

ANNUAL REPORT



THE REAL



WINNERS



OF



2002

NEW JERSEY
LOTTERY



LETTER FROM THE ACTING EXECUTIVE DIRECTOR



Dear Friends,

Each time a Lottery ticket is purchased in our state, it means a hearing-impaired child is ensured of a quality education or adults with special needs are getting the support and guidance they need to live fulfilling and productive lives. In Fiscal Year 2002, the Lottery contributed more than \$754 million, or 36 cents of every dollar earned to support State Education and Institutions, like the Marie Katzenbach School for the Deaf and various centers for the developmentally disabled.

As one of the most cost-efficient lotteries in the country, the New Jersey Lottery spends just 1% of its revenues to operate and promote its business. In Fiscal Year 2002 the Lottery had more than \$2 billion in sales. Since its inception in 1970, the Lottery has generated over \$12.3 billion to help fund a myriad of educational and human service programs in New Jersey, including community colleges, veterans homes and the Governor's School.

But clearly we would not be able to achieve these great heights without the partnership of more than 6,000 retailers. Their continued efforts on the Lottery's behalf has helped us become the state's fourth largest revenue producer. These retailers earned commissions in excess of \$113 million - the highest in the 31-year history of the Lottery.

New Jersey Lottery players were among the most successful in the country in FY 2002. More than 79 million players took home over \$1.1 billion in cash and prizes - one of the highest winning percentages for any lottery in the United States.

The New Jersey Lottery prides itself in the important role it plays in making a difference in the lives of "The Real Winners of 2002" - the people of New Jersey. Together we can make an even greater impact in 2003.

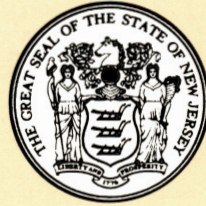
Sincerely,

A handwritten signature in black ink that reads "Carole Hedinger". The signature is written in a cursive, flowing style.

Carole Hedinger
Acting Executive Director

NEW JERSEY LOTTERY *has touched*
the entire state with contributions
to EDUCATION *and* INSTITUTIONS.

LETTER FROM THE GOVERNOR



Dear Friends,

Thank you for your dedication and support, which enabled the New Jersey Lottery to exceed all goals in 2002 and achieve its first \$2 billion sales year.

Through the leadership and professionalism provided by the Lottery Commissioners as well as the agency's staff and retailer network, the New Jersey Lottery returned more than \$1.1 billion to players in cash and prizes to 79 million lottery winners last year.

Most importantly, the Lottery contributed over \$754 million in funding for educational programs and State institutions. This revenue provides continued support for programs such as the Governor's School, county colleges, higher education, Centers for the Developmentally Disabled, Veterans' Memorial Homes and the Marie Katzenbach School for the Deaf.

In addition, members of the Lottery retailer network, which is primarily comprised of small businesses, earned \$113 million in commissions.

Last year's success continues a long tradition of excellence by the New Jersey Lottery. Since its inception 32 years ago, the Lottery has contributed more than \$12.3 billion to programs that bring positive change to the lives of countless Garden State residents.

Once again, congratulations to all of those who have contributed to this outstanding record of service. We look forward to continued success in 2003 for the New Jersey Lottery.

With all good wishes,

A handwritten signature in black ink that reads "James E. McGreevey". The signature is stylized and includes a large flourish at the end.

James E. McGreevey
Governor, State of New Jersey

New Jersey State Lottery



LETTER FROM THE TREASURER



Dear Friends,

For more than 32 years, the New Jersey Lottery has fulfilled its mission as a source of funding for educational programs and state institutions. Fiscal 2002, though, was a banner year for the Lottery. For the first time since its inception, the New Jersey Lottery amassed over \$2 billion in sales, securing a place among the most successful and efficient state lotteries in the country.

More importantly, the record sales allowed a contribution of more than \$754 million to the State Treasury. That total equates to 36 cents out of every dollar earned directly benefiting those causes that derive funding from the Lottery. The result has been a substantial savings for state taxpayers. The Lottery is currently the fourth largest revenue producer in New Jersey and provides the highest rate of return to the state of any lottery in the nation.

It is my pleasure to join in presenting this Annual Report to the people of New Jersey. Once again, the Lottery has helped make our state a better place in which to live, work and play.

Congratulations on a tremendous year.

Sincerely,

A handwritten signature in black ink that reads "John E. McCormac".

John E. McCormac, CPA
State Treasurer



WHERE THE MONEY GOES

STATE OF NEW JERSEY
PROGRAMS SUPPORTED BY STATE LOTTERY RESOURCES
FOR THE FISCAL YEAR ENDED JUNE 30, 2002
(Amounts expressed in thousands)

