

ANNUAL REPORT

2018

2525 N. MONTANA AVE., HELENA, MT 59601
PHONE: 406.444.5825 MONTANALOTTERY.COM



**MONTANA
LOTTERY**

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The 2018 fiscal year was a time of growth and success for the Montana Lottery.

The beginning of the year was busy with wrapping up the tail end of our 30th year anniversary. We offered a Scratch ticket with a Jeep® Wrangler 4X4 as a top prize and special promotions offered to our valued Player's Club members. The Montana Lottery was proud to share our anniversary celebration with the players and retailers who make our success possible.

Always looking for ways to increase revenue, game enhancements were strategically implemented to our product mix. In the fall months, we introduced an old favorite to the Lotto product line, Lotto America™. This game was offered about 25 years ago in Montana, and was refreshed and brought back into play. Significant changes were also made to the multi-state Mega Millions® game. Specifically, the price point was raised to \$2, the starting jackpot was increased to \$40 million and better odds were established for the \$1 million prize.

Along with the changes mentioned above, and all the other strategic marketing efforts and technology enhancements, we grew our transfer to the State General Fund by more than \$1.4 million as compared to FY17. Our Scratch revenue grew by more than \$768,000 and our revenue from our Lotto games also grew by more than 8 percent.

None of this success would be possible without the support and dedication of our retailers. With our network of over 950 small businesses across Montana selling our products, we are able to sustain sales increases and learn more about what players are looking for from our products.

Players interacted with us through many of our communication channels, including social media and through our growing Player's Club. These channels grew ever-more important in establishing a relationship and connection with our players. During FY18, the importance of nurturing this relationship became a key focus of our communication efforts and was used to help increase revenue.

Winners are the best thing about the Montana Lottery and we had a lot of them in FY18. More notable winners would be Kenneth and Deborah Swingley, of Helena, who claimed the top vehicle prize in our Jeep® Scratch ticket. The Swingleys were wonderful winners – as were all of the Montanans who claim prizes – and as Jeep® fans, they thoroughly enjoyed the process of driving away in their dream vehicle.

Overall, we are proud of the year we had and the changes the year brought. We continue to work to meet the Lottery's mission while ensuring product integrity. We're looking forward to more fiscal years like 2018!

A handwritten signature in black ink that reads "Angela Wong".

Angela Wong, Director

MONTANA LOTTERY COMMISSION

The Montana Lottery Commission is comprised of Montanans appointed by the Governor to approve games and contracts, establish policy and oversee operations.

WILBUR REHMANN, *Chair, Helena*

THOMAS KEEGAN, *Helena*

LEO PRIGGE, *Butte*

JESSIKA KYNETT, *Livingston*

JEAN PRICE, *Great Falls*



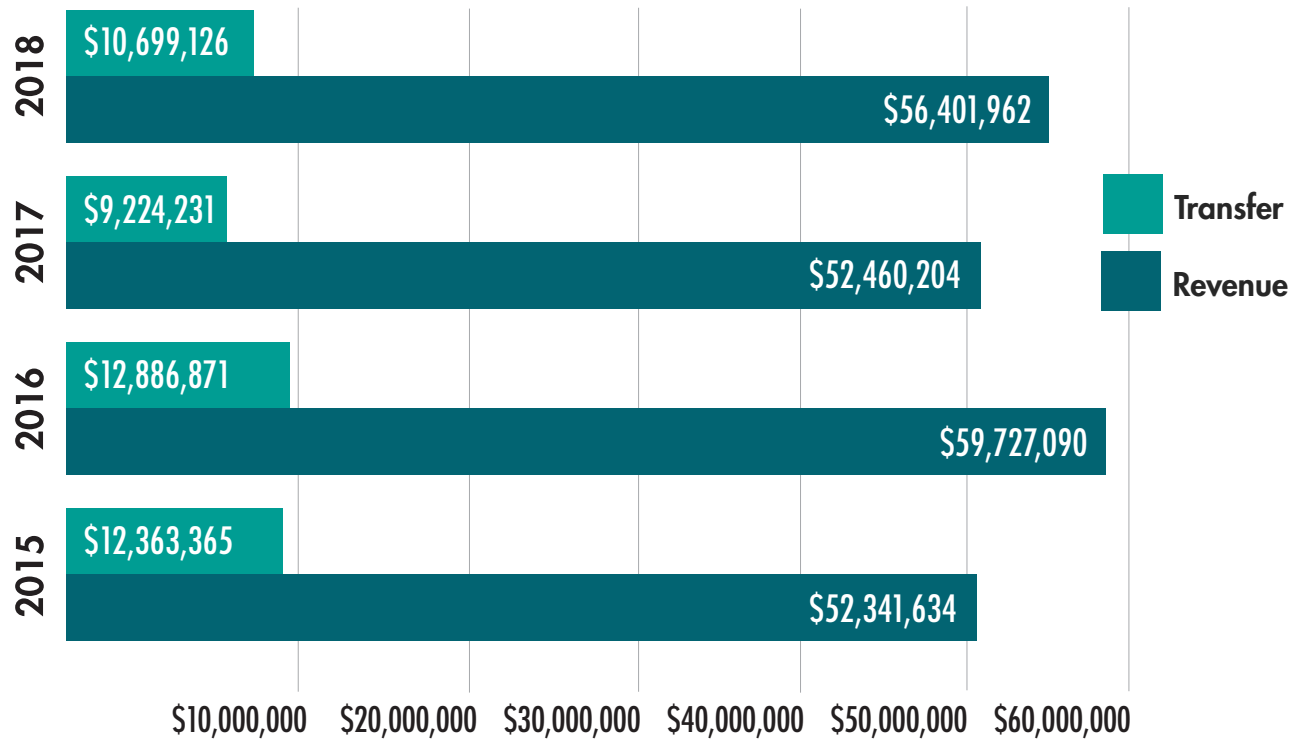
MONTANA**LOTTERY**

Contact the Montana Lottery Commission:

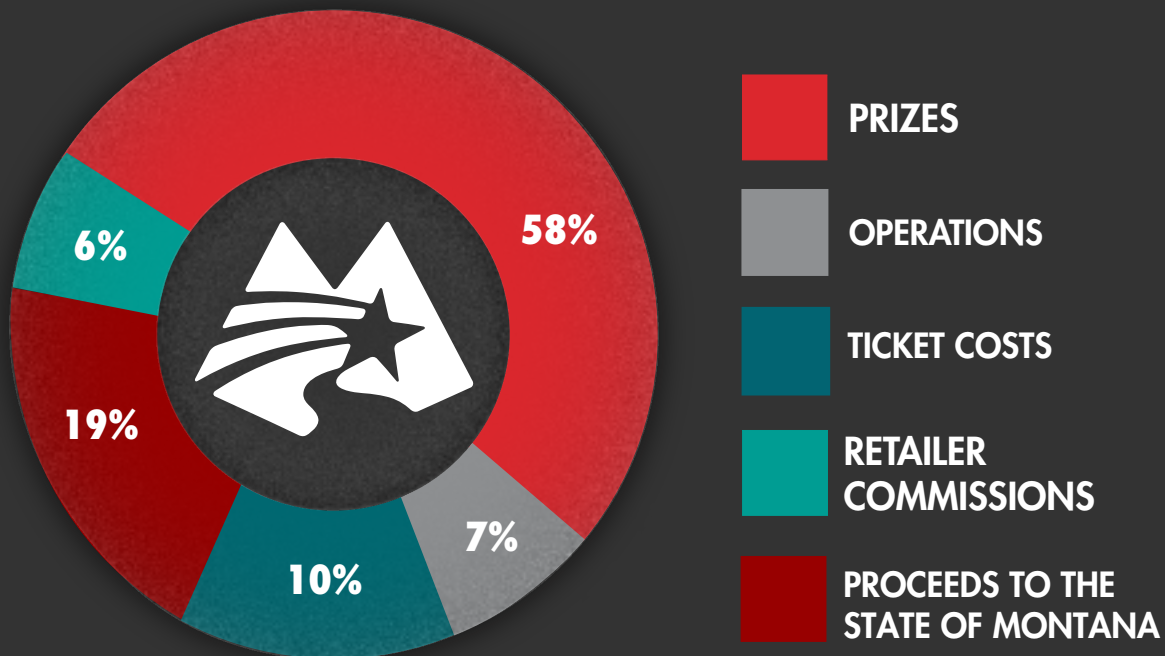
2525 North Montana Avenue | Helena, MT, 59601 | 406.444.5825

BENEFICIARY INFO

HISTORIC CHART ON REVENUES AND TRANSFERS



WHERE DOES THE **MONEY** GO?



FISCAL YEAR IN REVIEW

QUARTER 1: JULY 1, 2017 – SEPTEMBER 30, 2017

Big Winner: A Powerball ticket worth \$250,000 was sold at Albertsons #3004 in Helena.

Jeep® Scratch Ticket: In June of 2017, we launched our Jeep® Scratch ticket that offered an instant win of a Jeep® Wrangler Unlimited Sport 4X4 vehicle with all the taxes paid. Along with a \$75,000 top prize in the game, we also held three second chance drawings through our Player's Club. Jeep® Scratch ticket Bonus Play webcodes could be entered to win \$10,000 prizes drawn at the end of each month in June, July and August.

Events: The Montana Lottery was a proud sponsor and vendor at the Folk Fest in Butte on July 7-9, 2017, the Montana State Fair in Great Falls on July 28 through August 6, 2017 and Montana Fair in Billings on August 11-20, 2017.

Sponsorship: The Montana Lottery continued its proud sponsorship of the University of Montana and Montana State University athletics. The agreement included Lottery specific signage at each athletic facility during football and basketball games, in-game live messaging by announcers, along with advertising featured on game broadcasts.



QUARTER 2: OCTOBER 1, 2017 – DECEMBER 31, 2017

Big Winner: A Big Sky Bonus jackpot totaling \$34,476.00 was sold at 3 G's Convenience #3 in Billings on November 21, 2017.

Jeep® Awarded: On Nov. 8, 2017, our Jeep® Scratch ticket vehicle prize was claimed by Ken and Deborah Swingley of Helena. They selected their Jeep® Wrangler from Billion Motors in Bozeman. Also awarded in November was the \$75,000 top prize also offered in the Jeep® game.

Hot Lotto Ended: The Hot Lotto terminal game ended on October 28, 2017 in an effort to optimize the Lotto product line.

Mega Millions Enhanced: On October 28, 2017, the Mega Millions game changed from a \$1 base price, to a \$2 price point. Megaplier could still be added for an additional \$1. The enhancements included a revised prize structure, a larger starting jackpot of \$40 million and better odds of winning for the \$1 million prizes. The higher average jackpots help promote faster growth of the jackpot.

Lotto America Launched: Lotto America with the All-Star Bonus started selling on Sunday, November 12, 2017. This game provides players with exciting jackpots and base plays for only \$1. The All-Star Bonus provides players with an optional prize multiplier feature. Lotto America jackpots start at \$2 million and grow until won. Drawings are held every Wednesday and Saturday.

Eleventh Annual Montana Millionaire Game: The eleventh year for our Montana Millionaire raffle game began November 1, 2017. On the 45th day of sales, on December 15, we sold out of all 150,000 tickets in record time. The winning \$1 million ticket was sold at Town Pump of Butte #8 and claimed by Amy Lambert of Butte.

