

Oregon State Lottery

An Enterprise Fund of the State of Oregon

Annual Financial Report

For the Fiscal Year Ended June 30, 2021



**OREGON
LOTTERY®**

Together, we do good things.

Barry Pack
Director

Kathy Ortega, CPA, CGMA
Chief Financial Officer

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ANNUAL FINANCIAL REPORT
For the Fiscal Year Ended June 30, 2021

TABLE OF CONTENTS

	Page
Introductory Section	
Letter of Transmittal.....	2
Organization Chart with Principal Officials.....	6
Financial Section	
Independent Auditor's Report.....	8
Management's Discussion and Analysis	11
Basic Financial Statements:	
Statement of Net Position.....	18
Statement of Revenues, Expenses and Changes in Fund Net Position.....	19
Statement of Cash Flows.....	20
Notes to the Financial Statements.....	21
Supplementary Information:	
Budgetary Comparison Schedule.....	42
Other Reports	
Report on Internal Control Over Financial Reporting and Compliance.....	44

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Introductory Section



December 29, 2021

To the Honorable Governor Kate Brown and Citizens of the State of Oregon:

We are pleased to provide you with the Annual Financial Report of the Oregon State Lottery (Lottery) for fiscal year ended June 30, 2021. This report is published to meet the requirement in state law for an annual accounting of financial activities.

Lottery management assumes full responsibility for the completeness and reliability of the information contained in this report, based upon a comprehensive framework of internal controls established for this purpose. Because the cost of internal controls should not exceed anticipated benefits, the objective is to provide reasonable rather than absolute assurance that the financial statements are free of any material misstatements.

The Secretary of State Audits Division, the constitutional auditor of public accounts in Oregon, audited the Lottery's financial statements for the fiscal year ended June 30, 2021. The auditors used generally accepted auditing standards in conducting the engagement. Their unmodified opinion on the financial statements is the first component in the Financial Section of this report.

A narrative analysis of the Lottery's financial performance for the fiscal year can be found in the Management's Discussion and Analysis (MD&A) immediately following the independent auditor's report. This letter of transmittal complements the MD&A and should be read in conjunction with it.

Profile of Oregon State Lottery

The Oregon State Lottery was created through the initiative process in November 1984. Voters approved an amendment to the Oregon Constitution that required the establishment and operation of a State Lottery. Initially, Lottery profits were earmarked to create jobs and further economic development. In May 1995, voters approved a Constitutional amendment allowing Lottery profits to be used for the financing of public education. Similarly, voters added state parks and salmon habitat restoration projects to the list of allowable uses of Lottery proceeds in November 1998. Oregonians have voted to use Lottery profits for programs that make Oregon a great place to live and support veterans and outdoor schools.

The Lottery was established as a state agency to market and sell Lottery products to the public. As directed in statute, it operates to produce an optimal amount of net revenues for the people of Oregon commensurate with the public good. Development of new products and game enhancements is a continual process in the effort to sustain long-term revenues, while taking into consideration the potential impact of game decisions on problem gambling. The Lottery's commitment is to provide information and tools that help our customers make informed choices and enjoy Lottery games in a responsible way. Further, the Lottery is committed to ensuring that players and their families know how to access treatment for problem gambling, and that they understand treatment is free, confidential and effective.

Lottery has a network of 3,896 retailers through which it offers players a broad mix of Traditional Games as well as Video LotterySM. Traditional Lottery games include: Scratch-itsSM Instant Tickets, Keno, Powerball[®], Oregon's Game MegabucksSM, RaffleSM, Win for LifeSM, Mega Millions[®], Lucky LinesSM, and Pick 4SM. Video LotterySM is a product sold on stand-alone Video LotterySM terminals located in establishments licensed by Oregon Liquor Control Commission (OLCC). The Lottery has approximately 10,828 Video LotterySM terminals deployed throughout the state. In October 2019, Lottery launched an on-line sports betting game, ScoreboardSM. ScoreboardSM is currently sold only through Lottery's mobile application.

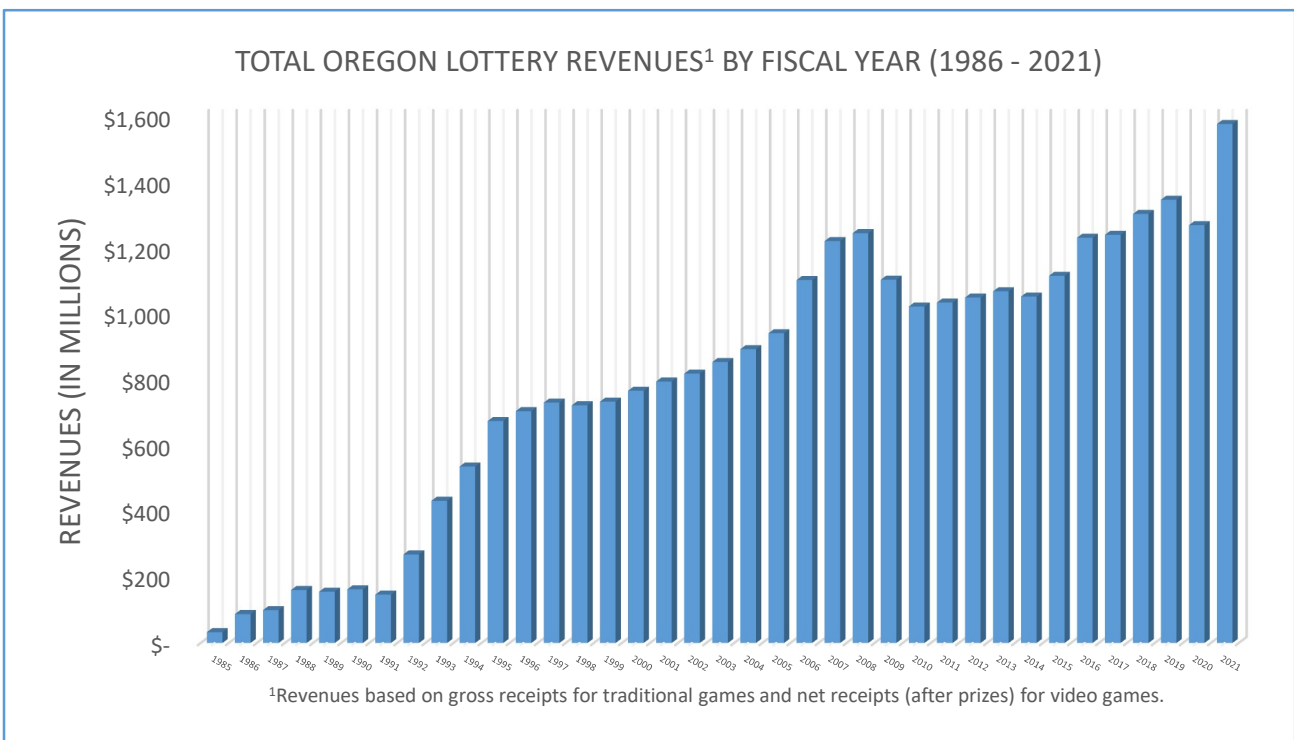
The Lottery, which is accounted for as a single enterprise fund, is entirely self-financed through its sales. Its operations are designed to fulfill its duty to develop, produce, and market Lottery games; pay winners and operating expenses; and

remit the remaining net profits to the State. These net profits are transferred to the Oregon Economic Development Fund and are then distributed by the State to finance the various uses allowed by law. Through its business units, the Lottery provides services that are necessary to operate successfully including security, marketing, retailer support, finance, management and information services. Additional information about the Lottery is available on its website at: <http://www.oregonlottery.org>.

The Lottery is operated under the direction of a five-member commission, with the commissioners appointed by the Governor and confirmed by the Senate. The Commission directs the activities of the Lottery, including the adoption of rules for the security and integrity of operations. The Governor also appoints a Director, who serves as the chief administrator of the Lottery. This position is also subject to Senate confirmation. The Director is responsible for operating the Lottery in accordance with state law and administrative rules and under the guidance of the Commission.

For budgeting purposes, the Commission adopts an annual Financial Plan based on activities identified in Lottery’s Strategic Business Plan. The Financial Plan uses revenue forecasts prepared by the Oregon Department of Administrative Services, Office of Economic Analysis. Budgeted revenues and direct expenses (prizes, commissions, game vendor charges, and tickets) are revised quarterly for changes in revenue forecasts. Revisions to other expense items in the adopted budget must be approved by the Commission. The budget is prepared on the accrual basis of accounting. Actual expenses are monitored throughout the year for compliance with the approved budget and appropriate adjustments are presented to the Commission for approval if necessary. By law, expenses to operate the Lottery are limited to no more than 16 percent of total annual revenues and fiscal year 2021 expenses were 3.31 percent.

Since the Lottery’s first full year of operation in 1986 through fiscal year 2008, Lottery revenues demonstrated strong and consistent growth. Lottery revenues declined in fiscal years 2009 and 2010 due to the impacts of Oregon’s economic recession and the implementation of a statewide smoking ban in bars and taverns where Lottery products are sold. Revenues stabilized in fiscal year 2011 and have shown steady but modest growth, except for fiscal year 2014 which showed a slight decline. However, revenue growth returned and continued to increase through fiscal year 2021. Beginning the fourth quarter of 2020 and fiscal year 2021, the COVID-19 pandemic caused two mandated retailer closures, which in turn lead to short periods of significantly decreased Video LotterySM revenue. Upon reopening retailers’ sales have rebounded to above pre-pandemic levels and forecasts are favorable as to the Lottery’s continued revenue growth.



Economic Condition and Outlook

According to the Oregon Office of Economic Analysis (OEA) December 2021 Economic and Revenue Forecast, despite the challenges of the COVID-19 pandemic, Oregon's economic and labor outlook remains robust. While employment is 4 percent below pre-pandemic levels, total wages and salaries have shown an increase of 8 percent. This wage trend is due in part to federal fiscal policy in response to the pandemic, and the need of labor to meet supply chain demands. Currently, supply chain constraints pose the greatest fundamental economic challenge. OEA forecasts show a return to full employment within the next year with federal aid ending the first quarter of fiscal year 2022 and continued labor demand.

In Oregon, as a result of fiscal policy and wage trends, overall personal income grew in 2020 despite the severe recession. Oregon's personal income is projected to increase 6.7 percent in 2021, .60 percent in 2022, and 5.6 percent in 2023. National averages for 2021 to 2023 are 6.4, .60 and 5.1 percent. Oregon wage and salary income for 2021 to 2023 are projected to increase 1.3, 1.5 and 1.6 percent.

Oregon faces several economic factors in the near-term; continued impacts of the U.S. economy resulting from the COVID-19 pandemic and federal fiscal policy, inflationary risks, increased supply chain constraints, the strength and affordability of the housing market, global economic instability, effects of the climate and natural disasters, and Oregon initiatives, referendums and referrals.

As an agency operating in the entertainment industry, we also encounter increased competition from other gambling offerings available to the citizens of Oregon.

Long-term Financial Planning

The Lottery uses a Strategic Plan in conjunction with an annual Strategic Business Plan and budget to manage operations. Lottery's main strategic objective is to responsibly offer games that appeal to both current and new players on the gaming platforms they want to use. The Lottery is assessing its ongoing operational program strategy for Video LotterySM considering the recent impacts from the global pandemic. New, cost-effective game and terminal replacement strategies to ensure maximum revenue are an on-going strategy. The Lottery will continue with major projects to further its business strategies. This includes the alignment of budgeting and strategic investment to the strategic growth plan.

In the December 2021 Economic and Revenue Forecast, the OEA is reflecting Lottery transfers of \$1.72 billion for the 2021-2023 biennium. A consideration in the current forecast is the concern of a new gaming facility in Grants Pass and potential for other such gaming facilities in the state. Should the potential for additional gaming facilities arise, they will be evaluated for any impact to revenues and transfers.

Relevant Financial Policies

In order to provide resources for current operations and future investment, the Lottery Commission established a contingency reserve fund. In May of 2014, the Commission authorized an increase to the cash portion of the reserve with a cap of \$100 million. At June 30, 2021 the actual cash balance in the reserve was \$87 million. The Lottery intends to use the contingency reserve to fund future business initiatives that are key to its ability to compete, remain relevant to our players, and maximize transfers to our beneficiaries and as a reserve in the event of revenue declines from COVID-19 or other economic factors. Further details on this can be found in the MD&A section of this report.

Major Initiatives

The Lottery is currently implementing upgrades to back-office support systems that are facing obsolescence and end-of-life support. The modernization roadmap under development includes enterprise architecture options and a digital transformation, staging plans for the implementation of solutions, and system integration. The timeline for the roadmap is three to five years. The assessment of Lottery's business processes and capabilities and analysis of the enterprise architecture has aided in the development of the foundational activities that will drive adoption and ensure the long-term success of the modernization program.

