custodial credit risk.

The Lottery’s custodial risk for investments is in accordance with Article 10, NMSA, 1978 Compilation. The Lottery’s investments are made in overnight repurchase agreements. Investments are made through a local financial institution and are held in safekeeping at the Federal Reserve Bank. Repurchase agreements are collateralized by Government Securities with a market value of at least 102% of the principal and are used for overnight investment only. Collateral must meet State of New Mexico “Security of Public Money” standards and be held in third party safekeeping. As of June 30, 2017 and 2016, the Lottery’s balances of \$4,727,172 and \$6,426,835, respectively, were exposed to custodial credit risk as follows:

	<u>2017</u>	<u>2016</u>
Uninsured and uncollateralized	\$ -	\$ -
Collateral held by the pledging bank’s trust department in the banks’ name	-	-
Collateral held by the pledging bank’s trust department in the Lottery’s name	<u>4,727,172</u>	<u>6,426,835</u>
	<u>\$ 4,727,172</u>	<u>\$ 6,426,835</u>

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

14. Custodial Credit Risk and Interest Rate Risk – Continued

Interest Rate Risk – Investments. Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Lottery does not have a specific policy to limit its exposure to interest rate risk.

At June 30, 2017 and 2016, the Lottery had overnight yield repurchase agreements with one-day maturities.

15. Bank Accounts

At June 30, 2017:

Description	Bank	Balance per Bank
Operating account - overnight repurchase agreement	Wells Fargo Bank, NA	\$ 4,727,172
Operating account – checking	Wells Fargo Bank, NA	-
Total amount deposited in bank		4,727,172
Less: FDIC coverage		-
*Total uninsured funds – deposits and overnight repurchase agreement		<u>\$ 4,727,172</u>
102% pledged collateral requirement per statute for repurchase agreement		\$ 4,821,716
* Total pledged security		<u>(4,821,716)</u>
Amount under (over) requirement at June 30, 2017		<u>\$ -</u>

*Wells Fargo Bank, NA securities are held in safekeeping at the Federal Reserve Bank in San Francisco, CA. Presented at fair value, CUSIP Number 3138NXES2 (cost \$4,797,059), matures January 01, 2043. The repurchase agreement is collateralized with securities held in the name of the New Mexico Lottery.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

15. Bank Accounts - Continued

Cash and cash equivalents per bank at June 30, 2017	\$ 4,727,172
Less reconciling items--outstanding checks	<u>(72,209)</u>
Reconciled cash in bank at June 30, 2017	4,654,963
Cash in vault	<u>5,750</u>
Total cash and cash equivalents per Statements of Net Position	<u><u>\$ 4,660,713</u></u>

At June 30, 2016:

<u>Description</u>	<u>Bank</u>	<u>Balance per Bank</u>
Operating account - overnight repurchase agreement	Wells Fargo Bank, NA	\$ 6,426,783
Operating account - checking	Wells Fargo Bank, NA	<u>52</u>
Total amount deposited in bank		6,426,835
Less: FDIC coverage		<u>(52)</u>
*Total uninsured funds - deposits and overnight repurchase agreement		<u><u>\$ 6,426,783</u></u>
102% pledged collateral requirement per statute for repurchase agreement		\$ 6,555,319
* Total pledged security		<u>(6,555,319)</u>
Amount under (over) requirement at June 30, 2016		<u><u>\$ -</u></u>

*Wells Fargo Bank, NA securities are held in safekeeping at the Federal Reserve Bank in San Francisco, CA. Presented at fair value, CUSIP Number 3128MJTQ3 (cost \$6,094,388), matures November 01, 2043. The repurchase agreement is collateralized with securities held in the name of the New Mexico Lottery.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

15. Bank Accounts – Continued

Cash and cash equivalents per bank at June 30, 2016	\$ 6,426,835
Less reconciling items--outstanding checks	<u>(54,735)</u>
Reconciled cash in bank at June 30, 2016	6,372,100
Cash in vault	<u>9,775</u>
Total cash and cash equivalents per Statements of Net Position	<u><u>\$ 6,381,875</u></u>

16. Risk Management

The Lottery is exposed to various risks of loss related to torts; theft of, damage to, and the destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Lottery purchases commercial insurance to cover these risks. The amount of coverage has not been exceeded by claims in the last three years.