QUARTER 3: JANUARY 1, 2018 – MARCH 31, 2018

Big Wins:

- January 10, 2018 - Powerball \$250,000 win – sold at Town Pump of Miles City #8300
- February 3, 2018 – Record Montana Cash jackpot won \$440,000, sold at Town Pump of Helena #3
- February 7, 2018 – Record Big Sky Bonus jackpot hit for \$80,777 sold at The Betsy in Townsend

February Free Mobile App Launched. On February 12, 2018, we launched our free mobile app for both iPhone and Android.

March Problem Gambling Awareness Month: As we have for many years, the Montana Lottery devoted our resources to Problem Gambling Awareness month throughout March of 2018. The Montana Lottery routinely partners with the Montana Council on Problem Gambling. This year, we devoted our advertising screens to messages that drove awareness of the council and the work they do as a resource to Montanans with concerns about problem gambling. In addition, the Montana Lottery began the process of completing the three verification levels necessary to achieve national best practices verification coordinated by the North American Association of State and Provincial Lotteries (NASPL) and the National Council on Problem Gambling.

Lucky Every Day Cash Giveaway: Every day between March 5 and March 16, we conducted special Player's Club drawings exclusively for Lucky for Life players. We gave away \$1,000 every weekday to one lucky player. On March 16, we conducted a draw for two additional \$5,000 prizes and one \$10,000 grand prize!



QUARTER 4: APRIL 1, 2018 – JUNE 30, 2018

Big Winner:

- June 16, 2018 - \$50,000 Powerball prize sold at Bitterroot Quick Stop in Marion

Lotto America Cash Blast Promotion: To spotlight our newest game – Lotto America – we conducted special giveaways from April 30 through May 17 only for Lotto America players. On May 4, 2018, we held a drawing for 10 prizes of \$500 each. On May 18, we held a drawing for 30 prizes of \$1,000 each. All told, we gave away 40 prizes, only to Montana Lotto America players.



Multiplier Family of Games & Promotion: Our big summer Scratch game and promotion launched on June 6, 2018, marking the first time the Montana Lottery has ever launched a related, branded game at nearly every price point. Our Multiplier Family of games featured \$1, \$2, \$5, and \$10 games, each with the opportunity of multiplying top prizes. We also conducted BIG second chance drawings only for Multiplier players. We conducted a \$10,000 drawing on July 27, a \$20,000 drawing on August 31 and a \$30,000 drawing on September 28.

Retailers of the Year: Each year we recognize Montana Lottery retailers who have gone the extra mile. Our fiscal year 2018 Retailers of the Year were:

- Montana Sports Action Retailer of the Year: The Dead Horse Saloon in Scobey
- The Bob Harper Memorial Excellence Award: Super 1 Foods in Stevensville
- Wyman Hewitt Retailer of the Year Award: Town Pump #128441 in Kalispell

PRODUCTS IN REVIEW



During the 2018 fiscal year, the Montana Lottery launched 46 Scratch games. Our price points included \$1, \$2, \$3, \$5, \$10 and \$20 games, with top prizes ranging from \$1,000 to \$500,000. Within each price point there were a variety of play styles including crossword, bingo, key number and key symbol match, Slingo® and licensed property games.

SCRATCH REVENUE

\$17,097,062 **\$17,865,674**
FY 2017 **FY 2018**

The \$1,000,000 Cash Blowout ticket continued to be one of our top performing games, activating on average over 100 packs per week. This unique \$10 game features only \$50 and \$100 prizes.

We also launched our multiprice point family of games summer promotion called The Multiplier Family. This game included four price points: \$1-5X, \$2-10X, \$5-20X and \$10-50X. All games performed very well, activating an average of 84 packs per week with the \$10-50X game activating at 119 packs per week.

Moving forward, we will refine our games further based on player data analytics and a strong vendor partnership. Licensed property games continue to be top performers along with unique play styles.

Sales for FY2018 were \$17,865,674. Sales were up by 4 percent compared to FY2017.



New Scratch Games: During the second quarter of FY17 two unique Scratch playstyle games were launched. The first one, Loteria features a unique bingo-like playstyle wherein a player matches Hispanic symbols in a bingo card pattern to form wins. The second game, Fishing For Cash was designed exclusively inhouse and is a \$3 game that had two side-by-side games, each with their own theme of fishing in winter and summer.

PRODUCTS IN REVIEW: LOTTO



The Montana Lottery finished the 2018 fiscal year with six Lotto games: Powerball, Mega Millions, Lotto America, Lucky For Life, Montana Cash and Big Sky Bonus. Four of those products are multi-state games, while Montana Cash and Big Sky Bonus are Montana-made and played exclusively in Montana. Our in-state only games are among our most popular games and offer the best overall odds. We had 944 licensed retailers in the 2018 fiscal year. Lotto retailers receive a 5 percent commission for selling tickets. Lotto revenue was \$31.59 million in the 2018 fiscal year, up 15.23 percent from the year before. This year also saw the introduction of our newest multi-state jackpot Lotto game, Lotto America. Lotto America with All-Star Bonus is a pick (5 +1) game and costs \$3. Mega Millions increased in price from \$1 to \$2 in October 2017. Lotto games paid out 3,248 prizes greater than \$100 which is \$4,920,959 in total.

TREASURE PLAY AND MONTANA SPORTS ACTION



Treasure Play: The Montana Lottery offers a selection of instant-win, terminal-issued games called Treasure Play at 343 licensed retailers. In the 2018 fiscal year, Treasure Play retailers received a 5 percent commission for selling Treasure Play tickets. During this timeframe, Treasure Play consisted of six non-progressive games and six progressive jackpot games. Progressive jackpot games are generally more popular than non-progressive games primarily because play increases as jackpots increase. Fiscal year 2018 annual revenue for our Treasure Play line of games has seen a decrease from the year prior. Treasure Play revenue was \$3,900,000, down 20.4 percent from the previous year. Treasure Play games paid out 1,180 prizes greater than \$100, totalling \$605,884. Treasure Play's revenue decline is related to a long-term pause in new game development. The pause in new game development was necessary to update and overhaul the terminal interface. The new terminal updates improve accessibility to Treasure Play games, improve winner awareness and new buttons for sample ticket images and prize legends.

Montana Sports Action (MSA) is a fantasy sports product line offered by the Montana Board of Horse Racing and facilitated by the Montana Lottery. MSA consists of two fantasy sports games: Fantasy Racing and Fantasy Football. MSA revenue for the Montana Lottery was \$7,846 down 3.42 percent from fiscal year 2017. In fiscal year 2018 Lotto games paid out 165 prizes greater than \$100, totalling \$154,269.

WINNERS SPOTLIGHT

Montana Millionaire winner is Amy Lambert, of Butte, claimed in January 2018

Amy Lambert, of Butte, became our eleventh Montana Millionaire in January of 2018. She bought a single Montana Millionaire ticket that year at the Town Pump on the corner of Harrison Avenue and Dewey Boulevard in Butte.

"I thought, 'I'm here. I'm just going to buy a ticket,'" Lambert said.

She could not believe it when she checked her tickets the day after the big drawing.

"I was shocked," Lambert said. "I kept thinking, 'Are these really the numbers?'"

Lambert plays Montana Millionaire every year.

"But I didn't play and expect to win."



New Dad wins \$15,000 December 2018

Jason Curtis, of Missoula, claimed his \$15,000 Montana Millionaire Early Bird prize Friday. The second, and final Early Bird drawing was held on December 15, 2017. Curtis purchased the lucky ticket at Hellgate Trading Post on Mullan Road in Missoula.

"I checked my ticket on the website and couldn't sleep at all that night," Curtis said.

He was in complete shock when he realized his number was the lucky winner. The big win comes at the perfect time for his family. Curtis recently welcomed his second child and plans to use the money to help pay off medical bills.

Swingleys Claim Jeep® in October 2017

Kenneth and Deborah Swingley claimed the Jeep® vehicle top prize in the Montana Lottery's Jeep® Brand Scratch ticket.

The Helena couple bought the winning ticket at the Cenex Zip Trip #42. Kenneth Swingley is an avid Jeep® fan and had all the specifications for his prize picked out when the couple came to the Montana Lottery headquarters to claim the prize. The couple ordered the exact model they wanted from Billion Dodge Chrysler Jeep® in Bozeman and picked up the prize a few weeks after claiming it.



Maureen Pettis wins \$25,000 a year for life.



Maureen Pettis of Great Falls claimed a \$25,000 year for life Lucky for Life prize in September of 2017. Pettis bought her winning ticket at the Emerald City Casino at 2517 10th Ave. N. in Great Falls.

The winning numbers are a set of numbers Pettis played repeatedly: The number of children she and her husband have all together, her husband's lucky baseball number and the number of years she's been buying Lucky for Life tickets from the Montana Lottery.

It was, truly, a winning combination!

Winners Happen!

Joseph Thompson of Salt Lake City thought he won \$30. It was really \$250,000.

Joseph Thompson bought some Powerball tickets on his way out of Helena in the late summer of 2017. He checked the numbers online a few weeks later and thought he'd won maybe \$30.

Thompson, who lives in Utah, but was in Montana for a charity dinner theater event, was shocked to learn one of those tickets actually won him \$250,000.

"I was shocked when they told me," he said.

Thompson drove back to Helena to claim his prize.



THE MONTANA LOTTERY MOBILE APP

Fun at Your Fingertips!



In February of 2018, the Montana Lottery launched its first mobile app. The free download was designed entirely in Montana by the staff of the Montana Lottery.

The app put everything our players want most in one spot: They can scan and check their tickets to see if they won! They can create electronic play slips for purchasing tickets at any of our more than 950 retailers. They can check jackpots for all our Lotto and Treasure Play games.

The app also represented a major step forward for members of our Player's Club. For the first time, players no longer needed to manually type in their Bonus Play webcodes, allowing the entire Player's Club to be experienced better and faster on a mobile device.

The app launched more than halfway through the 2018 fiscal year. In less than five months, we saw more than 5,100 downloads of the app. That's an average of 37 downloads of our app every day!





MEMBERS ONLY!

Players Club grew by 9.4 percent

The Montana Lottery began the 2018 fiscal year with 159,305 members in our exclusive Player's Club. The club grew by 15,078 new members that year, for a total of 174,383.

NEW RETAILERS IN FISCAL YEAR 2018

TRADITIONAL: 20 MSA: 44

What's the difference?

Our traditional retailers sell all our Lotto and Scratch games. They may sell from our Photon terminal or they may have a full-service vending machine. Or both. Traditional retailers are typically grocery stores, convenient stores or gas stations.

Our MSA retailers sell from a different terminal, one that offers all our Lotto games, Montana Sports Action games AND our entire suite of instant-win Treasure Play games. These retailers are taverns and casinos. They may or may not also sell Montana Lottery Scratch.

