



LETTER FROM THE ACTING EXECUTIVE DIRECTOR

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Dear Friends,

I am honored to join in presenting this annual report to the residents of our state. Although I have only recently become part of the exciting team at work here, I am well aware of the outstanding tradition that has existed at the lottery over the past 34 years. As we approach FY '05 and reflect back on the successes of the last fiscal year, I pay tribute to the New Jersey Lottery staff, our growing network of over 6,000 retailers and, of course, our players, without whom this banner year would not be possible.

The lottery's success during FY '04 is a direct reflection of the innovative thinking that takes place here everyday. Cyber Slingo, the nation's first Internet lottery game, was successfully launched right here in the Garden State and our Jersey Cash 5 game was re-tooled, producing a 70 percent sales increase. Furthermore, the "look and feel" of the lottery was given a "facelift" through a fresh marketing and sales approach combined with new advertising and creative media campaigns. Lastly, the lottery bolstered its presence in the community by kicking off an educational campaign entitled, Where the Money Goes.

This special speakers' bureau allows lottery staff to travel the state and educate local groups and organizations about the way in which lottery proceeds are utilized.

The New Jersey Lottery is proud to issue this annual report of the year's achievements and is already looking for new and exciting ways to build on that success and to provide further benefits to the state of New Jersey.



Best Wishes,

Michellene Davis, Esq.
Acting Executive Director

THE NEW
JERSEY
LOTTERY



LETTER FROM THE ACTING GOVERNOR

Dear Friends,

It is with great pride that I accept this annual report of the New Jersey Lottery. This vital state agency experienced yet another record-breaking sales year thanks to the tireless efforts of the entire lottery team. The dedication of the Lottery Commission, the staff and our 6,000 lottery retailers is evident in the continued growth of the state's fourth largest revenue producer.

With an astonishing 91 million lottery players winning an array of prizes last year, the New Jersey Lottery's most significant achievement continues to be its financial support to state education programs and institutions. Outlined in the pages of this annual report, it is noteworthy that lottery revenue far exceeds the amount required by lottery law.

Congratulations and many thanks to all those who have helped contribute to the New Jersey Lottery's continued success, especially during this exceptional year.



Regards,

Richard J. Codey
Acting Governor





LETTER FROM THE TREASURER

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Dear Friends,

Once again, the New Jersey Lottery has reached new levels in player prizes, commissions paid to retailers and state contributions, while at the same time maintaining its distinction as one of the most efficient lottery programs in the nation. With another \$2 billion sales year, the lottery's success represents the perfect balance between effectiveness and efficiency.

As an important revenue source for our state's budget, the lottery again has exceeded expectations and provided valuable funding for programs of great importance to all New Jersey residents. Given that the lottery returns approximately 36 cents of every dollar to support state education and institutions, FY '04 sales translated into \$794 million in funding for community colleges, Department of Human Services, Governors School, Department of Military and Veterans Affairs, Department of Agriculture (for school nutrition), and the Marie Katzenbach School for the Deaf.

The New Jersey Lottery continues to make the Garden State a better place to live, work and play.



Sincerely,

John E. McCormac, CPA
State Treasurer

THE NEW
JERSEY
LOTTERY



LETTER FROM THE CHAIRMAN

Dear Friends,

The success of the New Jersey Lottery, as you will see in the upcoming pages, is truly a team effort. The lottery is fueled by the pride and professionalism of not only our 6,000 retailers, but of our employees. From the sales staff, to the validation department, to the security and licensing department, the over 100 lottery employees year after year perform their responsibilities to the highest level.

My fellow commissioners and I are proud to serve an organization that has such a high level of professionalism and dedication. We look forward to another prosperous and exciting year ahead.



Sincerely,

Robert James D'Anton
Chairman



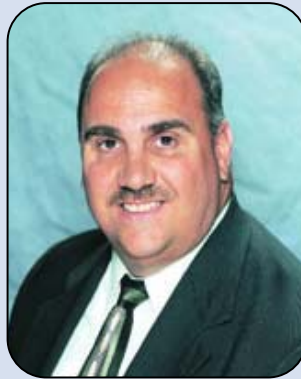
NEW JERSEY STATE LOTTERY COMMISSION



Daniel F. Becht, Esq.
Commissioner



Robert Slater
Commissioner



Robert James D'Anton
Chairman



Michellene Davis, Esq.
Acting Executive Director



John E. McCormac, CPA
Treasurer



Dr. Stephen T. Boswell
Vice-Chairman

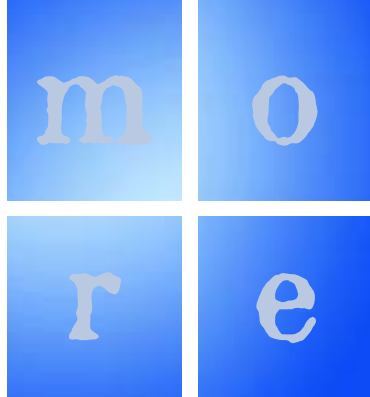


Dr. Anthony R. Caputo
Commissioner



Dr. Munir Kazmir
Commissioner





WHERE THE MONEY GOES

And the winner is...everyone in the state of New Jersey! In fiscal year 2004, the New Jersey State Lottery generated sales of approximately \$2.2 billion breaking records in terms of sales, overall winners, retailer commissions and contributions back to the Garden State.

