

Mississippi Lottery Corporation
A Component Unit of the State of Mississippi
Independent Auditor's Reports and Financial Statements
Year Ended June 30, 2020 and Period from
October 19, 2018 (Inception) through June 30, 2019

Mississippi Lottery Corporation
A Component Unit of the State of Mississippi
Year Ended June 30, 2020 and Period from
October 19, 2018 (Inception) through June 30, 2019

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Independent Auditor's Report

Board of Directors
Mississippi Lottery Corporation
Flowood, Mississippi

Report on the Financial Statements

We have audited the accompanying financial statements of the Mississippi Lottery Corporation (the Corporation), a component unit of the State of Mississippi, as of June 30, 2020 and 2019, and for the year ended June 30, 2020, and for the period from October 19, 2018 (inception) through June 30, 2019, and the related notes to the financial statements, which collectively comprise the Corporation'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 from 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 Mississippi Lottery Corporation as of June 30, 2020 and 2019, and the changes in its financial position and its cash flows for the year ended June 30, 2020, and for the period from October 19, 2018 (inception) through June 30, 2019, in accordance with accounting principles generally accepted in the United States of America.

Other Matter

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis as listed in the table of contents 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 audits 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 also have issued our report dated September 22, 2020, on our consideration of the Corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is solely 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 effectiveness of the Corporation's 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 Corporation's internal control over financial reporting and compliance.

BKD, LLP

Jackson, Mississippi
September 22, 2020

Mississippi Lottery Corporation
A Component Unit of the State of Mississippi
Management's Discussion and Analysis
Year Ended June 30, 2020 and Period from
October 19, 2018 (Inception) through June 30, 2019

The following discussion and analysis of the Mississippi Lottery Corporation's (the Corporation) financial performance provides an overview of the Corporation's financial activities for the year ended June 30, 2020 and for the period from October 19, 2018 (inception) through June 30, 2019. Readers are encouraged to consider the information presented here in conjunction with the Corporation's financial statements, which immediately follow this discussion and analysis. In future years, when prior-year information is available, additional comparative analysis of games offered by the Corporation and financial data will be presented.

2020 Financial Highlights

The Corporation launched the sale of statewide instant lottery tickets on November 25, 2019. *Powerball* and *Mega Millions* draw-style games began selling on January 30, 2020. The Corporation ended its fiscal year 2020 with total contributions of \$70.7 million to the State of Mississippi Lottery Proceeds Fund. In accordance with the Alyce G. Clarke Mississippi Lottery Law (the Law), the first \$80 million transferred of each fiscal year will be used to fund infrastructure projects throughout the state.

Gross ticket sales for the fiscal year 2020 were \$339.8 million. Total actual prizes paid to winners for the year were \$192.5 million. Included in the prizes paid was one \$2 million-dollar *Mega Millions* game winner.

Management attributes the success of the launch of both instant and draw-style game tickets to the Corporation's retailers and players. Management also credits the start-up success to the Corporation's focus on its mission to be managed in such a manner that the people of Mississippi benefit from its profits and the integrity of the lottery.

Twenty-eight instant ticket games were introduced during the fiscal year. These new games contributed to the instant product's success by providing players with new ways to play. For the current year, the highest earning instant ticket revenue was the Corporation's "Mega Ca\$h" game, which offers a scratch and match numbers style game.

Gross instant ticket sales for the year were \$317.8 million. Instant tickets accounted for 93.5% of all ticket sales.

The Corporation participates in the following multi-jurisdictional draw-style games:

Powerball sales began across the state on January 30, 2020. Sales for the period were \$11.8 million. Sales were hampered nationwide by the COVID-19 pandemic, causing beginning jackpot amounts to be lowered, as well as minimum jackpot increases between drawings to be determined by sales.

Mega Millions sales began across the state on January 30, 2020. Sales for the fiscal year were \$10.1 million. Sales were hampered nationwide by the COVID-19 pandemic, causing beginning jackpot amounts to be lowered, as well as minimum jackpot increases to be determined by sales.

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Total draw-style game sales for the year were \$21.9 million, accounting for 6.5% of total tickets sales.

In addition to the transfers made to the State of Mississippi, the Corporation was able to pay off the line of credit previously secured to fund the start-up of the operation. The Corporation has no long-term debt at the end of the fiscal year.

2019 Financial Highlights

The Corporation was established under the Law passed during the 2018 first extraordinary session of the Mississippi State Legislature. The Corporation's bylaws are dated March 5, 2019, and the Corporation began operations during the State of Mississippi's fiscal year ended June 30, 2019. The Corporation was in the start-up phase of operations and had not begun the sale of lottery tickets as of June 30, 2019.

The Corporation secured a line of credit in order to fund the costs of the initial start-up of the lottery.

