



FISCAL YEAR 09  
**ANNUAL  
REPORT**



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## HIGHLIGHTS OF FY2009

Sales .....	<b>\$1.293 billion</b>
Transfers to Education .....	<b>\$411 million*</b>
Number of Retailers.....	<b>6009</b>
Powerball Jackpot Winner.....	<b>Jeff Wilson</b>
New Game.....	<b>Carolina Pick 4</b>
Financial Audit .....	<b>No material findings</b>
Security Audit .....	<b>No material findings</b>

\*This number is the actual cash transfer.



# COMMISSION CHAIR'S NOTE



I was pleased to accept the appointment as Chairman from Governor Easley mid-year due to the departure of the previous chairman. The North Carolina Education Lottery (NCEL) completed our 2009 fiscal year in excellent shape. Sales increased 20 percent over fiscal year 2008. This increase in sales allowed the NCEL to transfer \$411 million to the education programs in North Carolina supported by the lottery. This was \$26 million more than had been budgeted by the Commission.

On April 17, the Commission added Carolina Pick 4 to the array of games offered. Carolina Pick 3 sales and our other games remained strong even with this addition.

The Commission asked that the Legislature make a few changes to the Lottery Act, NCGS Section 18C. We needed some modifications to streamline operations and to implement some cost saving improvements. H205 (Lottery Act Changes) passed the House by a vote of 110 to 4 and the Senate unanimously. Legislators cited the efficient and productive operations of our lottery as the major reason for supporting our legislative requests.

Once again our Executive Director Tom Shaheen and his staff have earned a clean financial audit, receiving an unqualified opinion, the highest rating possible. In addition, the NCEL again received a clean security audit with no significant findings. This was recognized by two outside awards: one from the Government Finance Officers Association of the United States and Canada, a non-industry group which presented the NCEL with its Certificate of Achievement for Excellence in Financial Reporting for our FY08 comprehensive annual financial report. Our second award was from an industry group, the North American Association of State & Provincial Lotteries Standards Initiative, under the Best Practice Quality Assurance of Product Development in the Lottery Industry for Acceptance Testing.

Our Commissioners share a wealth of expertise in diverse fields and apply it to our business. I thank them for their efforts, support and leadership. It is a pleasure to continue to work with an organization dedicated to operating with expertise, dedication, integrity and security. Our staff remains focused on increasing sales in these difficult times in order to maximize the return to education with no adverse issues.

The NCEL Commission looks forward to another outstanding year in FY 2010.



## NCEL COMMISSION

**Robert Farris, Jr. – Commission Chair**  
Attorney, Farris and Farris, P.A., Wilson  
term expires 8/31/13  
(appointed by Governor Easley)

**Carla Archie**  
Assistant General Counsel, Wells Fargo  
& Company, Charlotte  
term expires 8/31/11  
(appointed by Governor Easley)

**William Dowdy, III**  
Retired, NC State Bureau of Investigation,  
Greenville  
term expires 8/31/11  
(appointed by Governor Easley)

**Lawrence Spears**  
Owner/Broker, Raleigh Investment Real  
Estate, Raleigh  
term expires 8/31/11  
(appointed by Governor Perdue)

**Pamela Whitaker**  
President, Key Resources, Inc.,  
term expires 8/31/12  
(appointed by Governor Easley)

**Bridget-Anne Hampden** (not pictured)  
President and CEO of JHR &  
Associates, LLC, Charlotte  
term expires 8/31/12  
(appointed by President Pro Tem of the Senate)

**Max Cogburn** (not pictured)  
Attorney, Asheville  
term expires 8/31/12  
(appointed by Speaker of House)

**Dr. Fort** (not pictured)  
Chancellor Emeritus, A&T State University  
term expires 8/31/13  
(appointed by Speaker of the House)

**Norwood Clark, Jr.** (not pictured)  
CPA  
term expires 8/31/13  
(appointed by President Pro Tem of the Senate)

# EXECUTIVE DIRECTOR'S NOTE



Although the lottery is serious business, I've always felt at the same time it should be fun. This year was fun for North Carolina. We added a new game, tried some new promotions, and gave away some great prizes. Along with the fun goes a lot of work and the North Carolina Education Lottery (NCEL) staff certainly had their share of work this year.

Our efforts resulted in total sales topping \$3 billion since inception; quarterly transfers hitting all time highs; final FY09 transfer exceeding our budgeted return by \$26 million; and the number of retailers hitting the 6,000 mark. Sales for the year topped \$1.293 billion. Transfers were \$411 million.

Along the way we gave away Ford F-150 trucks in a Carolina Cash 5 promotion. We sent five North Carolina players to Hollywood to participate in the Deal or No Deal game. We had five second chance drawings associated with the \$130 Million Blockbuster game to pick ten finalists for the grand prize drawing of \$50,000 a year for life. We gave away Harley-Davidson® Fat Bob® motorcycles both on the Harley-Davidson® ticket and as a prize in a second chance drawing. And we added Carolina Pick 4 to our game offerings, bringing the NCEL to a full complement of basic games.

But the most exciting and fun happening was Jeff Wilson of Kings Mountain winning the Powerball jackpot of \$88 million. Jeff is a young man who is attending graduate school. His father bought tickets and let each member of the family choose one. Jeff chose the ticket that turned out to be the jackpot winner.

I would like to commend our retailers for their dedication to and efforts in promoting and selling lottery games. They came up with new ways to engage players and keep the games interesting. Players showed their interest by breaking previous sales records and their enthusiasm by entering second chance drawings at record numbers.

The NCEL Commission provided guidance and oversight and gave freely of their time. This Commission serves as non-compensated appointed volunteers. The staff stayed energized bringing in new retailers, promoting games, greeting big winners, and implementing new games. This was a very positive year for everyone associated with the lottery. We look forward to outperforming this past year in FY10 knowing it will be a challenging task.

*Thomas N. Shaheen*



## NCEL SENIOR STAFF

- |                                                                                                                                                                                                                                                                                                                                                                                                                                                             |                                                                                                                                                                                                                                                                                                                                                                                                                         |                                                                                                                                                                                                                                                                                                                                                          |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><b>1. Tom Shaheen</b><br/>Executive Director</p> <p><b>2. Sam Hammett</b><br/>Deputy Executive Director, Sales</p> <p><b>3. Quan Kirk</b><br/>Director, Legal Services</p> <p><b>4. Alice Garland</b><br/>Deputy Executive Director<br/>Legislative and Corporate Communications</p> <p><b>5. Deborah Doty</b><br/>Deputy Executive Director,<br/>Management Information and Gaming Systems</p> <p><b>6. Joe Norman</b><br/>Director, Gaming Systems</p> | <p><b>7. Lou Ann Russell</b><br/>Deputy Executive Director, Marketing and Advertising</p> <p><b>8. Pamela Walker</b><br/>Director, Corporate Communications</p> <p><b>9. Terri Avery</b><br/>Director, Sales</p> <p><b>10. Walter Ingram</b><br/>Director of Sales Development, Sales</p> <p><b>11. Penny Railey</b><br/>Director, Marketing</p> <p><b>12. Margaret Spindola-Bode</b><br/>Director, Human Resources</p> | <p><b>13. Tony Chung</b><br/>Director, MIS</p> <p><b>14. Nikki Howard</b><br/>Internal Auditor</p> <p><b>15. Jerry Carter</b><br/>Director, Security</p> <p><b>16. Jim Knight</b><br/>Director, Finance</p> <p><b>17. Fenita Shepard</b><br/>Deputy Executive Director, Legal and Security</p> <p><b>18. Bill Enlow</b><br/>Director, Administration</p> |
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# WHAT THE LEGISLATION SAYS

The NCEL transferred \$411 million to education programs in FY09, bringing the grand total to over \$1.136 billion. This amount represented \$26 million more than the Commission budgeted. The dollars were disbursed to the four programs as directed by law: pre-school for at-risk four year olds, class size reduction in grades K through 3, school construction and need-based college scholarships.

The disbursement process involves the NCEL transferring net proceeds quarterly to the Office of State Budget and Management who then disburses the funds to the four education programs. The Department of Public Instruction (DPI) administers the funds with the exception of need-based college scholarships that are administered by the State Education Assistance Authority (SEAA).

DPI allocates funds in the following manner. The More at Four program, the designated pre-kindergarten program for at-risk four year olds, receives their regular funding allotments from the DPI as do school systems for the class size reduction dollars. DPI posts the school construction dollars on their webpage and banks the funds for the counties that choose to do so. Each county decides when and how to use their school construction dollars. During FY09, county school construction projects grew from 223 to 458, all utilizing lottery dollars.

SEAA awards scholarships for the next school year with the current fiscal year dollars.

Students apply for an education lottery scholarship by completing the Free Application for Federal Student Aid (FAFSA). Any student who qualifies for the federal Pell grant will receive an education lottery scholarship.

**“Receiving the lottery scholarship has relieved some of the stress about paying for school. It helps, especially in my senior year, to be able to keep my focus on my studies versus worrying about financial pressures.” – Samantha Cibelli**



# COUNTY TOTALS FY09

ALAMANCE	\$5,941,803	CURRITUCK	927,501	LEE	2,848,527	ROCKINGHAM	3,728,543
ALEXANDER	1,537,566	DARE	1,278,598	LENOIR	2,744,248	ROWAN	5,461,048
ALLEGHANY	517,918	DAVIDSON	6,557,642	LINCOLN	3,035,919	RUTHERFORD	2,914,919
ANSON	1,263,159	DAVIE	1,914,193	MACON	1,371,620	SAMPSON	3,433,043
ASHE	1,151,482	DUPLIN	2,580,862	MADISON	693,784	SCOTLAND	2,160,838
AVERY	770,282	DURHAM	8,340,622	MARTIN	1,096,134	STANLY	2,926,403
BEAUFORT	1,997,143	EDGECOMBE	2,704,583	MCDOWELL	1,826,870	STOKES	2,064,777
BERTIE	1,039,220	FORSYTH	12,965,293	MECKLENBURG	33,586,120	SURRY	3,215,699
BLADEN	1,847,343	FRANKLIN	2,006,565	MITCHELL	596,612	SWAIN	617,482
BRUNSWICK	3,644,794	GASTON	9,238,103	MONTGOMERY	1,511,942	TRANSYLVANIA	936,850
BUNCOMBE	7,099,651	GATES	515,144	MOORE	2,667,648	TYRRELL	167,356
BURKE	4,310,496	GRAHAM	411,639	NASH	4,366,224	UNION	9,592,852
CABARRUS	8,222,794	GRANVILLE	2,230,819	NEW HANOVER	6,986,930	VANCE	2,062,546
CALDWELL	3,252,500	GREENE	1,018,462	NORTHAMPTON	950,902	WAKE	32,690,375
CAMDEN	497,117	GUILFORD	21,217,790	ONSLOW	6,839,356	WARREN	774,965
CARTERET	2,220,092	HALIFAX	2,538,577	ORANGE	4,464,078	WASHINGTON	651,443
CASWELL	888,780	HARNETT	4,698,164	PAMLICO	460,541	WATAUGA	1,303,218
CATAWBA	6,426,817	HAYWOOD	2,059,372	PASQUOTANK	1,602,857	WAYNE	5,916,927
CHATHAM	2,347,879	HENDERSON	3,309,485	PENDER	2,187,945	WILKES	3,388,518
CHEROKEE	1,092,355	HERTFORD	1,074,566	PERQUIMANS	607,417	WILSON	3,192,465
CHOWAN	648,971	HOKE	2,750,457	PERSON	1,531,965	YADKIN	1,716,984
CLAY	413,738	HYDE	195,972	PITT	6,707,129	YANCEY	630,394
CLEVELAND	4,872,224	IREDELL	6,510,537	POLK	786,586	UNKNOWN	113,178
COLUMBUS	3,115,814	JACKSON	1,020,719	RANDOLPH	5,786,287	DPI ADMIN COST	3,959,982
CRAVEN	3,738,451	JOHNSTON	7,672,255	RICHMOND	2,287,716	<b>FY09 TOTAL</b>	<b>\$390,572,219</b>
CUMBERLAND	16,354,374	JONES	475,431	ROBESON	7,979,943		



# INSTANT SCRATCH-OFF TICKETS

FY09 was the first full year of increased prize payouts for instant tickets and it proved that paying more in prizes delivers a big payoff in sales. Instant ticket sales increased 26 percent from FY08 which had the benefit of the increased payouts for five months. More impressively, sales increased 62 percent from FY07 when payouts were at the initial lower rate. Instant ticket sales have now jumped to 62 percent of total sales. In FY07, they were 56% of total sales. For FY09, instant ticket sales were \$798,676,404. This played a major role in the NCEL's increase of \$26 million over budget to education.

The \$5 and \$10 price points on instant tickets represented the greatest percentage of sales: 26.52 percent and 33.06 percent respectively. "\$200,000 Jackpot," "Megabucks," "Totally Topaz 7's," and "Dazzlin' Diamond 7's" were the most popular \$5 tickets. "\$130 Million Blockbuster," "Lifetime Riches" and "\$100 Million Cash Spectacular" were the most popular \$10 tickets.

