



it's good to play

Transition Document, Executive Cabinet, Tier One Report

Agency Name: Washington's Lottery
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Agency Responsibilities:

It is the Lottery's mandated responsibility to financially contribute, through the sale of lottery tickets, to the following state-named beneficiaries:

- The Education Construction Account
- Debt reduction for Safeco and Qwest stadiums
- The General Fund when applicable (see asterisk below)

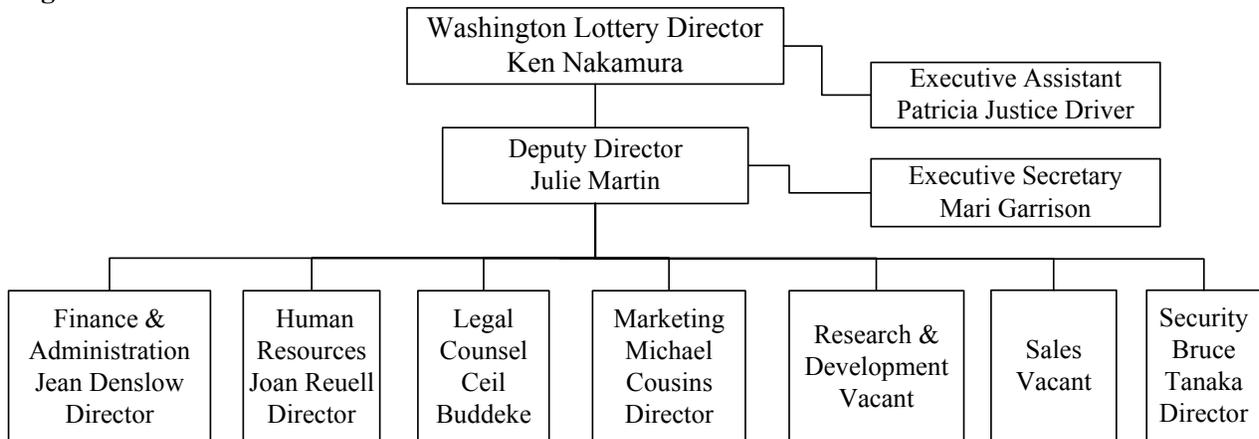
Money from sales flows through the Lottery; prizes, commissions, game and operating costs are deducted, and the profit is then distributed.

05-07 Biennium Budget by Source and Program: Program 010, Agency Code 116

Sales	Projected Sales		\$930,200,000	
Cost of Games Fund 433, Fund 577	Shared Game Lottery Account (<i>Mega Millions</i>) & State Lottery Account (all other games)	Non- appropriated	\$702,271,000	Prizes, Retailer Commissions, Vendor Payments, Marketing
Operating Costs Fund 578	Administrative Account	Appropriated	\$ 22,915,000	Operations
Profit Distributions	Education Construction Account*		\$180,022,113	
	Stadiums		\$ 24,991,887	

* If moneys eligible for the Education Construction Account exceed \$102 million in one year, the excess is distributed to the General Fund.

Organization Chart:



In addition, there is a Lottery Commission, comprised of five members appointed by the Governor to rotating six-year terms.

Background:

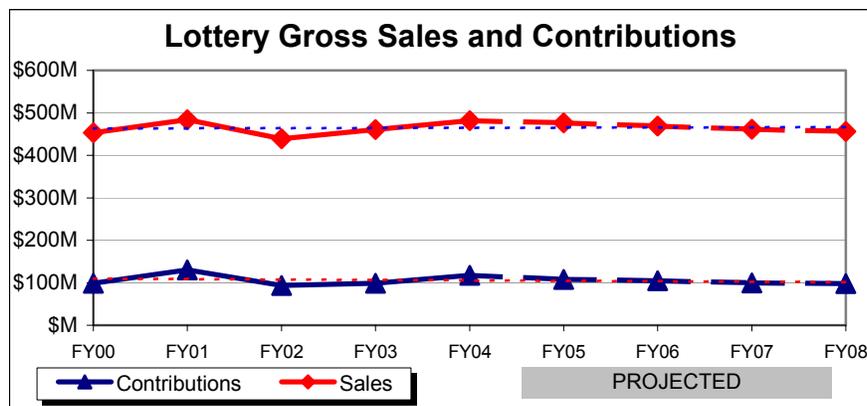
- ❖ Our product line currently consists of two types of games:
 - “Instant” games, with tickets produced with preprinted numbers, and winning numbers predetermined at time of production (e.g., “Scratch” tickets)
 - “Draw” games, with numbers printed only at time of sale, and winning numbers selected by drawing after close of sale (e.g., *Lotto*, *Mega Millions*)
- ❖ Approximately 3500 retailers across the state partner with the Lottery to sell our products.
- ❖ Gross sales revenue is first adjusted for winner prizes, retailer commissions, and other contractual costs of sales, then is distributed to state-mandated beneficiaries (currently education construction and Safeco and Qwest stadiums, with a provision for excess funds to go to the General Fund.)
- ❖ Approximately 150 full- and part-time employees staff the organization statewide, and are assisted by two major vendors providing specialized game production and communications services.

Major Issues:

1. Lottery sales are nearly flat in today’s dollars, and are declining in purchasing power.

What is the issue?

Gross Lottery sales show flat to minimal growth from FY 2000 through FY 2004. However, Lottery contributions to state-designated beneficiaries are projected to decline. When adjusted for inflation/purchasing power (not shown on chart), the decline is even more pronounced.



Without significant legislative adjustment to our authorized product lines, this negative trend is expected to continue.

What is the urgency?

There is continued pressure on the Lottery to provide more funding from its ticket sales. At the same time, some of the changes needed to do so require legislative action. It is important that legislators fully comprehend this dilemma as they approach the new session.

Why is it significant? If controversial, why?

This issue is significant for several reasons.

- Lower Lottery contributions mean the state must either finance existing beneficiaries from other funds or reduce their funding.
- Flat Lottery sales mean that rapidly growing gaming dollars are being spent in other gaming venues, none of which contribute their profits to the state.

The issue is controversial because it requires legislators

- to either confirm that a flat trend in sales from traditional Lottery products is acceptable
- or to take legislative action (e.g., allow an expansion of the Lottery’s game menu) to reverse that downward trend. Issues such as problem gambling could be raised.

Who are the key players/stakeholders?

- Governor
- State legislators
- Lottery Retailers
- Funding beneficiaries (the education community, stadiums, and General Fund recipients)

What is the status now and timeline for conclusion or resolution?

The Lottery does not take a position on whether or not its product lines should be expanded or its product access enhanced. However, in order to make sure this important trend data was in the hands of state decision makers, the Lottery produced a detailed Business Plan and a synopsis version entitled “State of the Lottery” earlier in 2004. These documents were discussed with Governor Locke and staff in August and September, 2004. At this time, we are awaiting feedback on strategic direction for the Lottery.

Links to websites with additional background information

<http://www.walottery.com/>

Staff contact(s) with e-mail address and phone number

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2. Rapid growth of tribal gaming results in substantial - and protected - competition.

What is the issue?

- Newly available 2004 data from the Washington State Gambling Commission show that the Washington State gaming market expanded 322 percent from FY 1996 to FY 2004, in terms of “net wins” (wagers minus prizes).
- The latest data also show that, from FY 2000 to FY 2004, tribal casinos’ market share grew from approximately \$280 million to \$888 million in net wins (or 317 percent).
- Instead of growing, Lottery net wins remained static.

What is the urgency?

- The state does not receive any share of profits from tribal casinos.
- By contrast, all Lottery income over and above the cost of doing business flows to state-designated beneficiaries. In FY 2004 that contribution amounted to **\$117.6 million**.

Why is it significant? If controversial, why?

