



# MEMORANDUM

**To:** California State Lottery Commission      **Date:** May 20, 2008

**From:** Joan M. Borucki  
Director

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**Subject:** Item 9(e) – Amendments to Lottery Regulations – Retailer  
Compensation

## **ISSUE**

Should the California State Lottery Commission (Commission) adopt amendments to the Regulations to give the Lottery Director (Director) the authority and flexibility to enter into alternative compensation agreements with retail partners operating under different business models from traditional Lottery retailers?

## **RECOMMENDATION**

California State Lottery (Lottery) Staff recommends that the Commission adopt amendments to the Regulations to give the Director the authority and flexibility to enter into alternative compensation agreements with retail partners operating under different business models upon notification of the Commission Chair.

## **BACKGROUND**

The Commission approved changes to the regulations on February 28, 2007 that gave the Director the authority to enter into alternative compensation agreements to pilot test new business models. A pilot test with CVS Pharmacy was undertaken

beginning in early March, 2007. A total of 29 locations were included in the test, with 17 of these stores being existing Lottery retailers and 12 stores never having sold Lottery as CVS locations. At all pilot locations, self-service devices that sell both Scratchers tickets and draw game tickets out of the same machine were installed.

A different model for business between the California State Lottery and the retailer was tested in that the Lottery had significantly more responsibilities over the equipment and tickets than with other retailers. With less responsibility, CVS did not receive compensation based on the traditional form of a percentage of sales.

## **DISCUSSION**

Overall, the Lottery and CVS are pleased with the results from the pilot test. Very quickly Scratchers sales in these stores were at levels above the per store average for drug stores in general. However, draw game sales are still below the sales levels of typical stores in this trade channel. The Lottery is addressing this issue and anticipates that draw game sales will grow over time. Store sales vary based on such factors as placement of the machine, signage, general store traffic and lottery sales history.

In addition, the pilot test showed that a different business arrangement can work for both the new retail organization as well as the Lottery. Based on the pilot test, CVS is interested in expanding the program to all 375 stores in California. During the test, Lottery staff learned what elements of the new business model worked well and which areas need to be modified. Changes to the current agreement would be addressed if the CVS pilot were rolled out statewide.

Section 8880.51 of the Lottery Act stipulates that “unless the Commission shall otherwise determine, the compensation paid to Lottery Game Retailers shall be a minimum of 5% of the retail price of tickets or shares.” The proposed amendment to the regulations grants the Director the authority to negotiate and develop alternative ways of doing business with other retail organizations – including plans that result in compensation that is less than 5% of retail sales. The regulations call for the Chair of the Commission to consent to the alternative compensation model prior to it’s becoming effective.

In addition, the Director will report to the Commission on a bi-annual basis to inform them of the various compensation packages being used by the Lottery.

Allowing the Director to negotiate and enter into new business models and alternate compensation structures will allow the Lottery to keep up with changing consumer shopping habits and retail trends. There are many types of locations that currently

do not sell Lottery tickets, and staff believes that alternative business models can be developed so many of these chain retailers can become Lottery locations. The proposed regulations do not assume that just one new business model will be adopted. It provides for flexibility to tailor a program to the needs of the specific retail organization.