Instant ticket sales were enhanced by several exciting second chance drawings. The "Deal or No Deal™" ticket included a drawing for five players to go to Hollywood for a chance to play a non-broadcast version of the game with Howie Mandel. Players entered 159,236 tickets in the second chance draw. While none of the North Carolina players were selected to play the broadcast game, they all had a once in a lifetime Hollywood experience.

The "\$130 Million Blockbuster" ticket included five preliminary draws to pick ten finalists for the grand prize drawing of \$50,000 a year for life. By the end of the fiscal year, eight of the ten finalists had been drawn. We received a total of 937,500 entries for these five draws. After the close of the fiscal year, we conducted the grand prize drawing at WRAL studios and showed a tape of the drawing to television audiences across the state. Darlene MacQuaide won \$50,000 a year for life. The other finalists won a one-time prize ranging from \$1,000 up to \$25,000.

The "Harley-Davidson®" ticket had six Fat Bob® motorcycles on the ticket and the opportunity to win a Fat Bob® in one of three second chance drawings. North Carolina is definitely motorcycle country based on the popularity of this ticket year after year. Players entered 525,000 tickets in these draws. As an added feature, players could submit any \$5 non-winning instant scratch-off ticket prior to this game launch and be entered into a draw for a 10th Fat Bob® motorcycle. We awarded this Fat Bob® motorcycle at a special televised half-time show at the Charlotte Bobcats vs. LA Lakers game.

Another popular ticket was the "Monopoly™" ticket with a tagline of "scratch and go directly to fun." This ticket was North Carolina's first foray into tickets patterned after board games. It turned out to be the number one seller for \$3 tickets.



# CAROLINA PICK 3

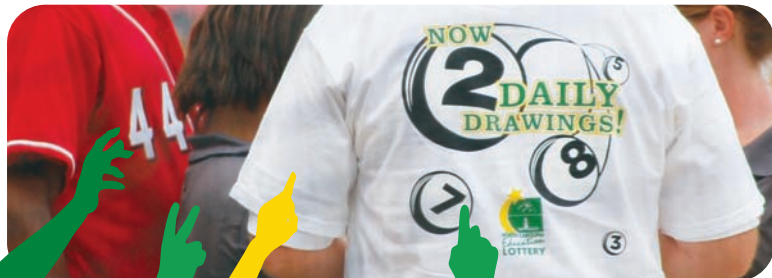
Carolina Pick 3 is giving Powerball stiff competition for the number two slot in game sales. Carolina Pick 3 sales topped out at \$208,883,766. This was an impressive 42 percent increase over FY08. Carolina Pick 3 sales now represent 16 percent of total sales.

The mid-day draw that was added fourth quarter FY08 proved to be as popular as players said it would be. The second daily draw is holding strong and appears to have enhanced the evening draw.

Triple numbers, a perennial player favorite, hit three times during the year. Players love to play triple numbers. Each time after they hit, we see a spike in sales.

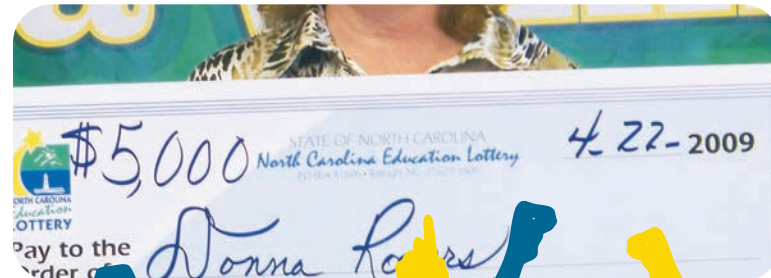
When we added Carolina Pick 4 in April, we also added the "combo" option to Carolina Pick 3. This is a play that allows players to play every combination of a 3-digit number in exact order on a single ticket.

Carolina Pick 3 and Carolina Pick 4 players have a different style of playing from the other two online games. Carolina Pick 3 players quick pick their numbers only eight percent of the time and Carolina Pick 4 players 14 percent of the time where Carolina Cash 5 players use quick pick 62 percent of the time and Powerball players 71 percent of the time.



# CAROLINA PICK 4

You asked for it...You got it. Players began asking for Carolina Pick 4 soon after the NCEL was up and running, so we felt it fitting to use that slogan to let players know we were listening. This was the final game to bring the NCEL's game offerings to a complete basic set. We kicked off Carolina Pick 4 on April 17 at 5am and conducted the first drawing that evening.



Carolina Pick 4 is a four-digit game where players pick a number between 0-0-0-0 and 9-9-9-9. They can play Exact, Any, 50/50 or Combo. They can win from \$100 up to \$5,000.

In just two and a half months, Carolina Pick 4 sales were \$15,793,159. This represented one percent of total sales for the year. It is not unusual to have twenty players a week win at the highest level of \$5,000.

We began with an evening draw for Carolina Pick 4 that occurs at the same time as the other evening draws. In conjunction with the addition of this game, WRAL-TV, our official lottery drawing station, moved the draw to a studio that allows for multiple backgrounds, giving us the flexibility to create awareness about new marketing initiatives.

WRAL-TV in Raleigh is the official lottery draw station. The nightly draw is televised live from the studio. The mid-day draw is taped and available to players to view on the web shortly after the draw. Our statewide drawing station network includes WITN-TV in Greenville, WCNC-TV in Charlotte, WILM-TV in Wilmington and WYCW-TV in Western North Carolina. And, this year we added WXLV-TV in Winston-Salem to the network. This covers the Triad market that had previously been unable to watch the evening draw live.



# CAROLINA CASH 5

"Get Truckin'" was the message to Carolina Cash 5 players as the NCEL gave away five Ford F-150s in a promotion. Players purchased a \$5 Carolina Cash 5 ticket and submitted 352,000 entries over five draws. These trucks proved to be very popular with our players. We delivered the trucks at the store where the player purchased the ticket. We also provided each winner with a \$1,000 gas card.

Overall Carolina Cash 5 sales experienced a slight increase over FY08. Sales finished at \$60,011,218 and represented five percent of total sales for the NCEL.

Eighty-nine players won the top prize in FY09 with 54 of those winning \$100,000 or more. The top prize was shared by multiple winners 12 times. George Baker of Hickory won the largest top prize of \$587,361. The top prize rolled 11 times to reach this amount, showing that Carolina Cash 5 gets exciting fast. The average top prize won in FY09 was \$179,013.

Carolina Cash 5 drawings occur nightly in concurrence with the Carolina Pick 4 and the nightly Carolina Pick 3 drawings.





# NORTH CAROLINA POWERBALL

How exciting is winning \$88.1 million? According to Jeff Wilson, extremely! Wilson's win was truly the luck of the draw. His father purchased Powerball tickets at the Petro Express on Cleveland Avenue in Kings Mountain and let each of his adult children pick a ticket. Wilson picked the winning ticket but plans on sharing with his family.

Wilson elected to take the lump sum cash payment of \$42.4 million, which after taxes is worth approximately \$28.8 million as opposed to \$88.1 million over 30 years. "I didn't believe my dad when he told me that I had won and I think I'm still in disbelief," Wilson said. When asked what he thought may be his first purchase he said, "Maybe a house or a car." Wilson added that the money will also be helpful for graduate school.

Wilson was the second Powerball jackpot winner in North Carolina since inception. Jackie Alston won \$74.5 million in FY07.

In addition to Wilson, there were 265 big winners in FY09 ranging from \$1 million to \$10,000. Two hundred twenty-

six winners matched four out of five white balls and the Powerball to win \$10,000 to \$50,000. Of those, 74 paid an additional dollar to Power Play and had their \$10,000 win multiplied by a factor of 2, 3, 4, or 5. Thirty-nine winners matched all five white balls to win \$200,000 to \$1 million. Of those, 18 Power Played and had their winnings multiplied.

The Powerball game matrix changed in January, 2009. White balls now range from number 1 to 59 while the Powerball ranges from number 1 to 39. In addition to the matrix change, the multiplier for matching the five white balls is an automatic 5, growing that prize amount to \$1 million. All set prizes and Power Play prizes, including the Match 5+0 prize, may become pari-mutuel if claims exceed available prize fund.

Powerball sales in FY09 were \$209,746,679. This represents a nine percent decrease from FY08. Powerball sales are now 16 percent of total sales. Adding to sales were several large jackpots: September 24, 2008 the jackpot hit \$176 million and May 27, 2009 it hit \$222 million.



# NCEL GETTING THE WORD OUT



From advertisements to sports promotions, from infomercials to special events, the NCEL's promotional efforts covered a wide array of activities. These activities accomplish a great deal by getting the lottery message out to the public, educating players about the games, supporting community activities, educating the public about the contribution of the lottery to education, and creating awareness of the lottery. The Marketing staff implemented 26 sponsorships equating to participation in 30 events statewide, with 120 on-site sales days in the field.

The advertising effort focused on building the instant scratch-off ticket brand with the theme "More Prizes, More Fun." We introduced Game Show Gary™ with the Carolina Cash 5 Ford F-150 giveaway. He became our icon or brand identifier and appeared in a number of lottery advertisements. His lively game show host jacket and sparkling teeth quickly became associated with NCEL products.

We also taped and ran infomercials on a Raleigh TV station. These infomercials, each lasting two minutes, ran weekly on Friday mornings. Using lottery staff only, the infomercials showcased new games, second chance

drawings, beneficiary and big winner information, and community responsibility actions. Due to the length of the spots, this new medium gave us the opportunity to deliver our message in a more thorough manner.

We built on efforts from previous years by continuing sponsorships with several very successful sports entities including Lowe's Motor Speedway and the Charlotte Bobcats. Sponsorship of the NCEL 200 Craftsman Truck Series allowed us to connect with NASCAR® fans. In North Carolina, NASCAR® is the second-highest rated sport behind football, based on television rankings. Our sponsorship with the Charlotte Bobcats included a live half-time show at the Bobcats vs. LA Lakers game, broadcasted live on FSN Carolinas where we awarded a lucky winner with a Harley-Davidson® Fat Bob® motorcycle. We also partnered with minor league baseball across the state, with minor league hockey and with the popular CIAA basketball tournament. In addition, we sponsored on-ice "Power Play" promotions at multiple Carolina Hurricanes hockey games. All of these sponsorships allowed the NCEL to reach a large fan base of new and existing lottery players.



We continued our participation in special events across the state at such venues as the Azalea Festival, Dogwood Festival, Cleveland County Fair, Mule Days, Dixie Classic Fair, Riverfest, MUMfest and the Seafood Festival. These special events give us a great opportunity to interact with players across the state at the local level and engage in informal conversations. We also meet citizens with no previous experience playing the lottery who are eager to learn more about our games and the education programs we support.

Promotional efforts also included fun and exciting second chance drawings. We gave away five Ford F-150s, Hollywood trip and Deal or No Deal™ game participation to five players, and four Harley-Davidson® Fat Bob® motorcycles through special drawings. In addition, we picked finalists for \$130 Million Cash Spectacular grand prize drawing of \$50,000 a year for life.

# OUR WINNING RETAILERS

The partnership between the NCEL and its retailers is invaluable to the success of the lottery. Lottery retailers are on the front line everyday providing the service of selling tickets; cashing out winning tickets under \$600; and helping players understand the games.

The number of retailers selling tickets grew from 5,860 on June 30, 2008 to 6,009 on June 30, 2009. Retailers receive a seven percent commission for selling lottery tickets. In FY09, we paid \$90,366,111 in commissions. The average commission paid to retailers was \$17,242.

We proudly take notice when our retailers do something special. Twice a year we recognize retailers that have increased their sales by the highest percentage in the region compared to the previous quarter. They earn the title of "Stellar Seller." Also, one location per region is named a S.T.A.R. (Spectacular Technique Achieving Retailer) based on our sales representative recommendations for a store's unique sales promotion technique.



