



**GOVERNMENT OF THE DISTRICT OF COLUMBIA
LOTTERY AND CHARITABLE GAMES CONTROL BOARD
FINANCIAL STATEMENTS**

September 30, 2000 and 1999

(with Independent Auditors' Report thereon)

**Government of the District of Columbia
Lottery and Charitable Games Control Board
September 30, 2000 and 1999**

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2001 M Street, N.W.
Washington, D.C. 20036

Independent Auditors' Report on Financial Statements

To the Mayor and Members of
The Council of the Government of the District of Columbia, and
The Lottery and Charitable Games Control Board
Washington, D.C.

We have audited the accompanying balance sheet of the Lottery and Charitable Games Control Board (Lottery), an enterprise fund of the Government of the District of Columbia (District), as of September 30, 2000, and the related statement of revenues, expenses and changes in retained earnings and the statement of cash flows for the year then ended. These financial statements are the responsibility of the Lottery's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Lottery as of and for the year ended September 30, 1999, were examined by other auditors whose report, dated December 22, 1999, expressed an unqualified opinion thereon.

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

As discussed in note 2, these financial statements only present the financial activity of the Lottery and are not intended to present the financial position, results of operations, and cash flows of the District taken as a whole.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Lottery as of September 30, 2000, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.



In accordance with *Government Auditing Standards*, we have also issued a report dated January 26, 2001 on our consideration of the Lottery's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

KPMG LLP

January 26, 2001

**Government of the District of Columbia
Lottery and Charitable Games Control Board
Balance Sheets
September 30, 2000 and 1999
(dollars presented in thousands)**

ASSETS

	<u>2000</u>	<u>1999</u>
Current assets:		
Cash and cash equivalents	\$ 8,846	\$ 10,637
Accounts receivable, net	3,951	2,958
Inventory	556	467
Prepaid expenses	<u>6</u>	<u>23</u>
Total current assets	<u>13,359</u>	<u>14,085</u>
Property and equipment, net	480	400
Restricted investments	<u>76,878</u>	<u>81,518</u>
Total assets	<u>\$ 90,717</u>	<u>\$ 96,003</u>

LIABILITIES AND RETAINED EARNINGS

Current liabilities:		
Accounts payable	\$ 1,763	\$ 1,939
Accrued payroll and related liabilities	613	576
Deferred revenue	133	151
Accrued prizes and commissions	7,730	8,572
Other current liabilities	325	19
Obligations for unpaid prizes, current portion	<u>8,631</u>	<u>8,631</u>
Total current liabilities	<u>19,195</u>	<u>19,888</u>
Obligations for unpaid prizes, long term portion	<u>68,247</u>	<u>72,887</u>
Total liabilities	<u>87,442</u>	<u>92,775</u>
Retained earnings	<u>3,275</u>	<u>3,228</u>
Total liabilities and retained earnings	<u>\$ 90,717</u>	<u>\$ 96,003</u>

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

**Government of the District of Columbia
 Lottery and Charitable Games Control Board
 Statements of Revenues, Expenses, and Changes in Retained Earnings
 For the Years Ended September 30, 2000 and 1999
 (dollars presented in thousands)**

	<u>2000</u>	<u>1999</u>
Operating revenues:		
Gaming revenues	\$ 215,938	\$ 207,091
Operating expenses:		
Prizes	112,813	110,520
Agent commissions	11,721	11,108
Contractor fees	11,686	13,200
Advertising	3,605	3,213
Administration	7,995	6,934
Amortization and depreciation	<u>155</u>	<u>234</u>
Total operating expenses	<u>147,975</u>	<u>145,209</u>
Operating income	67,963	61,882
Nonoperating revenue:		
Interest	<u>1,534</u>	<u>2,418</u>
Income before transfers	69,497	64,300
Transfers:		
Operating transfers to General Fund of the District	<u>(69,450)</u>	<u>(64,225)</u>
Net income	47	75
Retained earnings, beginning of the year	<u>3,228</u>	<u>3,153</u>
Retained earnings, end of the year	\$ <u>3,275</u>	\$ <u>3,228</u>

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

**Government of the District Of Columbia
Lottery and Charitable Games Control Board
Statements of Cash Flows
For the Years Ended September 30, 2000 and 1999
(dollars presented in thousands)**

