



STATE OF ILLINOIS
**OFFICE OF THE
AUDITOR GENERAL**

William G. Holland, Auditor General

SUMMARY REPORT DIGEST

DEPARTMENT OF THE LOTTERY

Financial Audit

For the Year Ended: June 30, 2012

Release Date: June 19, 2013

Summary of Findings:

Total this report:	2
Total last report:	0
Repeated from last report:	0

INTRODUCTION

This digest covers the financial audit of the State of Illinois, Department of the Lottery for the year ended June 30, 2012.

Effective October 15, 2011, the Department of Revenue transferred all functions performed for the Illinois Lottery and all associated powers, duties, rights and responsibilities to the Department of the Lottery in accordance with Public Act 97-0464. As a means of easing and transitioning, management elected to use an effective date of July 1, 2011 for the financial accounting and reporting.

SYNOPSIS

While performing audit procedures, auditors noted a number of errors, inaccuracies and weaknesses in the Department of the Lottery's (Department or Lottery) internal control structure. Because of the significance of the errors, inaccuracies and weaknesses the auditors considered them to be material weaknesses in the Lottery's internal control over financial and fiscal operations. A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. Auditors reported the following errors, inaccuracies and weaknesses at the Department:

- The Department's year-end financial reporting in accordance with generally accepted accounting principles (GAAP) to the Illinois Office of the Comptroller contained numerous errors, inaccuracies and incomplete data.
- Auditors noted a number of weaknesses related to the various computer systems utilized by the Department. Several of the Department's computer systems generate reports that are used to process, accumulate and analyze financial information.

{Financial data is summarized on the reverse page.}

**DEPARTMENT OF THE LOTTERY
FINANCIAL AUDIT
For the Year Ended June 30, 2012**

STATEMENT OF NET ASSETS (amounts in thousands)	June 30, 2012
ASSETS:	
Cash equity in State Treasury.....	\$ 141,986
Cash and cash equivalents	13,024
Accounts receivable, net of allowance of \$8,485.....	22,106
Investments (current and noncurrent).....	360,095
Capital assets being depreciated, net.....	229
Total Assets.....	537,440
LIABILITIES AND NET ASSETS:	
Prizes payable.....	151,565
Accounts payable and accrued liabilities.....	34,679
Due to other Government- Federal.....	27
Due to other State funds.....	18,624
Unearned revenue.....	5,427
Other liabilities.....	1,113
Long-term annuity prizes payable (current and noncurrent).....	300,719
Other noncurrent liabilities.....	920
Total Liabilities	513,074
Total Net Assets.....	\$ 24,366
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS (amounts in thousands)	FY 2012
OPERATING REVENUE:	
Charges for sales and services.....	\$ 2,676,996
Other.....	5,378
Total Operating Revenues.....	2,682,374
OPERATING EXPENSES:	
Cost of sales and services.....	151,421
Prizes and claims.....	1,620,405
General and administrative.....	152,210
Depreciation.....	107
Total Operating Expenses.....	1,924,143
Operating Income.....	758,231
NONOPERATING REVENUES (EXPENSES):	
Investment income.....	37,633
Interest expense.....	(17,192)
Total Nonoperating Revenues (Expenses), net.....	20,441
Changes in Net Assets Before Transfers.....	778,672
Transfers to other State funds.....	(758,236)
Change in Net Assets.....	20,436
Net Assets, July 1, 2011, as restated.....	3,930
Net Assets, June 30, 2012.....	\$ 24,366
SUPERINTENDENT	
During Engagement Period: Victor Golden (acting) 07-01-2011 through 10-09-2011; Michael Jones, effective 10-10-2011	
Currently: Michael Jones	

FINDINGS, CONCLUSIONS, AND RECOMMENDATIONS

NEED TO IMPROVE FINANCIAL REPORTING

The Department of the Lottery's year-end financial reporting in accordance with generally accepted accounting principles (GAAP) to the Illinois Office of the Comptroller contained numerous errors, inaccuracies and incomplete data.

During the audit of the June 30, 2012 Lottery financial statements the auditors noted errors in the GAAP Reporting forms and Department financial statements and deficiencies in internal controls over financial reporting. Some of the items noted follow:

- During planning for the financial audit, the auditors inquired of Lottery management to obtain an understanding of the general control environment over financial reporting. Though the Lottery has formal procedures related to the accumulation and processing of financial information, the auditors noted weaknesses. Specifically, the auditors noted that: (1) not all manual journal entries were reviewed by a person other than the preparer, (2) certain account reconciliations were not prepared or maintained, (3) account reconciliations, when performed, did not document that they had been reviewed by a person other than the preparer, and (4) supporting documentation that agreed to amounts in the financial records was not always readily available.
- Historically, the Lottery had made cash transfers to the Common School Fund in excess of their income before transfers. These excess cash transfers were reported as "Due from Other State funds" in the Lottery's financial statements. During testing, the auditors noted the "Due from other State funds", did not meet the criteria for being reported / recorded as a receivable. Subsequently, the Lottery, in conjunction with the Illinois Office of the Comptroller, concluded the balance should be eliminated and considered a prior period transfer. This account was reported in the Lottery's accounting records to the auditors with a balance of approximately \$69.9 million.
- The auditors noted the prizes payable liability did not agree to underlying/supporting records. During Department management's subsequent review of the data, missing reconciling items were identified. One item identified resulted in an overstatement of the liability of \$30.3 million. Department management appropriately recorded an entry to account for this reconciling item.

