

***Arizona State Lottery,  
A Component Unit of  
the State of Arizona***

*Financial Statements for the Year Ended  
June 30, 2003, Supplemental Schedule of  
Gross Profit by Game for the Year Ended  
June 30, 2003 and Independent Auditors'  
Report*

# ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA COMPREHENSIVE ANNUAL FINANCIAL REPORT

FOR THE FISCAL YEAR ENDED JUNE 30, 2003  
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Janet Napolitano  
Governor



Kathleen S. Pushor  
Executive Director

December 10, 2003

Dear Arizona Lottery Commissioners:

The Arizona Lottery is pleased to submit its audited financial statements for the year ended June 30, 2003, as compiled by the Lottery Administration Department and audited by Deloitte & Touche LLP. The Lottery is responsible for the accuracy and completeness of all data and disclosures in this report. To the best of our knowledge, the information presented is accurate and complete in all material respects and fairly depicts the financial position of the Arizona Lottery. This report includes a statement of net assets of the Arizona Lottery, the related statement of revenues, expenses and changes in Fund net assets, the statement of cash flows, footnotes related to the financial reports and the supplemental schedules of gross profit by game.

The audit of the Arizona Lottery was performed under the authority of A.R.S. § 5-505 and A.R.S. § 5-524, which require an annual audit of the Lottery.

The Arizona Lottery was created in 1980 when Arizona voters approved a ballot initiative adding Title 5, Chapter 5 to the Arizona Revised Statutes. The Lottery began selling instant "scratch-off" tickets in July 1981 and during its twenty-one years of operation has offered a variety of instant and on-line products. The Lottery operates as an agency of the State of Arizona and is reported as an enterprise fund within the state's Comprehensive Annual Financial Report. The fund is operated in a manner similar to a private business enterprise.

In fiscal year 2003, the Arizona Lottery had revenues of \$322.3 million from Lottery ticket sales, 9.3% greater than last fiscal year, and an income before transfers of \$96.3 million, 9.9% greater than last fiscal year. More than \$174 million was paid to our players in prizes, and our retail partners received \$21.4 million for sales commissions. In its twenty-one years of operation, the Lottery has produced over \$4.75 billion in Lottery ticket sales.

In fiscal year 2003, the Arizona Lottery made transfers to other State funds of \$23.0 million for the Local Transportation Assistance Fund, \$7.65 million for the County Assistance Fund, \$18.6 million for the Heritage Fund, \$2.7 million for the Economic Development Fund, \$6.0 million

for Mass Transit and \$34.5 million was transferred to the State General Fund for allocation by the state legislature. In addition, from the Lottery Prize Fund, over \$3.3 million was transferred to the Court Appointed Special Advocate (CASA). In total, \$95.7 million was transferred to the State for FY 2003. In its twenty-one years of operation the Lottery has returned almost \$1.6 billion to its beneficiaries.

Further financial results for fiscal year 2003 are detailed in Management's Discussion & Analysis, included in this report.

Sincerely,

A handwritten signature in black ink, appearing to read "KSPushor", written in a cursive style.

Kathleen S. Pushor  
Executive Director

## INDEPENDENT AUDITORS' REPORT

Commissioners  
Arizona State Lottery  
Phoenix, Arizona

We have audited the accompanying basic financial statements of Arizona State Lottery (the "Lottery"), a component unit of the State of Arizona as of and for the year ended June 30, 2003, as listed in the table of contents. These financial statements are the responsibility of the Lottery's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. 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 audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Lottery as of June 30, 2003 and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report, dated December 10, 2003, 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 grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Our audit was performed for the purpose of forming an opinion on the basic financial statements of the Lottery taken as a whole. The accompanying schedule of gross profit by game is presented for purposes of additional analysis and is not a required part of the basic financial statements. This schedule is the

responsibility of the Lottery's management. Such information has been subjected to the auditing procedures applied by us in the audit of the basic financial statements and, in our opinion, based on our audit, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

The accompanying required supplementary information, management's discussion and analysis, is presented on pages 3 through 7 and is not a requirement part of the basic financial statements, but is supplementary accounting information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Lottery's management. 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.

*Deloitte & Touche LLP*

December 10, 2003

**ARIZONA STATE LOTTERY  
A COMPONENT UNIT OF THE STATE OF ARIZONA  
PROPRIETARY FUND—ENTERPRISE FUND**

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
YEAR ENDED JUNE 30, 2003**

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This discussion and analysis of the Lottery's financial statements is a required component of financial reporting under governmental accounting standards and was prepared by Arizona Lottery Management. It provides an overview of financial activities for the year ended June 30, 2003 and should be read in conjunction with the Lottery's financial statements and notes to the financial statements.

This annual report consists of three types of financial statements and accompanying notes that provide explanations and details of accounting policies, account balances and activities. Account balances and activities are shown as of and for the year ended June 30, 2003, with comparative totals for June 30, 2002. The statement of net assets; the statement of revenues, expenses and changes in net assets; and the notes are presented using the accrual method of accounting. Under this method, financial transactions are recorded when earned or incurred regardless of when cash is received or disbursed. The statement of cash flows reflects cash receipts and disbursements during the same twelve month periods.

The statement of net assets provides information about the assets and liabilities of the Lottery. Assets consist of cash, substantially all held by the State Treasurer, amounts owed to the Lottery from licensed Lottery retailers and other State agencies, ticket inventory and property. Liabilities represent amounts owed by the Lottery to vendors, to employees for wages and benefits, to prize winners and to other State funds. Net assets represent the portion of the Lottery's assets that are not encumbered by liabilities. It serves an indicator of the net worth of the Lottery.

A summary of the financial results of operations for the twelve month periods is presented in the statement of revenues, expenses and changes in net assets. Operating revenues include sales of Lottery tickets, retailer licensing fees, and commissions earned on the sales of Lottery tickets at Lottery offices and special events. Direct costs and administrative expenses comprise the operating expenses section of this statement. Direct costs are variable expenses that fluctuate with the level of sales. Marketing and overhead costs are included in the administrative expenses category. Non-operating revenues consist of interest earned on prize fund cash investments from the State Treasurer and interest credited to the Multi-State Lottery Association (MUSL) unreserved account. The Transfers category includes transfers to other State Funds as required by Lottery statutes.

The statement of cash flows includes cash receipts and disbursements from operating, non-capital financing and investment earnings. This statement also includes a reconciliation of operating income presented on the accrual basis of accounting to net cash provided by operating activities.

The notes to the financial statements present information on accounting policies, transfers and statutory requirements, commitments, contingencies and retirement benefits. These notes are an integral part of the financial statements.

### **SALES ACTIVITIES**

Revenues from the sale of Lottery products for the fiscal year ended June 30, 2003 were the highest in the Lottery's twenty one year history. As shown in the financial statements, sales increased 9.3% from the prior year, from \$294.8 million in Fiscal Year 2002 to \$322.3 million in the current year. The increases in Scratchers<sup>SM</sup>, Powerball<sup>®</sup>, and Pick 3<sup>TM</sup> sales more than offset the decreases in The Pick<sup>TM</sup> and Fantasy 5<sup>TM</sup> sales.

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

| Product Sales | FY 2003 | FY 2002 | Difference | Percentage |
|---------------|---------|---------|------------|------------|
| Scratchers    | \$159.4 | \$143.4 | \$16.0     | 11.2%      |
| Powerball     | 112.3   | 96.2    | 16.1       | 16.7%      |
| The Pick      | 34.3    | 39.2    | -4.9       | -12.5%     |
| Fantasy 5     | 9.7     | 9.8     | -.1        | -1.0%      |
| Pick 3        | 6.6     | 6.2     | .4         | 6.5%       |
| Total         | \$322.3 | \$294.8 | \$27.5     | 9.3%       |

### **TOTAL REVENUES**

Non-operating revenues for the year ended June 30, 2003 were \$396,100 as compared to \$679,500 for the year ended June 30, 2002. Non-operating revenue is comprised of interest earned on invested cash. The decline of more than \$283,000 is due to interest rates that were substantially lower in Fiscal Year 2003.

