

\$2,000,000  
FOR EDUCATION



Tennessee Education Lottery  
Annual Report 2011

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## Letter from the Board Chair and the President and CEO

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On behalf of the Tennessee Education Lottery Corporation, we are pleased to present this overview of the organization's 2010–2011 Fiscal Year. As represented on the cover page, this year was noteworthy for one major milestone in particular — in May we surpassed the \$2 billion mark in funds raised to support education programs in Tennessee! A remarkable accomplishment, it speaks to the great success of our core mission and honors our commitment to the students and families who benefit most directly.

Indeed, the performance of the Tennessee Lottery this past fiscal year was superlative in every sense, as we overcame a sluggish economy and set records for sales and proceeds. Some highlights:

- Total sales of **\$1.186 billion** were the highest of any fiscal year since inception. Our growth was **4.2%**, compared to industry growth of 3.0%.
- Total education funding of **\$293.5 million** was the highest of any fiscal year since inception. On this key measure we *out-performed* the national lottery industry, growing our Lottery for Education Proceeds by 2.1% and our Total Education Funding by 1.6%. This is compared to overall industry growth of 0.5%.
- Tennessee's instant ticket sales of **\$948.7 million** (an increase of **\$58.5 million**), ranked 8th highest in per capita sales within the industry.
- All of this was accomplished while holding down non-direct expenses — that is, general and administrative expenses, advertising and other gaming — to only **2.4%** of gross sales.

From these record-breaking sales, our players claimed record winnings of more than \$732.1 million. Our retailer partners, now nearly 4,900 strong across the state, earned record commissions exceeding \$77.4 million.

Of course, the biggest winners were the Tennessee students and families who benefited from Lottery-funded scholarships and grants to attend education institutions within the state. More than 100,000 deserving recipients earned such awards last year, making the path to education attainment easier. This is the Lottery's charge and the purpose that drives our efforts.

We invite you to review details of our 2010–2011 Fiscal Year, including the audited financial statements from this record-setting period. And be sure and check our website, [tnlottery.com](http://tnlottery.com); and go to [seehowitaddsup.com](http://seehowitaddsup.com) for more information on how Lottery funds are used.

As always, we remain committed to maximizing dollars for education in Tennessee, welcoming the opportunity to help so many students pursue their dreams. Thank you for your continued support in this effort.



2010–11 Board of Directors: 1st row, L to R:  
Jim Hill, Elizabeth Seigenthaler Courtney  
2nd row, L to R: Garry McNabb, Marvell Mitchell,  
Lowell Perry, Keith Simmons, Jim Ripley

A handwritten signature in black ink, reading "Jim Hill".

Jim Hill, Chair of the Board of Directors

A handwritten signature in black ink, reading "Rebecca Hargrove".

Rebecca Hargrove, President and CEO

## Education Programs


From its inception following the passage of a statewide referendum, the Tennessee Lottery has remained an impressively successful engine to generate funds for education programs. Since Lottery-funded education programs began in the fall of 2004, including the well-known HOPE Scholarship initiative, the General Assembly has expanded eligibility to include 14 programs made up of 11 different scholarships and grants for Tennessee students pursuing higher education.

All Tennessee Education Lottery scholarships and grants are administered by the Tennessee Student Assistance Corporation (TSAC) using funds deposited into the Lottery for Education account. Lottery funds are also used to support other education-related initiatives, such as after-school programs and an ongoing project to make schools more energy efficient. For more information about after-school programs, visit <http://tennessee.gov/education/learningsupport/afterschool/index.shtml> or call 615-253-6037. For information about energy-efficient schools, visit <http://tn.gov/eesi/>.

According to TSAC, approximately **\$297.6 million** in Lottery-funded scholarships was awarded during fiscal year 2010–2011, breaking the previous record set the prior year by more than \$4.6 million. These funds were used to assist more than **100,000 students** at higher education institutions in the state and another **16,400** students in dual enrollment classes.

Details about these recipients include:

(Totals include dual enrollment students)



Board of Regents System (four-year)	27,889
University of Tennessee System	21,077
State Technical/Community Colleges	23,747
Technology Centers	14,424
Independent Four-Year Programs	15,072
Independent Two-Year Programs	8
Private/Business Trade	507
<b>Totals</b>	<b>102,724*</b>

In addition, Lottery funds were used to support 84 after-school programs in the 2010–2011 academic year.

For additional information about Lottery-funded programs, visit [SeeHowItAddsUp.com](http://SeeHowItAddsUp.com).

*\*Note: Totals represent a distinct count of students and are not always a sum of the numbers in the section.*

*Students can attend multiple institutions throughout an academic year, but these students are only counted once in each section total.*

*SOURCE: Tennessee Student Assistance Corporation*

## Games

The Tennessee Lottery introduced a variety of fresh, fun games during 2010–2011, which pushed gross ticket sales to a **record high of \$1.186 billion**.

Instant ticket (“scratch-off”) games remained extremely popular, and the TEL introduced 44 new games from which to choose. Sales for these games increased \$58.4 million (6.6 percent) over the previous fiscal year and accounted for 80 percent of overall ticket sales.

In addition to cash prizes, licensed property games such as *Trucks & Bucks*, *Tennessee Titans*, *Price Is Right*® and *Pac-Man Cash*® offered players the chance to win a variety of merchandise prizes by entering non-winning tickets into second-chance drawings. “Play It Again!”, the Lottery’s program that gives all other non-winning instant tickets a chance to win, continued to attract interest and awarded more than \$2.16 million in prizes during the past fiscal year alone.

Drawing-style games remained popular, as well, and the Lottery introduced Tennessee’s own Tennessee Cash game in October 2010.

Details of all game sales during fiscal year 2010–11 include:

Instant Tickets	\$ 948.7 million
Powerball	\$ 90.4 million
Mega Millions	\$ 45.3 million
Cash 3	\$ 58.1 million
Cash 4	\$ 25.5 million
Tennessee Cash	\$ 16.0 million
Pick 5	\$ 2.5 million

The Lottery also launched a new website, the “VIP Players Suite,” to give Lottery fans more ways to interact with the TEL by playing games, receiving exclusive e-alerts and earning points for a chance to win additional prizes.



## Players and Winners

Not only does every Lottery ticket sold mean a win for education in Tennessee, but it also means a chance for those who play to have fun and win prizes. During fiscal year 2010–2011, players won **\$732.1 million**, bringing the total won since inception to more than **\$4.66 billion**. Of the many winning tickets sold since inception, by the end of the 2010–2011 fiscal year, 78 were worth prizes of \$1 million or more.

Stories of luck and tears of joy are regular sights at the Corporation’s Nashville headquarters, as well as its District Offices and retailer locations throughout the state.

Just a few examples include:



Frances Sharp of Hixson, who won \$2 million playing the instant game *\$2 Million Bonanza*. “At first I thought I had won \$2,000, then I thought it was \$200,000,” said Frances, 69. Finally, when she got home, Frances and her sons learned the win was actually \$2 million — the largest instant prize in Tennessee Lottery history at that time.



For longtime friends Mark Hearon and Josh Caplinger of Alcoa, a “lucky feeling” paid off to the tune of \$1 million. “We just felt lucky,” said Mark, who split the cost of a *Tennessee Millionaires Club* instant ticket with his friend. “This just doesn’t happen to guys like us,” said Josh. “Everyone in the store went crazy!”



And according to Alex Thomas, a cook from Memphis who won \$1 million by playing Powerball, the thrill of winning was nearly matched by the anticipated excitement of getting a chance to “relax for a bit.”

For more information on winners, see our Winners section at [tnlottery.com](http://tnlottery.com).



## Retailers



The Lottery's network of 4,866 dedicated retailers earned more than **\$77.4 million** in commissions and retailer bonuses during the past year, for a total of over **\$509 million** since inception. As the primary contact with players throughout the state, not only do retailers sell the Lottery's products, but they also assist the Corporation by providing valuable feedback about player interest, market trends and frequently asked questions. In turn, Lottery Sales Representatives provide retailers with signage, hands-on training and useful selling tips to make the most of their relationship with the Lottery.



Rej Patel, who owns K&S Market in Lewisburg, enjoys providing a friendly and fun atmosphere for his customers.



James McNinch and Donna Siebrandt at Tobacco Outlet, 3142 S. Perkins in Memphis, enjoy sharing the latest Lottery news and games with their customers.



Bay's Mart 21 in Johnson City is a high-volume, high-energy Lottery retailer that attributes its success to "creativity and teamwork." Pictured is owner Amine Meskel.

The Corporation also maintains a toll-free helpline and website specifically for retailers, distributes a quarterly retailer newsletter and holds regular meetings with its "Retailer Advisory Board." This Board is made up of retailers from across the state who represent all types of trade styles. They share ideas, market trends and ways to assist the Lottery with its charge of maximizing dollars for education programs. Members of the 2010–2011 Board were Terry Roland, Rex Bintz, Adnan "Adam" Mohammad, Asa Hazelwood, Kun "Duke" An, Janet Croxdale, Jimmy Keen, Karim "Kenny" Boghani, Anish "Mike" Najhawan, Tommy Hunt, William "Sonny" Boyce and Roy Wesson.



## Equal Business Opportunity Program

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In addition to its mission of maximizing dollars for education, the Tennessee Education Lottery Corporation is committed to diversity and minority business participation through a variety of programs, including the composition of its workforce. The Corporation also gains valuable insight from its “Advisory Council on Minority Business Participation,” a group of Tennesseans dedicated to helping create strategies to develop and enhance economic development and educational opportunities for minority-owned businesses.

Members of the 2010–2011 Council were Chairman Marvell Mitchell, Elizabeth Courtney, Gwendolyn Davis, Mark Deathridge, Sherrie Gilchrist, Willie Martin, Garry McNabb and A. Gregory Ramos.

As it has every year since inception, the Corporation and its three major procurement vendors exceeded statutory and contractual goals set for its Equal Business Opportunity program during fiscal year 2010–2011. During this period, 28 percent, or \$532,789, of the Lottery’s non-major procurement items were purchased from minority businesses. The Buntin Group, GTECH Corporation and Scientific Games International exceeded their contractual minority business participation goals by paying an average of 25 percent of dollars earned, or more than \$7.6 million, to minority-owned businesses. Details about each major procurement vendor’s revenue earned from the Lottery paid to minority businesses during the past fiscal year include:

The Buntin Group: 24 percent, or \$1,657,000

GTECH: 23 percent, or \$3,126,000

Scientific Games: 29 percent, or \$2,902,000

These vendors support the Corporation’s commitment to diversity in other ways, as well. For example, The Buntin Group, GTECH and Scientific Games continued their sponsorship of and active involvement in the Lottery’s annual Summer Internship Program for students attending the state’s historical black colleges and universities.



The Lottery’s network of 4,866 retailer partners represents an impressive level of diversity, as well. Based on sampling of the retailer contracts, 720 (15%) answered the optional question identifying their minority status. Of the responses received, 179 (24.9%) were Not a Minority, 35 (4.9%) were African-American, 387 (53.8%) were Asian-American, 10 (1.4%) were Hispanic American, 6 (.8%) were Native American, and 103 (14.2%) were Women Owned.

