

FACTORS SHAPING REGULATORY POLICY IN THE DIGITAL AGE

Howard Glaser

Global Head of Government Affairs and Legislative Counsel, Scientific Games



Paul Jason: Sports betting is being approved across the country at a break-neck speed. Won't the whole process of legislating to legalize and regulate sports betting smooth a path for iLottery legislation too, making it easier and faster to implement legislation that regulates iLottery?

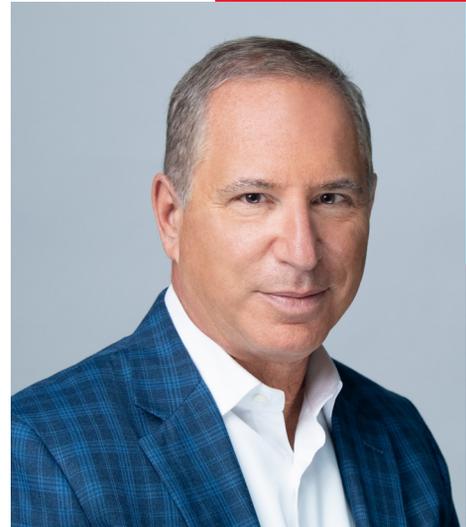
Howard Glaser: I do not agree with the assumption that sports betting is the leading edge, and we can expect that iGaming and iLottery will automatically draft in behind this process. iLottery and iGaming are different animals than sports-betting. State governments treat sports betting as an extension of sports, it's as much about sports as it is about gaming. iLottery and iGaming are purer forms of gaming – and that's the way state government policy-makers think about it so that is the way we should think about it. For this reason, I do not think that the pathway to regulating sports-betting is a great model to use for iLottery. Instead, I believe the industry needs to apply a thoughtful, deliberate, and consistent strategy that aligns with the way that shapers of public policy view these issues.

Legalizing and regulating the betting on sports is an important step for legislators to take, but it does set the tone for iLottery and iGaming. There are lots of differences between these game entertainment categories, and we should not base our strategies on how it has unfolded in the sports-betting space.

Could we drill down a little more on how the process of getting iLottery to be legalized and regulated differs from sports betting?

H. Glaser: Legislators don't view iLottery as being in the same bucket as sports betting. Lottery is a government function and not a commercial function in the eyes of many legislatures. When it comes to sports betting, legislators believe they are acceding to the wishes of a large group of constituents. That's especially true once the sports leagues came on board. There is not quite the same wide cross-section of vocal support for iLottery. Lottery players want to be able to play digitally, but they are not organized into a politically influential interest group within the state – at least not like there is for sports betting.

Lottery is fundamentally designed to benefit the public through the \$80 billion in sales and \$25 billion in net revenues that it delivers for good works. That's huge, but the societal benefit is not highly visible. The financial benefit to the state is already baked into their budgets. The prospect of revenue



increases from iLottery do not necessarily command enough attention to actually drive legislative action. That said, there has been a lot of legislative action to legalize and regulate iLottery and we expect that to continue. Sports betting, commercial casinos and tribal gaming have active and well-funded political action apparatuses. iLottery advocates need to develop consistent messaging to amplify its political voice and potential.

How about retailers? Are they warming up to the prospect of iLottery?

H. Glaser: Retailers are wary of competition from online retailers. Amazon and other online merchants have had a devastating impact on retail. Convenience stores say that they at least have one thing that online merchants don't have and that's lottery products. It has been hard for retailers to see how making these products available online

I believe the industry needs to apply a thoughtful, deliberate, and consistent strategy that aligns with the way that shapers of public policy view these issues.

would benefit them. But lotteries have always valued their partnership with retailers and will always be committed to the success of their channel partners. The retailers must be part of the solution and when they are, it's been very successful. Pennsylvania is a great example. Here you have a market which in just over a year went to a billion dollars in online sales. Their retail sales also increased because of the affiliate and partnership programs that tied everyone into the success of all channels, retail and online. Retailers are commissioned on the sales of the customers they bring to iLottery. That flips the whole equation such that the retailer becomes focused on giving the players what they want which is choice: options to play whenever, however, and wherever they want. Now that retailers have a stake in online sales, they become invested in the ability of lottery to attract and retain the players. They may start out as skeptics, but when they see how it works to everyone's advantage, they become supporters. That's what happened in Pennsylvania and Michigan, and that's what happens in other states where iLottery is successful.

