



Oklahoma Lottery Commission An Enterprise Fund of the State of Oklahoma

Financial Report
June 30, 2016 and 2015

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RSM US LLP

Independent Auditor's Report

To the Board of Trustees
Oklahoma Lottery Commission
An Enterprise Fund of the State of Oklahoma
Oklahoma City, Oklahoma

Report on the Financial Statements

We have audited the accompanying financial statements of the Oklahoma Lottery Commission (the OLC), an enterprise fund of the State of Oklahoma, as of and for the years ended June 30, 2016 and 2015; and the related notes to the financial statements, which collectively comprise the OLC's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Oklahoma Lottery Commission as of June 30, 2016 and 2015, and the respective changes in financial position, and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1 of the financial statements, the financial statements present only OLC and do not purport to, and do not, present fairly the financial position of the State of Oklahoma, as of June 30, 2016 and 2015, the changes in its financial position, or, where applicable, its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, the schedule of OLC's proportionate share of the net pension liability, and the schedule of OLC's contributions be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued a report for the year ended June 30, 2016 dated September 16, 2016 and our report for the year ended June 30, 2015 dated November 12, 2015, on our consideration of the OLC's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the OLC's internal control over financial reporting and compliance.

RSM US LLP

Oklahoma City, Oklahoma
September 16, 2016

**Oklahoma Lottery Commission
An Enterprise Fund of the State of Oklahoma**

**Management's Discussion and Analysis
June 30, 2016 and 2015**

Management of the Oklahoma Lottery Commission (the OLC) provides this management's discussion and analysis of their financial performance for the readers of the OLC's financial statements. This narrative provides an overview of the OLC's financial activity for the fiscal years ended June 30, 2016 and 2015. This analysis is to be considered in conjunction with the financial statements to provide an objective analysis of the OLC's financial activities based on facts, decisions and conditions currently facing management.

Understanding the OLC's Financial Statements

The OLC, an instrumentality of the State of Oklahoma, is accounted for as an enterprise fund that reports all assets and liabilities using the accrual basis of accounting, much like a private business entity. In accordance with accounting principles generally accepted in the United States of America, this report consists of a series of financial statements, along with explanatory notes to the financial statements. The financial statements immediately follow this Management's Discussion and Analysis and are designed to highlight the OLC's net position and changes to its net position resulting from the OLC's operations.

The most important relationship demonstrated within the OLC's financial statements is the requirement that the OLC transfer all net proceeds, "as defined," to the State Treasurer for the Oklahoma Education Lottery Trust Fund (OELTF). Accordingly, a significant focus of these financial statements is determining net proceeds available for transfer to the OELTF.

The OLC is also required to transfer annually the first \$750,000, for both 2016 and 2015, of unclaimed prize money to the Oklahoma Department of Mental Health and Substance Abuse Services (ODMHSAS). This is discussed further on page 6 of the management's discussion and analysis.

Financial and Activity Highlights

Revenues from lottery games totaled \$189,621,594 and \$171,633,476, respectively, for the fiscal years ending June 30, 2016 and 2015. The OLC returned \$95,517,232 and \$87,782,927 to winners of lottery games; paid commissions and incentives to retailers totaling \$12,421,019 and \$11,425,710; incurred other game related expenses of \$7,985,458 and \$7,271,417; and had operating expenses of \$4,465,112 and \$5,394,206 for each of the respective fiscal years of 2016 and 2015. The OLC's net position increased by \$2,528,359 in fiscal year 2016 and decreased by \$745,750 in fiscal year 2015 after the cumulative effect of accounting changes. Transfers made and due to the OELTF were \$66,406,789 and \$60,111,343, respectively, for fiscal years ending June 30, 2016 and 2015.

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Management's Discussion and Analysis
June 30, 2016 and 2015

The following table summarizes the OLC's Statement of Net Position as of June 30:

	2016	2015	2014
Current assets	\$ 35,941,023	\$ 22,955,061	\$ 29,238,675
Noncurrent assets:			
Capital assets, net	73,182	94,739	61,281
Deposit with MUSL	4,615,654	4,829,218	5,856,283
Total assets	<u>\$ 40,629,859</u>	<u>\$ 27,879,018</u>	<u>\$ 35,156,239</u>
Deferred outflows of resources	<u>\$ 531,815</u>	<u>\$ 265,713</u>	<u>\$ -</u>
Current liabilities	\$ 27,899,129	\$ 17,410,986	\$ 23,702,866
Noncurrent liabilities	385,097	229,307	58,316
Total liabilities	<u>\$ 28,284,226</u>	<u>\$ 17,640,293</u>	<u>\$ 23,761,182</u>
Deferred inflows of resources	<u>\$ 452,993</u>	<u>\$ 608,342</u>	<u>\$ -</u>
Net position			
Net position, invested in capital assets	\$ 73,182	\$ 94,739	\$ 61,281
Restricted net position—expendable	12,351,273	9,801,357	11,333,776
Total net position	<u>\$ 12,424,455</u>	<u>\$ 9,896,096</u>	<u>\$ 11,395,057</u>

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**Management's Discussion and Analysis
June 30, 2016 and 2015**

The following table summarizes the OLC's statement of revenues, expenses, and changes in net position for the years ended June 30:

	2016	2015	2014
Operating revenues:			
Gaming revenues	\$ 189,621,594	\$ 171,633,476	\$ 191,127,092
Other revenues	112,090	113,220	113,250
Total operating revenues	<u>189,733,684</u>	<u>171,746,696</u>	<u>191,240,342</u>
Nonoperating revenue, interest income	340,285	243,157	323,723
Total revenue	<u>\$ 190,073,969</u>	<u>\$ 171,989,853</u>	<u>\$ 191,564,065</u>
Less prize expense	\$ 95,517,232	\$ 87,782,927	\$ 97,496,555
Less retailer commissions/incentives	12,421,019	11,425,710	12,647,675
Less other direct game costs	7,985,458	7,271,417	7,798,373
Less operating expenses	4,465,112	5,394,206	4,486,957
Total expense	<u>120,388,821</u>	<u>111,874,260</u>	<u>122,429,560</u>
Nonoperating revenue (expense):			
Transfers to ODMHSAS	750,000	750,000	750,000
Transfers to OELTF	66,406,789	60,111,343	66,934,120
Nonoperating expense	<u>67,156,789</u>	<u>60,861,343</u>	<u>67,684,120</u>
Total expense	<u>\$ 187,545,610</u>	<u>\$ 172,735,603</u>	<u>\$ 190,113,680</u>
Changes in net position	\$ 2,528,359	\$ (745,750)	\$ 1,450,385
Net position at beginning of year	9,896,096	11,395,057	9,944,672
Restatement—Implementation of GASB 68 and 71	-	(753,211)	-
	<u>9,896,096</u>	<u>10,641,846</u>	<u>9,944,672</u>
Net position at end of year	<u>\$ 12,424,455</u>	<u>\$ 9,896,096</u>	<u>\$ 11,395,057</u>

Sales increased from fiscal year 2015 to fiscal year 2016. Online sales during this period increased mostly because of Power Ball sales. In FY 16, the OLC had only one jackpot over \$500 million. Powerball sales are significantly up in FY 16 compared to FY 15, due to the large jackpot that occurred on January 16, 2016. The jackpot amount reached \$1.59 billion dollars. There was also a decrease in overall scratcher sales from fiscal year 2015 to fiscal year 2016. The OLC slightly reduced prize payouts in fiscal 2014 to adjust to fluctuations in costs, because of this scratcher sales have continued to decline in fiscal year's 2015 and 2016.