And finally, the Lottery’s diverse workforce continued to represent the community at large. During the 2010–2011 fiscal year, of the 162 employees of the Tennessee Education Lottery Corporation, 51 percent were women; 49 percent were men; 50 percent were minority\*; and 50 percent were non-minority.

\*Minority represents those employees who chose to identify themselves as African-American, Hispanic, American Indian, Alaskan Native, Asian or Pacific Islander, or Other on their employment application.



## Management/Organization

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As set forth in the Lottery Implementation Act, a seven-member Board of Directors, appointed by the Governor and confirmed by the General Assembly, oversees the Tennessee Education Lottery Corporation. The Board provides guidance and oversight, while a team of dedicated professionals is charged with meeting the objectives designed to maximize dollars for education in Tennessee.

Members of the Board of Directors for the 2010–2011 Fiscal Year included:

Jim Hill, Chair, Chattanooga. Term expires June 30, 2011  
Marvell Mitchell, Vice Chair, Memphis. Term expires June 30, 2011  
Lowell Perry Jr., Nashville. Term expires June 30, 2012  
Keith Simmons, Nashville. Term expires June 30, 2013  
Elizabeth Seigenthaler Courtney, Nashville. Term expires June 30, 2013  
Garry McNabb, Cookeville. Term expires June 30, 2014  
Jim Ripley, Sevierville. Term expires June 30, 2014

### **EXECUTIVE DIVISION: Rebecca Hargrove, *President and CEO***

In addition to overseeing the daily operations of the Tennessee Lottery, the President and CEO is responsible for developing a broad vision for the organization and ensuring that strategies to achieve all objectives are implemented.

The Executive Division is also responsible for:

- Advertising strategy—Develops and oversees all advertising initiatives
- Corporate Affairs—Manages internal and external communications, including player services, media/public relations and social media; and Legislative/government affairs, including serving as liaison to state and local government officials.
- Internal Controls—This department reports and works directly with the Board of Directors to ensure adequate internal controls are in place to provide integrity and accountability in the operation of the Lottery through objective analysis.

Tom Jurkovich, Vice President, Corporate Affairs

Khristie Stoecklein, Vice President, Internal Controls (dual reporting to the Board of Directors and the CEO)

### **LEGAL DIVISION: Wanda Young Wilson, *Executive Vice President, General Counsel and Corporate Secretary***

The Legal Division includes:

- Human Resources—Responsible for managing employee and employment-related processes
- Legal Services—Provides legal advice and assistance to management and the Board of Directors, serves as the corporate records keeper, oversees litigation, and manages retailer and vendor contract compliance
- Security—Responsible for physical and intellectual property security
- Retailer Contract Administration—Manages all functions of retailer applications and contracts administration
- Corporate Services—Responsible for daily functions such as mail, reception and supplies

Cynthia Fitzgerald, Vice President, Legal Services for Compliance

David Jennings, Vice President, Security

Craig Miller, Vice President, Human Resources

Andrew Morin, Vice President, Legal Services for Corporate Transactions

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## Management/Organization

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### **SALES AND MARKETING DIVISION: Sidney Chambers, *Executive Vice President***

The Sales and Marketing Division oversees all aspects of the Lottery sales operation, including:

- Sales and marketing—Manages all sales activity and field marketing
- Retailer sales and services—Provides all facets of customer service for retailer network
- Corporate accounts—Manages corporate accounts
- Promotions and special events—Promotes the TEL at a variety of functions throughout the state
- Warehouse management and distribution
- District offices—Manages the TEL's four District offices

Joe Hills, Vice President, Sales

### **FINANCE AND INFORMATION SYSTEMS: Andy Davis, *Chief Financial and Information Systems Officer***

Finance and Information Systems is responsible for the following:

- Financial, product and retailer accounting
- Prize validation, statutory and financial reporting
- Cash management, budgeting, accounts receivables
- Procurement, facilities management and risk services
- Game drawings, including online and second-chance drawing activities
- Gaming systems and operations oversight
- Telecommunication, networking and software systems

Lucretia Kirk, Vice President, Information Systems

Vicki Updike, Vice President, Finance





STATE OF TENNESSEE  
**COMPTROLLER OF THE TREASURY**  
DEPARTMENT OF AUDIT  
DIVISION OF STATE AUDIT  
SUITE 1500  
JAMES K. POLK STATE OFFICE BUILDING  
NASHVILLE, TENNESSEE 37243-1402  
PHONE (615) 401-7897  
FAX (615) 532-2765

**Independent Auditor's Report**

November 17, 2011

The Honorable Bill Haslam, Governor  
and  
Members of the General Assembly  
State Capitol  
Nashville, Tennessee 37243  
and  
Board of Directors  
Tennessee Education Lottery Corporation  
Plaza Tower Metro Center  
200 Athens Way  
Nashville, TN 37228

Ladies and Gentlemen:

We have audited the accompanying statements of net assets of the Tennessee Education Lottery Corporation, a component unit of the State of Tennessee, as of June 30, 2011, and June 30, 2010, and the related statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the corporation's management. Our responsibility is to express an opinion on these financial statements, based on our audits.

## Auditor's Opinion Letter

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Tennessee Education Lottery Corporation as of June 30, 2011, and June 30, 2010, and the changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis, as listed in the table of contents, is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with generally accepted government auditing standards, we have also issued our report dated November 17, 2011, on our consideration of the corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be considered in assessing the results of our audit.

Sincerely,



Arthur A. Hayes, Jr., CPA  
Director

AAH/rs

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## Financials

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and Changes in Net Assets
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## Management's Discussion and Analysis

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The Tennessee Education Lottery Corporation ("TEL") offers the following Management Discussion and Analysis ("MD&A") to the readers of the financial statements. This narrative overview provides an objective analysis of the TEL's financial activity for the fiscal years ended June 30, 2011 and 2010, with comparative information presented for the fiscal year ended June 30, 2009. The overview should be considered in conjunction with the independent auditor's report, the accompanying audited financial statements and notes to the financial statements.

### UNDERSTANDING THE TEL'S FINANCIAL STATEMENTS

The TEL, a quasi-public instrumentality, is a component unit of the State of Tennessee. The TEL's activities are accounted for as a business-type activity using the full accrual basis of accounting, similar to a private business entity. In accordance with accounting principles generally accepted in the United States of America, this report consists of a series of comparative financial statements, along with notes to the financial statements designed to highlight the TEL's net assets and changes therein resulting from business operations.

The financial statements are comprised of three components:

- The Statements of Net Assets – Reflects the TEL's financial position at June 30, 2011 and June 30, 2010.
- The Statements of Revenues, Expenses, and Changes in Net Assets – Reports revenues and expenses incurred in relation to the sale of lottery products, as well as other non-gaming related activity for the fiscal years ended June 30, 2011 and June 30, 2010.
- The Statements of Cash Flows – Outlines the cash inflows and outflows related to the activity of selling lottery products and other business related activities for the fiscal years ended June 30, 2011 and June 30, 2010.

The Notes to the Financial Statements document additional information essential for readers to gain a comprehensive understanding of the data provided in the TEL's financial statements.

The TEL's primary business purpose is to generate revenues to fund college scholarships for residential Tennessee students attending higher educational institutions within the state. Accordingly, the main focus of the financial statements is determining funds available for payment to the State of Tennessee's Lottery for Education Account. Furthermore, in addition to funding this account, the TEL's unclaimed prize funds are deposited to the After-School Programs special account which benefits after-school programs throughout the state of Tennessee.

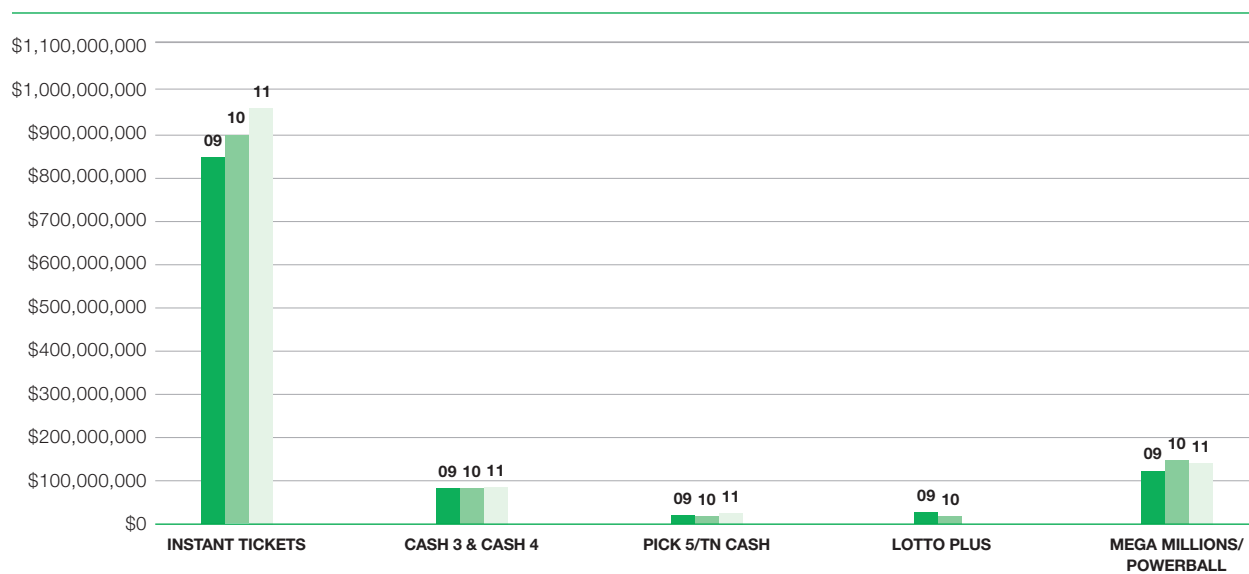
### FISCAL YEAR 2011 FINANCIAL HIGHLIGHTS

Despite the challenges of a sluggish economy, the TEL set a new record for the fiscal year ended June 30, 2011, raising an all-time high of \$293.5 million for education programs in the state of Tennessee. An increase of \$4.6 million over last year's record transfer, this brings the total generated for education since ticket sales began in January 2004, to \$2.07 billion!

Driving this increase in funds transferred to education was another record-setting achievement of nearly \$1.2 billion in total gross sales. This marked an impressive \$48.3 million (4.2%) increase over the previous fiscal year, not to mention the fifth straight year that the TEL has reached gross sales of over \$1 billion. Overall, total gross ticket sales since inception have surpassed a substantial \$7.8 billion!

## Management's Discussion and Analysis

### TENNESSEE EDUCATION LOTTERY GROSS TICKET REVENUES FISCAL YEAR 2011 COMPARISON TO 2010 AND 2009



As in recent prior years, upward movement in instant ticket sales was the primary factor fueling our sales growth. Management attributes this to the effectiveness of its instant ticket marketing strategy which emphasizes offering more, as well as a broader spectrum of games and prizes to lottery players. Accordingly, the TEL continued to launch new instant ticket games at varying price points during each month of fiscal year 2011. As added variety to its traditionally themed games, the TEL also introduced several licensed property games [i.e., *Trucks & Bucks* (\$5), *The Price Is Right* (\$5), *Tennessee Titans* (\$5) and *Orange Crush* (\$2)] and spotlight games [i.e., *\$2 Million Bonanza* (\$20), and *Lottery TN Black* (\$10)]. In February 2011, the TEL added *Lady Jumbo Bucks* (\$3) to the popular “*Jumbo Bucks*” family of instant ticket games. Additionally, available prizes, varying among a wide range of cash and non-cash prizes (automobiles, destination trips offering more prize-winning opportunities, season tickets, etc.), increased by \$36.1 million (6.7%). Ultimately, under this promotional approach, annual instant ticket sales were up by over \$58.4 million (6.6%).

