

**NEW MEXICO  
LOTTERY AUTHORITY**

**FINANCIAL STATEMENTS**

**JUNE 30, 2009 and 2008**

Moss Adams LLP  
6100 Uptown Blvd NE Suite 400  
Albuquerque, New Mexico  
(505) 878-7200

New Mexico Lottery Authority

**OFFICIAL ROSTER**

June 30, 2009

**BOARD OF DIRECTORS**

Reta Jones, CPA	Chairman
Michael Hawkes	Vice Chairman
Nino Trujillo	Secretary
Clifford Stroud, MBA	Treasurer
Ken Hoeksema	Assistant Secretary-Treasurer
Herman J. Tabet	Member
Marcus J. Rael, Jr., Esq.	Member

**OFFICIALS OF THE NEW MEXICO LOTTERY AUTHORITY**

Tom Romero	Chief Executive Officer
J. Vince Torrez	Executive Vice President of Security
Sylvia Ann Jaramillo, CPA	Director of Finance
Evelyn McKnight	Director of Human Resources
Adriana Binns	Director of Marketing and Communications
Pam Poteat	Director of Sales
David Ramirez	Interim Director of MIS

## **ORGANIZATIONAL DIVISIONS OF THE NEW MEXICO LOTTERY AUTHORITY**

The Executive Division, under the direction of the Chief Executive Officer, provides leadership for all activities of the New Mexico Lottery Authority (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. Also, within the Executive Division is Product Development, which manages and monitors the instant and online products, including such areas as game launches, game endings, and performance analysis using several key performance indicators.

The Finance Division, under the direction of the Director of Finance, 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; fixed asset accounting; game accounting; payroll and benefit 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; 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 proposed budget 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 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 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.

The Marketing and Communications Division, under the direction of the Director of Marketing and Communications, is responsible for implementing, managing and administering the activities associated with marketing the Lottery and its products, including advertising, communications, television 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

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

Lottery's participation in a number of statewide promotions and special events. The division is also responsible for all aspects of corporate communications including creating news releases and annual reports and responding to requests for information by the public and the media.

The Management Information Systems (MIS) Division, under the direction of the Interim Director of MIS, performs all the activities associated with the systems and data processing functions of the Lottery, including instant ticket transaction processing, back office functionality, order and distribution systems, financial applications, retailer network support, and game management.

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 retailer visits, customer relationship management, ticket sales, inventory management, point of sales material distribution, 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 of 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 Lottery drawings and conducts drawings when the prize amount is more than \$5,000. The division functions as liaison between 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 warehouse component of the Security 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 responsible for the management of building and grounds maintenance.

# TABLE OF CONTENTS

## NEW MEXICO LOTTERY AUTHORITY

INDEPENDENT AUDITORS' REPORT .....	1-2
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) .....	3-19
BASIC FINANCIAL STATEMENTS	
Statements of Net Assets .....	20
Statements of Revenues, Expenses and Changes in Net Assets .....	21
Statements of Cash Flows.....	22-23
Statements of Fiduciary Net Assets.....	24
Statements of Changes in Fiduciary Net Assets.....	25
Notes to Financial Statements .....	26-41
SUPPLEMENTAL INFORMATION	
Budgetary Comparison Statements .....	42
Schedule of Percentage Return to the State of New Mexico .....	43
OTHER INFORMATION	
Report on Internal Control Over Financial Reporting And on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With <i>Government Auditing Standards</i> .....	44-45
Summary Schedule of Prior Audit Findings .....	46
Current Year Audit Findings and Responses .....	46-49
Exit Conference .....	50

## Independent Auditors' Report

Board of Directors  
New Mexico Lottery Authority  
and  
Mr. Hector H. Balderas  
New Mexico State Auditor

We have audited the accompanying financial statements of the business-type activities, and the aggregate remaining fund information of the State of New Mexico Lottery Authority (Lottery), a component unit of the State of New Mexico, as of and for the years ended June 30, 2009 and 2008, which collectively comprise the Lottery's basic financial statements as listed in the table of contents. We have also audited the budgetary comparison statements presented as supplementary information in the accompanying financial statements for the years ended June 30, 2009 and 2008, as listed in the table of contents. These financial statements are the responsibility of the Lottery's management. Our responsibility is to express opinions on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities, and the aggregate remaining fund information of the Lottery as of June 30, 2009 and 2008, and the changes in its financial position and, where applicable, cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statements referred to above presents fairly, in all material respects, the budgetary comparison statements for the years ended June 30, 2009 and 2008 in conformity with accounting principles generally accepted in the United States of America.

Board of Directors  
New Mexico Lottery Authority  
and  
Mr. Hector H. Balderas  
New Mexico State Auditor

In accordance with *Government Auditing Standards*, we have also issued a report dated October 16, 2009 on our consideration of the Lottery'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 to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis, on pages 3 through 19, is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

The additional schedule listed as supplemental information in the table of contents is presented for purposes of additional analysis and is not a required part of the financial statements.

*Moss Adams LLP*

Albuquerque, New Mexico  
October 16, 2009

## MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)

This Management's Discussion and Analysis of the New Mexico Lottery Authority (the 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, 2009 and 2008 with comparative numbers for the fiscal year ended June 30, 2007. Please read it in conjunction with the financial statements, which begin on page 20.

### FINANCIAL HIGHLIGHTS

- At the end of fiscal years 2009 and 2008, the Lottery's total current assets decreased by 12.8% or \$1,257,964 and 10.1% or \$1,100,067, respectively, in comparison to June 30<sup>th</sup> of the previous fiscal years.
- The Lottery's total liabilities decreased by \$1,252,623 and \$1,210,051, 12.4% and 10.7%, respectively at the end of fiscal year 2009 and 2008, compared to end of the two previous fiscal years.
- In fiscal year 2009, total revenues were \$142,316,217, a decrease of \$4,836,242 or (3.3)%, compared to the previous fiscal year. In fiscal year 2008 total revenues were \$147,152,459, a decrease of \$927,795 or (0.6)%, compared to the total revenues for fiscal year 2007 of \$148,080,254.
- From the prior fiscal years, total game expenses decreased by \$5,368,125, (5.3)%, in fiscal year 2009 and \$6,456,454, (6.0)%, in fiscal year 2008.
- Total operating expenses increased by \$121,555 in fiscal year 2009, whereas, in fiscal year 2008 total operating expenses decreased by 8.8% or \$509,709 compared to the prior fiscal years.
- Non-operating income decreased in both fiscal years 2009 and 2008 by \$406,527 (62.08)% and by \$57,933, (8.1)%, respectively.
- Net Income in fiscal year 2009 was \$40,814,372, a \$3,801 increase over fiscal year 2008. In fiscal year 2008, net income was \$40,810,571, an increase of \$5,980,435 or 17.2% over net income for fiscal year 2007 of \$34,830,136. 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 fiscal year 2009, the Lottery transmitted 28.63%, surpassing the blended rate of 28.5%,--27% for the first six months and 30% for the second six months. In fiscal year 2008, the Lottery transmitted 27.61% of its gross revenues to the State, also surpassing the 27% required rate, in comparison to 23.41% for the previous fiscal year. The Lottery has continued to transfer its net income each month, regardless of whether or not the amount of net income exceeded the statutory requirement.
- Including the final transfer on July 31, 2009 of June 2009's net revenues (net income), the Lottery has transferred \$402,563,987 to the State of New Mexico since the commencement of sales in April 1996.

### 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 of the Lottery's assets and liabilities using the accrual basis of accounting, much like any private-sector business entity. The Lottery's financial



## MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

statements are incorporated into the State of New Mexico's Comprehensive Annual Financial Reports since the Lottery is a component unit of the State.

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

**Financial Statements.** The Statements of Net Assets on Page 20 and the Statements of Revenues, Expenses, and Changes in Net Assets on page 21 report the Lottery's assets, liabilities, revenues and expenses in comparative format for fiscal year 2009 and fiscal year 2008. The Statements of Cash Flows on pages 22 and 23 report the sources and uses of cash for fiscal years 2009 and 2008. The Statements of Fiduciary Net Assets on page 24 and Statements of Changes in Fiduciary Net Assets on page 25 report the balances and activity of the Lottery's Retirement Plan for fiscal years 2009 and 2008.

**Notes to Financial Statements.** The Notes to Financial Statements on pages 26 to 41 provide additional information that is essential for a full understanding of the financial statements and provide more detailed data.

**Budgetary Comparison Statements.** The Budgetary Comparison Statements on page 42 show the variances between the budgets and actual Lottery performance.

**Schedules of Percentage Return to the State of New Mexico.** The Schedules of Percentage Return to the State of New Mexico on page 43 reports the percentage of gross revenue that was returned to the State of New Mexico for fiscal years 2009 and 2008.

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 Assets; in changes in total revenues, game expenses, operating expenses, non-operating income and net income as set forth in the Statements of Revenues, Expenses, and Changes in Net Assets; and in the sources and uses of cash as set forth in the Statements of Cash Flows.

## FINANCIAL ANALYSIS

### Total Net Assets

At the end of fiscal years 2009 and 2008, the Lottery's total assets and total liabilities were equal with total net assets reduced to zero. The \$50,000 balance in the reserve account since fiscal year 1996 was recorded as a liability to the Lottery Tuition Fund at the close of fiscal year 2007. As of July 1, 2007, the provision for a 2% Reserve Fund was removed from the New Mexico Lottery Act. Therefore, the \$50,000 balance in the 2% Reserve Fund was transferred with the final transfer of net revenues for fiscal year 2007 to the Lottery Tuition Fund on July 31, 2007. The Lottery has no reserve balances on its books, transferring its net revenues for the previous month to the Lottery Tuition Fund each month.