Is Tribal Gaming opposed to iLottery?

H. Glaser: Tribal and commercial casino interests share the same concern and it is somewhat straightforward. They just want to be confident that iLottery will not cannibalize their business. There is no evidence that it ever has. And there is a lot of evidence to suggest that whatever cross-over play there is results in an expansion of the market as opposed to dividing a static revenue base. Casinos have continued to run very well even in states like Pennsylvania where iLottery took a fast running start. Casino revenues are bouncing back to all-time highs in many places. At the same time, mobile gaming has also grown exponentially with a boost from the pandemic when other forms of gaming were shut down. We expect mobile gaming to level off a little bit, but play continues to be up and now casino revenues are rising again. So the cannibalization of existing commercial and tribal casinos is very much a myth that has to be dispelled. The casinos are acknowledging this by being the first to support iGaming, right? They know it doesn't cannibalize their business. More consumer touch-points only reinforce their bond with the players. We believe that the

expansion of gaming options supports the whole market and reinforces each of the participants in that market.

How should the discussion with legislators and political stakeholders be framed?

H. Glaser: We encourage legislators to appreciate the incredible asset that is their own state lottery. They have invested a great deal of money in lottery. Good causes are receiving a lot of funding from lotteries. They are already in the business; all they have to do now is turn on the digital channel. Everybody else is online, so there is no longer any reason why anyone would choose to remain on the sidelines. And the longer you wait, the more market-share you will lose, and it will be hard to gain that back. We need to make the case for iLottery consistently and persistently within the industry and throughout the entire country.

Another aspect of this picture that should be emphasized: the amount of revenue generated for the state by iLottery and lottery is significantly higher than the net revenues generated by sports betting. For instance, New Jersey is an example of sports betting performing extremely well. The money it generates for the state, though, is a tiny fraction of the net funds generated by lottery.

We believe the net funding potential of iLottery is in the \$5 billion a year range. That's huge. States that do not participate in iLottery are leaving their share of revenues on the table.

You discussed how retailers are thinking defensively, as in how they are going to defend their market-share from the competition from online merchants. Similarly, don't lotteries need to consider the need to defend their position in the market-place against the migration of players over to online gaming and entertainment options?

H. Glaser: States that do not implement iLottery sooner than later will very quickly find that their current lotteries are the Sears and JC Penny of the gaming sector. There is a window of opportunity which may close at some point when online gaming operators consolidate their hold on the players. Look at what Amazon did and how difficult it is now for other retailers to carve out a role for themselves in the online general merchandise space. States that authorize

sports-betting, and then possibly iGaming, will likely experience an erosion of their lottery player-base if they do not implement iLottery at the same time. The increase in lottery revenues over the past 18 months may have masked these realities, but we need to recognize that the trend-lines towards eCommerce are quite entrenched, and the gaming sector is not immune.

Consider how movies, music and even video gaming are now primarily an online experience. Video on-demand is an estimated \$16 to 20 billion a year market. The iGaming and iLottery markets are each estimated to be in the neighborhood of \$20 billion. We estimate around \$27 billion in a mature market. Some project even higher potential. Of course, the revenue potential depends on more states enacting legislation to regulate iLottery and iGaming, and the higher projections are based on most of the states adding the online components to the lottery business that they're already in. We expect iLottery and iGaming to both ultimately eclipse the video-streaming Netflix market. So that's the scope of what we're looking at right now.

During the pandemic, we all watched Netflix instead of going to movie theatres. On the content-creation side of the business, we see distributors like Netflix, Amazon and Apple producing more and more original programming themselves. They had to create the technology and the content. Now, look at online lottery in this context. The pieces are already there. The technology exists. No one has to develop the technology and games for iLottery. The game content is there. The consumer interest is there. There's only one thing missing: government authorization. By contrast, Netflix does not have to get a law passed when they want to do a new series. And Apple doesn't need governmental approval to put a new song online. But iLottery typically needs the approval of two legislative houses and a governor to sign the bills before they can get online.

I do think we are nearing the tipping point at which states will look around at their neighbors who have online lottery and feel pressure to do the same just to keep the customers they have, to keep their players from being unhappy. They may even lose business to their neighbors if they don't offer the same kinds of products and services. I

Continued on page 34

What are the biggest obstacles for state legislatures that impinge on their willingness to authorize iLottery? Retailer opposition? Opposition from anti-gambling groups? How about sports betting interests – are they opposing iLottery and is that a factor? What or who else is impeding iLottery implementation?

