



**“Giving everyone’s  
dreams a chance”**

# ANNUAL REPORT 2006

## LETTER FROM THE GOVERNOR

Dear Friends,

It is my staunch belief that we in government have one clear and all-consuming mission—to serve the needs and care for the well being of all in our community. Touching people’s lives through measurable, effective assistance, guidance and support must be the ultimate “bottom line” for those whose mission it is to serve the public good.

“Those record sales also translated into a new record for revenues returned support education and institutions—over \$844 million.”



This is the mission that the New Jersey Lottery has willingly and generously undertaken each year since 1970; for the staff, leadership and members of the Lottery’s retailer network, the true “bottom line” is the positive impact their efforts have in the lives of so many of our fellow New Jerseyans.

The New Jersey Lottery’s national reputation for integrity, industry, continual innovation and fiscally sound management is well deserved. This past year, the New Jersey Lottery again displayed its deep and abiding commitment to the residents of this State—and its exceptional fiscal acumen—by operating at a 1 percent administrative budget while achieving record sales of over \$2.4 billion. Those sales also translated into a new record for revenues returned to support education and institutions—over \$844 million.

I applaud your efforts and on behalf of all New Jerseyans, I offer my sincere thanks to the New Jersey Lottery family. To every member of that family, I express my deep gratitude and the confidence that, as we continue to work together, we will meet—and exceed—all challenges which lie ahead.

With all good wishes,

A handwritten signature in blue ink, which appears to read "Jon Corzine". The signature is fluid and cursive, written in a professional style.

Jon S. Corzine  
*Governor*

## LETTER FROM THE TREASURER

Dear Friends,

When asked about the New Jersey Lottery, the words I use most often to describe this remarkable agency are words like “innovation”, “commitment”, “industry”, “professionalism” and “integrity.” There are other entities that possess several of the exemplary characteristics of our State Lottery, but I have encountered no other entity which has them all—and possessing all of these stellar qualities is what truly sets the New Jersey Lottery apart.

In the last three and one-half decades of the New Jersey Lottery’s existence, more than \$15.6 billion has been generated to support K-12 education, our entire collegiate community—both schools and students—and our State’s veterans and most vulnerable citizens. That’s over thirty-five years of (the New Jersey Lottery) making a difference in the lives of school children, families and communities.

“That’s over thirty-five years of (the New Jersey Lottery) making a difference in the lives of school children, families and communities.”



The New Jersey Lottery is among the most successful and efficient State lotteries currently operating in North America. But my pride in the Lottery’s accomplishments is not limited merely to its sterling reputation; I take pride in the Lottery for what it has been able to accomplish in its support of our developmentally disabled, our veterans, our schoolchildren, and those whose collegiate dreams have been realized through the Lottery’s support of a number of scholarship and tuition aid programs.

It is with great pleasure that I join in presenting this Annual Report to the people of New Jersey. Once again, the Lottery has helped make our state a better place to “*Give Your Dreams A Chance*”.

Congratulations on another exceptional year.

Sincerely,

A handwritten signature in blue ink that reads "Bradley Abelow".

Bradley I. Abelow  
*State Treasurer*

## LETTER FROM THE CHAIRMAN

Dear Friends,

**T**hroughout the many years of the New Jersey Lottery's existence, there have been two things that we could always count on—growth and change. Since its inception, the ability to adapt to an ever-changing gaming industry and produce exceptional results has been the hallmark of the Lottery's efforts. Fiscal year 2006 was no different. In a year that saw dramatic changes within the lottery and gaming communities, the New Jersey Lottery's offerings continued to resonate with winners, lottery retailers, and the many beneficiary organizations the Lottery's revenue helps support.



“From local economies to our winners to our beneficiary community, the funding the New Jersey Lottery contributes to our State affects the lives of so many persons.”

What makes this year's performance by the New Jersey Lottery so impressive is that this dynamic growth has been accomplished without sacrificing the Lottery's well-earned reputation for sound financial management, integrity, innovation, and commitment to its customers and retailers. For the sixth consecutive year, sales topped \$2 billion. Those sales also supported the return of more

than \$844 million in fiscal year 2006 to our State's educational programs and institutions, an increase of approximately \$32 million over fiscal year 2005 revenues.

From local economies to our winners to our beneficiary community, the funding the New Jersey Lottery contributes to our State affects the lives of so many persons. On behalf of the membership and leadership of the New Jersey Lottery Commission, we are grateful for the opportunity to guide this exemplary organization, and we look forward to a future filled with promise and possibility.

Sincerely,

A handwritten signature in dark ink, appearing to read "Robert J. D'Anton". The signature is fluid and cursive, written over a light-colored background.

Robert James D'Anton  
*Chairman*

## LETTER FROM THE EXECUTIVE DIRECTOR

**\$2.4 billion in annual sales in fiscal year 2006.**

**A record \$844.2 million in revenue generated in support of State educational programs and State institutions.**

**Over \$1 billion in instant ticket sales alone—for the second fiscal year in a row.**

**Over \$15.6 billion in support of education and institutions over the past thirty-six years.**

**T**hese are impressive statements, and some very impressive numbers. But for the New Jersey Lottery, doing the impressive is at the core of our efforts. What began as only the third lottery of its kind in the United States has grown and evolved into an entity that continues to record milestones in sales, support and—most importantly—positive impacts upon the lives of countless New Jerseyans.