LEGISLATIVE AUDIT DIVISION

Angus Maciver, Legislative Auditor
Deborah F. Butler, Legal Counsel



Deputy Legislative Auditors:
Cindy Jorgenson
Joe Murray

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

Introduction

We have audited the accompanying Statement of Net Position of the Montana State Lottery as of June 30, 2018, and 2017, the related Statement of Revenues, Expenses and Changes in Net Position, and the Statement of Cash Flows for each of the fiscal years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our 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 from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Montana State Lottery as of June 30, 2018, and 2017, and the changes in net position and cash flows for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

Emphasis of Matters

As discussed in Note 1 to the financial statements, the financial statements present only the enterprise fund of the Montana State Lottery and do not purport to, and do not, present fairly the financial position of the State of Montana, as of June 30, 2018, and 2017, the changes in its financial position, or its cash flows for each of the two fiscal years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

As discussed in Note 2 to the financial statements, Montana State Lottery adopted the Governmental Accounting Standards Board (GASB) Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* in fiscal year 2018. Our opinion is not modified with respect to this matter.

Other Matters

Our audit was conducted for the purpose of forming an opinion on the enterprise fund financial statements of the Montana State Lottery. The information on pages 1 through 12 of the report is presented for purposes of additional analysis and is not a required part of the enterprise fund financial statements of the Montana State Lottery. Such information has not been subjected to the auditing procedures applied in the audit of the enterprise fund financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated February 1, 2019, on our consideration of the Montana State Lottery's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering

the Montana State Lottery's internal control over financial reporting and compliance. It is included in the Legislative Auditor's separately issued report (17-30B) on the Montana State Lottery's financial statements.

Respectfully submitted,

/s/ Cindy Jorgenson

Cindy Jorgenson, CPA
Deputy Legislative Auditor
Helena, MT

February 1, 2019

<p align="center">MONTANA LOTTERY STATEMENT OF NET POSITION JUNE 30, 2018 AND 2017</p>

	2018	2017
ASSETS		
CURRENT ASSETS		
Cash and Cash Equivalents	\$ 2,609,121	\$ 1,973,494
Receivables (Net)	1,796,488	1,750,221
Multi-State Reserve Fund	65,000	65,000
Inventories	475,657	512,292
Prepaid Expenses	<u>34,713</u>	<u>38,455</u>
TOTAL CURRENT ASSETS	4,980,979	4,339,462
NONCURRENT ASSETS		
Computer, Furniture & Equipment	582,010	570,815
Leasehold Improvements	98,793	98,793
Accumulated Depreciation	(446,626)	(402,645)
Multi-State Reserve Fund	<u>821,138</u>	<u>1,028,333</u>
TOTAL NONCURRENT ASSETS	1,055,315	1,295,296
DEFERRED OUTFLOW OF RESOURCES		
Pension Deferred Outflows	484,499	320,057
OPEB Deferred Outflows	<u>2,399</u>	<u>0</u>
TOTAL DEFERRED OUTFLOWS OF RESOURCES	486,898	320,057
COMBINED ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	\$ <u>6,523,192</u>	\$ <u>5,954,815</u>
LIABILITIES		
CURRENT LIABILITIES		
Accounts Payable	\$ 759,486	\$ 285,856
Estimated Prize Liability	3,046,706	2,618,688
Transfer Obligations	1,153,531	1,480,492
Unearned Revenue	114,985	95,986
Accrued Compensated Absences	<u>158,852</u>	<u>201,653</u>
TOTAL CURRENT LIABILITIES	5,233,560	4,682,675
NONCURRENT LIABILITIES		
Multi-State Prize Liability	754,449	952,083
Accrued Compensated Absences	48,284	0
Net Pension Liability	2,201,008	1,967,263
Other Post Employment Benefits	<u>122,589</u>	<u>731,049</u>
TOTAL NONCURRENT LIABILITIES	3,126,330	3,650,395
DEFERRED INFLOWS OF RESOURCES		
Pension Deferred Inflows	29,163	11,855
OPEB Deferred Inflows	<u>11,663</u>	<u>0</u>
TOTAL DEFERRED INFLOWS OF RESOURCES	40,826	11,855
COMBINED LIABILITIES AND DEFERRED INFLOW OF RESOURCES	8,400,716	8,344,925
NET POSITION		
Net Investment in Capital Assets	234,177	266,963
Unrestricted	<u>(2,111,701)</u>	<u>(2,657,073)</u>
TOTAL NET POSITION	\$ <u>(1,877,524)</u>	\$ <u>(2,390,110)</u>

The accompanying notes are an integral part of these financial statements.

<p style="text-align: center;">MONTANA LOTTERY STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION FOR THE YEARS ENDED JUNE 30, 2018 AND 2017</p>
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	2018	2017
OPERATING REVENUES:		
Scratch Ticket Revenue	\$ 17,865,674	\$ 17,097,062
On Line Ticket Revenue	38,515,814	35,344,867
License, Permits, and Misc	20,474	18,275
Total Operating Revenues	56,401,962	52,460,204
DIRECT GAME COSTS:		
Scratch Ticket Prize Expense	11,268,840	10,497,914
On Line Ticket Prize Expense	21,282,363	20,096,926
Retailer Commissions	3,269,397	2,981,078
Cost of Tickets Sold	932,282	1,018,794
Vendor fees	4,840,700	4,353,879
Total Direct Game Costs	41,593,582	38,948,591
Income Before Operating Expenses	14,808,380	13,511,613
OPERATING EXPENSES:		
Advertising	588,502	598,988
Advertising Production	211,098	239,952
Audit Fees	76,262	26,409
Bad Debts Expense	(5,248)	123
Communications	149,765	147,116
Contractual Services	130,827	243,695
Depreciation and Amortization	50,497	46,798
Administrative Service Fee	80,432	73,734
Multi-State Dues	11,277	29,417
Public Relations	71,250	66,703
Other Post Employment Benefits	9,070	88,983
Other Expenses	30,876	36,690
Pension Expense	282,156	179,560
Personal Services	2,111,822	2,113,436
Repairs and Maintenance	21,177	30,290
Supplies and Materials	219,183	244,358
Travel	35,210	42,722
Utilities and Rent	241,765	217,519
Total Operating Expense	4,315,921	4,426,493
Operating Income	10,492,459	9,085,120
NONOPERATING REVENUES (EXPENSES):		
Interest Earnings	23,062	12,542
Security Lending Income	0	35
Security Lending Expense	0	(16)
Non Employer Pension Revenue	31,486	34,467
Gain/Loss on Sale of Assets	13,234	(1,711)
Total Nonoperating Revenues(Expenses)	67,782	45,317
Income Before Operating Transfers	10,560,241	9,130,437
Operating Transfers Out - General Fund	(10,699,126)	(9,224,231)
Operating Transfers Out - Other Agencies	0	0
CHANGE IN NET POSITION	(138,885)	(93,794)
Total Net Position, Beginning of Period	(2,390,110)	(2,239,546)
Prior Period Adjustment (Note 2)	651,471	(56,770)
TOTAL NET POSITION, END OF PERIOD	\$ (1,877,524)	\$ (2,390,110)

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED JUNE 30, 2018 AND 2017
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	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts for Sales & Services	\$ 56,379,942	\$ 52,841,748
Payments for Goods & Services	(10,395,996)	(10,980,398)
Payments to Employees	(2,227,193)	(2,288,174)
Payments for Prizes	(32,320,819)	(30,563,289)
Net Cash Provided by Operating Activities	<u>11,435,934</u>	<u>9,009,887</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Transfer to Other Funds	(11,026,087)	(9,271,335)
Net Cash Used For Noncapital Financing	<u>(11,026,087)</u>	<u>(9,271,335)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition of Fixed Assets	(18,054)	(198,386)
Proceeds from Sale of Fixed Assets	13,577	18,931
Net Cash Used For Capital Financing	<u>(4,477)</u>	<u>(179,455)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest and Dividends on Investments	23,062	12,561
Received from (Paid to) MUSL Prize Reserve Fund	207,195	93,302
Net Cash Provided by Investing Activities	<u>230,257</u>	<u>105,863</u>
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS	635,627	(335,040)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>1,973,494</u>	<u>2,308,534</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 2,609,121</u>	<u>\$ 1,973,494</u>
Reconciliation of Operating Income to Net Cash Provided by Operating Activities		
Operating Income	\$ 10,492,459	\$ 9,085,120
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities		
Depreciation	50,497	46,798
Change in Assets and Liabilities:		
Decr (Incr) in Account Receivable	(46,267)	389,978
Decr (Incr) in Inventories	36,635	(76,956)
Decr (Incr) in Collateral securities on loan	0	6,020
Decr (Incr) in Prepaid expenses	3,742	(2,060)
Incr (Decr) in Accounts Payable	473,630	(550,038)
Incr (Decr) in Lottery Prizes Payable	230,384	31,551
Incr (Decr) in Liability for securities on loan	0	(6,020)
Incr (Decr) in Unearned Income	18,999	(8,311)
Incr (Decr) in Other Post Employment Benefits	10,635	67,091
Incr (Decr) in Pension Liability	159,737	61,170
Incr (Decr) in Compensated Absences Payable	5,483	(34,456)
Total Adjustments	<u>943,475</u>	<u>(75,233)</u>
Net Cash Provided by Operating Activities	<u>\$ 11,435,934</u>	<u>\$ 9,009,887</u>

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
Notes to the Financial Statements
June 30, 2018 and 2017

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity.

The Montana Lottery, established under the provisions of Section 23-7-101, Montana Code Annotated (MCA), was approved by the Montana electorate through Legislative Referendum No. 100 on November 4, 1986.

Montana's first lottery tickets went on sale June 24, 1987.

The Montana Lottery is operated by a five-member commission consisting of Montana residents appointed by the Governor. The Commission, by law, has the power to operate a state lottery, determine the types and forms of lottery games, set the ticket price, number and size of prizes, conduct lottery drawings, enter into agreements to offer lottery games in conjunction with other lottery states and countries, and prepare financial reports. The Montana Lottery is attached to the Montana Department of Administration for administrative purposes.

The Montana Lottery is included as an enterprise fund in the State of Montana's Comprehensive Annual Financial Report. In accordance with governmental accounting and financial reporting standards, there are no component units to be included within the Montana Lottery's financial statements as a reporting entity.

Basis of Presentation. The Montana Lottery reports its financial activity in accordance with generally accepted accounting principles (GAAP) as prescribed in pronouncements of the Governmental Accounting Standards Board (GASB).

Enterprise Fund. The Montana Lottery is classified as an Enterprise Fund of the Proprietary Fund Type. Enterprise Funds account for operations: a) financed and operated similar to private business enterprises, where the intent of the Legislature is that costs are to be financed or recovered primarily through user charges, or b) where the Legislature has decided that periodic determination of revenue earned, expenses incurred, or net income is appropriate.

Basis of Accounting. The Montana Lottery's financial statements are prepared using the accrual basis of accounting. Revenues are recognized in the accounting period in which they are earned and become measurable; expenses are recognized in the period incurred, if measurable.

Property and equipment. Property and equipment are recorded at cost. Donated property and equipment are recorded at their estimated fair market value at the date of donation. Ordinary maintenance and repairs are charged to operations as incurred; major renewals and betterments are capitalized. Upon disposition or retirement of property and equipment, the cost and related accumulated depreciation or amortization are removed from the accounts. Gain or loss on disposal is reflected in non-operating revenues and expenses. Depreciation and amortization are calculated on a straight-line basis over estimated useful lives of three to ten years. The Lottery conforms to the State of Montana capitalization threshold for capitalizing property and equipment as well as buildings and building/land improvements. The threshold for capitalizing property and equipment is \$5,000 and the threshold for capitalizing buildings/land improvements is \$25,000.

