



NORTH DAKOTA OFFICE OF THE STATE AUDITOR

State Auditor Joshua C. Gallion

North Dakota Lottery

Audit Report for the Year Ended June 30, 2022

Client Code 125.10



Contents

<i>Independent Auditor’s Report</i>	<i>1</i>
<i>Management’s Discussion and Analysis</i>	<i>5</i>
<i>Financial Statements</i>	<i>10</i>
<i>Statement of Net Position</i>	<i>10</i>
<i>Statement of Revenues, Expenses, and Changes in Net Position</i>	<i>11</i>
<i>Statement of Cash Flows</i>	<i>12</i>
<i>Notes to the Financial Statements</i>	<i>14</i>
<i>Required Supplementary Information</i>	<i>33</i>
<i>Notes to the Required Supplementary Information</i>	<i>36</i>
<i>Exhibits</i>	<i>37</i>
<i>Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards</i>	<i>37</i>
<i>Governance Communication</i>	<i>39</i>



STATE OF NORTH DAKOTA
OFFICE OF THE STATE AUDITOR
STATE CAPITOL
600 E. BOULEVARD AVENUE – DEPT 117
BISMARCK, NORTH DAKOTA 58505

Independent Auditor's Report

Members of the Legislative Assembly
Honorable Drew Wrigley, Attorney General
Lance Gaebe, Director, North Dakota Lottery

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of the business-type activities of the North Dakota Lottery, a division of the Office of the Attorney General of the State of North Dakota, as of and for the year ended June 30, 2022, and the related notes to the financial statements, which collectively comprise the North Dakota Lottery's basic financial statements as listed in the table of contents.

In our opinion, the accompanying financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of the North Dakota Lottery, as of June 30, 2022, and the respective changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in the United States of America (GAAS) and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the North Dakota Lottery and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Emphasis of Matter

As discussed in Note 1, the financial statements of the North Dakota Lottery present the financial position, the changes in financial position, and cash flows of only that portion of the business-type

activities of the state of North Dakota that is attributable to the transactions of the North Dakota Lottery. They do not purport to, and do not present fairly the financial position of the state of North Dakota as of June 30, 2022, or the changes in its financial position, or its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Also as discussed in Note 1, the North Dakota Lottery adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 87, Leases, GASB Statement No. 89, Accounting for Interest Cost Incurred before the End of a Construction Period, GASB Statement No. 91, Conduit Debt Obligations, GASB Statement No. 92, Omnibus 2020, GASB Statement No. 93, Replacement of Interbank Offered Rates, and GASB Statement No. 97, Certain Component Unit Criteria, and Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans. Our opinion is not modified with respect to this matter.

Responsibilities of Management for the Financial Statements

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

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the North Dakota Lottery's ability to continue as a going concern for twelve months beyond the financial statement date, including any currently known information that may raise substantial doubt shortly thereafter.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinions. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS and *Government Auditing Standards*, we

- exercise professional judgment and maintain professional skepticism throughout the audit.
- identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.

- obtain an understanding of internal control relevant to the audit 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 North Dakota Lottery's internal control. Accordingly, no such opinion is expressed.
- evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the North Dakota Lottery's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, the Schedule of Employer's Share of Net Pension Liability, the Schedule of Employer Contributions (Pension), the Schedule of Employer's Share of Net OPEB Liability, and the Schedule of Employer Contributions (OPEB), as listed in the table of contents, be presented to supplement the basic financial statements. Such information is the responsibility of management and, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated April 13, 2023, on our consideration of the North Dakota 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 solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the North Dakota Lottery's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the North Dakota Lottery's internal control over financial reporting and compliance.

/S/

Joshua C. Gallion
State Auditor

Bismarck, North Dakota
April 13, 2023

Management's Discussion and Analysis

The Management's Discussion and Analysis is an overview of the Lottery's financial activity for the fiscal year ended June 30, 2022. The analysis considered in conjunction with the financial statements will provide an objective breakdown of the Lottery's financial activity based on facts, decisions, and conditions that presently face the division.

Understanding the Lottery's Financial Statements

The Lottery Division of the Office of Attorney General is accounted for as an enterprise fund that reports all income, expense, assets, and liabilities using the accrual basis of accounting, similar to a private business entity. In accordance with generally accepted accounting principles, this report consists of three financial statements and explanatory notes. The financial statements include 1) Statement of Net Position; 2) Statement of Revenues, Expenses, and Changes in Net Position; and 3) Statement of Cash Flows. The financial statements highlight the Lottery's operating activity and provide a snapshot of its financial condition.

The Lottery is required by statute to transfer all net proceeds, less the amount allocated to the Compulsive Gambling Prevention and Treatment Fund, amount allocated to the Multijurisdictional Drug Task Force Grant Fund, Lottery's share of a game's prize reserve pool, and reserve funds the division may need for continued operations, to the State Treasurer on at least an annual basis for deposit in the State General Fund.

Most of the assets included on the Statements of Net Position represent current amounts such as cash and accounts receivable from lottery retailers. Most liabilities represent current prizes, including prizes payable to players in North Dakota and prizes payable to the Multi-State Lottery Association (MUSL) to fund grand/jackpot prizes, and an amount due to the State General Fund.

Financial Highlights

Since the Lottery began in March 2004, North Dakota players have won over \$169 million in prizes and Lottery retailers earned over \$24.1 million in sales and bonus commissions. In addition, the Lottery contributed \$116 million to the General Fund, along with \$4.6 million to the Compulsive Gambling Prevention and Treatment Fund, and \$7.4 million to the Multijurisdictional Drug Task Force Grant Fund.

The Lottery's ticket sales for the fiscal year ended June 30, 2022, were \$29,177,163 as compared to \$30,383,394 for the fiscal year ended June 30, 2021. This reflects a decrease of \$1,206,231 or 3.97% in ticket sales. The primary reason for the decrease in sales was the Powerball and Mega Millions jackpots reached \$699 million and \$432 million in fiscal year ended June 30, 2022 respectively compared to \$731 million and \$1 billion in fiscal year ended June 30, 2021 respectively.

Total prizes won during the fiscal year ended June 30, 2022, were \$15,361,112, including prizes paid in North Dakota of \$10,111,605 and prizes paid to the MUSL to fund grand/jackpot prizes of \$5,786,912. In addition, North Dakota had expired prizes of \$537,405.

The Lottery optimized the efficiency of its organizational structure, functions, and gaming system features to minimize operating expenses. Expenses such as salaries and fringe benefits, travel, telephone, and MUSL board dues are generally fixed. Other expenses have a direct incremental relationship to sales increases or decreases such as prizes, retailer commissions, and contractual services.

Total operating expenses for the fiscal year ended June 30, 2022, were \$21,994,537 as compared to \$23,591,872 for the fiscal year ended June 30, 2021. This reflects a \$1,597,335 or 6.77% decrease in total operating expenses. The decrease was primarily due to the decrease in prize expenses as a result of lower jackpots during the fiscal year ended June 30, 2022, along with the incremental relationship in sales for retailer commissions and contractual services.

Income before transfers earned for the fiscal year ended June 30, 2022, was \$7,332,254. The total transfer of funds equated to \$6,720,000. Of that amount, the Lottery transferred \$320,000 to the Compulsive Gambling Prevention and Treatment Fund, and \$800,000 to the Multijurisdictional Drug Task Force Grant Fund. The Lottery transferred the balance of \$5,600,000, to the State General Fund.

- By law, effective July 1, 2015, the Lottery must transfer \$80,000 to the State Treasurer each quarter for deposit in the Compulsive Gambling Prevention and Treatment Fund.
- By law, effective July 1, 2019, the Lottery must transfer \$200,000 to the State Treasurer each quarter for deposit in the Multijurisdictional Drug Task Force Grant Fund.

