

**PUBLIC ROUNDTABLE ON
CA 23 – 168 – PROPOSED CONTRACT
CFOPD-19-C-041, SPORTS WAGERING, LOTTERY
GAMING SYSTEMS AND RELATED SERVICES**

**Before the
Committee of the Whole
Council of the District of Columbia**

THE HONORABLE PHIL MENDELSON, CHAIRMAN

**JUNE 26, 2018 AT 10:00 A.M.
JOHN A. WILSON BUILDING - ROOM 120**



**Testimony of
Beth Bresnahan, Executive Director
Office of Lottery and Gaming
Government of the District of Columbia**

Introduction

Good morning, Chairman Mendelson and members of the Committee of the Whole. I am Beth Bresnahan, the Executive Director of the Office of Lottery and Gaming (OLG). Thank you for this opportunity to present information on the proposed contract for a combined sports wagering, lottery gaming system and related services. With me today is my colleague Ridgely Bennett, the OLG's Chief Counsel.

As of May 2019, Lottery fiscal year sales to-date total \$144.7 million, an increase of \$3.4 million, or 2.4 percent, over the same period last year. OLG budgeted \$46.1 million for transfer to the General Fund for Fiscal Year 2019. Through the end of May, \$35.1 million, or 76 percent of this target, has been transferred. With four months remaining, OLG is on track to meet its Fiscal Year 2019 target transfer.

This year's sales increase can largely be attributed to growth in the Instant "Scratcher" Ticket portfolio, particularly in the \$3 and \$30 ticket categories, and gains in the multi-state games *Mega Millions* and *Powerball*. While our team will continue to identify, create and seize growth opportunities within the traditional game portfolio, without modernization of the technology and platforms through which we offer these games, growth will remain incremental as there isn't sufficient room to expand within the existing traditional portfolio.

Under the proposed contract submitted for the Council's consideration, the OLG will acquire the technology and expert services necessary to diversify our game portfolio, including the launch of a brand-new game category in sports wagering, and to modernize Office operations to support new sales channels, digitized platforms and innovative game offerings. These operational undertakings will enhance the Lottery's brand and product innovation and transform how we conduct business.

The District expects to realize a rapid return on investment with this new gaming technology. Approximately \$15.3 million in new revenue derived from the sports wagering has been incorporated into the Fiscal Year 2020 budget, with a total of \$92.4 million incorporated into the FY 2020 – FY 2023 financial plan recently passed by the Council.

As you know, on February 19, 2019, the Council approved the Sports Wagering Procurement Practices Reform Exemption Act to exempt the initial procurement for a combined sports wagering, lottery gaming system and related services contract from the Procurement Practices Reform Act of 2010. This law allows the OLG to engage in direct contract negotiations with its incumbent technology vendor, Intralot.

Following extensive market research, comparative analysis, financial due diligence and negotiations, OLG reached a proposed agreement with Intralot with terms that reflect fair pricing, support the long-term growth and profitability potential of Office operations and deliver maximum value to the District. As a part of the vetting process, the OLG reviewed Intralot's financial, technical and management services capabilities and found that the vendor has the necessary resources and expertise to perform its obligations under the proposed contract.

The Contract Outline

The base term of the proposed contract is five years with one five-year extension option. While the lottery industry is shifting toward longer-term gaming system contracts to achieve best pricing and maximize return on investment, with most U.S. contracts securing base terms of 7-10 years with multiple extension options, the OLG believes it is achieving those goals with the agreed upon five year base commitment and option to extend for a second five-year period.

The estimated overall value of the proposed contract is capped at \$215 million, which will result in approximately \$333 million in net profit transferred to the District over the five fiscal years (FY 2020 – FY 2024). For Intralot’s compensation to reach the stated contract maximum, the vendor must generate lottery and sports wagering ticket sales of approximately \$2.67 billion over five years. The vendor’s primary compensation is contingent upon the OLG’s sales performance, as is standard for vendor payment in the U.S. lottery industry, and is based on a percentage of sales for each of the three game categories (lottery, iLottery and sports wagering) supported in the proposed contract. Approximately 68 percent of the estimated profit/transfer to the General Fund during the five-year contract base is expected to be derived from traditional and digital lottery games, with 32 percent coming from sports wagering. Presently, OLG’s transfer to the District is generated primarily from the sale of traditional lottery games.

OLG’s fixed costs in the proposed contract are related to equipment supplied and maintained by Intralot (e.g. gaming terminals, vending machines and kiosks that sell both lottery and sports wagers, game monitors, etc.) necessary to sell game tickets at retail locations. It also includes fee-based services that support business operations such as third-party software licenses and cashless payment transactions, and invited options that will likely be exercised to enhance both the retail and digital player experience.