State Contributions

Given that the lottery returns approximately 36 cents of every dollar to support state education and institutions, FY '04 sales translated into nearly \$795 million in funding for: community colleges, Department of Human Services, Governor's School, Department of Military and Veterans Affairs, Department of Agriculture, and the Marie Katzenbach School for the Deaf.

Winners, Winners, Winners

While millions of people who never play the lottery certainly benefit, our players have had a very good year! More than 91 million people won some type of prize from the lottery last year, the most winners in the organization's history. The total prize amount given out by the lottery in FY '04 was \$1.23 billion. In particular, there were seven top-prize Pick 6 winners and 160 top-prize Jersey Cash 5 winners.

Supporting Small Business

For the past 34 years, the lottery has played a key role in supporting small businesses throughout the state. More than 6,000 businesses serve as lottery retailers and act as a direct link between the lottery and its players. These businesses earn five percent of their lottery ticket sales in the form of commissions.

This fiscal year, the lottery returned commissions totaling nearly \$121 million to retailers who operate at chain stores, supermarkets, pharmacies, convenience stores, and other establishments throughout the state. These commissions, as well as additional bonuses for selling top prize winning tickets, have provided many small businesses with an extra revenue source.

One of the Most Efficient Lotteries in the Country

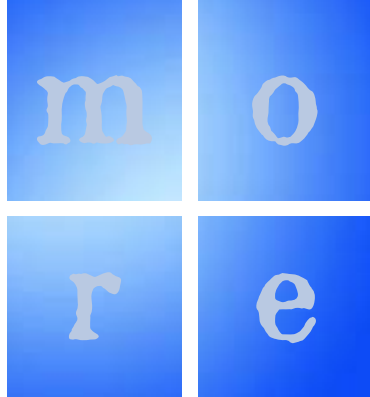
At a time when many of the state's financial resources have been strained by economic factors, the New Jersey State Lottery continues to serve as one of the most efficiently run programs in the nation.

Effectiveness and efficiency often can be conflicting goals; however, by balancing prize payouts and operating expenses, the lottery has been able to maintain its proficiency and maximize the money it gives back to the state for programs, such as: veterans' homes, community colleges and institutions for developmentally disabled individuals in New Jersey.



WHERE THE MONEY GOES

STATE OF NEW JERSEY PROGRAMS SUPPORTED BY STATE LOTTERY RESOURCES FOR THE YEAR ENDED JUNE 30, 2004 (Amounts expressed in thousands)	
	Amount Expended and/or Encumbered (a)
DEPARTMENT OF AGRICULTURE	
SCHOOL NUTRITION	\$ 6,180
DEPARTMENT OF EDUCATION	
GOVERNOR'S SCHOOL	962
MARIE KATZENBACH SCHOOL FOR THE DEAF	1,655
NON-PUBLIC SCHOOL AID	58,146
STATEWIDE ASSESSMENT PROGRAM (GRADES 4,8,11)	7,212
TOTAL DEPARTMENT OF EDUCATION	67,975
HIGHER EDUCATIONAL SERVICES	
SENIOR PUBLIC INSTITUTIONS-OPERATING AID	146,270
TUITION AID GRANTS	98,908
HIGHER EDUCATION CAPITAL IMPROVEMENT PLAN-DEBT SERVICE	10,561
OUTSTANDING SCHOLAR RECRUITMENT PROGRAM	7,651
AID TO COUNTY COLLEGES FOR OPERATIONAL COSTS	93,042
AID TO INDEPENDENT COLLEGES AND UNIVERSITIES	13,606
COORDINATED GARDEN STATE SCHOLARSHIP PROGRAM	3,922
HIGHER EDUCATION FACILITIES TRUST FUND - DEBT SERVICE	12,219
HIGHER EDUCATION FOR SPECIAL NEEDS STUDENTS	608
OPPORTUNITY PROGRAM GRANTS	12,738
SUPPLEMENTARY EDUCATION PROGRAM GRANTS	7,200
VETERINARY MEDICINE EDUCATION	779
TOTAL HIGHER EDUCATIONAL SERVICES	407,504
DEPARTMENT OF HUMAN SERVICES	
OPERATION OF CENTERS FOR DEVELOPMENTALLY DISABLED	123,640
OPERATION OF STATE PSYCHIATRIC HOSPITALS	158,009
TOTAL DEPARTMENT OF HUMAN SERVICES	281,649
DEPARTMENT OF MILITARY AND VETERANS' AFFAIRS	
OPERATION OF HOMES FOR DISABLED SOLDIERS	31,664
TOTAL REVENUE REALIZED - GAAP BASIS	\$ 794,972
(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.	



