Rhode Island Lottery

An Enterprise Fund of the
State of Rhode Island and Providence Plantations

Comprehensive Annual Financial Report

For the Fiscal Year Ended June 30, 2007

Prepared by the Finance Department

Your Rhode Island Lottery

Rhode Island Lottery

Comprehensive Annual Financial Report
For the Fiscal Year Ended June 30, 2007

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Introductory Section

THE RHODE ISLAND LOTTERY

October 1, 2007

The Honorable Donald L. Carcieri, Governor
Beverly E. Najarian, Acting Director, Department of Revenue

We are pleased to present to you the **COMPREHENSIVE ANNUAL FINANCIAL REPORT** of the Rhode Island Lottery (the Lottery) for the fiscal year ended June 30, 2007. This report has been prepared by the Finance Department of the Lottery. The Lottery is responsible for the accuracy of the financial data and the completeness and fairness of the presentation, including all disclosures.

The Lottery is a division of the Department of Revenue of the State of Rhode Island, and its financial statements are included in the State's Comprehensive Annual Financial Report. This report presents Lottery activity in a single enterprise fund. Only the activity of the Lottery, and no other data or information related to any other State agency or fund, is included in this report.

Generally Accepted Accounting Principles (GAAP) require that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. The Lottery's MD&A can be found immediately following the report of the independent auditors.

The Lottery was created by Constitutional Amendment passed on November 6, 1973. The legislation to create the Lottery was passed in March of 1974, and the Lottery began in May of 1974. The Lottery is operated as a business within the framework of State laws and regulations. Like any business, the Lottery's goal is to maximize income. As a State agency, however, the challenge lies in accomplishing this while maintaining the trust and best interest of the citizens of Rhode Island. It is our goal to achieve both.

THE LOT
1425 Pontiac Avenue Cranston, Rhode Island 02920 401-463-6500 www.rilot.com

History of the Lottery Industry

State run lotteries have long represented to governments an attractive alternative to other taxation methods, since their profits were returned to the public through community works, cultural activities, or financing of various projects. Two examples are the Vatican Museums and the Rialto Bridge in Venice.

To fully understand the history of lotteries in America, one must recognize the fact that the American colonies, at the time of their founding, lacked the capital, both in the public and private sector, needed to start the process of economic and cultural development.

As the English settled in America, the model of development that stressed private rather than public investment motivated them. Royalty in England were simply unwilling to spend their own money or tax their subjects to subsidize the development of the colonies, and lotteries became an important method of raising capital for both the public and private initiatives. In fact, the "Great Standing Lottery" held in London in 1612, was staged to help bail the Virginian Company, the corporation in charge of the settlement of Virginia, out of debt. A notable outcome for the first drawing of this lottery was that Anglican churches held two of the three winning tickets.

Perhaps one of the most poignant lottery stories is that of the abortive attempts to bail Thomas Jefferson out of an $80,000 debt by holding a lottery on his behalf on the 50th anniversary of the adoption of the Declaration of Independence, an anniversary that coincided with the precise day of his death.

In the 1700s, many other founding fathers also supported American lotteries and used them for projects such as the financing of cannons for the Revolutionary War (Benjamin Franklin), the rebuilding of historic Faneuil Hall in Boston (John Hancock) and the financing of construction on the Mountain Road, which opened westward expansion from Virginia (George Washington).

The period from 1740 to 1820 witnessed an explosion of public works construction, such as roads, bridges, and canals, much of which was financed by lottery proceeds.

Many of America's elite, private universities, Yale, Princeton, Harvard, University of Pennsylvania, and Columbia, have buildings funded through the proceeds of lotteries. The fact of the matter was that lacking the endowments built up over centuries by places like Oxford and Cambridge, American higher education had no choice but to resort to lotteries.

Many of the principal religious denominations of America (ironically, many of those which would, in the middle part of the 19th Century, lead the fight against lotteries) actually depended heavily on lotteries to get their start.

While very few people in America would have denied there was a need to raise money to build colleges, bridges, roads, or churches, then as now, America differed over whether lotteries were the appropriate way to raise those funds. The arguments for and against lotteries have not changed significantly over the course of the 200 years, from the 17th Century Puritan and Quaker denunciations of all games of chance, to those similarly voiced by fundamentalist Protestant religious groups in the 19th and 20th Centuries.

The concern about gambling, however, was often overwhelmed by the recognition that the lottery was a means that enabled the accomplishment of useful public projects. William Ames, a Cambridge teacher of many of the leaders of the Massachusetts Bay colony, denounced the playing of the lottery solely for the purpose of gain, but defended lotteries as long as they were intended for some pious end. The settlers of New England would find many virtuous purposes toward which to direct lottery proceeds. During the colonial period, the New England colonies authorized more lotteries than any other region of the country, which benefited colleges, churches, and every other manner of public works construction one could think of.

By the time of the Revolution, most every American colony joined the New England colonies in using lotteries as a primary method for financing both public works and private economic development. This reliance on lotteries was the result of the coming together of two powerful forces, a desperate need for capital to fight the war against Great Britain and the reluctance to impose taxes. It is during this time in history that some of America's most respected statesmen publicly campaigned for lotteries as a means of raising revenues. The two most well known for this were Thomas Jefferson and Alexander Hamilton.

Thomas Jefferson described a lottery as a "salutary instrument . . . where men run small risks for the chance of obtaining a high prize." It was, he said, a "tax laid only on the willing," and was therefore more accepted than any other form of direct taxation. Alexander Hamilton described lotteries as a means by which an ordinary man could "hazard a trifling sum for the chance of considerable gain." Hamilton offered advice, which has been relevant to every lottery organizer since that time. He said there were two cardinal rules for a successful lottery: keep it simple, so that everyone understands the rules, and keep the tickets cheap, so that everyone could afford to participate.

The period of time from 1800 to the Civil War was the most active time for lotteries. There were an incredible number of lotteries in America during this period, some held for public purposes, some for a mixture of public and private purposes, and some for private purposes as entrepreneurs attempted to raise money for their own projects. It was at this time in history that charges of fraud and deception, which coincided with a resurgence of religious opposition to lotteries as being sinful, began.

By the 1820s, there was a vast array of lotteries being conducted, sometimes at the same time on the same day, and although the lottery ticket sellers became increasingly clever in their efforts (P.T. Barnum was a lottery agent), the market was overwhelmed. Because of that, there were many instances where the proceeds from the lottery were not sufficient to pay the prizes, a problem that often resulted in lottery organizers leaving town with the money in hand before the drawing could be held.

Charges of fraud and deception surrounded lotteries of the 19th Century, and the two most commonly believed reasons for these were dishonest lottery promoters and increasing religious opposition. There were, however, many other factors, including the growth of the banking institution, which offered an alternative means for entrepreneurs to raise money; an economic boom in the 19th Century which created sources of excess capital that could be used for investment in public works; and lastly, the willingness of state governments to step in and raise taxes to finance worthwhile public projects.

The full history of the decline of the lottery in America lasted from the Civil War until the resumption of the lottery in 1964 when New Hampshire established a state-run lottery for the purpose of raising money for education. New York, which had been the State to pass the first constitutional prohibition of lotteries in the United States in the 1820s, followed New Hampshire's return into the lottery business in 1967. In 1971, the State of New Jersey started their lottery and introduced a computer-

based weekly game, which offered inexpensive tickets (50 cents), convenience of sale, and a weekly prize of $50,000. In its first year of operation, the New Jersey Lottery grossed $142.5 million and set the trend for the lottery industry. New York and New Hampshire revamped their systems, and other states introduced lotteries utilizing New Jersey's operation as a model.

Lotteries, through the years, have become more diversified. The vast array of lottery games in existence today caters to a variety of consumer tastes. These changes are largely attributable to the work of marketing experts. With greater selections, come increased sales. Considerable changes and new possibilities were introduced in lotteries through major technological innovations such as centralized on-line computer systems (1971) and magnetic strip tickets (1992).

By developing and tailoring products to the needs of clientele, the lottery has established itself as an everyday element in today's society.

History of the Rhode Island Lottery

In 1744, Rhode Island's first lottery raised money for a bridge at Weybosset Street in Providence. Tickets cost about $12 each and raised approximately $6,500 for the bridge. Several other lotteries were conducted throughout the 1700s including a lottery used to partially finance the building of a brick Colony House, which became Rhode Island's first State House following the Declaration of Independence. One of the most successful lotteries in Rhode Island was the one authorized to build Thames Street in Newport. It paid over $1 million in prizes and was so popular that the people of Newport were able to build, pave and extend streets throughout the city.

On November 6, 1973, more than a three to one margin passed a Constitutional Amendment to create a lottery in Rhode Island. The amendment mandated that the General Assembly proscribes and regulates all future lotteries in Rhode Island. Legislation was passed to start the Lottery in March 1974, and it began two months later in May. The original purpose of the Rhode Island Lottery was to make up for the revenue lost from allowing the value of a trade-in automobile toward the sales tax liability on a new automobile.

The Lottery's first drawing was held at the State House on May 30, 1974. This weekly 50-cent game had a top prize of $50,000. Rhode Island was the first state to televise a live lottery drawing in January of 1975, at no expense to the Lottery, which is still the case today. That same year Rhode Island became the first state to have a weekly lottery television program. The Numbers Game began on February 13, 1976 and continues today.

The first instant ticket game, Play Ball, was introduced on May 11, 1976. Since that time an additional 558 instant ticket games have been introduced.

On-line games started in February of 1978, and Lottery sales doubled with this new addition. The 4/40 Game began in the spring of 1981, with variations to that game being made throughout the years.

The Multi-State Lottery Association (MUSL) was formed in 1988 for the purpose of affording small states the opportunity to offer games with a higher jackpot than their population alone would generate. Along with Rhode Island, the initial members were the District of Columbia, Iowa, Oregon, Kansas and West Virginia. The first such game was called Lotto-America, which was replaced with PowerBall® on April 22, 1992. In February of 1998, Rhode Island replaced the Multi-State Daily

Millions Game with the introduction of its own lotto game called Roll Down. This lotto game was succeeded by Easy Win in March 2000, Money Roll in November 2000 and the current game of Wild Money in January 2002.

Keno was introduced in the State on September 13, 1992, becoming the second U.S. Lottery (Oregon was first) to do so. Around this same time, Video Lottery Terminals (VLTs) went on-line at the State's two pari-mutuel facilities.

On July 1, 2005, due to the separation of powers law previously passed, the Rhode Island Lottery Commission was disbanded; and the Division of Lotteries of the Rhode Island Department of Administration was formed. On July 1, 2006, the Division of Lotteries became the State Lottery Division of the State of Rhode Island Department of Revenue.

History of Lottery Games

Lotto Games

The Germans were the first to bring the modern lotto game to the market. Norwest Lotto in northwestern Germany launched the first game on October 9, 1955. Players simply marked 6 figures out of a total of 49 on their coupon. The idea quickly took off, and many other countries soon followed the Germans' lead.

With the "quick pick" feature, players can have the computer generate their numbers at random. Most lotteries offer this option.

Alexandre Fichet (1799-1862), who designed a system to replace manual draws using balls, developed technology for lotto drawings in France. He invented a way to carry out lottery drawings using wheels with numbers from 1 to 9 around the rim. At the end of the wheel's rotation, the winning number was clearly shown through a window.

In 1985, the launch of Tri-Sate Lotto, the first multi-state lottery, linked Maine, New Hampshire and Vermont state lotteries.

Instant Tickets

The first instant lottery ticket was marketed in 1974 in the Commonwealth of Massachusetts, which became the first state lottery to develop and sell an instant game. Today, all state lotteries offer instant tickets, and this type of lottery game is recognized as one of the most popular lottery offerings in North America.

Video Lottery

Although the invention of the "slot" machine dates back to 1890, it was only in 1976 that the first black and white video technology was developed. Color video terminals were launched on the market several months later.

Initially, video lottery machines were only associated with casinos; however, in 1985, the State of Nebraska changed its legislation and allowed the Nebraska Lottery to test a video lottery that was not linked to a central system. The experiment was terminated that same year.

Several years later, when the South Dakota Lottery was searching for new sources of revenue, it took up the idea of video lottery. In March of 1989, legislation allowing the establishment of the first server-connected video lottery was approved. In the fall of 1990, South Dakota offered the first operational video lottery in all of the United States. By 1992, Oregon, Rhode Island, and Louisiana had video lottery terminals up and running in their respective states.

Keno

Keno originated in China more than 2,000 years ago. Legend has it that this game financed the Great Wall of China. The original Chinese game was played with characters from the "Thousand Character Classic", an ancient poem of luck by Confucius. Keno subsequently spread far beyond the borders of China and was well established in both Europe and the United States by the turn of the 20th Century. Today, Keno is a very popular lottery offering because of its flexibility in the number of spots that can be played, which in effect means there are actually several games going on at the same time all with different odds of winning a prize. Daily Keno drawings have proven more successful than those held two or three times a week. Rhode Island is one of only a handful of lotteries offering a new Keno draw every 4 minutes.

Rhode Island Lottery Product Offerings

The Rhode Island Lottery provides the opportunity to participate in the following games:

Instant Tickets

Instant (or scratch) tickets are played by scratching the latex covering off the play area on the ticket. In order to win, the player must match two or three of a kind, get like symbols or wild features. Instant ticket offerings in Rhode Island include card games, as well as whimsical, sports, money, and holiday themes. Also offered are extended play games.

Daily Numbers

The Daily Numbers game has been very popular in Rhode Island since its inception in 1976. Players can wager on 2, 3, or 4 digits. Wagers on 3 and 4 digits can be played in exact or any order. Players can select their own numbers or utilize the computer "quick pick." The Daily Numbers drawing is televised live Monday through Saturday at 7:00 p.m. and at 6:30 p.m. on Sunday.

The Lottery added an Instant Match feature to the Daily Numbers game in September 2002. Instant Match offers the player the chance to win up to $500 instantly on a Daily Numbers ticket, for an additional $1 per wager.

Keno

Keno was introduced in September of 1992 and quickly proved to be a very popular game. Rhode Island Keno has a 10 of 20 of 80 matrix, with a $100,000 top prize. Players can wager on 1 to 10 numbers (spots) utilizing their own number selection or a computer "quick pick." In January of 2000, Keno drawings increased from every 5 minutes to every 4 minutes. These Keno drawings occur from 5:00 a.m. to 12:45 a.m., Monday through Saturday and 7:00 a.m. to 12:45 a.m. on Sunday. In April of 2001, Keno Plus was introduced. Players have the option to purchase this feature that could increase their winnings by ten times, thus giving Keno players the potential to win up to $1,000,000.

