

ARIZONA STATE LOTTERY



A Component Unit of the State of Arizona

FINANCIAL STATEMENTS

Year Ended June 30, 2011



ARIZONA STATE LOTTERY

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Janice K. Brewer
Governor



Jeff Hatch-Miller
Executive Director

November 16, 2011

Dear Arizona Lottery Commissioners:

The Arizona Lottery is pleased to submit its audited financial statements as of and for the year ended June 30, 2011, as prepared by the Lottery Accounting Department and audited by Henry & Horne, LLP. The Lottery is responsible for the accuracy and completeness of all data and disclosures in this report. To the best of our knowledge, the information presented is accurate and complete in all material respects and fairly depicts the financial position of the Arizona Lottery. This report includes a statement of net assets of the Arizona Lottery, the related statement of revenues, expenses, and changes in fund net assets; the statement of cash flows; footnotes related to the financial reports; and the supplemental schedule of gross profit by game.

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

The Arizona Lottery was created in 1980 when Arizona voters approved a ballot initiative adding Title 5, Chapter 5 to the Arizona Revised Statutes. The Lottery began selling instant "scratch-off" tickets in July 1981 and during its 30 years of operation has offered a variety of instant and on-line products. The Lottery operates as an agency of the State of Arizona and is reported as an enterprise fund within the state's Comprehensive Annual Financial Report. The fund is operated in a manner similar to a private business enterprise.

In fiscal year 2011 the Arizona Lottery had revenues of \$583.5 million from Lottery ticket sales, 5.8% more than last fiscal year, and an income before transfers of \$144.8 million, 1.0% more than last fiscal year. More than \$360 million was paid to our players in prizes and our retail partners received \$39.2 million for sales commissions. In its 30 years of operation, the Lottery has produced over \$8.5 billion in Lottery ticket sales.

In fiscal year 2011, the Arizona Lottery made transfers to other State Funds of \$10.0 million for the Heritage Fund, \$3.2 million for the Economic Development Fund, \$0.3 million for the Department of Gaming, \$18.8 million for the Healthy Arizona Fund, \$1.0 million for Homeless Shelters, \$6.0 million for University Capital Bonds and \$104.7 million was transferred to the State General Fund for allocation by the state legislature.

In addition, from the Lottery Prize Fund, over \$2.3 million was transferred to the Court Appointed Special Advocate (CASA). In total, over \$146.3 million was transferred to other State Funds for fiscal year 2011. In its 30 years of operation, the Lottery has returned almost \$2.7 billion to its beneficiaries.

Phoenix Office • 4740 E. University Drive • Phoenix, Arizona 85034 • (480) 921-4400 • Fax (480) 921-4488
Tucson Office • 4010 E. Grant Road • Tucson, Arizona 85712 • (520) 628-5107 • Fax (480) 921-4456
www.arizonalottery.com

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Further financial results for fiscal year 2011 are detailed in Management's Discussion and Analysis, included in this report.

Sincerely,

A handwritten signature in black ink, appearing to read "Jeff Hatch-Miller". The signature is stylized with a large, sweeping initial "J" and a long horizontal flourish at the end.

Jeff Hatch-Miller

Executive Director



HENRY & HORNE, LLP
Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

To the Commissioners of
Arizona State Lottery
Phoenix, Arizona

We have audited the accompanying financial statements of the The Arizona State Lottery (the "Lottery") of State of Arizona, as of and for the year ended June 30, 2011 (with comparative totals as of June 30, 2010) as listed in the table of contents. These financial statements are the responsibility of the Lottery's management.

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.

As discussed in Note 1, the financial statements present only the Lottery and do not purport to, and do not, present fairly the financial position of the State of Arizona, as of June 30, 2011, and the changes in its financial position, or, where applicable, its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Lottery of State of Arizona as of June 30, 2011, and the changes in financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying transmittal letter is not part of the required basic financial statements. Such information is the responsibility of the Lottery's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the transmittal letter. However, we did not audit the information and we do not express an opinion on it.

Tempe
2055 E. Warner Road
Suite 101
Tempe, AZ 85284-3487
(480) 839-4900
Fax (480) 839-1749

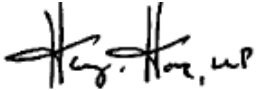
Scottsdale
7098 E. Cochise Road
Suite 100
Scottsdale, AZ 85253-4517
(480) 483-1170
Fax (480) 483-7126

Casa Grande
1115 E. Cottonwood Lane
Suite 100
Casa Grande, AZ 85122-2950
(520) 836-8201
Fax (520) 426-9432

The accompanying required supplementary information, management's discussion and analysis, is presented on pages 3 through 7 and is not a required part of the basic financial statements, but is supplementary accounting information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Lottery's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and we do not express an opinion on it.

Our audit was conducted for the purpose of forming an opinion on the Lottery's basic financial statements. The accompanying supplemental schedule of Gross Profit by Game is presented for purposes of additional analysis and is not a required part of the basic financial statements. This supplemental schedule is the responsibility of the Lottery's management. Such information has been subjected to the auditing procedures applied by us in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 16, 2011, on our consideration of the Lottery's internal control over financial reporting and our tests of its compliance and other matters. The purpose of that report is to describe the scope of our 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 read in conjunction with this report in considering the results of our audit.



Casa Grande, Arizona
November 16, 2011

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

**MANAGEMENT'S DISCUSSION AND ANALYSIS
AS OF AND FOR THE YEAR ENDED JUNE 30, 2011**

This discussion and analysis of the Lottery's financial statements is a required component of financial reporting under *Government Accounting Standards* and was prepared by Arizona Lottery Management. It provides an overview of financial activities as of and for the year ended June 30, 2011, and should be read in conjunction with the Lottery's financial statements and notes to the financial statements.

This annual report consists of three types of financial statements and accompanying notes that provide explanations and details of accounting policies, account balances and activities. Account balances and activities are shown as of and for the year ended June 30, 2011, with comparative totals for June 30, 2010. The statement of net assets; the statement of revenues, expenses, and changes in Fund net assets; and the notes are presented using the accrual method of accounting. Under this method, financial transactions are recorded when earned or incurred regardless of when cash is received or disbursed. The statement of cash flows reflects cash receipts and disbursements during the same 12-month periods.

