

MISSISSIPPI LOTTERY CORPORATION

CHAPTER 11 – FINANCE POLICIES

11.3 SIGNIFICANT ACCOUNTING PRACTICES

Rule 11.3.01 PURPOSE

This policy documents significant accounting practices of the Mississippi Lottery Corporation (“MLC”) relating to revenue, expenses, and the use of estimates in determining and reporting the overall financial results of the MLC.

Rule 11.3.02 BASIS OF PRESENTATION

The financial statements are prepared in conformity with the accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board. MLC is considered a public entity as established by the Alyce G. Clark Mississippi Lottery Law (“Act”).

Rule 11.3.03 BASIS OF ACCOUNTING

The MLC is accounted for as a business-type activity and is a discretely presented component unit of the State of Mississippi. The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. Under this method, revenues are recognized when they are earned and expenses are recognized when a liability is incurred, regardless of the timing of related cash flows.

Rule 11.3.04 REVENUE RECOGNITION

Revenue is recognized for instant games when retailers make them available for sale to the public, as indicated by the retailers’ activation of tickets. Certain instant games include free tickets, which entitle the holder to exchange one instant ticket for another of equal value. The selling price of free tickets reduces instant ticket revenue when the free ticket is claimed by a player.

Revenue is recognized for terminal-based drawing-style games based on the game characteristics. Revenues for drawing-style games whereby the prize expense is only determinable at the time of the related drawing will be recognized when the tickets are sold to players and the drawing occurs. Revenue collected from retailers for these games sold in advance of the draw are recorded as deferred revenue and recognized as the draw occurs.

Rule 11.3.05 ACCOUNTS RECEIVABLE

Retailer accounts receivable represents lottery proceeds due from retailers for net ticket sales and weekly fees less commissions and prizes paid by the retailers. Lottery proceeds are collected from retailer bank accounts established in trust for the MLC. Retailers are invoiced for net proceeds on a weekly basis for all billable activity from Sunday through Saturday.

Lottery proceeds for instant tickets sold by retailers are due and payable to the MLC upon pack settlement in accordance with Section 2.11(C) of Retailer Rules and Regulations. Proceeds for drawing-style tickets sold by retailers are due and payable on the date of sale. Instant Tickets will be settled in accordance with MLC's Retailer Rules and Regulations Policy Section 2.11(C).

Retailers are provided notice of funds due to the MLC via electronic statements available at the retailer's terminal on each Sunday after close of the accounting week which occurs at 11:59:59 pm on Saturday night of each week.

The MLC will record a bad debt expense and related allowance for bad debts based on a quarterly review of outstanding retailer accounts receivable as a result of non-payment. The outstanding balances will not be written off against the allowance account until management determines such account is deemed non collectible. Retailers will be charged NSF fees in accordance with MLC's Retailer Rules and Regulations Policy Section 2.12 (C).

Rule 11.3.06 RETAILER PAYMENTS

Retailers receive a commission of 6.0% on all instant tickets settled and drawing-style tickets sold. The commission expense is recorded in the period of the related ticket sales or settlements. Where commission has been paid to retailers for deferred ticket sales, this fee is recorded as a prepaid expense until the related revenue is recognized.

Rule 11.3.07 PRIZE EXPENSE

In accordance with the Act, at least 50% of ticket proceeds must be made available as prize money. The MLC recognizes prize expense in the period of related revenue recognition, regardless of when prizes are actually claimed by the player.

Gross prize expense for instant ticket sales is recognized based on a predetermined prize payout for each game and adjusted when a game ends. The Instant Ticket vendor will supply the MLC with an end of game prize structure adjusted for actual prizes claimed. The prize structure is included as part of each instant game's working papers, which is the contractual commitment for the instant vendor to produce the game at a predetermined payout.

Mississippi Lottery Corporation prize expense is recognized for terminal-based drawing-style games at 50-55% of net ticket sales (gross ticket sales less free ticket prizes) depending on the amount of prize payout allocated for each draw game.

Powerball prize expense is recognized as a percentage (%) of ticket sales in accordance with the game rules and the contractual agreement (PB Rule 28). Powerball prizes are shared based on contributions to the prize pool by all member lotteries of the Powerball Group of MUSL. All Powerball grand prizes won by players who purchase tickets in Mississippi, and choose to be paid on an annualized basis, will be funded by investments purchased by MUSL. The investments will be held by MUSL in trust for the MLC. The MLC will record the related activity in the financial statements as a receivable from MUSL and a corresponding deferred prize payable to the winner.

Mega Millions prize expense is recognized as a percentage (%) of ticket sales in accordance with the game rules and the contractual agreement (MM Rule 28). Mega Millions prizes are shared based on contributions to the prize pool by all member lotteries of the Mega Millions Group of MUSL. All Mega Millions grand prizes won by players who purchase tickets in Mississippi, and choose to be paid on an annualized basis, will be funded by investments purchased by MUSL. The investments will be held by MUSL in trust for the MLC. The MLC will record the related activity in the financial statements as a receivable from MUSL and a corresponding deferred prize payable to the winner.

Rule 11.3.08 UNCLAIMED PRIZES

Prizes not claimed within 90 days of the announced end-of-game date for instant games, and within 180 days of the drawing for all terminal-based drawing-style games, are forfeited as unclaimed prizes.

The MLC records estimated unclaimed prizes for each instant game within the month the game is closed and reconciles the actual amounts when the claim period ends. For terminal-based drawing-style games, the MLC records the actual unclaimed amounts determined after the expiration of the related claim period for the draw.

Rule 11.3.09 CONTINGENCIES

Liabilities for loss contingencies arising from claims, assessments, litigation, fines and penalties, and other sources will be recorded when it is probable that a liability has been incurred and the amount of the liability can be reasonably estimated.

Rule 11.3.10 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 certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures

of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

The MLC uses estimates in the recognition of game prize expense as defined in this policy and in recognition of certain prizes payable and unclaimed amounts. Estimates are also used in recognizing other significant expenses, such as compensating absences, sales-related commissions and bad debt. These estimates and assumptions are reviewed periodically and the effects of revisions are reflected in the financial statements in the period they are determined.