2014 ANNUAL REPORT

Benefiting Education and Institutions Since 1970

New Jersey Lottery™

Anything can happen in Jersey.™

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New Jersey Lottery has contributed more than

$23,000,000,000

in support of education, school construction and renovations, veterans' homes, school nutrition programs, tuition aid grants and so much more since 1970.

GOVERNMENT LEADERSHIP

Chris Christie
Governor

Kim Guadagno
Lieutenant Governor

Andrew P. Sidamon-Eristoff
State Treasurer

LOTTERY COMMISSIONERS

Thomas Tucci, Jr.
Chairman

Frank V. Ragazzo
Vice Chairman

Al Alvarez, Esq.
Commissioner

Robert J. D'Anton
Commissioner

Dr. Munr Kazmir
Commissioner

Robert Slater
Commissioner

EXECUTIVE DIRECTOR'S LETTER

Over the past 43 years, the New Jersey Lottery grew from a grand concept with the goal of building a better future for Garden State residents into a multi-billion dollar business that provides residents with millions of dollars in support of vital educational programs and institutions. The business was built on the creative ideas of talented and dedicated people who were willing to take measured risks in order to optimize rewards.

GROWING A BRAND

It takes time: Ticket sales during the first twelve years of the lottery business were nearly equal to the current fiscal year's sales.

It takes exploration of new ideas: A State Lottery Planning Commission, established pursuant to a Joint Resolution on Nov. 11, 1970, explored the possibility of creating a Lottery and provided recommendations to Governor William T. Cahill. On Feb. 16, 1970, he signed into law the establishment of the Division of the State Lottery. The Lottery began selling weekly tickets to one raffle game for 50 cents a ticket and held its first drawing on Jan. 7, 1971. Today, the Lottery portfolio includes seven draw-based games and more than 40 instant scratch games. Tickets are sold by more than 6,900 retailers across the state, seven days a week, and now for the first time in Lottery history, 365 days a year, if a CASH4LIFE draw night falls on Christmas day.

It takes dedication to create a process: The underpinnings of every organization are procedures and rules. There are seven distinct departments within the Lottery that operate individually while integrating structurally. These systems ensure standardization, quality control and efficient use of time and resources while maintaining public integrity and transparency. Optimum results require on-going review and modification.

Carole Hedinger, CPA
Executive Director

Numerous small achievements over the years have set up the organization for future success. The Lottery brand has grown and changed in so many ways but it has always maintained its singular mission of providing a substantial revenue stream in support of the vital programs and institutions it supports.

After review by an independent adviser, a Lottery Growth Management Services agreement was signed with Northstar New Jersey Lottery Group LLC ("Northstar") on June 20, 2013, to further increase Lottery sales and revenue for our beneficiaries.

The Lottery would continue to focus on its core departmental strengths while contracting external partners to manage advertising, marketing and sales. Advertising services already had been outsourced for many years.

After the agreement was signed, Lottery and Northstar leadership worked to define the goals and monitor progress during the months leading up to the transition when Northstar would manage sales, marketing and advertising. On Oct. 1, 2013, the transition was successfully executed.

In subsequent months following the transition, Northstar built and strengthened the transitioned sales staff, increased the team size, provided training and technology to support their efforts and incentivized them to perform optimally. The team expanded the ranks of our retailers and built relationships with corporate partners.

Advertising and marketing was reimagined, and the Lottery brand took on a new persona that included the introduction of Erica Young as Lottery television draw hostess. Erica, the daughter of the beloved, late, Hela Young, helped to re-launch an invigorated Lottery brand.

It was a year filled with challenges and accomplishments. Ultimately, there can be no progress without trials. The true test of an organization is its ability to define, reimagine and forge a forward vision with conviction and expertise — all of which have been accomplished this year. I am proud to present the New Jersey State Lottery Fiscal Year 2014 in review.

Very truly yours,
Carole Hedinger, CPA
Executive Director

NEW JERSEY LOTTERY MISSION STATEMENT

The mission of the New Jersey State Lottery is to raise revenue for maximum contribution to State education and institutions benefiting the citizens of New Jersey through the sale of lottery products. We accomplish this by providing entertaining products through a dynamic public business enterprise built upon honesty, integrity, customer satisfaction, teamwork, and public/private partnerships.

JULY 1, 2013 – JUNE 30, 2014

FISCAL YEAR **2014** HIGHLIGHTS

JULY 2013

July 8, 2013: The largest 2013 Pick-6 jackpot was won in Morris County with an annuity value of $10.5 million.

July 26, 2013: Today's $19 million jackpot-winning Mega Millions ticket was the fifth jackpot-winning ticket sold in NJ during 2013. The others were: Mega Millions on Jan. 25, May 17, May 31 and Powerball on March 23.

AUGUST 2013

August 6, 2013: NJ Lottery holds its "Not 18 Yet? No Bet" press conference reinforcing the age limit for lottery play.

August 7, 2013: Two out of three jackpot-winning Powerball tickets were sold in New Jersey. The annuity value of each winning ticket was $149 million.

AUGUST 2013

This was the first time in 20 years that two winning jackpot tickets were sold in the same state. The last time that occurred was on December 22, 1993 and they were sold in the District of Columbia. A Minnesota Lottery player claimed the third winning ticket.

OCTOBER 2013

October 1, 2013: Northstar New Jersey Lottery Group begins the sales, marketing and advertising services agreement.

October 22, 2013: Mega Millions game matrix change makes the second prize $1,000,000 with the potential to win $5,000,000 with the Megaplier option. Other changes will make more players winners of any prize.

NOVEMBER 2013

November 27, 2013: NJ Lottery partnered with the Council on Compulsive Gambling of New Jersey to discourage gifting of lottery tickets to minors in advance of the holiday season.

JANUARY 2014

January 17, 2014: Player Mike Ducker said he caught lightning in a bottle twice when he won $20,000, twice, in one week, with tickets purchased from the same store, playing the same game.

JANUARY 2014

January 22, 2014: The Powerball game has a matrix change offering players the opportunity to multiply their winnings up to 5 times when they purchase the enhanced Power Play option with the ticket.

FEBRUARY 2014

February 14, 2014: The Million Dollar Replay Grand Prize drawing was held at Lottery headquarters and created another new millionaire and gave away an additional $500,000 to 14 other players.

MARCH 2014

March 4, 2014: Governor Chris Christie proclaims March Problem Gambling Awareness Month in New Jersey and a joint press conference is held at the Lottery with the Council on Compulsive Gambling of New Jersey.

APRIL 2014

April 22, 2014: Vineland Truck Stop sells its third jackpot-winning ticket in under a year; a Jersey Cash 5 ticket worth $630,260; a $30 million Mega Millions ticket, and a $1 million $100,000,000 Spectacular scratch off ticket, making it a very popular retailer.

JUNE 2014

June 3, 2014: Shooting begins for a trio of Lottery commercials featuring NJ winners dancing to the hit-tune "Happy" written by Pharrell Williams.

June 13, 2014: The New Jersey and New York Lotteries held a cash give-away publicity event to introduce their new joint game, CASH4LIFE to the public.

JUNE 2014

June 15, 2014: The Pick-6 $20.1 million jackpot was won by an Ocean County family with 19 siblings making a mother's life-long dream a reality.

June 30, 2014: Erica Young is appointed Lottery Hostess following in the footsteps of her late mother, Hela Young.

WHERE THE MONEY GOES

New Jersey Lottery Fiscal Year 2014 Revenue Distribution

The New Jersey Lottery is the State's fourth largest revenue producer. In Fiscal Year 2014, the Lottery grossed more than $2.9 billion in sales; contributing $965 million, or 33 percent of sales, to the State in support of its beneficiaries.

Since its inception in 1970, the Lottery has contributed more than $23 billion to programs that benefit millions of New Jersey residents through the School Nutrition Program, Student Tuition Assistance Reward Scholarships, the Marie H. Katzenbach School for the Deaf, Homes for Disabled Soldiers and many other organizations and programs whose constituencies benefit from Lottery proceeds.

The New Jersey Lottery Speaker's Bureau program shares the benefits of Lottery contributions in support of these good causes with members of the general public. Rotary groups, senior citizen groups and other organizations are informed and entertained across the state with our no-cost program.

The presentations provide interesting facts about the New Jersey Lottery and its history, as well as information about our games, our retailers and our winners. The program also includes information about the importance of playing responsibly and about the Lottery's support of the Amber Alert and the Silver Alert Programs.

The New Jersey Lottery also plays a key role in supporting businesses throughout the state. At the end of Fiscal Year 2014, more than 6,900 Lottery retailer licenses were issued, up from 6,500 the prior year with more than 6,800 active retailers serving the public.

Retailers are the public face of the Lottery brand and provide customer service and product support. In return, retailers earn a 5-percent commission on their Lottery ticket sales in addition to ticket-cashing bonuses and special product promotion bonuses. In Fiscal Year 2014, the Lottery returned more than $162 million, up from $158 million, in commissions to its retail business partners throughout the state.

STATE OF NEW JERSEY PROGRAMS SUPPORTED BY STATE LOTTERY RESOURCES FOR THE YEAR ENDED JUNE 30, 2014
(Amounts expressed in thousands)

		Amount Expended and/or Encumbered (a)
DEPARTMENT OF AGRICULTURE		
School Nutrition	$	3,424
DEPARTMENT OF EDUCATION		
Marie Katzenbach School for the Deaf		2,161
Non-public School Aid		53,583
Statewide Assessment Program (Grades 4, 8, 11)		11,658
School Construction and Renovations		30,355
TOTAL DEPARTMENT OF EDUCATION		**97,757**
HIGHER EDUCATIONAL SERVICES		
Senior Public Institutions – operating Aid		223,365
Tuition Aid Grants		213,214
Higher Education Capital Improvement Plan – debt service		17,428
Aid to County Colleges for Operational Costs		70,350
Coordinated Garden State Scholarship Program		20
Student Tuition Assistance Reward Scholarships (NJStars)		4,333
Opportunity Program Grants		15,872
Supplementary Education Program Grants		7,810
TOTAL HIGHER EDUCATIONAL SERVICES		**552,392**
DEPARTMENT OF HUMAN SERVICES		
Operation of Centers for Developmentally Disabled		90,919
Operation of State Psychiatric Hospitals		173,899
TOTAL DEPARTMENT OF HUMAN SERVICES		**264,818**
DEPARTMENT OF MILITARY AND VETERANS AFFAIRS		
Operation of Homes for Disabled Soldiers		46,619
TOTAL REVENUE REALIZED – GAAP BASIS	**$**	**965,010**

(a) The amount of State Lottery funding in the programs designated above, may only represent a portion of its total State funding. Any balance of the appropriation for the program would be funded by the General Fund. Program funding is allocated in a manner consistent with prior year expenditures level for each respective program.
Andrew P. Sidamon-Eristoff, State Treasurer

RESPONSIBLE PLAY

The New Jersey Lottery is dedicated to promoting responsible play in the community. Our deep commitment is demonstrated in numerous ways, including recognition from the World Lottery Association by earning its Level I Responsible Gaming Framework Certificate of Accreditation in September 2012. The Lottery is actively working toward completing the remaining three certifications.

