

**REPORT OF THE AUDIT OF THE
KENTUCKY LOTTERY CORPORATION**

**For The Years Ended
June 30, 2023 and 2022**



**MIKE HARMON
AUDITOR OF PUBLIC ACCOUNTS
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MIKE HARMON
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky
Honorable Andy Beshear, Governor
Honorable Robert Stivers, President, Kentucky Senate
Honorable David Osborne, Speaker of the House, Kentucky House of Representatives
Board of Directors, Kentucky Lottery Corporation

The enclosed report prepared by MCM CPAs and Advisors, LLP presents the financial and compliance audit of the books and records of the Kentucky Lottery Corporation for the years ended June 30, 2023 and 2022, as required by KRS 154A.130.

We engaged MCM CPAs and Advisors, LLP to perform the audit in accordance with auditing standards generally accepted in the United States of America. We worked closely with the firm during our report review process.

Respectfully Submitted,

Farrah Petter, CPA
Assistant Auditor of Public Accounts

Enclosure

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Financial Report

June 30, 2023 and 2022

KENTUCKY LOTTERY CORPORATION

ANNUAL FINANCIAL REPORT
June 30, 2023 and 2022

CONTENTS

INDEPENDENT AUDITOR'S REPORT	1
MANAGEMENT'S DISCUSSION AND ANALYSIS.....	4
BASIC FINANCIAL STATEMENTS:	
STATEMENTS OF NET POSITION	19
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION....	20
STATEMENTS OF CASH FLOWS	21
NOTES TO FINANCIAL STATEMENTS.....	22
INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH <i>GOVERNMENT AUDITING STANDARDS</i>	41
SCHEDULE OF FINDINGS.....	43
SCHEDULE OF PRIOR AUDIT FINDINGS AND THEIR RESOLUTIONS.....	44

Independent Auditor's Report

To the Auditor of Public Accounts,
the Commonwealth of Kentucky, and
the Board of Directors of the Kentucky Lottery Corporation
Louisville, Kentucky

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of the Kentucky Lottery Corporation, a component unit of the Commonwealth of Kentucky as of and for the years ended June 30, 2023 and 2022, and the related notes to the financial statements, which collectively comprise Kentucky Lottery Corporation's basic financial statements as listed in the table of contents.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Kentucky Lottery Corporation, as of June 30, 2023 and 2022, and the changes in financial position and its cash flows 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* ("GAS"), 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 Kentucky Lottery Corporation 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 opinion.

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 Kentucky Lottery Corporation'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.

Independent Auditor's Report (Continued)

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 opinion. 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 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, 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 Kentucky Lottery Corporation'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 Kentucky Lottery Corporation'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 on pages 4 - 18 be presented to supplement the basic financial statements. Such information is the responsibility of management and, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Independent Auditor's Report (Continued)

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated September 22, 2023 on our consideration of the Kentucky Lottery Corporation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of 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 Kentucky Lottery Corporation's internal control over financial reporting and compliance.

A handwritten signature in black ink that reads "MCM CPAs & Advisors LLP". The signature is written in a cursive, stylized font.

Louisville, Kentucky
September 22, 2023

KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Our discussion of the Kentucky Lottery Corporation's ("KLC") financial performance provides an overview of the KLC's financial activities for the fiscal years ended June 30, 2023 and 2022. Please read it in conjunction with the financial statements, which follow.

Financial Highlights for Fiscal Year 2023

- Record operating revenues of \$1.841 billion were achieved in 2023, an increase of \$164.5 million or 9.8 percent over last year's previous sales record of \$1.677 billion. For fiscal year 2023 represents the twelfth consecutive year of record sales for the KLC.
- Sales at retail totaled \$1.416 billion and accounted for 77 percent of total sales. iLottery sales totaled \$424.7 million and made up the remaining 23 percent of sales for the year.
- Instant sales totaled \$943.5 million, which is a \$20.0 million decrease over last year. A total of 52 new games were launched in 2023 including the first \$50 game.
- Draw sales increased \$16.6 million to \$503.5 million. Mega Millions and Powerball record and near record jackpots accounted for most of the increase in sales, collectively increasing \$46.3 million over last year.
- iLottery instant play sales hit a record \$394.0 million. This was a \$167.9 million or 74.3 percent increase over last year. An expanded portfolio of game categories were offered, including progressive jackpot games with an 87 percent prize payout, compared to the 85 percent payout for other instant play games.
- Operating expenses totaled \$36.5 million which accounted for a record low 2.0 percent of sales.
- Record dividend transfers to the state of \$384.3 million, an increase of \$25.0 million or 7.0 percent over last year.

The KLC is accounted for as an enterprise fund, reporting on all of the activity's assets and liabilities using the accrual basis of accounting much like a private business activity. As such, this annual financial report consists of a series of financial statements, along with explanatory notes to the financial statements.

To assess the KLC's financial position and financial health, the reader of these statements should pay particular attention to changes in the components of assets and liabilities as set forth on the Statements of Net Position, and in changes in operating revenues and expenses as set forth in the Statements of Revenues, Expenses, and Changes in Net Position.

Total Assets

Total assets consist primarily of cash and equivalents, investments, accounts receivable, right-to-use lease assets, owned capital assets and deposits. As shown in Table 1, the KLC's total assets increased \$7.7 million to \$135.5 million in 2023. Total assets decreased \$2.5 million to \$127.8 million in 2022 from \$130.3 million in 2021. Investments consist of U.S. Treasury zero-coupon bonds and other U.S. Government backed securities carried at fair value. Accounts receivable represent revenue to be collected primarily from the sale of draw and instant game tickets. Accounts receivable decreased \$5.8 million to \$69.2 million in 2023. Accounts receivable increased \$9.8 million to \$75.0 million in 2022. Right-to-use lease assets represent equipment leases. Additional information on the KLC's lease can be found in Note 10 to the financial statements.

KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Capital Assets

The KLC's investment in capital assets, net of accumulated depreciation and right-to-use amortization in 2023 and 2022, was \$11.1 and \$14.2 million, respectively. The investment in capital assets includes buildings, game equipment, data processing equipment and software, automobiles, furniture, and fixtures, and right-to-use lease assets. The total decrease in the KLC's investment in capital assets for 2023 was \$3.1 million or 21.8 percent compared to a decrease of \$4.0 million or 22.0 percent in 2022. Additional information on the KLC's investment in capital assets can be found in Note 6 to the financial statements.

TABLE 1
NET POSITION
(In millions)

	2023	Increase (Decrease)	2022	Increase (Decrease)	2021
Current and other assets	\$ 110.9	\$ 7.9	\$ 103.0	\$ 3.6	\$ 99.4
Investments (noncurrent)	8.5	3.2	5.3	(1.8)	7.1
Capital assets					
Owned assets	4.4	(0.2)	4.6	(0.6)	5.2
Right-of-use lease Assets	<u>6.7</u>	<u>(2.9)</u>	<u>9.6</u>	<u>(3.4)</u>	<u>13.0</u>
Capital assets, net	11.1	(3.1)	14.2	(4.0)	18.2
Deposits with Multi State Lottery Association	<u>5.0</u>	<u>(0.3)</u>	<u>5.3</u>	<u>(0.3)</u>	<u>5.6</u>
Total assets	<u>135.5</u>	<u>7.7</u>	<u>127.8</u>	<u>(2.5)</u>	<u>130.3</u>
Current liabilities	105.8	10.5	95.3	2.4	92.9
Noncurrent liabilities	<u>12.8</u>	<u>(2.2)</u>	<u>15.0</u>	<u>(4.2)</u>	<u>19.2</u>
Total liabilities	<u>118.6</u>	<u>8.3</u>	<u>110.3</u>	<u>(1.8)</u>	<u>112.1</u>
Net position components					
Net investment in capital assets	4.4	(0.2)	4.6	(0.6)	5.2
Unrestricted - accumulated					
unrealized gains on investments	(0.2)	(0.5)	0.3	(0.7)	1.0
Unrestricted	<u>12.7</u>	<u>0.1</u>	<u>12.6</u>	<u>0.6</u>	<u>12.0</u>
Net position	<u>\$ 16.9</u>	<u>\$ (0.6)</u>	<u>\$ 17.5</u>	<u>\$ (0.7)</u>	<u>\$ 18.2</u>

KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Liabilities

TABLE 2
LIABILITIES
(In millions)

	Current			Noncurrent		
	2023	2022	2021	2023	2022	2021
Accounts payable and other liabilities	\$ 11.4	\$ 12.0	\$ 13.4	\$ 0.6	\$ 0.5	\$ 0.5
Prize liabilities	77.6	70.1	64.4	8.8	8.5	9.8
Due to Commonwealth	13.5	9.5	11.0	0.0	0.0	0.0
Lease Liabilities	<u>3.3</u>	<u>3.7</u>	<u>4.1</u>	<u>3.4</u>	<u>6.0</u>	<u>8.9</u>
Total liabilities	<u>\$ 105.8</u>	<u>\$ 95.3</u>	<u>\$ 92.9</u>	<u>\$ 12.8</u>	<u>\$ 15.0</u>	<u>\$ 19.2</u>

Total current liabilities increased \$10.5 million or 11.0 percent in 2023 and \$2.4 million or 2.6 percent in 2022. The account titled "Due to Commonwealth" increased \$4.0 million in 2023 and decreased \$1.5 million in 2022. This represents payments due to the General Fund and the Kentucky Educational Excellence Scholarship Reserve Account after the fiscal year-end.