The key business modernization drivers are based on responsibly increasing revenues and leveraging a holistic understanding of retailer and customer behavior, preferences, and motivators. The goal is to optimize investments in marketing, product innovations and internal capability enhancements, leveraging product costs and personnel. The

Lottery has developed a strategic business plan, and work has begun to transform the agency into a data-driven, learning organization, ensuring people have the right data to make informed decisions.

During fiscal year 2021, the Lottery completed the replacement of Lottery's traditional central system with IGT's Aurora software. The most significant project in-process as of June 30, 2021 is the replacement of Lottery's back-office ERP system Microsoft Dynamics AX 2009 with current cloud-based ERP software Microsoft Dynamics D365, which will continue throughout fiscal year 2022. The Lottery is also in the midst of a transition to a more modern technology platform for its sports book which will provide for improved customer experience and revenue potential.

The Lottery has defined a customer-centric brand promise strategy and developed an integrated communications plan. The Lottery has implemented a retail channel strategy to generate sustainable long-term growth that will expand the market by reaching players through relevant channels. During fiscal year 2021, Lottery continued to develop our Brand Promise initiative to attract new players and retailers, and appeal to a broad and diverse player and retailer base. We achieve this by investing in both retail operations and participating in local communities to improve funding for programs Oregonians care about.

Lottery has launched several initiatives to reach out to current and new players through a customer-first approach. A positive digital customer experience is instrumental to the Lottery modernization and growth success. The Lottery's existing and new games, platforms, and venues are being enhanced to attract more diverse demographic groups to maintain and enhance revenue performance.

The Oregon Lottery mobile application has fundamentally improved and enhanced mobile experience and utility for customers. Using a phased approach and data-driven research, additional features are on a roadmap for development, testing, and release through application updates.

The Lottery continues its commitment to enhancing and expanding its Responsible Gambling Program, as part of its overall commitment to Corporate Social Responsibility (CSR), which is an integral component of Lottery's Brand Promise. This includes sharing an Oregon Lottery Responsible Gambling Code of Practice with the public that details our values, commitments, and areas of focus regarding the promotion of responsible gambling and enabling free access to problem gambling treatment. The Lottery has created a program to produce an overall positive impact for Oregon by balancing our business priorities with our social, economic, and environmental responsibilities. The overall CSR goals include keeping lottery entertainment entertaining, promoting help and hope for those struggling with gambling addiction, championing diversity, equity and inclusion and supporting sustainability

Acknowledgements

The preparation of this report reflects the combined efforts of the Lottery's Finance and Accounting staff. We would like to express our gratitude to all Lottery staff for working cooperatively to ensure the integrity of Lottery's financial reporting. In addition, we appreciate the direction and support provided by the Lottery Commission.

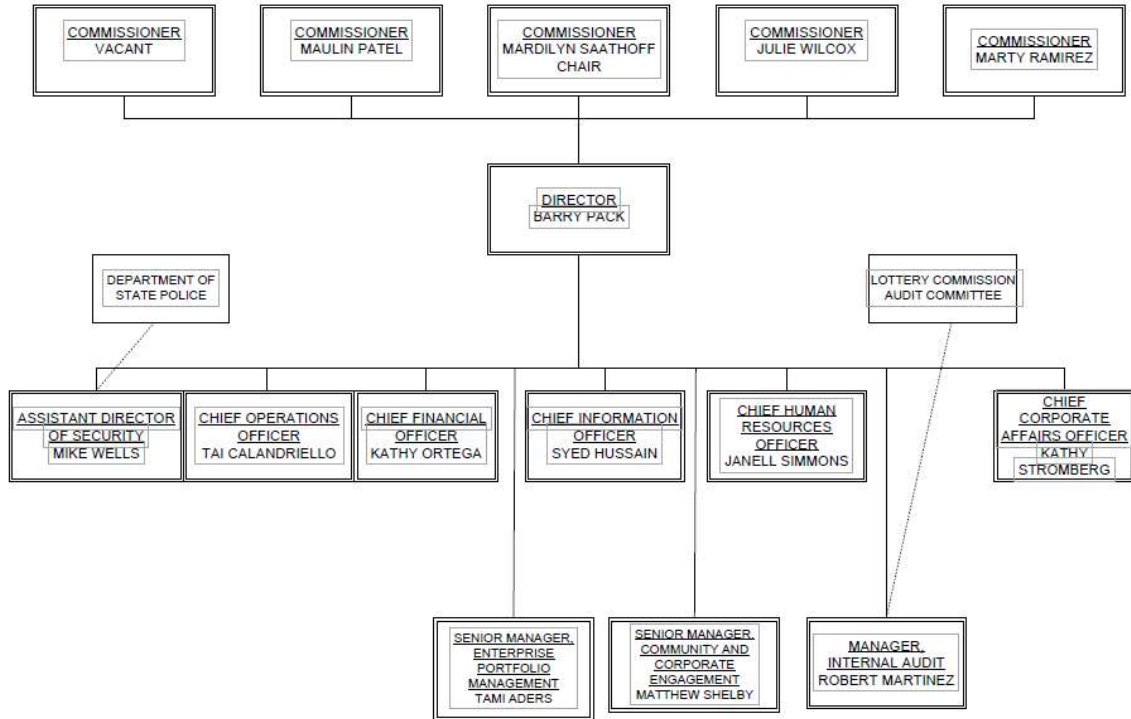
Respectfully submitted,



Kathy Ortega, Chief Financial Officer
Oregon State Lottery



OREGON STATE LOTTERY COMMISSION





Financial Section

Independent Auditor's Report

The Honorable Kate Brown, Governor of Oregon
MardiLyn Saathoff, Chair, Oregon State Lottery Commission
Barry Pack, Director, Oregon State Lottery

Report on the Financial Statements

We have audited the accompanying financial statements of the Oregon State Lottery, an enterprise fund of the State of Oregon, as of and for the year ended June 30, 2021, and the related notes to the financial statements, which collectively comprise the Oregon 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.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. 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 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 auditor's 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 entity'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 respective financial position of the Oregon State Lottery, an enterprise fund of the State of Oregon, as of June 30, 2021, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the financial position, the changes in financial position and, where applicable, cash flows that are attributable to the transactions of the Oregon State Lottery. They do not purport to, and do not, present fairly the financial position of the State of Oregon as of June 30, 2021, the changes in its financial position, or, where applicable, its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis 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 Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Oregon State Lottery's basic financial statements. The budgetary comparison schedule is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The budgetary comparison schedule 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. Such information 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, the budgetary comparison schedule is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

The introductory section 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 Governmental Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated December 29, 2021, on our consideration of Oregon State Lottery's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Oregon State Lottery's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Governmental Auditing Standards* in considering the Oregon State Lottery's internal control over financial reporting and compliance.

Office of the Secretary of State, Audits Division

State of Oregon
December 29, 2021

Oregon State Lottery

Management's Discussion and Analysis

This section of the Oregon State Lottery's (Lottery) Annual Financial Report presents our discussion and analysis of the Lottery's financial performance for the fiscal year ended June 30, 2021. This analysis is to be considered in conjunction with information in the transmittal letter of this report.

Financial Highlights

- Revenue for all Lottery products is \$1.3 billion, an increase of 13.4 percent over fiscal year 2020.
- Traditional (Scratch and Draw) game revenue increased 21.3 percent from the prior fiscal year and Video LotterySM revenue increased 7.9 percent.
- ScoreboardSM, had its first full fiscal year of operation bringing in \$29.1 million in sales.
- Pension expense allocated to the Lottery increased 172.9 percent, to \$26.7 million.
- Net position (equity) decreased by \$20.3 million.
- The Lottery transferred \$652.5 million to Oregon's Economic Development Fund, which is \$69 million more than the prior year.

Overview of the Financial Statements

In addition to this discussion and analysis, the Financial Section of this annual report contains the basic financial statements, which include the fund financial statements and accompanying notes and an optional budgetary comparison schedule.

The basic financial statements offer short-term and long-term financial information about the Oregon State Lottery, which is structured as a single enterprise fund. The budgetary comparison schedule presents budgeted and actual revenues and expenses for the fiscal year.

The Statement of Net Position provides information about the nature and amounts of resources with present service capacity that the Lottery controls (assets), resources that will be consumed in a future fiscal year (deferred outflows of resources), obligations at the end of the fiscal year to use resources that the Lottery has little or no discretion to avoid (liabilities), and acquisitions of resources that are applicable to a future fiscal year (deferred inflows of resources). The residual (net) of these four elements is reported as net position.

All the current year's revenues and expenses are accounted for in the Statement of Revenues, Expenses, and Changes in Fund Net Position. This statement measures the results of the Lottery's operations over the past year.

The primary purpose of the Statement of Cash Flows is to provide information about the Lottery's cash receipts and cash payments during the reporting period. This statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities.

The financial statements are prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. Thus, expenses are recorded when liabilities are incurred, and revenues are recognized when earned, not when received.

Analysis of Financial Position and Operations

Lottery's net position for the current and prior fiscal year is summarized in Table 1:

Table 1: Oregon State Lottery's Net Position			
	2021	2020	Change
Current assets	\$458,415,289	\$296,677,303	\$161,737,986
Capital assets	71,921,273	48,657,211	23,264,062
Other noncurrent assets	211,475,848	280,771,569	(69,295,721)
Total assets	741,812,410	626,106,083	115,706,327
Deferred Outflows of Resources	23,554,933	16,558,458	6,996,475
Total assets and deferred outflows of resources	765,367,343	642,664,541	122,702,802
Current liabilities	324,215,757	205,264,253	118,951,504
Noncurrent liabilities	192,182,164	167,768,604	24,413,560
Total Liabilities	516,397,921	373,032,857	143,365,064
Deferred Inflows of Resources	2,021,813	2,406,165	(384,352)
Total liabilities and deferred inflows of resources	518,419,734	375,439,022	142,980,712
Net position:			
Net investment in capital assets	63,784,030	38,040,215	25,743,815
Restricted for OPEB Asset- RHIA	680,959	592,770	88,189
Unrestricted	182,482,620	228,592,534	(46,109,914)
Total net position	\$246,947,609	\$267,225,519	(20,277,910)

Overall, assets increased \$115.7 million. Current cash and cash equivalents increased from fiscal year 2020 levels by \$230.2 million. Year-end current cash amounts are reflecting an increase of \$155.4 million in funds ready to be transferred to the Economic Development Fund in July; the collection of receivable amounts and \$58.4 million of cash which is no longer restricted for future projects and contracts. Accounts receivable balances are \$14.4 million less than the prior year as retailer COVID-19 payment extensions are no longer in effect. The reduction of restricted cash amounts and a \$10.9 million reduction in the long-term investments balance are the source of reduction in noncurrent assets. Long term investment balances declined as \$10.6 million became short-term as they neared maturity.

Capital assets, net of depreciation increased \$23.3 million with the purchase of Video LotterySM gaming terminals and new equipment needed for gathering and reporting traditional product transactions at retail establishments. These purchases totaled \$44.4 million. However, the increase was offset by \$22.6 million in depreciation for fiscal year 2021. Additional information on Lottery's capital assets can be found in Note 6 of the financial statements-

Liabilities increased \$143.4 million with \$119 million of the change in current liabilities. Amounts due to the Economic Development Fund increased 218.5 percent (\$155.4 million) over the prior year. Transfers to the Economic Development Fund are remitted quarterly leaving only the April to June amounts due at the end of the fiscal year. Last year at June 30, 2020 mandated bar and restaurant closures due to the COVID-19 pandemic were in effect causing significant declines in Video LotterySM transfers due. The liability at June 30, 2021 has returned to amounts due for sales at more normal levels. Current prize liabilities increased \$14.8 million. This was caused by COVID-19 facility restrictions making player payments more challenging and time consuming, as well as sales levels returning to normal levels by the end of the fiscal year. The Wilsonville payment center remained closed at June 30, 2021. The net pension liability increased \$28.6 million due to increases at the plan level, increases in the state's allocation and the subsequent pass through to Lottery. Obligations under securities lending declined \$51.8 million reflecting reduced lending at June 30, 2021 compared to the prior year.

A portion of the Lottery's net position, 25.8 percent, reflects investment in capital assets, primarily Video LotterySM gaming terminals. Investment in capital assets increased from the prior year by \$25.7 million as a result of traditional

transaction equipment and video gaming terminals. Of the \$182.5 million in unrestricted net position at fiscal year-end, \$92.1 million is committed for capital purchases, projects, and long-term contract obligations.

