



M E M O R A N D U M

Date: December 9, 2010

To: California State Lottery Commission

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Director

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Subject: Item 9(b) Amendment to Business Planning Contract

ISSUE

Should the California State Lottery Commission (Commission) approve an amendment to the business planning consulting contract with Camelot Global Services Limited (Camelot) for assistance in fully implementing the California State Lottery's business plan?

RECOMMENDATION

California State Lottery (Lottery) staff recommends that the Commission approve an amendment to the business planning consulting contract with Camelot for assistance in implementing the Lottery's business plan. Staff believes that this amendment will facilitate the full implementation of fundamental improvements to Lottery operations and significantly improve the Lottery's performance.

BACKGROUND

In June 2009, the Commission approved a consulting contract with Camelot for assistance in developing and implementing the Lottery's business plan with a total expenditure authority of \$13.5 million to cover a four year contract period from July 2009 through July 2013. The requested amendment to the current contract does not require any changes to this expenditure authority.

DISCUSSION

With Camelot's assistance, the Lottery has developed a three year 2010-2013 Business Plan that was approved by the Commission on May 20, 2010 and set a course toward sustainable growth and improved performance that will help it meet its mandate to education. There is undeniable evidence that implementation of the strategies in our business plan are starting to take effect and have had a positive impact on sales – we are now starting to see significant sales increases both as a result of AB 142 and the Renew initiatives that the Lottery has been implementing pursuant to these strategies.

There are a number of strategic initiatives currently in progress that are still critical to delivering this year's sales goals and providing the foundation for ongoing mid to long term growth and we don't want to lose momentum due to a gap in performance. In addition, as we have moved forward integrating the strategies, processes and procedures developed to achieve our business goals, it has become apparent that the Lottery significantly underestimated the number of days required to achieve these aggressive initiatives and that the Lottery will benefit from additional help from the Camelot team to accomplish the tasks identified by the numerous implementation project teams staffed by Lottery employees and advised by Camelot subject matter experts.

This proposed contract amendment will ensure that there are no gaps in work performed by Camelot due to the 400-contract-days-per-year limit set in the original contract. This amendment will also provide time for full implementation of the business plan strategies but, more importantly, it will allow time for the transfer of business knowledge and tools to Lottery staff, ensuring continued success and growth long after the engagement of Camelot has concluded by raising the contract day cap for the term of the engagement from 1,000 to 3,913 contract days.

There are two important principles set out in the original contract. These two principles remain. First, Camelot is paid for consulting services based on completion of specific deliverables (in the case of the business strategy), or, days actually expended (in the case of strategy implementation). The rate for these services reasonably enables Camelot to cover their own costs, but is significantly below market rate for strategic high value consulting services. Second, the payment of performance fees is a profit incentive for Camelot based on the realization of incremental profits to the Lottery of successfully implementing the strategy. With this construct, the contract establishes a complete alignment of incentives for the two organizations.

This amendment creates a provision to extend the number of implementation days, which are paid for according to exactly the same principles as the original contract. The performance incentive remains exactly that – an incentive for successful realization of the strategy with Camelot only benefitting if the implementation of the strategy is successful.

Contract Amendment Proposal

The proposed contract amendment will allow the Lottery to capitalize on the progress made to date and ensure the Lottery continues to benefit from the skilled resources required to deliver the business strategy, the projected net income growth and create a self-sustainable foundation going forward. It is therefore proposed that the following changes are made to the current consulting contract terms:

1. Removal of the 400 contract day limit and replace with annual invoicing goals that are aligned to the resourcing plan attached.
2. The staff day cap for Phase 2 will be increased from 1,000 days to 3,913 days.
3. The expenditure cap for Phase 2 will be increased from \$900,000 to \$3,521,000.
4. The staff day cap for Phase 3 will be increased from 744 days to 949 days.
5. The expenditure cap for Phase 3 will be increased from \$1,200,000 to \$1,684,000.
6. The maximum possible performance fee to be earned by Camelot will be reduced by \$3.105 million to \$6.895 million.

The following contract terms will not change:

1. The total amount of contract to remain at \$13.5 million.
2. The rate for implementation support will remain at \$900/day.
3. The rate for project management support will remain at \$1,613/day.
4. The performance fee rebate payment at the \$5 million performance fee level will remain.

CONCLUSION

With the Commission's approval, staff will move forward with the contract amendment and continue uninterrupted implementation of the Lottery's business strategy.

Changes to the economic fundamentals of the contract can be summarized as follows:

Consultancy Days				
	Contract	Proposed Days	Proposed Inc Contingency	Variance
Phase 1	n/a	n/a	n/a	n/a
Phase 2	1,000	3,557	3,913	2,913
Phase 3	744	949	1,044	300
	1,744	4,506	4,957	3,213

Consultancy \$'000				
	Contract	Proposed Cost	Proposed Inc Contingency	Variance
Phase 1	1,400	1,400	1,400	0
Phase 2	900	3,201	3,521	2,621
Phase 3	1,200	1,531	1,684	484
	3,500	6,132	6,605	3,105