PowerBall®

PowerBall® is a Multi-State Lottery game offered in 29 states (including Rhode Island), plus the District of Columbia and U.S. Virgin Islands. Players select "5 out of 55" numbers and a PowerBall® "1 out of 42." Players can select their own numbers or utilize a computer "quick pick." Jackpots start at $15 million and grow by a minimum of $5 million for each drawing not producing a jackpot winner. Televised drawings are shown on Wednesday and Saturday at 10:59 p.m. PowerPlay®, which is a multiplier for PowerBall® winnings, was introduced in March of 2001. Players who choose the PowerPlay® option on their PowerBall® ticket have the chance to increase their winnings by up to 5 times; however, the multiplier does not apply to a jackpot win.

Wild Money

Wild Money is an on-line game with a starting jackpot of $20,000 that continues to grow until a player matches 5 numbers selected out of a field of 35. Its first jackpot of $315,869 was won on April 13, 2002.

HotTrax®

HotTrax® was a monitor game, similar to Keno, in which players wagered on an animated auto race. The race consisted of ten cars which traveled three laps around the racetrack with races lasting approximately one minute. Players bet on the order in which the cars finished the race and wagered $1, $2, $5 and $10. Multiple race wagers were allowed on 1, 2, 5, 10, or 15 consecutive races with a maximum wager of $150 per race. A new prize structure was introduced in September 2005 which increased the number of subsidiary prizes and eliminated the super progressive jackpot. Under this new structure, prizes ranged from $1 to $100,000 based on a variety of $1 wagers. A new race was run approximately every four minutes. The first HotTrax® race was held in May, 2004 and was discontinued on August 19, 2006.

Rhody Poker™

Rhody Poker™ is a seven card poker game. The player combines the two cards on the printed wager with five (5) community cards presented on the monitor during the deal to create the best available five card hand. All plays for Rhody Poker™ are by quick pick only and the minimum wager is $2.

Video Lottery

Video Lottery debuted in Rhode Island in September of 1992. There are a total of 5,671 video lottery terminals (VLTs) located in the State's two pari-mutuel facilities, Twin River and Newport Grand. As of June 30, 2007, Twin River has 4,601 VLTs and Newport Grand has 1,070 VLTs. With anticipated expansion at both facilities, Twin River will have 4,752 VLTs by December 31, 2007 and Newport Grand will have 2,101 VLTs by December 31, 2008. Various card and reel games are offered on the VLTs.

Pull Tabs

Rhode Island General Laws mandate that pull tab tickets be sold only by non-profit organizations. The Rhode Island Lottery oversees the sale of pull tab tickets to these groups.

Rhode Island Economic Outlook

The Rhode Island economy boasts a population of approximately 1.07 million with the civilian labor force increasing 1.54%, total employment increasing 1.47% and unemployment increasing 2.84% over the previous year. The unemployment rate of 5.1% was above the national rate of 4.60%.

Also, the total number of construction housing permits decreased by 11.90%, with total construction costs decreasing by 7.58%.

Lottery Industry Economic Outlook

The United States Lottery Industry continues to experience growth. Based on unaudited figures from the North American Association of State & Provincial Lotteries (NASPL), sales increased from $52.6 billion in fiscal year 2005 to $57.4 billion in fiscal year 2006, up 9.13%.

Highlights of Fiscal Year 2007

- For fiscal year 2007, $320,989,831 was transferred to the State's General Fund.

- Fiscal year 2007 produced record video lottery sales of $1,561.4 million with a resulting net terminal income (sales less prize awards) of $416.7 million.

- Wild Money sales of $5.7 million were a record for the fiscal year ended June 30, 2007. This was a result of higher than average jackpot runs and advertising exposure related to those runs.

- On July 18, 2006, the first Multi-jurisdictional Wide Area Progressive (MWAP) video game began. The Rhode Island Lottery, along with the states of Delaware and West Virginia, is a member of the Video Lottery Game Group (VLGG) of the Multi-State Lottery Association (MUSL). Rhode Island has 65 out of the current 267 video lottery terminals (VLTs) linked among the three states.

- On September 24, 2006, a new state-of-the-art on-line lottery gaming system was implemented.

- At the same time as the introduction of the new on-line gaming system, a new monitor game, Rhody Poker™, was launched.

- During 2007, significant technology changes were introduced to the State's two video lottery facilities, including the implementation of TITO (Ticket-In Ticket-Out), and SAS (Slot Accounting System) technology in which protocol allows a terminal to accept a ticket via a bill acceptor and validate it to the host system, and a facility controlled player tracking system.

- A new instant ticket denomination, $20, was launched in November 2006 with the release of Quarter of a Mil.

GFOA Certificate of Achievement

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the Rhode Island Lottery for its comprehensive annual financial report (CAFR) for the fiscal year ended June 30, 2006. This was the tenth consecutive year that the Lottery has achieved this prestigious award (1997 through 2006). In order to be awarded a Certificate of Achievement, a governmental unit must publish an easily readable and efficiently organized CAFR. This report must comply with both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. The Rhode Island Lottery received a certificate on its first attempt, in May of 1998 and on each subsequent attempt. We believe that our current CAFR continues to meet the Certificate of Achievement Program's requirements, and we are submitting it to the GFOA to determine its eligibility for another certificate.

Accounting Systems and Procedures

The Rhode Island Lottery operates the Lottery fund, an enterprise fund that, like a private business, utilizes the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. Under the accrual basis of accounting, revenues are recognized when earned; and expenses are recognized at the time the related liabilities are incurred.

Budgetary Controls

The operating budget of the Rhode Island Lottery is submitted to the State Budget Office, through the Department of Revenue, for inclusion into the Governor's State Budget to the General Assembly. The State Budget is ultimately legally enacted by the General Assembly.

The Revenue Estimating Conference continues to adopt revenue estimates from the Lottery, which are incorporated into the State Budget.

Internal Control Environment

Management of the Lottery is responsible for establishing and maintaining an internal control structure designed to ensure that assets are protected from loss, theft, or misuse and to ensure that the accounting

system allows compilation of complete, accurate and timely financial information. The structure is designed to provide reasonable assurance that these objectives are met.

Since the Lottery manages a valuable ticket inventory, controls the disbursement of prizes and regulates video lottery activity at the State's two pari-mutuel facilities, the following steps are taken to ensure the operations remain honest and secure:

- Employing an Information Systems Security auditor.
- Continual audits of financial and organizational procedures by our internal auditor.
- Employing specialized security staff.
- Maintaining secure lottery facilities and limiting access to them.
- Performing background checks on Retailers, vendors, and employees.
- Printing lottery tickets with special security features.
- Independent IT security audits of Lottery networks.
- Providing a variety of access and other controls in the computer system.
- Implementing a Video Lottery System Monitoring Plan to ensure the integrity of video lottery games and to ensure that control procedures are operating as designed.
- Performing unannounced video lottery inspections at each facility to ensure compliance with operating procedures.
- Monitoring video lottery terminals on a daily and weekly basis and reconciling to a cash management system.
- Processing daily transaction data of all Retailer activity by Lottery personnel using the Lottery's internal control system programs and reconciling transactions to reports generated by the on-line system.
- Implementation of comprehensive information security objectives for the Lottery's on-line and video lottery systems as provided by its central system provider.

The Lottery currently has 57 employees, all of whom are located at the headquarters in Cranston, Rhode Island. Separated from the headquarters, the drawing studio is located at the broadcast facilities of the television station that produces the nightly drawing.

Cash Management

The Lottery collects cash due for instant and on-line sales from its approximately 1,200 Retailers, through electronic transfer. This was done on a bi-weekly basis until September 2006 when it was switched to a weekly basis. Net proceeds resulting from video lottery operations is deposited into the

Lottery's operating account each business day by the two video lottery facilities. The Office of the General Treasurer invests the Lottery's excess cash in short-term investments.

Risk Management

The Lottery's risk management and insurance program is independent of the State of Rhode Island. Lottery staff administers the program. Insurance with private carriers is maintained to prevent economic loss from uncontrollable risk subject to maximum limits.

Future Projects

The two video lottery facilities (Twin River and Newport Grand) continue to undergo renovations which will result in necessary space to install the full allotment of VLTs at both facilities, as well as new dining and entertainment areas. Newport Grand will also be implementing the Ticket-In Ticket-Out technology.

Installation of the Lottery's new on-line Retailer terminals will be completed to include Customer Display Units (CDUs) to advertise Lottery products, display drawing results of all on-line games, including Keno. Displaying the Keno drawing results in traditional non-Keno locations, will allow those Lottery Retailers the ability to sell Keno tickets.

The Lottery plans to increase advertising of the Keno game, including radio and television, to promote some planned game enhancements, as well as promotions geared toward increasing sales.

The Lottery will be implementing a new Interleave Show, which allows the ability to feature two monitor games running simultaneously on one monitor.

The Lottery is incorporating more licensed products in its Instant Ticket offerings and partnering with Retailers on unique POS (point of sale) and promotions.

The Lottery website capabilities are being enhanced to offer more second chance drawings, opportunities for player feedback, marketing surveys, and player group clubs. In addition, a Retailer page is being added allowing potential Retailers to submit applications on-line and providing licensed Retailers the ability to access their accounts, review their sales, and receive e-mail notifications.

Independent Audit

The Rhode Island General Laws require an annual audit to be performed by the State Auditor General. The fiscal year 2007 audit of the financial statements has been completed in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*. The Independent Auditor's Report on the Lottery's financial statements is included in the financial section of this report. Also, in accordance with *Government Auditing Standards*, the Independent Auditor's 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*, is included in a separate communication.

Acknowledgements

Preparation of this report could not have been accomplished without the efforts of Gina Grant and Sandra Lee.

This Comprehensive Annual Financial Report reflects our commitment to maintain the Rhode Island Lottery's financial statements and record keeping systems in compliance with the highest standards of accountability.

Respectfully submitted,

Gerald S. Aubin
Director

Daniel R. Sarro
Finance Administrator

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Rhode Island Lottery

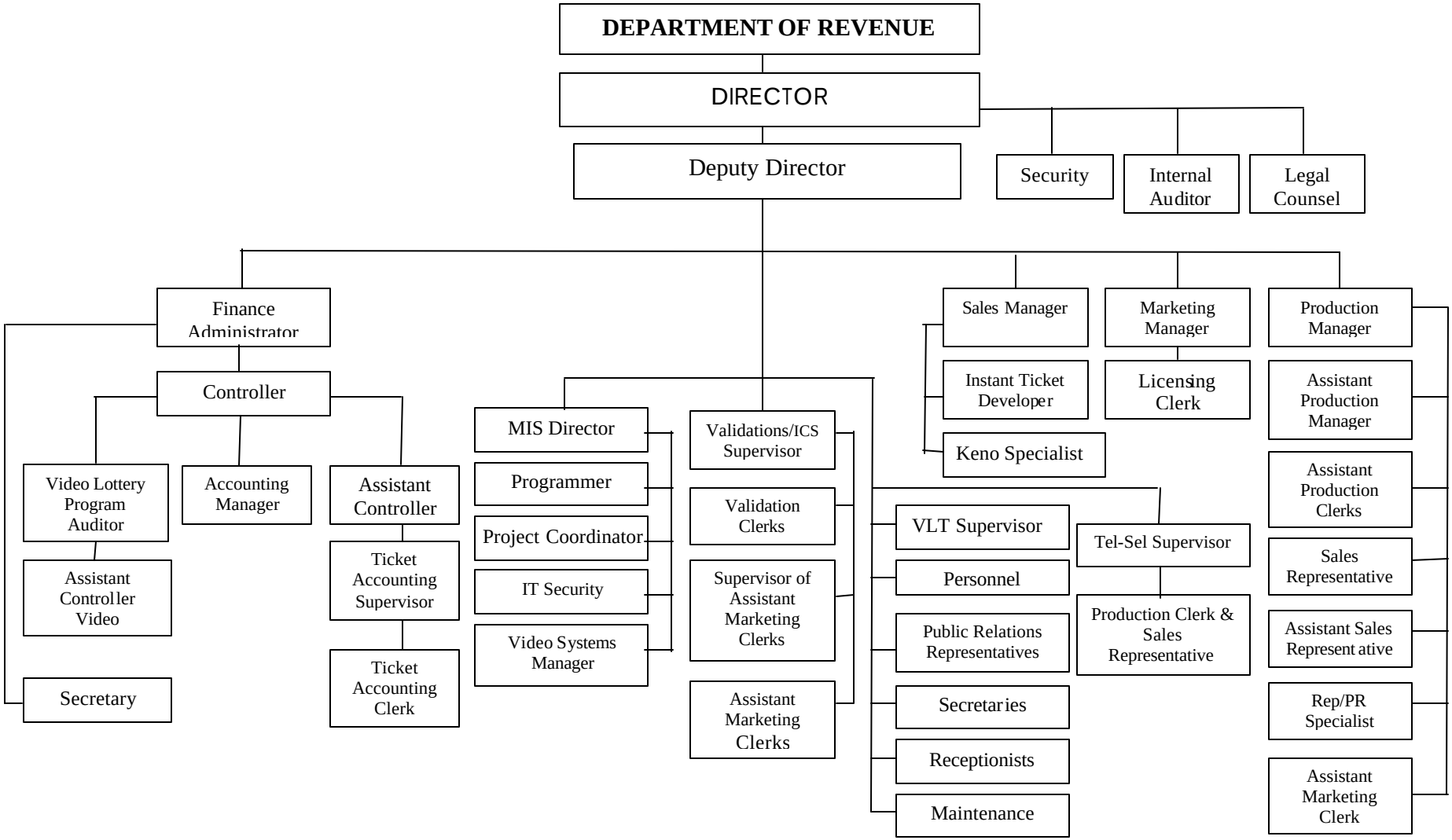
For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2006

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.