17. Shipping and Handling Costs

Shipping and handling costs associated with inventory distribution are expensed as incurred and included in game expenses.

18. Net Position

Net position represents the difference between all other elements in a statement of financial position and should be displayed in the applicable components of net investment in capital assets, restricted and unrestricted.

Net Investment in Capital Assets – consists of capital assets, net of accumulated depreciation, reduced by outstanding balances of bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, constructions, or improvement of those assets.

Restricted – consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. The Lottery does not have a restricted component of net position.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

18. Net Position – Continued

Unrestricted – consists of the net amount of assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position. In May 2014, the New Mexico Lottery Authority Board executed a resolution to establish contingency reserves from operating expenses for the sole purpose of allowing the New Mexico Lottery Authority to successfully carry out the provision of the New Mexico Lottery Act.

19. Unclaimed Prizes

The Act requires that prizes not claimed within the time period established by the Lottery are forfeited and shall be paid into the prize fund (unclaimed prize liability accounts). Unclaimed prizes have been applied against prize expense to supplement prizes in the Lottery's games and to promotions to increase sales. As of June 30, 2017 and 2016, the Lottery had unclaimed prizes in the amount of \$1,307,897 and \$2,553,494, respectively, reported as prizes payable that had not yet been applied against prize expense. The \$1,307,897 and \$2,553,494, respectively, in the unclaimed prize fund have already been committed and continue to supplement the prizes on instant games that have been printed and that are offered for sale. Any unclaimed prizes will continue to be a portion of the thirty percent return to the Legislative Lottery Scholarship Fund.

20. Use of Estimates in Preparation of Financial Statements

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 amount of assets and liabilities and 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.

21. Compensated Absences Payable

Annual leave and sick leave are accrued at rates specified by the Lottery's Business Operational Policy. Annual leave is awarded based on the employee's years of lottery service, leave status, and employment status (full-time or part-time) and sick leave is awarded at 3.7 hours biweekly for full-time employees. The maximum number of annual leave hours that full-time employees may carry over and retain in their annual leave bank varies from 80 hours for an employee with less than 5 years of service up to a maximum of 320 hours for an employee with fifteen or more years of service. The maximum number of sick leave hours that a full-time employee may carry over from year-to-year is 480 hours. Part-time employees receive leave and carry over and

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

21. Compensated Absences Payable – Continued

retain leave in their leave banks based on their percentage of employment. Upon separation from service, employees with at least one year of service will be compensated for their annual leave balance, not to exceed the maximum annual leave bank based on their years of service. Accrued sick leave hours will not be paid to an employee upon separation from service. During the years ended June 30, 2017 and 2016, the following changes occurred in the compensated absences liabilities:

<u>Balance July 1, 2016</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance June 30, 2017</u>
\$ 158,012	\$ 14,561	\$ (6,663)	\$ 165,910
<u>Balance July 1, 2015</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance June 30, 2016</u>
\$ 205,288	\$ 19,164	\$ (66,440)	\$ 158,012

The balances of compensated absences payable are reported on the Statements of Net Position in accounts payable and other current liabilities. The portion of accrued compensated absences due after one year is not material and, therefore is not presented separately.

22. Long-term Liabilities

During the years ended June 30, 2017 and 2016, the following changes occurred in long-term obligations:

	<u>Balance July 1, 2016</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance June 30, 2017</u>	<u>Amounts Due Within One Year</u>
Note payable	\$ 976,892	\$ -	\$ (231,127)	\$ 745,765	\$ 239,717
	<u>\$ 976,892</u>	<u>\$ -</u>	<u>\$ (231,127)</u>	<u>\$ 745,765</u>	<u>\$ 239,717</u>
	<u>Balance July 1, 2015</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance June 30, 2016</u>	<u>Amounts Due Within One Year</u>
Note payable	\$ 1,200,000	\$ -	\$ (223,108)	\$ 976,892	\$ 231,644
Capital leases	2,595	-	(2,595)	-	-
	<u>\$ 1,202,595</u>	<u>\$ -</u>	<u>\$ (225,703)</u>	<u>\$ 976,892</u>	<u>\$ 231,644</u>

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

22. Long-term Liabilities – Continued

A promissory note payable to Wells Fargo Bank, NA for the purchase of the building used as the Lottery’s facility and warehouse was issued on June 26, 2015. Principal and interest payments are due monthly on the 26th day of the month. The note bears interest at 3.6% and matures on June 26, 2020. The outstanding balance at June 30, 2017 and 2016 is \$745,765 and \$976,892, of which \$239,717 and \$231,644 are due within one year, respectively.