## STELLAR SELLERS (January to June)

RETAILER NAME	REGION	LOCATION	PERCENT CHANGE
Jonas Ridge Outfitters	Asheville	Jonas Ridge	92%
East Mountain Kwik Mart	Asheville	Rutherfordton	79%
Sunshine Mart	Charlotte	Conover	157%
A&G Express	Charlotte	Monroe	107%
Gill's Grocery Store	Greensboro	Eden	226%
67 Gas	Greensboro	Pfafftown	120%
Newport BP	Greenville	Newport	135%
Food Lion #1368	Greenville	New Bern	78%
Rose Gin Bait & Tackle	Raleigh	Henderson	127%
Food Lion #842	Raleigh	Yanceyville	106%

## S.T.A.R. (Spectacular Technique Achieving Retailer)

RETAILER NAME	REGION	LOCATION
Mr. Pete's Market VI	Asheville	Etowah
Skyway Exxon	Charlotte	Monroe
Nathans Creek General Store	Greensboro	Jefferson
Fuel Doc #12	Greenville	Greenville
Tommy's Mini Mart	Raleigh	Durham

## STELLAR SELLERS (July to December)

RETAILER NAME	REGION	LOCATION	PERCENT CHANGE
Mountain Energy #110	Asheville	Franklin	60%
Shop & Save #4	Asheville	Morganton	55%
Dollars 'R' Us	Charlotte	Charlotte	83%
Food Lion #1213	Charlotte	Seven Lakes	79%
Casablanca Stores	Greensboro	Greensboro	126%
Mahima Groceries	Greensboro	Greensboro	98%
The Community Store	Greenville	Ocracoke	136%
Charlie's Grill & Grocery	Greenville	Greenville	95%
La Jalisco	Raleigh	Sanford	202%
Oh' Mulligans	Raleigh	Wake Forest	164%

## S.T.A.R. (Spectacular Technique Achieving Retailer)

RETAILER NAME	REGION	LOCATION
Union Mills Country Market	Asheville	Union Mills
Lil Market	Charlotte	Gastonia
Jay's Place	Greensboro	Winston-Salem
Mike's Mini Mart	Greenville	Chocowinity
Tobacco Road Outlet #24	Raleigh	Wilson



# COMMUNITY SUPPORT

The NCEL continued to emphasize our critical community messages: play responsibly and no sales to minors. In FY09 we were able to use a new medium to get these messages out to the public: infomercials. Two of our infomercials dealt with community responsibility.

The play responsibly message is one that we repeat frequently. It is on all point-of-sale materials and in our television and radio ads. We provide the problem gambling helpline toll-free number on all printed materials. In talking with players, we remind them that playing the lottery is entertainment and fun and should be approached as such. One of the infomercials ran on the Friday preceding Problem Gambling Awareness Week and it emphasized this message of play responsibly.

Throughout the year, we provide \$1 million annually to the Department of Health and Human Services (DHHS) for their problem gambling program. DHHS uses the funds to cover the cost of a toll-free helpline number and to pay for counseling services for folks who call the helpline and request assistance.

We have made "No sales to minors" a cornerstone message with our retailers. Our sales representatives wore shirts bearing that message. We provided retailers with stickers for their terminals and for the back of their ticket dispensers. We put reminders in our retailer newsletter. We made buttons for retailers with this message imprinted on them. We were vigorous in pushing this message.

The NCEL has an active minority participation effort. Our staff, at the end of the fiscal year, was 70.1 percent minority with 32.7 percent female, 32.3 percent African-American, 3.2 percent Hispanic and 1.9 percent Asian. We conducted our annual Minority Business Conference in order to insure that we are reaching out to minority businesses with information on how to do business with the education lottery. Fifteen percent of our business is conducted with minority vendors including disabled vendors but excluding our advertising contract. If we include our advertising contract, the percentage increases

to 72.34. We conducted a minority internship program and provided lottery experience to three summer interns.

We also continue our participation in the Amber Alert program, the national program to help locate missing children. We receive the Amber Alert messages and immediately forward a message to all lottery terminals statewide which the retailers can print out and post. We also change the terminal screen message which can be read by any customer in the store and post notification on our player website.



# BY THE NUMBERS

## FY09 SALES BY REGION

REGION	Instant	Powerball	Pick 3	Pick 4	Cash 5	Total
Asheville	\$58,155,026.00	\$13,801,764.00	\$3,468,004.00	\$330,571.50	\$3,350,043.00	\$79,105,408.50
Greensboro	122,450,110.00	33,079,265.00	23,445,265.50	1,992,049.50	9,310,507.00	190,277,197.00
Charlotte	210,757,308.00	60,717,044.00	28,700,975.50	2,535,625.00	14,639,041.00	317,349,993.50
Raleigh	302,573,717.00	79,253,975.00	104,838,616.00	7,444,190.00	23,898,420.00	518,008,918.00
Greenville	104,740,243.00	22,894,631.00	48,430,905.00	3,490,723.00	8,813,207.00	188,369,709.00
<b>TOTAL</b>	<b>\$798,676,404.00</b>	<b>\$209,746,679.00</b>	<b>\$208,883,766.00</b>	<b>\$15,793,159.00</b>	<b>\$60,011,218.00</b>	<b>\$1,293,111,226.00*</b>
<b>% OF SALES</b>	<b>61.76%</b>	<b>16.22%</b>	<b>16.15%</b>	<b>1.22%</b>	<b>4.64%</b>	<b>100.00%</b>

## SALES TABLE

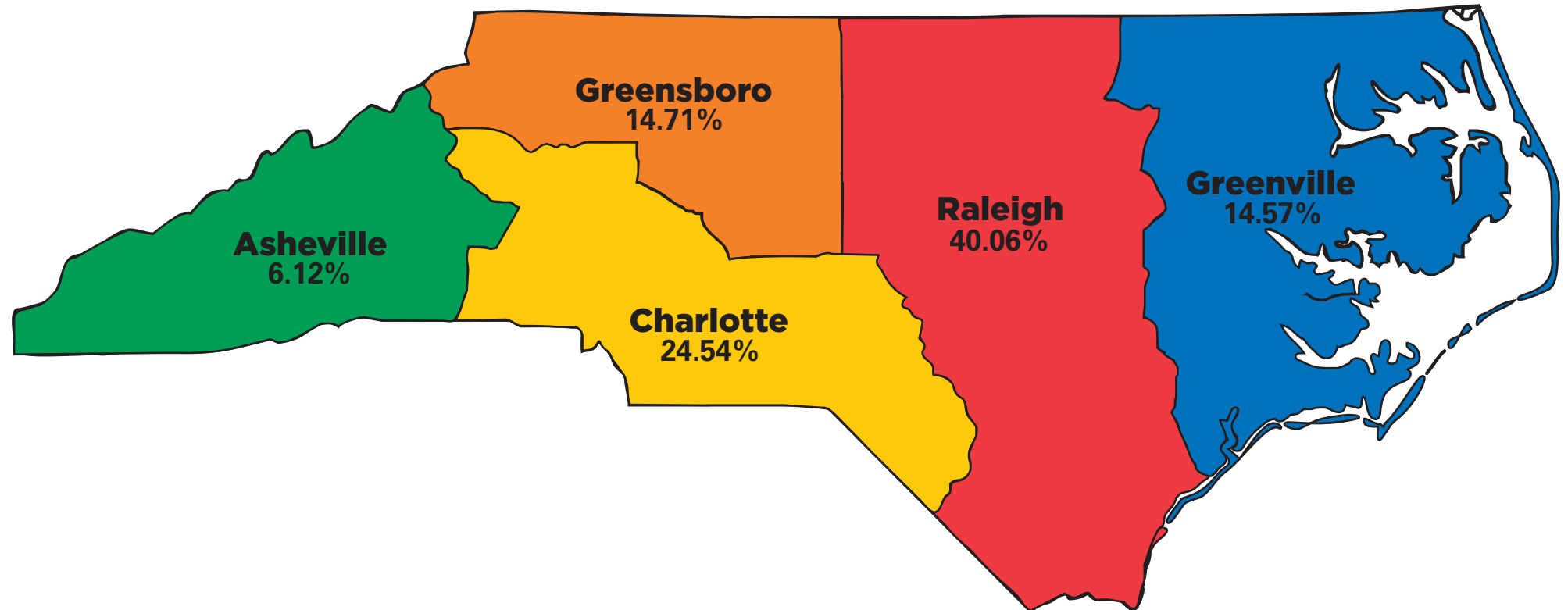
	Instant	Powerball	Pick 3	Pick 4	Cash 5	Raffle	Total
<b>FY 2009 (7/1-6/30)</b>	\$798,676,404.00	\$209,746,679.00	\$208,883,766.00	\$15,793,159.00	\$60,011,218.00	\$0.00	\$1,293,111,226.00
<b>FY 2008 (7/1-6/30)</b>	635,880,115.00	229,255,174.00	147,158,304.00	0.00	58,516,249.00	7,369,240.00	1,078,179,082.00
<b>FY 2007 (7/1-6/30)</b>	490,564,474.00	258,967,883.00	89,541,216.50	0.00	36,501,699.00	10,000,000.00	885,575,272.50
<b>FY 2006 (03/30-06/30)</b>	198,454,677.00	27,317,594.00	0.00	0.00	0.00	0.00	225,772,271.00
<b>Life to Date</b>	2,123,575,670.00	725,287,330.00	445,583,286.50	15,793,159.00	155,029,166.00	17,369,240.00	3,482,637,851.50
<b>% incr prev yr 09-08</b>	26	-09	42		03		20
<b>% incr prev yr 08-07</b>	30	-11	64		60	-26	22
<b>% incr 09-07</b>	63	-19	133		64		46
<b>% yr sales 09</b>	62	16	16	01	05	00	100
<b>% yr sales 08</b>	59	21	14	00	05	01	100
<b>% yr sales 07</b>	55	29	10	00	04	01	100

## THREE YEAR SALES COMPARISON

	2007	2008	2009
Instant	\$490,564,474	\$635,880,115	\$798,676,404
Powerball	258,967,883	229,255,174	209,746,679
Pick 3	89,541,217	147,158,304	208,883,766
Pick 4			15,793,159
Cash 5	36,501,699	58,516,249	60,011,218
Raffle	10,000,000	7,369,240	
<b>TOTAL</b>	<b>885,575,273*</b>	<b>1,078,179,082*</b>	<b>1,293,111,226*</b>

\* See notes to Financial Statements Note 3.

## % OF SALES BY REGION



## THREE YEAR BENEFICIARY COMPARISON\*\*

2007	2008	2009
\$325,357,596	\$350,012,384	\$410,876,050

\*\*These numbers are actual cash transfers.



Beth A. Wood, CPA  
State Auditor

**STATE OF NORTH CAROLINA**  
**Office of the State Auditor**

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**AUDITOR'S TRANSMITTAL**

The Honorable Beverly Eaves Perdue, Governor  
Members of the North Carolina General Assembly  
North Carolina State Lottery Commission

This report presents the results of the financial statement audit of the North Carolina Education Lottery (the Lottery), an enterprise fund of the State of North Carolina, for the period ended June 30, 2009. Cherry, Bekaert, and Holland, L.L.P. performed this audit under contract with the Office of the State Auditor and their report is submitted herewith.

General Statute 18C-116 requires the State Auditor to conduct an annual audit of the Lottery's accounts and transactions. General Statute 147-64.7 allows the State Auditor to obtain the services of independent public accountants to carry out its duties and functions.

*North Carolina General Statutes* require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.

Beth A. Wood, CPA  
State Auditor



**Independent Auditors' Report**

To the Commissioners  
North Carolina Education Lottery  
Raleigh, North Carolina

We have audited the accompanying statements of net assets of the North Carolina Education Lottery (NCEL), a major enterprise fund of the State of North Carolina as of June 30, 2009, 2008 and 2007, and the related statements of revenues, expenses and changes in fund net assets and cash flows for the years then ended. These financial statements are the responsibility of the NCEL's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

As discussed in Note 2, the financial statements present only the NCEL and do not purport to, and do not, present fairly the financial position of the State of North Carolina, as of and for the years ended June 30, 2009, 2008, and 2007, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the NCEL as of June 30, 2009, 2008 and 2007, and the respective changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated October 15, 2009 on our consideration of the NCEL's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

The management's discussion and analysis is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

CHERRY, BEKAERT & HOLLAND, L.L.P.

Raleigh, North Carolina

October 15, 2009

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## JUNE 30, 2009, 2008 AND 2007

The following is a discussion and analysis of the financial performance of the North Carolina Lottery Commission [aka, North Carolina Education Lottery (NCEL)] for the fiscal years ended June 30, 2009, 2008 and 2007 and should be read in conjunction with the financial statements, including the footnotes. This report consists of three parts: management's discussion and analysis, the basic financial statements and the notes to the financial statements. Included below and on the following pages are the financial highlights, summary of contributions to the state, and summary results of operations for years ended June 30, 2009, 2008 and 2007.

### FINANCIAL HIGHLIGHTS

For fiscal year 2009, gross ticket sales again surpassed \$1 billion representing a \$214.9 million dollar increase over 2008. Total revenues earned for the NC Education Lottery fund were \$413.9 million, which represented an increase of \$65.6 million over fiscal year 2008. Other significant financial highlights include the following:

- Due to a full year of enhanced instant prize payouts, gross instant tickets sales for fiscal year 2009 grew by 25.6% over 2008.
- During the fiscal year we introduced two new instant games with chances to win lifetime annuities.
- We launched our third daily draw online game, Carolina Pick 4 in April.
- This year we increased the number of retailers to over 6,000 and provided service to our retailers on a regular basis.
- We created 45 new instant scratch-off games and released them every two to four weeks.