Sales decreased from fiscal year 2014 to fiscal year 2015. Online sales during this period decreased mostly because of Power Ball sales. In fiscal year 2014, there were 11 jackpots with an average jackpot amount of \$209 million. In fiscal year 2015, there were 13 jackpots with an average jackpot amount of \$153 million. When jackpots are lower revenue tends to be lower. There was also a decrease in overall scratcher sales from fiscal year 2014 to fiscal year 2015. The OLC slightly reduced prize payouts in fiscal 2014 to adjust to fluctuations in costs, because of this scratcher sales have continued to decline in fiscal year 2015.

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**Management's Discussion and Analysis
June 30, 2016 and 2015**

Net proceeds of the OLC must be transferred to the State Treasurer for the OELTF, with the following exceptions: 1) the cost of property and equipment, net of depreciation, and related debt and 2) other assets that cannot be transferred due to statutory or other legal restriction, including restricted cash from unclaimed prizes, deposits with Multi-State Lottery (MUSL), and the Restricted Fidelity Fund. Unclaimed prizes, after required transfers to the Department of Mental Health and Substance Abuse Services, must be added to a pool from which future prizes are awarded or used for special prize promotions. Deposits with MUSL result from a set-aside of prize expenses paid to MUSL and are available for prize reserves and promotional expenses of MUSL games. The Restricted Fidelity Fund is derived from the licensing fees of new retailers, which may be retained by the OLC up to the budgeted expenses from the fund for the next fiscal year plus \$500,000, in 2015 and 2014, and used to cover losses the OLC may experience due to nonfeasance, misfeasance or malfeasance of a lottery retailer and to pay the costs of vendor, retailer and employee background investigations conducted by the Oklahoma State Bureau of Investigation and for audits conducted by the State Auditor and Inspector.

For the years ended June 30, 2016 and 2015, the total transfers made or due to the OELTF related to operations were \$66,406,789 and \$60,111,343, respectively. Since inception to June 30, 2016, total transfers made or due to the OELTF were \$745,793,919. For each of the years ended June 30, 2016 and 2015, the OLC transferred \$750,000 in unclaimed prize funds to the Department of Mental Health and Substance Abuse Services for the treatment of compulsive gambling disorders and educational programs related to such disorders. From inception to June 30, 2016, total transfers to the Oklahoma Department of Mental Health and Substance Abuse Services were \$5,794,600.

The following is a condensed version of the OLC's statement of cash flows for the years ended June 30:

	2016	2015	2014
Cash provided by (used in):			
Operating activities	\$ 71,403,997	\$ 62,419,502	\$ 67,031,666
Noncapital financing activities	(58,257,720)	(68,893,217)	(69,446,790)
Capital and related financing activities	(11,978)	(71,380)	(14,144)
Investing activities	322,477	252,739	329,721
Net increase (decrease) in cash	13,456,776	(6,292,356)	(2,099,547)
Cash at beginning of year	16,801,831	23,094,187	25,193,734
Cash at end of year	<u>\$ 30,258,607</u>	<u>\$ 16,801,831</u>	<u>\$ 23,094,187</u>

Potential Factors Impacting Future Operations

Future operations always have the potential to be impacted by economic factors and rising costs. The OLC strives to maximize the contribution to education, while maintaining new and entertaining games that engage players. In order to meet these goals, the OLC strives to keep costs low and introduce new games regularly. The OLC is always looking for opportunities to participate in new regional and multi state games. The OLC is also trying to develop new local games to stay up-to-date with player demands.

Contacting the OLC's Financial Management

This financial report is designed to provide a general overview of the OLC's financial activity for all those interested in the OLC's operations. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Executive Director, Oklahoma Lottery Commission, 405-522-7700, 3817 North Santa Fe, Oklahoma City, Oklahoma 73118.

Oklahoma Lottery Commission
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Statements of Net Position
June 30, 2016 and 2015

	2016	2015
Assets		
Current assets:		
Cash and cash equivalents	\$ 22,285,837	\$ 11,321,420
Cash equivalents—restricted	7,972,770	5,480,411
Retailer accounts receivable	5,175,739	5,801,220
Accounts receivable—Multi-State Lottery	506,677	352,010
Total current assets	35,941,023	22,955,061
Noncurrent assets:		
Capital assets, net	73,182	94,739
Deposit with Multi-State Lottery	4,615,654	4,829,218
Total noncurrent assets	4,688,836	4,923,957
Total assets	\$ 40,629,859	\$ 27,879,018
Deferred outflows of resources:		
Deferred pension plan outflows	\$ 531,815	\$ 265,713
Liabilities		
Current liabilities:		
Due to Oklahoma Education Lottery Trust Fund	\$ 17,998,490	\$ 9,099,421
Due to Multi-State Lottery	1,427,206	741,878
Prizes payable	7,174,144	6,467,578
Accounts payable	624,466	577,476
Accrued liabilities	166,289	143,820
Unearned revenue	508,534	380,813
Total current liabilities	27,899,129	17,410,986
Noncurrent liabilities:		
Accrued compensated absences	69,124	63,683
Net pension liability	315,973	165,624
Total noncurrent liabilities	385,097	229,307
Total liabilities	\$ 28,284,226	\$ 17,640,293
Deferred inflows of resources:		
Deferred pension plan inflows	\$ 452,993	\$ 608,342
Net position:		
Investment in capital assets	\$ 73,182	\$ 94,739
Restricted net position—expendable	12,351,273	9,801,357
Total net position	\$ 12,424,455	\$ 9,896,096

See notes to financial statements.