The Lottery has a long-standing partnership with the Council on Compulsive Gambling of New Jersey (CCGNJ). The Lottery maintains a position on the Council's Board of Directors and remains actively engaged in its mission. To further support the responsible play mission, New Jersey Lottery promotes the responsible play message and the 1-800-GAMBLER phone number to millions of players each year on every Lottery product and on all Lottery advertising and marketing messaging.

800-GAMBLER

Aware of the importance of educating the public on underage gambling, the Lottery held a press conference on August 6, 2013, to kick-off its annual "Not 18 Yet? No Bet" campaign to remind players and retailers that children under the age of 18 may not play the lottery. This message coincides with the American Gaming Association's Responsible Gaming Education Week and with the back-to-school season.

On Nov. 27, 2013, Lottery officials and CCGNJ officials issued a joint press release discouraging the purchase of lottery tickets as gifts for minors during the holiday season. Both organizations continued to stress that message throughout the season.

Gov. Chris Christie issued a proclamation declaring March 2014 as Problem Gambling Awareness Month in New Jersey. In support of his leadership, the Lottery once again worked with the CCGNJ to educate the public and healthcare professionals about the warning signs of problem gambling and raise awareness about help that is available. The two organizations held a press conference at Lottery headquarters to mark the event and to build public awareness of the signs and treatment options for compulsive gambling.

The Lottery sponsored and its personnel attended the 32nd Annual Statewide Conference on Compulsive Gambling held on Sept. 19, 2014, in West Windsor. National leaders, including treatment professionals, educators and members of the gaming community, came together to discuss matters related to problem gambling, its prevention and treatment.

In its commitment to encourage responsible gaming, the Lottery continued to participate in meetings with members of the Responsible Gaming for the Future Working Group to address problem gambling issues. These meetings brought together professionals from the fields of regulatory gaming, the casino industry, academics, criminal justice and public health to exchange ideas and to work together to promote public awareness of responsible gaming and raise awareness of treatment options available for individuals with gambling problems.

BUILDING A FOUNDATION FOR GROWTH WITH NORTHSTAR NEW JERSEY

On Oct. 1, 2013, Northstar New Jersey officially began the 15-year contract to provide growth-management services to the Lottery. The contract focuses on: sales force expansion, retailer expansion, product innovation, marketing optimization and reinvigorated advertising and branding. At the contract's onset, each pillar of service was defined, goals were set, core strategies were developed and tactics were laid out and planned.

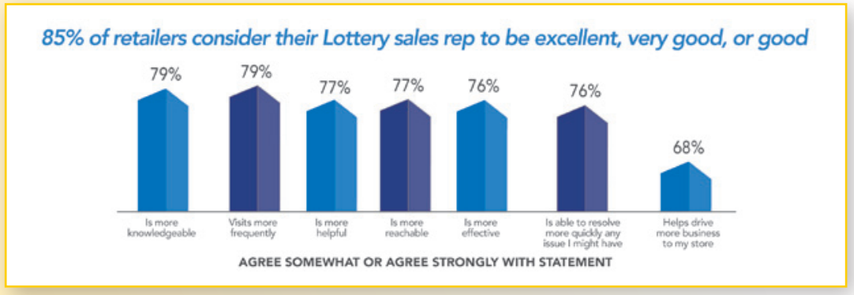
*More than **40,000 work-hours** were expended by Northstar, in conjunction with technology partner GTECH, to add new features and products to the Lottery gaming system.*

Fiscal Year 2014 reflects the first nine months that the contract was in force. Leadership and staff devoted that time to establishing channels of communication, creating workflow procedures and a seamless process between the two organizations. Together, they built a solid foundation for future growth. New Jersey Lottery and Northstar New Jersey achieved an impressive list of accomplishments since the services transition.

SALES FORCE EXPANSION AND DEVELOPMENT

The New Jersey Lottery had 52 sales representatives servicing the needs of more than 6,300 retailers across the state prior to the contract. At fiscal year end, the Northstar sales team numbered 120 Lottery Sales Representatives (LSR). The on-boarded staff was equipped for success with technology tools and specialized software and participated in weekly sales training sessions and quarterly team-building meetings.

Retailers benefited from the expanded sales team and received more frequent and effective sales visits than in the past. Each visit provided business-building data and allowed for coaching opportunities. A retailer survey revealed that 75 percent have a positive opinion of Northstar's management of the Lottery's sales and marketing programs. Some 68 percent of retailers reported that they have seen increases in their overall Lottery sales since the change.



RETAILER EXPANSION USING CUTTING-EDGE TECHNOLOGY

Increasing the number of retailers was one of the pillars of the Lottery growth management structure. The increased LSR team produced positive results with the retailer network expanding from 6,378 to 6,839, a 7-percent increase as of June 30, 2014. This growth was accomplished, in many instances, by removing obstacles through technology and innovation that may have prevented businesses from bringing the lottery into their product mix.

For years, Lottery retailers asked for an improved way to manage instant ticket inventory. Northstar enabled Smart Count inventory management software for all new retailers and other retailers needing inventory management assistance. This innovation streamlined the inventory management process and increased productivity.

Another key retailer request was for the Lottery to allow returns of partial packs of instant tickets. Northstar addressed that request by providing the Lottery with new machinery, staff training and accompanying technology. This innovation enables Lottery staff to process partial pack returns quickly, efficiently and accurately with inventory management tools on a regular schedule. Eighty-seven percent of retailers polled said that the initiation of partial pack returns was a key area of improvement provided by Northstar.

Northstar hosts Retailer Partnership 101 meetings at which retailers work directly with management to share operational insights, discuss suggestions for improvements and resolve matters of concern. These meetings build relationships and keep communication on-going.

Retail partners benefited from advanced analytics made possible by leading-edge technology. New insights were used to significantly increase the percentage of retailers that receive, activate and sell new instant ticket games, which ensures broad market penetration.

All of these technological advancements, in the hands of trained lottery sales representatives, served to simplify operations for retailers and make entering into a partnership with the Lottery a more viable opportunity for businesses of all sizes. It also motivated existing retailers to increase sales and broadened market penetration with the product line.

MARKETING OPTIMIZATION

The Northstar contract brought with it the expansion of the Lottery's minimal marketing team to a robust team of 20 full-time employees. Their expertise includes advertising and marketing creative development, an events promotion team, social media specialists and a graphic design team. The team enables Northstar, on behalf of the Lottery, to conceive, develop and execute marketing promotions in-house, thereby reducing turnaround time and costs while maintaining oversight and providing analytics.

By actively managing and expanding the social media channel mix, player engagement has increased from 2.4 percent to 18.4 percent during the initial term of the contract period.

Interacting with the public at events of various sizes also is an essential marketing tool that Lottery staff alone could not accomplish. With the increased marketing support team, Northstar has held 148 in-store retailer promotions and participated in 23 festivals and special events representing the Lottery, selling tickets, promoting goodwill and introducing the latest products to the market.

One group of winners getting ready to board the "Happy Bus" to begin their day of filming the New Jersey Lottery's new "Happy Dance" TV commercial.

Once again, a hostess officiates over the evening draws, matching a positive personality with the brand on television and at live events. Erica Young is a Northstar team member but more importantly the new face of the Lottery brand. Erica Young is the daughter of the beloved Hela Young, who served as Lottery hostess for more than 25 years.

The New Jersey Lottery Pro Football Hall of Fame Powerball promotion winners were overwhelmed by their up-close and personal experience at the Ultimate Tailgate Party; they called it an event that created memories to last a lifetime.

The New Jersey Lottery was a proud sponsor of the Quick Chek Festival of Ballooning at Solberg Airport in Readington, NJ.

Lottery revenue supports NJ Veterans Homes and other important programs and institutions. A ceremonial contribution check appeared at events across the state with a kick-off at the Menlo Park Veterans Home. (l-r) Steven Ferrari, Brigadier General, Director, Veterans Healthcare Services, NJ Dept. of Military and Veterans' Affairs, Raymond Zawacki, New Jersey Deputy Commissioner for Veterans Affairs, Carole Hedinger, NJ Lottery Executive Director, Joseph Brandspiegel, CEO, Veterans Memorial Home, Menlo Park.

HALLOWEEN RAFFLE

New Jersey Lottery participated in a multi-state Halloween Raffle drawn on Nov. 1, 2013. The drawing resulted in a New Jersey Lottery player winning one of the three $1 million jackpot prizes. Deborah and Keith Andrews from Paterson were the fortunate winners. Mr. Andrews bought one ticket at the behest of his wife.

The raffle game was sold through lottery retailer terminals as an online game in seven states: Indiana, Iowa, Michigan, New Jersey, New York, Ohio and Oklahoma. There were 765,711 tickets sold, bringing total sales for the draw to $7.6 million. There were four $50,000 winners, one each in Iowa, Indiana, New York and Oklahoma, creating a total cash prize payout of $3.2 million.

The draw was held at the draw facility of the Multi-State Lottery Association.

"HAPPY DANCE" COMMERCIAL

The radio airwaves, social media, television programing and public places in the U.S. and internationally were buzzing with the infectious Pharrell Williams song "Happy" that was released at the end of 2013. The uplifting beat and positive song lyric had people of all ages gleefully dancing and shooting amateur videos mimicking the artist's music video.

The Lottery advertising team recognized the power of the song and wanted to meld the experience of winning the lottery to the positive emotion created by it. The team decided to shoot a Lottery commercial using the song as its anthem. They devised a social media contest to attract Lottery players, cast them and produced three 30-second commercials. The commercials featured 30 New Jersey Lottery winners with the "Happy" song playing as the soundtrack. The commercials were shot at iconic locations across the state including a street scene in front of the Stone Pony in Asbury Park, outside of and including the fire-fighters of the Tinton Falls Fire Company, Wightman Farm in Morristown, the Absecon Lighthouse in Atlantic City and at Lucy the Elephant in Margate.

> *The extremely successful advertising and public relations campaign reached millions of consumers.*

News media were excited with the events and featured the lottery-winning-dancers and the Lottery in primetime television segments, in print and online. The extremely successful advertising and public relations campaign reached millions of consumers.

