

**Report 20-4
April 2020**

Wisconsin Lottery

Fiscal Year 2018-19

STATE OF WISCONSIN



Legislative Audit Bureau ■

Wisconsin Lottery

Fiscal Year 2018-19

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Joe Chrisman
State Auditor

April 29, 2020

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator Cowles and Representative Kerkman:

As required by s. 13.94 (1) (em), Wis. Stats., we have completed a financial audit of the Wisconsin Lottery, which is administered by the Wisconsin Department of Revenue. We have provided an unmodified opinion on the Wisconsin Lottery's financial statements as of and for the years ended June 30, 2019, and June 30, 2018.

Wisconsin Lottery ticket sales increased from \$667.4 million in fiscal year (FY) 2017-18 to \$713.1 million in FY 2018-19, or by 6.9 percent. This increase is the result of increased instant ticket sales as well as increased Mega Millions ticket sales resulting from a large jackpot in FY 2018-19. As ticket sales increase, Wisconsin Lottery expenses also increase. Operating expenses increased from \$487.2 million in FY 2017-18 to \$520.8 million in FY 2018-19, or by 6.9 percent.

2017 Wisconsin Act 59, the 2017-19 Biennial Budget Act, created a general purpose revenue appropriation to pay basic commission to retailers. Under Act 59, the Wisconsin Lottery was provided with \$8.0 million in FY 2017-18 and \$40.0 million in FY 2018-19 to pay retailer compensation. This increased proceeds available for the Lottery and Gaming Tax Credit in FY 2018-19.

The Wisconsin Constitution requires that net proceeds from the Wisconsin Lottery be used exclusively for property tax relief for Wisconsin residents. During FY 2018-19, lottery proceeds used for property tax relief totaled \$234.9 million. In September 2019, the Wisconsin Department of Administration and the Legislature's Joint Committee on Finance authorized the use of \$271.2 million in lottery proceeds for property tax relief during FY 2019-20.

We appreciate the courtesy and cooperation extended to us by Department of Revenue staff in completing this audit.

Respectfully submitted,


Joe Chrisman
State Auditor

JC/ES/ss

Introduction ■

The Wisconsin Lottery began operations in September 1988 after Wisconsin voters adopted a constitutional amendment in 1987 that allowed the Legislature to create a state lottery with net proceeds to be distributed for property tax relief. Since 1995, the Department of Revenue has managed the Wisconsin Lottery. As required by s. 13.94 (1) (em), Wis. Stats., we have completed a financial audit of the Wisconsin Lottery and have provided an unmodified opinion on its financial statements as of and for the years ended June 30, 2019, and June 30, 2018. We reviewed ticket sales, operating expenses, balances related to Wisconsin Lottery's participation in the Multi-State Lottery Association, property tax relief funded by net proceeds available from the Wisconsin Lottery, and compliance with selected statutory provisions.

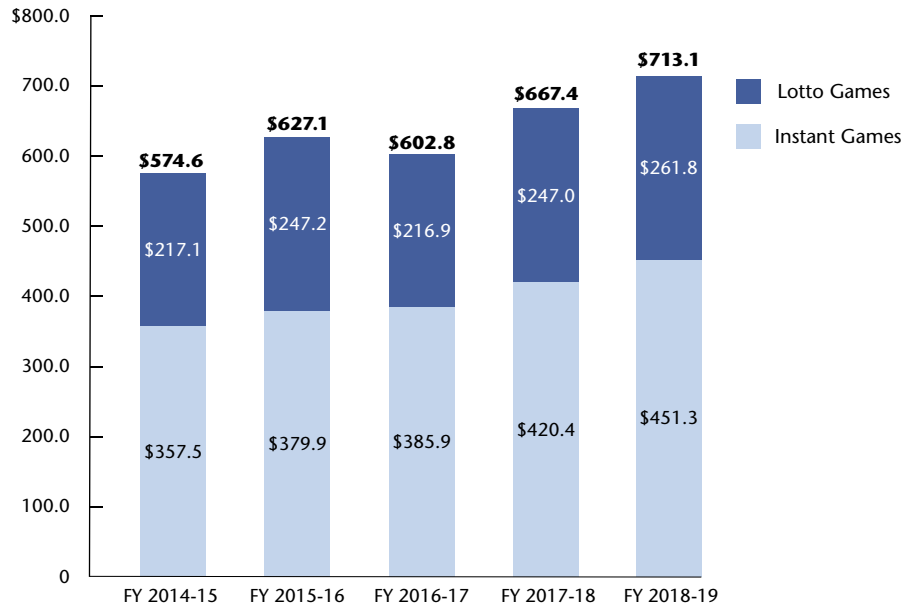
Wisconsin Lottery Ticket Sales

Ticket sales were \$713.1 million in FY 2018-19, which was an increase of 6.9 percent from FY 2017-18.

As shown in Figure 1, the Wisconsin Lottery's ticket sales increased from \$667.4 million in fiscal year (FY) 2017-18 to \$713.1 million in FY 2018-19, or by 6.9 percent. Sales of instant tickets, which are scratch-off and pull-tab tickets, increased by \$30.9 million, or by 7.4 percent. Lotto ticket sales increased \$14.8 million, or 6.0 percent. This increase is due to increased Mega Millions ticket sales resulting from a large jackpot in FY 2018-19.

Figure 1

Wisconsin Lottery Ticket Sales
(in millions)



Wisconsin Lottery Operating Expenses

Operating expenses were \$520.8 million in FY 2018-19, which was an increase of 6.9 percent from FY 2017-18.

The Wisconsin Lottery’s largest expenses are prizes and retailer compensation. Retailer compensation includes commissions and incentives that are paid to retailers to promote higher ticket sales. As shown in Table 1, the Wisconsin Lottery’s operating expenses increased from \$487.2 million in FY 2017-18 to \$520.8 million in FY 2018-19, or by 6.9 percent, primarily because expenses for lotto prizes increased as lotto ticket sales increased.

Game development and production expenses include donated prize expense, instant game ticket printing and delivery costs, and payments to IGT Global Solutions Corporation, which provides an integrated gaming computer system to account for instant and lotto game activity and to network with retailer terminals. Game development and production expenses generally fluctuate based on changes in ticket sales. The Wisconsin Lottery paid IGT Global Solutions Corporation approximately \$17.2 million in FY 2017-18 and \$18.3 million in FY 2018-19.

Table 1

Wisconsin Lottery Operating Expenses
(in millions)

Operating Expense Type	FY 2014-15	FY 2015-16	FY 2016-17	FY 2017-18	FY 2018-19
Prize Expenses	\$342.4	\$372.5	\$363.0	\$404.4	\$431.9
Retailer Compensation	39.6	43.5	41.3	46.5	49.7
Game Development and Production	17.8	19.4	18.9	19.7	20.2
Product Information	7.5	7.5	7.5	8.5	8.5
Other ¹	8.1	9.0	9.6	8.1	10.5
Total	\$415.4	\$451.9	\$440.3	\$487.2	\$520.8

¹ Includes staff salaries, fringe benefits, supplies and services, and depreciation.

In FY 2018-19, the Wisconsin Lottery spent \$8.5 million to provide information about its products.

The Wisconsin Constitution prohibits public funds or revenues derived from lottery operations from being spent for promotional advertising and requires that any advertising provide only information about the prize structures and chances of winning. The Wisconsin Lottery's annual product information budget, which is established through the State's biennial budget, was unchanged at \$8.5 million from FY 2017-18 to FY 2018-19.

Property Tax Relief

The Wisconsin Constitution requires that net proceeds from the Wisconsin Lottery be used exclusively for property tax relief. The proceeds are largely distributed to owners of primary residences in Wisconsin through the Lottery and Gaming Tax Credit. In FY 2018-19, \$234.9 million in lottery proceeds was used to fund the Lottery and Gaming Tax Credit, as shown in Table 2. The total amount distributed for property tax relief is authorized early in the fiscal year and is based on an estimate of proceeds that will be available for distribution. Property tax relief is lower in years where fewer proceeds are anticipated to be available for distribution and is higher in years where more proceeds are anticipated to be available for distribution. The Wisconsin Lottery was provided with general purpose revenue to pay retailer compensation in FY 2017-18 and FY 2018-19, which increased proceeds available for the Lottery and Gaming Tax Credit in FY 2018-19.

Table 2

Property Tax Relief¹
(in millions)

Fiscal Year	Lottery and Gaming Tax Credit
2014-15	\$166.4
2015-16	158.1
2016-17	183.3
2017-18 ²	170.3
2018-19 ²	234.9
Total	\$913.0

¹ Property tax relief is funded by net proceeds from the Wisconsin Lottery and by transfers from other gaming-related appropriations, including racing and charitable bingo operations.

² Under 2017 Wisconsin Act 59, the 2017-19 Biennial Budget Act, the Wisconsin Lottery was provided with general purpose revenue of \$8.0 million in FY 2017-18 and \$40.0 million in FY 2018-19 to pay retailer compensation.

From its inception in 1988 through FY 2018-19, the Wisconsin Lottery has provided \$4.6 billion in property tax relief.

In September 2019, the Department of Administration and the Legislature's Joint Committee on Finance authorized the use of \$271.2 million in Wisconsin Lottery proceeds for the FY 2019-20 Lottery and Gaming Tax Credit. From its inception in 1988 through FY 2018-19, the Wisconsin Lottery has provided \$4.6 billion in property tax relief.

Statutory Requirements

Wisconsin Statutes impose limitations on certain types of lottery expenses. For example, s. 25.75 (3) (a), Wis. Stats., requires that at least 50 percent of lottery ticket sales be used as prize payments to players. From FY 2014-15 through FY 2018-19, the Wisconsin Lottery's prize expenses exceeded 50 percent of ticket sales, in compliance with the statutory requirement, as shown in Table 3. Prize expenses fluctuated because of changes in the types of games offered and played. Lotto game prize payments, which are dependent on jackpot amounts and the frequency of winners claiming prizes, tend to fluctuate more than payments for instant games.

Table 3

Prize Expenses as a Percentage of Ticket Sales¹
(in millions)

Fiscal Year	Prize Expenses	Ticket Sales	Prize Expenses as a Percentage of Ticket Sales
2014-15	\$342.4	\$574.6	59.6%
2015-16	372.5	627.1	59.4
2016-17	363.0	602.8	60.2
2017-18	404.4	667.4	60.6
2018-19	431.9	713.1	60.6

¹ Section 25.75 (3) (a), Wis. Stats., requires that at least 50 percent of lottery sales be used as prize payments to players.

The Wisconsin Lottery's administrative expenses were below the statutory limit from FY 2014-15 through FY 2018-19.

Section 25.75 (3) (b), Wis. Stats., provides that certain administrative expenses may not exceed 10 percent of gross lottery revenues. Gross lottery revenues for this calculation are statutorily defined to consist of instant and lotto ticket sales and retailer fees. Statutory administrative expenses include most expenses and transfers, except prize payments; retailer compensation; transfers to property tax relief; and transfers to the Wisconsin Department of Justice for lottery-related law enforcement activities. As shown in Table 4, the Wisconsin Lottery's administrative expenses remained below the statutory limit from FY 2014-15 through FY 2018-19.

Table 4

Administrative Expenses as a Percentage of Lottery Revenues¹
(in millions)

Fiscal Year	Statutorily Defined Administrative Expenses	Lottery Revenues ²	Percentage of Lottery Revenues
2014-15	\$34.1	\$574.7	5.9%
2015-16	36.6	627.2	5.8
2016-17	36.7	602.8	6.1
2017-18	37.0	667.5	5.5
2018-19	40.2	713.2	5.6

¹ Section 25.75 (3) (b), Wis. Stats., provides that certain administrative expenses may not exceed 10 percent of gross lottery revenues.

² Lottery revenues include instant and lotto ticket sales and retailer fees.

In FY 2018-19, the Wisconsin Lottery spent \$42.7 million on basic commissions to retailers who sell lottery tickets.

Statutes establish maximum compensation rates for basic commissions and performance program payments to retailers who sell lottery tickets. Basic commission rates, as established in s. 565.10 (14) (b), Wis. Stats., are currently 5.5 percent of the retail price for lotto tickets and 6.25 percent for instant tickets. The Wisconsin Lottery spent \$42.7 million on basic commissions in FY 2018-19. Of this amount, \$40.0 million was funded by a general purpose revenue appropriation that was created by 2017 Wisconsin Act 59. Wisconsin Lottery reports this amount as a transfer in from the General Fund on its financial statements.

In FY 2018-19, the Wisconsin Lottery spent \$6.9 million in Retailer Performance Program payments.