Oklahoma Lottery Commission
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Statements of Revenues, Expenses, and Changes in Net Position
Years Ended June 30, 2016 and 2015

	2016	2015
Operating revenues:		
Scratcher games	\$ 78,559,351	\$ 81,600,192
Pick 3 game	5,320,251	5,250,569
Cash 5 game	4,105,388	4,212,739
Poker Pick game	1,322,221	2,040,522
Hot Lotto game	7,801,035	9,917,136
Mega Millions game	19,470,982	22,099,568
Powerball game	73,042,366	46,512,750
Total revenue from the sale of lottery tickets	189,621,594	171,633,476
Retailer application fees	105,390	105,245
Other	6,700	7,975
Total operating revenues	189,733,684	171,746,696
Direct costs:		
Prize expense:		
Scratcher games	42,797,935	44,669,301
Pick 3 game	2,494,230	2,518,670
Cash 5 game	1,676,095	1,849,789
Poker Pick game	756,160	1,018,738
Hot Lotto game	3,811,922	4,621,711
Mega Millions game	9,360,915	10,669,022
Powerball game	34,619,975	22,435,696
Total prize expense	95,517,232	87,782,927
Commissions and incentives to retailers	12,421,019	11,425,710
Instant and online costs	7,985,458	7,271,417
Total direct costs	115,923,709	106,480,054
Gross profit	73,809,975	65,266,642
Operating expenses:		
Advertising and promotion	1,767,255	2,743,837
Salaries, wages and benefits	2,184,676	2,129,873
Contracted and professional services	181,897	163,050
Depreciation	33,535	37,922
Equipment	12,626	18,186
Rent expense	150,092	166,777
Office supplies	18,696	17,720
Travel	19,626	20,171
Other general and administrative	96,709	96,670
Total operating expenses	4,465,112	5,394,206
Operating income	69,344,863	59,872,436

(Continued)

Oklahoma Lottery Commission
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Statements of Revenues, Expenses, and Changes in Net Position (Continued)
Years Ended June 30, 2016 and 2015

	2016	2015
Nonoperating income (expense):		
Interest income	\$ 340,285	\$ 243,157
Transfers to Oklahoma Department of Mental Health and Substance Abuse Services	(750,000)	(750,000)
Transfers to and due to Oklahoma Education Lottery Trust Fund	(66,406,789)	(60,111,343)
Net nonoperating income (expense)	(66,816,504)	(60,618,186)
Changes in net position	2,528,359	(745,750)
Net position at beginning of year	9,896,096	11,395,057
Restatement—Implementation of GASB 68 and 71	-	(753,211)
Net position at beginning of year, as restated	9,896,096	10,641,846
Net position at end of year	\$ 12,424,455	\$ 9,896,096

See notes to financial statements.

Oklahoma Lottery Commission
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Statements of Cash Flows
Years Ended June 30, 2016 and 2015

	2016	2015
Cash flows from operating activities:		
Cash received from retailers	\$ 177,892,331	\$ 160,298,299
Cash payments to prize winners	(94,125,338)	(86,015,232)
Cash payments to suppliers for goods and services	(10,148,692)	(10,501,074)
Cash payments to employees for services	(2,427,868)	(2,389,556)
Cash receipts to fund deposit with Multi-State Lottery	213,564	1,027,065
Net cash provided by operating activities	71,403,997	62,419,502
Cash flows from noncapital financing activities:		
Payments to Oklahoma Department of Mental Health and Substance Abuse Services	(750,000)	(750,000)
Payments to Oklahoma Education Lottery Trust Fund	(57,507,720)	(68,143,217)
Net cash used in noncapital financing activities	(58,257,720)	(68,893,217)
Cash flows from capital and related financing activities:		
Purchase of capital assets	(11,978)	(71,380)
Cash flows from investing activities:		
Interest received	322,477	252,739
Net change in cash and cash equivalents	13,456,776	(6,292,356)
Cash and cash equivalents at beginning of year	16,801,831	23,094,187
Cash and cash equivalents at end of year	\$ 30,258,607	\$ 16,801,831
Operating activities:		
Operating income	\$ 69,344,863	\$ 59,872,436
Adjustment to reconcile operating income to net cash provided by operating activities:		
Depreciation	33,535	37,922
Bad debt expense	37,379	7,105
Changes in operating assets, deferred outflows, liabilities and deferred inflows:		
Retailer accounts receivable	605,910	72,855
Accounts receivable—Multi-State Lottery	(154,667)	(98,284)
Deposit with Multi-State Lottery	213,564	1,027,065
Deferred pension plan outflows	(266,102)	(13,493)
Due to Multi-State Lottery	685,328	36,856
Accounts payable and accrued liabilities	74,900	(41,456)
Prizes payable	706,566	1,730,839
Net pension liability	150,349	(839,807)
Unearned revenue	127,721	19,122
Deferred pension plan inflows	(155,349)	608,342
Net cash provided by operating activities	\$ 71,403,997	\$ 62,419,502

See notes to financial statements.

**Oklahoma Lottery Commission
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Notes to Financial Statements

Note 1. Reporting Entity

The Oklahoma Lottery Commission (the OLC), was formed by the citizens of Oklahoma upon passage of a legislative referendum authorizing the Oklahoma Education Lottery Act (the Act), codified as Title 3A, Section 701, et. seq., of the Oklahoma Statutes. The OLC is an enterprise fund of the State of Oklahoma (the State) responsible for administering lotteries in accordance with the Act. The Act established a board of seven trustees appointed by the governor to oversee operations of the OLC. The OLC transfers net proceeds as defined by the Act.

Note 2. Significant Accounting Policies

Method of accounting: The OLC is accounted for as an enterprise fund. Enterprise funds are used to account for activities that are financed and operated in a manner similar to private business enterprises where the costs of providing lottery games to the general public on a continuing basis are to be financed through the sale of lottery game tickets. The Act requires that all costs of providing lottery games, including capital costs, be recovered from the sale of lottery game tickets.

The Governmental Accounting Standards Board (GASB) is the recognized standard-setting body for accounting principles generally accepted applicable to governmental proprietary activities in the United States of America. The OLC applies all applicable GASB pronouncements.

Basis of accounting: The financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. Under this method, revenues are recognized when they are earned, and expenses are recognized when they are incurred.

The primary operating revenue of the OLC is ticket sales from games. Nonoperating income primarily consists of interest income. "Operating expenses" are defined under the Act as "all costs of doing business, including but not limited to prizes, commissions, and other compensation paid to retailers, advertising and marketing costs, personnel costs, capital costs, amounts held in or paid from the fidelity revolving fund, administration and operation of the OLC and other operating costs." All expenses not meeting this definition are reported as nonoperating expenses. The only nonoperating expenses are statutory required transfers to the Oklahoma Education Lottery Trust Fund (OELTF) and the Oklahoma Department of Mental Health and Substance Abuse Services.

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 disclosures 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.

Revenue recognition: Revenue for Pick 3, Cash 5, Poker Pick, Hot Lotto, Mega Millions, and Powerball (collectively referred to as online games) is recognized when tickets are sold to the public by contracted retailers, except for tickets sold in advance of the draw date for which unearned revenue is recorded. Revenue for scratcher games is recognized upon activation of ticket packs for sale by the retailers.