Total revenues were \$323.0 million for the year ended June 30, 2003 as compared to \$295.6 million for the year ended June 30, 2002. As mentioned above, the majority of the increase was due to the increase in sales revenues.



## **MAJOR EXPENSES**

\$209.7 million of the Lottery's total operating expenses of \$226.7 million for the year ended June 30, 2003 were incurred in direct support of the sales of Lottery games. These expenses include prize expense, retailer commissions and incentives, purchases of Scratchers tickets, telecommunication network costs, compensation to the vendor for Scratchers ticket distribution and compensation to the vendor who maintains and supports the on-line gaming system.

In comparison, \$192.5 million of the Lottery's total operating expenses of \$208.0 million for the year ended June 30, 2002 were game-related expenses.

The following table compares the game-related expenses between fiscal years. All expenses are presented in millions of dollars.

| Game Related Expenses                          | FY 2003 | FY 2002 | Difference | Percentage |
|--|---------|---------|------------|------------|
| Prize Expense                                  | \$174.0 | \$160.2 | \$13.8     | 8.6%       |
| Retailer Commissions                           | 21.4    | 20.0    | 1.4        | 7.0%       |
| On-line System Expenses                        | 10.4    | 9.8     | .6         | 6.5%       |
| Scratchers System and<br>Distribution Expenses | .7      | 0.0     | .7         | 0.0%       |
| Tickets Purchased                              | 3.2     | 2.5     | .7         | 28.0%      |
| Total  | \$209.7 | \$192.5 | \$17.2     | 8.9%       |

The increase in prize expense, retailer commissions, and tickets purchased is reflective of the increase in product sales. See the product sales schedule above. The increase in on-line system expenses is made up of two elements. On-line vendor fees are based on a contracted percentage of on-line sales and increase with the higher level of on-line sales this fiscal year. The second element is the telecommunications costs associated with the Lottery retailer network. The telecommunications costs increased almost \$54,000 over last fiscal year. The Lottery contracted with an outside vendor for Scratchers ticket distribution and accounting services in January resulting in increased costs of \$657,900 over last fiscal year.

Of the \$17.0 million in Fiscal Year 2003 in other operating expenses, \$8.5 million was used for advertising and promotion and \$5.3 million was used to compensate Lottery employees. In comparison, of the \$15.6 million in Fiscal Year 2002 other operating expenses, \$7.4 million was used for advertising and promotion and \$5.0 million was used to compensate Lottery employees.

## **TRANSFERS TO OTHER STATE FUNDS**

Note 3 to the financial statements details the amounts transferred to other State Funds. The increase in product sales of \$27.4 million in this fiscal year resulted in an increase of \$8.9 million in the amount transferred to other State Funds. This year's transfers included almost \$8.0 million above the minimum transfers required in Lottery Statutes.

## **OTHER FINANCIAL INFORMATION**

The Lottery's total assets at June 30, 2003 were \$53.1 million. Assets consisted of cash held substantially by the State Treasurer of \$34.9 million, receivables from Lottery retailers for the sale of Lottery products of \$6.4 million, Scratchers ticket inventory of \$1.2 million, net investment in fixed assets of \$3.4 million and a deposit with MUSL of \$7.0 million.

Comparable figures at June 30, 2002 were \$43.6 million in total assets, including \$28.4 million in cash held by the State Treasurer, \$2.9 million in receivables from retailers, \$1.8 million in Scratchers ticket inventory, net investment in fixed assets of \$3.7 million, and MUSL deposit of \$6.7 million.

Total liabilities at June 30, 2003 were \$43.0 million consisting of \$4.0 million in accounts payable and accrued expenses, prize liabilities of \$26.8 million, and amounts due to other State Funds of \$12.3 million. All of the Lottery's liabilities were current liabilities.

The Lottery's total liabilities at June 30, 2002 were \$34.1 million which consisted of \$2.5 million of accounts payable and accrued expenses, prize liabilities of \$21.1 million and amounts due to other State Funds of \$10.5 million. All liabilities were current liabilities.

Total net assets at June 30, 2003 were \$10.0 million, an increase of \$0.6 million or 6.1% over total net assets at June 30, 2002. \$6.6 million of the Lottery's total net assets are unrestricted.

## **BUDGETARY HIGHLIGHTS**

The Lottery's budget is set by the legislative appropriations process on a biennial basis. The budgets for Fiscal Years 2003 and 2004 were set in the regular legislative session of 2002. The Lottery's budget for Fiscal Year 2003 was amended by Laws 2002, Chapter 327, to include a mandatory transfer to the State General Fund of \$3.5 million. The Lottery's appropriation for sales related expenditures is based on approved percentages of projected revenues and is allowed to increase for these items without a supplemental appropriations request if actual revenues exceed projected revenues. The appropriation does not include an amount for prizes because Lottery statutes set this amount at "not less than fifty percent of the total annual revenues accruing from the sale of Lottery tickets or shares".

The Lottery's appropriation was \$48.7 million at the beginning of the year and increased to \$51.9 million as actual revenues exceeded projections.

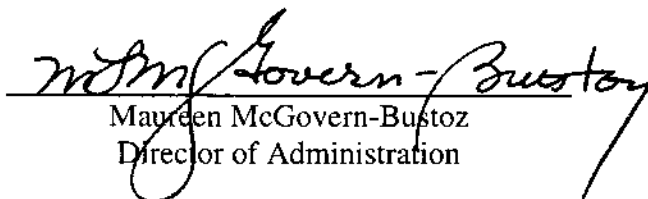
### **CONTACTING THE LOTTERY'S FINANCIAL MANAGEMENT**

This management's discussion and analysis (MD&A) is designed to provide Arizona citizens, Arizona government officials, our players, retailers and other interested parties with an overview of the Lottery's financial activity for Fiscal Year 2003 and to demonstrate the Lottery's accountability for the money it received from the sale of Lottery products.

If you have questions about the MD&A or need additional information, contact the Arizona Lottery's Director of Administration, 4740 East University, Phoenix, Arizona 85034.



Kathleen S. Pushor  
Executive Director



Maureen McGovern-Bustoz  
Director of Administration

**ARIZONA STATE LOTTERY,  
A COMPONENT UNIT OF THE STATE OF ARIZONA  
PROPRIETARY FUND—ENTERPRISE FUND**

**STATEMENT OF NET ASSETS  
JUNE 30, 2003  
(With comparative totals for June 30, 2002)**

| <b>ASSETS</b>  | <b>2003</b>          | <b>2002</b>         |
|--|----------------------|---------------------|
| <b>CURRENT ASSETS:</b>   |                      |                     |
| Cash, substantially all held by the State Treasurer  | \$ 34,937,465        | \$ 28,378,720       |
| Accounts receivable—net of allowance for doubtful<br>accounts of \$200,000 and \$300,000 in 2003<br>and 2002, respectively | 6,429,314            | 2,933,513           |
| Scratch ticket inventory   | <u>1,248,381</u>     | <u>1,851,721</u>    |
| Total current assets   | <u>42,615,160</u>    | <u>33,163,954</u>   |
| <b>CAPITAL ASSETS:</b>   |                      |                     |
| Land   | 937,830              | 937,830             |
| Land improvements  | 330,865              | 330,865             |
| Buildings  | 3,158,251            | 3,158,251           |
| Furniture, fixtures and equipment  | 3,756,564            | 3,763,948           |
| Less accumulated depreciation  | <u>(4,746,813)</u>   | <u>(4,485,688)</u>  |
| Total capital assets   | <u>3,436,697</u>     | <u>3,705,206</u>    |
| OTHER ASSETS—Deposit, Powerball  | <u>7,023,423</u>     | <u>6,710,016</u>    |
| <b>TOTAL ASSETS</b>  | <u>53,075,280</u>    | <u>43,579,176</u>   |
| <b>LIABILITIES</b>   |                      |                     |
| <b>CURRENT LIABILITIES:</b>  |                      |                     |
| Accounts payable and accrued expenses  | 3,987,746            | 2,540,647           |
| Prize liability  | 26,775,671           | 21,123,421          |
| Due to other state funds   | <u>12,282,446</u>    | <u>10,466,618</u>   |
| Total current liabilities  | <u>43,045,863</u>    | <u>34,130,686</u>   |
| <b>TOTAL LIABILITIES</b>   | <u>43,045,863</u>    | <u>34,130,686</u>   |
| <b>NET ASSETS</b>  |                      |                     |
| Invested in capital assets   | 3,436,697            | 3,705,206           |
| Unrestricted   | <u>6,592,720</u>     | <u>5,743,284</u>    |
| <b>TOTAL NET ASSETS</b>  | <u>\$ 10,029,417</u> | <u>\$ 9,448,490</u> |

See notes to financial statements.