The New Jersey Lottery is among the most efficiently run lotteries in the United States, annually relying upon only approximately one percent of its revenues for its operations. The high level of efficiency in our operations is sustained by balancing prize payouts and operating expenses, thus maximizing the money we have available to return to support K-12 education, our colleges, universities, and the students who attend them, our State’s developmentally disabled individuals and our veterans’ homes. That support has meant school lunches for many of our state’s school-age children. It has meant scholarships for bright young collegians looking to pursue their dreams. And it has meant a home and daily care for the many valiant veterans of our armed forces, to whom we owe so much.



“Our success is a direct reflection of our hard-working and creative staff and Commission members, our diverse network of retailers, and the ongoing support of the people of this State.”

But our State’s students and those served by our State’s institutions have not been the sole beneficiaries of the Lottery’s success in fiscal year 2006. Local and regional economies have benefited as well during this landmark sales year. The Lottery’s network of 6,100 retailers—the majority of whom are small business owners—earned commissions of over \$133.6 million. These are dollars that can be used to grow their business or expand their offerings to the community. It is the result of a staunch commitment to their customers, one that is truly second to none.

And our customers? Well, in fiscal year 2006, our playing public boasted more than 102.5 million winners who were awarded an unprecedented \$1.38 billion in prizes.

We are proud of the significant achievements of the Lottery and are grateful for the role we play in improving the quality of life for so many of our fellow residents.

Sincerely,

A handwritten signature in blue ink that reads "William T. Jourdain". The signature is fluid and cursive.

William T. Jourdain  
*Acting Executive Director*

## WHERE THE MONEY GOES

### STATE OF NEW JERSEY PROGRAMS SUPPORTED BY STATE LOTTERY RESOURCES FOR THE FISCAL YEAR ENDED JUNE 30, 2006

#### DEPARTMENT OF AGRICULTURE

School Nutrition	\$ 4,143
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#### DEPARTMENT OF EDUCATION

Governor's School	793
Marie Katzenbach School for the Deaf	1,273
Non-Public School Aid	44,360
Statewide Assessment Program (Grades 4, 8, 11)	6,605
School Construction and Renovations	22,975
<b>Total Department of Education</b>	<b>76,006</b>

#### HIGHER EDUCATIONAL SERVICES

Senior Public Institutions - Operating Aid	392,632
Tuition and Grants	79,545
Higher Education Capital Improvement Plan - Debt Service	651
Outstanding Scholar Recruitment Program	5,735
Aid to County Colleges for Operational Costs	61,043
Aid to Independent Colleges and Universities	9,846
Coordinated Garden State Scholarship Program	3,020
Higher Education Facilities Trust Fund - Debt Service	7,660
Higher Education for Special Needs Students	427
Opportunity Program Grants	11,057
Supplementary Education Program Grants	5,294
Veterinary Medicine Education	593
<b>Total Higher Educational Services</b>	<b>577,503</b>

#### DEPARTMENT OF HUMAN SERVICES

Operation of Centers for Developmentally Disabled	44,949
Operation of State Psychiatric Hospitals	115,411
<b>Total Department of Human Services</b>	<b>160,360</b>

#### DEPARTMENT OF MILITARY AND VETERANS' AFFAIRS

Operation of Homes for Disabled Soldiers	26,144
<b>Total Revenue Realized - GAAP Basis</b>	<b>\$ 844,156</b>

(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 for the program would be funded by the General Fund.

The Lottery is so much more than jackpots and making millionaires. It's about helping to feed a nutritious meal to a young student or providing scholarships to a high school student. It's about improving the quality of life for disabled veterans and developmentally disabled individuals, and providing treatment programs for troubled youth.

As one of the most cost-efficient lotteries in the United States, the New Jersey Lottery spends approximately 1% of its revenues to operate and promote its business. As the State's fourth largest revenue producer, the Lottery raised over \$2.4 billion in sales for fiscal year 2006, and was able to contribute more than \$844 million to the state to help fund education and institutions, making everyone in the Garden State a winner.

Since its inception 36 years ago, the Lottery has dedicated more than \$15.6 billion to programs that benefit millions of New Jersey residents. Community Colleges, the Department of Human Services, the Department of Military and Veterans Affairs, our School Nutrition Program, and the Marie Katzenbach School for the Deaf are just a few of the organizations and programs whose constituencies benefit from Lottery proceeds.

The New Jersey Lottery also plays a key role in supporting small businesses throughout the state. Over 6,100 businesses serve as Lottery retailers and act as a direct link between the Lottery and its players. Retailers earn five percent of their lottery ticket sales in the form of commissions. Last fiscal year, the Lottery returned over \$133.6 million in commissions to support chain stores supermarkets, pharmacies, convenience stores and other establishments throughout the state.

### THE VIP CLUB

The Lottery's VIP Club has over 109,000 members – the most of any Lottery in the country. The VIP Club is free of charge and its members enjoy such privileges as having the daily results directly e-mailed to them; the ability to participate in special drawings for tickets to concerts, sporting events and family entertainment; and a newsletter that details games and promotions that are on the horizon. Members sign up by logging onto the Lottery's website, [www.njlottery.net](http://www.njlottery.net).