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) -- CONTINUED

OVERVIEW OF THE FINANCIAL STATEMENTS - CONTINUED

Assets

Table 1

Assets

	2009	2008	2007	Increase (Decrease) \$ Change 2008 to 2009	Increase (Decrease) % Change 2008 to 2009	Increase (Decrease) \$ Change 2007 to 2008	Increase (Decrease) % Change 2007 to 2008
Cash and cash equivalents	\$ 4,089,266	\$ 5,359,828	\$ 6,828,460	\$(1,270,562)	(23.7)%	\$(1,468,632)	(21.5)%
Accounts receivable, net	1,717,935	1,817,274	1,650,965	(99,339)	(5.5)	166,309	10.1
Reserves on deposit	2,648,344	2,542,282	2,338,018	106,062	4.2	204,264	8.7
Inventory	9,262	15,680	15,790	(6,418)	(40.9)	(110)	(0.7)
Prepaid expenses	105,998	93,705	95,603	12,293	13.1	(1,898)	(2.0)
Total current assets	8,570,805	9,828,769	10,928,836	(1,257,964)	(12.8)	(1,100,067)	(10.1)
Capital assets, net	254,593	249,252	359,236	5,341	2.1	(109,984)	(30.6)
Total assets	<u>\$ 8,825,398</u>	<u>\$ 10,078,021</u>	<u>\$ 11,288,072</u>	<u>\$(1,252,623)</u>	(12.4)%	<u>\$(1,210,051)</u>	(10.7)%

The Lottery's cash and cash equivalents balances decreased at the end of both fiscal years 2009 and 2008 by \$1,270,562 (23.7) % and \$1,468,632 (21.5%) % compared to the prior fiscal years. The changes in cash and cash equivalents relate mainly to changes in accounts payable and prizes payable at the end of each fiscal year.

Accounts receivable from the Lottery's retailers are collected weekly through electronic bank transfers. Receivables are equal to sales by retailers net of any prizes paid by the retailers and any commissions earned and any miscellaneous receivables from any other source. Accounts receivable decreased at the end of fiscal year 2009 by \$99,339 (5.5) % and increased in fiscal year 2009 by \$166,309 or 10.1%. In fiscal year 2009, a major component of the change was the reduction by \$178,198 in the amount of receivable from the Multi-State Lottery Association (MUSL) for interest and royalty income earned on its reserve accounts for the fiscal year. In fiscal year 2008, there were two additional days of receivables at year-end in comparison to the prior fiscal year and also include a \$194,920 receivable from MUSL of interest and royalty income earned for the fiscal year.

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED**

**FINANCIAL ANALYSIS - CONTINUED**

**Assets - Continued**

The Lottery has reserves on deposit with MUSL, as required by the Powerball® (Powerball) and Hot Lotto® (Hot Lotto) game rules. The changes in these reserve amounts in both fiscal years 2009 and 2008 were caused by the receipt of interest earned on the reserve deposits from MUSL, additions to the Hot Lotto reserve account, as required by the Hot Lotto game rules, and in fiscal year 2009 payments for the costs of a Hot Lotto promotion and changes in one of the Powerball reserve accounts.

Under a contract signed by the Lottery with its ticket printer in March 2003, instant tickets are owned by the vendor with the Lottery having an obligation to pay for the tickets when the tickets are sold. Thus, during the last few years, the inventory has declined as the tickets owned by the Lottery were distributed and replaced by tickets printed under this contract. In fiscal year 2009 the inventory for the last game owned by the Lottery was depleted.

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 of 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 and, therefore, the ICS cost of \$43,600 is reflected in capital assets in fiscal years 2009. The related liability for the ICS is included in the current portion of capital lease obligation (\$6,228 at June 30, 2009) and in the noncurrent portion of capital lease obligation (\$33,738 at June 30, 2009).

There were no significant changes in capital assets in fiscal years 2009 and 2008; \$177,656, including the \$43,600 capital lease purchase, and \$81,923 in purchases and \$172,315 and \$191,907 in depreciation, for the two fiscal years respectively.

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS - CONTINUED

Liabilities

Table 2  
Liabilities

	2009	2008	2007	Increase (Decrease) \$ Change 2008 to 2009	Increase (Decrease) % Change 2008 to 2009	Increase (Decrease) \$ Change 2007 to 2008	Increase (Decrease) % Change 2007 to 2008
Accounts payable and other current liabilities	\$ 1,883,818	\$ 1,239,586	\$ 2,550,728	\$ 644,232	52.0%	\$(1,311,142)	(51.4)%
Current portion of capital lease obligation	6,228	-	-	6,228	100.0	-	-
Prizes payable	4,142,150	5,885,786	5,576,596	(1,743,636)	(29.6)	309,190	5.5
Due to Lottery Tuition Fund	2,759,464	2,952,649	3,160,748	(193,185)	(6.5)	(208,099)	(6.6)
Total current Liabilities	8,791,660	10,078,021	11,288,072	(1,286,361)	(12.8)	(1,210,051)	(10.7)
Noncurrent portion of capital lease obligation	33,738	-	-	33,738	100.0	-	-
Total liabilities	\$ 8,825,398	\$ 10,078,021	\$ 11,288,072	\$(1,252,623)	(12.4)%	\$(1,210,051)	(10.7)%

Accounts payable and other current liabilities increased by \$644,232 or 52% at the end of fiscal year 2009, while in fiscal year 2008 the balance decreased by \$1,311,142 or (51.4)%. In both fiscal years, the changes compared to the prior fiscal year were mainly due to amounts owed to four vendors for advertising, on-line system and instant ticket printing fees, and the lottery's share of prizes payable to MUSL for Powerball and Hot Lotto. Sales amounts and advertising placed during the last few weeks of each fiscal year will generally determine the amounts owed at the end of each fiscal year and whether that amount is higher or lower than in the prior fiscal year.

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS - CONTINUED

Liabilities - Continued

Prizes payable is essentially comprised of amounts accrued based on the Lottery's game designs and prize structures for drawing 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 year 2009, prizes payable decreased by \$1,743,636 or (29.6) %, whereas, at the end of fiscal year 2008, prizes payable increased by \$309,190 or 5.5%. These differences relate to the changes of prizes payable on individual Lottery games between the years as a result of sales in each year and prizes not yet claimed. At the end of fiscal year 2009, the liability for instant game prizes and Powerball prizes was approximately \$333,000 and \$218,000 less than at the end of the previous year; while at the end of fiscal year 2008, the liability for Powerball prizes alone was almost \$474,000 more than at the end of fiscal year 2007, thus, contributing to a change in liability for prizes payable at the end of one fiscal year compared to the prior fiscal year. In addition, at the end of the previous two fiscal years, the changes in prizes payable can be attributed to decreases of about \$1,222,000 and \$181,000 of unclaimed prizes being carried over for planned use in the game designs and prize structures of Lottery games.

At the end of fiscal years 2009 and 2008, \$2,759,464 and \$2,952,649, 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 on July 31<sup>st</sup> of each year.

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS – CONTINUED

Net Sales and Prize Expense

Table 3  
Net Sales and Prize Expense

	2009		
	Net Sales	Prize Expense	Gross Margin
Instant ticket, net of prize, stolen, and promotional tickets	\$ 80,579,767	\$ 46,955,185	\$ 33,624,582
Powerball, net of spoiled and promotional tickets	43,938,481	21,996,737	21,941,744
Hot Lotto, net of spoiled and promotional tickets	8,418,573	4,129,217	4,289,356
Roadrunner Cash, net of spoiled and promotional tickets	6,444,473	3,489,220	2,955,253
Pick 3, net of spoiled and promotional tickets	2,894,735	1,736,980	1,157,755
Total	<u>\$ 142,276,029</u>	<u>\$ 78,307,339</u>	<u>\$ 63,968,690</u>
	2008		
	Net Sales	Prize Expense	Gross Margin
Instant ticket, net of prize, stolen, and promotional tickets	\$ 86,582,636	\$ 48,995,046	\$ 37,587,590
Powerball, net of spoiled and promotional tickets	44,461,165	22,252,480	22,208,685
Hot Lotto, net of spoiled and promotional tickets	5,975,142	2,956,245	3,018,897
Roadrunner Cash, net of spoiled and promotional tickets	6,544,441	3,679,225	2,865,216
Pick 3, net of spoiled and promotional tickets	2,325,347	1,420,360	904,987
Raffle game, net of spoiled and promotional tickets	1,001,400	625,000	376,400
4 This Way!, net of spoiled and promotional tickets	215,546	163,409	52,137
Total	<u>\$ 147,105,677</u>	<u>\$ 80,091,765</u>	<u>\$ 67,013,912</u>
	2007		
	Net Sales	Prize Expense	Gross Margin
Instant ticket, net of prize, stolen, and promotional tickets	\$ 91,366,360	\$ 56,153,065	\$ 35,213,295
Powerball, net of spoiled and promotional tickets	42,578,490	21,312,734	21,265,756
Hot Lotto, net of spoiled and promotional tickets	3,474,154	1,657,403	1,816,751
Roadrunner Cash, net of spoiled and promotional tickets	7,905,584	4,448,375	3,457,209
Pick 3, net of spoiled and promotional tickets	2,056,965	1,192,340	864,625
4 This Way!, net of spoiled and promotional tickets	652,910	355,838	297,072
Total	<u>\$ 148,034,463</u>	<u>\$ 85,119,755</u>	<u>\$ 62,914,708</u>
\$ (Decrease) from FY 2008 to FY 2009	<u>\$ (4,829,648)</u>	<u>\$ (1,784,426)</u>	<u>\$ (3,045,222)</u>
% (Decrease) from FY 2008 to FY 2009	<u>(3.3)%</u>	<u>(2.2)%</u>	<u>(4.5)%</u>
\$ Increase (decrease) from FY 2007 to FY 2008	<u>\$ (928,786)</u>	<u>\$ (5,027,990)</u>	<u>\$ 4,099,204</u>
% Increase (decrease) from FY 2007 to FY 2008	<u>(0.6)%</u>	<u>(5.9)%</u>	<u>6.5%</u>

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED****FINANCIAL ANALYSIS – CONTINUED****Net Sales and Prize Expense – Continued**

Table 3 compares net sales, prize expense and gross margin (net sales minus prize expense) for each lottery game for fiscal year 2009, 2008, and 2007. In fiscal year 2009, Hot Lotto and Pick 3 net sales, prize expense and gross margin increased, but decreased for instant game and Powerball. For Roadrunner Cash, both net sales and prize expense decreased, but gross margin increased in comparison to the previous fiscal year. There were no Raffle game and 4 This Way! games sales in fiscal year 2009. In fiscal year 2008, Powerball, Hot Lotto and Pick 3 net sales, prize expense and gross margin increased, but decreased for Roadrunner Cash and 4 This Way. For instant tickets, net sales and prize expense decreased, but the gross margin increased for the fiscal year. The Lottery issued a Raffle game in fiscal year 2008. This game produced a gross margin of more than \$376,000. During the fiscal year, the Lottery ended the 4 This Way! game.