### OVERVIEW OF THE FINANCIAL STATEMENTS

This financial report is designed to inform the public and other interested parties of the financial results of the NCEL and show its accountability in meeting the legislated mandate to generate funds to further the goal of providing enhanced educational opportunities. Accordingly, the focus of the financial statements is determining funds available for payment to the State's Education Lottery Fund. It is important to note that most financial statement balances have a direct or indirect relationship to revenue. As lottery sales increase, the amount paid to the State's Education Lottery Fund also increases. Similarly, increases in revenues generally result in direct increases to cost of sales including, but not limited to, prize expense, retailer commission expense and gaming system vendor charges.

The NCEL is a major enterprise fund of the primary government of the State of North Carolina. The financial statements were prepared on the accrual basis of accounting in a manner similar to a private business entity. The principal operating revenues of the NCEL are sales of lottery products to retailers. Operating expenses include the cost of prizes, retailer commissions, gaming system vendor charges, personnel, and other administrative expenses.

Included in this report are the Statements of Net Assets as of June 30, 2009, 2008 and 2007, the Statements of Revenues, Expenses, and Changes in Fund Net Assets for the periods ended June 30, 2009, 2008 and 2007, and the Statements of Cash Flows for the periods ended June 30, 2009, 2008 and 2007.

As established in House Bill 1023, Section 18C-164, the NCEL transfers its net assets to the Office of State Budget and Management (OSBM) for credit to the State's Education Lottery Fund. Education Lottery Funds are distributed by OSBM in the following manner:

*"(1) A sum equal to fifty percent (50%) to support reduction of class size in early grades to class size allotments not exceeding 1:18 in order to eliminate achievement gaps and to support academic prekindergarten programs for at risk four year olds who would otherwise not be served in a high quality education program in order to help those four year olds be prepared developmentally to succeed in school.*

*(2) A sum equal to forty percent (40%) to the Public School Building Capital Fund in accordance with G.S. 115C 546.2.*

*(3) A sum equal to ten percent (10%) to the State Educational Assistance Authority to fund college and university scholarships in accordance with Article 35A of Chapter 115C of the General Statutes."*

### TOTAL ASSETS

Total assets at the end of fiscal year 2009 were \$62 million compared to \$81 million at the end of fiscal year 2008, representing a decrease of \$19 million.

Current assets decreased from \$79 million in 2008 to \$61 million in 2009, representing a decrease of \$18 million. This decline mainly resulted from a \$9 million decrease in accounts receivable in 2009 from 2008. This primarily represents amounts due from retailers for settlement of packs of tickets less commissions and prizes paid by the retailers. The reduction is essentially due to the timing of the end of the accounting week for billing and collections from our retailers at year end. Electronic Funds Transfer is used to sweep receivables weekly from retailer bank accounts that are set up in trust for the NCEL.

Current assets were also affected by a \$5.5 million decrease in cash and cash equivalents, which consist of deposits held by the State Treasurer in the State Treasurer's Short Term Investment portfolio. These decreases were due to the transfers to the State Education Fund before year-end.

The Short Term Investment portfolio has the general characteristics of a demand deposit account in that participants may deposit additional cash at any time and may withdraw cash at any time without prior notice or penalty. All deposits are combined with other State agencies and invested by the State Treasurer until needed to cover disbursements. Investments are limited to those authorized for the State's General Fund, pursuant to NC General Statute 147-69.1. Interest earned of \$3.6 million on these balances is recorded as non-operating revenue. Earnings on the accounts are credited on a monthly basis. The allocable share of the revenues arising from State Treasurer's Securities Lending Collateral program transactions are also included as non-operating revenue.

The NCEL's investment in capital assets, net of accumulated depreciation in 2009 was \$1.3 million which is approximately \$177,000 lower than 2008. The majority of capital asset investments were during our first full year of operation in 2007. The investment in capital assets includes game equipment, data processing equipment, telephone equipment, software and fixtures. The capitalization of all items including equipment, computers, and furniture follows North Carolina's Office of State Controller's policies. The NCEL defines capital assets as assets with an initial unit cost of \$5,000 or greater and an estimated useful life of two or more years. Capital assets are carried at cost less accumulated depreciation.

Additional information on the NCEL's capital assets can be found in Notes 2F and 5D to the financial statements.

The activity for capital assets for the year ended June 30, 2009 was (in thousands):

Category	Balance July 1, 2008	Increases	Decreases	Balance June 30, 2009
Capital Assets, depreciable				
Furniture	\$ 29	\$ -	\$ -	\$ 29
Equipment	2,239	367	-	2,606
Motorized equipment	67	-	-	67
Total capital assets, depreciable	2,335	367	-	2,702
Less accumulated depreciation for:				
Furniture	11	7	-	18
Equipment	813	523	-	1,336
Motorized equipment	24	14	-	38
Total accumulated depreciation	848	544	-	1,392
Total capital assets, depreciable, net	1,487	(177)	-	1,310
<b>Capital assets, net</b>	<b>\$ 1,487</b>	<b>\$ (177)</b>	<b>\$ -</b>	<b>\$ 1,310</b>

### TOTAL LIABILITIES

Total current liabilities for the NCEL were \$61 million in 2009 decreasing by \$19 million from 2008. The reduction in current liabilities resulted from a significantly lower prize liability from the previous year. Current liabilities also consist of trade payables to vendors, and obligations under State Treasurer's Security Lending Agreements. See Total Assets for an explanation of the State Treasurer's Security Lending Agreements. More detailed information can be found in Note 2D in the financial statements.

Noncurrent liabilities are Accrued Paid Time Off or Compensated Absences. A liability is recorded to reflect the balances for unpaid Paid Time Off (PTO) earned, which is provided to employees for use whenever vacation, sick leave, personal leave or bereavement leave is requested and approved. Current and noncurrent liability for Accrued Paid Time Off is shown below in thousands.

Beginning	Earned	Used	Ending	Current Liability	Long Term Portion
\$ 1,152	\$ 1,112	\$ 990	\$ 1,274	\$ 43	\$ 1,231

### NET ASSETS AND CHANGES IN NET ASSETS

As required in the Lottery Act, net revenues of the NCEL are transferred quarterly to the NC Education Lottery Fund at the Office of State Budget and Management. At year end, Net Revenues/Assets are zero for the NCEL. There are no changes in the Net Assets from year to year. **Condensed Statement of Net Assets (in thousands)**

	2009	2008	2007
<b>ASSETS</b>			
Total Current Assets	\$ 60,968	\$ 79,443	\$ 118,760
Capital Assets, Depreciable (Net)	1,310	1,487	1,282
Total Assets	62,278	80,930	120,042
<b>LIABILITIES</b>			
Total Current Liabilities	61,047	79,835	119,258
Noncurrent Liabilities	1,231	1,095	784
Total Liabilities	62,278	80,930	120,042
<b>NET ASSETS</b>			
Invested in Capital Assets	1,310	1,487	1,282
Unrestricted Net Assets	(1,310)	(1,487)	(1,282)
<b>Total Net Assets</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>

Current liabilities consist of "Due to Other Funds" in the amount of \$6.6 million. Of this amount, \$6.5 million represents the remaining amount of the "Net Revenues" and "50% of Unclaimed Prizes" for Fiscal Year 2009 not yet transferred to the NC Education Fund as of June 30, 2009, but will be transferred during Fiscal Year 2010. The remainder is due other state agencies for services provided to the NCEL. Additional information on the Due to Other Funds is found in Note 6C to the financial statements.

## REVENUES

Operating revenues consist of gross sales, fees and licenses.

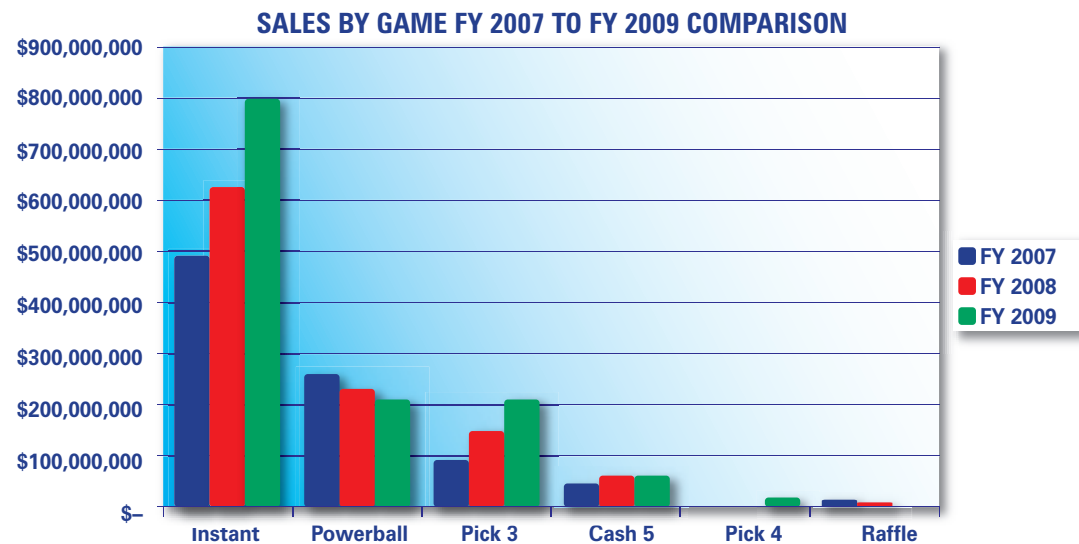
## SALES

Total gross lottery ticket sales for the fiscal year 2009 were approximately \$1.293 billion as compared to \$1.078 billion in fiscal year 2008 and \$885.5 million in fiscal year 2007. This represents an increase of almost \$215 million over 2008 and \$408 million over 2007.

Gross instant ticket sales increased significantly during fiscal year 2009, up \$163 million over one year ago. The 25.6% increase is attributable to several factors. The NCEL launched three \$10 Instant Scratch-off mega games; \$130 Million Cash Blockbuster, Lifetime Riches, and \$500,000 Jackpot, with prize payouts between 73% and 74%. The extremely successful merchandise game, Harley-Davidson® Instant Scratch-Off was reintroduced and provided players the chance to win one of nine Harley-Davidson® Fat Bob® Motorcycles, cash, and merchandise. This game was also launched by giving away a motorcycle as part of a promotion at a Charlotte Bobcats game. Also, the NCEL launched its Deal or No Deal™ Instant Scratch-Off licensed game, which awarded players the opportunity to travel to Hollywood and play in an un-televised version of the popular game show with Howie Mandel.

On-line sales during fiscal year 2009 grew by \$52 million to \$494 million. Fiscal year 2008 on-line sales were \$442 million. On-line sales benefited from two jackpots over \$200 million for POWERBALL during the year. The largest single sales day for POWERBALL was November 20, 2008 with sales of \$3.0 million. Carolina Pick 3's additional daytime drawing occurred for the entire fiscal year resulting in a 42% increase in Carolina Pick 3 sales over the previous year. The Carolina Cash 5 promotion "Get Truckin'" offered players the chance to win one of five Ford F150 Lariats and provided the NCEL a 5% increase in sales during the promotional window. The Carolina Cash 5 top prize exceeded \$820 thousand in October and again in April, resulting in an increase of on-line sales. The NCEL also launched its newest daily online game, Carolina Pick 4 on April 17th 2009, which had sales of \$15.8 million to the end of the fiscal year.

The following chart depicts the distribution of sales by product for the fiscal years ended June 30, 2009, 2008 and 2007.

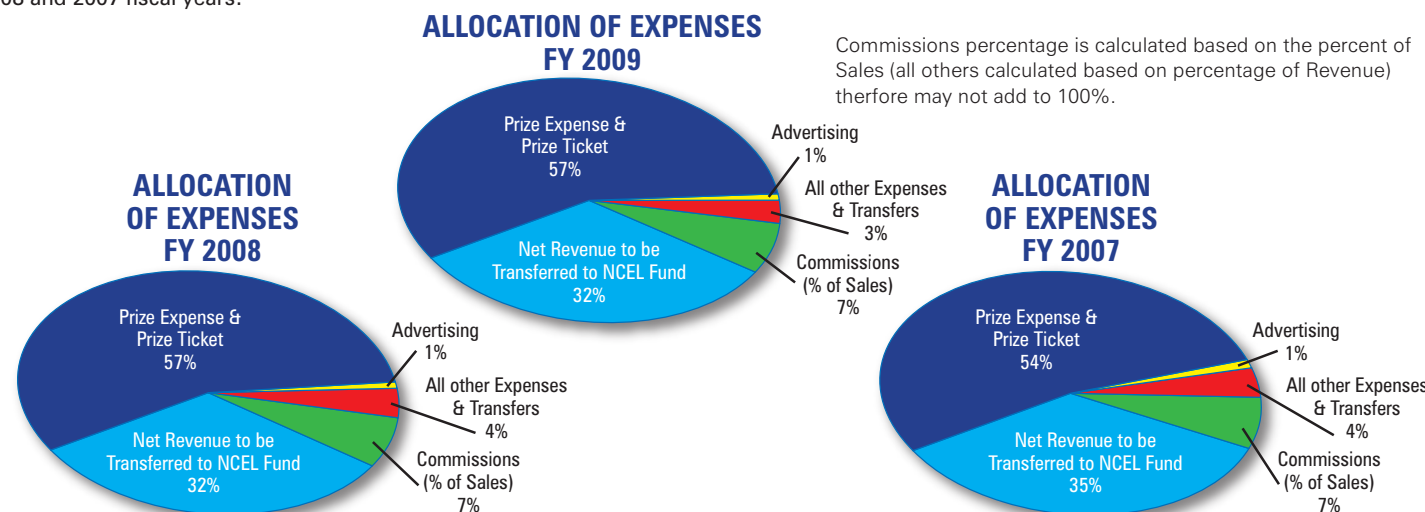


Nonoperating Revenues consist of investment earnings from the Short Term Investment Fund held at the State Treasurer's office and Multi-State Lottery Association (MUSL) dividends received.