Every scratcher ticket game has a predetermined number of free tickets in its prize structure. The majority of free tickets relate to scratcher ticket games. Revenue and prize expense are shown net of free tickets.

Commissions: Retailers receive a 6 percent commission on total sales and 0.75 percent commission on prizes cashed.

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Notes to Financial Statements

Note 2. Significant Accounting Policies (Continued)

Prizes: Prize expense for scratcher ticket games is recorded at the time the related revenue is recognized based on the predetermined prize structure for each game; periodically, the prize expense is adjusted for unclaimed prizes. Prize expense for online games is recorded at the time the related revenue is recognized based on the known prizes.

Unclaimed prizes: Prizes must be claimed within 90 days after the game-end (end of sales) for scratcher games and within 180 days after the draw date for online games. The first \$750,000 for fiscal year 2016 and 2015 of unclaimed prize money accruing annually must be transferred to the Oklahoma Department of Mental Health and Substance Abuse Services for the treatment of compulsive gambling disorders and educational programs related to such disorders.

In accordance with section 724 of the Act, unclaimed prizes are added to a pool from which future prizes are awarded or used for special prize promotions. Under the Act, unclaimed prizes do not constitute net lottery proceeds and are restricted funds that are not available for transfer to the OELTF. Total unclaimed prizes amounted to \$5,478,051 and \$4,459,518 for fiscal years 2016 and 2015, respectively. Unclaimed prizes are netted against prize expense in the statement of revenues, expenses, and changes in net position.

Pensions: For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Oklahoma Public Retirement System (OPERS) and additions to/ deductions from OPERS' and fiduciary net position have been determined on the same basis as they are reported by OPERS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Deferred inflows of resources: Deferred inflows of resources are the acquisition of net position by the OLC that are applicable to a future reporting period. At June 30, 2016 and 2015, the OLC had deferred inflows of resources of \$452,993 and \$608,342, respectively. See Note 8 for additional discussion regarding deferred inflows of resources.

Deferred outflows of resources: Deferred outflows of resources are the consumption of net position by the OLC that are applicable to a future reporting period. At June 30, 2016 and 2015, the OLC had deferred outflows of resources of \$531,815 and \$265,713, respectively. See Note 8 for additional discussion regarding deferred outflows of resources.

Net position: The OLC's net position is classified as follows.

Investment in capital assets: This represents the OLC's total investment in capital assets.

Restricted net position, expendable: Net position not invested in capital is restricted by state statute. Restricted net position consists primarily of cash maintained in the OLC's restricted fidelity fund, deposits with the Multi-State Lottery (MUSL), and balance of unclaimed prizes to be used on future prizes or special prize promotions.

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Notes to Financial Statements

Note 2. Significant Accounting Policies (Continued)

Gross proceeds: Gross proceeds, as defined by the Act, consist of all revenue derived from the sale of lottery game tickets or shares and all other monies derived from the lottery games.

Operating expenses: Operating expenses, as defined by the Act, in the determination of net proceeds, consist of all costs of doing business including, but not limited to, prizes, commissions, and other compensation paid to lottery retailers, advertising and marketing costs, rental fees, personnel costs, capital costs, depreciation of property and equipment, and other operating costs.

Cash and cash equivalents: The OLC's cash and cash equivalents are considered to be cash on hand and on interest in an internal investment pool held by the Oklahoma State Treasurer.

Retailer accounts receivable: Retailer accounts receivable represents lottery proceeds due from retailers for online ticket sales and activated ticket packs for scratcher games, less commissions due to retailers and prizes paid by the retailers. Lottery proceeds are collected weekly by the OLC from retailer trust accounts established in trust for benefit of the OLC.

Capital assets, net: Capital assets, which consist of machinery, equipment, computers and software, are stated at cost less accumulated depreciation. The OLC capitalizes all property and equipment purchases of \$500 or more. Depreciation is computed using the straight-line method over the following estimated useful lives: machinery and equipment—five to ten years; computers and software—three to five years. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is reflected in the results from operations in the period of disposal.

Restricted cash: In accordance with the Act, retailers contribute a fee to a fidelity fund upon acceptance as a retailer for the OLC. The fund is used to cover losses the OLC may incur due to misfeasance, nonfeasance, or malfeasance of retailers and to contract for investigations, reviews, or audits. At the end of any fiscal year, the OLC must transfer to the OELTF any amount in the restricted fidelity fund which exceeds the budgeted expenses from the fund for the next fiscal year plus \$500,000 for both fiscal years 2016 and 2015. At June 30, 2016 and 2015, no amounts were available for transfer as net proceeds. During fiscal years 2016 and 2015, \$80,441 and \$163,464, respectively, was used to reimburse the OLC for retailer accounts that were delinquent and in collection status and for the retailer application fees. Receipts from retailers in collection status are deposited back to the fidelity fund. The fidelity fund is held in a separate account. As of June 30, 2016 and 2015, the balance in the fidelity fund totaled \$133,103 and \$172,576, respectively and appears in the accompanying statement of net position as restricted funds and expendable restricted net position.

Current unclaimed prizes in excess of \$750,000 for both fiscal years 2016 and 2015, and the balance from prior years are included in restricted cash in the accompanying statement of net position and expendable restricted net position. These funds are to be utilized to enhance future OLC prizes or promotions and totaled \$7,839,667 and \$5,307,835 as of June 30, 2016 and 2015, respectively.

Risk management: The OLC is exposed to various risks of loss related to torts, destruction of assets due to theft or damage, errors and omissions, injuries to employees, and natural disasters. The OLC has coverage to substantially cover these risks through a self-insured pool for agencies of the State of Oklahoma. This coverage is administered by the Risk Management Division of the Department of Central Services for the State of Oklahoma.

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Notes to Financial Statements

Note 2. Significant Accounting Policies (Continued)

Compensated absences: Employees earn the right to be compensated during absences for vacation and compensatory time. Unused leave benefits are paid to employees upon separation from service. The cost of vacation and compensatory time is accrued in the period in which it is earned.

Bad-debt expense: The OLC recognizes bad-debt expense when retailer account receivables are greater than 90 days old. The accounts receivable balance due to the OLC is satisfied at that time by a transfer of funds from the restricted fidelity fund. The OLC may continue its effort to collect these accounts. Any collection from a retailer balance previously charged to bad-debt expense will be deposited back to the restricted fidelity fund. For the years ended June 30, 2016 and 2015, bad-debt expense was \$37,379 and \$7,105, respectively.