***Net Sales***

In both fiscal years 2009 and 2008, 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 continue to place calls each week to each retailer location, review the inventory at each location with the retailer, and place orders continually as needed based on the inventory turnover at each location. In fiscal year 2009, fifty-four new instant ticket games were launched – 17-\$1, 14-\$2, 9-\$3, 10-\$5, 2-\$10, and 2-\$20—1 more \$1, 3 less \$2, 1 more \$3, and 1 more \$20 than in the previous fiscal year, but the same total number of games were launched for each fiscal year. In fiscal year 2008, sales for fifty-four new instant ticket games were launched –16-\$1, 17-\$2, 8-\$3, 10-\$5, 2-\$10 and 1-\$20—4 less \$1, 1 less \$2, and 2 less \$3 than in the prior fiscal year. In fiscal year 2009, the Lottery launched 18 games with prize tickets and 36 games without prize tickets, while in fiscal year 2008, the Lottery launched 22 games with prize tickets and 32 games without prize tickets. Instant ticket sales for every month in fiscal year 2009 were lower than for the comparable month in fiscal year 2008. Instant ticket sales for only one month in fiscal year 2008 (July 2007) were higher than in fiscal year 2007.

Powerball sales are generally driven by the advertised jackpot. In fiscal year 2009, there were 4 jackpots that surpassed \$150 million with two jackpots exceeding \$200 million (\$206.9 million and \$232.1 million). There was also a jackpot that rose to \$144 million. In fiscal year 2008, there were also 4 jackpots that climbed to more than \$150 million with one going to \$314.3 million and one reaching \$276.3 million before being won. In fiscal year 2007, there were three jackpots that were more than \$200 million, the largest going to \$254 million. There were also two jackpots that rose to \$106 and \$182 million each. The differences in the jackpot amounts in these fiscal years reflect in the net sales for each fiscal year.

Similar to Powerball, Roadrunner Cash sales are driven by the top prize amount. In fiscal year 2009, the top prize was more than \$150,000 for five drawings, climbing to \$280,000, \$245,000 and \$230,000. In fiscal year 2008, the top prize was more than \$150,000 for six drawings, going to \$330,000 and \$210,000. These differences in the top prizes reflected on the net sales in the two fiscal years.

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS - CONTINUED

Net Sales and Prize Expense - Continued

*Net Sales – Continued*

The MUSL game, Hot Lotto, was first introduced in New Mexico on November 12, 2006 with the first drawing on November 15, 2006. In January 2008, a Sizzler multiplier feature was added to Hot Lotto. Net sales for fiscal year 2009 were more than \$2.4 million greater than in the prior fiscal year. During the current fiscal year the jackpot prize climbed to \$12.2 million before being won and ended the year at \$10.1 million. These higher jackpots may have lent to higher sales this fiscal year than in the prior fiscal year. Net sales for fiscal year 2008 increased by approximately \$500,000 over the annualized net sales in fiscal year 2007. The jackpot for the first week in fiscal year 2008 was \$12.9 before being won. Three other jackpots exceeded \$5 million with the largest jackpot climbing to \$7.19 million.

Pick 3 net sales increased by more than \$569,000 in fiscal year 2009 compared to the previous fiscal year. Pick 3 net sales in fiscal year 2008 increased by approximately \$268,000 from the net sales in fiscal year 2007. 4 This Way! sales had been decreasing during the last few fiscal years, thus, the game was ended in October 2007. The Lottery introduced a Raffle game in October 2007. The game did not meet the expectations of the Lottery, contributing \$1,001,400 to drawing game net sales. Thus, another Raffle game was not held in fiscal year 2009.

*Prize Expense*

Prize expense for drawing games with a rolling jackpot or a top prize is based on the overall prize payout per the game design, while prize expense for the other drawing games is determined by the prizes won for each drawing. 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 year 2009, prize expense increased by about 1% prior to the application of unclaimed prizes, while in fiscal year 2008, prize expense decreased by about 2% prior to the application of unclaimed prizes.

At the end of the claim period for each game, unclaimed prizes for the Lottery's instant games and drawing games are paid into the "Prize Fund," in accordance with the New Mexico Lottery Act. These unclaimed prizes from the Lottery's prize fund are used to supplement the prizes in instant and drawing games and for second chance drawings and, therefore, reduce the prize expense for Lottery products and help the Lottery to maximize its sales and its return to education.

Prize Tickets

In fiscal years 2009 and 2008, prize tickets decreased in instant games by \$1,744,558 (52.3) % and \$1,002,590 (23.1) %, respectively. Prize tickets are 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. In the last few years, the Lottery has been studying the market to determine the optimum quantity of prize tickets to place each fiscal year in its instant ticket games in order to optimize its instant ticket sales.



New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS – CONTINUED

Game Expenses

Table 4  
Game Expenses

	2009	2008	2007	(Decrease) \$ Change 2008 to 2009	(Decrease) % Change 2008 to 2009	Increase (Decrease) \$ Change 2007 to 2008	Increase (Decrease) % Change 2007 to 2008
Prize expense	\$ 78,307,339	\$ 80,091,765	\$ 85,119,755	\$ (1,784,426)	(2.2)%	\$(5,027,990)	(5.9)%
Retailer							
commissions	9,271,602	9,676,366	9,754,742	(404,764)	(4.2)	(70,376)	(0.8)
On-line vendor							
fees	4,009,103	6,999,633	6,597,580	(2,990,530)	(42.7)	402,053	6.1
Advertising	2,177,579	2,192,858	2,913,129	(15,279)	(0.7)	(720,271)	(24.7)
Ticket vendor							
fees	1,596,931	1,648,674	1,444,683	(51,743)	(3.1)	203,991	14.1
Other game							
expenses	993,965	1,115,348	2,351,209	(121,383)	(10.9)	(1,235,861)	(52.6)
Total game							
Expenses	<u>\$ 96,356,519</u>	<u>\$ 101,724,644</u>	<u>\$ 108,181,098</u>	<u>\$ (5,368,125)</u>	(5.3)%	<u>\$(6,456,454)</u>	(6.0)%

The changes in retailer commissions for fiscal years 2009 and 2008 are consistent with the changes in gross ticket sales for the two years. Retailer commissions are paid to the Lottery's retailers for selling Lottery tickets and cashing Lottery prizes. Prior to fiscal year 2008, retailers were also paid quarterly incentives for meeting pre-determined sales goals and marketing the Lottery's products with point of sale advertising and display. The Lottery budgeted these quarterly incentives in the 2% Reserve line item, which was part of other game expenses. Until July 1, 2007, the Lottery was allowed by the New Mexico Lottery Act to set aside up to two percent of the Lottery's gross annual revenues for incentive plans for lottery retailers. In comparing fiscal year 2008 to 2007, this change in not paying quarterly incentives is approximately \$660,000.

Prior to November 21, 2008, on-line vendor fees were made up of two fees that were paid to the provider of the Lottery's on-line gaming system. One fee was 8.5236% of drawing game sales. The other fee was a weekly communication fee of \$24.00 for each retailer terminal. Since November 21, 2008, the on-line vendor fee has been fixed at 1.5% of net sales with no additional terminal fee. Normally, the on-line fee, the old and new fee, increases or decreases as drawing game/net sales increase or decrease and the communication fee increased or decreased depending on the number of sales terminals located at the Lottery's retailer

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS – CONTINUED

Game Expenses – Continued

locations. The changes in the on-line vendor fees for the two fiscal years are consistent with the changes in drawing game sales/net sales in 2009 and 2008.

Advertising is expended to market the Lottery and its products to the public and to inform the public about the games available, the jackpot and top prize amounts for the drawing 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 promote sales. Advertising expense amounts in fiscal year 2009 and 2008 are consistent between the two years. Fiscal years' 2009 and 2008 advertising expense was approximately 1.53% and 1.48% of gross revenues, respectively.

In fiscal year 2003, the Lottery signed a new contract with its ticket printer effective in March 2003. Under this new contract, the instant tickets are owned by the vendor with the Lottery paying for the tickets as a percentage of sales when the tickets are sold. The cost for the tickets under this new contract also included a cost for the CRM system used by the Lottery. In fiscal year 2009 and 2008, the cost for any licensing fees or special printing costs were also included in this line item rather than allocated to the prize structure for the game. The ticket vendor fees for fiscal years 2009 and 2008 are consistent with each other at 1.12% of gross revenues for each of the two years.

Included in other game expenses are promotions, shipping and postage, instant ticket vending machine lease, responsible gaming, drawing game and game membership expenses. Fiscal year 2009 reflects a 10.9% decrease in other game expenses or a decrease of \$121,383. This decrease is mainly due to savings in promotion expense and in the lease for instant ticket vending machines. Vending machines for both drawing game tickets and instant game tickets were included as part of the new on-line system agreement's percentage of net sales fee, effective on November 21, 2008. In fiscal year 2007, the 2% reserve fund expense, which had included responsible gaming, was also included in other game expenses. In fiscal year 2008, other game expenses decreased by \$1,235,861. The elimination of the 2% reserve fund expense reflects an \$830,813 change on the financial statements in fiscal year 2008. Some of the costs for security system maintenance and testing and game testing, which had previously been reflected in the 2% reserve fund expense, were reclassified and are now reflected in other line items since these costs are necessary to maintain the security and integrity of the Lottery and could not be eliminated as costs. The cost for the lease for instant ticket vending machines was reduced in fiscal year 2008 by \$172,932. In fiscal year 2007, the expense primarily contributing to the increase in other game expenses was the purchase of electronic signs to display the jackpot and top prizes for the next drawing at retailer locations. These signs are being used in lieu of a number of outdoor board signs throughout New Mexico that were eliminated to decrease costs.

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS - CONTINUED

Operating Expenses

Table 5  
Operating Expenses

	2009	2008	2007	Increase (Decrease) \$ Change 2008 to 2009	Increase (Decrease) % Change 2008 to 2009	(Decrease) \$ Change 2007 to 2008	(Decrease) % Change 2007 to 2008
Salaries, wages, and benefits	\$3,580,649	\$3,387,288	\$3,685,704	\$ 193,361	5.7%	\$ (298,416)	(8.1)%
Leases and insurance	610,217	617,220	632,380	(7,003)	(1.1)	(15,160)	(2.4)
Other operating expenses	<u>1,202,808</u>	<u>1,267,611</u>	<u>1,463,744</u>	<u>(64,803)</u>	(5.1)	<u>(196,133)</u>	(13.4)
Total operating expenses	<u>\$5,393,674</u>	<u>\$5,272,119</u>	<u>\$5,781,828</u>	<u>\$ 121,555</u>	2.3%	<u>\$ (509,709)</u>	(8.8)%

Other operating expenses include depreciation and amortization, utilities and maintenance, professional fees, materials and supplies, travel, and other expenses. In fiscal year 2009, the Lottery increased its total operating expenses by \$121,555 or 2.3%. This increase is essentially due to the salaries and related benefits for a few additional employee positions that were needed for the on-line conversion and the day-to-day operations of the Lottery. In fiscal year 2008, the Lottery had decreased its total operating expenses by more than half-a-million dollars. To bring about this change, the Lottery had eliminated 11 employee positions and reduced the replacement of infrastructure assets and materials and supplies purchases. Professional fees in fiscal year 2008 increased by approximately \$82,000, mainly due to the cost of legal fees for continuing litigation; the expense for these legal fees decreased in fiscal year 2009.