Revenue Recognition. Lottery scratch ticket sales are recorded as revenue based on the time the retailer activates the pack of tickets for sale. In accordance with an established policy, retailers may return unsold tickets to the Lottery for credit. Sales are decreased by an allowance for estimated ticket returns.

Ticket sales for lotto games Powerball, Montana Cash, Hot Lotto, Montana Millionaire, Mega Millions, Lucky for Life, Big Sky Bonus, and Lotto America are recorded as revenue based on drawings. Tickets sold in advance for future drawings are recorded as unearned income until such time as the tickets become valid for the most current drawing.

Treasure Play revenue is recorded on a daily basis as games are played. Treasure Play games are instant chances for wins, so when these games are played the revenue from these games are earned as played.

Ticket sales for Fantasy Sports games are based upon MCA 23-4-302 and an interagency agreement between the Lottery and the Board of Horse Racing. The Lottery is only a facilitator of these games and charges an administrative fee for this service. The actual sales of these games are not reflected on the Lottery's financial statements as they are not income to the Lottery.

Classification of Revenues. The Lottery has classified its revenues as either operating or non-operating according to the following criteria:

Operating revenues – include activities that have characteristics of exchange transactions, including (1) ticket sales, net of returns, and (2) retailer license fees and administrative fees in relation to selling lottery tickets.

Non-Operating revenues – include activities that have the characteristics of non-exchange transactions, such as gifts and other revenue sources that are defined as non-operating revenues by GASB No. 9, “Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting,” and GASB No. 34, “Basic Financial Statements and Management Discussion and Analysis for State and Local Governments.” Types of revenue sources that fall into this classification are investment income, and gain or loss on disposition of assets.

Free Tickets. Some Montana Lottery scratch games award free tickets as prizes. Net lottery ticket revenue does not include the value of free tickets given away and free plays won. The face value of these free ticket prizes distributed for the year ended June 30, 2018, and 2017 was \$589,834, and \$624,380, respectively.

Promotional Credits. The Lottery issues promotional credits to retailers to be used to distribute free tickets to players. The tickets are distributed as part of a promotion run by the retailer, e.g., “Ask for the Sale” or second chance drawings. The Lottery also directly distributes scratch tickets for promotional purposes at trade shows, for media give-aways, and during new game introductions. The tickets distributed as a result of promotional credits are reflected as a reduction in revenue. The related prize expense and ticket cost for all promotions are reclassified as an advertising expense. For the year ended June 30, 2018, promotional credits resulted in a revenue reduction of approximately \$21,186 and an expense reclassification of approximately \$15,772. For the year ended June 30, 2017, promotional credits resulted in a revenue reduction of approximately \$29,730 and an expense reclassification of approximately \$20,029.

Prizes. Expenses for scratch prizes are recorded based on the predetermined prize structure for each game. Expenses for lotto prizes are recorded based on the predetermined prize structure for each individual game. No prize expense is recorded for free tickets distributed.

Unclaimed Prizes. Prizes for the lotto games must be claimed within six months after the appropriate draw date. Prizes for scratch games must be claimed within six months of the announced end of each game. The unclaimed prize amounts for these games are taken as a reduction in the Lottery Prizes Payable liability and the Prize Expense and are transferred to the State of Montana General Fund as a portion of the quarterly transfer. The amount of unclaimed prizes for all Montana Lottery games is represented in the table below.

	Quarter Ended 6/30/18	Quarter Ended 6/30/17	Year to Date 6/30/18	Year to Date 6/30/17
Lotto	\$126,429	\$122,496	\$ 575,706	\$ 763,255
Scratch	\$ 60,729	\$285,889	\$ 609,859	\$ 825,586
TOTALS	\$187,158	\$408,385	\$1,185,565	\$1,588,841

2. OTHER ACCOUNTING ISSUES

Prior Period Adjustment. The prior period adjustments for the year ended June 30, 2017, were made by the State Accounting Bureau for changes made to the Lottery's pension accounts. These adjustments were made to account for a change in methodology used to allocate the pension figures amongst multiple funds within a single business unit at the State level. An increase was made to the Pension Deferred Outflows for \$30, an increase of \$11,655 was made to the Pension Deferred Inflows, and an increase was made to the Net Pension Liability for \$45,145. The result of the above equates to a \$56,770 reduction to the Lottery's Net Position.

New Accounting Guidance Implemented. For the year ended June 30, 2018, the Lottery implemented the provisions of GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* (GASB 75). The objective of this Statement is to improve the accounting and financial reporting by state and local governments for postemployment benefits other than pensions. It also improves the information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. GASB 75 replaces the requirements of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and GASB Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*. An actuarial valuation of the total OPEB liability is required at least biennially for all plans.

GASB Statement No. 75 requires a retroactive restatement of financial statements for all prior periods presented. If restatement for prior periods is not practical, the cumulative effect of applying the statements is presented as a restatement of the beginning net position for the earliest period restated. In accordance with GASB 75, the Lottery restated OPEB liabilities beginning with the year ended June 30, 2018. A significant decrease of OPEB liabilities has been reported in the amount of \$608,460, creating an increase to beginning net position in the same amount. There was also an amount adjusted to the beginning net position for \$43,011 associated with GASB 68, *Pension Accounting for Employer and Nonemployer Contributing Entities*. This adjustment was made to record employer amounts for the Public Employee Retirement System pension plan for nongovernmental fund types.

3. SUMMARY OF ACCOUNTS

Cash and Cash Equivalents. Cash and cash equivalents consist of interest-bearing deposits with the Montana Board of Investments short-term investment pool; cash on deposit in a revolving account with an approved non-state financial institution; and cash on deposit with the Montana State Treasurer that is part of the State's pooled cash and is not separately identifiable as to specific types of securities. These funds are highly liquid and may be drawn on daily.

Cash and cash equivalents consist of the following:

	June 30,	
	<u>2018</u>	<u>2017</u>
Short-term investment pool	\$1,460,079	\$1,439,929
Cash on deposit with State Treasurer	1,138,842	523,365
Cash in revolving deposit account	10,000	10,000
Petty Cash & Cash On-Hand	200	200
TOTALS	\$2,609,121	\$1,973,494

The bank balance of the revolving deposit account, not including outstanding deposits or checks, was \$32,098, and \$10,438 as of June 30, 2018 and 2017, respectively, and was covered by federal depository insurance. The carrying amount reported in the balance sheet for cash and cash equivalents approximates the fair market value.

Receivables. For the year ended June 30, 2018, receivables include \$2,088,392, representing amounts due the Lottery for tickets purchased by retailers. Receivables also include \$2,453 for interest income due from the Montana Board of Investments short-term investment pool. An allowance for ticket returns is included in the receivables amount. This allowance represents a reduction in receivables as of June 30, 2018, for estimated ticket returns. This is an estimate based on returns received to date, as well as an estimate of tickets unsold by retailers for games that have a public sale end date prior to July 1, 2018. The allowance for ticket returns is \$321,666 as of June 30, 2018. The return of vendor fees related to the allowance for returns is \$27,309.

For the year ended June 30, 2017, receivables included \$1,994,028, representing amounts due the Lottery for tickets purchased by retailers. Receivables also include \$1,281 for interest income due from the Montana Board of Investments short-term investment pool. An allowance for ticket returns is included in the receivables amount. This allowance represents a reduction in receivables as of June 30, 2017, for estimated ticket returns. This is an estimate based on returns received to date, as well as an estimate of tickets unsold by retailers for games that have a public sale end date prior to July 1, 2017. The allowance for ticket returns is \$267,827 as of June 30, 2017. The return of vendor fees related to the allowance for returns is \$22,739.

Inventories. Inventories consist of merchandise and supplies inventories. Merchandise inventory for years ended June 30, 2018 and 2017 include scratch tickets valued at \$405,463, and \$460,462, respectively, that are stored in the warehouse, at retailers prior to being activated by the retailer, and with the marketing representatives. These ticket inventories are recorded at cost using the specific identification method and maintained on a perpetual inventory system. Tickets are charged to cost of tickets sold upon activation or after game end.

Supplies inventories include ticket dispensers, premiums and point-of-sale materials. For the years ended June 30, 2018, and 2017, supplies inventories totaled \$70,194, and \$51,830, respectively. These inventories are also recorded at cost using the specific identification method.

Other Current Assets. Other current assets include the following:

	June 30,	
	<u>2018</u>	<u>2017</u>
Prepaid Expenses	\$34,713	\$38,455

The prepaid expenses for the year ended June 30, 2018 consisted of \$9,000 for booth fees for upcoming events, \$10,000 in annual lottery industry dues, \$245 in employee advances, and \$15,468 for prepaid commissions and vendor fees related to unearned revenue. The prepaid expenses for the year ended June 30, 2017 consisted of \$5,250 for booth fees for upcoming events, \$20,000 in annual lottery industry dues, \$256 in employee advances, and \$12,949 for prepaid commissions and vendor fees related to unearned revenue.

Property and Equipment. A summary of property and equipment for the Lottery for both years is as follows:

	June 30, 2016	Additions	Deletions	June 30, 2017
Leasehold Improvements	\$ 59,781	\$ 39,012	-	\$ 98,793
Furniture & Equipment	\$ 538,153	\$ 159,374	\$ (126,712)	\$ 570,815
Accumulated Depreciation	\$ (461,917)	\$ (46,798)	\$ 106,070	\$ (402,645)

	June 30, 2017	Additions	Deletions	June 30, 2018
Leasehold Improvements	\$ 98,793	\$ -	-	\$ 98,793
Furniture & Equipment	\$ 570,815	\$ 18,054	\$ (6,859)	\$ 582,010
Accumulated Depreciation	\$ (402,645)	\$ (50,497)	\$ 6,516	\$ (446,626)

Estimated Prize Liability. The estimated prize liability represents the Lottery's estimate of prizes payable related to games in process at year-end based on the predetermined prize structure of each outstanding game.

Obligation to Transfer Funds. The Lottery is required to transfer its net revenue to the Montana State General Fund. This change was enacted through the passage of SB83 by the 1995 Legislature and signed into law by Governor Racicot in April 1995. The 2015 Legislature passed HB617 which changed the transfer requirements. Any year forward, the Lottery is to transfer an amount to the General Fund that equals the transfer made by the Lottery for FY2015. Any amount over and above this threshold will then be transferred to the Office of Commissioner for Higher Education (OCHE) for the Montana STEM scholarship program. The transfer obligations outstanding at June 30, 2018 were \$1,153,531 to the General Fund and \$0 to OCHE. For the year ending June 30, 2017, the obligation outstanding at year end was \$1,480,492 due to the General Fund and \$0 to OCHE.

Compensated Absences. State employees earn vacation leave ranging from 15 to 24 days per year depending on the individual's years of service. Vacation leave may be accumulated not to exceed two times the maximum number of days earned annually. With no limit on accumulation, sick leave is earned at 12 days per year. Upon retirement or termination, an employee is paid 100% for unused vacation and 25% for unused sick leave. The Lottery's liability for compensated absences is detailed below.