In addition, s. 565.02 (4) (g), Wis. Stats., authorizes a performance program to provide incentives to retailers and requires that payments not exceed 1.0 percent of gross revenues from the sale of lottery tickets. Table 5 shows the Wisconsin Lottery's performance program payments did not exceed 1.0 percent of gross revenues from the sale of lottery tickets from FY 2014-15 through FY 2018-19. In FY 2018-19, the Wisconsin Lottery spent \$6.9 million on Retailer Performance Program payments.

Table 5

Retailer Performance Program Payments as a Percentage of Ticket Sales¹
(in millions)

Fiscal Year	Retailer Performance Program Payments	Ticket Sales	Payments as a Percentage of Ticket Sales
2014-15	\$5.1	\$574.6	0.9%
2015-16	6.0	627.1	1.0
2016-17	5.0	602.8	0.8
2017-18	6.5	667.4	1.0
2018-19	6.9	713.1	1.0

¹ Section 565.02 (4) (g), Wis. Stats., authorizes a performance program to provide incentives to retailers and requires that payments not exceed 1.0 percent of gross revenues from the sale of lottery tickets.

The Retailer Performance Program includes sales incentives for retailers that increase ticket sales, a bonus for retailers that sell winning tickets, and short-term incentives for retailers that increase ticket sales of certain games for specific time periods. During FY 2018-19, performance payments for the sales incentives for increasing ticket sales accounted for 74.7 percent of the total incentive payments, winning ticket bonuses accounted for 19.4 percent, and short-term incentives accounted for 5.9 percent.

There were six short-term incentives during FY 2018-19. Total payments for each of the six short-term incentives ranged from \$1,560 to \$174,065, and the number of retailers who participated in each of these short-term incentives ranged from 298 retailers to all retailers, which totaled approximately 3,600.

In addition to limitations on certain types of lottery expenses, Wisconsin Statutes prescribe various transfers to and from the Wisconsin Lottery. Unencumbered balances and related interest for the following appropriations are to be transferred to the Wisconsin Lottery at the end of the fiscal year:

- the appropriation for the Department of Health Services' compulsive gambling awareness campaigns, under s. 20.435 (5) (kg), Wis. Stats.;
- the appropriation for the Department of Justice's gaming law enforcement, under s. 20.455 (2) (g), Wis. Stats.; and
- the appropriations for general operations of the Department of Administration's Division of Gaming related to racing and bingo, under s. 20.505 (8) (g) and (jm), Wis. Stats.

The Wisconsin Lottery received \$8,886 from these transfers in FY 2017-18. No unencumbered balances were available to be transferred to the Wisconsin Lottery in FY 2018-19.

In addition, the Wisconsin Lottery is required to transfer amounts to the General Fund related to annual appropriation bonds issued by the State of Wisconsin to pay off certain unfunded liabilities in the pension and other employee benefit programs. The Wisconsin Lottery transferred \$126,588 in FY 2017-18 and \$112,270 in FY 2018-19 for this purpose.

Events Subsequent to FY 2018-19

2019 Wisconsin Act 9, the 2019-21 Biennial Budget Act enacted in July 2019, provided \$71.7 million and \$73.1 million in general purpose revenue for the Wisconsin Lottery in FY 2019-20 and FY 2020-21, respectively. Under Act 9, \$48.0 million is appropriated for retailer compensation and \$17.8 million is appropriated for fees paid to the vendor for the integrated gaming computer system in both FY 2019-20 and FY 2020-21. In addition, \$5.9 million and \$7.3 million is appropriated to pay for general program operations, excluding salaries and product information, in FY 2019-20 and FY 2020-21, respectively.

***Changes to Powerball
jackpots were announced
in April 2020.***

In April 2020, due to economic uncertainty and anticipated decreased lottery sales resulting from the COVID-19 global pandemic, the national Powerball Product Group announced changes to the Powerball jackpots. Following the April 8, 2020 drawing, guaranteed starting jackpot amounts and minimum jackpot increases would be eliminated. Previously, Powerball jackpots started at \$40.0 million and increased by a minimum of \$10.0 million between drawings. Further, the Powerball Product Group announced that future starting jackpot amounts and jackpot increases will be determined on a drawing-by-drawing basis considering game sales and interest rates and will be announced prior to each drawing.

***Changes to Mega
Millions jackpots were
announced in April 2020.***

Similarly, in April 2020 the Mega Millions Consortium announced changes to its jackpots. Following the April 3, 2020 drawing, guaranteed starting jackpots and minimum jackpot increases would be eliminated. Previously, Mega Millions jackpots started at \$40.0 million and increased by a minimum of \$5.0 million for each roll. Further, the Mega Millions Consortium announced that future starting jackpot amounts and jackpot increases will be determined on a drawing-by-drawing basis considering game sales and interest rates and will be announced prior to each drawing. The Wisconsin Lottery discusses how the Lottery's performance is subject to economic conditions and its impact on consumer spending within the Factors Impacting Future Results section in its Management's Discussion and Analysis, which begins on page 17.

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Audit Opinion ■



Independent Auditor's Report on the Financial Statements and Other Reporting Required by *Government Auditing Standards*

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee

Mr. Peter Barca, Secretary
Department of Revenue

Ms. Cindy Polzin, Administrator
Division of Lottery
Department of Revenue

Report on the Financial Statements

We have audited the accompanying financial statements and the related notes of the Wisconsin Lottery as of and for the years ended June 30, 2019, and June 30, 2018, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the

financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion on these financial statements.

Opinion

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Wisconsin Lottery as of June 30, 2019, and June 30, 2018, and the respective changes in its financial position and its cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 2A to the financial statements, the financial statements referred to in the first paragraph present only the Wisconsin Lottery and do not purport to, and do not, present fairly the financial position of the State of Wisconsin as of June 30, 2019, and June 30, 2018, the changes in its financial position, or where applicable, its cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information—Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis, which is on pages 17 through 28, be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, which considers it to be essential for placing the financial statements in an appropriate operational, economic, or historical context. In accordance with auditing standards generally accepted in the United States of America, we have applied certain limited procedures to the required supplementary information that included inquiries of management about the methods of preparing the information. We further compared the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Accompanying Information—Our audits for the years ended June 30, 2019, and June 30, 2018, were conducted for the purpose of forming an opinion on the financial statements of the Wisconsin Lottery. Schedules 1 and 2 on pages 60 and 61, respectively, are presented for purposes of additional analysis and are not a required part of the financial statements for the years ended June 30, 2019, and June 30, 2018. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying

accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.


We also previously audited, 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*, the financial statements of the Wisconsin Lottery as of and for the years ended June 30, 2017, June 30, 2016, and June 30, 2015 (not presented herein), and issued reports thereon dated August 3, 2018 (report 18-7), August 29, 2017 (report 17-15), and July 20, 2016 (report 16-7), which contained unmodified opinions on the respective financial statements of the Wisconsin Lottery. In this report (report 20-4), Schedule 1, on page 60, for the year ended June 30, 2017, and Schedule 2, on page 61, for the years ended June 30, 2017, June 30, 2016, and June 30, 2015, are presented for purposes of additional analyses and are not a required part of the financial statements.

Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements for the years ended June 30, 2017, June 30, 2016, and June 30, 2015. The information has been subjected to the auditing procedures applied in the audits of those financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare those financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole for the years ended June 30, 2017, June 30, 2016, and June 30, 2015.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued a report dated April 23, 2020, on our consideration of the Department of Revenue's and Wisconsin Lottery's internal control over financial reporting; our tests of its compliance with certain provisions of laws, regulations, contracts; and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the Department of Revenue's and Wisconsin Lottery's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be used when considering the Department of Revenue's and the Wisconsin Lottery's internal control over financial reporting and compliance.

LEGISLATIVE AUDIT BUREAU



Joe Chrisman
State Auditor

April 23, 2020

Management's Discussion and Analysis ■

Prepared by Wisconsin Lottery Management

This section of the Wisconsin Lottery's (Lottery) financial statements provides the Management's Discussion and Analysis of the Lottery's financial performance for the fiscal years ended June 30, 2019, and June 30, 2018, with comparative information from the fiscal year ended June 30, 2017. This discussion should be read in conjunction with the accompanying financial statements and notes. The financial statements, notes, and this discussion are the responsibility of the Wisconsin Department of Revenue and Lottery management.

Financial Highlights

In fiscal year (FY) 2017-18, the Lottery implemented Governmental Accounting Standards Board (GASB) Statement Number 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. This established accounting and financial reporting standards for defined benefit other postemployment benefits (OPEB) and defined contribution OPEB provided to state and local governmental employers.

Operating Revenues/Program Expenses

The Lottery's operating revenues generated from ticket sales were \$713.1 million in FY 2018-19 compared to \$667.4 million in FY 2017-18, an increase of 6.9 percent. Total FY 2018-19 ticket sales increased from FY 2017-18 due to the largest-ever Mega Millions jackpot of \$1.5 billion. This multi-state game was won on October 23, 2018, from a ticket bought in South Carolina. In FY 2018-19, instant scratch-off tickets also had their highest annual sales in Lottery history.

Program expenses for FY 2018-19 increased by \$31.2 million, or 6.5 percent, primarily due to increased prize expense and retailer commissions and incentives, which rise with increased sales. Administrative expenses (salaries and fringe benefits, and supplies) increased to \$10.5 million in FY 2018-19 from \$8.1 million in FY 2017-18. Supplies and services increased by \$2.2 million from FY 2017-18. Salaries and fringe benefits increased by \$0.2 million due to the general wage adjustments that were part of the 2017-2019 State of Wisconsin Compensation Plan. Net income before transfers was \$196.0 million for FY 2018-19, compared to \$180.2 million in FY 2017-18.

Total statutory administrative expenses were 5.6 percent of gross Lottery revenues in FY 2018-19, well below the statutory maximum of 10.0 percent (sec. 25.75 (3) (b), Wis. Stats.). Total statutory administrative expenses, including administrative expenses reported in the financial statements, all program expenses except prizes and retailer compensation, and certain transfers out, were \$40.2 million in FY 2018-19, which was an increase of \$3.2 million from \$37.0 million in FY 2017-18.

Understanding the Financial Statements

The Wisconsin Constitution requires the Lottery to use its net proceeds from operations to provide property tax relief. The Lottery is considered an enterprise activity, a proprietary fund type that reports all the activity's assets and liabilities using the accrual basis of accounting, much like a private business entity.

This Management's Discussion and Analysis consists of comparative financial statements, and explanatory notes to the financial statements and supplemental schedules. The financial statements are comprised of these three components:

- Statement of Net Position—provides detailed information on the nature and amount of the Lottery's assets, deferred outflows, liabilities, deferred inflows, and net position as of June 30, 2019, and June 30, 2018;
- Statement of Revenues, Expenses, and Changes in Net Position—reports the revenues and expenses incurred in relation to the sale of Lottery products, and other non-gaming related activity for FY 2018-19 and FY 2017-18; and
- Statement of Cash Flows—outlines the cash inflows and outflows related to the sale of Lottery products and other business-related activities for FY 2018-19 and FY 2017-18.

The Lottery's financial position and financial health can be assessed by paying attention to the changes in:

- the components of assets and liabilities in the Statement of Net Position;
- income and expenses in the Statement of Revenues, Expenses, and Changes in Net Position; and
- the Statement of Cash Flows.

Overview of Financial Position

The Statement of Net Position provides detailed information on the Lottery's assets, deferred outflows, liabilities, deferred inflows, and net position at the end of FY 2018-19 and FY 2017-18.

Table A presents condensed data for the past three fiscal years. The relationship of assets and deferred outflows to liabilities and deferred inflows, and the resulting net position is an indicator of the Lottery's financial condition.

Table A

Statement of Net Position (in millions)

	June 30, 2019	Change	June 30, 2018	Change	Restated June 30, 2017
Assets					
Investments	\$ 15.2	\$(3.8)	\$ 19.0	\$(5.5)	\$24.5
Capital Assets (net of accumulated depreciation)	0.1	(0.1)	0.2	0.0	0.2
Other Assets	96.2	9.1	87.1	19.9	67.2
Total Assets	111.5	5.2	106.3	14.4	91.9
Total Deferred Outflows of Resources	2.8	1.2	1.6	(0.2)	1.8
Liabilities					
Current Liabilities	55.5	9.4	46.1	(0.4)	46.5
Noncurrent Liabilities	12.6	(2.6)	15.2	(3.4)	18.6
Total Liabilities	68.1	6.8	61.3	(3.8)	65.1
Total Deferred Inflows of Resources	1.8	(0.1)	1.9	1.1	0.8
Net Position					
Invested in Capital Assets	0.1	(0.1)	0.2	0.0	0.2
Restricted for Pensions	0.0	(0.9)	0.9	0.9	0.0
Restricted for MUSL Reserves	6.7	0.9	5.8	0.6	5.2
Restricted for Investment Fair Value Adjustment	1.3	(0.2)	1.5	(1.2)	2.7
Restricted for Property Tax Relief	36.3	0.0	36.3	16.6	19.7
Total Net Position	<u>\$ 44.4</u>	<u>\$(0.3)</u>	<u>\$ 44.7</u>	<u>\$16.9</u>	<u>\$27.8</u>

Assets

Lottery's assets consist primarily of cash and cash equivalents, investments for prize annuities, accounts receivable, Multi-State Lottery Association (MUSL) reserve accounts, and instant ticket inventory.