New accounting pronouncement adopted in fiscal year 2016: The OLC adopted the following new accounting pronouncement during the year ended June 30, 2016:

GASB Statement No. 72, *Fair Value Measurement and Application*, issued February 2015, defines fair value and describes how fair value should be measured, what assets and liabilities should be measured at fair value, and what information about fair value should be disclosed in the notes to the financial statements. This Statement defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Investments, which generally are measured at fair value, are defined as a security or other asset that governments hold primarily for the purpose of income or profit and the present service capacity of which are based solely on their ability to generate cash or to be sold to generate cash. The adoption of this pronouncement did not have a material impact on the OLC.

New accounting pronouncements issued not yet adopted: The GASB has issued a new accounting pronouncement which will be effective to OLC in fiscal years ended June 30, 2017. OLC is currently evaluating the impact that this new standard will have on its financial statements. A description of the new accounting pronouncement is described below:

GASB Statement No. 82, *Pension Issues*, issued April 2016, is designed to improve consistency in the application of the pension standards by clarifying or amending related areas of existing guidance with respect to Statements No. 67, *Financial Reporting for Pension Plans*, No. 68, *Accounting and Financial Reporting for Pensions*, and No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. Specifically, this Statement addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements.

Reclassifications: Certain amounts in the 2015 financial statements have been reclassified to conform to the current year presentation. These reclassifications had no impact on total net position or changes in net position.

**Oklahoma Lottery Commission
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Notes to Financial Statements

Note 3. Cash and Cash Equivalents

The OLC's investment in OK INVEST is carried at \$30,258,607 and \$16,801,831 at June 30, 2016 and 2015, respectively. Cash equivalents are recorded at cost. The OLC obtained the fair value from the State Treasurer of their interest in the pool, which amounted to \$30,724,189 and \$16,984,862 at June 30, 2016 and 2015, respectively. Management believes the difference between cost and fair value is immaterial to the financial statements as a whole due to the short duration of investments held by the pool and information provided by the State.

Agencies and funds that are considered to be part of the State's reporting entity in the State's Comprehensive Annual Financial Report are allowed to participate in OK INVEST. Oklahoma statutes and the State Treasurer establish the primary objectives and guidelines governing the investment of funds in OK INVEST. Safety, liquidity, and return on investment are the objectives that establish the framework for the day-to-day OK INVEST management, with an emphasis on safety of the capital and the probable income to be derived and meeting the State and its funds' and agencies' daily cash flow requirements. Guidelines in the Investment Policy address credit quality requirements, diversification percentages and the types and maturities of allowable investments. The specifics regarding these policies can be found on the State Treasurer's website at <http://www.ok.gov/treasurer>. The State Treasurer, at his discretion, may further limit or restrict such investments on a day-to-day basis. OK INVEST includes a substantial investment in securities with an overnight maturity as well as in U.S. government securities with a maturity of up to three years. OK INVEST maintains an overall weighted average maturity of less than 270 days.

Participants in OK INVEST maintain interest in its underlying investments and, accordingly, may be exposed to certain risks. As stated in the State Treasurer information statement, the main risks are interest rate risk, credit/ default risk, liquidity risk, and U.S. government securities risk. Interest rate risk is the risk that during periods of rising interest rates, the yield and market value of the securities will tend to be lower than prevailing market rates; in periods of falling interest rates, the yield will tend to be higher.

Custodial credit risk of investments is the risk that in the event of a bank failure, the government's investments may not be returned to it. Interest in OK INVEST are not insured or guaranteed by the State, the FDIC, or any other government agency.

**Oklahoma Lottery Commission
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Notes to Financial Statements

Note 4. Capital Assets, Net

The following is a summary of changes in capital assets and accumulated depreciation during the years ended June 30, 2016 and 2015:

Capital Assets	Year Ended June 30, 2016			
	Beginning Balance	Additions	Deletions	Ending Balance
Machinery and equipment	\$ 855,604	\$ 11,978	\$ -	\$ 867,582
Computers and software	409,567	-	-	409,567
	<u>1,265,171</u>	<u>11,978</u>	<u>-</u>	<u>1,277,149</u>
Accumulated depreciation:				
Machinery and equipment	766,595	30,354	-	796,949
Computers and software	403,837	3,181	-	407,018
	<u>1,170,432</u>	<u>33,535</u>	<u>-</u>	<u>1,203,967</u>
Total capital assets, net	<u>\$ 94,739</u>	<u>\$ (21,557)</u>	<u>\$ -</u>	<u>\$ 73,182</u>

Capital Assets	Year Ended June 30, 2015			
	Beginning Balance	Additions	Deletions	Ending Balance
Machinery and equipment	\$ 788,646	\$ 66,958	\$ -	\$ 855,604
Computers and software	405,145	4,422	-	409,567
	<u>1,193,791</u>	<u>71,380</u>	<u>-</u>	<u>1,265,171</u>
Accumulated depreciation:				
Machinery and equipment	731,197	35,398	-	766,595
Computers and software	401,313	2,524	-	403,837
	<u>1,132,510</u>	<u>37,922</u>	<u>-</u>	<u>1,170,432</u>
Total capital assets, net	<u>\$ 61,281</u>	<u>\$ 33,458</u>	<u>\$ -</u>	<u>\$ 94,739</u>

Note 5. Compensated Absences

The current portion of accrued compensated absences is included in accrued liabilities in the accompanying statements of net position. The following is a summary of changes in the OLC's liability for compensated absences during the year ended June 30:

	Beginning Balance	Additions	Deletions	Ending Balance	Current Portion
Compensated absences 2016	<u>\$ 191,049</u>	<u>\$ 118,581</u>	<u>\$ 102,260</u>	<u>\$ 207,370</u>	<u>\$ 138,246</u>
Compensated absences 2015	<u>\$ 174,948</u>	<u>\$ 113,710</u>	<u>\$ 97,609</u>	<u>\$ 191,049</u>	<u>\$ 127,366</u>

Note 6. Operating Leases

The OLC has entered into various operating leases for office space and equipment used in its daily operations. Pursuant to Oklahoma State Statutes, the OLC's operating leases are limited to terms of one year and must be renewed annually. Accordingly, the OLC has no long-term commitments under the operating leases as of June 30, 2016 or 2015. Rent expense under all operating leases was \$150,092 for the year ended June 30, 2016, and \$166,777 for the year ended June 30, 2015.

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Notes to Financial Statements

Note 7. Education Lottery Account

In accordance with the Act, all net proceeds of the OLC are transferred to the Education Lottery Account. Net proceeds consist of all revenue derived from the sale of lottery game tickets or shares and all other monies derived from the lottery games, less operating expenses and prizes. OLC estimates that net proceeds will approximate 35 percent of total revenue. Each month, OLC transfers the amounts necessary to satisfy appropriations made by the Legislature to Higher Education and Common Education. Each quarter, OLC transfers amounts to cover the appropriations to Career Tech, Teachers' Retirement and the Voluntary School Consolidation Fund. OLC transfers the remaining 35 percent of revenues plus any additional profits, unless specifically exempted by statute, at the end of the year. According to the Act, amounts transferred to the OELTF are to be appropriated by the legislature to education programs according to the parameters established in the Act. Following is an executive summary of these statutory provisions. For the full text, see Title 3A, Section 713 of the Oklahoma Statutes, available on the OLC website.