The commercials were aired in select New Jersey movie theatres in June, 2014, and were featured in social media and cable television advertising flights.

(L to R - top) Lottery winners dancing to the hit song "Happy": Eleise Queensbury in front of Lucy the Elephant, Margate; Diana Gleason and Joanna Alfieri, Margate beach; David John, Stone Pony; Felix Guillermo, Americana Diner, Shrewsbury; Susan Cucolo and Angelo Granata, Americana Diner, Shrewsbury. (L to R - bottom) Tinton Falls Fire Company members; group shot at Americana Diner, Shrewsbury; Valerie Stewart, Absecon.

PRODUCT INNOVATIONS

DRAW-BASED GAME CATEGORY

Northstar supported the introduction of the modified Mega Millions game matrix that was introduced to the public beginning with the Oct. 22, 2013, draw. The Northstar team continued Lottery player favorite promotions including Red Ball, Green Ball and Instant Match. The Jersey Cash 5 game was reinvigorated with innovative promotional offers. Then, the fiscal year closed with the introduction of the New Jersey and New York exclusive new draw-based game, CASH4LIFE.

Pick 3™

Since its inception in 1977, the Pick-3 remains the longest on-going and best-selling draw-based game at the Lottery. Drawings are held twice daily and provide players multiple strategic play opportunities beginning with a 50-cent wager. Tickets also are available for purchase with an Instant Match option providing players an additional opportunity to win prior to the draw. Sales topped $436.7 million in Fiscal Year 2014, up from $434 million the prior year. More than $4.7 million of sales were from Instant Match. The total sales for Pick-3 represent 15.01 percent of overall ticket sales for the Lottery.

Lottery players anticipate the yearly Pick-3 Red Ball promotion. This year it was held on Sept. 2 through Sept. 29, 2013, for the evening draw. It provided players with the chance to double their Pick-3 winnings based on a second drawing that occurs each evening after the initial Pick-3 draw. If the red ball pops up, all prizes for that draw are doubled. The red ball is guaranteed to be drawn a minimum of once every seven days. It is a highly anticipated player favorite.

The Green Ball promotion, another annual Lottery event, ran from March 10 through March 30, 2014. During the month of March, sales topped $40 million — claiming the top spot in gross sales for the year. Players claimed nearly $22 million in prizes for the month, making March the month with the highest Pick-3 player payout for the year.

In total, Pick-3 players won more than $223 million during the year, up from the prior year which was $221.8 million.

In total, the Pick-3 game generated more than $182 million, or 19 percent of the Lottery's overall contribution to the Treasury's General Fund for the year.

Pick 4™

Playing Pick-4 is fun and easy and perhaps the reason why it is a player favorite and the second highest revenue producer in the Lottery's draw-based game category. Sales topped $268 million, up from $266 million the previous year, representing 9 percent of the Lottery's total sales. There were 552,316 Pick-4 winners in Fiscal Year 2014 who won more than $133 million.

The game's popularity can be attributed to its simplicity. Players choose four numbers between 0 and 9, or request a Quick Pick, and let the excitement begin. For a mere 50 cents, Lottery players can play midday and evening draws choosing straight or box combinations to win cash prizes. For an additional dollar per wager, players can instantly become winners with Instant Match. Instant Match provides a second, immediate opportunity to win up to $500 with each board purchase.

The annual Red Ball promotion provided players with an additional opportunity to win at no additional cost. It ran from Sept. 2 through Sept. 29, 2013, and with each drawing, players had a chance to double their winnings. Every night during the Red Ball promotion, after the regular Pick-3 and Pick-4 drawings occur, a separate machine containing six white balls and one red ball is used for a subsequent drawing. When the red ball is chosen, all winning ticket payouts are doubled. The staple Pick-4 game accounted for an estimated contribution to the State of more than $115 million in Fiscal Year 2014.

The top Jersey Cash 5 jackpot in Fiscal Year 2014 was $1,316,860. The winning ticket was sold at Home Wine and Liquor, 224 Elizabeth Ave., Newark in Essex County for the Saturday, November 16, 2013 drawing. Executive Director Carole Hedinger said the winning ticket was the only one sold for Saturday's drawing that matched all five numbers drawn. The winning numbers were: 03, 20, 22, 34 and 38.

Jersey Cash 5™

Jersey Cash 5 draw-based game sold more than 1.34 million winning tickets during Fiscal Year 2014, up from 1.30 million the prior year. Of those tickets, 223 were jackpot winners, with the highest jackpot reaching $1,316,860 on Nov. 16, 2013. In total, players claimed more than $38.4 million in cash prizes, up from $37 million the prior year. The average jackpot payout was $172,278. Jersey Cash 5 game odds are a player favorite with 39.56 percent of draws resulting in a jackpot-winning ticket. Introduced in September 1992, the game remains a favorite among Lottery players, with ticket sales topping $148 million, up from $144 million in the prior fiscal year. Instant Match is a game enhancement available to Jersey Cash 5 players that provides the opportunity to play and win cash prizes at the point of purchase for an additional dollar. Instant Match contributed more than $3.2 million to total sales. Overall, Jersey Cash 5 sales contributed more than 5 percent toward total Lottery sales. The game contributed more than $65 million for the year.

It's not often that we meet a player who buys two tickets for the same draw with the same numbers and gets to claim two shares of a jackpot prize. That's precisely what John R. did for the Dec. 12, 2013, drawing. "I told the clerk my numbers for the first ticket. Then I filled out another bet slip with the same numbers and three other sets of numbers." John won two-thirds of the jackpot prize, with the third share going to a player in Ocean County. John also claimed the 4 out of 5 prize worth $515.

Endreson family members (L to R): Emma Pirie, Marie McHenry, Sigrid Endreson, and Jennifer Pirie.

Pick 6 Six lotto™

New Jersey's Pick-6 Lotto game produced a winning story with media reach that stretched around the country and beyond due to its sentimentality and relatability. The ticket was purchased by a member of a Jersey Shore family that matched all six numbers to win the $20.1 million jackpot. In doing so, the win fulfilled a life-long dream of the deceased matriarch of the Endreson family to share a jackpot prize with her 19 children. Twenty members of the Endreson family claimed their prize and participated in a press conference to tell their story to honor their late mother, Flossie. The winning ticket was purchased for the Monday, June 16, 2014 draw and had a cash value of more than $14 million.

At the podium, Endreson family member Jonas Endreson.

Endreson family members (L to R): John Endreson, Faith Schiabor, Dawn Pascarelli, Kristine Rasile, and Anne Rioux.

There were five Pick-6 jackpot winning tickets claimed in Fiscal Year 2014 totaling more than $33.58 million in prizes for the 34-year-old game. Pick-6 created nearly 1.46 million winners paying out more than $39.6 million to players. This year's game sales topped $77.5 million, up from $65 million the prior year, representing 2.67 percent of overall sales.

On behalf of State institutions and programs for residents, the game contributed more than $32.9 million.

NEW JERSEY LOTTERY CASH4LIFE™

The New Jersey and New York Lotteries announced a first-of-its-kind draw-based game, CASH4LIFE, with an enthusiastic crowd and press conference in Manhattan on June 12, 2014. Acting New York Lottery Director Gardner Gurney and New Jersey Lottery Executive Director Carole Hedinger were in attendance to introduce the game. Two money booths were featured at the event with flying bills of varying denominations for the public to capture and claim. The event and associated advertising effectively launched the new game in both Lottery markets.

Carole Hedinger, Executive Director, addresses the public and media announcing the CASH4LIFE game launch with New York State Lottery Director Gardner Gurney.

The CASH4LIFE game was designed to give players on both sides of the Hudson a chance to win one of two "for life" prizes in addition to other cash prizes. First prize in the exclusive multistate game is $1,000 a day for life and a second prize of $1,000 a week for life is also available with the purchase of a single $2 ticket. CASH4LIFE also features seven additional prize levels ranging from $2 to $2,500.

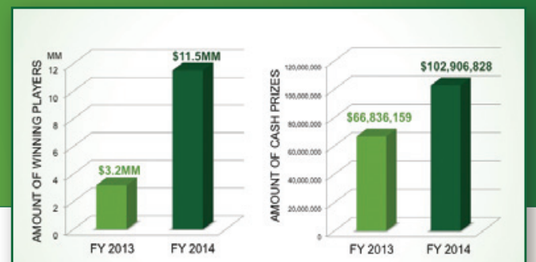
Game sales began on Friday, June 13, 2014, and the inaugural draw was held on Monday, June 16, 2014, at approximately 9 pm. The drawings are held on Mondays and Thursdays, and originate from New Jersey's drawing studio in Lawrenceville.

General public launch event participants won cash in the two CASH4LIFE money grab booths.

Ticket sales began 18 days prior to the close of the fiscal year allowing for five game draws. The game had a strong start. Remarkably, in that short span of time, the game created a New York $1,000 a week for life second prize winner on June 19, 2014; then a New York top prize winner of the $1,000 a day for life on June 23; and then a New Jersey second-prize winner of $1,000 a week for life on June 30, the final day of the Fiscal Year.

There were 18 days in which the game was for sale during Fiscal Year 2014. During that time, New Jersey players won more than $5.2 million in prizes. There were 306,145 winning tickets claimed from game launch to the end of the year.

New Jersey Lottery MEGA MILLIONS with MEGAPLIER™



Mega Millions game contributed **$86,461,580** to Lottery beneficiaries

Fiscal Year 2014 began with a New Jersey Mega Millions jackpot win on July 26, 2013. That lucky ticket was worth $19 million, and the proceeds were shared by two players from Kearny. The retailer who sold the lucky ticket, Dollar Subs in Kearny, earned a $30,000 bonus commission. Between July 1 and Oct. 31, 2013, nine New Jersey players purchased tickets that matched five out of the six winning numbers and claimed prizes worth $250,000 each. Two of those players purchased their tickets with the Megaplier option, making their winning tickets worth $1 million.

New Jersey Mega Millions ticket sales increased in Fiscal Year 2014, closing at $205.8 million.

During the last half of the fiscal year, a phenomenon known as jackpot fatigue became evident. Historical evidence shows that as jackpot size increases, media coverage of the game expands, and more people become interested in participating in the game and purchase tickets. However, this leads to a need for larger and larger jackpots in order to attract additional players. To address this situation and to increase the number of winning prizes, the Mega Millions game matrix was modified beginning with the Oct. 22, 2013, drawing. It changed the match prizes from $250,000 to $1 million. Additionally, a number of other game changes were made to create larger and faster growing jackpots and provide better odds of winning to allow for more overall game winners of any prize — all for the same $1 ticket price.