Table 2 below reflects a summary of changes in net position for the current and prior fiscal year:

Table 2: Oregon State Lottery's Changes in Net Position			
	2021	2020	Increase/ (Decrease)
Operating revenue:			
Video Lottery SM game sales, net	\$ 860,326,742	\$ 797,498,371	\$ 62,828,371
Scoreboard SM sales, net	29,147,647	8,620,945	20,526,702
Scratch-its SM instant ticket sales	196,029,843	149,831,274	46,198,569
Draw game sales	212,942,872	187,307,053	25,635,819
Other Income	380,966	2,053,562	(1,672,596)
Total operating revenues	1,298,828,070	1,145,311,205	153,516,865
Operating expenses:			
Prizes	266,065,927	223,500,660	42,565,267
Retailer commissions	239,197,863	217,920,495	21,277,368
Other operating expenses	156,492,256	152,701,534	3,790,722
Total operating expenses	661,756,046	594,122,689	67,633,357
Operating income	637,072,024	551,188,516	85,883,508
Interest and investment income	(2,561,203)	24,122,455	(26,683,658)
Insurance recoveries	9,932	4,053	5,879
Nonoperating expenses	(359,041)	(1,093,255)	(734,214)
Total nonoperating revenues (expenses)	(2,910,312)	23,033,253	(25,943,565)
Income before transfers	634,161,712	574,221,769	59,939,943
Transfers	(654,439,622)	(585,736,371)	68,703,251
Change in net position:	(20,277,910)	(11,514,602)	8,763,308
Net position - beginning	267,225,519	278,740,121	(11,514,602)
Net position - ending	\$ 246,947,609	\$ 267,225,519	\$ (20,277,910)

Product sales increased \$155.2 million (13.6 percent) over the prior year. Of the increase, 40.5 percent was from increases in video revenue. Fiscal year 2021 did not have pandemic mandated establishment closures for as many days as fiscal year 2020. Other income decreased \$1.7 million because fiscal year 2020 had a \$1.7 million unexpected gain from defeasance of a Win For LifeSM prize liability.

Total operating expenses increased 11.4 percent from the prior fiscal year. Prizes and retailer commissions, which are expenses directly related to sales, increased as product sales increased. One of the larger and more significant expense increases for fiscal year 2021 came not from Lottery operations, but the annual share of state PERS expense passed down from the statewide accounting office. The expense from fiscal year 2019 was \$11 million, for fiscal year 2020 it was \$9.8 million and for fiscal year 2021 is \$26.7 million. The amount for fiscal year 2021 represents an increase of 172.9% over the prior year. The intent of the entry is for all participating State agencies to share in the total expense allocated actuarially to the State of Oregon as one employer of the pension plan. The overall plan expense increase was 12.5%. Expense allocated to the State of Oregon employer increased 12.6 percent. The reason for the significant increase for Lottery is the allocation methodology used by the statewide accounting office, as there were only minor changes in staffing and salaries during fiscal year 2020 (the measurement year). The impact of the entry was a reduction to retained earnings, and as such available working capital. Lottery will monitor the impact of this entry on working capital available for operations in the future.

Expense reductions were seen in nearly all areas not directly related to sales. Advertising, including public information, as well as other services and supplies was reduced by \$8 million from the prior year. The reduction was intentional due to the unknown pandemic environment. Game equipment, parts and maintenance expenses declined \$3.5 million as

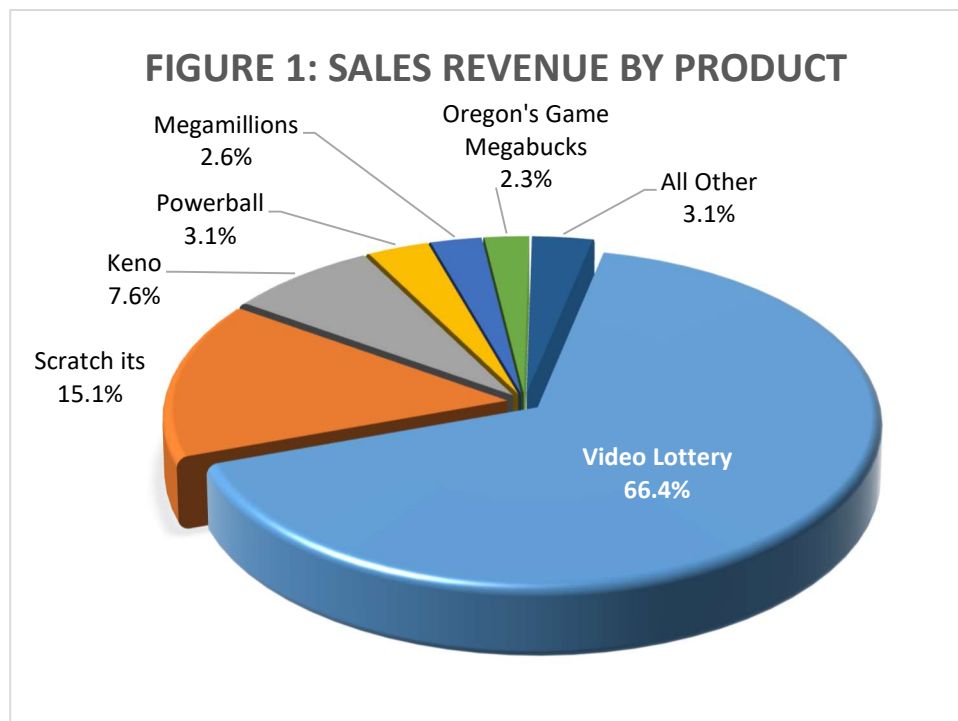
newer video terminals were replacing older models. Depreciation expense was \$2.4 million less than the prior year as older video terminals reached the end of their life and the new terminals were not added until several months later.

Total nonoperating revenues/(expenses) decreased \$25.9 million. While fiscal year 2020 had investment fair value increases of \$14.9 million, fiscal year 2021 saw a decline in the fair value resulting in a loss of \$5.6 million. Lottery holds securities to maturity; thus, fair value fluctuations do not impact operational decisions or cash position. Interest income was \$6.2 million less in fiscal year 2021 which is the result of lower cash balances throughout the year. This was due to the timing of sales decreases/increases as well as acquisition purchases.

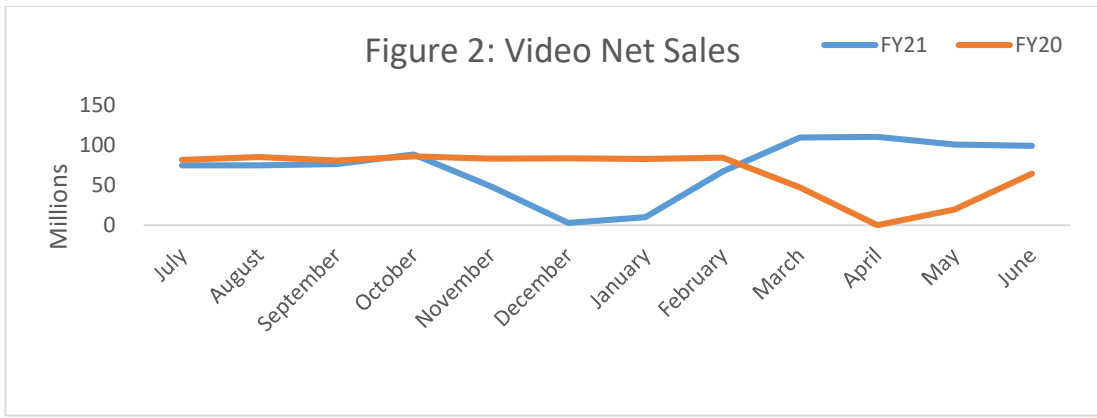
Overall, income before transfers increased 10.4 percent. This resulted in an increase of \$68.7 million in transfers to the Economic Development fund.

Sales Revenue

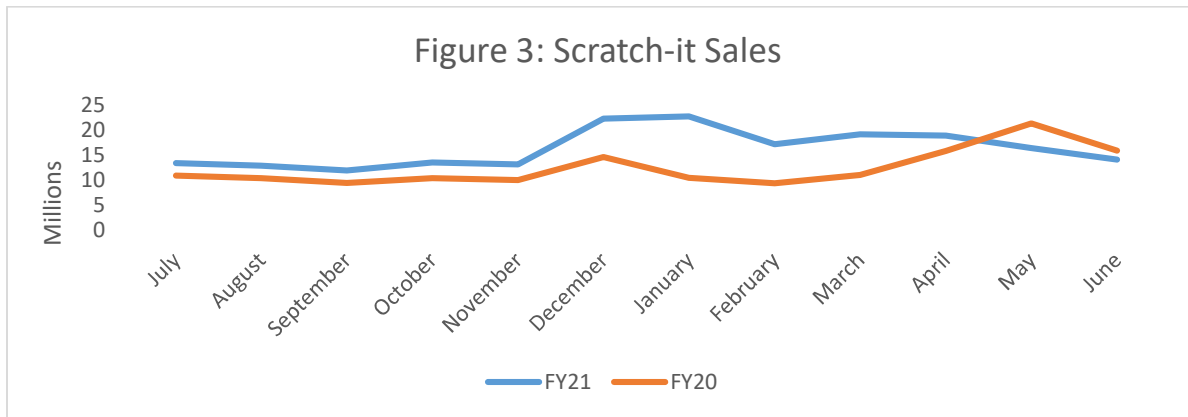
Figure 1 below shows the major sources and percentages of sales revenue for fiscal year 2021:



Video LotterySM remains the Lottery's largest source of revenue representing 66.4 percent of total sales. While fiscal year 2020 had approximately five months of pandemic sales volatility, fiscal year 2021 was affected the entire year. Despite this and another round of business closures in December 2020 and January 2021, video revenues surpassed the prior year by \$62.8 million or 7.9 percent. At fiscal year-end, monthly video revenues were surpassing pre-pandemic levels of fiscal year 2020. (See Figure 2) During the year the Lottery continued to actively promote problem gambling programs.



Sales of Scratch-itsSM, the second largest source of sales revenue at 15.1 percent, had 30.8 percent growth compared to fiscal year 2020. Sales for the period April through June 2020 increased considerably demonstrating a shift in player behavior as Video LotterySM experienced pandemic related establishment closures. Scratch sales for fiscal year 2021 continued to remain higher than the prior year even as video gaming returned to normal levels. This trend continued through most of the year with sales over the prior year in nearly every month. Figure 3 below displays the trend:



Draw game sales increased 13.7 percent from the prior year driven mostly by sales for Powerball[®] and Mega Millions[®]. These two games, both in the month of January, had very high jackpot levels. Powerball[®] reached \$730 million before it was won on January 20, and the Mega Millions[®] jackpot reached \$1 billion when it was won on January 22. Keno also contributed to the growth in draw game revenue with sales increasing 5.9 percent over the prior year.

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Basic Financial Statements

OREGON STATE LOTTERY
Statement of Net Position
June 30, 2021

Assets

Current Assets:

Cash and Cash Equivalents	\$ 402,699,034
Securities Lending Cash Collateral	20,785,766
Investments for Prize Payments	10,778,584
Accounts Receivable (Net)	20,752,906
Ticket Inventory	1,349,118
Prepaid Expenses	2,049,881
Total Current Assets	458,415,289

Noncurrent Assets:

Cash and Cash Equivalents	92,077,146
Investments for Prize Payments	111,602,798
Prize Reserves	7,114,945
Net Other Post Employment Benefits (OPEB) Asset	680,959

Capital Assets:

Buildings, Equipment and Vehicles	248,530,096
Computer Software	30,105,868
Other Assets	1,695,660
Less Accumulated Depreciation and Amortization	(208,410,351)

Total Noncurrent Assets	283,397,121
Total Assets	741,812,410

Deferred Outflows of Resources

Deferred Amounts for Pensions	23,022,200
Deferred Amounts for Other Post Employment Benefits (OPEB)	532,733
Total Deferred Outflows of Resources	23,554,933
Total Assets and Deferred Outflows of Resources	765,367,343

Liabilities

Current Liabilities:

Due to Economic Development Fund	226,478,617
Obligations Under Securities Lending	20,785,766
Prize Liability	51,395,326
Accounts Payable	18,077,049
Compensated Absences	3,285,756
Unearned Revenue	922,656
Contracts Payable	3,270,587
Total Current Liabilities	324,215,757

Noncurrent Liabilities:

Prize Liability	109,230,049
Compensated Absences	1,769,253
Net Pension Liability	72,097,398
Other Post Employment (OPEB) Liabilities	1,270,966
Contracts Payable	7,814,498
Total Noncurrent Liabilities	192,182,164
Total Liabilities	516,397,921

Deferred Inflows of Resources

Deferred Amounts for Pensions	1,637,995
Deferred Amounts for Other Post Employment Benefits (OPEB)	383,818
Total Deferred Inflows of Resources	2,021,813
Total Liabilities and Deferred Inflows of Resources	518,419,734

Net Position:

Net Investment in Capital Assets	63,784,030
Restricted for Net Other Post Employment (OPEB) Asset	680,959
Unrestricted	182,482,620
Total Net Position	\$ 246,947,609

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

OREGON STATE LOTTERY
Statement of Revenues, Expenses, and Changes in Fund Net Position
For the Year Ended June 30, 2021