As was shown in Table A, total assets were \$111.5 million at the end of FY 2018-19, compared to \$106.3 million at the end of FY 2017-18, and \$91.9 million at the end of FY 2016-17. Cash and cash equivalents increased by \$6.6 million in FY 2018-19.

Liabilities

At the end of FY 2018-19, the Lottery's total liabilities were \$68.1 million, compared to \$61.3 million at the end of FY 2017-18 and \$65.1 million at the end of FY 2016-17.

Current liabilities consist primarily of accrued prizes payable, annuity prizes payable, and accounts payable due to suppliers.

Noncurrent liabilities consist primarily of annuity prizes payable more than a year beyond the date of the Statement of Net Position. Since 2007, no winners have chosen to receive their prize as an annuity. As a result, total annuity prizes payable continues to decrease each year as existing annuitants receive their annual payments.

Net Position

At the end of FY 2018-19, the Lottery's total net position was \$44.4 million, a \$0.3 million decrease from the prior year. The FY 2018-19 decrease was primarily due to a \$64.7 million increase in property tax relief, a \$15.8 million increase in Net Income Before Transfers, and a \$32.0 million increase in the Transfers in From General Fund. The total net position at the end of FY 2017-18 was \$44.7 million, a \$16.9 million increase from FY 2016-17. Total net position was \$27.8 million at the end of FY 2016-17.

The Lottery's net position is generally restricted for property tax relief unless restricted for other uses. The Lottery's net position currently has four restrictions other than property tax relief:

- amounts invested in capital assets;
- reserve accounts held by MUSL;
- unrealized gains or losses related to the change in the fair value of investments because investments have been purchased for the payment of annuity prizes payable and are generally held to maturity; and
- restricted for pensions, which are amounts reserved for adjustments required by governmental accounting standards for Wisconsin Retirement System and OPEB activity.

The Statement of Revenues, Expenses, and Changes in Net Position provides detailed information on the financial impact of the Lottery's operations for FY 2018-19 and FY 2017-18. Table B presents condensed data for the past three fiscal years.

Table B

Statement of Revenues, Expenses, and Changes in Net Position
(in millions)

	FY 2018-19	Change	FY 2017-18	Change	Restated FY 2016-17
Revenues					
Operating Revenues:					
Ticket Sales	\$713.1	\$45.7	\$667.4	\$64.6	\$602.8
Retailer Fees and Miscellaneous Revenue	1.3	1.1	0.2	(0.2)	0.4
Nonoperating Revenues:					
Gain (Loss) on Disposal of Fixed Assets	0.0	0.0	0.0	(0.1)	0.1
Investment Income (Loss)	2.4	2.6	(0.2)	1.1	(1.3)
Total Revenues	716.8	49.4	667.4	65.4	602.0
Expenses					
Program Expenses:					
Prize Expenses	431.9	27.5	404.4	41.4	363.0
Retailer Commissions and Incentives	49.7	3.2	46.5	5.2	41.3
Instant and Lotto Vendor Services	18.3	1.1	17.2	3.3	13.9
Other Game-Related Expenses	10.4	(0.6)	11.0	(1.4)	12.4
Administrative Expenses	10.5	2.4	8.1	(1.5)	9.6
Total Expenses	520.8	33.6	487.2	47.0	440.2
Net Income Before Transfers	196.0	15.8	180.2	18.4	161.8
Transfers					
Transfers Out—Property Tax Relief	(235.0)	(64.7)	(170.3)	13.0	(183.3)
Transfers In—General Fund	40.0	32.0	8.0	8.0	0.0
Transfers Out—Compulsive Gambling Programs	(0.4)	0.0	(0.4)	0.0	(0.4)
Transfers Out—Law Enforcement	(0.3)	0.0	(0.3)	0.1	(0.4)
Transfers Out—Lottery Credit Administration	(0.2)	0.0	(0.2)	0.0	(0.2)
Transfers Out—General Fund	(0.4)	(0.3)	(0.1)	0.0	(0.1)
Change in Net Position	\$ (0.3)	\$ (17.2)	\$ 16.9	\$ 39.5	\$ (22.6)

Revenues

Operating revenues are generated almost entirely from ticket sales. The Lottery had \$713.1 million in ticket sales in FY 2018-19, \$667.4 million in FY 2017-18, and \$602.8 million in FY 2016-17.

Table C presents condensed data for the past three fiscal years, comparing ticket sales for each game category.

Table C

Wisconsin Lottery Ticket Sales (in millions)

	FY 2018-19	Change	FY 2017-18	Change	FY 2016-17
Instant Ticket Sales					
Scratch-off	\$450.3	\$30.9	\$419.4	\$34.6	\$384.8
Pull-tab	1.0	0.0	1.0	(0.1)	1.1
Total Instant Ticket Sales	451.3	30.9	420.4	34.5	385.9
Lotto Ticket Sales					
SuperCash!	24.6	(1.2)	25.8	0.2	25.6
Powerball	84.8	(13.4)	98.2	16.2	82.0
Wisconsin's Megabucks	14.6	3.2	11.4	(0.7)	12.1
Wisconsin's Megabucks EZ Match	1.9	0.3	1.6	0.0	1.6
Daily Pick 3	23.6	(0.3)	23.9	(0.2)	24.1
Daily Pick 4	14.1	0.1	14.0	1.0	13.0
Badger 5	24.4	(1.2)	25.6	(0.1)	25.7
Mega Millions	63.3	23.9	39.4	13.5	25.9
5 Card Cash ¹	4.7	(1.6)	6.3	0.2	6.1
All or Nothing ¹	5.0	5.0	0.0	0.0	0.0
Raffle Games	0.8	0.0	0.8	0.0	0.8
Total Lotto Ticket Sales	261.8	14.8	247.0	30.1	216.9
Total Sales	<u>\$713.1</u>	<u>\$45.7</u>	<u>\$667.4</u>	<u>\$64.6</u>	<u>\$602.8</u>

¹ 5 Card Cash ended during FY 2018-19 and All or Nothing began during FY 2018-19.

Total ticket sales increased by 6.9 percent in FY 2018-19 compared to FY 2017-18. Instant scratch-off ticket sales increased by \$30.9 million from FY 2017-18 to FY 2018-19. Lotto ticket sales increased by \$14.8 million from FY 2017-18 to FY 2018-19, primarily due to increased Mega Millions ticket sales resulting from a large jackpot in FY 2018-19. Pull-tab sales remained consistent from FY 2016-17 through FY 2018-19.

Expenses

Lottery expenses consist of prize amounts, retailer commissions and incentives, fees paid to the Lottery's gaming system vendor (instant and lotto vendor services), other game-related expenses, and administrative expenses. In FY 2018-19, total operating expenses were \$520.8 million, an increase of \$33.6 million from FY 2017-18 expenses of \$487.2 million, which was an increase from FY 2016-17 expenses of \$440.2 million. The fluctuation in expenses is primarily a result of changes in prize expense, which tend to follow changes in sales. Prizes are the Lottery's largest expense. Table D compares ticket prize awards for each lottery game category for the last three fiscal years.

Table D

Wisconsin Lottery Ticket Prize Awards (in millions)

	FY 2018-19	Change	FY 2017-18	Change	FY 2016-17
Instant Prize Expense					
Scratch-off	\$299.6	\$18.4	\$281.2	\$26.4	\$254.8
Pull-tab	0.6	0.0	0.6	(0.1)	0.7
Super 2nd Chance ¹	0.3	0.0	0.3	0.0	0.3
Total Instant Prize Awards	300.5	18.4	282.1	26.3	255.8
Lotto Prize Expense					
SuperCash!	15.4	1.9	13.5	(0.9)	14.4
Powerball	41.3	(6.3)	47.6	9.5	38.1
Wisconsin's Megabucks	7.8	1.6	6.2	(0.1)	6.3
Wisconsin's Megabucks EZ Match	1.2	0.2	1.0	0.0	1.0
Daily Pick 3	10.9	(0.2)	11.1	(0.7)	11.8
Daily Pick 4	6.3	(0.4)	6.7	0.3	6.4
Badger 5	11.8	(0.6)	12.4	0.2	12.2
Mega Millions	30.8	11.4	19.4	6.7	12.7
5 Card Cash ²	2.5	(1.2)	3.7	0.1	3.6
All or Nothing ²	2.8	2.8	0.0	0.0	0.0
Raffle Games	0.3	(0.1)	0.4	0.0	0.4
Super 2nd Chance ¹	0.3	0.0	0.3	0.0	0.3
Total Lotto Prize Awards	131.4	9.1	122.3	15.1	107.2
Total Prize Expense	<u>\$431.9</u>	\$27.5	\$404.4	\$41.4	\$363.0

¹ Super 2nd Chance prizes are awarded through drawings to players who send in non-winning instant scratch-off and lotto tickets. The prizes are funded from instant scratch-off and lotto ticket sales.

² 5 Card Cash ended during FY 2018-19 and All or Nothing began during FY 2018-19.

Chart A and Chart B compare ticket sales and prize expense for each lottery game category (lotto and instant games, respectively) for the last three fiscal years. This is the same data that was shown in Table C and Table D presented by game category in another format.

Chart A

Lotto Ticket Sales and Prize Expense
(in millions)

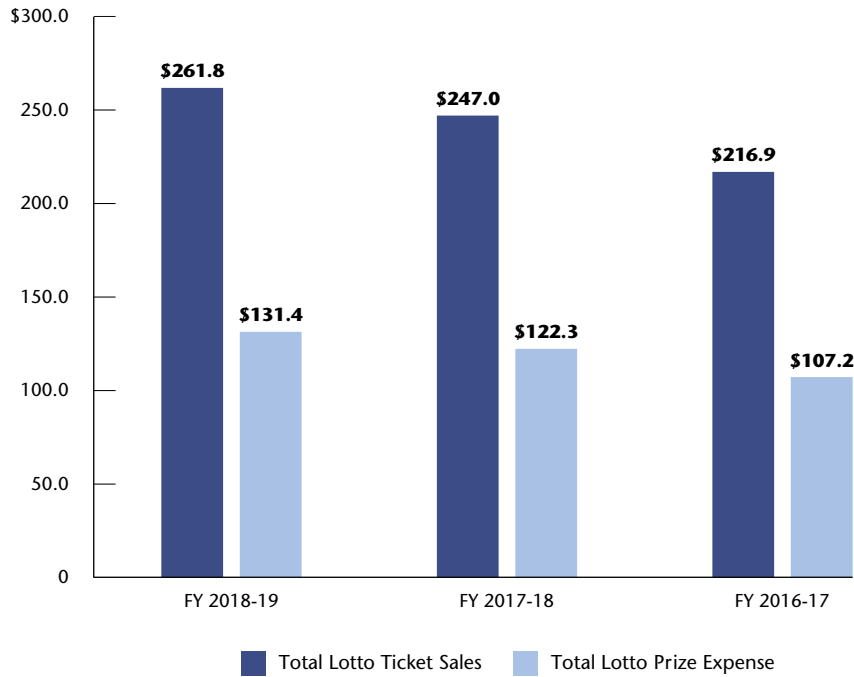
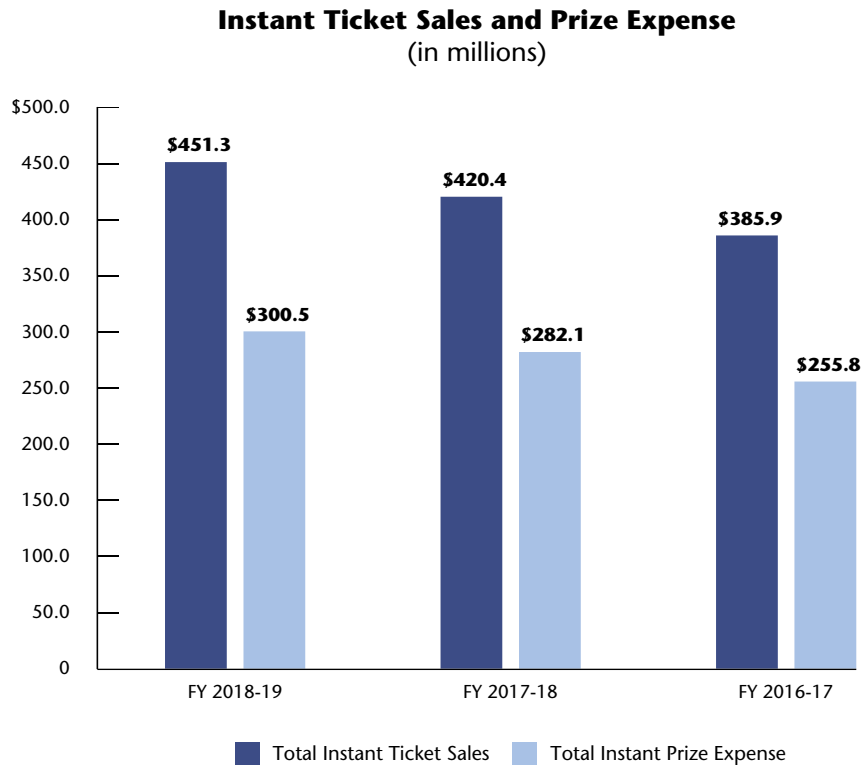


Chart B



Generally, prizes awarded are a function of ticket sales. Higher ticket sales result in greater prize expense, while lower sales result in lower prize expense. However, the change in prize expense is not always perfectly proportional to sales. Each individual game has a unique prize structure. As sales shift among the games being offered, prize expenses can fluctuate more or less than would be expected based on the change in sales. In FY 2018-19, ticket sales across all games increased by \$45.7 million, while prize expense increased by \$27.5 million. In FY 2017-18, ticket sales increased by \$64.6 million, while prize expense increased by \$41.4 million. Schedule 2, on page 61, shows a multi-year summary of ticket sales and their related prize expenses.