	Amount Expended and or Encumbered (a)
DEPARTMENT OF AGRICULTURE	
SCHOOL NUTRITION	\$ 4,907
DEPARTMENT OF EDUCATION	
GOVERNOR'S SCHOOL	988
MARIE KATZENBACH SCHOOL FOR THE DEAF	3,150
NON-PUBLIC SCHOOL AID	47,681
STATEWIDE ASSESSMENT PROGRAM (GRADES 4,8,11)	10,676
TOTAL DEPARTMENT OF EDUCATION	<u>62,495</u>
HIGHER EDUCATIONAL SERVICES	
SENIOR PUBLIC INSTITUTIONS-OPERATING AID	130,282
TUITION AND GRANTS	91,870
EXCELLENCE IN HIGH TECHNOLOGY WORKFORCE	8,431
HIGHER EDUCATION CAPITAL IMPROVEMENT PLAN-DEBT SERVICE	7,144
OUTSTANDING SCHOLAR RECRUITMENT PROGRAM	6,626
UNIVERSITY RESEARCH IN TECHNOLOGY	4,657
AID TO COUNTY COLLEGES FOR OPERATIONAL COSTS	115,381
AID TO INDEPENDENT COLLEGES AND UNIVERSITIES	10,047
COORDINATED GARDEN STATE SCHOLARSHIP PROGRAM	3,995
HIGHER EDUCATION FACILITIES TRUST FUND - DEBT SERVICE	11,640
HIGHER EDUCATION FOR SPECIAL NEEDS STUDENTS	587
OPPORTUNITY PROGRAM GRANTS	12,339
SUPPLEMENTARY EDUCATION PROGRAM GRANTS	6,412
VETERINARY MEDICINE EDUCATION	795
TOTAL HIGHER EDUCATIONAL SERVICES	<u>410,206</u>
DEPARTMENT OF HUMAN SERVICES	
OPERATION OF CENTERS FOR DEVELOPMENTALLY DISABLED	111,568
OPERATION OF STATE PSYCHIATRIC HOSPITALS	137,259
TOTAL DEPARTMENT OF HUMAN SERVICES	<u>248,827</u>
DEPARTMENT OF MILITARY AND VETERANS AFFAIRS	
OPERATION OF HOMES FOR DISABLED SOLDIERS	<u>28,115</u>
TOTAL REVENUE REALIZED - GAAP BASIS	<u>\$ 754,550</u>

(a) The amount of State Lottery funding in the programs designated above may only represent a portion of its total state funding. Any Balance of the appropriation would be funded by the General Fund.

John E. McCormac, CPA
State Treasurer

For more than thirty years, the Lottery has been coming face to face with New Jersey's needs, helping improve the lives of countless Garden State residents.

In FY '02, the Lottery returned 36 cents of every dollar to benefit education and institutions, while again earning the distinction as the most state supportive lottery in North America.

That translated into more than \$754 million - an 8% increase over last year - to support Community Colleges, School Nutrition, the Governor's School Program, the Department of Human Services, the Department of Military and Veterans Affairs and other such programs.

The Lottery had a \$2 billion record sales year - a 14% increase over last year. As the state's fourth largest revenue producer, the Lottery spent just 1% of its gross revenue on administrative costs, and is ranked as one of the most cost-efficient lotteries in the industry.

The Lottery is indebted to its retailer network for its record-breaking sales year. As a result of their hard work, in FY '02 over 6,000 lottery retailers earned commissions in excess of \$113 million - the highest of any year on record.

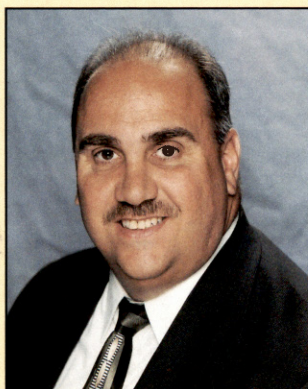
Our players still remained our biggest winners. In FY '02, the Lottery saw more than 79 million winners take home over \$1.14 billion in cash and prizes - one of the highest winning percentages for any lottery in the United States.

Aside from helping thousands of Garden State players see their lottery dreams come true, the Lottery has demonstrated that some of its biggest winners don't even play! The New Jersey Lottery is proud to have remained committed to its "Real Winners" - the people of the Great State of New Jersey.

NEW JERSEY STATE LOTTERY COMMISSION



Daniel F. Becht, Esq.
Commissioner



Robert James D'Anton
Chairman



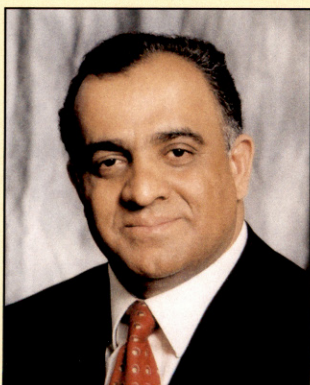
Robert Slater
Commissioner



John E. McCormac, CPA
Treasurer



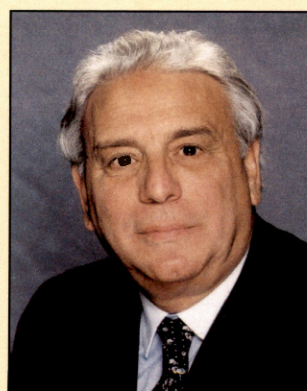
Carole Hedinger
Acting Executive Director



Dr. Munir Kazmir
Commissioner

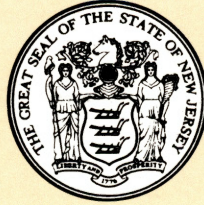


Dr. Stephen T. Boswell
Vice-Chairman



Dr. Anthony R. Caputo
Commissioner

LETTER FROM THE CHAIRMAN



Dear Friends,

As Chairman of the New Jersey State Lottery Commission, I am pleased to report that, as it enters its 33rd year of operation, the New Jersey Lottery is stronger than ever.