	<u>2000</u>	<u>1999</u>
Cash flow from operating activities:		
Operating income	\$ 67,963	\$ 61,882
Adjustments to reconcile operating income to net cash provided by operating activities:		
Amortization and depreciation	155	234
Decrease (increase) in assets:		
Accounts receivable, net	(993)	(1,315)
Inventory	(89)	(12)
Prepaid expenses	17	(18)
Increase (decrease) in liabilities:		
Accounts payable	(176)	(922)
Accrued payroll and related liabilities	37	(10)
Deferred revenue	(18)	20
Accrued prizes and commissions	(842)	(1,203)
Other current liabilities	<u>306</u>	<u>(31)</u>
Net cash provided by operating activities	66,360	58,625
Cash flows from capital and related financing activities:		
Acquisition of property and equipment	(235)	(106)
Cash flows from noncapital financing activities:		
Operating transfers to General Fund of the District	(69,450)	(64,225)
Cash flows from investing activities:		
Receipt of interest	<u>1,534</u>	<u>2,418</u>
Net decrease in cash and cash equivalents	(1,791)	(3,288)
Cash and cash equivalents, beginning of the year	<u>10,637</u>	<u>13,925</u>
Cash and cash equivalents, end of the year	\$ <u>8,846</u>	\$ <u>10,637</u>

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

**Government of the District of Columbia
Lottery and Charitable Games Control Board
Notes to Financial Statements
September 30, 2000 and 1999
(dollars presented in thousands)**

Note 1 - Organization

Organization

The Lottery and Charitable Games Control Board (Lottery) was established by Public Law 3-172 as an independent agency of the Government of the District of Columbia (District). In accordance with the law, the Lottery must remit its monthly gaming revenues, less prizes, operating expenses and a reserve not to exceed 2 percent of projected annual prize payments to the General Fund of the District.

Financial Responsibility and Management Assistance Authority

The District of Columbia Financial Responsibility and Management Assistance Authority (Authority) was created in 1995 with the enactment of Public Law 104-8 to review and approve the budget, legislation, contracts, and borrowing activities of the District. The President of the United States of America (President) appoints the five members of the Authority, who are granted broad powers during a control year to achieve the objectives for which the Authority was created.

A control year is a fiscal year which commences during a control period. A control period commences upon the occurrence of a borrowing from the U.S. Treasury pursuant to D.C. Code 47-3401, a cash deficit estimated to last beyond the current fiscal year or the first half of the subsequent fiscal year, or failure to pay debt service, payroll, employee benefits, or interstate compact payments. The fiscal years ended September 30, 2000 and 1999 were control years for the District. The Lottery, as an enterprise fund of the District was subject to the oversight of the Authority in the fiscal years ended September 30, 2000 and 1999.

Note 2 - Summary of Significant Accounting Policies

Basis of Presentation

The Lottery's financial transactions are accounted for as an enterprise fund in the District's financial statements. The accompanying financial statements are only those of the Lottery and are not intended to present the financial position, results of operations, and cash flows of the District taken as a whole. The District provides certain legal, central accounting, and other services to the Lottery. The costs and revenue associated with these services are not reflected in these financial statements.

**Government of the District of Columbia
Lottery and Charitable Games Control Board
Notes to Financial Statements
September 30, 2000 and 1999
(dollars presented in thousands)**

Basis of Accounting

The accompanying financial statements are prepared on the accrual basis of accounting. Under this method revenues are reported when earned and expenses are reported at the time the related liabilities are incurred. In accordance with Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting*, the Lottery has elected not to follow Financial Accounting Standards Board (FASB) Statements and Interpretations, APB Opinions, and Accounting Research Bulletins issued after November 30, 1989.

Cash and Cash Equivalents

The Lottery participates in the District's pooled cash program whereby cash that is not needed for immediate disbursements is pooled with that of the District and used to purchase current investments. In accordance with the law, the District may invest the pooled cash directly in, or through repurchase agreements, obligations of the United States or its agencies, which are fully guaranteed by the federal government, and in certificates of deposit, which are issued by federally insured banks. In accordance with District policies, substantially all deposits in the pooled cash program were insured or collateralized with securities held by the District or its agent in the District's name. Interest income from the investment of pooled cash is allocated to the Lottery based on the amount the Lottery invests in the pool. The Lottery considers the pooled cash to be cash equivalents for the purpose of cash flows because the pool may not hold the securities for more than 91 days.

Inventory

Inventory, consisting of instant lottery tickets, is valued at cost. The costs of the instant lottery tickets are recorded as expenses when the tickets are sold.