Noncurrent liabilities decreased \$2.2 million or 14.7 percent in 2023 and decreased \$4.2 million or 21.9 percent in 2022. Noncurrent liabilities consist principally of prize liabilities for prizes paid in installments over several years and the noncurrent portion of accrued compensated absences. More detailed information can be obtained in Note 8 to the financial statements. Lease liabilities represent the present value of future payments related to equipment leases. Additional information on the KLC's lease can be found in Note 10 to the financial statements.

Net Position

As shown in Table 1 on page 5, the KLC's net position in 2023 decreased \$0.6 million. Most of the decrease is due to increases in current prize liabilities and an increase in the payable to the Commonwealth. Total net position of \$16.9 million included the KLC's net investment in capital assets of \$11.1 million and \$12.5 million in unrestricted net position. Unrestricted net position was comprised of \$200,000 in accumulated unrealized loss on investments and \$12.7 million in working capital and cash flow that is utilized in the KLC's day-to-day operations. In 2022, the KLC's net position decreased \$0.7 million to \$17.5 million due to the decrease in the accumulated unrealized gains on investments.

KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Net Position (Continued)

TABLE 3
CHANGES IN NET POSITION
(In millions)

	Increase		Increase		
	<u>2023</u>	<u>(Decrease)</u>	<u>2022</u>	<u>(Decrease)</u>	<u>2021</u>
Operating revenues					
Instant games	\$ 943.5	\$ (20.0)	\$ 963.5	\$ 1.8	\$ 961.7
Draw games	503.5	16.6	486.9	(19.1)	506.0
iLottery instant play games	394.0	167.9	226.1	107.5	118.6
Total operating revenues	<u>\$1,841.0</u>	<u>\$ 164.5</u>	<u>\$1,676.5</u>	<u>\$ 90.2</u>	<u>\$1,586.3</u>
Direct costs and operating expenses:					
Direct costs					
Prize expense	1,292.1	140.1	1,152.0	84.6	1,067.4
Other direct costs	130.3	1.3	129.0	(1.7)	130.7
Total direct costs	<u>1,422.4</u>	<u>141.4</u>	<u>1,281.0</u>	<u>82.9</u>	<u>1,198.1</u>
Operating expenses	36.5	0.1	36.4	3.2	33.2
Total direct costs and operating expenses	<u>1,458.9</u>	<u>141.5</u>	<u>1,317.4</u>	<u>86.1</u>	<u>1,231.3</u>
Non-operating expense (revenue)	(1.6)	(2.1)	0.5	0.1	0.4
Payments to the Commonwealth of Kentucky	384.2	24.9	359.3	4.2	355.1
Total expenses	<u>1,841.5</u>	<u>164.3</u>	<u>1,677.2</u>	<u>90.4</u>	<u>1,586.8</u>
Changes in net position	<u>(0.5)</u>	<u>0.2</u>	<u>(0.7)</u>	<u>(0.2)</u>	<u>(0.5)</u>
Net position at beginning of year	<u>17.5</u>	<u>(0.7)</u>	<u>18.2</u>	<u>(0.5)</u>	<u>18.7</u>
Net position at end of year	<u>\$ 17.0</u>	<u>\$ (0.5)</u>	<u>\$ 17.5</u>	<u>\$ (0.7)</u>	<u>\$ 18.2</u>

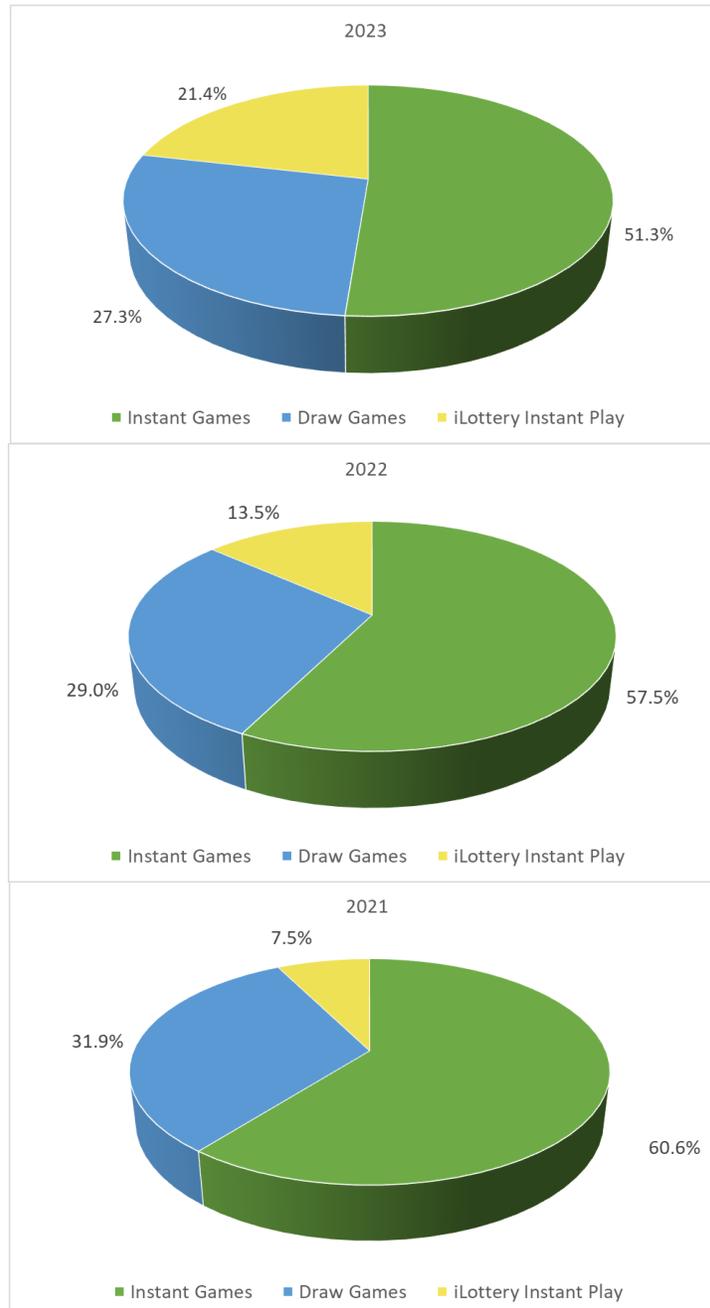
KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Operating Revenues and Prize Expense

Operating Revenues

In 2023, operating revenues consisted of ticket sales from three product categories, instant, draw, and iLottery instant play. In 2023, the KLC generated record ticket sales of \$1.841 billion, an increase of \$164.5 million or 9.8 percent when compared to 2022. In 2022, the KLC generated ticket sales of \$1.677 billion, an increase of \$90.2 million or 5.7 percent when compared to 2021.

SALES BY PRODUCT CATEGORY AS A PERCENT OF SALES



KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Instant Games

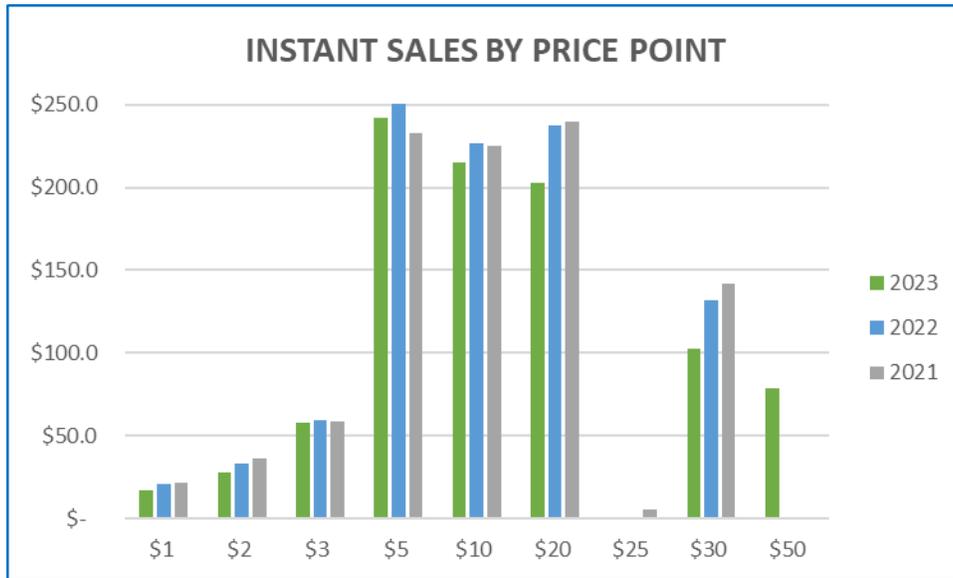
Table 4 and the accompanying chart compares sales for each instant game price point for 2023, 2022, and 2021.

TABLE 4
INSTANT SALES BY PRICE POINT
(In millions)

Price Point	2023			2022			2021	
	Sales	% of Total	Increase (Decrease)	Sales	% of Total	Increase (Decrease)	Sales	% of Total
\$1	\$ 17.1	1.8%	\$ (3.7)	\$ 20.8	2.2%	\$ (0.9)	\$ 21.7	2.3%
\$2	27.9	3.0%	(5.2)	33.1	3.4%	(2.8)	35.9	3.7%
\$3	58.0	6.1%	(1.7)	59.7	6.2%	0.9	58.8	6.1%
\$5	242.2	25.7%	(12.3)	254.5	26.4%	22.1	232.4	24.2%
\$10	214.7	22.8%	(11.9)	226.6	23.5%	1.3	225.3	23.4%
\$20	202.7	21.5%	(34.6)	237.3	24.6%	(2.6)	239.9	24.9%
\$25	-	0.0%	-	-	0.0%	(5.6)	5.6	0.6%
\$30	102.6	10.9%	(28.9)	131.5	13.7%	(10.6)	142.1	14.8%
\$50	78.3	8.4%	78.3	-	0.0%	-	-	0.0%
Totals	\$ 943.5	100.0%	\$ (20.0)	\$ 963.5	100.0%	\$ 1.8	\$ 961.7	100.0%

KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Instant Games (Continued)



KLC instant ticket sales of \$943.5 million were achieved in 2023 and accounted for 51.3 percent of all KLC sales, a decrease of \$20.0 million or 2.1 percent over 2022. Instant ticket sales of \$963.5 million were achieved in 2022, and accounted for 57.5 percent of all KLC sales, or an increase of \$1.8 million or 0.2 percent over 2021.