To understand the significant strides the New Jersey Lottery has made over the past three decades, consider that it began with a single weekly 50-cent game. Today, the Lottery offers its players six different computerized games and over 50 instant games a year, all of which led to this year's record sales.

What's more, our Lottery's commitment to beneficiaries and players alike is exemplified by its ranking as one of the most efficiently run lotteries in North America for seven straight years.

I know I speak for my fellow Commissioners when I thank Governor McGreevey for the opportunity to serve as a member of the board of an organization that contributes so significantly to New Jersey's educational system and institutions. And, we are grateful for the opportunity to do even more for New Jersey in the coming year.

On behalf of the entire New Jersey State Lottery Commission, thank you for supporting the New Jersey Lottery and its beneficiaries.

Sincerely,

A handwritten signature in black ink, appearing to read 'Robert James D'Anton'.

Robert James D'Anton

Chairman

IN FY '02 *New Jersey Lottery*
contributed over **\$28 MILLION**
in aid to Homes for Disabled Soliders.



NEW JERSEY LOTTERY BREAKS SALES RECORDS

On July 22, 2002, the New Jersey Lottery announced that it had generated approximately \$2.07 Billion in sales in Fiscal Year 2002. This figure represents the highest revenue total in the Lottery's 32-year history and makes it one of only seven lotteries in the United States to reach that level of sales.

In fact, a recent study by the trade publication, "International Gaming & Wagering Business" named New Jersey Lottery as one of only two states consistently ranking in the top 10 for measures of effectiveness and efficiency. New Jersey Lottery is ranked #1 for spending the least to generate its government contribution and second for spending least to generate a sales dollar.

The New Jersey Lottery spends just 1% of its revenues to operate and promote its business and has the highest rate of overall return to the state of any state lottery. Last year that amount was up by 8% to \$754 million, allowing Lottery to continue as New Jersey's fourth largest revenue producer. Our return to players and retailers reached record numbers as well with \$1.14 billion in prize money and \$113.4 million in commissions.

NEW JERSEY LOTTERY *promotes responsible play, including 1-800-GAMBLER® on all products and publications.*

LOTTERY LAUNCHES VIP CLUB



This Lottery's success is a reflection of a long-term customer related marketing strategy that began with a daily winning number email service. This service evolved in January 2002 into the first lottery loyalty program - the VIP CLUB. Customers register via the Internet to receive daily emails on game results as well as new games and promotions and are automatically entered into drawings for trips and prizes. The VIP Club is an inexpensive and effective way to communicate with and market to our valuable loyal customers. Currently, 44,000 players have registered for the services provided by the VIP Club.

BIG GAME BECOMES MEGA MILLIONS



Photo Credit - D. Hulshizer, Associated Press

Jorge and Joanne Lopes of Englishtown, NJ leave the podium at a news conference held in Trenton, NJ on Tuesday, April 30, 2002, with a ceremonial check for \$58.9 million, their winning share of the BIG GAME lottery drawing held on April 16, 2002.

On May 15, 2002, the New Jersey Lottery debuted its newest multi-state, mega jackpot game - Mega Millions. With the help of the historic battleship USS New Jersey, the game was branded as a New Jersey favorite, and the ship's size reflected the bigger prizes players could win. Specifically, players now had a chance to win an average jackpot of \$80 million with the potential to reach over \$500 million!

New Jersey again enjoyed tremendous success participating in BG/MM. For the 4th year in a row, New Jersey amassed over \$293 million to lead all member states in sales; created over \$14 million in commissions for its retailer network; while at the same time awarding over \$147 million in prizes - including 4 top prize winners! Most importantly, in FY '02 New Jersey's participation in the BG/MM resulted in \$124 million generated for education and institutions.

Perhaps the most memorable moment was in April 2002 when the BG/MM jackpot caught the attention of the nation as it grew to \$331 million. On April 16, 2002, after 20 draws without a winner, three winning tickets were drawn - one each from New Jersey, Georgia and Illinois. As all of New Jersey waited for the identity of its newest mega-millionaire, the Lottery worked to solve the mystery.

Shortly after the drawing, the Lottery was contacted by two attorneys each claiming to represent the legitimate ticketholders. To ensure the rightful ticketholder was awarded the prize the Lottery launched an investigation to determine the winner. After careful review and consideration, the Lottery announced the genuine ticketholders had been identified and on April 30, 2002 introduced Jorge and Joann Lopes of Englishtown, NJ as the Garden State's newest multi-millionaires!



To win the Mega Millions jackpot, players must match five numbers from a pool of 51, plus the "Gold Mega Ball," also from a pool of 51. Including New Jersey, the other member states are: Georgia, Illinois, Maryland, Massachusetts, Michigan, New York, Ohio, Virginia and Washington.



New Jersey Lottery Drawing Personalities Renai Ellison and Carmen Delia Torres on the Battleship NJ.

PICK-3, PICK-4, JERSEY CASH 5 AND LOTZEE



Pick-3 and Pick-4 experienced lagging sales prior to FY '01 when the NJ Lottery took steps to turn these core games around. On November 11, 2001, the Lottery introduced "Midday Draw" for Pick-3 and Pick-4. This game expansion allows players the chance to play and win their favorite games twice a day, every day. Midday Draw produced combined sales increases in these core games of \$30.5 million. Pick-3 and Pick-4 remains a solid favorite among NJ Lottery's player base, accounting for 34% of total sales and returning \$356 million to players and \$300 million to NJ education and institutions.