WHERE THE MONEY GOES TOUR 2004

Lotteries around the country struggle with the best way to educate the general public about what happens to the money they spend on lottery tickets. Most experience shows that the public is either unaware that lotteries dedicate significant portions of their sales to support state programs, or misinformed about which programs receive funding. The New Jersey Lottery has met this challenge head-on by launching a useful, cost-effective campaign to educate the public about the lottery and where the money goes, while at the same time building a strong network of supporters throughout the state.



The New Jersey Lottery *Where the Money Goes Tour* was designed in fiscal year 2004 as a speaker's bureau program aimed at boosting public awareness of the significant financial contribution that the lottery makes in the community and to the state's economy. To get the program started, lottery representatives reached out to local businesses, as well as service and social groups, while at the same time developing a fun, interactive presentation.

The public relations team began a systematic outreach campaign to its target audiences via a letter of introduction describing the program. As the lottery followed-up with each group and started to arrange presentation dates and times, a master schedule of events was created using the Executive Director and Public Information Officer as primary lottery spokespersons. A *Where the Money Goes Tour* link also was added to the lottery's home page (www.njlottery.net) where interested organizations could learn more about the program. The program debuted in March 2004 and has already presented before more than 20 different groups and organizations throughout the state, with reservations for 16 more events in fiscal year 2005.

Future plans call for an expansion of the program, including the creation of several audience-specific presentations; outreach to target audiences, such as state trade associations, colleges and universities; as well as the addition of a video component. The New Jersey Lottery will develop a questionnaire that invites feedback from each group they visit.

DOING MORE FOR THE ENTIRE STATE

The New Jersey Lottery does not often get the opportunity to provide other than financial assistance to the people of New Jersey. In the past fiscal year however, the lottery took the opportunity to partner with the NJ State Police in an important community project.

In July 2003, the New Jersey Lottery and its network of 6,000 retailers became proud members of the state's AMBER Alert system. The AMBER Plan (America's Missing: Broadcast Emergency Response) was created in 1996 by the National Center for Missing & Exploited Children (NCMEC) in memory of 9-year-old victim, Amber Hagerman of Texas.

Each of the lottery's ticket terminals now can broadcast emergency notices through a scroll-messaging feature alerting the public when a child has been abducted. The attention-grabbing scroll feature is a critical component of New Jersey's AMBER Alert system due to the high volume of people that frequent convenience stores, supermarkets, service stations and specialty shops.

IT'S MUCH
MORE THAN
A GAME.





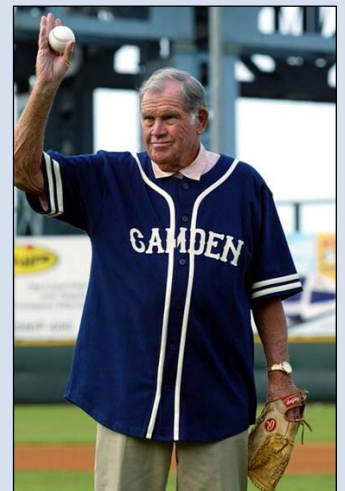
LICENSED GAMES ARE AN INSTANT SUCCESS

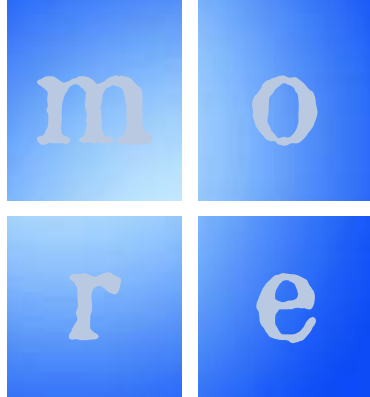
Instant games accounted for almost half of the lottery's total sales in fiscal year 2004. With as many as 52 different scratch-off tickets introduced each year, players are exposed to a wide variety of different themes, play formats, and well-known brands. What's more, many of the lottery instant games not only offer fast cash, but exclusive Lottery Bonus Zone games also provide a second chance to win even more prizes. The lottery's licensed product games, *The Honeymooners*, *Fast Cash Corvette*, and *I Love Lucy*, just to name a few, were particularly popular with players in FY '04.

The Honeymooners became an instant hit among lottery players due to the huge fan base for the television show, which translated into huge sales for this game. This particular game featured two plays and offered three \$30,000 top prizes, as well as four \$10,000 prizes. Given that the main character of *The Honeymooners* was a bus driver, the lottery partnered with New Jersey Transit to plan a special promotion around the game. Not only did the lottery advertise the game on the side of several New Jersey Transit buses, but it also hired a Ralph Kramden look-a-like to visit bus terminal locations throughout the state to meet players, pose for pictures and give away free lottery tickets.

Winning Legends was another licensed game that was an instant success for the lottery. The game ticket, which featured the likenesses of notable retired players from the New York Mets, Philadelphia Phillies and the New York Yankees, offered lottery players a top-prize of \$30,000. To promote the game, the lottery capitalized on the popularity of minor league baseball in New Jersey and arranged for two of the icons featured on the *Winning Legends* game to throw out the first pitch at a minor league game.

