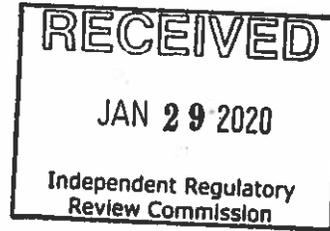


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January 28, 2020

Via E-mail and Federal Express

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Re: PA Department of Revenue's Final-Form Regulation #15-460 on iLottery

Dear Ms. Campbell and Ms. Miller:

Penn National Gaming, Inc. and its Pennsylvania Category 1 Casino / Slots Licensee Mountainview Thoroughbred Racing Association, LLC (d/b/a Hollywood Casino at Penn National Race Course) (collectively "Mountainview") respectfully submit this correspondence in order to share their position on the Pennsylvania Department of Revenue's ("Department") final-form regulation #15-460 on iLottery. Mountainview respectfully requests that the Independent Regulatory Review Commission ("IRRC") disapprove the final-form regulation for the reasons set forth below.

IRRC is tasked with determining whether a final-form regulation is in the public interest. At the outset of its evaluation, IRRC must determine whether the agency has the statutory authority to promulgate the regulation and whether the regulation conforms to the intention of the General Assembly.¹ If IRRC finds that the regulation is consistent with the statutory authority of the agency and the intention of the General Assembly, IRRC is required to consider various criteria, including the economic or fiscal impacts of the regulation.² The State Lottery continues to directly contravene the General Assembly's prohibition on the State Lottery offering casino-style games and games that simulate them. Mountainview urges IRRC to find that the Department's final-form regulation on iLottery is inconsistent with the intent of the General Assembly that the State Lottery offer distinct products from

¹ 71 P.S. § 745.5b.

² 71 P.S. § 745.5b(b)(1).

those offered by casinos. If IRRC should find that the regulation is consistent with the intent of the General Assembly, Mountainview encourages IRRC to find that the regulation is not in the public interest due to the economic and fiscal impacts of the regulation. The State Lottery's continued contravention of the prohibition on offering casino-style games and games that simulate them will result in a loss of significant tax revenue to the Commonwealth that funds various legislative priorities.

The Final-Form Regulation Is Inconsistent with the Intent of the General Assembly

The General Assembly authorized an online presence for both the State Lottery and slot machine licensees in Act 42 of 2017 ("Act" or "Act 42").³ The General Assembly created a clear distinction between the offerings, prohibiting the State Lottery from offering casino-style games or games that simulate them.⁴ In its final-form regulation, the Department failed to establish a process to ensure that the iLottery games it offers are not casino-style games or games that simulate casino-style games, as required by Act 42. The only reference in the final-form regulation to the prohibition on the Department offering "casino-style lottery games" and games that simulate "casino-style lottery games" is in the definition of the term "iLottery game."⁵ The final-form regulation does not provide any parameters for what features or game characteristics simulate a "casino-style lottery game." Nor does the regulation establish any mechanism to evaluate whether a game the Department intends to offer is prohibited.

In its comments to the proposed rulemaking on iLottery, IRRC requested that the Department "explain in the preamble to the final-form regulation how it will evaluate iLottery games to ensure that iLottery games conform to the intention of the General Assembly."⁶ More specifically, IRRC sought an explanation as to how the Department evaluates games to ensure that they comply with the definition of an "iLottery game" in Act 42, which excludes "games that represent physical, Internet-based or monitor-based

³ Act of Oct. 30, 2017, P.L. 419, No. 42.

⁴ 4 Pa.C.S. § 502. The Act defines an "iLottery game" as follows: "Internet instant games and other lottery products offered through iLottery. The term does not include games that represent physical, Internet-based or monitor-based interactive lottery games which simulate casino-style lottery games, specifically including poker, roulette, slot machines or blackjack." 4 Pa.C.S. § 502.

⁵ 61 Pa. Code § 876.2.

⁶ Comments of the Independent Regulatory Review Commission, Department of Revenue Regulation #15-460 (IRRC #3234) iLottery Games, July 2, 2019.

interactive lottery games which simulate casino-style lottery games, specifically including poker, roulette, slot machines or blackjack.”⁷ In the Preamble to the final-form regulation, the Department spurned IRRC’s request and asserted that: (1) the definition of “iLottery game”⁸ in the regulation reflects the prohibition on offering casino-style games and games that simulate them; and (2) the regulations set forth the types of iLottery games that may be offered, the way that the outcome is determined, the prize structures, and that those characteristics “establish them as lottery games and not casino-style games.”⁹ The Department’s final-form regulation does not explain in the preamble or in the text of the regulation how it will evaluate games to ensure that it does not offer casino-style games or games that simulate them.