Cash 3 and Cash 4 sales in fiscal year 2011 remained relatively consistent with those of fiscal year 2010.

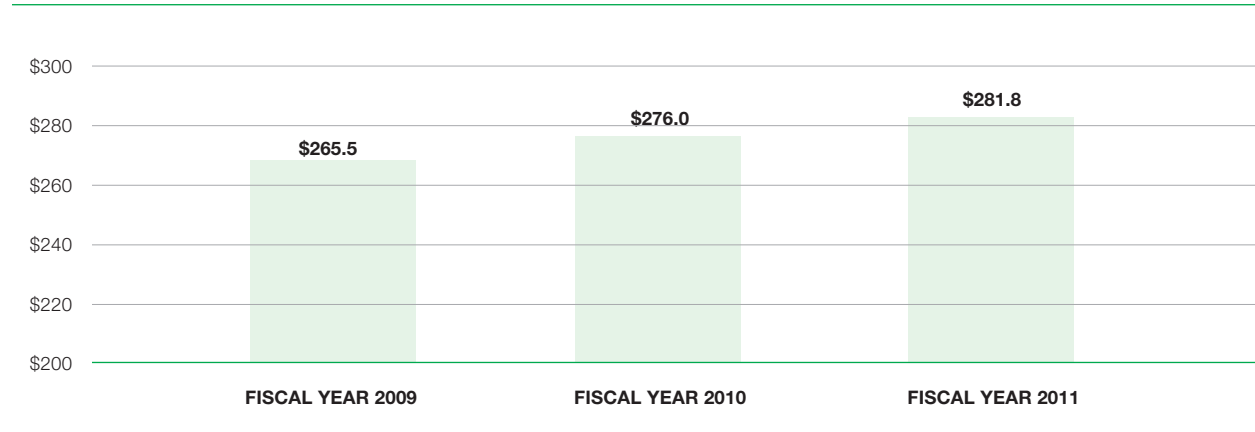
In October 2010, Pick 5 was discontinued and replaced with the new in-state, cash jackpot game, Tennessee Cash. The Tennessee Cash game gives players an additional opportunity to win prizes as well as offering higher average jackpot payouts than its predecessor. As a result of this change, combined Pick 5 and Tennessee Cash gross ticket sales grew to \$18.5 million from the prior year's Pick 5 gross ticket sales of \$11.9 million – a \$6.6 million (55.5%) increase.

In January 2010, the TEL ended the Lotto Plus game in order to shift focus to the January 31st introduction of the multijurisdictional jackpot game, Mega Millions. Along with Powerball, this game gives Tennessee players the opportunity to play large jackpot games four times each week. Both Mega Millions and Powerball sales are driven by the size of jackpots; specifically, as the jackpot increases, ticket sales tend to trend upwards as well. Sales for Powerball declined in 2011 by 30%. This decrease is directly related to lower average jackpots compared to fiscal year 2010. Mega Millions sales were \$45.3 million in 2011, and were driven by two jackpot cycles exceeding \$300 million.

The TEL generated \$281.8 million for the Lottery for Education Account in fiscal year 2011, compared to \$276.0 million in fiscal year 2010 and \$265.5 million in fiscal year 2009.

## Management's Discussion and Analysis

### TENNESSEE EDUCATION LOTTERY PROCEEDS FOR THE LOTTERY FOR EDUCATION ACCOUNT (IN MILLIONS)

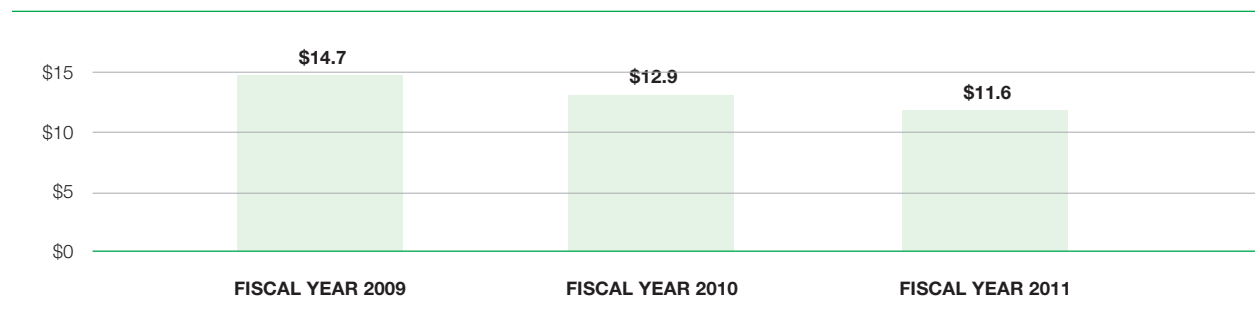


The amounts deposited to the After-School Programs special account are derived from unclaimed instant and online draw game prizes at fiscal year end. Prizes not claimed within 90 days of the announced game-end date for instant games, and within 180 days for all terminal-based online games, are forfeited as unclaimed prizes.

The TEL records estimated unclaimed prizes for each instant game within the month the game is closed and reconciles the actual amounts when the claim period ends. For terminal-based online games, the TEL records the actual unclaimed amounts determined after the expiration of the related claim period for the draw.

In fiscal year 2011, the TEL recognized \$11.6 million for the After-School Programs special account as compared to \$12.9 million in fiscal year 2010, and \$14.7 million in fiscal year 2009.

### TENNESSEE EDUCATION LOTTERY PROCEEDS FOR THE AFTER-SCHOOL PROGRAMS ACCOUNT (IN MILLIONS)



## Management's Discussion and Analysis

### CONDENSED STATEMENT OF NET ASSETS

Assets	JUNE 30, 2011	INCREASE/ (DECREASE)	JUNE 30, 2010	INCREASE/ (DECREASE)	JUNE 30, 2009
<i>Current assets</i>					
Cash	\$ 66,414,000	\$ (1,908,000)	\$ 68,322,000	\$ 651,000	\$ 67,671,000
Retailer accounts receivable, net	53,510,000	5,804,000	47,706,000	4,999,000	42,707,000
Other	7,008,000	521,000	6,487,000	(9,000)	6,496,000
Total current assets	126,932,000	4,417,000	122,515,000	5,641,000	116,874,000
<i>Non-current assets</i>					
Other	2,345,000	48,000	2,297,000	(207,000)	2,504,000
Capital assets, net	1,020,000	(339,000)	1,359,000	(363,000)	1,722,000
Total non-current assets	3,365,000	(291,000)	3,656,000	(570,000)	4,226,000
<b>Total assets</b>	<b>130,297,000</b>	<b>4,126,000</b>	<b>126,171,000</b>	<b>5,071,000</b>	<b>121,100,000</b>
<i>Liabilities</i>					
<i>Current liabilities</i>					
Due to Lottery for Education Account	70,281,000	(1,385,000)	71,666,000	4,002,000	67,664,000
Due to After-School Programs Account	11,644,000	(1,250,000)	12,894,000	(1,772,000)	14,666,000
Prizes payable	40,897,000	6,595,000	34,302,000	2,355,000	31,947,000
Accounts payable and accrued liabilities	3,632,000	(27,000)	3,659,000	1,155,000	2,504,000
Deferred liabilities	992,000	226,000	766,000	(345,000)	1,111,000
Total current liabilities	127,446,000	4,159,000	123,287,000	5,395,000	117,892,000
<i>Non-current liabilities</i>					
Non-current portion of other liabilities	2,850,000	(27,000)	2,877,000	(331,000)	3,208,000
Total non-current liabilities	2,850,000	(27,000)	2,877,000	(331,000)	3,208,000
<b>Total liabilities</b>	<b>130,296,000</b>	<b>4,132,000</b>	<b>126,164,000</b>	<b>5,064,000</b>	<b>121,100,000</b>
<i>Net Assets</i>					
Investment in capital assets	1,020,000	(339,000)	1,359,000	(363,000)	1,722,000
Unrestricted assets	(1,020,000)	339,000	(1,359,000)	363,000	(1,722,000)
Restricted assets	1,000	(6,000)	7,000	7,000	-
<b>Total net assets</b>	<b>\$ 1,000</b>	<b>\$ (6,000)</b>	<b>\$ 7,000</b>	<b>\$ 7,000</b>	<b>\$ -</b>

### OVERVIEW OF FINANCIAL POSITION

**ASSETS:** The \$4.13 million increase in total assets at June 30, 2011, and the \$5.07 million increase in total assets at June 30, 2010, were primarily due to the noted increase in lottery ticket sales for the related fiscal years and the subsequent timing of collection of the relevant Retailer Accounts Receivable balances.

## Management's Discussion and Analysis

**LIABILITIES:** The \$4.13 million increase in total liabilities at June 30, 2011, relates primarily to increased fiscal year sales and thus accordingly, more prizes payable to players.

The \$5.06 million increase in total liabilities at June 30, 2010, related primarily to increased fiscal year 2010 ticket sales, resulting in higher net proceeds payable to the Lottery for Education Account, and more prizes payable to players.

### CONDENSED STATEMENT OF REVENUES & EXPENSES

	JUNE 30, 2011	INCREASE/ (DECREASE)	JUNE 30, 2010	INCREASE/ (DECREASE)	JUNE 30, 2009
<i>Revenues:</i>					
Instant games	\$ 948,710,000	\$ 58,437,000	\$ 890,273,000	\$ 48,901,000	\$ 841,372,000
Online games	237,847,000	(10,270,000)	248,117,000	1,604,000	246,513,000
Less instant/promotional tickets provided as prizes	(83,978,000)	(6,068,000)	(77,910,000)	(5,457,000)	(72,453,000)
<b>Games revenue, net</b>	<b>1,102,579,000</b>	<b>42,099,000</b>	<b>1,060,480,000</b>	<b>45,048,000</b>	<b>1,015,432,000</b>
Bad debt recoveries/(expense), net	(239,000)	135,000	(374,000)	122,000	(496,000)
Retailer service fees	3,396,000	(14,000)	3,410,000	143,000	3,267,000
Interest income	110,000	(101,000)	211,000	(1,052,000)	1,263,000
Other revenue	639,000	143,000	496,000	(146,000)	642,000
<b>Total revenues</b>	<b>1,106,485,000</b>	<b>42,262,000</b>	<b>1,064,223,000</b>	<b>44,115,000</b>	<b>1,020,108,000</b>
<i>Expenses:</i>					
Cost of sales	797,490,000	36,951,000	760,539,000	35,717,000	724,822,000
General, administrative and other operating expenses	15,461,000	695,000	14,766,000	(335,000)	15,101,000
Other expenses	50,000	12,000	38,000	(92,000)	130,000
Proceeds to After-School Program Account	11,644,000	(1,250,000)	12,894,000	(1,772,000)	14,666,000
Proceeds to Lottery for Education Account	281,846,000	5,867,000	275,979,000	10,493,000	265,486,000
<b>Total expenses</b>	<b>1,106,491,000</b>	<b>42,275,000</b>	<b>1,064,216,000</b>	<b>44,011,000</b>	<b>1,020,205,000</b>
Change in net assets	(6,000)	(13,000)	7,000	104,000	(97,000)
Total net assets, beginning of year	7,000	7,000	-	(97,000)	97,000
<b>Total net assets, end of year</b>	<b>\$ 1,000</b>	<b>\$ (6,000)</b>	<b>\$ 7,000</b>	<b>\$ 7,000</b>	<b>\$ -</b>