Since retailer commissions and incentives expenses are a function of sales, they typically rise and fall with sales. In FY 2018-19, retailers were paid \$49.7 million in commissions and incentives, up \$3.2 million from the \$46.5 million paid in FY 2017-18. In FY 2016-17, retailer commissions and incentives were \$41.3 million.

The Lottery contracts with IGT Global Solutions Corporation (IGT) for an integrated gaming computer system and services (instant and lotto vendor services). The initial terms of this seven-year contract from the operational start date of May 14, 2017, requires the Lottery to pay IGT 2.57 percent of weekly net sales. This contract is eligible for up to three one-year renewals. The Lottery

executed one of the renewals on amendment one. The contract requires IGT to provide:

- a lottery gaming system;
- seventy percent of instant scratch-off ticket printing;
- distribution services;
- warehousing facility and services;
- telemarketing services; and
- a hot-site backup.

In FY 2018-19, payments to IGT were \$18.3 million compared to \$17.2 million in FY 2017-18.

Net Income and Transfer for Property Tax Relief

Net income before transfers was \$196.0 million in FY 2018-19, up from \$180.2 million in FY 2017-18. Net income before transfers, as restated, was \$161.8 million in FY 2016-17.

As shown in Table B, the property tax relief amount transferred out differs from net income. This is because the transfers occur before the end of the fiscal year and are based on an estimate of the total funds that will be available for distribution. The transfers out for property tax relief increased by \$64.7 million, or by 38.0 percent, during FY 2018-19, after decreasing by \$13.0 million, or by 7.1 percent, during FY 2017-18.

Factors Impacting Future Results

The Lottery's success is dependent on its ability to effectively gauge the market for its products. It regularly changes its product offerings, responding to consumer preferences. The Lottery is engaged in a long-term growth strategy for instant scratch-off ticket sales by meeting consumer demand for more games with higher price points. Sales continue to build for tickets priced \$10 and higher. While the Lottery makes every effort to ensure the success of its products, overall sales are adversely affected if the Lottery misjudges the market.

Approximately 20.8 percent of all ticket sales in FY 2018-19 came from two MUSL jackpot games, Mega Millions and Powerball. The sales of these games can be volatile as they are driven by the random occurrence (size and frequency) of large jackpots. For example, Powerball sales significantly increased in FY 2017-18 by 19.8 percent only to see a decrease in FY 2018-19 of 13.6 percent. The volatility of

jackpot games makes forecasting ticket sales difficult. The Lottery has established a range to forecast future performance based on past performance. However, that range is broad and jackpot game sales can vary from year-to-year by tens of millions of dollars from estimates.

Since lottery tickets are a discretionary purchase, the Lottery's performance is subject to economic conditions and its impact on consumer spending. Some factors influencing consumer spending include unemployment, fuel costs, the cost of essential goods (such as food, clothing, and shelter), and consumer confidence in the economy. Consumer purchases of discretionary items, including Lottery tickets, generally decline during periods when disposable income is adversely affected or when there is a lack of consumer confidence in the economy.

In September 2015, the Lottery asked the Wisconsin Department of Justice (DOJ) to review the December 29, 2007 Wisconsin's Megabucks drawing to determine if any illegal activity may have occurred in Wisconsin. The Lottery made this request because an individual previously employed by MUSL had access to Wisconsin's random number generators (RNGs) and was since convicted of fraud in Iowa. Suspected fraud related to this individual was also being investigated in Colorado, Kansas, and Oklahoma. DOJ's investigation resulted in two individuals pleading guilty to fraud related charges. One individual was convicted of a felony, Computer Crime as Party to a Crime. On August 28, 2017, this individual's sentence was withheld, and the individual was placed on probation for one year. As conditions of the probation, this individual was required to serve six months of confinement and make restitution to the Lottery. This sentence is concurrent to this individual's sentence in Iowa. Another individual pled guilty to two felony charges, one of which was Computer Crime and the other was Theft—False Representation >\$10,000. On September 15, 2017, this individual was sentenced to four years of initial confinement and five years of extended supervision. Additionally, this individual was ordered to pay restitution to the Lottery. This individual is serving his sentence concurrently with an Iowa conviction in a prison in Polk County, Iowa.

The Lottery purchased new RNGs from a third-party independent of MUSL and had them forensically examined by security experts before implementation. Since then, a strict protocol has been implemented requiring that all RNG updates go through this forensic examination process before being implemented. Additional security measures were also implemented to insure and protect the Lottery's integrity.

2019 Wisconsin Act 9 increased the existing \$40.0 million general purpose revenue (GPR) funding for the Lottery in FY 2019-20 and FY 2020-21 by \$31.7 million and \$33.1 million, respectively. The total 2019-2021 biennium GPR funding is shown in Table E.

Table E

2019-2021 Lottery General Purpose Revenue

	FY 2019-20	FY 2020-21
General Program Operations— Excluding Salaries and Product Information	\$ 5,893,300	\$ 7,276,700
Retailer Compensation	47,980,700	47,980,700
Vendor Fees	17,826,000	17,826,000
Total GPR Funding	\$71,700,000	\$73,083,400

Contacting Wisconsin Lottery's Financial Management

These financial statements provide the Legislature and the government's executive branch, the public, and other interested parties with an overview of the financial results of the Lottery's activities and to show accountability for the money it receives.

If you have questions about these financial statements or need more information, contact:

Wisconsin Department of Revenue
 Attn: Director, Bureau of Financial Management Services—Laurie Grams
 MS 6-261
 PO Box 8931
 Madison, Wisconsin 53708-8931
 (608) 266-8469

If you have general questions about the Wisconsin Lottery, contact:

Wisconsin Department of Revenue
 Attn: Wisconsin Lottery Director—Cindy Polzin
 PO Box 8941
 Madison, Wisconsin 53708-8941
 (608) 261-8800



Financial Statements ■

Statement of Net Position

June 30, 2019, and June 30, 2018

	<u>June 30, 2019</u>	<u>June 30, 2018</u>
ASSETS		
Current Assets:		
Cash and Cash Equivalents (Note 3)	\$ 57,052,434	\$ 50,402,545
Investments for Prize Annuities (Note 3)	3,878,588	4,520,223
Accounts Receivable (Note 4)	30,970,171	28,550,942
Due from Other State Programs (Note 4)	0	8,944
Ticket Inventory	887,542	816,228
MUSL Reserve Accounts (Note 5)	287,241	310,975
Prepaid Expenses	<u>407,232</u>	<u>365,447</u>
Total Current Assets	<u>93,483,208</u>	<u>84,975,304</u>
Noncurrent Assets:		
Prepaid Expenses	6,122	0
Investments for Prize Annuities (Note 3)	11,299,444	14,463,027
MUSL Reserve Accounts (Note 5)	6,644,193	5,774,081
Net Pension Asset	0	908,718
Capital Assets:		
Equipment	452,958	431,463
Leasehold Improvements	90,288	90,288
Accumulated Depreciation	<u>(401,693)</u>	<u>(372,831)</u>
Total Noncurrent Assets	<u>18,091,312</u>	<u>21,294,746</u>
TOTAL ASSETS	<u>111,574,520</u>	<u>106,270,050</u>
DEFERRED OUTFLOWS OF RESOURCES (Notes 6 and 7)	<u>2,768,519</u>	<u>1,628,205</u>
LIABILITIES		
Current Liabilities:		
Annuity Prizes Payable (Note 8)	4,027,792	4,447,435
Prizes Payable	43,944,136	37,047,090
Accounts Payable	5,560,471	3,070,528
Due to Other State Programs	391,431	123,394
MUSL Payable	812,798	750,895
Unearned Revenue	509,672	408,886
Due to Other Governments	106,363	117,232
Compensated Absences	<u>191,492</u>	<u>176,137</u>
Total Current Liabilities	<u>55,544,155</u>	<u>46,141,597</u>
Noncurrent Liabilities:		
Annuity Prizes Payable (Note 8)	10,043,175	13,237,710
Compensated Absences	539,572	470,865
Other Postemployment Benefits	1,009,674	1,451,887
Net Pension Liability	<u>982,623</u>	<u>0</u>
Total Noncurrent Liabilities	<u>12,575,044</u>	<u>15,160,462</u>
TOTAL LIABILITIES	<u>68,119,199</u>	<u>61,302,059</u>
DEFERRED INFLOWS OF RESOURCES (Notes 6 and 7)	<u>1,846,514</u>	<u>1,936,891</u>
NET POSITION		
Net Position: (Note 12)		
Invested in Capital Assets	141,552	148,920
Restricted for Pensions	0	908,718
Restricted for MUSL Reserves	6,644,193	5,774,081
Restricted for Investment Fair Value Adjustment	1,310,067	1,494,105
Restricted for Property Tax Relief	<u>36,281,514</u>	<u>36,333,481</u>
TOTAL NET POSITION	<u>\$ 44,377,326</u>	<u>\$ 44,659,305</u>

The accompanying notes are an integral part of this statement.

Statement of Revenues, Expenses, and Changes in Net Position for the Years Ended June 30, 2019, and June 30, 2018

	Year Ended June 30, 2019	Year Ended June 30, 2018
OPERATING REVENUES		
Instant Ticket Sales (Net of Allowances of \$8,567,297 and \$8,265,160, respectively) (Note 9)	\$ 451,343,267	\$ 420,434,815
Lotto Ticket Sales (Net of Ticket Discounts of \$2,611,004 and \$0, respectively) (Note 9)	261,789,507	246,957,605
Retailer Fees	56,674	60,490
Miscellaneous Revenue	1,196,465	158,572
Total Operating Revenues	714,385,913	667,611,482
OPERATING EXPENSES		
Program Expenses:		
Instant Prize Expense (Note 10)	300,532,518	282,121,683
Lotto Prize Expense (Note 10)	131,413,329	122,325,292
Retailer Commissions and Incentives	49,703,093	46,486,279
Instant and Lotto Vendor Services	18,290,471	17,196,328
Product Information Costs	8,467,617	8,484,215
Instant Ticket Printing Costs	1,906,778	2,527,750
Donated Prize Expense	5,536	4,359
Total Program Expenses	510,319,342	479,145,906
Administrative Expenses:		
Salaries and Fringe Benefits	5,663,494	5,466,208
Supplies and Services	4,809,574	2,568,434
Depreciation Expense	28,862	29,224
Total Administrative Expenses	10,501,930	8,063,866
Total Operating Expenses	520,821,272	487,209,772
NET OPERATING INCOME	193,564,641	180,401,710
NONOPERATING REVENUES (EXPENSES) AND TRANSFERS		
Investment Income (Loss)	2,399,834	(144,178)
Miscellaneous Revenue (Expense)	(2,737)	(367)
Net Income Before Transfers	195,961,738	180,257,165
Transfers:		
Transfers Out—Lottery Proceeds for Property Tax Relief (Note 13)	(234,879,988)	(170,255,138)
Transfers In—General Fund	40,000,000	8,008,886
Transfers Out—Department of Health and Family Services for Compulsive Gambling Programs	(396,000)	(396,000)
Transfers Out—Department of Justice for Law Enforcement	(344,029)	(345,588)
Transfers Out—Department of Revenue for Lottery Credit Administration	(224,430)	(226,065)
Transfers Out—General Fund	(399,270)	(126,588)
CHANGE IN NET POSITION	(281,979)	16,916,672
NET POSITION		
Net Position—Beginning of the Year	44,659,305	27,742,633
Net Position—End of the Year	\$ 44,377,326	\$ 44,659,305