## EXPENSES

Section 18C-162, NC General Statutes stipulates no more than 8% of the total annual revenues shall be allocated for payment of expenses of the Lottery. Advertising expenses shall not exceed 1% of the total annual revenues.

The following chart shows the major components of NCEL operating expenses and transfers as a percentage of total revenues for the June 30, 2009, 2008 and 2007 fiscal years:



Prizes, commissions and gaming vendor charges all directly relate to sales. As expected, as sales have increased, and so have these expenses. In fiscal year 2009, prizes, commissions and gaming vendor charges increased to \$843 million from \$681 million in 2008. The other expenses, which consist of advertising, salary and benefits, professional fees, rent, maintenance, bad debt, depreciation and transfers, have decreased to 4% of Total Annual Revenues from 5% the previous year. Fiscal year 2009, 2008 and 2007 administrative expenses were \$34 million, \$29 million and \$27 million respectively.

## Condensed Statement of Revenues and Expenses (in thousands)

	2009	2008	2007
<b>Operating Revenues</b>			
Gross Sales	\$ 1,293,020	\$ 1,078,082	\$ 885,575
Less: Prize Tickets	(9,580)	(29,733)	(23,901)
Fees and Licenses	4,663	4,782	4,521
<b>Total Operating Revenues</b>	<u>1,288,103</u>	<u>1,053,131</u>	<u>866,195</u>
<b>Operating Expenses</b>			
Salaries, Wages, and Benefits	14,694	13,793	12,279
Lottery Prizes	731,690	588,485	451,792
Retailer Commissions	90,366	75,371	61,932
Gaming Systems Services	20,599	17,286	14,315
Advertising	11,172	8,619	7,810
Marketing	1,751	1,220	953
Other Services	2,975	2,576	3,038
Furniture, Fixtures, and Equipment	249	240	1,433
Depreciation	544	382	391
Other General and Administrative Expenses	2,750	1,674	1,490
<b>Total Operating Expenses</b>	<u>876,790</u>	<u>709,646</u>	<u>555,433</u>
<b>Operating Income</b>	411,313	343,485	310,762
<b>Nonoperating Revenues (Expenses)</b>			
Investment Earnings and Other Miscellaneous Revenue (Expense)	4,251	8,897	8,544
Compulsive Gambling Contribution	(1,000)	(1,000)	(1,000)
Unclaimed Prizes to NC Education Lottery Fund	(19,901)	(16,789)	(8,037)
Net Revenues to NC Education Lottery Fund	(394,028)	(331,521)	(306,317)
Miscellaneous Nonoperating Expenses	(635)	(3,072)	(3,952)
<b>Total Nonoperating Revenues (Expenses)</b>	<u>(411,313)</u>	<u>(343,485)</u>	<u>(310,762)</u>
<b>Net Income</b>	-	-	-
<b>Net Assets</b>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

## BUDGET AND ECONOMIC OUTLOOK

On June 23, 2009, the Commission approved the Fiscal Year 2010 budget for the NCEL to provide a projected \$370 million to the State's Education Lottery Fund. This projected budget is a 4% decrease from the fiscal year 2008 budget of \$385.5 million for transfer to the State's Education Lottery Fund. The reason for a budgeted decrease in return to Education reflects the current economic conditions in the State of North Carolina, and its impact on lottery ticket sales. As per the General Assembly Fiscal Research Division: "The nation has been mired in the longest, sustained period of economic contraction since the depression of the 1930s. "Also "North Carolina is expected to see a continued decline in Gross State Product for this fiscal year and a modest rebound that is well below the long-term average the following year." Therefore, the NCEL has constructed a conservative budget and sales forecast for the upcoming fiscal year.

At inception, the NCEL did not have a formal documented revenue forecasting methodology due to a lack of sales history. Beginning with the fiscal year 2009 budget, the NCEL applied a more formal approach to forecasting revenues. Forecasted sales figures are based on the recent sales trends by product. They are then adjusted by a future performance factor determined by senior staff and reflective of game performance, game changes, and uncertainty in the market. The NCEL completed writing a strategic plan in fiscal year 2009 which will benefit the organization now and in the future.

A focus of the Commission is to ensure sound operations, and is apparent in audits conducted by outside firms. The Commission has undergone several audits this fiscal year. Delehanty Consulting LLC, an independent security organization, conducted our second security audit and determined that the controls designed by the North Carolina Education Lottery are adequate and operating as intended.

For the third consecutive year, the State Auditor contracted with an outside CPA firm to conduct the fiscal year financial audit, which resulted in an unqualified opinion.

## REQUESTS FOR INFORMATION

Any request for information about this report should be sent to the Public Information Officer at the North Carolina Education Lottery, 2100 Yonkers Road, Raleigh, North Carolina 27604.



**STATEMENTS OF NET ASSETS (IN THOUSANDS)**  
**JUNE 30, 2009, 2008 AND 2007**

	<u>2009</u>	<u>2008</u>	<u>2007</u>
<b>ASSETS</b>			
Current Assets:			
Cash and Cash Equivalents:			
Cash	\$ 119	\$ 75	\$ 62
Pooled Cash	33,124	38,680	49,503
Receivables:			
Accounts Receivable	4,919	13,728	11,054
Interest Receivable	138	418	406
Inventory	293	910	795
State Treasurer's Security Lending Collateral	22,375	25,632	56,940
Total Current Assets	<u>60,968</u>	<u>79,443</u>	<u>118,760</u>
Capital Assets, Depreciable (Net):			
Furniture and Equipment	2,702	2,335	1,748
Accumulated Depreciation	(1,392)	(848)	(466)
Total Capital Assets, Depreciable (Net)	<u>1,310</u>	<u>1,487</u>	<u>1,282</u>
Total Assets	<u>62,278</u>	<u>80,930</u>	<u>120,042</u>
<b>LIABILITIES</b>			
Current Liabilities:			
Accounts Payable	29,406	48,221	56,308
Accrued Payroll	332	405	16
Other Payables	2,266	1,956	3,333
Accrued Paid Time Off - Current	43	57	80
Due to Other Funds	6,625	3,564	2,581
Obligations Under State Treasurer's Security Lending Agreements	22,375	25,632	56,940
Total Current Liabilities	<u>61,047</u>	<u>79,835</u>	<u>119,258</u>
Noncurrent Liabilities:			
Accrued Paid Time Off	1,231	1,095	784
Total Liabilities	<u>62,278</u>	<u>80,930</u>	<u>120,042</u>
<b>NET ASSETS</b>			
Invested in Capital Assets	1,310	1,487	1,282
Unrestricted Net Assets	(1,310)	(1,487)	(1,282)
Total Net Assets	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

See Notes to the Financial Statements.

**STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS (IN THOUSANDS)**  
**YEARS ENDED JUNE 30, 2009, 2008 AND 2007**

	<u>2009</u>	<u>2008</u>	<u>2007</u>
Operating Revenues:			
Gross Sales	\$ 1,293,020	\$ 1,078,082	\$ 885,575
Less: Prize Tickets	(9,580)	(29,733)	(23,901)
Fees and Licenses	4,663	4,782	4,521
Total Operating Revenues	<u>1,288,103</u>	<u>1,053,131</u>	<u>866,195</u>
Operating Expenses:			
Salaries, Wages, and Benefits	14,694	13,793	12,279
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Total Operating Expenses	<u>876,790</u>	<u>709,646</u>	<u>555,433</u>
Operating Income	<u>411,313</u>	<u>343,485</u>	<u>310,762</u>
Nonoperating Revenues (Expenses):			
Investment Earnings and Other Miscellaneous Revenue	4,251	8,897	8,544
Compulsive Gambling Contribution	(1,000)	(1,000)	(1,000)
Unclaimed Prizes to NC Education Lottery Fund	(19,901)	(16,789)	(8,037)
Net Revenues to NC Education Lottery Fund	(394,028)	(331,521)	(306,317)
Miscellaneous Nonoperating Expenses	(635)	(3,072)	(3,952)
Total Nonoperating Revenues (Expense)	<u>(411,313)</u>	<u>(343,485)</u>	<u>(310,762)</u>
Net Income	-	-	-
Change in Net Assets	-	-	-
Net Assets Beginning, July 1	-	-	-
Net Assets Ending, June 30	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

See Notes to the Financial Statements.

**STATEMENTS OF CASH FLOWS (IN THOUSANDS)  
YEARS ENDED JUNE 30, 2009, 2008 AND 2007**

	2009	2008	2007
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Receipts from Customers	\$ 1,206,591	\$ 975,093	\$ 803,256
Payments to Employees and Fringe Benefits	(14,644)	(13,117)	(11,924)
Payments for Prizes, Benefits and Claims	(751,430)	(598,203)	(406,235)
Payments to Vendors and Suppliers	(37,688)	(31,484)	(30,964)
Other Receipts/Payments	8	548	569
Net Cash Flows Provided by Operating Activities	402,837	332,837	354,702
<b>CASH USED FOR NONCAPITAL FINANCING ACTIVITIES</b>			
Transfers to State Education Fund	(410,868)	(347,327)	(325,397)
Transfers to Other State Agencies	(1,000)	(1,000)	(1,013)
Total Cash Used for Noncapital Financing Activities	(411,868)	(348,327)	(326,410)
<b>CASH USED FOR CAPITAL AND RELATED FINANCING ACTIVITIES</b>			
Acquisition and Construction of Capital Assets	(367)	(587)	(1,059)
Proceeds from Sale of Capital Assets	—	—	10
Total Cash Used for Capital and Related Financing Activities	(367)	(587)	(1,049)
<b>CASH PROVIDED FROM INVESTING ACTIVITIES</b>			
Investment Earnings	3,886	5,267	3,822
Total Cash Provided from Investing Activities	3,886	5,267	3,822
Net Increase/(Decrease) in Cash and Cash Equivalents	(5,512)	(10,810)	31,065
Cash and Cash Equivalents at Beginning of Year	38,755	49,565	18,500
Cash and Cash Equivalents at End of Year	\$ 33,243	\$ 38,755	\$ 49,565
<b>RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES</b>			
Operating Income	\$ 411,313	\$ 343,485	\$ 310,762
Adjustments to Reconcile Operating Income to Cash Provided by Operating Activities:			
Depreciation Expense	545	382	391
Nonoperating Income - MUSL Dividend	7	544	554
Other Nonoperating Income	1	2	6
(Increase) Decrease in Assets:			
Accounts Receivable	8,809	(2,674)	(1,007)
Inventories	617	(115)	(795)
Increase (Decrease) in Liabilities:			
Accounts Payable	(18,549)	(9,481)	44,436
Accrued Payroll and Related Liabilities	50	677	355
Other Liabilities	44	17	—
Total Cash Provided by Operating Activities	\$ 402,837	\$ 332,837	\$ 354,702
<b>NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES</b>			
Assets Acquired through the Assumption of a Liability	\$ 22,375	\$ 25,632	\$ 56,940

See Notes to the Financial Statements.

**NOTES TO FINANCIAL STATEMENTS (IN THOUSANDS)  
JUNE 30, 2009, 2008 AND 2007**

**NOTE 1 - ORGANIZATION**

The North Carolina State Lottery Commission [aka, North Carolina Education Lottery (NCEL)] was created with the enactment of House Bill 1023 effective August 31, 2005 as an independent, self-supporting, and revenue-raising agency of the State of North Carolina (the State). The NCEL commenced operations on March 30, 2006 with the sale of instant scratch-off tickets. In March 2006, the NCEL joined the Multi-State Lottery Association (MUSL) composed of a group of U.S. lotteries that combine jointly to sell on-line POWERBALL lottery tickets. POWERBALL sales began on May 30, 2006. Carolina Pick 3 online game sales began on October 6, 2006, Carolina Cash 5 online game sales began on October 27, 2006. A second daily (Monday through Saturday) Carolina Pick 3 drawing was added on March 31, 2008. Carolina Pick 4 online game sales began on April 17, 2009.

The purpose of the NCEL is to generate funds to further the goal of providing enhanced educational opportunities, to support school construction, and to fund college and university scholarships. The operations of the NCEL are overseen by a nine member commission, five of whom are appointed by the Governor and four of whom are appointed by the General Assembly.

**NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**A. REPORTING ENTITY**

For financial reporting purposes, the North Carolina Education Lottery is a major enterprise fund of the primary government of the State of North Carolina and is reported as such in the Comprehensive Annual Financial Report (CAFR) of the State. These financial statements for the NCEL are separate and apart from those of the State of North Carolina and do not present the financial position of the State nor changes in the State's financial position and cash flows.

**B. BASIS OF PRESENTATION**

The financial statements are prepared on the accrual basis of accounting in a manner similar to a private enterprise. The NCEL elected to apply all applicable Governmental Accounting Standards Board (GASB) pronouncements as well as Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. As permitted by GASB Statement Number 20, the NCEL elected not to apply FASB statements or interpretations issued on or after November 30, 1989, unless specifically adopted by GASB.

As an enterprise fund, the NCEL is accounted for using the "economic resources" measurement focus. This means that all the assets and liabilities related to its operations are included on its statement of net assets, and its operating statement includes all revenues (increases) and expenses (decreases) in total assets. The NCEL distinguishes operating from non-operating revenues and expenses. Operating revenues and expenses generally relate to the NCEL's primary ongoing operations of selling lottery tickets and redeeming prizes; all revenues and expenses not meeting this definition are reported as non-operating. The principal operating revenues of the NCEL are charges to retailers for sales of lottery products. The significant operating expenses include the cost of prizes, commissions, gaming system vendor charges, personnel, and other administrative expenses.

**C. CASH AND CASH EQUIVALENTS**

Cash and cash equivalents include regional office deposited operating funds, imprest funds, and deposits held by the State Treasurer in the State Treasurer's Short Term Investment portfolio. The Short Term Investment portfolio maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit additional cash at any time and also may withdraw cash at any time without prior notice or penalty.

**D. STATE TREASURER'S SECURITIES LENDING COLLATERAL**

While the NCEL does not directly engage in securities lending transactions, it deposits certain funds with the State Treasurer's Short-Term Investment Fund which participates in securities lending activities. Based on the State Treasurer's allocation of these transactions, the NCEL recognizes its allocable share of the assets and liabilities related to these transactions on the accompanying financial statements as "State Treasurer's Securities Lending Collateral" and "Obligations Under State Treasurer's Securities Lending Agreements." The NCEL's allocable share of these assets and liabilities is based on the NCEL's year end deposit balance per the State Treasurer's records.

Based on the authority provided in General Statutes 147-69.3(e), the State Treasurer lends securities from its investment pool to brokers-dealers and other entities (borrowers) for collateral that will be returned for the same securities in the future. The Treasurer's securities custodian manages the securities lending program. During the year, the Treasurer's custodian lent U.S. government and agency securities, GNMA's, corporate bonds and notes for collateral. The Treasurer's custodian is permitted to receive cash, U.S. government and agency securities, or irrevocable letters of credit as collateral for the securities lent.

The collateral is initially pledged at 102 percent of the market value of the securities lent, and additional collateral is required if its value falls to less than 100 percent of the market value of the securities lent. There are no restrictions on the amount of loans that can be made. Substantially all security loans can be terminated on demand by either the State Treasurer or the borrower.

Additional details on the State Treasurer's securities lending program are included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.ncosc.net/> and clicking on "Financial Reports," or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

**E. ALLOWANCE FOR DOUBTFUL ACCOUNTS**

An allowance for doubtful accounts has not been established because there are no indications of significant delinquencies from the collection of retailer accounts as of June 30, 2009, 2008 and 2007.

**F. CAPITAL ASSETS**

The NCEL defines capital assets as assets with an initial unit cost of \$5,000 or greater and an estimated useful life of two or more years. This definition conforms to the policy of the NC Office of State Controller. Depreciation is computed using the straight-line method over the estimated lives of the assets. The NCEL uses the half year convention. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation will be removed from the books and any resulting gain or loss reflected in operations of the period of disposal. Capital assets are carried at cost less accumulated depreciation. The estimated useful lives by general category are as follows:

Category	Years
Equipment	5-7
Furniture	5
Computers and Software	3-5

## G. GAME REVENUE RECOGNITION

For the NCEL's on-line games, POWERBALL, Carolina Cash 5, Carolina Pick 4, Carolina Pick 3, and raffles offered, revenue is recognized at the time of sale on a daily basis. For instant games, revenue is recognized at the time a pack of tickets is settled (See Note 3A.1 – Game Revenue).

## H. LOTTERY PRIZE EXPENSE RECOGNITION

For POWERBALL, Carolina Cash 5, Carolina Pick 4, Carolina Pick 3, and for raffles, prize expense is recorded at 50 percent of sales on a daily basis. For instant games, prize expense is accrued based on the final production prize structure percentage provided by the gaming vendor for each game and recorded daily on value of packs settled. Certain games include free tickets (prize tickets) which entitle the holder to exchange one instant ticket for another of equal value. For the instant games with prize tickets, the final prize structure percentage used is adjusted to eliminate the value of the prize tickets. Prize expense for merchandise prizes is recognized as prizes are fulfilled.

## I. USE OF ESTIMATES

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

## NOTE 3 – REVENUE

### A. OPERATING REVENUE

#### 1. Game Revenue

Instant packs are settled manually by the retailer or automatically by the gaming system 21 days after pack activation, whichever is earlier. Operating revenues are reduced by the value of prize tickets validated during a period.

<u>Gross revenue</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>
Instant	\$ 798,676	\$ 635,880	\$ 490,564
On-line	494,435	442,299	395,011
Bad debt write off	(86)	(89)	–
Damaged tickets	(5)	(8)	–
Total	<u>\$ 1,293,020</u>	<u>\$ 1,078,082</u>	<u>\$ 885,575</u>

#### 2. Fees and Licenses

The majority of Fees and Licenses represent a weekly retailer communication fee charged to active retailers for terminal satellite communications and an application fee for new retailers and changes in ownership.

### B. NON-OPERATING REVENUE

The cash accounts of the NCEL are Short-term Investment Fund (STIF) Accounts which are interest bearing accounts held with the NC State Treasurer. Investments are limited to those authorized for the State's General Fund, pursuant to NC General Statute 147-69.1. The interest earned on these balances is recorded as non-operating revenue, and is \$3,608, \$5,278 and \$4,044 for the years ended June 30, 2009, 2008 and 2007, respectively. The allocable share of the revenue arising from the State Treasurer's Securities Lending Collateral program is included as investment earnings. This also reflects a dividend from MUSL of \$7, \$544 and \$554 for the years ended June 30, 2009, 2008 and 2007, respectively. The remaining \$1, \$3 and \$7 for the years ended June 30, 2009, 2008 and 2007, respectively, is composed of miscellaneous items.

## NOTE 4 – EXPENSES

### A. OPERATING EXPENSES

#### 1. Lottery Prize Expense

<u>Prize Expense</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>
Instant	\$ 474,111	\$ 350,165	\$ 257,460
On-line	237,678	221,531	194,332
50% of unclaimed prizes	19,901	16,789	–
Total	<u>\$ 731,690</u>	<u>\$ 588,485</u>	<u>\$ 451,792</u>

#### 2. Retailer Commissions

<u>Commissions</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>
Instant	\$ 55,788	\$ 44,441	\$ 34,308
On-line	34,578	30,930	27,624
Total	<u>\$ 90,366</u>	<u>\$ 75,371</u>	<u>\$ 61,932</u>

### 3. Other Services

The principal expenses included are: security services, background checks, communications, legal services, travel, financial audit services, network support, and costs for temporary employees.

<u>Other Services</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>
Security services	\$ 10	\$ 17	\$ 407
Background checks	849	699	701
Communications, including wiring	1,032	708	769
Legal services	14	79	139
Travel	104	92	102
Other	966	981	920
	<u>\$ 2,975</u>	<u>\$ 2,576</u>	<u>\$ 3,038</u>

### 4. Furniture, Fixtures, and Equipment

To operate a lottery, numerous items of equipment, furniture, and ticket dispensers are required. Most of these items were one time purchases to be replaced as needed at various points in the future. These items were also below our threshold for capitalization (see Note 5D – Capital Assets) and therefore expensed. The total for these expenses was \$249 in Fiscal Year 2009, \$240 in Fiscal Year 2008 and \$1,433 in Fiscal Year 2007.

### 5. Leases – Buildings and Offices

The NCEL has entered into various operating leases through the North Carolina State Department of Administration for building and office facilities. These leases are for initial terms of seven to ten years. Projected lease payments for these facilities are:

<u>Year Ending</u>	<u>Amount</u>
2010	\$ 878
2011	890
2012	646
2013	644
2014	639
2015-2019	1,455
Total	<u>\$ 5,152</u>

The total space rental costs for the year ended June 30, 2009 was \$858, \$838 for the year ended June 30, 2008, and \$836 for the year ended June 30, 2007.

### B. NON-OPERATING EXPENSES

The allocable share of the expenses arising from State Treasurer's Securities Lending Collateral program transactions, totaling \$635, \$3,072 and \$3,939 for the years ended June 30, 2009, 2008 and 2007, respectively, are also included as non-operating expense.

### C. TRANSFERS OUT

There were three significant transfers out of the NCEL which are considered nonoperating expenses. \$1,000 was transferred to the NC Department of Health and Human Services for a gambling addiction education and treatment program as stipulated in the North Carolina Lottery Act for years ended June 30, 2009, 2008 and 2007 (Note 7C).

The second transfer is \$19,854, \$16,789 and \$8,037 for the years ended June 30, 2009, 2008 and 2007, respectively, from unclaimed prizes during the year; the remaining \$47 will be transferred during October 2009. The North Carolina State Lottery Act requires the NCEL to transfer "Fifty percent (50%)" of unclaimed prizes to the NC Education Lottery Fund each year (Note 7B).

The third transfer is in compliance with the North Carolina State Lottery Act. This Act requires all "Net Revenues" of the NCEL to be transferred to the NC Education Lottery Fund for the educational purposes set forth in the legislation. Of the \$394,028, \$331,521 and \$306,317 of June 30, 2009, 2008 and 2007 "Net Revenues" (see Note 12), respectively, \$387,474, \$328,020 and \$303,774, respectively, was actually transferred to the NC Education Lottery Fund. The remaining was recorded as a payable to the State, but remained in the NCEL. The remaining \$6,554, \$3,501 and \$2,543 for the years ended June 30, 2009, 2008 and 2007, respectively, were transferred subsequent to year-end. NC General Statute 18C states: "The funds remaining in the North Carolina State Lottery Fund after receipt of all revenues to the Lottery Fund and after accrual of all obligations of the Commission for prizes and expenses shall be considered to be the net revenues of the North Carolina State Lottery Fund."

## NOTE 5 – ASSETS

### A. CASH

The cash and cash equivalents balances at June 30, 2009, 2008 and 2007 include no undeposited receipts on hand.

Unless specifically exempt, the NCEL is required by North Carolina General Statute 147-77 to deposit moneys received with the State Treasurer or with a depository institution in the name of the State Treasurer. Except as noted above, all NCEL funds are deposited with the State Treasurer. The NCEL has no deposit policy concerning credit risk, as all deposits are held by the State Treasurer.

At June 30, 2009, 2008 and 2007, respectively, \$33,124, \$38,680 and \$49,503 of the amount shown on the Statements of Net Assets as cash and cash equivalents represents the NCEL's equity position in the State Treasurer's Short-Term Investment Fund. The Short-Term Investment Fund (a portfolio within the State Treasurer's Investment Pool, an external investment pool that is not registered with the Securities and Exchange Commission and does not have a credit rating) had a weighted average maturity of 1.8, 2.9 and 1.6 years as of June 30, 2009, 2008 and 2007, respectively. Assets and shares of the Short-Term Investment Fund are valued at amortized cost, which approximates fair value. Deposit and investment risks associated with the State Treasurer's Investment Pool (which includes the State Treasurer's Short-Term Investment Fund) are included in the State of North Carolina's *Comprehensive Annual Financial Report*.

An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.ncosc.net/> and clicking on "Financial Reports" or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

## B. ACCOUNTS RECEIVABLE

Accounts Receivable primarily represents amounts due from retailers for settlement of packs of tickets less commissions and prizes paid by the retailers. Electronic Funds Transfer is used to collect receivables weekly from retailer bank accounts that were set up in trust for the NCEL.

## C. INVENTORY

Inventory for the NCEL consists of all merchandise prizes that are paid for before distribution, inventory is reduced as prizes are fulfilled. Inventory as of June 30, 2009 was \$293, \$910 as of June 30, 2008, and \$795 as of June 30, 2007.