Sales decreased in 2023 within the instant product category at all existing price points. Like other consumer products, lottery sales, specifically scratch-off sales, were impacted by a softening economy and pressure on disposable income. A new \$50 price point was introduced and generated \$78.3 million in sales or 8.3 percent of all instant ticket sales. See Table 4 for all price point sales and changes from prior year.

Sales growth in 2022 within the instant product category occurred at the \$3, \$5, and \$10 price points, which saw increases of \$0.9 million, \$22.1 million, and \$1.3 million respectively.

Sales decreases in 2022 were recognized at the \$1, \$2, \$20, and \$30 price point with a decrease of 0.9 percent, 2.8 percent, 2.6 percent, and 10.6 percent respectively. The Lottery industry had seen a shift away from the lower price points.

KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Draw Games

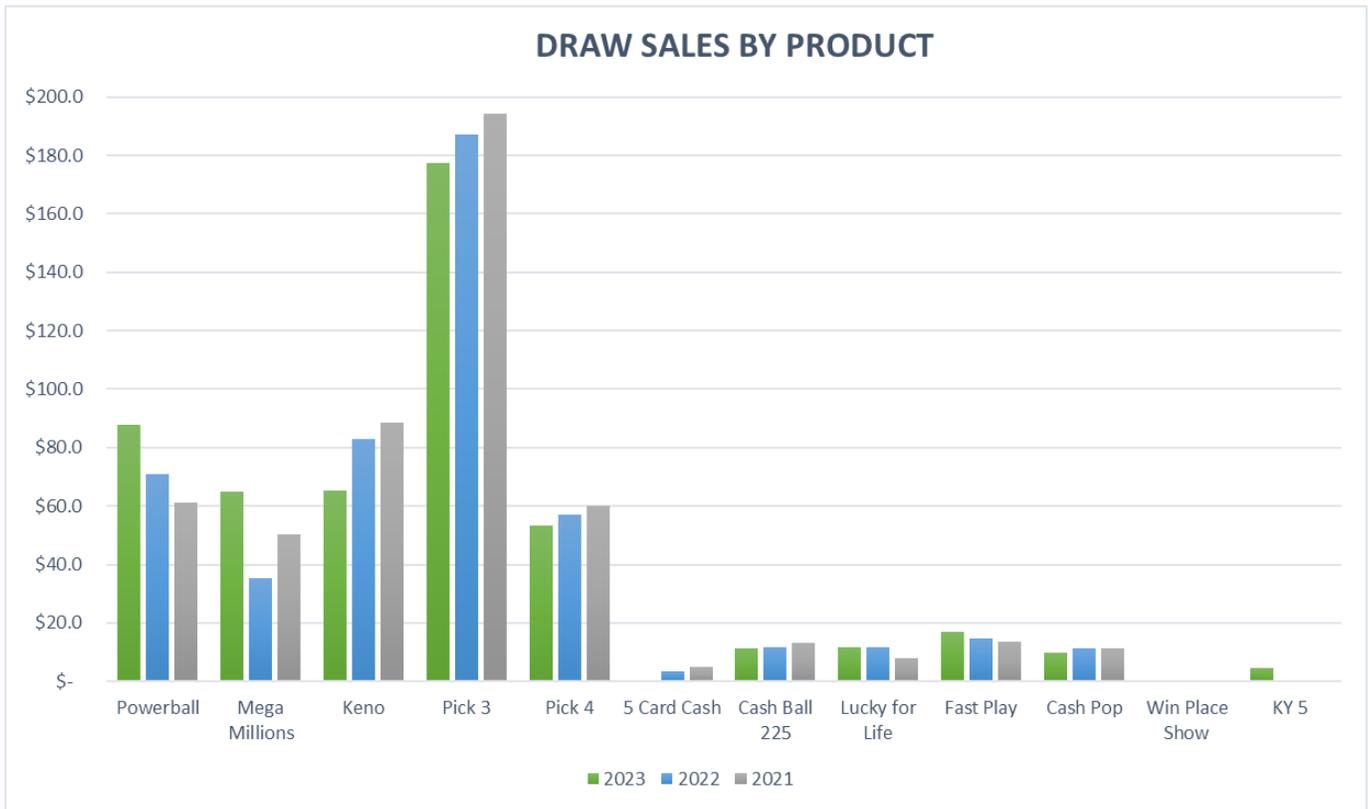
Table 5 and the accompanying chart compares draw sales by product for 2023, 2022, 2021.

**TABLE 5
DRAW SALES BY PRODUCT
(In millions)**

Product	2023			2022			2021	
	Sales	% of Total	Increase (Decrease)	Sales	% of Total	Increase (Decrease)	Sales	% of Total
Powerball	\$ 87.9	17.5%	\$ 16.8	\$ 71.1	14.6%	\$ 9.8	\$ 61.3	12.1%
Mega Millions	65.0	12.9%	29.5	35.5	7.3%	(14.7)	50.2	9.9%
Keno	65.4	13.0%	(17.7)	83.1	17.1%	(5.5)	88.6	17.5%
Pick 3	177.2	35.2%	(9.9)	187.1	38.4%	(7.1)	194.2	38.4%
Pick 4	53.3	10.6%	(3.8)	57.1	11.7%	(3.1)	60.2	11.9%
5 Card Cash	-	0.0%	(3.3)	3.3	0.7%	(1.7)	5.0	1.0%
Cash Ball 225	11.3	2.2%	(0.6)	11.9	2.4%	(1.4)	13.3	2.6%
Lucky for Life	11.9	2.4%	0.2	11.7	2.4%	3.9	7.8	1.5%
Fast Play	17.1	3.4%	2.5	14.6	3.0%	1.0	13.6	2.7%
Cash Pop	9.8	1.9%	(1.7)	11.5	2.4%	-	11.5	2.3%
Win Place Show	-	0.0%	-	-	0.0%	(0.3)	0.3	0.1%
KY 5	4.6	0.9%	4.6	-	0.0%	-	-	0.0%
Totals	\$ 503.5	100.0%	\$ 16.6	\$ 486.9	100.0%	\$ (19.1)	\$ 506.0	100.0%

KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Draw Games (Continued)



Draw sales were \$503.5 million in 2023, an increase of \$16.6 million or 3.4 percent when compared to 2022. Draw games sales accounted for 27.3 percent of all of 2023 sales, and consisted of Powerball, Mega Millions, Keno, Pick 3, Pick 4, Cash Ball 225, Lucky for Life, Fast Play, Cash Pop, and a new draw game, Kentucky 5, introduced in 2023.

Draw sales were \$486.9 million in 2022, a decrease of \$19.1 million or 3.8 percent when compared to 2021. Draw games sales accounted for 29.0 percent of all 2022 sales, and consisted of Powerball, Mega Millions, Keno, Pick 3, Pick 4, 5 Card Cash, Cash Ball 225, Lucky for Life, Fast Play, and Cash Pop. Sales ended for 5 Card Cash in March 2022.

Sales increases were recognized in Powerball, Mega Millions, Lucky for life, and Fast Play when compared to 2022. During 2023 the KLC introduced a new daily rolling jackpot draw game, Kentucky 5, which accounted for \$4.6 million or 0.9 percent of total draw sales.

Sales decreases were recognized in all other draw games.

iLottery Instant Play Games

iLottery instant play 2023 sales were \$394.0 million, an increase of \$167.9 when compared to the \$226.1 million achieved in 2022. iLottery instant play sales accounted for 21.4 percent of all 2023 sales and 13.5 percent of all 2022 sales. Instant play games consist of a variety of play styles, categories, and price points, ranging from \$0.10 to \$20.00.

KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Prize Expense

In general, prize expense by game should increase or decrease from year-to-year in proportion to the increase or decrease in sales for a particular game. However, except for the instant game product category, prize expense is also impacted by the luck of the draw. Prize expense for the instant game product category is controllable, to a large degree, by printing a predetermined number and value of winning tickets in the production of each instant game. Payouts range from 62 percent to 79 percent, depending on the game price point. Prize expense for draw games is not predetermined. While each of the draw games is designed to yield a certain ratio of prizes to sales revenue over a large number of drawings, actual prize payout is determined by lottery players' luck in matching the particular set of numbers randomly selected in each drawing for each game. Prize expense for iLottery instant play games is designed to yield a certain percent of prizes to sales revenue. The actual prize payout is determined at the time these games are played and the outcome is revealed. Actual prize payout may vary from the designed payout.

The following is a discussion of prize expense within certain product categories. With that background, Table 6 compares the actual gross payout percentages for 2023, 2022, and 2021.

