

MINUTES OF THE HOUSE COMMITTEE ON FEDERAL & STATE AFFAIRS

The meeting was called to order by CHAIRMAN MILLER at \_\_\_\_\_  
Chairperson

1:30 a.m./p.m. on January 14, 1987 in room 313S of the Capitol.

All members were present except:

Representatives Sifers, Peterson-E, Hensley-E

Committee staff present:

Lynda Hutfles, Secretary  
Mary Galligan, Research  
Raney Gilliland, Research

Conferees appearing before the committee:

Harley Duncan, Secretary of Revenue

The meeting was called to order by Chairman Miller at 2:30.

Harley Duncan, Secretary of Revenue, distributed a packet of materials containing the following information: a state lottery overview, a lottery organizational chart, a glossary, U.S. Lottery State & Their Games, 1986 lottery election results, a memo explaining the bill section by section and a Lottery Project Team Tasks Outline. See attachment A.

Mr. Duncan presented an overview of the lottery describing game design, start up, allocation of lottery revenue, functions a state agency must perform, estimated revenue for the state and enabling legislation. Mr. Duncan then began explaining the bill section by section stopping with Section 4. See attachment B.

The Chairman announced that because of the time limit, Mr. Duncan would return on Thursday to finish the explanation of the bill.

The meeting was adjourned.

## INTRODUCTION

Kansas was one of six states which considered the issue of whether to adopt a state operated lottery during the last general election. Initiatives were approved in Florida (64-36), Idaho (60-40), Montana (69-31), South Dakota (60-40), and Kansas (64-36) with North Dakota (56-44) being the only state to defeat the issue. These states join 22 existing lottery states, plus the District of Columbia, in what was a \$10.16 billion dollar business in calendar year 1985.

This presentation updates the paper presented during the last legislative session and covers the areas of game design, start-up, allocation of lottery revenue, functions a state agency must perform, estimated state revenue, and enabling legislation.

## GAME DESIGN

Lottery games can be divided into two categories, active and passive. Active games are those in which the player participates in the bet by choosing a number or set of numbers. Passive games are those in which the player takes no action to determine whether he has won or lost; instead a ticket is purchased and the outcome is then revealed.

There are currently several types of lottery products being played. The first is what is commonly referred to as the weekly game or draw lottery. Though rare in the United States, this is the game which was used when the modern lottery first started in 1964 in New Hampshire and remains the main game in overseas lotteries. Similar to a raffle ticket in appearance and in play, the player purchases a pre-numbered ticket and waits for a weekly drawing.

The second type of lottery product is the instant lottery ticket. The instant ticket has play data which is concealed by a removable latex material. A player buys the ticket, usually for \$1, and scrapes off the material to reveal whether or not it is a winner. As an example, a game may have a match three theme; match three dollar figures and you win that amount as a prize.

In addition, states have introduced jackpot prize drawings which use the instant ticket as a method to gain entry. Players are entered in a weekly drawing and if selected can participate in a televised event to "spin the wheel" for prizes such as \$5,000, \$10,000, \$25,000, or a jackpot which increases each week if not won.

The third type lottery product involves an on-line system. This was introduced in the mid-1970s. The on-line system is a series of computer terminals which are similar to cash registers in appearance and are geographically located throughout a state. The terminals are linked to a central computer site, usually in the state capital. There are currently three on-line games. The first on-line game to be introduced was the three-digit game, commonly referred to as the numbers game. Numbers games were originally designed to compete directly with Eastern illegal numbers games. A player approaches the agent who has a terminal and selects three digits. The agent enters those three digits at the terminal and the play is recorded at the central site. Every day there is a random drawing of a number and matching that number in prescribed ways wins prescribed prizes. The second game is the pick four or four-digit game, which is basically run the same way as pick three.

The third on-line game is the increasingly popular lotto game. A player picks six numbers out of a specified field of numbers, such as 36, 40, or 44. A certain percentage of the revenues is placed in a grand prize fund which is only paid when an exact match of the six digit numbers is made. Drawings of the winning numbers are held once or twice a week and if there is no winner, the jackpot "rolls over" to the next drawing. If no one wins for several weeks, the jackpot can become enormous, as evidenced by New York's \$41 million lotto jackpot. Most lotto games also include lesser prizes for matching four or five out of six numbers, for instance.

#### START-UP

Without exception, new lottery states have started with instant games. State lottery directors testify that to ensure successful start-up, instant games have proven to be the most efficient direction to take. With the timely passage of the enabling legislation and the seed money appropriation, plans call for instant game tickets to go on sale in September 1987 and the introduction of an on-line game six to eight months later.

A seed money or start-up appropriation is needed to allow the lottery to make payments for goods and services rendered before it generates its own cash flow. The funding is necessary primarily for salaries, consultant services, facility leases, office equipment, and computer hardware and software as well as capitalizing an initial prize pool. The lottery should be able

to negotiate a schedule of deferred payments to the successful instant game vendor to minimize the required funding. State General Fund appropriations will be needed in both FY 1987 and FY 1988 with prompt payback once lottery revenues are received.

Total required seed money will be between \$2.5 and \$3 million.

#### ALLOCATION OF LOTTERY REVENUE

Lottery gross sales are divided into three expenditure categories: prize payments, net proceeds, and operating expenses. Operating expenses include commissions to retailers (usually 5-6%), and actual administrative costs such as ticket production, consulting services from private lottery firms, advertising, computer services, salaries, and other support services. These costs will vary with size of the state and maturity of the lottery, but commonly run 10 to 15% in addition to the retailer commissions. After deducting operating costs, and prize payouts (45-50%), the remaining portion (30-40%) represents the net proceeds to the state.

In reviewing the administrative cost proportions of the lottery states, administrative expenses of the smaller states are well above the national average, and the costs of the larger states fall well below the average. There appears to be evidence of economies of scale, especially in advertising and computer expenses. Therefore, it is inappropriate to take at face value, the administrative costs of a large, mature lottery such as New Jersey and New York and compare that to a new lottery state.

FY 1985		Prizes	Net Rev	Expenses
Total Sales (\$ Millions)	State(Population)	% Sales	% Sales	% Sales
0 - 199	Vermont(.5)	49.6	23.7	26.7
	New Hampshire(.95)	42.3	31.5	26.2
	Maine(1.1)	52.6	25.8	21.6
	Delaware(.6)	49.7	39.0	11.3
	Oregon(2.6)	50.6	34.1	15.3
	Rhode Island(.96)	47.5	35.7	16.8
	Arizona(2.9)	46.7	30.2	23.1
	Colorado(3.0)	46.8	33.2	20.0
	Washington D.C.(.63)	47.9	34.8	17.3
	Washington State(4.2)	47.6	34.7	17.7
200 - 399	Connecticut(3.2)	46.8	43.2	10.0
400 - 599	-	-	-	-
600 - 799	Maryland(4.3)	53.6	38.7	7.7

800 - 999	Ohio(10.8)	49.1	39.6	11.3
	Michigan(9.1)	47.5	40.6	11.9
	New Jersey(7.4)	48.5	42.3	9.2
	Massachusetts(5.8)	55.1	34.7	10.2
1000 & Over	Illinois(11.4)	48.4	43.0	8.6
	New York(17.7)	47.5	41.8	10.7
	Pennsylvania(11.9)	46.7	44.2	9.1

In FY 1985, in the ten lotteries with less than \$200 million in gross sales, net proceeds amounted to less than 35% in six cases and less than 30% in two other. Only Delaware which began a lottery in 1975 and Rhode Island which started games in 1974 approached the 40% mark.