Property and Equipment

Property and equipment are recorded at cost. The cost of major remodeling, betterments, and improvements are capitalized. Repairs and maintenance costs are expensed as incurred. When property and equipment are retired or sold, the cost and related accumulated depreciation are removed from the appropriate property and equipment accounts, and resulting gains or losses are recorded.

**Government of the District of Columbia
Lottery and Charitable Games Control Board
Notes to Financial Statements
September 30, 2000 and 1999
(dollars presented in thousands)**

Amortization and depreciation expense are calculated using the straight-line method over the following estimated useful lives:

<u>Category</u>	<u>Estimated Useful Life</u>
Machinery and equipment	5-8 years
Office furniture and fixtures	5-8 years
Leasehold improvements	5-15 years

Gaming Revenue

Revenue from on-line tickets is recorded as gaming revenue when the drawings are held. On-line tickets sold in advance are recorded as deferred revenue until the drawings are held. Revenue from instant tickets is recorded as gaming revenue when the tickets are activated.

Prize Expense

Prize expense is based on the prize payout percentage for each lottery game and is accrued as the related gaming revenue is earned. The accrued prize liability represents a payable for prize amounts that have not been claimed as of the balance sheet date.

Compensated Absences

The Lottery permits employees to accumulate earned but unused vacation and sick pay benefits. Employees may not accumulate more than 240 hours of vacation benefits depending on the employee's length of service. The Lottery accrues for accumulated vacation as the benefits are earned by employees.

There is not a maximum limitation on the amount of unused sick pay benefits that employees may accumulate. The Lottery does not accrue for non-vesting accumulating rights to receive sick pay benefits. At the time of retirement, unused sick pay benefits are credited at the rate of 22 days for each month of service and are added to the retirees' years of service in the retirement programs. The Lottery accrues for earned sick pay benefits to the extent that it is probable the benefits will result in termination payments at time of retirement rather than used for sick leave. The Lottery estimates the sick pay benefits liability based on the sick pay accumulated at the balance sheet date by employees who are currently eligible for retirement and to receive sick leave payments upon separation, or who are expected to become eligible in the future to receive such payments.

**Government of the District of Columbia
 Lottery and Charitable Games Control Board
 Notes to Financial Statements
 September 30, 2000 and 1999
 (dollars presented in thousands)**

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Note 3 - Accounts Receivable

The components of accounts receivable as of September 30, 2000 and 1999 are as follows:

<u>Description</u>	<u>2000</u>	<u>1999</u>
Due from agents:		
On-line games	\$1,714	\$1,095
Instant games	<u>2,502</u>	<u>2,102</u>
Total due from agents	4,216	3,197
Other	<u>191</u>	<u>217</u>
Total accounts receivable	4,407	3,414
Less allowance for doubtful accounts	<u>(456)</u>	<u>(456)</u>
Total accounts receivable, net	<u>\$3,951</u>	<u>\$2,958</u>

**Government of the District of Columbia
 Lottery and Charitable Games Control Board
 Notes to Financial Statements
 September 30, 2000 and 1999
 (dollars presented in thousands)**

Note 4 - Property and Equipment

A summary of property and equipment as of September 30, 2000 and 1999 is as follows:

<u>Description</u>	<u>2000</u>	<u>1999</u>
Machinery and equipment	\$2,203	\$2,293
Office furniture and fixtures	321	301
Leasehold improvements	<u>605</u>	<u>560</u>
Total property and equipment	3,129	3,154
Less accumulated amortization and depreciation	<u>(2,649)</u>	<u>(2,754)</u>
Total property and equipment, net	<u>\$ 480</u>	<u>\$ 400</u>

Note 5 - Multi-State Lottery Association

Background

The Lottery is a member of the Multi-State Lottery Association (MUSL). MUSL has 22 members and administers a multi-state lottery game. Powerball, the current game, was initiated on April 20, 1992 and is a semi-weekly pari-mutual drawing with a minimum grand prize of \$10,000. MUSL previously administered the Lotto-America game which was terminated on April 18, 1992. All MUSL members remit a portion of their Powerball revenue to MUSL for the prize payments and administrative expenses of Powerball.

Restricted Investments and Obligations for Unpaid Prizes

Lotto-America and Powerball prizes of \$250 or greater are payable to the winner in annual installments over 25 years. The Lottery is responsible for sending the annual payments to Lotto-America and Powerball winners who purchased their winning tickets from the Lottery. MUSL is responsible for providing the Lottery cash to fund these installment payments.