S. Gunn: All of the stakeholders you mention are relevant to the debate, as Speaker Tip O’Neill said, “all politics is local.” iLottery has been in the United States for nearly a decade after Illinois and Georgia launched programs in 2012. It has been difficult to move the iLottery needle from a policy perspective, but new legal developments and changing attitudes among key stakeholders are shifting. As with most every lottery and gaming innovation, the adoption of iLottery will be dependent on the politics that surround gaming issues in each state. The challenge for lotteries is ensuring they have a seat at the table and voice in the legislative and policy discussion. This is challenging because a lottery functions as a “gaming” operator, but without the flexibility and resources of other commercial gaming

operators. Another challenge is the historic opposition from the National Association of Convenience Stores (NACS) and their local affiliates. NACS opposition was very much aligned with the Coalition to Stop Internet Gambling and their political activities at the federal level. Now that the Coalition to Stop Internet Gambling is not as engaged as they were previously, I think the main opposition will be with the state-based retail associations and organizations. I have found that their opposition is more politically motivated than objectively based on the fact that their business will be harmed by iLottery. I think the solution for lotteries is two-pronged: ensure that fact-based objective information is injected into the debate and develop a political plan that addresses all opposition, including purely politically motivated opposition. I have found lotteries to be savvy and sophisticated in their approach to working with legislatures to ensure they have a full understanding of the policy alternatives that exist for digital gaming expansion. As the market for digital products continues to liberalize in the U.S., and more states become comfortable with answering consumer demand for anytime, anywhere

products on any device, iLottery will gain a foothold and become more commonplace. The stage is definitely being set for more states to embrace iLottery in the next five years.

As I look at the totality of the situation, lotteries are well positioned to benefit from digital gaming expansion. It will require engagement in the political process that is sensitive to the unique circumstances of each lottery and their role in the approval process in their state.

A coalition-based approach, that brings together the supporters of lottery in general, and iLottery in particular, and utilizes the resources of those coalition partners, is the best path to success. There are many stakeholders in this process that should be heard and will have a role in the discussion, including considerations around Responsible Gaming, so that players, the public, and lottery beneficiaries will benefit from the addition of iLottery and the increased funding it provides. That is an indisputable fact, and one that should be central to any discussion about expanding a lottery’s portfolio to include iLottery. ■

also think it’s very helpful that the successful iLottery states are regionally distributed. You have Pennsylvania and Virginia in the Mid-Atlantic, Michigan and Illinois in the Midwest, New Hampshire and Connecticut in New England, and Georgia and Kentucky in the South. Their neighboring states will eventually feel pressure to keep up with the same product and channel offering.

Do legislators study how these issues are unfolding in other states? Is the process of building a regulatory framework informed by the experience of other jurisdictions or do legislators focus on their own in-state issues and environment?

H. Glaser: Unless they are assessing the competitive threats from neighboring states, legislators focus on what’s happening in their state more than anything else, and then build to suit their own state-specific public policy objectives. Legislators sometimes underestimate the complexity

of market-driven businesses like lottery, iLottery and sports betting. Of course, there are professionals like lottery directors and technology partners like Scientific Games and others who make sure the business is operated effectively and will always work hard to protect current lottery revenues, ensure business continuity, and position the business for long-term growth.

One thing we hope for is that legislators will appreciate the importance of moving forward with iLottery in tandem with iCasino gaming. That should be a goal for all lottery stakeholders as it would disadvantage them if iCasino gaming were to launch before iLottery launches. Launching them in tandem would provide the entire range of games to appeal to the broadest range of play styles. Providing that diversity from the start enables players to embark on their digital gaming journey with full and equal exposure to iLottery. It may be hard for iLottery to attract players if

iLottery is launched after iCasino gaming. I think the best chance to expedite iLottery legislation is to join iGaming and have both of them proceed down the path together to legislative approval.

In closing ...

H. Glaser: We want to look for the common ground shared by diverse interest groups so that we all – lotteries, sports-betting operators, iGaming and casinos – work together to expand the diversity of choices for players. Delivering the widest variety of games through all the different channels of distribution is not only the best way to meet the needs of the consumer, but it is the best way to foster creativity and innovation within the industry so that we lead the way and exceed consumer expectations and the expectations of all our stakeholders including the retailers, our political constituents, and the good causes supported by lottery funding. ■