Operating Revenues

Sales:		
Video Lottery SM (Net Receipts)	\$	860,326,742
Scoreboard SM (Net Receipts)		29,147,647
Scratch-its SM Instant Tickets (Net of Returns)		196,029,843
Keno		98,927,011
Powerball [®]		40,541,274
Megabucks SM		29,242,902
Mega Millions [®]		33,631,835
Raffle SM		2,499,850
Win For Life SM		3,820,432
Lucky Lines SM		2,282,856
Pick 4 SM		1,996,712
Provision For Uncollectibles		(39,809)
Other Income		420,775
Total Operating Revenues		<u>1,298,828,070</u>

Operating Expenses

Prizes	266,065,927
Retailer Commissions	239,197,863
Salaries and Wages	74,189,390
Depreciation and Amortization	22,561,417
Services and Supplies	25,490,902
Game Vendor Charges	19,233,957
Advertising and Market Research	5,458,147
Public Information	837,416
Tickets	3,497,439
Game Equipment Parts and Maintenance	4,849,767
Sales Support	373,821
Total Operating Expenses	<u>661,756,046</u>
Operating Income	<u>637,072,024</u>

Nonoperating Revenues (Expenses/Losses)

Interest	3,065,583
Investment and Securities Lending Income (Loss)	(5,626,786)
Insurance Recoveries	9,932
Gain (Loss) on Disposition of Assets	172,067
Investment Expenses - Securities Lending	(32,558)
Investment Expenses	(14,083)
Interest Expense	(484,467)
Total Nonoperating Revenues (Expenses/Losses)	<u>(2,910,312)</u>
Income Before Transfers	634,161,712
Transfers to the Economic Development Fund	(652,457,782)
Transfers to the General Obligation Bond Fund	(1,981,840)
Total Transfers	<u>(654,439,622)</u>
Change in Net Position	(20,277,910)
Net Position - Beginning	267,225,519
Net Position - Ending	<u>\$ 246,947,609</u>

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

OREGON STATE LOTTERY
Statement of Cash Flows
For the Year Ended June 30, 2021

Cash Flows from Operating Activities:	
Receipts from Customers	\$1,312,782,848
Payments to Employees for Services	(35,541,714)
Payments to Suppliers	(314,960,060)
Payments to Prize Winners	(246,305,215)
Other Cash Receipts/(Payments)	1,711,824
Net Cash Provided (Used) by Operating Activities	<u>717,687,683</u>
Cash Flows from Noncapital Financing Activities:	
Principal and Interest Payments on Long-term Pension Debt	(663,813)
Transfers to the Economic Development Fund	(502,907,148)
Transfers to the General Obligation Bond Fund	(1,981,840)
Net Cash Provided (Used) by Noncapital Financing Activities	<u>(505,552,801)</u>
Cash Flows from Capital and Related Financing Activities:	
Acquisition of Capital Assets	(45,482,972)
Proceeds from Disposition of Capital Assets	365,584
Payments on Contracts	(3,255,919)
Insurance Recoveries for Capital Assets	9,932
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>(48,363,375)</u>
Cash Flows from Investing Activities:	
Purchases of Investments	(5,597,707)
Proceeds from Sales and Maturities of Investments	10,644,000
Interest on Investments and Cash Balances	3,065,583
Securities Lending Expenses	(32,558)
Investment Expenses	(14,083)
Net Cash Provided (Used) by Investing Activities	<u>8,065,235</u>
Net Increase (Decrease) in Cash and Cash Equivalents	171,836,742
Cash and Cash Equivalents - Beginning	322,939,438
Cash and Cash Equivalents - Ending	<u>\$ 494,776,180</u>
Reconciliation of Operating Income to Net Cash Provided (Used) by Operating Activities:	
Operating Income	\$ 637,072,024
Adjustments to Reconcile Operating Income to Net Cash Provided (Used) by Operating Activities:	
Depreciation and Amortization	22,561,417
Net Changes in Assets and Liabilities:	
(Increase) / Decrease in Accounts Receivable	14,372,390
(Increase) / Decrease in Ticket Inventory	259,136
(Increase) / Decrease in Prepaid Expenses	2,197,138
(Increase) / Decrease in Prize Reserves	137,520
(Increase)/Decrease in Pension Deferred Outflows	(6,665,205)
(Increase)/Decrease in Net OPEB Asset and OPEB Deferred Outflows	(419,460)
Increase / (Decrease) in Accounts Payable	230,908
Increase / (Decrease) in Compensated Absences Liability	384,707
Increase / (Decrease) in Unearned Revenue	63,457
Increase / (Decrease) in Prize Liability	19,482,464
Increase / (Decrease) in Net Pension Liability and Deferred Inflows	28,205,995
Increase / (Decrease) in OPEB Liability and OPEB Deferred Inflows	(194,808)
Total Adjustments	<u>80,615,659</u>
Net Cash Provided (Used) by Operating Activities	<u>\$ 717,687,683</u>
Noncash Investing, Capital, and Related Financing Activities:	
Net Change in Fair Value of Investments	\$ (5,626,786)
Intangible Assets Acquired Through Contract	563,772
Total Noncash Investing, Capital, and Related Financing Activities	<u>\$ (5,063,014)</u>

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

OREGON STATE LOTTERY

Notes to the Financial Statements

June 30, 2021

1. Summary of Significant Accounting Policies

A. Reporting Entity

The Oregon State Lottery Commission (Commission) was created as an agency of the State of Oregon by enactment of Article XV, Section 4 (3), of the Oregon Constitution, an initiative measure approved by Oregon voters at the November 1984 general election. The Commission established the Oregon State Lottery (Lottery), which is an enterprise fund of the State of Oregon. The Lottery commenced operations to market and sell Lottery products to the public in January 1985. The net profits of the Lottery are transferred to the Oregon Economic Development Fund and are then distributed by the State of Oregon to finance the various public purposes allowed by law.

B. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The accompanying financial statements of the Lottery have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB).

The Lottery uses an enterprise fund, the Oregon State Lottery Fund, with a self-balancing set of accounts to record its assets, deferred outflows of resources, liabilities, deferred inflows of resources, net position, revenues, and expenses. Enterprise funds account for activities that are financed and operated in a manner like private business enterprises.

Lottery financial statements are reported using the economic resources measurement focus and accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

Revenues and expenses are categorized as operating or nonoperating in the Statement of Revenues, Expenses and Changes in Fund Net Position. Operating revenues and expenses are those that result from selling Lottery games to the public. Operating revenues include the sale of Lottery products and incidental revenues associated with operating the Lottery. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. Revenues and expenses that do not result from selling Lottery games, such as investment income and investment expenses, are reported as nonoperating revenues and expenses.

Assets and liabilities are classified on the Statement of Net Position as current and noncurrent. Current assets are resources expected to be realized in cash or consumed within a year from the financial statement date. Current liabilities are obligations generally expected to be paid using resources that are classified as current assets and obligations due within one year from the date of the financial statements. Noncurrent assets are capital assets, resources that are restricted to use for other than current operations, resources designated to be used to acquire noncurrent assets, or resources that are not expected to be collected within one year. Noncurrent liabilities are obligations generally expected to be paid using resources that are classified as noncurrent assets and obligations due beyond one year from the date of the financial statements.

Total net position is segregated into three categories: net investment in capital assets, restricted for net OPEB asset and unrestricted net position. Article XV of the Oregon Constitution restricts the use of Lottery revenues for payment of prizes and administrative expenses, and remaining revenues are to be used for public purposes allowed in Article XV. Net proceeds not yet transferred are reflected in liabilities as the amount Due to the Economic Development Fund. Net position reported at year end will be used for Lottery operations.

C. Sales Revenue

Revenues for draw games Oregon's Game MegabucksSM, Powerball[®], Mega Millions[®], Keno, Win for LifeSM, RaffleSM, Pick 4SM, and Lucky LinesSM are recognized when the draws occur. Revenues for instant scratch ticket games are recognized when retailers activate ticket packs for sale to the public. Scoreboard revenues are recognized when events have completed, and the outcome is known and are reported net of returns to players. Revenues for Video LotterySM games are recognized when sales to the public occur and are reported net of prizes awarded. (Refer to Note 2(B) for more information on Video LotterySM and Scoreboard revenue and prize expense). All revenues are reported net of free plays, discounts, and allowances.

D. Unearned Revenue

All draw games can be purchased in advance of the drawings and Scoreboard wagers can be placed prior to an event. When shares are sold or wagers are placed in advance of the draw or event date, sales revenue is not yet earned. Unearned revenue includes revenue associated with draw or event dates occurring after the June 30 fiscal year end.

E. Prize Expense

Instant ticket prize expense is estimated and recognized when ticket packs are activated and is based on the game design. Game design includes certain guaranteed prizes in each pack of tickets and prizes placed randomly by the gaming vendor. When validations for the game have ended, differences between estimated and actual prizes awarded for the randomly placed prizes are adjusted to prize expense and prize liability. Guaranteed prizes not claimed by winners are transferred to the Economic Development Fund.

Prize expense for draw games is recognized as drawings are held, based on the shares sold and the estimated or known cost of the prize payments. Prize expense is adjusted as prizes are claimed and the actual cost of the prize is known. Expense for prizes with long-term payments is recognized when the prize liability is recorded, at the discounted present value of estimated future cash payments. Scoreboard prize expense is recognized when the outcome of the wagered event is known. Video LotterySM prize expense is recognized as game play completes and prizes are known. More detailed information for Video LotterySM is in Note 2(B).

Prize expense for fiscal year ending June 30, 2021 also includes \$3,697,795 of amortization expense related to the long-term prize liability discount (see Note 1(F)).

The cost of Lottery products distributed through various promotional activities is included in ticket expense and any prizes (actual or estimated) are recorded in prize expense. The sales value of these products for the fiscal year ended June 30, 2021 was \$24,776.

F. Prize Liability

Prize liability is recorded when the prize expense is recognized (see Note 1(E) above) and is reported at the discounted present value of estimated future cash payments. Discount rates are based on interest rates earned on securities purchased to fund long-term prize payments. Estimated and known prize payments due within one year of the financial statement date are recorded as a current liability and payments due later than the upcoming year are classified as a noncurrent liability. Unclaimed prizes (winning shares known to be sold and not presented for payment within one year from the draw date or official end of a game) are reclassified from Prize Liability to Due to Economic Development Fund.

G. Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, test cash held by employees, cash in demand deposit accounts and cash and investments held in the Oregon Short-Term Fund (OSTF). For purposes of the Statement of Cash Flows, all Lottery moneys held by the Office of the State Treasurer in the OSTF are cash equivalents. The OSTF is an investment pool that functions as a demand deposit account.

H. Investments

Investments are reported at fair value based on quoted market prices for similar assets at June 30, 2021. The fair value hierarchy established by generally accepted accounting principles categorizes valuation inputs in three levels. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; and Level 3 inputs are unobservable. The quoted prices used by Lottery are Level 2 inputs. Changes in the fair value of investments are recognized as investment income or loss in the current year.

I. Securities Lending

Securities lending amounts are reported at the value of the cash collateral received. The security lending liability is reported at the cash amount received as collateral.

J. Accounts Receivable

Accounts receivable is reported net of an allowance for uncollectible accounts. Accounts receivable primarily consist of proceeds due from Lottery retailers. Most retailers selling Lottery products are required to remit weekly proceeds (Sunday through Saturday), less commissions, on the following Wednesday. Corporate accounts with multiple establishments may remit proceeds on the second Wednesday following the end of the business week.

K. Inventories

Inventories are valued at cost using the specific identification method. Ticket inventory consists of Scratch-itsSM instant tickets primarily stored in the Lottery warehouse. A small amount of inventory is stored at retail establishments. Ticket inventory held in the warehouse is destroyed and recorded as an expense when distributions to retailers are no longer allowed. When activations are no longer allowed, tickets not sold at retail establishments are expensed. The tickets are returned to the warehouse and subsequently destroyed.

L. Prize Reserves

Prize reserves held by the Multi-State Lottery (MUSL) are amounts held to indemnify participating lotteries for prizes that may be won. Should the Lottery decide against participation in MUSL, these amounts would be returned. Prize reserves for Scoreboard are held in escrow and are available to our payment processor in the event cash amounts are not sufficient to cover player account withdrawals.

M. Capital Assets

Capital assets, which mainly include gaming equipment and related software and licensing agreements, are reported at historical cost. Physical and intangible assets with a cost of \$5,000 or more and a useful life of more than one year are capitalized. Capital assets are depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings and improvements	5 to 40
Video lottery equipment	5 to 7 or per agreement
Other machinery and equipment	5 to 25
Leasehold improvements	3 to 10 or per lease agreement
Vehicles	5 to 10
Computer hardware and software	2 to 10 or per agreement
Intangibles - Non-software	Term of contract

N. Compensated Absences

Employees earn vacation leave of 10 to 20 hours per month, depending upon length of service. All Lottery employees may accumulate a maximum of 350 hours per employee. Accumulated vacation leave and accumulated compensatory time is recorded as an expense and a liability (compensated absences) as the benefits accrue to employees. The compensated absences liability is calculated based upon salary rates in effect at the fiscal year-end and includes estimated tax and retirement costs. No liability is reported for accumulated sick leave benefits since employees are not paid for unused sick leave benefits when leaving State service.