Hall of Fame pitchers Whitey Ford (below center) and Robin Roberts (below right) visited the Trenton Thunder and the Camden Riversharks, respectively, to sign autographs, talk to fans, and conduct interviews with the media to promote *Winning Legends*.





SUPPORTING SMALL BUSINESSES



For the past 34 years, the New Jersey Lottery has played a key role in supporting small businesses throughout the state. In addition to its 1,000 corporate partners, the New Jersey Lottery's 6,000 retailer network is made up primarily of supermarkets, pharmacies, convenience stores and many "mom and pop" businesses throughout the state.

Retailers earn five percent of their lottery ticket sales in the form of commissions. Last year alone, retailers earned nearly \$121 million. Many tell us that the lottery has enabled them to send children to college or take otherwise unaffordable family vacations, and has kept their businesses going during tough economic times.

The lottery's family of business partners grows more diverse each and every year. In June 2004, the lottery teamed up with the Port Authority of New York and New Jersey to install the first "Green Machine" in Terminal C in the Liberty International Airport. This partnership allows more than 25,000 visitors from around the world each day the opportunity to purchase lottery products.

Duane Reade, one of the fastest-growing drugstore chains in the industry, bolstered its community presence in New Jersey by registering all 12 of its locations in the state as lottery retailers. This partnership not only provides Duane Reade customers with the added convenience of purchasing lottery tickets while they shop for other products, but it also boosts lottery sales that will provide aid to state programs as well.

The added sales and exposure from these and thousands of other locations translate into increased revenue for the state's small business community and, in turn, New Jersey's economy. The lottery looks forward to continued success among its retailer community for years to come.

IT'S MUCH
MORE THAN
A GAME.

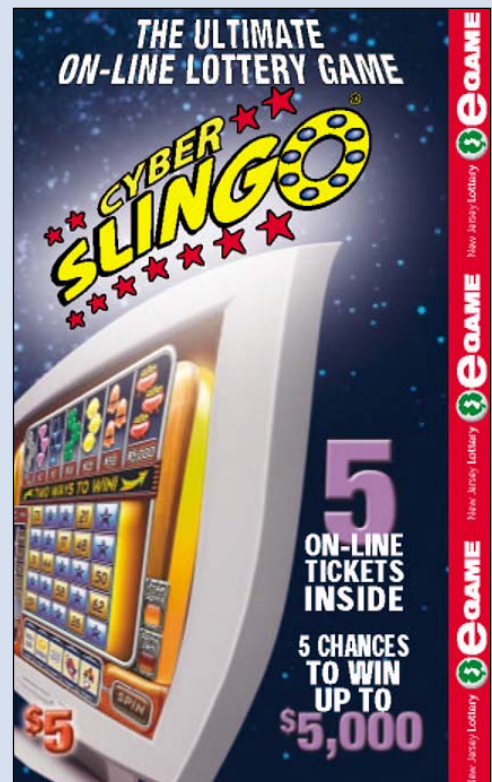


MOVING FROM “SCRATCH-AND-WIN” TO “CLICK-AND-WIN”

Slingo began as an AOL internet game in 1995, combining the fun of slots and bingo to become one of the most popular online games. The brand has been used in the past by several lotteries, including New Jersey, as a traditional instant game. With the new wave of internet savvy consumers, the New Jersey Lottery introduced a new hybrid instant lottery game - Cyber Slingo.

In fiscal year 2004, New Jersey was the first lottery in the world to venture into the realm of lottery “e-games” with the unveiling of Cyber Slingo on February 23, 2004. Played on the Internet, Cyber Slingo is the first game of its kind, offering an entertaining multi-media playing experience for everyone who enjoys playing the lottery and interactive online games.

After purchasing their Cyber Slingo tickets at the retailer, New Jersey players visit our website, www.njlottery.net; input the access code printed on the ticket; and “play” a short, five-minute Slingo game by completing a series of horizontal, vertical and diagonal rows to achieve the highest score. Priced at \$5.00, Cyber Slingo offers players five chances to win a top prize of \$5,000 and includes a password-controlled, parental monitoring feature that can be enabled by the player at any time. Prizes are redeemed at lottery retailer locations.



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MOVING FROM “SCRATCH-AND-WIN” TO “CLICK-AND-WIN”



“Our younger customers really love it (Cyber Slingo),” said Praful Thakkar from Todd’s News Agency in Vineland, NJ, one of the state’s 6,000 retailers. “They like the experience of taking the game home and playing online on their computers. Cyber Slingo brings customers into my store who normally do not play the lottery. They like the fact that they can take it home and spend more time playing.”

Sales of Cyber Slingo have been impressive considering players were not accustomed to playing lottery games at home on their computer. In fiscal year 2004, Cyber Slingo sales totaled \$12 million.

To promote the new game, the lottery hosted several mobile-marketing events at “cyber cafes” throughout New Jersey that allowed players to experience Cyber Slingo in a controlled environment. In addition to allowing players to try the game for free, and in some cases win cash prizes, players also received a free “goody bag” filled with giveaways. The turnout was impressive and the players had a great time experiencing the next generation of lottery gaming.