23. Debt Service Requirements for Note Payable

Debt service requirements on note payable as of June 30, 2017, are as follows:

<u>Year Ending June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2018	\$ 239,717	\$ 23,244	\$ 262,961
2019	248,614	14,347	262,961
2020	257,434	5,128	262,562
	<u>\$ 745,765</u>	<u>\$ 42,719</u>	<u>\$ 788,484</u>

24. Accounts Payable and Other Current Liabilities

Accounts payable and other current liabilities are comprised of the following at June 30:

	<u>2017</u>	<u>2016</u>
Accounts payable	\$ 1,206,369	\$ 1,187,354
Accrued liabilities, vendors*	469,173	278,532
Accrued liabilities, retailers*	12,500	12,500
Accrued payroll, and payroll taxes and benefits	126,045	124,550
Compensated absences	165,910	158,012
	<u>\$ 1,979,997</u>	<u>\$ 1,760,948</u>

* The Lottery has accrued an estimated amount of services delivered by its vendors and deposits for its retailers as of June 30, 2017 and 2016, respectively.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE B – CAPITAL ASSETS

Capital assets at June 30, 2017 consisted of:

	Beginning Balance	Reclass- ification	Increases	Decreases	Ending Balance
Land	\$ 730,000	\$ -	\$ -	\$ -	\$ 730,000
Works of Art	13,700	-	-	-	13,700
Building	1,975,163	-	-	-	1,975,163
Data processing software	2,193,682	-	-	-	2,193,682
Data processing equipment	676,551	(21,639)	48,020	-	702,932
Equipment - Security and disaster recovery	620,944	-	97,543	(17,220)	701,267
Vehicles	210,932	-	-	-	210,932
Furniture and fixtures	232,265	-	-	-	232,265
Intellectual property	179,073	-	-	-	179,073
Equipment - communications	160,507	-	-	-	160,507
Equipment - warehouse	71,174	-	-	-	71,174
Equipment - office	29,018	-	-	-	29,018
Building improvements	76,367	-	22,492	(1,285)	97,574
Obsolete capital assets	845,650	21,639	-	(30,652)	836,637
Capital assets	<u>8,015,026</u>	<u>-</u>	<u>168,055</u>	<u>(49,157)</u>	<u>8,133,924</u>
Building	(46,779)	-	(46,781)	-	(93,560)
Data processing software	(2,121,054)	-	(16,332)	-	(2,137,386)
Data processing equipment	(601,767)	21,639	(16,870)	-	(596,998)
Equipment - Security and disaster recovery	(573,509)	-	(30,790)	17,220	(587,079)
Vehicles	(130,070)	-	(23,026)	-	(153,096)
Furniture and fixtures	(220,357)	-	(2,381)	-	(222,738)
Intellectual property	(86,449)	-	(24,700)	-	(111,149)
Equipment - communications	(51,689)	-	(21,763)	-	(73,452)
Equipment - warehouse	(71,174)	-	-	-	(71,174)
Equipment - office	(18,386)	-	(2,126)	-	(20,512)
Building improvements	(72)	-	(1,824)	-	(1,896)
Obsolete capital assets	(845,650)	(21,639)	-	30,652	(836,637)
Accumulated depreciation	<u>(4,766,956)</u>	<u>-</u>	<u>(186,593)</u>	<u>47,872</u>	<u>(4,905,677)</u>
Capital assets, net	<u>\$ 3,248,070</u>	<u>\$ -</u>	<u>\$ (18,538)</u>	<u>\$ (1,285)</u>	<u>\$ 3,228,247</u>

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE B - CAPITAL ASSETS - CONTINUED

Capital assets at June 30, 2016 consisted of:

	Beginning Balance	Reclass- ification	Increases	Decreases	Ending Balance
Land	\$ 730,000	\$ -	\$ -	\$ -	\$ 730,000
Works of Art	6,850	-	6,850	-	13,700
Building	1,975,163	-	-	-	1,975,163
Data processing software	2,193,682	-	-	-	2,193,682
Data processing equipment	758,810	(76,251)	-	(6,008)	676,551
Equipment - Security and disaster recovery	635,622	(14,678)	-	-	620,944
Vehicles	452,284	(22,674)	75,943	(294,621)	210,932
Furniture and fixtures	230,767	(10,410)	11,908	-	232,265
Intellectual property	179,073	-	-	-	179,073
Equipment - communications	160,507	-	-	-	160,507
Equipment - warehouse	71,174	-	-	-	71,174
Equipment - office	49,508	-	10,632	(31,122)	29,018
Equipment - drawing	35,472	(35,472)	-	-	-
Building improvements	-	-	76,367	-	76,367
Obsolete capital assets	709,452	159,485	-	(23,287)	845,650
Capital assets	<u>8,188,364</u>	<u>-</u>	<u>181,700</u>	<u>(355,038)</u>	<u>8,015,026</u>
Building	-	-	(46,779)	-	(46,779)
Data processing software	(2,112,120)	-	(8,934)	-	(2,121,054)
Data processing equipment	(670,014)	76,251	(14,012)	6,008	(601,767)
Equipment - Security and disaster recovery	(557,397)	14,678	(30,790)	-	(573,509)
Vehicles	(357,697)	22,674	(52,164)	257,117	(130,070)
Furniture and fixtures	(230,767)	10,410	-	-	(220,357)
Intellectual property	(61,750)	-	(24,699)	-	(86,449)
Equipment - communications	(29,925)	-	(21,764)	-	(51,689)
Equipment - warehouse	(69,852)	-	(1,322)	-	(71,174)
Equipment - office	(49,508)	-	-	31,122	(18,386)
Equipment - drawing	(10,050)	35,472	(25,422)	-	-
Building improvements	-	-	(72)	-	(72)
Obsolete capital assets	<u>(709,452)</u>	<u>(159,485)</u>	<u>-</u>	<u>23,287</u>	<u>(845,650)</u>
Accumulated depreciation	<u>(4,858,532)</u>	<u>-</u>	<u>(225,958)</u>	<u>317,534</u>	<u>(4,766,956)</u>
Capital assets, net	<u>\$ 3,329,832</u>	<u>\$ -</u>	<u>\$ (44,258)</u>	<u>\$ (37,504)</u>	<u>\$ 3,248,070</u>

Land and works of art are non-depreciable assets.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE C - TRANSFERS TO LOTTERY TUITION FUND/THIRTY PERCENT RETURN

	Due to Lottery Tuition Fund
	<hr/>
Balance at June 30, 2015	\$ 3,052,921
Prior year 30% return	46,324,157
Prior year transfers	<u>(45,936,991)</u>
Balance at June 30, 2016	3,440,087
Current year 30% return	37,835,459
Current year transfers	<u>(38,231,013)</u>
Balance at June 30, 2017	<u><u>\$ 3,044,533</u></u>

In accordance with the Lottery Act, no later than the last business day of each month, the Lottery shall transmit at least thirty percent of the gross revenue of the previous month, to the New Mexico State Treasurer, who shall deposit it into state agency number 950, New Mexico Higher Education Department, the Lottery Tuition Fund, SHARE fund number 63700. As of July 31, 2017 and 2016, the Lottery has transferred \$37,835,459 and \$46,324,157, respectively, for the years ended June 30, 2017 and 2016 to the New Mexico State Treasurer.

NOTE D - RETIREMENT PLANS

Plan Descriptions and Funding

Money Purchase Pension Plan

All the Lottery's eligible employees participate in a plan provided by the Lottery pursuant to the New Mexico Lottery Act (Chapter 6, Article 24 NMSA 1978). The Lottery is the administrator of the Plan, which is a defined contribution money purchase pension plan. Benefit terms, including contribution requirements are established and may be amended by the Lottery's Board of Directors. The plan provides for retirement benefits to plan members and their beneficiaries. The benefit that a plan member will receive when eligible will depend on the contributions to the member's individual account, actual earnings or losses on investments of those contributions, and any fees that are assessed to the member's account. Fifty-four and fifty-six current and former employees of the Lottery were participants in the plan at the end of fiscal years 2017 and 2016, respectively.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE D - RETIREMENT PLANS - CONTINUED

Plan Descriptions and Funding- Continued

Money Purchase Pension Plan - Continued

Newport Group (formerly Verisight Trust Company) has been the trustee of the retirement plan (the "New Mexico Lottery Authority Retirement Plan") since August 15, 2014. As of this same date, new employees enter the retirement plan on their date of hire. The money purchase pension plan allows employees to self-direct their investments into any of the forty-one investment funds.