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

A summary of the financial results of operations for the 12-month periods is presented in the statement of revenues, expenses, and changes in net assets. Operating revenues include sales of Lottery tickets, retailer licensing fees, and commissions earned on the sales of Lottery tickets at Lottery offices, and special events. Direct costs and administrative expenses comprise the operating expenses section of this statement. Direct costs are variable expenses that fluctuate with the level of sales. Marketing and overhead costs are included in the administrative expenses category.

Nonoperating revenues consist of interest earned on prize fund cash investments from the State Treasurer, interest credited to the Lottery's Multistate Lottery Association (MUSL) unreserved account for interest earned on prize reserves at MUSL and income recognized from common stock. The transfers category includes transfers to other state funds as required by Lottery statutes.

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

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

Sales Activities

Revenues from the sale of Lottery products for the fiscal year ended June 30, 2011 were higher than Fiscal Year 2010. As shown in the financial statements, sales increased 5.8% from the prior year, from \$551.5 million in Fiscal Year 2010 to \$583.5 million in the current year. The increases in ScratchersSM, Arizona RaffleTM and a full year of Mega Millions[®] sales more than offset the decrease in The Pick, Pick 3TM, Powerball[®], Pick 5TM, Cash 4, 2 by 2 and Fast PlayTM sales. The Lottery also introduced Instant Tab tickets sold by charitable organizations that produced \$1.0 million in revenue.

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

Product Sales	FY 2011	FY 2010	Difference	Percentage
Scratchers (including economic development)	\$373.5	\$336.9	\$36.6	10.8%
Instant Tabs	1.0	0	1.0	-
Powerball	89.1	118.8	-29.7	-25.0%
Mega Millions	47.3	6.8	40.5	597.3%
The Pick	34.6	44.4	-9.8	-21.9%
Fantasy 5	15.6	16.5	-0.9	-5.7%
Arizona Raffle	6.0	5.3	0.7	13.1%
Pick 3	8.3	8.6	-0.3	-8.5%
Cash 4	3.0	5.4	-2.4	-44.1%
2 by 2	3.9	6.5	-2.6	-40.5%
Fast Play	1.2	2.3	-1.1	-47.5%
Total	\$583.5	\$551.5	\$32.0	5.8%

Total Revenues

Nonoperating revenues for the year ended June 30, 2011, were \$143,153 as compared to \$1,734,523 for the year ended June 30, 2010. Nonoperating revenue is comprised of interest earned on invested cash, periodic recognition of commissions earned by the Lottery and income from common stock.

Total revenues were \$583.8 million for the year ended June 30, 2011, as compared to \$551.8 million for the year ended June 30, 2010. As mentioned above, most of the increase was due to an increase in sales revenues.

Major Expenses

\$416.5 million of the Lottery's total operating expenses of \$439.1 million for the year ended June 30, 2011 were incurred in direct support of the sales of Lottery games. These expenses include prize expense, retailer commissions and incentives, purchases of Scratchers tickets, compensation to the vendor for Scratchers ticket distribution, and compensation to the vendor who maintains and supports the on-line gaming system.

In comparison, \$387.6 million of the Lottery's total operating expenses of \$410.1 million for the year ended June 30, 2010, were game-related expenses.

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

Game Related Expenses	FY 2011	FY 2010	Difference	Percentage
Prize Expense	\$360.5	\$333.1	\$27.4	17.9%
Retailer Commissions	39.2	37.0	2.2	13.8%
On-line System Expenses	7.8	8.0	-0.2	2.6%
Scratchers System and Distribution Expenses	3.5	4.0	-0.5	-13.0%
Tickets Purchased	5.5	5.5	0	0%
Total	\$416.5	\$387.6	\$-2.0	16.1%

The increase in prize expense and retailer commissions is reflective of the increase in product sales. See the product sales schedule above. The decrease in tickets purchased is mostly related to the inventory write-off that was included in last year's results.

The pricing in the Lottery's new contract with an outside vendor for scratch ticket system and distribution expenses resulted in decreased costs of approximately \$500 thousand over last fiscal year.

Of the \$22.5 million in Fiscal Year 2011 in other operating expenses, \$14.9 million was used for advertising and promotion and \$5.7 million was used to compensate Lottery employees. In comparison, of the \$22.5 million in Fiscal Year 2010 other operating expenses, \$14.5 million was used for advertising and promotion and \$6.1 million was used to compensate Lottery employees.

Transfers to Other State Funds

Note 2 to the financial statements details the amounts transferred to other State Funds. In Fiscal Year 2011 the Lottery transferred \$146.3 million to other State Funds. In comparison, in Fiscal Year 2010 the Lottery transferred \$141.9 million to other State Funds.

Other Financial Information

Statement of Net Assets	FY 2011	FY 2010
Current Assets	\$55.9	\$47.2
Capital Assets	3.3	3.5
Other Assets — Deposits	9.0	9.7
Total Assets	68.2	60.4
Current Liabilities	57.7	48.4
Net Assets	\$10.5	\$12.0

The Lottery's total assets at June 30, 2011 were \$68.2 million. Assets consisted of cash held substantially by the State Treasurer of \$43.8 million, receivables from Lottery retailers for the sale of Lottery products of \$8.0 million, Scratchers ticket inventory of \$4.1 million, net investment in fixed assets of \$3.3 million and a deposit with MUSL of \$9.0 million.

Comparable figures at June 30, 2010, were \$60.4 million in total assets, including \$36.2 million in cash held by the State Treasurer, \$7.1 million in receivables from retailers, \$3.9 million in Scratchers ticket inventory, net investment in fixed assets of \$3.5 million, a MUSL deposit of \$8.2 million and investment in common stock of \$1.5 million.

Total liabilities at June 30, 2011, were \$57.7 million, consisting of \$3.4 million in accounts payable and accrued expenses, prize liabilities of \$29.2 million, and amounts due to other State Funds of \$25.1 million. All of the Lottery's liabilities were current liabilities.

The Lottery's total liabilities at June 30, 2010, were \$48.4 million, which consisted of \$4.7 million of accounts payable and accrued expenses, prize liabilities of \$26.6 million, and amounts due to other State Funds of \$17.1 million. All liabilities were current liabilities.

Total net assets at June 30, 2011, were \$10.5 million, which is \$1.5 million less than the amount of total net assets at June 30, 2010. \$7.3 million of the Lottery's total net assets are unrestricted.