**TABLE 6
GROSS PRIZE PAYOUT PERCENTAGES
ALL PRODUCTS**

	ACTUAL 2023	ACTUAL 2022	ACTUAL 2021
Instant Games	71.9%	71.4%	71.5%
Draw Games:			
Powerball	50.1%	49.9%	50.6%
Mega Millions	50.1%	50.6%	50.0%
Keno	65.1%	65.4%	65.2%
Pick 3	58.1%	59.7%	55.9%
Pick 4	46.7%	47.3%	56.7%
5 Card Cash	0.0%	69.8%	60.6%
Cash Ball 225	59.8%	51.7%	56.0%
Lucky for Life	63.5%	60.4%	68.1%
Fast Play	70.6%	70.0%	68.2%
Cash Pop	66.4%	67.4%	66.6%
Win Place Show	0.0%	0.0%	47.6%
Kentucky 5	53.6%	0.0%	0.0%
Draw Games	56.2%	57.5%	57.2%
iLottery Instant Play	86.6%	86.7%	84.2%
Total Gross Prize Payout Percentage	70.8%	69.4%	67.9%
Less: Unclaimed Prizes	-0.6%	-0.7%	-0.6%
Total Prize Payout Percentage	<u>70.2%</u>	<u>68.7%</u>	<u>67.3%</u>

KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Game Margin for Total Products

Table 7 and the accompanying chart compares game margin for total products for 2023, 2022, and 2021. Game margin is operating revenues less total prize expense.

**TABLE 7
GAME MARGIN FOR TOTAL PRODUCTS
(In millions)**

Total Products			
	2023	2022	2021
Operating revenues	\$ 1,841.0	\$ 1,676.5	\$ 1,586.3
Gross prize expense	1,302.8	1,164.0	1,077.2
Less: unclaimed prizes	(10.7)	(12.0)	(9.8)
Total prize expense	<u>1,292.1</u>	<u>1,152.0</u>	<u>1,067.4</u>
Game margin	<u>\$ 548.9</u>	<u>\$ 524.5</u>	<u>\$ 518.9</u>



For 2023, gross prize expense (excluding unclaimed prizes) of \$1.303 billion, reflects a \$138.3 million or 11.9 percent increase from 2022 of \$1.164 billion.

Total prize expense in 2023 was \$1.292 billion or 70.2 percent of total operating revenues compared to \$1.152 billion or 68.7 percent in 2022.

Total game margin in 2023 increased to \$548.9 or 29.8 percent of total operating revenues compared to \$524.5 million or 31.3 percent of total operating revenues in 2022. The increase in total game margin is \$24.4 million or 4.7 percent more than 2022.

Game Margin for Instant Games

Table 8 and the accompanying chart compares game margin for instant games 2023, 2022, and 2021.

**TABLE 8
GAME MARGIN FOR INSTANT GAMES
(In millions)**

Instant Games			
	2023	2022	2021
Operating revenues	\$ 943.5	\$ 963.5	\$ 961.7
Gross prize expense	678.6	687.8	687.9
Less: unclaimed prizes	(5.4)	(6.9)	(5.5)
Total prize expense	<u>673.2</u>	<u>680.9</u>	<u>682.4</u>
Game margin	<u>\$ 270.3</u>	<u>\$ 282.6</u>	<u>\$ 279.3</u>



In 2023, gross prize expense for instant games decreased to \$678.6 million or 71.9 percent of total instant game operating revenues compared to 71.4 percent in 2022.

KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Game Margin for Instant Games (Continued)

Total prize expense for instant games decreased to \$673.2 million or 71.4 percent of total instant game operating revenues compared to \$680.9 million or 70.7 percent in 2022.

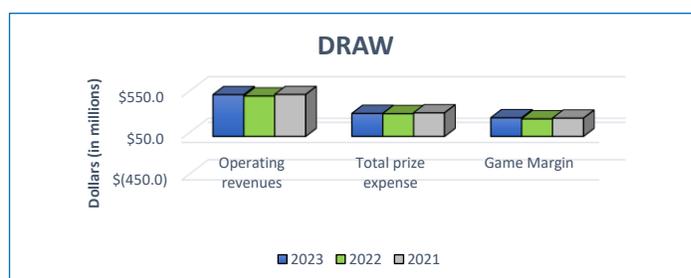
Game margin for instant games decreased to \$270.3 million or 28.6 percent of operating revenues for instant games compared to \$282.6 million or 29.3 percent in 2022. This decrease in game margin is \$12.3 million or 4.4 percent less than 2022.

Game Margin for Draw Games

Table 9 and the accompanying chart compares game margin for draw games for 2023, 2022, and 2021.

TABLE 9
GAME MARGIN FOR DRAW GAMES
(In millions)

Draw Games			
	2023	2022	2021
Operating revenues	\$ 503.5	\$ 486.9	\$ 506.0
Gross prize expense	283.0	280.1	289.4
Less: unclaimed prizes	(5.3)	(5.1)	(4.3)
Total prize expense	<u>277.7</u>	<u>275.0</u>	<u>285.1</u>
Game margin	<u>\$ 225.8</u>	<u>\$ 211.9</u>	<u>\$ 220.9</u>



In 2023, gross prize expense for draw games was \$283.0 million or 56.2 percent of operating revenues for draw games compared to \$280.1 million or 57.5 percent in 2022.

Total prize expense for draw games increased to \$277.7 or 55.2 percent of operating revenues for draw games in 2023 compared to \$275.0 million or 56.5 percent in 2022.

Game margin increased to \$225.8 million or 44.8 percent of operating revenues for draw games in 2023 compared to \$211.9 million or 43.5 percent in 2022. This increase in game margin is a \$13.9 million or 6.6 percent increase from 2022.

KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Game Margin for iLottery Instant Play Games

Table 10 and the accompanying chart compares operating revenues, prize expense, and game margin for iLottery instant play games for 2023, 2022, and 2021.

TABLE 10
GAME MARGIN FOR iLOTTERY INSTANT PLAY GAMES
(In millions)

iLottery Instant Play Games			
	2023	2022	2021
Operating revenues	\$ 394.0	\$ 226.1	\$ 118.6
Gross prize expense	341.2	196.1	99.9
Less: unclaimed prizes	0.0	0.0	0.0
Total prize expense	<u>341.2</u>	<u>196.1</u>	<u>99.9</u>
Game margin	<u>\$ 52.8</u>	<u>\$ 30.0</u>	<u>\$ 18.7</u>



In 2023, net prize expense for iLottery instant play games was \$341.2 million or 86.6 percent of operating revenues for iLottery instant play games compared to \$196.1 million or 86.7 percent in 2022.

Game margin for iLottery instant play games increased to \$52.8 million or 13.4 percent of operating revenues for iLottery instant play games in 2023 compared to \$30.0 million or 13.3 percent 2022. This increase in game margin is \$22.8 million or 76.0 percent more than 2022.

Other Expenses

TABLE 11
OTHER DIRECT COSTS, OPERATING, AND NON-OPERATING (REVENUE) EXPENSE
(In millions)

	Increase		Increase		
	2023	(Decrease)	2022	(Decrease)	2021
Payments to retailers	\$ 84.4	\$ (2.7)	\$ 87.1	\$ (3.5)	\$ 90.6
Draw games and iLottery vendor expense	30.9	4.5	26.4	2.1	24.3
Instant ticket costs	15.0	(0.5)	15.5	(0.3)	15.8
Total other direct costs	<u>130.3</u>	<u>1.3</u>	<u>129.0</u>	<u>(1.7)</u>	<u>130.7</u>
Operating expenses	36.5	0.1	36.4	3.2	33.2
Non-operating (revenue) expense	(1.6)	(2.1)	0.5	0.1	0.4

Payments to retailers cover base selling and cashing commissions as well as a retailer incentive plan based on the sale of instant tickets. Payments to retailers for 2023 and 2022 were 4.6 and 5.2 percent of total operating revenues. Draw games and iLottery vendor expenses for 2023 and 2022 were 1.7 percent and 1.6 percent of total operating revenues, respectively. Instant ticket costs include the cost to acquire and ship instant tickets to retailers and were 0.8 percent and 0.9 percent of total operating revenues in 2023 and 2022, respectively. Operating expenses were 2.0 percent and 2.2 percent of total operating revenues for 2023 and 2022, respectively.

KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Other Expenses (Continued)

Non-operating (revenue) expense, which includes investment income, accretion of investments, and other income, increased \$2.1 million in 2023 and decreased \$0.1 million in 2022.

Investment Income (Loss)

TABLE 12
INVESTMENT INCOME (LOSS)
(In millions)

	2023	Increase (Decrease)	2022	Increase (Decrease)	2021
Unrealized change in fair value of investments	\$ (0.5)	\$ 0.2	\$ (0.7)	\$ (0.2)	\$ (0.5)
Accretion of investments	0.3	(0.1)	0.4	0.0	0.4
Interest income	<u>1.8</u>	<u>1.8</u>	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>
Total investment income (loss)	<u>\$ 1.6</u>	<u>\$ 1.9</u>	<u>\$ (0.3)</u>	<u>\$ (0.2)</u>	<u>\$ (0.1)</u>

Unrealized change in fair value of investments represents the impact on income of recording investments at their fair value compared to the historical cost method. Accretion of investments reflects the net increase in the accreted cost of the investment.

Payments to the Commonwealth of Kentucky

In 2023 and 2022, payments to the Commonwealth of Kentucky represent transfers and an accrual of funds from the KLC to the Commonwealth's general fund, Trust and Agency account, and to the Kentucky Educational Excellence Scholarship ("KEES") Reserve Account. Payments to the general fund, which are approved by the Board of Directors and remitted to the Commonwealth on a monthly basis, are predominantly used by the General Assembly to pay for college scholarships, grants, and education programs. Payments to the KEES Reserve Account represent prizes of instant and draw games that expired (went unclaimed) during the fiscal year. Payments to the Commonwealth of Kentucky in 2023 were \$384.3 million which consisted of \$373.6 million or an increase of \$26.3 million to the Commonwealth's general fund and Trust and Agency account and \$10.7 million or a decrease of \$1.3 million to the KEES Reserve Account. Payments in 2022 were \$359.3 million, which consisted of \$347.3 million to the Commonwealth's general fund and \$12.0 million the KEES Reserve Account.