- By virtue of state-negotiated compacts, tribal casinos are able to offer players cutting edge games prohibited to non-tribal gaming entities, including the Lottery.
- Traditional Lottery products struggle to compete with the excitement of tribal games.
- Other gaming entities are aggressively working to level the playing field. With approximately 70 percent of all U.S. casino revenues now coming from video “slot” machines, and only tribal casinos allowed to offer these in Washington, private casino operators have mobilized to achieve parity in their own game offerings (I-892.) Should I-892 pass and private casinos gain the ability to modernize and expand their game offerings to include video “slot” machines, the Lottery faces even stronger competition for gaming dollars.

Who are the key players/stakeholders?

- Lottery retailers
- Traditional lottery players
- Public education community

What is the status now and timeline for conclusion or resolution?

Until now, tribal casinos and the Lottery have offered different products. However, in an overt strike at the Lottery’s premium product line - “Scratch” tickets - one tribal casino now advertises its own scratch-off tickets, stating that they provide much greater rewards than the Lottery’s. This situation has no foreseeable resolution.

Links to websites with additional background information

None at this time

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3. Gaming via networked systems (Internet, mobile devices, interactive television) can offer a huge opportunity or overwhelming competition.

What is the issue?

The gaming industry is migrating toward electronic customer service, providing access to games via the Internet and mobile devices. Although Internet gaming is illegal in the United States, fully functional Internet purchase and wagering account management is already offered outside the U.S., including in Canada. Many U.S. residents participate now in Internet gaming; being illegal has neither shut down these sites nor prevented Washingtonians from using them.

What is the urgency?

U.S. law is currently being tested in the courts (by the World Trade Organization.) Lottery overseers must understand and be prepared to deal with the consequences of a court decision opening the door to this kind of entertainment in our own state.

Why is it significant? If controversial, why?

The potential for gaining or losing revenue by being ready (or not) for electronic games is massive. As of 2003:

- 50 percent of all world gaming was in offshore lotteries.
- An estimated 1500 to 1800 Internet gaming sites were up and running.
- Internet gaming generated \$6 billion in sales.
 - 53 percent to 60 percent of those sales came from U.S. players.
- Internet gaming is projected to double (sales of \$12 billion) by 2006.

Who are the key players/stakeholders?

- Federal and state law makers
- Game players
- Offshore lottery businesses

What is the status now and timeline for conclusion or resolution?

The industry is growing exponentially and there is no foreseeable resolution.

Links to websites with additional background information

None at this time

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4. Original product lines are aging.

What is the issue?

Scratch games were the Lottery's first product, launched in 1982. Draw games were launched in 1984. Both products have returned sizeable revenues to the state. With variations, enhancements and graphics, every attempt is made to keep these basic products exciting, attractive and fun to play. However, the mechanics of play and of access to play have not changed in over 20 years. Monumental changes in the way today's consumers access entertainment means the Lottery must update its game offerings and its product access.

What is the urgency?

Competitors offer new games of chance and new ways to play them. Players are flocking to these games. Younger game players, our primary *Scratch* customer segment, show a marked preference for games they can readily access (on-line or via mobile communications devices). They also prefer games they can play socially (i.e., through in-person or electronic interactivity). None of the Lottery's existing products meet those requirements.

Why is it significant? If controversial, why?

Prohibited from launching most of the competition's new games, either by law or by expressed political opposition, the Lottery risks losing customers and revenue. The issue is controversial because these games would expand opportunities for players to risk discretionary dollars. On the other hand, with these games missing from the Lottery's play menu, players may simply move to other venues where they can play newer games.

Who are the key players/stakeholders?

- Governor
- State Legislators

What is the status now and timeline for conclusion or resolution?

Legislation permitting businesses to install video lottery terminals (VLTs) was considered during the state's 2003 session, but did not pass. Installed in adult social settings, VLTs have attracted players in other states. Another proposal dealt with changing a once/day drawing game to a multi-draw game. That proposal, also proving popular in other states, failed to garner political support. At this time it is unknown whether any legislators or Washington's new Governor will support a revitalized Lottery games menu.