Financial Position

The Lottery's net position (assets and deferred outflows of resources less liabilities and deferred inflows of resources) is one measure of the financial health or financial position. Total net position for the fiscal year ended June 30, 2022, was \$1,784,423. This reflects an increase of \$612,254 or 52.2% in total net position compared to the fiscal year ended June 30, 2021. The total net position restricted for MUSL uses was \$1,397,053. Each year in mid to late July, the Lottery estimates the State General Fund transfer amount. Therefore, the Lottery's net assets will increase or decrease depending on the amount transferred compared to the Lottery's net position. This year the General Fund transfer calculation resulted in an increase of the final balance of the unrestricted net position.

Overview of the Financial Statements

Statement of Net Position Summary:

	<u>June 30, 2022</u>	<u>June 30, 2021</u>
Assets:		
Current Assets	\$ 8,182,543	\$ 8,821,765
Noncurrent Assets	1,581,404	1,381,247
Total Assets	<u>\$ 9,763,947</u>	<u>\$ 10,203,012</u>
Deferred Outflows of Resources		
Deferred Outflows - Pension	<u>\$ 796,728</u>	<u>\$ 1,148,704</u>
Liabilities:		
Current Liabilities	\$ 6,678,391	\$ 7,880,080
Noncurrent Liabilities	860,206	2,011,260
Total Liabilities	<u>\$ 7,538,597</u>	<u>\$ 9,891,340</u>
Deferred Inflows of Resources		
Deferred Inflows - Pension	<u>\$ 1,237,655</u>	<u>\$ 288,207</u>
Net Position:		
Invested in Capital Assets	\$ 8,719	\$ 11,841
Restricted	1,397,053	1,369,406
Unrestricted	378,651	(209,078)
Total Net Position	<u>\$ 1,784,423</u>	<u>\$ 1,172,169</u>

Statement of Revenues, Expenses, and Changes in Net Position Summary:

	<u>June 30, 2022</u>	<u>June 30, 2021</u>
Revenues:		
Ticket Sales	\$ 29,177,163	\$ 30,383,394
Other Operating Revenue	152,046	117,892
Total Revenues	<u>\$ 29,329,209</u>	<u>\$ 30,501,286</u>
Expenses:		
Prizes	\$ 15,361,112	\$ 16,276,625
Retailer Commissions	1,322,119	1,403,760
Retailer Bonuses	44,250	56,250
Other Operating Expenses	5,267,056	5,855,237
Total Expenses	<u>\$ 21,994,537</u>	<u>\$ 23,591,872</u>

Statement of Revenues, Expenses, and Changes in Net Position Summary

(Continued):

	<u>June 30, 2022</u>	<u>June 30, 2021</u>
Nonoperating Revenues (Expenses)	(\$2,418)	\$7,049
Income Before Transfers	\$7,332,254	\$6,916,463
Transfers to Other Funds	(6,720,000)	(7,420,000)
Change in Net Position	<u>\$612,254</u>	<u>(\$503,537)</u>
Net Position, Beginning of Year	<u>\$1,172,169</u>	<u>\$1,675,706</u>
Net Position, End of Year	<u><u>\$1,784,423</u></u>	<u><u>\$1,172,169</u></u>

Supplemental Information

	<u>June 30, 2022</u>	<u>June 30, 2021</u>
Ticket Sales by Game		
Powerball	\$12,008,945	\$10,541,688
Mega Millions	5,537,197	8,817,242
Lotto America	2,254,191	2,248,769
Lucky for Life	4,603,942	3,422,848
2by2	4,773,350	5,354,382
Retailer Credit Adjustments	(462)	(1,535)
Total Ticket Sales by Game	<u>\$29,177,163</u>	<u>\$30,383,394</u>

Potential Factors Affecting Future Sales

The challenge facing the Lottery is to sustain sales and net position by actively promoting sales of tickets for present and new games in a very competitive retail environment.

The Lottery is unique compared to most other state lotteries since the constitution restricts the Lottery to multi-state online games. The Lottery must partner with one or more other government-authorized lotteries to conduct a game. This restriction generally limits the Lottery to games administered by MUSL. MUSL may not have a broad range of games available to fulfill the Lottery's desired product mix or the MUSL's games may become stale. Should MUSL dissolve, although it is not anticipated, the Lottery would not have a source of games to conduct.

Looking Ahead

The Lottery's goal is to provide a service to the citizens of North Dakota and, while considering the sensitive nature of the Lottery, promote games, and ensure the integrity, security, and fairness of its operation. To accomplish this, the Lottery must offer attractive games that add value to the Lottery's product mix, license retailers that are in convenient locations, create effective annual marketing plans, provide quality customer service to retailers and players, and control operating expenses.

To attract players, games must be interesting to play and have a broad range of player odds and starting jackpot prizes. The MUSL game groups periodically refresh their games by replacing them or re-launching the games with new features or options. Total sales of a game are dramatically affected by the size of the game's jackpot and, to a lesser degree, on the odds of winning a prize. Larger jackpots generate higher sales. However, larger jackpots cannot be predicted or relied upon. Therefore, a variety of games with varying jackpots and odds of winning a prize is necessary to attract players.

For the fiscal year 2023, the Lottery plans to:

- Implement a procurement effort to select a lottery vendor nine months in advance of the expiration of the current contract which expires in 2024;
- Along with other member states, evaluate the modification and add-on enhancements to Powerball and Mega Millions games with marketing partnerships, multiplier options, double jackpots, or matching prize options;
- Increase awareness and usage of the Players Club Mobile Applications and reward players for continued loyalty;
- Improve security and geo-location rigor of mobile apps;
- Increase Pick & Click online play sales;
- Continue to develop and conduct innovative marketing promotions, customer relationship management communications, and public awareness campaigns;
- Continue to review and enhance security policies and procedures, and work with the Multi-State Lottery Association to ensure the integrity and fairness of operations;
- Continue to streamline operations with paperless processes and transaction approval; and
- Identify a replacement for the gift certificate program.

If a person has a question on any information in this report or desires additional information, please contact:

North Dakota Lottery
Office of Attorney General
1720 Burlington Drive, Suite C
Bismarck, ND 58504-7736
ndlottery@nd.gov

Financial Statements

Statement of Net Position

	<u>June 30, 2022</u>	
Assets:		
Current Assets:		
Cash and Cash Equivalents	\$	7,361,549
Cash at Fiscal Agent		537,526
Accounts Receivable		271,758
Prepaid Expenses		11,710
Total Current Assets	\$	<u>8,182,543</u>
Noncurrent Assets:		
Reserves on Deposit	\$	1,397,053
Equipment and Software, Net		8,719
Leases – Right of Use, Net		175,632
Total Noncurrent Assets	\$	<u>1,581,404</u>
Total Assets	\$	<u>9,763,947</u>
Deferred Outflows of Resources		
Deferred Outflows - Pension	\$	<u>796,728</u>
Liabilities:		
Current Liabilities:		
Accounts Payable	\$	130,791
Due to Other State Funds		5,620,320
Accrued Payroll		85,897
Prizes Payable		487,893
Unearned Revenue		312,495
Leases Payable		40,995
Total Current Liabilities	\$	<u>6,678,391</u>
Noncurrent Liabilities:		
Leases Payable	\$	134,637
Net Pension Liability		630,842
Net Other Postemployment Benefit Plan Liability		34,963
Compensated Absences Payable		59,764
Total Noncurrent Liabilities	\$	<u>860,206</u>
Total Liabilities	\$	<u>7,538,597</u>
Deferred Inflows of Resources		
Deferred Inflows - Pension	\$	<u>1,237,655</u>
Net Position:		
Net Investment in Capital Assets	\$	8,719
Restricted		1,397,053
Unrestricted		378,651
Total Net Position	\$	<u>1,784,423</u>

The accompanying Notes to the Financial Statements are an integral part of this statement.