President

Executive Director

Rhode Island Lottery
Organizational Chart
June 30, 2007



PRINCIPAL OFFICIALS

GERALD S. AUBIN
DIRECTOR

MARGARET D. ROSE
DEPUTY DIRECTOR

DANIEL R. SARRO
FINANCE ADMINISTRATOR

SANDRA M. LEE
CONTROLLER

DONALD J. CATALDI
SALES AND MARKETING MANAGER

Financial Section

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STATE OF RHODE ISLAND and PROVIDENCE PLANTATIONS

GENERAL ASSEMBLY

OFFICE of the AUDITOR GENERAL

- INTEGRITY
- RELIABILITY
- INDEPENDENCE
- ACCOUNTABILITY

INDEPENDENT AUDITOR'S REPORT

Joint Committee on Legislative Services, General Assembly,
State of Rhode Island and Providence Plantations:

We have audited the accompanying financial statements of the Rhode Island Lottery (Lottery), an enterprise fund of the State of Rhode Island and Providence Plantations, as of and for the year ended June 30, 2007, as listed in the table of contents. These financial statements are the responsibility of the Lottery's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 2(B), the financial statements present only the Lottery enterprise fund and do not purport to, and do not, present fairly the financial position of the State of Rhode Island and Providence Plantations, as of June 30, 2007, the changes in its financial position, or, where applicable, its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Lottery as of June 30, 2007, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

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In accordance with *Government Auditing Standards*, we have also issued our report dated September 28, 2007 on our consideration of the Lottery's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis on pages 18 through 24 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Lottery's basic financial statements. The supplementary information included in Schedule 1 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Schedule 1 has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

Ernest A. Almonte

Ernest A. Almonte, CPA, CFE
Auditor General

September 28, 2007

RHODE ISLAND LOTTERY

Management's Discussion and Analysis

Management of the Lottery provides this *Management's Discussion and Analysis* of their financial performance for the readers of the Lottery's financial statements. This narrative provides an overview of the Lottery's financial activity for the fiscal year ended June 30, 2007. This analysis is to be considered in conjunction with the financial statements to provide an objective analysis of the Lottery's financial activities based on facts, decisions, and conditions currently facing management.

Understanding the Lottery's Financial Statements

The Lottery, a division of the Department of Revenue of the State of Rhode Island and Providence Plantations (State), 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 notes to the financial statements and a supplementary schedule detailing sales, commissions and prize awards expense for each lottery game. The financial statements immediately follow this *Management's Discussion and Analysis* and are designed to highlight the Lottery's net assets and changes to those assets resulting from Lottery operations.

The most important relationship demonstrated within the Lottery's financial statements is the requirement that the Lottery transfer all net income to the State's General Fund. Accordingly, the primary focus of these financial statements is determining net income available for payment to the State's General Fund rather than the change in net assets of the Lottery. It is also important to note that most financial statement balances have a direct or indirect relationship to revenue. As lottery sales increase, the amount paid to the State's General Fund also increases. Similarly, increases in revenue for a particular lottery game result in direct increases to the related prize awards and commissions expense.

Most assets included on the Statement of Net Assets represent current amounts such as cash and accounts receivable from Lottery Retailers. Most liabilities represent current prize awards owed, vendor commission payments and amounts due to the State's General Fund. Current assets approximate the amounts required to satisfy current liabilities at June 30. Few capital assets are required for Lottery operations.

The deficiency in net assets of $10.0 million reported at June 30, 2007 relates entirely to the Lottery's sale of its exclusive rights to operate its gaming systems. The Lottery sold this exclusive right to its current gaming systems provider for a 20-year period at a cost of $12.5 million and immediately paid the proceeds to the State's General Fund. According to the terms of the agreement, if for any reason, this contract is voided prior to its completed term; the Lottery will be required to refund a pro-rata share of the sales price to the gaming system provider. In accordance with generally accepted accounting principles, the Lottery will recognize the revenue related to this transaction over the 20-year life of the contract.

Financial Highlights

- The Rhode Island Lottery's sales for fiscal year 2007 totaled $1,806,217,630; a 4.33% increase compared to fiscal year 2006 sales of $1,731,315,483.

- Gross video lottery sales increased $91.2 million. Video lottery operations for fiscal 2007 continued without interruption amongst significant renovations and construction being conducted to Twin River.

- During fiscal year 2007, the Lottery transferred $321 million to the State's General Fund as compared to $323.9 million for fiscal year 2006. The State's share of video lottery operations for the months of April through June 2007 increased by 15% over the same periods in fiscal 2006 due to the completion of renovations and expansion at Twin River.

Assets and Liabilities

	June 30, 2007	June 30, 2006
Assets:		
Current assets		
Cash and cash equivalents	$ 12,087,958	$ 9,925,829
Accounts receivable, net	8,577,343	7,735,467
Other	1,451,760	1,292,252
Total current assets	$ 22,117,061	$ 18,953,548
Long-term assets		
Capital assets, net	$ 1,138,619	$ 1,314,290
Total assets	$ 23,255,680	$ 20,267,838
Liabilities:		
Current liabilities		
Due to State's General Fund	$ 2,989,832	$ 1,099,490
Accounts payable	12,641,860	10,705,641
Prize obligations	5,970,841	7,028,196
Other liabilities	2,278,147	2,059,511
Total current liabilities	$ 23,880,680	$ 20,892,838
Long term liabilities		
Unearned contract revenue	$ 9,375,000	$ 10,000,000
Total liabilities	$ 33,255,680	$ 30,892,838
Net Assets:		
Invested in capital assets	$ 1,138,619	$ 1,314,290
Unrestricted	(11,138,619)	(11,939,290)
Total net assets (deficiency)	$ (10,000,000)	$ (10,625,000)

The majority of the Lottery's assets consist of cash (including amounts invested in cash equivalent type instruments) and accounts receivable derived from sales of the Lottery's games. At June 30, 2007, the Lottery's assets included $12.1 million in cash and cash equivalents as compared with $9.9 million at June 30, 2006. The Lottery's accounts receivable approximated $8.6 and $7.7 million, respectively, at June 30, 2007 and 2006.

Management's Discussion and Analysis

The Lottery's liabilities included at the balance sheet date are amounts owed for vendor payables, prize obligations, and a residual amount owed to the State's General Fund for June's net operations. The amount owed to the General Fund approximated $3.0 million at June 30, 2007 as compared with $1.1 million due at June 30, 2006. Vendor payables, made up largely of commissions due to video lottery participants, and prize obligations, attributable mostly to instant ticket games and PowerBall®, were $12.6 million and $6.0 million, respectively. In comparison, vendor payables and prize obligations at June 30, 2006 were $10.7 and $7.0 million, respectively.

The majority of the Lottery's assets represent current resources necessary to pay the current liabilities owed to vendors, prize winners, video lottery participants, and ultimately the State's General Fund.

The deficiency in net assets reported at June 30, 2007, as previously explained, relates to the Lottery's immediate transfer, in a prior fiscal year, to the State's General Fund of all proceeds received from the sale of its exclusive rights over the operation of its gaming systems.

Lottery Operations

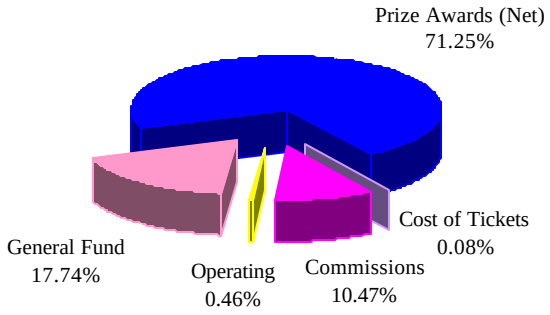
	Year Ended June 30, 2007	Year Ended June 30, 2006
Revenue:		
On-line games	$ 164,867,948	$ 177,103,410
Instant games	79,980,026	84,018,698
Video lottery	1,561,369,656	1,470,193,375
Other income	2,635,722	2,342,618
Total revenue	$ 1,808,853,352	$ 1,733,658,101
Expenses:		
Cost of sales	$ (1,479,059,694)	$ (1,401,879,818)
Operating expenses	(8,178,827)	(7,253,792)
Payments to State's General Fund	(320,989,831)	(323,899,491)
Total expenses	$ (1,808,228,352)	$ (1,733,033,101)
Change in net assets	$ 625,000	$ 625,000
Total net assets (deficiency), beginning of year	(10,625,000)	(11,250,000)
Total net assets (deficiency), end of year	$ (10,000,000)	$ (10,625,000)

RHODE ISLAND LOTTERY

Management's Discussion and Analysis

Sales

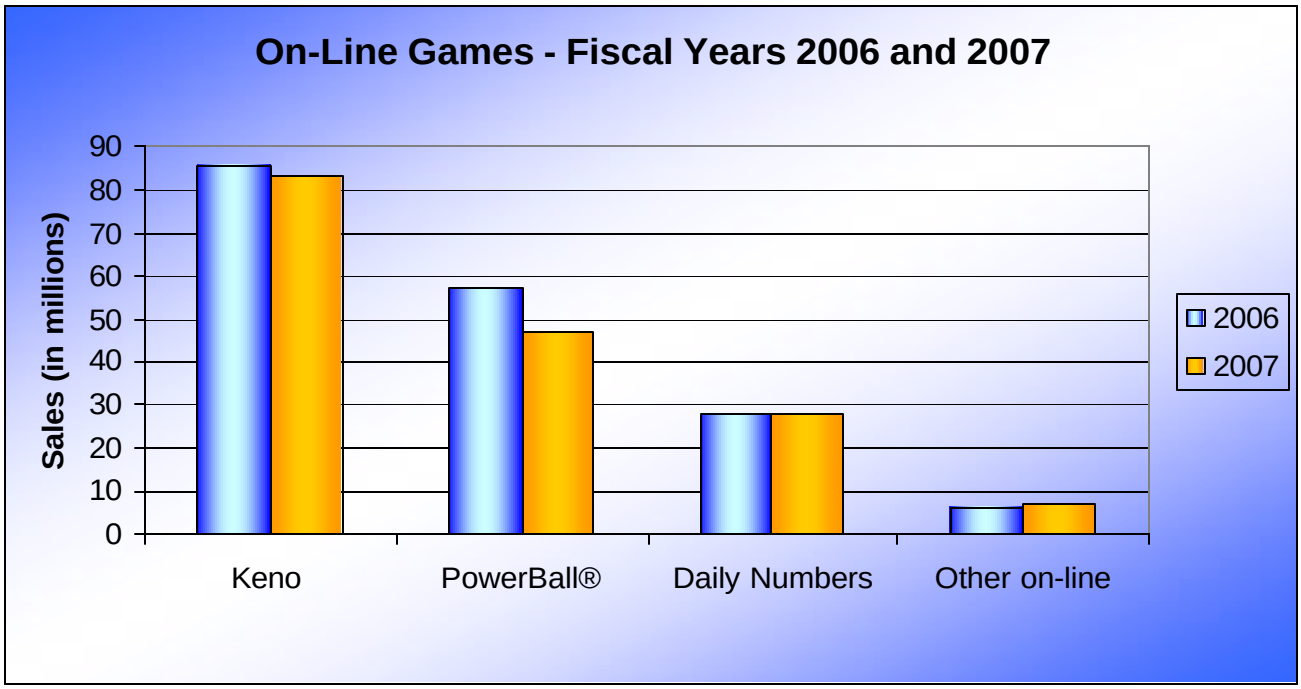
Distribution of the year's revenue was as follows:



Lottery sales are categorized as on-line, instant and video lottery games. The first category, on-line games, consisted of PowerBall®, Keno, Daily Numbers, Rhody Poker™ and Wild Money at June 30, 2007. In total, on-line sales decreased by $12.2 million, which is mostly attributable to decreased PowerBall® sales. PowerBall® sales for the fiscal year ended June 30, 2007 decreased $10.1 million or 17.68% over the prior fiscal year due to a decrease in the number of substantially larger jackpots.

Keno sales for the fiscal year ended June 30, 2007 decreased by $2.5 million or 2.94%.

The following graph depicts the Lottery's on-line sales for the fiscal years ended June 30, 2006 and 2007.



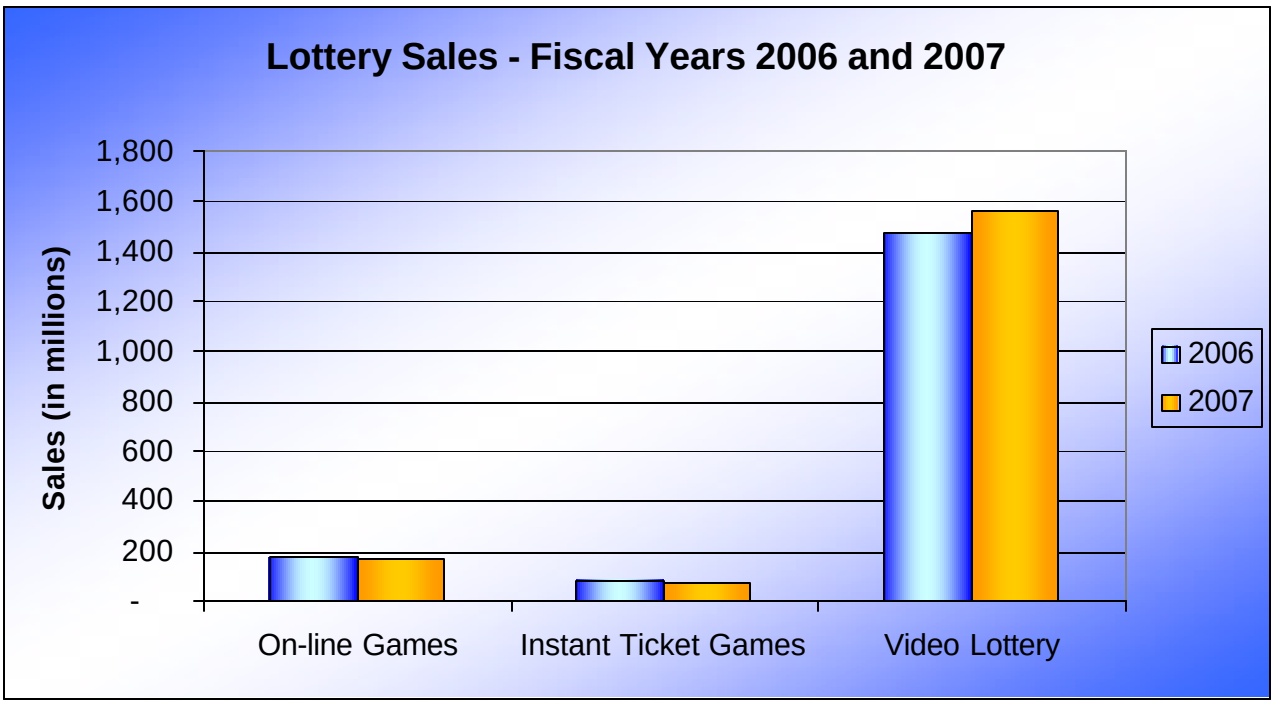
Management's Discussion and Analysis

Instant tickets or "scratch" tickets are the second type of Lottery game offered to the public. Instant ticket sales for the fiscal year ended June 30, 2007 decreased $4.0 million or 4.81% over the preceding fiscal year.