**Government of the District of Columbia
 Lottery and Charitable Games Control Board
 Notes to Financial Statements
 September 30, 2000 and 1999
 (dollars presented in thousands)**

As of September 30, 2000 and 1999, MUSL had purchased for the Lottery, U.S. Government securities aggregating \$114,687 and \$123,318, respectively to fund future installment payments for the Lottery's Lotto-America and Powerball winners. The market value of these securities was \$76,878 and \$81,518 as of September 30, 2000 and 1999, respectively. The investments provide the Lottery cash payments corresponding to the Lottery's obligations to send the annual installments to the prize winners. The Lottery has reflected the market value of the securities as restricted investments and as corresponding obligations for unpaid prizes on the balance sheet.

All restricted investments are insured and registered or are held by the Lottery or its agent in the Lottery's name. The cost and fair market value of the restricted investments at September 30, 2000 and 1999 are as follows:

	<u>2000</u>		<u>1999</u>	
	<u>Cost</u>	<u>Market</u>	<u>Cost</u>	<u>Market</u>
U.S. Government Securities	\$78,027	\$76,878	\$82,637	\$81,518

MUSL Prize Reserves

The prize pool for Powerball consists of 50 percent of each drawing period's sales, including tax. Two percent of the prize pool is placed in a MUSL prize reserve fund and a MUSL set prize reserve fund. These reserve funds serve as contingency funds to protect MUSL from unforeseen liabilities. As of September 30, 2000 and 1999, the total MUSL prize reserve fund is approximately \$52,000, of which the Lottery's share is approximately \$1,887 and \$1,900 respectively. In addition, the total MUSL set prize reserve fund as of September 30, 2000 and 1999, is approximately \$25,000, of which the Lottery's share is approximately \$839 and \$480 respectively. In 1998, MUSL also established a prize reserve fund for the Cash for Life Jackpot introduced in March 1998. As of September 30, 2000 and 1999 the Cash For Life reserve fund is \$6,629 and \$6,190 respectively, of which the Lottery's share is \$450 and \$431 respectively.

The balance remaining in the reserve funds are refundable to MUSL members if a member leaves or if MUSL disbands. If a member leaves, the member must wait one year before their portion of the prize reserve funds is returned. The balance in the reserve funds may be used at the discretion of MUSL's Board of Directors. Accordingly, the Lottery's share of the reserve funds is not reflected in the accompanying financial statements.

**Government of the District of Columbia
 Lottery and Charitable Games Control Board
 Notes to Financial Statements
 September 30, 2000 and 1999
 (dollars presented in thousands)**

Note 6 - Gaming Revenues and Expenses

Gaming revenues and expenses for the fiscal years ended September 30, 2000 and 1999, are as follows:

Fiscal Year Ended September 30, 2000

	<u>Lucky Number</u>	<u>DC Four</u>	<u>Powerball</u>	<u>Quick Cash</u>	<u>Daily Millions</u>	<u>Cash for Life</u>	<u>Hot Five</u>	<u>Instant Games</u>	<u>Total</u>
Ticket revenue	\$74,180	\$66,428	\$31,612	\$4,344	\$ -	\$ 979	\$5,809	\$32,586	\$215,938
Prizes	(36,837)	(34,972)	(14,484)	(1,492)	-	(315)	(3,176)	(21,537)	(112,813)
Agent commissions	<u>(4,117)</u>	<u>(3,413)</u>	<u>(1,480)</u>	<u>(205)</u>	-	<u>(38)</u>	<u>(322)</u>	<u>(2,146)</u>	<u>(11,721)</u>
Gross margin	<u>\$33,226</u>	<u>\$28,043</u>	<u>\$15,648</u>	<u>\$2,647</u>	<u>\$ -</u>	<u>\$ 626</u>	<u>\$2,311</u>	<u>\$ 8,903</u>	<u>\$ 91,404</u>