## D. CAPITAL ASSETS

The activity for capital assets for the year ended June 30, 2009 was:

Category	Balance July 1, 2008	Increases	Decreases	Balance June 30, 2009
Capital Assets, depreciable				
Furniture	\$ 29	\$ -	\$ -	\$ 29
Equipment	2,239	367	-	2,606
Motorized equipment	67	-	-	67
Total capital assets, depreciable	2,335	367	-	2,702
Less accumulated depreciation for:				
Furniture	11	7	-	18
Equipment	813	523	-	1,336
Motorized equipment	24	14	-	38
Total accumulated depreciation	848	544	-	1,392
Total capital assets, depreciable, net	1,487	(177)	-	1,310
<b>Capital assets, net</b>	<b>\$ 1,487</b>	<b>\$ (177)</b>	<b>\$ -</b>	<b>\$ 1,310</b>

The activity for capital assets for the year ended June 30, 2008 was:

Category	Balance July 1, 2007	Increases	Decreases	Balance June 30, 2008
Capital Assets, depreciable				
Furniture	\$ 29	\$ -	\$ -	\$ 29
Equipment	1,652	587	-	2,239
Motorized equipment	67	-	-	67
Total capital assets, depreciable	1,748	587	-	2,335
Less accumulated depreciation for:				
Furniture	4	7	-	11
Equipment	450	363	-	813
Motorized equipment	12	12	-	24
Total accumulated depreciation	466	382	-	848
Total capital assets, depreciable, net	1,282	205	-	1,487
<b>Capital assets, net</b>	<b>\$ 1,282</b>	<b>\$ 205</b>	<b>\$ -</b>	<b>\$ 1,487</b>

The activity for capital assets for the year ended June 30, 2007 was:

Category	Balance July 1, 2006	Increases	Decreases	Balance June 30, 2007
Capital Assets, nondepreciable				
Improvements in progress	\$ 194	\$ -	\$ 194	\$ -
Total capital assets, nondepreciable	194	-	194	-
Capital Assets, depreciable				
Furniture	-	29	-	29
Equipment	484	1,179	11	1,652
Motorized equipment	22	45	-	67
Total capital assets, depreciable	506	1,253	11	1,748
Less accumulated depreciation for:				
Furniture	-	4	-	4
Equipment	74	377	1	450
Motorized equipment	2	10	-	12
Total accumulated depreciation	76	391	1	466
Total capital assets, depreciable, net	430	862	10	1,282
<b>Capital assets, net</b>	<b>\$ 624</b>	<b>\$ 862</b>	<b>\$ 204</b>	<b>\$ 1,282</b>

Equipment expenditures for 2009 include Carolina Pick 4 draw machines and an upgraded telephone system. Equipment expenditures for 2008 include storage area networks (SAN) in Greensboro and Raleigh offices for disaster recovery and improvement of network efficiency. In 2007 numerous items of equipment were purchased since it was the first full year of operations.

## NOTE 6 – LIABILITIES

### A. ACCOUNTS PAYABLE

This primarily represents trade payables to vendors, prize liabilities, and POWERBALL low-tier liability. At year-end, June 30, 2009, 2008 and 2007, the balances were:

Type Account	2009	2008	2007
Trade payables to vendors	\$ 4,607	\$ 3,413	\$ 3,109
Instant prize liability	8,987	25,434	35,633
Prize liability – unused unclaimed prizes	7,294	9,279	8,037
POWERBALL low-tier liability	3,449	5,318	4,563
Prize liability – breakage	5,068	4,742	4,943
Other	1	35	23
Total accounts payable	<u>\$ 29,406</u>	<u>\$ 48,221</u>	<u>\$ 56,308</u>

### B. OTHER PAYABLES

This represents amounts due MUSL of \$2,108, \$1,846 and \$3,255 for the years ended June 30, 2009, 2008 and 2007, respectively for the NCEL's share of POWERBALL jackpot prizes. The remainder resulted from federal and state withholding on prize payments, and various clearing accounts.

### C. DUE TO OTHER FUNDS

As explained in Note 4C, \$6,554, \$3,501 and \$2,543 for the years ended June 30, 2009, 2008 and 2007, respectively, represents the amounts of the "Net Revenues" and "50% of Unclaimed Prizes" for the year not yet transferred to the NC Education Fund as of June 30, but will be transferred subsequent to year-end. The remainder is due to other state agencies for services provided to the NCEL.

### D. ACCRUED PAID TIME OFF

Paid time off (PTO) is provided to employees for use whenever vacation, sick leave, personal leave or bereavement leave is requested and approved. Under this policy, every calendar year, on January 1st, a specific amount of PTO will be credited to Director's and above PTO accounts. All other employees' PTO accounts will be credited on a monthly basis as earned. Employees must be employed at least one year to receive pay for accrued leave balances. Directors and above will be paid out accrued leave balances upon separation provided they have attained a minimum of six (6) months' service on the date of separation.

Activity for the year ended June 30, 2009:

Beginning	Earned	Used	Ending	Current Liability	Long Term Portion
\$ 1,152	\$ 1,112	\$ 990	\$ 1,274	\$ 43	\$ 1,231

Activity for the year ended June 30, 2008:

Beginning	Earned	Used	Ending	Current Liability	Long Term Portion
\$ 864	\$ 1,839	\$ 1,551	\$ 1,152	\$ 57	\$ 1,095

Activity for the year ended June 30, 2007:

Beginning	Earned	Used	Ending	Current Liability	Long Term Portion
\$ 524	\$ 943	\$ 603	\$ 864	\$ 80	\$ 784

## NOTE 7 – OTHER IMPORTANT ITEMS

### A. DEPOSITS WITH MULTI-STATE LOTTERY ASSOCIATION (MUSL)

MUSL is a voluntary association created for the purpose of administering joint, multi-jurisdictional lottery games, such as POWERBALL. Through June 30, 2009, MUSL includes 30 state lotteries, the District of Columbia and the U.S. Virgin Islands. The chief executive officer of each member lottery serves on the MUSL board of directors.

As a member of MUSL, the NCEL is required to contribute to various prize reserve funds maintained by MUSL. These contributions are included in the 50% prize expense computed on POWERBALL sales. The net amount of the 50% prize expense less the amount required to pay low-tier prizes within the State is paid to MUSL. This payment is to cover the NCEL's share of current jackpot prizes based on the NCEL's percent of sales for each drawing and the NCEL's share of the prize reserve fund. The prize reserve fund serves as a contingency reserve to protect all MUSL members including the NCEL from unforeseen prize liabilities. All prize reserve funds remitted, and the related interest earnings, will be returned to the NCEL upon leaving MUSL, less any portion of unanticipated prize claims which may have been paid from the fund. As of June 30, 2009, 2008, and 2007, the NCEL had been credited with \$6,906, \$4,505 and \$2,369 in the MUSL prize reserve funds.

## B. UNCLAIMED PRIZES

As of June 30, 2009 and 2008, the NCEL had unclaimed prizes from both online and instant games. The first POWERBALL draw after the NCEL started selling tickets was on May 31, 2006, and therefore, the NCEL began recognizing unclaimed prizes on November 27, 2006 (180 days after the first draw). The first Carolina Pick 3 unclaimed prizes were recorded on April 4, 2007 and the first unclaimed prizes for Carolina Cash 5 were recorded on April 25, 2007. Unclaimed prizes for Carolina Pick 4 were not recorded, since the end of the fiscal year was less than 180 days after the first draw. The NCEL closed fifty two instant games during the 2009 fiscal year resulting in \$29,953 in unclaimed prizes.

<u>Game Type</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>
Instant	\$ 29,953	\$ 22,792	\$ 9,586
POWERBALL	5,594	7,598	5,748
Carolina Cash 5	2,322	1,892	333
Carolina Pick 3	1,933	1,150	408
Raffle	–	73	–
Total unclaimed prizes	<u>\$ 39,802</u>	<u>\$ 33,505</u>	<u>\$ 16,075</u>

## C. COMPULSIVE GAMBLING CONTRIBUTION

By North Carolina General Statute the NCEL must make “a transfer of \$1,000 annually to the Department of Health and Human Services (DHHS) for gambling addiction education and treatment programs.” (See Note 4C)

## D. LIMITATIONS ON OPERATING AND ADVERTISING EXPENSES:

As established in North Carolina General Statute 18C-162(a)(3); “No more than eight percent (8%) of the total annual revenues, as described in this Chapter, shall be allocated for payment of expenses of the Lottery. Advertising expenses shall not exceed one percent (1%) of the total annual revenues.” The one percent for advertising expenses is included in the eight percent maximum for Lottery expenses. Total annual revenues include proceeds from the sale of lottery tickets, interest earned by the NCEL, and all other funds credited to the Lottery from any source.

## NOTE 8 – RISK MANAGEMENT

The NCEL is exposed to various risks of loss related to torts; theft of, damage to, and the destruction of assets; errors and omissions; injuries to employees; and natural disasters. The NCEL participates in the State’s Risk Management Program for property, liability, crime and automobile coverage, and pays an annual premium for this coverage. The Lottery has not experienced any losses during the year ended June 30, 2009.

The types of coverage, limits, and deductibles as of June 30, 2009 are described below (the following chart is not shown in thousands).

<b>Type Coverage</b>	<b>Limits (\$)</b>	<b>Deductible (\$)</b>	<b>Comments</b>
Public officers and employee liability	1,000,000/5,000,000	The first 150,000 /1,000,000 per person is paid by the Commission.	State is self-insured up to \$1,000,000; excess up to \$5,000,000 is with a private insurer.
All risk – property contents	3,506,848	5,000	
Auto – liability	1,000,000 per person/ 10,000,000 per accident		
Auto – comp/collision	29,470	50 100	Comp. deductible Collision deductible
Theft, disappearance, destruction	250,000	2,500	Inside premises
Theft, disappearance, destruction	50,000	2,500	Outside premises
Computer fraud	5,000,000	75,000	+10% over \$75,000
Employee dishonesty	5,000,000	75,000	+10% over \$75,000
Forgery and alteration	100,000	2,500	
Robbery and safe burglary – money/securities	500,000	1,000	

Employees and retirees are provided health care coverage by the State of North Carolina’s Comprehensive Major Medical Plan. This employee benefit plan is funded by employer and employee contributions.

The North Carolina Workers’ Compensation Program provides benefits to workers injured on the job. All employees of the State are included in the program. When an employee is injured, the NCEL’s primary responsibility is to arrange for and provide the necessary treatment for work related injury. The State is self-insured for workers’ compensation. A third party administrator processes workers’ compensation claims. State agencies, including the NCEL, contribute to a fund administered by the office of the State Controller to cover their workers’ compensation claims. The third party administrator receives a per case administration fee and draws down State funds to make medical and indemnity payments on behalf of the State in accordance with the North Carolina Workers’ Compensation Act.

Term life insurance of \$25 to \$50 is provided to eligible employees. This self-insured death benefit program is administered by the Department of the State Treasurer and funded via employer contributions. The employer contribution rate was .16% for the current fiscal year.

Additional details on State-administered risk management programs are disclosed in the State of North Carolina’s Comprehensive Annual Financial Report. An electronic version of this report is available by accessing the North Carolina Office of the State Controller’s Internet home page <http://www.ncosc.net/> and clicking on “Financial Reports,” or by calling the State Controller’s Financial Reporting Section at (919) 981-5454.

## NOTE 9 – PENSION AND DEFERRED COMPENSATION PLANS

### A. RETIREMENT PLAN

Each permanent full-time employee, as a condition of employment, is a member of the Teachers’ and State Employees’ Retirement System (TSERS) and is automatically enrolled in the Teachers’ and State Employees’ Retirement System.

The Teachers’ and State Employees’ Retirement System is a cost sharing multiple-employer defined benefit pension plan established by the State to provide pension benefits for employees of the State, its component units and local boards of education. The plan is administered by the North Carolina State Treasurer.

Benefit and contribution provisions for the Teachers’ and State Employees’ Retirement System are established by North Carolina General Statutes 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contribution rates are set each year by the North Carolina General Assembly based on annual actuarial valuations.

For the years ending June 30, 2009, 2008 and 2007, respectively, the NCEL had a total payroll of \$11,696, \$10,862 and \$9,720, of which \$11,240, \$10,340 and \$9,677 was covered under the Teachers’ and State Employees’ Retirement System. Total employer and employee contributions for pension benefits for the year ended June 30, 2009, 2008 and 2007 were \$915, \$805 and \$621, respectively. Required employer contribution rates for the years ended June 30, 2009, 2008 and 2007, were 3.36%, 3.05% and 2.66%, respectively, while employee contributions were 6% each year. The NCEL made 100% of its annual required contributions for the years ended June 30, 2009, 2008, and 2007, which were \$378, \$313, and \$257, respectively.

The Teachers’ and State Employees’ Retirement System’s financial information is included in the State of North Carolina’s Comprehensive Annual Financial Report. An electronic version of this report is available by accessing the North Carolina Office of the State Controller’s Internet home page <http://www.ncosc.net/> and clicking on “Financial Reports,” or by calling the State Controller’s Financial Reporting Section at (919) 981-5454.

### B. SUPPLEMENTAL RETIREMENT INCOME PLAN

IRC Section 401(k) Plan – All full-time employees are eligible to enroll in the Supplemental Retirement Income Plan, a defined contribution plan, created under Internal Revenue Code Section 401(k). All costs of administering the Plan are the responsibility of plan participants. The Plan is provided by Prudential Retirement, administered by the NC Department of the State Treasurer and sponsored by the State of North Carolina. The effective date of participation was January 30, 2006. The voluntary contributions by employees amounted to \$206, \$194, and \$115 for the years ended June 30, 2009, 2008 and 2007, respectively.