**ARIZONA STATE LOTTERY,  
A COMPONENT UNIT OF THE STATE OF ARIZONA  
PROPRIETARY FUND—ENTERPRISE FUND**

**STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS  
YEAR ENDED JUNE 30, 2003**

**(With comparative totals for year ended June 30, 2002)**

|  | <b>2003</b>          | <b>2002</b>         |
|--|----------------------|---------------------|
| <b>OPERATING REVENUES:</b>                 |                      |                     |
| Ticket sales:                              |                      |                     |
| Scratchers                                 | \$ 148,383,301       | \$ 134,902,026      |
| Economic development                       | 10,855,654           | 8,521,242           |
| Powerball                                  | 112,325,881          | 96,172,642          |
| The Pick                                   | 34,345,784           | 39,265,013          |
| Fantasy 5                                  | 9,727,699            | 9,771,944           |
| Pick 3                                     | <u>6,628,694</u>     | <u>6,190,869</u>    |
| Total ticket sales                         | 322,267,013          | 294,823,736         |
| Other operating revenue                    | <u>304,461</u>       | <u>90,714</u>       |
| Total operating revenues                   | <u>322,571,474</u>   | <u>294,914,450</u>  |
| <b>OPERATING EXPENSES:</b>                 |                      |                     |
| Direct costs:                              |                      |                     |
| Prize expense                              | 173,956,018          | 160,205,615         |
| Retailer commissions and incentives        | 21,433,978           | 19,985,425          |
| On-line system expenses                    | 10,427,636           | 9,794,100           |
| Scratcher system and distribution expenses | 657,917              |                     |
| Tickets purchased                          | <u>3,181,390</u>     | <u>2,462,938</u>    |
| Total direct costs                         | 209,656,939          | 192,448,078         |
| Advertising and promotion                  | 8,531,211            | 7,402,277           |
| Wages and related expenses                 | 5,259,172            | 4,966,563           |
| Contract services                          | 693,699              | 515,485             |
| Depreciation                               | 268,509              | 305,432             |
| Administrative expenses                    | <u>2,266,275</u>     | <u>2,369,863</u>    |
| Total operating expenses                   | <u>226,675,805</u>   | <u>208,007,698</u>  |
| <b>OPERATING INCOME</b>                    | 95,895,669           | 86,906,752          |
| <b>NONOPERATING REVENUES</b>               | <u>396,083</u>       | <u>679,491</u>      |
| <b>INCOME BEFORE TRANSFERS</b>             | 96,291,752           | 87,586,243          |
| <b>TRANSFERS TO OTHER STATE FUNDS</b>      | <u>95,710,825</u>    | <u>86,812,820</u>   |
| <b>CHANGES IN NET ASSETS</b>               | 580,927              | 773,423             |
| <b>TOTAL NET ASSETS, BEGINNING OF YEAR</b> | <u>9,448,490</u>     | <u>8,675,067</u>    |
| <b>TOTAL NET ASSETS, END OF YEAR</b>       | <u>\$ 10,029,417</u> | <u>\$ 9,448,490</u> |

See notes to financial statements.

**ARIZONA STATE LOTTERY,  
A COMPONENT UNIT OF THE STATE OF ARIZONA  
PROPRIETARY FUND—ENTERPRISE FUND**

**STATEMENT OF CASH FLOWS**

**YEAR ENDED JUNE 30, 2003**

**(With comparative totals for year ended June 30, 2002)**

|  | <b>2003</b>                 | <b>2002</b>                 |
|--|-----------------------------|-----------------------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>   |                             |                             |
| Cash received from retailers—net of commission and incentives                                  | \$ 184,535,183              | \$ 171,419,191              |
| Cash from other sources  | 12,516,458                  | 62,616,410                  |
| Cash payments for prizes and related taxes   | (68,473,392)                | (118,311,330)               |
| Cash payments to suppliers of goods or services  | (23,291,009)                | (22,913,351)                |
| Cash payments to employees   | <u>(5,232,735)</u>          | <u>(5,084,488)</u>          |
| Net cash provided by operating activities  | <u>100,054,505</u>          | <u>87,726,432</u>           |
| <b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>  |                             |                             |
| Cash payments to beneficiaries per Lottery Statutes  | (93,894,997)                | (86,960,614)                |
| Cash repayments from beneficiaries   | <u>284,088</u>              | <u>                    </u> |
| Net cash used by noncapital financing activities   | <u>(93,610,909)</u>         | <u>(86,960,614)</u>         |
| <b>CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES—Payments for acquisition of capital assets</b> |                             |                             |
|  | <u>                    </u> | <u>(263,624)</u>            |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES—Receipts of interest</b>                               |                             |                             |
|  | <u>115,149</u>              | <u>290,019</u>              |
| <b>NET INCREASE IN CASH</b>  | <b>6,558,745</b>            | <b>792,213</b>              |
| <b>CASH, BEGINNING OF YEAR</b>   | <u><b>28,378,720</b></u>    | <u><b>27,586,507</b></u>    |
| <b>CASH, END OF YEAR</b>   | <u><b>\$ 34,937,465</b></u> | <u><b>\$ 28,378,720</b></u> |

(Continued)

**ARIZONA STATE LOTTERY,  
A COMPONENT UNIT OF THE STATE OF ARIZONA  
PROPRIETARY FUND—ENTERPRISE FUND**

**STATEMENT OF CASH FLOWS**

**YEAR ENDED JUNE 30, 2003**

**(With comparative totals for year ended June 30, 2002)**

|   | <b>2003</b>           | <b>2002</b>         |
|---|-----------------------|---------------------|
| RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:        |                       |                     |
| Operating income  | <u>\$ 95,895,669</u>  | <u>\$86,906,752</u> |
| Adjustments to reconcile operating income to net cash provided by operating activities: |                       |                     |
| Depreciation  | 268,509               | 305,432             |
| Loss on disposal of equipment   |                       | 2,451               |
| Changes in assets and liabilities:  |                       |                     |
| Accounts receivable and due from other State agencies                                   | (3,498,955)           | (103,230)           |
| Ticket inventory  | 603,340               | (977,630)           |
| Deposit—Powerball   | (313,407)             | 340,991             |
| Accounts payable and accrued expenses   | 1,447,099             | (278,079)           |
| Prizes and withholdings payable   | <u>5,652,250</u>      | <u>1,529,745</u>    |
| Total adjustments   | <u>4,158,836</u>      | <u>819,680</u>      |
| NET CASH PROVIDED BY OPERATING ACTIVITIES   | <u>\$ 100,054,505</u> | <u>\$87,726,432</u> |

See notes to financial statements.

(Concluded)

# ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA

## NOTES TO FINANCIAL STATEMENTS YEAR ENDED JUNE 30, 2003

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### 1. DESCRIPTION OF OPERATIONS

The Arizona State Lottery (the "Lottery") was created by enactment of Title 5, Chapter 5 to the Arizona Revised Statutes, which was an initiative measure approved by the voters of the State of Arizona in 1980. The Lottery commenced operations in 1981. The Lottery is a component unit of the State of Arizona (the "State"). The accompanying financial statements present information as to the transactions of the Lottery.

For the period July 1, 2002 through June 30, 2003, the Lottery held 61 instant games (games 257, 284, 298, 300, 302, 306, 309-310, 316-318, 320, 322-356, 358-359, 362-370 and 373-375), five of which were Economic Development (games 284, 298, 306, 335 and 342). During 2003, the Lottery continued the "Pick 3," "Fantasy 5," "The Pick," and "Powerball" on-line games. As required, the Lottery has a deposit with "Powerball," a multistate on-line lottery game, of \$7,023,423.