Overview of the Financial Statements

The Corporation is accounted for as a business-type activity and is a discretely presented component unit of the State of Mississippi, reporting transactions using the full accrual basis of accounting. This discussion and analysis is intended to serve as an introduction to the Corporation's basic financial statements, along with notes to the financial statements. The basic financial statements include the Corporation's statements of net position on page 12; statements of revenues, expenses and changes in net position on page 13; and statements of cash flows on page 14.

The statements of net position reflect the Corporation's financial position at June 30, 2020 and 2019.

The statements of revenues, expenses and changes in net position report the activity of start-up expenses related to the preparation of selling lottery products for the period from October 19, 2018 through June 30, 2019. For the year ended June 30, 2020, this statement reports both the start-up expenses mentioned above, as well as revenues and expenses related to lottery operations since ticket sales began on November 25, 2019.

The statements of cash flows outline the cash inflows and outflows related to the activity of start-up costs related to selling lottery products for the period from October 19, 2018 through June 30, 2019. For the year ended June 30, 2020, this report outlines the cash inflows and outflows related to both the activity of start-up expenses mentioned above, as well as cash inflows and outflows related to lottery operations since ticket sales began on November 25, 2019.

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes to the financial statements begin on page 16 of the financial statements.

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Financial Analysis

The Corporation's Net Position (Deficit)

The Corporation's net position (deficit) is the difference between its assets and liabilities reported in the statements of net position. The Corporation's net position (deficit) increased by approximately \$2.5 million as of June 30, 2020, compared to 2019, as shown in the following table.

	2020	2019
Assets		
Current assets	\$ 41,273,922	\$ 403,122
Capital assets, net	1,806,885	-
	<u>\$ 43,080,807</u>	<u>\$ 403,122</u>
Liabilities		
Prizes payable	\$ 28,555,549	\$ -
Other current liabilities	2,021,719	309,049
Due to State of Mississippi Highway Fund	10,696,654	-
Long-term debt	-	750,000
	<u>41,273,922</u>	<u>1,059,049</u>
Net Position (Deficit)		
Investment in capital assets	1,806,885	-
Unrestricted (deficit)	-	(655,927)
	<u>1,806,885</u>	<u>(655,927)</u>
	<u>\$ 43,080,807</u>	<u>\$ 403,122</u>

Assets

The \$42.7 million increase in total assets is attributable to the launch of the Corporation's lottery ticket sales. Retailer accounts receivable were \$11 million at June 30, 2020, where no retailer accounts receivable existed at June 30, 2019. Cash increased \$29.7 million during fiscal year 2020. This increase is related to the cash received from lottery ticket sales that is earmarked for winning prizes payable to players.

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At the end of fiscal year 2020, the Corporation had \$1.8 million of net capital assets as detailed in Note 3 to the financial statements. At the end of fiscal year 2019, the Corporation had no capital assets. The purchase of capital assets during the year was part of the start-up costs associated related to the selling of lottery products.

Liabilities

Total liabilities increased \$40.2 million in 2020. \$28.6 million of the increase in liabilities is related to prizes payable to players for both instant and draw-style ticket sales at June 30, 2020. Additionally, the Corporation was set to transfer the net proceeds for June 2020 in the amount of \$10.7 million.

A line of credit in the amount of \$15 million was established during FY2019, and one draw of \$750 thousand was made before the end of the FY2019 reporting period. The line of credit was used to fund operations until sales of lottery tickets commenced. An additional \$4.5 million was drawn on the line of credit during FY2020 before the line was fully repaid in April 2020.

Operating Results and Changes in the Corporation's Net Position (Deficit)

In 2020, the Corporation's net position increased by approximately \$2.5 million, as shown in the following table. This increase is a result of the start of lottery instant ticket sales on November 25, 2019 and draw-style games on January 30, 2020.

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	<u>2020</u>	<u>2019</u>
Operating Revenues		
Net ticket sales	\$ 311,195,835	\$ -
Other operating revenues	<u>1,062,562</u>	<u>-</u>
Total operating revenues	<u>312,258,397</u>	<u>-</u>
Operating Net Prize Expense	<u>198,262,912</u>	<u>-</u>
Other Operating Expenses		
Retailer commissions	20,387,909	-
Gaming vendor fees	10,741,698	-
Other operating expenses	<u>9,727,522</u>	<u>653,411</u>
Total other operating expenses	<u>40,857,129</u>	<u>653,411</u>
Operating Income (Loss)	<u>73,138,356</u>	<u>(653,411)</u>
Nonoperating Revenues (Expenses)		
Payments to State of Mississippi Highway Fund	(70,703,360)	-
Interest income	109,836	-
Interest expense	(92,144)	(2,516)
Other	<u>10,124</u>	<u>-</u>
Total nonoperating revenues (expenses)	<u>(70,675,544)</u>	<u>(2,516)</u>
Increase (Decrease) in Net Position (Deficit)	2,462,812	(655,927)
Net Position (Deficit), Beginning of Year/Period	<u>(655,927)</u>	<u>-</u>
Net Position (Deficit), End of Year/Period	<u>\$ 1,806,885</u>	<u>\$ (655,927)</u>