In the sixth special session of the State Legislature in 2010, amendments were made to the Lottery statutes allowing the State to issue Lottery Revenue Bonds. These bonds provide additional working capital to pay appropriated expenditures of the State's General Fund. The bonds are payable solely from and secured by pledged revenues consisting of, until July 1, 2012, amounts distributable to the State General Fund from the Lottery pursuant to Lottery law, and from and after July 1, 2012 all Lottery revenues deposited to the Lottery fund net of Lottery operating expenses. (See note 3 to the financial statements.)

BUDGETARY HIGHLIGHTS

The Lottery's budget is set by the legislative appropriations process on a biennial basis. The budgets for Fiscal Years 2011 and 2012 were set in the regular legislative session of 2010. The Lottery's Fiscal Year 2011 budget was amended in the regular legislative session of 2011. The Lottery's appropriation for sales-related expenditures is based on approved percentages of projected revenues and is allowed to increase for these items without a supplemental appropriations request if actual revenues exceed projected revenues. The appropriation does not include an amount for prizes because Lottery statutes set this amount at "not less than 50% of the total annual revenues accruing from the sale of Lottery tickets or shares."

The Lottery's appropriation was \$81.0 million at the beginning of the year and increased to \$84.0 million, as actual revenues were more than budgeted projections.

CONTACTING THE LOTTERY'S FINANCIAL MANAGEMENT

This management's discussion and analysis (MD&A) is designed to provide Arizona citizens, Arizona government officials, our players, retailers, and other interested parties with an overview of the Lottery's financial activity for Fiscal Year 2011 and to demonstrate the Lottery's accountability for the money it received from the sale of Lottery products.

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



Jeff Hatch-Miller

Executive Director



William B. Kahler

Director of Accounting and Audit



ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
STATEMENT OF NET ASSETS
June 30, 2011
(with comparative totals for June 30, 2010)

	<u>2011</u>	<u>2010</u>
ASSETS		
CURRENT ASSETS		
Cash - substantially all held by the State Treasurer	\$ 43,843,094	\$ 36,193,820
Accounts receivable - net of allowance for doubtful accounts of \$145,000 as of June 30, 2011 and 2010	8,018,310	7,090,214
Scratch ticket inventory	3,942,775	3,927,375
Pull tab inventory	131,120	-
TOTAL CURRENT ASSETS	<u>55,935,299</u>	<u>47,211,409</u>
CAPITAL ASSETS		
Land and land improvements	1,268,695	1,268,695
Buildings	3,648,272	3,648,272
Furniture, fixtures and equipment	2,361,824	2,271,713
Construction in progress	76,348	83,580
Less accumulated depreciation	<u>(4,100,729)</u>	<u>(3,793,332)</u>
TOTAL CAPITAL ASSETS	<u>3,254,410</u>	<u>3,478,928</u>
OTHER ASSETS		
Investments	-	1,528,410
Deposit - MUSL	9,048,732	8,203,374
TOTAL OTHER ASSETS	<u>9,048,732</u>	<u>9,731,784</u>
TOTAL ASSETS	<u>68,238,441</u>	<u>60,422,121</u>
LIABILITIES		
CURRENT LIABILITIES		
Accounts payable	2,774,277	4,363,723
Accrued expenses	674,168	328,970
Prize liability	29,217,211	26,648,369
Due to other state funds	25,056,404	17,071,082
TOTAL CURRENT LIABILITIES	<u>57,722,060</u>	<u>48,412,144</u>
NET ASSETS		
Invested in capital assets	3,254,410	3,478,928
Unrestricted	7,261,971	8,531,049
TOTAL NET ASSETS	<u>\$ 10,516,381</u>	<u>\$ 12,009,977</u>

See accompanying notes.

ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
Year Ended June 30, 2011
(with comparative totals for the year ended June 30, 2010)

	<u>2011</u>	<u>2010</u>
OPERATING REVENUES		
Ticket sales:		
Scratchers	\$ 361,097,419	\$ 313,175,361
Powerball	89,101,991	118,802,400
The Pick	34,623,614	44,354,631
Fantasy 5	15,597,083	16,541,074
Pick 3	8,343,169	8,563,207
Mega Millions	47,317,197	6,785,931
2 By 2	3,849,966	6,466,860
Cash 4	3,031,492	5,425,860
Arizona Raffle	6,000,000	5,307,060
Economic development	12,354,770	23,766,275
Instant tab	1,011,642	-
Fast Play	1,209,150	2,303,042
TOTAL TICKET SALES	<u>583,537,493</u>	<u>551,491,701</u>
Other operating revenues	224,147	321,640
TOTAL OPERATING REVENUES	<u>583,761,640</u>	<u>551,813,341</u>
OPERATING EXPENSES		
Direct costs:		
Prize expense	360,491,232	333,105,221
Retailer commissions and incentives	39,247,401	36,995,955
Online system expense	7,735,726	7,991,552
Scratcher system and distribution expenses	3,529,021	3,974,913
Tickets purchased	5,514,726	5,545,973
TOTAL DIRECT COSTS	<u>416,518,106</u>	<u>387,613,614</u>
Advertising and promotion	14,859,476	14,454,016
Wages and related expenses	5,735,458	6,077,733
Contract services	365,916	422,473
Depreciation	307,397	352,766
Administrative expenses	1,282,770	1,149,630
TOTAL OPERATING EXPENSES	<u>439,069,123</u>	<u>410,070,232</u>
OPERATING INCOME	144,692,517	141,743,109
NONOPERATING REVENUES - Investment income and other	143,153	1,734,523
INCOME BEFORE TRANSFERS	144,835,670	143,477,632
TRANSFERS TO OTHER STATE FUNDS	146,329,266	141,858,578
CHANGE IN NET ASSETS	(1,493,596)	1,619,054
NET ASSETS - BEGINNING OF YEAR	<u>12,009,977</u>	<u>10,390,923</u>
NET ASSETS - END OF YEAR	<u>\$ 10,516,381</u>	<u>\$ 12,009,977</u>

See accompanying notes.

ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
STATEMENT OF CASH FLOWS
Year Ended June 30, 2011
(with comparative totals for the year ended June 30, 2010)

	<u>2011</u>	<u>2010</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from retailers-net of commissions and incentives	\$ 273,904,802	\$ 263,951,121
Cash received from other sources	62,416,807	10,691,153
Cash payments for prizes and related taxes	(151,598,498)	(99,789,628)
Cash payments to suppliers of goods or services	(34,520,303)	(34,831,299)
Cash payments to employees	<u>(5,757,723)</u>	<u>(6,024,094)</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	144,445,085	133,997,253
CASH FLOWS USED BY NONCAPITAL FINANCING ACTIVITIES		
Payments to beneficiaries per Arizona Statutes	(138,343,942)	(133,432,900)
CASH FLOWS USED BY CAPITAL FINANCING ACTIVITIES		
Payments for acquisition of capital assets	(50,879)	(43,809)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sale of investments	1,528,410	-
Receipts of interest	<u>70,600</u>	<u>135,457</u>
NET INCREASE IN CASH	7,649,274	656,001
CASH AT BEGINNING OF YEAR	<u>36,193,820</u>	<u>35,537,819</u>
CASH AT END OF YEAR	<u><u>\$ 43,843,094</u></u>	<u><u>\$ 36,193,820</u></u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating income	\$ 144,692,517	\$ 141,743,109
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	307,397	352,766
(Increase) decrease in:		
Accounts receivable	(855,542)	(1,236,354)
Ticket inventory	(146,520)	(1,559,642)
Deposit - MUSL	(845,357)	126,202
Increase (decrease) in:		
Accounts payable and accrued expenses	(1,276,252)	(147,000)
Prizes payable	<u>2,568,842</u>	<u>(5,281,828)</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u><u>\$ 144,445,085</u></u>	<u><u>\$ 133,997,253</u></u>

See accompanying notes.

ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2011

NOTE 1 NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING
POLICIES

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

The financial statements include prior-year comparative information, but the notes to the financial statements omit prior-year information required for a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such prior-year information should be read in conjunction with the Lottery's financial statements for the year ended June 30, 2010, from which the information was derived.

For the period July 1, 2010 through June 30, 2011, the Lottery held 142 instant games (games 453, 619, 623, 626, 628-629, 634, 636, 638-641, 645, 647-652, 654-665, 667-765, 767, 769-774, 780, 781, 787, 790, and 791), four of which were Economic Development games (games 636, 662, 707 and 724). During 2011, the Lottery continued the "Pick 3," "Pick 5," "The Pick," "Powerball," "Fast Play," "Mega Millions," "2 By 2" and "Cash 4" online games, continued the "Arizona Raffle" game, which was held one time in the fiscal year. As required, the Lottery has deposits with "Powerball," and "Mega Millions," multistate online lottery games, of \$9,048,732 at June 30, 2011. The Lottery also sold instant tab lottery tickets to non-profit organizations. These games are printed and sold by the Lottery, though are administered and paid out by the purchasing non-profit organizations.

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

State Lottery Fund

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

- Not less than 50% of the total annual revenue from Lottery ticket sales is apportioned for the payment of prizes to the holders of winning tickets for the period July 1, 2010 to June 30, 2011.

ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2011

NOTE 1 NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING
 POLICIES (Continued)

State Lottery Fund (Continued)

- Not more than 18.5% is apportioned for payment of Lottery operating expenditures. Legislation enacted in 2008 set this limit and also removed a 4% cap on advertising expenditures.

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

Cash

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

Accounts Receivable

Retailers are billed weekly for tickets sold. Payments from retailers are mainly received through electronic withdrawals from retailer accounts one week after the amounts are billed. Accounts receivable represents amounts that have been billed but not yet collected. An allowance for doubtful accounts is recorded in the amount of any balances that are not paid by retailers, generally one week after amounts are billed.

Ticket Inventory

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

Property and Equipment

Property and equipment of the Fund, which consists principally of buildings, land, land improvements, and office furniture and equipment are stated at historical cost.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized. Expenditures for normal repairs and maintenance are charged to operations as incurred, whereas expenditures for major renewals, replacements, and betterments are capitalized and depreciated. Depreciation is provided for as follows:

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

ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2011

NOTE 1 NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING
POLICIES (Continued)

Investments and Investment Income

Investments are reported at fair value on the Statement of Net Assets as determined by quoted market prices with any realized or unrealized gains and losses reported in the Statement of Revenues, Expenses and Changes in Net Assets.

Investment income from all investments is recognized by the Lottery in the period it is earned and gains and losses are recognized as revenue in the period in which they occur. Investment income also includes earnings on invested cash held by the State Treasurer and invested prize reserves held by the Multistate Lottery Association (MUSL).

Ticket Sales and Revenue Recognition

Revenue is recognized and the related direct expenses of ticket sales, including prize expense, are accrued based upon the known relationship of the amount of ticket sales to the amount of prizes for each game. This method of measuring revenue is necessary in order to properly match revenues and expenses.

Compensated Absences

Vacation leave vests with the employee as it is earned. Employees may carry forward only the amount of vacation benefits equal to the maximum allowable accumulated credits for the preceding calendar year. Accordingly, at June 30, 2011, the Fund's accounts payable and accrued expenses balance includes an accrual of vacation pay and related benefits of \$311,218. Upon termination or retirement, an employee will be compensated for accumulated leave up to a maximum of 240 hours, dependent upon accumulated time and the individual's benefits associated with their rank as defined by State personnel rule #R2-5-403. Payment will be based on the individual's rate of pay at termination or retirement. Upon death, the same benefits shall be paid to the employee's beneficiary.

Use of Estimates

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

ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2011

NOTE 2 CASH AND INVESTMENTS HELD BY THE STATE TREASURER

All cash is deposited or invested with the Arizona State Treasurer (Treasurer). The Treasurer is part of the State's financial reporting entity and issues a separately published Annual Financial Report. A copy of the Treasurer's Annual Financial Report can be obtained from its Web site at www.aztreasury.gov or by contacting the Treasurer's Office at 1700 West Washington St., 1st Floor, Phoenix, AZ, 85007-2812.

A.R.S. requires state agencies' monies to be deposited with the Treasurer, and further requires those deposits to be invested in various pooled funds. Cash and investments held by the Treasurer represent the Board's portion of those monies. The Treasurer invests idle monies of the state agencies in an internal investment pool (Pool 3) and distributes interest to the participants. Interest earned from these invested monies is allocated monthly based on the average daily balance. Participant shares in the pool are purchased and sold based on the net asset value of the shares, and a participant's portion of the pool is not identified with specific investments. Accordingly, the Board's portion of these deposits and investments approximates the Board's value of pool shares.

The Treasurer's internal investment Pool 3 is not required to be registered (and is not registered) with the Securities and Exchange Commission under the Investment Company Act of 1940. In accordance with A.R.S. §35-311, the State Board of Investments reviews the activities and performance of the pool monthly.