#### FUNCTIONS A STATE AGENCY MUST PERFORM

State lotteries are operated in generally the same way with the day-to-day administration of three major organizational divisions resting with a Lottery Director appointed by the Governor. The attached organization chart reflects a staffing proposal for 119 positions. This is consistent with the staff size in Iowa (131) and Missouri (210).

**Security** will be responsible for employee background checks and facility security; ticket security and procedures for receiving, handling, distributing and storing tickets; game security and monitoring access to computer software and hardware; retailer and vendor background investigations; and breach of security issues and investigation of invalid claims because of ticket tampering.

**Administration** will be in charge of all accounting systems, ticket accounting and validation systems, payment of prizes, procurement and contract services, facilities management, personnel, data processing, and network telecommunications.

**Marketing** will have primary responsibility for the design, distribution, promotion, and sale of all lottery products. This will include the management of a comprehensive retail sales network, regional offices, and lottery sales representatives.

#### ESTIMATED STATE REVENUE

Projecting revenues from a state lottery is precarious and difficult because there are so many unknowns and no objective data upon which to base calculations. Factors that influence the estimate include economies of scale, population distribution, population mobility, types and number of games played, operating expenses, public education and acceptance, and interstate competition.

Nonetheless, we have estimated that a lottery could generate roughly \$30 to \$35 million in net revenues annually. This is based primarily on experience in Colorado and estimates in Iowa and should be considered to reflect primarily the operation of an instant game. Essentially they equate to \$40 to \$50 per capita purchases annually with a net take of 30 to 35%.

The operation of an on-line game and some maturity in the lottery could increase the gross revenues and reduce the operating costs, thus increasing the projected revenues. One should be extremely cautious, however, for several reasons:

1. Until recently, lotteries tended to be concentrated in more populous urban, and/or Eastern states.
2. We will be competing with another state having twice our population for our largest market. This may significantly affect our ability to sell both instant and on-line tickets in Johnson and Wyandotte counties.
3. Since Kansas is grappling with a series of long-term serious economic problems, the projected per capita sales may not develop.

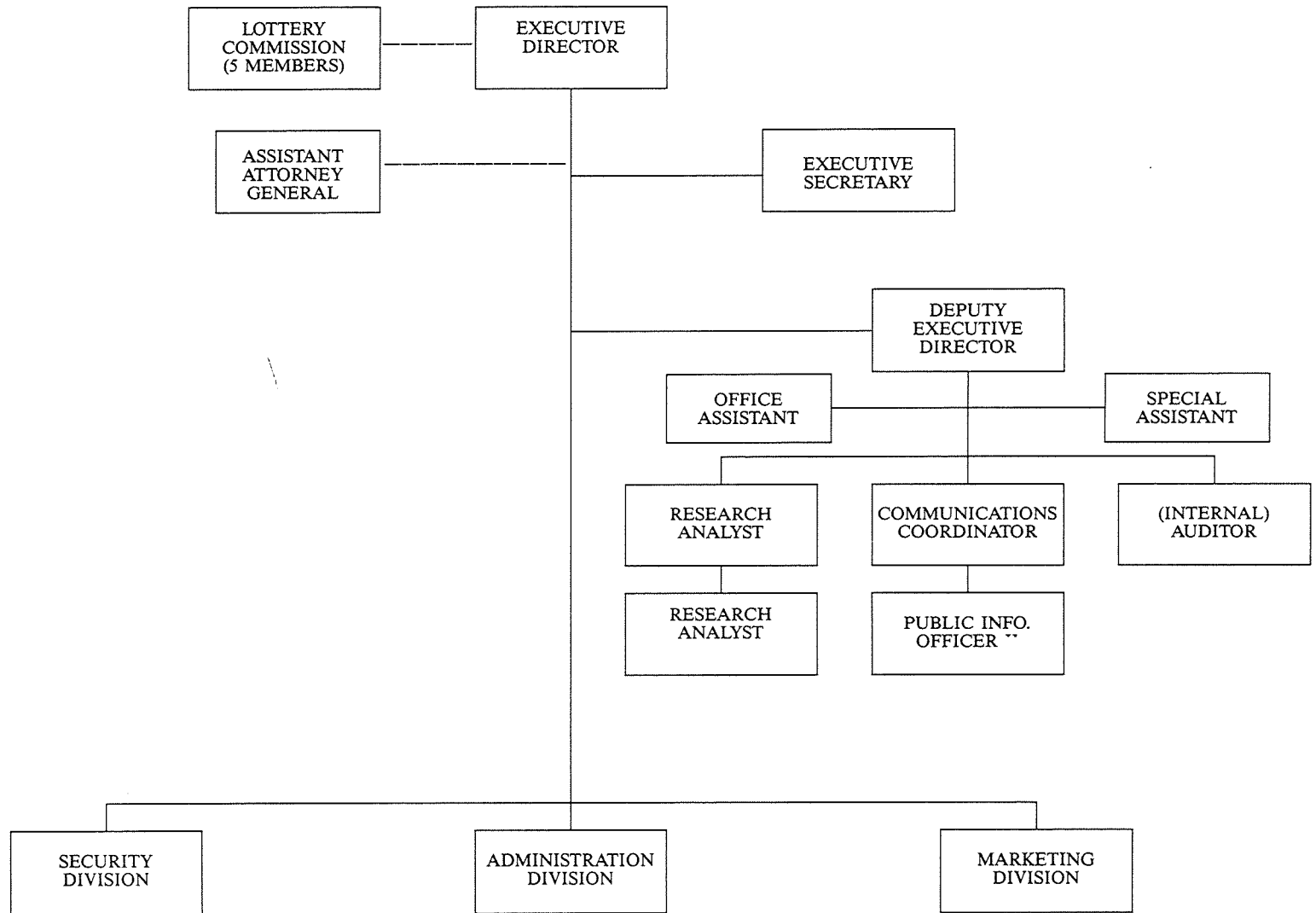
#### ENABLING LEGISLATION

A lottery is a unique entity in state government, in that it is the only state agency with a mission identical to a private business - selling a product in a fashion which maximizes revenue. In drafting the enabling legislation, three key ideas were consistently addressed: flexibility, integrity, and security. Fortunately, we can learn from the mistakes made by established lottery states.