Non-Operating Income

Non-operating income decreased in fiscal year 2009 and 2008 mainly due to the decrease in interest rates and the related interest earned on the Lottery's deposits. In fiscal year 2009, the sublease for the building occupied by the former on-line vendor also ended in January 2009, thus, reducing other income in comparison to the previous fiscal year.

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS - CONTINUED

Net Income

	<u>Total Revenues</u>	<u>Net Income</u>
Fiscal Year 2009	\$ 142,316,217	\$40,814,372
Fiscal Year 2008	147,152,459	40,810,571
Fiscal Year 2007	148,080,254	34,830,136
Increase (decrease) from FY 2008 to FY 2009	<u>\$ (4,836,242)</u>	<u>\$ 3,801</u>
% Increase (decrease) from FY 2008 to FY 2009	<u>(3.3)%</u>	<u>0.0%</u>
Increase (decrease) from FY 2007 to FY 2008	<u>\$ (927,795)</u>	<u>\$ 5,980,435</u>
% Increase (decrease) from FY 2007 to FY 2008	<u>(.6)%</u>	<u>17.2%</u>

Effective July 1, 2007, the New Mexico Lottery Act, Chapter 6, Article 24 NMSA 2978, 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 year 2009, the Lottery transmitted its net income each month, totaling \$40,814,372. The gross revenue percentage return for fiscal year 2009 was 28.63%, exceeding the required blended rate of 28.5%; 27% for the first six months and 30% for the last six months in the fiscal year. In fiscal year 2008, the Lottery transmitted its net income each month, totaling \$40,810,571 for the year. The gross revenue percentage return for fiscal year 2008 was 27.61%, surpassing the required rate of 27%, in comparison to 23.41% for the previous fiscal year.

The changes in net income for fiscal years 2009 and 2008 were related to the changes in sales for the Lottery's games during the two years netted against the cost of the product and operating expenses during the two fiscal years.

In addition to the changes that had been made in fiscal year 2008 to meet the statutory requirement of 27% through December 2008 and 30% thereafter, the Lottery also commenced a new on-line system agreement in November 2008, whereby the fee to the on-line vendor was reduced, and separate terminal communication fees and vending machine fees that had previously been paid to the former on-line vendor were eliminated. This change provided a percentage reduction of the on-line vendor fees to gross revenues of almost 2% in fiscal year 2009.

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS - CONTINUED

Net Income – Continued

In fiscal year 2008, in order to meet the mandated 27% gross revenue return, prize payout per the game structures of the Lottery's games was decreased by about 2% prior to the application of unclaimed prizes; prize tickets in instant games were reduced causing claims for prize tickets to be decreased by over \$1,000,000; advertising expenditures were decreased by approximately \$720,000 for the year; \$660,000 in quarterly sales incentives paid to retailers for meeting pre-determined sales goals and marketing the Lottery's products with point of sale advertising and display were eliminated; eleven employee positions were not filled (a 16% reduction in personnel); incentives paid to sales employees for meeting sales goals were eliminated; and materials and supplies purchases and the replacement of infrastructure assets were reduced.

At this time, the long-term impact of the changes that have been made in the last two years to future years' sales and net income cannot be readily determined.

New Mexico Lottery Authority

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED

FINANCIAL ANALYSIS - CONTINUED

Budgetary Comparison

	2009				
	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	<u>Variance with Final Budget</u>	<u>% Variance with Final Budget</u>
Total revenues	\$ 147,124,000	\$ 138,140,000	\$ 142,316,217	\$ 4,176,217	3.0%
Total game expenses	99,383,000	92,885,000	96,356,519	3,471,519	3.7
Total operating expenses	<u>6,067,000</u>	<u>5,631,000</u>	<u>5,393,674</u>	<u>(237,326)</u>	(4.2)
Operating income	41,674,000	39,624,000	40,566,024	942,024	2.4
Total non-operating income	<u>398,000</u>	<u>251,000</u>	<u>248,348</u>	<u>(2,652)</u>	(1.1)
Net income before transfers to Lottery Tuition Fund	<u>\$ 42,072,000</u>	<u>\$ 39,875,000</u>	<u>\$ 40,814,372</u>	<u>\$ 939,372</u>	2.4%
	2008				
	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	<u>Variance with Final Budget</u>	<u>% Variance with Final Budget</u>
Total revenues	\$ 150,850,000	\$ 141,475,000	\$ 147,152,459	\$ 5,677,459	4.0%
Total game expenses	103,977,000	97,972,000	101,724,644	3,752,644	3.8
Total operating expenses	<u>5,833,000</u>	<u>5,642,000</u>	<u>5,272,119</u>	<u>(369,881)</u>	(6.6)
Operating income	41,040,000	37,861,000	40,155,696	2,294,696	6.1
Total non-operating income	<u>460,000</u>	<u>491,000</u>	<u>654,875</u>	<u>163,875</u>	33.4
Net income before transfers to Lottery Tuition Fund	<u>\$ 41,500,000</u>	<u>\$ 38,352,000</u>	<u>\$ 40,810,571</u>	<u>\$ 2,458,571</u>	6.4%

In fiscal year 2009, the original fiscal year budget was revised as a result of sales not performing as planned. The total revenues budget was reduced by almost \$9,000,000. The Lottery revised its fiscal year 2009 original annual budget to decrease instant ticket sales by \$9 million, Powerball sales by \$3 million, Roadrunner Cash sales by \$900,000 and to increase Hot Lotto sales by \$2.2 million and Pick 3 sales by \$200,000. Prize tickets and spoiled, stolen and promotional tickets were reduced by approximately \$1.5 million.

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED**

**FINANCIAL ANALYSIS - CONTINUED**

**Budgetary Comparison - Continued**

Related game expenses for prize expense, retailer commissions, on-line vendor fees, ticket vendor fees, and shipping and postage, along with expenses for promotions, drawing game, and responsible gaming expenses were also reduced by a total of \$6.5 million. Each line item of operating expenses was also reduced in total by \$436,000 in the revised budget. These changes to sales and expenses resulted in a reduction to net income of \$2,197,000.

Actual net sales for fiscal year 2009 improved, surpassing the sales projected for each product per the revised budget and providing about \$4.2 million in total revenues in excess of the revised budget; ending the fiscal year at 103.0% of the revised budget. Net income exceeded the revised budget by \$939,372. The Powerball run-ups in April 2009 and May 2009 lent to Powerball net sales exceeding the revised FY 2009 budget by almost \$2 million. Net sales for instant tickets and the other three drawing games contributed the remaining \$2.2 million during the last months of the fiscal year to surpass the revised net sales budget for their respective line items. Game expenses ended the fiscal year at 103.7% of the revised budget and were directly in correlation with the total revenues revised budget percentage. At the end of the fiscal year, total operating expenses were at 95.8% of the revised budget or almost \$240,000 less than the revised budget.

In March 2008, the original fiscal year 2008 budget was revised as a result of sales not performing as planned during the first half of the fiscal year. The total revenues budget was reduced by over \$9.3 million. The Lottery revised its fiscal year 2008 annual budget to decrease instant ticket sales by \$4.5 million, Powerball sales by \$2 million, Roadrunner Cash sales by \$1.2 million, and the Raffle game sales by almost \$1.5 million and increased Hot Lotto sales by \$200,000, Pick 3 sales by \$100,000, and revised 4 This Way! sales to actual of \$215,000. The budget for prize tickets was increased by \$700,000. The related game expenses for prize expense, retailer commissions, on-line vendor fees, ticket vendor fees, and shipping and postage were also decreased in relation to the change in budgeted sales. Advertising expense was increased by \$200,000 to combat the decrease in sales. Operating expenses were reduced in total by \$191,000 in the revised budget. Because of the change in budgeted sales, the projected net income was decreased by over \$3.1 million to \$38,352,000.

During the 2<sup>nd</sup> half of fiscal year 2008, sales for Instant ticket, Powerball, Hot Lotto and Pick 3 improved, so that sales for the fiscal year surpassed the revised budget by over \$2.9 million, \$1.5 million, \$700,000, and \$227,000 for these games, respectively. Roadrunner Cash was short of the revised budget by nearly \$750,000. At the end of the fiscal year, total revenues were nearly \$5.7 million more than the revised budget or 104% of the revised budget. The game expenses budget had also been decreased for the fiscal year by over \$6,000,000 to coincide with the change in sales. Game expenses ended the fiscal year at 103.8% of the revised budget and directly in parallel with the increase in net sales. At the end of the fiscal year, operating expenses totaled 93.4% of the budget or almost \$370,000 less than the revised budget. The final net income was over \$2.4 million more than the revised budget at 106.4% of its budget.

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) - CONTINUED**

**FINANCIAL ANALYSIS - CONTINUED**

**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 as of June 30, 2009 and 2008, and results of its operations, cash flows, variances from budgets, and percentage return to the state for the years then ended for the New Mexico Lottery Authority and to demonstrate the Lottery's accountability for the revenues it receives.

If you have any questions about this report or need additional financial information, contact the Director of Finance at the New Mexico Lottery Authority, P.O. Box 93130, Albuquerque, New Mexico 87199-3130.