<u>Balance</u> <u>June 30, 2016</u>	<u>Net Leave</u> <u>Earned/(Used)</u>	<u>Balance</u> <u>June 30, 2017</u>
\$236,109	\$(34,456)	\$201,653
<u>Balance</u> <u>June 30, 2017</u>	<u>Net Leave</u> <u>Earned/(Used)</u>	<u>Balance</u> <u>June 30, 2018</u>
\$201,653	\$5,483	\$207,136

Non-Current Liabilities. Following are the changes in non-current liabilities for the years ended June 30, 2018 and 2017:

Year ended June 30, 2018					
	<u>Balance</u> <u>July 1, 2017</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>June 30, 2018</u>	<u>Amounts</u> <u>due within</u> <u>one year</u>
Multi-State Prize Liability	\$ 952,083	\$220,722	\$(418,356)	\$ 754,449	\$ -
Accrued Compensated Absences	\$ -	\$ 87,373	\$(39,089)	\$ 48,284	\$ -
Net Pension Liability	\$1,967,263	\$233,745	\$ -	\$2,201,008	\$ -
Other Post Employment Benefits	\$ 731,049	\$ -	\$(608,460)	\$ 122,589	\$ -

Year ended June 30, 2017

	Balance			Balance	Amounts
	July 1, 2016	Additions	Reductions	June 30, 2017	due within
					one year
Multi-State Prize Liability	\$1,016,794	\$ 10,368	\$(75,079)	\$ 952,083	\$ -
Accrued Compensated Absences	\$ 102,379	\$ 40,241	\$(142,620)	\$ -	\$ -
Net Pension Liability	\$1,651,762	\$481,540	\$(166,039)	\$1,967,263	\$ -
Other Post Employment Benefits	\$ 663,958	\$111,105	\$(44,014)	\$ 731,049	\$ -

Commissions. Section 23-7-301(10), MCA, provides retailers a commission on scratch and lotto tickets or chances sold. The Lottery Commission established this commission at 5% of the face value of scratch tickets activated by the retailers and the face value of lotto tickets sold. Section 23-4-302 (5)(b)(i), MCA, establishes a 3.99% commission for the face value of Fantasy Sports tickets sold. In addition retailers can earn bonus commissions on tickets sold based on incremental sales of scratch tickets. For the years ended June 30, 2018 and 2017, retailers earned bonus commissions of \$421,698 and \$332,840, respectively. For the years ended June 30, 2018 and 2017, total commissions were \$3,269,397 and \$2,981,078, respectively.

4. PAYMENTS TO OTHER STATE AGENCIES

The Lottery receives a variety of services, supplies, and materials from other state agencies. These services and materials are detailed below for the fiscal years ended June 30, 2018 and 2017:

Year Ended June 30	2018	2017
Administrative Service Fees	\$80,432	\$73,734
Audit Fees	76,262	26,409
Computer Fees	82,407	79,633
Insurance	13,854	12,874
Mail Processing Fees	12,589	11,066
Other Expenses	3,235	5,450
Payroll Services	7,518	7,026
Printing	11,149	6,265
Record Retention	1,018	1,018
State Accounting System Support	4,027	4,013
Supplies & Materials	375	247
Telecommunications	9,526	10,598
Warrant Writing Services	1,672	1,013
	<u>\$304,064</u>	<u>\$239,346</u>

5. PRIZES

Paid Prizes. Section 23-7-402, MCA states, "A minimum of 45% of the money paid for tickets or chances must be paid as prize money". Prize expense is recorded based on the predetermined prize structure percentage for each game less unclaimed prizes. For the year ended June 30, 2018, the prize expense of \$32,551,203 is 57.73% of net Lottery ticket revenue of \$56,381,488. For the year ended June 30, 2017, the prize expense of \$30,594,840 was 58.34% of net Lottery ticket revenue of \$52,441,929.

6. TRANSFERS OF NET REVENUE

Section 23-7-402(3), MCA, states "That part of all gross revenue not used for payment of prizes, commissions, and operating expenses, together with the interest earned on the gross revenue while the gross revenue is in the enterprise fund, is net revenue. Net revenue must be transferred quarterly from the enterprise fund established by 23-7-401, MCA, to the state general fund. Once the amount of revenue transferred to the general fund during a fiscal year equals the amount transferred to the general fund in fiscal year 2015, any additional net revenue must be transferred to the Montana STEM scholarship program special revenue account established in 20-26-617, MCA. For the years ended June 30, 2018 and 2017, the net revenue payable to the State General Fund totaled \$10,699,126, and \$9,224,231, respectively. For the years ended June 30, 2018 and 2017, the net revenue payable to the Montana STEM scholarship totaled \$0, and \$0, respectively.

7. MULTI-STATE LOTTERY

In November 1989 the Montana State Lottery joined the Multi-State Lottery Association (MUSL). MUSL was created in September 1987 to operate a multi-state lottery game for the benefit of party lotteries. Powerball, Hot Lotto, Mega Millions, and Lotto America are the games jointly operated by the members, in which Montana presently participates. Each lottery participating in MUSL is represented on the Board of Directors.

The Multi-State Lottery Reserve Fund with a balance of \$886,138 and \$1,093,333 as of June 30, 2018, and 2017, respectively, is comprised of several reserve accounts, which are maintained by the Multi-State Lottery Association (MUSL). A portion of the Powerball Unreserved Account is classified as a current asset which represents an amount expected to be converted into cash and collected from MUSL within the next fiscal year. The balance of these reserve accounts and investment category is as follows:

June 30, 2018

	US Treasury	Federal Agencies	Total
Powerball Prize Reserve Account	\$347,294	\$ 15,377	\$ 362,671
Powerball Set Prize Reserve Account	39,886	118,960	158,846
Powerball Unreserved Account	7,559	124,129	131,688
Lotto America Prize Reserve Account	-	28,812	28,812
Mega Millions Prize Reserve Account	<u>185,362</u>	<u>18,759</u>	<u>204,121</u>
Total Reserves	<u>\$580,101</u>	<u>\$306,037</u>	<u>\$886,138</u>
Less Current Portion			<u>(65,000)</u>
Non Current Reserves			<u>\$821,138</u>

June 30, 2017

	US Treasury	Federal Agencies	Total
Powerball Prize Reserve Account	\$343,544	\$ 55,926	\$ 399,470
Powerball Set Prize Reserve Account	44,637	129,046	173,683
Powerball Unreserved Account	20,382	120,868	141,250
Hot Lotto Set Prize Reserve Account	-	238,527	238,527
Mega Millions Prize Reserve Account	<u>113,081</u>	<u>27,322</u>	<u>140,403</u>
Total Reserves	<u>\$521,644</u>	<u>\$571,689</u>	<u>\$1,093,333</u>
Less Current Portion			<u>(65,000)</u>
Non Current Reserves			<u>\$1,028,333</u>

The Powerball Prize Reserve Account is to be used only in the event of an unanticipated prize claim. It is an insurance fund intended to protect the member lotteries against the liability that could result from a system failure at one of the member lotteries. All money paid to this fund would be returned to the Lottery one year after the Lottery leaves the Powerball game, assuming that no unanticipated prize claims have been paid.

The Powerball Set Prize Reserve Account is used to fund prize payments for current drawings. Since the Powerball game has fixed prizes, it is often necessary to draw from this reserve to fund payment of prizes at the fixed amount. This account would be returned to the Lottery upon withdrawal from the Powerball game.

The Lottery contributes to these reserve funds through the 50% set aside for prizes. In addition the Lottery was required to contribute for its portion of the reserve funds accumulated since the start of the Powerball game. Payments made to this fund are considered a portion of prize expense associated with the game.

The Powerball Unreserved Account is a separate account used by a participating Lottery to have MUSL hold funds due to the Lottery. Balances in this account are created when any MUSL jackpot expires and goes unclaimed. Each Lottery is then refunded its pro rata share of the jackpot based on sales during the accumulation of that specific jackpot. This money is then invested in U.S. Treasury securities until withdrawn. Interest earned on the Lottery's share of the fund is added to the Unreserved Account on a quarterly basis. The amount in the Unreserved Account has limited uses and are set and approved by the Board with the stipulation that requests to use the funds are accompanied by certification from the requesting Board Member that the payment is made in conformance with state or jurisdiction law and is related to a MUSL activity.

During fiscal year ended 2018, the Lottery received \$1,715 in interest, and had \$11,277 withdrawn for annual MUSL dues and assessments. During the fiscal year ended 2017, the Lottery received \$827 in interest, and had \$29,417 withdrawn for annual MUSL dues and assessments.

The Hot Lotto Set Prize Reserve Account is administered by MUSL and is to be used only in the event of unanticipated prize claims. Like other MUSL games the reserve amount would be returned to the Lottery one year after withdrawal from the Hot Lotto game. The Lottery contributes to the reserve through the 50% set aside for prizes. Payments made to the reserve are considered a portion of the prize expense related to the game.

The Lotto America Prize Reserve Account is administered by MUSL and is to be used only in the event of unanticipated prize claims. Like other MUSL games the reserve amount would be returned to the Lottery one year after withdrawal from the Lotto America game. The Lottery contributes to the reserve through the 50% set aside for prizes. Payments made to the reserve are considered a portion of the prize expense related to the game.

The Mega Millions Prize Reserve Account is to be used only in the event of an unanticipated prize claim. It is an insurance fund intended to protect the member lotteries against the liability that could result from a system failure at one of the member lotteries. All money paid to this fund would be returned to the Lottery one year after the Lottery leaves the Mega Millions game, assuming that no unanticipated prize claims have been paid. The Lottery contributes to the reserve through the 50% set aside for prizes for Mega Millions plays and 50% for Megaplier plays. Payments made to the reserve are considered a portion of the prize expense related to the game.

8. GAMES

Currently, Montana Lottery games are Scratch ticket games and seven Lotto games referred to as Powerball, Montana Cash, Hot Lotto, Lotto America, Mega Millions, Lucky for Life, and Big Sky Bonus. The Lottery also offers Treasure Play, a line of instant terminal-issued games with pre-determined odds, and Montana Millionaire, a limited-edition Lottery game. The Lottery is facilitating Fantasy Sports games on behalf of the Board of Horse Racing. Currently the Lottery is selling Montana Sports Action Fantasy Football and Fantasy Racing games.

Scratch ticket games provide players the opportunity to win instantly by scratching the latex covering to reveal a prize. The lottery sells tickets for \$1, \$2, \$3, \$5, \$10, and \$20. Cash prizes range from \$1 to \$500,000, plus specialty prizes for certain games.

The Powerball game allows players a chance to win a minimum parimutuel jackpot of \$40 million. A player must match all six numbers to win the jackpot. Players also win prizes ranging from \$4 to \$1 million for matching fewer than all six numbers. Drawings are held twice weekly on Wednesday and Saturday nights. Powerball is offered in 45 lottery jurisdictions including Montana. For any drawing, if no ticket matches 6 out of 6 numbers, the jackpot rolls over to the next drawing, creating a progressive jackpot. In March 2001, the Lottery added Power Play to the Powerball game. For an additional \$1 per play, Power Play doubles the Match 5 prize from \$1 million to \$2 million and increases other prizes as well. Each Powerball prize (except for the jackpot and the Match 5 prize) increases by 2x, 3x, 4x, 5x, or 10x with Power Play.