**THE KANSAS LOTTERY  
DIRECTOR'S OFFICE**

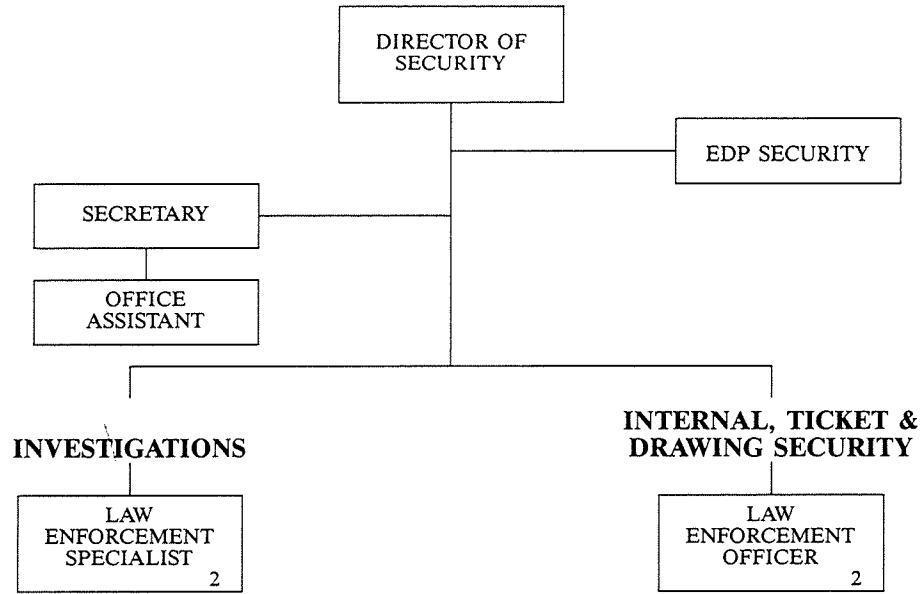
DIRECTOR'S OFFICE  
TOTAL POSITIONS - 11