### 2. SIGNIFICANT ACCOUNTING POLICIES

The Lottery prepares its financial statements in accordance with accounting principles generally accepted in the United States of America.

**State Lottery Fund**—The State Lottery Fund, which is an Enterprise Fund of the State of Arizona, accounts for revenues received from the sale of lottery tickets and the receipt of license fees. The fund is operated in a manner similar to a private business enterprise where the governing body has decided that periodic determination of revenues earned, expenses incurred and net income is appropriate for capital maintenance, management control, accountability or other purposes. Activities accounted for in the proprietary fund follow all applicable GASB pronouncements as well as applicable Financial Accounting Standards Board pronouncements issued on or before November 30, 1989. The State Lottery Fund accounts for prize payments, operational expenses, including consulting, promotional and advertising expenses, and transfers of monies to other State funds. Receipts from each type of lottery game are to be allocated as follows:

- Not less than 50% of the total annual revenue from lottery ticket sales is apportioned for the payment of prizes to the holders of winning tickets for the period July 1, 2002 to June 30, 2003.
- During the period of July 1, 2002 to June 30, 2003, not less than 29% of receipts for "Fantasy 5," "Pick 3," and "The Pick," not less than 31.6% of receipts for "Powerball," and not less than 21.5% of receipts for instant games must be apportioned for transfer to a designated State fund.
- Expenditures related to promotional or advertising services are restricted to not more than 4.0% of the total annual gross revenues of the Lottery. Legislative appropriation further restricted advertising expenditures to 2.7% of the gross revenues during fiscal years 2003 and 2002. All other receipts can be used by the Lottery for operations or transferred to other State funds.



In addition, State statute requires that 30% of all unclaimed prizes to be transferred to the Court Appointed Special Advocate Account, a fund within the State’s General Fund.

***Ticket Sales and Revenue Recognition***—Revenue is recognized and the related direct expenses of ticket sales are accrued based upon the known relationship of the amount of ticket sales to the amount of prizes for each game. This method of measuring revenue is necessary in order to properly match revenues and expenses.

***Property and equipment*** of the State Lottery Fund, which consists principally of buildings, land, land improvements, and office furniture and equipment are stated at historical cost. Expenditures for normal repairs and maintenance are charged to operations as incurred, whereas expenditures for major renewals, replacements and betterments are capitalized and depreciated. Depreciation is provided for as follows:

|  | <b>Method</b> | <b>Estimated Useful Life</b> |
|--|---------------|------------------------------|
| Buildings                                  | Straight-line | 40 years                     |
| Land improvements                          | Straight-line | 20 years                     |
| Furniture, fixtures and computer equipment | Straight-line | 5-7 years                    |

***Investment income*** from all investments is recognized in the State Lottery Fund. An amount equal to the calculated amount of earnings on the State Lottery Prize Fund cash balances is transferred to the Prize Fund.

***Ticket inventory*** is stated at cost, which represents the amount incurred by the Lottery for purchasing the tickets.

***Cash***—Substantially all the Lottery’s cash is held by the State Treasurer for pooled investment purposes. Statutes require the State Treasurer to invest these pooled funds in obligations of the U.S. government and are recorded at fair value.

***Compensated Absences***—Vacation leave vests with the employee as it is earned. Employees may carry forward only the amount of vacation benefits equal to the maximum allowable accumulated credits for the preceding calendar year. Accordingly, at June 30, 2003, the State Lottery Fund’s accounts payable balance includes an accrual of vacation pay and related benefits of approximately \$396,500. Upon termination or retirement, an employee will be compensated for accumulated leave up to a maximum of 240 hours, dependent upon accumulated time and the individual’s benefits associated with their rank as defined by State personnel rule #R2-5-403. Payment will be based on the individual’s rate of pay at termination or retirement. Upon death, the same benefits shall be paid to the employee’s beneficiary.

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

### 3. TRANSFERS AND STATUTORY REQUIREMENTS

The Lottery made the following transfers during the year ended June 30, 2003 as required by Arizona Revised Statutes (“ARS”) Section 5-505.

|   |                     |
|---|---------------------|
| Transfers to the State of Arizona:              |                     |
| County Assistance Fund                          | \$ 7,650,000        |
| Court Appointed Special Advocate Account        | 3,263,125           |
| General Fund                                    | 34,455,000          |
| Heritage Fund                                   | 18,614,900          |
| Local Transportation Assistance Fund            | 28,994,200          |
| Economic Development Commission Fund            | <u>2,733,600</u>    |
| Total transfers to other State of Arizona funds | <u>\$95,710,825</u> |

These transactions met the minimum percentage requirements imposed upon the Lottery by statute.

### 4. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2003 was as follows:

|                                    | <b>Beginning<br/>Balance</b> | <b>Increases</b>    | <b>Decreases</b> | <b>Ending<br/>Balance</b> |
|------------------------------------|------------------------------|---------------------|------------------|---------------------------|
| Capital assets:                    |                              |                     |                  |                           |
| Land                               | \$ 937,830                   | \$ -                | \$ -             | \$ 937,830                |
| Land improvements                  | 330,865                      |                     |                  | 330,865                   |
| Buildings                          | 3,158,251                    |                     |                  | 3,158,251                 |
| Furniture, fixtures and equipment  | <u>3,763,948</u>             |                     | <u>(7,384)</u>   | <u>3,756,564</u>          |
| Total capital assets               | <u>8,190,894</u>             |                     | <u>(7,384)</u>   | <u>8,183,510</u>          |
| Less accumulated depreciation for: |                              |                     |                  |                           |
| Land improvements                  | (247,180)                    | (16,544)            |                  | (263,724)                 |
| Buildings                          | (956,941)                    | (74,517)            |                  | (1,031,458)               |
| Furniture, fixtures and equipment  | <u>(3,281,567)</u>           | <u>(177,448)</u>    | <u>7,384</u>     | <u>(3,451,631)</u>        |
| Total accumulated depreciation     | <u>(4,485,688)</u>           | <u>(268,509)</u>    | <u>7,384</u>     | <u>(4,746,813)</u>        |
| Total capital assets—net           | <u>\$ 3,705,206</u>          | <u>\$ (268,509)</u> | <u>\$ -</u>      | <u>\$ 3,436,697</u>       |

### 5. PRIZE LIABILITY

Prize liability activity for the year ended June 30, 2003 was as follows:

|                 | <b>Beginning<br/>Balance</b> | <b>Increases</b>     | <b>Decreases</b>       | <b>Ending<br/>Balance</b> |
|-----------------|------------------------------|----------------------|------------------------|---------------------------|
| Prize liability | <u>\$21,123,421</u>          | <u>\$177,420,842</u> | <u>\$(171,768,592)</u> | <u>\$26,775,671</u>       |

## **6. COMMITMENTS**

The Lottery enters into various contracts for goods and services during the normal course of its business. All contacts and purchasing activity are subject to the Arizona State Procurement Code and the rules of the State Procurement Office. All contracts have incorporated into them the "Standard Terms and Conditions" as required by the State Procurement Office. These terms and conditions in all the contracts allow for cancellation for lack of funding in the current fiscal year or next fiscal year. The contract may also be terminated for the Lottery's convenience at any time with no penalty when it is in the best interest of the State.

Net rental expense for the years ended June 30, 2003 and 2002 was \$57,134.

Effective September 2, 1999, the Lottery entered into a five-year contract with G-Tech Services, Inc. for computer processing services. The base contract rate is 4.9854% of on-line sales and the Lottery has exercised an option to extend the contract through August 31, 2006.

## **7. CONTINGENCIES**

Annuities are purchased for all prizes over \$400,000 for which winners will receive the jackpot in annual installments for The Pick on-line game. These annuities are purchased from qualifying insurance companies which have the highest ratings from among A.M. Best Company, Standard & Poor's, Moody, Duff & Phelps, or Weiss. The Lottery remains contingently liable on all annuities. Aggregate future payments to prize winners on existing annuities totaled approximately \$271,821,000 at June 30, 2003. Approximately \$184,215,000 of the total aggregate future payments at June 30, 2003 relate to annuities purchased from five separate insurance companies, of which approximately \$81,431,000 relates to a single insurance company.