Operating Revenues

Operating revenues consist primarily of ticket sales and fees charged to retailers. Gross ticket sales totaled \$339.8 million for the year ended June 30, 2020. These revenues represented the beginning of the

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lottery sales in Mississippi. As the Corporation had not started the sale of lottery tickets as of June 30, 2019, no operating revenues were reported in the prior year. Gross and net ticket sales for the year ended June 30, 2020, were as follows:

Ticket Sales	2020
Mega Cash	\$ 32,549,780
3 Times Lucky	32,103,058
\$100,000 Jackpot	29,362,130
Triple 777	27,936,334
Mississippi Blues	19,980,070
Fast 50	13,720,217
Double Doubler	11,743,820
MS Limited	11,168,920
\$200,000 Bonus Jackpot	10,548,500
Easy Money	9,718,060
Break the Bank	9,653,700
25,000 Payday	9,604,794
Money Bags	9,553,744
Jewel 7 Doubler	9,284,124
Happy Holidays Yall	9,257,958
Cash Money	8,734,350
Diamond Dazzler	8,086,330
Solid Gold	7,175,760
Cash King	6,219,805
Electric 8s	5,537,570
BlackJack	5,311,928
Crawfish Cash	5,268,491
123 Mississippi	4,997,380
Hit 100	4,731,624
White Hot 5s	4,500,415
Love Yall	3,804,923
Hot 5s	3,669,487
Crossword	3,611,868
Total instant ticket sales	<u>317,835,140</u>
Less instant tickets provided as prizes	<u>(28,580,571)</u>
	289,254,569
<i>Mega Millions</i>	10,109,350
<i>Powerball</i>	11,831,916
Total draw-style game sales	<u>21,941,266</u>
Net ticket sales	<u><u>\$ 311,195,835</u></u>

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Operating Expenses

In 2020, net prizes were \$198.3 million, and other operating expenses were \$40.8 million. In 2019, there was no prize expense and operating expenses were \$653 thousand. Operating costs include both start-up costs and gaming related costs.

Net prize expense of \$198.3 million relates directly to the proportional sales mix of instant and draw-style games.

For instant tickets, the prize expense is managed through an approved prize structure for each game. The prize structure is established prior to the printing of the instant tickets for each game. Prize expense is recognized based on the established prize structure in relation to ticket sales. Gross prize expense for instant tickets for the current year equaled \$189.2 million

For multi-jurisdictional (*Powerball and Mega Millions*) draw-style games, prize expense is recorded based on the respective game rules. Prize expense is a percentage of each drawing's sales and is recorded on the day of the draw. Gross prize expense for these draw-style games for FY2020 was \$11.1 million.

Prize expense is reduced by unclaimed prizes. During 2020, both instant and draw-style games were estimated to have an unclaimed prize amount of \$2.0 million. Unclaimed prize amounts are adjusted to actual for instant games after the game has closed and the 90-day claim period for prizes has ended. For draw-style games, unclaimed prize amounts are adjusted to actual after the 180-day claim period for each drawing has passed.

Nonoperating Revenues and Expenses

Nonoperating revenues and expenses consist primarily of required transfers to the State of Mississippi Lottery Proceeds Fund, as well as interest income and expense.

Monthly, the Corporation is required to transfer their net proceeds to the Lottery Proceeds Fund of the State Treasury. For the fiscal year 2020, \$70.7 million was transferred. The Corporation did not have positive net proceeds in fiscal year 2019; therefore, no transfers were made during that fiscal year.

The Law requires the first \$80 million of net proceeds to be used to support the Mississippi State Highway Fund through June 30, 2028. Any proceeds exceeding the \$80 million will be deposited into the Education Enhancement Fund for the purposes of funding the Early Childhood Learning Collaborative, the Classroom Supply Fund and other educational purposes.

Net Position

In FY2020, the Corporation's net position increased by \$2.5 million. This increase is a result of the launch of lottery ticket sales on November 25, 2019. In accordance with the Law, the Corporation's net proceeds are transferred to the State of Mississippi Lottery Proceeds Fund monthly. In accordance with

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the Law, capital expenditures are excluded from the calculation of net proceeds. Beginning December 2019, the Corporation had a positive net position and transfers to the Lottery Proceeds Fund began.

Other Economic Factors

The Corporation's operations have adapted to the new business environment influenced by the COVID-19 pandemic. The Corporation's claim center has implemented safety procedures for players to claim prizes at their headquarters. The Corporation has postponed the rollout of new draw-style games until the next fiscal year.

Significant Factors Affecting Next Year

The Corporation's mission is to enable the people of the State of Mississippi to benefit from its profits. The following is presented to inform readers of the financial statements about factors that could potentially affect future results:

- The Corporation will continue to introduce new instant ticket games with varied price points.
- The Corporation will expand its current library of draw-style game offerings.
- The Corporation will continually review prize payout percentages for instant game products to ensure the highest net proceeds are eligible for transfer to the State.