TOTAL FTE  
POSITIONS - 119



**THE KANSAS LOTTERY  
SECURITY DIVISION**

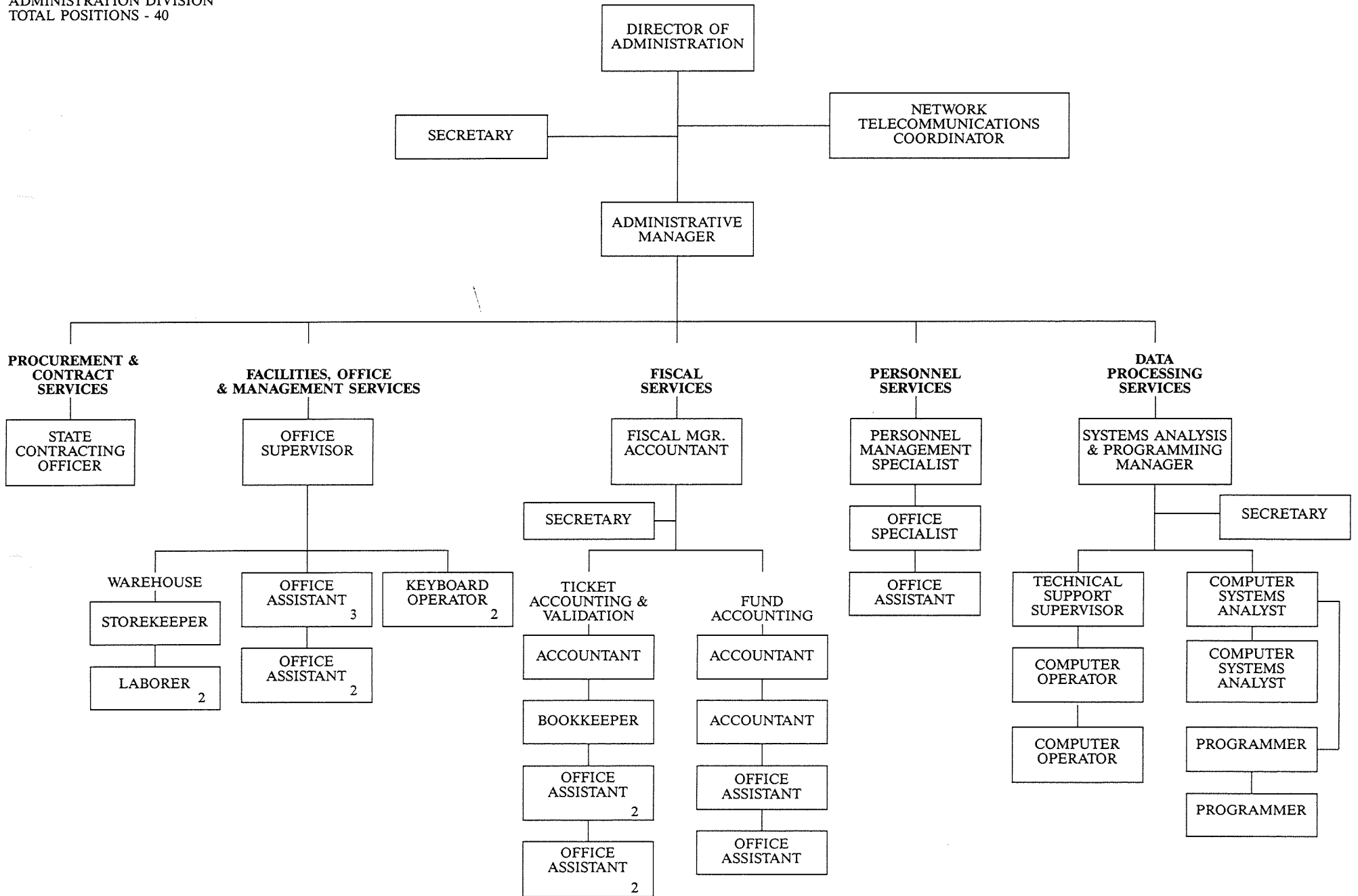
SECURITY DIVISION  
TOTAL POSITIONS - 8





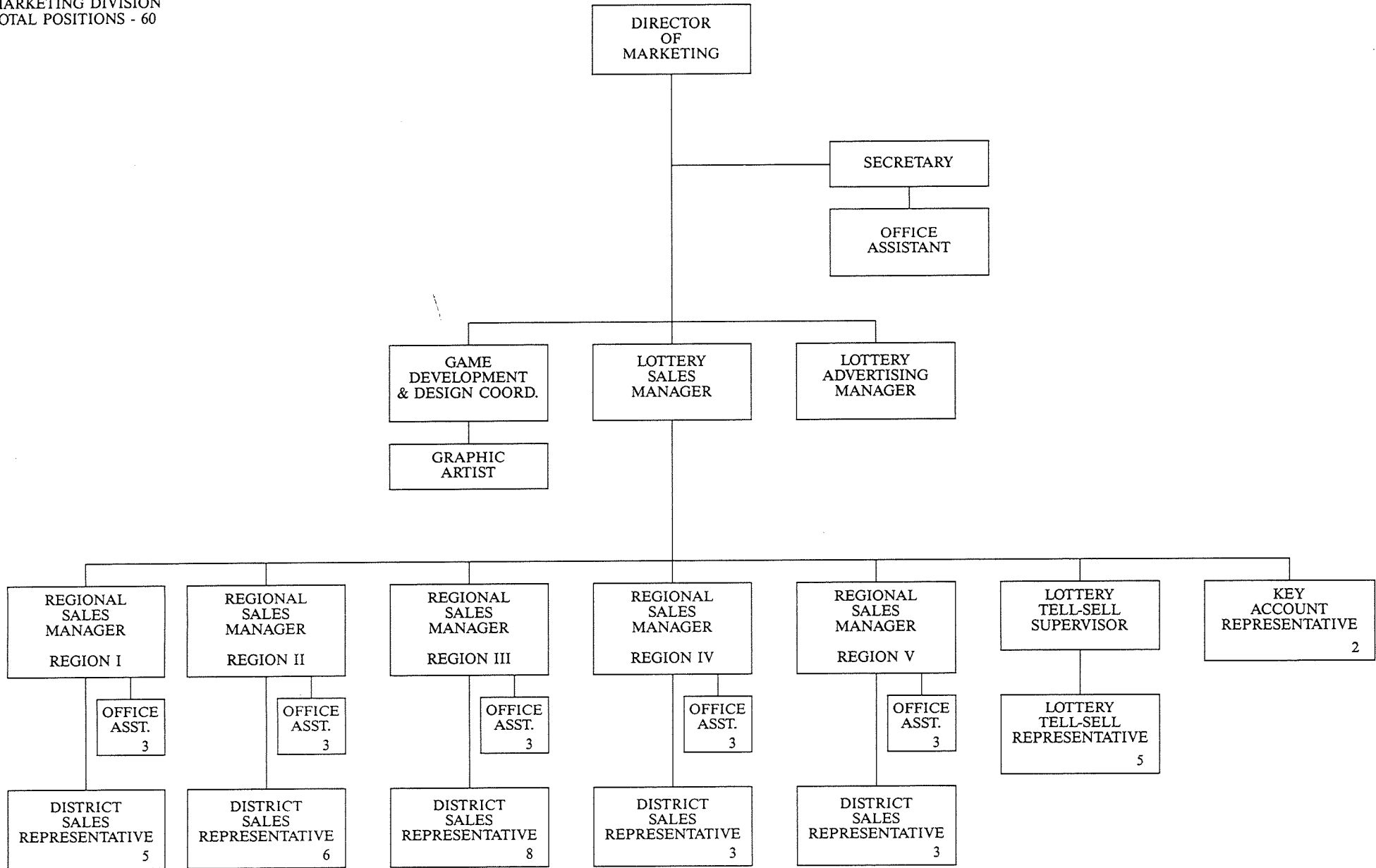
**THE KANSAS LOTTERY  
ADMINISTRATION DIVISION**

ADMINISTRATION DIVISION  
TOTAL POSITIONS - 40



**THE KANSAS LOTTERY  
MARKETING DIVISION**

MARKETING DIVISION  
TOTAL POSITIONS - 60



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# Glossary

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**active game:** a lottery game in which the player takes action to determine the outcome by choosing a number or set of numbers to bet on, attempting to match the numbers later drawn.

**agents (sales, ticket):** retail merchants chosen by the lotteries to sell tickets, using either a computerized ticket generator (for on-line games) or a ticket supply furnished by a vendor (for instant games).

**annuity:** a type of insurance policy purchased by lotteries that pays off a large jackpot to the winner in equal installments, which allows the balance to accumulate interest over time, thereby permitting the lottery to offer a prize larger than the policy cost.

**audit features:** an accounting system built into video lottery terminals that logs all sales transactions and cash received.

**back pair:** a betting feature used in three-digit and four-digit numbers games that allows the player to bet on what the final two digits in the number drawn will be.

**box bet:** a betting feature in numbers games allowing the player to bet on all possible combinations of three or four digits.

**central site computer:** a computer in one location that controls ticket-producing terminals or video lottery games at various locations around a state.

**dial-up:** a system of communications between video lottery terminals and a central site computer that permits the sending of electronic messages over telephone lines.

**downloading:** the transfer of a store of plays from a central computer to a video lottery terminal.

**draw lottery (also "traditional lottery" and "weekly game"):** a lottery game similar to a raffle, involving the sale of pre-numbered tickets, with the winners chosen at random in a weekly drawing.

**electronic survey:** a computerized demographic questionnaire built into video lottery terminals that awards a free play for answering questions regarding age, education, income level, etc.

**fixed payout:** a prize that remains set at the same odds regardless of how much money is bet for a particular drawing.

**front pair:** a betting feature used in three-digit and four-digit numbers games that allows the player to bet on what the first two digits in the number drawn will be.

**game format:** the individual games offered on the computer software used with video lottery terminals.

**game mix:** the complete collection of games offered by a state lottery.

**instant game (also "instant lottery"):** a lottery game that offers pre-printed tickets, normally selling for \$1 each, that indicate immediately whether or not the player has won.

**line of credit:** money lent a lottery bureau by the state's legislature for use in initiating operations.

**lotto (also "Pick 6"):** a lottery game originated in Europe that offers the player a choice of four, five or six numbers out of a field ranging from 30 to 49 numbers, the winner being determined by a drawing.

**lotto boards:** the betting slips used in lotto games.

**mini-pool:** the store of plays in a video lottery terminal, which is replenished via telephone line from a central computer.

**numbers games (also "Pick 3" and "Pick 4"):** lottery games permitting the player to choose his or her own three-digit or four-digit number, the winner being determined by a drawing.

**on-line:** hooked up to a central computer via telecommunications lines, as with ticket-generating terminals used in numbers and lotto games.

**P.A.L.M.:** Player-Activated Lottery Machine—the stand-alone terminals used in video lottery games.

**parimutuel:** a system of prize payouts in which the jackpot is created solely with money wagered.

**parimutuel industry:** term used to describe all legalized wagering that involves prizes created on a parimutuel basis, including horse racing, dog racing, and off-track betting parlors.

**passive game:** a lottery game in which the player takes no active part in determining the outcome; the ticket sold is either a winner or a loser, and no choices of numbers are made.