KENTUCKY LOTTERY CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2023 and 2022

Currently Known Facts, Decisions, or Conditions

The Kentucky Lottery Corporation's mission is to produce the maximum net revenues for the Commonwealth by offering the best lottery games to its citizens, games of the highest quality and integrity, which are consistent with good public policy and social responsibility, and to operate within the framework of public accountability. The lottery faces challenges with increased gaming competition and inflation. To achieve KLC's mission and overcome these obstacles, the KLC will continue to introduce new and/or enhanced instant, draw, and iLottery instant play product offerings to further increase sales in fiscal year 2024.

Budgeted sales for fiscal year 2024 total \$1.936 billion. Retail sales total \$1.368 billion and iLottery sales total \$568.0 million.

Instant sales are budgeted to produce sales of \$936.5 million during fiscal year 2024, an decrease of \$7.0 million or 0.7 percent.

- The KLC will introduce its second \$50 scratch-off game in September 2023.
- The KLC will introduce different prize structures, increasing the number of mid-tier prizes that players can redeem at retail locations. The KLC will also continue to assess and modify the variety of game offerings to attract new and existing players.

Draw game sales are budgeted to produce sales of \$459.5 million during fiscal year 2024, a decrease of \$44.0 million or 8.7 percent.

- The KLC does not anticipate record and near record Powerball and Mega Millions jackpots in fiscal year 2024. Combined sales for both games are expected to decline \$40.3 million, accounting for most of the total draw game sales decrease from fiscal year 2023.

iLottery instant play sales are budgeted to produce sales of \$540.0 million during fiscal year 2024, an increase of \$146.0 million or 37.1 percent.

- KLC will introduce additional game content, enhance promotions, and offer additional progressive jackpot games with a higher payout.

Contacting the KLC's Financial Management

This financial report is designed to provide the public and other interested parties with an overview of the financial results of the KLC's activities, and to show the KLC's accountability for the revenue that it generates. If you have any questions about this report or need additional financial information, contact the KLC's Public Relations Department at the Kentucky Lottery Corporation, 1011 West Main Street, Louisville, Kentucky 40202.

KENTUCKY LOTTERY CORPORATION

STATEMENTS OF NET POSITION Ended June 30, 2023 and 2022 (dollars in thousands)

	2023	2022
ASSETS		
Current Assets		
Cash and equivalents	\$ 38,931	\$ 22,895
Cash and equivalents, annuitants	0	2,639
Investments at fair value, current portion	1,343	1,384
Accounts receivable, net	69,209	74,956
Other assets	1,385	1,120
Total current assets	<u>110,868</u>	<u>102,994</u>
Noncurrent Assets		
Investments at fair value, less current portion	8,545	5,330
Capital assets		
Owned assets	4,405	4,577
Right-to-use lease assets	6,680	9,638
Capital assets, net	<u>11,085</u>	<u>14,215</u>
Deposits with Multi-State Lottery Association	4,990	5,268
Total noncurrent assets	<u>24,620</u>	<u>24,813</u>
Total assets	<u>135,488</u>	<u>127,807</u>
LIABILITIES		
Current Liabilities		
Accounts payable, accrued expenses, and compensated absences, current portion	11,392	12,018
Due to the Commonwealth of Kentucky	13,461	9,545
Estimated prize liability, current portion	77,648	70,071
Lease liability, current Portion	3,301	3,667
Total current liabilities	<u>105,802</u>	<u>95,301</u>
Noncurrent Liabilities		
Accrued compensated absences, less current portion	621	539
Estimated prize liability, less current portion	8,750	8,547
Lease liability, noncurrent portion	3,379	5,971
Total noncurrent liabilities	<u>12,750</u>	<u>15,057</u>
Total liabilities	<u>118,552</u>	<u>110,358</u>
NET POSITION		
Net investment in capital assets	11,085	14,215
Unrestricted	5,851	3,234
Net position	<u>\$ 16,936</u>	<u>\$ 17,449</u>

See accompanying notes.

KENTUCKY LOTTERY CORPORATION

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION For the Years Ended June 30, 2023 and 2022 (dollars in thousands)

	2023	2022
Operating revenues		
Instant games	\$ 943,456	\$ 963,495
Draw games	503,540	486,945
iLottery instant play games	394,001	226,062
Total operating revenues	<u>1,840,997</u>	<u>1,676,502</u>
Direct costs		
Prizes expense		
Instant games	673,151	680,908
Draw games	277,750	275,028
iLottery instant play games	341,225	196,071
Total prize expense	<u>1,292,126</u>	<u>1,152,007</u>
Payments to retailers	84,370	87,135
Draw games and iLottery vendor expense	30,921	26,377
Instant ticket costs	15,000	15,453
Total direct costs	<u>1,422,417</u>	<u>1,280,972</u>
Operating revenues net of direct costs	<u>418,580</u>	<u>395,530</u>
Operating expenses		
Advertising and promotion	11,999	12,991
Salaries, wages, and benefits	18,445	17,941
Contracted and professional services	2,485	2,314
Depreciation	1,303	1,142
Other general and administrative	2,228	2,027
Total operating expenses	<u>36,460</u>	<u>36,415</u>
Operating income	<u>382,120</u>	<u>359,115</u>
Non-operating (expense) revenue		
Payments to the Commonwealth of Kentucky	(384,258)	(359,333)
Investment income/(loss)	1,593	(353)
Accretion of investments	(346)	(363)
Other income	378	218
Total non-operating expense	<u>(382,633)</u>	<u>(359,831)</u>
Change in net position	<u>(513)</u>	<u>(716)</u>
Net position at beginning of year	<u>17,449</u>	<u>18,165</u>
Net position at end of year	<u>\$ 16,936</u>	<u>\$ 17,449</u>

See accompanying notes.

KENTUCKY LOTTERY CORPORATION

STATEMENTS OF CASH FLOWS For the Years Ended June 30, 2023 and 2022 (dollars in thousands)

	<u>2023</u>	<u>2022</u>
Cash Flows from Operating Activities		
Cash received from customers	\$ 1,846,744	\$ 1,666,739
Cash receipts for deposits at the Multi-State Lottery Association	278	314
Cash payments to prize winners	(1,284,346)	(1,147,623)
Cash payments to suppliers	(148,490)	(148,603)
Cash payments to employees for services	(18,126)	(17,312)
Net cash provided by operating activities	<u>396,060</u>	<u>353,515</u>
Cash Flows from Noncapital Financing Activities		
Payments to the Commonwealth of Kentucky	<u>(380,341)</u>	<u>(360,819)</u>
Cash Flows from Capital and Related Financing Activities		
Purchases of capital assets	<u>(1,168)</u>	<u>(531)</u>
Cash Flows from Investing Activities		
Proceeds from sale of investments	1,384	1,384
Purchases of investments	(4,725)	0
Investment income	2,187	242
Net cash (used in)/provided by investing activities	<u>(1,154)</u>	<u>1,626</u>
(Decrease) Increase in cash and equivalents	13,397	(6,209)
Cash and equivalents at beginning of year	<u>25,534</u>	<u>31,743</u>
Cash and equivalents at end of year	\$ 38,931	\$ 25,534
Reconciliation of Operating Income to Net Cash		
Provided by Operating Activities		
Operating income	<u>\$ 382,120</u>	<u>\$ 359,115</u>
Adjustments to reconcile operating income to net cash provided by operating activities		
Depreciation	1,303	1,142
Provision for losses on accounts receivable	(47)	34
Increase (decrease) in cash due to changes in:		
Accounts receivable, net	5,794	(9,797)
Other assets	(265)	(24)
Deposits with Multi-State Lottery Association	278	314
Accounts payable, accrued expenses, and compensated absences	(557)	(1,290)
Estimated prize liability	<u>7,434</u>	<u>4,021</u>
Total adjustments	<u>13,940</u>	<u>(5,600)</u>
Net cash provided by operating activities	<u>\$ 396,060</u>	<u>\$ 353,515</u>

Noncash capital and investing activities:

The accretion of interest on investments held to fund grand prizes, which increased prize liability for the years ended June 30, 2023 and 2022 totaled \$346 and \$363, respectively.

The unrealized fair value of investments decreased for the years ended June 30, 2023 and 2022 by \$513 and \$716, respectively.

See accompanying notes.

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2023 and 2022

(dollars in thousands)

Note 1 - Organization

The Kentucky Lottery Corporation ("KLC") was created with the enactment of House Bill No. 1 in December 1988 as an independent de jure municipal corporation and political subdivision of the Commonwealth of Kentucky ("Commonwealth"). The KLC is to be managed in such a manner that enables the people of the Commonwealth to benefit from its profits and to enjoy the best possible lottery games. The operations of the KLC are separate and distinct from other operations of the Commonwealth.

The KLC commenced operations on April 4, 1989 with the sale of instant game tickets. Sales of draw games began October 16, 1989. In January 1991, the KLC joined the Multi-State Lottery Association ("MUSL"), a group of states that combine lottery sales for draw games.

Note 2 - Summary of Significant Accounting Policies

Reporting Entity

The KLC has adopted the provisions of Government Accounting Standards Board ("GASB") Section 2100: *Defining the Financial Reporting Entity*, under which the financial statements include all the organizations, activities, functions, and component units for which the KLC is financially accountable. Financial accountability is defined as (1) the appointment of a voting majority of the potential component unit's Board, and either (a) the KLC's ability to impose its will over the potential component unit, or (b) the possibility that the potential component unit will provide a financial benefit to or impose a financial burden on the KLC, or (2) the potential component unit is fiscally dependent on the KLC, and will provide a financial benefit to or impose a financial burden on the KLC.