The Montana Cash game allows players the chance to win a minimum parimutuel jackpot of \$40,000. Players select five numbers from a field of 45 and must match at least two out of five to win a prize. Matching 2 of 5 wins \$1, 3 of 5 wins \$5, and 4 of 5 wins \$200. The drawings are conducted twice weekly on Wednesday and Saturday nights. If no ticket matches all five numbers, the jackpot rolls over to the next drawing to create a progressive jackpot.

Hot Lotto allows players in the 16 participating lotteries a chance to win an all-cash parimutuel jackpot with a guaranteed minimum of \$1 million, plus tax withholdings paid. This change was implemented in May 2013. Each time the jackpot is not won, it grows, thus creating a progressive jackpot. Players choose five numbers from one to 47, and one Hot Ball number from 1 to 19. To win the parimutuel jackpot, a player must match all six numbers drawn. Players can also win prizes from \$2 to \$30,000 by matching fewer than all six numbers. If a player chooses, they can add Sizzler to their ticket for \$1. This multiplies any prize by three, except the jackpot. Drawings are held twice weekly on Wednesday and Saturday nights. This game ended November 11, 2017.

Mega Millions is a multi-state game that allows players to win a minimum parimutuel jackpot starting at \$15 million. If no one wins the jackpot, the jackpot continues to grow. Mega Millions went on sale March 1, 2010, in Montana. To win the jackpot, players must match all six numbers drawn; other prizes range from \$2 to \$1,000,000. For an additional \$1 per play, Mega Millions has a Megaplier option which multiplies non-jackpot prizes by two, three, or four. Drawings are held each Tuesday and Friday night.

Lucky for Life debuted January 2015. Lucky for Life is a multi-state game that allows players to win a top prize of \$1,000 a day for life. The second prize is \$25,000 a year for life. This pari-mutuel game has a set top prize and tickets cost \$2 each. Players select five numbers from a field of 48 and must match at least the Lucky Ball to win a prize. The drawings are conducted twice weekly on Monday and Friday nights.

Big Sky Bonus debuted April 2016. Big Sky Bonus is a Montana-only game that allows players to win a progressive jackpot. Players select 4 numbers from a field of 28 and must match at least 2 out of 4 to win a prize unless they hit the bonus number which is a 5th number picked out of a field of 17. Matching the bonus number at any time wins \$10. Matching 2 of 4 wins \$2, 3 of 4 wins \$20, and 4 of 4 wins the jackpot. The drawing is held every day at 7:30 p.m. If no ticket matches all 4 numbers, the jackpot rolls over to the next day to create a progressive jackpot.

Lotto America is the newest on-line game for the Lottery. Lotto America allows players in the 13 participating lotteries a chance to win an all-cash pari-mutuel jackpot with a guaranteed minimum of \$2 million. Each time the jackpot is not won, it grows, thus creating a progressive jackpot. Players choose five numbers from 1 to 52, and one Bonus number from 1 to 10. To win the pari-mutuel jackpot, a player must match all six numbers. Drawings are held twice weekly on Wednesday and Saturday nights. A multiplier called the All Star Bonus can be added to win 2X, 3X, 4X, or 5X to any prize except the jackpot for bigger prizes. Drawings are held every Wednesday and Saturday.

The Treasure Play games are offered on self-serve terminals in taverns and casinos that are licensed to sell Montana Lottery products. Introduced in November 2011, they are a suite of games with a pre-determined prize structure like a Scratch game. Players can tell instantly if they have won a prize. The tickets sell for \$1, \$2, \$3, \$5, and \$10.

Montana Millionaire is a seasonal raffle-type game offering a \$1 million top prize. The first offering went on sale October 1, 2007. The lottery has sold the game every winter since. Tickets are sold sequentially and are sold for \$20 each. Early bird drawings for \$25,000 and \$15,000, respectively, will be offered on Thanksgiving weekend and the second week of December to stimulate early sales. There will also be 400 \$100 instant winners and 625 \$500 instant winners. On December 29, 2017, one \$1 million prize was awarded, along with three \$100,000 prizes and five \$10,000 prizes. Montana Millionaire is scheduled to sell from November 1 through December 31, 2018, with a drawing on New Year's Day 2019 or earlier if it is sold out.

The Montana Lottery offers a product line called Montana Sports Action on behalf of the Montana Board of Horse Racing. The product line began in August 2008 with a game called Fantasy Football. To play the game, players choose five offensive players and a defensive unit from the official roster of professional football players and teams. The players can also select a bet amount (\$5, \$10, \$20, \$50, or \$100) which determines the shares of the prize pool players are eligible to win should their team have one of the three highest point totals for the week. Tickets are sold weekly through the professional playoffs, excluding the championship game. A second game called Fantasy Racing was introduced in February 2009 and follows the NASCAR® Sprint Cup Series. Teams are created by selecting a driver from the top nine ranked drivers for the week, three drivers ranked from 10 through 34, and one driver ranked 35 or above. The sixth element in a player's Fantasy Racing team is the number of yellow-flag cautions the player believes might occur in that week's race. Like Fantasy Football, players may also choose to purchase a higher-cost ticket to increase the share of the prize pool in the event their team has one of the three highest point totals for that race.

9. COMMITMENTS - GAMING SUPPLIER CONTRACTS

Scratch Tickets. On July 30, 2015 the Montana Lottery Commission approved the award of a five-year contract with Scientific Games International (SGI) for the provision of scratch tickets. The contract is for five years with the option for two additional one-year renewals. The contract contains specifications regarding ticket design, printing, game ownership, inspection, and prize structure.

SGL, as the vendor, provided a performance bond covering the contract term and an errors and omissions policy covering an ultimate net loss of \$5,000,000. The Lottery may terminate this contract by providing proper notification to Scientific Games.

On-line Services. On February 13, 2015, the Lottery signed a seven-year contract with Intralot, Inc. of Duluth, GA to provide an on-line gaming system and the associated services beginning March 31, 2016. The contract requires Intralot to provide new terminals to all retailers with the associated software and communications. Payment under the contract is based on 8.49% of net weekly Lottery sales of lotto and scratch games. The contract currently has a termination date of March 30, 2023.

10. LEASES/INSTALLMENT PURCHASES PAYABLE

Rent. The Montana Lottery leases its office, administrative and warehouse facilities under a lease agreement that is effective January 1, 2017 through August 2027. The monthly lease payment is \$18,068.

11. INVESTMENTS

Effective June 30, 2005, the State of Montana implemented the provisions of Governmental Accounting Standards Board (GASB) Statement No. 40, *Deposit and Investment Risk Disclosures*. The Lottery participates in two investment pools: the Multi-State Lottery Association (MUSL) reserve accounts and the State of Montana's Short Term Investment Pool (STIP). The applicable investment disclosures are described in the following paragraphs.

Multi-State Lottery Association The MUSL investment policy for prize reserve and unreserved funds states that permitted investments "include direct obligations of the United States government, perfected repurchase agreements, and obligations issued or guaranteed as to payment of principal and interest by agencies or instrumentalities of the United States government, and mutual funds of approved investments".

Short-term Investment Pool The State's Short Term Investment Pool (STIP) is an external investment pool managed and administered under the direction of the Montana Board of Investments as statutorily authorized by the Unified Investment Program. It is a commingled external investment pool and participants may request for redemption on a daily basis. The fair values of the investments in this category have been determined using the NAV per share (or its equivalent) of the investment.

Credit risk is defined as the risk that an issuer of an investment will not fulfill its obligation, i.e., not make timely principal and interest payments. The STIP securities have credit risk as measured by major credit rating services, however, the pool is not rated. The Lottery does not have a policy regarding credit risk

Per MUSL, for 2018 the prize reserves held on behalf of the Montana Lottery are invested in the Montana Winners Trust. In this trust, 73% was invested in Federal Agencies; another 2% was invested in the First American Government Obligation Fund which is used for overnight investing and does not have a rating from S&P or Moodys, etc. However, it is a very conservatively managed vehicle, investing exclusively in short-term U.S. government securities. The other 25% of the prize reserves are invested in Federal Agency repurchase agreements secured by U.S. government securities. The Lottery does not have any authority or a policy regarding the investment portfolios.

Custodial credit risk is the risk that the Lottery would not be able to recover the value of the investment or collateral securities that are in the possession of an outside party in the event of the failure of that party.

The MUSL prize reserves are held in the Montana Winners Trust using policies set forth by the MUSL board regarding policies for the type of securities, as well as the custody, trading and the use of proceeds of the securities. The Lottery does not have any authority or a policy regarding the investment portfolios.

Concentration of credit is the risk of loss attributed to the magnitude of a government's investment in a single issuer. Because STIP is a pooled investment, this risk does not apply. Because the MUSL reserves are also a pooled investment, this risk does not apply to them either.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Lottery does not have any authority or a policy regarding the investment portfolios.

The MUSL prize reserves are invested through the Montana Winners Trust with daily liquidity, and therefore, has no interest rate risk. The MUSL board's investment policy limits the individual security and the portfolio's maturity. As of June 30, 2018, the duration for the U.S. Government Treasury securities was a blended rate of 1.13 years.

The STIP securities are invested in various bond pools and investment portfolios which are liquid on a daily basis. Therefore, STIP, itself does not have this risk. The duration for this pool as of June 30, 2018 is 46 days.

According to the STIP Investment Policy, “the STIP portfolio will minimize interest rate risk by:

- 1) Structuring the investment portfolio so securities mature to meet cash requirements for ongoing operations, thereby normally avoiding the need to sell securities on the open market prior to maturity;
- 2) Maintaining a dollar-weighted average portfolio maturity (WAM) for 60 days or less (for this purpose, the date to the next coupon reset date will be used for all floating or variable rate securities); and
- 3) STIP will maintain a reserve account.”

12. FAIR VALUE MEASUREMENT

The Lottery categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles as follows:

Level 1 – Quoted prices for identical assets or liabilities in active markets.

Level 2 – Prices determined using inputs, other than quoted prices included within Level 1, that are observable for an asset or liability, either directly or indirectly.

Level 3 – Prices are determined using unobservable inputs.

Investments Measured at Net Asset Value

		Fair Value Measurements Using		
	June 30, 2018	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservab le (Level 3)
<u>Investments by Net Asset Value</u>				
Short Term Investment Pool (STIP)	\$1,460,079			
Total Investments by net asset value level	\$1,460,079	\$ -	\$ -	\$ -

Investments Measured at Net Asset Value

		Fair Value Measurements Using		
	June 30, 2017	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservab le (Level 3)
<u>Investments by Net Asset Value</u>				
Short Term Investment Pool (STIP)	\$1,439,929			
Total Investments by net asset value level	\$1,439,929	\$ -	\$ -	\$ -

The Short Term Investment Pool (STIP) has a daily redemption frequency and a daily redemption notice period. The fair value of this pool has been determined using the Net Asset Value (or its equivalent).

13. OTHER POST EMPLOYMENT BENEFITS

General. The State of Montana and the Montana Lottery provide optional postemployment healthcare benefits in accordance with Montana Code Annotated, Title 2, Chapter 18, Section 704 to the following employees and dependents who elect to continue coverage and pay administratively established contributions: (1) employees and dependents who retire under applicable retirement provisions, and (2) surviving dependents of deceased employees. Medical, dental, and vision benefits are available through this plan.

