



Economic Impact Analysis Virginia Department of Planning and Budget

11 VAC 5-41 – State Lottery Department Lottery Game Regulations October 8, 2002

The Department of Planning and Budget (DPB) has analyzed the economic impact of this proposed regulation in accordance with Section 2.2-4007.G of the Administrative Process Act and Executive Order Number 21 (02). Section 2.2-4007.G requires that such economic impact analyses include, but need not be limited to, the projected number of businesses or other entities to whom the regulation would apply, the identity of any localities and types of businesses or other entities particularly affected, the projected number of persons and employment positions to be affected, the projected costs to affected businesses or entities to implement or comply with the regulation, and the impact on the use and value of private property. The analysis presented below represents DPB's best estimate of these economic impacts.

Summary of the Proposed Regulation

The proposed amendments include numerous editorial and other changes, which will update the regulations to reflect the operational and procedural changes occurred in practice since 1996 when these regulations were last amended.

Estimated Economic Impact

These regulations will apply to both instant and online lottery games offered by the State Lottery Department (the department). Both games give players the chance to win a prize or entry into a prize drawing. For instant games, whether the player has won is revealed immediately after scratching off the latex covering over a portion of the ticket. Instant games are also known as "scratchers." Currently, the department offers about 60 different types of instant games with top prizes varying from \$50 to \$1 million. Online games, on the other hand, are played through sales terminals linked to central computers via communications networks. The department also offers five types of online games, which include Pick 3, Pick 4, Cash 5, Lotto South, and Mega Millions. The prizes offered by online games may be high ranging from \$2 to

multi-millions for Lotto South and Mega Millions. For example, on May 9, 2000, the jackpot for an online game then known as the Big Game reached a record \$363 million. The jackpot for Mega Millions, a recently adopted multi state game in place of the Big Game, is believed to have the potential to reach up to \$500 million. Last year, revenues from instant and online games were slightly over \$1 billion. Of this amount, approximately \$557 million was distributed to winners, \$56 million was distributed to retailers, \$73 million was kept by the department as operating expenses, and \$329 million was revenues to the Lottery Proceeds Fund for public education.

The proposed changes are, in large part, designed to help reorganize two of the department's current regulations into two new regulations. Currently, the department has instant game regulations (11 VAC 5-30) and online game regulations (11 VAC 5-40) in place. The instant game regulations contain regulations for both licensing of lottery retailers and for gaming. Licensing requirements establish eligibility criteria for retailers, application procedures, general licensing standards, license fees, rules for termination of licenses, rules for inspection of retailers, etc. And, gaming requirements contain provisions on prize structures, ticket prices, chances of winning, retailer compensation, retailer transactions, payment of prizes, etc. Similarly, online regulations contain requirements both for licensing of lottery retailers and for gaming. Since the two current regulations contain similar provisions for different games, there is significant overlapping regulatory language on licensing and gaming. In order to reduce and simplify the regulatory language, the State Lottery Board (the board) proposes to reorganize the lottery regulations that contain provisions for instant and online games under two new categories: licensing (11 VAC 5-31) and gaming (11 VAC 5-41) regulations. In short, the board proposes to reorganize instant and online game regulations under licensing and gaming regulations.

In addition to the reorganization, the board proposes to update the regulations to reflect the changes in practice that occurred since 1996 when these regulations were last amended. Although this proposed action will introduce a completely new regulation, most of the proposed requirements are in current regulations, which are being repealed under a separate regulatory action. The requirements, which are simply a replica of current requirements, are not discussed in this report. This report discusses only new or modified provisions.