In 1994, an insurance company from which the Lottery purchased annuities during the period 1983 through 1989 was placed under State supervision. At June 30, 2003, remaining aggregate minimum future payments on such purchased annuities approximated \$8,186,000. In 1997, an insurance company from which the Lottery purchased annuities in 1986, was placed under State supervision. At June 30, 2003, remaining aggregate minimum future payments on such purchased annuities approximated \$1,566,000. As of December 10, 2003, both insurance companies were current in their required annuity payments. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the operations or financial position of the Lottery.

The Lottery is involved in various legal proceedings which arose in the normal course of business. Management of the Lottery does not believe that the ultimate resolution of these matters will have a material effect on the financial position, results of operations, or cash flows of the Lottery.

## **8. RETIREMENT PLAN**

Permanent, full-time employees of the Lottery are covered by the Arizona State Retirement Plan (the "Plan"), a retirement plan administered by the Arizona State Retirement System, which is a multiple-employer, cost-sharing pension plan. The Comprehensive Annual Financial Report of the Arizona State Retirement System can be obtained by accessing [www.asrs.state.az.us](http://www.asrs.state.az.us). The Plan was established by the State of Arizona to provide benefits for employees of the state and employees of participating political subdivisions and school districts. The Plan became effective on July 1, 1971. By actuarial computation, employee member contributions to the Plan were fixed at 2.00%, 2.00% and 2.17% of their compensation for the years ended June 30, 2003, 2002 and 2001, respectively, with the

contributions made through payroll deduction. Employee contributions vest immediately. Total contributions to the Plan for the years ended June 30, 2003, 2002 and 2001 by the Lottery's covered employees were \$85,146, \$78,337 and \$86,113, respectively.

Matching employer member contributions were actuarially determined and fixed at 2.00%, 2.00% and 2.17% of the compensation of all employee members for the years ended June 30, 2003, 2002 and 2001, respectively. Total matching contributions to the Plan for the years ended June 30, 2003, 2002 and 2001 by the Lottery were \$85,146, \$78,337 and \$86,113, respectively. In the event the Plan's actuary determines that additional contributions are needed in order to amortize an unfunded accrued liability, every employer member will be required to contribute the revised contribution percentage that is set by the Plan.

All full-time employees of the Lottery are required to become members of the Plan. The Lottery's total payroll for employees covered by this Plan for the years ended June 30, 2003, 2002 and 2001 was \$4,288,181, \$4,099,597 and \$4,119,380, respectively. Contributions to the Plan by the Lottery for its covered employees become fully vested immediately after membership in the Plan. All required employer contributions were made to the Plan within 30 days after June 30, 2003.

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**ARIZONA STATE LOTTERY,  
A COMPONENT UNIT OF THE STATE OF ARIZONA**

**SUPPLEMENTAL SCHEDULE OF GROSS PROFIT BY GAME  
FOR GAMES EXPIRING DURING THE  
YEAR ENDED JUNE 30, 2003**

|                       | <u>Game 190</u> |          | <u>Game 225</u> |          | <u>Game 240</u> |          |
|-----------------------|-----------------|----------|-----------------|----------|-----------------|----------|
| TICKET SALES          | \$ 3,753,291    | 100.00 % | \$ 2,896,296    | 100.00 % | \$ 6,195,078    | 100.00 % |
| DIRECT EXPENSES:      |                 |          |                 |          |                 |          |
| Commissions           | 243,964         | 6.50 %   | 188,259         | 6.50 %   | 402,680         | 6.50 %   |
| Prizes—low tier       | 2,101,843       | 56.00 %  | 1,535,038       | 53.00 %  | 3,655,096       | 59.00 %  |
| Prizes—high tier      | 103,300         | 2.75 %   | 334,700         | 11.56 %  | 329,625         | 5.32 %   |
| Total prizes          | 2,205,143       | 58.75 %  | 1,869,738       | 64.56 %  | 3,984,721       | 64.32 %  |
| Ticket purchases      | 88,641          | 2.36 %   | 70,259          | 2.43 %   | 105,616         | 1.70 %   |
| Advertising           | 265             | 0.01 %   | 106,876         | 3.68 %   | 85,756          | 1.39 %   |
| Total direct expenses | 2,538,013       | 67.62 %  | 2,235,132       | 77.17 %  | 4,578,773       | 73.91 %  |
| GROSS PROFIT BY GAME  | \$ 1,215,278    | 32.38 %  | \$ 661,164      | 22.83 %  | \$ 1,616,305    | 26.09 %  |
|                       |                 |          |                 |          |                 |          |
|                       | <u>Game 248</u> |          | <u>Game 252</u> |          | <u>Game 254</u> |          |
| TICKET SALES          | \$ 1,799,804    | 100.00 % | \$ 1,921,624    | 100.00 % | \$ 1,399,653    | 100.00 % |
| DIRECT EXPENSES:      |                 |          |                 |          |                 |          |
| Commissions           | 116,988         | 6.50 %   | 124,906         | 6.50 %   | 90,978          | 6.50 %   |
| Prizes—low tier       | 881,904         | 49.00 %  | 960,812         | 50.00 %  | 615,848         | 44.00 %  |
| Prizes—high tier      | 161,551         | 8.98 %   | 197,312         | 10.27 %  | 211,600         | 15.12 %  |
| Total prizes          | 1,043,455       | 57.98 %  | 1,158,124       | 60.27 %  | 827,448         | 59.12 %  |
| Ticket purchases      | 38,823          | 2.15 %   | 38,551          | 2.00 %   | 38,762          | 2.77 %   |
| Advertising           |                 |          |                 |          |                 |          |
| Total direct expenses | 1,199,266       | 66.63 %  | 1,321,581       | 68.77 %  | 957,188         | 68.39 %  |
| GROSS PROFIT BY GAME  | \$ 600,538      | 33.37 %  | \$ 600,043      | 31.23 %  | \$ 442,465      | 31.61 %  |
|                       |                 |          |                 |          |                 |          |
|                       | <u>Game 255</u> |          | <u>Game 258</u> |          | <u>Game 261</u> |          |
| TICKET SALES          | \$ 9,329,278    | 100.00 % | \$ 40,520,104   | 100.00 % | \$ 1,933,056    | 100.00 % |
| DIRECT EXPENSES:      |                 |          |                 |          |                 |          |
| Commissions           | 606,404         | 6.50 %   | 2,633,806       | 6.50 %   | 125,649         | 6.50 %   |
| Prizes—low tier       | 3,977,867       | 42.64 %  | 21,723,459      | 53.61 %  | 1,101,841       | 57.00 %  |
| Prizes—high tier      | 1,305,501       | 13.99 %  | 1,729,200       | 4.27 %   | 49,900          | 2.58 %   |
| Total prizes          | 5,283,368       | 56.63 %  | 23,452,659      | 57.88 %  | 1,151,741       | 59.58 %  |
| Ticket purchases      | 136,631         | 1.46 %   | 617,123         | 1.52 %   | 38,828          | 2.01 %   |
| Advertising           | 555,811         | 5.96 %   |                 |          |                 |          |
| Total direct expenses | 6,582,214       | 70.55 %  | 26,703,588      | 65.90 %  | 1,316,218       | 68.09 %  |
| GROSS PROFIT BY GAME  | \$ 2,747,064    | 29.45 %  | \$ 13,816,516   | 34.10 %  | \$ 616,838      | 31.91 %  |

(Continued)