New Mexico Lottery Authority

STATEMENTS OF NET ASSETS

June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
CURRENT ASSETS		
Cash and cash equivalents	\$ 4,089,266	\$ 5,359,828
Accounts receivable (net of allowance for doubtful accounts)	1,717,935	1,817,274
Reserves on deposit	2,648,344	2,542,282
Inventory	9,262	15,680
Prepaid expenses	<u>105,998</u>	<u>93,705</u>
Total current assets	8,570,805	9,828,769
CAPITAL ASSETS, NET		
	<u>254,593</u>	<u>249,252</u>
Total assets	<u>\$ 8,825,398</u>	<u>\$ 10,078,021</u>
CURRENT LIABILITIES		
Accounts payable and other current liabilities	\$ 1,883,818	\$ 1,239,586
Current portion of capital lease obligation	6,228	-
Prizes payable	4,142,150	5,885,786
Due to Lottery Tuition Fund	<u>2,759,464</u>	<u>2,952,649</u>
Total current liabilities	8,791,660	10,078,021
LONG-TERM LIABILITIES		
Noncurrent portion of capital lease obligation	<u>33,738</u>	<u>-</u>
Total liabilities	<u>\$ 8,825,398</u>	<u>10,078,021</u>
NET ASSETS		
Invested in capital assets, net of related debt	\$ 254,593	\$ 249,252
Unrestricted net assets (deficit)	<u>(254,593)</u>	<u>(249,252)</u>
Total net assets	<u>\$ -</u>	<u>\$ -</u>

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

New Mexico Lottery Authority

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS  
Years ended June 30, 2009 and 2008

	2009	2008
<b>REVENUES</b>		
Instant ticket sales	\$ 82,178,010	\$ 89,925,612
Powerball sales	43,983,020	44,504,959
Hot Lotto sales	8,424,318	6,004,241
Roadrunner Cash sales	6,451,302	6,552,774
Pick 3 sales	2,897,012	2,327,283
Raffle game sales	-	1,001,400
4 This Way! sales	-	215,546
Retailer fees	40,188	46,782
Prize tickets	(1,588,669)	(3,333,227)
Spoiled, stolen, and promotional tickets	(68,964)	(92,911)
Total revenues	<u>142,316,217</u>	<u>147,152,459</u>
<b>GAME EXPENSES</b>		
Prize expense	78,307,339	80,091,765
Retailer commissions	9,271,602	9,676,366
On-line vendor fees	4,009,103	6,999,633
Advertising	2,177,579	2,192,858
Ticket vendor fees	1,596,931	1,648,674
Shipping and postage	366,280	376,029
Promotions	289,495	368,766
Drawing game	133,113	142,298
Game membership	90,207	66,135
Responsible gaming	81,120	81,120
Instant ticket vending machine lease	33,750	81,000
Total game expenses	<u>96,356,519</u>	<u>101,724,644</u>
<b>OPERATING EXPENSES</b>		
Salaries, wages, and benefits	3,580,649	3,387,288
Leases and insurance	610,217	617,220
Utilities and maintenance	417,736	421,690
Other	261,897	69,339
Professional fees	200,270	402,993
Depreciation and amortization	172,315	191,907
Materials and supplies	102,952	108,370
Travel	47,638	73,312
Total operating expenses	<u>5,393,674</u>	<u>5,272,119</u>
<b>OPERATING INCOME</b>	<u>40,566,024</u>	<u>40,155,696</u>
<b>NON-OPERATING INCOME</b>		
Interest income	142,683	492,351
Other income	105,665	162,524
Total non-operating income	<u>248,348</u>	<u>654,875</u>
Net income before transfers	40,814,372	40,810,571
Transfers to Lottery Tuition Fund	<u>(40,814,372)</u>	<u>(40,810,571)</u>
Change in net assets	-	-
Net assets at beginning of year	<u>-</u>	<u>-</u>
Net assets at end of year	<u>\$ -</u>	<u>\$ -</u>

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

New Mexico Lottery Authority

**STATEMENTS OF CASH FLOWS**

Years ended June 30, 2009 and 2008

Increase (Decrease) in Cash and Cash Equivalents

	<u>2009</u>	<u>2008</u>
Cash flows from operating activities		
Cash received:		
From retailers-sales net of commissions, incentives, and prize, spoiled, and stolen ticket credits	\$ 133,127,232	\$ 137,504,704
From MUSL - Powerball and Hot Lotto jackpots	102,903,653	4,117,513
Cash payments:		
To prize winners and related taxes	(170,567,957)	(70,519,847)
To suppliers of goods or services	(10,593,510)	(15,680,192)
To MUSL	(12,386,671)	(13,380,242)
To employees for services and related taxes	<u>(2,907,184)</u>	<u>(2,793,486)</u>
Net cash provided by operating activities	<u>39,575,563</u>	<u>39,248,450</u>
 Cash flows from investing activities		
Receipts of interest	226,578	258,773
Receipt of royalties	28,226	-
Receipts of rent	79,169	131,204
Other	<u>8,749</u>	<u>319</u>
Net cash provided by investing activities	<u>342,722</u>	<u>390,296</u>
 Cash flows from noncapital financing activities		
Transfers to Lottery Tuition Fund	<u>(41,007,557)</u>	<u>(41,018,670)</u>
 Cash flows from capital and related financing activities		
Purchases of capital assets	(177,656)	(88,708)
Principal payments under capital lease	<u>(3,634)</u>	<u>-</u>
Net cash used by capital and related financing activities	<u>(181,290)</u>	<u>(88,708)</u>
 NET DECREASE IN CASH AND CASH EQUIVALENTS	(1,270,562)	(1,468,632)
 Cash and cash equivalents at beginning of year	<u>5,359,828</u>	<u>6,828,460</u>
 Cash and cash equivalents at end of year	<u>\$ 4,089,266</u>	<u>\$ 5,359,828</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, 2009 and 2008

Increase (Decrease) in Cash and Cash Equivalents

	<u>2009</u>	<u>2008</u>
Reconciliation of operating income to net cash provided by operating activities		
Operating income	\$ 40,566,024	\$ 40,155,696
Adjustments to reconcile operating income to net cash provided by operating activities		
Depreciation	172,315	191,907
Interest on MUSL unreserved account	8,347	179,283
Vendor's non-cash transactions	(525)	(2,775)
Net changes in assets and liabilities:		
Accounts receivable	82,617	28,611
Reserves on deposit	(106,062)	(204,264)
Inventory	6,418	110
Prepaid expenses	(12,293)	1,898
Accounts payable and other liabilities	644,232	(1,311,142)
Accrued	(41,874)	(100,064)
Prizes payable	(1,743,636)	309,190
	<u>\$ 39,575,563</u>	<u>\$ 39,248,450</u>

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

New Mexico Lottery Authority

STATEMENTS OF FIDUCIARY NET ASSETS

June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
ASSETS		
Cash and cash equivalents	\$ 292,788	\$ 213,131
Marketable securities and other investments	2,211,022	2,630,150
Contribution receivable	<u>16,765</u>	<u>13,957</u>
Total assets	<u>\$ 2,520,575</u>	<u>\$ 2,857,238</u>
NET ASSETS		
Pension plan participants' benefits	<u>\$ 2,520,575</u>	<u>\$ 2,857,238</u>

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

New Mexico Lottery Authority

STATEMENTS OF CHANGES IN FIDUCIARY NET ASSETS

Years ended June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
ADDITIONS		
Investment earnings	\$ 282,355	\$ 42,659
Employer contributions	<u>340,012</u>	<u>312,122</u>
Total additions	622,367	354,781
DEDUCTIONS		
Investment losses	863,892	354,824
Distributions to participants	95,030	512,369
Fees	<u>108</u>	<u>-</u>
Total deductions	959,030	867,193
	(336,663)	(512,412)
Net assets - beginning	<u>2,857,238</u>	<u>3,369,650</u>
Net assets - ending	<u><u>\$ 2,520,575</u></u>	<u><u>\$ 2,857,238</u></u>

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

NOTES TO FINANCIAL STATEMENTS

June 30, 2009 and 2008

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. Reporting Entity

The financial reporting entity as defined by Governmental Accounting Standards Board (GASB) Statement 14, 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 or incomplete. 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 drawing 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.

In accordance with Governmental Accounting Standards Board (GASB) Statement Number 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Lottery has elected to follow all GASB pronouncements, and all Statements and Interpretations of the Financial Accounting Standards Board, Opinions of the Accounting Principles Board, Accounting Research Bulletins, and authoritative pronouncements of the American Institute of Certified Public Accountants, issued on or before November 30, 1989 (collectively representing the generally accepted private-sector accounting hierarchy in the United States of America). In instances where GASB guidance conflicts with private sector principles, the Lottery conforms to GASB.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2009 and 2008

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

2. Basis of Presentation - Continued

A Fiduciary Fund is used to account for assets held in a trustee capacity for Lottery employees. The Lottery's only fiduciary fund is a pension trust fund.

The pension trust fund per Statements of Fiduciary Net Assets and Statements of Changes in Fiduciary Net Assets and Note D reflects the activities of the New Mexico Lottery Authority Retirement Plan (Plan) pursuant to a trust agreement with a national bank. The bank 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 nonoperating 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 drawing game tickets. The Lottery also recognizes retailer fees for connecting new retailers to the system and for the use of digital signage by the retailers at their stores 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 nonoperating 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 2009 and 2008 there were no restricted resources.

3. Budgets and Budgetary Accounting.

Each year Lottery management prepares a budget in conformity to 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 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 Statement 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.

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



NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2009 and 2008

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

5. Accounts Receivable - Continued

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, 2009 and 2008, an allowance for doubtful accounts of \$72,338 and \$82,597, respectively, has been provided to recognize future uncollectible billings. In fiscal years 2009 and 2008, ten customers (457 and 463 retailer locations) represented 52% and 52% of sales and 54% and 51% 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) and Hot Lotto® (Hot Lotto) games for the Lottery. Each MUSL member sells Powerball and Hot Lotto 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 both Powerball and Hot Lotto are 50% of each game's drawing period's sales after the prize reserve accounts are funded to the amounts set by the MUSL product group. MUSL included 2% of the Lottery's Powerball drawing period's sales in two prize reserve accounts until the Lottery's share of the prize reserve accounts reached the amounts designated by the MUSL product group. Both the Lottery's Powerball Prize Reserve Account (PRA) and the Set Prize Reserve Account are fully funded. MUSL includes from 1% 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 until the Lottery's share of the prize reserve account reaches the amount designated by the MUSL product group. At June 30, 2009 and 2008, the Lottery's remaining Hot Lotto prize reserve buy-in amount was \$272,908 and \$311,593, respectively. MUSL has placed a \$100,000,000 cap on the two Powerball prize reserve funds and a \$9,000,000 cap on the Hot Lotto prize reserve fund. Once the prize reserve funds exceed these designated caps, the excess becomes part of the grand prize pool. The prize reserve funds serve as contingency reserves to protect MUSL from unforeseen prize liabilities and the money in these reserve funds are to be used at the discretion of the MUSL Board of Directors. The prize reserve funds are refundable to MUSL members if MUSL disbands, a member leaves MUSL, or a game is discontinued. In these instances, members must wait one year before receiving their remaining share, if any, of the prize reserve funds. 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, 2009 and 2008, the Lottery's share of the Powerball prize reserve funds was \$1,849,264 and \$1,854,490, respectively; the Lottery's share of the

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2009 and 2008

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

6. Reserves on Deposit - Continued

Hot Lotto prize reserve funds was \$468,757 and \$351,530, respectively; and the Lottery's share of the unreserved fund was \$330,323 and \$336,262, respectively.