Contact Information

This financial report is designed to provide a general overview of the Corporation's finances for all those with interest. Questions concerning any of the information contained in this report or requests for any additional information should be addressed to the Vice President of Finance at Mississippi Lottery Corporation, Post Office Box 321433, Flowood, MS 39232.

Mississippi Lottery Corporation
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Statements of Net Position
Year Ended June 30, 2020 and Period from
October 19, 2018 (Inception) through June 30, 2019

Assets

	2020	2019
Current Assets		
Cash	\$ 30,105,264	\$ 378,485
Retailer accounts receivable, net of allowance for doubtful accounts of \$3,297 in 2020	10,992,077	-
Prepaid expenses	86,219	24,637
Other current assets	90,362	-
	<hr/>	<hr/>
Total current assets	41,273,922	403,122
	<hr/>	<hr/>
Noncurrent Assets		
Capital assets, net	1,806,885	-
	<hr/>	<hr/>
Total noncurrent assets	1,806,885	-
	<hr/>	<hr/>
Total assets	<u>\$ 43,080,807</u>	<u>\$ 403,122</u>

Liabilities and Net Position (Deficit)

Current Liabilities		
Prizes payable	\$ 28,555,549	\$ -
Accounts payable and accrued expenses	1,111,319	309,049
Due to MUSL	421,967	-
Unearned revenue	488,433	-
Due to State of Mississippi Highway Fund	10,696,654	-
	<hr/>	<hr/>
Total current liabilities	41,273,922	309,049
	<hr/>	<hr/>
Line of Credit	-	750,000
	<hr/>	<hr/>
Total liabilities	41,273,922	1,059,049
	<hr/>	<hr/>
Net Position (Deficit)		
Investment in capital assets	1,806,885	-
Unrestricted (deficit)	-	(655,927)
	<hr/>	<hr/>
Total net position (deficit)	1,806,885	(655,927)
	<hr/>	<hr/>
Total liabilities and net position (deficit)	<u>\$ 43,080,807</u>	<u>\$ 403,122</u>

Mississippi Lottery Corporation
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Statements of Revenues, Expenses and Changes in Net Position (Deficit)
Year Ended June 30, 2020 and Period from
October 19, 2018 (Inception) through June 30, 2019

	<u>2020</u>	<u>2019</u>
Operating Revenues		
Instant ticket sales	\$ 317,835,140	\$ -
Draw-style game sales	21,941,266	-
Gross ticket sales	339,776,406	-
Less instant tickets provided as prizes	(28,580,571)	-
Net ticket sales	311,195,835	-
Other operating revenues	1,062,562	-
Total operating revenues	312,258,397	-
Operating Net Prize Expense	198,262,912	-
Other Operating Expenses		
Retailer commissions	20,387,909	-
Gaming vendor fees	10,741,698	-
Salaries and wages	4,530,779	31,253
Advertising	2,136,374	-
Professional fees and services	1,491,441	606,759
General, administrative and other operating	737,927	15,399
Contractor fees	237,695	-
Other gaming costs	162,305	-
Depreciation	161,132	-
Occupancy	135,009	-
Retailer merchandising and marketing	132,288	-
Repairs and maintenance	2,572	-
Total other operating expenses	40,857,129	653,411
Operating Income (Loss)	73,138,356	(653,411)
Nonoperating Revenues (Expenses)		
Payments to State of Mississippi Highway Fund	(70,703,360)	-
Interest income	109,836	-
Interest expense	(92,144)	(2,516)
Other revenue	10,124	-
Total nonoperating revenues (expenses)	(70,675,544)	(2,516)
Increase (Decrease) in Net Position (Deficit)	2,462,812	(655,927)
Net Position (Deficit), Beginning of Year/Period	(655,927)	-
Net Position (Deficit), End of Year/Period	<u>\$ 1,806,885</u>	<u>\$ (655,927)</u>

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Statements of Cash Flows
Year Ended June 30, 2020 and Period from
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	<u>2020</u>	<u>2019</u>
Cash Flows from Operating Activities		
Receipts from and on behalf of retailers	\$ 301,754,753	\$ -
Payments to winners	(169,285,396)	-
Payments to suppliers	(35,553,324)	(347,063)
Payments to employees	(4,489,831)	(24,452)
	<u>92,426,202</u>	<u>(371,515)</u>
Net cash provided by (used in) operating activities		
Cash Flows from Noncapital Financing Activities		
Advances under line of credit	4,500,000	750,000
Repayments on line of credit	(5,250,000)	-
Interest paid on line of credit	(94,660)	-
Payments to the State of Mississippi Highway Fund	(60,006,706)	-
	<u>(60,851,366)</u>	<u>750,000</u>
Net cash provided by (used in) noncapital financing activities		
Cash Flows from Capital and Related Financing Activities		
Purchase of property and equipment	(1,968,017)	-
	<u>(1,968,017)</u>	<u>-</u>
Net cash used in capital and related financing activities		
Cash Flows from Investing Activities		
Investment income	109,836	-
Other	10,124	-
	<u>119,960</u>	<u>-</u>
Net cash provided by investing activities		
Increase in Cash	29,726,779	378,485
Cash, Beginning of Year/Period	<u>378,485</u>	<u>-</u>
Cash, End of Year/Period	<u>\$ 30,105,264</u>	<u>\$ 378,485</u>