The proposed regulation’s definition of the term “iLottery game” does nothing more than repeat the definition of that term in Act 42. As such, the regulation’s definition is completely superfluous, and offers no additional guidance as to how an iLottery game will be differentiated from a casino-style game or games that simulate casino-style games. Nor does the remainder of the Department’s regulations effectively implement the statutory prohibition on simulating casino-style games. First, much more goes into determining whether or not a game simulates a casino-style game than merely the method for determining the outcome or the prize structure. To “simulate,” in its common and accepted usage, means to imitate, mimic or assume the outward qualities or appearance of another thing.¹⁰ Accordingly, when determining whether an iLottery game imitates or mimics a casino-style game, the Department must take into account the outward qualities and appearance of a game and the player perception and experience in relation to the game.

Notably, Act 42 is not the first time that the Legislature has used the term “simulate” in the gaming context. In the Crimes Code, in relation to the criminalization of Internet sweepstakes cafes, the Legislature made it unlawful to engage in certain conduct in conjunction with the use of electronic video monitors to offer or allow persons to play a “simulated” gambling program. 18 Pa. C.S. § 5513(a.1) and (f). In interpreting the meaning of the Legislature’s use of the term simulated gambling program, the U.S. District Court for the Middle District of Pennsylvania found that the outward appearance of the games offered

⁷ *Id.*

⁸ 61 Pa. Code § 876.2.

⁹ Preamble at 53-60

¹⁰ Webster’s Ninth New Collegiate Dictionary 1099 (1988); 1 Pa. C.S. § 1903(a).

by Internet sweepstakes operators and the players' experience playing such games were the governing consideration:

[T]he games are set up in such a way that customers are led to believe that their choices may affect the outcome of the game. The exhibits presented at the evidentiary hearing show that the games look like the very same slot machines or video poker games one would find in a casino. Plaintiffs attempt to draw a distinction between the randomization at work in slot machines and the randomization used by Telesweeps through the predetermination of a finite pool of entries does not change the fact that both methods present to the player a game of chance. The only real difference is that there are no state regulations governing Plaintiffs payout percentage in its sweepstakes. What is demonstrably the same, however, and deliberately so, is the simulated gambling program "does give the participant the, if you will, the look and feel of participating in actual poker." For Plaintiff to argue that its sweepstakes is not gambling when it works to create a player experience which mimics casino-style games as closely as possible is too much for this Court to accept.

Telesweeps of Butler Valley, Inc. v. Kelley, No. 3:12-CV-1374, 2012 WL 4839010, at *10 (M.D. Pa. Oct. 2012) (citation and footnote omitted).

The Department's regulations utterly fail to address these paramount considerations identified by the courts for determining if an iLottery game simulates a casino-style game. Indeed, when such factors are taken into account, the conclusion that the Department's current iLottery offerings simulate casino-style games is inescapable.

Second, the regulation addressing how the outcome of a game is determined and the prize structures of iLottery games – Section 876.2c – does not set forth characteristics that "establish them as lottery games and not casino-style games."¹¹ Not only does the provision fail to comprehensively address the simulation issue, but it actually includes factors that are characteristic of casino-style games. Section 876.2.c(c) provides that a random number generator may be used to determine the outcome of an iLottery game. A random number generator, however, is a core mechanic of a slot machine. Likewise, Section 876.2c(d) provides that a prize structure for an iLottery game may include a progressive structure. Again, a progressive prize structure is a common feature of slot machines.

¹¹ Preamble at 60.

Without establishing clear parameters for what features or game characteristics simulate a “casino-style game,” the Department’s rulemaking fails to offer the necessary guidance and will not ensure compliance with Act 42’s prohibition on the Department offering games that are casino-style games or that simulate them. In addition to enunciating such clear standards, the regulation should include a process for evaluating whether a game the Department intends to offer satisfies those standards or is prohibited under Act 42’s directive.

In the absence of such a process, the Department will continue to offer games that are prohibited under Act 42. The Department makes the bald assertion that “the games as defined in the final-form regulation rulemaking are generally accepted in the industry to be lottery games and do not simulate casino-style games.”¹² The Department’s assertion is preposterous as numerous iLottery games currently offered by the Department are slightly varied versions of slot machines offered in Pennsylvania casinos or online slot machines offered by casinos in the Commonwealth or other jurisdictions. Further, the vast majority of the iLottery games offered by the Department offer the same appearance, feel and patron-experience as casino games.

The General Assembly designed Act 42 so that the Lottery and slot machine licensees would have distinct offerings. The failure to implement iLottery in a manner that respects the Legislature’s directive for such separation will result in the cannibalization of slot machine revenue (of which the Commonwealth receives approximately 54%), and undermine the Legislature’s priorities for the use of those funds, including for the support of property tax relief, senior citizen and income-based rent rebates, the promotion of economic development and tourism, support for Pennsylvania agriculture and horse racing, local share for counties and municipalities hosting and surrounding casinos, funding for problem and compulsive gambling efforts and more.