The third type of game offered is video lottery. Video lottery sales increased $91.2 million with a corresponding increase of $90.9 million in prize awards. This comparable increase in both video lottery sales and prize awards expense is mostly related to the Lottery's implementation of TITO ("Ticket In / Ticket Out") technology during March 2007 for the majority of video terminals located at Twin River. TITO technology allows video terminals to accept cash-out tickets so that patrons can transfer their credits from terminal to terminal without having to redeem them for cash. The convenience of transferring credits between terminals increases reported revenue and also results in a comparable increase in reported prize awards.

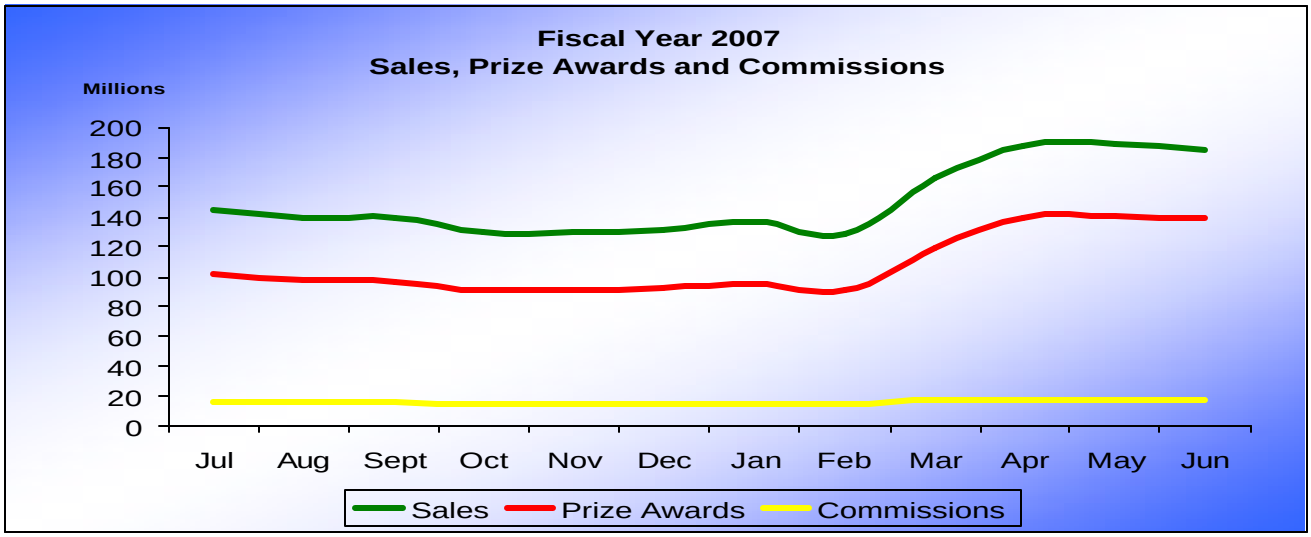
During the fiscal year ended June 30, 2007, significant construction in the form of renovations and expansion took place at the Twin River facility. The expansion included a new gaming area, entertainment facility and additional dining establishments. The construction work, while having minimal impact on video operations, did result in certain inconvenience to the public. The initial decrease in video revenue during the year caused by the facility construction was quickly offset by the increase in revenues generated by the Twin River "Grand Re-opening" and the completion of significant expansion and renovations at the facility during March 2007.

The following graph depicts the Lottery's on-line, instant, and video lottery sales for the fiscal year ended June 30, 2006 in comparison to fiscal year ended June 30, 2007.



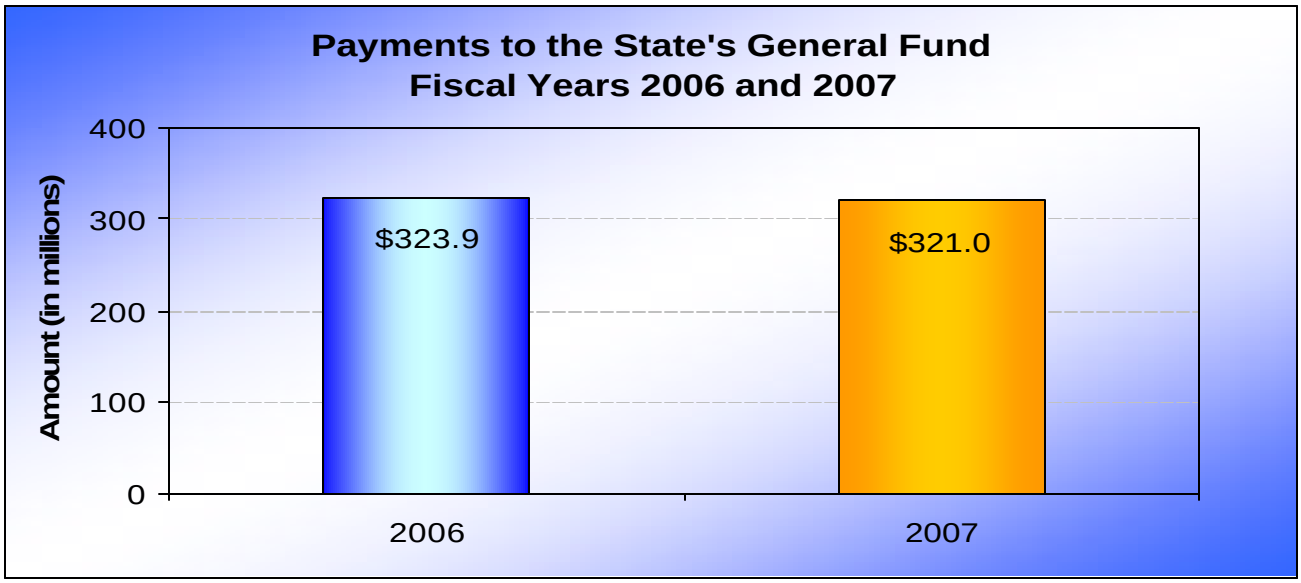
Commissions and Prize Awards Expense

As the following graph depicts, the Lottery's most significant expenses (commissions and prize awards) are predictable because they have a direct correlation to sales. As lottery sales increase, so do the related prizes and commissions paid by the Lottery. While each Lottery game has a designed prize payout structure, the overall amount paid as prize awards expense is consistent in relation to sales.



Payments to the State's General Fund

Payments to the State's General Fund for the fiscal year ended June 30, 2007 decreased by $2.9 million to a total of $321.0 million for the period as compared to $323.9 million for the fiscal year ended June 30, 2006. Payments to the State's General Fund are estimated to reach $339.7 million for the fiscal year ended June 30, 2008.



Debt Administration

Jackpot prizes awarded under PowerBall® are satisfied through investments purchased by MUSL. MUSL purchases United States government obligations, which are held in irrevocable trusts established by MUSL for the benefit of participating state lotteries. Accordingly, the Lottery does not record an obligation for PowerBall® jackpot awards which are payable in installments from funds provided by MUSL.

Capital Assets

For further information, refer to Notes to Financial Statements, Note 4.

Potential Factors Impacting Future Operations

The Lottery's mission is to maximize revenues for the purpose of maximizing payments to the State's General Fund. A continuous assessment of the State's financial environment and the Lottery's own product lines and operations are essential to accomplish this mission. The following considerations have been presented to inform those interested in the Lottery's operations about potential factors that could affect future operations:

- The Lottery's video lottery operations currently compete with Indian gaming casinos in nearby Connecticut. Proposals are continually made in Rhode Island, as well as neighboring Massachusetts, to seek approval from the voters to allow Indian gaming or other casinos in Rhode Island and Massachusetts. The Lottery's operations may be impacted by competition from other gaming interests that may be developed within Rhode Island or neighboring states.

- The Lottery has entered into long-term agreements with both of its video lottery facility operators. These agreements, in general, guarantee the facilities a set commission percentage over the contract term and require the facilities to make significant capital investments to renovate the existing facilities. In addition, the agreements authorized a total of 6,853 video lottery terminals to be allocated to the facilities as renovations are completed. The extent and timing of facility renovations are expected to have a significant impact on future video revenues.

Contacting the Lottery's Financial Management

This financial report is designed to provide a general overview of the Lottery's financial activity for all those interested in the Lottery's operations. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Office of the Finance Administrator, Rhode Island Lottery, 1425 Pontiac Avenue, Cranston, Rhode Island, 02920.

RHODE ISLAND LOTTERY

Statement of Net Assets

June 30, 2007

Assets

Current assets:		
Cash and cash equivalents (note 3)	$	12,087,958
Accounts receivable-less allowance for doubtful accounts of $311,317		8,577,343
Deposits with Multi-State Lottery Association (MUSL) (note 1)		481,743
Ticket inventory		970,017
Total current assets	$	22,117,061
Capital assets, net (note 4)		1,138,619
Total assets	$	23,255,680

Liabilities

Current liabilities:		
Due to State's General Fund (note 5)	$	2,989,832
Current obligation for unpaid prize awards		5,970,841
Accounts payable		12,641,860
Accrued expenses		1,471,165
Deferred revenue		181,982
Unearned contract revenue (note 8)		625,000
Total current liabilities	$	23,880,680
Long-term portion of unearned contract revenue (note 8)		9,375,000
Total liabilities	$	33,255,680

Net Assets

Invested in capital assets (note 8)		1,138,619
Unrestricted (note 8)		(11,138,619)
Total net assets (deficiency)	$	(10,000,000)

See accompanying notes to financial statements.

RHODE ISLAND LOTTERY

Statement of Revenue, Expenses and Changes in Net Assets

Year Ended June 30, 2007

Sales (schedule 1):		
On-line games	$	164,867,948
Instant games		79,980,026
Video lottery		1,561,369,656
Total sales	$	1,806,217,630
Cost of sales:		
Commissions (note 6)	$	189,395,675
Prize awards		1,292,188,767
Unclaimed prize recovery		(3,979,177)
Cost of tickets		1,454,429
Total cost of sales		1,479,059,694
Gross profit	$	327,157,936
Operating expenses:		
Personal services	$	4,450,807
Advertising		2,361,834
Contract services		136,973
Depreciation		261,956
Other		967,257
Total operating expenses		8,178,827
Operating income	$	318,979,109
Non-operating income (expense):		
Other income		2,635,722
Payments to State's General Fund		(320,989,831)
Change in net assets	$	625,000
Total net assets (deficiency), beginning of year		(10,625,000)
Total net assets (deficiency), end of year (note 8)	$	(10,000,000)

See accompanying notes to financial statements.

RHODE ISLAND LOTTERY

Statement of Cash Flows

Year Ended June 30, 2007

Cash flows from operating activities:	
Cash received from lottery sales	$ 1,805,273,680
Cash received from MUSL for grand prize winners	7,136,250
Cash received from sale of other tickets	228,582
Cash received from rental income and other receipts	219,906
Cash paid for prizes other than MUSL grand prize winners	(1,289,266,946)
Cash paid to MUSL grand prize winners	(7,136,250)
Cash paid for commissions - retailers	(17,675,226)
Cash paid for commissions - video lottery	(157,009,564)
Cash paid for commissions - on-line games contractor	(12,346,295)
Cash paid to suppliers for goods and services	(5,057,261)
Cash paid to employees for services	(4,431,229)
Net cash provided by operating activities	319,935,647
Cash flows from noncapital financing activities:	
Payments to State's General Fund	(319,099,489)
Net cash used for noncapital financing activities	(319,099,489)
Cash flows from capital and related financing activities:	
Purchase of capital assets	(86,285)
Net cash used for capital and related financing activities	(86,285)
Cash flows from investing activities:	
Interest income	1,412,256
Net cash provided by investing activities	1,412,256
Net decrease in cash and cash equivalents	2,162,129
Cash and cash equivalents at July 1, 2006	9,925,829
Cash and cash equivalents at June 30, 2007	$ 12,087,958

See accompanying notes to financial statements.

Continued.

RHODE ISLAND LOTTERY

Statement of Cash Flows (continued)

Year Ended June 30, 2007

Reconciliation of operating income to net cash provided by operating activities:	
Operating income	$ 318,979,109
Adjustments to reconcile operating income to net cash provided by (used for) operating activities:	
Depreciation	261,956
Miscellaneous receipts classified as operating activities	167,577
Rental income and other receipts	430,889
Provision for doubtful accounts	(20,191)
(Increase) decrease in assets:	
Accounts receivable	(821,685)
Inventory	51,475
Deposits with MUSL	(210,983)
Increase (decrease) in liabilities:	
Obligation for unpaid prize awards	(1,057,356)
Accounts payable	1,936,220
Accrued expenses	353,301
Deferred revenue	(134,665)
Total adjustments	956,538
Net cash provided by operating activities	$ 319,935,647

See accompanying notes to financial statements.

(1) *Organization*

The Lottery was created in 1974 under the General Laws of the State of Rhode Island (General Laws) to establish and operate lottery games for the purpose of generating resources for the State's General Fund. On July 1, 2006 the Lottery became a division of the Department of Revenue.

The Lottery offers:

- On-line games that include: Daily Numbers, Keno, Rhode Poker™, Wild Money and PowerBall®, which is operated by the Multi-State Lottery Association (MUSL);
- Instant tickets, some of which involve top prize drawings, and
- Video lottery games which are located at two licensed facilities.

Prize payout percentages and amounts required to be paid to the State's General Fund as stipulated in the General Laws are summarized below for the various games operated by the Lottery.

Game	Prize Payout	State's General Fund Share
Daily Numbers Rhody Poker™ Instant Ticket Games MUSL – PowerBall® Wild Money	Not less than 45% or more than 65% of sales	Not less than 25% of ticket sales
Keno	Not less than 45% or more than 72% of sales	Not less than 15% of ticket sales
Video Lottery	Prize payout not established by law	Net terminal income (video lottery credits purchased less credits redeemed or redeemable) after 4% MWAP contribution and commission payments mandated by RI General Laws

Chapter 42-61.2 of the General Laws authorizes the Division of Lotteries to conduct and control video lottery games. This chapter stipulates the allocation of video lottery net terminal income (video lottery credits purchased less credits redeemed or redeemable). Net terminal income is divided among licensed video lottery facility operators, the technology providers (video lottery terminal providers), the central communications system provider, the city or town in which the video facility is licensed and the Narragansett Indian Tribe. All residual net

(1) *Organization - (Continued)*

terminal income after mandated commission payments is remitted to the State's General Fund.

The Lottery sells PowerBall® tickets, collects all revenues, and remits prize funds to MUSL net of low-tier prize awards. Jackpot prizes are payable in either a lump-sum cash distribution or annual installments. Annual installments are satisfied through investments purchased by MUSL. MUSL purchases U.S. government obligations, which are held in irrevocable trusts established by MUSL for the benefit of participating state lotteries. Accordingly, the Lottery does not record an obligation for jackpot awards which are payable in installments from funds provided by MUSL.