The timing of those changes was fortunate for four New Jersey players who matched the five white balls on their tickets during the month of December, increasing their wins four-fold to $1 million each up from $250,000 before the matrix change. In addition, the total number of winners of any prize increased to 11.5 million players up from 3.2 million the prior year. That equates to a 260 percent increase in the number of winners year over year. In total, 11,503,500 Mega Millions players won $102,906,828 in cash prizes for the year, up from 3,223,901 players winning $66,836,159 the previous year.

Mega Millions ticket sales represented 7.08 percent of overall ticket sales for the year, up from 4.85 percent the prior year. The game contributed more than $89.9 million in State contributions, and retailers' commissions topped $10.5 million.

New Jersey Mega Millions ticket sales increased in Fiscal Year 2014, closing at $205.8 million up from $136.8 million the previous year. Ticket sales saw a boost when the game's jackpot skyrocketed to $648 million for the Dec. 17, 2013, drawing which was and remains the second largest jackpot in game history.

New Jersey **Lottery**

POWERBALL POWERPLAY®

OCEAN'S **16**

The Powerball story of the year, and perhaps for many years to come, is of the drawing held on August 7, 2013, when three jackpot winning tickets were sold — two of which were sold in New Jersey and the third in Minnesota. The last time that two jackpot winning tickets were sold in the same state for the same draw was on Dec. 22, 1993. Those tickets were sold in the District of Columbia.

The Powerball jackpot for the August 7 draw climbed to $448 million after rolling 12 times. One of the New Jersey tickets was sold at Super Stop & Shop, South Brunswick in Middlesex County, and the other ticket was sold at ACME Markets #7858, Little Egg Harbor in Ocean County.

Ocean's 16 group Powerball winners.

On the morning of August 12, a group of people came to Lottery Headquarters in a chartered bus. The group leader, Brian McCarthy, presented a Powerball ticket that he said was purchased at ACME Markets for validation and filed a claim as the group watched. The Lottery staff declared that the ticket was valid and payable at which time the group jumped to their feet, cheered, clapped and hugged one another in joy.

Carole Hedinger, New Jersey Lottery Executive Director, was present to greet the winners, all of whom are Ocean County employees. Ocean County is a special place for Hedinger as she was the Chief Clerk of the Ocean County Surrogate Court from 2004—2010. "I know that these folks are hard-working, reliable employees who have served the public well for many years," she said. "In their positions in the Department of Vehicle Services they handle maintenance operations that support all County departments by keeping their vehicles and equipment functioning in a safe and proper manner."

William (Willie) Seeley, Ocean's 16 group member, had a persona that made an impression on the media and public.

Many of the winners in the group had suffered devastating financial losses resulting from Superstorm Sandy. This win provided a new beginning for many of them although most of the members said they would remain at their jobs for the near future and perhaps beyond.

This 16-member group, self-named Ocean's 16, became national celebrities after appearing at a press conference held at the Ocean County Library in Toms River. They were featured on Good Morning America and in TV news, in print and online media across the country.

The story resonated with the public and was trending news for weeks. Adding an additional layer of interest to the story was that Barbara Jo Riivald, one of the group's members, is the daughter of former State Senator John F. Brown, who was one of the founding fathers of the Lottery as a sponsor of the Lottery bill.

The Ocean's 16 women are featured on Good Morning America sharing their personal life stories including devastation from Superstorm Sandy and more.

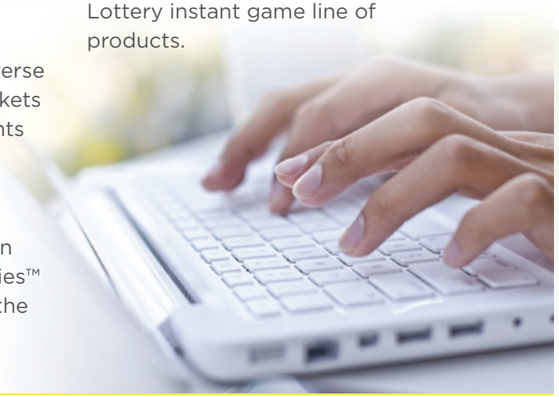
Powerball was a winning proposition for millions of New Jersey Lottery players in Fiscal Year 2014. In total, more than 3.4 million New Jersey players won cash prizes equaling more than $113 million playing Powerball. Of those, 16 ticketholders won $1 million dollars by matching five out of the six winning numbers.

Barbara Jo Riivald, member of the Ocean's 16 Powerball jackpot winning group, and daughter of the former State Senator, John F. Brown, one of the Lottery's founding fathers.

Ticket sales in Fiscal Year 2014 were more than $233.6 million, down from $300 million the prior year. Powerball ticket sales represented 8 percent of overall sales. Lottery retailers received more than $11.8 million in commissions during the year while the game contributed more than $108 million toward Lottery beneficiaries.

The VIP Club is a free, online lottery membership club that provides players access to daily winning number emails, special promotions through the Lottery Bonus Zone Second Chance Drawings games and the Million Dollar Replay second chance program. Membership in the club increased to more than 275,000 people, up from 226,755 in the prior fiscal year.

The Lottery Bonus Zone Second Chance Drawing games provide player opportunities to win a diverse array of prizes such as tickets to concerts, sporting events and family entertainment. Second chance drawings were available for instant games such as The Golden Nugget®, Plants vs. Zombies™ and ZUMA™. Players had the opportunity to win prizes such as a trip for two to Atlantic City, an iPad and iPad Mini. Those opportunities fostered continued interest and excitement in playing the Lottery instant game line of products.



Fiscal Year 2014 marked the third year in which the Million Dollar Replay program provided lottery players with the opportunity to enter non-winning instant game tickets into a second chance drawing. The year-long program began on April 3, 2013 and ran through Jan. 6, 2014. Each quarter, the Million Dollar Replay program awards 100 semi-finalists $250 each and entry into the final Grand Prize drawing. The Grand Prize Drawing was held on Feb. 14, 2014 at which fifteen lucky players were chosen to win one of the top cash prizes: one $1 million grand prize, two $100,000 prizes, three $50,000 prizes, four $25,000 prizes, and five $10,000 prizes for a total of $1.5 million.

Excitement for the program remained robust with our instant game players. There were more than 7.4 million entries during the year. Each entry signified $10 worth of non-winning, eligible instant scratch-off tickets.

(L to R) Carole Hedinger, NJ Lottery Executive Director, Jerry Pavlick, Edith Spruill, Sandra Brodbeck, 2013 Million Dollar Replay winners, John Custodio, NJ Lottery Deputy Executive Director.

PRODUCT INNOVATIONS

INSTANT TICKET CATEGORY

Northstar, in collaboration with Scientific Games, developed an exciting instant ticket product mix designed to appeal to a broad range of players. The annual number of games available was reduced from 52 to 44, which increased product visibility at retail. In-store promotional support, including installation of new display bins, was increased for featured games including roll-outs of game families — groupings of branded games available at different price points and offering different prize payouts.

Fiscal Year 2014 was truly a spectacular year for players in the instant ticket category of games. There were 49 instant ticket players that won $1,000,000 or more in prizes during the year. The wide variety of games and price points make the New Jersey Lottery instant game line appealing to diverse categories of players. The most popular game price point was $5, resulting in sales of more than $401 million worth of tickets. Coming in second was the $10 price point at nearly $317 million in sales. There are dozens of instant games, ranging in price from $1 to $20, offering cash prizes of up to $1 million or the opportunity to win quarterly installments of cash for life.

Offering a top prize of $1 million, the $100,000,000 Spectacular game, at the $10 price point, was the highest selling ticket for the year. There were more than $119 million worth of tickets sold for the game. The Spectacular family of games offered games in price points ranging from $2 up to $10 with varying odds and top prizes. This game family contributed more than $355.5 million in sales for the year.

Total instant ticket sales topped $1.53 billion, a year-over-year increase from $1.47 billion. Instant game ticket sales represent 52.67 percent of all ticket sales, up from 52.25 percent the prior year. Retailers earned more than $88 million in commissions from these sales, up from $84.8 the prior year.

The Crossword brand of games, offering tickets ranging in price from $3 to $10, is another player favorite. In Fiscal Year 2014, Crossword games collectively produced revenues of more than $320 million, up from $315 million in Fiscal Year 2013.

Instant ticket sales generated a State contribution of $371 million, down from a record $373 million the previous year. This represents 23.99 percent of the total State contribution for the year. Additionally, a record $1.03 billion was paid out in cash and prizes to instant ticket winners, up from $989 million in Fiscal Year 2013.

The New Jersey Lottery paid out more than

$1.7 BILLION

in prizes in Fiscal Year 2014.

New Jersey Lottery retailers earned commissions and bonuses of more than

$162 MILLION

in Fiscal Year 2014.

STATE OF NEW JERSEY, DEPARTMENT OF THE TREASURY, DIVISION OF STATE LOTTERY

Financial Statements

June 30, 2014

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INTRODUCTION

The following discussion and analysis provides an analytical overview of the financial position and activities of the State of New Jersey, Department of Treasury, Division of State Lottery, (the "Division of State Lottery") for the years ended June 30, 2014 and 2013. This statement was prepared by management and should be read in conjunction with the financial statements and notes hereto, which follow this section.

The Division of State Lottery was established in 1970 pursuant to the "State Lottery Law," N.J.S.A. 5:9-1 et seq. The Division of State Lottery operates within the Department of Treasury of the State of New Jersey. The New Jersey Lottery Commission is a seven-member board, appointed by the Governor, authorized and empowered to promulgate rules and regulations in the operation of the Lottery. The "State Lottery Law" also mandates that a minimum of 30% of gross revenues from ticket sales be allocated for contributions to state aid for education and state institutions N.J.S.A. 5:9-7a (11).

As of June 30, 2014, the Division of State Lottery licenses more than 6,900 retailers throughout the State of New Jersey to act as retailers in the sale of New Jersey Lottery tickets. Lottery retailers receive compensation in the form of commissions on each ticket sold or validated, bonuses and retailer incentive programs.

On June 20, 2013, a competitively bid 15-year (plus fiscal year 2014 stub year) contract was awarded to Northstar New Jersey Lottery Group, LLC ("Northstar NJ") to provide sales and marketing services to the Division of State Lottery for the purpose of increasing lottery sales and net income (net proceeds for state aid for education and state institutions). If contracted net income targets for a given fiscal year are met or exceeded, Northstar NJ will earn incentive compensation. Conversely, if net income targets for a given fiscal year are not met it could result in reduced incentive or a contribution shortfall payment to the Division of State Lottery. In addition to compensation for its sales and marketing efforts, Northstar NJ is reimbursed for certain direct costs it incurs on behalf of the Division of State Lottery.