### C. DEFERRED COMPENSATION PLAN

IRC Section 457 Plan – The State of North Carolina offers its permanent employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457 through the North Carolina Public Employee Deferred Compensation Plan (the “Plan”). The Plan permits each participating employee to defer a portion of his or her salary until future years. The deferred compensation is available to employees upon separation from service, death, disability, retirement or financial hardships if approved by the Board of Trustees of the Plan. The Board, a part of the North Carolina Department of State Treasurer, maintains a separate fund for the exclusive benefit of the participating employees and their beneficiaries, the North Carolina Public Employee Deferred Compensation Trust Fund. The Board also contracts with an external third party to perform certain administrative requirements and to manage the trust fund’s assets. All costs of administering and funding the Plan are the responsibility of the Plan participants.

The effective date of participation was January 30, 2006. The voluntary contributions by employees amounted to \$44, \$67 and \$50 for the years ended June 30, 2009, 2008 and 2007.

## NOTE 10 – OTHER POSTEMPLOYMENT BENEFITS

### A. HEALTH CARE FOR LONG-TERM DISABILITY BENEFICIARIES AND RETIREES

The NCEL participates in the Comprehensive Major Medical Plan (the Plan), a cost-sharing, multiple-employer defined benefit health care plan that provides postemployment health insurance to eligible former employees. Eligible former employees include long-term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers’ and State Employees’ Retirement System. Coverage eligibility varies depending on years of contributory membership service in the retirement system prior to disability or retirement.

The Plan’s benefit and contribution provisions are established by Chapter 135-7, Article 1, and Chapter 135, Article 3, of the General Statutes and may be amended only by the North Carolina General Assembly. The Plan does not provide for automatic post-retirement benefit increases.

By General Statute, a Retiree Health Benefit Fund (the Fund) has been established as a fund in which accumulated contributions from employers and any earnings on those contributions shall be used to provide health benefits to retired and disabled employees and applicable beneficiaries. By statute, the Fund is administered by the Board of Trustees Teachers’ and State Employees’ Retirement System and contributions to the fund are irrevocable. Also by law, Fund assets are dedicated to providing benefits to retired and disabled employees and applicable beneficiaries and are not subject to the claims of creditors of the employers making contributions to the Fund. Contribution rates to the Fund, which are intended to finance benefits and administrative expenses on a pay-as-you-go basis, are determined by the General Assembly in the Appropriations Bill.

For the current fiscal year the NCEL contributed 4.1% of the covered payroll under the Teachers’ and State Employees’ Retirement System. Required contribution rates for the years ended June 30, 2008 and 2007, were 4.1% and 3.8%, respectively. The NCEL made 100% of its annual required contributions to the Plan for the years ended June 30, 2009, 2008, and 2007, which were \$461, \$421, and \$368, respectively. The NCEL assumes no liability for retiree health care benefits provided by the programs other than its required contribution.

Additional detailed information about these programs can be located in the State of North Carolina’s Comprehensive Annual Financial Report. An electronic version of this report is available by accessing the North Carolina Office of the State Controller’s Internet home page <http://www.ncosc.net/> and clicking on “Financial Reports,” or by calling the State Controller’s Financial Reporting Section at (919) 981-5454.

### B. LONG-TERM DISABILITY

The NCEL participates in the Disability Income Plan of North Carolina (DIPNC), a cost-sharing, multiple-employer defined benefit plan, to provide short-term and long-term disability benefits to eligible members of the Teachers’ and State Employees’ Retirement System. Benefit and contribution provisions are established by Chapter 135, Article 6, of the General Statutes, and may be amended only by the North Carolina General Assembly. The plan does not provide for automatic post-retirement benefit increases.

Disability income benefits are funded by actuarially determined employer contributions that are established in the Appropriations Bill by the General Assembly. For the fiscal year ended June 30, 2009, the NCEL made a statutory contribution of .52% of covered payroll under the Teachers’ and State Employees’ Retirement System to the DIPNC. Required contribution rates for the years ended June 30, 2009, 2008 and 2007 were .52%, .52% and .52%, respectively. The NCEL made 100% of its annual required contributions to the DIPNC for the years ended June 30, 2009, 2008, and 2007, which were \$58, \$54, and \$50, respectively. The NCEL assumes no liability for long-term disability benefits under the Plan other than its contribution.

Additional detailed information about the DIPNC is disclosed in the State of North Carolina’s Comprehensive Annual Financial Report. An electronic version of this report is available by accessing the North Carolina Office of the State Controller’s Internet home page <http://www.ncosc.net/> and clicking on “Financial Reports,” or by calling the State Controller’s Financial Reporting Section at (919) 981-5454.

## NOTE 11 – LITIGATION

As of June 30, 2009, the NCEL is not, nor anticipates being, a party to any litigation.

## NOTE 12 – ALLOCATION OF TOTAL ANNUAL REVENUES/TRANSFERS TO NC EDUCATION LOTTERY FUND

		2009	
Lottery Ticket Sales	\$	1,293,020	
Fees and Licenses		4,663	
Investment Earnings and Other Revenues		4,251	
Total Annual Revenue		1,301,934	
Less Prize Tickets		( 9,580)	1%
Total Net Revenue		1,292,354	Of Total Annual Revenue
Prize Expense		( 731,690)	56%
Advertising		( 11,172)	1%
All Other Expenses and Transfers		( 45,197)	
Total Section 18C-162.a.3		( 56,369)	4%
Commissions (per 18C-142)		( 90,366)	7%
Unclaimed Prizes to NC Education Lottery Fund		19,901	
Net Revenues to NC Education Lottery Fund		394,028	
Total Revenues to NC Education Fund	\$	413,929	32%
			Of Total Annual Revenue

		2008	
Lottery Ticket Sales	\$	1,078,082	
Fees and Licenses		4,782	
Investment Earnings and Other Revenues		8,897	
Total Annual Revenue		1,091,761	
Less Prize Tickets		( 29,733)	3%
Total Net Revenue		1,062,028	Of Total Annual Revenue
Prize Expense		( 588,485)	54%
Advertising		( 8,619)	1%
All Other Expenses and Transfers		( 41,243)	
Total Section 18C-162.a.3		( 49,862)	5%
Commissions (per 18C-142)		( 75,371)	7%
Unclaimed Prizes to NC Education Lottery Fund		16,789	
Net Revenues to NC Education Lottery Fund		331,521	
Total Revenues to NC Education Fund	\$	348,310	32%
			Of Total Annual Revenue

		2007	
Lottery Ticket Sales	\$	885,575	
Fees and Licenses		4,521	
Investment Earnings and Other Revenues		8,544	
Total Annual Revenue		898,640	
Less Prize Tickets		( 23,901)	3%
Total Net Revenue		874,739	Of Total Annual Revenue
Prize Expense		( 451,792)	50%
Advertising		( 7,810)	1%
All Other Expenses and Transfers		( 38,851)	
Total Section 18C-162.a.3		( 46,661)	5%
Commissions (per 18C-142)		( 61,932)	7%
Unclaimed Prizes to NC Education Lottery Fund		8,037	
Net Revenues to NC Education Lottery Fund		306,317	
Total Revenues to NC Education Fund	\$	314,354	35%
			Of Total Annual Revenue

In accordance with Section § 18C-162 of the NCEL Act: Allocation of revenues.

- (a) The Commission shall allocate revenues to the North Carolina State Lottery Fund in order to increase and maximize the available revenues for education purposes, and to the extent practicable, shall adhere to the following guidelines:
- (1) At least fifty percent (50%) of the total annual revenues, as described in this Chapter, shall be returned to the public in the form of prizes.
  - (2) At least thirty-five percent (35%) of the total annual revenues, as described in this Chapter, shall be transferred as provided in G.S. 18C-164.
  - (3) No more than eight percent (8%) of the total annual revenues, as described in this Chapter, shall be allocated for payment of expenses of the Lottery. Advertising expenses shall not exceed one percent (1%) of the total annual revenues.
  - (4) No more than seven percent (7%) of the total annual revenues, as described in this Chapter, shall be allocated for compensation paid to lottery game retailers.
- (b) To the extent that the expenses of the Commission are less than eight percent (8%) of total annual revenues, the Commission may allocate any surplus funds:
- (1) To increase prize payments; or
  - (2) To the benefit of the public purposes as described in this chapter.
- (c) Unclaimed prize money shall be held separate and apart from the other revenues and allocated as follows:
- (1) Fifty (50%) to enhance prizes under subdivision (a)(1) of this section.
  - (2) Fifty (50%) to the Education Lottery Fund to be allocated in accordance with G.S. 18C-164(c).(2005-344, s. 1; 2005-276, s. 31.1(r); 2007-323, s.5.2(c).)

Additionally, in accordance with Section § 18C 142 of the NCEL Act, Compensation for lottery game retailers, "The amount of compensation paid to lottery game retailers for their sales of lottery tickets or shares shall be seven percent (7%) of the retail price of the tickets or shares sold for each lottery game."

§ 18C-161. Types of income to the North Carolina State Lottery Fund.

- (1) All proceeds from the sale of lottery tickets or shares.
- (2) The funds for initial start-up costs provided by the State.
- (3) All other funds credited or appropriated to the Commission from any sources.
- (4) Interest earned by the North Carolina Lottery Fund.

As of September 30, 2009 the NCEL transferred \$407.4 million and \$344.8 million for the years ended June 30, 2009 and 2008, respectively, to the NC Education Lottery Fund. As explained in Note 4C, \$6.5 million and \$3.5 million for the years ended June 30, 2009 and 2008, respectively, is the amount of the "Net Revenues" and "50% of Unclaimed Prizes" for the year not yet transferred to the NC Education Fund as of June 30, but will be transferred during the subsequent fiscal year.

## NOTE 13 – CHANGES IN FINANCIAL ACCOUNTING AND REPORTING

For the fiscal year ended June 30, 2009, the NCEL implemented the following pronouncements issued by the Governmental Accounting Standards Board (GASB):

GASB Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*.

GASB Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*.

GASB Statement No. 55, the statement incorporates the hierarchy of generally accepted accounting principles (GAAP) for state and local governments into the GASB's authoritative literature. It is intended to make it easier for preparers of state and local government financial statements to identify and apply the "GAAP hierarchy," which consists of sources of accounting principles used in the preparation of financial statements so that they are presented in conformity with GAAP and the framework for selecting those principles.

GASB Statement No. 56 is part of the GASB's effort to codify all generally accepted accounting principles for state and local governments so that they derive from a single source. This is intended to make it easier for preparers of state and local government financial statements to identify and apply relevant accounting guidance.

For the fiscal year ended June 30, 2010, the NCEL anticipates implementing the following pronouncement issued by the Governmental Accounting Standards Board (GASB):

GASB Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*.

GASB Statement No. 51, the Statement provides needed guidance regarding how to identify, account for, and report intangible assets.

## NOTE 14 – CONTINGENCIES

The NCEL has a potential commitment to the Internal Revenue Service (IRS) for an assessment made under IRC Section 6651 for the late deposit of withheld federal income tax. As of July 23, 2009, the commitment amount was less than \$400. This potential commitment results from an accounting processing change made in early 2008 that resulted in a short delay in remitting withheld income tax to the IRS. The NCEL, with the assistance of the North Carolina Office of the State Controller, has provided to the IRS-Office of Appeals documentation and other relevant information we believe fully justifies the abatement of this late deposit penalty. As of October 15, 2009, the NCEL has not received a response from the IRS-Office of Appeals.



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

To the Commissioners  
North Carolina Education Lottery  
Raleigh, North Carolina

We have audited the accompanying statements of net assets of the North Carolina Education Lottery (NCEL), a major enterprise fund of the State of North Carolina as of June 30, 2009, 2008 and 2007, and the related statements of revenues, expenses, and changes in fund net assets and cash flows for the years then ended, and have issued our report thereon dated October 15, 2009. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

As discussed in Note 2, the financial statements present only the NCEL and do not purport to, and do not, present fairly the financial position of the State of North Carolina, as of and for the years ended June 30, 2009, 2008, and 2007, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

**Internal Control over Financial Reporting**

In planning and performing our audit, we considered the NCEL's internal control over financial reporting as a basis for designing our audit procedures 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 NCEL's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the NCEL's internal control over financial reporting.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the NCEL's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the NCEL's financial statements is more than inconsequential will not be prevented or detected by the NCEL's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the NCEL's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the NCEL's financial statements are free of 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*.

This report is intended solely for the information and use of management, the Commissioners, others within the organization, and the State of North Carolina and is not intended to be and should not be used by anyone other than these specified parties.

CHERRY, BEKAERT & HOLLAND, L.L.P.

*Cherry, Bekaert & Holland L.L.P.*

Raleigh, North Carolina  
October 15, 2009

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