**payback schedule (or payback time):** the time it takes a lottery bureau to repay the state legislature money appropriated to initiate operations.

**payout (or "payoff"):** the amount of a prize or the odds by which a prize is paid.

**pool:** the cash amount in a parimutuel jackpot, or the total money wagered.

**pool size:** the amount of cash one would need to purchase all possible combinations of numbers in a lotto game.

## Glossary

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**prize tiers:** various levels of prizes in lotto and instant lottery games—lower tier prizes are normally paid out by lottery agents at retail locations.

**“Quick Pick”:** betting feature for lotto games consisting of a machine that electronically selects random numbers for a player.

**rollover:** the situation where money in a lotto jackpot is carried over to two or more drawings when no one wins the grand prize.

**rub-off:** type of instant lottery ticket with a latex spot which, when removed, reveals whether or not the ticket is a winner.

**seed money (also seed cost):** the amount of money appropriated a lottery by a state’s legislature for the purpose of initiating operations.

**6/40:** a term describing the choices offered in a lotto game; 6/40 means a choice of six numbers from a field ranging from 1 to 40 (same formula applies for 6/36 and other such terms).

**spillover sales:** lottery sales made to residents of a bordering non-lottery state.

**straight bet:** betting method used in numbers games that requires an exact match of the number drawn to win.

**subscription game:** a lottery game for which tickets are purchased in advance, entering the participant in a series of drawings lasting a specific time.

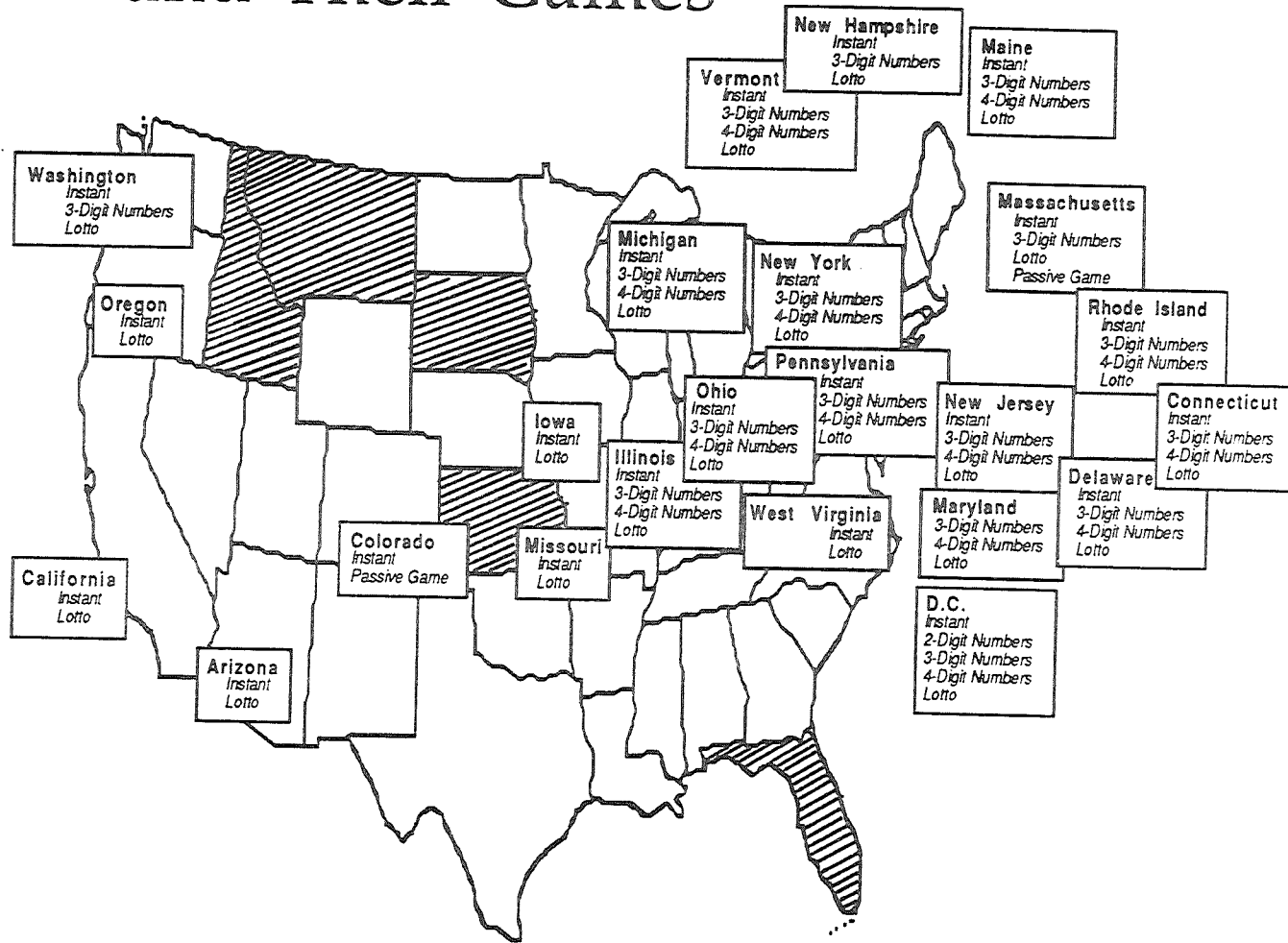
**“System Betting”:** a betting method used in lotto games that involves choosing eight numbers, and having the computer record bets for all possible combinations of those numbers.

**telecommunications:** the linking of a main computer with lottery terminals around a state for the transmitting of information and programs, via telephone lines.

**transaction rates:** the amount of transactions recorded by one or more of the lottery terminals in a state during a specific time frame.

**video lottery:** a lottery game involving a stand-alone machine designed similar to a video amusement game, but with prizes offered for winning (at random) by the state lottery.

# U.S. Lottery States and Their Games



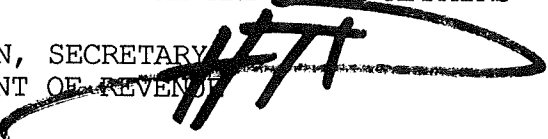
New States (shaded): Florida  
 Idaho  
 Montana  
 South Dakota  
 Kansas