Links to websites with additional background information

None at this time

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5. A cumbersome business model, part governmental and part entrepreneurial, exerts conflicting demands on Lottery staff.

What is the issue?

Lottery staff is charged with generating ever-expanding sales, but must adhere to legislative timelines and considerations to do so. A successful sales organization must be able to quickly implement change as it meets rapidly changing customer requirements. Not only must the product line continuously offer new value but product access must also be able to change with the times. With an appropriated administrative budget, many new Lottery business needs must go through the legislative budget process. Due deliberation is, by its nature, likely to conflict with rapid customer response. Legislators, required to make business decisions in the midst of their governmental responsibilities, are at risk of losing or delaying additional revenues or savings that could result from a quick organizational decision. A non-appropriated, privatized, or quasi-privatized business model would allow the Lottery to more readily respond to the voice of the customer.

What is the urgency?

Personal communication devices and the Internet are changing consumer habits at breath-taking speed, and fierce competition is eroding the purchasing power of revenues the Lottery contributes to beneficiaries. The Lottery's existing operating model, which impedes our ability to initiate swift change, points toward continuing loss of market share and the associated revenues.

Why is it significant? If controversial, why?

The Lottery currently funds its operations without additional money from the state. However this self-sustaining condition is not fully supported by the authority to make its own business decisions. Once restructured so it can do so, it will be easier for Lottery staff to move predictably and rapidly toward their goal of increased contributions to beneficiaries. Controversy, if it exists, would likely involve loss of oversight. Mechanisms can be put in place to resolve this concern.

Who are the key players/stakeholders?

- Governor
- Legislators
- Lottery Commissioners
- Office of Financial Management

What is the status now and timeline for conclusion or resolution?

The Lottery intends to request non-appropriation of its 578 Administrative Fund in the near future.

Links to websites with additional background information

None at this time

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Board Member Listing by Board Position

LOTTERY COMMISSION (GS100)

Agency 116 - State Lottery Commission	Senate Conf. Y	Positions: Maximum 005
Authority Governor	Public Disc. Y	Minimum 000
Authoriztn. RCW 67.70.030	Term Length 072	Actual 005
Rem. Auth. GC	Meetings/Yr. 06	

<u>Pos. #</u>	<u>Name and Address</u>	<u>Status</u>	<u>Race</u>	<u>Appointed</u>	<u>Expires</u>
001	Keljo, Carol 1913 NW Lacama Drive Camas, WA 98607	A	C	02/27/2002	08/02/2008
		Terms Served	01		
		Position	a member		
		Comments	General Public		

<u>Pos. #</u>	<u>Name and Address</u>	<u>Status</u>	<u>Race</u>	<u>Appointed</u>	<u>Expires</u>
002	Travis, Melinda E. 7022 South Brookshire Court Spokane, WA 99223	A	C	08/03/2003	08/02/2009
		Terms Served	02		
		Position	a member		
		Comments	General Public		

<u>Pos. #</u>	<u>Name and Address</u>	<u>Status</u>	<u>Race</u>	<u>Appointed</u>	<u>Expires</u>
003	Garson, Rachel 1500 East McGraw Street Seattle, WA 98112	A	C	10/01/2004	08/02/2010
		Terms Served	03		
		Position	a member		
		Comments	General Public		

<u>Pos. #</u>	<u>Name and Address</u>	<u>Status</u>	<u>Race</u>	<u>Appointed</u>	<u>Expires</u>
004	Scarbrough, Robert 5727 South Mason Avenue Tacoma, WA 98409	A	AA	05/01/2002	08/02/2005
		Terms Served	01		
		Position	a member		
		Comments	General Public		

<u>Pos. #</u>	<u>Name and Address</u>	<u>Status</u>	<u>Race</u>	<u>Appointed</u>	<u>Expires</u>
005	Taylor, CHA, Larry 541 29th Avenue Seattle, WA 98122	A	AA	08/03/2000	08/02/2006
		Terms Served	01		
		Position	a member		
		Comments	General Public		