



M E M O R A N D U M

Date: June 26, 2009

To: California State Lottery Commission

From: Joan M. Borucki
Director

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Subject: Item 9(e) – Extension of the United Parcel Service (UPS) Contract

ISSUE

Should the California State Lottery Commission (Commission) approve an amendment to the UPS Scratchers® Ticket Delivery contract to extend the contract term for one year with an additional expenditure authority of \$3.6 million for a total contract expenditure authority of \$14.1 million for Contract #11710?

RECOMMENDATION

Staff recommends that the Commission approve an amendment to the UPS Scratchers Ticket Delivery contract to extend this contract for one year. To accommodate this extension, staff recommends that the Commission approve an additional expenditure authority of \$3.6 million for a total contract expenditure authority of \$14.1 million for Contract #11710. This extension deal will result in ticket delivery cost savings to the California State Lottery (Lottery).

BACKGROUND

A key component of the Lottery's product line is its instant games, known as Scratchers. Each year, the Lottery introduces between 40 and 45 new Scratchers games and Scratchers account for approximately half of annual Lottery sales. The Lottery has used a contracted Scratchers ticket delivery service to deliver Scratchers tickets to our retailers since sales began in 1985. Over the course of the last 24 years, Scratchers sales have grown to the point where we currently ship around 60,000 orders (or about 585,000 packs of tickets) to our retailers each month.

On August 9, 2006, the Commission awarded UPS a three-year contract for Scratchers delivery services with the option to extend an additional two years and a total expenditure authority of \$10.5 million. The contract began on August 20, 2006 and it will expire on August 19, 2009.

The current contract with UPS requires that all deliveries must be made with 48 hours of pick-up from the Lottery's two Distribution Centers. The current contract also requires UPS to provide two full-time staff for each of the Distribution Centers to assist with shipping Scratchers orders and producing bar-coded shipping labels for each delivery.

DISCUSSION

UPS was awarded the Scratchers Delivery Services contract based in large part on its excellent pricing proposal of \$4.15 per delivery for the first year with relatively modest increases of 15 cents per delivery in each of the two subsequent years of the contract. Accordingly, the Lottery now pays UPS \$4.45 per delivery. The current contract allows UPS to raise their rates by an additional 16 cents per delivery in each of the two 1 year contract extension periods (to \$4.61 and \$4.77 respectively).

In preparation for the impending expiration of this contract, the Lottery invited UPS to propose a cost per delivery that would reduce the Lottery's expense in exchange for a contract extension. UPS responded by offering to maintain its rates at the current level of \$4.45 per delivery for a one-year extension thus saving the Lottery approximately \$115,000. It is also important to note that, because UPS is offering a fixed cost per delivery regardless of the size or weight of the order, if Scratchers sales increase significantly over the course of the next 12 to 14 months, the Lottery will not incur any additional expense associated with the delivery of larger orders of tickets.

The Lottery has also assessed UPS's overall performance during the last three years in making this recommendation to extend the current contract. The Lottery is very pleased with the services that UPS has provided. Our assessment of their performance revealed that UPS is very well recognized by our retailers, they have provided timely and accurate delivery services, and they have provided all of the equipment necessary to produce bar-coded shipping labels as well as the required support staff to assist with packaging and shipping thus saving personnel costs that would otherwise be incurred by the Lottery.

Based on UPS's favorable pricing proposal and their satisfactory performance to date, staff recommends that the Lottery exercise the first of two available one-year contract extension options. This extension will require an additional expenditure authority of \$3.6 million to cover Scratchers ticket delivery costs. With the one-year extension, the new contract expiration date will be August 19, 2010 and the total contract expenditure authority will be \$14.1 million.