Previously drawn every weekday, Jersey Cash 5 players can now win the big money every day. In October 2001, the New Jersey Lottery increased the frequency of Jersey Cash 5 to 7 days a week. The event was kicked off with a month long "Double Cash Weekends" promotion, where all prizes on weekend tickets were doubled. The promotion resulted in the desired level of player awareness and an 11% increase in the total sales of \$75 million.

The online ticket that plays like an Instant offers players multiple ways to win on every ticket, while allowing players to select their own lucky numbers. The relatively new game first launched in 1998, was given a refresh in March 2002 and finished the year with over \$23 million in sales. The top LOTZEE prize remains \$500,000, but the matrix was reduced which responded to players request for a "less confusing" play. The relaunch included a couponing effort in conjunction with the new internet VIP CLUB.

In Fiscal Year 2002, 79 MILLION

New Jersey Lottery players shared an unprecedented \$1.1 BILLION in prizes!

PICK-6 AND INSTANTS



New Jersey's Pick 6 Lotto game, which made its first millionaire in 1981, continues as one of the Lottery's most popular online games. With sales totaling over \$189 million, and returns to the state equaling \$68 million, the Pick 6 Lotto once again established itself as one of the Lottery's premier games.

In June 2002, the Pick 6 Lotto came close to making history when John and Myrtle Connell from Clifton, NJ won \$45.8 million - the third largest jackpot in Pick 6 Lotto history.

As one of the first six digit games in the industry, New Jersey's Pick 6 Lotto has continually produced a high level of return and evolved to maintain player interest.

Since its inception, the Pick 6 Lotto has generated \$6.9 billion in sales, paid out \$3.4 billion to winners and returned more than \$1.65 billion to state education and institutions.

Fiscal Year 2002 saw the introduction of fifty-two new Instant Games ranging in price from \$1 to \$10 and offering a variety of cash prizes together with unique merchandise and travel prizes. Core games like "Win for Life", "Crossword" and "Classic Bingo" continue to have a loyal player base. Holiday Gift Packs once again proved a favorite in the 2nd Quarter.

The addition of the Lottery VIP Club, (an internet preferred customer feature) with its Lottery Bonus Zone, offers players "second chance drawings" to win merchandise and travel prizes.

Instant Game Sales grew to over \$773 , representing a 14% increase over the previous year. From season to season, Instant Games continue to play a vital role in generating funding for state programs and Lottery sales



MANAGEMENT'S DISCUSSION AND ANALYSIS

FISCAL YEAR 2002

INTRODUCTION:

The following discussion and analysis provides an analytical overview of the financial position and activities of the New Jersey State Lottery (The Lottery) for the year ended June 30, 2002. This statement was prepared by management and should be read in conjunction with the financial statements and notes here to, which follow this section.

The Lottery was established in 1970 pursuant to the "State Lottery Law," N.J.S.A. 5:9-1, et seq. The Lottery operates within the Department of Treasury of the State of New Jersey. The New Jersey Lottery Commission is a seven member board, appointed by the Governor, authorized and empowered to promulgate rules and regulations in the operation of the Lottery. The "State Lottery Law" also mandates that a minimum of 30 % of gross revenues from ticket sales be allocated for Contribution to Education and State Institutions.

The Lottery licenses over 6,000 retailers throughout the State of New Jersey to act as agents in the sale of New Jersey Lottery tickets. Lottery retailers receive compensation in the form of commissions on each ticket sold or validated. The Lottery also contracts with various ticket vendors in the production, distribution and management of lottery products.

- > Gtech Corporation is contracted to provide ticket sales through the on-line terminal network and the warehousing and distribution of instant tickets and promotional materials.
- > Creative Games, Pollard Bank Note and Scientific Games, are contracted to print and support instant game products.
- > Verizon Communications is contracted to provide digital communication between the Lottery's 6,000 sales terminals and the Gtech data center.

The Lottery offers various products for sale with prize awards ranging from \$2.00 to Annuity prizes excess of \$100 million. The various products sold are:

- > Instant Games
- > Pick 3
- > Pick 4
- > Jersey Cash 5
- > Pick 6 Lotto
- > Lotzee
- > The Big Game / Mega Millions

FINANCIAL HIGHLIGHTS:

The Lottery's financial position at June 30, 2002 consisted of total assets of \$1.242 billion and total liabilities of \$1.213 billion. A substantial portion of the asset and liability numbers is due to the Lottery's annuity investment in prize awards. The total invested and due to Lottery winners as future installment payments at June 30, 2002 was \$1.110 billion. Net assets increased \$21 million from the prior fiscal year as a result of it's operating and non-operating activities, which are summarized as follows (in millions):

	<u>FY '02</u>	<u>FY '01</u>
Total operating revenue	\$2,098	\$1,838
Total operating expense	<u>1,326</u>	<u>1,150</u>
Operating Income	772	688
Non-operating revenue	<u>3</u>	<u>6</u>
Income before transfers	775	694
Operating transfers out	<u>754</u>	<u>697</u>
Net inc. (dec.) in net assets	<u>\$ 21</u>	<u>\$ (3)</u>

The \$21 million increase in net assets is a result of the unclaimed prize awards, which are restricted to fund either future prizes or state contributions.