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	2020	2019
Reconciliation of Operating Income (Loss) to Net Cash		
Provided by (Used in) Operating Activities		
Operating income (loss)	\$ 73,138,356	\$ (653,411)
Depreciation and amortization	161,132	-
Changes in operating assets and liabilities		
Retailer accounts receivable, net	(10,992,077)	-
Prepaid expenses	(61,582)	(24,637)
Other current assets	(90,362)	-
Prizes payable	28,555,549	-
Accounts payable and accrued expenses	1,226,753	306,533
Unearned revenue	488,433	-
	\$ 92,426,202	\$ (371,515)
Net cash provided by (used in) operating activities	\$ 92,426,202	\$ (371,515)

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Notes to Financial Statements
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Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations and Reporting Entity

The Alyce G. Clarke Mississippi Lottery Law (the Law), Senate Bill 2001 (First Extraordinary Session 2018) [the Act], formed the Mississippi Lottery Corporation (the Corporation) to administer the State of Mississippi's first lottery. The Corporation's Board of Directors (the Board) governs the Corporation. The Board is comprised of five members appointed by the Governor, with the advice and consent of the Senate, in addition to the Commissioner of the Department of Revenue and the State Treasurer as ex officio members. The Corporation is a component unit of the State of Mississippi (the State).

The Corporation began conducting lottery games during the year ended June 30, 2020.

The Corporation accounts for the operations of the lottery in which a statutorily defined amount of the first \$80,000,000 of annual net proceeds (as defined in the Act) shall be used to support the State of Mississippi Highway Fund through June 30, 2028. Beginning July 1, 2028, the statutorily defined amount of the first \$80,000,000 shall be transferred to the State General Fund. Any net proceeds remaining after the statutorily required transfers are transferred to the State's Education Enhancement Fund.

Basis of Accounting and Presentation

The financial statements of the Corporation have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP), as prescribed by the Governmental Accounting Standards Board (GASB). The basic financial statements provide information about the Corporation's proprietary fund. Proprietary fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded at the time the liabilities are incurred, regardless of when the related cash flow takes place.

Enterprise Fund

The Corporation accounts for its operations as an enterprise fund. The intent of the State of Mississippi Legislature is that the Corporation's costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered solely through user charges. The Corporation defines operating revenues as those earned as a direct result of the fund's principal ongoing operations, i.e., the sale of lottery products. Operating expenses include expenses incurred in earning those revenues such as prize payments, the cost of tickets, vendor fees, retailer commissions and other incentives, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting these definitions are reported as nonoperating revenues and expenses.

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Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and deferred inflows and outflows of resources 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.

Cash Equivalents

The Corporation considers all liquid investments with original maturities of three months or less to be cash equivalents. At June 30, 2020 and 2019, the Corporation held no cash equivalents.

Accounts Receivable

Accounts receivable consist of amounts due from retailers for gross ticket sales and weekly fees less commissions and prizes paid by the retailers. Lottery proceeds for instant tickets sold by retailers are due and payable to the Corporation upon pack settlement, and lottery proceeds for draw-style game tickets are due and payable at the end of the accounting period in accordance with Section 2.11 of Retailer Rules and Regulations. Lottery proceeds are collected from retailer bank accounts established in a trust. Retailers are invoiced for net proceeds on a weekly basis for all billable activity from Sunday through Saturday.

The Corporation will record a bad debt expense and related allowance for bad debt based on a quarterly review of outstanding retailer accounts receivable as a result of nonpayment. The outstanding balances will not be written off against the allowance account until management determines such account is deemed noncollectible. Retailers will be charged NSF fees in accordance with the Corporation's Retailer Rules and Regulations Policy Section 2.12.

In accordance with the Law, each retailer is required to post a surety bond in an amount not to exceed twice the average lottery ticket sales of the lottery retailer for the period within which the lottery retailer is required to remit lottery funds to the Corporation. For 2020, the required bond amounts for retailers was \$8,000.

Prepaid Items

Certain payments to vendors reflect cost applicable to future accounting periods and are recorded as prepaid items.

Capital Assets

Capital assets are recorded at cost at the date of acquisition. The Corporation adheres to the state policy of capitalizing equipment only if the cost exceeds \$5,000 and has a useful life in excess of

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one year. Depreciation is computed using the straight-line method over the estimated useful life of each asset. The following estimated useful lives are being used by the Corporation:

Buildings and leasehold improvements	10-25 years
Equipment	3-15 years

Unearned Revenue

Unearned revenue represents amounts collected from retailers for draw-style game tickets for *Mega Millions* and *Powerball* sold in advance of the drawing. These amounts collected are recognized as revenue once the related drawing occurs.