The prize pool for PowerBall® is 50% of each drawing period's ticket sales. MUSL has placed 2% of each drawing period's ticket sales for PowerBall®, included as part of each member's prize liability, in prize reserve funds. The maximum balance on the prize reserve funds for PowerBall® is $100.0 million. Once the prize reserve funds exceed this designated cap, the excess becomes part of the prize pool. The prize reserve funds serve as a contingency reserve to protect MUSL from unforeseen prize liabilities, and these reserve funds are to be used at the discretion of the MUSL Board of Directors. The prize reserve funds are refundable to MUSL members if the MUSL disbands or if a member leaves MUSL. Members leaving MUSL must wait one year before receiving their remaining share, if any, of prize reserve funds. At June 30, 2007, the prize reserve funds for the PowerBall® game reported a balance of $69.7 million of which the Lottery's share was $1.6 million. The Lottery has charged amounts placed into the prize reserve funds to prize awards expense as the related sales have occurred.

All investment earnings relating to the prize reserve funds are credited to an unreserved account for each member state. This account can be utilized to offset operating costs or for the promotion of any MUSL game as approved by the MUSL Board of Directors. During fiscal year 2007, MUSL reduced the Lottery's unreserved account by $61,529 for a pro rata share of annual operating expenses. The Lottery has recorded all income and operating expenses related to its unreserved account and has reported the balance of $231,743 at June 30, 2007 on the Statement of Net Assets in "Deposits with MUSL".

The remaining $250,000 that makes up the account balance of $481,743 represents the contribution for the initial MWAP prize reserve account.

MUSL issues a publicly available annual financial report that may be obtained by writing to the Multi-State Lottery Association, 4400 NW Urbandale Drive, Urbandale, Iowa 50322.

(2) *Summary of Significant Accounting Policies*

(a) *Basis of Accounting*

The financial records of the Lottery, an enterprise fund, are accounted for using the economic resources measurement focus and are maintained on the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned

(2) *Summary of Significant Accounting Policies – (Continued)*

and expenses are recognized at the time the related liabilities are incurred. The Governmental Accounting Standards Board (GASB) has the responsibility for establishing generally accepted accounting principles for governmental proprietary fund type activities.

In accordance with GASB Statement No. 20, in the absence of specific guidance from a GASB pronouncement, pronouncements of the Financial Accounting Standards Board (FASB) issued on or before November 30, 1989 have been followed.

The Lottery has considered the impact and requirements of newly issued GASB Statements in the preparation of these financial statements.

(b) *Reporting Entity*

The Lottery, a division of the Department of Revenue of the State of Rhode Island and Providence Plantations (State), is accounted for as an enterprise fund for financial reporting purposes. Accordingly, its annual financial statements are included in the State's Comprehensive Annual Financial Report (CAFR). The accompanying financial statements are not intended to present the financial position and results of operations of the State.

(c) *Revenues and Expenses*

The Lottery defines all revenues and expenses deriving from on-line, instant ticket and video lottery sales as operating. All other revenues and expenses are defined as non-operating.

Revenue from the sale of lottery tickets and video lottery, and expenses for prizes and commissions are recognized as follows:

1. On-line lottery games with specific drawing dates - when the related drawings are held.

2. Instant ticket lottery games - when ticket packets are charged to retailers. Prize expense is recognized in proportion to the number of tickets sold based on the stated prize structure for a specific instant ticket game.

3. Video lottery games - when game credits are purchased and when game credits are redeemable. Video lottery revenue and prize expenses are recorded at the amount of credits purchased and the amount of credits redeemable or allocated to progressive jackpots. These amounts are net of credits won and played.

The Lottery accrues for the maximum prizes payable. Prize obligations, other than those relating to prizes payable in installments, that remain unclaimed one year after the drawing date are reported as a reduction to the cost of sales.

(2) *Summary of Significant Accounting Policies* – (Continued)

(d) *Capital Assets*

Capital assets are stated at historical cost. Depreciation is computed using the straight-line method based on the estimated useful lives of the assets. The Lottery's capitalization threshold is $5,000.

(e) *Cash Equivalents*

Cash equivalents consist of highly liquid investments with a maturity of three months or less at the time of purchase and are stated at cost plus accrued interest which approximates fair value.

(f) *Ticket Inventory*

Inventory consists of the cost of tickets for the instant games, which is expensed as a percentage of sales from instant ticket games.

(g) *Deferred Revenue*

Tickets can be purchased in advance of scheduled drawing dates. Revenue from advance ticket sales is recognized during the period in which the related drawing is held. Sales pertaining to future drawings are reported as deferred revenue.

(h) *Unearned Contract Revenue*

Unearned contract revenue relates to the sale of the exclusive rights to the operation of the Lottery's gaming systems. The revenue is recognized ratably over the life of the contract.

(i) *Use of Estimates*

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

(3) *Deposits and Investment Risk*

(a) *Deposits*

A cash balance of $198,348 existed at June 30, 2007; the bank balance at that date was $211,597. The primary difference between the book and bank balances was outstanding checks. All deposits were in the custody of the State General Treasurer. All General Treasurer accounts at a single institution are aggregated for purposes of determining

(3) *Deposits and Investment Risk* – (Continued)

Federal Depository Insurance coverage.

In accordance with Chapter 35-10.1 of the General Laws, depository institutions holding deposits of the State, its agencies or governmental subdivisions of the State, shall at a minimum, insure or pledge eligible collateral equal to one hundred percent of time deposits with maturities greater than 60 days. Any of these institutions which do not meet capital standards prescribed by federal regulators shall insure or pledge eligible collateral equal to one hundred percent of deposits, regardless of maturity. None of the cash deposits of the Lottery was required to be collateralized at June 30, 2007.

(b) *Investments*

All investments, principally cash equivalent type investments, are made by the State General Treasurer in accordance with guidelines established by the State Investment Commission (SIC), which is responsible for the investment of all State funds. Pursuant to Chapter 35-10 of the General Laws, the SIC may, in general, "invest in securities as would be acquired by prudent persons of discretion and intelligence in these matters who are seeking a reasonable income and the preservation of their capital."

At June 30, 2007, the Lottery's investment balances were as follows:

Investment Type	Fair Value	Maturity	Rating
Money Market	$ 10,290,038	N/A	N/A
Federal Farm Credit Bank Discount Note	$ 1,599,572	July 2, 2007	AAA[1]
Total:	$ 11,889,610		

[1] - Rating per Standard & Poor's Investors Service

Custodial Credit Risk: Pursuant to guidelines established by the SIC, securities purchased, or underlying collateral, are required to be delivered to an independent third party custodian.

Interest Rate Risk: Based on SIC policy, the State's short-term investment portfolio, whenever possible, will be structured to minimize interest rate risk, by matching the maturities of investments with the requirements for funds disbursement. The State invests the Lottery's available cash in short-term investments limiting its exposure to fair value losses arising from rising interest rates. The Lottery's investments are typically either overnight or with maturities less than 30 days thereby minimizing the Lottery's exposure to interest rate risk.

Credit Risk: The SIC has adopted policies regarding acceptable short-term investment

(3) *Deposits and Investment Risk* – (Continued)

types. Credit risk policies have been developed for investments in commercial paper. The investment in the Federal Farm Credit Bank Discount Note is rated AAA by Standard and Poor's Investors Service.

Concentration of Credit Risk: The SIC has adopted limitations as to the maximum percentages of the State's total short-term investment portfolio that may be invested in a specific investment type or with any one issuer of securities. The Lottery's only investment at June 30, 2007 is the $11.89 million Federal Farm Credit Bank Discount Note. Federal Farm Credit Bank securities are implicitly guaranteed by the Federal Government.

(c) *Cash and Cash Equivalents*

Cash and cash equivalents on the Statement of Net Assets consist of the following:

Cash balance per books	$ 198,348
Investments classified as cash equivalents	11,889,610
Cash and cash equivalents	$ 12,087,958

(4) *Capital Assets*

Lottery headquarters are situated on land owned by the State of Rhode Island. The State has assigned custody, control and supervision of the land to the Lottery at no cost. However, since title to such land remains vested in the State, it is not recorded in the statement of net assets.

(4) *Capital Assets* – (Continued)

A summary of capital assets follows:

	Estimated Useful Life	2006 Balance	2007 Additions	2007 Disposals	2007 Balance
Cost					
Building	20	$ 1,468,983	$ -	$ -	$ 1,468,983
Building improvements	10	1,868,165	7,681	-	1,875,846
Ticket production equipment	10	14,938	-	-	14,938
Office equipment	10	69,906	-	-	69,906
Furniture and fixtures	10	92,500	-	-	92,500
Lottery drawing equipment	3	87,023	-	-	87,023
Automobiles	3	282,158	78,604	(96,570)	264,192
Computer equipment	3	317,270	-	(8,478)	308,792
Trucks	3	22,445	-	-	22,445
Total		$ 4,223,388	$ 86,285	$ (105,048)	$ 4,204,625
Less: Accumulated Depreciation					
Building		$ 1,445,239	$ 1,553	$ -	$ 1,446,792
Building improvements		748,444	177,050	-	925,494
Ticket production equipment		13,688	946	-	14,634
Office equipment		46,576	5,062	-	51,638
Furniture and fixtures		43,207	7,424	-	50,631
Lottery drawing equipment		87,023	-	-	87,023
Automobiles		196,934	63,269	(96,570)	163,633
Computer equipment		305,542	6,652	(8,478)	303,716
Trucks		22,445	-	-	22,445
Total		$ 2,909,098	$ 261,956	$ (105,048)	$ 3,066,006
Capital assets, net		$ 1,314,290	$ (175,671)	$ -	$ 1,138,619

(5) *Due to State's General Fund*

Due to State's General Fund represents the balance of net income for the period (after adjustment of $625,000 relating to recognition of the pro-rata share of contract revenue - see Note 8) that is to be paid to the State's General Fund. The amounts paid and amounts due to State's General Fund are summarized as follows:

Due to State's General Fund, beginning of year	$ 1,099,490
Payments to State's General Fund	320,989,831
Cash paid during fiscal year	(319,099,489)
Due to State's General Fund, end of year	$ 2,989,832

(6) *Commissions*

The Lottery pays commissions to ticket retailers and its on-line games contractor based on a percentage of gross ticket sales. Video lottery commissions, as specified in the General Laws,

(6) *Commissions* – (Continued)

are paid to the facility operators, technology providers (video lottery terminal providers), the central communications provider and others based on various percentages of net terminal income (video lottery credits purchased less credits redeemed or redeemable).

The General Laws provide for reductions of certain video lottery commissions. The amount reduced is to be credited to the State's Distressed Communities Relief Fund, which is part of the State's General Fund. The Lottery has reflected the actual video commissions paid as an expense. The amount to be credited to the Distressed Communities Relief Fund is included in the payments to the State's General Fund.

(7) *Compensated Absences*

The Lottery accrues an estimated liability for vested benefits relating to future compensated absences. This includes an expected obligation in connection with vacation credits and accumulated vested sick pay for those employees eligible for retirement. As of June 30, 2007, the estimated liability was $242,292. The liability is calculated using the current hourly rates of pay.

(8) *Net Assets - (Deficiency)*

On May 12, 2003, the Lottery entered into a 20-year contract, effective July 1, 2003, with its current gaming system provider. The contract granted the provider the right to be the Lottery's exclusive vendor of hardware and software, together with the related services necessary for the operation of the Lottery's computerized games, through June 30, 2023. In return, the provider made a one-time payment of $12.5 million to the Lottery as consideration for this exclusive contract right. The Lottery recorded unearned contract revenue in the amount of $12.5 million and transferred the cash to the State's General Fund on June 30, 2003. This prior year transfer of unearned contract revenue resulted in a deficiency in net assets at June 30, 2007 of $10 million. As the contract revenue is recognized over the twenty-year life of the contract, the deficiency in net assets will be reduced by $625,000 per year.

Net assets reported by the Lottery also include its investment in capital assets, net of accumulated depreciation. The Lottery had no debt related to capital assets at June 30, 2007.

(9) *Retirement Plan*

Plan Description:

All Lottery employees must participate in a cost-sharing multiple-employer defined benefit pension plan administered by the State of Rhode Island Employees' Retirement System (ERS). The plan provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. The level of benefits provided to state employees is established by Chapter 36-10 of the General Laws, which is subject to amendment by the General Assembly. The ERS issues a publicly available financial report that

(9) *Retirement Plan* – (Continued)

includes financial statements and required supplementary information for plans administered by the system. The report may be obtained by writing to the Employees' Retirement System, 40 Fountain Street, Providence, RI 02903.

Funding Policy:

The funding policy, as set forth in the General Laws, Section 36-10-2, provides for actuarially determined periodic contributions to the plan. Lottery employees are required to contribute 8.75% of their annual covered salary. The Lottery is required to contribute at an actuarially determined rate; the rate was 18.40% of annual covered payroll for the fiscal year ended June 30, 2007. The Lottery contributed $508,684, $408,133 and $291,216 for the fiscal years ended June 30, 2007, 2006 and 2005, respectively, equal to 100% of the required contributions for each year.

(10) *Post employment Benefits*

In accordance with the General Laws, post employment healthcare benefits are provided to all state employees who retire on or after July 1, 1989. The benefits in general cover medical and hospitalization costs for pre-Medicare eligible retirees and a Medicare supplement for Medicare eligible retirees. The retiree portion of the monthly premium varies with years of service and ranges from 50% for retirees with 10-15 years of service to 0% for retirees with 35 years of service. The Lottery contributed 3.63% of covered payroll, or $87,202, for the fiscal year ended June 30, 2007 to fund the current cost of these benefits. This benefit program is administered by the State, therefore all required disclosures are included in the State's CAFR.

(11) *Deferred Compensation*

Employees of the Lottery may participate in a deferred compensation plan offered by the State. Required disclosures are reported in the State's CAFR.

(12) *Commitments*

(a) Gaming Systems Provider – GTECH (a combined company with Lottomatica S.p.A.)

During May 2003, the Lottery entered into a 20-year master contract with its gaming systems provider granting them the right to be the exclusive provider of information technology hardware, software, and related services for all lottery games. This contract is effective from July 1, 2003 through June 30, 2023, and amends all previous agreements between the parties.

As consideration for this exclusive right, the gaming systems provider paid the Lottery $12.5 million. In the event that the contract term is not fulfilled, the Lottery will be obligated to refund a pro-rata share of this amount to the gaming systems provider. Additionally, GTECH was obligated to invest $100 million in connection with the

(12) *Commitments* – (Continued)

construction of a new corporate headquarters and expansion of its manufacturing operations in the State. The gaming system contractor is also required to employ no less than 1,000 full time active employees during the term of the agreement.