FINANCIAL STATEMENTS:

The Lottery's financial statements include a Statement of Net Assets as of June 30, 2002, a Statement of Revenues, Expenses and Changes in Net Assets for Fiscal Year June 30, 2002, and a Statement of Cash Flows for Fiscal Year ended June 30, 2002. The financial statements are prepared in accordance with the accounting principles established by the Governmental Accounting Standards Board (GASB).

Summary of Net Assets:

The statement of net assets presents the Lottery's financial position as of the last day of the fiscal year. The Lottery's assets, liabilities and net assets are summarized as follows (in millions):

	<u>FY '02</u>	<u>FY '01</u>
Current Assets	\$ 297	\$ 321
Long Term Annuity Investments	<u>945</u>	<u>1,005</u>
Total Assets	1,242	1,326
Current Liabilities	267	312
Non-current Liabilities	<u>946</u>	<u>1,006</u>
Total Liabilities	<u>1,213</u>	<u>1,318</u>
Restricted Net Assets	26	8
Unrestricted Net Assets	<u>3</u>	<u>-</u>
Total Net Assets	<u>\$ 29</u>	<u>\$ 8</u>

Current assets consist of cash and cash equivalents, investment in the State of New Jersey Cash Management Fund, accounts receivable, current year annuity investments and prepaid expenses. The investment in the State Cash Management Fund totaled \$99 million at June 30, 2002.

The Lottery funds long term installment prizes with insurance company annuities and United States Treasury securities. The total value of these investments at June 30, 2002 was \$1.11 billion. The Lottery has annuity investments with thirteen (13) insurance companies. The total market value of the United States Treasury securities as of June 30, 2002 was \$25.6 million. The annuity prizes due in fiscal years 2004 and beyond totaled \$945 million and represented the non-current assets reported on the Lottery's Statement of Net Assets.

Current liabilities consist of unpaid prizes awards, accounts payable and outstanding contribution due to the State of New Jersey General Fund. The total unpaid prizes due and payable as of June 30, 2002 totaled \$59 million. There is also \$166 million due to annuity winners in the fiscal year 2003.

Non current liabilities represent annuity prizes due in fiscal years 2004 and beyond and the total due for unused vacation and sick leave.

Net assets represent the excess of the Lottery's assets over its liabilities and are summarized as follows (in millions):

	<u>FY '02</u>	<u>FY '01</u>
Restricted (Expired Prize Awards)	\$ 26	\$ 8
Unrestricted	<u>3</u>	<u>-</u>
Total Net Assets	<u>\$ 29</u>	<u>\$ 8</u>

Expired prizes are restricted to fund either future prizes or state contributions.

MANAGEMENT'S DISCUSSION AND ANALYSIS
FISCAL YEAR 2002

Summary of Revenues, Expenses and Changes in Net Assets:

The results of the Lottery's operations are presented in the Statement of Revenues, Expenses and Changes in Net Assets, which is summarized (in Millions) as follows for the year ended June 30, 2002:

	<u>FY '02</u>	<u>FY '01</u>
Ticket Sales	\$2,068	\$1,807
Forfeited Prizes	29	29
Miscellaneous Income	<u>1</u>	<u>2</u>
Total Operating Revenue	2,098	1,838
Prize Awards	1,145	995
Administrative Expenses	23	18
Agent Commissions	113	99
Vendor Fees	38	31
Network Fees	<u>7</u>	<u>7</u>
Total Operating Expenses	<u>1,326</u>	<u>1,150</u>
Operating Income	772	688
Investment Interest Income	<u>3</u>	<u>6</u>
Income Before Transfers	775	694
Operating Transfers - State Contribution	<u>754</u>	<u>697</u>
Increase (Decrease) in Net Assets	<u>\$ 21</u>	<u>\$ (3)</u>

The Lottery awarded over \$1.144 billion in prize awards in fiscal year 2002. Over 79 million winning tickets were validated and paid. The highlight was the Big Game drawing of April 16, 2002 when a New Jersey ticket was one of three top tier winning tickets to share in a \$330 million jackpot. Each winning ticket was entitled to an annuity prize of \$110 million.

Lottery vendors provided critical services to the The Lottery in fiscal Year 2002. Their services included the production, warehousing, distribution and accounting for all lottery tickets. The total compensation paid for lottery vendors and network fees, in fiscal year 2002 was \$44.9 million.

The Lottery's administrative expenses for the fiscal year 2002 totaled \$22.7. These administrative expenses include salaries, advertising, auditing services, rent, security, data processing services, office supplies and attorney general fees.

The Lottery is required by State of New Jersey law to contribute at least 30 % of total revenue to the State of New Jersey for Education and State Institutions. The fiscal year 2002 original budget projection was for the Lottery to contribute \$747 million. As a result of various sales initiatives, game enhancements and efficient operations, The Lottery contributed over \$754 million, 35.9% of total revenue.

SUMMARY AND OUTLOOK:

The Lottery continues its position as a major revenue source for the State of New Jersey. Lottery revenue funds various educational and institutional programs throughout the state.

Lottery management will continue to monitor its product mix to maintain player interest. Various programs such as "double draw", "double payout" and "free play coupons" have proven to be successful in maintaining this interest. Management will also monitor prize payout percentages and drawing odds in order to achieve an effective mix, which will be both beneficial to players and state contributions.