Fiscal Year Ended September 30, 1999

	<u>Lucky Number</u>	<u>DC Four</u>	<u>Powerball</u>	<u>Quick Cash</u>	<u>Daily Millions</u>	<u>Cash for Life</u>	<u>Hot Five</u>	<u>Instant Games</u>	<u>Total</u>
Ticket revenue	\$73,197	\$60,210	\$34,104	\$5,129	\$ -	\$1,619	\$3,326	\$29,506	\$207,091
Prizes	(36,532)	(34,440)	(14,159)	(2,604)	(83)	(735)	(1,899)	(20,234)	(110,520)
Agent commissions	<u>(4,024)</u>	<u>(3,142)</u>	<u>(1,466)</u>	<u>(265)</u>	<u>(2)</u>	<u>(75)</u>	<u>(184)</u>	<u>(1,954)</u>	<u>(11,108)</u>
Gross margin	<u>\$32,641</u>	<u>\$22,628</u>	<u>\$18,479</u>	<u>\$2,260</u>	<u>(\$85)</u>	<u>\$ 809</u>	<u>\$1,243</u>	<u>\$ 7,318</u>	<u>\$ 85,463</u>

Note 7 - Operating Transfers to the General Fund of the District

The District Budget Act (PL 4-162) (the Act) of 1983 requires the Lottery to transfer its revenues less expenses and less a reserve not to exceed 2 percent of projected annual prize payments, to the General Fund of the District. The Mayor may approve a change in the reserve limit, as necessary, upon the request of the Lottery. During the fiscal years ended September 30, 2000 and 1999, the Lottery's net transfers to the General Fund of the District were \$69,450 and \$64,225 respectively. The Lottery was in compliance with the Act for the fiscal years ended September 30, 2000 and 1999.

**Government of the District of Columbia
Lottery and Charitable Games Control Board
Notes to Financial Statements
September 30, 2000 and 1999
(dollars presented in thousands)**

Note 8 - Retirement Programs

Defined Benefit Pension Plan

The majority of the full-time Lottery employees hired before October 1, 1987 are covered by the Federal Civil Service Retirement System (5 U.S.C. 833 1). The Federal Civil Service Retirement System is a cost-sharing multiple employer pension plan. The U.S. Civil Service Commission is responsible for administering the Federal Civil Service Retirement System, including collecting the contributions and disbursing the benefits.

In accordance with the Balanced Budget Act of 1997 (Public Law 105-33), the Lottery contributes 8.51% and employees contribute 7.25% of employees' covered compensation to the Federal Civil Service Retirement System. The Lottery's contribution will decrease to 7.50% in October 2002 and to 7.00% in January 2003. Contributions by the Lottery amounted to \$138 and \$113 for the years ended September 30, 2000 and 1999, respectively. For the years ended September 30, 2000 and 1999, the number of Lottery employees covered under the Federal Civil Service Retirement System is 43 and 45, respectively.

Defined Contribution Plan

All full-time employees hired after September 30, 1987 are covered by the District-sponsored defined contribution plan. Employees do not contribute to this plan and are eligible to participate after one year of service. The Lottery contributes 5% of an eligible employee's base salary, which amounted to \$117 and \$106 for the fiscal years ended September 30, 2000 and 1999, respectively. Contributions and earnings vest fully after 4 years of service following a one-year waiting period. Contributions and earnings are forfeited if separation occurs before five years of credited service. These contributions are not considered assets of the Lottery or the District, which have no further liability to this plan.

Deferred Compensation Plan

Lottery employees are eligible to participate in the District-sponsored deferred compensation plan (D.C. Code 47-3601) created in accordance with Internal Revenue Code Section 457. Employees may defer up to 25% of their compensation, not to exceed \$8. Compensation deferred and income earned are taxable when paid or made available to the participant or beneficiary upon retirement, death, termination, or unforeseeable emergency. Contributions are not assets of the Lottery or District, which have no further liability to the plan.

**Government of the District of Columbia
Lottery and Charitable Games Control Board
Notes to Financial Statements
September 30, 2000 and 1999
(dollars presented in thousands)**

Note 9 – Commitments and Contingencies

Risk of Loss

The Lottery is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Lottery or District covers all of the Lottery's claim settlements and judgments out of the Lottery revenues or the District's General Fund resources.

Annuity Contracts

Prizes awarded for the Lucky Lotto game, which ended effective May 1, 1989, are payable to the winners in annual installments over 10 or 20 years. The first installment payments were made by the Lottery at the time of the drawing. The Lottery has entered into agreements with insurance companies under which the Lottery purchased annuities contracts that provide the annual installment payments to the Lucky Lotto prize winners. As the insurance companies are responsible for the annual installment payments, neither the present value of the annuities nor the present value of the related future payments is reflected in the accompanying financial statements. The Lottery would be liable for such future installment payments if the insurance companies were to default on their payments. As of September 30, 2000 and 1999, future installment payments due to Lucky Lotto winners were approximately \$11,343 and \$13,363 respectively.