O. Net Pension Liability, Pension Related Deferred Inflows and Outflows of Resources and Pension Expense

These items are included at amounts equal to Lottery’s portion of the State of Oregon’s proportionate share of Oregon Public Employee’s Retirement System (PERS) plan totals measured as of June 30, 2020. Amounts are recognized on the same basis the plan uses. PERS uses the accrual basis of accounting. As such, revenues are recognized when earned, contributions are recognized when due, benefits and withdrawals are recognized when due and payable. Lottery pension expense is included in Salaries and Wages expense.

P. Net Other Postemployment Benefits Asset and Other Postemployment Benefits Liabilities, Related Deferred Inflows and Outflows of Resources, and Expense

Lottery employees may be covered by one of three postemployment benefit plans. The associated assets and liabilities for the two plans administered by the Oregon Public Employee’s Retirement System (PERS) are measured as of June 30, 2020 and recognized on the same basis the plan uses. PERS recognizes revenues when earned, contributions when due and benefits/withdrawals are recognized when payable. The other plan is administered by the Public Employees Benefit Board (PEBB) and is measured as of June 30, 2021. Amounts included are Lottery’s portion of the State of Oregon’s amount of the respective other postemployment benefit plans. Expense for the plans is included in Salaries and Wages expense.

2. Stewardship and Legal Compliance

A. Budgetary Compliance

The Oregon State Lottery is exempt from State of Oregon Budget Laws. For budgeting purposes, the Commission adopts an annual Financial Plan based on revenue forecasts prepared by the Oregon Department of Administrative Services, Office of Economic Analysis, and activities identified in Lottery's annual Business and Strategic Plan. Quarterly, budgeted revenues and direct expenses (prizes, commissions, game vendor charges, and tickets) are revised for changes to the revenue forecasts. Revisions to other expense items in the adopted budget must be approved by the Commission. The budget is prepared on the accrual basis of accounting. Actual expenses are monitored throughout the year for compliance with the approved budget and appropriate adjustments, if necessary, are presented to the Commission for approval. A comparison of revenues and expenses to the final revised and approved fiscal year 2021 Financial Plan is presented as supplementary information in this report.

B. Video LotterySM and ScoreboardSM Net Revenue

Video LotterySM revenue is reported net of discounts and prize expense in the Statement of Revenues, Expenses, and Changes in Fund Net Position. The following schedule reconciles cash received with actual wagering and prize activity:

	<u>Revenue</u>		<u>Prize Expense</u>
Cash Received	\$ 3,014,210,946	Cash Paid Out	\$ 2,153,884,204
Dollars Won and Played	8,448,959,525	Dollars Won and Played	8,448,959,525
Total Revenue	<u>\$ 11,463,170,471</u>	Total Prizes	<u>\$ 10,602,843,729</u>
Net Revenue before Discounts = \$860,326,742			

ScoreboardSM revenue is reported net of discounts and prize expense in the Statement of Revenues, Expenses, and Changes in Fund Net Position. The following schedule shows actual wagering activity:

	<u>Amount</u>
Wagers Placed	\$ 315,777,289
Wagers Refunded Due to Cancellations	(1,558,624)
Prizes Won	<u>(283,965,387)</u>
Net Revenue Before Discounts	<u>\$ 30,253,278</u>

C. Use of Revenues and Net Revenues

Article XV of the Oregon Constitution requires that all prizes and expenses of the Lottery be paid from Lottery revenues and any remaining proceeds be used to benefit the public purposes of economic development, public education (including outdoor school), veterans services, or restoring and protecting parks, beaches, watersheds and native fish and wildlife habitats. ORS 461.500 requires that at least 84 percent of the total annual revenues be returned to the public in the form of prizes and net revenues benefiting the public purposes in the Constitution and statutes, that at least 50 percent of the total annual revenues be returned to the public in the form of prizes, and that no more than 16 percent of total annual revenues may be allocated for the payment of administrative expenses.¹

¹ Attorney General Opinion No. 8220 advises that ORS 461.548 regarding Video LotterySM proceeds is unconstitutional and is not applicable. It is not included here.

The following table shows that for fiscal year 2021 the Lottery operated within the legal limits defined by ORS 461.500:

<u>Fiscal Year 2021 Revenues</u>		
Sales	\$12,185,216,411	
Other Distributable Income	3,071,406	
Total Distributable Revenue	<u>\$12,188,287,817</u>	
<u>Fiscal Year 2021 Distribution of Revenues</u>		
Revenues Returned to the Public:		
Prizes to the Public	\$11,146,785,684	91.45%
Unclaimed Prizes Paid/Due to Economic Development Fund	5,811,111	0.05%
Transfers Paid/Due to Economic Development Fund	632,179,873	5.19%
Total Revenues Returned to the Public	<u>11,784,776,668</u>	<u>96.69%</u>
Administrative Expenses	403,511,149	3.31%
Total Revenue Distribution	<u>\$12,188,287,817</u>	<u>100.00%</u>

D. Unclaimed Prizes

ORS 461.500 requires all unclaimed prizes to be allocated to the benefit of public purpose. Lottery administrative rules declare a prize as unclaimed when it is known that winning shares have been sold and have not been redeemed within one year of the end of the game, one year from the draw date, or one year from the date of issue. During fiscal year 2021, prizes in the amount of \$5,811,111 were determined to be unclaimed and were either transferred or accrued for transfer to the Economic Development Fund.

E. Contingency Reserve

ORS 461.510 (4) and Administrative Rule 177-010-0045 allows for the creation of a contingency reserve. In May 2014, the Lottery Commission approved a contingency reserve amount such that the cash available for future investment does not exceed \$100,000,000. The following table shows the liquidity detail of Unrestricted Net Position shown on the Statement of Net Position at June 30, 2021:

Cash Available for Future Investment (Uncommitted Contingency Reserve)	\$ 87,006,475
Committed by Contract for Asset Purchases/Licensing (See Note 7 and 10)	32,973,638
Committed by Commission for Capital Purchases/Projects	59,103,508
Inventory and Prepaid Expenses	3,398,999
Total Unrestricted Net Position	<u>\$ 182,482,620</u>

F. Transfers to Economic Development Fund

All current year income remaining after transfers to the General Obligation Bond Fund as well as \$20,277,909 of contingency reserve was accrued for transfer to the Economic Development Fund. Actual cash transferred, including unclaimed prizes, during fiscal year 2021 was \$502,907,148. The remaining balance is included on the Statement of Net Position in current liabilities. The following schedule reconciles the amounts:

	Balance Owed as of June 30, 2020	Amounts Accrued	Cash Paid to Economic Development	Balance Remaining as of June 30, 2021
Income	\$ 69,860,728	\$ 652,457,782	\$ 497,273,679	\$ 225,044,831
Unclaimed Prizes	1,256,143	5,811,112	5,633,469	1,433,786
Total	<u>\$ 71,116,871</u>	<u>\$ 658,268,894</u>	<u>\$ 502,907,148</u>	<u>\$ 226,478,617</u>

3. Deposits

The Lottery uses a financial institution qualified by the Oregon State Treasurer to hold public funds, and the Oregon Short-Term Fund (OSTF) for deposits. The Office of the State Treasurer maintains the OSTF, an investment pool available for use by state agencies and local governments. A separate financial report for the OSTF may be obtained from the Office of the State Treasurer, 350 Winter Street NE, Suite 100, Salem, OR 97301-3896 or from the Treasurer's website at: <https://www.oregon.gov/treasury/public-financial-services/oregon-short-term-funds/Documents/oregon-short-term-fund-osft/OSTF-Annual-Financial-Statement-June-30-2021.pdf>

The custodial credit risk for deposits is the risk that, in the event of a bank failure, the Lottery or State Treasurer will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The Lottery does not have a policy regarding custodial credit risk for deposits; however, the insurance and collateral requirements for state deposits are established by banking regulations and Oregon Revised Statute (ORS) Chapter 295. This statute creates a shared liability structure through a collateral pool of pledged securities held by a custodian. ORS 295 is administered by the Oregon State Treasurer using the Public Funds Collateralization Program (PFCP). This program monitors public funds balances in excess of Federal Deposit Insurance of \$250,000, total public funds on deposit, depository net worth and capitalization information. All depositories are required to report quarterly at a minimum but may be required to report as often as weekly. Reported information determines each depository's minimum market value of securities that must be pledged as collateral.

The PFCP determines collateral requirements based on the capitalization of each depository. Well capitalized depositories must pledge securities with a market value of 10% of their last reported uninsured public funds deposits. Collateral requirements increase for depositories considered to be less than well capitalized. Collateral requirements may be up to 110% of uninsured public funds deposits. The Oregon State Treasurer, in consultation with the Department of Consumer and Business Services, may also require collateral up to 110% for well capitalized banks. Depositories with increased collateral requirements are required to report weekly to ensure collateralization at the appropriate level.

Consequently, Lottery's bank balance at June 30, 2021 of \$498,063,534, deposited in financial institutions and the OSTF, is insured or collateralized.

4. Investments

The State Treasurer is the Investment Officer for the State of Oregon. Investment standards are established in ORS 293.726 and require funds to be managed as a prudent investor would do. The Lottery does not have an independent investment policy.

A. Custodial Credit Risk

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the State Treasurer will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. Lottery's investments with the Office of the State Treasurer are registered in street name and held with the State Treasurer's agent in the name of the State of Oregon and segregated in the Treasurer's records in Lottery's name.

B. Credit Risk and Concentration of Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Lottery holds both US Treasury STRIPS as well as US Agency STRIPS of the Resolution Funding Corporation (RFC). The RFC investments are not explicitly guaranteed by the U.S. government and do not have a credit rating. However, interest payments are backed by the U.S. government, and the principal is protected by the purchase of zero-coupon bonds with an equivalent face value.

Concentration of credit risk is the risk of loss attributed to the magnitude of investments in a single issuer. Investments in the RFC represents 1.45 percent of the Lottery's investment holdings on June 30.

C. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The length of time until maturity affects the exposure of the investment to fair value fluctuations. Lottery's investments are purchased to closely match the liability stream for prize payouts and are intended to be held until maturity.

The following table shows the segmented time distribution of the fair value of all Lottery investments on June 30, 2021:

<u>Investment Type</u>	<u>Less than 1 Year</u>	<u>1-5 Years</u>	<u>6-10 Years</u>	<u>More Than 10 Years</u>	<u>Fair Value</u>
U.S. Agency STRIPS	\$ 71,995	\$ 1,700,425	\$ -	\$ -	\$ 1,772,420
U.S. Treasury STRIPS	10,706,589	39,356,894	34,753,130	35,792,349	120,608,962
Total Investments	<u>\$10,778,584</u>	<u>\$41,057,319</u>	<u>\$34,753,130</u>	<u>\$35,792,349</u>	<u>\$122,381,382</u>

5. Securities Lending

In accordance with State of Oregon (State) investment policies, state agencies may participate in securities lending. The Office of the State Treasurer has authorized its custodian to act as its agent in the lending of the State's securities pursuant to a form of loan agreement. There were no significant violations of the provisions of securities lending agreements during the fiscal year.

During fiscal year 2021, the State's securities lending agent lent short-term and fixed income securities from the OSTF and U.S. Government securities segregated to the Lottery and received as collateral U.S. dollar-denominated cash and U.S. Treasury securities. Borrowers were required to deliver collateral for each loan equal to not less than 102 percent of the market value of the loaned securities. The State can impose restrictions on the amount of the loans that the securities lending agent made on its behalf. No such restrictions were made during the year ended June 30, 2021. The State may pledge or sell collateral securities in the event of a borrower default; however, the Lottery and the State, through the State Treasurer's Securities Lending Agreements, are fully indemnified against losses due to borrower default. There were no losses during the year from the failure of borrowers to return loaned securities.

During the year, the State and borrowers maintained the right to terminate all securities lending transactions on demand. Therefore, the maturities of investments made with cash collateral generally did not match the maturities of the securities loans. On June 30, 2021, the State and the Lottery had no credit risk exposure to borrowers related to securities on loan.

As of June 30, 2021, the total fair value of securities on loan from the OSTF was \$300,543,601, the collateral received was \$306,679,928 and the fair value of invested collateral was \$67,060,777. Cash collateral received for OSTF and Lottery investments is invested in a securities lending collateral pool and is not exposed to custodial credit risk.

