



M E M O R A N D U M

Date: September 3, 2009

To: California State Lottery Commission

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Director

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Subject: Item 9(h) – Gaming Contract Amendment

ISSUE

Should the California State Lottery Commission (Commission) approve an amendment to the California State Lottery (Lottery) Gaming Contract #7871 with GTECH Corporation (GTECH) that reflects the Lottery's change of focus from increasing retailers to investing in the existing retailer network through the use of innovative messaging devices and enhanced player services?

RECOMMENDATION

Lottery staff recommends that the Commission approve the requested amendment to Gaming Contract #7871 with GTECH. The amendment will extend the term of the GTECH contract for gaming and telecommunication services for one additional year and will allow the Lottery to acquire a total value of over \$17.3 million in products and services focused on innovative messaging devices and enhanced player services instead of \$10.5 million of gaming equipment that is no longer needed for retailer expansion. This amendment provides the Lottery with an additional value of over \$6.7 million that consists of gaming system equipment, software enhancements, and services. The amendment will increase the total expenditure authorized by \$65 million, which will cover additional costs through October 13, 2014.

BACKGROUND

As the result of a formal, competitive solicitation, the Lottery awarded a six-year contract to GTECH Corporation in 2002 with a total expenditure authority of \$300 million based on a sales compensation rate of 1.36%. The original term of the contract was from October 14, 2003 through October 13, 2009, but the contract's terms allow the Lottery to extend the term of the contract for up to four additional one-year periods. At the end of the four one-year options, the contract may remain in effect under the same terms and conditions until either party provides a two year advance notice of termination.

In July 2008, the Commission approved an amendment to extend the term of the gaming system contract with GTECH for four additional years (exercising the four one-year options) while maintaining the current base compensation rate of 1.36% of sales (with a reduced compensation rate for sales above \$4 billion). In return, GTECH agreed to provide the Lottery with a total value of over \$40 million that consisted of equipment, gaming system software enhancements, and discounts on future equipment orders. The amendment increased the spending authority by \$310 million and extended the contract through October 13, 2013.

The services being provided under this contract include an integrated gaming system that manages millions of gaming-related transactions through a satellite telecommunications network; provision, installation, and maintenance of 50,000 gaming equipment units in over 21,000 retailer locations across the state; software development and support for the core gaming and administrative applications; and marketing and research services that support the Lottery's gaming operations.

DISCUSSION

At the time of the July 2008 amendment, the Lottery's long-term Business Plan called for retailer recruitment, therefore the contract extension included the necessary equipment to support additional retailers. Though we have added two thousand retailers in the past three years, due to the declining economy, the recruitment of quality retailers became difficult. Our focus became sustaining our retailer numbers and investing in ways to increase revenue to our existing retailer network. Rather than acquiring an additional \$10.5 million of gaming equipment described in the July 2008 amendment, the Lottery began analyzing other options. Approval of this recommendation will allow the Lottery to replace the unnecessary equipment with a total value of over \$17.3 million in products and services, focused on innovative messaging devices to attract players at retailer locations and additional player services.

These products and services will allow the Lottery to be the first lottery in the nation to deploy such innovative ideas. The Lottery has been successful with an electronic multi-media "point-of-sale" system (ePOS) that has increased sales by 10% in retailers with ePOS. Building on this success, the Lottery will install ePOS monitors on Self-Service Terminals and will perform a pilot on the next generation of ePOS in

Lottery play centers. This next generation of ePOS will provide enhanced content and robust messaging with the ability to update content in minutes, and it will become a destination for Lottery players in retailer locations. To increase the flow of information to players, we will install in retailer windows bright and colorful lighted jackpot amount signs that are wirelessly updated by the gaming system. Through GTECH's new player platform, the Lottery will expand the Jackpot Captain and Replay programs by creating a player loyalty program and other future programs that will provide more services, such as customized promotions, to Lottery players.

With the approval of the one-year amendment to extend the term of the GTECH contract, the new expiration date of this contract will be October 13, 2014 and the total expenditure authority will not exceed \$675 million.