# State of Kansas 1986 Lottery Election Results

56% Cheyenne	64% Rawlins	61% Decatur	54% Norton	49% Phillips	44% Smith	48% Jewell	58% Republic	56% Washington	56% Marshall	64% Nemaha	52% Brown	60% Doniphan
71% Sherman	65% Thomas	62% Sheridan	58% Graham	59% Rooks	49% Osborne	59% Mitchell	56% Cloud	43% Clay	64% Riley	66% Pottawatomie	61% Jackson	71% Atchison
53% Wallace	54% Logan	48% Gove	61% Trego	75% Ellis	70% Russell	60% Lincoln	52% Ottawa	58% Dickinson	72% Geary	66% Wabaunsee	72% Shawnee	67% Jefferson
59% Greeley	58% Wichita	59% Scott	56% Lane	53% Ness	66% Rush	71% Barton	62% Ellsworth	45% McPherson	38% Marion	63% Morris	60% Lyon	62% Osage
62% Hamilton	64% Kearny	65% Finney	55% Hodgeman	58% Pawnee	49% Stafford	58% Reno	51% Rice	47% Harvey	57% Chase	60% Coffey	60% Anderson	68% Franklin
56% Stanton	59% Grant	46% Haskell	56% Gray	64% Ford	40% Klowa	55% Pratt	51% Edwards	64% Sedgwick	59% Butler	64% Greenwood	62% Woodson	55% Allen
52% Morton	46% Stevens	52% Seward	49% Meade	45% Clark	47% Comanche	55% Barber	54% Kingman	58% Sumner	60% Cowley	59% Elk	59% Wilson	66% Neosho
										54% Chautauqua	58% Montgomery	61% Labette
												76% Wyandotte
												72% Johnson
												76% Miami
												63% Linn
												57% Bourbon
												76% Crawford
												64% Cherokee

MEMORANDUM

TO: THE HONORABLE ROBERT H. MILLER, CHAIRMAN  
HOUSE COMMITTEE ON FEDERAL AND STATE AFFAIRS

FROM: HARLEY T. DUNCAN, SECRETARY  
KANSAS DEPARTMENT OF REVENUE 

RE: HOUSE BILL NO. 2043 - LOTTERY ENABLING LEGISLATION

DATE: JANUARY 14, 1987

Thank you for the opportunity to appear before you on House Bill No. 2043, the enabling legislation for the Kansas Lottery. The bill before you is the product of the Special Committee on Federal and State Affairs which operated during the interim and is based on draft legislation developed by the Department of Revenue. Our goal in the legislation was to draft a document that would establish the foundation for a secure, efficient lottery organization, serve the best interest of the state, and above all, respond to the desires of 64 percent of the voting public.

The bill incorporates provisions taken from the legislation of several states and recommendations received from experienced lottery officials. On October 21, at our invitation, 17 individuals representing 7 lottery industry vendors and other interested parties met to discuss an earlier draft. Excellent comments and suggestions were received. Most are included in the version before you.

My intent is to review each section the bill and to highlight what I consider to be the "policy relevant" features of each section.

**SEC. 1. Title.** The Kansas Lottery Act.

**SEC. 2. Definitions.** Of primary importance here is the definition of "major procurement." It is defined as the procurement, through contract or otherwise, of gaming products and services such as tickets, computer facilities, advertising and promotional services, annuity contracts, prize payment services, consulting services, equipment and other products and services unique to the operation of the Kansas lottery. It becomes important because of special bidding and procurement provisions contained in Section 4.

*Attachment B*

**SEC. 3. Organizational Structure.** This section establishes the Lottery as an independent state agency with an executive director and certain positions in the unclassified service. The executive director is to be appointed by the Governor, confirmed by the Senate and serve at the pleasure of the Governor. The positions in the unclassified service include the deputy director, director of security, director of administration, director of marketing, all other marketing division personnel and a personal secretary and special assistant. The section also requires the Department of Revenue to take the lead role in the start-up of the lottery with other agencies to assist as directed by the Governor. Finally, it provides that the Director of Purchases is to use the provisions of current law relating to emergency purchases when requested by the lottery director during the first 18 months of operation.

In reviewing the twenty-three U.S. lotteries, the organizational location appears to be determined as much by individual state philosophy as anything else. The majority of lotteries, at the least the newer ones, are organized as separate agencies while the older lotteries in the Northeast tend to be part of other departments. In some cases, such as Missouri and Iowa, where the lottery is part of the Department of Revenue, the Department, either by practice or by law, cannot exercise any binding authority over the lottery.

What is consistent among all states, regardless of location, is the lottery must have its own identity and be clearly responsible for its decisions for purposes of efficiency, security, marketing and public perception. For security reasons, a Lottery Division within the Department of Revenue could not utilize centralized processing systems and support services within the agency. The potential benefit to be derived from placing it in the Department would be greater executive oversight through a cabinet level officer. Such oversight can also be obtained through the gubernatorially appointed executive director and Lottery Commission.

Regardless of the organizational location, it is common for the lottery executive director to be appointed by and removable by the Governor or some other executive branch official. Only in Missouri and Vermont is the director appointed by a lottery commission, and that appointment must be approved by the Governor in Vermont.

The bill proposes that all professional marketing and sales related positions within the marketing division would be in the unclassified service. Marketing activities would include sales strategies, product promotion, product design and development, long term game schedule, sales and distribution, advertising, and sales management. These skills are not readily available within the current



civil service system and recruiting efforts will have to focus on private industry and existing lottery states. Establishing these positions within the unclassified service recognizes the special skills required. It also recognizes it would not be in the best interest of the state personnel system to expand the classification plan to incorporate classified positions other state agencies would never use.

**SEC. 4. Powers of the executive director.** Specified authority includes appointment and supervision of all staff, contracting for necessary gaming services and products, contracting with retailers for sale of tickets, entering into agreements for multi-state lotteries, and auditing the records of retailers and compelling the production of those records if necessary.

The section also sets the procedures to be utilized in contracting for gaming services and products or the "major procurements" defined in section 2. It allows the director to enter into such contracts with approval of the Commission. It requires the director to solicit competitive bids for such products and services, but exempts the contracts from the lowest responsible bid requirement of current law. Instead, the competitive bids would be evaluated against a variety of stated criteria that include all relevant factors including price. The other factors include security, competence, experience, timely performance and maximization of net revenues to the State.

The purpose of this provision is to allow the lottery to consider all relevant factors when making contract decisions rather than being restricted to just one - price. Security, competence, experience, timely performance, in addition to price, are all key elements. In short, it is designed to obtain not only the best price, but the best vendor. This request is not unique in that similar procedures have been established for architectural and engineering service and telecommunication procurements. Of all the recommendations received from other states, this one is most often mentioned.

Security needs and the degree to which states must rely on lottery vendors have caused some states to include financial disclosure requirements for potential vendors in their statutes. The issue is essentially how far reaching and detailed the disclosures need to be to protect the interests of the State and, at the same time, insure full competition among vendors and avoid adding unnecessary costs to lottery contracts.

The bill incorporates language similar to the Iowa law. It provides that before a contract is awarded to a vendor that the vendor, any parent or subsidiary corporation and all principal stockholders would be subject to background criminal and financial investigations. It is envisioned that certain information would be required of all bidders in the invitation for bid and that a more exhaustive investigation would be conducted of apparent winners before a contract award. The Secretary of Revenue, Securities Commissioner, Attorney General and Director of the KBI are to cooperate in such investigations.