IT'S MUCH
MORE THAN
A GAME.



JERSEY CASH 5, PICK 3 AND PICK 4



In FY '04, the lottery made several enhancements to one of the state's more popular games designed to give players the chance to win higher jackpots more often.

Since its inception in 1992, Jersey Cash 5 served as a "roll-down" game, whereby if there was no top winner (five out of five numbers), the jackpot was divided into the remaining prize pools (four out of five numbers). In FY '04, Jersey Cash 5 changed to a "roll over" structure, where the jackpot grows and carries over to the next drawing if there is not a top winner. Additionally, Jersey Cash 5 players now choose five numbers from a field of 40, instead of 38.

The changes have had an amazing impact. The average top-prize has grown to \$250,000, as compared to the previous average jackpot of \$35,000. The changes produced a 69% increase in games sales, producing \$115,426,263 in revenue in fiscal year 2004. Jersey Cash 5 is now drawn seven days per week and costs \$1.00 per game.



Pick-3, formerly known as "Pick It" when it was first introduced in 1970, has been a success since inception. Originally pioneered as a trial game for six months, its popularity propelled this game to become a classic; and it is still a favorite among players today. In order to keep the game fresh for players, the New Jersey Lottery has enhanced the game by offering a midday draw and through initiatives like the "Bonus Match" feature. Pick-3 has produced \$452 million this past fiscal year and \$11 billion overall.



With the success of Pick-3, lottery officials introduced Pick-4 in 1977. The game was designed to be more challenging for players by increasing the odds of winning in return for larger prizes. The logistics of the game have remained the same through the years, although payouts have differed. The game is still only \$.50 a bet, and the features have remained the same. Pick-4 has been a favorite among players, generating \$261 million in sales in fiscal year 2004 and \$5 billion total.

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PICK 6, MEGA MILLIONS AND INSTANTS



First drawn on May 9, 1980, Pick 6 produced its first millionaire, Manuel Collada of Hillside, on May 28, 1981. Since then it has remained one of the lottery's most popular games.

Pick 6 has generated more than \$7 billion in sales over the past 34 years. In FY '04, Pick 6 had sales of over \$130 million and produced seven top-prize winners.



With five jackpots over \$100 million dollars, the multi-state game MEGA MILLIONS lived up to its name in fiscal year 2004.

Available in 10 other states - Georgia, Illinois, Maryland, Massachusetts, Michigan, New York, Ohio, Virginia and Washington, the addition of Texas in FY '04 allowed jackpots to reach higher levels in less rolls. Sales from the MEGA MILLIONS game reached \$251,295,751 in fiscal year 2004, an increase of over 9%.



New Jersey Lottery Instant Games continued to reach record sales in FY '04. The increase of Licensed Products and innovations such as Cyber Slingo and the Lottery Bonus Zone (offering prizes to holders of non-winning tickets) propelled the total sales of Instant Games to over \$973 Million.

IT'S MUCH
MORE THAN
A GAME.



MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal Years 2004 and 2003

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, 2004 and 2003. 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 (N.J.S.A. 5:9-7,a,(11)).

The Lottery licenses over 6,000 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 Bank Note, 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 6,000 sales terminals and the Gtech data center.

The Lottery offers various products for sale with prize awards ranging from \$1.00 to 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 3 Instant Match)
- Lotzee (product discontinued September 13, 2003)
- Jersey Cash 5
- Pick 6 Lotto
- Mega Millions (formerly The Big Game)

FINANCIAL HIGHLIGHTS:

The Lottery's financial position at June 30, 2004 and 2003 consisted of total assets of \$1.174 billion and \$1.214 billion, respectively, and total liabilities of \$1.153 billion and \$1.196 billion respectively. A substantial portion of the asset and liability numbers is due to the Lottery's annuity investment in prize awards. The total amount invested and due to Lottery winners as future installment payments at June 30, 2004 and 2003 was \$972 million and \$1.04 billion, respectively. Net assets increased \$3 million from the prior fiscal year.

FINANCIAL STATEMENTS:

The Lottery's financial statements include a Statement of Net Assets as of June 30 2004 and 2003, Statements of Revenues, Expenses and Changes in Net Assets for Fiscal Years June 30, 2004 and 2003, and Statements of Cash Flows for fiscal years ended June 30, 2004 and 2003. The financial statements are prepared in accordance with the accounting principles established by the Governmental Accounting Standards Board (GASB).

Statement 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):

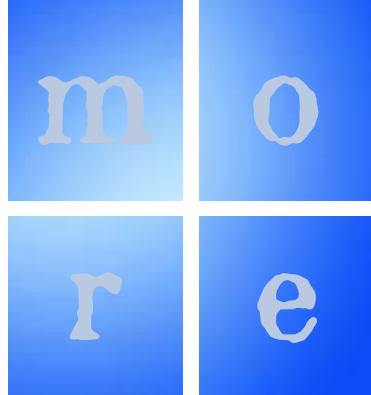
	<u>FY '04</u>	<u>FY '03</u>
Current Assets	\$ 353	\$ 340
Long Term Annuity Investments	<u>821</u>	<u>874</u>
Total Assets	<u>1,174</u>	<u>1,214</u>
Current Liabilities	331	321
Non-Current Liabilities	<u>822</u>	<u>875</u>
Total Liabilities	<u>1,153</u>	<u>1,196</u>
Restricted Net Assets	18	15
Unrestricted Net Assets	<u>3</u>	<u>3</u>
Total Net Assets	<u>\$ 21</u>	<u>\$ 18</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 \$148 million and \$140 million at June 30, 2004 and 2003 respectively.