**ARIZONA STATE LOTTERY,  
A COMPONENT UNIT OF THE STATE OF ARIZONA**

**SUPPLEMENTAL SCHEDULE OF GROSS PROFIT BY GAME  
FOR GAMES EXPIRING DURING THE  
YEAR ENDED JUNE 30, 2003**

|                       | <u>Game 262</u> |          | <u>Game 265</u> |          | <u>Game 266</u> |          |
|-----------------------|-----------------|----------|-----------------|----------|-----------------|----------|
| TICKET SALES          | \$ 2,018,704    | 100.00 % | \$ 1,605,177    | 100.00 % | \$ 1,236,730    | 100.00 % |
| DIRECT EXPENSES:      |                 |          |                 |          |                 |          |
| Commissions           | 131,216         | 6.50 %   | 104,337         | 6.50 %   | 80,388          | 6.50 %   |
| Prizes—low tier       | 1,049,726       | 52.00 %  | 674,174         | 42.00 %  | 556,529         | 45.00 %  |
| Prizes—high tier      | 132,350         | 6.56 %   | 240,501         | 14.98 %  | 152,950         | 12.37 %  |
| Total prizes          | 1,182,076       | 58.56 %  | 914,675         | 56.98 %  | 709,479         | 57.37 %  |
| Ticket purchases      | 38,829          | 1.92 %   | 38,829          | 2.42 %   | 38,827          | 3.14 %   |
| Advertising           |                 |          |                 |          |                 |          |
| Total direct expenses | 1,352,121       | 66.98 %  | 1,057,841       | 65.90 %  | 828,694         | 67.01 %  |
| GROSS PROFIT BY GAME  | \$ 666,583      | 33.02 %  | \$ 547,336      | 34.10 %  | \$ 408,036      | 32.99 %  |
|                       |                 |          |                 |          |                 |          |
|                       | <u>Game 272</u> |          | <u>Game 273</u> |          | <u>Game 284</u> |          |
| TICKET SALES          | \$ 2,837,810    | 100.00 % | \$ 3,955,048    | 100.00 % | \$ 4,236,898    | 100.00 % |
| DIRECT EXPENSES:      |                 |          |                 |          |                 |          |
| Commissions           | 184,458         | 6.50 %   | 257,078         | 6.50 %   | 275,399         | 6.50 %   |
| Prizes—low tier       | 1,530,796       | 53.94 %  | 1,847,103       | 46.70 %  | 2,118,449       | 50.00 %  |
| Prizes—high tier      | 208,100         | 7.33 %   | 506,360         | 12.80 %  | 547,160         | 12.91 %  |
| Total prizes          | 1,738,896       | 61.28 %  | 2,353,463       | 59.51 %  | 2,665,609       | 62.91 %  |
| Ticket purchases      | 63,897          | 2.25 %   | 90,059          | 2.28 %   | 85,632          | 2.02 %   |
| Advertising           |                 |          | 2,049           | 0.04 %   | 133,817         | 3.16 %   |
| Total direct expenses | 1,987,251       | 70.03 %  | 2,702,649       | 68.33 %  | 3,160,457       | 74.59 %  |
| GROSS PROFIT BY GAME  | \$ 850,559      | 29.97 %  | \$ 1,252,399    | 31.67 %  | \$ 1,076,441    | 25.41 %  |
|                       |                 |          |                 |          |                 |          |
|                       | <u>Game 286</u> |          | <u>Game 292</u> |          | <u>Game 293</u> |          |
| TICKET SALES          | \$ 1,649,785    | 100.00 % | \$ 1,383,591    | 100.00 % | \$ 1,509,563    | 100.00 % |
| DIRECT EXPENSES:      |                 |          |                 |          |                 |          |
| Commissions           | 107,237         | 6.50 %   | 89,935          | 6.50 %   | 98,122          | 6.50 %   |
| Prizes—low tier       | 857,889         | 52.00 %  | 733,303         | 53.00 %  | 724,591         | 48.00 %  |
| Prizes—high tier      | 70,100          | 4.25 %   | 27,625          | 2.00 %   | 138,701         | 9.19 %   |
| Total prizes          | 927,989         | 56.25 %  | 760,928         | 55.00 %  | 863,292         | 57.19 %  |
| Ticket purchases      | 38,572          | 2.34 %   | 38,579          | 2.79 %   | 41,636          | 2.76 %   |
| Advertising           |                 |          | 47,228          | 3.41 %   |                 |          |
| Total direct expenses | 1,073,798       | 65.09 %  | 936,670         | 67.70 %  | 1,003,050       | 66.45 %  |
| GROSS PROFIT BY GAME  | \$ 575,987      | 34.91 %  | \$ 446,921      | 32.30 %  | \$ 506,513      | 33.55 %  |

(Continued)

**ARIZONA STATE LOTTERY,  
A COMPONENT UNIT OF THE STATE OF ARIZONA**

**SUPPLEMENTAL SCHEDULE OF GROSS PROFIT BY GAME  
FOR GAMES EXPIRING DURING THE  
YEAR ENDED JUNE 30, 2003**

|                       | <u>Game 296</u>             |          | <u>Game 298</u>             |          | <u>Game 299</u>             |          |
|-----------------------|-----------------------------|----------|-----------------------------|----------|-----------------------------|----------|
| TICKET SALES          | \$ <u>2,710,622</u>         | 100.00 % | \$ <u>5,171,764</u>         | 100.00 % | \$ <u>3,082,176</u>         | 100.00 % |
| DIRECT EXPENSES:      |                             |          |                             |          |                             |          |
| Commissions           | <u>176,191</u>              | 6.50 %   | <u>336,165</u>              | 6.50 %   | <u>200,343</u>              | 6.50 %   |
| Prizes—low tier       | 1,219,780                   | 45.00 %  | 2,611,741                   | 50.50 %  | 1,386,979                   | 45.00 %  |
| Prizes—high tier      | <u>385,440</u>              | 14.22 %  | <u>624,400</u>              | 12.07 %  | <u>360,570</u>              | 11.70 %  |
| Total prizes          | 1,605,220                   | 59.22 %  | 3,236,141                   | 62.57 %  | 1,747,549                   | 56.70 %  |
| Ticket purchases      | 53,616                      | 1.98 %   | 114,569                     | 2.22 %   | 85,128                      | 2.76 %   |
| Advertising           | <u>                    </u> |          | <u>25,286</u>               | 0.49 %   | <u>867,155</u>              | 28.14 %  |
| Total direct expenses | <u>1,835,027</u>            | 67.70 %  | <u>3,712,161</u>            | 71.78 %  | <u>2,900,175</u>            | 94.10 %  |
| GROSS PROFIT BY GAME  | \$ <u>875,595</u>           | 32.30 %  | \$ <u>1,459,603</u>         | 28.22 %  | \$ <u>182,001</u>           | 5.90 %   |
|                       |                             |          |                             |          |                             |          |
|                       | <u>Game 301</u>             |          | <u>Game 302</u>             |          | <u>Game 303</u>             |          |
| TICKET SALES          | \$ <u>1,656,338</u>         | 100.00 % | \$ <u>1,896,014</u>         | 100.00 % | \$ <u>1,217,039</u>         | 100.00 % |
| DIRECT EXPENSES:      |                             |          |                             |          |                             |          |
| Commissions           | <u>107,662</u>              | 6.50 %   | <u>123,242</u>              | 6.50 %   | <u>79,107</u>               | 6.50 %   |
| Prizes—low tier       | 828,169                     | 50.00 %  | 872,167                     | 46.00 %  | 596,349                     | 49.00 %  |
| Prizes—high tier      | <u>116,880</u>              | 7.06 %   | <u>197,100</u>              | 10.40 %  | <u>93,180</u>               | 7.66 %   |
| Total prizes          | 945,049                     | 57.06 %  | 1,069,267                   | 56.40 %  | 689,529                     | 56.66 %  |
| Ticket purchases      | 42,950                      | 2.59 %   | 43,023                      | 2.27 %   | 31,183                      | 2.56 %   |
| Advertising           | <u>                    </u> |          | <u>                    </u> |          | <u>                    </u> |          |
| Total direct expenses | <u>1,095,661</u>            | 66.15 %  | <u>1,235,532</u>            | 65.16 %  | <u>799,819</u>              | 65.72 %  |
| GROSS PROFIT BY GAME  | \$ <u>560,677</u>           | 33.85 %  | \$ <u>660,482</u>           | 34.84 %  | \$ <u>417,220</u>           | 34.28 %  |
|                       |                             |          |                             |          |                             |          |
|                       | <u>Game 304</u>             |          | <u>Game 305</u>             |          | <u>Game 306</u>             |          |
| TICKET SALES          | \$ <u>1,082,491</u>         | 100.00 % | \$ <u>1,663,491</u>         | 100.00 % | \$ <u>2,455,496</u>         | 100.00 % |
| DIRECT EXPENSES:      |                             |          |                             |          |                             |          |
| Commissions           | <u>70,362</u>               | 6.50 %   | <u>108,127</u>              | 6.50 %   | <u>159,607</u>              | 6.50 %   |
| Prizes—low tier       | 541,246                     | 50.00 %  | 848,380                     | 51.00 %  | 1,178,638                   | 48.00 %  |
| Prizes—high tier      | <u>69,000</u>               | 6.37 %   | <u>77,650</u>               | 4.67 %   | <u>346,400</u>              | 14.11 %  |
| Total prizes          | 610,246                     | 56.37 %  | 926,030                     | 55.67 %  | 1,525,038                   | 62.11 %  |
| Ticket purchases      | 31,176                      | 2.88 %   | 43,991                      | 2.64 %   | 79,380                      | 3.23 %   |
| Advertising           | <u>                    </u> |          | <u>                    </u> |          | <u>25,322</u>               | 1.03 %   |
| Total direct expenses | <u>711,784</u>              | 65.75 %  | <u>1,078,148</u>            | 64.81 %  | <u>1,789,347</u>            | 72.87 %  |
| GROSS PROFIT BY GAME  | \$ <u>370,707</u>           | 34.25 %  | \$ <u>585,343</u>           | 35.19 %  | \$ <u>666,149</u>           | 27.13 %  |