- 5 percent Teachers' Retirement System Dedicated Revenue Revolving Fund
- 5 percent School Consolidation and Assistance Fund (SCAF): If the SCAF equals \$5,000,000, this 5 percent will be allocated to public schools to purchase technology equipment to conduct on-line testing
- 45 percent Kindergarten through twelfth grade public education, including compensation and benefits for public school teachers and support employees, and early childhood development programs
- 45 percent Tuition grants, loans, and scholarships to citizens of this state for attending colleges and universities located within this state or to attend Oklahoma Department of Career and Technology Education institutions; construction of educational facilities or capital outlay projects or technology for elementary school districts, independent school districts, the Oklahoma State System of Higher Education, and career and technology education; endowed chairs for professors at institutions of higher education operated by the Oklahoma State System of Higher Education; and programs and personnel of the Oklahoma School for the Deaf and the Oklahoma School for the Blind

The following is a summary of the amounts available for transfer to the OELTF during the years ended June 30, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Net position, beginning of year	\$ 9,896,096	\$ 11,395,057
Restatement - implementation of GASB 68 and 71	-	(753,211)
Change in net position before transfers to OELTF	<u>68,935,148</u>	<u>59,365,593</u>
Net position available for transfer to OELTF before capital assets and assets restricted from transfer	78,831,244	70,007,439
Less capital assets, net of accumulated depreciation	(73,182)	(94,739)
Less assets restricted from transfer	<u>(12,588,424)</u>	<u>(10,309,629)</u>
Net position available for transfer to OELTF	<u>\$ 66,169,638</u>	<u>\$ 59,603,071</u>

Actual transfers to and due to OELTF for the years ended June 30, 2016 and 2015 totaled \$66,406,789 and \$60,111,343, respectively. Actual transfers exceeded amounts available for transfer due to pension activity being unknown at the time of calculation and therefore being excluded.

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Notes to Financial Statements

Note 8. Retirement Program

Plan description: The OLC contributes to the Oklahoma Public Employees Retirement System (OPERS) cost sharing multiple-employer defined benefit plan. OPERS was established in 1964 by the Oklahoma Legislature and covers substantially all employees of the State, except those covered by six other plans sponsored by the State, and also covers employees of participating counties and local agencies. The plan provides that all eligible persons, except those specifically excluded, shall become members of OPERS as a condition of their employment. The supervisory authority for the management and operation of OPERS is its Board of Trustees.

OPERS offers retirement and disability benefits, cost of living adjustments on an ad-hoc basis, life insurance benefits, and survivor benefits. The Plan's provisions are established under Title 74 of the Oklahoma Statutes.

Benefits provided: Members qualify for full retirement benefits at their specified normal retirement age or, for any person who became a member prior to July 1, 1992, when the sum of the member's age and years of credited service equals or exceeds 80 (Rule of 80), and for any person who became a member after June 30, 1992, when the member's age and years of credited service equals or exceeds 90 (Rule of 90).

Normal retirement date is further qualified to require that all members employed on or after January 1, 1983 must have six or more years of full-time equivalent employment with a participating employer before being eligible to receive benefits. Credited service is the sum of participating and prior service. Prior service includes nonparticipating service before January 1, 1975, or the entry date of the employer and active wartime military service.

A member with a minimum of ten years of participating service may elect early retirement with reduced benefits beginning at age 55 if the participant became a member prior to November 1, 2011, or age 60 if the participant became a member on or after November 1, 2011.

Disability retirement benefits are available for members having eight years of credited service whose disability status has been certified as being within one year of the last day on the job by the Social Security Administration. Disability retirement benefits are determined in the same manner as retirement benefits, but payable immediately without an actuarial reduction.

Benefits are determined at 2 percent of the average annual salary received during the highest thirty-six months of the last ten years of participating service, but not to exceed the applicable annual salary cap, multiplied by the number of years of credited service. Members who join OPERS on or after July 1, 2013, will have their salary averaged over the highest 60 months of the last ten years. Normal retirement age under the Plan is 62 or Rule of 80/90 if the participant became a member prior to November 1, 2011, or age 65 or Rule of 90 if the participant became a member on or after November 1, 2011.

Members who elect to pay the additional contribution rate, which became available in January 2004, will receive benefits using a 2.5 percent computation factor for each full year the additional contributions are made. In 2004, legislation was enacted to provide an increased benefit to retiring members who were not yet eligible for Medicare. The Medicare Gap benefit option became available to members under age 65 who retired on or after May 1, 2006. Members may elect to receive a temporary increased benefit to cover the cost of health insurance premiums until the member is eligible to receive Medicare. After the member becomes eligible for Medicare, the retirement benefit will be permanently reduced by an actuarially determined amount. The option is irrevocable, must be chosen prior to retirement, and is structured to have a neutral actuarial cost to the Plan.

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Notes to Financial Statements

Note 8. Retirement Program (Continued)

Members become eligible to vest fully upon termination of employment after attaining eight years of credited service, or the members' contributions may be withdrawn upon termination of employment.

Contributions: The contribution rates for each member category of the Plan are established by the Oklahoma Legislature after recommendation by the Board based on an actuarial calculation, which is performed to determine the adequacy of such contribution rates.

Each member participates based on their qualifying gross salary earned, excluding overtime. There is no cap on the qualifying gross salary earned, subject to Internal Revenue Service (IRS) limitations on compensation.

For 2016 and 2015, *state agency employers* contributed 16.5 percent on all salary, and *state employees* contributed 3.5 percent on all salary.

For 2016 and 2015, contributions of *Oklahoma Lottery Commission* totaled 20.0 percent of salary composed of employee contribution rate of 3.5 percent and employer contribution rate of 16.5 percent. Contributions to the pension plan from the Oklahoma Lottery Commission were \$266,041 and 256,235 for the years ended June 30, 2016 and 2015, respectively.

Members have the option to elect to increase the benefit computation factor for all future service from 2.0 percent to 2.5 percent. The election is irrevocable, binding for all future employment under OPERS, and applies only to full years of service. Those who make the election pay the standard contribution rate plus an additional contribution rate, 2.91 percent which is actuarially determined.