A winner of a Powerball grand prize or a Hot Lotto grand prize may select that the prize be paid at the cash value of the prize or as an annuity. A Powerball grand prize annuity is paid out in 30 installments and a Hot Lotto grand prize annuity is paid out in 25 installments. Government securities at the discounted value of the grand prize annuity are purchased by MUSL 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.

7. Inventory

At the inception of the Lottery, inventory, which mainly consisted of lottery instant tickets for future use, was carried at the lower of cost or market using the specific identification method. In March 2003, the Lottery entered into an agreement with its instant ticket printer whereby the vendor retains title to the instant ticket inventory until the instant tickets are sold. At that time, the Lottery pays the vendor a fee based on a fixed percentage of the instant tickets sold. In fiscal year 2004, the Lottery commenced distributing games printed under this new agreement. During fiscal year 2009, the Lottery depleted the remaining instant ticket inventory that it owned. As of June 30, 2009 and 2008, respectively, \$9,262 and \$0 in merchandise prizes for second chance drawings are included in inventory.

8. Capital Assets

Capital assets, which include data processing software and hardware, tenant improvements, vehicles, furniture and fixtures, and equipment are stated at cost net of accumulated depreciation. The Lottery capitalizes all capital assets that have a cost greater than \$5,000 and an expected useful life of more than one year. Depreciation is computed using the straight-line method over the estimated useful lives of 2 to 5 years, except for leasehold improvements, which are amortized over their expected useful lives or the lease term, whichever is shorter. When assets are retired or otherwise disposed of, 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.

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2009 and 2008

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

9. Revenue and Accounts Receivable Recognition

Lottery games are sold to the public by contracted retailers and directly by the Lottery. Revenue and accounts receivable for instant tickets are recognized when packs are settled and retailers are billed for the tickets. Revenues and accounts receivable for drawing game games are recognized when drawings are held. Accounts receivable are stated at their net realizable value and their past due status is based upon contractual terms.

10. Prizes

Prize expense for instant, Powerball 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, Raffle, and 4 This Way! games is recorded based on the actual prizes won for each game's drawings.

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.

14. Custodial Credit Risk and Interest Rate Risk

At June 30, 2009 and 2008, 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 and \$100,000, respectively, 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

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2009 and 2008

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

14. Custodial Credit Risk and Interest Rate Risk - Continued

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 in its trust departments. Repurchase agreements are collateralized by the Federal Home Loan Mortgage and Federal National Mortgage Association 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, 2009 and 2008, the Lottery's bank balances of \$4,195,040 and \$5,582,168, respectively, were exposed to custodial credit risk as follows:

	<u>2009</u>	<u>2008</u>
Uninsured and uncollateralized	\$ -	\$ -
Collateral held by the pledging bank's trust department in the Lottery's name	<u>4,195,040</u>	<u>5,582,168</u>
	<u>\$ 4,195,040</u>	<u>\$ 5,582,168</u>

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, 2009 and 2008, the Lottery had an overnight yield repurchase agreement with a one-day maturity.

15. Bank Accounts

<u>Description</u>	<u>Bank</u>	<u>Balance per Bank</u>
Operating account - overnight repurchase agreement	First Community Bank	\$ 4,194,880
Operating account – checking	First Community Bank	<u>160</u>
Total amount deposited in bank		4,195,040
Less: FDIC coverage		<u>(160)</u>
*Total uninsured funds – deposits and overnight repurchase agreement		<u>\$ 4,194,880</u>

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2009 and 2008

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

15. Bank Accounts - Continued

102% pledged collateral requirement per statute for repurchase agreement	\$ 4,278,777
* Total pledged security	<u>(4,293,705)</u>

Amount under (over) requirement at June 30, 2009	<u>\$ (14,928)</u>
--	--------------------

\* Securities are held in safekeeping at the Federal Home Loan Bank in Dallas, Texas. Presented at fair value, CUSIP Numbers 3128MBQF7 (fair market value \$2,237,791) and 31371LWL9 (fair market value \$2,055,914), mature August 1, 2022 and October 1, 2019, respectively. The deposits and repurchase agreement are collateralized with securities held in the name of the New Mexico Lottery.

Cash and cash equivalents per bank at June 30, 2009	\$ 4,195,040
Less reconciling items--outstanding checks	<u>(109,537)</u>

Reconciled cash in bank at June 30, 2009	4,085,503
--	-----------

Cash in vault	<u>3,763</u>
---------------	--------------

Total cash and cash equivalents per Statements of Net Assets	<u>\$ 4,089,266</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.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2009 and 2008

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

18. Net Assets

Net assets are categorized as invested in capital assets (net of related debt), restricted and unrestricted.

*Invested in Capital Assets, net of related debt* - is intended to reflect the portion of net assets which is associated with non-liquid, capital assets, net of related debt.

*Restricted Assets*-are liquid assets (generated from revenues and not bond proceeds), which have third-party (statutory, bond covenant or granting agency) legally enforceable, limitations on their use.

*Unrestricted Assets*-represent unrestricted liquid assets.

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 are applied against prize expense to supplement prizes in the Lottery's games.

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

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2009 and 2008

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES -CONTINUED

21. Compensated Absences Payable

Annual leave and sick leave are accrued at rates specified by the Lottery's Leave Policy. Annual leave is awarded based on the employee's years of 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 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 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, 2009 and 2008, the following changes occurred in the compensated absences liabilities:

Balance			Balance
<u>July 1, 2008</u>	<u>Increase</u>	<u>Decrease</u>	<u>June 30, 2009</u>
\$ 169,875	\$ 13,491	\$ (10,272)	\$ 173,094
Balance			Balance
<u>July 1, 2007</u>	<u>Increase</u>	<u>Decrease</u>	<u>June 30, 2008</u>
\$ 177,892	\$ 20,148	\$ (28,165)	\$ 169,875

The balances of compensated absences payable are reported on the Statements of Net Assets in accounts payable and other current liabilities. The Lottery estimates all compensated absences are due within one year.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2009 and 2008

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES -CONTINUED

23. Long-term Liabilities - Capital Lease Obligations

During the years ended June 30, 2009 and 2008 the following changes occurred in the capital lease obligations:

<u>Balance July 1, 2008</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance June 30, 2009</u>	<u>Amounts Due Within One Year</u>
\$ -	\$ 43,600	\$ (3,634)	\$ 39,966	\$ 6,228

<u>Balance July 1, 2007</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance June 30, 2008</u>	<u>Amounts Due Within One Year</u>
\$ -	\$ -	\$ -	\$ -	\$ -

24. Accounts Payable and Other Current Liabilities

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

	<u>2009</u>	<u>2008</u>
Accounts payable	\$ 1,373,368	\$ 759,397
Accrued liabilities, vendors*	145,605	135,099
Accrued liabilities, retailers*	14,500	20,120
Accrued payroll, and payroll taxes and benefits	177,251	155,095
Compensated absences	<u>173,094</u>	<u>169,875</u>
	<u>\$ 1,883,818</u>	<u>\$ 1,239,586</u>

\* The Lottery has accrued an estimated amount of services delivered by its vendors and retailers as of June 30, 2009 and 2008, respectively.



New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2009 and 2008

NOTE B – CAPITAL ASSETS

Capital assets at June 30, 2009 consisted of:

	Beginning Balance	Reclass- ification	Increases	Decreases	Ending Balance
Data processing software	\$ 2,084,202	\$ -	\$ 25,731	\$ -	2,109,933
Data processing equipment	1,821,034	-	27,980	-	1,849,014
Equipment - Security and disaster recovery	-	572,479	-	-	572,479
Vehicles	472,992	-	112,385	(139,296)	446,081
Tenant improvements	797,602	(468,575)	11,560	-	340,587
Furniture and fixtures	245,048	6,026	-	-	251,074
Equipment - drawing	179,647	(32,119)	-	-	147,528
Equipment - communications	116,260	-	-	-	116,260
Equipment - warehouse	156,698	(86,867)	-	-	69,831
Equipment - office	75,050	(23,063)	-	-	51,987
Obsolete capital assets	499,015	32,119	-	-	531,134
<b>Capital assets</b>	<b>6,447,548</b>	<b>-</b>	<b>177,656</b>	<b>(139,296)</b>	<b>6,485,908</b>
Data processing software	(2,074,455)	-	(12,752)	-	(2,087,207)
Data processing equipment	(1,775,235)	-	(32,923)	-	(1,808,158)
Equipment - Security and disaster recovery	-	(526,137)	(3,706)	-	(529,843)
Vehicles	(388,243)	-	(62,443)	139,296	(311,390)
Tenant improvements	(743,069)	422,232	(19,750)	-	(340,587)
Furniture and fixtures	(242,011)	(6,025)	(1,176)	-	(249,212)
Equipment - drawing	(146,607)	32,119	(22,821)	-	(137,309)
Equipment - communications	(109,769)	-	(6,113)	-	(115,882)
Equipment - warehouse	(155,060)	86,867	(893)	-	(69,086)
Equipment - office	(64,832)	23,063	(9,738)	-	(51,507)
Obsolete capital assets	(499,015)	(32,119)	-	-	(531,134)
<b>Accumulated depreciation</b>	<b>(6,198,296)</b>	<b>-</b>	<b>(172,315)</b>	<b>139,296</b>	<b>(6,231,315)</b>
<b>Capital assets, net</b>	<b>\$ 249,252</b>	<b>\$ -</b>	<b>\$ 5,341</b>	<b>\$ -</b>	<b>\$ 254,593</b>

Included in data processing software and data processing equipment are \$43,600 and \$0, respectively in assets under a capital lease at June 30, 2009 and 2008. For each fiscal year there were \$3,634 and \$0, respectively, in related amortization on these assets.