Under District law, the specific pricing included in the proposed contract is proprietary and confidential until a contract is awarded, which is why I will refrain from sharing specific details today; however, this pricing information and other details were included in the contract package provided to Councilmembers earlier this month.

Smaller lotteries typically carry higher contract rates, as there is less opportunity for the vendor to recoup capital expenditures and operating costs based on lower annual sales. In comparison, vendor rates under the proposed contract fall below or are consistent with the U.S. lottery industry averages for jurisdictions comparable to the District both in size and in annual sales. In Fiscal Year 2018, the DC Lottery generated \$210.2 million in sales and paid a vendor rate of 2.5999 percent. In comparison, the Oklahoma Lottery, which generated \$221 million in sales, paid its gaming system vendor, Scientific Games, 3.99 percent of sales. The South Dakota Lottery generated \$278.8 million in sales last year and paid its vendor, IGT, a rate of 7.38 percent. In contrast, Virginia, a much larger state, partnered with IGT, tallied more than \$2.1 billion in sales last year and paid 0.7699 percent of total sales in vendor fees. The proposed pricing for equipment leases and maintenance under the proposed contract are also in line with those paid by similar-sized U.S. lotteries.

Sports Wagering No-Risk Strategy

Additionally, as part of the sports wagering services provided by Intralot, OLG will adopt a “no-risk” contract model that protects the District from suffering losses in this volatile and largely unpredictable gaming category – a contract feature that is essential for a public agency such as the OLG. Adopting a no-risk model also enables greater predictability of the revenue stream returned to the District.

Under this model, Intralot will bear the risk of all potential losses. OLG will set a specific payout percentage that it expects to achieve in a given fiscal year and Intralot will be responsible for not exceeding the threshold. Intralot could lose money but still will be responsible for paying any

winnings above the set payout. In return for this protection, Intralot retains a higher percentage of the net revenue.

CBE Participation

The proposed contract significantly exceeds the District's 35 percent minimum CBE participation requirement by delivering 55.58 percent participation through the support of seven Certified Business Enterprises selected by Intralot from the District's Department of Small and Local Business Development's list of certified businesses.

New Gaming Categories and Lottery Modernization

The OLG's retail presence and daily business operations will also undergo modernization, with new equipment installed at store locations, along with enhancements to the central gaming system's capabilities and back office business functions that will increase efficiencies and drive profitability. Each of these undertakings will support the OLG's long-term growth, and viability in the competitive and rapidly expanding gaming market in the DMV.

The OLG plans to roll out new equipment to retailers in a thoughtful phased approach, first outfitting top-selling stores as well as new retailers that are licensed as sports wagering locations. We will continue to monitor and coach mid-range and lower-grossing retailers on their sales performance and provide updated equipment as warranted. The cost to equip and service the average licensed location is approximately \$12,500 a year. As such, we want to ensure those dollars are invested with retail partners who are committed to selling lottery games and will work to produce a return on the District's investment in their business.

The launch of sports wagering will provide a prime opportunity for OLG to broaden its appeal and brand recognition, particularly through the mobile app, at the same time expanding our player base to new audiences and expanding to new retail locations. The OLG and Intralot estimate system development, testing and implementation of the sports wagering platform will take approximately six months. If the proposed contract is approved by Council in the coming weeks, this timeline brings the estimated launch date of the OLG's citywide mobile sports wagering app to January 2020.

It is also important to note that the OLG will commit an estimated \$30 million over five years, to fund marketing and advertising to sufficiently support and grow this new game category.

Under the proposed contract, Intralot will also provide OLG with the technology platform and provide the marketing-related managed services to offer digital lottery, also known as iLottery, sales through a wide area network mobile platform and web-based platform. The OLG's digital lottery offering will launch no later than year two of the proposed contract (but not sooner than June 2020 to ensure launches of Lottery-operated digital game verticals are not concurrently competing in the marketplace).

Private Operators and Sports Wagering

On the privately-operated sports wagering side, proposed regulations were published in the *D.C. Register* on June 14, 2019 and are subject to a 30-day public comment period before they can be formally adopted. We anticipate we will be able to license qualified applicants in time to begin sports wagering in early September through a process in the proposed rules that will allow applicants licensed in other "Office-approved gaming jurisdictions" to receive a provisional

license while completing the necessary steps for a standard operational license. Regulations governing Lottery-operated sports wagering are anticipated to be published in Fall 2019.

Conclusion

The proposed contract will enable OLG to adopt new sales channels and platforms that will increase net revenues, competitively retain market share, attract the next generation of players and take the District's gaming offerings into the 21st century. Should the Council vote favorably on the proposed contract, OLG will work diligently to fully implement these programs and initiatives that serve to support our long-term growth, profitability potential, and transfer to the General Fund.

Thank you for this opportunity. I am happy to answer any questions you may have.