The contract mandates commission percentages as detailed in the following chart.

Commission Percentages	
On-Line and Instant Tickets	
Total Lottery Sales in the Year	Percent Thereof
$0 - $275 Million	5.00%
Over $275 Million - $400 Million	1.00%
Over $400 Million	5.00%
Video Lottery Central System	
Total Net Terminal Income for the Year	Percent Thereof
$0 - $500 Million	2.50%
Over $500 Million - $1 Billion	1.00%
Over $1 Billion	2.50%

The Lottery also leases to the vendor a portion of its headquarters to house the computer hardware and office space necessary for the operation of the Lottery's games. The term of the lease is five (5) years, commencing October 19th, 2002 and the square footage leased is 5,101 square feet. The annual lease amount for the first year was $79,065 and the four (4) remaining years will increase by four percent (4%) per annum, effective October 19. The tenant has three (3) renewal options; two (2) for additional five (5) year terms and one (1) for an additional four (4) year term. The base rate for the renewal options will be an increase of four percent (4%) per annum unless a mutually acceptable rate is negotiated.

(b) Video Lottery Facility Operator – UTGR, Inc. (Twin River)

On July 18, 2005, the Lottery entered into a five (5) year Master Video Lottery Terminal Contract with UTGR, Inc., the owners of Twin River, to operate one of the State's licensed video lottery facilities. The agreement entitles UTGR, Inc. to compensation ranging from 26% to 28.85% of video lottery net terminal income at the facility. At the time of the agreement, the Lottery authorized an additional 1,750 video lottery terminals to be installed at Twin River and UTGR, Inc. agreed to invest no less than $125 million in the construction and development of its gaming facility during the first three (3) years of the agreement.

UTGR, Inc. has the right and option to extend the term of the agreement for two (2)

(12) *Commitments* – (Continued)

successive five (5) year periods by giving notice to the Lottery at least ninety (90) days prior to the expiration of the agreement. The option can be exercised if UTGR, Inc. is not in default of any major term or condition of the agreement and the full-time employee requirement at Twin River has been met.

(c) Video Lottery Facility Operator – Newport Grand Jai Alai, LLC (Newport Grand)

On November 23, 2005, the Lottery entered into a five (5) year Master Video Lottery Terminal Contract with Newport Grand to continue to operate as one of the State's licensed video lottery facilities. The agreement entitles Newport Grand to 26% of video lottery net terminal income at the facility. At the time of the agreement, the Lottery authorized an additional 800 video lottery terminals to be installed at Newport Grand, which has agreed to invest no less than $20 million in the construction and development of its gaming facility during the first three (3) years of the agreement.

Newport Grand has the right and option to extend the term of the agreement for one (1) additional five (5) year period by giving notice to the Lottery at least ninety (90) days prior to the expiration of the agreement. The option can be exercised if Newport Grand is not in default of any major term or condition of the agreement and the full-time employee requirement at Newport Grand has been met.

(13) *Contingencies*

The Lottery's master contracts with its video lottery facility operators contain revenue protection provisions in the event that existing video lottery facility operators incur revenue losses caused by new gaming ventures within the State.

(14) *Risk Management*

The Lottery is exposed to various types of risk related to its operations. These risks can result in losses incurred from property damage or destruction, inability to operate gaming activities and worker compensation claims. The Lottery manages these risks through the purchase of commercial insurance. During fiscal year 2007, the Lottery has maintained its amount of purchased insurance coverage. Claims and settlements incurred for fiscal years 2007, 2006 and 2005 have not exceeded the Lottery's insurance coverage.

The Lottery participates in the health insurance program for all State employees.

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Supplementary Information

RHODE ISLAND LOTTERY

Sales, Commissions and Prize Awards Expense

Year Ended June 30, 2007

Schedule 1

	Sales	Commissions	Prize Awards Expense	Unclaimed Prize Recovery	Cost of Tickets	Cost of Sales	Gross Profit
Lottery games:							
On-line games							
Keno	$ 83,189,252	$ 10,779,875	$ 54,142,673	$ (360,592)	$ -	$ 64,561,956	$ 18,627,296
PowerBall®	47,082,311	6,101,046	23,545,356	(1,180,322)	-	28,466,080	18,616,231
Daily Numbers	27,835,994	3,607,059	12,942,562	(228,738)	-	16,320,883	11,515,111
Hot Trax®	48,097	6,233	33,544	(5,379)	-	34,398	13,699
Rhody Poker	1,003,564	130,044	674,554	-	-	804,598	198,966
Wild Money	5,708,730	739,751	3,154,439	(96,049)	-	3,798,141	1,910,589
	164,867,948	21,364,008	94,493,128	(1,871,080)	-	113,986,056	50,881,892
Instant tickets	79,980,026	8,469,884	53,119,346	(1,855,317)	1,454,429	61,188,342	18,791,684
Video Lottery	1,561,369,656	159,561,783	1,144,576,293	(252,780)	-	1,303,885,296	257,484,360
Totals	$ 1,806,217,630	$ 189,395,675	$ 1,292,188,767	$ (3,979,177)	$ 1,454,429	$ 1,479,059,694	$ 327,157,936

Video Commissions - Detail	
Facilities	$ 114,946,669
Technology Providers	28,546,798
Central Communications Provider	10,419,833
City/Town	5,065,255
Narragansett Indian Tribe	583,228
Total	$ 159,561,783

See independent auditor's report.

Statistical Section

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Rhode Island Lottery Statistics

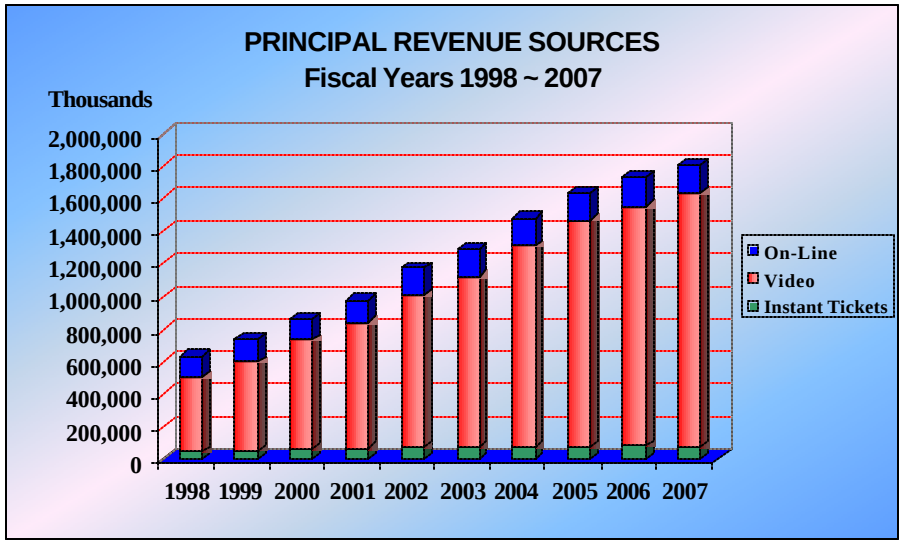
RHODE ISLAND LOTTERY

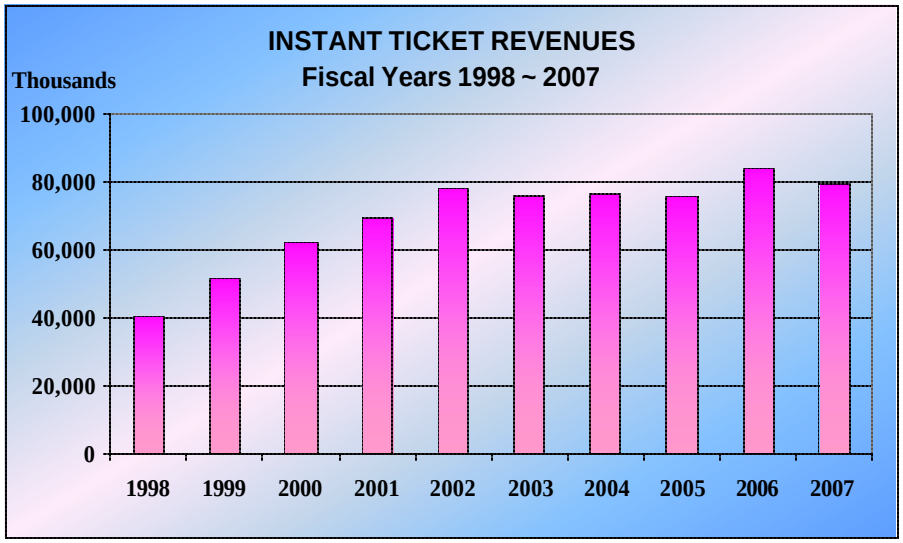
Principal Revenue Sources

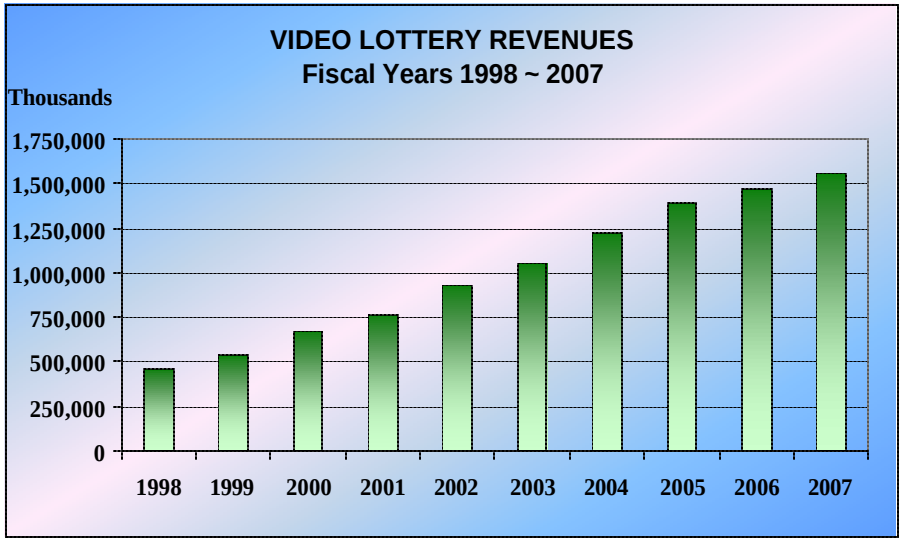
Fiscal Years 1998 through 2007

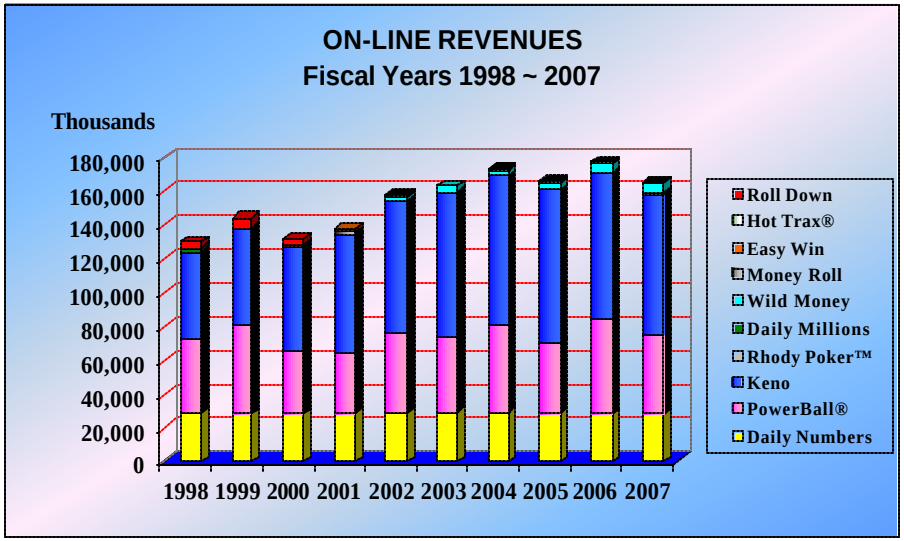
	Fiscal Year									
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Sales										
Instant tickets										
Instant tickets	$ 40,323,292	$ 51,372,959	$ 61,813,004	$ 69,394,994	$ 78,034,555	$ 75,789,417	$ 76,521,924	$ 75,598,569	$ 84,018,698	$ 79,980,026
Percentage of total sales and revenues	6.3%	6.9%	7.1%	7.1%	6.7%	5.9%	5.2%	4.6%	4.8%	4.4%
Video										
VLTs	464,068,675	545,474,154	670,764,767	771,019,263	935,208,511	1,051,411,493	1,231,226,093	1,394,753,542	1,470,193,375	1,561,369,656
Percentage of total sales and revenues	73.1%	73.5%	77.4%	78.7%	79.7%	81.4%	83.1%	85.1%	84.8%	86.3%
On-line										
Daily Numbers	29,257,141	28,221,328	28,159,762	28,459,883	28,994,464	29,649,149	29,681,795	28,584,281	27,838,055	27,835,994
PowerBall®	43,345,345	52,582,676	37,456,233	36,437,944	46,295,253	44,289,173	50,869,394	41,969,907	57,196,851	47,082,311
Keno	51,617,137	57,637,832	60,801,993	69,190,444	78,837,210	85,589,259	88,327,994	90,550,499	85,708,538	83,189,252
Daily Millions	2,162,126	-	-	-	-	-	-	-	-	-
Wild Money	-	-	-	-	2,207,213	3,677,479	3,762,342	3,742,142	5,415,054	5,708,730
Money Roll	-	-	-	1,971,470	1,282,450	-	-	-	-	-
Easy Win	-	-	1,802,708	1,545,704	-	-	-	-	-	-
Hot Trax®	-	-	-	-	-	-	235,570	1,439,442	944,912	48,097
Rhody Poker™	-	-	-	-	-	-	-	-	-	1,003,564
Roll Down	3,300,928	5,880,770	3,293,258	-	-	-	-	-	-	-
Total on-line	129,682,677	144,322,606	131,513,954	137,605,445	157,616,590	163,205,060	172,877,095	166,286,271	177,103,410	164,867,948
Percentage of total sales and revenues	20.4%	19.4%	15.2%	14.0%	13.4%	12.6%	11.7%	10.1%	10.2%	9.1%
Total sales	**634,074,644**	**741,169,719**	**864,091,725**	**978,019,702**	**1,170,859,656**	**1,290,405,970**	**1,480,625,112**	**1,636,638,382**	**1,731,315,483**	**1,806,217,630**
Nonoperating revenues										
Investment earnings	488,379	528,425	766,591	969,516	456,858	285,934	251,175	605,983	1,216,873	1,412,256
Net pull tab sales	196,280	214,300	229,991	211,876	238,905	194,302	220,180	201,848	161,363	155,177
Contract revenue	-	-	-	-	-	-	625,000	625,000	625,000	625,000
Miscellaneous	264,405	169,985	1,072,583	472,068	1,277,365	466,758	217,966	402,146	339,382	443,289
Total nonoperating revenues	**949,064**	**912,710**	**2,069,165**	**1,653,460**	**1,973,128**	**946,994**	**1,314,321**	**1,834,977**	**2,342,618**	**2,635,722**
Percentage of total sales and revenues	0.1%	0.1%	0.2%	0.2%	0.2%	0.1%	0.1%	0.1%	0.1%	0.1%
Total sales and revenues	**$635,023,708**	**$742,082,429**	**$866,160,890**	**$979,673,162**	**$1,172,832,784**	**$1,291,352,964**	**$1,481,939,433**	**$1,638,473,359**	**$1,733,658,101**	**$1,808,853,352**