Risk Management

The Corporation is exposed to various risks of loss from torts; theft of, damage to and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters and employee health and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters other than workers' compensation and natural disasters. Settled claims have not exceeded this commercial coverage since the Corporation was formed.

Net Position (Deficit)

Net position (deficit) of the Corporation is classified in three components.

- Investment in capital assets consists of capital assets net of accumulated depreciation. At June 30, 2020, the Corporation had \$1,806,885 of their cumulative net position included in this category, and there were no outstanding balances of borrowings used to finance the purchase or construction of those assets.
- Restricted net position is made up of noncapital assets that must be used for a particular purpose, as specified by legislation, creditors, grantors or donors external to the Corporation, including amounts deposited with trustees as required by bond indentures, reduced by the outstanding balances of any related borrowings. At June 30, 2020, the Corporation had no net position included in this category.
- Unrestricted net position (deficit) is the remaining net position that does not meet the definition of investment in capital assets or restricted net position.

Classification of Revenues

The Corporation has classified its revenues as either operating or nonoperating revenues according to the following criteria.

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Operating revenues include activities that have the characteristics of exchange transactions, such as

- (1) Instant ticket sales
- (2) Draw-style game sales
- (3) Retailer fees

Nonoperating revenues include activities that have the characteristics of nonexchange transactions, such as

- (1) Interest income
- (2) Other income

Income Taxes

The Corporation was created by the Mississippi Legislature and is exempt from state and federal income taxes.

Revenue Recognition

The Corporation recognizes revenue for instant games when retailers make them available for sale to the public, as indicated by the retailers' activation of tickets. Certain games include free tickets, which entitle the holder to exchange one instant ticket for another of equal value. The selling price of free tickets reduces instant ticket revenue when the free ticket is claimed by a player.

The Corporation recognizes revenue for terminal-based draw-style games based on the game characteristics. Revenues for draw-style games, whereby the prize expense is only determinable at the time of the related drawing, will be recognized after the tickets are sold to the players and the drawing occurs. Revenue collected from retailers for these games sold in advance of the draw are recorded as unearned revenue and recognized as the draw occurs.

Gaming Vendor Fees

The Corporation has contracted with IGT Corporation (IGT) for the gaming systems and supplies. IGT operates a gaming network in Mississippi that consists of approximately 1,675 instant and draw-style retailer ticket terminals as of June 30, 2020. The contract is for a period continuing seven years after December 1, 2019, and is subject to three, one-year contract extensions. Terms of the contract include a service fee rate of 1.9241% of gross on-line ticket sales revenue less cancelled transactions, plus the retail face value of all instant tickets activated during the week, less the retail face value of instant tickets returned, given as free tickets, returned as defective, reported stolen by a retailer, or issued by the Corporation as a promotion. The contract also includes a service fee rate of 1.4938% of the total face value of all instant tickets activated during the week, less the sum of the total face value of activated tickets returned by retailers during the given week,

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activated defective tickets, activated tickets reported stolen by retailers, and activated promotional tickets issued by the Corporation during the week. These fees are recorded as gaming vendor fees in the accompanying financial statements.

Prize Liability and Prize Expense

In accordance with the Law, as nearly as practical, at least 50% of ticket proceeds must be made available as prize money. Gross prize expense for instant ticket sales is recognized based on a predetermined prize structure for each game in accordance with the approved game working papers when tickets are activated for sale. Draw-style games gross prize expense is recognized based on historical payout experience when the drawings occur.

The Corporation recognizes prize expense in the period of related revenue recognition, regardless of when prizes are claimed by the player. All games are accounted for using the accrual basis of accounting. Instant ticket liability and expense are recognized at the point of ticket pack activation based on a predetermined prize payout for each game and are adjusted when the game ends. The Corporation will reconcile prize expense and prizes payable when the game is closed and the claim period has ended. The prize structure is included as part of each instant game's working papers, which is the contractual commitment for the instant vendor to produce the game at a predetermined payout.

The liability and expense for draw-style game prizes are recognized at the point of retail sale and are adjusted as the jackpot game draws occur and actual prize liability is determined. Prize liability for all games is reduced as prizes are paid to winners. The Corporation prize expense is recognized for terminal-based draw-style games at 50% to 55% of net ticket sales, depending on the amount of prize payout allocated for each draw game.

Powerball and *Mega Millions* prize expense is recognized as a percentage of ticket sales in accordance with the game rules and contractual agreement (*Powerball* Rule 28 and *Mega Millions* Rule 28, respectively).

Unclaimed Prizes

Prizes not claimed within 90 days of the announced end-of-game date for instant games, and within 180 days of the drawing for all terminal-based draw-style games, are forfeited as unclaimed prizes.