Statement of Cash Flows for the Years Ended June 30, 2019, and June 30, 2018

	Year Ended June 30, 2019	Year Ended June 30, 2018
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash Received from Retailers	\$ 710,960,917	\$ 665,044,848
Cash Paid for Prizes	(428,510,367)	(407,598,120)
Cash Paid for Retailer Commissions and Incentives	(49,418,516)	(44,869,629)
Cash Paid/Received for MUSL Reserve Accounts	(840,581)	(607,522)
Cash Paid to Employees	(5,358,858)	(5,211,756)
Cash Paid to Suppliers	(31,078,423)	(30,794,106)
Net Cash Provided by Operating Activities	195,754,172	175,963,715
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Transfers Out—Proceeds for Property Tax Credit	(234,879,988)	(170,255,138)
Transfers Out—Proceeds for Law Enforcement	(345,142)	(349,263)
Transfers Out—Proceeds for Lottery Credit Administration	(223,405)	(225,547)
Transfers Out—Proceeds for Compulsive Gambling Programs	(396,000)	(396,000)
Transfers Out—General Fund	(399,270)	(126,588)
Transfers In—General Fund	40,008,886	8,000,000
Net Cash Used by Noncapital Financing Activities	(196,234,919)	(163,352,536)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Cash Paid for Purchase of Equipment	(21,496)	(13,712)
Cash Received from Sale of Equipment	0	68,340
Net Cash Used by Capital and Related Financing Activities	(21,496)	54,628
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest Received	2,578,132	1,054,080
Cash Received for Redemption of Bonds	4,574,000	5,533,000
Net Cash Provided by Investing Activities	7,152,132	6,587,080
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	6,649,889	19,252,887
Cash and Cash Equivalents—Beginning of the Year	50,402,545	31,149,658
Cash and Cash Equivalents—End of the Year	\$ 57,052,434	\$ 50,402,545

Statement of Cash Flows for the Years Ended June 30, 2019, and June 30, 2018 (continued)

	Year Ended June 30, 2019	Restated Year Ended June 30, 2018
RECONCILIATION OF NET OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Net Operating Income	\$ 193,564,641	\$ 180,401,710
Adjustments to Reconcile Net Operating Income to Net Cash Provided by Operating Activities:		
Depreciation Expense	28,862	29,224
Cancelled Draft Nonoperating Revenue	(8,270)	(4,726)
Noncash Donated Prize Expense	5,536	4,358
Changes in Assets, Liabilities, and Deferreds:		
Decrease (Increase) in Accounts Receivable	(2,419,229)	462,291
Decrease (Increase) in MUSL Reserve Accounts	(840,581)	(607,522)
Decrease (Increase) in Ticket Inventory	(71,314)	345,693
Decrease (Increase) in Prepaid Expenses	(47,908)	39,409
Decrease (Increase) in Net Pension Asset and Related Deferred Outflows	(231,597)	(732,838)
Increase (Decrease) in Prizes Payable	2,330,046	(4,237,640)
Increase (Decrease) in Unearned Revenue	100,787	(276,724)
Increase (Decrease) in Due to Other State Programs	260,900	(414,395)
Increase (Decrease) in Accounts Payable	2,496,589	(395,858)
Increase (Decrease) in MUSL Payable	61,903	314,643
Increase (Decrease) in Due to Other Governments	(10,288)	43,098
Increase (Decrease) in Compensated Absences	84,061	(5,074)
Increase (Decrease) in Other Postemployment Benefits	(442,213)	146,420
Increase (Decrease) in Net Pension Liability and Related Deferred Inflows	892,247	851,646
Total Adjustments	2,189,531	(4,437,995)
Net Cash Provided by Operating Activities	\$ 195,754,172	\$ 175,963,715
Noncash Activities:		
Increase (Decrease) in Fair Value of Investments	\$ (184,038)	\$ (1,202,244)
Amortization of Long-Term Annuity Prize Liability	952,821	1,223,138

Notes to the Financial Statements ■

1. DESCRIPTION OF THE WISCONSIN LOTTERY

On April 7, 1987, Wisconsin voters authorized a lottery's creation by the passage of a constitutional amendment, with a 65 percent to 35 percent margin. The Wisconsin Constitution requires the net proceeds from the lottery's operations be used for local property tax relief. The Wisconsin Lottery (Lottery) began in December 1987 and sold its first ticket on September 14, 1988. The Lottery is administered by the Lottery Division within the Wisconsin Department of Revenue. During fiscal year (FY) 2018-19 and FY 2017-18, the Lottery sold instant games (scratch-off and pull-tab tickets) and lotto games. Lotto games have drawings to determine winning tickets, which include raffle tickets and tickets produced from a terminal located at a Lottery retailer (e.g., Powerball, Badger 5).

Since June 1989, the Lottery has been a member of the Multi-State Lottery Association (MUSL). In FY 2018-19 and FY 2017-18, as a member of MUSL, the Lottery participated in two multi-jurisdictional lotto games: Powerball and Mega Millions. See Note 5 for information about MUSL.

During FY 2017-18 and FY 2018-19, the Lottery sold tickets for the following lotto games:

<u>Game Name</u>	<u>Start Date</u>
SuperCash!	February 4, 1991
Powerball	April 19, 1992
Wisconsin's Megabucks	June 20, 1992
Daily Pick 3	September 21, 1992
Daily Pick 4	September 15, 1997
Badger 5	February 17, 2003
Mega Millions	January 31, 2010
Wisconsin's Megabucks- EZ Match	April 3, 2011
5 Card Cash ¹	April 6, 2014

¹ 5 Card Cash ended on April 6, 2019.

In FY 2018-19, the Lottery also sold tickets for All or Nothing, which was a new game with a start date of April 7, 2019.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Financial Reporting Entity and Basis of Presentation

The Lottery's financial statements are prepared in conformance with generally accepted accounting principles (GAAP) for proprietary funds as prescribed by the Governmental Accounting Standards Board (GASB). These statements only present the financial position and results of the Lottery's operations and are not meant to present the financial activity for the State of Wisconsin as a whole. The Lottery is accounted for within the Lottery Fund, which is part of the State of Wisconsin financial reporting entity. The Lottery's stand-alone financial statements do not include the Lottery Fund appropriations from which the property tax credit disbursements are made. However, funding for these appropriations is reported on the Statement of Revenues, Expenses, and Changes in Net Position as "Transfers Out-Lottery Proceeds for Property Tax Relief."

B. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The accompanying financial statements are prepared based on the flow of economic resources and full accrual basis of accounting. With this measurement focus, all assets, deferred outflows of resources, liabilities, and deferred inflows of resources associated with the operation of the Lottery are included on the Statement of Net Position. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized when incurred.

The Statement of Revenues, Expenses, and Changes in Net Position classifies the Lottery's activities as either operating or nonoperating. Because the Lottery Fund is an enterprise fund (proprietary fund type), it accounts for operations similar to private businesses where operating revenues are derived from exchange transactions, such as sales. Operating expenses include the costs of sales, administrative expenses, and depreciation on capital assets. Certain revenues and expenses not related to the Lottery's primary purpose, such as investment income, are reported as nonoperating revenues and expenses.

In FY 2017-18, the Lottery implemented GASB Statement Number 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. This statement changed the presentation and disclosure requirements for employers that offer governmental other postemployment benefits (OPEB) plans.

C. Cash and Cash Equivalents

Cash and cash equivalents reported on the Statement of Net Position and on the Statement of Cash Flows include cash deposited in the State's bank and the Lottery's pro rata share of the State Investment Fund, a short-term pool of state and local funds managed by the State of Wisconsin Investment Board. Balances pooled in the State Investment Fund are restricted to legally stipulated investments valued consistent with GASB Statement Number 72, *Fair Value Measurement and Application*.

D. Investments for Prize Annuities

Investments for prize annuities consist entirely of securities backed by the full faith and credit of the U.S. government or its agencies. The securities finance jackpot prizes that are payable as annuities over a 20-, 25-, or 30-year period and are scheduled to mature near the time prize payments become payable to winners. Lottery investments are reported at fair value consistent with the provisions of GASB Statement Number 72, *Fair Value Measurement and Application*. Increases or decreases in fair value are recognized as investment income (loss).

E. Accounts Receivable

Accounts receivable balances primarily represent amounts due from Lottery retailers. Receivables are recorded when the Lottery sells instant tickets to retailers. The receivable balance is shown net of amounts due to retailers. These amounts include commissions, performance incentives, winning ticket incentives, and ticket redemption amounts. Payments for instant ticket orders are due 21 days after activation, except for nonprofit organizations where payments are due on delivery. Receivables are recorded for lotto games when retailers sell lotto tickets and have payments due within a week. The Lottery collects receivables weekly from retailer deposit accounts.

To receive a refund, retailers must return unsold instant scratch-off tickets to the Lottery any time before the game’s end date. Therefore, receivables and cash collected in advance of these tickets being sold represent a contingent liability of the Lottery. A sales allowance estimate is made for the portion of the tickets that may be returned based on historical information on unsold tickets retailers returned and is reported as a reduction of the receivable balance. For more information on accounts receivable, see Note 4.

F. Ticket Inventory

A portion of the instant scratch-off ticket printing services is included in the lottery gaming system contract with IGT Global Solutions Corporation (IGT), effective May 14, 2017. Under the contract, IGT accepts ownership of tickets printed after May 14, 2017, for both IGT and Pollard Banknote. The Lottery maintains ownership of tickets printed by any other vendor. Only the tickets owned by the Lottery are included in the ticket inventory balance. This balance consists of ticket printing costs and related royalty fees for instant ticket games in progress that have not yet been sold or shipped, and tickets for new games. The tickets are valued at cost using the first-in, first-out method. The cost of tickets sold is charged to operations. Unused tickets are charged to operations in the fiscal year the game ends or at the end of ticket distribution for a given game, whichever occurs first.

G. Capital Assets

Tangible assets purchased for \$5,000 or more and intangible assets with a cost or value greater than \$1.0 million are capitalized and recorded at historic cost. As applicable, assets are depreciated using the straight-line method according to the following schedule:

	<u>Estimated Life</u>
Leasehold Improvements	10 Years
Office Furniture and Security Equipment	10 Years
Printing and Microfilming Equipment	7 Years
Office, Computer, and Data Processing Equipment	5 Years

H. Employee Retirement Benefits/Pensions

The following are determined on the same basis as they are reported by the Wisconsin Retirement System (WRS):

- measurement of the net pension liability (asset);
- deferred outflows of resources;
- deferred inflows of resources;

- pension expense;
- information about the fiduciary net position of the WRS; and
- additions to or deductions from the fiduciary net position.

For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value. For more information on deferred outflows and inflows of resources related to employee retirement benefits/pensions, see Note 6.

I. Other Post-Employment Benefits (OPEB)

The fiduciary net position of the State Retiree Life Insurance Fund (SRLIF) and the State Retiree Health Insurance Fund (SRHIF) was determined using the flow of economic resources measurement focus and the accrual basis of accounting. This includes for purposes of measuring the net OPEB liability, deferred outflows of resources and deferred inflows of resources related to OPEB, OPEB expense, and information on the fiduciary net position of the SRLIF and of the SRHIF and additions to/deductions from the fiduciary net position, which were determined on the same way as they are reported by the SRLIF and the SRHIF. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value. For more information on deferred outflows and inflows of resources related to OPEB, see Note 7.

J. Prizes Payable and Annuity Prizes Payable

For lotto games, a liability is recognized when the drawing is held. For instant ticket games, a liability is recognized when tickets are sold to retailers. For more information on annuity prizes payable, see Note 8.

K. Unearned Revenue

Depending on the game, lotto tickets may be sold for up to eight future drawings. Lotto ticket revenue is recognized when the related drawings are held. All ticket sales for future drawings are reported as unearned revenue.

L. Compensated Absences

Consistent with the compensated absences reporting standards of GASB Statement Number 16, *Accounting for Compensated Absences*, an accrual for certain salary-related payments associated with annual leave and an accrual for a certain portion of sick leave is included in the compensated absences liability at year end. The Lottery's compensated

absence liability consists of accumulated unpaid annual leave, personal holiday hours, and Saturday/legal holiday hours earned and vested as of June 30.

M. Ticket Sales Revenue

Ticket sales are made to the public through licensed retailers.