INDEPENDENT AUDITORS' REPORT



Princeton Pike Corporate Center
P.O. Box 7348
Princeton, NJ 08543-7348

Commissioners of the New Jersey State Lottery Commission:

We have audited the accompanying basic financial statements of the New Jersey State Lottery Commission (the "Commission"), as of and for the years ended June 30, 2002 and 2001, as listed in the accompanying table of contents. These financial statements are the responsibility of the Commission's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

As discussed in note 1, the financial statements present only the Commission and do not purport to, and do not, present fairly the financial position of the State of New Jersey as of June 30, 2002 and 2001, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the New Jersey State Lottery Commission as of June 30, 2002 and 2001, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in note 1, the Commission adopted Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended by GASB Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, as of July 1, 2001.

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

The combined statements of revenues expenses and changes in net assets for the cumulative 354 months ended June 30, 2000, and the cumulative 378 months ended June 30, 2002, were not audited by us and accordingly, we do not express an opinion on them.

KPMG LLP

September 30, 2002

STATEMENTS OF NET ASSETS

JUNE 30, 2002 AND 2001

	FISCAL YEAR 2002	FISCAL YEAR 2001
ASSETS		
Current Assets:		
Cash	\$ 513,748	\$ 1,411,250
Accounts Receivable, Net	19,519,004	15,698,463
Other Assets	12,412,233	9,942,911
Investments:		
Deposit Fund Contracts	165,708,704	166,702,004
State Of New Jersey Cash Management Fund	99,284,467	127,522,317
Total Current Assets	297,438,156	321,276,945
Non Current Assets:		
Investments:		
Deposit Fund Contracts	944,904,514	1,004,952,136
Total Non Current Assets	944,904,514	1,004,952,136
Total Assets	1,242,342,670	1,326,229,081
LIABILITIES		
Current Liabilities:		
Accounts Payable and Accrued Expenses	26,819,156	20,958,591
Obligation for Unpaid Prize Awards	59,359,092	47,252,192
Current Year Installment Prize Awards	165,708,704	166,702,004
Due To State Of New Jersey - Education	15,549,833	77,397,293
Total Current Liabilities	267,436,785	312,310,080
Non Current Liabilities:		
Compensated Absences	872,089	818,951
Installment Prize Awards	944,904,514	1,004,952,136
Total Non Current Liabilities	945,776,603	1,005,771,087
Total Liabilities	1,213,213,388	1,318,081,167
NET ASSETS		
Unrestricted	2,771,534	(327,267)
Restricted	26,357,748	8,475,181
Total Net Assets	\$ 29,129,282	\$ 8,147,914



New Jersey
Lottery

COMPARATIVE STATEMENTS

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

	Cumulative 354 Months *Ended June 30, 2000	12 Months Ended June 30, 2001	12 Months Ended June 30, 2002	Cumulative 378 Months *Ended June 30, 2002	%
REVENUES:					
Gross Sales	\$ 26,123,127,413	\$ 1,806,694,611	\$ 2,068,506,868	\$ 29,998,328,892	98.78%
Forfeited Prizes	299,752,544	28,611,726	28,842,236	357,206,506	1.18%
Miscellaneous Income	9,164,858	2,484,374	904,236	12,553,468	0.04%
Total Operating Revenue	26,432,044,815	1,837,790,711	2,098,253,340	30,368,088,866	100.00%
EXPENDITURES:					
Prize Expense	13,307,383,151	994,764,296	1,144,736,660	15,446,884,107	50.87%
Commission to Agents & Banks	1,425,968,466	99,305,191	113,440,214	1,638,713,871	5.40%
Administrative Expenses	376,959,555	18,545,994	22,742,189	418,247,738	1.38%
Vendor Fees	432,977,156	30,807,278	37,703,888	501,488,322	1.65%
Courier Collection Fee	12,235,328	-	-	12,235,328	0.04%
On Line Network Fees	35,576,140	6,816,802	7,247,920	49,640,862	0.16%
Start Up Costs	686,137	-	-	686,137	0.00%
Multi State Fees	25,270	18,875	51,418	95,563	0.00%
Provision for Doubtful Accounts	299,896	-	-	299,896	0.00%
Total Operating Expenses	15,592,111,099	1,150,258,436	1,325,922,289	18,068,291,824	59.50%
Operating Income	10,839,933,716	687,532,275	772,331,051	12,299,797,042	40.50%
NON OPERATING REVENUE					
Interest Income	72,967,359	6,540,964	3,200,150	82,708,473	0.27%
Total	72,967,359	6,540,964	3,200,150	82,708,473	0.27%
Income Before Transfers	10,912,901,075	694,073,239	775,531,201	12,382,505,515	40.77%
TRANSFERS OUT					
Contributions for Aid to Education and State Institutions	10,901,429,107	697,397,293	754,549,833	12,353,376,233	41.32%
Change in Net Assets	11,471,968	(3,324,054)	20,981,368	29,129,282	0.10%
Net Assets, Beginning of Period	-	11,471,968	8,147,914	-	-
Net Assets, End of Period	\$ 11,471,968	\$ 8,147,914	\$ 29,129,282	\$ 29,129,282	0.10%

See accompanying notes to financial statements.

*See accompanying independent auditors' report.