Pension liabilities, pension expense, and deferred outflows of resources and deferred inflows of resources related to pensions: At June 30, 2016 and 2015, the Oklahoma Lottery Commission reported a liability of \$315,973 and \$165,624, respectively, for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2015 and 2014, respectively, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of June 30, 2015 and 2014, respectively. The Oklahoma Lottery Commission's proportion of the net pension liability was based on the Oklahoma Lottery Commission's share of contributions to the pension plan relative to the contributions of all participating employers. At June 30, 2016 and 2015, the Oklahoma Lottery Commission's proportion was 0.08784744 percent and 0.090226546 percent, respectively.

**Oklahoma Lottery Commission
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Notes to Financial Statements

Note 8. Retirement Program (Continued)

For the year ended June 30, 2016 and 2015, the Oklahoma Lottery Commission recognized pension expense of \$(5,059) and \$11,276, respectively. At June 30, 2016 and 2015, the Oklahoma Lottery Commission reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	June 30, 2016		June 30, 2015	
	Deferred Outflows of Resources	Deferred Inflows of Resources	Deferred Outflows of Resources	Deferred Inflows of Resources
Changes of assumption	\$ 4,916	\$ -	\$ 9,478	\$ -
Differences between expected and actual experience	-	35,133	-	54,834
Difference between projected and actual investment earnings on pension plan investments	260,858	404,184	-	553,508
Changes in proportion and differences between OLC contributions and proportionate share of contributions	-	13,676	-	-
Total deferred amounts to be recognized in pension expense in future periods	265,774	452,993	9,478	608,342
OLC contributions subsequent to the measurement date	266,041	-	256,235	-
Total deferred amounts related to pension	\$ 531,815	\$ 452,993	\$ 265,713	\$ 608,342

Deferred pension outflows resulting from the OLC's Employer' contributions subsequent to the measurement date, totaling \$266,041 and \$256,235 at June 30, 2016 and 2015, will be recognized as a reduction of the net pension liability in the year ended June 30, 2017 and 2016, respectively. Deferred outflows and inflows totaling \$260,858 and \$404,184, as of June 30, 2016 and deferred inflow of \$553,508, resulting from the difference between projected and actual investment earnings will be recognized in pension expense over five years. The other amounts reported as deferred outflows of resources and deferred inflows of resources related to pension will be recognized in pension expense using the average expected remaining service life of the Plan members, both active and inactive. The average expected remaining service life of the Plan is determined by taking the calculated total future service years of the Plan divided by the number of people in the Plan including retirees. The total future service years of the plan are estimated at 3.11 years as of June 30, 2016 and 3.14 years as of June 30, 2015 and are determined using the mortality, termination, retirement and disability assumptions associated with the Plan. Deferred outflows of resources and deferred inflows of resources will be recognized in pension expense as follows at June 30:

Oklahoma Lottery Commission
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Notes to Financial Statements

Note 8. Retirement Program (Continued)

	June 30, 2016	
	Deferred Outflows	Deferred Inflows
2017	\$ 69,527	\$ (169,329)
2018	65,819	(147,874)
2019	65,214	(135,790)
2020	65,214	-
	<u>\$ 265,774</u>	<u>\$ (452,993)</u>

	June 30, 2015	
	Deferred Outflows	Deferred Inflows
2016	\$ 4,429	\$ (164,000)
2017	4,429	(164,000)
2018	620	(141,964)
2019	-	(138,377)
	<u>\$ 9,478</u>	<u>\$ (608,342)</u>

Actuarial assumptions: The total pension liability as of June 30, 2015 and 2014, was determined based on an actuarial valuation prepared as of July 1, 2015 and July 1, 2014, using the following actuarial assumptions:

- Investment return—7.5 percent compounded annually net of investment expense and including inflation
- Salary increases—4.5 percent to 8.4 percent per year including inflation
- Mortality rates—Active participants and nondisabled pensioners—RP-2000 Mortality Table projected to 2010 by Scale AA (disabled pensioners set forward 15 years)
- No annual post-retirement benefit increases
- Assumed inflation rate—3.0 percent
- Payroll growth—4.0 percent per year
- Actuarial cost method—Entry age
- Select period for the termination of employment assumptions—10 years

The actuarial assumptions used in the July 1, 2015 and 2014, valuation are based on the results of the most recent actuarial experience study, which cover the three-year period ending June 30, 2013. The experience study report is dated May 9, 2014.

The long-term expected rate of return on pension plan investments was determined using a log-normal distribution analysis in which best estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target asset allocation and best estimates of geometric real rates of return for each major asset class as of June 30, 2015 and 2014, are summarized in the following table:

Oklahoma Lottery Commission
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Notes to Financial Statements

Note 8. Retirement Program (Continued)

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
U.S. Large Cap Equity	38.0%	5.3%
U.S. Small Cap Equity	6.0%	5.6%
U.S. Fixed Income	25.0%	0.7%
International Stock	18.0%	5.6%
Emerging Market Stock	6.0%	6.4%
TIPS	3.5%	0.7%
Rate Anticipation	3.5%	1.5%
Total	100.0%	

Discount rate: The discount rate used to measure the total pension liability was 7.50 percent. The projection of cash flows used to determine the discount rate assumed that contributions from plan members and the employers will be made at the current contribution rate as set out in state statute. Based on those assumptions, the pension plan's fiduciary net position was projected through 2114 to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability. The discount rate determined does not use a municipal bond rate.

Sensitivity of the Oklahoma Lottery Commission's proportionate share of the net pension liability to changes in the discount rate: The following presents the Oklahoma Lottery Commission's proportionate share of the net pension liability calculated using the discount rate of 7.50 percent, as well as what Oklahoma Lottery Commission's net pension liability would be if it were calculated using a discount rate that is one percentage point lower (6.50 percent) or one percentage point higher (8.50 percent) than the current rate:

	June 30, 2016			June 30, 2015		
	1% Decrease (6.50%)	Current Discount Rate (7.50%)	1% Increase (8.50%)	1% Decrease (6.50%)	Current Discount Rate (7.50%)	1% Increase (8.50%)
Oklahoma Lottery Commission's proportionate share of the net pension liability	\$ 1,177,397	\$ 315,973	\$ (416,374)	\$ 1,031,133	\$ 165,624	\$ (570,183)

Pension plan fiduciary net position: Detailed information about the pension plan's fiduciary net position is available in separately issued financial statements, June 30, 2015 CAFR, available at <http://www.opers.ok.gov/Websites/opers/images/pdfs/CAFR-2015-OPERS.pdf>.

Note 9. Contingencies

The OLC is subject to litigation in the ordinary course of its operations. In the opinion of the OLC's management and its legal counsel, the outcome of such litigation will not have a material impact on the financial position or cash flows of the OLC for the years ended June 30, 2016 and 2015.