The KLC has determined that no outside agency meets the above criteria; therefore, no other agency has been included as a component unit in the KLC's financial statements. In addition, since the KLC provides a financial benefit for the Commonwealth, the KLC is part of the reporting entity of the Commonwealth and is, therefore, included in the Commonwealth's Annual Comprehensive Financial Report as a discretely presented component unit. The accompanying financial statements are not intended to present the financial position or the results of operations and cash flows of the Commonwealth or its proprietary funds.

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 2 - Summary of Significant Accounting Policies (Continued)

Basis of Presentation

The KLC is accounted for as an enterprise fund. The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. The financial statements are reported using the economic resources measurement focus. The financial statements include the accounts of KLC and have been prepared on the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when an obligation has been incurred.

As an enterprise fund, the KLC distinguishes *operating* revenues and expenses and direct costs from *non-operating* items. Operating revenues and expenses and direct costs generally result from providing services and delivering goods in connection with the KLC's principal ongoing operations. The principal operating revenues of the KLC are sales of lottery products. Direct expenses include the cost of sales and services and operating expenses include administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Revenue and Accounts Receivable Recognition

Revenue and accounts receivable for draw games are recognized when tickets are sold to the public.

Revenue and accounts receivable for instant games are recognized at the time packs of tickets are marked due or upon activation, whichever is sooner.

Revenue and accounts receivable for iLottery instant play games are recognized when games are sold to players on the iLottery portal. These games are played and results are revealed immediately after purchase.

Allowance for Doubtful Accounts

The KLC uses the allowance method to account for uncollectible accounts receivable. Trade receivables are written-off when deemed uncollectible. Recoveries of trade receivables previously written-off are recorded when received. KLC wrote off approximately \$90 and \$146 for the years ended June 30, 2023 and 2022, respectively. A trade receivable is considered uncollectible based on pertinent facts and circumstances.

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 2 - Summary of Significant Accounting Policies (Continued)

Prizes

Prize expense for instant ticket games is recorded as an estimate at the time the related revenue is recognized based on the predetermined prize structure for each game; after the last date to claim has passed, the prize expense is adjusted, if necessary, to reflect amounts actually won. Prize expense for draw games is recorded after each draw and is based on actual draw results. Prize expense for iLottery instant play games is recorded at the time of the purchase, when the outcome is determined.

Estimated Prize Liability

A liability for grand prize winners electing annual installments is recorded based on the cost of U.S. Treasury zero-coupon bonds and other U.S. Government agency securities purchased to fund the liability, adjusted for the accretion of interest based upon the purchased yield and maturity date. The estimated prize liability is presented in the statement of net position, net of this imputed interest. Imputed interest is amortized to accretion of investments over the life of the annuity utilizing the effective interest method. Grand prizes with annual installment options are awarded related to the Win for Life, Lucky for Life, Powerball, Mega Millions, and certain scratch-off games.

Win for Life draw grand prizes are paid in quarterly installments for the life of a winner. Initial prize liability for grand prize winners was based on an actuarial study. The KLC reviews those statistics to actual results for any changes that needed to be made based on the age of the winner. The KLC ended participation in the Win for Life draw game in January 2011 but continues to have financial obligations to eight past winners.

Lucky for Life grand prizes and second tier prizes are paid in annual installments for the life of a winner, or a minimum of 20 years. A single lump-sum cash payment is also available. As of June 30, 2023, the KLC did not have any grand prize or second tier prize winners elect the grand prize annuity option.

Powerball grand prizes are paid in 30 annual installments or in a single lump-sum payment equal to the estimated present cash value of 30 annual payments. The KLC has one grand prize winner that elected the annuity option and continues to be paid annually.

Mega Millions grand prizes are paid in 30 annual installments or in a single lump-sum payment equal to the estimated present cash value of 30 annual payments. The KLC does not have any grand prize winners currently being paid.

Various instant games have grand prizes with annuity options, paid quarterly or annually for varying amounts and time periods, including installments for the life of a winner. The KLC has eight grand prize winners that elected the annuity option and continue to be paid quarterly or annually.

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022
(dollars in thousands)

Note 2 - Summary of Significant Accounting Policies (Continued)

Cash and Equivalents

For financial statement purposes, the KLC considers all highly liquid investments with an original maturity of less than 90 days to be cash and equivalents. Cash and equivalents are reported at cost.

Investments

Investments consist of U.S. Treasury zero-coupon bonds and other U.S. Government agency securities carried at fair value in accordance with GASB Statement No. 72, *Fair Value Measurement and Application*. Fair value of investments is based on quoted market prices or matrix pricing. Investments are in U.S. Treasury zero-coupon bonds and other U.S. Government backed securities and are purchased to meet future installment payments to grand prize winners. There are generally no realized gains or losses on investments, as it is the KLC's policy to hold the investments to maturity.

Capital Assets

Capital assets are carried at cost less accumulated depreciation. The KLC defines capital assets as assets with an initial, individual cost of more than \$5 and an estimated useful life in excess of one year. Depreciation is computed using the straight-line method over estimated lives of the assets. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is reflected in operations in the period of disposal. The estimated useful lives by general classification are as follows:

Buildings	30 years
Game equipment	5 years
Data processing equipment and software	3 - 5 years
Automobiles, furniture, and fixtures	3 - 5 years
Computer software	7 years

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 2 - Summary of Significant Accounting Policies (Continued)

Deposits with MUSL

Deposits are carried at cost. MUSL is a non-profit, government-benefit association created for the purpose of administering joint lottery games, such as Powerball. In January 2010, the Mega Millions states and MUSL signed an agreement for cross-selling of each other's products. MUSL currently includes 35 state lottery entities, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands. The chief executive officer of each member lottery serves on the MUSL Board of Directors. As a member of MUSL, the KLC is required to contribute to various prize reserve funds maintained by MUSL. The prize reserve funds serve as a contingency reserve to protect MUSL from unforeseen prize liabilities.

All prize reserve funds remitted, and the related interest earnings, will be returned to the KLC upon leaving MUSL, less any portion of unanticipated prize claims which may have been paid from the fund.

Net Position

Net position of the KLC is classified and displayed as three components:

- Net investment in capital assets - Consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.
- Restricted net position - Consists of assets with constraints placed on the use either by (1) external groups such as creditors, grantors, contributors, or laws or regulations of other governments; or (2) law through constitutional provisions or enabling legislation.
- Unrestricted net position - All other net position that does not meet the definition of "net investment in capital assets" or "restricted".

As of June 30, 2023 and 2022, the KLC had no restricted net position.

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 estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Accordingly, actual results could differ from those estimates.

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 2 - Summary of Significant Accounting Policies (Continued)

Subsequent Events Evaluation

Since the KLC is part of the reporting entity of the Commonwealth and is included in the Commonwealth's Annual Comprehensive Financial Report as a discretely presented component unit, management has evaluated subsequent events through September 22, 2023, and will re-evaluate subsequent events before the Commonwealth completes its Annual Comprehensive Financial Report in December 2023.

Recently Adopted Accounting Pronouncements

GASB Statement No. 87, *Leases*, issued June 2017 was adopted in fiscal year 2022. The provisions of this statement require governments to recognize certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities. Changes adopted to conform to the provisions of this statement have been retroactively applied. The implementation of this statement did not have a material impact on the KLC's financial position or results of operations.

GASB Statement No. 96, *Subscription-Based Information Technology Arrangements*, issued May 2020. The provisions of this statement require governments with subscription-based information technology arrangements to recognize a right-to-use subscription asset (an intangible asset) and a corresponding subscription liability. This statement is effective for fiscal years beginning after June 15, 2022 and all reporting periods thereafter. All subscriptions for software have been reviewed by the KLC and no arrangements were long term subscriptions. The implementation of this statement did not have a material impact on the KLC's financial position or results of operations.

Pending Accounting Pronouncements Not Yet Adopted

The GASB has issued the following statement not yet implemented by the KLC:

In June 2022, the GASB issued Statement No. 101, *Compensated Absences*. The provisions of the statement are effective for fiscal years beginning after December 15, 2023. The objective of this Statement is to better meet the information needs of financial statement users by updating the recognition and measurement guidance for compensated absences. This Statement requires that liabilities for compensated absences be recognized for leave that has not been used and leave that has been used but not yet paid in cash or settled through noncash means when certain defined circumstances exist. This statement is not expected to have a material impact on the KLC's financial position or results of operations.

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 3 - Cash and Equivalents

The components of cash and equivalents for the years ended June 30, 2023 and 2022 consisted of the following:

	2023	2022
Cash on deposit in banks	\$ 39,454	\$ 26,528
Checks issued against cash on deposit	(523)	(994)
	\$ 38,931	\$ 25,534

All of the KLC's deposits are either insured or collateralized. All deposits exceeding the federal depository insurance coverage level are collateralized with securities held by the KLC's agents in the KLC's name. The KLC's policy regarding custodial credit risk for cash on deposit in banks is to be fully collateralized by U.S. Government securities held by the KLC or by the KLC's agent in the KLC's name. The cash and equivalents, annuitants amount represents funds earmarked for future annuity prize payments. The balance is equal to the difference in the recorded annuity liability balance and the related investment balance. Additional investments were purchased in 2023 to cover all expected future annuity prize payments, so the cash and equivalents, annuitants amount is zero.

Note 4 - Investments

The KLC categorizes its fair value measurements within the fair value hierarchy established by accounting principles generally accepted in the United States of America. The hierarchy is based on the valuation inputs to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. The KLC's investments in U.S. Treasury Strips are valued using quoted market prices (Level 1 inputs) and U.S. Government backed investments are valued using similar assets using matrix pricing (Level 2 inputs).