New Jersey
Lottery

STATEMENTS OF CASH FLOWS
FOR FISCAL YEARS ENDED JUNE 30, 2002 AND 2001

	FISCAL YEAR 2002	FISCAL YEAR 2001
CASH FLOWS FROM OPERATIONS:		
Current Operations:		
Sales and Receivables Receipts	\$ 1,155,641,151	\$ 990,392,881
Payments for Prize Awards	(330,377,661)	(248,782,303)
Payments for Commissions and Vendor Fees	(47,509,563)	(33,443,593)
Payments for Bond Insurance	(483,360)	(476,525)
Payments for Administrative Expenses	(15,119,193)	(16,664,680)
Other Payments	(43,634)	-
Annuity Operations:		
Annuity Award Receipts	169,908,079	165,887,599
Annuity Award Purchases	(25,397,712)	(25,288,978)
Annuity Prize Payments	(122,556,316)	(176,557,479)
Net Cash Provided by Operating Activities	784,061,791	655,066,922
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State Transfers	(816,397,293)	(687,928,948)
Net Cash Used by Noncapital Financing Activities	(816,397,293)	(687,928,948)
CASH FLOWS FROM INVESTING ACTIVITIES		
Cash Management Fund Sales	1,118,893,000	989,281,000
Cash Management Fund Purchases	(1,087,455,000)	(957,887,174)
Net Cash Provided by Investing Activities	31,438,000	31,393,826
Net Decrease in Cash	(897,502)	(1,468,200)
Cash July 1	1,411,250	2,879,450
Cash June 30	\$ 513,748	\$ 1,411,250
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating Income	\$ 772,331,051	\$ 687,532,275
Net Changes in Assets and Liabilities:		
Accounts Receivable	(3,820,541)	(2,832,792)
Investments: Deposit Fund Contracts	61,040,922	21,187,922
Other Assets	(2,469,322)	(1,222,934)
Accounts Payable and Accrued Expenses	5,860,565	(11,076,134)
Unpaid Prize Awards	(48,934,022)	(38,435,613)
Compensated Absences	53,138	(85,802)
Net Cash Provided by Operations	\$ 784,061,791	\$ 655,066,922



New Jersey
Lottery

NEW JERSEY STATE LOTTERY COMMISSION

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2002 AND 2001

(1) Summary of Significant Accounting Policies

Reporting Entity

The New Jersey State Lottery Commission (the Commission) was established in 1970 pursuant to the "State Lottery Law," N.J.S.A. 5:9-1, et seq. The Commission operates within the Department of Treasury of the State of New Jersey. The Commission's financial statements are presented as an enterprise fund and include the operations for which the Commission is financially accountable and exercises oversight responsibility. The Commission is authorized and empowered to promulgate rules and regulations regarding the conduct of lottery games, including the price or prices of tickets, the number and size of prizes on winning tickets, the licensing of agents, and the apportionment of ticket revenues.

Basis of Accounting

Effective July 1, 2001, the Commission adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended by GASB Statement No. 37, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*. GASB Statement No. 34 establishes financial reporting standards for state and local governments. Based on the provisions of GASB Statement No. 34, the Commission is now included in the State of New Jersey Comprehensive Annual Financial Report as an enterprise fund and subjected to full accrual accounting. As a result of the adoption, the opening net assets for July 1, 2000 have been restated (see note 4). Resulting significant changes to the financial statements are:

- > The inclusion of a Management's Discussion and Analysis section.
- > The classification of assets and liabilities as either current or noncurrent.
- > The categorization of net assets as invested in capital assets, net of related debt, restricted (nonexpendable and expendable), or unrestricted.
- > The classification of revenues and expenses as either operating or nonoperating.
- > The presentation of a statement of cash flows using the direct method.
- > The recording of a compensated absences liability.

The Commission prepares its financial statements using the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized when incurred. GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Government Entities that Uses Proprietary Funds*, provides proprietary activities with a choice of authoritative guidance issued after November 30, 1989. The Commission has elected to follow GASB pronouncements exclusively after that date. The following is a summary of other significant accounting policies of the Commission.

Contributions and Prize Awards

The State Lottery Law requires at least 30% of gross revenues from ticket sales to be paid to the State Treasury for aid to education and State institutions. Pursuant to this law, the Commission has also designated all unallocated revenues for aid to education and State institutions. Contributions for the years ended June 30, 2002 and 2001 aggregated \$754,549,833 and \$697,397,293, respectively, of which \$15,549,833 and \$77,397,293 was due to the State Treasury at June 30, 2002 and 2001, respectively.

The Commission has designated that a minimum of 45% of gross revenues be allocated for prize awards, including agent bonuses. A prize expense is recorded when the winning ticket number is selected for the respective lottery game based on eligible winning tickets sold.

Forfeited Prizes

New Jersey Law requires that prizes not claimed within one year from the date of the drawing are forfeited and are included in other revenues during the period forfeited. Effective November 21, 1991, the Commission authorized that 70% of forfeited prizes are to be maintained in a reserve for prize awards. Such funds are available to augment future prize awards or, at the discretion of the executive director, to augment the Lottery's contribution for aid to education and State institutions. For the year ended June 30, 2002 unclaimed prizes aggregating \$28,842,236 were forfeited and are included in other revenues. For the year ended June 30, 2001 unclaimed prizes aggregating \$28,611,726 were forfeited and are included in other revenues.