The Lottery's allocated portion of the OSTF securities on loan and Lottery owned investments on loan at June 30, 2021, is presented in the following schedule:

	<u>Securities Lending Balances</u>		
	<u>Fair Value of Securities on Loan</u>	<u>Collateral Received</u>	<u>Fair Value of Invested Cash Collateral</u>
Lottery Share OSTF	\$ 6,772,385	\$ 6,910,660	\$ 1,511,133
Lottery Investments	21,631,945	22,067,975	19,275,485
Total	<u>\$ 28,404,330</u>	<u>\$ 28,978,635</u>	<u>\$ 20,786,618</u>

6. Capital Assets

Capital asset activity for the year ended June 30, 2021, is shown in the following schedule:

	Beginning Balance	Increases	Decreases	Ending Balance
<u>Depreciable Capital Assets</u>				
Equipment	\$184,670,469	\$ 43,426,363	\$ 363,128	\$227,733,704
Building and Improvements ¹	15,388,341	-	-	15,388,341
Vehicles	5,515,251	-	552,049	4,963,202
Computer Software	27,911,153	2,311,381	116,666	30,105,868
Other Assets	1,386,660	309,000	-	1,695,660
Total Assets Being Depreciated	234,871,874	46,046,744	1,031,843	279,886,775
<u>Accumulated Depreciation</u>				
Equipment	157,699,753	18,344,115	320,968	175,722,900
Building and Improvements	8,248,534	438,641	-	8,687,175
Vehicles	2,724,784	563,757	409,193	2,879,348
Computer Software	16,604,083	3,070,327	80,417	19,593,993
Other Assets	1,382,358	144,577	-	1,526,935
Total Accumulated Depreciation	186,659,512	22,561,417	810,578	208,410,351
<u>Capital Assets Not Being Depreciated</u>				
Building and Improvements ¹	444,849	-	-	444,849
Capital Assets, Net	\$ 48,657,211	\$ 23,485,327	\$ 221,265	\$ 71,921,273

¹Vacated backup center reclassified to capital assets not being depreciated

Included in the equipment category above is \$6,736,500 of Video Retailer Terminals acquired through a capital lease. Equipment accumulated depreciation includes capital lease amortization of \$4,090,018.

On June 27, 2014 the Lottery vacated its backup center and it remained idle at June 30, 2021. Carrying value included in capital assets is \$444,849.

7. Long-term Liabilities

The following schedule presents changes in long-term liabilities during the fiscal year, as well as the amounts due in the next fiscal year:

	Beginning Balance	Increases	Decreases	Ending Balance	Due Within One Year
Prizes	\$146,954,022	\$266,065,927	\$252,394,574	\$160,625,375	\$51,395,326
Compensated Absences	4,670,301	3,407,547	3,022,839	5,055,009	3,285,756
Licensing Contracts	6,897,617	563,772	2,043,759	5,417,630	1,808,091
Capital Lease Obligation	3,719,379	-	999,766	2,719,613	1,075,777
Pre-SLGRP Pension Debt	3,367,330	-	419,489	2,947,841	386,719
Total	\$165,608,649	\$270,037,246	\$258,880,427	\$176,765,468	\$57,951,669

As of June 30, 2021, there were 79 Oregon Lottery prizes with remaining long-term annual prize payments. The estimated number of years remaining for payments extends to 46 years. During fiscal year 2021, a \$278,248 gain was recognized for defeasance of a previously estimated liability in the Win For LifeSM game. The following schedule of payments includes claimed prizes with payments for a fixed period. Although estimated and included in prize liability, contingent prize payments are not shown in the table (next page):

Fiscal Year Ending June 30	Principal	Interest
2022	\$ 8,942,075	\$ 140,779
2023	8,413,242	372,425
2024	8,029,670	596,997
2025	7,408,529	797,137
2026	7,097,636	1,008,031
2027-2031	23,128,331	5,236,003
2032-2036	14,658,687	5,825,647
2037-2041	4,770,626	2,338,708
2042-2046	1,681,263	942,071
2047-2051	751,975	398,025
Total	<u>\$ 84,882,034</u>	<u>\$ 17,655,823</u>

The Lottery currently has six software licensing contracts requiring monthly, quarterly, or annual payments for a defined period. Gaming software licenses include the video gaming system and instant ticket second chance drawing licenses. Beginning in September 2016 Lottery contracted for a video gaming system. The system includes all hardware and software necessary for a host and backup system that communicates and stores transactions occurring on Video LotterySM terminals throughout the State. The contract will expire in September 2024. Should the Lottery default through non-payment or breach of contract, undisputed amounts on invoices for services performed and deliverables delivered, less any amounts previously paid, are due immediately. The second chance drawing software contract includes draw configuration and support for one or more application programming interfaces. The contract began in February 2021 and continues through February 2024. After the initial three-year term Lottery may extend the contract on an annual basis. Lottery does have the right to terminate the contract with a 30-day notice to the contractor.

The Lottery also has licenses for recruitment tracking, recruitment and job description writing, and compensation data software.

The following table shows the total annual liability payments required by the licensing contracts:

Fiscal Year Ending June 30	Amount
2022	\$ 1,808,091
2023	1,641,255
2024	1,583,702
2025	384,583
Total	<u>\$ 5,417,631</u>

Prior to the formation of the PERS State and Local Government Rate Pool (SLGRP), the State and community colleges were pooled together in the State and Community College Pool (SCCP), while local government employers participated in the Local Government Rate Pool (LGRP). These two pools combined to form the SLGRP effective January 1, 2002. The unfunded actuarial liability (UAL) attributable to the SCCP at the time the SLGRP was formed is maintained separately, is reduced by contributions and increased for interest charges at the assumed interest rate. The balance of the pre-SLGRP pooled liability attributable to the State is being amortized over the period ending December 31, 2027. The Pre-SLGRP Pension Debt of \$2,947,841 represents Lottery's allocation of the state liability. The payment schedule is shown in the following table (next page):

Year Ending June 30	Principal	Interest
2022	\$ 386,719	\$ 214,904
2023	415,064	186,559
2024	445,486	156,137
2025	478,139	123,484
2026	513,184	88,439
2027 & 2028	709,249	61,277
Total	\$ 2,947,841	\$ 830,800

8. Discounts and Allowances

Revenues are reported net of discounts and free plays in the Statement of Revenues, Expenses and Changes in Fund Net Position. Some Lottery game structures offer free tickets as prizes instead of cash. The sales value of these prizes reduces sales rather than being included as prize expense. For fiscal year ended June 30, 2021 Lottery awarded free play prizes of \$688,480. Promotional discounts and free plays also reduced sales by \$1,162,530.

At June 30, 2021, accounts receivable in the Statement of Net Position is reported net of \$309,772 allowance for uncollectible amounts.

9. Joint Venture

The Multi-State Lottery Association (MUSL) was established September 16, 1987, to coordinate lottery games with larger prizes than the individual states could offer by themselves. The Oregon Lottery has been a participating member since the inception of MUSL. Each participating state sells its choice of MUSL products and keeps all profits earned. Participating states contribute amounts necessary to fund the estimated and actual prizes won, reserve prize pools, and fees for services of MUSL and the Product Groups. In the fiscal year ending June 30, 2021 there were sufficient revenues to cover expenses and no additional amounts were paid for fees and services.

MUSL is a non-profit, government-benefit association owned and operated by its member lotteries. It is governed by a board on which each member lottery is represented. Each member lottery has one vote. The Board's responsibilities to administer multi-state lottery games are performed through product groups, advisory committees, or panels staffed by officers and independent contractors as appointed by the Board. These officers and consultants serve at the pleasure of the Board and the Board prescribes their powers, duties, and qualifications. Product groups manage product offerings, establish budgets, establish rules and policies for a product as well as the fees for services. The Audit and Finance Committee recommends all fees for services to be charged by MUSL and product groups to the Executive Committee who review and submit to the Board for final action. MUSL is subject to annual audits conducted by independent auditors that are retained by the Board. Upon termination of the MUSL's existence, if such termination should occur, the member lottery would receive any proceeds determined available for distribution by the Board.

The fiscal year end for MUSL is June 30. Long-term liabilities of MUSL are limited to prize annuities due, which are fully funded through investments in U.S. Government Securities. The following schedule presents the summarized financial activity from MUSL financial statements as of June 30, 2021 and June 30, 2020 (in thousands):

	<u>2021</u>	<u>2020</u>
Assets	\$ 848,610	\$ 534,266
Total Assets	<u>\$ 848,610</u>	<u>\$ 534,266</u>
Liabilities	\$ 836,396	\$ 519,556
Net Assets ¹ - Unrestricted	12,214	14,710
Total Liabilities and Net Assets ¹	<u>\$ 848,610</u>	<u>\$ 534,266</u>
Revenue	\$ 1,324	\$ 7,523
Expenses	4,832	5,982
Other Changes in Net Assets ¹	1,011	(7,800)
Decrease in Net Assets	<u>\$ (2,497)</u>	<u>\$ (6,259)</u>

¹Because MUSL is organized as a non-profit, its financial statements have been prepared in accordance with accounting standards promulgated by the Financial Accounting Standards Board (FASB). Therefore, MUSL's financial statements use the term "net assets" rather than "net position" for equity.

The financial statements for MUSL may be obtained from the Multi-State Lottery Association, 4400 NW Urbandale Drive, Urbandale, Iowa, 50322.

10. Capital Lease Commitments

In October 2016, the Lottery began a capital lease of 2,700 video retailer terminals, known as iLinks, which are part of the communication infrastructure between the Video LotterySM game terminals and the host system. Lease payments total \$8,679,364 with the last payment due in September 2024. After all payments are made ownership will transfer to the Lottery. The gross amount of the assets acquired is \$6,736,500 and is included in Buildings, Equipment and Vehicles on the Statement of Net Position.

Future minimum capital lease payments for agreements in effect as of June 30, 2021 are shown in the following schedule:

Fiscal Year Ending June 30,	Future Minimum Capital Lease Payments	
	Principal	Interest
2022	\$ 1,075,777	\$ 164,132
2023	1,157,566	82,343
2024	463,587	10,946
2025	22,683	279
Total Future Minimum Lease Payments	<u>\$ 2,719,613</u>	<u>\$ 257,700</u>

11. Other Significant Commitments and Contingencies

A. Commitments

In October 2019 the Lottery signed a comprehensive agreement for software and services associated with processing transactions for traditional products. The initial contract term is five years from the go-live date of May 23, 2021. During this term Lottery will pay 2.5047 percent of net sales of traditional products. Contract extension options are available for two more five-year terms.

In May 2019, Lottery contracted for services and access to software for a sports betting solution. The contract is for five years from the launch date of October 16, 2019. The contract will automatically renew for additional three-year periods unless one party notifies the other of intent not to renew. Software access fees are a percentage of net gaming revenues (NGR), which is revenue net of prizes and other allowed expenses. In the first three years the percentage varies from 11% to 9%, declining as NGR increases. The fourth year and after Lottery will pay 12% of NGR. Service fees are also a percentage of NGR, and during the first three years Lottery

will pay 16%. The percentage then increases to 17% for year 4 and after. The current minimum service fee is \$350,000 per month and extends through the end of the term. Lottery has also agreed to reimburse the vendor for expenses related to third-party products required for the sports betting solution. If the contract is terminated a termination fee based on the average fees paid or \$300,000, whichever is greater, multiplied by the lesser of 24 months or remaining months of the term becomes due. However, Lottery does retain the right to terminate the contract under specified criteria with no termination fee. Lottery expenses for software access, services, and third-party reimbursements for the fiscal year ending June 30, 2021 were \$10,087,200. These expenses are included in Game Vendor Charges on the Statement of Revenues, Expenses, and Changes in Fund Net Position.

In April 2020 Lottery's sports betting provider merged with another sports betting company. Although there was no change to our current services contract, Lottery is currently in contract negotiations with the new vendor.

In early June 2021 Lottery issued a commitment to purchase 1,050 Video LotterySM gaming terminals. At June 30 \$14,606,712 remained to be purchased in fiscal year 2022.

B. Unemployment Benefits

State employees who qualify are entitled to benefit payments during periods of unemployment. Each state agency is required to reimburse the Employment Department for benefit payments made to former employees. There is no practical method of estimating the amount of future benefit payments that may be made to former employees for wage credits earned prior to fiscal year end. Consequently, this potential obligation is not reported in the accompanying financial statements. For the fiscal year ended June 30, 2021, \$344,296 of reimbursements were expensed.

12. Employee Retirement Plan

A. General Information

The State of Oregon participates in the Oregon Public Employees Retirement System (PERS) plan. As an agency of the State of Oregon, eligible Lottery employees receive pension benefits through the plan. PERS is a defined benefit, cost-sharing multiple-employer plan, administered by the Public Employees Retirement Board (Board) as required by Chapters 238 and 238(A) of the Oregon Revised Statutes (ORS). Board members are appointed by the governor and confirmed by the state Senate.

Pension benefits are based on hire dates and are provided under the PERS plan or the Oregon Public Service Retirement Plan (OPSRP). PERS members who established membership before January 1, 1996 receive PERS Tier 1 benefits while those who established membership on or after that date receive PERS Tier 2 benefits. The PERS plan was closed to new members on August 28, 2003. Eligible employees hired after that date are members of OPSRP. Both plans provide a life pension, death, and disability benefits.