For the purposes of the incentive and/or shortfall calculation, the calculation is predicated on the net income targets contained in the Northstar NJ contract (see Schedule of Northstar NJ Net Income Targets). The Division of Lottery's actual net income for a fiscal year is decreased when Northstar NJ earns an incentive payment and is increased if Northstar NJ is obligated to pay a shortfall payment.

Due to the complexities of the contract with Northstar NJ, a transition period was necessary. The transition period commenced with the contract signing in June 2013 and ended on September 30, 2013. During this time, most of the Division of State Lottery's marketing and sales force left State service and became Northstar NJ employees. Also during this period, Northstar NJ assumed the marketing, advertising and related functions of the Division of State Lottery.

Northstar NJ's first operational year, the year ending June 30, 2014 was a stub year October 1, 2013 through June 30, 2014. The remaining fifteen years (Fiscal years 2015 — 2029) of the contract will coincide with the Lottery's fiscal year, starting on July 1 and ending on June 30 through the year ending June 30, 2029.

INTRODUCTION (Continued)

As part of the agreement, certain lottery contracts were assigned to Northstar NJ. Such contracts included:

- GTECH Corporation is contracted to provide ticket sales through the online terminal network and the warehousing and distribution of instant tickets and promotional materials. GTECH is also responsible for providing communications between sales terminals and GTECH data centers.
- Pollard Bank Note, Scientific Games and GTECH Printing are contracted to print and support instant game products.
- Brushfire, Inc. is contracted to provide marketing and advertising services.

Under the terms of Northstar NJ's contract, Northstar NJ will have the latitude to renew, renegotiate, extend or rebid contracts for such services as it deems necessary subject to the Division of State Lottery's approval.

The Division of State Lottery offers various products for sale with prize awards ranging from $1.00 to annuity prizes well in excess of $100 million. The various products sold are:

- Instant Games
- Pick 3 (Including Pick 3 Instant Match)
- Pick 4 (Including Pick 4 Instant Match)
- Jersey Cash 5 (including Jersey Cash 5 Instant Match)
- Pick 6 Lotto
- Mega Millions
- Powerball
- CASH4LIFE (*Initiated on June 13, 2014 with the first drawing conducted on June 16, 2014.)

FINANCIAL HIGHLIGHTS

The Division of State Lottery's financial position at June 30, 2014 and 2013, consisted of total assets of $517 million and $589 million, respectively, and total liabilities of $516 million and $580 million, respectively. A substantial portion of the asset and liability amounts relates to the Division of State Lottery's annuity investment in prize awards. The total amounts invested and due to Division of State Lottery winners as future installment payments at June 30, 2014 and 2013, were $296 million and $333 million, respectively. Net position decreased from $9 million in fiscal year 2013 to $0.80 million in fiscal year 2014.

FINANCIAL STATEMENTS

The Division of State Lottery's financial statements include the statement of net position as of June 30, 2014 and 2013, the statement of revenues, expenses and changes in net position for the years ended, June 30, 2014 and 2013, and the statement of cash flows for the years ended June 30, 2014 and 2013. The financial statements are prepared in accordance with the accounting principles established by the Governmental Accounting Standards Board.

FINANCIAL STATEMENTS (Continued)

Statement of Net Position

The statement of net position presents the Division of State Lottery's financial position as of the last day of the fiscal year. The Division of State Lottery's assets, liabilities and net position are summarized (in millions) as follows:

	June 30,		
	2014	2013	2012
Current Assets	$ 272	$ 321	$ 297
Deposit Fund Contracts	245	268	306
Total Assets	517	589	603
Current Liabilities	270	311	284
Non-Current Liabilities	246	269	307
Total Liabilities	516	580	591
Restricted Net Position	0.50	2	5
Unrestricted Net Position	0.30	7	7
Total Net Position	$ 0.80	$ 9	$ 12

Current assets consist of cash and investments in the State of New Jersey Cash Management Fund (the "NJCMF"), accounts receivable, current year annuity investments, and deferred expenses. The investment in the NJCMF totaled $204 million and $238 million at June 30, 2014 and 2013, respectively.

The Division of State Lottery funds long-term installment prizes with insurance company annuities and United States Treasury securities. The total value of these investments was $296 million and $333 million as of June 30, 2014 and 2013, respectively. The Division of State Lottery has annuity investments with ten (10) insurance companies. The total market value of the United States Treasury securities was $45 million and $43 million at June 30, 2014 and 2013, respectively. The annuities due beyond fiscal year 2015 total $246 million and represent the non-current assets reported on the Division of State Lottery's statement of net position. Although categorized as an asset, annuities represent an obligation that the Division of State Lottery has to the annuitants to fund the monies due to them over a fixed period of time based on the amount of the annuitized jackpot at the time of the "win." The duration of an annuity varies from twenty to thirty years. Because of the true nature of these annuities, the Division of State Lottery has a fiduciary responsibility to continue to administer these instruments in a responsible and prudent manner. The current amounts due to annuity winners totaled $51 million and $65 million as of June 30, 2014 and 2013, respectively.

Non-current liabilities represent annuity prize awards due beyond 2015 and also include the total due for unused vacation and sick leave (compensated absences).

FINANCIAL STATEMENTS (Continued)

Statement of Net Position (Continued)

Net position represents the excess of the Division of State Lottery's assets over its liabilities and are summarized as follows (in millions):

	June 30,		
	2014	2013	2012
Restricted (Unclaimed Prize Reserves)	$ 0.50	$ 2	$ 5
Unrestricted	0.30	7	7
Total Net Position	$ 0.80	$ 9	$ 12

Expired prizes, or unclaimed prize reserves, are restricted to fund either future prizes or state contributions.

Statement of Revenues, Expenses and Changes in Net Position

The results of the Division of State Lottery's operations are presented in the statement of revenues, expenses and changes in net position, which is summarized (in millions) as follows:

	Years Ended June 30,		
	2014	2013	2012
Operating revenues			
Ticket sales	$ 2,901	$ 2,821	$ 2,759
Forfeited prizes	39	39	38
Miscellaneous income	2	1	1
Total operating revenue	2,942	2,861	2,798
Operating expenses			
Prize expenses	1,732	1,670	1,618
Retailer commissions	162	158	154
Northstar NJ fees and expenses	29	-	-
Vendor fees	46	36	37
Administrative expense	16	35	37
Bad debt expense	1	-	-
Total operating expenses	1,986	1,899	1,846
Operating income	956	962	952
Non-Operating Revenue (expenses)	1	120*	(1)
Income before transfers out	957	1,082	951
Operating transfers - state contributions	965	1,085	950
(Decrease) increase in net position	$ (8)	$ (3)	$ 1

*As part of the contract terms, Northstar NJ provided a $120 million "accelerated guarantee payment" to the Division of State Lottery which was reflected in the FY 2013 financials as non-operating revenue. Of this amount, $20 million is apportioned for use by Northstar NJ to offset any Contribution Shortfall Payments required under the compensation terms of the contract.

The Division of State Lottery awarded approximately $1.732 billion in prize awards in fiscal year 2014 and over $1.670 billion in fiscal year 2013. Almost 111 million winning tickets were validated and paid in fiscal year 2014 and over 107 million were validated and paid in fiscal year 2013.

FINANCIAL STATEMENTS (Continued)

Statement of Revenues, Expenses and Changes in Net Position (Continued)

The Division of State Lottery's vendors provided critical services including the production, warehousing, distribution and accounting for all lottery tickets. The total compensation paid for the Division of State Lottery's vendors and network fees was $75 million in fiscal year 2014. Of this amount $29 million was paid directly to Northstar NJ for the services it provided or procured on behalf of the Division of State Lottery subsequent to the October 1, 2013 start date of the management contract. Included in the $29 million paid to Northstar NJ was $16 million for advertising and marketing costs. In fiscal year 2013, $56 million was paid to all such vendors, including $21 million for advertising and marketing costs. Overall, advertising and marketing costs for fiscal years 2014 and 2013 totaled $22 million and $21 million, respectively.

The Division of State Lottery's administrative expenses for the fiscal years 2014 and 2013 totaled $16 million and $35 million, respectively. These administrative expenses include salaries, advertising, auditing services, rent, security, data processing services, office supplies and attorney general fees. The decline from fiscal 2013 to fiscal 2014 is directly attributable to the inception of the Northstar NJ contract which shifted advertising expenses from the Division of State Lottery to Northstar NJ. Other contributing factors for the decline are reduced rent and salary expenses due to reduced space needs and staffing levels.

The Division of State Lottery is required by State of New Jersey Lottery law to contribute a minimum of 30% of net revenues from ticket sales to the State of New Jersey, Department of Treasury for state aid for education and state institutions. As a result of various sales initiatives, game enhancements and efficient operations, the Division of State Lottery contributed $965 million, 33% of net sales, in fiscal year 2014 and $965 million, 34% of net sales, in fiscal year 2013. In fiscal year 2013, an additional $120 million was contributed to the State for state aid to education and state institutions as a result of a contract award to Northstar NJ. As part of the contract terms, Northstar NJ provided an "accelerated guarantee payment" in the amount of $120 million.

During the term of the contract, Northstar NJ's incentive compensation is reduced in the event the annual contractual net income target is not met or increased in the event that the net income target is exceeded. Furthermore, in the event that actual net income is significantly below the contracted net income target, then the contribution shortfall payment provisions are invoked.

The base services commencement date for Northstar NJ was October 1, 2013, this was the date that Northstar NJ became responsible to meet their net income target for fiscal year 2014, which was the stub year. Northstar NJ's net income target for the stub year period was prorated based on 9 months of services. The net income target was adjusted to $760.9 million.

In fiscal year 2014, the actual stub year net income was $705.5 million; this shortfall of more than $55 million would necessarily have caused a contribution shortfall payment.

The contract contains two scenarios for calculating the contribution shortfall payment. In the first scenario, if net income for the contract year is less than the Net Income Target but greater than the Base Level Income, then Northstar will issue to the Division of State Lottery a Contribution Shortfall Payment equal to 50% of the difference between the Net Income Target and the actual Net Income for that specific contract year. If Net Income is less than the Base Level Income, then Northstar NJ will issue to the Division of State Lottery a Contribution Shortfall Payment equal to the sum of 50% of the difference between the Base Level Income and the Net Income Target plus 100% of the difference between the Net Income and the Base Level Income.

