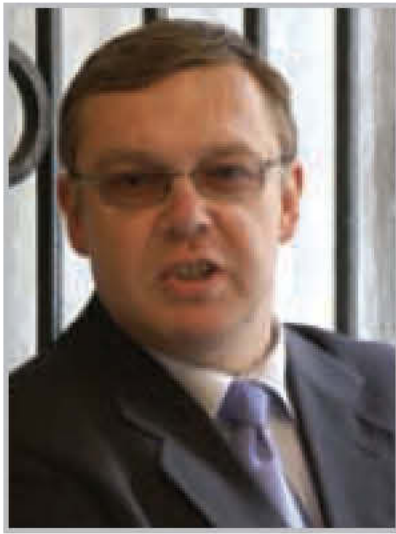


Privatization or Modernization of State Lotteries?

That is the question!

By Philippe Vlaemminck, Jean-Marc Lafaille and Clea Mitchell



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Looking to generate billions of dollars in the short term to cover a current budget deficit, the State of Florida announced recently that it will consider “privatization” of its state lottery presumably with the goals of increasing revenues and enhancing efficiency. Similar announcements have been made in other states, like California and Illinois. Given the time, complexity and political will required to achieve this goal, privatization (however it is defined) may or may not be the solution to find the

financial projections to evaluate how much it can pay up front. It then needs to figure out which games will be played during the term of the license and forecast their sales results for the term of the license: 10, 15 and even 25 years. This is a very difficult “crystal ball” exercise. No consumer goods company can predict the sale of their products over such a long period of time. The taste of the consumers will change and new technology could eliminate current products and create totally new and unpredictable type of products. Who could predict 10 years ago that the most important distribution mean for the sale of gaming products in the world would be the Internet, and that lotteries in the United States would be prohibited from using this channel of distribution?

If a state is looking not only at solving a short-term deficit prob-

Privatization companies often are already providing advertising, promotion and communications services to state lotteries. In practice, the typical U.S. government lottery is already privatized to a large extent.

substantial revenue needed to cover the State’s current budget deficit. Depending on how and what is done, one can ask ourselves whether such an effort is necessarily the right course of action.

Many state lotteries are already largely privatized. Facility management contracts frequently delegate to private companies the operations of large segments of their business in return for an agreed-upon small percentage of lottery sales. For example, private companies are already provide scratch ticket system covering printing, distribution and accounting, for on-line terminal system covering the design and implementa-

tion of the hardware, software and network, the sale, distribution and accounting of the games going through the system, the back office MIS, etc. Private companies often are already providing advertising, promotion and communications services to state lotteries. In practice, the typical U.S. government lottery is already privatized to a large extent, leaving aside the questions of draws and the security aspects of the organization. Thus, current talk of privatization needs to take this practical reality into account.

In a “full privatization” model, the future licensee must develop

lem but also at improving the efficiency and productivity of its lottery, it would be well advised to examine as well its lottery’s current operational structure and, doing so, it may find additional helpful steps to deal with its short-term financial problem. State governments have traditionally assumed direct responsibility over lottery operations by giving the responsibility for the lottery to a department, to a commission reporting to the legislature or to a State corporation. Which way is better, or is there a better way? If one would like to get into the details of each model the reader could read the book *Dissected & Re-assembled* – an analysis of gaming which concludes that, considering the nature of a Government, a State Corporation should do better than a department or a Commission. Very few states in United States have decided to go that route and it is difficult to compare the results of each model as many other important variables may influence the results, the most important of which being the type and number of games authorized by the state government’s legislation.

In most of the other countries of Western Europe, Canada and Australia, the state corporation approach is the most popular model chosen by governments and with good results. In countries where a full privatization was implemented under the control of a state regulator or commission, the licensee does not seem to have a larger freedom to operate than a state corporation. Very often, the private licensee is operating within a very tight regulatory framework with little maneuvering room for entrepreneurship behavior.

In Europe, both the privatization and modernization approach has been tested. Having evaluated both approaches, it is clear to us that a well-conceived and effectively empowered state corporation can provide huge advantages to a government. Considering the specific situation of the U.S. state lotteries, an strategy focused on regulatory and corporate modernization could be very beneficial and provide the respective governors and legislatures with the solution for both the budgetary problems and the necessary responses to the demands of consumers and society at large. Such approach will need to take into consideration all international, federal and state law requirements to avoid that an uncontrolled liberalization of the gaming market would occur or that some inconsistencies in the policy would lead to further legal battles as it was the case with the IHRA.

A solution could be to create a state corporation with the proper degree of autonomy to run the state lottery. This corporation could be asked to pay up front for its license an amount equal to the current yearly profits multiplied by the number of years of the license (should not be much more than 7 to 10 years because of the incertitude). The state corporation could then go to the banks and borrow the money to pay for the license. This way the state government will get up front money to cover its deficit, and will achieve increased efficiencies and productivity, which will inure to the benefit of the State Lottery as well. After the term of the license, the Government can repeat the operation or decide to do otherwise. ♦

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What does it mean?

Cost aside, regulators typically want assurances to two fundamental questions in their evaluation of a Video Lottery Central Monitoring System (CMS):

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If so, does the supplier have the depth of staff, breadth of experience and financial strength to deliver, install and operate the system?

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