Pension Benefit

Tier 1/Tier 2 member's basic pension benefits are calculated based on years of service and final average salary, multiplied by 1.67 percent for general service employees and 2.0 percent for police and fire (P&F) employees. Benefits may also be calculated under a money match computation if a greater benefit results. For members contributing prior to August 21, 1981 benefits may also be calculated under a formula plus annuity computation. Pension benefit options include survivorship and lump sum refunds. The retirement allowance is payable monthly for life.

Tier 1 full pension benefits are available at age 58 (age 55 for P&F) or any age with 30 years of service (25 for P&F). There is a reduced benefit option available at age 55 (50 for P&F) and fewer than 30 years of service (25 for P&F). Tier 2 members can retire at age 60.

OPSRP member pension benefits are calculated based on years of service and the final average salary multiplied by 1.5 percent for general service employees and 1.8 percent for P&F. General service employees may retire at 65 or at age 58 with 30 years of service. P&F employees are eligible at age 60 or age 53 with 25 years of service.

OPSRP also includes the Individual Account Program (IAP) for employee contributions. Beginning January 1, 2004 all Tier 1/Tier 2 plan non-retired members also established an account in the IAP. Prior to July 1, 2020 all employee contributions were deposited in the member's account along with earnings. Beginning July 1, 2020 employee's whose monthly salary exceeds established monthly thresholds have a portion of their contributions redirected to an Employee Pension Stability Account (EPSA) which will be used to pay for part of the future pension benefit. Employees have the option to make additional voluntary contributions to replace any redirected amounts. IAP accounts are reduced by administrative expenses and losses. At retirement, IAP

account balances are distributed to employees through a choice of a lump-sum payment or annuity options. Tier 1/Tier 2 employee contributions prior to January 1, 2004 remain in the member's defined benefit account.

Death Benefit

Upon the death of a non-retired PERS Tier 1/Tier 2 member the beneficiary receives a lump-sum refund of the member's accumulated contributions and interest. The beneficiary also receives a lump-sum payment from employer funds equal to the account balance. Upon the death of a non-retired OPSRP member the spouse (or person constitutionally required to be treated as a spouse) receives a life pension at 50 percent of what would have been paid to the member.

Disability Benefit

All members can receive non job-related disability benefits after 10 years of service. Job-related disability is available for any length of service. Tier 1/Tier 2 monthly benefits are calculated with service time to age 58 (55 for P&F). OPSRP members receive 45 percent of their salary during the last full month of service.

Benefit Changes

After retiring, PERS plan members may choose to continue participation in a variable equities investment account and may experience benefit fluctuations due to changes in the market value of equity investments. Cost-of-living benefit adjustments (COLA) for both PERS and OPSRP members are required annually in current Oregon statutes. For service time before October 1, 2013 adjustments are tied to the Portland Consumer Price Index with a 2% annual cap. Service time on or after October 1 receives a 1.25% increase on the first \$60,000 of annual benefit and .15% for benefit over \$60,000. The Oregon legislature has authority to change benefits.

Contributions

As required by Oregon statute, employer contribution rates are actuarially determined and allow accumulation of assets sufficient to pay defined pension benefits when due. Employer contribution rates are expressed as a percentage of covered payroll. The Board's practice is to implement new rates in each odd-numbered year based on the valuation of the previous odd-numbered year. Rates used in fiscal year 2021 were effective July 1, 2019 and based on the December 31, 2017 valuation. Lottery contributions in fiscal year 2021 were \$5,182,228.

Set by statute, Lottery employees contribute 6 percent of covered salary to their IAP account. However, beginning in July 2020 a portion of monthly employee contributions may be redirected to the employee's EPSA account and used to fund their pension benefit. Redirects are required when the PERS system is less than 90% funded and an employee's monthly salary exceeds the monthly salary threshold established by the legislature. The percentage of monthly contributions redirected is determined by plan. For Tier 1/Tier 2 members 2.5 percent of employee contribution is redirected and for OPSRP members .75 percent is redirected.

B. Net Pension Liability, Pension Expense and Deferred Outflows/Inflows of Resources Related to Pensions

The collective net pension liability, measured as of June 30, 2020, is based on the December 31, 2018 actuarial valuation rolled forward to the measurement date. IAP accounts are not included in the measurement of the total pension liability. Assumptions used for the measurement include the following table below and are continued on the next page:

Experience Study Report	2018, published July 2019
Actuarial Cost Method	Entry Age Normal
Actuarial Assumptions:	
Inflation Rate	2.50 percent
Investment Rate of Return	7.20 percent
Projected Salary Increases	3.50 percent compounded
Cost of living adjustments (COLA)	Blend of 2.00 percent COLA and graded COLA (1.25/0.15 percent in accordance with Moro decision; blend based on service.)

Mortality	<p><u>Healthy retirees and beneficiaries:</u> Pub-2010 Healthy Retiree, sex-distinct, generational with Unisex, Social Security Data Scale, with job category adjustments and set-backs as described in the valuation.</p> <p><u>Active members:</u> Pub-2010 Employee, sex-distinct, generational with Unisex, Social Security Data Scale, with job category adjustments and set-backs as described in the valuation.</p> <p><u>Disabled Retirees:</u> Pub-2010 Disable Retiree, sex-distinct, generational with Unisex, Social Security Data Scale, with job category adjustments and set-backs as described in the valuation.</p>
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The discount rate used to measure the collective pension liability was 7.20 percent. The projection of cash flows used to determine the discount rate assumed contributions from contributing employers and plan members are made at the actuarially determined rates required to meet projected benefit payments. Therefore, the long-term expected rate of return was applied to all periods of projected benefit payments.

The long-term expected rate of return used in projecting the collective pension liability is based on a forward-looking capital market economic model. The assumed asset allocation is based on the Oregon Investment Council's (OIC) target allocation and actual investments in May 2019 based on the target. Using the OIC description of asset classes, investments were mapped to the asset classes and percentages below. Each asset class assumption is based on a consistent set of underlying assumptions and includes adjustment for the inflation assumption. The following assumptions were used:

Asset Class	Target Allocation	Annual Arithmetic Return	20-Year Annualized Geometric Mean	Annual Standard Deviation
Core Fixed Income	9.60%	4.14%	4.07%	3.90%
Short-Term Bonds	9.60	3.70	3.68	2.10
Bank/Leveraged Loans	3.60	5.40	5.19	6.85
High Yield Bonds	1.20	6.13	5.74	9.35
Large/Mid Cap US Equities	16.17	7.50	6.30	15.50
Small Cap US Equities	1.35	8.35	6.68	19.75
Micro Cap US Equities	1.35	8.86	6.79	22.10
Developed Foreign Equities	13.48	8.30	6.91	17.95
Emerging Market Equities	4.24	10.35	7.69	25.35
Non-US Small Cap Equities	1.93	8.81	7.25	19.10
Private Equity	17.50	11.95	8.33	30.00
Real Estate (Property)	10.00	6.19	5.55	12.00
Real Estate (REITS)	2.50	8.29	6.69	21.00
Hedge Fund of Funds - Diversified	1.50	4.28	4.06	6.90
Hedge Fund - Event-driven	0.38	5.89	5.59	8.10
Timber	1.13	6.36	5.61	13.00
Farmland	1.13	6.87	6.12	13.00
Infrastructure	2.25	7.51	6.67	13.85
Commodities	1.13	5.34	3.79	18.70
Assumed Inflation - Mean			2.50%	1.65%

PERS actuarially determined each employer’s proportionate share by comparing each employer’s projected long-term contribution effort to the plan with the total projected long-term contribution effort of all employers. The projected long-term contribution effort is estimated by combining the present value of projected future normal cost contributions with projected contributions required for past unfunded actuarial liabilities (UAL) and reducing those projections with any transition surpluses, lump sum payments from employers, and pre-State and Local Government Rate Pool (SLGRP) surpluses at the valuation date. Estimated future normal cost rate contributions represent future service contributions while UAL estimated contributions represent contributions for past service. PERS has determined employer transition liabilities to meet the definition of separately financed employer liabilities and are not included in the projected contribution effort. The State of Oregon’s proportion was 27.65% as of the prior June 30, 2019 measurement date and increased to 28.36% as of the June 30, 2020 measurement date.

The State of Oregon’s proportionate share of the net pension liability was allocated to individual funds based on actual fiscal year 2020 contributions. Lottery is 1.16 percent of the State’s share, an increase of .27 percent from the June 30, 2019 measurement date. Lottery’s proportion of the State’s share equates to .33 percent of the collective net pension liability. On June 30, 2021 Lottery reported a net pension liability of \$72,097,398. The following demonstrates Lottery’s proportionate share of the net pension liability/(asset) sensitivity to a 1 percentage point change in the discount rate:

1% higher discount rate – 8.2%	\$ 42,780,741
1% lower discount rate – 6.2%	\$107,058,682

For the year ended June 30, 2021 Lottery recognized pension expense of \$26,723,019. At June 30, 2021 Lottery reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 3,173,158	\$ -
Changes in assumptions	3,869,239	(135,570)
Net difference between projected and actual earnings on investments	8,477,717	-
Changes in proportion and differences between fund contributions and proportionate share of contributions	2,319,858	(1,502,425)
Lottery contributions subsequent to the measurement date	5,182,228	-
Total	\$ 23,022,200	\$ (1,637,995)

Lottery contributions subsequent to the measurement date will reduce the net pension liability in the upcoming fiscal year. Other deferred amounts will be included in pension expense as shown in the following table:

Fiscal Year Ending June 30	Amount to Pension Expense
2022	\$ 3,782,991
2023	4,779,804
2024	4,481,457
2025	3,075,507
2026	82,218
Thereafter	-
Total	\$ 16,201,977

Detailed information about the PERS pension plan’s fiduciary net position is available in the separately issued Comprehensive Annual Financial Report on the PERS website at:

<https://www.oregon.gov/pers/Documents/Financials/CAFR/2021-ACFR.pdf>

13. Other Postemployment Benefit Plans

Oregon Lottery employees may be eligible for post-retirement insurance coverage through three other postemployment benefit (OPEB) plans available. Two plans are administered by the Public Employees Retirement System (PERS) and the other is administered by the Public Employees Benefit Board (PEBB). Lottery, as an enterprise fund of the State of Oregon, recognizes a portion of each plan in the financial statements.

A. Plans Administered by the Public Employees Retirement System

The Retirement Health Insurance Account (RHIA), administered by PERS, is a cost-sharing, multiple-employer OPEB plan. The plan authorizes a payment of up to \$60 towards the monthly cost of health insurance for eligible PERS members. To be eligible the PERS member must have eight or more years of qualifying service in PERS at the time of retirement, receive both Medicare Parts A and B coverage, and enroll in a PERS-sponsored health plan. The coverage also extends to members receiving a disability allowance, as if the member had at least eight years of creditable service. A surviving spouse or dependent of a deceased PERS retiree is eligible if he or she is receiving a retirement benefit or allowance from PERS or was insured at the time of the member’s death and the member retired before May 1, 1991. The plan is closed to entrants hired on or after August 29, 2003.

The RHIA plan and benefit amount is established by ORS 238.420. There are no automatic or ad-hoc adjustments to the benefit amount in the statute.

The other plan administered by PERS is the Retiree Health Insurance Premium Account (RHIPA). This plan is a single employer plan with the State of Oregon as the single employer. As authorized by ORS 238.415 retirees receive payment for the average difference between the health insurance premiums paid by retired state employees and the premiums paid by active state employees. The average amount is determined by the PERS Board on or before January 1 of each year. This plan is closed to entrants hired on or after August 29, 2003.

Retirees are eligible for the RHIPA plan if they have eight or more years of qualifying service but are not eligible for federal Medicare coverage. Retirees receiving a disability pension are also eligible if the pension was calculated as if they had eight or more years qualifying service and are not receiving federal Medicare coverage. A surviving spouse or dependent of a retired state employee is eligible if he or she is receiving a retirement benefit from PERS or was insured at the time the member died and the member retired on or after September 29, 1991.