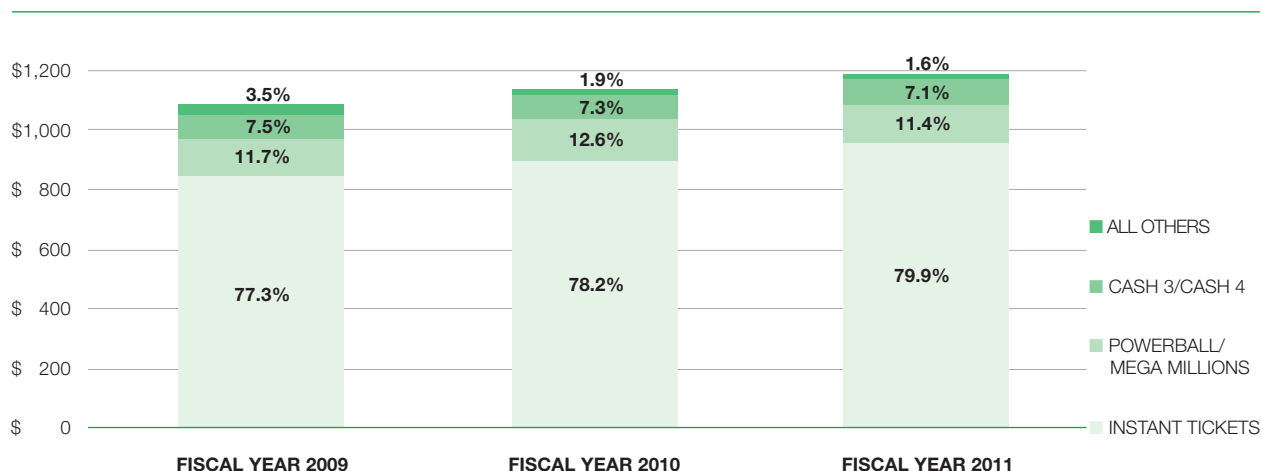


## Management's Discussion and Analysis

### REVENUES

Gross lottery ticket sales for the fiscal years ended June 30, 2011, 2010, and 2009 were \$1.187 billion, \$1.138 billion, and \$1.088 billion, respectively. The following chart depicts the distribution of sales by product for the three fiscal years ended June 30:

**TENNESSEE EDUCATION LOTTERY  
SALES BY MAJOR PRODUCT PER FISCAL YEAR  
(IN MILLIONS)**



**GROSS INSTANT TICKET** sales for 2011 grew to \$948.7 million, which represents a 6.6% increase over 2010 instant ticket sales of \$890.3 million. Gross instant ticket sales for 2010 of \$890.3 million represented a 5.8% increase over 2009 instant sales of \$841.4 million. Instant tickets represent approximately 80% of total gross sales in fiscal year 2011, approximately 78% in 2010 and approximately 77% in 2009. The year over year increase in gross instant ticket sales is attributed to the instant ticket marketing strategy, which involves ongoing introduction of multiple games, including special themed games, and higher price point games with higher prize payouts. The games most popular with the players in 2011 were *Jumbo Bucks*, *Giant Jumbo Bucks*, *Junior Jumbo Bucks*, *Millionaire Jumbo Bucks*, *Lady Jumbo Bucks*, *Lucky 7's* and *Tennessee Millionaire's Club*.

**POWERBALL** sales for the fiscal years 2011, 2010, and 2009 were \$90.4 million, \$127.9 million, and \$126.7 million, respectively. These amounts represent approximately 8%, 11%, and 12% of gross ticket sales, respectively, for each fiscal year.

Powerball is a multi-jurisdictional lottery game operated in the following jurisdictions in addition to Tennessee; Arizona, Arkansas, Colorado, Connecticut, Delaware, District of Columbia, Florida, Idaho, Iowa, Indiana, Kansas, Kentucky, Louisiana, Maine, Minnesota, Missouri, Montana, Nebraska, New Hampshire, New Mexico, North Carolina, North Dakota, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, South Dakota, US Virgin Islands, Vermont, Wisconsin, and West Virginia. On January 31, 2010, Powerball began cross-selling tickets in 10 Mega Millions states. Those states were Georgia, Illinois, Maryland, Massachusetts, Michigan, New Jersey, New York, Texas, Virginia, and Washington.

## Management's Discussion and Analysis

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**MEGA MILLIONS** is a multi-jurisdictional lottery game administered by a lottery consortium group. The group includes the following state lotteries: California, Georgia, Illinois, Maryland, Massachusetts, Michigan, New Jersey, New York, Ohio, Texas, Virginia, and Washington. Tennessee and certain other MUSL lottery members are authorized to sell the Mega Millions game by the consortium as part of a cross-sell agreement. Tennessee began sales for the game in January 2010. Sales for fiscal years 2011, and 2010 were \$45.3 million, and \$15.9 million. This amount represents 4% and 1% of gross ticket sales, respectively for each of the fiscal years 2011 and 2010.

**CASH 3** sales for fiscal years 2011, 2010, and 2009 were \$58.1 million, \$57.2 million, and \$57.2 million. These amounts represent approximately 5% of gross ticket sales, respectively for each of the noted fiscal years.

**CASH 4** sales were \$25.5 million, \$25.6 million, and \$24.5 million in the years 2011, 2010, and 2009, respectively. These amounts represent approximately 2% of gross ticket sales for each of the noted fiscal years.

**TENNESSEE CASH**, an online, jackpot driven game, was introduced on October 3, 2010. Ticket sales for 2011 were \$16 million.

**PICK 5** sales were \$2.5 million, \$11.9 million and \$13.9 million in the years 2011, 2010, and 2009, respectively. The significant decrease in fiscal year 2011 sales is reflective of the discontinuance of the game in October 2010. The \$2 million decrease in 2010 sales compared to 2009 sales was attributable to smaller jackpot cycles occurring in fiscal year 2009 as compared to the prior year.

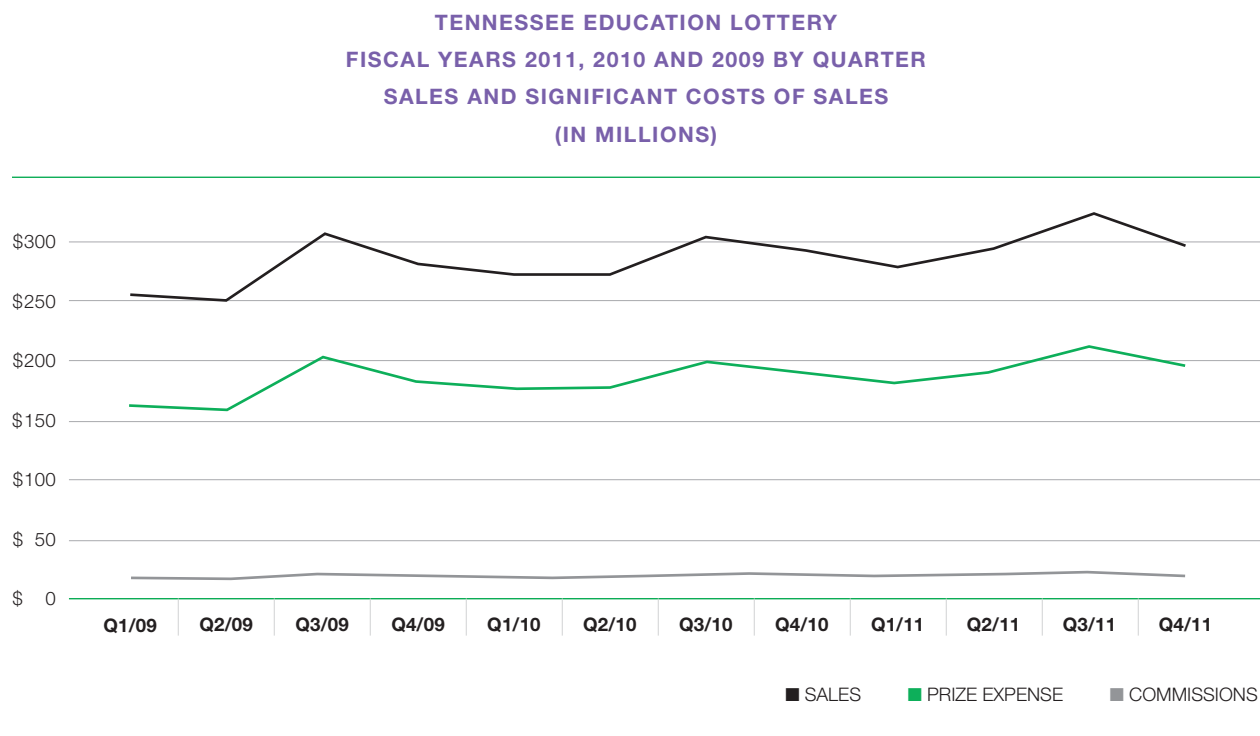
**LOTTO PLUS**, a TEL online game, was ended in January 2010, due to the declining profitability and the conflicting draw schedule with Mega Millions. Sales were \$9.5 million and \$23.4 million in 2010 and 2009, respectively.

**HOT TRAX CHAMPIONS** sales were \$793 thousand in 2009. This game was discontinued on December 31, 2008 due to declining sales and limited retailer support.

## Management's Discussion and Analysis

### COST OF SALES

Cost of sales is comprised of prize expense net of unclaimed prizes, retailer commissions, contractor fees, and other marketing costs. As the following chart depicts, these expenses are relational to and change in direct proportion with changes in ticket sales:



Gross prize expense was \$695.1 million, \$664.0 million and \$633.3 million in the years 2011, 2010 and 2009, respectively. Increases of \$31.1 million in 2011 and \$30.71 million in 2010 are reflective of the increases in overall ticket sales realized in the related period.

Instant games prize expense is managed through the number of tickets printed for each game and value of prizes as determined prior to ticket production. Prize expense is recorded based on an established prize structure and related percentage of sales for each game introduced, and is recognized when products are made available for sale to the public. The aggregated prize payout for all instant games was 66.6%, 66.4%, and 66.1% of instant game sales, net of free tickets for 2011, 2010, and 2009, respectively.

Gross prize expense for online games generally increases or decreases in direct proportion to ticket sales of the related game and is recorded at the time of the related draw. The aggregated prize payout for all online drawing style games were 50.2%, 50.1%, and 50.6% for 2011, 2010, and 2009, respectively.

Retailer commissions were \$77.5 million, \$74.3 million, and \$71.0 million for the years ended June 30, 2011, 2010, and 2009, respectively. Consistent with the cost driver relationship of ticket sales to retailer commissions, the increases of \$3.2 million in 2011, and \$3.3 million in 2010, are reflective of the increases in overall ticket sales realized in the related period.