Instant scratch-off ticket revenues are recognized when tickets are sold to the retailers. Lottery retailers may return unsold instant scratch-off tickets for a full refund. Consequently, instant scratch-off ticket sales are reduced through a sales allowance estimate, based on historical information of unsold tickets returned by the retailers.

Revenues for pull-tab games are recognized when tickets are sold to retailers. Lottery retailers must return full packs of unsold tickets for a full refund. However, pull-tab ticket sales are not reduced using a sales allowance estimate as historically the amounts are insignificant.

Ticket revenues for lotto games are recognized when the related drawings are held. The Lottery occasionally features lotto game promotions that offer bonus tickets, such as six tickets for the price of five. Revenue is recognized for all tickets sold, and a sales discount is used to record the value of the bonus tickets.

N. Prize Expenses

Under s. 25.75 (3) (a), Wis. Stats., at least 50 percent of Lottery sales must be returned in the form of prizes. Winners may claim their prizes for a period of 180 days after the drawing for lotto games, or 180 days from the start of the end of a game for instant games. A summary of prize expenses is shown in Schedule 2.

O. Retailer Commissions and Incentives

Retailer commissions, which are classified as program expenses, are set by statute and are 5.5 percent for lotto ticket sales and 6.25 percent for instant scratch-off and instant pull-tab tickets. Nonprofit organizations receive higher commissions.

In addition to the retailer commissions, the Lottery administers an incentive program for retailers meeting certain performance goals the Lottery identified. This program began on January 1, 2000. Retailers must be in good standing and sell instant tickets to participate in the program. It has three components: winning ticket, short-term incentive, and a sales goals incentive. The total compensation provided to all retailers under the program's components may not exceed 1.0 percent of gross revenues from the sale of lotto and instant tickets.

Winning Ticket—under the winning ticket component, participating retailers that sell a winning instant scratch-off or lotto game ticket of \$600 or more receive a 2.0 percent commission of the prize award, up to

a maximum of \$100,000 per winning ticket. If there is a pari-mutuel drawing with a large jackpot shared by multiple winning tickets, retailers can earn total compensation of up to a maximum of \$300,000. Winning ticket incentive payments are made weekly.

Short-term Incentive—under the short-term component, incentives are offered throughout the year for predefined periods and focus on supporting one product or category of ticket products. Each incentive has a predetermined goal the lottery retailer must achieve to receive additional compensation. Each short-term incentive’s aggregate payment amount to retailers is limited to \$300,000.

Sales Goal Incentive—under the sales goal component, participating retailers can earn additional commission based on increased sales. Subject to certain restrictions and allowances, retailers can earn up to 2.0 percent of the increase in quarterly sales compared to sales of the previous quarter for instant tickets and certain non-jackpot lotto games (SuperCash!, Daily Pick 3, Daily Pick 4, Badger 5, 5 Card Cash, (which ended April 6, 2019), and All or Nothing). These payments are made quarterly. Retailers also earn up to 10.0 percent of the increase in annual sales over the previous year. Due to variability of sales of jackpot lotto games (Wisconsin’s Megabucks, Mega Millions, and Powerball) and raffle games, sales goals incentive payments for these games are made annually. The annual payments may be limited to ensure total payments do not exceed the statutory cap of 1.0 percent of gross instant and lotto ticket sales.

P. Administrative Expenses

Section 25.75 (3) (b), Wis. Stats., limits the Lottery’s statutory administrative expenses to 10.0 percent of gross lottery revenues. Statutory administrative expenses were 5.63 percent for FY 2018-19. A summary of statutory administrative expenses and related calculations of the administrative expense limit is included in Schedule 1.

Q. Disbursement of Lottery Proceeds for Property Tax Relief

The Wisconsin Department of Revenue disburses net lottery proceeds through the Lottery and Gaming Tax Credit. The Wisconsin Department of Administration, with the approval of the Legislature’s Joint Committee on Finance, determines the annual amount available for distribution as the Lottery and Gaming Tax Credit in a given fiscal year. However, the amount to be disbursed is determined by November, well before the end of the fiscal year. The credit is based on the prior year’s balance carryover and estimated proceeds for the current year.

R. Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect

the reported amount of assets and liabilities, disclose contingent assets and liabilities as of the dates of the financial statements, and affect the reported amounts of revenues and expenses during the reporting periods. Accordingly, actual results could differ from those estimates.

3. CASH AND INVESTMENTS

The Lottery's cash and cash equivalents balance consists of cash deposited in the State's bank and shares in the State Investment Fund, a short-term pool of state and local funds managed by the State of Wisconsin Investment Board with oversight by its Board of Trustees. The State Investment Fund is not registered with the U.S. Securities and Exchange Commission. The carrying amount of shares in the State Investment Fund, which approximates fair value, was \$57.2 million as of June 30, 2019, and \$50.5 million as of June 30, 2018.

The types of securities in which the State Investment Fund may invest are stated in sec. 25.17 (3) (b), (ba), (bd), and (dg), Wis. Stats., and include direct obligations of the U.S. or its agencies, corporations wholly owned by the U.S. or chartered by an act of Congress, securities guaranteed by the U.S., unsecured notes of financial and industrial issuers, direct obligations of or guaranteed by the government of Canada, certificates of deposit issued by banks in the U.S. and solvent financial institutions in Wisconsin, and bankers acceptances. The Investment Board's trustees may specifically approve other prudent legal investments.

The Lottery manages its investments for prize annuities separately from the cash and investment activities of the State Investment Fund. The Lottery's investments were purchased to finance jackpot prizes payable as annuities over a 20-, 25-, or 30-year period and consist entirely of securities backed by the full faith and credit of the U.S. government or its agencies. These investments are held by the Lottery and are scheduled to mature near the time prize payments become payable to winners.

Credit Risk—is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. While the Lottery does not have a formal policy on its investments for prize annuities, it follows MUSL's policy requiring all investments for prize annuities to be in the form of securities backed by the full faith and credit of the U.S. government or its agencies, which are not considered to have credit risk. All of the Lottery's total investments for prize annuities balance as of June 30, 2019, and June 30, 2018, consist of these types of securities.

The State Investment Fund's shares classified as cash and cash equivalents are unrated. However, the State Investment Fund's investment guidelines establish specific maximum exposure limits by security type based on the minimum credit ratings as issued by nationally recognized statistical rating organizations.

Interest Rate Risk—is the risk that changes in interest rates will adversely affect the fair value of an investment or a deposit. Typically, this risk is higher in debt securities with longer maturities. The Lottery manages this risk by holding investments for prize annuities to maturity, at which time the fair value of the investment is equal to its stated maturity value. If an annuitant requests premature termination of an annuity that would necessitate an investment be redeemed prior to maturity, any loss or gain due to market fluctuations is passed through to the redeeming annuitant. Therefore, the Lottery has minimal interest rate risk exposure related to these investments, which consisted of U.S. Treasury and agency investments with the following maturities as of June 30, 2019, and June 30, 2018:

<u>Maturity</u>	<u>Fair Value as of June 30, 2019</u>	<u>Fair Value as of June 30, 2018</u>
Less than 1 year	\$ 3,878,588	\$ 4,520,223
1 to 5 years	9,466,928	12,279,830
6 to 10 years	1,305,973	1,606,153
More than 10 years	<u>526,543</u>	<u>577,044</u>
Total	<u>\$15,178,032</u>	<u>\$18,983,250</u>

The State Investment Fund uses the weighted average maturity method to analyze interest rate risk. Its investment guidelines mandate that the weighted average maturity for the entire portfolio not exceed one year. The weighted average maturity of the State Investment Fund was 16 days as of June 30, 2019, and 20 days as of June 30, 2018.

Fair Value Measurements—Lottery investments are reported at fair value as defined by GASB Statement Number 72—*Fair Value Measurement and Application* and are categorized based on the investment valuation hierarchy established by GASB.

The hierarchy is based on the valuation inputs used to measure the fair value of the assets:

- Level 1 inputs—are quoted prices in active markets for identical assets.
- Level 2 inputs—are significant other observable inputs.
- Level 3 inputs—are significant unobservable inputs.

The Lottery had the following recurring fair value measurements:

As of June 30, 2019

<u>Investments</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>NAV</u>
U.S. Government and Agency Securities	\$ 0	\$15,178,032	\$ 0	\$ 0
State Investment Fund	<u>0</u>	<u>0</u>	<u>0</u>	<u>57,222,000</u>
Total Investments at Fair Value	<u>\$ 0</u>	<u>\$15,178,032</u>	<u>\$ 0</u>	<u>\$57,222,000</u>

As of June 30, 2018

<u>Investments</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>NAV</u>
U.S. Government and Agency Securities	\$ 0	\$18,983,250	\$ 0	\$ 0
State Investment Fund	<u>0</u>	<u>0</u>	<u>0</u>	<u>50,451,000</u>
Total Investments at Fair Value	<u>\$ 0</u>	<u>\$18,983,250</u>	<u>\$ 0</u>	<u>\$50,451,000</u>

Debt securities are categorized as Level 2 and are valued by third-party pricing services using the matrix-pricing technique that values securities based on their relationship to quoted market prices for securities with similar interest rates, maturities, and credit ratings.

The fair value of investments in the State Investment Fund is based on net asset value (NAV) per share (or its equivalent) as of June 30, 2019. This is a commingled fund with the objective of safety of principal and liquidity while earning a competitive money market rate of return. The valuation of the underlying investments of the State Investment Fund depends on asset class and maturity date. Repurchase agreements and non-negotiable certificates of deposit are valued at cost. All other short-term debt investments with remaining maturities of up to 90 days are valued at amortized cost. Finally, all other short-term investments with remaining maturities of over 90 days are valued at fair value by third-party pricing services using a matrix-pricing technique. There are no unfunded commitments relating to the State Investment Fund, and shares of the State Investment Fund can be fully redeemed at any time with no notice or other restrictions. For more information on the investments in the State Investment Fund, review the separately issued *State Investment Fund Annual Financial Report* for the fiscal year ended June 30, 2019. The report is located at <https://www.swib.state.wi.us/publications>.

4. ACCOUNTS RECEIVABLE

Accounts receivable balances are disaggregated as follows:

	<u>June 30, 2019</u>	<u>June 30, 2018</u>
Accounts Receivable:		
Retailers:		
Ticket Sales and Contract Fees	\$46,931,398	\$45,478,947
Commissions and Incentives	(7,672,359)	(7,240,163)
Ticket Redemptions	(6,627,584)	(5,811,152)
Allowance for Returns	(2,289,957)	(3,970,576)
MUSL Receivable	583,591	0
Miscellaneous	<u>45,082</u>	<u>93,886</u>
Total Accounts Receivable	<u>\$30,970,171</u>	<u>\$28,550,942</u>
Due from Other State Programs:		
Transfers for Gaming	\$ 0	\$ 8,944
Total Due from Other State Programs	<u>\$ 0</u>	<u>\$ 8,944</u>

5. MULTI-STATE LOTTERY ASSOCIATION**A. Joint Venture Association**

The Lottery is a member of MUSL, a nonprofit, government-benefit voluntary association. As of June 30, 2019, MUSL had 38 member lotteries from 35 states, the District of Columbia, the U.S. Virgin Islands, and Puerto Rico. MUSL is owned and operated by the member lotteries, which sell one or more games administered by MUSL. It is controlled by its Board of Directors, consisting of the director or chief executive officer of each member lottery. Each MUSL member sells tickets through its licensed retailers and makes weekly wire transfers to MUSL in an amount equivalent to the member lottery's share of the weekly prize liability less the actual low-tier prize liability for tickets sold by the respective lottery. The Lottery participates in two multi-jurisdictional lotto games: Powerball and Mega Millions.

B. MUSL Financial Position and Activity

The following schedule presents the summarized audited financial position and activity of MUSL as of June 30, 2019, and June 30, 2018, as audited by other auditors.

	<u>June 30, 2019</u>	<u>June 30, 2018</u>
Total Assets	<u>\$507,711,452</u>	<u>\$486,935,976</u>
Total Liabilities	\$486,742,374	\$477,887,537
Total Unrestricted Net Assets	<u>20,969,078</u>	<u>9,048,439</u>
Total Liabilities and Net Assets	<u>\$507,711,452</u>	<u>\$486,935,976</u>
Total Revenues	\$ 18,637,167	\$ 10,421,784
Total Expenses	<u>(6,716,528)</u>	<u>(6,517,482)</u>
Increase (Decrease) in Unrestricted Net Assets	<u>\$ 11,920,639</u>	<u>\$ 3,904,302</u>

For a complete separate financial statements for MUSL, contact:

Multi-State Lottery Association
 Attention: Bret Toyne
 4400 NW Urbandale Drive
 Urbandale, Iowa 50322

C. Wisconsin Lottery's MUSL Balances

Lotteries participating in Powerball and Mega Millions transfer 50.0 percent of ticket sales, less actual low-tier prizes, to MUSL for prize pools and reserve accounts for each game.