The Corporation records estimated unclaimed prizes for each instant game within the month the ticket is sold and reconciles the actual amounts when the claim period ends. For terminal-based draw-style games, the Corporation records a monthly estimate of unclaimed amounts, and the actual unclaimed amounts are determined after the expiration of the related claim period for the draw.

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Contingencies

Liabilities for loss contingencies arising from claims, assessments, litigation, fines and penalties, and other sources will be recorded when it is probable that a liability has been incurred, and the amount of the liability can be reasonably estimated.

Retailer Payments

Retailers receive a commission of 6.0% on all instant tickets settled and draw-style tickets sold. The commission expense is recorded in the period of related ticket sales or activations. Where commission has been paid to retailers for deferred ticket sales, this fee is recorded as a prepaid expense until the related revenue is recognized.

Retailers are also subject to receive incentive payments in accordance with the following guidelines. The Corporation will pay an incentive of \$25,000 to a retailer that sells a jackpot winning *Powerball* or *Mega Millions* draw-style game play. The Corporation will pay an incentive of \$5,000 to a retailer who sells a winning draw-style game play (excluding a play described by the previous sentence) when the prize won is equal to or greater than \$1 million. If there are multiple winning plays sold in Mississippi in a single drawing that qualify for one of the incentives described in this section to be paid, the respective incentive will be divided between and among the respective retailers equally, based on the number of winning plays sold by each retailer. The retailer incentive expense is accrued in the same period in which the winning ticket is drawn.

Prize Reserve

As part of the Lottery's agreement with the Multi-State Lottery Association (MUSL), for both the *Powerball* and *Mega Millions* games, a certain percentage of sales must be paid to MUSL, when required, to bring the set prize and grand prize reserves up to the reserve requirement amounts as determined by MUSL. In accordance with MUSL requirements, during FY2020, a total of \$101,194 was transferred from the Corporation to MUSL to cover *Mega Millions*' set prize reserves. At June 30, 2020, the balance held by MUSL for *Mega Millions*' set-aside prize reserve for the Corporation was \$7,551. There were no amounts transferred, repaid or owed during FY2019 related to the *Powerball*'s prize reserve. For FY2019, there were no amounts transferred, repaid or owed, as lottery gaming operations had not yet begun.

Compensated Absences

Effective October 15, 2019, the Corporation implemented an attendance and leave policy allowing employees to earn paid time off (PTO) during their employment on a calendar-year basis. The Corporation recognizes expense for PTO in the current year and does allow PTO not used in its entirety to be added to the next calendar year. The total maximum balance to be added to an employee's PTO for the next calendar year is 120 hours. Notwithstanding, the maximum number of additional PTO hours will never exceed 120 hours in any one year.

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Expense and the related liability are recognized as PTO hours are earned. Compensated absence liabilities are computed using the regular pay rates in effect at the statement of net position date. Employees are not compensated for any unused PTO upon termination of employment.

Reclassifications

Certain reclassifications have been made to the 2019 financial statements to conform to the 2020 financial statement presentation. These reclassifications had no effect on the change in net position.

Note 2: Deposits, Investments and Investment Income

Deposits

Custodial credit risk is the risk that in the event of a bank failure, a government's deposits may not be returned to it. The Corporation's deposit policy for custodial credit risk and the Act require compliance with the provisions of Section 27-105-5 Miss. Code Ann. (1972).

The collateral for public entities' deposits in financial institutions is held in the name of the State Treasurer under a program established by the Mississippi State Legislature and is governed by Section 27-105-5 Miss. Code Ann. (1972). Under this program, the entity's funds are protected through a collateral pool administered by the State Treasurer. Financial institutions holding deposits of public funds must pledge securities as collateral against those deposits. In the event of failure of a financial institution, securities pledged by that institution would be liquidated by the State Treasurer to replace the public deposits not covered by the Federal Deposit Insurance Corporation (FDIC).

At June 30, 2020 and 2019, the carrying amount of the Corporation's deposits was \$30,105,264 and \$378,485, respectively, and the bank balances totaled \$30,379,273 and \$378,710. Of the bank balances, \$250,000 was insured by FDIC. At June 30, 2020, the remaining \$30,129,273 is collateralized as described above.