## Management's Discussion and Analysis

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Retailers are compensated a set commission percentage of 6.5% on all instant tickets settled and online tickets sold. They also receive an additional 1% bonus for cashing Cash 3 and Cash 4 ticket prizes. Additionally, the TEL will pay a bonus of \$25,000 to a retailer who sells a single jackpot winning ticket for Powerball or Mega Millions; however, if there are multiple winning Powerball or Mega Millions jackpot winning tickets sold in Tennessee in a single drawing, the \$25,000 selling bonus will be proportionately divided among the respective retailers based on the number of winning tickets sold by the retailer. The TEL will also pay a \$5,000 bonus to retailers selling any online game ticket where the prize won is equal to or greater than \$1 million. No Powerball or Mega Millions jackpot ticket selling bonuses were paid during the last three fiscal years. Online game ticket selling bonuses equaling \$50,000, \$60,000, and \$45,000 were awarded for fiscal years 2011, 2010, and 2009, respectively.

Contractor fees for fiscal years 2011, 2010, and 2009, were \$23.8 million, \$22.6 million and \$22.0 million, respectively. The TEL has retained two contractors for the operation of its online gaming network and the manufacturing, warehousing and distribution of its instant ticket games. As compensation, the instant ticket vendor receives a contractually negotiated fee on the selling price of all instant ticket activations, whereas the online gaming vendor receives a contractually negotiated fee on the selling price of online tickets sold, and on instant ticket activations net of free instant tickets available as prizes.

Effective April 1, 2009, the instant ticket gaming contract was renegotiated to extend through April 9, 2015, and also to include a reduction of the contractor service fee from 1.139% to 1.07%. For fiscal years 2011 and 2010, the related contractor was compensated at the rate of 1.07%. The fee received for fiscal year 2009 was 1.139% for the fiscal period July 1, 2008 through March 31, 2009, and 1.07% for the fiscal period April 1, 2009 to June 30, 2009.

For fiscal years 2011, 2010 and 2009, the online gaming contractor was compensated at the rate of 1.24% of ticket sales. For fiscal year 2009, the contractor also earned an additional .6% on Hot Trax Champions ticket sales. Additionally, effective March 3, 2009, this contract was renegotiated to extend through April 9, 2015. Terms of this contract include the continuation of the contractor fee at 1.24%, as well as this vendor's agreement to provide, install and maintain up to eight hundred (800) instant ticket vending machines (ITVMs) for the TEL.

Advertising costs incurred by the TEL were \$9.4 million, \$9.4 million, and \$10.5 million for the fiscal years 2011, 2010, and 2009, respectively. These costs are significantly influenced by budget directives and constraints, as well as correlated to sales revenue. On a continuous basis, management strives to achieve an optimal balance between these costs and obtained benefits while keeping these costs relatively consistent with prior year amounts. As such, 2011 and 2010 amounts reflect continuation of the TEL's cost-saving initiatives implemented subsequent to fiscal year 2009.

### **GENERAL, ADMINISTRATIVE AND OTHER OPERATING EXPENSES**

General, administrative, and other operating expenses were \$15.46 million, \$14.80 million, and \$15.23 million for the fiscal years 2011, 2010, and 2009, respectively. For each of these years, the five (5) major expense components were depreciation, personnel, professional fees, property and telecommunications expenses. These expenses do not change in direct proportion with revenues, but are instead significantly influenced by budget directives and constraints, and current business and economic conditions. In view of these factors, moderate variances in these expenses are expected to occur over fiscal periods. Nevertheless, to the most reasonable extent possible, TEL's management team works diligently to control these expenses to relatively consistent year over year amounts.

## Management's Discussion and Analysis

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### POTENTIAL FACTORS IMPACTING FUTURE RESULTS

The TEL's mission is to maximize revenues for the purpose of maximizing payments to the Lottery for Education Account. A continuous assessment of Tennessee's economic environment and the TEL's own product lines and operations are essential to accomplish this mission. The following considerations have been presented to inform those interested in the TEL's operations about factors that could potentially affect future results:

- The TEL will continue to implement promotional offerings to improve brand awareness and increase player participation in our games.
- The TEL will continue to introduce new and/or enhanced instant and online game product offerings, as well as consider the expansion of our licensed property games that are gaining nationwide popularity.
- The TEL will continually review the prize payout percentages for its instant game products to ensure we are receiving the highest actual net proceeds for each game and/or price point category.

### CONTACTING THE TEL'S FINANCIAL MANAGEMENT

This financial report is designed to provide the State of Tennessee, the public, and other interested parties with an overview of the financial results of the TEL's activities and to show the TEL's accountability for conducting business in a fiscally responsible manner. If you have questions about this report or require additional financial information, contact the TEL's Finance Department at the following address:

#### Tennessee Education Lottery Corporation

Plaza Tower Metro Center  
200 Athens Way, Suite 200  
Nashville, Tennessee 37228



**TENNESSEE EDUCATION LOTTERY CORPORATION**  
**STATEMENTS OF NET ASSETS**  
**AS OF JUNE 30, 2011 AND JUNE 30, 2010**

<b>ASSETS</b>	<b>JUNE 30, 2011</b>	<b>JUNE 30, 2010</b>
<b>CURRENT ASSETS</b>		
Cash (Note 2)	\$ 66,413,000	\$ 68,315,000
Restricted fidelity fund cash	1,000	7,000
Retailer accounts receivable, net	53,510,000	47,706,000
Prepaid expenses and other assets	6,904,000	6,383,000
Prize annuity investments (Note 3)	104,000	104,000
Total current assets	126,932,000	122,515,000
<b>NON-CURRENT ASSETS</b>		
Prepaid expenses and other assets	35,000	56,000
Prize annuity investments (Note 3)	2,310,000	2,241,000
Capital assets, net of depreciation of \$4,149,000 and \$3,802,000 (Note 4)	1,020,000	1,359,000
Total noncurrent assets	3,365,000	3,656,000
<b>TOTAL ASSETS</b>	<b>130,297,000</b>	<b>126,171,000</b>
<b>LIABILITIES</b>		
<b>CURRENT LIABILITIES</b>		
Due to Lottery for Education Account (Note 7)	70,281,000	71,666,000
Due to After-School Programs Account (Note 8)	11,644,000	12,894,000
Prizes payable	40,793,000	34,198,000
Accounts payable	173,000	50,000
Prize annuities payable (Note 3)	104,000	104,000
Accrued liabilities	3,459,000	3,609,000
Deferred rent (Note 6)	61,000	61,000
Deferred revenue	931,000	705,000
Total current liabilities	127,446,000	123,287,000
<b>NON-CURRENT LIABILITIES</b>		
Prize annuities payable (Note 3)	2,310,000	2,241,000
Accrued liabilities (Note 10)	181,000	119,000
Deferred rent (Note 6)	359,000	517,000
Total non-current liabilities	2,850,000	2,877,000
<b>TOTAL LIABILITIES</b>	<b>130,296,000</b>	<b>126,164,000</b>
<b>NET ASSETS</b>		
Investment in capital assets	1,020,000	1,359,000
Unrestricted assets:		
Capital assets	(1,020,000)	(1,359,000)
Restricted assets:		
Restricted for uncollectible retailer receivables	1,000	7,000
<b>TOTAL NET ASSETS</b>	<b>\$ 1,000</b>	<b>\$ 7,000</b>

See notes to financial statements.

**TENNESSEE EDUCATION LOTTERY CORPORATION**  
**STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS**  
**FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010**

	<b>JUNE 30, 2011</b>	<b>JUNE 30, 2010</b>
<b>OPERATING REVENUES</b>		
Ticket sales, net	\$ 1,186,318,000	\$ 1,138,016,000
Less tickets provided as prizes	(83,978,000)	(77,910,000)
Net ticket sales	1,102,340,000	1,060,106,000
Retailer service fees	3,396,000	3,410,000
Other	594,000	451,000
Net operating revenues	1,106,330,000	1,063,967,000
<b>OPERATING EXPENSES</b>		
Available prizes	695,149,000	664,042,000
Current year actual unclaimed prizes (Note 8)	(11,644,000)	(12,894,000)
Net prizes	683,505,000	651,148,000
Retailer commissions and bonuses	77,457,000	74,331,000
Contractor fees	23,794,000	22,638,000
Advertising	9,393,000	9,378,000
Salaries and benefits	11,755,000	11,134,000
Retailer merchandising and marketing	3,341,000	3,044,000
Rent, utilities, and maintenance	1,659,000	1,730,000
Depreciation	740,000	769,000
Professional fees	346,000	262,000
General administrative and other operating	961,000	871,000
Total operating expenses	812,951,000	775,305,000
Operating income	293,379,000	288,662,000
<b>NONOPERATING REVENUES (EXPENSES)</b>		
Interest revenue	110,000	211,000
Retailer fees for future uncollectible retailer receivables	45,000	45,000
Fidelity fund retailer non-feasance recoupments (Note 1)	(50,000)	(38,000)
Proceeds to After-School Programs Account (Note 8)	(11,644,000)	(12,894,000)
Proceeds to Lottery for Education Account (Note 7)	(281,846,000)	(275,979,000)
Total nonoperating revenues (expenses)	(293,385,000)	(288,655,000)
Change in Net Assets	(6,000)	7,000
NET ASSETS, beginning of year	7,000	-
NET ASSETS, end of year	\$ 1,000	\$ 7,000

See notes to financial statements.

**TENNESSEE EDUCATION LOTTERY CORPORATION**  
**STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010**

	JUNE 30, 2011	JUNE 30, 2010
OPERATING ACTIVITIES		
Cash received from customers	\$ 1,096,798,000	\$ 1,054,805,000
Other operating cash received	3,934,000	3,815,000
Cash paid for prizes	(677,295,000)	(648,850,000)
Cash paid to/on behalf of gaming vendors	(23,701,000)	(22,567,000)
Cash paid to retailers	(77,467,000)	(74,304,000)
Cash paid for advertising	(9,938,000)	(8,554,000)
Cash paid to/on behalf of employees	(11,563,000)	(10,898,000)
Other operating payments	(6,285,000)	(5,992,000)
Net cash provided by operating activities	294,483,000	287,455,000
NONCAPITAL FINANCING ACTIVITIES		
Payments to Lottery for Education Account	(283,231,000)	(271,977,000)
Payments to After-School Programs Account	(12,894,000)	(14,666,000)
Fidelity fund cash received from retailers	50,000	49,000
Fidelity fund cash refunded to retailers	(6,000)	(4,000)
Fidelity fund cash non-feasance recoupments	(50,000)	(38,000)
Net cash used in noncapital financing activities	(296,131,000)	(286,636,000)
CAPITAL AND RELATED FINANCING ACTIVITIES		
Purchase of property and equipment	(409,000)	(406,000)
Proceeds from disposal of capital assets	39,000	27,000
Net cash used in capital and related financing activities	(370,000)	(379,000)
INVESTING ACTIVITIES		
Interest income	110,000	211,000
Net cash provided by investing activities	110,000	211,000
NET CASH (USED IN)/PROVIDED BY ALL ACTIVITIES	(1,908,000)	651,000
CASH at beginning of year	68,322,000	67,671,000
CASH at end of year	66,414,000	68,322,000
<b>Reconciliation of cash on the statement of net assets</b>		
Cash	\$ 66,413,000	\$ 68,315,000
Restricted fidelity fund cash	1,000	7,000
Cash at end of year	\$ 66,414,000	\$ 68,322,000

See notes to financial statements.