### RESPONSIBLE PLAY

As part of its continuing efforts to increase public awareness and understanding of playing responsibly, the Lottery has redesigned a brochure for distribution to the public that provided guidelines to use when playing the lottery and other gaming activities.

The brochure, entitled "It's Only a Game," is distributed to the Lottery's 6,100 retailers throughout the state. The free brochure encourages the public to call the 1-800-GAMBLER® hotline if they think they or someone they know may have a gambling problem. The staff at the hotline can direct them to assistance. Additionally, the Lottery also reinforced its commitment to combating underage gambling by partnering with the Council on Compulsive Gambling to increase public awareness of the Lottery's "Not 18 Yet? No Bet" campaign, which conveys to Lottery retailers the importance of not selling to minors.



The 1-800-GAMBLER® number is featured on all of the Lottery's product line and as a tagline in its print, radio and television advertising.

### NEW AND IMPROVED WEBSITE

The Lottery's website, [njlottery.net](http://njlottery.net), receives an average of 40,000 visitors each day and close to 1.5 million visitors each month, making it the most visited site among all state agencies in New Jersey and one of the most popular state lottery websites in the country. In fiscal year 2006, enhancements continued to be made to the site, including layout revisions, the addition of new links, and animated panels for special promotions.

Many of the website's more popular features now can be accessed without leaving the main homepage. The addition of flash drop-down menus, rollover images and jackpot amounts aligning at the top of the website add an interactive twist. Thanks to alterations such as these, visitors to the website can view winning numbers and jackpot amounts for each game with only a click of their mouse.





## WHERE THE MONEY GOES

Everyday, the New Jersey Lottery helps other agencies improve the quality of life in our State. In fiscal year 2006 alone, the Lottery contributed \$844.2 million to support State-sponsored programs that benefit players and non-players alike. The following are a sampling of the impact Lottery-generated revenue has in our communities.

## DEPARTMENT OF MILITARY AND VETERANS AFFAIRS

### *Veterans Health Services*

At all three of our State's Homes for Disabled Soldiers – Menlo Park, Paramus and Vineland – New Jersey Lottery funds are a portion of all operating expenses, including salaries, equipment, medical and office supplies. Last year alone, this amounted to over \$26.1 million—and, more importantly, made a difference in the lives of hundreds of veterans.

## DEPARTMENT OF HUMAN SERVICES

### *Operation of Centers for the Developmentally Disabled*

Our State's Developmental Centers—Green Brook Regional, Hunterdon, New Lisbon, North Jersey, Vineland, Woodbine, Woodbridge—are caring for the urgent needs of some of the most vulnerable of all of New Jersey citizens. Lottery-generated revenue is a portion of all operating expenses including food, transportation, therapy and equipment. Nearly \$45 million in fiscal year 2006 was dedicated to ensuring the quality of life for the residents of these facilities.

## K - 12 EDUCATION

### *School Nutrition Program*

Lottery-generated revenue is a significant portion of the State aid used to support the School Lunch and School Breakfast programs. In FY'06, the New Jersey Lottery contributed \$4.1 million to these programs which provide a nutritious, well-balanced breakfast and lunch for children in order to promote sound eating habits, to foster good health and academic achievement and to reinforce the nutrition education taught in the classroom. Currently, there are over 3,000 public and non-public schools in New Jersey under School Nutrition Programs supported by Lottery-generated funds.

### *Marie Katzenbach School For The Deaf*

Last year, the New Jersey Lottery contributed nearly \$1.3 million to the State's only school for the hearing impaired schoolchildren of New Jersey. Lottery proceeds at the Katzenbach School play a key role in the support of programs in Early Intervention, Nursery School, and Lower/Middle/Higher School.

### *Non-Public School Aid*

Non-public school aid is available to reimburse a public school district's expenses that are incurred on behalf of students enrolled in non-public schools with the district. In fiscal year 2006, school districts throughout the State were reimbursed nearly \$44.4 million—at no cost to local property taxpayers.

## HIGHER EDUCATION

### *Senior Public Institutions – Operating Aid*

Lottery-generated revenue, which is divided among higher education institutions according to class size, helps pay for the general operating expenses, including payroll and contracted services. In fiscal year 2006, nearly \$393 million went to such exceptional institutions as: Kean University, Montclair State University, New Jersey City University, the New Jersey Institute of Technology, Rowan University, Rutgers, The State University of New Jersey, Thomas Edison State College, and the University of Medicine and Dentistry of New Jersey. Public support of the New Jersey Lottery’s games has been beneficial for our public institutions as they continue to strive to provide exceptional education at affordable tuition prices.

### *Aid to Community Colleges for Operational Costs*

All 19 New Jersey Community Colleges receive funds from Lottery that helps defray operational expenses. Last year, our Community Colleges received over \$61 million to aid in offsetting the cost of payroll and contracted services. These funds were divided among our State’s Community Colleges according to class size.

### *Aid to Independent Colleges and Universities*

All of New Jersey’s independent Colleges and Universities receive funds from the New Jersey Lottery. Lottery funds help pay for general operating expenses, including payroll and contracted services, and are divided among the independent Colleges and Universities according to class size. Fiscal year 2006 saw these exceptional institutions receive almost \$10 million in support from the New Jersey Lottery.