Participating lotteries do not have rights to balances in the prize pool. Therefore, these funds are not reported as assets on the Lottery's financial statements. However, member lotteries have the right to a refund of their share of Prize Reserve Account balances if they withdraw from MUSL. The Lottery reports the total of its MUSL Prize Reserve Accounts as a restricted noncurrent asset (MUSL Reserve Accounts—Noncurrent).

In addition, the Lottery has an Unreserved Account, which accumulates interest. All administrative expenses are reduced from the Unreserved Account. Member lotteries may withdraw Unreserved Accounts at any time. The Lottery records its share of the balance of this account as an unrestricted current asset (MUSL Reserve Accounts—Current).

The total MUSL Reserve and Unreserved Account balances are made up of the following:

	<u>June 30, 2019</u>	<u>June 30, 2018</u>
Powerball Set Prize Reserve Account	\$1,234,715	\$1,175,095
Powerball Prize Reserve Account	2,696,327	2,763,145
Mega Millions Prize Reserve Account	2,671,400	1,735,023
Designated for Patent Acquisition	41,751	100,818
Unreserved Account	<u>287,241</u>	<u>310,975</u>
Total MUSL Accounts	<u>\$6,931,434</u>	<u>\$6,085,056</u>

In FY 2012-13, the Lottery designated \$396,313 of its Unreserved Account balance to pay MUSL for its allocated share of acquisitions costs related to a patent obtained by MUSL. Because these funds are reserved for a specific purpose, the Lottery recorded this amount as a restricted noncurrent asset (MUSL Reserve Accounts—Noncurrent). At the end of FY 2018-19, the Lottery’s remaining share of the cost was \$41,751.

6. EMPLOYEE RETIREMENT PLAN

The Lottery’s permanent employees are participants in the WRS, which is administered by the Wisconsin Department of Employee Trust Funds (ETF), under the direction of the ETF Board. The WRS is a cost-sharing multiple-employer defined benefit pension plan administered through a trust. WRS benefits, required contributions, and other plan provisions are established by ch. 40 of the Wisconsin Statutes. Eligible state and local government public employees are entitled to a retirement benefit based on the higher calculation of a formula benefit or a money purchase benefit. The formula benefit is calculated based on a formula factor, the employee’s final average earnings, and creditable service. The money purchase benefit is based on the employee’s contributions plus matching employer’s contributions, with interest.

Additional information about the WRS is included in the State of Wisconsin Comprehensive Annual Financial Report (CAFR), located at <https://doa.wi.gov/Pages/StateFinances/ComprehensiveAnnualFinancialReportCAFR.aspx>.

ETF also issues a standalone CAFR, located at <http://etf.wi.gov/publications/cafr.htm>.

Required contributions are determined by an annual actuarial valuation. The employee required contribution is one-half of the actuarially determined contribution rate for general category employees. Employers are required to contribute the remainder of the actuarially determined contribution rate. The employer may not pay the employee required

contribution unless provided for by an existing collective bargaining agreement. The WRS recognized employer contributions from the Lottery of \$273,921 for calendar year 2017 and \$282,401 for calendar year 2018.

As of June 30, 2019, the Lottery reported a net pension liability of \$982,623 for its proportionate share of the net pension liability, compared to the net pension asset of \$908,718 as of June 30, 2018. The net pension liability as of June 30, 2019, was measured as of December 31, 2018, and the total pension liability used to calculate the net pension liability (asset) was determined by an actuarial valuation as of December 31, 2017, rolled forward to December 31, 2018. No material changes in assumptions or benefit terms occurred between the actuarial valuation date and the measurement date. The Lottery's proportion of the net pension liability (asset) was based on the Lottery's share of contributions to the pension plan relative to the contributions of all participating employers. As of December 31, 2018, the Lottery's proportion was 0.03 percent, no change from the previous year.

The Lottery recognized pension expense reported in the Salaries and Fringe Benefits account of \$288,050 and \$290,996 for the fiscal years ended June 30, 2018, and June 30, 2019, respectively.

As of June 30, 2019, the Lottery reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

Deferred Outflows and Deferred Inflows of Resources Related to Pensions

Fiscal Year 2019	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences Between Expected and Actual Pension Experience	\$ 873,033	\$(1,418,454)
Change of Pension Assumptions	187,461	-
Net Differences Between Projected and Actual Earnings on Pension Plan Investments	1,435,054	-
Changes in Proportion and Differences Between Actual and Proportionate Share of Contributions	12,711	(9,477)
Pension Contributions Subsequent to the Measurement Date	<u>149,717</u>	<u>-</u>
Total	<u>\$2,657,976</u>	<u>\$(1,427,931)</u>
Fiscal Year 2018	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences Between Expected and Actual Pension Experience	\$1,150,784	\$(553,564)
Change of Pension Assumptions	184,034	-
Net Differences Between Projected and Actual Earnings on Pension Plan Investments	-	(1,248,948)
Changes in Proportion and Differences Between Actual and Proportionate Share of Contributions	19,335	(13,883)
Pension Contributions Subsequent to the Measurement Date	<u>148,904</u>	<u>-</u>
Total	<u>\$1,503,057</u>	<u>\$(1,816,395)</u>

7. POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS

Other postemployment benefits are benefits other than pensions that state and local governments provide to their retired employees. Under Wisconsin Statutes ch. 40, ETF and the Group Insurance Board (GIB) have statutory authority for program administration and oversight of postemployment benefits. ETF administers postemployment benefit plans other than pension plans for State employees, including the Retiree Life Insurance program and Retiree Health Insurance program (for retired State employees). Lottery employees are employees of the State.

Additional information on other postemployment benefits provided to state employees is included in the State of Wisconsin CAFR, located at <https://doa.wi.gov/Pages/StateFinances/ComprehensiveAnnualFinancialReportCAFR.aspx>.

ETF also issues a standalone CAFR, located at <http://etf.wi.gov/publications/cafr.htm>.

A. State Retiree Life Insurance Program

This program provides postemployment life insurance coverage to all eligible retired Lottery employees. The GIB approves contribution rates annually, based on recommendations from the insurance carrier. Recommended rates are based on an annual valuation, taking into consideration a present value estimate of future benefits and future contributions. A portion of employer contributions made during a member's working lifetime funds a post-retirement benefit. During the reporting period, the State Retiree Life Insurance Program recognized \$5,224 in contributions from the Lottery.

As of June 30, 2019, the Lottery reported a liability of \$513,945 for its proportionate share of the net OPEB liability compared to \$687,305 as of June 30, 2018. The net OPEB liability was measured as of December 31, 2018, and the total OPEB liability used to calculate the net OPEB liability was determined by an actuarial valuation as of January 1, 2018, rolled forward to December 31, 2018. No material changes in assumptions or benefit terms occurred between the actuarial valuation date and the measurement date. The Lottery's proportion of the net OPEB liability was based on its share of contributions to the OPEB plan relative to the contributions of all participating employers. As of December 31, 2018, the Lottery's proportion was 0.26 percent, which was a decrease of 0.03 percent from its proportion measured as of December 31, 2017.

The Lottery recognized OPEB expense for the Retiree Life Insurance Program reported in the Salaries and Fringe Benefits account of \$119,774 and \$46,366 for the fiscal years ended June 30, 2018, and June 30, 2019, respectively.

As of June 30, 2019, the Lottery reported deferred outflows of resources and deferred inflows of resources related to OPEBs from the following sources:

**Deferred Outflows and Deferred Inflows of Resources
Related to State Retiree Life Insurance**

Fiscal Year 2019	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences Between Expected and Actual Experience	\$ –	\$ (22,996)
Changes of Assumptions	48,288	(96,364)
Net Difference Between Projected and Actual Earnings on OPEB Plan Investments	10,912	–
Change in Proportionate Share	12,053	(5,996)
Employer’s Contribution Subsequent to the Measurement Date	<u>–</u>	<u>–</u>
Total	<u>\$71,253</u>	<u>\$(125,356)</u>
	Deferred Outflows of Resources	Deferred Inflows of Resources
	Deferred Outflows of Resources	Deferred Inflows of Resources
Fiscal Year 2018		
Differences Between Expected and Actual Experience	\$ –	\$(6,288)
Changes of Assumptions	58,526	–
Net Difference Between Projected and Actual Earnings on OPEB Plan Investments	6,598	–
Change in Proportionate Share	14,055	–
Employer’s Contribution Subsequent to the Measurement Date	<u>–</u>	<u>–</u>
Total	<u>\$79,179</u>	<u>\$(6,288)</u>

B. State Retiree Health Insurance Program

This program provides postemployment health insurance coverage to all eligible retired employees of the Lottery. Contribution requirements are established and may be amended by the GIB. Premiums for non-Medicare retirees are based on an effective rate structure for the health care service provider selected. Monthly rates range from \$537 to \$1,400 for single coverage and \$1,331 to \$3,495 for family coverage. The employers do not directly pay any portion of the premium for participating retirees.

To determine the total OPEB liability for the program, the actuary performed an actuarial valuation as of January 1, 2018, and adjusted for changes such as interest earned, contributions paid, and benefits paid through June 30, 2018. The actuarial valuation was based on the plan of retiree benefits and was made for purposes of fulfilling GASB accounting standards, which require recognition of the employer cost of postemployment benefits over an employee’s career. The total cost of providing postemployment benefits is projected, considering relevant

assumptions, then discounted to determine the total OPEB liability. As of June 30, 2019, the Lottery reported a liability of \$495,730 for its proportionate share of the total OPEB liability compared to \$764,582 as of June 30, 2018.

The Lottery recognized health OPEB expense reported in the Salaries and Fringe Benefits account of \$106,252 and \$91,553 for the fiscal years ended June 30, 2018, and June 30, 2019, respectively.

As of June 30, 2019, the Lottery reported deferred outflows of resources and deferred inflows of resources related to OPEBs from the following sources:

Deferred Outflows and Deferred Inflows of Resources Related to State Retiree Health Insurance		
Fiscal Year 2019	Deferred Outflows of <u>Resources</u>	Deferred Inflows of Resources
Differences Between Expected and Actual Experience	\$ 699	\$ (3,542)
Changes of Assumptions	–	(281,231)
Net Difference Between Projected and Actual Earnings on OPEB Plan Investments	–	–
Change in Proportionate Share	1,020	(8,453)
Employer's Contribution Subsequent to the Measurement Date	<u>37,570</u>	<u>–</u>
Total	<u>\$39,289</u>	<u>\$(293,226)</u>
Fiscal Year 2018	Deferred Outflows of <u>Resources</u>	Deferred Inflows of Resources
Differences Between Expected and Actual Experience	\$ –	\$ (3,920)
Changes of Assumptions	–	(105,573)
Net Difference Between Projected and Actual Earnings on OPEB Plan Investments	–	–
Change in Proportionate Share	–	(4,715)
Employer's Contribution Subsequent to the Measurement Date	<u>45,968</u>	<u>–</u>
Total	<u>\$45,968</u>	<u>\$(114,208)</u>

8. ANNUITY PRIZES PAYABLE

The Lottery has an unconditional obligation to pay all prize winners the future value of their prizes. The present value of future jackpot prize payment obligations is included in the financial statements as “Annuity Prizes Payable.” To finance the annuity prize payments, the Lottery purchases, or has acquired from MUSL, investments scheduled to mature near the time prize payments become payable to the winners. For information on the investments for prize annuities, see Note 3. Each year, an adjustment to the Annuity Prizes Payable account is made using the effective interest method. The amortization of annuity adjustment was \$952,821 for FY 2018-19 and \$1,223,138 for FY 2017-18.