The Lottery funds long term installment prizes with insurance company annuities and United States Treasury securities. The total value of these investments was \$972 million and \$1.04 billion as of June 30, 2004 and 2003, respectively. The Lottery has annuity investments with thirteen (13) insurance companies. The total market value of the United States Treasury securities was \$31.2 million and \$25.7 million at June 30, 2004 and 2003, respectively. The annuity prizes due in fiscal years 2005 and beyond totaled \$822 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 totaled \$71 million and \$52 million as of June 30, 2004 and 2003, respectively. There is also \$151 million due to annuity winners in fiscal year 2005.

Non-Current liabilities represent annuity prizes due in fiscal years 2005 and beyond and the total due for unused vacation and sick leave.



MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal Years 2004 and 2003

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

	<u>FY '04</u>	<u>FY '03</u>
Restricted (Expired Prize Awards)	\$ 18	\$ 15
Unrestricted	<u>3</u>	<u>3</u>
Total Net Assets	\$ 21	\$ 18

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

Statement 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 years ended June 30:

	<u>FY '04</u>	<u>FY '03</u>
Ticket Sales	\$ 2,187	\$ 2,074
Forfeited Prizes	43	38
Miscellaneous Income	<u>1</u>	<u>1</u>
Total Operating Revenue	<u>2,231</u>	<u>2,113</u>
Prize Awards	1,240	1,171
Administrative Expenses	21	22
Agent Commissions	121	115
Vendor Fees	43	40
Network Fees	8	13
Drawing Broadcast Fees	<u>1</u>	<u>(a)</u>
Total Operating Expenses	<u>1,434</u>	<u>1,361</u>
Operating Income	797	752
Investment Interest Income	<u>1</u>	<u>2</u>
Income Before Transfers	798	754
Operating Transfers-State Contribution	795	765
Increase (Decrease) in Net Assets	\$ <u>3</u>	\$ <u>(11)</u>

(a) Included in administrative expenses in FY 2003

The Lottery awarded over \$1.240 billion in prize awards in fiscal year 2004 and over \$1.171 in fiscal year 2003. Over 91 million winning tickets were validated and paid in fiscal year 2004 while over 88 million winning tickets were validated and paid in fiscal year 2003.

Lottery vendors provided critical services to the Lottery, including the production, warehousing, distribution and accounting for all lottery tickets. The total compensation paid for lottery vendors and network fees, was \$50.8 million in fiscal year 2004 and \$52.5 million in fiscal year 2003. Drawing broadcast fees in fiscal year 2004 was \$1,141,555; in prior fiscal years drawing broadcast fees were incorporated into administrative expenses.

The Lottery's administrative expenses for the fiscal years 2004 and 2003 totaled \$21.1 million and \$22.3 million, respectively. These administrative expenses include salaries, advertising, auditing services, rent, security, data processing services, office supplies and attorney general fees.

As a result of various sales initiatives, game enhancements and efficient operations, the Lottery contributed nearly \$795 million, 35.6% of total revenue in fiscal year 2004 and over \$765 million, 36.2% of total revenue in fiscal year 2003.

Statement of Cash Flows:

Below is the statement of cash flows which is summarized (in millions) as follows for the years ended June 30:

	<u>FY '04</u>	<u>FY '03</u>
Cash flows from operating activities	\$ 796	\$ 737
Cash flows used in non-capital		
financing activities	(790)	(697)
Cash flows used in investing activities	<u>(7)</u>	<u>(39)</u>
Net (decrease) increase in cash	\$ <u>(1)</u>	\$ <u>1</u>

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 and Pick 4 "Instant Match"
- Jersey Cash 5 - game modified to jackpot rollover.
- "Cyber Slingo", the first in the nation instant game playable on the Internet.

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

Commissioners of NEW JERSEY STATE LOTTERY COMMISSON

We have audited the accompanying statement of net assets of the NEW JERSEY STATE LOTTERY COMMISSION as of June 30, 2004 and the related statements of revenues, expenses and changes in net assets and cash flows for the year 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 audit. The financial statements of the NEW JERSEY STATE LOTTERY COMMISSION as of June 30, 2003 were audited by other auditors whose report, dated September 19, 2003, expressed an unqualified opinion on those financial statements.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the NEW JERSEY STATE LOTTERY COMMISSION at June 30, 2004 and the results of its operations and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