Statement of Revenues, Expenses and Changes in Net Position (Continued)

The contract does establish bottom and top caps on Northstar NJ's compensation. In the event of a particularly lucrative contract year (Upper Income Levels are surpassed) total compensation to Northstar NJ cannot exceed 5% of Net Income for the entire contract year. Conversely, in a subpar contract year, the contribution shortfall payment cannot exceed 2% of Net Income.

In fiscal year 2014, the latter scenario was utilized to calculate the Contribution Shortfall Payment as outlined below.

Contribution Shortfall Payment, below Target, above Base	($21,808,805)
Contribution Shortfall Payment below Base	($11,737,583)
Net Contribution Shortfall Payment	($33,546,387)
Low Cap (Contribution Shortfall cannot exceed 2% of Target)	**($14,110,837)**

The Northstar NJ contract provides for an allowance of $20 million to offset any potential contribution shortfall payments over the life of the contract. The calculated contribution shortfall amount of $14,110,837 was deducted from the $20 million allowance for such purposes leaving a contribution shortfall allowance balance of $5,889,163 moving forward.

Statement of Cash Flows

The statement of cash flows are summarized (in millions) as follows:

	Years Ended June 30,		
	2014	2013	2012
Cash flows provided by operating activities	$ 916	$ 1,022	$ 978
Cash flows used in non-capital financing activities	(950)	(1,081)	(953)
Cash flows provided from investing activities	34	57	(23)
Net (decrease) increase in cash	$ -	$ (2)	$ 2

SUMMARY AND OUTLOOK

Division of State Lottery management has been working closely with Northstar NJ throughout fiscal year 2014, and looks forward to continuing this exciting partnership going into the first full year of the contract.

On June 13, 2014, the Division of State Lottery launched "CASH4LIFE", a new multi-state draw game (New Jersey and New York) in which players can win $1,000 a day for life, $1,000 a week for life or a variety of other prizes. To date "CASH4LIFE" has exceeded expectations and is proving very popular with players. Additionally, on October 19, 2014, another new multi-state draw game called "Monopoly Millionaires' Club" will be launched. Monopoly Millionaires Club offers three different ways to win $1 million or more on each ticket and is designed to create hundreds of millionaires. The game will also have its own national TV game show that is scheduled to premiere in February 2015.

Looking forward, players and retailers can expect to see new promotions and incentive programs, expansion of the retailer base, other new games and other beneficial changes. With the assistance of Northstar NJ, the Division of State Lottery will continue to enhance its position as a major revenue source for the State of New Jersey. The revenue generated by the Division of State Lottery funds various educational and institutional programs throughout the State.

CONTACTING THE DIVISION OF STATE LOTTERY'S FINANCIAL MANAGEMENT

This financial report is designed to provide citizens with a general overview of the Division of State Lottery's finances. If you have any questions about this report or need additional financial information, contact the Division of State Lottery's Deputy Director of Finance at One Lawrence Park Complex, 1333 Brunswick Avenue, PO Box 041, Lawrenceville, New Jersey 08625-0041.

MERCADIEN, P.C.
CERTIFIED PUBLIC ACCOUNTANTS

INDEPENDENT AUDITORS' REPORT

State of New Jersey
Department of Treasury
Division of State Lottery

Report on the Financial Statements

We have audited the accompanying financial statements of the State of New Jersey, Department of Treasury, Division of State Lottery (the "Division of State Lottery") as of and for the years ended June 30, 2014 and 2013, and the related notes to financial statements, which collectively comprise the Division of State Lottery's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes 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.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Division of State Lottery as of June 30, 2014 and 2013, and the respective changes in its financial position and cash flows thereof for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages one through six be presented to supplement the basic financial statements. Such information, 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.

Other Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Division of State Lottery's basic financial statements. The accompanying schedules of revenues, expenses and changes in net position budget and actual, instant game revenues and administrative expenses are presented for the purposes of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information except for the portion marked "unaudited," has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, except for the portion marked "unaudited," the schedules of revenues, expenses and changes in net position budget and actual, instant game revenues and administrative expenses are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

The schedule of Northstar NJ net income targets as listed in the table of contents has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our reports dated October 31, 2014 and November 1, 2013, for the years ended June 30, 2014 and 2013, respectively, on our consideration of Division of State Lottery's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Division of State Lottery's internal control over financial reporting and compliance.

Mercadien, P.C.
Certified Public Accountants

MERCADIEN, P.C.
CERTIFIED PUBLIC ACCOUNTANTS

October 31, 2014

MERCADIEN, P.C.
CERTIFIED PUBLIC ACCOUNTANTS

INDEPENDENT AUDITORS' 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*

State of New Jersey
Department of Treasury
Division of State 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 Division of State Lottery as of and for the years ended June 30, 2014 and 2013, and the related notes to financial statements, which collectively comprise the Division of State Lottery's basic financial statements, and have issued our report thereon dated October 31, 2014.

Internal Control over Financial Reporting

In planning and performing our audits of the basic financial statements, we considered the Division of State Lottery's internal control over financial reporting (internal control) to determine the 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 Division of State Lottery's internal control. Accordingly, we do not express an opinion on the effectiveness of the Division of State 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 Division of State Lottery'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 may exist that have not been identified.

INDEPENDENT AUDITORS' 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)

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Division of State Lottery's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. 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 entity'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.

Mercadien, P.C.
Certified Public Accountants

MERCADIEN, P.C.
CERTIFIED PUBLIC ACCOUNTANTS

October 31, 2014

STATE OF NEW JERSEY, DEPARTMENT OF TREASURY, DIVISION OF STATE LOTTERY

STATEMENT OF NET POSITION

	Years Ended June 30, 2014	2013
ASSETS		
Current Assets		
Cash	$ 407,418	$ 434,249
Accounts receivable, net of allowance for doubtful accounts of $2,395,000 and $2,527,000 in 2014 and 2013, respectively	13,220,416	5,179,496
Deferred expenses	3,027,054	12,823,215
Investments		
Deposit fund contracts	50,768,499	64,581,504
State of New Jersey Cash Management Fund	204,414,284	238,214,847
Total Current Assets	271,837,671	321,233,311
Non-Current Assets		
Investments - deposit fund contracts	245,502,273	268,039,828
Total Non-Current Assets	245,502,273	268,039,828
Total Assets	517,339,944	589,273,138
LIABILITIES		
Current Liabilities		
Accounts payable and accrued expenses	$ 13,772,463	$ 46,603,451
Obligation for unpaid prize awards	89,780,528	99,041,473
Installment prize awards	50,768,499	64,581,504
Due to State of New Jersey - education and state institutions	116,010,000	101,009,581
Total Current Liabilities	270,331,490	311,236,009
Non-Current Liabilities		
Compensated absences	686,899	984,403
Installment prize awards	245,502,273	268,039,828
Total Non-Current Liabilities	246,189,172	269,024,231
Total Liabilities	516,520,662	580,260,240
NET POSITION		
Restricted for prize awards or contributions for aid to education and state institutions	499,998	2,139,036
Unrestricted	319,284	6,873,862
Total Net Position	$ 819,282	$ 9,012,898

See accompanying notes to financial statements.

STATE OF NEW JERSEY, DEPARTMENT OF TREASURY, DIVISION OF STATE LOTTERY

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

	Years Ended June 30, 2014	2013
Operating Revenues		
Ticket Sales		
Pick 3	$ 436,742,690	$ 434,042,304
Pick 4	268,396,396	266,142,981
Jersey Cash 5	148,226,709	144,392,456
Pick 6 Lotto	77,529,761	65,323,206
CASH4LIFE	4,727,306	-
Mega Millions	205,860,905	136,832,941
Powerball	233,653,931	300,381,206
Raffle sales	1,227,770	-
Instant games	1,531,771,568	1,474,285,065
Sales discounts/tickets provided as prizes	(6,491,474)	-
Total Ticket Sales	2,901,645,562	2,821,400,159
Other Revenues		
Forfeited prizes	38,866,559	38,677,399
Miscellaneous	1,705,289	881,235
Total Operating Revenues	2,942,217,410	2,860,958,793
Operating Expenses		
Prize expenses	1,731,959,514	1,670,394,764
Retailer commissions	162,107,574	157,880,945
Instant ticket vendor printing fees	18,706,070	18,140,608
Gaming system vendor fees	27,220,623	17,398,700
Northstar NJ management fee	3,552,740	-
Northstar NJ manager expenses	9,383,269	-
Northstar NJ advertising & marketing expenses	16,331,995	-
Administrative expenses	15,877,577	35,276,475
Multi-state fees	65,122	14,751
Drawing broadcast fees	5,980	126,906
Bad debt expense	400,000	-
Total Operating Expenses	1,985,610,464	1,899,233,149
Operating Income	956,606,946	961,725,644
Non-Operating Revenue		
Interest	209,438	213,544
Accelerated guarantee payment	-	120,000,000
Income before Transfers Out	956,816,384	1,081,939,188
Northstar NJ incentive (shortfall) payment	-	-
Income available for Transfers Out	956,816,384	1,081,939,188
Transfers Out - contributions for state aid to education and state institutions	965,010,000	1,085,009,581
Change in net position	(8,193,616)	(3,070,393)
Net position, beginning of year	9,012,898	12,083,291
Net position, end of year	$ 819,282	$ 9,012,898

See accompanying notes to financial statements.