The Lottery contributes 13.25% of compensation for each eligible employee to individual employee accounts for the money purchase pension plan. Employees are immediately 100% vested in the contributions and any earnings on those contributions. For the years ended June 30, 2017 and 2016, the Lottery recognized \$233,876 and \$263,884 of pension expense for the plan on eligible compensation of \$1,765,101 and \$1,991,581, respectively. There were no forfeitures of employee balances for the years ended June 30, 2017 and 2016, respectively. The entire pension amounts applicable to all compensation paid during the respective fiscal years have been paid to the plan by June 30, 2017 and 2016, respectively. For the years ended June 30, 2017 and 2016, the Lottery recognized a contribution liability of \$11,028 and \$10,820, respectively, for contributions owed on compensation earned, but not paid, for the last few days of each fiscal year.

457(b) Plan

Effective August 2, 2014, a Section 457(b) Plan, (the "New Mexico Lottery Authority 457(b) Plan") that allows both pre-tax and Roth (after tax) contributions by employees for their retirement up to applicable annual Internal Revenue Code limits commenced. Newport Group (formerly Verisight Trust Company) is the trustee for the 457(b) plan. This plan, like the money purchase pension plan, allows employees to self-direct their investments into any of the forty-one investment funds. Thirty-two and thirty-four current and former employees were participants in the plan at the end of fiscal years 2017 and 2016. All amounts withheld from employee compensation for Section 457(b) contributions have been paid to the plan by June 30, 2017 and 2016, respectively.

Fair Value Measurement of Retirement Plan Investments

In February 2015, GASB issued Statement No. 72, Fair Value Measurement and Application. This Statement establishes new requirements on how fair value should be measured, which assets and liabilities should be measured at fair value, and what information about fair value should be disclosed in the notes to the financial statements. The Lottery has implemented the standard for the fiscal year ending June 30, 2017 and 2016.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE D - RETIREMENT PLANS- CONTINUED

The Lottery categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the investment. Level 1 investments reflect prices quoted in active markets; Level 2 investments reflect prices that are based on a similar observable asset either directly or indirectly; and Level 3 investments reflect prices based upon significant unobservable sources.

The Lottery has the following fair value measurements as of June 30, 2017 and 2016:

Mutual funds – Valued at the daily closing price as reported by the fund. These funds are required to publish their daily net asset value and to transact at that price. The mutual funds held by the Lottery are deemed to be actively traded and are registered with the Securities and Exchange Commission.

The Lottery had investments in various mutual funds that were comprised of bonds at June 30, 2017 and 2016, in the amount of \$691,381 and \$713,679, respectively, with varying investment quality ratings and maturities. The maturities averaged between six and ten years with an average rating of primarily A on the underlying investments.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE D - RETIREMENT PLANS - CONTINUED

The plan has the following fair value measurements as of June 30:

	2017		2016	
	Money Purchase Pension Plan	457(b) Retirement Plan	Money Purchase Pension Plan	457(b) Retirement Plan
Total Investments in the fair value measurement:				
Level 1 - Quoted prices in active markets				
<u>Mutual funds:</u>				
US Equity				
Value	\$ 711,090	\$ 125,483	\$ 864,850	\$ 102,452
Blend	221,127	43,741	271,782	30,486
Growth	652,131	40,719	530,815	2,137
Total US Equity	1,584,348	209,943	1,667,447	135,075
Bonds	108,216	721	200,397	704
Target Date	1,023,701	101,909	1,118,589	94,860
Balanced Asset Allocation	1,050,645	14,202	837,228	8,486
Foreign Equity	294,711	5,036	327,000	2,985
Specialty/Other	496,936	32,988	228,930	10,446
Total Level 1	4,558,557	364,799	4,379,591	252,556
Level 2 - Similar observable assets	-	-	-	-
Level 3 - Significant unobservable sources	-	-	-	-
Total investments in the fair value measurement	4,558,557	364,799	4,379,591	252,556
Total investments exempt from the fair value measurement:				
Money market/cash	200,835	-	319,959	-
Contribution receivable	11,028	-	10,820	-
Total Investments	\$ 4,770,420	\$ 364,799	\$ 4,710,370	\$ 252,556

The balances and activity of both Plans as of and for the years ended June 30, 2017 and 2016 are presented in the Statements of Fiduciary Net Position and Statements of Changes in Fiduciary Net Position. There are no separately issued financial statements available for the New Mexico Lottery Authority Retirement Plans.