Several proposed changes are editorial. One is the proposed use of the term “barcode” in the regulations. Technological advances in the last decade allow the department to use barcodes for lottery tickets in practice. Similarly, the proposed regulations incorporate the term “cash option” in the regulations because this prize payment option was not available to players until 1997. Also proposed is a provision to permit the director to delay payment of a prize if there is question whether a cash option election is made and a provision that the director may not accelerate payment unless the cash option is elected. Additionally, the term “natural person” will be used in the regulations due to the amendments to the section 58.1-4019.B of the Code of Virginia which require that all prizes must be claimed by a natural person to prevent hiding winner’s identity under a limited liability corporation or other types of organizations. Further, it will be clarified that the director of the department has the authority to reimburse retailers for prize claims a retailer paid in error. Under the current language, the same authority exists. Another proposed change will add that the player assumes all risk for mailing a ticket through the mail. This has been the current practice. Finally, based on the Attorney General’s recommendation, it will be clarified that when there is more than one ticket issued with winning numbers, a holder of one of the winning ticket is entitled only to his or her share of the prize, regardless of whether the other holders of tickets with the winning numbers actually claim their share of the prize. Since these proposed requirements are editorial, no significant economic effect is expected.

Similar to other changes already discussed, provisions regarding several operational requirements that have been enforced in practice will be included in the regulations. These changes appear to be policy related and imposed at the discretion of the department to change the department’s operations or procedures. One of these proposed changes will update the language to require all retailers to cash winning tickets up to \$601 regardless of the location from which the winning ticket was purchased as currently enforced in practice. Previously, the retailer could elect to cash any prize amount from \$26 to \$601, but most chose to cash either up to \$101 or \$601 and they could only cash the instant tickets they sold because of the lack of barcode technology. This proposed change will not have any effect on current enforcement of this rule. Additionally, it is proposed that the liability of the department may end sooner than the prize payment if so provided in game rules as currently enforced. Similar to other changes, this change will not have any effect in practice. Further, a definition for the term “probability game”

is added as a potential future lottery product. In a probability game, all tickets are potential winning tickets and the outcome of the game is determined by scratching a limited number of play spots chosen by the player as opposed to scratching all available spots. The department indicates that these games are not planned but may be offered in the future. These proposed amendments also will not change the way the regulations are currently implemented and consequently are not expected to create any economic effects upon promulgation.

The proposed changes will also provide authority to the department to require prize winners to participate in press conferences as well as to use their names, photographs, the name of city or town they live in for public information purposes. Among these, enforcement of the requirement to participate in press conferences may be problematic. Since the department does not plan to withhold winnings¹ if the winner refuses to participate in the press conference, it is unclear how this requirement could be enforced.² Also, there is a chance that a winner may attend the press conference, but at the same time he may refuse to cooperate. It is highly unlikely that the outcome of such a press conference would be beneficial either for the department or for the winners. Finally, compliance with this requirement may be physically impossible in some cases for the winners, or may be possible at a tremendous cost. In short, the compliance with the requirement to participate in press conferences appears to be very difficult to enforce without the winner's consent. Thus, it may be worthwhile to revise this requirement to provide discretion to the winners so that they can choose what to do.

The department's current approach to implement operational or procedural changes on issues such as cashing winning tickets and other similar issues without going through the regulatory process and then updating the regulations to reflect what is implemented in practice is problematic as the agency is operating contrary to its regulation in this case. The lack of authority to enforce these provisions combined with discrepancies between regulations and procedures followed in practice creates the potential for costly litigation expenses. However, this does not mean that the department would not forgo potential benefits if operational or procedural changes are implemented in practice only after going through the usual regulatory process as timely response to developments in the market place the department operates in may be valuable. One way to reduce potential costs associated with delay would be to seek an

¹ Source: State Lottery Department.

expedited process for promulgating regulations. This might take the form of an exemption, or the use of an expedited process such as the “fast track” process proposed in the 2002 General Assembly Session (SB 536).

Businesses and Entities Affected

Lottery retailers selling instant and online games and the game players are subject to these regulations. According to the department, 4,971 retailers are licensed to sell both instant and online games. Based on a survey conducted by the department in 2002, about 3.5 million adults have played an instant or online Virginia lottery game some time in their lives and approximately 2.9 million players have played in the past 12-month period.

Localities Particularly Affected

The proposed regulations apply to all localities in Virginia.

Projected Impact on Employment

No significant impact on employment is expected upon promulgation of the proposed amendments.

Effects on the Use and Value of Private Property

The proposed changes are not expected to affect the use and value of private property upon promulgation.

² It is also unclear whether the agency has statutory authority to enforce this provision.