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Notes to Financial Statements

Note 10. Contractual Arrangements

In August 2005, the OLC entered into a contract with Scientific Games International, Inc. (SGI) to provide, amongst other things, services and equipment to operate its lotteries. Due to Oklahoma Statutes, the OLC may not contract for a period longer than one year. However, the contract with SGI contained seven one-year renewal options, which the OLC's Board of Trustees renewed annually. In August 2013, the last one-year renewal option matured and a similar contract was entered into with SGI. This contract contains nine one-year renewal options. Under the terms of the contract, the OLC pays SGI a fee based on a percentage of the OLC's sales. For the years ended June 30, 2016 and 2015, the OLC paid SGI \$7,985,458 and \$7,271,417, respectively.

The OLC is a member of the MUSL, which operates games on behalf of participating lotteries. MUSL currently operates the Powerball, Mega Millions, and Hot Lotto games for the OLC. Under the OLC's agreement with the MUSL, the OLC must remit 50 percent of its Powerball ticket sales, 50 percent of its Hot Lotto ticket sales, and 50 percent of its Mega Millions ticket sales. This payment is to cover the OLC's share of current jackpot prizes based on the OLC's percent of sales for each drawing and the OLC share of the prize reserve fund. The OLC is responsible for paying winning tickets purchased in Oklahoma; therefore, it is able to deduct winning tickets sold from the amount due to the MUSL on its ticket sales. As of June 30, 2016 and 2015, the OLC owed the MUSL \$1,427,206 and \$741,878 for ticket sales, and the MUSL owed the OLC \$506,677 and \$352,010 for nonjackpot-winning tickets. The OLC has recorded these items at their gross amounts in the accompanying statements of net position.

As noted above, OLC's payments to MUSL includes the OLC share of the prize reserve fund. The prize reserve fund serves as a contingency reserve to protect all the MUSL members, including the OLC, from unforeseen prize liabilities. These funds are in the possession of the MUSL and are included in expendable restricted net position.

The balances of the deposits are made up of the following:

	June 30	
	2016	2015
Set prize reserve account	\$ 671,012	\$ 693,400
Prize reserve account	2,957,070	3,112,906
Balance of unreserved account	987,572	1,022,912
	<u>\$ 4,615,654</u>	<u>\$ 4,829,218</u>

Note 11. Subsequent Event

In September 2016, the OLC exercised an option within their contract with Scientific Games International to upgrade the gaming system. The exercised option cost approximately \$2.32 million.

Required Supplementary Information

**Oklahoma Lottery Commission
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**Required Supplementary Information
Schedule of OLC's Proportionate Share of the Net Pension Liability
Oklahoma Public Employees Retirement Plan
Last 10 Fiscal Years***

	June 30	
	2015	2014
OLC's proportion of the net pension liability	0.08784744%	0.0902265446%
OLC's proportionate share of the net pension liability	\$ 315,973	\$ 165,624
OLC's covered-employee payroll	1,552,939	1,528,606
OLC's proportionate share of the net pension liability as a percentage of its employee payroll	20.35%	10.84%
Plan fiduciary net position as a percentage of the total pension liability	96.0%	97.9%

Notes to Schedule:

* Only the fiscal years ended June 30, 2015 and 2014 are presented because 10-year data is not yet available.

**Oklahoma Lottery Commission
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**Required Supplementary Information
Schedule of OLC's Contributions
Oklahoma Public Employees Retirement Plan
Last 10 Fiscal Years**

	June 30									
	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007
Contractually required to contribute	\$ 266,041	\$ 256,235	\$ 252,220	\$ 260,035	\$ 289,515	\$ 295,643	\$ 317,954	\$ 295,497	\$ 276,686	\$ 255,819
Contributions in relation to the contractually required contributions	266,041	256,235	252,220	260,035	289,515	295,643	317,954	295,497	276,686	255,819
Contributions deficiency (excess)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
OLC's covered-employee payroll	1,610,474	1,552,939	1,528,606	1,575,970	1,754,636	1,907,374	2,051,316	2,037,910	2,049,526	2,046,552
Contributions as a percentage of covered- employee payroll	16.52%	16.50%	16.50%	16.50%	16.50%	15.50%	15.50%	14.50%	13.50%	12.50%

**Oklahoma Lottery Commission
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**Required Supplementary Information
Notes to Required Supplementary Information
Oklahoma Public Employees Retirement Plan**

Valuation Date

Actuarially determined contributions are calculated as of the beginning of the fiscal year in which contributions are reported.

Methods and assumptions used to determine contribution rates:

Actuarial cost method	Entry age
Amortization method	Level percentage of payroll, closed
Remaining amortization period	13 years
Asset valuation method	5-year moving average
Inflation	3.00%
Salary increase	4.50 to 8.40 percent, including inflation
Investment rate of return	7.50%, compounded annually, net of investment expense and including inflation
Retirement age	Age 65 for all members hired on or after November 1, 2011 age 62 for members hired prior to November 1, 2011
Mortality	Active participants and nondisabled pensioners – RP-2000 Mortality Table projected to 2010 by Scale AA (disabled pensioners set forward 15 years)

Other Information

The Plan has been amended by House Bill 2630 in 2014 which states that effective November 1, 2015, OPERS shall create a defined contribution plan for most people first employed by a participating employer. Exemptions from the new defined contribution plan include hazardous duty members and district attorneys, assistant district attorneys and employees of the district attorney's office. Each employer shall send to OPERS the difference between the required employer contribution to OPERS and the amount required to match the participating employee's contribution in the defined contribution plan.

Senate Bill 2120, also enacted in 2014, amends House Bill 2630 to further exempt from the new defined contribution plan county elected officials and employees of a county, county hospital, city or town, conservation district, circuit engineering district, and any public or private trust in which a county, city or town participates. Senate Bill 2120 also states that employees who participate in the defined contribution system are excluded from the \$105 health subsidy.

New employees specifically exempted from the defined contribution plan will participate in the existing defined benefit plan.

**Report Required by
*Government Auditing Standards***

**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***

Independent Auditor's Report

To The Board of Trustees
Oklahoma Lottery Commission
An Enterprise Fund of the State of Oklahoma
Oklahoma City, Oklahoma

We have audited, in accordance with the 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, the financial statements of the Oklahoma Lottery Commission (the OLC), an enterprise fund of the State of Oklahoma, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the OLC's basic financial statements, and have issued our report thereon dated September 16, 2016. Our report includes an emphasis of matter paragraph acknowledging that the OLC is an enterprise fund of the State of Oklahoma and these financial statements reflect only the assets, liabilities and revenues and expenses of that enterprise fund and not the State of Oklahoma as a whole.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the OLC's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the OLC's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the OLC'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. A significant deficiency is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the OLC's financial statements are free from 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*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

RSM US LLP

Oklahoma City, Oklahoma
September 16, 2016