Source: Rhode Island Lottery









Source: Rhode Island Lottery

RHODE ISLAND LOTTERY

Change in Net Assets

Fiscal Years 1998 through 2007

	Fiscal Year									
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Operating revenues										
Instant tickets	$ 40,323,292	$ 51,372,959	$ 61,813,004	$ 69,394,994	$ 78,034,555	$ 75,789,417	$ 76,521,924	$ 75,598,569	$ 84,018,698	$ 79,980,026
Video	464,068,675	545,474,154	670,764,767	771,019,263	935,208,511	1,051,411,493	1,231,226,093	1,394,753,542	1,470,193,375	1,561,369,656
On-line	129,682,677	144,322,606	131,513,954	137,605,445	157,616,590	163,205,060	172,877,095	166,286,271	177,103,410	164,867,948
Total operating revenues	634,074,644	741,169,719	864,091,725	978,019,702	1,170,859,656	1,290,405,970	1,480,625,112	1,636,638,382	1,731,315,483	1,806,217,630
Nonoperating revenues										
Interest income	488,379	528,425	766,591	969,516	456,858	285,934	251,175	605,983	1,216,873	1,412,256
Contract revenue	-	-	-	-	-	-	625,000	625,000	625,000	625,000
Other	460,685	384,285	1,302,574	683,944	1,516,270	661,060	438,146	603,994	500,745	598,466
Total nonoperating revenues	949,064	912,710	2,069,165	1,653,460	1,973,128	946,994	1,314,321	1,834,977	2,342,618	2,635,722
Total Revenues	**635,023,708**	**742,082,429**	**866,160,890**	**979,673,162**	**1,172,832,784**	**1,291,352,964**	**1,481,939,433**	**1,638,473,359**	**1,733,658,101**	**1,808,853,352**
Operating Expenses										
Prizes	$ 429,277,957	$ 503,522,789	$ 590,679,183	$666,947,849	$ 796,582,302	$ 880,866,451	$1,023,688,902	$1,142,353,743	$ 1,211,627,476	$1,292,188,767
Retailer/vendor commissions	18,442,716	21,219,277	20,392,735	21,584,246	25,760,434	25,572,841	30,544,726	29,684,102	31,987,214	29,833,892
Video commissions	67,859,963	80,153,944	100,930,356	107,436,913	132,116,020	145,408,704	141,385,014	153,449,964	160,092,955	159,561,783
Cost of tickets	1,102,638	985,173	990,209	1,112,469	1,300,380	1,149,999	997,689	1,034,313	1,475,528	1,454,429
Unclaimed prize recovery	(1,849,978)	(2,299,067)	(2,778,517)	(3,973,358)	(3,043,175)	(4,428,408)	(3,006,492)	(3,355,320)	(3,303,355)	(3,979,177)
Advertising and promotion	1,384,429	1,242,550	1,511,749	1,220,577	1,411,592	1,466,628	1,606,350	1,675,078	2,018,181	2,361,834
Personal services	2,687,572	2,792,014	3,016,103	3,146,406	3,331,963	3,559,981	3,740,101	3,963,421	4,232,168	4,450,807
Contract services	164,067	71,152	101,236	309,762	105,068	58,200	86,182	208,100	95,493	136,973
Equipment leasing	331,819	325,802	293,822	259,212	260,783	222,680	51,295	-	-	-
Depreciation	172,439	191,481	218,768	217,457	224,648	314,618	330,088	312,825	292,694	261,956
Other	450,359	474,162	593,506	739,627	713,088	656,268	748,934	972,485	615,256	967,257
Total operating expenses	520,023,981	608,679,277	715,949,150	799,001,160	958,763,103	1,054,847,962	1,200,172,789	1,330,298,711	1,409,133,610	1,487,238,521
Nonoperating expenses										
Payments to State's General Fund	115,071,622	133,475,047	150,283,635	180,743,897	214,141,576	249,040,055	281,141,644	307,549,648	323,899,491	320,989,831
Total Expenses	635,095,603	742,154,324	866,232,785	979,745,057	1,172,904,679	1,303,888,017	1,481,314,433	1,637,848,359	1,733,033,101	1,808,228,352
Increase (decrease) in Net Assets	$ (71,895)	$ (71,895)	$ (71,895)	$ (71,895)	$ (71,895)	$ (12,535,053)	$ 625,000	$ 625,000	$ 625,000	$ 625,000

The decrease in net assets for fiscal year 2003 is explained in Note 8 to Financial Statements.

Source: Rhode Island Lottery

RHODE ISLAND LOTTERY

Net Assets

June 30, 1998 through 2007

	Fiscal Year									
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Net Assets at Year-End										
Invested in capital assets	$ 618,690	$ 600,219	$ 618,752	$ 513,244	$ 1,281,124	$ 1,838,506	$ 1,707,113	$ 1,549,770	$ 1,314,290	$ 1,138,619
Unrestricted	(296,057)	(349,481)	(439,909)	(406,296)	(1,246,071)	(14,338,506)	(13,582,113)	(12,799,770)	(11,939,290)	(11,138,619)
Total Net Assets (Deficiency)	$ 322,633	$ 250,738	$ 178,843	$ 106,948	$ 35,053	$(12,500,000)	$(11,875,000)	$(11,250,000)	$(10,625,000)	$(10,000,000)

Note: Fiscal Year 2003 has been restated to conform with current year presentation.

Source: Rhode Island Lottery

RHODE ISLAND LOTTERY

Changes in Cash and Cash Equivalents

Fiscal Years 1998 through 2007

	Fiscal Year									
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Cash Flows from Operating Activities										
Cash received from lottery sales	$ 632,957,669	$ 737,396,996	$ 869,926,894	$ 976,709,169	$ 1,169,266,319	$ 1,291,972,781	$ 1,480,468,819	$ 1,634,938,802	$ 1,731,568,880	$ 1,805,273,680
Cash received from MUSL for grand prize winners	6,245,000	20,584,610	6,296,897	6,245,000	6,387,968	4,335,000	6,272,538	6,279,032	6,251,891	6,245,000
Cash received from sale of other tickets	286,767	297,594	315,625	211,876	238,905	194,303	220,179	294,516	238,707	228,582
Cash received from rental income and other receipts	262,565	168,435	676,849	682,946	1,363,913	709,312	228,469	410,740	258,364	219,906
Cash paid for prizes other than MUSL grand prize winners	(428,999,959)	(501,016,896)	(590,091,008)	(665,587,967)	(793,596,769)	(876,389,227)	(1,020,498,593)	(1,138,601,963)	(1,207,880,771)	(1,289,266,946)
Cash paid to MUSL grand prize winners	(6,245,000)	(20,584,610)	(6,296,897)	(6,245,000)	(6,387,968)	(4,335,000)	(6,272,538)	(6,279,032)	(6,251,891)	(6,245,000)
Cash paid for commissions - Retailers	(12,383,005)	(14,105,401)	(13,635,606)	(14,472,546)	(16,585,518)	(18,483,744)	(18,124,635)	(17,624,409)	(18,959,373)	(8,469,884)
Cash paid for commissions - video lottery	(65,646,618)	(80,609,682)	(99,171,862)	(108,676,974)	(130,758,688)	(141,353,902)	(143,889,867)	(153,345,011)	(159,580,145)	(157,009,564)
Cash paid for commissions - on-line games contractor	(6,023,266)	(6,944,908)	(6,872,420)	(7,035,140)	(7,989,218)	(7,473,926)	(12,858,316)	(12,017,289)	(12,028,077)	(21,551,637)
Cash paid to suppliers for goods and services	(4,053,131)	(2,962,769)	(3,788,918)	(3,568,487)	(3,368,424)	(3,977,096)	(3,846,370)	(3,544,227)	(3,964,374)	(5,057,261)
Cash paid to employees for services	(2,596,707)	(2,764,756)	(2,999,553)	(3,103,567)	(3,401,260)	(3,527,831)	(3,582,394)	(3,901,173)	(4,412,858)	(4,431,229)
Net cash provided (used) by operating activities	113,804,315	129,458,613	154,360,001	175,159,310	215,169,260	241,670,670	278,117,292	306,609,986	325,240,353	319,935,647
Cash Flows from Noncapital Financing Activities										
Payments to State's General Fund	(114,444,452)	(133,671,622)	(138,375,047)	(192,183,635)	(213,443,897)	(250,241,576)	(280,940,052)	(307,141,649)	(324,349,647)	(319,099,489)
Negative cash balance implicitly financed	-	-	-	432,782	(220,808)	(211,974)	-	23,964	(23,964)	-
Proceeds from sale of exclusive contract rights	-	-	-	-	-	12,500,000	-	-	-	-
Net cash provided (used) by noncapital financing activities	(114,444,452)	(133,671,622)	(138,375,047)	(191,750,853)	(213,664,705)	(237,953,550)	(280,940,052)	(307,117,685)	(324,373,611)	(319,099,489)
Cash Flows from Capital and Related Financing Activities										
Purchase of capital assets	(150,816)	(173,009)	(237,940)	(193,649)	(1,062,872)	(877,031)	(183,260)	(155,534)	(57,214)	(86,285)
Proceeds from sale of capital assets	12,500	-	-	-	-	-	-	-	-	-
Net cash provided (used) by capital and related financing activities	(138,316)	(173,009)	(237,940)	(193,649)	(1,062,872)	(877,031)	(183,260)	(155,534)	(57,214)	(86,285)
Cash Flows from investing Activities										
Proceeds from maturity of investments for jackpot awards	2,387,259	1,809,122	1,461,956	1,209,579	902,165	691,045	294,800	-	-	-
Interest income	488,379	528,425	766,591	969,516	456,858	285,934	251,175	605,983	1,216,872	1,412,256
Net cash provided (used) by investing activities	2,875,638	2,337,547	2,228,547	2,179,095	1,359,023	976,979	545,975	605,983	1,216,872	1,412,256
Net increase (decrease) in cash	2,097,185	(2,048,471)	17,975,561	(14,606,097)	1,800,706	3,817,068	(2,460,045)	(57,250)	2,026,400	2,162,129
Cash and cash equivalents, beginning of year	1,380,772	3,477,957	1,429,486	19,405,047	4,798,950	6,599,656	10,416,724	7,956,679	7,899,429	9,925,829
Cash and cash equivalents, end of year	$ 3,477,957	$ 1,429,486	$ 19,405,047	$ 4,798,950	$ 6,599,656	$ 10,416,724	$ 7,956,679	$ 7,899,429	$ 9,925,829	$ 12,087,958

Source: Rhode Island Lottery

Rhode Island Demographics

Rhode Island Demographics

	2000	2001	2002	2003	2004	2005	2006
Population by County				As of July 1			
Providence County	622,878	627,885	634,111	638,509	641,295	638,595	635,596
Kent County	167,529	168,955	169,962	171,270	171,534	171,097	170,053
Washington County	124,028	125,171	126,733	127,589	128,418	128,053	127,561
Newport County	85,662	85,452	85,630	85,395	84,812	83,233	82,144
Bristol County	50,739	51,047	52,132	52,020	52,871	52,601	52,256
Total Rhode Island Population	1,050,836	1,058,510	1,068,568	1,074,783	1,078,930	1,073,579	1,067,610
Percent Increase/(Decrease)		0.73%	0.95%	0.58%	0.39%	-0.50%	-0.56%
				Annual			
Total Personal Income	30,696,701	32,478,381	33,635,436	35,062,588	36,652,002	37,902,666	39,915,802
Per Capita Personal Income	29,212	30,683	31,477	32,631	33,996	35,324	37,388
Unemployment Rate	4.2%	4.5%	5.1%	5.4%	5.2%	5.1%	5.1%

Top 10 Rhode Island Employers

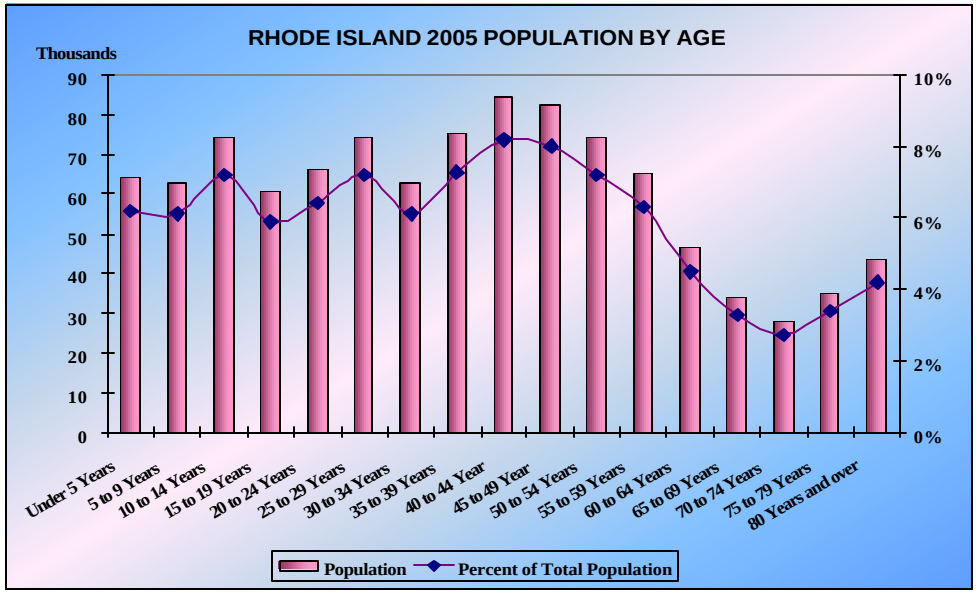
Employer	Total RI Based Employment
State of Rhode Island	11,907
Lifespan	10,935
US Government	9,982
Care New England	6,611
Roman Catholic Diocese of Providence	6,200
CVS Corp.	5,683
Citizens Financial Group	5,500
Stop & Shop Supermarket Co., Inc.	4,455
Brown University	3,943
Bank of America Corp.	3,000