(Continued)

**ARIZONA STATE LOTTERY,  
A COMPONENT UNIT OF THE STATE OF ARIZONA**

**SUPPLEMENTAL SCHEDULE OF GROSS PROFIT BY GAME  
FOR GAMES EXPIRING DURING THE  
YEAR ENDED JUNE 30, 2003**

|                       | <u>Game 307</u>             |          | <u>Game 308</u>             |          | <u>Game 309</u>             |          |
|-----------------------|-----------------------------|----------|-----------------------------|----------|-----------------------------|----------|
| TICKET SALES          | \$ 4,729,444                | 100.00 % | \$ 1,898,427                | 100.00 % | \$ 7,807,130                | 100.00 % |
| DIRECT EXPENSES:      |                             |          |                             |          |                             |          |
| Commissions           | <u>307,414</u>              | 6.50 %   | <u>123,400</u>              | 6.50 %   | <u>507,464</u>              | 6.50 %   |
| Prizes—low tier       | 2,364,722                   | 50.00 %  | 930,230                     | 49.00 %  | 3,903,566                   | 50.00 %  |
| Prizes—high tier      | <u>574,750</u>              | 12.15 %  | <u>141,869</u>              | 7.47 %   | <u>1,062,550</u>            | 13.61 %  |
| Total prizes          | 2,939,472                   | 62.15 %  | 1,072,099                   | 56.47 %  | 4,966,116                   | 63.61 %  |
| Ticket purchases      | 62,596                      | 1.33 %   | 44,005                      | 2.32 %   | 241,568                     | 3.09 %   |
| Advertising           | <u>                    </u> |          | <u>                    </u> |          | <u>395,519</u>              | 5.07 %   |
| Total direct expenses | <u>3,309,482</u>            | 69.98 %  | <u>1,239,504</u>            | 65.29 %  | <u>6,110,667</u>            | 78.27 %  |
| GROSS PROFIT BY GAME  | <u>\$ 1,419,962</u>         | 30.02 %  | <u>\$ 658,923</u>           | 34.71 %  | <u>\$ 1,696,463</u>         | 21.73 %  |
|                       |                             |          |                             |          |                             |          |
|                       | <u>Game 310</u>             |          | <u>Game 311</u>             |          | <u>Game 312</u>             |          |
| TICKET SALES          | \$ 4,311,794                | 100.00 % | \$ 1,137,148                | 100.00 % | \$ 1,617,943                | 100.00 % |
| DIRECT EXPENSES:      |                             |          |                             |          |                             |          |
| Commissions           | <u>280,267</u>              | 6.50 %   | <u>73,915</u>               | 6.50 %   | <u>105,167</u>              | 6.50 %   |
| Prizes—low tier       | 2,155,897                   | 50.00 %  | 568,574                     | 50.00 %  | 857,510                     | 53.00 %  |
| Prizes—high tier      | <u>516,752</u>              | 11.98 %  | <u>67,750</u>               | 5.96 %   | <u>69,675</u>               | 4.31 %   |
| Total prizes          | 2,672,649                   | 61.98 %  | 636,324                     | 55.96 %  | 927,185                     | 57.31 %  |
| Ticket purchases      | 77,333                      | 1.80 %   | 31,153                      | 2.74 %   | 38,434                      | 2.37 %   |
| Advertising           | <u>                    </u> |          | <u>                    </u> |          | <u>                    </u> |          |
| Total direct expenses | <u>3,030,249</u>            | 70.28 %  | <u>741,392</u>              | 65.20 %  | <u>1,070,786</u>            | 66.18 %  |
| GROSS PROFIT BY GAME  | <u>\$ 1,281,545</u>         | 29.72 %  | <u>\$ 395,756</u>           | 34.80 %  | <u>\$ 547,157</u>           | 33.82 %  |
|                       |                             |          |                             |          |                             |          |
|                       | <u>Game 313</u>             |          | <u>Game 314</u>             |          | <u>Game 315</u>             |          |
| TICKET SALES          | \$ 2,024,244                | 100.00 % | \$ 1,662,339                | 100.00 % | \$ 1,199,506                | 100.00 % |
| DIRECT EXPENSES:      |                             |          |                             |          |                             |          |
| Commissions           | <u>131,576</u>              | 6.50 %   | <u>108,052</u>              | 6.50 %   | <u>77,969</u>               | 6.50 %   |
| Prizes—low tier       | 951,395                     | 47.00 %  | 914,287                     | 55.00 %  | 623,743                     | 52.00 %  |
| Prizes—high tier      | <u>303,600</u>              | 15.00 %  | <u>38,150</u>               | 2.29 %   | <u>54,900</u>               | 4.58 %   |
| Total prizes          | 1,254,995                   | 62.00 %  | 952,437                     | 57.29 %  | 678,643                     | 56.58 %  |
| Ticket purchases      | 59,914                      | 2.96 %   | 38,352                      | 2.31 %   | 31,198                      | 2.60 %   |
| Advertising           | <u>73,171</u>               | 3.61 %   | <u>                    </u> |          | <u>                    </u> |          |
| Total direct expenses | <u>1,519,656</u>            | 75.07 %  | <u>1,098,841</u>            | 66.10 %  | <u>787,810</u>              | 65.68 %  |
| GROSS PROFIT BY GAME  | <u>\$ 504,588</u>           | 24.93 %  | <u>\$ 563,498</u>           | 33.90 %  | <u>\$ 411,696</u>           | 34.32 %  |