### *Student Assistance For Higher Education*

**Opportunity Program Grants** – All New Jersey higher education institutions are eligible to receive these grants that are used to fund specific programs run by that institution’s Educational Opportunity Fund. In fiscal year 2006, over \$11 million went to help New Jersey college students pursue their careers.

**Outstanding Scholar Recruitment Program** – Graduating high school students who meet the academic criteria and enroll at any New Jersey college or university are eligible to receive one of the scholarships awarded through this program. These scholarships are given to outstanding high school graduates who are going to pursue a college education in New Jersey and, last year, the New Jersey Lottery helped provide \$5.7 million in funds to support scholarships that will aid hundreds of young New Jerseyans to realize their dreams.

**Tuition Aid Grants** - Students in need of financial assistance who are enrolled at any New Jersey collegiate institution are eligible to apply for grants available through this program. Family income, assets, size, number of students in college, and cost of the school are taken into account, and the \$79.5 million in Lottery revenues which supported this worthy program in fiscal year 2006 have made the hope of collegiate education a reality for a diverse array of students.

## PICK 3 AND PICK 4

Pick 3 (originally dubbed Pick-It) was first introduced on May 22, 1975 and astonished Lottery officials with its instant success among players. The game was originally slated for a six-month trial period, but in just five months, officials were astounded when the fledgling game recorded sales of nearly \$18 million. Thirty years later, the game has generated nearly \$12 billion in sales over those three decades, with \$458.7 million generated in this past fiscal year alone.

Two years after the 1975 debut of Pick 3, with the foundation laid by the success of the Pick 3 game, Lottery officials introduced the Pick 4. The weekly Pick 4 game was designed to produce larger prizes with higher odds of winning in comparison to the daily Pick 3.

Although payouts have evolved over the years, the characteristics of the Pick 3 and Pick 4 games remain the same. The games are still only \$.50 per bet, and the straight and combination features still remain. The Pick 4 has remained a steady favorite among players, amassing \$5.8 billion since its introduction. In fiscal year 2006, this cornerstone game earned \$260.3 million in sales and returned \$109.6 million to the State to support education and institutions.

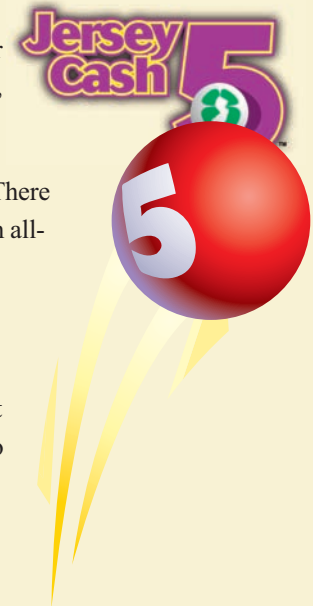


## JERSEY CASH 5

Jersey Cash 5 is drawn seven days per week and is one of the Lottery's most popular live-drawing games. And, with more people winning higher jackpots throughout the year, Jersey Cash 5 has become one of the most popular games the Lottery offers.

The average top-prize in 2006 was \$167,000 and 1,168,075 players won \$62.5 million. There were also 201 jackpot winners over the course of the year. Sales for the game reached an all-time high of nearly \$126 million in fiscal year 2006 as well.

Players also had the chance to win a Mustang convertible through a special promotion done in conjunction with Jersey Cash 5. This unique promotion marked the second time a bonus drawing had been added to the Jersey Cash 5 game. Like the first promotion, which awarded a 4x4 Jeep Laredo as a grand prize, this promotion was also a resounding success.



## PICK 6 LOTTO



Since its inception, the Pick 6 Lotto has generated \$7.4 billion in sales, paid out \$4 billion to winners and returned more than \$3.1 billion to state education and institutions.

Pick 6 Lotto, which made its first millionaire in 1981, turned out 8 millionaires in fiscal year 2006. With fiscal year 2006 sales totaling \$102.7 million, and returns to the state equaling nearly \$43 million, the Pick 6 Lotto once again established itself as one of the Lottery’s flagship games. In addition to continuing to turn ordinary citizens into overnight millionaires, Pick 6 Lotto was further enhanced by offering players the chance to win one of several all-expense paid trips in conjunction with playing Pick 6.

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. In the months and years ahead, while the essence of this singular game remains intact, expect to see new and exciting enhancements added on for the benefit of our playing public.

## MEGA MILLIONS



Fiscal year 2006 was a very noteworthy year for the New Jersey Lottery’s Mega Millions game. During fiscal year 2006, fortunate New Jersey players of this exciting multi-state game won more than \$158.2 million. In September of 2005, and again in June of 2006, New Jersey residents were sole winners of Mega Millions jackpots. In addition, the September 2005 jackpot set a new record for a sole New Jersey Mega Millions jackpot winner—\$258 million.

Sales from Mega Millions were quite strong, reaching \$317,207,674 in New Jersey during fiscal year 2006. During this time, there were five jackpots that exceeded \$100 million, three that topped the \$200 million mark, and one jackpot that even exceeded the \$300 million mark.

## INSTANT GAMES

New Jersey’s instant game product line continues to be one of the most popular in the nation. For the third year in a row, sales from instant games topped the \$1 billion mark. In fiscal year 2006, dozens of new instant games, ranging in prices from \$1 to \$10, were introduced. Among the most popular were *Orange County Choppers*®, *Crossword* and *Win For Life*. Instant tickets were responsible for contributing just under \$300 million to State education and institutions. Additionally, a record \$737.6 million was paid out in cash and prizes to our many instant ticket winners.