Approval of the Final-Form Regulation Would Be Contrary to the Public Interest

The economic or fiscal impacts of a regulation are to be evaluated by IRRC when determining whether a regulation is in the public interest. Act 42’s prohibition on the Department offering iLottery games that simulate casino-style games reflects the General Assembly’s clear objective to prevent competition between the State Lottery and Pennsylvania casinos in the offering of online games. The Department is well aware of the financial negative impacts on the Commonwealth if the State Lottery competes with casinos. The Department’s explanation of the regulation in the preamble and the information in the

¹² Preamble at 55.

Regulatory Analysis Form (“RAF”) fail to demonstrate that the economic or fiscal impacts of the regulation are in the public interest. The Department claims in Section 21 of the RAF that “[c]osts...for the administration of iLottery are negligible” and that it has determined that the final-form regulation will have “no adverse fiscal impact on the Commonwealth.”¹³ However, the Department’s cost analysis conveniently omits any analysis of how iLottery conducted with disregard of the prohibition on the simulation of casino-style games would negatively impact tax revenue generated by Pennsylvania’s casino industry. The projected loss of revenue from the casino industry is a significant financial and economic impact of the regulation, worthy of evaluation by IRRC.

Act 42 authorized the conduct of interactive gaming in Pennsylvania, with slot machine licensees that hold table game certificates having the exclusive right to conduct interactive gaming in the first instance. Slot machine licensees were entitled to apply for and obtain an interactive gaming certificate from the Pennsylvania Gaming Control Board that would authorize them to conduct peer-to-peer interactive games (e.g., poker), non peer-to-peer games that simulate slot machines, and non peer-to-peer games that simulate table games. Mountainview, a slot machine licensee, paid an interactive gaming certificate fee of \$10 million (separate from the substantial slot machine license and table game certificate fees it previously paid). Mountainview commenced interactive gaming operations in July 2019. Now that Mountainview and other slot machine licensees have commenced interactive gaming, it has become imperative that the distinction be clearly made between: (1) iLottery games; and (2) casino-style games and games that simulate casino-style games. The final-form regulation fails to establish a process to ensure that the iLottery games it offers are not casino-style games or games that simulate casino-style games, as required by Act 42 and the State Lottery Law.¹⁴

The Department’s launch of iLottery with casino-style games is in direct violation of Act 42 and the State Lottery Law, and directly cuts into the exclusive market of the licensed gaming operators, such as Mountainview. The General Assembly’s plain intent in promulgating Act 42 was to authorize online lottery games while preserving the licensed gaming operators’ market without unfair competition from iLottery. Currently, iLottery and the licensed

¹³ Regulatory Analysis Form, Section 21, page 7, and Preamble, Fiscal Impact Section, pages 67-68.

¹⁴ The State Lottery Law specifically prohibits the Secretary from offering “any Internet-based or monitor-based interactive lottery game or simulated casino-style lottery game, including video poker, video roulette, slot machines or video blackjack, through the State Lottery.” 72 P.S. § 3761-303(a.1). Act 42 of 2017 mirrors the State Lottery law by defining the term “iLottery” to exclude “games that represent physical, Internet-based or monitor-based interactive lottery games which simulate casino-style lottery games, specifically including poker, roulette, slot machines or blackjack.” 4 Pa. C.S. § 502.

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gaming operators engaged in interactive gaming are in direct competition, which is wholly inequitable to licensed gaming operators, each of whom paid a \$10 million license fee, as the State Lottery has no license fees, a lower age restriction, pays no taxes, and has the advantage of having the imprimatur of the Commonwealth.

Moreover, the public interest is not served by allowing the Department to continue offering the unlawful iLottery games as the General Assembly has established a public policy in favor of prohibiting the Department from offering casino-style games and games that simulate them. The State Lottery is undercutting the interactive gaming regulatory assessment utilized to fund agencies involved in the administration of interactive gaming. Additionally, by offering games that simulate casino-style games, the Department is diverting monies away from the funding priorities the Legislature has directed for slot machine and casino game tax revenue. For each dollar played on iLottery instead of slot machines, 34 cents is diverted from property tax relief, 10-12 cents is diverted from the Pennsylvania Race Horse Development Trust Fund, 5.5 cents is diverted from the Pennsylvania Gaming Economic Development and Tourism Fund, and 2 cents is diverted from local share funds. For each dollar played on iLottery instead of interactive games, 34 cents is diverted from property tax relief, 5 cents is diverted from local share funds, and 13 cents is diverted from the Commonwealth Financing Authority for grants for projects in the public interest. The aforementioned legislative priorities are co-equal to, and no less important than, the uses of Lottery revenue.

If IRRC permits the Department to promulgate its iLottery regulation, the regulation will not only be inconsistent with the intent of the General Assembly, but also contrary to the public interest. For the aforementioned reasons, IRRC should disapprove the Department's final-form regulation on iLottery and require it to uphold the explicit intent of Act 42.

Thank you for your consideration of Mountainview's position on these important matters. Should you have any questions on these comments, please feel free to contact me.

Very truly yours,



Adrian R. King, Jr.

ARK/jfs