At June 30, 2011, the Lottery's deposits with the Treasurer were as follows:

Cash	\$ 30,769,123
Investment-Pool 3	13,073,971
	<u>\$ 43,843,094</u>

NOTE 3 TRANSFERS AND STATUTORY REQUIREMENTS

As required by ARS Section 5-505, the Lottery made transfers during the year ended June 30, 2011, as follows:

Commerce Authority Arizona Competes Fund	\$ 3,203,600
Court-appointed special advocate fund	2,381,451
Department of gaming	300,000
Economic Security Homeless Services	1,000,000
Heritage fund	10,000,000
General Fund	104,668,300
Healthy Arizona fund	18,812,000
University Bond Fund	5,963,915
	<u>\$ 146,329,266</u>
Total transfers to other State funds	<u>\$ 146,329,266</u>

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

ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2011

NOTE 4 PLEDGED REVENUES (GASB 48)

The Lottery has pledged portions of its gross revenues towards the payment of debt service on the State Lottery Revenue Bonds Series 2010A issued by the State. These bonds provide additional working capital to the State to pay appropriated expenditures of the State's General Fund. The bonds are payable solely from and secured by pledged revenues consisting of, until July 1, 2012, amounts distributable to the State General Fund from the Lottery pursuant to Lottery law, and from and after July 1, 2012, all Lottery revenues deposited to the Lottery Fund net of operating expenses of the Lottery. At June 30, 2011, pledged revenues totaled approximately \$96,200,000, of which \$21,630,000 was required to be transferred to cover debt service. Future pledged revenues required to be transferred to pay all remaining debt service for the bonds through final maturity of July 1, 2029 is approximately \$656,000,000.

NOTE 5 CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2011 is as follows:

	Beginning Balance	Increases	Decreases	Transfers	Ending Balance
Capital assets:					
Land	\$ 937,830	\$ -	\$ -	\$ -	\$ 937,830
Land improvements	330,865	-	-	-	330,865
Buildings	3,648,272	-	-	-	3,648,272
Furniture, fixtures and equipment	2,271,713	50,879	-	39,232	2,361,824
Construction in progress	83,580	32,000	-	(39,232)	76,348
Total capital assets	<u>7,272,260</u>	<u>82,879</u>	<u>-</u>	<u>-</u>	<u>7,355,139</u>
Less accumulated depreciation for:					
Land improvements	(330,865)	-	-	-	(330,865)
Buildings	(1,705,693)	(86,983)	-	-	(1,792,676)
Furniture, fixtures and equipment	<u>(1,756,775)</u>	<u>(220,413)</u>	<u>-</u>	<u>-</u>	<u>(1,977,188)</u>
Total accumulated depreciation	<u>(3,793,333)</u>	<u>(307,396)</u>	<u>-</u>	<u>-</u>	<u>(4,100,729)</u>
Total capital assets, net	<u>\$ 3,478,927</u>	<u>\$ (224,517)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 3,254,410</u>

ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2011

NOTE 6 INVESTMENTS

During the year ended June 30, 2010, the Lottery was notified that they owned common stock in publicly traded companies with a fair value of \$1,528,410. These stocks were issued to the Lottery as incentives for purchasing annuity contracts for prize payouts. The Lottery liquidated these investments during the year ended June 30, 2011.

NOTE 7 PRIZE LIABILITY

Prize liability activity for the year ended June 30, 2010, was as follows:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Prize liability	<u>\$ 26,648,369</u>	<u>\$ 363,004,319</u>	<u>\$ (360,435,477)</u>	<u>\$ 29,217,211</u>

NOTE 8 COMMITMENTS

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

Effective September 1, 2006, the Lottery entered into a five-year contract with G-Tech Services, Inc. for computer processing services at a base contract rate of 3.8012% of online sales.

NOTE 9 CONTINGENCIES

Annuities are purchased for all prizes over \$400,000 for which winners will receive the jackpot in annual installments for The Pick online game. These annuities are purchased from qualifying insurance companies, which have the highest ratings from among A.M. Best Company, Standard & Poor's, Moody's, Duff & Phelps or Weiss. The Lottery may incur future liabilities on these annuities. Aggregate future payments to prize winners on existing annuities totaled \$63,973,686 at June 30, 2011. Approximately \$46,845,976 of the total aggregate future payments at June 30, 2011, relate to annuities purchased from five separate insurance companies, of which \$12,016,972 relates to a single insurance company.

Tort claims against the Lottery, its agents, officers, and employees who are acting in the scope and course of their employment with the Lottery are covered pursuant to the State Risk Management statute, ARS § 41-621. There is no limit to that coverage. Therefore, as to any claims based on tort, there is no contingent liability to the budget of the Lottery.

ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
NOTES TO FINANCIAL STATEMENTS
June 30, 2011

NOTE 9 CONTINGENCIES (Continued)

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

NOTE 10 RETIREMENT AND PENSION PLAN

Permanent, full-time employees of the Lottery are covered by the Arizona State Retirement Plan (the "Plan"), a retirement plan administered by the Arizona State Retirement System (ASRS), which is a multiple-employer, cost-sharing pension plan.

The Comprehensive Annual Financial Report of the ASRS can be obtained by accessing www.azasrs.gov. The Plan was established by the State to provide benefits for employees of the State and employees of participating political subdivisions and school districts. The Plan became effective on July 1, 1971. By actuarial computation, employee member contributions to the Plan were fixed at 9.6%, 9.0%, and 8.95% of their compensation for the years ended June 30, 2011, 2010, and 2009, with the contributions made through payroll deduction. Employee contributions vest immediately. Total contributions to the Plan for the years ended June 30, 2011, 2010, and 2009; by the Lottery's covered employees were \$382,812, \$381,883, and \$384,476, respectively.

Matching employer member contributions were actuarially determined and fixed at 9.0%, 8.95%, and 9.10% of the compensation of all employee members for the years ended June 30, 2011, 2010, and 2009. Total matching contributions to the Plan for the years ended June 30, 2011, 2010, and 2009 by the Lottery were \$382,812, \$381,883, and \$384,476. In the event the Plan's actuary determines that additional contributions are needed in order to amortize an unfunded accrued liability, every employer member will be required to contribute the revised contribution percentage that is set by the Plan.