Statement of Revenues, Expenses, and Changes in Net Position

	June 30, 2022
Operating Revenues:	
Ticket Sales	\$ 29,177,163
Other Operating Revenue	152,046
Total Operating Revenues	\$ 29,329,209
Operating Expenses:	
Prizes	\$ 15,361,112
Retailer Commissions and Bonuses	1,366,369
Contractual Services	3,040,108
Players Club	325,000
Marketing	537,652
Salaries and Benefits	1,062,179
Other Operating Expenses	302,117
Total Operating Expenses	\$ 21,994,537
Operating Income	\$ 7,334,672
Nonoperating Revenues (Expenses):	
Interest Income	\$ 4,841
Interest Expense	(7,259)
Total Nonoperating Revenues	\$ (2,418)
Income Before Transfers	\$ 7,332,254
Transfers to Other Funds:	
Compulsive Gambling Fund	\$ 320,000
Multijurisdictional Drug Task Force Fund	800,000
State General Fund	5,600,000
Total Transfers to Other Funds	\$ 6,720,000
Change in Net Position	\$ 612,254
Total Net Position- Beginning of Fiscal Year	\$ 1,172,169
Total Net Position- End of Year	\$ 1,784,423

The accompanying Notes to the Financial Statements are an integral part of this statement.

Statement of Cash Flows

	June 30, 2022
Cash Flows from Operating Activities:	
Ticket Sales	\$ 21,126,189
Other Revenues	83,210
Paid to Prize Winners	(3,475,489)
Paid to Vendors	(10,047,444)
Paid to Employees	(1,053,096)
Payments to MUSL Prize Reserve	(104,155)
Funds Received from MUSL Prize Reserve	76,508
Net Cash Provided by Operating Activities	\$ 6,605,723
Cash Flows from Noncapital Financing Activities:	
Transferred to Compulsive Gambling Treatment Fund	\$ (320,000)
Transferred to Multi-Jurisdictional Drug Task Force Fund	(800,000)
Transferred to State General Fund	(6,300,000)
Net Cash Used in Noncapital Financing Activities	\$ (7,420,000)
Cash Flows from Capital and Related Financing Activities:	
Leases - Interest Expense	\$ (7,259)
Leases – Principal Paid	(33,463)
Net Cash Used in Capital and Related Financing Activities	\$ (40,722)
Cash Flows from Investing Activities:	
Interest Income	\$ 3,065
Net Cash Provided by Investing Activities	\$ 3,065
Cash and Cash Equivalents at Beginning of Year	\$ 8,213,483
Cash and Cash Equivalents at End of Year	\$ 7,402,271

(continued)

Statement of Cash Flows – Continued

	<u>June 30, 2022</u>
Reconciliation of Operating Income to Net Cash	
Provided by Operating Activities:	
Operating Income	\$ 7,334,672
Adjustments to Reconcile Operating Income to Net Cash	
Provided by Operating Activities:	
Depreciation	36,585
Deferred Outflows – Pension	351,976
Deferred Inflows - Pension	949,448
Changes in Assets and Liabilities:	
(Increase) Decrease in Cash at Fiscal Agent	(84,137)
(Increase) Decrease in Accounts Receivable	(126,911)
(Increase) Decrease in Prepaid Expenses	(1,710)
(Increase) Decrease in Reserves on Deposit	(25,825)
Increase (Decrease) in Accounts Payable	(371,595)
Increase (Decrease) in Due to Other State Funds	(86,310)
Increase (Decrease) in Accrued Payroll	(6,650)
Increase (Decrease) in Prizes Payable	(124,734)
Increase (Decrease) in Unearned Revenue	46,605
Increase (Decrease) in Net Pension Liability	(1,253,727)
Increase (Decrease) in Net Other Postemployment Benefit Plan Liability	(13,799)
Increase (Decrease) in Compensated Absences Payable	(18,165)
Total Adjustments	<u>\$ (728,949)</u>
Net Cash Provided by Operating Activities	<u>\$ 6,605,723</u>
Noncash Investing, Capital, and Financing Activities:	
Lease for Building	\$ 175,632
Interest Revenue on Prize Reserves	1,822
Total Noncash Activity	<u>\$ 177,454</u>

The accompanying Notes to the Financial Statements are an integral part of this statement.

Notes to the Financial Statements

Note 1. Summary of Significant Accounting Policies

Reporting Entity

In accordance with Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*, the Lottery should include all component units over which the Lottery exercises such aspects as (1) appointing a voting majority of an organization's governing body and (2) has the ability to impose its will on that organization; or (3) the potential for the organization to provide specific financial benefits to, or impose specific burdens on the Lottery.

Based on the criteria of GASB Statement No. 14, no organization was determined to be part of the Lottery as a reporting entity. The Lottery is a division of the Office of Attorney General, which is part of the primary government of the state of North Dakota.

Basis of Accounting and Measurement Focus

The Lottery's activity is accounted for as a proprietary type enterprise fund for the state of North Dakota. A proprietary fund is accounted for using the accrual basis of accounting. Revenues are recognized when they are earned, and expenses are recognized when they are incurred.

An enterprise fund is used to account for an activity that is financed and operated in a manner similar to a private business enterprise where the costs of providing goods or services to the public on a continuing basis are financed through the sale of those goods or services. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. An enterprise fund is accounted for by using the economic resources measurement focus in which all assets and liabilities associated with the operation of the funds are included on the statement of net position. Net position is segregated into investments in capital assets and restricted and unrestricted components. The statement of revenues, expenses, and changes in net position presents increases and decreases in total net position. The statement of cash flows presents the cash flows for operating, investing, capital, and non-capital financing activities.

According to North Dakota Century Code chapter 53-12.1, the Lottery must be self-funded and self-sustaining. As a result, general fund monies of the state may not be used or obligated to pay expenses or prizes of the Lottery.

Accounting Standards

The Lottery follows the pronouncements of the GASB, which is the nationally accepted standard-setting body for establishing generally accepted accounting principles for governmental entities.

Operating and Nonoperating Revenues

An enterprise fund distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the proprietary fund's principal ongoing operation. The principal operating revenue of the Lottery is sales of tickets. The principal operating expenses of the Lottery are prizes, retailer commissions, contractual services, marketing, MUSL game group dues, and salaries and fringe benefits. All revenue and expenses not meeting the criteria are reported as nonoperating revenues and expenses.

Cash and Cash Equivalents

Cash and cash equivalents are defined as deposits with the Bank of North Dakota and the State Treasurer. The Lottery does not invest in marketable securities.

Cash at Fiscal Agent

Cash at fiscal agent is the balance in the bank account held by Scientific Games, Inc. to service Pick & Click on the internet. This account balance consists of ticket sales netted with prize expense, player account withdrawals, discounts, and bank fees. As of June 30, 2022, the balance was \$537,526.

Accounts Receivable

Accounts receivable primarily represents prizes due from MUSL and Lottery funds due from retailers for ticket sales, less commissions and prizes on winning tickets paid by retailers. Lottery funds are collected weekly through electronic funds transfer by the Lottery from retailers' bank accounts. The Lottery has not incurred and does not project any bad debts.

Reserves on Deposit

As of June 30, 2022, the Lottery has \$1,397,053 on deposit with MUSL related to the Prize Reserve Pools and Unreserved Account. When both restricted and unrestricted resources are available, which is only applicable for certain MUSL related expenses, it is the Lottery's policy to generally use restricted resources first. See Note 8.

Prepaid Expenses

The prepaid expenses are primarily dues and postage. There was \$11,710 of prepaid expenses on June 30, 2022.

Equipment and Software

Equipment and software are stated at cost, net of accumulated depreciation. Equipment and software with a cost of \$5,000 or more per unit are capitalized and reported in the accompanying financial statements. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, which range from three to fifteen years.

Leases – Right of Use

A right-of-use lease or lease asset is a contract that conveys control of the right to use another entity's nonfinancial asset as specified in the contract for a period in an exchange or exchange-like transaction.

The contract with Scientific Games, LLC to use machines, software and services required to conduct the business of the North Dakota Lottery is paid based on a percentage of tickets sold using the underlying assets of the contract. These variable payments are recognized as expenses in the period the obligation is incurred.

Prizes

Prize expense is recorded based on actual drawing results. Prize expense also includes the net prize expense paid to MUSL according to the prize pool rates and game terms disclosed in the Multi-State Lottery Association note to the financial statements.

Prizes payable is the difference between the amounts of prize expense recognized (won) and actual prizes paid (claimed).