Second chance drawings on games like *Cash Catcher*, *Pink Panther*® and *iCash* offered players the opportunity to win some unique prizes and trips in our Lottery Bonus Zone “Second Chance” Drawings, and the success of these Drawings continues to be seen, even in the present day.



## INDEPENDENT AUDITORS' REPORT

To the Commissioners of the **NEW JERSEY STATE LOTTERY COMMISSION**:

We have audited the accompanying statements of net assets of the **NEW JERSEY STATE LOTTERY COMMISSION** (the "Commission") as of June 30, 2006 and 2005, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. 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, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

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** at June 30, 2006 and 2005, and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 30, 2006 on our consideration of New Jersey State Lottery Commission's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audit was performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The schedules included in the supplementary information are presented for the purpose of additional analysis and are not a required part of the basic financial statements. Such information, except for the portion marked "unaudited," on which we express no opinion, has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

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

MERCADIEN, P.C., CPAs

October 30, 2006

## MANAGEMENT DISCUSSION AND ANALYSIS

### Fiscal Years 2006 and 2005

#### INTRODUCTION

The following discussion and analysis provides an analytical overview of the financial position and activities of the New Jersey State Lottery Commission (the "Lottery") for the years ended June 30, 2006 and 2005. This statement was prepared by management and should be read in conjunction with the financial statements and notes hereto, 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 contributions to state aid for education and state institutions (N.J.S.A. 5:9-7a (11)).

The Lottery licenses over 6,100 retailers throughout the State of New Jersey to act as retailers 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 Banknote, Scientific Games and Oberthur Gaming Technologies are contracted to print and support instant game products.
- Verizon Communications is contracted to provide digital communication between the Lottery's 6,100 sales terminals and the Gtech data center.

The Lottery offers various products for sale with prize awards ranging from \$1.00 to cash and annuity prizes in excess of \$100 million. The various products sold are:

- Instant Games
- Pick 3 (Including Pick 3 Instant Match)
- Pick 4 (Including Pick 4 Instant Match)
- Jersey Cash 5
- Pick 6 Lotto
- Mega Millions

#### FINANCIAL HIGHLIGHTS

The Lottery's financial position at June 30, 2006 and 2005 consisted of total assets of \$977 million and \$1.071 billion, respectively, and total liabilities of \$964 million and \$1.058 billion, respectively. A substantial portion of the asset and liability numbers is due to the Lottery's annuity investment in prize awards. The total amounts invested and due to Lot-

tery winners as future installment payments at June 30, 2006 and 2005 were \$799 million and \$904 million, respectively. Net assets remained relatively stable at \$13 million in fiscal year 2006.

#### FINANCIAL STATEMENTS

The Lottery's financial statements include Statements of Net Assets as of June 30, 2006 and 2005, Statements of Revenues, Expenses and Changes in Net Assets for fiscal years ended June 30, 2006 and 2005, and Statements of Cash Flows for fiscal years ended June 30, 2006 and 2005. The financial statements are prepared in accordance with the accounting principles established by the Governmental Accounting Standards Board ("GASB").

#### STATEMENTS OF NET ASSETS

The statements of net assets present 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):

	June 30,	
	2006	2005
Current Assets	\$ 332	\$ 327
Deposit Fund Contracts	645	744
<b>Total Assets</b>	<b>977</b>	<b>1,071</b>
Current Liabilities	318	313
Non-Current Liabilities	646	745
<b>Total Liabilities</b>	<b>964</b>	<b>1,058</b>
Restricted Net Assets	10	10
Unrestricted Net Assets	3	3
<b>Total Net Assets</b>	<b>\$ 13</b>	<b>\$ 13</b>

Current assets consist of cash and 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 \$145 million and \$125 million at June 30, 2006 and 2005, respectively.

The Lottery funds long-term installment prizes with insurance company annuities and United States Treasury securities. The total value of these investments was \$799 million and \$904 million as of June 30, 2006 and 2005, respectively. The Lottery has annuity investments with thirteen (13) insurance companies. The total market value of the United States Treasury securities was \$31.4 million and \$34.4 million at June 30, 2006 and 2005, respectively. The annuity prizes due in fiscal years 2008 and beyond totaled \$645 million and represent the non-current assets reported on the Lottery's Statements of Net Assets.

## MANAGEMENT DISCUSSION AND ANALYSIS

### *Fiscal Years 2006 and 2005*

Current liabilities consist of unpaid prize awards, accounts payable and outstanding contributions due to the State of New Jersey General Fund. The total unpaid prizes due and payable totaled \$64 million and \$51 million as of June 30, 2006 and 2005, respectively. There is also \$154 million due to annuity winners in fiscal year 2007.