**SEC. 5. Duties of the executive director.** Specified responsibilities include keeping complete accounting records, making periodic financial reports to the Commission, Legislature and Governor, securing an annual independent financial audit, providing for an periodic independent security review, arranging a periodic independent evaluation of promotional and public information activities, submitting budget proposals and using electronic funds transfers for transferring monies from retailers to the lottery where possible. This section also requires that the odds of winning each lottery game are to be included in all printed promotional materials and information associated with the game.

In the 1986 Legislature, there was considerable discussion of requiring that the odds of winning a lottery prize to be printed on each ticket. The bill attempts to capture the intent of this discussion by requiring that the director include in all promotional materials and information printed for each game a list of the odds of winning such game.

In other states with this type of requirement, the system works as follows. In games utilizing pre-printed tickets, the average odds of winning some prize will be printed on each ticket. Also, a detailed listing of the estimated number of prizes of each particular denomination that are expected to be awarded in **any** type of game is available at each location at which tickets or shares are offered for sale to the public.

**SEC. 6. Lottery Retailers.** This section authorizes the director to enter into contracts with retailers for the sale of lottery tickets. Contracting, rather than licensing, was recommended by several states and industry representatives because of the ability it provides to move expeditiously when necessary.

The director may contract with such retailers as he considers necessary and desirable after considering such items as security, financial responsibility, access, integrity, volume of sale expectations and such other factors as deemed appropriate. The bill also specifically authorizes contracts with non-governmental groups on governmental property and retail liquor stores.

To be selected as a retailer, a person must be 18, be of good character, have sufficient financial resources, and be current in the payment of all taxes to the State. No one may be a retailer who has been convicted of a felony in the last 10 years, convicted of a gambling violation in any jurisdiction, violated provisions of the act, is a lottery vendor or employee thereof, or is a member of the same household of a lottery employee. Most of the provisions are also applied to partnerships and corporations.

This section also states that where rental rates are based on retail sales, only the commission paid to the retailer shall be deemed the sales price unless the rental contract otherwise specifically speaks to lottery tickets. Otherwise some retailers could face a situation where the additional rent exceeds their commission. This would allow the rate to be negotiated by a retailer and a landlord.

**SEC. 7. Kansas lottery commission.** This section establishes the Kansas Lottery Commission to consist of five members appointed by the Governor and confirmed by the Senate. Members are to serve overlapping four-year terms, and not more than three may be members of one political party. The bill provides that the Commission is to meet at least quarterly, advise the director on the lottery, and, in conjunction with the director, conduct on-going studies of lotteries and the Kansas lottery. The commission also must approve "major procurement" contracts and the annual budget submission.

**SEC. 8. Adoption of rules and regulations.** This section provides that the Commission is to approve rules promulgated to govern the lottery. Such rules are to be recommended to the Commission by the director. The rules will govern the types of games to be played, the manner of selecting winning tickets or shares, the payment of prizes, the frequency of drawings, types of ticket selling locations, and the amount and method of compensating retailers, and the types of information to be provided by vendors, among other things.

Based on a recommendaton received from the Iowa Lottery, the bill exempts the lottery from the notice, hearing and Joint Committee review requirements for temporary rules and regulations. The rules

would still be subject to review by the Attorney General, filed with the Revisor and published in the **Kansas Register**. During the play of a game, it may become necessary to make changes due to the lack of participation or deficiencies in the game itself. To avoid a substantial drop in sales, the lottery must be able to act promptly before the game is jeopardized.

**SEC. 9. Lottery operating fund.** This section outlines the financial structure of the lottery. It provides for a lottery operating fund into which are paid all ticket and share proceeds and other receipts. Monies in the fund are to be invested by the Pooled Money Investment Board with interest being credited to the fund. Proceeds are to be used to pay the expenses of the lottery, including the administrative costs of the agency and compensation to retailers. Remaining revenues are to be transferred to the lottery prize payment fund as necessary to pay prizes, and to the State Gaming Revenues Fund created by the 1986 Legislature. In FY 1988, monies not needed for other purposes are to be transferred to the Gaming Revenues Fund, while in Fiscal Year 1989 and beyond, the bill requires that not less than 30 percent of gross receipts is to be transferred to the Gaming Revenues Fund. All expenditures of the lottery are to be made in accord with appropriation acts of the Legislature.

**SEC.10. Lottery Prize Payment Fund.** This section establishes the lottery prize payment fund and provides that is to be capitalized by transfers from the lottery operating fund. Proceeds are to be invested by the Pooled Money Investment Board with interest accruing to the fund.

**SEC. 11. State General Fund Start-Up Appropriation.** This section provides that any State General Fund appropriation to the lottery is to be considered a loan and is to be repaid within 24 months from the effective date of the appropriation. It also provides that the loan is not be considered an indebtedness of the State and that aside from the start-up appropriation, the State General Fund shall not be used or obligated to pay any expense of the lottery.

**SEC.12. Power and authority of peace and police officers.** This section authorizes the director to designate certain lottery employees as peace officers. The designation of employees within the Security Division as law enforcement officers was recommended by the Iowa and California Director of Security. This gives lottery security employees the authority necessary to make independent investigations

of internal security, retailer security and game security. Most importantly, it allows access to the law enforcement information network and other information that otherwise would not be available. It also facilitates communication and cooperation among law enforcement agencies within the state and between states. This designation will probably be given to less than seven employees.

**SEC.13. Appointment of an Assistant Attorney General.** This section provides for appointment of an Assistant Attorney General by the Attorney General with approval of the director. The recommended system is similar to the situation with the ABC Division of the Department of Revenue. The Assistant AG is to be assigned exclusively to the lottery.

**SEC.14. Conflict of interest.** This section prohibits commissioners, employees of the lottery and members of their household from knowingly having an interest in a business which contracts with the lottery or accepting gifts, hospitality or service of more than \$100 per year from someone known to be or to be seeking to contract with the lottery or to be or seeking to be a lottery retailer. It also prohibits vendors and the like from offering gifts of more than \$100 per year and makes the employees subject to all other state conflict of interest statutes.

**SEC.15. Fraud provisions.** Makes attempts to defraud the lottery by altering, forging or counterfeiting tickets a class D felony.

**SEC.16. Prohibitions on selling tickets.** Prohibits the sale of a ticket for a price other than the stated price, the sale of a ticket by other than a lottery retailer, and the sale to a person under 18 years of age.

**SEC.17. Prohibitions on purchasing tickets.** Prohibits the purchase of tickets by, or the knowing payment of a prize, to employees of the lottery, a lottery commissioner or any officer or employee of a company currently engaged in supplying gaming services or products to the lottery. It also prohibits the purchase of tickets by, or knowing payment of a prize, to certain family or household members of the persons identified above. Lottery and vendor employees could be authorized in writing by the director to purchase tickets for purposes of an investigation. Retailers are not prohibited from purchasing tickets.