**TENNESSEE EDUCATION LOTTERY CORPORATION**  
**STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010**

**RECONCILIATION OF NET OPERATING INCOME TO**  
**NET CASH PROVIDED BY OPERATING ACTIVITIES**

	JUNE 30, 2011	JUNE 30, 2010
Operating income	\$ 293,379,000	\$ 288,662,000
Adjustments to reconcile operating income to net cash provided by operating activities:		
Bad debt expense	239,000	374,000
Depreciation	740,000	769,000
Gain on disposal of capital assets	(34,000)	(25,000)
Changes in assets and liabilities:		
Retailer accounts receivable	(6,044,000)	(5,372,000)
Prepays and other assets	(500,000)	29,000
Accounts payable and accrued liabilities	40,000	1,166,000
Prizes payable	6,595,000	2,355,000
Deferred rent	(158,000)	(158,000)
Deferred revenue	226,000	(345,000)
Net cash provided by operating activities	\$ 294,483,000	\$ 287,455,000
<b>NONCASH INVESTING ACTIVITIES</b>		
Increase/(Decrease) in fair value of prize annuity investments	\$ 225,000	\$ (31,000)

See notes to financial statements.

# Notes to the Financial Statements (As of and for the Years Ended June 30, 2011 and June 30, 2010)

## (1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**ORGANIZATION AND DESCRIPTION OF REPORTING ENTITY** — Effective June 11, 2003, the Tennessee Education Lottery Implementation Law (the “Act”), Tennessee Code Annotated §§ 4-51-101, et.seq., was signed into law, creating the Tennessee Education Lottery Corporation (the “TEL”). Pursuant with the Act, the TEL was incorporated in the State of Tennessee as a body, politic and corporate, and a quasi-public instrumentality.

The TEL is considered a component unit of the State of Tennessee as the state has financial accountability for fiscal matters as follows:

1. The board of directors is appointed by the governor;
2. Upon dissolution of the TEL, title to all TEL property shall vest in the State of Tennessee; and
3. The TEL provides financial benefits to the state in the form of deposit payments to the state treasury.

The accompanying financial statements present information only as to the transactions of the programs of the TEL. The TEL is reported as a discretely presented component unit within the State of Tennessee’s *Comprehensive Annual Financial Report*, which may be viewed at <http://tennessee.gov/finance/act/cafr.html>.

The TEL is responsible for the provision of lotteries on behalf of the State of Tennessee in accordance with the Act and is deemed to be acting, in all respects, for the benefit of the people of the State of Tennessee.

On January 20, 2004, the TEL began lottery ticket sales. During the years ended June 30, 2011 and 2010, the TEL’s lottery sales included a variety of instant ticket games and online, terminal-based, ticket games: Cash 3, Cash 4, Pick 5, Lotto Plus, Tennessee Cash, Powerball, and Mega Millions. Effective January 31, 2010, Lotto Plus was ended, and Mega Millions, a multi-state jackpot game, was added to the TEL’s online game offerings. Also, on October 1, 2010, Pick 5 was discontinued and replaced with the in-state jackpot game, Tennessee Cash.

**BASIS OF PRESENTATION** – The accompanying financial statements have been prepared in conformity with the accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board. Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in the financial statements to the extent those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. The TEL has elected to follow subsequent private-sector guidance subject to this same limitation.

**BASIS OF ACCOUNTING AND MEASUREMENT FOCUS** – Basis of accounting refers to the timing of recognition of revenues and expenses in the accounts and reporting in the financial statements, and the measurement focus refers to what transactions and events should be recorded. The financial statements are reported using the accrual basis of accounting and the economic resources measurement focus in accordance with accounting principles generally accepted in the United States of America. Under this method, revenues are recognized when they are earned, and expenses are recognized when a liability is incurred, regardless of the timing of related cash flows.

**REVENUE RECOGNITION** – Lottery games are sold to the public by contracted retailers. Revenue is recognized for instant games when retailers make them available for sale to the public, as indicated by the retailers’ activation of tickets.

Revenue for terminal-based online games is recognized based on the game characteristics. For online games where the prize expense is determinable only upon occurrence of the related draw, revenues for sold tickets are recognized when the related drawing occurs. Also, amounts collected from retailers in advance of the draw are recorded as deferred revenue and recognized once the drawing occurs.

## Notes to the Financial Statements (As of and for the Years Ended June 30, 2011 and June 30, 2010)

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Revenues for online games where both prize expense and the draw date are known prior to ticket sales occurring are recognized at the time of the sale.

Certain instant and online games include free ticket prizes that entitle the holder to exchange a winning ticket for another of equal value. The selling price of the game ticket awarded as a prize reduces ticket revenue when the related winning ticket is validated.

Revenues are presented net of Bad Debt Expense.

**NET ASSETS** – Net assets represent cumulative revenues less expenses and required beneficiary program payments in accordance with the Act (see Notes 7 and 8). Net assets include funds invested in capital assets, restricted assets and unrestricted net assets.

**CASH** – Cash includes cash in banks, petty cash, and deposits on account in the State of Tennessee Local Government Investment Pool (LGIP) (see Note 2).

**RETAILER ACCOUNTS RECEIVABLE** – Retailer accounts receivable represents lottery proceeds due from retailers for ticket sales net of commissions due to and prizes paid by the retailers, and allowance for bad debt.

Lottery proceeds are collected weekly from retailer bank accounts established in trust for the TEL. Amounts not collected upon the established collection date are deemed delinquent. Delinquent accounts are reviewed periodically by TEL management. Accounts outstanding more than 180 days from the most recent date of delinquency or date of last payment are considered doubtful. At June 30, 2011 and 2010, the Allowance for Doubtful Accounts was \$270 thousand and \$471 thousand, respectively.

**CAPITAL ASSETS** – Capital assets are stated at cost less accumulated depreciation. Depreciation on capital assets is computed using the straight line method over the estimated useful lives of the assets, which is three to seven years for most assets. Leasehold improvements are amortized over their expected useful lives or the lease term, whichever is shorter. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation is removed from the accounts, and any resulting gain or loss is reflected in the results from operations in the period of disposal. The TEL's general threshold for capitalization is assets valued at \$500 or greater.

**DEFERRED REVENUE** – Funds collected from retailers for online game tickets sold in advance of the game drawings are recorded as deferred revenue and recognized as revenue once the related drawing occurs.

**FIDELITY FUND** – In accordance with the Tennessee Code Annotated §§ 4-51-118 (a), TEL retailers are assessed a one-time fidelity fund fee of \$50. Fidelity fund proceeds are held in a demand deposit account at Citizens Bank and are classified as restricted fidelity fund cash on the Statement of Net Assets. These funds may be used to cover losses incurred as a result of the nonfeasance, malfeasance or misfeasance of TEL retailers. During the years ended June 30, 2011 and June 30, 2010, \$50 thousand and \$38 thousand were respectively used to cover losses incurred as a result of uncollected accounts of TEL retailers.

At the end of each fiscal year, fidelity funds exceeding \$500,000 may be treated as net proceeds from the TEL subject to deposit to the Lottery for Education Account. As of the years ended June 30, 2011 and 2010, there were no fidelity funds available for deposit as net proceeds.

**RETAILER COMMISSIONS AND BONUSES** – Retailers receive a commission of 6.5% on all instant tickets settled and online tickets sold. In addition, retailers cashing Cash 3 and Cash 4 tickets receive an additional 1% for amounts cashed. Where commission has been paid to retailers for deferred revenue ticket sales, this fee is recorded as a prepaid expense until the related revenue is recognized.

## Notes to the Financial Statements (As of and for the Years Ended June 30, 2011 and June 30, 2010)

The TEL will pay a bonus of \$25,000 to a retailer who sells a single jackpot winning ticket for Powerball or Mega Millions; however, if there are multiple winning Powerball or Mega Millions jackpot winning tickets sold in Tennessee in a single drawing, the \$25,000 selling bonus will be divided proportionately (based on the number of winning tickets sold by each retailer) between or among the respective retailers.

The TEL will pay a selling bonus of \$5,000 to a retailer who sells a winning Powerball Power Play or Mega Millions Megaplier ticket if the prize is equal to or greater than one million dollars (\$1,000,000).

The TEL will pay a selling bonus of \$5,000 to a retailer who sells an online game winning ticket other than Powerball and Mega Millions if the prize is equal to or greater than one million dollars (\$1,000,000).

Bonuses were earned as follows during the years ended June 30:

ONLINE GAME	2011	2010
Powerball	\$ 30,000	\$ 40,000
Mega Millions	10,000	5,000
Tennessee Cash	10,000	-
Lotto Plus	-	15,000
<b>Total Retailer Bonuses</b>	<b>\$ 50,000</b>	<b>\$ 60,000</b>

**CONTRACTOR FEES** – The TEL has contracted with two vendors, GTECH Corporation (“GTECH”) and Scientific Games, Inc. (“SGI”) for the majority of the gaming systems and supplies.

GTECH operates the gaming network that consists of approximately 4,800 instant and online retailer ticket terminals and associated software. In accordance with its contract, GTECH receives the negotiated fee on the selling price of online tickets sold, and on instant ticket activations net of free tickets available as prizes. During fiscal years 2011 and 2010, GTECH was compensated at the rate of 1.24% for all online and instant ticket game sales.

Effective March 3, 2009, the TEL renegotiated its contract with GTECH to extend through April 9, 2015. Terms of this contract include the continuation of the contractor service fee rate of 1.24%, as well as GTECH's agreement to provide, install and maintain up to eight hundred (800) instant ticket vending machines (ITVMs) for the TEL.

SGI prints, warehouses, and distributes the instant game tickets to retailers. In accordance with its contract, SGI receives the negotiated fee on the selling price of all instant ticket activations. Effective April 1, 2009, the TEL renegotiated its contract with SGI to extend through April 9, 2015, and also to include a reduction of the contractor service fee from 1.139% to 1.07%. During the years ended June 30, 2011 and 2010, SGI was compensated at the rate of 1.07% for all instant ticket activations.

**PRIZES** – In accordance with the Act, as nearly as practical, at least 50% of ticket proceeds must be made available as prize money. Gross prize expense for instant ticket sales is recognized based on a predetermined prize structure for each game in accordance with the approved game working papers when tickets are activated for sale. Gross prize expense for Cash 3, Cash 4, Pick 5, Lotto Plus, and Tennessee Cash is recognized based on historical payout experience when the related drawings occur.

Powerball and Mega Millions prizes are shared based on contributions made to the prize pool by all member lotteries of the Powerball Group and the Mega Millions Group of the Multi-State Lottery Association (“MUSL”). All Powerball and Mega Millions grand prizes won by players who purchase tickets in Tennessee are funded from pooled contributions by all participating lottery states.