Non-current liabilities represent annuity prize awards due in fiscal years beyond 2007 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):

	June 30,	
	2006	2005
Restricted (Expired Prize Awards)	\$ 10	\$ 10
Unrestricted	3	3
<b>Total Net Assets</b>	<b>\$ 13</b>	<b>\$ 13</b>

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

### STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

The results of the Lottery's operations are presented in the Statements of Revenues, Expenses and Changes in Net Assets, which is summarized (in millions) as follows:

	Year Ended June 30,	
	2006	2005
Operating revenues		
Ticket sales	\$ 2,406	\$ 2,274
Forfeited prizes	35	31
Miscellaneous income	1	1
<b>Total operating revenue</b>	<b>2,442</b>	<b>2,306</b>
Operating expenses		
Prize expenses	1,380	1,297
Administrative expenses	30	28
Retailer commissions	134	126
Vendor fees	48	44
Network fees	9	8
Drawing broadcast fees	1	1
Bad debt and amortization expenses	1	-
<b>Total operating expenses</b>	<b>1,603</b>	<b>1,504</b>
Operating income	839	802
Investment income	5	2
Income before transfers	844	804
<b>Operating transfers - state contributions</b>	<b>844</b>	<b>812</b>
<b>Decrease in net assets</b>	<b>\$ -</b>	<b>\$ (8)</b>

The Lottery awarded over \$1.38 billion in prize awards in fiscal year 2006 and approximately \$1.297 billion in fiscal year 2005. Over 102 million winning tickets were validated and paid in fiscal year 2006, while approximately 95 million winning tickets were validated and paid in fiscal year 2005.

The Lottery's vendors provided critical services to the Lottery, including the production, warehousing, distribution and accounting for all lottery tickets. The total compensation paid for the Lottery's vendors and network fees was \$57.5 million in fiscal year 2006 and \$52.0 million in fiscal year 2005. Drawing broadcast fees were \$1,141,548 in fiscal year 2006 and \$1,141,540 in fiscal year 2005.

The Lottery's administrative expenses for the fiscal years 2006 and 2005 totalled \$29.6 million and \$27.5 million, respectively. These administrative expenses include salaries, advertising, auditing services, rent, security, data processing services, office supplies and attorney general fees. The majority of the increase in administrative expenses for fiscal year 2006 was for advertising.

The Lottery is required by State of New Jersey law to contribute at least 30% of gross revenues from ticket sales to the State of New Jersey Treasury for State aid for education and State institutions. As a result of various sales initiatives, game enhancements, and efficient operations, the Lottery contributed \$844 million, 34.6% of total revenues, in fiscal year 2006 and \$812 million, 35.2% of total revenues, in fiscal year 2005.

### STATEMENTS OF CASH FLOWS:

Below are the statements of cash flows, which are summarized (in millions) as follows:

	Year Ended June 30,	
	2006	2005
Cash flows from operating activities	\$ 866	\$ 796
Cash flows used in non-capital financing activities	(847)	(822)
Cash flows (used in) provided by investing activities	(16)	26
<b>Net increase in cash</b>	<b>\$ 3</b>	<b>-</b>

### 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. To this end, the following programs and products have proven to be successful in maintaining this interest:

- Free play coupons
- Pick 3 "Green Ball"
- Holiday gift giving with purchase of various games

Management will also monitor prize payout percentages and drawing odds in order to achieve an effective mix, which will be beneficial both to players and to the state contributions.

**STATEMENTS OF NET ASSETS**  
*June 30, 2006 and 2005*

	Fiscal Year 2006	Fiscal Year 2005
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash	\$ 3,228,501	\$ 521,666
Accounts receivable, net of allowance for doubtful accounts of \$650,000 in 2006 and \$150,000 in 2005	13,740,316	27,346,355
Investments		
Deposit fund contracts	153,857,004	160,286,504
State of New Jersey Cash Management Fund	145,453,450	124,740,315
Other assets	15,270,368	14,889,807
<b>Total current assets</b>	<b>331,549,639</b>	<b>327,784,647</b>
Non-Current Assets		
Investments - deposit fund contracts	644,974,326	743,996,848
<b>Total assets</b>	<b>976,523,965</b>	<b>1,071,781,495</b>
<b>LIABILITIES</b>		
<b>Current Liabilities</b>		
Accounts payable and accrued expenses	23,619,358	22,821,118
Obligation for unpaid prize awards	64,216,529	50,783,599
Installment prize awards	153,857,004	160,286,504
Due to State of New Jersey - education and State institutions	76,155,935	79,546,973
<b>Total current liabilities</b>	<b>317,848,826</b>	<b>313,438,194</b>
<b>Non-Current Liabilities</b>		
Compensated absences	998,542	876,398
Installment prize awards	644,974,326	743,996,848
<b>Total non-current liabilities</b>	<b>645,972,868</b>	<b>744,873,246</b>
<b>Total liabilities</b>	<b>963,821,694</b>	<b>1,058,311,440</b>
<b>NET ASSETS</b>		
Restricted for prize awards or contributions for aid to education and state institutions	9,875,921	10,698,521
Unrestricted	2,826,350	2,771,534
<b>Total net assets</b>	<b>\$ 12,702,271</b>	<b>\$ 13,470,055</b>