STATE OF NEW JERSEY, DEPARTMENT OF TREASURY, DIVISION OF STATE LOTTERY

STATEMENT OF CASH FLOWS

	Years Ended June 30, 2014	2013
Cash Flows from Operating Activities		
Sales to customers, net	$ 1,428,992,039	$ 1,399,110,374
Payments for prize awards	(423,866,990)	(332,958,165)
Payments for vendor commissions and fees	(67,742,494)	(35,953,906)
Payments to suppliers	(34,833,546)	(23,552,491)
Other payments	(19,526)	(36,652)
Cash flows from annuity operations		
Annuity receipts	64,581,504	77,794,504
Purchases of annuities	(8,408,676)	(7,744,300)
Payments of annuity prizes	(42,729,559)	(54,811,336)
Net Cash Provided by Operating Activities	915,972,752	1,021,848,028
Cash Flows used in Non-Capital Financing Activities		
Contributions for aid to education and state institutions	(950,009,581)	(1,081,082,267)
Cash Flows from Investment Activities		
Cash Management Fund proceeds	1,281,510,000	1,278,268,000
Cash Management Fund purchases	(1,247,500,000)	(1,341,250,000)
Accelerated Guarantee Payment	-	120,000,000
Net Cash Provided by Investing Activities	34,010,000	57,018,000
Net decrease in cash	(26,830)	(2,216,239)
Cash, beginning of year	434,249	2,650,488
Cash, end of year	$ 407,418	$ 434,249
Reconciliation of Operating Income to Net Cash Provided by Operating Activities		
Operating Income	$ 956,606,946	$ 961,725,644
Changes in assets and liabilities		
Accounts receivable	(8,040,920)	6,346,946
Investments - deposit fund contracts	36,350,560	67,317,443
Other assets	9,796,161	1,089,073
Accounts payable and accrued expenses	(32,830,987)	19,471,278
Obligation for unpaid prize awards	(45,611,505)	(34,047,207)
Compensated absences	(297,504)	(55,149)
Net Cash Provided by Operating Activities	$ 915,972,752	$ 1,021,848,028

STATE OF NEW JERSEY, DEPARTMENT OF TREASURY, DIVISION OF STATE LOTTERY

NOTES TO FINANCIAL STATEMENTS

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The State of New Jersey, Department of Treasury, Division of State Lottery (the "Division of State Lottery") and the State Lottery Commission (the "Commission") were concurrently established in 1970, pursuant to the "State Lottery Law" (N.J.S.A. 5:9-1 et seq.). The Division of State Lottery operates within the Department of Treasury of the State of New Jersey. The Commission consists of the State Treasurer and six public members and is authorized and empowered to promulgate rules and regulations regarding the conduct of lottery games, including the price or prices of tickets, the number and size of prizes on winning tickets, the licensing of retailers, and the apportionment of ticket revenues. The Division of State Lottery's financial statements are presented as those of an enterprise fund and include the operations for which the Division of State Lottery is financially accountable and exercises oversight responsibility.

Basis of Accounting

The Division of State Lottery prepares its financial statements using the accrual basis of accounting. Revenues are recognized when earned, and expenses are recognized when incurred.

In its accounting and financial reporting, the Division follows the pronouncements of the Governmental Accounting Standards Board ("GASB") and other entities that promulgate accounting principles. Per GASB Statement 55, The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments, priority is established as to which source of accounting principles to utilize in determining proper accounting treatment. The hierarchy is as follows: GASB Statements and Interpretations; GASB Technical Bulletins; American Institute of Certified Public Accountants ("AICPA") Industry Audit and Accounting Guides and AICPA Statements of Position, if applicable, and cleared by GASB; AICPA Practice Bulletins, if applicable, and cleared by GASB; Implementation Guides published by the GASB; AICPA pronouncements that are not specifically applicable to state and governmental entities; Financial Accounting Standards Board ("FASB") Statements and Interpretations; and Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee of Accounting Procedure issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. GASB Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting, provides proprietary activities with a choice of authoritative guidance issued after November 30, 1989. The Division of State Lottery has elected to follow GASB pronouncements exclusively after that date.

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 and disclosures. Accordingly, actual results could differ from those estimates.

State of New Jersey Cash Management Fund

Investments in the State of New Jersey Cash Management Fund are valued at cost, which approximates fair value.

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Accounts Receivable

Accounts receivable is comprised primarily of amounts due from retailers. The allowance for uncollectible accounts is funded by a $100 per year license renewal fee paid by the Division's retailers. Operating expense is charged with an allowance for estimated uncollectible accounts based on past experience and an analysis of current accounts receivable collectibility. Accounts deemed uncollectible are charged to the allowance in the year they are deemed uncollectible.

Installment Prize Awards and Prize Expenses

Installment prize awards are recorded based upon the present value of an annuity at terms to yield a series of future payments needed to meet the obligations of the Division of State Lottery for prize disbursements. The Division of State Lottery purchases annuity contracts from insurance companies and U.S. government securities to fund its liability for installment prize awards. An annuity contract represents an obligation by an insurance company to provide a fixed series of payments over a specified period. Annuity contracts are subject to credit risk. The Division of State Lottery seeks to control its exposure to such credit risk by purchasing annuity contracts only from insurance companies that meet certain minimum standards. Such standards include the following requirements:

1. Combined capital and surplus of at least $1 billion;
2. Admitted assets of at least $10 billion;
3. Risk-based capital ratio of at least 300%; and
4. Must have ratings equal to or better than at least two of the three private rating agencies:
   - Standard & Poor's long-term insurer financial strength rating of AA- or higher
   - AM Best financial strength rating of "A" or higher
   - Moody's long-term insurance financial strength rating of "Aa3" or higher

Due to the long-term nature of these contracts, the credit quality of the issuer is subject to change. Amounts recorded as prize expense reflect the cost of annuity contracts and U.S. government securities necessary to satisfy stated prize awards plus any single payment awards. These annuities are presented on the statements of net position as deposit fund contracts, carried at contract value which approximates fair value.

Equipment

The Division follows the state's threshold for capitalizing equipment as follows: machinery and equipment over $20,000 and motor vehicles over $30,000. Purchases that do not meet the threshold for capitalization are recognized as expenses in the statements of revenues, expenses and changes in net assets in the period during which they are acquired and are included in administrative expenses. As of June 30, 2014 and 2013, leasehold improvements included in deferred expenses were $594,968. For the years ended June 30, 2014 and 2013, amortization expense was $52,668 and $99,159, respectively.

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Net Position

Restricted

Amounts restricted for prize awards or contributions for aid to education and state institutions consist of prizes that are not claimed within one year from the date of the drawing for machine games and within one year from the date of game's closing for instant games.

Unrestricted

The unrestricted net position represents resources available for current operating expenses in compliance with legal and budgetary restrictions.

Revenue Recognition

Revenues from the sale of lottery tickets are recognized as follows:

- "Pick-3," "Pick-4," "Jersey Cash 5," "Pick-6 Lotto," "Mega Millions," "Megaplier," "Powerball," "Power Play," "CASH4LIFE," and various raffle games on the drawing date.
- Instant games are recognized daily, based upon the settlement of instant game inventory packs by selling retailers. Sales adjustments are recorded based upon final reconciliations prepared after the termination of a lottery instant game.
- Sales discounts are recorded for the sales value of tickets provided to retailers at no cost, to be used for promotional purposes. Tickets provided as prizes are recorded as sales at the face value of each ticket, then backed out as discounts and are not included in prize expense.

Forfeited Prizes

The State Lottery Law requires that prizes not claimed within one year from the date of the drawing for machine games and within one year from the date of the game's closing for instant games be forfeited. Effective November 21, 1991, the Commission authorized that 70% of forfeited prizes are to be maintained restricted for prize awards and are available to augment future prize awards or, at the discretion of the executive director, to augment the Division of State Lottery's contribution for state aid for education and state institutions. The remaining 30% goes directly to contributions to aid education and institutions to be consistent with the 30% minimum contribution requirement of the State Lottery Law. Forfeited prizes are recognized as "Other Revenues" during the period forfeited. For the years ended June 30, 2014 and 2013, forfeited prizes were $38,866,559 and $38,677,399, respectively.

Contributions and Prize Awards

The State Lottery Law requires no less than 30% of total revenues accruing from ticket sales to be paid to the State Treasury for state aid for education and state institutions. Contributions for the years ended June 30, 2014 and 2013, aggregated $965,010,000 and $1,085,009,581, respectively, of which $116,010,000 and $101,009,581 was due to the State Treasury at June 30, 2014 and 2013, respectively. The 2013 contribution included a $120 million Accelerated Guarantee Payment received from Northstar New Jersey Lottery Group, LLC ("Northstar NJ" or "NSNJ").

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Contributions and Prize Awards (Continued)

For machine games, the Division of State Lottery has designated that a minimum of 45% of gross revenues be allocated for prize awards, including retailer bonuses. Prize expense is recorded when the winning ticket number is selected for the respective lottery game based on eligible winning tickets sold. For instant games, the percentage of gross revenues to be allocated for prize awards varies by game.

Commissions and Fees

Retailers receive a commission of 5% based on the total tickets sold and a commission of 1.25% of terminal validations. The online game contractor receives a fee equal to a contractual percentage of the revenue generated through the respective network maintained by the contractor. All other gaming contractors are paid fees based on the units of service provided.

Northstar NJ has had numerous retailer incentive programs for the purpose of boosting sales, these include temporary commission increases and bonuses. Both of these incentives are recorded as prize expense.

Vacation and Sick Leave

The Division records vacation and sick time incurred during the period in "administrative expenses" in the accompanying statements of revenues, expenses and changes in net assets. Payments for accumulated sick leave balances are made to retiring employees upon regular retirement from the State of New Jersey's General Fund. Such payment is based on 50% of the employee's sick leave accumulation at the pay rate in effect at the time of retirement, up to a maximum of $15,000. Employees separating from service prior to retirement are not entitled to payments for accumulated sick leave.

Advertising

The Division of State Lottery uses advertising to promote the sale of lottery tickets. The costs of advertising are expensed as incurred. Advertising expense included in administrative expense amounted to $5,204,308 and $20,736,101 for the years ended June 30, 2014 and 2013, respectively. Starting October 1, 2013, these services were transferred to Northstar NJ as part of the management contract.

New Accounting Pronouncement

The Governmental Accounting Standards Board has issued Statement No. 68, "Accounting and Financial Reporting for Pension Plans" effective for fiscal years beginning after June 15, 2014. The objective of the statements is to improve information about financial support for pensions and improve financial reporting and accounting by state and local governmental pension plans. Statement No. 68 establishes standards for measuring and recognizing liabilities, deferred outflows and inflows, and expenses and requires the calculation and recording of a net pension liability and subsequent allocation of the unfunded liability to individual employers participating in the plans, including a proportionate share of the actuarial valuation. Full time employees of the Lottery are covered by the Public Employee's Retirement System of the State of New Jersey ("PERS") which is a cost sharing, multiple-employer defined benefit plan. As such, the Lottery will receive information from the State of New Jersey for inclusion in its financial statements and disclosures. The Lottery plans to implement these standards for its fiscal year ending June 30, 2015.

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

New Accounting Pronouncement (Continued)

The GASB has issued Statement No. 71, "Pension Transition for Contributions Made Subsequent to the Measurement Date - an amendment of GASB Statement No. 68". This Statement amends paragraph 137 of Statement 68 to require that, at transition, a government recognize a beginning deferred outflow of resources for its pension contributions, if any, made subsequent to the measurement date of the beginning net pension liability. Statement 68, as amended, continues to require that beginning balances for other deferred outflows of resources and deferred inflows of resources related to pensions be reported at transition only if it is practical to determine all such amounts. The provisions of this Statement are required to be applied simultaneously with the provisions of Statement 68.

Reclassification of Prior Year Balances

Certain prior year balances have been reclassified to conform with the current year's presentation.