Revenue Recognition

Revenues from the sale of lottery tickets are recognized as follows:

- > "Pick-3", "Pick-4", "Pick-6 Lotto", "Jersey Cash 5", "Lotzee", and "Mega Millions" (formerly The Big Game) on the drawing date.
- > Instant games, daily based upon the settlement of instant game inventory packs by selling agents. Sales adjustments are recorded based upon final reconciliations prepared after the termination of a lottery instant game.

Commissions and Fees

Agents receive a commission of 5% based on the total tickets sold and a commission of 1.25% of terminal validations. The on-line game contractor receives a fee equal to a contractual percentage of the revenue generated through the respective network maintained by the contractor. All other gaming contractors are paid fees based on the units of service provided.

State of New Jersey Cash Management Fund

Investments in the State of New Jersey Cash Management Fund are valued at cost, which approximates fair value. The State of New Jersey Cash Management Fund is a common trust fund administered by the State Department of the Treasury, Division of Investment. Securities in the fund are insured, registered or held by the Division of Investment or its agent in the Commission's name.

Accounts Receivable

Accounts receivable is comprised primarily of amounts due from agents.

Equipment and Inventory

The Commission follows the State's threshold for capitalizing equipment and inventory as follows; machinery and equipment \$20,000; and motor vehicles \$30,000. Purchases that do not meet the threshold for capitalization are recognized as expenses in the statements of revenues, expenses, and changes in net assets in the period in which they are acquired.

Installment Prize Awards and Prize Expenses

Installment prize awards are recorded based upon the present value of an annuity at terms to yield a series of future payments needed to meet the obligations of the Commission for prize disbursements. The Commission

NEW JERSEY STATE LOTTERY COMMISSION

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2002 AND 2001

purchases annuity contracts from insurance companies and U.S. Government securities to fund its liability for installment prize awards. Amounts recorded as prize expense reflect the cost of annuity contracts and U.S. Government securities necessary to satisfy stated prize awards plus any single payment awards.

Vacation and Sick Leave

The Commission records vacation and sick time incurred during the period in administrative expenses in the accompanying statements of revenues, expenses, and changes in net assets.

Payments for accumulated sick leave balances are made to retiring employees upon regular retirement. The payment is based on 50% of the employee's sick leave accumulation, at the pay rate in effect at the time of retirement up to a maximum of \$15,000. Employees separating from service prior to retirement are not entitled to payments for accumulated sick leave.

Use of Estimates

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

(2) Future Installment Prize Awards

The Commission purchases annuity contracts from insurance companies and U.S. Government securities to fund its liability for future installment prize awards. An annuity contract represents an obligation by an insurance company to provide a fixed series of payments over a specified period. U.S. Government securities are carried at fair value. Annuity contracts are carried at their current contract values, which are based upon their original purchase price adjusted for credited interest and amounts already received. Annuity contracts are subject to credit risk. The Commission seeks to control its exposure to such credit risk by purchasing annuity contracts only from insurance companies, which meet certain minimum standards. Such standards include a minimum required claims payment rating from Standard and Poors Corporation, a private rating agency, of at least "AA". However, due to the long-term nature of these contracts, the credit quality of the issuer is subject to change. At June 30, 2002 and 2001, the Commission held annuity contracts totaling \$1,110,613,218 and \$1,171,654,140, respectively, issued through thirteen insurance companies. The projected future costs of installment prize awards amount to \$1,624,623,624, which are due in installments ranging from ten years to the lifetime of the recipient. A significant portion of the Commission's investment in annuity contracts at such date is concentrated among five companies as follows:

- > Ohio National Life
- > New York Life Insurance Co.
- > Mutual of America
- > Alexander Hamilton Life Insurance Co.
- > Great West Life Assurance Co.

The estimated fair value of annuity contracts approximates the carrying value reflected in the accompanying statements of net assets at June 30, 2002 and 2001. Fair value has been estimated by discounting future cash flows using the current rates of annuity contracts with similar credit ratings and maturities.

(3) Litigation

The Commission is a party to a number of legal actions arising out of the conduct of its business. While the ultimate results of the lawsuits or other proceedings against the Commission cannot be predicted with certainty, management of the Commission does not expect that these matters will have a material adverse effect on the financial position or results of operations of the Commission.

(4) Net Assets as of Beginning of Period

As a result of the implementation of Governmental Accounting Standards Board No. 34, the Commission has restated its July 1, 2000 fund balances and recorded compensated absences as follows:

Net assets as of July 1, 2000, as previously reported	\$12,376,721
Compensated absences liability	<u>(904,753)</u>
Net assets as of July 1, 2000, as restated	<u>\$11,471,968</u>

(4) Commitments

Contractual Arrangements

The Commission maintains a gaming network of over 6,000 on-line locations where all games are sold. GTECH Corporation is responsible for operating the on-line games and providing courier services under a contract expiring November 23, 2006.

Operating Leases

The Commission leases certain office facilities under noncancelable operating lease agreements expiring through fiscal year 2005.

Future minimum lease payments are as follows:

Year ending	Amount
<u>June 30,</u>	
2003	\$ 668,650
2004	668,650
2005	278,604

Rent expense for office facilities in 2002 and 2001 was \$839,649 and \$857,015, respectively.

NEW JERSEY
LOTTERY



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Robert James D'Anton, Chairman
Benefits Education and Institutions

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Carole Hedinger, Acting Executive Director
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