Future prize payments and the present value of those payments are as follows:

<u>Fiscal Year Ended June 30</u>	<u>Future Payments as of June 30, 2019</u>
2020	\$ 4,116,098
2021	3,735,771
2022	2,739,037
2023	2,387,660
2024	1,050,649
Following Years	<u>2,228,233</u>
Total Future Prize Payments	16,257,448
Less: Present Value Adjustment	<u>(2,186,482)</u>
Present Value of Future Prize Payments	<u>\$14,070,966</u>

Annuity prizes payable activity for the fiscal years ended June 30, 2019, and June 30, 2018, was as follows:

<u>Fiscal Year</u>	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>	<u>Due within One Year</u>
2018-19	\$17,685,145	\$952,821	\$(4,567,000)	\$14,070,966	\$4,027,792
2017-18	22,040,006	1,223,138	(5,577,999)	17,685,145	4,447,435

9. INSTANT AND LOTTO TICKET SALES

Instant and lotto ticket sales shown on the financial statements consist of the following:

	<u>FY 2018-19</u>	<u>FY 2017-18</u>
Instant Ticket Sales:		
Scratch-off	\$450,364,292	\$419,398,240
Pull-tab	<u>978,975</u>	<u>1,036,575</u>
Total Instant Ticket Sales	<u>\$451,343,267</u>	<u>\$420,434,815</u>
Lotto Ticket Sales:		
SuperCash!	\$ 24,574,345	\$ 25,770,982
Powerball	84,789,329	98,231,031
Wisconsin's Megabucks	14,572,207	11,385,835
Wisconsin's Megabucks EZ Match	1,938,294	1,628,876
Daily Pick 3	23,575,461	23,867,808
Daily Pick 4	14,117,357	13,910,214
Badger 5	24,366,719	25,636,170
Mega Millions	63,320,243	39,472,858
5 Card Cash ¹	4,737,352	6,295,616
All or Nothing ¹	5,038,390	0
Raffle Games	766,260	765,210
General Sales and Discounts	<u>(6,450)</u>	<u>(6,995)</u>
Total Lotto Ticket Sales	<u>\$261,789,507</u>	<u>\$246,957,605</u>

¹ 5 Card Cash ended during FY 2018-19 and All or Nothing began during FY 2018-19.

10. INSTANT AND LOTTO PRIZE EXPENSE

Instant and lotto prize expenses shown on the financial statements consist of the following:

	<u>FY 2018-19</u>	<u>FY 2017-18</u>
Instant Prize Expense:		
Scratch-off	\$299,660,079	\$281,212,167
Pull-tab	613,439	650,016
Super 2nd Chance ¹	<u>259,000</u>	<u>259,500</u>
Total Instant Prize Expense	<u>\$300,532,518</u>	<u>\$282,121,683</u>
Lotto Prize Expense:		
SuperCash!	\$ 15,363,120	\$ 13,534,696
Powerball	41,283,657	47,575,988
Wisconsin's Megabucks	7,788,393	6,187,768
Wisconsin's Megabucks EZ Match	1,173,287	980,362
Daily Pick 3	10,925,780	11,180,800
Daily Pick 4	6,347,700	6,670,600
Badger 5	11,761,164	12,451,126
Mega Millions ²	30,822,356	19,427,601
5 Card Cash ²	2,536,942	3,685,851
All or Nothing	2,803,700	0
Raffle Games	348,230	371,000
Super 2nd Chance ¹	<u>259,000</u>	<u>259,500</u>
Total Lotto Prize Expense	<u>\$131,413,329</u>	<u>\$122,325,292</u>

¹ There are no sales for the Super 2nd Chance drawing. Players enter the drawing by submitting non-winning tickets. Prizes are funded from the original ticket sales.

² 5 Card Cash ended during FY 2018-19 and All or Nothing began during FY 2018-19.

11. CONTRACTUAL OBLIGATIONS**A. Scratch-off Tickets**

The Lottery completed a request for bid and awarded a contract for scratch-off ticket printing services to Scientific Games for the period November 1, 2015, through October 31, 2020, with the option to renew up to five additional one-year periods.

In addition, scratch-off ticket printing services are included in the lottery gaming system contract with IGT and any applicable subcontractor, which became effective on May 14, 2017. The contract term is for seven years with an option to renew for up to three additional one-year periods.

In addition, the Lottery purchased ticket printing services of approximately \$1.6 million in FY 2018-19 and approximately \$1.8 million in FY 2017-18.

B. Pull-tab Tickets

The Lottery entered into a two-year contract with Pollard Banknote Ltd. for pull-tab ticket printing services that expired on February 28, 2017, but included four one-year renewal options. The Lottery exercised its right to renew this contract, which now has an expiration date of February 28, 2020. This is the third of the four one-year renewals. The Lottery purchased approximately \$37,609 in ticket printing services for pull-tabs in FY 2018-19 compared to \$50,043 in FY 2017-18.

C. Gaming System Vendor

On February 16, 2016, the Lottery entered into a contract with IGT for an integrated gaming computer system, which was implemented on May 14, 2017. The initial term of this contract is for seven years from the operational start date. The contract requires the Lottery to pay IGT 2.57 percent of weekly net sales. In addition, the new contract includes the lottery gaming system, 70 percent of instant scratch-off ticket printing, warehousing, distribution, and telemarketing services. Net vendor service payments to IGT were approximately \$18.3 million in FY 2018-19 and approximately \$17.2 million in FY 2017-18.

D. Product Information Costs

The Lottery primarily contracts with HY Connect to provide informational advertising services. The Lottery signed a two-year contract with HY Connect starting July 12, 2015, through June 30, 2017, with an option to renew for four additional one-year periods. The Lottery exercised its right to renew this contract, which has an expiration date of June 30, 2020. Payments to HY Connect were approximately \$8.2 million during FY 2018-19 and \$8.3 million during FY 2017-18, while total spending on product information costs was approximately \$8.5 million during FY 2018-19 and FY 2017-18.

12. RESTRICTED NET POSITION

The Lottery reported net position invested in capital assets of \$141,552 as of June 30, 2019, and \$148,920 as of June 30, 2018.

The Lottery did not report restricted net position for pensions as of June 30, 2019, because it reported a net pension liability. As of June 30, 2018, Lottery reported \$908,718 as restricted net position for pensions because it reported a net pension asset. Restricted for pensions can be primarily attributed to adjustments required by governmental accounting standards for the WRS.

The Lottery also had a restricted net position related to MUSL reserves, as described in Note 5. The restricted net position related to the MUSL reserves was \$6,644,193 as of June 30, 2019, and \$5,774,081 as of June 30, 2018.

The Lottery also had a restricted net position for investment fair value adjustments of \$1,310,067 as of June 30, 2019, and \$1,494,105 as of June 30, 2018. The Lottery does not realize gains or losses from the change in fair value of its annuity investments because it holds the investments until maturity to pay the annual annuity prize payments. Therefore, fair value adjustments recognized as investment income and any cash held for annuity prize payments, are restricted and are not available for distribution as property tax credits.

Finally, the Wisconsin Constitution requires net proceeds from the operations of the Lottery to be used to provide local property tax relief. Balances from other gaming-related appropriations, including racing and charitable bingo operations, are transferred to the Lottery Fund for distribution in the form of property tax relief. The net proceeds and gaming-related transfers available for property tax relief make up the remainder of the restricted net position and were \$36,281,514 as of June 30, 2019, and \$36,333,481 as of June 30, 2018.

13. DISTRIBUTION OF NET PROCEEDS

Lottery net proceeds and other gaming-related proceeds were used for the Lottery and Gaming Tax Credit, as described in Note 2Q. The total Lottery and Gaming Tax Credit for FY 2018-19 was \$234,879,988 compared to \$170,255,138 for FY 2017-18.

14. TRANSFERS IN FROM GENERAL FUND

2017 Wisconsin Act 59 directed a transfer of \$40.0 million in FY 2018-19 and a transfer of \$8.0 million in FY 2017-18 of general purpose revenue from the General Fund to the Lottery Fund. These transfers were to be applied towards the Retailer Commissions and Incentives account.

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Supplementary Schedules ■

Statutorily Defined Lottery Administrative Expenses for the Years Ended June 30, 2019, June 30, 2018, and June 30, 2017

	Year Ended June 30, 2019	Restated Year Ended June 30, 2018	Restated Year Ended June 30, 2017
ADMINISTRATIVE EXPENSES			
Instant and Lotto Vendor Services	\$ 18,290,471	\$ 17,196,328	\$ 13,869,095
Product Information Costs	8,467,617	8,484,215	7,496,736
Instant Ticket Printing Costs	1,906,778	2,527,750	4,252,627
Instant Ticket Delivery Costs	0	0	784,499
Salaries and Fringe Benefits	5,663,494	5,466,208	7,074,319
Supplies and Services	4,809,574	2,568,434	2,505,689
Depreciation Expense	28,862	29,224	27,458
Transfers Out—Department of Health and Family Services for Compulsive Gambling Programs	396,000	396,000	396,000
Transfers Out—Department of Revenue for Lottery Credit Administration	224,430	226,065	179,664
Transfers Out—General Fund	399,270	126,588	151,526
Total Administrative Expenses as Determined in Accordance with s. 25.75 (3) (b), Wis. Stats.	<u>\$ 40,186,496</u>	<u>\$ 37,020,812</u>	<u>\$ 36,737,613</u>
Gross Lottery Revenues per s. 25.75 (1) (b), Wis. Stats.	\$ 713,189,448	\$ 667,452,910	\$ 602,810,672
Administrative Expenses as a Percentage of Gross Lottery Revenues	5.63%	5.55%	6.09%

Section 25.75 (3) (b), Wis. Stats., limits the Wisconsin Lottery's administrative expenses to 10 percent of gross lottery revenues. Gross lottery revenues, as defined in s. 25.75 (1) (b), Wis. Stats., include lottery ticket sales and retailer fees. Administrative expenses, as defined in s. 25.75 (3) (b), Wis. Stats., do not include retailer commissions and incentives and transfers to the Department of Justice for law enforcement.

Note: The above amounts are based on the accrual basis of accounting.

Summary of Prize Expenses for the Years Ended June 30, 2015, through June 30, 2019

Section 25.75 (3) (a), Wis. Stats., requires that at least 50 percent of each year's revenues from the sale of lottery tickets be returned as prizes to the holders of winning lottery tickets. The amounts expended for winning lottery tickets for the past five years, for both instant and online games, are summarized below.

Fiscal Year 2018-19			
	Prize Expense	Ticket Sales	Prize Expense as a Percentage of Sales
Instant Games	\$ 300,532,518	\$ 451,343,267	66.6%
Lotto Games	131,413,329	261,789,507	50.2
Total for Fiscal Year	\$ 431,945,847	\$ 713,132,774	60.6

Fiscal Year 2017-18			
	Prize Expense	Ticket Sales	Prize Expense as a Percentage of Sales
Instant Games	\$ 282,121,683	\$ 420,434,815	67.1%
Lotto Games	122,325,292	246,957,605	49.5
Total for Fiscal Year	\$ 404,446,975	\$ 667,392,420	60.6

Fiscal Year 2016-17			
	Prize Expense	Ticket Sales	Prize Expense as a Percentage of Sales
Instant Games	\$ 255,812,830	\$ 385,866,619	66.3%
Lotto Games	107,152,950	216,906,158	49.4
Total for Fiscal Year	\$ 362,965,780	\$ 602,772,777	60.2

Fiscal Year 2015-16			
	Prize Expense	Ticket Sales	Prize Expense as a Percentage of Sales
Instant Games	\$ 249,991,398	\$ 379,930,973	65.8%
Lotto Games	122,567,099	247,233,964	49.6
Total for Fiscal Year	\$ 372,558,497	\$ 627,164,937	59.4

Fiscal Year 2014-15			
	Prize Expense	Ticket Sales	Prize Expense as a Percentage of Sales
Instant Games	\$ 236,549,274	\$ 357,463,506	66.2%
Lotto Games	105,892,045	217,167,877	48.8
Total for Fiscal Year	\$ 342,441,319	\$ 574,631,383	59.6

NOTE: The above amounts are based on the accrual basis of accounting, with adjustments made to prize expense for unclaimed winning tickets and reserve accounts. For each game, the prize structure represents the number, value, and odds of winning for each prize and is used to estimate the expected amounts to be paid to lottery winners. The games' actual prizes (prize expense) may be less than the games' structure because of unclaimed winning tickets and deposits in reserve accounts.

Auditor's Report ■



Report 20-4

Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee

Mr. Peter Barca, Secretary
Department of Revenue

Ms. Cindy Polzin, Administrator
Division of Lottery
Department of Revenue

We have audited the financial statements and the related notes of the Wisconsin Lottery as of and for the years ended June 30, 2019, and June 30, 2018, and have issued our report thereon dated April 23, 2020. 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*, which is issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

Management of the Department of Revenue and the Wisconsin Lottery are responsible for establishing and maintaining effective internal control over financial reporting (internal control). In planning and performing our audits of the financial statements, we considered the Department of Revenue's and Wisconsin Lottery's internal control to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Department of Revenue's and Wisconsin Lottery's internal control. Accordingly, we do not express an opinion on the effectiveness of the Department of Revenue's and Wisconsin Lottery's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent misstatements, or to detect and correct misstatements on a timely basis. *A material weakness* is a deficiency or a combination of deficiencies in internal control such that there is a reasonable possibility that a material misstatement of the Wisconsin Lottery financial

statements will not be prevented, or that a material misstatement will not be detected and corrected on a timely basis. A *significant deficiency* is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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

Compliance and Other Matters

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

Purpose of This Report

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

LEGISLATIVE AUDIT BUREAU



Joe Chrisman
State Auditor

April 23, 2020