See accompanying notes to financial statements

## COMPARATIVE STATEMENTS

### *Statements of Revenues, Expenses and Changes in Net Assets*

	Fiscal Year 2006	Fiscal Year 2005
<b>Operating revenues</b>		
Ticket Sales		
Pick 3	\$ 458,716,926	\$ 456,582,545
Pick 4	260,267,470	265,003,920
Jersey Cash 5	125,903,092	123,253,335
Pick 6 Lotto	102,732,860	109,983,537
Mega Millions	317,207,674	253,408,054
Instant games	1,141,676,642	1,066,130,914
Sales discounts	(587,835)	(556,188)
<b>Total ticket sales</b>	<b>2,405,916,829</b>	<b>2,273,806,117</b>
<b>Other revenues</b>		
Forfeited prizes	34,737,378	30,662,853
Miscellaneous	852,043	1,247,318
<b>Total operating revenues</b>	<b>2,441,506,250</b>	<b>2,305,716,288</b>
<b>Operating expenses</b>		
Prize expenses	1,380,414,193	1,296,810,791
Administrative expenses	29,564,516	27,492,371
Retailer commissions	133,595,624	126,248,659
On-line vendor fees	31,461,000	29,924,546
Instant vendor fees	16,633,464	14,340,331
Multi-state fees	19,313	16,852
On-line network fees	9,394,721	7,759,214
Drawing broadcast fees	1,141,548	1,141,540
Bad debt expense	500,000	-
Amortization expense	26,854	2,086
<b>Total operating expenses</b>	<b>1,602,751,233</b>	<b>1,503,736,390</b>
Operating income	838,755,017	801,979,898
<b>Non-operating revenue</b>		
Interest	4,633,134	2,435,472
Income before transfers out	843,388,151	804,415,370
Transfers out - contributions for state aid to education and State institutions	844,155,935	812,046,973
Change in net assets	(767,784)	(7,631,603)
<b>Net assets, beginning of year</b>	<b>\$ 13,470,055</b>	<b>\$ 21,101,658</b>
<b>Net assets, end of year</b>	<b>\$ 12,702,271</b>	<b>\$ 13,470,055</b>

See accompanying notes to financial statements

**STATEMENTS OF CASH FLOWS**  
*For Fiscal Years Ended June 30, 2006 and 2005*

	Fiscal Year 2006	Fiscal Year 2005
<b>Cash flows from operating activities</b>		
Sales to customers	\$ 1,257,696,195	\$ 1,174,590,351
Payments for prize awards	(323,000,738)	(326,209,724)
Payments for vendor commissions and fees	(57,422,846)	(50,052,629)
Payments to suppliers	(33,930,650)	(20,614,419)
Other payments	(1,560)	(341,701)
<b>Cash flows from annuity operations:</b>		
Annuity receipts	154,726,746	164,104,704
Purchases of annuities	(11,942,462)	(26,503,851)
Payments of annuity prizes	(119,790,876)	(119,425,366)
<b>Net cash provided by operations</b>	<b>866,333,809</b>	<b>795,547,365</b>
<b>Cash flows used in non-capital financing activities</b>		
<b>Contributions for aid to education and state institutions</b>	<b>(847,546,974)</b>	<b>(821,471,914)</b>
<b>Cash flows from investing activities</b>		
Cash Management Fund proceeds	1,204,545,000	1,106,480,000
Cash Management Fund purchases	(1,220,625,000)	(1,080,650,000)
<b>Net cash (used in) provided by investment activities</b>	<b>(16,080,000)</b>	<b>25,830,000</b>
Net increase (decrease) in cash	2,706,835	(94,549)
Cash, beginning of year	521,666	616,215
<b>Cash, end of year</b>	<b>\$ 3,228,501</b>	<b>\$ 521,666</b>
<b>Reconciliation of operating income to net cash provided by operating activities</b>		
<b>Operating Income</b>	<b>\$ 838,755,017</b>	<b>\$ 801,979,898</b>
<b>Changes in assets and liabilities</b>		
Accounts receivable	13,606,039	11,803,407
Investments - deposit fund contracts	105,452,022	68,037,432
Other assets	(380,561)	(686,057)
Accounts payable and accrued expenses	798,240	2,308,407
Obligation for unpaid prize awards	(92,019,092)	(87,943,169)
Compensating absences	122,144	47,447
<b>Net cash provided by operating activities</b>	<b>\$ 866,333,809</b>	<b>\$ 795,547,365</b>

See accompanying notes to financial statements

## NEW JERSEY STATE LOTTERY COMMISSION

### Notes to Financial Statements June 30, 2006 and 2005

#### A. 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 those of 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 retailers (vendors), and the apportionment of ticket revenues.

##### Basis of Accounting

The Commission prepares its financial statements using the accrual basis of accounting. Revenues are recognized when earned, and expenses are recognized when incurred. Governmental Accounting Standards Board ("GASB") Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Government Entities that Use 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.

##### 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 state aid for 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, 2006 and 2005, aggregated \$844,155,935 and \$812,046,973, respectively, of which \$76,155,935 and \$79,546,973 was due to the State Treasury at June 30, 2006 and 2005, respectively.

The Commission has designated that a minimum of 45% of gross revenues be allocated for prize awards, including retailer bonuses. Prize expense is recorded when the winning ticket number is selected for the respective lottery game based on eligible winning tickets sold. For instant games, the percentage of gross revenues to be allocated for prize awards varies by game.

##### Forfeited Prizes

The State Lottery Law requires that prizes not claimed within one year from the date of the drawing be forfeited and be 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 Commission's contribution for aid to education and state institutions. For the years ended June 30, 2006 and 2005, forfeited prizes were \$34,737,378 and \$30,662,853, respectively.