At June 30, 2023, the KLC's investment balances were as follows:

At June 30, 2023

<u>Investment Type</u>	<u>Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Maturity</u>
U.S. Treasury Strips	\$ 8,353	\$ 8,353	\$ 0	Weighted average maturity of 8.05 years
Other U.S. Government backed	1,535	0	1,535	Weighted average maturity of 1.08 years
Total	\$ 9,888	\$ 8,353	\$ 1,535	

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 4 - Investments (Continued)

At June 30, 2022, the KLC's investment balances were as follows:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Maturity</u>
U.S. Treasury Strips	\$ 4,634	\$ 4,634	\$ 0	Weighted average maturity of 3.23 years
Other U.S. Government backed	<u>2,080</u>	<u>0</u>	<u>2,080</u>	Weighted average maturity of 2.24 years
Total	<u>\$ 6,714</u>	<u>\$ 4,634</u>	<u>\$ 2,080</u>	

Credit Rating - U.S. Treasury obligations which are backed by the full faith and credit of the U.S. Government are not rated. For 2023, \$1,001 of the other U.S. Government backed investments are not rated and the remaining \$534 is rated Aaa. For 2022, \$1,556 of the other U.S. Government backed investments are not rated and the remaining \$524 is rated Aaa.

Interest Rate Risk - The KLC has a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. It is the policy of the KLC to hold investments to maturity.

Credit Risk - This is the risk that a counter party will fail to fulfil its obligation. The KLC mitigates this risk through its investment policy, which limits the purchase of investments to U.S. Treasury Strips or other debt securities backed by the U.S. Government.

Concentration of Credit Risk - The KLC's general investment policy is to take a very conservative approach when investing KLC money. The policy requires 100 percent of KLC's investments must be in U.S. Treasuries or other debt securities backed by the U.S. Government. For 2023 and 2022, approximately 10 and 17 percent of total investments were in Resolution Funding Corporation Strips, respectively, 5 and 8 percent in Israel Bonds, respectively, and 0 and 6 percent in Federal Judiciary Bonds, respectively, all of which are U.S. Government backed. The remaining 85 and 69 percent were in U.S. Treasuries for 2023 and 2022, respectively.

Custodial Credit Risk - The custodial credit risk for investments is the risk that in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of its investments or collateral securities that are in the possession of another party. A trust agreement documenting the custody arrangement is executed between the custodian and the KLC. Such agreement provides, among other stipulations, that the securities are not assets of the custodian subject to disposition in the event of the insolvency of the custodian.

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 4 - Investments (Continued)

The net change in the fair value of investments includes all changes in fair value that occurred during the year. The calculation of realized gains and losses is independent of the calculation of the change in the fair value of investments. Realized gains and losses of the current period include unrealized amounts from prior periods. The components of investment income/(loss) for the years ended June 30, 2023 and 2022 consisted of the following:

	<u>2023</u>	<u>2022</u>
Unrealized change in fair value of investments	\$ (513)	\$ (716)
Accretion of investments	346	363
Interest income	<u>1,760</u>	<u>0</u>
Total investment income/(loss)	<u>\$ 1,593</u>	<u>\$ (353)</u>

When compared to the historical cost method, recording investments at fair value results in a decrease in income of approximately \$513 and \$716 in 2023 and 2022, respectively.

Unrestricted net position at June 30, 2023 and 2022 is as follows:

	<u>2023</u>	<u>2022</u>
Unrestricted net position excluding unrealized gains on investments	\$ 12,735	\$ 12,562
Accumulated unrealized (loss)/gain on investments	<u>(204)</u>	<u>310</u>
Total unrestricted net position	<u>\$ 12,531</u>	<u>\$ 12,872</u>

The KLC is authorized by state statutes and investment policies approved by the Board of Directors to lend its investment securities. At June 30, 2023 and June 30, 2022 the KLC had no loaned investments.

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 5 - Accounts Receivable

Accounts receivable at June 30, 2023 and 2022 consisted of the following:

	<u>2023</u>	<u>2022</u>
Accounts receivable	\$ 69,709	\$ 75,593
Allowance for doubtful accounts	<u>(500)</u>	<u>(637)</u>
Accounts receivable, net	<u>\$ 69,209</u>	<u>\$ 74,956</u>

Balances due from retailers for the sales of lottery tickets make up 96 and 98 percent of the accounts receivable balances above for 2023 and 2022, respectively.

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 6 - Capital Assets

Capital asset activity for the year ended June 30, 2023 was as follows:

	Beginning Balance	Additions	Disposals	Ending Balance
Capital assets not being depreciated				
Land	\$ 423	\$ 0	\$ 0	\$ 423
Net capital assets, non-depreciable	423	0	0	423
Capital assets being depreciated				
Buildings	8,630	262	(80)	8,812
Game equipment	569	0	(1)	568
Data processing equipment and software	6,363	291	(18)	6,636
Automobiles, furniture, and fixtures	3,178	615	(1,080)	2,713
Total other capital assets at cost	18,740	1,168	(1,179)	18,729
Right-to-use assets, being amortized				
Right-to-use, equipment	19,619	0	0	19,619
Less accumulated depreciation/amortization for				
Buildings	(6,237)	(248)	48	(6,437)
Game equipment	(515)	(12)	1	(526)
Data processing equipment and software	(5,139)	(662)	18	(5,783)
Right-to-use, equipment	(9,981)	(2,958)	0	(12,939)
Automobiles, furniture, and fixtures	(2,695)	(381)	1,075	(2,001)
Total accumulated depreciation/amortization	(24,567)	(4,261)	1,142	(27,686)
Net capital assets, depreciable/amortization	13,792	(3,093)	(37)	10,662
Total capital assets, net	\$ 14,215	\$ (3,093)	\$ (37)	\$ 11,085

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 6 - Capital Assets (Continued)

Capital asset activity for the year ended June 30, 2022 was as follows:

	Beginning Balance	Additions	Disposals	Ending Balance
Capital assets not being depreciated				
Land	\$ 423	\$ 0	\$ 0	\$ 423
Net capital assets, non-depreciable	423	0	0	423
Capital assets being depreciated, amortized				
Buildings	8,544	86	0	8,630
Game equipment	569	0	0	569
Data processing equipment and software	6,311	217	(165)	6,363
Automobiles, furniture, and fixtures	3,025	228	(75)	3,178
Total other capital assets at cost	18,449	531	(240)	18,740
Right-to-use assets, being amortized				
Right-to-use, equipment	19,619	0	0	19,619
Less accumulated depreciation/amortization for				
Buildings	(5,952)	(285)	0	(6,237)
Game equipment	(466)	(49)	0	(515)
Data processing equipment and software	(4,734)	(565)	160	(5,139)
Right-to-use, equipment	(6,586)	(3,395)	0	(9,981)
Automobiles, furniture, and fixtures	(2,508)	(243)	56	(2,695)
Total accumulated depreciation/amortization	(20,246)	(4,537)	216	(24,567)
Net capital assets, depreciable/amortization	17,822	(4,006)	(24)	13,792
Total capital assets, net	\$ 18,245	\$ (4,006)	\$ (24)	\$ 14,215

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 7 - Compensated Absences

It is the KLC's policy to permit employees to accumulate earned but unused paid time off benefits. Employees can accrue no more than 696 hours of paid time off. Accrued paid time off at June 30, 2023 and 2022, included in accrued compensated absences in the accompanying Statements of Net Position, consisted of the following:

	2023	2022
Current	\$ 1,389	\$ 1,449
Compensated absences, less current portion	621	539
Total compensated absences	\$ 2,010	\$ 1,988

Years Ended June 30,	Beginning Balance	Increases	Decreases	Ending Balance
2023	\$ 1,988	\$ 1,326	\$ (1,304)	\$ 2,010
2022	\$ 1,903	\$ 1,469	\$ (1,384)	\$ 1,988

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 8 - Estimated Prize Liability

Estimated prize liability at June 30, 2023 and 2022 consisted of the following:

	<u>2023</u>	<u>2022</u>
Current:		
Grand prizes	\$ 1,355	\$ 1,407
Other prizes	<u>76,293</u>	<u>68,664</u>
Total current portion	<u>77,648</u>	<u>70,071</u>
Long-term:		
Grand prizes	<u>8,750</u>	<u>8,547</u>
Total prize liability	<u>\$ 86,398</u>	<u>\$ 78,618</u>

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 8 - Estimated Prize Liability (Continued)

Liability activity of grand prize awards payable was as follows:

Years Ended June 30,	Beginning Balance	Increases	Decreases	Ending Balance
2023	\$ 9,954	\$ 1,532	\$ (1,381)	\$ 10,105
2022	11,223	381	(1,650)	9,954

Liabilities for future payments of grand prize liabilities are summarized as follows:

Years Ending June 30,	
2024	\$ 1,355
2025	1,305
2026	1,255
2027	645
2028	595
2029 through 2033	2,819
2034 through 2038	2,353
2039 through 2043	1,585
2044 through 2048	1,248
2049 through 2053	572
2054 through 2056	260
Total	13,992
Less unamortized discount	(3,887)
Total at present value	10,105
Less current portion	(1,355)
Total long-term portion at present value	\$ 8,750

Estimated prize liability for grand prizes is based on the cost of U.S. Treasury zero-coupon bonds and other U.S. Government agency securities purchased to fund the liability, adjusted for the accretion of interest based upon the purchased yield and maturity date. This adjustment of approximately \$346 and \$363 in 2023 and 2022, respectively, is included in accretion of investments.