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2009 and 2008

NOTE B – CAPITAL ASSETS - CONTINUED

Capital assets at June 30, 2008 consisted of:

	Beginning Balance	Reclass- ification	Increases	Decreases	Ending Balance
Data processing software	\$ 2,075,202	\$ -	\$ 9,000	\$ -	\$ 2,084,202
Data processing equipment	1,815,102	-	5,932	-	1,821,034
Equipment - Security and disaster recovery	-	-	-	-	-
Vehicles	483,143	-	42,966	(53,117)	472,992
Tenant improvements	797,602	-	-	-	797,602
Furniture and fixtures	245,048	-	-	-	245,048
Equipment - drawing	155,622	-	24,025	-	179,647
Equipment - communications	116,260	-	-	-	116,260
Equipment - warehouse	156,698	-	-	-	156,698
Equipment - office	75,050	-	-	-	75,050
Obsolete capital assets	499,015	-	-	-	499,015
<b>Capital assets</b>	<b>6,418,742</b>	<b>-</b>	<b>81,923</b>	<b>(53,117)</b>	<b>6,447,548</b>
Data processing software	(2,069,794)	-	(4,661)	-	(2,074,455)
Data processing equipment	(1,728,397)	-	(46,838)	-	(1,775,235)
Equipment - Security and disaster recovery	-	-	-	-	-
Vehicles	(386,308)	-	(55,052)	53,117	(388,243)
Tenant improvements	(714,434)	-	(28,635)	-	(743,069)
Furniture and fixtures	(240,232)	-	(1,779)	-	(242,011)
Equipment - drawing	(124,372)	-	(22,235)	-	(146,607)
Equipment - communications	(89,850)	-	(19,919)	-	(109,769)
Equipment - warehouse	(153,545)	-	(1,515)	-	(155,060)
Equipment - office	(53,559)	-	(11,273)	-	(64,832)
Obsolete capital assets	(499,015)	-	-	-	(499,015)
<b>Accumulated depreciation</b>	<b>(6,059,506)</b>	<b>-</b>	<b>(191,907)</b>	<b>53,117</b>	<b>(6,198,296)</b>
<b>Capital assets, net</b>	<b>\$ 359,236</b>	<b>\$ -</b>	<b>\$ (109,984)</b>	<b>\$ -</b>	<b>\$ 249,252</b>

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2009 and 2008

NOTE C – ALLOCATION OF NET INCOME/TRANSFERS TO LOTTERY TUITION FUND

	<u>Net Income</u>	<u>Due to Lottery Tuition Fund</u>	<u>Net Assets</u>
Balance at June 30, 2008	\$ 2,952,649	\$ 2,952,649	\$ -
Current year net income	40,814,372	40,814,372	-
Current year transfers	<u>(41,007,557)</u>	<u>(41,007,557)</u>	<u>-</u>
Balance at June 30, 2009	<u>\$ 2,759,464</u>	<u>\$ 2,759,464</u>	<u>\$ -</u>

In accordance with the Lottery Act, no later than the last business day of each month, the Lottery shall transmit at least twenty-seven percent of the gross revenue of the previous month until December 31, 2008 and at least thirty percent of the gross revenue of the previous month, thereafter, to the New Mexico State Treasurer, who shall deposit it into state agency number 950, the Lottery Tuition Fund, SHARE fund number 63700. As of July 31, 2009 and 2008, the Lottery has transferred \$40,814,372 and \$40,810,571, respectively, for the years ended June 30, 2009 and 2008 to the New Mexico State Treasurer.

NOTE D - RETIREMENT PLAN

Plan Description

All of 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. The New Mexico Lottery Authority Retirement Plan provides for retirement benefits to plan members and their beneficiaries. The balances and activity of the Plan as of and for the years ended June 30, 2009 and 2008 are presented in the Statements of Fiduciary Net Assets and Statements of Changes in Fiduciary Net Assets. There are no separately issued financial statements available for the New Mexico Lottery Authority Retirement Plan.

**NOTES TO FINANCIAL STATEMENTS - CONTINUED**

June 30, 2009 and 2008

**NOTE D - RETIREMENT PLAN - CONTINUED**

Funding Policy

The Lottery contributes 13.25% of compensation for eligible employees to the Plan. Lottery contributions are 100% vested when deposited monthly. For the years ended June 30, 2009 and 2008, the Lottery recognized \$339,981 and \$312,122 of pension expense for the Plan on eligible compensation of \$2,565,894 and \$2,355,638, respectively. The entire pension amounts have been paid to the Plan by June 30, 2009 and 2008, respectively, for all compensation paid during the respective fiscal years.

**NOTE E – CREDIT AGREEMENT**

In July 2005, the Lottery entered an agreement with First Community Bank effective May 15, 2005 for an automatic unsecured overdraft line of credit sweep in the amount of \$1,000,000 with a fixed interest rate at the Wall Street Journal interest rate less .500 percentage points (2.75% and 4.5% at June 30, 2009 and 2008, respectively). The line matured in May 2008 and was extended through May 14, 2010. For the periods ended June 30, 2009 and 2008, the Lottery had no outstanding borrowings against the line.

**NOTE F - LEASES**

The Lottery has entered into operating leases for the rental of office and warehouse space, and vending machines. Rent expense was \$509,560 and \$556,860 for the years ending June 30, 2009 and 2008, respectively. In August 2002, the Lottery renegotiated its leases for office and warehouse space. These leases were extended for an additional seven years at the same lease amounts that were paid for the final year of the original lease in 2006. Future minimum rental payments on non-cancelable leases with original terms of one year or more are scheduled as follows:

<u>Year ended June 30,</u>	<u>Amount</u>
2010	431,485
2011	431,485
2012	431,485
2013	323,615
	<u>\$ 1,618,070</u>

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2009 and 2008

NOTE F – LEASES - CONTINUED

Following is a schedule of the composition of net rental expense for all long-term operating leases for the years ended June 30:

	<u>2009</u>	<u>2008</u>
Minimum rentals	\$ 465,235	\$ 512,485
Less: Sublease rentals	<u>(73,800)</u>	<u>(122,000)</u>
	<u>\$ 391,435</u>	<u>\$ 390,485</u>

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%.

Years ending June 30:

2010	\$ 8,237
2011	8,237
2012	8,237
2013	8,237
2014	8,237
2015-2016	<u>11,671</u>
Total minimum payments	52,856
Less the amount representing interest	<u>(12,890)</u>
Present value of net minimum payments	<u>\$ 39,966</u>

New Mexico Lottery Authority

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2009 and 2008

**NOTE G - COMMITMENT**

The Lottery had an agreement for the on-line gaming system with GTECH Corporation until November 20, 2008

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 with the option of three additional one year periods or any combination thereof. 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, 500 ticket scanners to enable players to check their tickets for prizes, 225 self service ticket vending machines that sell both instant and drawing game tickets, a disaster recovery and business continuity facility, 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. Since November 21, 2008, the on-line vendor fee has been fixed at 1.5% of net sales, plus the applicable gross receipts tax.

**NOTE H - OTHER EXPENSES**

Other expenses at June 30, consisted of:

	<u>2009</u>	<u>2008</u>
Other	218,408	18,613
Registrations and memberships	22,368	23,681
Training	18,323	24,152
Publications and subscriptions	<u>2,798</u>	<u>2,893</u>
	<u>\$ 261,897</u>	<u>\$ 69,339</u>

New Mexico Lottery Authority

**BUDGETARY COMPARISON STATEMENTS**

Years ended June 30, 2009 and 2008

	2009		2008					
	Original Budget	Final Budget	Actual	Variance with Final Budget	Original Budget	Final Budget	Actual	Variance with Final Budget
<b>Revenues</b>								
Instant ticket sales	\$ 91,000,000	\$ 82,000,000	\$ 82,178,010	\$ 178,010	\$ 91,500,000	\$ 87,000,000	\$ 89,925,612	\$ 2,925,612
Powerball sales	45,000,000	42,000,000	43,983,020	1,983,020	45,000,000	43,000,000	44,504,959	1,504,959
Hot Lotto sales	5,800,000	8,000,000	8,424,318	424,318	5,100,000	5,300,000	6,004,241	704,241
Roadrunner Cash sales	6,900,000	6,000,000	6,451,302	451,302	8,500,000	7,300,000	6,552,774	(747,226)
Pick 3 sales	2,300,000	2,500,000	2,897,012	397,012	2,000,000	2,100,000	2,327,283	227,283
Raffle game sales	-	-	-	-	2,500,000	1,001,000	1,001,400	400
4 This Way! sales	-	-	-	-	-	215,000	215,546	546
Retailer fees	24,000	33,000	40,188	7,188	42,000	45,000	46,782	1,782
Prize tickets	(3,700,000)	(2,300,000)	(1,588,669)	711,331	(3,600,000)	(4,300,000)	(3,333,227)	966,773
Spoiled, stolen, and promotional tickets	(188,000)	(83,000)	(68,964)	14,036	(180,000)	(180,000)	(92,911)	87,089
Bad debts	(12,000)	(10,000)	-	10,000	(12,000)	(6,000)	-	6,000
Total revenues	147,124,000	138,140,000	142,316,217	4,176,217	150,850,000	141,475,000	147,152,459	5,677,459
Total game expenses	99,383,000	92,885,000	96,356,519	3,471,519	103,977,000	97,972,000	101,724,644	3,752,644
Total operating expenses	6,067,000	5,631,000	5,393,674	(237,326)	5,833,000	5,642,000	5,272,119	(369,881)
Operating income	41,674,000	39,624,000	40,566,024	942,024	41,040,000	37,861,000	40,155,696	2,294,696
Total non-operating income	398,000	251,000	248,348	(2,652)	460,000	491,000	654,875	163,875
Net income before transfers to Lottery Tuition Fund	\$ 42,072,000	\$ 39,875,000	\$ 40,814,372	\$ 939,372	\$ 41,500,000	\$ 38,352,000	\$ 40,810,571	\$ 2,458,571

SCHEDULES OF PERCENTAGE RETURN TO THE STATE OF NEW MEXICO  
Years ended June 30, 2009 and 2008