NOTE E - CREDIT AGREEMENT

In July 2012, the Lottery entered into an agreement with Wells Fargo Bank effective May 15, 2012 for an unsecured overdraft line of credit sweep in the amount of \$4,000,000 with a variable interest rate, which was 3.50% as of June 30, 2016.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE E - CREDIT AGREEMENT - CONTINUED

This line matured on May 14, 2016, 2015, 2014, and 2013 and was renewed for another year under the same terms and conditions each year. For 2017, the line matured on May 15, 2017, but the renewal was still in process as of June 30, 2017. On August 23, 2017, the line was renewed through May 15, 2018 under the same terms and conditions. For the years ended June 30, 2017 and 2016, the Lottery had no outstanding borrowings against the line-of-credit.

NOTE F - LEASES

As part of the agreement with INTRALOT, Inc., to provide an updated on-line gaming system, the Lottery installed and implemented a new internal control system (ICS) in fiscal year 2009. The cost for the ICS is included in the fixed fee paid to the vendor as a percentage of net sales. The Lottery has accounted for this transaction as a capital lease. The ICS cost was projected over the initial term of the contract of seven years and has been capitalized on the books of the Lottery at the present value of this cost, as determined with a discount rate of 4%. The initial term of the contract ended on November 20, 2015, at which time the cost had been amortized to zero.

NOTE G - COMMITMENT

Effective on November 15, 2007, the Lottery entered into an agreement with INTRALOT, Inc., a Georgia-based company, to provide an updated on-line gaming system for a total of seven years. The system includes the supply, installation, maintenance, service, and operation of a communication network, lottery terminals and peripheral equipment for the Lottery's existing and future retailers, ticket scanners to enable players to check their tickets for prizes, self-service ticket vending machines that sell both instant and draw game tickets, disaster recovery services, and various employees to operate the system and provide sales and marketing support to the Lottery. The transition to this new on-line gaming system took place on November 16, 2008.

Effective November 22, 2015, the Lottery entered into an agreement with INTRALOT, Inc. to provide an updated on-line gaming system for a total of eight years. The system shall include the provisions of the 2007 on-line system along with a new back office accounting system and new lottery terminals for the Lottery's retailers. Intralot shall also employ and manage a fifteen-member lottery sales team.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2017 and 2016

NOTE H - OTHER EXPENSES

Other expenses at June 30 consisted of:

	<u>2017</u>	<u>2016</u>
Registrations and memberships	\$ 23,430	\$ 23,863
Other	13,773	17,301
Training	8,063	11,102
Publications and subscriptions	<u>1,865</u>	<u>2,612</u>
	<u>\$ 47,131</u>	<u>\$ 54,878</u>