**SEC. 18. Prizes.** The section provides that as nearly as practical, 45 percent of lottery proceeds, computed on an annual basis is to be paid in prizes. It also provides that prizes are to be paid to one person only. Prizes are not assignable, but can be bequeathed in a will or probate. It also provides that unclaimed prizes are to be added to the prize pool of subsequent games, and lottery winnings are to be taxed as Kansas source income.

**SEC. 19. Sales tax exemption.** Exempts the sale of lottery tickets from state and local retail sales taxes. Iowa is the only lottery state that does not exempt ticket sales from sales tax. The tax is paid by the Iowa Lottery and submitted to the Iowa Department of Revenue. The practical effect of imposing the sales tax would be to reduce net earnings and transfer them to the State General Fund and those local governments with a sales tax.

**SEC. 20. Wagering.** This section makes conforming amendments to current law governing gambling and betting.

**SEC. 21. Retail Liquor Stores.** Amends provisions of current law to allow retail liquor stores to sell lottery tickets if selected by the lottery as a retailer.

**SEC. 22. Law Enforcement Training.** Makes conforming amendments to the Kansas Law Enforcement Training Act.

**SEC. 23. Check Writing Authority.** Authorizes the Director of Accounts and Reports to designate one or more persons to sign warrants, on behalf of the Director of Accounts and Reports, for the payment of lottery prizes. This is considered essential to providing a service to lottery players.

**SEC. 24. Computers.** This section amends current law to allow the lottery to acquire its own independent computer systems and facilities and to issue bids for such equipment independent of the Division of Information Systems and Communications. This is identical to the authority granted to Regents' institutions. All lotteries operate with their own computer systems and facilities because of the security needs.

**SEC. 25. Income Tax.** This section makes conforming amendments to the Kansas Income Tax Act to include lottery winnings as Kansas source income.

**SEC. 26. Sales Tax.** This section makes conforming amendments to the Retailers' Sales Tax Act to exempt lottery tickets from the sales tax.

**SEC. 27. Repealers.** The section repeals required sections of laws.

**SEC. 28. Effective date.** Makes the bill effective upon publication in the **Kansas Register**.

THE KANSAS LOTTERY  
1987 EXAMPLE IMPLEMENTATION SCHEDULE

- JANUARY  
&  
FEBRUARY**                    **APPOINT PROJECT TEAM**  
- address organizational issues  
- develop staffing recommendations  
- draft rules and regulations  
- prepare budget proposals  
- outline specifications for the IFBs
- MARCH**                        **APPROVAL OF LOTTERY LEGISLATION  
AND APPROPRIATIONS**  
- appoint lottery commission members  
- hire executive director  
- hire general consultant  
- finalize staffing plan  
- identify office facilities  
- finalize rules and regulations  
- order office furniture and equipment
- APRIL**                        **RELEASE IFB FOR INSTANT GAME CONSULTANT**  
- conduct pre-bid conference  
- address vendor questions  
- hire key management personnel  
- assemble initial list of retailers  
- move into headquarters facility
- MAY**                         **ANNOUNCEMENT OF SUCCESSFUL BIDDER**  
- conduct background investigation of vendor  
- negotiate and sign contract  
- hire support personnel  
- preparation of regional office facilities
- JUNE**                         **INSTANT GAME CONSULTANT BEGINS**  
- set major policies & goals  
- order computer equipment  
- order telephone lines  
- select advertising agency  
- order first game tickets
- JULY**                        - install telephone lines and test  
- install application software  
- produce advertising  
- train lottery staff  
- ship tickets to distribution centers  
- test drawing equipment
- AUGUST**                      - complete system testing  
- conduct retailer training  
- introduce tel-sell to retailers  
- deliver point of sale materials  
- distribute tickets to retailers  
- begin ad campaign
- SEPTEMBER**                 **FIRST INSTANT TICKETS GO ON SALE**



## LOTTERY PROJECT TEAM TASKS

1. **INVITATION FOR BIDS (IFB)** The blueprints for establishing a successful lottery. A critical step which requires extensive research of other states as well as acquiring a working knowledge of Kansas purchasing statutes.
  - Start-up consultant services
  - Computer hardware/software supplier
  - Marketing
  - Instant ticket production
  - Advertising/public relations
  - Automated accounting system
  - Major prize payments
  - On-line games
2. **LEGAL** Prepare legal impact statements on proposed amendments to the lottery bill. Draft administrative rules and regulations for distribution to the Lottery Commission upon appointment. Finalize the format for contractual agreements between retailers and the lottery.
  - Enabling legislation
  - Administrative rules and regulations
  - Retailer contracts
3. **FACILITIES** Locate potential sites for lottery operations and determine costs and alternatives available to the State. Once facilities have been identified, prepare office layouts.
  - Headquarters
  - Regional offices
  - Main warehouse
  - Floorplans and office design
4. **PERSONNEL** Classification, examination and scoring mechanisms, and other related personnel work must be completed prior to passage of the legislation to allow for the immediate recruitment of lottery employees.
  - Organizational issues
  - Staffing
  - Class specifications
  - Salary surveys
  - Position descriptions
  - Recruitment

5. **DATA PROCESSING** The lottery industry is highly automated and technical expertise is needed to educate project team members on the advantages and shortcomings of vendor bid proposals. A determination will have to be made regarding the network requirements of the Lottery and its immediate impact, if any, on the state system currently being developed.
  - Office automation
  - Telecommunications
  - Technical consultation
  - Communications network planning
6. **ACCOUNTING** Coordination with Accounts and Reports and the State Treasurer and the development of a clear understanding of system requirements will be given high priority.
  - Internal controls
  - CASK
  - Check writing authority
  - Electronic funds transfers
  - Lottery operating fund
  - Lottery prize fund
  - Gaming revenues fund
7. **FISCAL NOTE** The fiscal note on the pre-filed enabling legislation bill will have to be ready for submission early in the session.
  - FY 1987 seed money
  - FY 1988 operating budget
  - Revenue projections
8. **PURCHASING** The immediate needs confronting a new organization require the advance preparation of purchase orders.
  - Major procurements
  - Capital outlay items
  - General office supplies
9. **MISCELLANEOUS** Issues will be raised both internally and externally which will require extensive research of lottery states and the development of position papers and staff recommendations.
  - Number and location of regional offices
  - Retailer recruitment
  - Ticket distribution system
  - Investigation guidelines and procedures
  - Employee background checks
  - Lottery 101 staff training
  - Project implementation plan

10. GENERAL OFFICE SUPPORT Traffic in this area will rapidly increase as lottery legislation moves toward approval.

- Receptionist
- Secretarial and clerical support
- Retailer and vendor correspondence files
- Employment inquiries
- Lottery resource library

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