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**ARIZONA STATE LOTTERY,  
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**SUPPLEMENTAL SCHEDULE OF GROSS PROFIT BY GAME  
FOR GAMES EXPIRING DURING THE  
YEAR ENDED JUNE 30, 2003**

|                       | <u>Game 316</u> |          | <u>Game 318</u> |          | <u>Game 319</u> |          |
|-----------------------|-----------------|----------|-----------------|----------|-----------------|----------|
| TICKET SALES          | \$ 932,239      | 100.00 % | \$ 7,254,768    | 100.00 % | \$ 722,029      | 100.00 % |
| DIRECT EXPENSES:      |                 |          |                 |          |                 |          |
| Commissions           | 60,596          | 6.50 %   | 471,560         | 6.50 %   | 46,933          | 6.50 %   |
| Prizes—low tier       | 419,507         | 45.00 %  | 3,627,384       | 50.00 %  | 361,015         | 50.00 %  |
| Prizes—high tier      | 101,101         | 10.84 %  | 910,620         | 12.55 %  | 44,650          | 6.18 %   |
| Total prizes          | 520,608         | 55.84 %  | 4,538,004       | 62.55 %  | 405,665         | 56.18 %  |
| Ticket purchases      | 33,917          | 3.64 %   | 78,747          | 1.09 %   | 33,934          | 4.70 %   |
| Advertising           |                 |          |                 |          |                 |          |
| Total direct expenses | 615,121         | 65.98 %  | 5,088,311       | 70.14 %  | 486,532         | 67.38 %  |
| GROSS PROFIT BY GAME  | \$ 317,118      | 34.02 %  | \$ 2,166,457    | 29.86 %  | \$ 235,497      | 32.62 %  |
|                       |                 |          |                 |          |                 |          |
|                       | <u>Game 320</u> |          | <u>Game 321</u> |          | <u>Game 322</u> |          |
| TICKET SALES          | \$ 12,400,380   | 100.00 % | \$ 1,085,637    | 100.00 % | \$ 2,112,683    | 100.00 % |
| DIRECT EXPENSES:      |                 |          |                 |          |                 |          |
| Commissions           | 806,025         | 6.50 %   | 70,569          | 6.50 %   | 137,325         | 6.50 %   |
| Prizes—low tier       | 6,820,209       | 55.00 %  | 470,443         | 43.33 %  | 1,140,849       | 54.00 %  |
| Prizes—high tier      | 1,036,110       | 8.36 %   | 248,221         | 22.87 %  | 68,736          | 3.25 %   |
| Total prizes          | 7,856,319       | 63.36 %  | 718,664         | 66.20 %  | 1,209,585       | 57.25 %  |
| Ticket purchases      | 112,148         | 0.90 %   | 114,532         | 10.55 %  | 50,542          | 2.40 %   |
| Advertising           | 412,064         | 3.32 %   | 78,979          | 7.27 %   |                 |          |
| Total direct expenses | 9,186,556       | 74.08 %  | 982,744         | 90.52 %  | 1,397,452       | 66.15 %  |
| GROSS PROFIT BY GAME  | \$ 3,213,824    | 25.92 %  | \$ 102,893      | 9.48 %   | \$ 715,231      | 33.85 %  |
|                       |                 |          |                 |          |                 |          |
|                       | <u>Game 323</u> |          | <u>Game 324</u> |          | <u>Game 325</u> |          |
| TICKET SALES          | \$ 3,892,275    | 100.00 % | \$ 1,729,379    | 100.00 % | \$ 1,428,784    | 100.00 % |
| DIRECT EXPENSES:      |                 |          |                 |          |                 |          |
| Commissions           | 252,998         | 6.50 %   | 112,410         | 6.50 %   | 92,871          | 6.50 %   |
| Prizes—low tier       | 2,023,983       | 52.00 %  | 778,221         | 45.00 %  | 671,528         | 47.00 %  |
| Prizes—high tier      | 410,525         | 10.55 %  | 189,900         | 10.98 %  | 144,450         | 10.11 %  |
| Total prizes          | 2,434,508       | 62.55 %  | 968,121         | 55.98 %  | 815,978         | 57.11 %  |
| Ticket purchases      | 128,563         | 3.30 %   | 40,305          | 2.33 %   | 43,985          | 3.08 %   |
| Advertising           | 152             | .00 %    |                 |          |                 |          |
| Total direct expenses | 2,816,221       | 72.35 %  | 1,120,836       | 64.81 %  | 952,834         | 66.69 %  |
| GROSS PROFIT BY GAME  | \$ 1,076,054    | 27.65 %  | \$ 608,543      | 35.19 %  | \$ 475,950      | 33.31 %  |

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**ARIZONA STATE LOTTERY,  
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**SUPPLEMENTAL SCHEDULE OF GROSS PROFIT BY GAME  
FOR GAMES EXPIRING DURING THE  
YEAR ENDED JUNE 30, 2003**

|                       | <u>Game 326</u>     |          | <u>Game 329</u>     |          | <u>Game 330</u>     |          |
|-----------------------|---------------------|----------|---------------------|----------|---------------------|----------|
| TICKET SALES          | <u>\$ 1,129,128</u> | 100.00 % | <u>\$ 1,217,389</u> | 100.00 % | <u>\$ 1,198,075</u> | 100.00 % |
| DIRECT EXPENSES:      |                     |          |                     |          |                     |          |
| Commissions           | <u>73,393</u>       | 6.50 %   | <u>79,131</u>       | 6.50 %   | <u>77,875</u>       | 6.50 %   |
| Prizes—low tier       | 560,801             | 49.67 %  | 633,042             | 52.00 %  | 634,979             | 53.00 %  |
| Prizes—high tier      | <u>69,350</u>       | 6.14 %   | <u>47,900</u>       | 3.93 %   | <u>38,100</u>       | 3.18 %   |
| Total prizes          | 630,151             | 55.81 %  | 680,942             | 55.93 %  | 673,079             | 56.18 %  |
| Ticket purchases      | 39,202              | 3.47 %   | 34,096              | 2.81 %   | 33,901              | 2.83 %   |
| Advertising           | <u>          </u>   |          | <u>          </u>   |          | <u>          </u>   |          |
| Total direct expenses | <u>742,746</u>      | 65.78 %  | <u>794,169</u>      | 65.24 %  | <u>784,855</u>      | 65.51 %  |
| GROSS PROFIT BY GAME  | <u>\$ 386,382</u>   | 34.22 %  | <u>\$ 423,220</u>   | 34.76 %  | <u>\$ 413,220</u>   | 34.49 %  |

(Continued)

**ARIZONA STATE LOTTERY,  
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**SUPPLEMENTAL SCHEDULE OF GROSS PROFIT BY GAME  
FOR GAMES EXPIRING DURING THE  
YEAR ENDED JUNE 30, 2003**

|                       | <b>Pick Drawings</b>     |          | <b>Fantasy 5 Drawings</b> |          | <b>Powerball Drawings</b> |          |
|-----------------------|--------------------------|----------|---------------------------|----------|---------------------------|----------|
|                       | <b>(1/1/02-12/31/02)</b> |          | <b>(1/1/02-12/31/02)</b>  |          | <b>(1/1/02-12/31/02)</b>  |          |
| TICKET SALES          | \$ 17,387,335            | 100.00 % | \$ 4,830,482              | 100.00 % | \$ 64,936,916             | 100.00 % |
| DIRECT EXPENSES:      |                          |          |                           |          |                           |          |
| Commissions           | 1,130,164                | 6.50 %   | 313,969                   | 6.50 %   | 4,220,886                 | 6.50 %   |
| Total prizes          | 8,758,871                | 50.38 %  | 2,294,478                 | 47.50 %  | 32,468,458                | 50.00 %  |
| Advertising           | <u>346,556</u>           | 1.99 %   | <u>21,242</u>             | 0.44 %   | <u>288,151</u>            | 0.44 %   |
| Total direct expenses | <u>10,235,591</u>        | 58.87 %  | <u>2,629,689</u>          | 54.44 %  | <u>36,977,495</u>         | 56.94 %  |
| GROSS PROFIT BY GAME  | <u>\$ 7,151,744</u>      | 41.13 %  | <u>\$ 2,200,793</u>       | 45.56 %  | <u>\$ 27,959,421</u>      | 43.06 %  |

|                       | <b>Pick 3 Drawings</b>   |          |
|-----------------------|--------------------------|----------|
|                       | <b>(1/1/02-12/31/02)</b> |          |
| TICKET SALES          | \$ 3,170,130             | 100.00 % |
| DIRECT EXPENSES:      |                          |          |
| Commissions           | 206,050                  | 6.50 %   |
| Total prizes          | 1,585,065                | 50.00 %  |
| Advertising           | <u>341,152</u>           | 10.76 %  |
| Total direct expenses | <u>2,132,267</u>         | 67.26 %  |
| GROSS PROFIT BY GAME  | <u>\$ 1,037,863</u>      | 32.74 %  |

**NOTE:** After the announced completion of ticket sales for each game, customers have a 180-day period in which to redeem their winning tickets. The above gross profit information includes games in which the 180-day grace period expired during the fiscal year ended June 30, 2003.

(Concluded)