During 1991, Executive Life Insurance Company (ELIC), with whom the Lottery holds two annuities, was placed into conservancy with the Los Angeles, California Superior Court (Superior Court). In 1993, the Superior Court approved the terms of a rehabilitation plan and purchase of ELIC by the Aurora National Life Insurance Company. As a result, the Lottery is required to fund a percentage of the annual installment payments for these annuities. The Lottery's accrued prize liability as of September 30, 2000 and 1999 includes \$374 and \$512 respectively, for the Lottery's percentage of the annual installment payments to these Lucky Lotto winners.

**Government of the District of Columbia
 Lottery and Charitable Games Control Board
 Notes to Financial Statements
 September 30, 2000 and 1999
 (dollars presented in thousands)**

Operating Leases

The Lottery leases certain facilities under long-term, non-cancelable, and operating leases. The total future minimum rental commitments for the fiscal years ending September 30, 2001 and beyond are as follows:

<u>Fiscal Year</u>	<u>Amount</u>
2001	\$1,193
2002	1,225
2003	1,240
2004	1,240
2005	1,240
Thereafter	<u>1,654</u>
Total	<u>\$7,792</u>

Rent expense for the fiscal years ended September 30, 2000 and 1999 is as follows:

	<u>2000</u>	<u>1999</u>
Gross rental expense	\$1,315	\$1,272
Less income from subleases	<u>(170)</u>	<u>(170)</u>
Net rent expense	<u>\$1,145</u>	<u>\$1,102</u>



2001 M Street, N.W.
Washington, D.C. 20036

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

To the Mayor and Members of
The Council of the Government of the District of Columbia, and
The Lottery and Charitable Games Control Board
Washington, D.C.

We have audited the financial statements of the Lottery and Charitable Games Control Board (Lottery), an enterprise fund of the Government of the District of Columbia (District), as of and for the year ended September 30, 2000, and have issued our report thereon dated January 26, 2001. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether Lottery's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, 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 that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Lottery's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on internal control over financial reporting. However, we noted a matter involving internal control that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control over financial reporting that, in our judgment, could adversely affect the Lottery's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable condition is described as follows:



Access Controls over Information Systems

Least privilege and *segregation of duties* are key components of access controls on information systems. The control measures for each of these two areas must be implemented in a manner that minimizes operational burdens and disruptions to the work flow without compromising control objectives.

Least privilege refers to measures that ensure that data access reflects the minimum access privileges required for each internal system user (employee) and each external system user (customer, general public, etc.). The required access privileges for external systems users are dictated by the business model the system is supporting while the access privileges for internal system users are dictated by their position descriptions and specific job responsibilities.

We observed that, for specific areas, least privilege controls are not in place, allowing the possibility of excessive access to information system resources by Lottery Technology Enterprise employees.

Without effective policies and procedures governing data access, individuals can intentionally or inadvertently be granted excessive access to information system resources. Lottery management should take steps to ensure the establishment, documentation, and implementation of comprehensive data security policies and procedures addressing least privilege access controls.

Segregation of duties refers to measures that ensure proper segregation of specific job responsibilities in order to maintain data integrity and availability. Proper segregation of duties, for instance, will not allow a computer programmer position to also have the responsibilities of a production control position, which includes independent assessment of the quality of the programmer's work prior to incorporating it into the systems application software in the production environment.

We observed lack of proper segregation of duties in several key positions including the computer specialist and database administrator. Lottery management should modify the position descriptions and specific job responsibilities for the above positions to ensure that data integrity and availability cannot be comprised.

A material weakness is a condition in which the design or operation of one or more internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of internal control over financial reporting would not necessarily disclose all matters in internal control over financial reporting that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable condition described above is not a material weakness. We also noted a matter involving internal control over financial reporting, which we have reported to management of the Lottery in a separate letter dated January 26, 2001.

This report is intended solely for the information and use of the Mayor, Council, and Inspector General of the Government of the District of Columbia, the Financial and Management Assistance Authority, management of the Lottery, the U.S. General Accounting Office, and the U.S. Congress and is not intended to be, and should not be used by anyone other than these specified parties.

KPMG LLP

January 26, 2001