Weaknesses noted in review of journal entries and general ledger account reconciliations

Prior excess cash transfers reclassified

Prize liability did not agree to underlying/supporting records

- Transfers to Capital Projects Fund; The Illinois Lottery Law (20 ILCS 1605/9.1(o)), as amended by Public Act 96-0034 effective July 1, 2009, requires the Lottery to distribute all proceeds of lottery tickets and shares sold in a specific priority and manner. The last priority requires the Lottery to transfer any remaining proceeds to the Capital Projects Fund on or before the last day of each fiscal year. Since the change in the Lottery Law, the Lottery has made an estimate of the remaining proceeds and made the required transfer based on that estimate. As a result of normal adjustments and completion of the annual audit, there has been a difference between transfers of estimated remaining proceeds and actual net income. As of June 30, 2012, the Lottery has recorded a balance of \$18.6 million due to the Capital Projects Fund, reflecting actual net income in excess of amounts previously transferred to the Capital Projects Fund through that date. The Lottery needs to establish a policy to allow for amounts deposited into the Capital Projects Fund at the end of each fiscal year to be adjusted in the subsequent fiscal year to reflect the final distributions due. This amount should be based upon the actual results of operations for such fiscal year. The policy should be supported by the Lottery Law and legal determinations.

Transfers to Capital Projects Fund

Adjustments decreased expenses \$106.3 million

The aggregate impact of all of the adjustments made since the initial June 30, 2012 GAAP Reporting Forms were submitted to the Illinois Office of the Comptroller was a \$63.0 million increase in assets, a \$45.7 million decrease in liabilities, a \$106.3 decrease in expenses and a \$1.5 million increase in revenue.

The errors and inaccuracies noted, if not detected and corrected, can materially misstate the Lottery's financial statements and negatively impact the statewide financial statements. Accurate and timely preparation of the Lottery's financial information is important and impacts the statewide financial statements reporting process. (Finding 12-01, pages 24-27).

We recommended the Lottery implement procedures to ensure GAAP Reporting Packages and financial statements are prepared in an accurate and complete manner.

Lottery agrees with auditors

Lottery Management agrees and indicated they will review current procedures to ensure they are up-to-date and implement any additional procedures, as necessary, to ensure GAAP financial reporting and financial statements are prepared completely, accurately and timely with appropriate supporting documentation.

NEED TO IMPROVE GENERAL INFORMATION TECHNOLOGY ENVIRONMENT OVER KEY SYSTEMS

Control deficiencies noted in Department's computing environment

During the audit of the June 30, 2012 financial statements, the auditors noted a number of control deficiencies related to the various computer systems utilized by the Department. Several of the Department's computer systems generate reports that are used to process, accumulate and analyze financial information. Specific areas where weaknesses were identified are as follows:

Six areas noted with weaknesses

- Change Management
- Segregation of Duties
- Documented Access Reviews
- Password Complexity
- Security Policy
- Excessive Access Rights to the Drawing Room

The areas noted with weaknesses have specific controls that are considered to be key controls which should be in place and functioning in the Department's computing environment to prevent or detect unauthorized access or changes to the Department's systems. (Finding Code No. 12-02, pages 28-30).

We recommended the Department implement and document the controls over its computing environment and ensure the controls provide sufficient protection against unauthorized access and inappropriate changes.

Lottery agrees with auditors

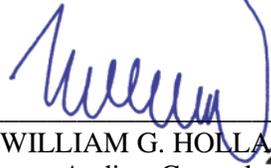
The Lottery management agrees and: 1) commented on compensating controls, and 2) they intended to improve controls in their computing environment.

DELAY IN FINANCIAL REPORTING AND AUDIT COMPLETION

The conditions noted by the auditors during the course of the engagement negatively impacted the ability to complete the financial audit before May 29, 2013. These conditions also impacted the completion of the statewide financial statements prepared by the Office of the State Comptroller and our audit thereon.

AUDITORS' OPINION

The auditors stated the Department of the Lottery financial statements as of June 30, 2012 and for the year then ended were presented fairly in all material respects.



A handwritten signature in blue ink, appearing to read 'William G. Holland', is written over a horizontal line.

WILLIAM G. HOLLAND
Auditor General

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SPECIAL ASSISTANT AUDITORS

KPMG LLP were the Special Assistant Auditors for this engagement.