Players may redeem winning tickets for up to 180 days after the draw. As of June 30, 2022, prizes payable was \$487,893. Prizes that expired during fiscal year ended June 30, 2022, were \$537,405.

Unearned Revenue

The Lottery recorded a liability for lottery tickets, multi-draw tickets and for Pick & Click sales for draws that will occur after June 30, 2022. The amount related to future ticket sales on multi-draw tickets was \$141,561, as of June 30, 2022. Future sales for Pick & Click, as of June 30, 2022, were \$107,585.

Sales of uncashed gift certificates for fiscal year ended June 30, 2022, were \$7,554. Sales of uncashed play central terminal (PCT) vouchers for fiscal years ended June 30, 2022, were \$63,060. The Lottery classifies uncashed gift certificates and uncashed PCT vouchers as unearned revenue.

Interfund Balances and Transfers

On June 30, 2022, the Lottery had nominal accounts payable and accounts receivable involving normal business expenses with several state agencies and had net proceeds due to one state fund.

By statute, the net proceeds of the Lottery, less the amount allocated to the Compulsive Gambling Prevention and Treatment Fund, amount allocated to the Multijurisdictional Drug Task Force Grant Fund, Lottery's share of a game's prize reserve pool, and holdback of any reserve funds the division may need for continuing operations, must be transferred to the State Treasurer on at least an annual basis for deposit in the State General Fund. By statute, \$80,000 must be transferred to the State Treasurer each quarter for deposit in the Compulsive Gambling Prevention and Treatment Fund. By statute, \$200,000 must be transferred to the State Treasurer each quarter for deposit in the Multijurisdictional Drug Task Force Grant Fund. The reserve funds held by the division are required to be transferred to MUSL for prize reserve pools. The balance of the net proceeds is transferred to the State General Fund.

Retailer Commissions

Lottery retailers receive a 5% commission on each ticket sold or otherwise provided to players, and for Pick & Click, players may choose to designate to a recipient retailer. Effective January 1, 2006, the Lottery provides retailers a bonus commission, as a sales incentive, for selling jackpot/grand prize and certain high tier prize winning tickets. The Lottery does not provide retailers a commission for redeeming winning tickets. Total retailer commissions for June 30, 2022, were \$1,366,369, including bonus commissions of \$44,250.

Marketing and Advertising

Costs incurred for developing creative, including point-of-sale items, research, and media advertising are expensed when incurred which generally is when point-of-sale items are first distributed to retailers or advertising first takes place.

Pensions

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

Other Post-Employment Benefits (OPEB)

For purposes of measuring the net OPEB liability, deferred outflows of resources and deferred inflows of resources related to OPEB, and OPEB expense, information about the fiduciary net position of the North Dakota Public Employees Retirement System (NDPERS) and additions to/deductions from NDPERS' fiduciary net position have been determined on the same basis as they are reported by NDPERS. For this purpose, benefit payments are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Accumulated Unpaid Vacation, Sick Pay, and Compensatory Pay

Annual leave and sick leave are a part of permanent employees' compensation as set forth in Section 54-06-14 of the North Dakota Century Code. Annual leave is earned based on tenure of employment, within a range of a minimum of one working day per month of employment, to a maximum of two working days per month of employment, to be fixed by rules and regulations adopted by the employing unit. In general, accrued annual leave cannot exceed 30 days on April 30 each year, as set by the North Dakota Administrative Code Section 4-7-12-08. Employees are paid for unused annual leave upon termination or retirement.

Sick leave is earned at the rate of one working day per month of employment. There are no limitations on the amount of sick leave that an employee can accumulate. Employees who have ten continuous years of service are paid one-tenth of their accumulated sick leave upon termination or retirement under chapter 54-52 of the North Dakota Century Code. A liability is recognized for that portion of accumulated sick leave benefits that is estimated will be taken as required by the GASB Statement No. 16, *Accounting for Compensated Absences*.

Compensatory leave is earned by employees who work overtime each week in accordance with the Office of Attorney General's policy. Generally, upon termination or retirement, employees are not eligible to receive compensation for their compensatory leave balances.

Deferred Outflows/Inflows of Resources

In addition to assets, the statement of net position reports a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense/expenditure) until then.

In addition to liabilities, the statement of net position reports a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources*, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time.

New Accounting Pronouncements

During fiscal year 2022, the Lottery adopted GASB Statement No. 87, Leases, GASB Statement No. 89, Accounting for Interest Cost Incurred before the End of a Construction Period, GASB Statement No. 91, Conduit Debt Obligations, GASB Statement No. 92, Omnibus 2020, GASB Statement No. 93, Replacement of Interbank Offered Rates, GASB Statement No. 97, Certain Component Unit Criteria, and Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans.

The Lottery will implement the following new pronouncements for fiscal years ending after 2022: GASB Statement No. 94, Public-Private and Public-Public Partnerships and Availability Payment Arrangements, GASB Statement No. 96, Subscription-Based Information Arrangements (SBITAs), GASB Statement No. 99, Omnibus 2022, GASB Statement No. 100, Accounting Changes and Error Corrections—an amendment of GASB Statement No. 62, and GASB Statement No. 101, Compensated Absences. The effect that these GASB Statements will have on future financial statements has not yet been determined.

Note 2. Deposits

Custodial Credit Risk

State law generally requires all state funds be deposited in the state-owned Bank of North Dakota. North Dakota Century Code (NDCC) Section 21-04-01 provides that public funds belonging to or in the custody of the state shall be deposited in the Bank of North Dakota. Also, NDCC Section 6-09-07 states, “[a]ll state funds ... must be deposited in the Bank of North Dakota” or must be deposited in accordance with constitutional and statutory provisions.

The Lottery deposits at the Bank of North Dakota on June 30, 2022, were \$7,361,549.

These deposits are exposed to custodial credit risk as uninsured and uncollateralized. However, these deposits at the Bank of North Dakota are guaranteed by the state of North Dakota through NDCC Section 6-09-10.

Note 3. Compensated Absences

A summary of compensated absences follows for 2022:

Balance July 1, 2021	\$ 77,929
Addition	-
Reduction	<u>(18,165)</u>
Balance June 30, 2022	<u>\$ 59,764</u>
Amount payable within one year	<u>\$ -</u>

Note 4. Due to / Due from Other State Funds

On June 30, 2022, accounts payable due to several state agencies and transfers of net proceeds due to the state general fund are:

	<u>June 30, 2022</u>
Due to the Department of Transportation	\$ 1,676
Due to the Information Technology Department	4,899
Due to the Office of Management and Budget	137
Due to the Office of State Tax Commissioner	13,572
Due to the Office of the Secretary of State	36
Due to the State General Fund	<u>5,600,000</u>
Total	<u>\$ 5,620,320</u>

Note 5. Equipment and Software

A summary of changes in equipment, software, and accumulated depreciation is as follows for 2022:

	<u>Equipment</u>	<u>Software</u>	<u>Accumulated Depreciation</u>	<u>Net</u>
Balance, June 30,2021	\$ 58,337	\$ 32,000	\$ 78,496	\$ 11,841
Additions	-	-	3,122	(3,122)
Disposals	-	-	-	-
Balance, June 30,2022	<u>\$ 58,337</u>	<u>\$ 32,000</u>	<u>\$ 81,618</u>	<u>\$ 8,719</u>

Note 6. Employee Pension Plan

General Information about the Pension Plan

North Dakota Public Employees Retirement System (Main System)

The following brief description of NDPERS is provided for general information purposes only. Participants should refer to NDCC Chapter 54-52 for more complete information.

NDPERS is a cost-sharing multiple-employer defined benefit pension plan that covers substantially all employees of the State of North Dakota, its agencies and various participating political subdivisions. NDPERS provides for pension, death and disability benefits. The cost to administer the plan is financed through the contributions and investment earnings of the plan.

Responsibility for administration of the NDPERS defined benefit pension plan is assigned to a Board comprised of nine members. The Board consists of a chairman, who is appointed by the Governor; one member appointed by the Attorney General; one member appointed by the State Health Officer; three members elected by the active membership of the NDPERS system, one member elected by the retired public employees and two members of the legislative assembly appointed by the chairman of the legislative management.