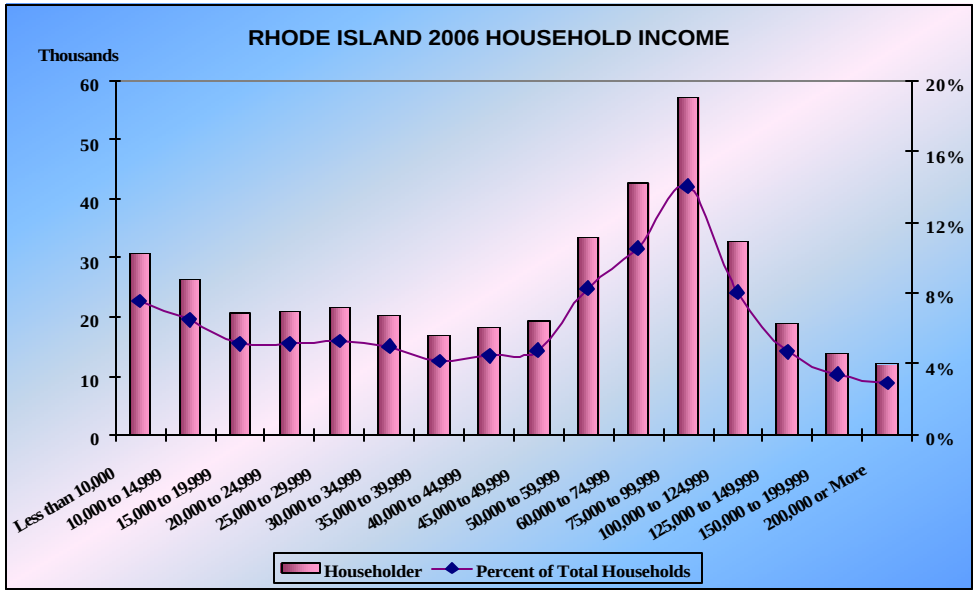
Source: U.S. Census Bureau and the Rhode Island Economic Development Corporation

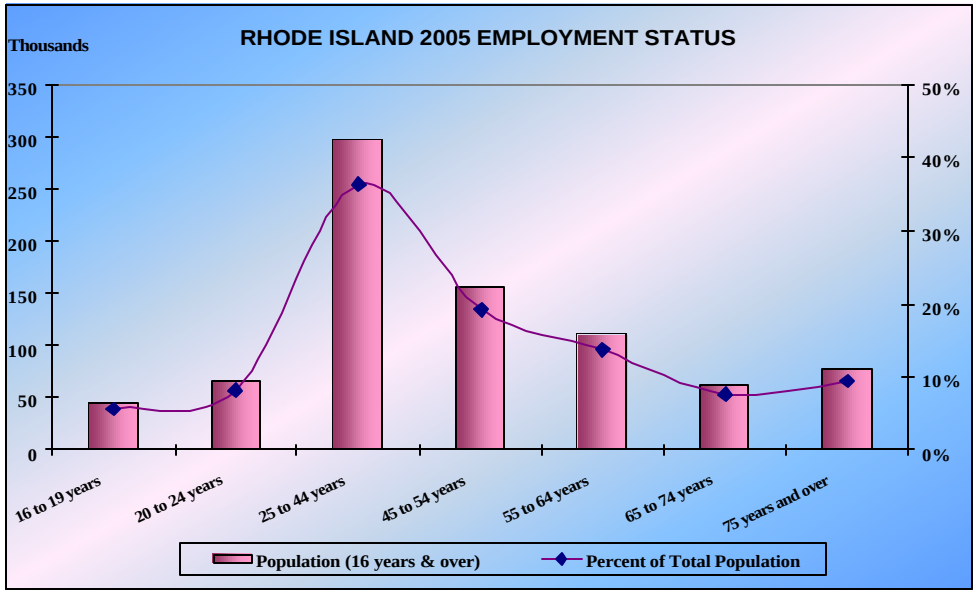
RI Lottery Government Employees by Function

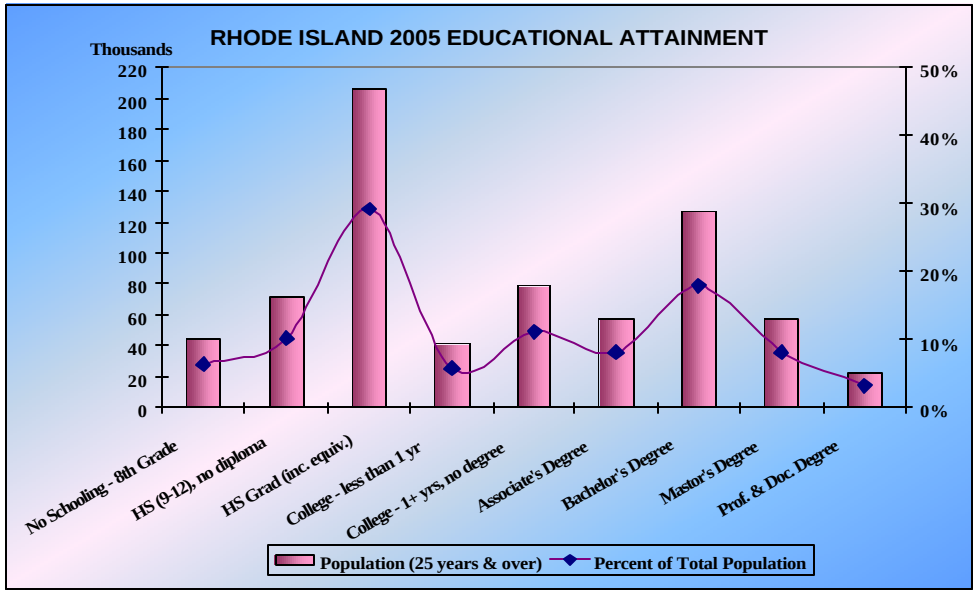
Categories	Total Employees
Officials/Managers/Administrators	6
Professionals	13
Technicians	5
Protective Services	2
Para Professionals	17
Administrative Support	12
Maintenance	2
Total	57

Source: Rhode Island Lottery









Source: U.S. Census Bureau

National Statistics

U.S. LOTTERIES RANKED BY FISCAL YEAR 2006 SALES

RANK	LOTTERY	FY '05 SALES ($M)	FY '06 SALES ($M)
1	New York * (1)	6,270.49	6,803.00
2	Massachusetts	4,484.72	4,534.12
3	Florida	3,537.00	4,030.00
4	Texas **	3,662.46	3,774.69
5	California	3,333.60	3,585.00
6	Georgia	2,922.33	3,177.59
7	Pennsylvania	2,644.86	3,070.00
8	New Jersey	2,273.81	2,406.57
9	Ohio	2,159.10	2,221.00
10	Michigan *** (3)	2,069.49	2,212.37
11	Illinois	1,806.75	1,964.83
12	***RHODE ISLAND (2)***	***1,636.84***	***1,731.47***
13	Maryland	1,485.73	1,560.91
14	West Virginia (1)	1,399.07	1,522.00
15	Virginia	1,333.94	1,365.00
16	South Carolina	956.95	1,144.60
17	Oregon (1)	943.11	1,104.00
18	Tennessee (5)	844.32	996.27
19	Connecticut	932.93	970.33
20	Missouri	785.59	913.52
21	Indiana	739.63	816.40
22	Kentucky	707.26	742.30
23	Delaware (1)	689.29	727.99
24	South Dakota (2)	675.58	686.16
25	Wisconsin	451.87	508.90
26	Washington	457.62	477.89
27	Colorado	416.97	468.80
28	Arizona	397.56	468.70
29	Minnesota	408.57	450.00
30	Iowa	210.67	339.52
31	Puerto Rico	317.90	334.50
32	Louisiana	307.01	332.12
33	District of Columbia *** (4)	233.43	266.20
34	New Hampshire	227.98	262.74
35	Kansas	206.72	236.05
36	Maine	209.29	229.69
37	North Carolina (8)		229.53
38	Oklahoma (7)		204.84
39	New Mexico	139.27	154.71
40	Idaho	113.50	131.13
41	Nebraska	100.66	113.11
42	Vermont	92.59	104.88
43	Montana	33.81	39.92
44	North Dakota (6)	19.15	22.33
	TOTAL	**52,639.42**	**57,435.68**

U.S. LOTTERIES RANKED BY SALES % CHANGE

RANK	LOTTERY	% CHANGE
1	Iowa	61.2%
2	South Carolina	19.6%
3	Montana	18.1%
4	Tennessee (5)	18.0%
5	Arizona	17.9%
6	Oregon (1)	17.1%
7	North Dakota (6)	16.6%
8	Missouri	16.3%
9	Pennsylvania	16.1%
10	Idaho	15.5%
11	New Hampshire	15.2%
12	Kansas	14.2%
13	District of Columbia *** (4)	14.0%
14	Florida	13.9%
15	Vermont	13.3%
16	Wisconsin	12.6%
17	Colorado	12.4%
18	Nebraska	12.4%
19	New Mexico	11.1%
20	Indiana	10.4%
21	Minnesota	10.1%
22	Maine	9.7%
23	West Virginia (1)	8.8%
24	Illinois	8.7%
25	Georgia	8.7%
26	New York * (1)	8.5%
27	Louisiana	8.2%
28	California	7.5%
29	Michigan *** (3)	6.9%
30	New Jersey	5.8%
31	***RHODE ISLAND (2)***	***5.8%***
32	Delaware (1)	5.6%
33	Puerto Rico	5.2%
34	Maryland	5.1%
35	Kentucky	5.0%
36	Washington	4.4%
37	Connecticut	4.0%
38	Texas **	3.1%
39	Ohio	2.9%
40	Virginia	2.3%
41	South Dakota (2)	1.6%
42	Massachusetts	1.1%
		9.11%

Results are unofficial and unaudited
* FY ends 3/31
** FY ends 8/31
*** FY ends 9/30
(1) Includes net VLT sales (cash in less cash out)
(2) Includes gross VLT sales (cash in)
(3) Sales estimated through September 30, 2004
(4) Sales/Profits reported for July 1, 2003 to June 30, 2004
(5) Sales began January 20, 2004 and only reflect 5 months and 12 days of fiscal year 2004
(6) Sales began March 25, 2004
(7) No sales for fiscal year 2005
(8) Instant sales began March 30, 2006, online sales began October 2006

Source: North American Association of State & Provincial Lotteries

U.S. LOTTERIES RANKED BY FISCAL YEAR 2006 PROFIT

RANK	LOTTERY	FY '05 PROFIT ($M)	FY '06 PROFIT ($M)
1	New York * (1)	2,062.70	2,203.00
2	California	1,795.30	1,240.57
3	Florida	1,103.63	1,230.00
4	Texas **	1,076.82	1,036.11
5	Pennsylvania	852.56	975.85
6	Massachusetts	936.13	951.24
7	New Jersey	804.42	849.25
8	Georgia	802.24	822.40
9	Michigan *** (3)	667.58	688.02
10	Ohio	645.10	646.30
11	Illinois	614.00	637.67
12	West Virginia (1)	563.32	610.00
13	Maryland	477.10	500.97
14	Oregon (1)	415.48	483.00
15	Virginia	423.52	454.90
16	***RHODE ISLAND (2)***	***307.55***	***323.90***
17	South Carolina	277.50	319.40
18	Connecticut	268.52	284.87
19	Tennessee (5)	227.42	277.66
20	Missouri	218.64	260.67
21	Delaware (1)	234.00	248.80
22	Indiana	189.04	218.00
23	Kentucky	158.19	204.30
24	Wisconsin	128.54	150.60
25	Arizona	116.80	141.12
26	Colorado	103.74	125.60
27	Minnesota	106.18	121.30
28	South Dakota (2)	119.32	118.99
29	Louisiana	108.92	118.76
30	Washington	115.60	116.95
31	Puerto Rico	79.00	115.90
32	Iowa	51.09	80.88
33	New Hampshire	69.30	80.32
34	District of Columbia *** (4)	71.05	73.40
35	Oklahoma (7)		68.95
36	Kansas	62.28	67.09
37	North Carolina (8)		64.59
38	Maine	50.33	51.70
39	New Mexico	32.23	36.86
40	Idaho	26.00	33.00
41	Nebraska	23.86	30.32
42	Vermont	20.35	22.88
43	Montana	6.22	9.11
44	North Dakota (6)	6.46	6.92
	TOTAL	**16,418.03**	**17,102.12**

U.S. LOTTERIES RANKED BY PROFIT % CHANGE

RANK	LOTTERY	% CHANGE
1	Iowa	58.3%
2	Puerto Rico	46.7%
3	Montana	46.5%
4	Kentucky	29.1%
5	Nebraska	27.1%
6	Idaho	26.9%
7	Tennessee (5)	22.1%
8	Colorado	21.1%
9	Arizona	20.8%
10	Missouri	19.2%
11	Wisconsin	17.2%
12	Oregon (1)	16.3%
13	New Hampshire	15.9%
14	Indiana	15.3%
15	South Carolina	15.1%
16	Pennsylvania	14.5%
17	New Mexico	14.4%
18	Minnesota	14.2%
19	Vermont	12.4%
20	Florida	11.5%
21	Louisiana	9.0%
22	West Virginia (1)	8.3%
23	Kansas	7.7%
24	Virginia	7.4%
25	North Dakota (6)	7.1%
26	New York * (1)	6.8%
27	Delaware (1)	6.3%
28	Connecticut	6.1%
29	New Jersey	5.6%
30	***RHODE ISLAND (2)***	***5.3%***
31	Maryland	5.0%
32	Illinois	3.9%
33	District of Columbia *** (4)	3.3%
34	Michigan *** (3)	3.1%
35	Maine	2.7%
36	Georgia	2.5%
37	Massachusetts	1.6%
38	Washington	1.2%
39	Ohio	0.2%
40	South Dakota (2)	-0.3%
41	Texas **	-3.8%
42	California	-30.9%
		4.17%

Results are unofficial and unaudited
* FY ends 3/31
** FY ends 8/31
*** FY ends 9/30
(1) Includes net VLT sales (cash in less cash out)
(2) Includes gross VLT sales (cash in)
(3) Sales estimated through September 30, 2004
(4) Sales/Profits reported for July 1, 2003 to June 30, 2004
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(8) Instant sales began March 30, 2006, online sales began October 2006

Source: North American Association of State & Provincial Lotteries