	2009	2008
<b>REVENUES</b>		
Instant ticket sales	\$ 82,178,010	\$ 89,925,612
Powerball sales	43,983,020	44,504,959
Hot Lotto sales	8,424,318	6,004,241
Roadrunner Cash sales	6,451,302	6,552,774
Pick 3 sales	2,897,012	2,327,283
Raffle game sales	-	1,001,400
4 This Way! sales	-	215,546
Retailer fees	40,188	46,782
Prize tickets	(1,588,669)	(3,333,227)
Spoiled, stolen, and promotional tickets	(68,964)	(92,911)
Total revenues	142,316,217	147,152,459
<b>NON-OPERATING INCOME</b>		
Interest income	142,683	492,351
Other income	105,665	162,524
Total non-operating income	248,348	654,875
<b>GROSS REVENUES</b>	142,564,565	147,807,334
<b>GAME EXPENSES</b>		
Prize expense	78,307,339	80,091,765
Retailer commissions	9,271,602	9,676,366
On-line vendor fees	4,009,103	6,999,633
Advertising	2,177,579	2,192,858
Ticket vendor fees	1,596,931	1,648,674
Shipping and postage	366,280	376,029
Promotions	289,495	368,766
Drawing game	133,113	142,298
Game membership	90,207	66,135
Responsible gaming	81,120	81,120
Instant ticket vending machine lease	33,750	81,000
Total game expenses	96,356,519	101,724,644
<b>OPERATING EXPENSES</b>		
Salaries, wages, and benefits	3,580,649	3,387,288
Leases and insurance	610,217	617,220
Utilities and maintenance	417,736	421,690
Other	261,897	69,339
Professional fees	200,270	402,993
Depreciation and amortization	172,315	191,907
Materials and supplies	102,952	108,370
Travel	47,638	73,312
Total operating expenses	5,393,674	5,272,119
<b>OPERATING INCOME</b>	40,566,024	40,155,696
<b>NET INCOME</b>	\$ 40,814,372	\$ 40,810,571
<b>GROSS REVENUE PERCENTAGE RETURN</b>	28.63%	27.61%



**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. Hector H. Balderas  
New Mexico State Auditor

We have audited the basic financial statements of the New Mexico Lottery Authority (the Lottery) and its fiduciary fund as of and for the year ended June 30, 2009, including the budget to actual comparison statement presented as supplemental information and have issued our report thereon dated October 16, 2009. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Lottery's internal control over financial reporting in order to determine our auditing procedures 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 Lottery's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the entity's internal control over financial reporting.

A *control deficiency* 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Lottery's financial statements that is more than inconsequential will not be prevented or detected by the Lottery's internal control.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Lottery's internal control.

Board of Directors  
New Mexico Lottery Authority  
and  
Mr. Hector H. Balderas  
New Mexico State Auditor

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

#### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Lottery's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed one instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of current year findings and responses as item 2009-01.

The Lottery's response to the finding identified in our audit is described in the accompanying schedule of current year findings and responses. We did not audit the Lottery's response and, accordingly, we express no opinion on it.

This report is intended solely for the information of the Lottery's management, Board of Directors, New Mexico Department of Finance and Administration, New Mexico Legislature, and the State Auditor, and is not intended to be and should not be used by anyone other than these specified parties.

*Moss Adams LLP*

Albuquerque, New Mexico  
October 16, 2009

New Mexico Lottery Authority

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Year Ended June 30, 2009

None

SCHEDULE OF CURRENT YEAR AUDIT FINDINGS AND RESPONSES

Year Ended June 30, 2009

**2009-01 COMPLIANCE WITH LOTTERY ACT -- TRANSMISSION OF REQUIRED GROSS REVENUE PERCENTAGES**

**Condition**

Each month of fiscal year 2009, the Lottery transmitted all excess net asset amounts. The Lottery was unable to transmit the required amount of gross revenue to the State Treasurer in five out of twelve months of fiscal year 2009.

**Criteria**

Per NMSA 1978, Section 6-24-24, paragraph B, *Disposition of Revenue*: No later than the last business day of each month, the authority shall transmit at least twenty-seven percent of the gross revenue of the previous month until December 31, 2008 and at least thirty percent of the gross revenue of the previous month thereafter to the state treasurer, who shall deposit it in the lottery tuition fund.

**Effect**

The Lottery was not in compliance with NMSA 1978, Section 6-24-24, paragraph B, *Disposition of Revenue*. The effect of the non-compliance was as follows:

The gross revenue percentages were short of the required transmittal amount in August 2008 (.09% short), October 2008 (.14% short), March 2009 (1.19% short), April 2009 (1.10% short), and June 2009 (4.69% short).

**Cause**

Net income fluctuates from month to month primarily due to fluctuations in ticket sales (net of game expenses) that increase or decrease with the rise or fall in the level of outstanding Powerball or other jackpots.

**SCHEDULE OF CURRENT YEAR AUDIT FINDINGS AND RESPONSES  
(CONTINUED)**

Year Ended June 30, 2009

**2009-01 COMPLIANCE WITH LOTTERY ACT – TRANSMISSION OF REQUIRED  
GROSS REVENUE PERCENTAGES (CONTINUED)**

**Recommendation**

During the past two fiscal years, the Lottery has reduced its expenses in many categories to increase its net revenue return from 23.41% in fiscal year 2007, to 27.61% in fiscal year 2008, and to 28.63% in fiscal year 2009. Given the size and operations of the Lottery, it appears to us that all material reductions in expenses have been made. As a result, due to the fluctuation in sales from month to month (mostly due to the size and frequency of Powerball and other jackpots) it does not seem reasonable that the Lottery will be able to make the statutory requirement of 30% return of net revenue each and every month in future fiscal years.

We recommend that Lottery's Board of Directors respectfully request the New Mexico State Legislature to consider amending NMSA 1978, Section 6-24-24, paragraph B. *Disposition of Revenue*, to include language that is not as restrictive in nature as requiring a set monthly percentage. We believe that an annualized requirement may be more suitable wording considering the monthly fluctuations in sales.

**Management's Response**

The Board of Directors and executive management of the New Mexico Lottery Authority are very cognizant of their fiduciary duty to meet the requirements of the New Mexico Lottery Act "the Act". Therefore, in order to meet the gross revenue percentage return requirements of the Act effective on July 1, 2007, the Lottery has reduced its expenses for salaries, wages and benefits, advertising, retailer incentives, prize payout and online gaming system fees to increase its net revenue return each year.

It is difficult to return a set percentage of revenue every month because jackpots – both the amounts and the frequencies – drive sales in the Powerball, Hot Lotto and Roadrunner Cash games. Jackpots are impossible to predict and the additional sales they drive cannot be forecast accurately into monthly budgets. Although, many Lottery expenses are directly related to these sales, other expenses are not and they occur each month throughout the year, making it a challenge to achieve the statutory required return each and every month.

The Lottery has chosen to continue transferring net revenues (income) to the State of New Mexico each month, regardless of whether the amount is above or below the statutory requirement. We believe we were in substantial compliance with the statutory requirement.

New Mexico Lottery Authority

**SCHEDULE OF CURRENT YEAR AUDIT FINDINGS AND RESPONSES  
(CONTINUED)**

Year Ended June 30, 2009

**2009-01 COMPLIANCE WITH LOTTERY ACT – TRANSMISSION OF REQUIRED  
GROSS REVENUE PERCENTAGES (CONTINUED)**

**Management's Response (Continued)**

With the excess transferred in many months of FY 2009, the Lottery cumulatively exceeded the statutory requirements of 27% for the first half of FY 2009 and 30% for the second half, or a blended rate of 28.5% for the year. (See table attached on the next page).

In an effort to be fully transparent, the Lottery transfers its entire net revenues each month rather than retaining the excess in a reserve fund for a month when net revenues might fall short. Since we may not always achieve net revenues that meet the requirement each month, our goal is to achieve net revenues that meet the statutory requirement for each fiscal year and cumulatively exceed the requirement each month.

With declining sales, it cannot be determined at this time whether we will be able to achieve the statutory requirement each fiscal year. Reductions in expenses in the last few years have left the Lottery with limited resources to support sales growth for existing and future games.

The Board of Directors and executive management of the New Mexico Lottery Authority will take this recommendation into consideration.

SCHEDULE OF CURRENT YEAR AUDIT FINDINGS AND RESPONSES (CONTINUED)

Year Ended June 30, 2009

2009-01 COMPLIANCE WITH LOTTERY ACT -- TRANSMISSION OF REQUIRED GROSS REVENUE PERCENTAGES (CONTINUED)

Analysis of Fiscal Year 2009 transfers to State Compared to Statutory Requirements

	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09	Feb-09	Mar-09	Apr-09	May-09	Jun-09	Total
Gross Revenues	\$ 11,106,173	10,762,546	12,763,136	11,101,504	10,799,551	11,553,331	12,978,363	12,852,686	11,691,808	12,324,974	13,727,808	10,902,686	\$ 142,564,565
Calculation of mandatory transfer to State of NM - 27% 1st 6 Mos. & 30% 2nd 6 Mos.	2,998,667	2,905,887	3,446,047	2,997,406	2,915,879	3,119,399	3,893,509	3,855,806	3,507,542	3,697,492	4,118,342	3,270,806	40,726,782
Net Revenues transferred each month	3,136,696	2,896,626	3,457,567	2,977,779	3,154,860	3,231,563	4,128,104	3,945,535	3,368,551	3,562,391	4,195,236	2,759,464	40,814,372
Excess transferred over statutory requirement	138,029	(9,261)	11,520	(19,627)	238,981	112,164	234,595	89,729	(138,991)	(135,101)	76,894	(511,342)	\$ 87,590
Cumulative excess that could have been used in subsequent months to meet statutory requirement if kept in reserve fund	-	9,261	-	19,627	-	-	-	-	138,991	135,101	-	511,342	-
Year-to-date cumulative remaining	\$ 138,029	128,768	140,288	120,661	359,642	471,806	706,401	796,130	657,139	522,038	598,932	\$ 87,590	\$ 87,590

New Mexico Lottery Authority

**EXIT CONFERENCE**

For the year ended June 30, 2009

An exit conference was held at the New Mexico Lottery Authority on October 13, 2009. The following individuals participated:

<u>Name</u>	<u>Title</u>
<i>New Mexico Lottery Authority Audit Committee</i>	
Reta Jones, CPA	Chairman of the Board
Clifford Stroud, MBA	Treasurer
Herman J. Tabet	Member
 <i>New Mexico Lottery Authority Employees</i>	
Tom Romero	Chief Executive Officer
Sylvia Ann Jaramillo, CPA	Director of Finance
Michael Boland, CPA	Internal Auditor
 <i>Moss Adams LLP</i>	
Scott Eliason, CPA	Audit Partner
Corrine Zajac-Clarkson	Supervisor

**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.