Pension Benefits

Benefits are set by statute. NDPERS has no provisions or policies with respect to automatic and ad hoc post-retirement benefit increases. Member of the Main System are entitled to unreduced monthly pension benefits beginning when the sum of age and years of credited service equal or exceed 85 (Rule of 85), or at normal retirement age (65). For members hired on or after January 1, 2016, the Rule of 85 was replaced with the Rule of 90 with a minimum age of 60. The monthly pension benefit is equal to 2.00% of their average monthly salary, using the highest 36 months out of the last 180 months of service, for each year of service. For members hired on or after January 1, 2020, the 2.00% multiplier was replaced with a 1.75% multiplier. The plan permits early retirement at ages 55-64 with three or more years of service.

Members may elect to receive the pension benefits in the form of a single life, joint and survivor, term-certain annuity, or partial lump sum with ongoing annuity. Members may elect to receive the value of their accumulated contributions, plus interest, as a lump sum distribution upon retirement or termination, or they may elect to receive their benefits in the form of an annuity. For each member electing an annuity, total payment will not be less than the members' accumulated contributions plus interest.

Death and Disability Benefits

Death and disability benefits are set by statute. If an active member dies with less than three years of service for the Main System, a death benefit equal to the value of the member's accumulated contributions, plus interest, is paid to the member's beneficiary. If the member has earned more than three years of credited service for the Main System, the surviving spouse will be entitled to a single payment refund, life-time monthly payments in an amount equal to 50% of the member's accrued normal retirement benefit, or monthly payments in an amount equal to the member's accrued 100% Joint and Survivor retirement benefit if the member had reached normal retirement age prior to date of death. If the surviving spouse dies before the member's accumulated pension benefits are paid, the balance will be payable to the surviving spouse's designated beneficiary.

Eligible members who become totally disabled after a minimum of 180 days of service, receive monthly disability benefits equal to 25% of their final average salary with a minimum benefit of \$100. To qualify under this section, the member has to become disabled during the period of eligible employment and apply for benefits within one year of termination. The definition for disabled is set by the NDPERS in the North Dakota Administrative Code.

Refunds of Member Account Balance

Upon termination, if a member of the Main System is not vested (is not 65 or does not have three years of service), they will receive the accumulated member contributions and vested employer contributions, plus interest, or may elect to receive this amount at a later date. If the member has vested, they have the option of applying for a refund or can remain as a terminated vested participant. If a member terminated and withdrew their accumulated member contribution and is subsequently reemployed, they have the option of repurchasing their previous service.

Member and Employer Contributions

Member and employer contributions paid to NDPERS are set by statute and are established as a percent of salaries and wages. Member contribution rates are 7% and employer contribution rates are 7.12% of covered compensation. For members hired on or after January 1, 2020, member contribution rates are 7% and employer contribution rates are 8.26% of covered compensation.

The member's account balance includes the vested employer contributions equal to the member's contributions to an eligible deferred compensation plan. The minimum member contribution is \$25, and the maximum may not exceed the following:

- 1 to 12 months of service – Greater of one percent of monthly salary or \$25
- 13 to 24 months of service – Greater of two percent of monthly salary or \$25
- 25 to 36 months of service – Greater of three percent of monthly salary or \$25
- Longer than 36 months of service – Greater of four percent of monthly salary or \$25

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

On June 30, 2022, the North Dakota Lottery reported a liability of \$630,842 for its proportionate share of the net pension liability. The net pension liability was measured as of July 1, 2021, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The North Dakota Lottery's proportion of the net pension liability was based on the North Dakota Lottery's share of covered payroll in the Main System pension plan relative to the covered payroll of all participating Main System employers. On June 30, 2021, the North Dakota Lottery's proportion was 0.060524%, which was an increase of 0.000621% from its proportion measured as of June 30, 2020, which was 0.059903%.

For the year ended June 30, 2022, the North Dakota Lottery recognized pension expense of \$102,055. On June 30, 2022, the North Dakota Lottery reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 10,891	\$ 64,386
Changes of assumptions	698,219	910,332
Net difference between projected and actual earnings on pension plan investments	-	233,969
Changes in proportion and difference between employer contributions and proportionate share of contributions	21,484	14,622
Employer contributions subsequent to the measurement date (see below)	48,758	-
Total	<u>\$ 779,352</u>	<u>\$ 1,223,309</u>

The \$48,758 reported as deferred outflows of resources related to pensions resulting from employer contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2023.

Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended June 30:	
2023	\$ (72,170)
2024	(110,694)
2025	(86,555)
2026	(223,295)
2027	-
Thereafter	-

Actuarial assumptions

The total pension liability in the July 1, 2021, actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	2.25%
Salary increases	3.5% to 17.75% including inflation
Investment rate of return	7.00% net of investment expenses
Cost-of-living adjustments	None

For active members, inactive members and healthy retirees, mortality rates were based on the Sex-distinct Pub-2010 table for General Employees, with scaling based on actual experience. Respective corresponding tables were used for healthy retirees, disabled retirees, and active members. Mortality rates are projected from 2010 using the MP-2019 scale.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic real rates of return for each major asset class included in the Fund's target asset allocation are summarized in the following table:

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Domestic Equity	30%	6.00%
International Equity	21%	6.70%
Private Equity	7%	9.50%
Domestic Fixed Income	23%	0.73%
International Fixed Income	0%	0.00%
Global Real Assets	19%	4.77%
Cash Equivalents	0%	0.00%

Discount Rate

For PERS, GASB Statement No. 67 includes a specific requirement for the discount rate that is used for the purpose of the measurement of the Total Pension Liability. This rate considers the ability of the System to meet benefit obligations in the future. To make this determination, employer contributions, employee contributions, benefit payments, expenses and investment returns are projected into the future. The current employer and employee fixed rate contributions are assumed to be made in each future year. The Plan Net Position (assets) in future years can then be determined and compared to its obligation to make benefit payments in those years. In years where assets are not projected to be sufficient to meet benefit payments, which is the case for the PERS plan, the use of a municipal bond rate is required.

The Single Discount Rate (SDR) is equivalent to applying these two rates to the benefits that are projected to be paid during the different time periods. The SDR reflects (1) the long-term expected rate of return on pension plan investments (during the period in which the fiduciary net position is projected to be sufficient to pay benefits) and (2) a tax-exempt municipal bond rate based on an index of 20-year general obligation bonds with an average AA credit rating as of the measurement date (to the extent that the contributions for use with the long-term expected rate of return are not met).

For the purpose of this valuation, the expected rate of return on pension plan investments is 7.00%; the municipal bond rate is 1.92%; and the resulting Single Discount Rate is 7.00%.

Sensitivity of the Employer's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate

The following presents the North Dakota Lottery's proportionate share of the net pension liability calculated using the discount rate of 7.00 percent, as well as what the North Dakota Lottery's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (6.00 percent) or 1-percentage-point higher (8.00 percent) than the current rate:

	1% Decrease (6.00%)	Current Discount Rate (7.00%)	1% Increase (8.00%)
North Dakota Lottery's proportionate share of the net pension liability	\$1,003,250	\$630,842	\$320,753

Pension Plan Fiduciary Net Position

Detailed information about the pension plan's fiduciary net position is available in the separately issued NDPERS financial report.

Note 7. Other Postemployment Benefit Plan (OPEB)

General Information about the OPEB Plan

North Dakota Public Employees Retirement System

The following brief description of NDPERS is provided for general information only. Participants

should refer to NDAC Chapter 71-06 for more complete information.

NDPERS OPEB plan is a cost-sharing multiple-employer defined benefit OPEB plan that covers members receiving retirement benefits from the PERS, the HPRS, and Judges retired under Chapter 27-17 of the North Dakota Century Code a credit toward their monthly health insurance premium under the state health plan based upon the member's years of credited service. Effective July 1, 2015, the credit is also available to apply towards monthly premiums under the state dental, vision and long-term care plan and any other health insurance plan. Effective August 1, 2019, the benefit may be used for any eligible health, prescription drug plan, dental, vision, or long-term care plan premium expense. The Retiree Health Insurance Credit Fund is advance funded on an actuarially determined basis.