Plan Description. The State OPEB plans are single employer plans. There are a number of State agencies who are participating employers under this plan. Each participating employer is required to disclose additional information as required per GASB No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions* (GASB 75).

The healthcare OPEB plans allow retirees to participate, as a group, at a rate that does not cover all of the related costs. This results in reporting the total OPEB liability in the related financial statements and note disclosures. Reported contributions are not a result of direct funding to the plans or for associated liabilities, but are a measure of the difference in retiree payments into the plans and actual medical costs associated with those individuals paid for by the plans. The healthcare OPEB plans are reported as agency funds and no assets are accumulated in a trust. There are no assets or liabilities as only contributions collected and distributions made are reflected in these funds. See the funding policy that follows.

Basis of Accounting. OPEB is recorded on an accrual basis on proprietary fund financial statements. Plan member contributions are recognized in the period in which the contributions are made. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

Funding Policy. The State of Montana pays for postemployment healthcare benefits on a pay-as-you-go basis. Montana Code Annotated, Title 2, Chapter 18, Part 8 gives authority for establishing and amending the funding policy to the Department of Administration. As of June 2018, the State plan's administratively established retiree medical premiums vary between \$327 and \$2,403 per month. Retiree dental premiums vary between \$52.00 and \$156.00 per month while vision premiums vary between \$9.71 and \$28.31, depending on the types and number of dependents enrolled. The plan provides different coinsurance amounts and deductibles depending on whether members use in-network or out-of-network providers. The plan automatically reduces claim reimbursement for members eligible for Medicare, even if the member is not enrolled in Medicare.

Annual Other Postemployment Benefit Cost and Contributions. The annual required contribution (ARC), an actuarially determined rate in accordance with the parameters of GASB Statement No. 45, represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years.

The following table presents the OPEB cost for the year, the amount contributed, and changes in the OPEB plan for fiscal year 2017;

Year ended June 30,	2017
Annual Required Contribution/OPEB Cost	\$82,900
Interest on net OPEB obligation	28,205
Amortization Factor	(22,122)
Annual OPEB cost	88,983
Retiree Claims Paid	(21,892)
Increase in net OPEB obligation	67,091
Net OPEB obligation – beginning of year	663,958
Net OPEB obligation – end of year	<u>\$731,049</u>

Since the plan pays other postemployment benefits on a pay-as-you-go basis prior to fiscal year end 2018, the funded ratio of the OPEB obligation for fiscal year end 2017 is 0%.

The Lottery's annual healthcare OPEB cost, the percentage of annual implicit contributions toward the OPEB cost through retiree claims paid on their behalf, and the net OPEB obligation for the fiscal years 2017 through 2015 was as follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
6/30/2017	\$88,983	24.6%	\$731,049
6/30/2016	\$88,769	24.8%	\$663,958
6/30/2015	\$90,075	28.2%	\$597,244

Actuarial Methods and Assumptions. The total OPEB liability (TOL) measured under GASB 75 is based upon service cost and more standardized reporting assumptions than prior GASB Statements. As a pay-as-you-go public entity, GASB 75 requires a 20-year current municipal bond discount rate to establish an Actuarially Determined Contribution (ADC). The GASB 75 valuation is further required to show both historical and projected future net changes in TOL, as well as sensitivity to changes in key underlying assumptions. Actuarially determined amounts are subject to continual revisions being actual results are compared with past expectations and new estimates are made about the future. Actuarial calculations reflect a long-term perspective. The projection of benefits for financial reporting purposes does not explicitly incorporate the potential effects of legal or contractual funding limitations on the pattern of cost sharing between the employer and plan members in the future.

The State's OPEB Plan TOL in December 31, 2017, rolled forward to March 31, 2018, actuarial assumptions and other inputs, applied to all periods included in the measurement, unless otherwise specified:

Actuarial valuation date	December 31, 2017
Measurement date	March 31, 2018
Discount rate	3.89%
Projected payroll increases	4.00%
Actuarial funding method	Entry age normal
Amortization period	20 years
Asset valuation	Not applicable since no assets meet the definition of plan assets
Average retirement age	62
Participation (of future retirees)	55% future retirees and 60% of future eligible spouses
Marital status	Actual spouse information is used for current retirees. Marital status at retirement for future members assumed to be 70%.
Mortality – Healthy	Assumed to follow RP2000 Combined Mortality Table with improvements projected by Scale BB to 2020, set back one year for males.
Mortality – Disabled	Assumed to follow RP2000 Combined Mortality Table with no projections.
Healthcare cost trend rates	7.5% for both medical and prescription initially, decreasing 0.1% per year to an ultimate rate of 3.8%. Cost increases are assumed to apply at the end of the plan year.
Retiree Contribution Increases	Current year was based on actual trend. For retiree/surviving spouse and spouse the increase is 7.0% in 2019 decreasing between 0.1% and 0.5% per year to an ultimate rate of 3.8%.

Changes in actuarial assumptions and methods since last measurement date: Changes in actuarial methods include adjustments to the amortization period and actuarial cost method to conform with GASB 75 requirements. Changes in actuarial assumptions include revised rates per the retirement system pension valuations as of July 1, 2017 and interest rate based upon the March 31, 2018, 20-year municipal bond index per GASB 75 requirements. Other changes include revised rates based on actual data and projected trend and updated projected healthcare trend rates to follow the Getzen model.

Changes in benefit terms since last measurement date: Medical plans moved from Cigna to Allegiance as of January 1, 2016, the State implemented reference-based pricing hospital contracts effective July 1, 2016, and pharmacy moved from URx to Navitus as of January 1, 2017. The State implemented an Employer Group Waiver Program for Medicare retirees effective January 1, 2017.

Sensitivity of the TOL to changes in discount rate. The following presents the TOL of the Lottery's plan, as well as what they would be if calculated using a discount rate that is 1-percentage-point lower (2.89%) or 1-percentage-point higher (4.89%) than the current discount rate:

	1.0% Decrease (2.89%)	Current Discount Rate (3.89%)	1.0% Increase (4.89%)
<u>Lottery OPEB</u>			
June 30, 2018	\$150,438	\$122,589	\$101,302

Sensitivity of the TOL to changes in the healthcare cost trend rates. The following presents the TOL of the Lottery plan, as well as what they would be if calculated using healthcare cost trends that are 1-percentage-point lower (6.5%) or 1-percentage-point higher (8.5%) than the current healthcare cost trend rates:

	1.0% Decrease (6.5%)	Current Discount Rate (7.5%)	1.0% Increase (8.5%)
<u>Lottery OPEB</u>			
June 30, 2018	\$100,721	\$122,589	\$152,127

OPEB Expense, Liability and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB. For the year ended June 30, 2018, the Lottery's plan's OPEB expense is \$9,070. The Lottery's proportionate share of the State's total OPEB liability is \$122,589 which is 0.242949% of the total State's OPEB liability at year end. Since this is the first year of implementation of GASB 75, there was no prior measurement date applicable to compare the proportionate percentage to the prior year.

At June 30, 2018, the Lottery's OPEB plan deferred outflows and inflows of resources are from the following sources:

June 30, 2018

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual experience	\$ -	\$10,976
Changes in Assumptions or other inputs	\$ -	\$ 687
Actual vs. Expected Investment Earnings	\$ -	\$ -
Amounts associated with transaction subsequent to the measurement date of the total OPEB liability	\$ 2,399	\$ -
Total	\$ 2,399	\$11,663

Amounts reported as deferred outflows of resources and deferred inflows of resources related to OPEB will be recognized in OPEB expense as follows:

Year Ended June 30,	Amount Recognized in OPEB expense as an increase or (decrease) to OPEB expense
2019	\$ 962
2020	\$ 962
2021	\$ 962
2022	\$ 962
2023	\$ 962
Thereafter	\$ 6,853

14. EMPLOYEE RETIREMENT PLAN

Plan Description. The PERS-Defined Benefit Retirement Plan (DBRP) and Defined Contribution Retirement Plan (DCRP) are administered by the Montana Public Employee Retirement Administration (MPERA), and are a multiple-employer, cost-sharing plans established July 1, 1945, and governed by Title 19, chapters 2 & 3, Montana Code Annotated (MCA). These plans cover the State, local governments, certain employees of the Montana University System, and school districts.

All new members are initially members of the PERS-DBRP and have a 12-month window during which they may choose to remain in the PERS-DBRP or join the PERS-DCRP by filing an irrevocable election. Members may not be members of both the *defined contribution* and *defined benefit* retirement plans.

The PERS-DBRP provides retirement, disability, and death benefits to plan members and their beneficiaries. Benefits are established by state law and can only be amended by the Legislature. Benefits are based on eligibility, years of service, and highest average compensation. Member rights are vested after five years of service.

Summary of Benefits. **Member's highest average compensation (HAC)**

Hired prior to July 1, 2011 - highest average compensation during any consecutive 36 months;

Hired on or after July 1, 2011 – highest average compensation during any consecutive 60 months;

Hired on or after July 1, 2013 – 110% annual cap on compensation considered as part of a member's highest average compensation.

Eligibility for benefit

Service retirement:

Hired prior to July 1, 2011: Age 60, 5 years of membership service;
Age 65, regardless of membership service; or
Any age, 30 years of membership service.

Hired on or after July 1, 2011: Age 65, 5 years of membership service;
Age 70, regardless of membership service.

Early retirement, actuarially reduced:
Hired prior to July 1, 2011: Age 50, 5 years of membership service; or
Any age, 25 years of membership service.

Hired on or after July 1, 2011: Age 55, 5 years of membership service.

Vesting; 5 years of membership service

Monthly benefit formula

Members hired prior to July 1, 2011:

- Less than 25 years of membership service: 1.785% of HAC per year of service credit;
- 25 years of membership service or more: 2% of HAC per year of service credit.

Members hired on or after July 1, 2011:

- Less than 10 years of membership service: 1.5% of HAC per year of service credit;
- 10 years or more, but less than 30 years of membership service: 1.785% of HAC per year of service credit;
- 30 years or more of membership service: 2% of HAC per year of service credit.

Guaranteed Annual Benefit Adjustment (GABA)

- 3% for members hired **prior to** July 1, 2007
- 1.5% for members hired **on or after** July 1, 2007
- Members hired on or after July 1, 2013:
 - (a) 1.5% for each year PERS is funded at or above 90%;
 - (b) 1.5% is reduced by 0.1% for each 2% PERS is funded below 90%; and
 - (c) 0% whenever the amortization period for PERS is 40 years or more.

After the member has completed 12 full months of retirement, the member's benefit increases by the applicable percentage each January, **inclusive** of other adjustments to the member's benefit.

Overview of Contributions.

Rates are specified by state law for periodic employer and employee contributions and are a percentage of the member's compensation. Contributions are deducted from each member's salary and remitted by participating employers. The State legislature has the authority to establish and amend contribution rates to the plan.

Member contributions to the system: a. Plan members are required to contribute 7.90% of member's compensation. Contributions are deducted from each member's salary and remitted by participating employers.

The 7.90% member contributions is temporary and will be decreased to 6.9% on January 1 following actuary valuation results that show the amortization period has dropped below 25 years and would remain below 25 years following the reduction of both the additional employer and additional member contribution rates.