New Mexico Lottery Authority

SUPPLEMENTARY INFORMATION
SCHEDULES OF PERCENTAGE RETURN TO THE STATE OF NEW MEXICO
 Years ended June 30,

	<u>2017</u>	<u>2016</u>
OPERATING REVENUES		
Instant ticket sales	\$ 72,398,832	\$ 83,105,873
Powerball sales	26,329,419	43,321,879
Mega Millions sales	9,655,935	10,509,262
Roadrunner Cash sales	7,141,187	7,394,565
Pick 3 sales	5,364,936	4,891,153
Hot Lotto sales	4,294,146	4,283,277
Quickster sales	741,067	691,531
Lucky Numbers Bingo sales	115,742	147,228
Net ticket sales	<u>126,041,264</u>	<u>154,344,768</u>
Retailer fees	11,800	14,720
Instant game gift card commissions	4,880	-
Bad debts	-	(21,000)
Total operating revenues	<u>126,057,944</u>	<u>154,338,488</u>
NON-OPERATING INCOME		
Interest income	33,641	17,141
Other income	20,188	47,173
Total non-operating income	<u>53,829</u>	<u>64,314</u>
GROSS REVENUES	<u>126,111,773</u>	<u>154,402,802</u>
GAME EXPENSES		
Prize expense	67,184,150	84,754,383
Retailer commissions	8,196,191	10,035,060
On-line vendor fees	4,612,157	4,284,035
Advertising	2,126,939	2,053,906
Ticket vendor fees	1,172,844	1,314,494
Shipping and postage	289,581	276,853
Promotions	122,588	116,770
Retailer equipment	114,539	182,538
Responsible gaming	70,250	69,999
Game membership	60,004	56,878
Total game expenses	<u>83,949,243</u>	<u>103,144,916</u>
OPERATING EXPENSES		
Salaries, wages, and benefits	2,350,058	2,609,094
Utilities and maintenance	223,841	313,846
Depreciation and amortization	186,593	225,958
Professional fees	154,181	229,908
Leases, property taxes, and insurance	113,646	145,591
Other	47,131	54,878
Materials and supplies	46,313	48,743
Travel	10,589	24,607
Operational Reserve Fund expense	1,163,000	1,241,000
Total operating expenses	<u>4,295,352</u>	<u>4,893,625</u>
OPERATING INCOME	<u>37,813,349</u>	<u>46,299,947</u>
NON-OPERATING EXPENSE		
Interest expense	31,719	40,104
Total nonoperating expense	<u>31,719</u>	<u>40,104</u>
NET INCOME	<u>\$ 37,835,459</u>	<u>\$ 46,324,157</u>
GROSS REVENUE PERCENTAGE RETURN	<u>30.00%</u>	<u>30.00%</u>



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

Board of Directors
New Mexico Lottery Authority and
Mr. Tim Keller
New Mexico State Auditor
Albuquerque, New Mexico

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the business-type activities, and the aggregate remaining fund information of the New Mexico Lottery Authority, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the New Mexico Lottery Authority's basic financial statements, and have issued our report thereon dated October 10, 2017.

Internal Control Over Financial Reporting

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Board of Directors
New Mexico Lottery Authority and
Mr. Tim Keller
New Mexico State Auditor

Compliance and Other Matters

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

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



CliftonLarsonAllen LLP

Albuquerque, New Mexico
October 10, 2017

New Mexico Lottery Authority

SCHEDULE OF FINDINGS AND RESPONSES

Year Ended June 30, 2017

There were no findings for the year ended June 30, 2017.

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Year Ended June 30, 2017

2016-001 Network Access (Compliance and Other Matters) - Resolved

Condition: During our review and testing of user account request process, we noted three out of three BOS user account request forms could not be located.

Criteria: The Lottery should have effective controls and procedures in place to ensure user account request forms are maintained evidencing proper review and approval of access.

2016-002 Disaster Recovery and Business Continuity Plans (Compliance and Other Matters) – Resolved

Condition: The Lottery developed a disaster recovery plan. However, since the creation of the plan, there have been changes to the IT environment, vendors, and personnel that make the plan outdated. Also, the Lottery has not tested the disaster recovery plan at least annually.

Criteria: In accordance with ISACA’s Control Objectives for Information and related Technology (COBIT) 4.1 framework (DS4), to ensure continuous service, a Disaster Recovery and Business Continuity Plans need to be developed and tested to reduce impact of a major disruption on key business functions and processes. The plans should be based on risk understanding of potential business impacts and address requirements for resilience, alternative processing and recovery capability of all critical IT services. They should also cover usage guidelines, roles and responsibilities, procedures, communication processes, and the testing approach.

New Mexico Lottery Authority

EXIT CONFERENCE

For the Year Ended June 30, 2017

An exit conference was held at the New Mexico Lottery Authority on October 12, 2017. The following individuals participated:

<u>Name</u>	<u>Title</u>
<i>New Mexico Lottery Authority Finance/Audit Committee</i>	
Mark Koson	Finance/Audit Committee Chairman
John Kubiak, CPA	Board Secretary/Treasurer
<i>New Mexico Lottery Authority Employees</i>	
David M. Barden, Esq.	Chief Executive Officer
Sylvia Ann Jaramillo, CPA	Chief of Staff/Director of Administration
Kevin Duda, CPA	Deputy Director of Administration
<i>CliftonLarsonAllen LLP</i>	
Matt Bone, CPA, CGFM, CGMA	Principal
Elizabeth Nunez, CPA	Senior Associate

Financial Statement Preparation

The New Mexico Lottery Authority's financial statements, notes, and management's discussion and analysis have been prepared by the New Mexico Lottery Authority's accountants.