Responsibility for administration of the NDPERS defined benefit OPEB plan is assigned to a Board comprised of nine members. The Board consists of a chairman, who is appointed by the Governor; one member appointed by the Attorney General; one member appointed by the State Health Officer; three members elected by the active membership of the NDPERS system, one member elected by the retired public employees and two members of the legislative assembly appointed by the chairman of Legislative Management.

OPEB Benefits

The employer contribution for the PERS, the HPRS and the Defined Contribution Plan is set by statute at 1.14% of covered compensation. The employer contribution for employees of the state board of career and technical education is 2.99% of covered compensation for a period of eight years ending October 1, 2015. Employees participating in the retirement plan as part-time/temporary members are required to contribute 1.14% of their covered compensation to the Retiree Health Insurance Credit Fund. Employees purchasing previous service credit are also required to make an employee contribution to the Fund. The benefit amount applied each year is shown as "prefunded credit applied" on the Statement of Changes in Plan Net Position for the OPEB trust funds. Beginning January 1, 2020, members first enrolled in the NDPERS Main System and the Defined Contribution Plan on or after that date will not be eligible to participate in RHIC. Therefore, RHIC will become for the most part a closed plan. There were no other benefit changes during the year.

Retiree health insurance credit benefits and death and disability benefits are set by statute. There are no provisions or policies with respect to automatic and ad hoc post-retirement benefit increases. Employees who are receiving monthly retirement benefits from the PERS, the HPRS, the Defined Contribution Plan, the Chapter 27-17 judges or an employee receiving disability benefits, or the spouse of a deceased annuitant receiving a surviving spouse benefit or if the member selected a joint and survivor option are eligible to receive a credit toward their monthly health insurance premium under the state health plan.

Effective July 1, 2015, the credit is also available to apply towards monthly premiums under the state dental, vision and long-term care plan and any other health insurance plan. Effective August 1, 2019, the benefit may be used for any eligible health, prescription drug plan, dental, vision, or long-term care plan premium expense. The benefits are equal to \$5.00 for each of the employee's, or deceased employee's, years of credited service not to exceed the premium in effect for selected coverage. The retiree health insurance credit is also available for early retirement with reduced benefits.

OPEB Liabilities, OPEB Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB

On June 30, 2022, the North Dakota Lottery reported a liability of \$34,963 for its proportionate share of the net OPEB liability. The net OPEB liability was measured as of July 1, 2021, and the total OPEB liability used to calculate the net OPEB liability was determined by an actuarial valuation as of that date. The North Dakota Lottery's proportion of the net OPEB liability was based on the North Dakota Lottery's share of covered payroll in the OPEB plan relative to the covered payroll of all participating OPEB employers. On June 30, 2021, the North Dakota Lottery's proportion was 0.062863%, which was an increase of 0.004896% from its proportion measured as of June 30, 2020, which was 0.057967%.

For the year ended June 30, 2022, the North Dakota Lottery recognized OPEB expense of \$4,846. On June 30, 2022, the Lottery reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 2,008	\$ 958
Changes of assumptions	5,414	-
Net difference between projected and actual earnings on OPEB plan investments	-	11,979
Changes in proportion and difference between employer contributions and proportionate share of contributions	2,147	1,409
Employer contributions subsequent to the measurement date (see below)	7,807	-
Total	<u>\$ 17,376</u>	<u>\$ 14,346</u>

\$7,807 reported as deferred outflows of resources related to OPEB resulting from Employer contributions subsequent to the measurement date will be recognized as a reduction of the net OPEB liability in the year ended June 30, 2023.

Other 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:	
2023	\$ (655)
2024	(742)
2025	(1,298)
2026	(2,300)
2027	218
Thereafter	-

Actuarial Assumptions

The total OPEB liability in the July 1, 2021, actuarial valuation was determined using the following

actuarial assumptions, applied to all periods included in the measurement:

Inflation	2.25%
Salary increases	Not Applicable
Investment rate of return	6.50% net of investment expenses
Cost-of-living adjustments	None

For active members, inactive members and healthy retirees, mortality rates were based on the MortalityPub-2010 Healthy Retiree Mortality table (for General Employees), sex-distinct, with rates multiplied by 103% for males and 101% for females. Pub-2010 Disabled Retiree Mortality table (for General Employees), sex-distinct, with rates multiplied by 117% for males and 112% for females. Pub-2010 Employee Mortality table (for General Employees), sex-distinct, with rates multiplied by 92% for both males and females. Mortality rates are projected from 2010 using the MP-2019 scale.

The long-term expected investment rate of return assumption for the RHIC fund was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of RHIC investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Estimates of arithmetic real rates of return, for each major asset class included in the RHIC’s target asset allocation as of July 1, 2021, are summarized in the following table:

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Large Cap Domestic Equities	33%	5.85%
Small Cap Domestic Equities	6%	6.75%
Domestic Fixed Income	40%	0.50%
International Equities	21%	6.25%

Discount Rate

The discount rate used to measure the total OPEB liability was 6.50%. The projection of cash flows used to determine the discount rate assumed plan member and statutory rates described in this report. For this purpose, only employer contributions that are intended to fund benefits of current RHIC members and their beneficiaries are included. Projected employer contributions that are intended to fund the service costs of future plan members and their beneficiaries are not included. Based on those assumptions, the RHIC fiduciary net position was projected to be sufficient to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on RHIC investments was applied to all periods of projected benefit payments to determine the total OPEB liability.

Sensitivity of the Employer's proportionate share of the net OPEB liability to changes in the discount rate

The following presents the net OPEB liability of the Plans as of June 30, 2021, calculated using the discount rate of 6.50%, as well as what the RHIC net OPEB liability would be if it were calculated using a discount rate that is 1-percentage-point lower (5.50 percent) or 1-percentage-point higher (7.50 percent) than the current rate

	1% Decrease (5.50%)	Current Discount Rate (6.50%)	1% Increase (7.50%)
North Dakota Lottery's proportionate share of the net OPEB liability	\$51,854	\$34,963	\$20,670

Note 8. Multi-State Lottery Association (MUSL)

The Lottery is a member of MUSL, which administers games on behalf of member lotteries. MUSL administers the Powerball, Mega Millions, Lotto America, and 2by2 games for the Lottery. Each member lottery sells game tickets through its retailers and makes weekly wire transfers to MUSL in an amount equal to the member lottery's share of the jackpot prize liability. If this results in a negative amount, MUSL transfers funds to the Lottery. Lesser prizes are paid directly to the winners by each member lottery. The prize pools for Powerball, Powerplay, Lotto America and All Star Bonus are 50% of each drawing period's sales, after the prize reserve accounts are funded to the amounts set by the game groups. The prize pool for Mega Millions is up to 50% of the Mega Millions and Megaplier sales. The prize pool for 2by2 is 39.5% with the prize expense being 67% after the free tickets as of June 30, 2022. Up to 5% of sales for Powerball are deducted from the prize pool contribution and placed in one or more prize pool and prize reserve accounts. Up to 5% of sales for Mega Millions are added to the prize pool contribution and placed in one or more prize pool and prize reserve accounts. The Lotto America prize pool and prize reserve deduction is set at 2% when the annuity jackpot is \$3 million or more and less than \$5 million, and 4% when the annuity jackpot is \$5 million or more. The game group places the deducted sales in one or more prize pool and prize reserve accounts.

The prize reserve funds serve as a contingency reserve to protect MUSL from unforeseen prize liabilities and the money in this reserve fund is used at the discretion of the MUSL board of directors. The prize reserve fund monies are refundable to MUSL member lotteries if MUSL dissolves or if a member lottery leaves MUSL. A member lottery leaving MUSL must wait one year before receiving their remaining share, if any, of the prize reserve funds. Any amount remaining in the prize pools at the end of the games is carried forward to a replacement game or expended in a manner as directed by the game group. The MUSL prize reserve account balance and the Lottery's share of that balance are as follows:

	<u>June 30, 2022</u>
MUSL prize reserve account	\$ 216,388,841
Lottery's share of the MUSL prize reserve account (on deposit)	\$ 1,006,501

The Lottery also has an unreserved account with MUSL. Interest earned on MUSL funds, and any unclaimed jackpot prizes may be deposited into this account and Lottery board and game group dues and other MUSL related expenses may be paid from this fund.