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 9 - Retirement Plan

Kentucky Revised Statute ("KRS") 154A.080 states, "The Corporation shall provide a retirement plan for its employees." The KLC Board of Directors has the authority to establish contribution requirements and amend any of the plan's provisions. The KLC has a money-purchase retirement plan ("Plan") covering eligible employees that is a Defined Contribution plan. The Plan is currently administered by Fidelity Investments. The fair value of investments is determined by the quoted market prices for each investment at the close of market.

Prior to April 1, 2007, under the terms of the Plan, the KLC and employees each contribute 6.2 percent (Mandatory and Supplemental Contributions) of the employee's compensation for the calendar year, not to exceed the Taxable Wage Base as defined by the Plan. Employees become eligible for participation and are fully vested at the date of employment for this portion of the Plan. On and after April 1, 2007, a participant, as defined by the Plan, who makes and for whom the employer makes payments into the Social Security System under the Federal Insurance Contributions Act, shall not be eligible for the Mandatory and Supplemental Contributions.

The KLC also makes a contribution (Basic Contribution) equal to eight percent of the employee's earned annual base salary. Employees become eligible one year after the date of employment and are fully vested after five years of service, or at normal retirement age defined in the Plan, providing participation requirements are met.

During 2023 and 2022, the KLC's contributions were calculated using the eligible compensation amount for eligible employees of \$4,154 and \$4,803, respectively, for the 6.2 percent employer contribution (Mandatory and Supplemental Contributions), and \$11,852 and \$11,120, respectively, for the 8 percent employer contribution (Basic Contributions). Employer contributions actually made to the Plan were approximately \$1,206 and \$1,187 in 2023 and 2022, respectively. Employee contributions to the Plan were approximately \$258 and \$298 in 2023 and 2022, respectively. At June 30, 2023 and 2022, the KLC had an outstanding liability of approximately \$46 and \$40, respectively, owed to the Plan, as part of the accrued salaries balance.

During 2023 and 2022, forfeitures of \$0 and \$45, respectively, were reflected as a reduction to retirement plan expense.

In addition to the Plan, the KLC's employees are also eligible to participate in two deferred compensation plans sponsored by the Commonwealth. These plans are organized as a Section 457 plan and as a Section 401(k) plan under the Internal Revenue Code. Both plans permit employees to defer a portion of their salary until future years. The Commonwealth's Annual Comprehensive Financial Reports should be referred to for further disclosures related to the deferred compensation plans. The KLC provides no matching of contributed funds to the deferred compensation plans.

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 10 - Leases

The KLC has entered into operating leases for the rental of lottery vending machines as part of the lottery gaming system contract with International Game Technologies ("IGT"). The terms of the leases are up to seven years.

We recognize right-of-use assets and liabilities for equipment leases. As of June 30, 2023, and June 30, 2022, these amounts were as follows:

Years Ending June 30,	2023	2022
Right-to-use, equipment	\$ 6,680	\$ 9,638
Current portion of lease liability	3,301	3,667
Lease liabilities, net of current portion	3,379	5,971
Total operating lease liabilities	\$ 6,680	\$ 9,638

Liabilities for future equipment lease liabilities are summarized as follows:

Years Ending June 30,	Vending Machines
2024	\$ 3,301
2025	3,168
2026	1,769
2027	567
Total	8,805
Less amortization expense	(2,125)
Total discounted right-to-use lease liabilities	\$ 6,680

Total expense for 2023 and 2022 was approximately \$3,667 and \$4,086, respectively.

Activity of lease liabilities was as follows:

Years Ended June 30,	Beginning Balance	Increases	Decreases	Ending Balance
2023	\$ 9,638	\$ -	\$ (2,958)	\$ 6,680
2022	13,033	-	(3,395)	9,638

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 11 - Payments to the Commonwealth

Payments to the Commonwealth represent transfers of funds from the KLC to the Commonwealth's General Fund, Trust and Agency account, and the Kentucky Educational Excellence Scholarship ("KEES") Reserve Account. The payments to the General Fund and Trust and Agency account, which are approved by the Board of Directors and remitted to the Commonwealth on a monthly basis, are used to pay for college scholarships, grants, and education programs. The payments to the KEES Reserve Account are used to cover any funding shortfalls to the merit-based KEES program, which provides college or technical school scholarships to Kentucky high school students. The amounts payable to the KEES Reserve Account result from unclaimed prizes on instant and draw games. Prizes not claimed within 180 days of the drawing date for draw games or game ending date for instant tickets are forfeited and considered unclaimed. During the years ended June 30, 2023 and 2022, all unclaimed prize money was transferred to the KEES Reserve Account as required by HB 192 of the 2021 Regular Session and HB 1 of the 2022 Regular Session. Payments are made after the end of each quarter.

Payments, including amounts accrued, to the Commonwealth for the years ended June 30, 2023 and 2022 included payments to the following funds:

	<u>2023</u>	<u>2022</u>
General Fund and Trust and Agency Account	\$ 373,549	\$ 347,291
KEES Scholarship Reserve Fund	<u>10,709</u>	<u>12,042</u>
	<u>\$ 384,258</u>	<u>\$ 359,333</u>

Note 12 - Risk Management

The KLC is exposed to various risks of loss related to torts; theft of, damage to, and the destruction of assets; errors and omissions; injuries to employees; data breach; and natural disasters. The KLC has purchased commercial insurance to cover these risks except for workers' compensation and damage to buildings and personal property for which the KLC utilizes the Commonwealth's Risk Management Fund to cover the exposure to these potential losses. The Commonwealth's Annual Comprehensive Financial Reports should be referred to for additional disclosures related to the Risk Management Fund. The amount of commercial coverage decreased in 2022, but is still adequate to protect against exposure and risk. The amount of settlements has not exceeded coverage.

KENTUCKY LOTTERY CORPORATION

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

June 30, 2023 and 2022

(dollars in thousands)

Note 13 - Commitments and Contingencies

The Lottery contracted with IGT to provide for the operation of the gaming system, with an initial term of July 10, 2011 through July 9, 2021. Through contract negotiations, this contract was amended September 30, 2019 and extended five years, from July 10, 2021 through July 9, 2026. Effective July 12, 2020, the weekly fees paid to IGT decreased by five percent. The commission paid to IGT for draw game lottery sales decreased from 1.5395 percent to 1.4625 percent of gross draw sales. The commission paid to IGT for scratch-off lottery sales decreased from 0.438 percent to 0.416 percent of net scratch-off sales. In addition, and in consideration of the additional products and services provided by IGT under the contract amendment and extension, KLC pays IGT a fixed fee of \$250,000 per month, which began August 12, 2020. IGT receives compensation of \$56.37 per retail location, per month, for retail communications network and management, plus an additional \$18.25 for locations with dual communication. IGT receives additional compensation of \$30.00 per retail location, per month, for cashless equipment communication.

The Lottery also contracted with IGT to provide an iLottery system, game content, and related services, with an initial term of December 23, 2014 through April 16, 2020, with a sales start date of April 17, 2016. Through contract negotiations, this contract was amended on April 17, 2020 and extended for an additional two years to April 16, 2022. The contract was amended again on December 18, 2020 and further extended until July 9, 2026. KLC pays commission to IGT for these services equal to 16.99 percent of net iLottery sales, defined as gross instant play and draw game sales, minus the statistical payout for each game.

The Lottery contracted with Scientific Games, LLC (SG) to provide ticket production and cooperative services, including ticket ordering and distribution functions, with a contract extension term of March 9, 2018 through June 25, 2026. The rate paid on ticket production services is 0.8617 percent of net scratch-off sales of SG games. The rate paid on cooperative services is 0.43 percent of net scratch-off sales of all games.

The KLC is a party to various litigation and other claims in the ordinary course of business. KLC management is of the opinion, based upon the advice of legal counsel, that the ultimate resolution of these matters will not have a material effect on the financial statements of the KLC.

**Independent Auditor's Report on Internal Control over
Financial Reporting and on Compliance and Other Matters
Based on an Audit of Financial Statements Performed in
Accordance with *Government Auditing Standards***

To the Auditor of Public Accounts,
the Commonwealth of Kentucky, and
the Board of Directors of the Kentucky Lottery Corporation
Louisville, Kentucky

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 Kentucky Lottery Corporation as of and for the year ended June 30, 2023, and the related notes to the financial statements, which collectively comprise Kentucky Lottery Corporation's basic financial statements, and have issued our report thereon dated September 22, 2023.

Report on Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Kentucky Lottery Corporation'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 opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Kentucky Lottery Corporation's internal control. Accordingly, we do not express an opinion on the effectiveness of the Kentucky Lottery Corporation's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Kentucky Lottery Corporation'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.

**Independent Auditor's Report on Internal Control over
Financial Reporting and on Compliance and Other Matters
Based on an Audit of Financial Statements Performed in
Accordance with *Government Auditing Standards* (Continued)**

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether Kentucky Lottery Corporation's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the 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 Kentucky Lottery Corporation's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Kentucky Lottery Corporation's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Louisville, Kentucky
September 22, 2023

KENTUCKY LOTTERY CORPORATION

SCHEDULE OF FINDINGS

Year Ended June 30, 2023

Schedule of auditor's results

We have issued an unmodified opinion dated September 22, 2023, on the financial statements of the Kentucky Lottery corporation as of and for the year ended June 30, 2023.

Our audit disclosed no instances of noncompliance which are material to the Kentucky Lottery Corporation's financial statements.

Findings relating to the financial statements

Our audit disclosed no findings which are required to be reported in accordance with *Government Auditing Standards*.

KENTUCKY LOTTERY CORPORATION

SCHEDULE OF PRIOR AUDIT FINDINGS AND THEIR RESOLUTIONS
Year Ended June 30, 2022

The prior year's audit disclosed no findings which are required to be reported in accordance with *Government Auditing Standards*.