##### Revenue Recognition

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

- "Pick-3," "Pick-4," "Pick-6 Lotto," "Jersey Cash 5," and "Mega Millions" are recognized on the drawing date.
- Instant games are recognized daily, based upon the settlement of instant game inventory packs by selling retailers. Sales adjustments are recorded based upon final reconciliations prepared after the termination of a lottery instant game.
- Sales discounts are recorded for the sales value of tickets provided to

retailers at no cost to be used for promotional purposes.

##### Commissions and Fees

Retailers 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.

##### Cash

For the purpose of the statements of cash flows, cash includes unrestricted time deposits and highly liquid debt instruments with original maturities of three months or less.

##### 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.

##### Accounts Receivable

Accounts receivable is comprised primarily of amounts due from retailers. The reserve for uncollectible accounts is funded by a \$100 per year bonding fee paid by the Commission's retailers. The reserve also comprises an allowance for uncollectible accounts of \$650,000 and \$150,000 for the years ended June 30, 2006 and 2005, respectively. The Commission also maintains a designated net assets cash reserve of \$500,000.

##### Equipment

The Commission follows the state's threshold for capitalizing equipment as follows: machinery and equipment over \$20,000 and motor vehicles over \$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 during which they are acquired and are included in administrative expenses. For the years ended June 30, 2006 and 2005, leasehold improvements included in other assets were \$257,160 and \$202,344, respectively. For the years ended June 30, 2006 and 2005, amortization expense was \$26,854 and \$2,086, respectively.

##### 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 purchases annuity contracts from insurance companies and U.S. government securities to fund its liability for installment prize awards. Amounts recorded as "prize expenses" 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.

##### 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 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.

## NEW JERSEY STATE LOTTERY COMMISSION

### Notes to Financial Statements June 30, 2006 and 2005

#### B. CASH AND INVESTMENTS

Deposits are with contracted depository banks in interest-bearing accounts which are insured under the Government Unit Deposit Protection Act ("GUDPA") of the State of New Jersey. All such deposits are held in the Commission's name.

GUDPA permits the deposit of public funds into the State of New Jersey Cash Management Fund or into institutions located in New Jersey which are insured by the Federal Deposit Insurance Corporation or by any other agencies of the United States that insure deposits.

GUDPA requires public depositories to maintain collateral for deposits of public funds that exceed insurance limits as follows:

The market value of the collateral must equal 5% of the average daily balance of public funds or, if the public funds deposited exceed 75% of the capital funds of the depository, the depository must provide collateral having a market value equal to 100% of the amount exceeding 75%.

All collateral must be deposited with the Federal Reserve Bank, the Federal Home Loan Bank Board, or a banking institution that is a member of the Federal Reserve System and has capital funds of not less than \$25,000,000.

Uninsured and uncollateralized deposits are covered under the unit certificate of eligibility, as required by GUDPA.

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.

#### Custodial Credit Risk

Custodial credit risk is the risk that, in the event of a bank failure, the Commission's deposits may not be returned to it. The Commission does not have a deposit policy for custodial credit risk. Since the New Jersey Cash Management Fund balance is a pooled investment and the cash balance is covered under GUDPA, the Commission's cash and investments are not subject to custodial credit risk under GASB Statement No. 40.

#### C. 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. Generally, annuity contracts fund instant product annuity prizes, and U.S. government securities fund annuity prizes for Pick 6 and Mega Millions. 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. At June 30, 2006 and 2005, the Commission held U.S. government securities totaling \$31,456,233 and \$34,387,398, respectively.

Annuity contracts are carried at their current contract values, which are based upon their original purchase prices 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 that meet certain minimum standards. Such standards include a minimum required claims payment rating from Standard and Poor's 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. As of June 30, 2006, only one of

the companies had a rating under "AA," as compared to three at June 30, 2005. At June 30, 2006 and 2005, the Commission held insurance company annuity contracts totaling \$798,831,330 and \$904,283,352, respectively, issued through thirteen insurance companies, 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 the following eight companies:

- Ohio National Life
- Metropolitan Life
- New York Life Insurance Co.
- Keyport Life/Sun Life
- Alexander Hamilton Life Insurance Co. (Jefferson Pilot)
- Mutual of America
- Protective Life
- Great West Life

The estimated fair value of annuity contracts approximates the carrying value reflected in the accompanying statements of net assets at June 30, 2006 and 2005.

#### Concentrations of Credit Risk

"Concentration of Credit Risk" is the risk that relates to the amount of investment at any one entity. The disclosure requirement of this risk factor is limited to investments in excess of 5% of the total. Guaranteed annuity contracts are the only category subject to concentration of credit risk disclosure.

#### D. 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.

#### E. COMMITMENTS

##### Contractual Arrangements

The Commission maintains a gaming network of over 6,100 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 December 20, 2007.

##### Operating Leases

The Commission leases certain office facilities under non-cancelable operating lease agreements expiring through fiscal year 2013.

Future minimum lease payments are as follows:

Year Ending June 30	Amount
2007	\$ 697,438
2008	\$ 638,550
2009	\$ 638,550
2010	\$ 638,550
2011	\$ 638,550
2012	\$ 638,550
2013	\$ 638,550

Rent expense for office facilities in 2006 and 2005 was \$1,041,127 and \$750,100, respectively.