All full-time employees of the Lottery are required to become members of the Plan. The Lottery's total payroll for employees covered by this Plan for the years ended June 30, 2011, 2010, and 2009, was \$3,996,101, \$4,334,699, and \$4,410,518, respectively. Contributions to the Plan by the Lottery for its covered employees become fully vested immediately after membership in the Plan. All required employer contributions were made to the Plan within 30 days after June 30, 2011.

SUPPLEMENTAL INFORMATION



ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
 SUPPLEMENTAL SCHEDULE OF GROSS PROFIT BY GAME
 FOR GAMES EXPIRING DURING THE YEAR
 Year Ended June 30, 2011

	We Got Your Ticket Game 453		Vegas VIP Game 619		2X the Money Game 626	
TICKET SALES	\$ 220,444	100%	\$ 449,400	100%	\$ 2,872,642	100%
DIRECT EXPENSES:						
Commissions	14,329	6.50%	29,211	6.50%	186,722	6.50%
Prizes - low tier	114,631	52.00%	179,760	40.00%	1,407,595	49.00%
Prizes - high tier	16,800	7.62%	157,050	34.95%	455,400	15.85%
Total prizes	131,431	59.62%	336,810	74.95%	1,862,995	64.85%
Ticket purchases	26,611	12.07%	60,631	13.49%	43,794	1.52%
Total direct expenses	172,371	78.19%	426,652	94.94%	2,093,511	72.88%
GROSS PROFIT BY GAME	\$ 48,073	21.81%	\$ 22,748	5.06%	\$ 779,131	27.12%
	Money Jar Game 628		Flying Aces Game 629		Red Hot 7s Game 634	
TICKET SALES	\$ 1,108,879	100%	\$ 2,350,204	100%	\$ 9,912,650	100%
DIRECT EXPENSES:						
Commissions	72,078	6.50%	152,763	6.50%	644,322	6.50%
Prizes - low tier	559,985	50.50%	1,139,849	48.50%	5,451,958	55.00%
Prizes - high tier	126,300	11.39%	375,980	16.00%	996,429	10.05%
Total prizes	686,285	61.89%	1,515,829	64.50%	6,448,387	65.05%
Ticket purchases	38,208	3.45%	46,883	1.99%	113,705	1.15%
Total direct expenses	796,571	71.84%	1,715,475	72.99%	7,206,414	72.70%
GROSS PROFIT BY GAME	\$ 312,308	28.16%	\$ 634,729	27.01%	\$ 2,706,236	27.30%
	Wild \$\$ Doubler Game 639		4s Galore Game 640		Cactus Cash Game 641	
TICKET SALES	\$ 1,355,693	100%	\$ 2,070,434	100%	\$ 1,037,934	100%
DIRECT EXPENSES:						
Commissions	88,121	6.50%	134,578	6.50%	67,466	6.50%
Prizes - low tier	664,290	49.00%	993,808	48.00%	493,019	47.50%
Prizes - high tier	175,860	12.97%	346,900	16.75%	182,260	17.56%
Total prizes	840,150	61.97%	1,340,708	64.75%	675,279	65.06%
Ticket purchases	38,208	2.82%	43,789	2.11%	46,879	4.52%
Total direct expenses	966,479	71.29%	1,519,075	73.37%	789,624	76.08%
GROSS PROFIT BY GAME	\$ 389,214	28.71%	\$ 551,359	26.63%	\$ 248,310	23.92%

ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
 SUPPLEMENTAL SCHEDULE OF GROSS PROFIT BY GAME
 FOR GAMES EXPIRING DURING THE YEAR
 Year Ended June 30, 2011

	Roll the Dice Game 645		Crossword Clues Game 647		Super Cash Crossword Game 648	
TICKET SALES	<u>\$ 1,326,702</u>	100%	<u>\$ 24,401,625</u>	100%	<u>\$ 11,163,930</u>	100%
DIRECT EXPENSES:						
Commissions	<u>86,237</u>	6.50%	<u>1,586,107</u>	6.50%	<u>725,655</u>	6.50%
Prizes - low tier	696,521	52.50%	9,763,092	40.01%	3,936,402	35.26%
Prizes - high tier	<u>122,640</u>	9.24%	<u>7,711,870</u>	31.60%	<u>3,787,900</u>	33.93%
Total prizes	<u>819,161</u>	61.74%	<u>17,474,962</u>	71.61%	<u>7,724,302</u>	69.19%
Ticket purchases	<u>40,908</u>	3.08%	<u>275,738</u>	1.13%	<u>120,308</u>	1.08%
Total direct expenses	<u>946,306</u>	71.33%	<u>19,336,807</u>	79.24%	<u>8,570,265</u>	76.77%
GROSS PROFIT BY GAME	<u>\$ 380,396</u>	28.67%	<u>\$ 5,064,818</u>	20.76%	<u>\$ 2,593,665</u>	23.23%
	Trump Card Game 651		Sizzlin' Red 7s Game 652		Blackjack Game 654	
TICKET SALES	<u>\$ 4,357,140</u>	100%	<u>\$ 5,926,480</u>	100%	<u>\$ 1,395,819</u>	100%
DIRECT EXPENSES:						
Commissions	<u>283,216</u>	6.50%	<u>385,222</u>	6.50%	<u>90,729</u>	6.50%
Prizes - low tier	1,960,713	45.00%	2,815,277	47.50%	715,359	51.25%
Prizes - high tier	<u>1,135,300</u>	26.06%	<u>1,343,050</u>	22.66%	<u>136,960</u>	9.81%
Total prizes	<u>3,096,013</u>	71.06%	<u>4,158,327</u>	70.17%	<u>852,319</u>	61.06%
Ticket purchases	<u>78,826</u>	1.81%	<u>83,850</u>	1.41%	<u>44,820</u>	3.21%
Total direct expenses	<u>3,458,055</u>	79.37%	<u>4,627,399</u>	78.08%	<u>987,868</u>	70.77%
GROSS PROFIT BY GAME	<u>\$ 899,085</u>	20.63%	<u>\$ 1,299,081</u>	21.92%	<u>\$ 407,951</u>	29.23%
	Sparkling 7s Game 657		Bingo Game 660		Crossword Game 661	
TICKET SALES	<u>\$ 1,728,926</u>	100%	<u>\$ 20,019,366</u>	100%	<u>\$ 20,791,204</u>	100%
DIRECT EXPENSES:						
Commissions	<u>112,382</u>	6.50%	<u>1,301,259</u>	6.50%	<u>1,351,428</u>	6.50%
Prizes - low tier	847,174	49.00%	10,710,361	53.50%	10,395,602	50.00%
Prizes - high tier	<u>219,520</u>	12.70%	<u>2,113,910</u>	10.56%	<u>3,029,800</u>	14.57%
Total prizes	<u>1,066,694</u>	61.70%	<u>12,824,271</u>	64.06%	<u>13,425,402</u>	64.57%
Ticket purchases	<u>92,621</u>	5.36%	<u>398,656</u>	1.99%	<u>412,560</u>	1.98%
Total direct expenses	<u>1,271,697</u>	73.55%	<u>14,524,186</u>	72.55%	<u>15,189,390</u>	73.06%
GROSS PROFIT BY GAME	<u>\$ 457,229</u>	26.45%	<u>\$ 5,495,180</u>	27.45%	<u>\$ 5,601,814</u>	26.94%

ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
 SUPPLEMENTAL SCHEDULE OF GROSS PROFIT BY GAME
 FOR GAMES EXPIRING DURING THE YEAR
 Year Ended June 30, 2011

	Jackpot Game 663		Super Jackpot Game 664		Jumbo Jackpot Game 665	
TICKET SALES	<u>\$ 1,199,156</u>	100%	<u>\$ 2,240,288</u>	100%	<u>\$ 4,895,000</u>	100%
DIRECT EXPENSES:						
Commissions	<u>77,946</u>	6.50%	<u>145,619</u>	6.50%	<u>318,176</u>	6.50%
Prizes - low tier	608,574	50.75%	1,052,935	47.00%	2,141,564	43.75%
Prizes - high tier	<u>135,350</u>	11.29%	<u>404,050</u>	18.04%	<u>1,345,100</u>	27.48%
Total prizes	<u>743,924</u>	62.04%	<u>1,456,985</u>	65.04%	<u>3,486,664</u>	71.23%
Ticket purchases	<u>47,354</u>	3.95%	<u>48,545</u>	2.17%	<u>66,144</u>	1.35%
Total direct expenses	<u>869,224</u>	72.49%	<u>1,651,149</u>	73.70%	<u>3,870,984</u>	79.08%
GROSS PROFIT BY GAME	<u>\$ 329,932</u>	27.51%	<u>\$ 589,139</u>	26.30%	<u>\$ 1,024,016</u>	20.92%
	Super 7s Game 667		What's Your Number Game 668		Fast Cash Game 669	
TICKET SALES	<u>\$ 1,451,078</u>	100%	<u>\$ 1,329,208</u>	100%	<u>\$ 1,307,376</u>	100%
DIRECT EXPENSES:						
Commissions	<u>94,321</u>	6.50%	<u>86,400</u>	6.50%	<u>84,981</u>	6.50%
Prizes - low tier	812,604	56.00%	657,960	49.50%	647,153	49.50%
Prizes - high tier	<u>87,300</u>	6.02%	<u>161,720</u>	12.17%	<u>160,700</u>	12.29%
Total prizes	<u>899,904</u>	62.02%	<u>819,680</u>	61.67%	<u>807,853</u>	61.79%
Ticket purchases	<u>37,482</u>	2.58%	<u>40,257</u>	3.03%	<u>40,241</u>	3.08%
Total direct expenses	<u>1,031,707</u>	71.10%	<u>946,337</u>	71.20%	<u>933,075</u>	71.37%
GROSS PROFIT BY GAME	<u>\$ 419,371</u>	28.90%	<u>\$ 382,871</u>	28.80%	<u>\$ 374,301</u>	28.63%
	Blackout Bingo Game 673		Fantastic 5s Game 674		Snow Dough Game 675	
TICKET SALES	<u>\$ 9,006,730</u>	100%	<u>\$ 5,311,135</u>	100%	<u>\$ 1,349,977</u>	100%
DIRECT EXPENSES:						
Commissions	<u>585,439</u>	6.50%	<u>345,227</u>	6.50%	<u>87,750</u>	6.50%
Prizes - low tier	3,602,994	40.00%	2,655,568	50.00%	674,989	50.00%
Prizes - high tier	<u>2,818,265</u>	31.29%	<u>1,190,700</u>	22.42%	<u>149,880</u>	11.10%
Total prizes	<u>6,421,259</u>	71.29%	<u>3,846,268</u>	72.42%	<u>824,869</u>	61.10%
Ticket purchases	<u>216,369</u>	2.40%	<u>77,988</u>	1.47%	<u>46,307</u>	3.43%
Advertising			<u>-</u>	0.00%	<u>45,415</u>	3.36%
Total direct expenses	<u>7,223,067</u>	80.20%	<u>4,269,483</u>	80.39%	<u>1,004,341</u>	74.40%
GROSS PROFIT BY GAME	<u>\$ 1,783,663</u>	19.80%	<u>\$ 1,041,652</u>	19.61%	<u>\$ 345,636</u>	25.60%

ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
 SUPPLEMENTAL SCHEDULE OF GROSS PROFIT BY GAME
 FOR GAMES EXPIRING DURING THE YEAR
 Year Ended June 30, 2011