Both plans are required by statute to be funded through employer contributions actuarially necessary to fund the liabilities of the plans. Employer contribution levels must be established by the PERS Board using the same actuarial assumptions it uses to determine employer contribution rates for the Public Employees Retirement Fund. Contribution rates for the fiscal year ending June 30, 2021 were effective July 1, 2019 and based on the December 31, 2017 valuation. The rates are a percentage of covered payroll and vary by the retirement plan of the participant. The contribution rates and amounts contributed by Lottery during the year ended June 30, 2021 are shown in the following table:

	RHIA		RHIPA	
	PERS		PERS	
	Tier 1/Tier 2	OPSRP	Tier 1/Tier 2	OPSRP
Normal Cost	0.06%	0.00%	0.12%	0.00%
Unfunded Actuarial Liability	0.00%	0.00%	0.27%	0.27%
Total Required Rate	0.06%	0.00%	0.39%	0.27%
Amounts Contributed	\$ 7,203	\$ 0	\$ 46,819	\$ 61,216

Both plans use assumptions and other inputs to measure the total OPEB liability. These assumptions and inputs are shown in the following table:

	RHIA	RHIPA
Plan Type	Cost-Sharing Multiple Employer	Single Employer (State of Oregon)
Valuation date	December 31, 2018	December 31, 2018
Measurement date	June 30, 2020	June 30, 2020
Experience Study	2018, published July 24, 2019	2018, published July 24, 2019
Actuarial assumptions:		
Actuarial cost method	Entry Age Normal	Entry Age Normal
Inflation rate	2.50 percent	2.50 percent
Long-term expected rate of return	7.20 percent	7.20 percent
Discount rate	7.20 percent	7.20 percent
Projected salary increases	3.50 percent	3.50 percent
Retiree healthcare participation	Healthy retirees: 32%, Disabled retirees: 20%	8-14 years of service: 10% 15-19 years of service: 15% 20-24 years of service: 19% 25-29 years of service: 26% 30+ years of service: 34%
Healthcare cost trend rate	Not Applicable	Applied at beginning of plan year, starting with 7.1% for 2019, decreasing to 5.0% for 2022, increasing to 5.9% for 2031, and decreasing to an ultimate rate of 4.1% for 2094 and beyond
Mortality	<p>Healthy retirees and beneficiaries: Pub-2010 Healthy Retiree, sex distinct, generational with Unisex, Social Security Data Scale, with job category adjustments and set-backs as described in the valuation.</p> <p>Active members: Pub-2010 Healthy Retiree, sex distinct, generational with Unisex, Social Security Data Scale, with job category adjustments and set-backs as described in the valuation.</p> <p>Disabled retirees: Pub-2010 Healthy Retiree, sex distinct, generational with Unisex, Social Security Data Scale, with job category adjustments and set-backs as described in the valuation.</p>	<p>Healthy retirees and beneficiaries: Pub-2010 Healthy Retiree, sex distinct, generational with Unisex, Social Security Data Scale, with job category adjustments and set-backs as described in the valuation.</p> <p>Active members: Pub-2010 Healthy Retiree, sex distinct, generational with Unisex, Social Security Data Scale, with job category adjustments and set-backs as described in the valuation.</p> <p>Disabled retirees: Pub-2010 Healthy Retiree, sex distinct, generational with Unisex, Social Security Data Scale, with job category adjustments and set-backs as described in the valuation.</p>

For both plans, the projections of cash flows used to determine the discount rate assumes that employer(s) contributions are made at the contractually required rates, as actuarially determined.

The long-term expected rate of return for both plans is the same as that used for pension benefit projections. A description of how this rate is determined and information on the assumed asset allocation of the portfolio is included in Note 12(B). This long-term rate was applied to all periods of projected benefit payments to determine the total OPEB liability for both plans.

For the RHIA cost-sharing multiple-employer plan, employer proportionate share was determined by comparing the employer's actual, legally required contributions made during the measurement date fiscal year to the total actual contributions made during that period by all employers. For both plans, the State of Oregon's internal allocation among funds was based on fiscal year 2020 actual contributions from each fund. Lottery's share of both plans is shown below. The amounts are measured as of June 30, 2020 based on a December 31, 2018

actuarial valuation rolled forward. Effects of a 1 percentage point change in the healthcare cost trend rate and the discount rate are also shown in the following table:

	RHIA	RHIPA
State of Oregon Share of Plan	16.48%	100.00%
Lottery Percent of State of Oregon Share	2.03%	1.24%
Lottery Share of Net OPEB Liability/(Asset)	\$ (680,959)	\$ 123,521
Lottery Share with:		
1% increase in healthcare cost trend rate	N/A	\$ 170,012
1% decrease in healthcare cost trend rate	N/A	\$ 87,017
1% increase in the discount rate – 8.2%	\$ (793,140)	\$ 76,807
1% decrease in the discount rate – 6.2%	\$ (549,760)	\$ 173,566

In the fiscal year ending June 30, 2021, Lottery recognized expense for the RHIA and RHIPA plans in the following amounts respectively; \$(431,161) and \$91,308. The following table shows the balances of Lottery’s deferred outflows and inflows for the two plans:

	RHIA		RHIPA	
	Deferred Outflow of Resources	Deferred Inflow of Resources	Deferred Outflow of Resources	Deferred Inflow of Resources
Differences between expected and actual experience	\$ -	\$ (69,614)	\$ -	\$ (46,738)
Changes in assumptions	-	(36,196)	2,992	(83,030)
Net difference between projected and actual earnings on investments	75,728	-	28,161	-
Changes in proportion and differences between fund contributions and proportionate share of contributions	283,085	(2,705)	-	-
Contributions Subsequent to Measurement Date	7,203	-	108,035	-
Total	<u>\$ 366,016</u>	<u>\$ (108,515)</u>	<u>\$ 139,188</u>	<u>\$ (129,768)</u>

Contributions subsequent to the measurement date will reduce the liability in the upcoming fiscal year. The other deferred amounts will increase/(reduce) OPEB expense as follows:

Fiscal Year Ending June 30	RHIA	RHIPA
2022	\$ 78,870	\$ (19,065)
2023	119,547	(17,493)
2024	27,993	(16,866)
2025	23,888	(17,366)
2026	-	(19,977)
Thereafter	-	(7,848)
Total	<u>\$ 250,298</u>	<u>\$ (98,615)</u>

Detailed information about the PERS other postemployment benefit plan’s fiduciary net position is available in the separately issued Comprehensive Annual Financial Report on the PERS website at:
<https://www.oregon.gov/pers/Documents/Financials/CAFR/2021-ACFR.pdf>

B. Plan Administered by the Public Employees Benefit Board

The Public Employees Benefit Board (PEBB), through the authority of Oregon Revised Statutes Chapter 243, offers healthcare assistance to eligible retired employees and their beneficiaries. The PEBB plan is a single-employer plan (State of Oregon) that allows retired employees to continue their health insurance coverage on a self-pay basis until they are eligible for Medicare. The premium rate for retired employees is determined by pooling the retirees with active employees and thus creates an implicit rate subsidy. Employees are eligible if they retire and are immediately eligible for a pension benefit from PERS. In addition, the retiree must have been enrolled in a PEBB medical or dental plan immediately prior to retirement. Retirees must apply for retiree coverage within 60 days of the end of their active coverage.

The total OPEB liability for the PEBB plan was actuarially measured as of July 1, 2019 and projected forward to June 30, 2021. In projecting the future benefits the current discount rate used is based on the Bond Buyer 20-Year General Obligation Bond Index which changed from the prior year. There are no assets accumulated for payment of the liability. The following table shows significant assumptions used:

Valuation Date	July 1, 2019
Measurement Date	June 30, 2021
Discount Rate	2.16%
Health Care Cost Trend	Pursuant to ORS 243.135(8), growth in per-member expenditures under self-insured plans and premium amounts is assumed to be 3.4% per year
General Inflation	2.5% per year
Annual Salary Increases	3.5% per year
Mortality	December 31, 2018 Oregon PERS Valuation
Election and Lapse Rates	30% of eligible employees, 60% spouse coverage for males, 35% for females. 7% annual lapse rate.
Actuarial Cost Method	Entry Age Normal

Lottery, as a fund of the State of Oregon, recognizes a portion of the total liability. Fund proportions are based on each fund’s fiscal year 2021 actual contributions. Lottery’s share of the liability at June 30, 2021 is \$1,147,445 which is 0.76 percent of the State of Oregon’s liability. The sensitivity of the liability to changes in the discount rate and healthcare cost trend rate are shown in the table below:

Lottery Share with:	
1% increase in healthcare cost trend rate – 4.4%	\$ 1,283,030
1% decrease in healthcare cost trend rate – 2.4%	\$ 1,032,325
1% increase in the discount rate – 3.16%	\$ 1,069,962
1% decrease in the discount rate – 1.16%	\$ 1,229,793

For the fiscal year ended June 30, 2021 Lottery recognized \$76,175 of income for the PEBB plan. The following table shows the balances of Lottery’s deferred outflows and inflows for the plan:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ -	\$ (4,592)
Changes in assumptions	27,530	(140,944)
Total	<u>\$ 27,530</u>	<u>\$ (145,536)</u>

The amounts will reduce Lottery’s proportion of OPEB expense in future years as follows:

Fiscal Year Ending June 30,	
2022	\$ (18,218)
2023	(18,218)
2024	(18,218)
2025	(18,219)
2026	(15,485)
Years thereafter	(29,648)
Total	<u>\$ (118,006)</u>

14. Risk Financing

The State of Oregon administers property and casualty insurance programs covering State government through its Insurance Fund (included in the Central Services Fund). The Insurance Fund services claims for direct physical loss or damage to state property; tort liability claims brought against the State, its officers, employees, or agents; workers’ compensation; cyber security liability, employee dishonesty; and faithful performance coverage for certain positions required by law to be covered and other key positions.

As a state agency, the Lottery participates in the Insurance Fund. The cost of servicing insurance claims and payments is covered by charging an assessment to each state agency based on its share of services provided in a prior period. The total statewide assessment for each coverage type is based on independent biennial actuarial forecasts and administrative costs, less any available equity in the Insurance Fund from the prior biennium. Lottery’s fiscal year 2021 share of the 2019-2021 biennial assessment was \$682,027. For the Lottery, the amount of claim settlements did not exceed insurance coverage for each of the past three fiscal years.



Supplementary Information

Oregon State Lottery
An Enterprise Fund of the State of Oregon
Budgetary (Non-GAAP) Basis Comparison Schedule
For the Fiscal Year Ended June 30, 2021

	Actual	Budget ⁽¹⁾	Variance Favorable/ (Unfavorable)
Revenue			
Video Lottery SM (Gross Receipts)	\$ 11,463,170,471	\$ 11,483,396,386	\$ (20,225,915)
Scoreboard SM (Gross Receipts)	313,113,033	349,360,410	(36,247,377)
Scratch-its SM Instant Tickets	196,029,843	197,076,904	(1,047,061)
Keno	98,927,011	99,008,641	(81,630)
Powerball [®]	40,541,274	41,100,301	(559,027)
Megabucks SM	29,242,902	29,535,560	(292,658)
Mega Millions [®]	33,631,835	33,272,725	359,110
Raffle SM	2,499,850	2,499,970	(120)
Win For Life SM	3,820,432	3,844,682	(24,250)
Lucky Lines SM	2,282,856	2,139,029	143,827
Pick 4 SM	1,996,712	2,018,640	(21,928)
Total Revenue	<u>12,185,256,219</u>	<u>12,243,253,248</u>	<u>(57,997,029)</u>
Prize Expense	11,149,177,247	11,214,729,579	65,552,332
Net Revenue	<u>1,036,078,972</u>	<u>1,028,523,669</u>	<u>7,555,303</u>
Direct Expenses			
Retailer Commissions	239,197,863	239,804,239	606,376
Game Vendor Charges	19,233,957	21,417,701	2,183,744
Tickets	3,497,439	3,317,127	(180,312)
Advertising	5,577,470	8,462,467	2,884,997
Sales Support	373,821	659,850	286,029
Game Equipment/Parts & Maintenance	4,849,767	8,637,639	3,787,872
Depreciation	19,648,759	21,209,148	1,560,389
Total Direct Expenses	<u>292,379,076</u>	<u>303,508,171</u>	<u>11,129,095</u>
Gross Profit	<u>743,699,896</u>	<u>725,015,498</u>	<u>18,684,398</u>
Indirect Revenue			
Other Income (Loss)	(5,889,309)	9,000,000	(14,889,309)
Indirect Expenses			
Public Information	837,416	1,382,144	544,728
Research	(119,323)	512,800	632,123
Personal Services	76,415,555	58,334,332	(18,081,223)
Services and Supplies	25,344,266	46,750,152	21,405,886
Depreciation	2,912,658	3,437,333	524,675
Interest Expense	240,143	300,000	59,857
Total Indirect Expenses	<u>105,630,715</u>	<u>110,716,761</u>	<u>5,086,046</u>
Net Profit	<u>\$ 632,179,872</u>	<u>\$ 623,298,737</u>	<u>\$ 8,881,135</u>

⁽¹⁾ Budget adopted by the Lottery Commission and adjusted by the Economic and Revenue Forecasts published by the Department of Administrative Services throughout the year.



Other Reports

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

The Honorable Kate Brown, Governor of Oregon
MardiLyn Saathoff, Chair, Oregon State Lottery Commission
Barry Pack, Director, Oregon 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 Oregon State Lottery, an enterprise fund of the State of Oregon, as of and for the year ended June 30, 2021, and the related notes to the financial statements, which collectively comprise the Oregon State Lottery's basic financial statements, and have issued our report thereon dated December 29, 2021.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Oregon 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 Oregon State Lottery's internal control. Accordingly, we do not express an opinion on the effectiveness of the Oregon 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 entity's financial statements will not be prevented, or detected and corrected on a timely basis. A **significant deficiency** is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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

deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

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

Office of the Secretary of State, Audits Division

State of Oregon
December 29, 2021