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Note 3: Capital Assets

Capital assets activity for the year ended June 30, 2020, was:

	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Buildings and leasehold improvements	\$ -	\$ 674,975	\$ -	\$ -	\$ 674,975
Equipment	-	1,293,042	-	-	1,293,042
	-	1,968,017	-	-	1,968,017
Less accumulated depreciation					
Buildings and leasehold improvements	-	(33,472)	-	-	(33,472)
Equipment	-	(127,660)	-	-	(127,660)
	-	(161,132)	-	-	(161,132)
Capital assets, net	\$ -	\$ 1,806,885	\$ -	\$ -	\$ 1,806,885

Note 4: Due to State of Mississippi and Transfers to State of Mississippi

In accordance with Section 26(c) of the Law, all net proceeds of the Corporation are due to the State of Mississippi. The net proceeds amount is defined by the Corporation as total net operating and nonoperating income plus additions to property, plant and equipment, less depreciation expense. In accordance with the Law, distributions of net proceeds shall be made within 20 days following the close of each calendar month. In accordance with Section 43 of the Law, net proceeds generated by the Corporation shall be paid to the State of Mississippi Highway Fund until June 30, 2028, not to exceed \$80 million per fiscal year. All monies deposited into the Lottery Proceeds Fund over \$80 million per fiscal year shall be transferred into the Education Enhancement Fund for the purposes of funding the Early Childhood Learning Collaborative, the Classroom Supply Fund and other educational purposes.

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Net proceeds for the year ended June 30, 2020 are summarized as follows:

Operating Revenues	
Ticket sales	\$ 339,776,406
Less tickets provided as prizes	<u>(28,580,571)</u>
Net ticket sales	<u>311,195,835</u>
Other operating revenues	<u>1,062,562</u>
Operating Expenses	
Gaming	198,262,912
Operating	<u>40,857,129</u>
Total operating expenses, as defined	<u>239,120,041</u>
Operating Income	73,138,356
Nonoperating Revenues and Expenses	
Interest income	109,836
Interest expense	(92,144)
Other revenue	<u>10,124</u>
Total nonoperating revenues and expenses	<u>27,816</u>
Adjustments to Amount Due to State	
Prior-year deficit	(655,927)
Depreciation expense	161,132
Additions to fixed assets	<u>(1,968,017)</u>
	<u>(2,462,812)</u>
Net Proceeds	<u><u>\$ 70,703,360</u></u>

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Note 5: Line of Credit

The Corporation has a \$15,000,000 revolving bank line of credit maturing on May 31, 2023. The line is unsecured, with interest payments monthly at a variable rate of 1.65% over an index rate, which was 3.69% at June 30, 2020. The balances at June 30, 2020 and 2019 were \$0 and \$750,000 respectively.

Note 6: Lease Liabilities

The Corporation leases office space under operating leases, the terms of which expire August 1, 2029. During the year year/period ended June 30, 2020 and 2019, the Corporation recognized \$135,009 and \$0, respectively, of rental expense for the office space.

Future minimum lease payments at June 30, 2020, were:

2021	\$ 256,241
2022	260,637
2023	263,778
2024	263,778
2025	263,778
2026-2029	<u>1,195,162</u>
Future minimum lease payments	<u><u>\$ 2,503,374</u></u>

Note 7: Contingencies

Litigation

In the normal course of business, the Corporation is, from time to time, subject to allegations that may or do result in litigation. The Corporation evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of legal counsel, management records an estimate of the amount of ultimate expected loss, if any, for each. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term. No estimate for loss is recorded at June 30, 2020 or 2019.

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Note 8: Employee Retirement Plans

The Corporation has two types of defined contribution retirement plans for its employees. The first is a Governmental 401(a) Plan. The second plan is an Eligible Governmental 457 Plan which permits employees to make additional pretax contributions from their wages up to defined Internal Revenue Service (IRS) limitations. In the 401(a) plan, the Corporation will contribute 100% of each employee's pretax wages that are deferred in the 457 plan up to 4%. The Corporation's contributions are limited to 4% and only to the extent of each individual employee's contributions to the 457 Plan up to a total of \$19,500 (\$26,000 for catch-up eligible employees) per employee.

Retirement expense is recorded for the amount of the Corporation's required contributions and administrative fees determined in accordance with the terms of the plans. The Corporation has an appointed investment committee, including the President and an external investment advisor, to administer the plans. Benefit provisions are contained in the plan documents and, where established, can be amended by action of the Corporation's Board of Directors and management. Employee contributions of pretax wages are subject to a maximum set by the IRS.

Contributions made by the Corporation are \$27,543 during the year ended June 30, 2020.

Note 9: Subsequent Events

As a result of the spread of the SARS-CoV-2 virus and the incidence of COVID-19, economic uncertainties have arisen which may negatively affect the financial position, results of operations and cash flows of the Corporation. The duration of these uncertainties and the ultimate financial effects cannot be reasonably estimated at this time.

**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

Board of Directors
Mississippi Lottery Corporation
Flowood, Mississippi

We have audited, 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, the financial statements of Mississippi Lottery Corporation (the Corporation), a component unit of the State of Mississippi, which comprise the statement of net position as of June 30, 2020, and the related statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the financial statements, which collectively comprise the Corporation's basic financial statements, and have issued our report thereon dated September 22, 2020.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Corporation'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 Corporation's internal control. Accordingly, we do not express an opinion on the effectiveness of the Corporation's internal control.

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 Corporation'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.

BKD, LLP

Jackson, Mississippi
September 22, 2020