	<u>June 30, 2022</u>
MUSL unreserved account	\$ 20,501,598
Lottery's share of the MUSL's unreserved account	\$ 390,552

A winner of a Powerball, Mega Millions or Lotto America jackpot prize may select that the prize be paid at the cash value of the prize or as an annuity. A Powerball or Lotto America jackpot prize is paid out in 30 installments and a Mega Millions jackpot prize is paid out in 26 installments. If a jackpot winner selects annual installments for Powerball, Mega Millions or Lotto America, MUSL purchases United States government securities to fund awarded prizes. The securities are held in Winner Trust accounts with the member lottery named as the trust beneficiary. MUSL transfers cash to the member lotteries to facilitate the payment of the annual jackpot prize amount. The source of this money is a game group's grand prize pool. The assets and related liabilities are reflected in MUSL's financial statements and, therefore, are not reflected in the Lottery's financial statements. MUSL is responsible for transferring the cash or the annuity installment amounts to the member lottery before the payment to the jackpot prize winner. The Lottery currently is not paying any Powerball, Mega Millions or Lotto America prize winner annuity prize payments. The 2by2 grand prize is paid in a single cash payment. The Powerball, Mega Millions and Lotto America jackpot prizes are divided equally among multiple winning tickets among the participating jurisdictions.

The North Dakota Lottery is a member of the MUSL board and Powerball, Mega Millions, Lotto America, and 2by2 game groups. The Lottery is responsible for its pro-rated share of the MUSL board dues. The MUSL Board dues for fiscal year ended June 30, 2022, were \$20,000. MUSL's non-game earnings including interest, web advertising, and trademark license fees decrease the MUSL board dues and game group dues.

During fiscal year ended June 30, 2016, the Lottery was licensed to begin selling the Lucky for Life game as offered by the group of lotteries known as the New England Lotteries. The New England Lotteries consists of the Connecticut Lottery Corporation, the Main State Liquor & Lottery Commission, the Massachusetts State Lottery Commission, the New Hampshire Lottery Commission, the Rhode Island Division of Lotteries and the Vermont Lottery Commission.

If a top prize or second tier prize winner selects annual installments for Lucky for Life, the Lottery is responsible for the purchase of an insurance annuity or other financial instrument to fully fund the respective annuitized prize won in North Dakota. The Lottery has contracted MUSL to purchase annuities following a claim of a lifetime prize that requires the acquisition of an annuity. The Lottery is currently paying one Lucky for Life second tier prize winner annuity prize payments.

The Lottery is assessed dues quarterly in proportion to the Lottery's percentage of Lucky for Life game sales to pay for operating expenses incurred during the assessed quarter. The New England Lotteries contracted MUSL as the Lucky for Life game administrator.

Note 9. Commitments and Contingencies

The Lottery entered contracts with:

1. Scientific Games International, Inc. (SGI) of Alpharetta, GA provides an online lottery gaming system; retailer network including retailer training, communications, equipment, ticket stock and management; and an internet lottery service. The contract was signed on February 19, 2014, with an operations date of July 6, 2014, and shall continue through June 30, 2024.

Payments for the fiscal year ended June 30, 2022, totaled \$3,040,108 based on 10.473% of ticket sales. The Lottery's future obligation through June 30, 2024, is based on 9.573% of ticket sales. Additionally, the Lottery pays SGI an annual minimum fee of \$325,000 to provide the Player's Club Points for Prizes program. In addition, SGI provides other products and services for which the Lottery pays various contracted fees. The total fees paid to SGI for all services for the fiscal year ended June 30, 2022, were \$3,430,665.

2. KKBold of Bismarck, ND provides marketing and related services. The Lottery awarded a contract to KKBold with a term from July 1, 2017, through June 30, 2022. As of June 30, 2022, this contract expired.

In accordance with the terms and conditions of the State Term Contract #268 Marketing Communications Services Pool master agreement between State and Vendor, the Lottery executed a one-year Task Order request with KK Bold. The contract is not to exceed \$650,000 which includes, but not limited to, all professional services, production, travel, and purchasing of media advertisements. The contract will cover a period beginning July 1, 2022 and conclude on June 30, 2023.

Payments for the fiscal year ended June 30, 2022, totaled \$267,059. The Lottery's future obligation is for actual services requested; there is no minimum fee or retainer fee.

The Lottery has a contingent gain estimated at \$177,968 on June 30, 2022, from prizes that may be forfeited due to winning players not claiming them within the required time frame. The Lottery did not accrue this contingent gain on these financial statements. The Lottery will recognize the gain when realized.

Note 10. Line of Credit

In accordance with subsection 2 of section 53-12.1-02 of the North Dakota Century Code, the Lottery has secured a short-term line of credit with the Bank of North Dakota. The law provides that the line of credit be limited to the amount of each cash prize of \$100,000 or more that relates to prize funds known to be due and forthcoming to the Lottery from other government-authorized lotteries through MUSL. The line of credit may not exceed \$1 million in the aggregate. The North Dakota Lottery did not request a credit advance during the fiscal year ending June 30, 2022.

Note 11. Risk Management

The Lottery is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Lottery, as a division of the Office of Attorney General, participates in the same funds/pools established by the state for risk management issues.

The 1995 Legislative Assembly established the Risk Management Fund (RMF), an internal service fund, to provide a self-insurance vehicle for funding the liability exposures of state agencies resulting from the elimination of the state's sovereign immunity. The RMF manages the tort liability of the state, its agencies' employees, and the University System. All state agencies participating in the RMF, and their fund contributions were determined using a projected cost allocation approach. The statutory liability of the state is limited to a total of \$250,000 per person and \$1 million per occurrence.

The Office of Attorney General also participates in the North Dakota Fire and Tornado Fund. The office pays an annual premium to the Fire and Tornado Fund to cover property damage to building and office contents. Replacement cost coverage is provided by estimating replacement cost in consultation with the Fire and Tornado Fund.

The Office of Attorney General also participates in the State Bonding Fund in which the office has blanket employee fidelity bond coverage in the amount of \$2 million. The State Bonding Fund did not charge any premium for this coverage at this point.

Note 12. Lease Commitments

The State of North Dakota, Attorney General's Office entered a lease commencing on July 1, 2021, for office space located at 1720 Burlington Avenue, Bismarck, ND. The Lottery occupies 3,988 square feet or 12.08% of the rented space.

The lease term i.e., period of a noncancelable right to use the office space, is 10 years with one ten-year extension. However, as of June 30, 2022, an amendment to the lease has been drafted and is reasonably certain to be ratified. The amendment will modify the term of the lease to 60 months (5 years) and includes three renewal options for a period of 60 months each renewal term. For purposes of this note disclosure, management has determined it is reasonably certain, based on all relevant factors, the State of North Dakota, Attorney General's Office will not exercise any of the renewal options.

The basis of the lease is \$11.94 per square foot per annum for the first year and \$12.05 per square foot thereafter. Additionally, rent associated with the operating expenses of the building and grounds, commonly known as CAM expenses, are to be paid at \$5.70 per square foot per annum. Cam expenses will be adjusted annually by one percent. Cam expenses are not included in the amount of lease assets or liabilities.