B. CASH AND INVESTMENTS

The Division of State Lottery adopted GASB Statement No. 40, "Deposits and Investment Risk Disclosures," which requires uncollateralized deposits exposed to custodial credit risk to be disclosed. The custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits that are in possession of an outside party. The following is a summary of the Division's cash deposits by financial institution and the amount exposed to custodial credit risk at June 30, 2014 and 2013. The Division's deposits with Wells Fargo are insured by the Federal Deposit Insurance Corporation up to $250,000.

	June 30,	
	2014	2013
Wells Fargo	$ 407,418	$ 434,249
New Jersey Cash Management Fund	204,414,284	238,214,847
Total	$ 204,821,702	$ 238,649,096

The New Jersey Cash Management Fund is a common trust fund administered by the Department of the Treasury, Division of Investments. Securities in the fund are insured, registered or held by the Division of Investment or its agents in the Division's name. Since the New Jersey Cash Management Fund is a pooled investment and the cash balance is guaranteed by the State of New Jersey, the Commission's investment in the New Jersey Cash Management Fund is not subject to custodial credit risk under GASB Statement No. 40.

Fair Value Measurements

The Division of State Lottery follows the Fair Value Measurements Topic of the FASB Accounting Standards Codification, which provides a framework for measuring fair value under accounting principles generally accepted in the United States of America.

As defined in the Fair Value Measurements Topic of the FASB Accounting Standards Codification, fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In determining fair value, the Division of State Lottery uses the stock market index approach. Based on this approach, the Division of State Lottery often utilizes certain assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and or the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated, or generally unobservable inputs.

B. CASH AND INVESTMENTS (Continued)

The Division of State Lottery utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. Based on the observability of the inputs used in the valuation techniques the Division of State Lottery is required to provide the following information according to the fair value hierarchy. The fair value hierarchy ranks the quality and reliability of the information used to determine fair values. Financial assets and liabilities carried at fair value will be classified and disclosed in one of the following three categories:

Level 1 - Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange. Level 1 also includes U.S. Treasury and federal agency securities and federal agency mortgage-backed securities, which are traded by dealers or brokers in active markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 - Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained from third-party pricing services for identical or similar assets or liabilities.

Level 3 - Valuations for assets and liabilities that are derived from other valuation methodologies, including option pricing models, discounted cash flow models and similar techniques, and not based on market exchange, dealer or broker-traded transactions. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets or liabilities.

Fair Value on a Recurring Basis
The table below presents the balances of investments - deposit fund contracts measured at fair value on the statement of net position as of June 30, 2014 and 2013:

	June 30, 2014			
	Total	Level 1	Level 2	Level 3
Annuity Investment Deposit Fund Contracts	$ 296,270,772	$ 44,563,284	$ 251,707,488	$ -
Total	$ 296,270,772	$ 44,563,284	$ 251,707,488	$ -
	June 30, 2013			
Annuity Investment Deposit Fund Contracts	$ 332,621,332	$ 43,409,922	$ 289,211,410	$ -
Total	$ 332,621,332	$ 43,409,922	$ 289,211,410	$ -

C. FUTURE INSTALLMENT PRIZE AWARDS

The Division of State Lottery purchases annuity, or deposit fund contracts, from insurance companies and U.S. government securities to fund its liability for future installment prize awards. Generally, annuity contracts fund Win for Life instant game annuity prizes, and U.S. government securities fund annuity prizes for Pick 6, Mega Millions and Powerball. An annuity contract represents an obligation by an insurance company to provide a fixed series of payments over a specified period.

Annuity contracts are carried at their current contract values, which are based upon their original purchase prices adjusted for credited interest and amounts already received. Annuity contracts are subject to credit risk. The Division of State Lottery seeks to control its exposure to such credit risk by purchasing annuity contracts only from insurance companies that meet certain minimum standards. Such standards include the following requirements:

1. Combined capital and surplus of at least $1 billion;
2. Admitted assets of at least $10 billion;
3. Risk-based capital ratio of at least 300%; and
4. Must have ratings equal to or better than at least two of the three private rating agencies:
   - Standard & Poor's long-term insurer financial strength rating of AA- or higher
   - AM Best financial strength rating of "A" or higher
   - Moody's long-term insurance financial strength rating of "Aa3" or higher.

According to the Division of State Lottery's calculation, only one company does not meet the criteria, that of Sun Life Assurance; as of June 30, 2014, Sun Life Assurance had annuity contracts totaling approximately $36,773,973. However, due to the long-term nature of these contracts, the credit quality of the issuer is subject to change. At June 30, 2014 and 2013, the Division of State Lottery held insurance company annuity contracts totaling $251,707,488 and $289,211,410, respectively, issued through ten insurance companies, which are due in installments ranging from twenty-five years to the lifetime of the recipient. The estimated fair value of annuity contracts approximates the carrying value reflected in the accompanying statement of net position at June 30, 2014 and 2013.

U.S. government securities are carried at fair value. At June 30, 2014 and 2013, the Division of State Lottery had $44,563,284 and $43,409,922, respectively, in U.S. treasuries.

Concentrations of Credit Risk

"Concentration of Credit Risk" is the risk that relates to the amount of investment at any one entity. The disclosure requirement of this risk factor is limited to investments in excess of 5% of the total. Guaranteed annuity contracts, as stated above, are the only category subject to concentration of credit risk disclosure.

A significant portion (in excess of 5% of total) of the Division of State Lottery's investment in annuity contracts at such date is invested with each of the following five companies:

- Ohio National Life
- New York Life Insurance Co.
- Protective Life
- Metropolitan Life
- Sun Life Assurance

D. LITIGATION

The Division of State Lottery is a party to a number of lawsuits arising out of the conduct of its business. While the ultimate results of the lawsuits or other proceedings against the Division of State Lottery cannot be predicted with certainty, management of the Division of State Lottery does not expect that these matters will have a material adverse effect on the financial position or results of operations of the Division of State Lottery.

E. COMMITMENTS

Contractual Arrangements

The Division of State Lottery maintains a gaming network of over 6,900 retailer locations where all games are sold. GTECH Corporation is responsible for operating the network games and providing courier services under a contract that was assigned to Northstar New Jersey (NSNJ) on October 1, 2013 and expires concurrent with Northstar NJ's contract.

On June 20, 2013, a competitively bid 15-year contract was awarded to Northstar New Jersey Lottery Group, LLC to provide sales and marketing services to the Division of State Lottery. Northstar New Jersey Lottery Group, LLC is owned directly by two members: (1) Scientific Games New Jersey, LLC, and (2) Northstar New Jersey Holding Company, LLC, and indirectly by three companies: (1) GTECH Corporation and (2) OSI LTT NJ Holdings Inc., which are the Members of Northstar New Jersey Holding Company, LLC, and (3) Scientific Games International, Inc., which is the owner of Scientific Games New Jersey, LLC. The base services commenced on October 1, 2013. The contract required NSNJ to bid net income targets for each fiscal year of the 15-year contract. If NSNJ meets or exceeds the net income target for a given fiscal year, they can earn an incentive pay or alternatively, if they don't meet the net income target, they are assessed a penalty. The NSNJ contract provides for an allowance of $20 million to offset any potential contribution shortfall payments over the life of the contract. For fiscal year 2014 (stub year), the calculated contribution shortfall amounted to $14,110,837 which was deducted from the $20 million contractual allowance for such purposes leaving a contribution shortfall allowance balance of $5,889,163.

E. COMMITMENTS (Continued)

Contractual Arrangements (Continued)

Prior to the beginning of each fiscal year the Division of State Lottery and NSNJ agree to an annual business plan that includes the projected operating expenses of NSNJ for the fiscal year. Each month NSNJ may invoice the Division of State Lottery one twelfth (1/12) of the total operating expenses for the fiscal year. Each monthly invoice is accompanied by detailed backup data and information supporting expenses incurred. At the end of the fiscal year NSNJ operating expenses are aggregated and reconciled with any excess returned to the Division of State Lottery. The NSNJ expenses for services to the Division of State Lottery amounted to $29,268,004 for the year ended June 30, 2014.

In addition to the budgeted monthly expenditures, NSNJ receives a system provider vendor fee based on 1.05% of ticket sales and an instant ticket printing fee based on 1.216% of ticket sales as part of its subcontractor agreements. All other gaming contractors are paid fees based on the units of service provided.

Operating Leases

The Division of State Lottery leases certain office facilities and equipment under non-cancelable operating lease agreements expiring through fiscal year 2024.

Future minimum lease payments for office facilities are as follows:

Year Ended June 30,	Amount
2015	$ 793,433
2016	793,433
2017	767,619
2018	638,550
2019	648,583
2020-2024	2,896,229
	$ 6,537,847

Rent expense for office facilities and equipment for the years ended June 30, 2014 and 2013, was $1,127,424 and $1,070,081, respectively.

F. GASB STATEMENT NUMBER 45 - ACCOUNTING AND FINANCIAL REPORTING BY EMPLOYERS FOR POST-RETIREMENT BENEFITS OTHER THAN PENSION

The Division of State Lottery is a member of the State of New Jersey's cost sharing multiple-employer plan for health and post-retirement medical benefits. Thus, the Division of State Lottery's portion of this liability and cost is included in the State of New Jersey's Comprehensive Annual Financial Report, as such, the Liability of Division of State Lottery's employees is covered under the State plan on an annual basis.

Please refer to State website www.state.nj.us for more information regarding the plan.

G. PENSION PLAN

The Division of State Lottery's employees participate in the Public Employees Retirement System of New Jersey ("PERS"), a cost sharing multiple-employer defined benefit plan. The Division of State Lottery's contribution is determined by State statute and is based upon an actuarial computation performed by the PERS.

The Division of State Lottery's total and covered payroll for the years ended June 30, 2014, 2013 and 2012, was $6,421,066, $8,871,554 and $9,000,095, respectively. The State of New Jersey's (the "State") contribution is based on the employer contribution rate developed by the system's actuary. The rate is then applied against the pension eligible salary for all State employees. The State does not keep track of contributions made to PERS for each separate state agency. For fiscal year ended June 30, 2014 and 2013, the contribution rate was 3.06% and 6.03%, respectively. For fiscal year ended June 30, 2012, the contribution rate was 2.71%.

The State of New Jersey, Division of Pension and Benefits, issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the State of New Jersey, Division of Pension and Benefits, P.O. Box 295, Trenton, NJ 08625-0295 or by visiting their website at: www.state.nj.us/treasury/pensions.

H. ROUNDING

Some schedules in the financial statements may have dollar differences due to rounding adjustments.

Must be 18 or older to buy a lottery ticket. Please play responsibly. If you or someone you know has a gambling problem, call 1-800-GAMBLER®.