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 22, 2004

STATEMENTS OF NET ASSETS

June 30, 2004 and 2003

	Fiscal Year 2004	Fiscal Year 2003
ASSETS		
Current Assets:		
Cash	\$ 616,215	\$ 2,009,197
Accounts Receivable, net of allowance for doubtful accounts of \$150,000 in 2004 and 2003	39,149,762	20,566,151
Other Assets	14,203,750	11,861,099
Investments:		
Deposit Fund Contracts - current portion (note 2)	150,691,304	164,801,704
State Of New Jersey Cash Management Fund	148,134,843	140,313,400
Interfund Receivable - Administration	-	-
Total Current Assets	352,795,874	339,551,551
Non Current Assets:		
Investments:		
Deposit Fund Contracts (note 2)	821,629,480	874,227,407
Total Non Current Assets	821,629,480	874,227,407
Total Assets	1,174,425,354	1,213,778,958
LIABILITIES		
Current Liabilities:		
Accounts Payable and Accrued Expenses	20,512,711	19,432,721
Obligation for Unpaid Prize Awards	70,689,336	52,406,969
Current Year Installment Prize Awards	150,691,304	164,801,704
Due To State Of New Jersey - Education & Institutions	88,971,914	84,401,159
Interfund Payable - Administration	-	-
Total Current Liabilities	330,865,265	321,042,553
Non Current Liabilities:		
Compensated Absences	828,951	797,047
Installment Prize Awards	821,629,480	874,227,407
Total Non Current Liabilities	822,458,431	875,024,454
Total Liabilities	1,153,323,696	1,196,067,007
NET ASSETS		
Unrestricted	2,771,534	2,771,534
Restricted for Prize Awards and Contributions	18,330,124	14,940,417
Total Net Assets	\$ 21,101,658	\$ 17,711,951

See accompanying notes to financial statements



COMPARATIVE STATEMENTS

Statements of Revenues, Expenses, and Changes in Net Assets

	Cumulative 378 Months *Ended June 30, 2002	12 Months Ended June 30, 2003	12 Months Ended June 30, 2004	Cumulative 402 Months *Ended June 30, 2004	%
REVENUES:					
GROSS SALES	29,998,328,892	\$ 2,073,824,348	\$ 2,186,669,795	34,258,823,035	98.69%
FORFEITED PRIZES	357,206,506	38,517,867	42,984,774	438,709,147	1.26%
MISCELLANEOUS INCOME	12,553,468	661,374	1,382,932	14,597,774	0.04%
TOTAL OPERATING REVENUE	30,368,088,866	2,113,003,589	2,231,037,501	34,712,129,956	100.00%
EXPENDITURES:					
PRIZE EXPENSE	15,446,884,107	1,171,456,861	1,239,739,587	17,858,080,555	51.45%
COMMISSION TO AGENTS & BANKS	1,638,713,871	114,820,488	120,998,201	1,874,532,560	5.40%
ADMINISTRATIVE EXPENSES	418,247,738	22,305,736	21,083,924	461,637,398	1.33%
VENDOR FEES	501,488,322	39,917,717	42,761,283	584,167,322	1.68%
COURIER COLLECTION FEE	12,235,328	-	-	12,235,328	0.04%
ON LINE NETWORK FEES	49,640,862	12,555,061	8,053,690	70,249,613	0.20%
DRAWING BROADCAST FEES	-	-	1,141,555	1,141,555	0.00%
START UP COSTS	686,137	-	-	686,137	0.00%
MULTI STATE FEES	95,563	16,831	24,083	136,477	0.00%
PROVISION FOR DOUBTFUL ACCOUNTS	299,896	-	-	299,896	0.00%
TOTAL EXPENSES	18,068,291,824	1,361,072,694	1,433,802,323	20,863,166,841	60.10%
OPERATING INCOME	12,299,797,042	751,930,895	797,235,178	13,848,963,115	39.90%
NON OPERATING REVENUE:					
INTEREST INCOME	82,708,473	2,052,933	1,126,443	85,887,849	0.25%
TOTAL	82,708,473	2,052,933	1,126,443	85,887,849	0.25%
INCOME BEFORE TRANSFERS	12,382,505,515	753,983,828	798,361,621	13,934,850,964	40.14%
OPERATING TRANSFERS OUT:					
CONTRIBUTIONS FOR AID TO EDUCATION AND STATE INSTITUTIONS	12,353,376,233	765,401,159	794,971,914	13,913,749,306	40.08%
CHANGE TO NET ASSETS	29,129,282	(11,417,331)	3,389,707	21,101,658	0.06%
NET ASSETS, BEGINNING OF PERIOD	8,147,914	29,129,282	17,711,951	-	-
NET ASSETS, END OF PERIOD	37,277,196	\$ 17,711,951	\$ 21,101,658	21,101,658	0.06%

See accompanying notes to financial statements.

*Figures not covered by independent auditor's report.