Employer contributions to the system: State and University System employers are required to contribute 8.27% of members' compensation. Following the 2013 Legislative Session, PERS-employer contributions were temporarily increased. Effective July 1, 2013, employer contributions increased 1.0%. Beginning July 1, 2014, employer contributions increased an additional 0.1% a year over 10 years, through 2024. The employer additional contributions including the 0.27% added in 2007 and 2009, terminates on January 1 following actuary valuation results that show the amortization

period of the PERS-DBRP has dropped below 25 years and would remain below 25 years following the reductions of both the additional employer and member contributions rates. Effective July 1, 2013, employers are required to make contributions on working retirees' compensation. Member contributions for working retirees are not required.

Stand-Alone Statements. The PERS financial information is reported in the Public Employees' Retirement Board's *Comprehensive Annual Financial Report* for the fiscal year ended. It is available from the PERB at 100 North Park, PO Box 200131, Helena MT 59620-0131, 406-444-3154.

CAFR information including the stand alone financial statements can be found at the MPERA's website, <http://mpera.mt.gov/annualReports.shtml>. The latest actuarial valuation and experience study can be found at the MPERA's website, <http://mpera.mt.gov/actuarialValuations.asp>.

Actuarial Assumptions. The Total Pension Liability as of June 30, 2018, is based on the results of an actuarial valuation date of June 30, 2016 with update procedures to roll forward the Total Pension Liability to June 30, 2017. There were several significant assumptions and other inputs used to measure the Total Pension Liability. The actuarial assumptions used in the June 30, 2017 valuation were based on the results of the actuarial experience study, dated May 2017 for the six year period ended June 30, 2016. Among those assumptions were the following:

- General Wage Growth 3.50% (includes Inflation at 2.75%)
- Merit Increases 0% to 4.8%
- Investment Return 7.65%
- Postretirement Benefit Increases;
 - (a) 3% for members hired **prior** to July 1, 2007,
 - (b) 1.5% for members hired **on or after** July 1, 2007, and for members hired **on or after** July 1, 2013;
 - (a) 1.5% for each year PERS is funded at or above 90%;
 - (b) 1.5% is reduced by 0.1% for each 2% PERS is funded below 90%; and
 - (c) 0% whenever the amortization period for PERS is 40 years or more.

Mortality assumptions among contributing members, terminated vested members, service retired members and beneficiaries based on RP 2000 Combined Employee and Annuitant Mortality Tables projected to 2020 with scale BB. Mortality assumptions among Disabled Retirees are based on RP 2000 Combined Employee and Annuitant Mortality Tables with no projections. No future mortality improvement is assumed.

Discount Rate. The discount rate used to measure the Total Pension Liability was 7.65%. The projection of cash flows used to determine the discount rate assumed that contributions from participating plan members, employers, and non-employer contributing entities will be made based on the Board's funding policy, which establishes the contractually required rates under Montana Code Annotated. The State contributes 0.1% of salaries for local governments and 0.37% for school districts. In addition, the State contributes coal severance tax and interest money from the general fund. The interest is contributed monthly and the severance tax is contributed quarterly. Based on those assumptions, the System's fiduciary net position was projected to be adequate to make all the projected future benefit payments of current plan members through the year 2121. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the Total Pension Liability. No municipal bond rate was incorporated in the discount rate.

Target Allocations.

Asset Class	Target Asset Allocation	Long-Term Expected Real Rate of Return
Cash Equivalents	2.60%	4.00%
Domestic Equity	36.00%	4.55%
Foreign Equity	18.00%	6.35%
Fixed Income	23.40%	1.00%
Private Equity	12.00%	7.75%
Real Estate	8.00%	4.00%

The long-term expected return on pension plan assets is reviewed as part of the regular experience studies prepared for the System. The most recent analysis, performed for the six year period ended June 30, 2016, is outlined in a report dated May 2017, which can be located on the MPERA website. The long-term expected rate of return on pension plan investments was determined by considering information from various sources, including historical rates of return, rate of return assumptions adopted by similar public pension systems, and by using a building block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment and inflation) are developed for each major asset class. These ranges were combined to produce the long-term expected rate of return by weighing the expected future real rates of return by the target asset allocation percentage and then adding expected inflation.

Best estimates of the arithmetic real rates of return for each major asset class included in the System's target asset allocation as of June 30, 2017, is summarized in the above table.

Sensitivity Analysis.

<u>Employer Net Pension Liability</u>	1.0% Decrease (6.65%)	Current Discount Rate	1.0% Increase (8.65%)
June 30, 2018	\$3,205,580	\$2,201,008	\$1,357,746
June 30, 2017	\$2,854,644	\$1,967,263	\$1,202,872
June 30, 2016	\$2,546,659	\$1,651,762	\$ 896,042

In accordance with GASB 68 regarding the disclosure of the sensitivity of the Net Pension Liability to changes in the discount rate, the above table presents the Net Pension Liability calculated using the discount rate that is 1.00% lower (6.65%) or 1.00% higher (8.65%) than the current rate.

Summary of Significant Accounting Policies. The Montana Public Employee Retirement Administration (MPERA) prepares its financial statements using the accrual basis of accounting. For the purposes of measuring the Net Pension Liability, deferred inflows of resources and deferred outflows of resources related to pensions, Pension Expense, information about the fiduciary net position and additions to/deductions from fiduciary net position have been determined on the same accrual basis as they are reported by MPERA. For this purpose, member contributions are recognized in the period in which contributions are due. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Revenues are recognized in the accounting period they are earned and become measurable. Benefit payments and refunds are recognized in the accounting period when due and payable in accordance with the benefit terms. Expenses are recognized in the period incurred. Investments are reported at fair value. MPERA adheres to all applicable Governmental Accounting Standards Board (GASB) statements.

Net Pension Liability. In accordance with GASB Statement 68, Accounting and Financial Reporting for Pensions, employers are required to recognize and report certain amounts associated with their participation in the Public Employees' Retirement System (PERS). Statement 68 became effective for fiscal year ended June 30, 2015 and includes requirements to record and report their proportionate share of the collective Net Pension Liability, Pension Expense, Deferred Inflows and Deferred Outflows of resources associated with pensions.

In accordance with Statement 68, PERS has a special funding situation in which the State of Montana is legally responsible for making contributions directly to PERS on behalf of the employers. Due to the existence of this special funding situation, local governments and school districts are required to report the portion of the State of Montana's proportionate share of the collective Net Pension Liability that is associated with the non-State employer. The State of Montana also has a funding situation that is not Special Funding whereby the State General Fund provides contributions from the Coal Severance Tax collections and interest. All employers are required to report the portion of Coal Tax Severance Tax and interest attributable to the employer as a grant revenue.

Lottery Proportionate Share of Net Pension Liability:

Net Pension Liability as of 6/30/18	Net Pension Liability as of 6/30/17	Percent of Collective NPL as of 6/30/18	Percent of Collective NPL as of 6/30/17	Change in Percent of Collective NPL
\$2,201,008	\$1,967,263	0.113008%	0.115492%	(0.002484%)

At June 30, 2018, the Lottery recorded a liability of \$2,201,008 for its proportionate share of the Net Pension Liability. The Net Pension Liability was measured as of June 30, 2018, and the Total Pension Liability used to calculate the Net Pension Liability was determined by an actuarial valuation as of June 30, 2016, with roll forward provisions to June 30, 2017. For the fiscal years ended June 30, 2018, and 2017, the employer's proportion of the Net Pension Liability was based on the employer's contributions received by PERS during the measurement periods July 1, 2016 to June 30, 2017. Relative to the total employer contributions received from all of PERS' participating employers, at June 30, 2018, the Lottery's proportion was 0.113008%.

Changes in actuarial assumptions and methods:

Effective July 1, 2017, the following assumption changes were used:

- Lowered the interest rate from 7.75% to 7.65%
- Lowered the inflation rate from 3.00% to 2.75%
- Updated non-disabled mortality to the RP-2000 Combined Employee and Annuitant Mortality Table projected to 2020 using scale BB, males set back 1 year
- Increased rates of withdrawal
- Lowered the merit component of the total salary increase
- Lowered the wage base component of the total salary increase from 4.00% to 3.50%
- Decreased the administrative expense load from 0.27% to 0.26%

Effective July 1, 2017, the following method changes were used:

- Administrative expenses are recognized by an additional amount added to the normal cost contribution rate for the System. This amount will vary from year to year based on the prior year's actual administrative expenses.
- To be consistent with the wage base growth change, the payroll growth assumption for amortization as a level percent of pay was reduced from 4.00% to 3.50%

Changes in benefit terms:

Effective July 1, 2017, the following benefit changes were:

- The interest rate credited to member accounts increased from 0.25% to 0.77%
- Lump sum payouts in all systems are limited to the member's accumulated contributions rather than the present value of the member's benefit

Changes in proportionate share: There were no changes between the measurement date of the collective Net Pension Liability and the employer's reporting date that are expected to have a significant effect on the employer's proportionate share of the collective net pension liability.

Pension Expense. At June 30, 2018, the Lottery recognized \$282,156 for its proportionate share of the Plan's pension expense and recognized grant revenue of \$0 for the state of Montana proportionate share of the pension expense associated with the Lottery. Additionally, the employer recognized grant revenue of \$31,486 from the Coal Severance Tax Fund.

Recognition of Deferred Inflows and Outflows. At June 30, 2018 and 2017, the Lottery reported its proportionate share of PERS' deferred outflows of resources and deferred inflows of resources related to PERS from the following sources:

June 30, 2018

	Deferred Outflows of Resources	Deferred Inflows of Resources
Actual vs. Expected Experience	\$ 54,204	\$ 3,186
Changes in Assumptions	\$300,855	\$ -
Actual vs. Expected Investment Earnings	\$ -	\$14,782
Changes in Proportion Share and Differences between Employer Contributions and Proportionate Share of Contributions	\$ -	\$11,195
Employer contributions subsequent to the measurement date – FY 2018 contributions	\$129,440	\$ -
Total	\$484,499	\$29,163

June 30, 2017

	Deferred Outflows of Resources	Deferred Inflows of Resources
Actual vs. Expected Experience	\$ 10,615	\$ 6,512
Changes in Assumptions	\$185,080	\$ -
Actual vs. Expected Investment Earnings	\$ -	\$ -
Changes in Proportion Share and Differences between Employer Contributions and Proportionate Share of Contributions	\$ -	\$ 5,343
Employer contributions subsequent to the measurement date – FY 2017 contributions	\$124,362	\$ -
Total	\$320,057	\$ 11,855

Amounts reported as deferred outflows of resources related to pensions resulting from the Lottery's contributions subsequent to the measurement date will be recognized as a reduction of the Net Pension Liability in each year end. Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in Pension Expense as follows:

Year Ended June 30,	Amount Recognized in Pension Expense as an Increase or (decrease) to Pension Expense
2018	\$ 77,965
2019	\$172,109
2020	\$133,864
2021	\$(46,847)
2022	\$ 0
Thereafter	\$ 0



MONTANA LOTTERY

2525 N. MONTANA AVE., HELENA, MT 59601
PHONE: 406.444.5825 MONTANALOTTERY.COM