	Betty Boop Christmas Game 676		Holiday Crossword Game 677		Merry Money Game 678	
TICKET SALES	\$ 1,783,764	100%	\$ 2,374,806	100%	\$ 3,941,500	100%
DIRECT EXPENSES:						
Commissions	115,945	6.50%	154,362	6.50%	256,200	6.50%
Prizes - low tier	874,044	49.00%	1,163,655	49.00%	1,872,215	47.50%
Prizes - high tier	272,720	15.29%	375,550	15.81%	967,150	24.54%
Total prizes	1,146,764	64.29%	1,539,205	64.81%	2,839,365	72.04%
Ticket purchases	86,793	4.87%	80,496	3.39%	139,723	3.54%
Advertising	45,415	2.55%	45,415	1.91%	45,415	1.15%
Total direct expenses	1,394,917	78.20%	1,819,478	76.62%	3,280,703	83.23%
GROSS PROFIT BY GAME	\$ 388,847	21.80%	\$ 555,328	23.38%	\$ 660,797	16.77%
	Holiday Riches Game 679		Slingo Trio Game 680		Betty Boop - Valentines Game 681	
TICKET SALES	\$ 4,723,710	100%	\$ 7,439,115	100%	\$ 1,768,418	100%
DIRECT EXPENSES:						
Commissions	307,041	6.50%	483,544	6.50%	114,947	6.50%
Prizes - low tier	1,908,383	40.40%	2,603,690	35.00%	866,525	49.00%
Prizes - high tier	1,299,950	27.52%	2,693,985	36.21%	291,980	16.51%
Total prizes	3,208,333	67.92%	5,297,675	71.21%	1,158,505	65.51%
Ticket purchases	88,712	1.88%	131,366	1.77%	88,077	4.98%
Advertising	45,415	0.96%	-	0.00%	-	0.00%
Total direct expenses	3,649,501	77.26%	5,912,585	79.48%	1,361,529	76.99%
GROSS PROFIT BY GAME	\$ 1,074,209	22.74%	\$ 1,526,530	20.52%	\$ 406,889	23.01%
	Triple Cash Crossword Game 683		Extreme Cash Game 685			
TICKET SALES	\$ 11,944,077	100%	\$ 14,243,060	100%		
DIRECT EXPENSES:						
Commissions	776,367	6.50%	925,799	6.50%		
Prizes - low tier	5,156,263	43.17%	3,888,355	27.30%		
Prizes - high tier	2,428,720	20.33%	6,112,900	42.92%		
Total prizes	7,584,983	63.50%	10,001,255	70.22%		
Ticket purchases	182,464	1.53%	78,010	0.55%		
Advertising	-	0.00%	40,053	0.28%		
Total direct expenses	8,543,814	71.53%	11,045,117	77.55%		
GROSS PROFIT BY GAME	\$ 3,400,263	28.47%	\$ 3,197,943	22.45%		

ARIZONA STATE LOTTERY, A COMPONENT UNIT OF THE STATE OF ARIZONA
 SUPPLEMENTAL SCHEDULE OF GROSS PROFIT BY GAME
 FOR GAMES EXPIRING DURING THE YEAR
 Year Ended June 30, 2011

	Pick/Pick Extra Drawings January 1, 2010 to December 31, 2010		Pick 5/Pick 5 Extra Drawings January 1, 2010 to December 31, 2010		Powerball Drawings January 1, 2010 to December 31, 2010	
TICKET SALES	\$ 41,492,659	100.00%	\$ 16,540,551	100.00%	\$ 99,993,976	100.00%
DIRECT EXPENSES:						
Commissions	2,697,091	6.50%	1,075,202	6.50%	6,499,461	6.50%
Total prizes	21,084,829	50.82%	8,412,993	50.86%	49,995,488	50.00%
Online system expenses	1,533,989	3.70%	611,527	3.70%	3,695,797	3.70%
Advertising	1,047,110	2.52%	-	0.00%	2,534,025	2.53%
Total direct expenses	<u>26,363,019</u>	63.54%	<u>10,099,722</u>	61.06%	<u>62,724,771</u>	62.73%
GROSS PROFIT BY GAME	<u>\$ 15,129,640</u>	36.46%	<u>\$ 6,440,829</u>	38.94%	<u>\$ 37,269,205</u>	37.27%

	Pick 3 Drawings January 1, 2010 to December 31, 2010		Arizona Raffle Drawings January 1, 2010 to December 31, 2010		Fast Play Drawings January 1, 2010 to December 31, 2010	
TICKET SALES	\$ 8,386,169	100.00%	\$ 5,968,440	100.00%	\$ 2,025,861	100.00%
DIRECT EXPENSES:						
Commissions	545,128	6.50%	387,949	6.50%	130,833	6.46%
Total prizes	4,193,085	50.00%	3,023,699	50.66%	1,185,099	58.50%
Online system expenses	310,007	3.70%	219,505	3.68%	74,889	3.70%
Advertising	-	0.00%	1,748,974	29.30%	-	0.00%
Total direct expenses	<u>5,048,220</u>	60.20%	<u>5,380,127</u>	90.14%	<u>1,390,821</u>	68.65%
GROSS PROFIT BY GAME	<u>\$ 3,337,949</u>	39.80%	<u>\$ 588,313</u>	9.86%	<u>\$ 635,040</u>	31.35%

	Cash 4 Drawings January 1, 2010 to December 31, 2010		2 By 2 January 1, 2010 to December 31, 2010		Mega Millions January 1, 2010 to December 31, 2010	
TICKET SALES	\$ 3,036,194	100.00%	\$ 4,865,104	100.00%	\$ 26,405,725	100.00%
DIRECT EXPENSES:						
Commissions	197,353	6.50%	316,232	6.50%	1,716,366	6.50%
Total prizes	1,521,133	50.10%	2,520,122	51.80%	13,442,302	50.91%
Online system expenses	115,412	3.80%	179,785	3.70%	977,012	3.70%
Advertising	751,355	24.75%	30,148	0.62%	2,500,625	9.47%
Total direct expenses	<u>2,585,253</u>	85.15%	<u>3,046,287</u>	62.62%	<u>18,636,305</u>	70.58%
GROSS PROFIT BY GAME	<u>\$ 450,941</u>	14.85%	<u>\$ 1,818,817</u>	37.38%	<u>\$ 7,769,420</u>	29.42%

NOTE: After the announced completion of ticket sales for each game, customers have a 180-day period in which they can redeem their winning tickets. The above gross profit information includes games in which the 180-day grace period expired during the fiscal year ended June 30, 2011.

Economic Development games are denoted with (*)





HENRY & HORNE, LLP
Certified Public Accountants

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING
STANDARDS

The Commissioners
Arizona State Lottery

We have audited the financial statements of the Arizona State Lottery (the "Lottery"), as of and for the year ended June 30, 2011, and have issued our report thereon dated November 16, 2011. We conducted our audit 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Lottery's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Lottery's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Lottery's internal control over financial reporting.

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Tempe
2055 E. Warner Road
Suite 101
Tempe, AZ 85284-3487
(480) 839-4900
Fax (480) 839-1749

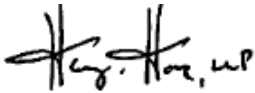
Scottsdale
7098 E. Cochise Road
Suite 100
Scottsdale, AZ 85253-4517
(480) 483-1170
Fax (480) 483-7126

Casa Grande
1115 E. Cottonwood Lane
Suite 100
Casa Grande, AZ 85122-2950
(520) 836-8201
Fax (520) 426-9432

Compliance and Other Matters

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

This report is intended solely for the information and use of the Lottery Commissioners, management, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink, appearing to read "Greg. Hae, CPA". The signature is written in a cursive style with some loops and flourishes.

Casa Grande, Arizona
November 16, 2011