STATEMENTS OF CASH FLOWS

For Fiscal Years Ended June 30, 2004 and 2003

	Fiscal Year 2004	Fiscal Year 2003
CASH FLOWS FROM OPERATIONS:		
Current Operations:		
Sales and Receivables Receipts	\$ 1,134,667,315	\$ 1,079,567,156
Payments for Prize Awards	(289,215,390)	(295,827,721)
Payments for Commissions and Vendor Fees	(53,828,028)	(52,809,080)
Payments for Bond Insurance	(597)	(452,921)
Payments for Administrative Expenses	(22,097,230)	(26,541,810)
Other Payments	(7,139)	(43,604)
Annuity Operations:		
Annuity Award Receipts	166,328,612	168,452,204
Annuity Award Purchases	(17,434,881)	(13,276,578)
Annuity Prize Payments	(122,709,485)	(122,046,363)
Net cash provided by operations	795,703,177	737,021,282
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:		
State Transfers	(790,401,159)	(696,549,833)
Net cash used by noncapital financing activities	(790,401,159)	(696,549,833)
CASH FLOWS FROM INVESTMENT ACTIVITIES:		
Cash Management Fund Sales	1,049,055,000	998,049,000
Cash Management Fund Purchases	(1,055,750,000)	(1,037,025,000)
Net cash provided by investment activities	(6,695,000)	(38,976,000)
Net Decrease in Cash	(1,392,982)	1,495,449
Cash July 1	2,009,197	513,748
Cash June 30	\$ 616,215	\$ 2,009,197
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating Income	\$ 797,235,178	\$ 751,930,895
Net Changes in Assets and Liabilities:		
Accounts Receivable	(18,583,611)	(1,047,148)
Investments: deposit fund contracts	66,708,327	71,584,106
Other Assets	(2,342,651)	551,133
Accounts Payable and Accrued Expenses	1,079,990	(7,386,434)
Unpaid Prize Awards	(48,425,960)	(78,536,229)
Compensated Absences	31,904	(75,042)
Net cash provided by operations	\$ 795,703,177	\$ 737,021,282

See accompanying notes to financial statements.



NEW JERSEY STATE LOTTERY COMMISSION

Notes to Financial Statements June 30, 2004 and 2003

(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 lottery retailers, 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 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.

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, 2004 and 2003 aggregated \$794,971,914 and \$765,401,159, respectively, of which \$88,971,914 and \$84,401,159 was due to the State Treasury at June 30, 2004 and 2003, respectively.

For machine games, the Commission has designated that a minimum of 45% of gross revenues be allocated for prize awards, including agent 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 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 Commission's contribution for aid to education and State institutions. For the year ended June 30, 2004 and 2003 unclaimed prizes were \$42,984,774 and \$38,517,867, respectively and are reported as 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" on the drawing date.
- Instant games, 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 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.

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 in institutions located in New Jersey which are insured by the Federal Deposit Insurance Corporation ("FDIC"), or by any other agencies of the United States that insure deposits or the State of New Jersey Cash Management Fund.

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.

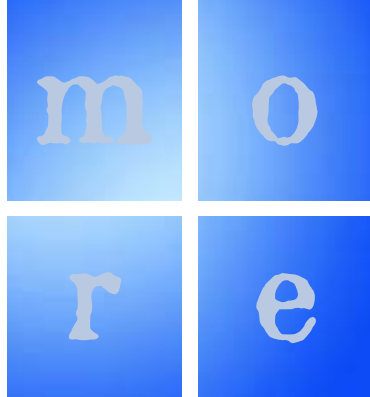
State of New Jersey Cash Management Fund

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 lottery retailers. The reserve for uncollectible accounts is funded by a \$100 per year bonding fee paid by lottery retailers. The reserve also comprises an allowance for uncollectible accounts of \$150,000 and designated net assets reserve of \$250,000.

The significant increase in accounts receivable at June 30, 2004 represents timing differences between the end of the reporting period and electronic transfer of retailer bank funds to the Commission's account.



NEW JERSEY STATE LOTTERY COMMISSION

Notes to Financial Statements June 30, 2004 and 2003

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 and are included in administrative expenses. During 2004 and 2003, there were no capitalized equipment or inventory purchases.

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 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. 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, 2004 and 2003, the Commission held U.S. securities totaling \$31,238,581 and \$25,717,192, respectively.

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, 2004 and 2003, the Commission held insurance company annuity contracts totaling \$972,320,785 and \$1,039,029,111, 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 eight companies as follows:

- Ohio National Life
- Protective Life
- Mutual of America
- New York Life Insurance Co.
- Alexander Hamilton Life Insurance Co. (Jefferson Pilot)
- Metropolitan Life
- Keyport Life / Sun 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, 2004 and 2003.

(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) 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 June 20, 2006.

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:

<u>Year ending</u> <u>June 30</u>	<u>Amount</u>	<u>Year ending</u> <u>June 30</u>	<u>Amount</u>
2005	\$697,438	2010	\$638,550
2006	\$697,438	2011	\$638,550
2007	\$697,438	2012	\$638,550
2008	\$638,550	2013	\$638,550
2009	\$638,550		

Rent expense for office facilities in 2004 and 2003 was \$762,564 and \$874,337, respectively.





Richard J. Codey, Acting Governor
John E. McCormac, C.P.A., State Treasurer

Michellene Davis, Esq., Acting Executive Director
Robert J. D'Anton, Chairman

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