## Notes to the Financial Statements (As of and for the Years Ended June 30, 2011 and June 30, 2010)

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The contributions are held by MUSL in trust for the TEL and are paid, at the option of the prize winner, in either a lump-sum, or thirty (30) annual installments for Powerball and twenty-six (26) annual payments for Mega Millions. Lump-sum payments are discounted to present value, as calculated by MUSL for the Powerball game, and the Mega Millions Consortium Group for the Mega Millions game. As of the years ended June 30, 2011 and June 30, 2010, there were no grand prize winners in Tennessee.

**UNCLAIMED PRIZES** – Prizes not claimed within 90 days of the game-end date for instant games, and within 180 days of a game draw date for online games, are forfeited as unclaimed prizes.

**BUDGET** – Pursuant with the Act, annually by June 30th, the TEL is required to submit a proposed operating budget for the next fiscal year to the Tennessee Department of Finance and Administration, Office of Legislative Budget Analysis, and Comptroller of the Treasury. Additionally, by September 1, the TEL is required to submit a proposed operating budget for the succeeding fiscal year to the Tennessee Department of Finance and Administration for informational purposes.

**CONTINGENCIES** – The TEL is subject to various claims and contingencies related to litigation, fines and penalties, assessments and other matters arising out of the normal course of business. Liabilities related to contingencies are recognized when a loss is probable and reasonably estimable. As of the years ended June 30, 2011 and 2010, the TEL has not incurred, nor was it aware of any related liabilities.

**USE OF ESTIMATES** – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Estimates and assumptions are reviewed periodically and the effects of revisions are reflected in the financial statements in the period they are determined.

**ADVERTISING** – In accordance with AICPA Statement of Position 93-7, *Reporting on Advertising Costs*, with the exception of outdoor billboards advertising leases which are expensed in accordance with FASB 13 (Note 5), advertising costs are expensed when the related advertising takes place.

**RISK MANAGEMENT** – Effective July 31, 2005, the TEL became a member of the Risk Management Fund, an internal service fund of the State of Tennessee. The Risk Management Fund allocates the cost of providing claims servicing and claims payment by charging a premium to the TEL based on a percentage of the TEL's expected loss costs which include both experience and exposures. This self-insurance risk pool provides general, property and automobile liability up to \$300,000 per person and \$1,000,000 per occurrence.

Additionally, in order to minimize financial losses resulting from the occurrence of theft; employee dishonesty; legal judgments; work-related employee injury and accidents; and catastrophic events, the TEL maintains insurance from various other providers. At June 30, 2011, additional insurance coverage was provided at the following maximum amounts:

COVERAGE	2011
Employee Fidelity	\$ 500,000
Automobile/Property	1,000,000
Workers' Compensation	1,000,000
Employment Practices	5,000,000
General Liability/Umbrella	5,000,000

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## Notes to the Financial Statements (As of and for the Years Ended June 30, 2011 and June 30, 2010)

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Over the past three fiscal years, in the ordinary course of business, the TEL has filed insurance claims with both the risk pool and the commercial insurers. None of the related settlements exceeded the provided insurance coverage.

**NON-OPERATING REVENUES AND EXPENSES** – Revenues and expenses resulting from activities not directly associated with the sale of lottery tickets are reflected as non-operating revenues and expenses.

**COMPENSATED ABSENCES** – Effective November 29, 2004, the TEL implemented an attendance and leave policy allowing employees to earn vacation and sick leave during their employment. The corporation recognizes expense for accrued but unused vacation leave for all employees who have completed one year of service. No such expense exists for accrued but unused sick leave (Note 9).

**EMPLOYMENT SEPARATION** – Corporate officers earn separation pay for each year of employment with the TEL. Such expense is accrued in the period it is earned (Note 9).

### (2) CASH

A significant portion of TEL's deposits are in a financial institution that participates in the bank collateral pool administered by the State Treasurer. The securities pledged to protect these accounts are pledged in the aggregate rather than against each individual account. The members of the pool may be required by agreement to pay an assessment to cover any deficiency. Under this additional assessment agreement, public fund accounts covered by the pool are considered to be insured for purposes of credit risk disclosure. At June 30, 2011 and 2010, bank balances of approximately \$1.477 million and \$1.866 million, respectively, were insured by the bank collateral pool.

For the years ended June 30, 2011 and 2010, bank balances of approximately \$22,000, were also maintained in a demand deposit account that was insured by the Federal Deposit Insurance Corporation for up to a maximum of \$250,000.

The TEL also has deposits in the Local Government Investment Pool (LGIP) administered by the State Treasurer. The TEL's deposits with the LGIP were approximately \$65.3 million and \$66.7 million at June 30, 2011 and 2010, respectively. The LGIP is part of the State Pooled Investment Fund. The fund is not rated by a nationally recognized statistical rating organization. The fund's investment policy and required risk disclosures are presented in the *State of Tennessee Treasurer's Report*. That report is available on the state's website at <http://www.tn.gov/treasury/> or by calling (615) 741-2956.

### (3) PRIZE ANNUITY INVESTMENTS

The prize structure of the *Win for Life* instant ticket game included three grand prizes in the form of lifetime annuities. These grand prizes guarantee the winner will receive \$52,000 a year for the remainder of his/her life, with a minimum of 20 annual payments totaling \$1,040,000. As of June 30, 2006, all of the grand prizes have been claimed by and awarded to winners.

In fiscal year 2007, the TEL purchased one (1) single premium, sum certain lifetime annuity contract for approximately \$739,000, in its name from Aviva Life, and appointed the respective *Win for Life* prize winner as the beneficiary.

In fiscal year 2006, the TEL purchased two (2) single premium, sum certain lifetime annuity contracts for approximately \$904,000 and \$848,000, in its name from Metropolitan Life (Met Life), and appointed the respective *Win for Life* prize winners as the beneficiaries.

In accordance with its investment policy, the TEL may enter into insurance annuity contracts in order to fund annuity prizes. All life insurance annuity contracts must be issued by companies which are financially rated "A" or better by a nationally recognized rating agency and duly licensed, admitted and authorized to transact business in the State of Tennessee.

## Notes to the Financial Statements (As of and for the Years Ended June 30, 2011 and June 30, 2010)

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*Credit risk.* This is the risk that a counterparty will fail to fulfill its obligation. The TEL mitigates this risk through its investment policy, which limits purchase of investments to those financially rated "A" or better by a nationally recognized rating agency. Consistent with this policy, the annuities purchased from Met Life were rated "A+" (Superior) by A.M. Best as of June 30, 2011 and June 30, 2010. The annuity purchased from Aviva was rated "A" (Excellent) by A.M. Best as of June 30, 2011 and June 30, 2010.

*Concentration of credit risk.* This risk relates to an investor's failure to adequately diversify its investments and is specifically defined as investments of 5 percent or more in the securities of a single issuer. Though the TEL does not have a policy specific to this risk, as a condition of the purchase, and for the duration of the contract, Met Life and Aviva are required to maintain insurance sufficient to reimburse the TEL for any losses resulting from its failure or inability to meet related obligations.

*Custodial credit risk.* For an investment, this is the risk that in the event of the failure of the counterparty to a transaction, the investor will not be able to recover the value of its investments that are in the possession of an outside party. Investments are subject to custodial credit risk only if they are evidenced by securities that exist in physical or book entry form. Given that annuity contracts do not meet this condition, no related custodial credit risk exists as of the years ended June 30, 2011 and June 30, 2010.

The TEL records all investments purchased to fund annuity prizes at fair value. Liabilities for annuity prizes are recorded at their discounted present value as prize annuities payable.

In relation to both the prize annuity investments and prize annuities payables, payments due from insurance companies and due to prize winners within the next fiscal year are classified as current, whereas the remaining portion is classified as noncurrent on the Statement of Net Assets.

Changes in the fair market value of the prize annuity investments are deferred as noncurrent prize annuities payable. As of the years ended June 30, 2011 and 2010, the fair market value of the prize annuity investments respectively increased by \$225 thousand and decreased by \$31 thousand.

## Notes to the Financial Statements (As of and for the Years Ended June 30, 2011 and June 30, 2010)

### (4) CAPITAL ASSETS

Capital assets consisted of the following as of June 30, 2011:

	BEGINNING BALANCE	INCREASES	DECREASES	ENDING BALANCE
Furniture and fixtures	\$ 903,000	\$ 2,000	\$ (12,000)	\$ 893,000
Computer equipment	436,000	8,000	(38,000)	406,000
Vehicles	261,000	37,000	(73,000)	225,000
High mileage vehicles—vans	1,016,000	281,000	(242,000)	1,055,000
Leasehold improvements	401,000	31,000	(32,000)	400,000
Communication equipment	891,000	13,000	-	904,000
Software	686,000	27,000	-	713,000
Gaming equipment	567,000	6,000	-	573,000
Total capital assets	5,161,000	405,000	(397,000)	5,169,000
Less accumulated depreciation	(3,802,000)	(740,000)	393,000	(4,149,000)
<b>Total capital assets, net</b>	<b>\$ 1,359,000</b>	<b>\$ (335,000)</b>	<b>\$ (4,000)</b>	<b>\$ 1,020,000</b>

Capital assets consisted of the following as of June 30, 2010:

	BEGINNING BALANCE	INCREASES	DECREASES	ENDING BALANCE
Furniture and fixtures	\$ 901,000	\$ 2,000	\$ -	\$ 903,000
Computer equipment	407,000	31,000	(2,000)	436,000
Vehicles	200,000	78,000	(17,000)	261,000
High mileage vehicles—vans	960,000	173,000	(117,000)	1,016,000
Leasehold improvements	344,000	57,000	-	401,000
Communication equipment	879,000	12,000	-	891,000
Software	631,000	55,000	-	686,000
Gaming equipment	567,000	-	-	567,000
Total capital assets	4,889,000	408,000	(136,000)	5,161,000
Less accumulated depreciation	(3,167,000)	(769,000)	134,000	(3,802,000)
<b>Total capital assets, net</b>	<b>\$ 1,722,000</b>	<b>\$ (361,000)</b>	<b>\$ (2,000)</b>	<b>\$ 1,359,000</b>

### (5) LEASING ARRANGEMENTS

The TEL's leasing arrangements consist of non-cancelable operating leases for office space, outdoor advertising billboards, and related equipment that expire at various dates through 2018. Certain of these leases contain provisions for scheduled rental increases and are renewable at the option of the TEL. No options were exercised during the year ended June 30, 2011, and one option was exercised during the year ended June 30, 2010.

In addition, the TEL subleases office space under operating leases expiring through 2014 to its major vendors.

The following is a schedule by years of future minimum rental payments required of TEL under all non-cancelable operating leases with original terms of one year or more as of June 30:

## Notes to the Financial Statements (As of and for the Years Ended June 30, 2011 and June 30, 2010)

YEAR ENDING JUNE 30:	2011	2010
2011	\$ -	\$ 2,259,000
2012	2,562,000	1,932,000
2013	2,099,000	1,755,000
2014	1,372,000	1,079,000
2015	323,000	223,000
2016	129,000	153,000
2017 and thereafter	383,000	-
<b>Total minimum rental payments</b>	<b>\$ 6,868,000</b>	<b>\$ 7,401,000</b>

Minimum rental payments at June 30, 2011 and 2010, have not been reduced by minimum sublease rentals of \$531 thousand and \$728 thousand, respectively, due in future years under non-cancelable subleases.