Lease Asset and Accumulated Amortization:

<u>Description</u>	<u>Net Asset Balance</u>	<u>Accumulated Amortization</u>	<u>Gross Asset Balance</u>
Office Space	\$175,632	\$33,463	\$209,095

Principal and interest requirements to maturity:

<u>Fiscal Year Ending</u>	<u>Leases</u>			<u>Total Outflows</u>
	<u>Payable (Principal)</u>	<u>Interest</u>	<u>CAM</u>	
6/30/2023	\$ (40,995)	\$ (7,065)	\$ (22,734)	\$ (70,794)
6/30/2024	(42,879)	(5,181)	(22,734)	(70,794)
6/30/2025	(44,849)	(3,211)	(22,734)	(70,794)
6/30/2026	(46,909)	(1,151)	(22,734)	(70,794)
	<u>\$ (175,632)</u>	<u>\$ (16,608)</u>	<u>\$ (90,936)</u>	<u>\$ (283,176)</u>

Required Supplementary Information

Schedule of Employer's Share of Net Pension Liability ND Public Employees Retirement System Last 10 Fiscal Years*

	Employer's proportion of the net pension liability (asset)	Employer's proportionate share of the net pension liability (asset)	Employer's covered- employee payroll	Employer's proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll	Plan fiduciary net position as a percentage of the total pension liability
2022	0.060524%	\$ 630,842	\$ 685,368	92.04%	78.26%
2021	0.059903%	1,884,569	660,805	285.19%	48.91%
2020	0.061636%	722,420	641,120	112.68%	71.66%
2019	0.062132%	1,048,537	638,288	164.27%	62.80%
2018	0.059981%	964,098	612,316	157.53%	61.98%
2017	0.058897%	574,007	593,541	96.71%	70.46%
2016	0.062919%	427,838	560,531	76.33%	77.15%
2015	0.065803%	417,667	554,314	75.35%	77.70%

*Complete data for this schedule is not available prior to 2015.

The amounts presented for each fiscal year have a measurement date of the previous fiscal year end.

**Schedule of Employer Contributions
ND Public Employees Retirement System
Last 10 Fiscal Years***

	Statutorily required contribution	Contributions in relation to the statutorily required contribution	Contribution deficiency (excess)	Employer's covered- employee payroll	Contributions as a percentage of covered-employee payroll
2022	\$ 50,543	\$ (53,666)	\$ (3,123)	\$ 684,810	7.38%
2021	46,791	(43,784)	3,007	685,368	6.83%
2020	46,677	(47,333)	(656)	660,805	7.06%
2019	47,013	(45,765)	1,248	641,120	7.33%
2018	44,400	(47,399)	(2,999)	638,288	6.96%
2017	42,972	(43,789)	(817)	612,316	7.02%
2016	42,577	(42,514)	63	593,541	7.17%
2015	39,467	(39,467)	-	560,531	7.04%

*Complete data for this schedule is not available prior to 2015.

**Schedule of Employer's Share of Net OPEB Liability
ND Public Employees Retirement System
Last 10 Fiscal Years***

	Employer's proportion of the net OPEB liability (asset)	Employer's proportionate share of the net OPEB liability (asset)	Employer's covered- employee payroll	Employer's proportionate share of the net OPEB liability (asset) as a percentage of its covered-employee payroll	Plan fiduciary net position as a percentage of the total OPEB liability
2022	0.062863%	\$ 34,963	\$ 685,368	5.10%	76.63%
2021	0.057967%	48,762	660,805	7.38%	63.38%
2020	0.057455%	46,147	641,120	7.20%	63.13%
2019	0.058333%	45,941	638,288	7.20%	61.89%
2018	0.056599%	44,771	612,316	7.31%	59.78%

*Complete data for this schedule is not available prior to 2018.

The amounts presented for each fiscal year have a measurement date of the previous fiscal year end.

**Schedule of Employer Contributions
ND Public Employees Retirement System
Last 10 Fiscal Years***

	Statutorily required contribution	Contributions in relation to the statutorily required contribution	Contribution deficiency (excess)	Employer's covered- employee payroll	Contributions as a percentage of covered-employee payroll
2022	\$ 8,242	\$ (8,649)	\$ (407)	\$ 684,810	1.20%
2021	7,763	(7,033)	730	685,368	1.13%
2020	7,456	(7,476)	(20)	660,805	1.13%
2019	7,487	(7,096)	391	641,120	1.17%
2018	7,118	(7,422)	(304)	638,288	1.12%

*Complete data for this schedule is not available prior to 2018

Notes to the Required Supplementary Information

Changes of benefit terms

The interest rate earned on member contributions decreased from 7.00 percent to 6.50 percent effective January 1, 2021 (based on the adopted decrease in the investment return assumption). New Main System members who are hired on or after January 1, 2020, will have a benefit multiplier of 1.75 percent (compared to the current benefit multiplier of 2.00 percent). The fixed employer contribution for new members of the Main System increased from 7.12 percent to 8.26 percent. For members who terminate after December 31, 2019, final average salary is the higher of the final average salary calculated on December 31, 2019, or the average salary earned in the three highest periods of twelve consecutive months employed during the last 180 months of employment. There have been no other changes in plan provisions since the previous actuarial valuation as of July 1, 2020.

Beginning January 1, 2020, members first enrolled in the NDPERS Main System and the Defined Contribution Plan on or after that date will not be eligible to participate in RHIC. Therefore, RHIC will become for the most part a closed plan. There have been no other changes in plan provisions since the previous actuarial valuation as of July 1, 2020.

Changes of assumptions

All other actuarial assumptions and the actuarial cost method are unchanged from the last actuarial valuation as of July 1, 2020.



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Exhibits

Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards

Independent Auditor's Report

Members of the Legislative Assembly

Honorable Drew Wrigley, Attorney General

Lance Gaebe, Director North Dakota Lottery

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the business-type activities of the North Dakota Lottery, a division of the Office of the Attorney General of the state of North Dakota as of and for the year ended June 30, 2022, and the related notes to the financial statements, which collectively comprise the North Dakota Lottery's financial statements, and have issued our report thereon dated April 13, 2023.

Report on Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the North Dakota Lottery's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the North Dakota Lottery's internal control. Accordingly, we do not express an opinion on the effectiveness of the North Dakota Lottery's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to

prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether the North Dakota Lottery's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

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

/S/

Joshua C. Gallion
State Auditor

Bismarck, North Dakota
April 13, 2023

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Governance Communication

April 13, 2023

Honorable Drew Wrigley, Attorney General

Legislative Audit and Fiscal Review Committee

We have audited the financial statements of the business-type activities of the North Dakota Lottery for the year ended June 30, 2022. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated September 16, 2022. Professional standards also require that we communicate to you with the following information related to our audit.

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the North Dakota Lottery are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year. We noted no transactions entered into by the North Dakota Lottery during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the North Dakota Lottery's financial statements were:

- Useful lives of capital assets
- Net pension and OPEB liabilities

Management's estimate of the useful lives, as described in Note 1, is used to compute depreciation on capital assets. Management's estimate of the net pension liability and net OPEB liability is based on an actuary's calculation in accordance with the employment contracts. We evaluated the key factors and assumptions used to develop the useful lives, net pension liability, and net OPEB liability in determining that they are reasonable in relation to the financial statements taken as a whole.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and report them to the appropriate level of management. No such misstatements were noted.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, or reporting matter that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated April 13, 2023.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the North Dakota Lottery financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the North Dakota Lottery's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Other Matters

We applied certain limited procedures to the management's discussion and analysis, the Schedule of Employer's Share of Net Pension Liability, the Schedule of Employer Contributions (Pension), the Schedule of Employer's Share of Net OPEB Liability, and the Schedule of Employer Contributions (OPEB) which are required supplementary information (RSI) that supplements the basic financial statements. Our procedures consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We did not audit the RSI and do not express an opinion or provide any assurance on the RSI.

Restriction on Use

This information is intended solely for the use of Attorney General Drew Wrigley, the Legislative Audit and Fiscal Review Committee, and management of the North Dakota Lottery and is not intended to be, and should not be, used for any other purpose. We would be happy to meet with you and any member of your staff to discuss any of the items in this letter in more detail if you so desire.

Thank you to Mr. Gaebe and the employees of the North Dakota Lottery for the courteous and friendly assistance we received during the course of our audit. It is a pleasure for us to be able to serve the North Dakota Lottery.

Respectfully,



Lindsey Slappy, CPA
Audit Manager



Office of the
State Auditor

NORTH DAKOTA STATE AUDITOR
JOSHUA C. GALLION

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