The following is a schedule by years of future minimum sublease rental payments due to TEL under all non-cancelable operating leases with original terms of one year or more as of June 30:

YEAR ENDING JUNE 30:	2011	2010
2011	\$ -	\$ 203,000
2012	203,000	197,000
2013	197,000	197,000
2014	131,000	131,000
<b>Total minimum sublease payments</b>	<b>\$ 531,000</b>	<b>\$ 728,000</b>

The following schedule shows the composition of total rental expense, net of deferred rent expense and income, for all operating leases for the years ended June 30:

	2011	2010
MINIMUM RENTALS:		
Property	\$ 1,427,000	\$ 1,429,000
Billboards	1,248,000	1,049,000
Less: Sublease rentals	(203,000)	(206,000)
<b>Total minimum rentals</b>	<b>\$ 2,472,000</b>	<b>\$ 2,272,000</b>

## Notes to the Financial Statements (As of and for the Years Ended June 30, 2011 and June 30, 2010)

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### (6) DEFERRED RENT

As an incentive for entering into certain lease agreements, the TEL received rent abatements approximating \$667,000 from landlords. In accordance with Financial Accounting Standards 13 (FAS 13), *Accounting for Leases*, and Governmental Accounting Standards Board Statement No. 13, *Accounting for Operating Leases with Scheduled Rent Increases*, the TEL defers rent incentives over the entire lease term on a straight-line basis. Additionally, where lease agreements stipulate escalation of rental payments over the term of the lease, the TEL recognizes related rental expense on a straight-line basis over the entire term of the lease.

At June 30, 2011, total deferred rent of \$420,000 consisted of \$162,000 related to rent abatements and \$258,000 to the straight-lining of rental expense over the life of the related lease terms.

At June 30, 2010, total deferred rent of \$578,000 consisted of \$223,000 related to rent abatements and \$355,000 to the straight-lining of rental expense over the life of the related lease terms.

## Notes to the Financial Statements (As of and for the Years Ended June 30, 2011 and June 30, 2010)

### (7) DUE TO LOTTERY FOR EDUCATION ACCOUNT

In accordance with the Act, all net proceeds of the TEL are due to the Lottery for Education Account. "Net proceeds" is defined under the Act as "all revenue derived from the sale of lottery tickets or shares and all other monies derived from lottery games less operating expenses. "Operating expenses" are defined under the Act as "all costs of doing business, including, but not limited to, prizes, commissions, and other compensation paid to lottery retailers, advertising and marketing costs, rental fees, personnel costs, capital costs, depreciation of property and equipment, amounts held in or paid from a fidelity fund, and all other operating costs." All other expenses are considered non-operating.

Net proceeds and operating expenses for the years ended June 30, 2011 and June 30, 2010, are summarized as follows:

	2011	2010
OPERATING REVENUES		
Ticket sales (Net)	\$1,186,318,000	\$1,138,016,000
Less instant tickets provided as prizes	(83,978,000)	(77,910,000)
Net ticket sales	1,102,340,000	1,060,106,000
Fees and other revenue	3,990,000	3,861,000
<b>Total lottery proceeds</b>	<b>1,106,330,000</b>	<b>1,063,967,000</b>
OPERATING EXPENSES, AS DEFINED		
Gaming	809,134,000	773,433,000
Operating	15,460,000	14,766,000
<b>Total operating expenses, as defined</b>	<b>824,594,000</b>	<b>788,199,000</b>
<b>Net proceeds before distribution of unrestricted net assets</b>	<b>281,736,000</b>	<b>275,768,000</b>
NON-OPERATING REVENUE AND EXPENSES		
Interest income	110,000	211,000
<b>Total non-operating revenue and expenses</b>	<b>110,000</b>	<b>211,000</b>
<b>Net Proceeds</b>	<b>\$ 281,846,000</b>	<b>\$ 275,979,000</b>
Amount due to Lottery for Education Account for year	281,846,000	275,979,000
Amount paid during year	(211,565,000)	(204,313,000)
<b>Amount due to Lottery for Education Account, end of year</b>	<b>\$ 70,281,000</b>	<b>\$ 71,666,000</b>

All amounts due at the end of each fiscal year were deposited to the Lottery for Education Account in July of the subsequent fiscal year.



## Notes to the Financial Statements (As of and for the Years Ended June 30, 2011 and June 30, 2010)

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### (8) DUE TO AFTER-SCHOOL PROGRAMS ACCOUNT

In accordance with the Act, at the end of each fiscal year, one hundred percent of any unclaimed prize money shall be deposited in the After-School Programs Account.

The amounts due to the After-School Programs special account are derived from unclaimed prizes for instant games that have been officially closed and online draws that have exceeded the 180-day claim period.

Effective in fiscal year 2010, unclaimed prizes for instant games are estimated based upon historical percentages of actual unclaimed dollars at the time of game close and reconciliation at the end of the 90-day redemption period.

For online games, the actual unclaimed amounts are determined after the expiration of the related claim period for the draw.

For instant games, prizes not claimed within 90 days of the announced game end date are forfeited as unclaimed prizes. For online games, prizes not claimed within 180 days of a game draw date are forfeited as unclaimed prizes.

For fiscal year 2011, unclaimed prizes were \$11,644,000, which was current and payable to the After-School Programs Account at June 30, 2011.

For fiscal year 2010, unclaimed prizes were \$12,894,000, which was current and payable to the After-School Programs Account at June 30, 2010.

All amounts due at the end of each fiscal year were deposited to the After-School Programs Special Account in July of the subsequent fiscal year.

### (9) EMPLOYEE BENEFITS

#### A. *Deferred Compensation*

Effective September 22, 2003, the TEL provided its employees with a deferred compensation plan created in accordance with Internal Revenue Code Section 457 (the "457 Plan"). The 457 Plan is available to all eligible employees at their option and permits participants to defer a portion of their salary until future years. The deferred compensation is not available to participants until termination, retirement, death, or unforeseeable emergency. During the years ended June 30, 2011 and 2010, employees contributed approximately \$416,000 and \$373,000, respectively to the 457 Plan.

The aggregate fair value of the plan's assets was approximately \$2,758,000 and \$2,051,000, net of administrative fees, as of June 30, 2011 and 2010, respectively.

#### B. *Defined Contribution Plan*

Effective September 22, 2003, the TEL Board of Directors established a defined contribution plan in accordance with Internal Revenue Code Section 401(a) (the "401(a) Plan"). Under the 401(a) Plan all eligible employees receive compensation from the TEL in the form of non-voluntary deferrals to their individual 401(a) accounts as follows:

1. Contribution of five percent (5%) of employee's compensation, and
2. Matching contribution of seventy-five percent (75%) of the participant's contributions to the 457 Plan up to the first five (5) percent of the participant's compensation.

These contributions vest over a four-year period at a rate of twenty-five percent (25%) per year and are not available to participants until termination, retirement, death or unforeseeable emergency. The TEL contributed approximately \$634,000 and \$618,000 to

## Notes to the Financial Statements (As of and for the Years Ended June 30, 2011 and June 30, 2010)

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the 401(a) Plan on behalf of its employees in the years ended June 30, 2011 and 2010, respectively. Of these contributions, approximately \$29,000 and \$14,000 were forfeited by separated employees as of June 30, 2011 and June 30, 2010, respectively.

In accordance with the 401(a) Plan, forfeitures of employer contributions may be used to offset plan administrative expenses and/or reduce future contribution costs. As of the years ended June 30, 2011 and 2010, forfeited amounts of approximately \$37,000 and \$6,000, respectively, were used to offset employer contributions and plan administrative expenses.

Section 1448 of the Small Business Job Protection Act of 1996 added Subsection (g) to Section 457 of the Internal Revenue Code to provide that all assets and income under a Section 457(b) plan that are maintained by a state or local government employer must be held in trust for the exclusive benefit of plan participants and their beneficiaries. The 457 Plan and 401(a) Plan assets are held in aggregate by John Hancock Financial, the plans' custodian.

The aggregate fair value of the plan's assets was approximately \$4,158,000 and \$3,043,000, net of forfeitures and administrative fees, as of June 30, 2011 and 2010, respectively.

### *C. Compensated Absences*

Vacation leave can be earned at various rates depending on the employee's position and years of service. Carryover of vacation leave is limited to the number of hours earned in the prior year. Employees must complete twelve months of service from the date of hire before they receive termination payment for any unused vacation hours. The current portion of the compensated absence liability, expected to be due within one year of the statement date, June 30, 2011, is estimated using historical trends. At June 30, 2011 and 2010, the estimated current portion of the compensated absences liability was \$383 thousand and \$414 thousand, respectively.

Sick leave is earned at the end of each month at the rate of eight hours per month for all employees. Sick leave may be carried over from year to year, but all such accrued sick leave is forfeited upon separation of employment.

### *D. Employment Separation*

Corporate officers accrue forty hours of separation pay for every year of employment with TEL. The TEL had \$295 thousand and \$243 thousand accrued for employment separation obligations for each of the years ending June 30, 2011 and 2010, respectively.

## Notes to the Financial Statements (As of and for the Years Ended June 30, 2011 and June 30, 2010)

### (10) LONG-TERM LIABILITIES

Long-term liabilities consisted of the following as of June 30, 2011:

	BEGINNING BALANCE	INCREASES	DECREASES	ENDING BALANCE	DUE WITHIN ONE YEAR
Prize Annuities Payable	\$ 2,345,000	\$ 225,000	\$ (156,000)	\$ 2,414,000	\$ 104,000
Compensated Absences	533,000	629,000	(597,000)	565,000	383,000
Deferred Rent	578,000	-	(158,000)	420,000	61,000
<b>Total long-term liabilities</b>	<b>\$ 3,456,000</b>	<b>\$ 854,000</b>	<b>\$ (911,000)</b>	<b>\$ 3,399,000</b>	<b>\$ 548,000</b>

Long-term liabilities consisted of the following as of June 30, 2010:

	BEGINNING BALANCE	INCREASES	DECREASES	ENDING BALANCE	DUE WITHIN ONE YEAR
Prize Annuities Payable	\$ 2,532,000	\$ -	\$ (187,000)	\$ 2,345,000	\$ 104,000
Compensated Absences	470,000	606,000	(543,000)	533,000	414,000
Deferred Rent	736,000	-	(158,000)	578,000	61,000
<b>Total long-term liabilities</b>	<b>\$ 3,738,000</b>	<b>\$ 606,000</b>	<b>\$ (888,000)</b>	<b>\$ 3,456,000</b>	<b>\$ 579,000</b>

Compensated absences presented within the noted schedules are included in accrued liabilities presented on the Statement of Net Assets.

### (11) COMMITMENTS AND CONTINGENCIES

*Legal* – The TEL is subject to litigation in the ordinary course of its business. In the opinion of management and legal counsel, the outcome of such litigation will not have a material impact on the financial position or cash flows of the TEL. Furthermore, as of the year ended June 30, 2011, management is not aware of any related liabilities.



**Tennessee Education Lottery Corporation**

Plaza Tower, Metro Center  
200 Athens Way, Suite 200  
Nashville, TN 37228

[tnlottery.com](http://tnlottery.com)

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