

STATE INTERPRETATIONS OF “SKILL” AND “CHANCE”

INCONSISTENT OPPORTUNITIES FOR STATE LOTTERIES AND OTHERS



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The gaming landscape in the United States is quickly evolving and gaming operators, including state lotteries, are working to innovate within the existing regulatory framework to access a new generation of players. Games of skill offer one opportunity to expand game offerings. Generally, U.S. states define a “lottery” as an activity that involves (1) the opportunity to win a prize, (2) determined on the basis of chance, (3) for which one gives consideration. Thus, if the outcome of a game is determined by player skill (rather than chance), usually it may be lawfully conducted by commercial operators without a license. See, for example, www.Skillz.com, which makes available cash prizes for winners of video skill games, except in thirteen states.¹

Given the potential opportunity within the games of skill space, whether a particular game is one of skill or chance is increasingly relevant. For example, much debated is whether poker is a game of skill or chance. Though overturned, District Court Judge Jack Weinstein’s opinion in *DiCristina* analyzing voluminous expert testimony and holding that Texas Hold’em poker is a game of skill is instructive as to the legal debate and because it may signal the types of decisions we can expect in the future.

Though the District Court decision in *DiCristina* now provides little legal support for the argument that poker is a game of skill and not chance (because the decision was overturned² and the U.S. Supreme Court declined to hear the case³), it highlights the fact that states define gambling differently. These differences may soon produce odd and surprising results, among them, that in some states, peer-to-peer poker will be considered a game of chance, and thus able to be offered as a state lottery game, while in other states, the same game will be considered a game of skill and thus prohibited as a state lottery game.

In most states, whether a pay-to-play game involving skill and prizes is a lottery depends on the relative degrees of skill and chance present in the game. Most states and federal law make this determination using what is known as the “predominance test” – meaning that if the element of skill predominates over the element of chance,

1) See: <http://skillz.com/legal> (last accessed March 4, 2014). 2) *United States v. DiCristina*, 726 F.3d 92 (2d Cir. 2013). 3) *DiCristina v. United States*, 2014 U.S. LEXIS 1457 (February 24, 2014). 4) Indiana Code § 4-30-3-7 and New York Tax Law § 1604. In regard to the manner of selecting winning tickets, the Indiana law also provides: “However, if a lottery game involves a drawing, the drawing must be public and witnessed by an independent certified public accountant. The equipment used in the drawing shall be inspected before and after the drawing.” Also, “[c]oins or currency may not be dispensed from an electronic computer terminal or device used in a lottery game.” *Id.* 5) *Id.* 6) *George v. NCAA*, 945 N.E.2d 150, 157 (Ind. 2011), citing *Tinder v. Music Operating, Inc.*, 142 N.E.2d 610 (1957) 7) *Tinder v. Music Operating, Inc.*, 142 N.E.2d 610, 614 (1957) 8) *Meinert v. State*, 131 N.E. 515 (Ind. 1921), referring to poker as “a game of chance.” 9) N.Y. Const., Art. I, section 9(1). Pari-mutuel betting on horse races, as prescribed by the legislature, is also allowed, and, pursuant to a 2013 amendment to the New York Constitution, New York allows casino gambling at up to seven facilities as authorized and prescribed by the legislature. *Id.* 10) NY Penal § 225.00(2) 11) NY Penal § 225.00(10) (Note: raffles, as defined in subdivision 3(b) of Section 186 of the general municipal law, are excluded from the definition of “lottery.”) 12) NY Penal § 225.00(1) (emphasis added) 13) *Dalton v. Pataki*, 835 N.E. 2d 1180, 1192-1193 (NY Ct. App. 2005), affirmed as modified (5 N.Y.3d 243), reargument denied (5 N.Y.3d 783), and certiorari to the U.S. Supreme Court denied (546 U.S. 1032 (2005)). Video lottery meets this description in New York, because players purchase virtual instant tickets and receive a prize in the form of compensation or chances to play additional games. “Multiple participation is satisfied in that the VLTs are linked through the site controllers to a central system, and players compete against one another for prizes by purchasing tickets from a finite depleting pool of electronic instant lottery tickets, with a set number of predetermined winners randomly distributed, or by choosing a series of keno numbers, colors or symbols from a finite pool in the hope that they, as opposed to other players, will have matched those colors, numbers or symbols later drawn, thus satisfying the element of chance. It is of no constitutional significance that the tickets are electronic instead of paper.” *Id.* 14) Note that in 2013, New York voters approved a constitutional amendment to allow casino gambling in as many as seven casino facilities. See footnote 11. 15) *Dalton v. Pataki*, 11 A.D.3d 62, 90 (N.Y. App. Div. 3d Dep’t 2004).

then the activity is a “skill game,” and the game is not a lottery. Other states, however, employ what is known as the “material element” test. In these states, a game is considered a game of chance if chance plays a material role in the outcome, even if skill is also involved – indeed, arguably even if skill predominates. Accordingly, it is more risky for commercial operators to offer skill-based games in those states. To be lawful, player skill must clearly determine the outcome – i.e., chance cannot play a material role. A handful of states use the “gambling instincts” test. This subjective test deems a game to be a gambling game if it appeals to the players “gambling instincts.”

The application of these different tests may, in the future, lead to differences in the types of games state lotteries can offer. By way of example only, the laws in Indiana and New York give the state lottery authority the power to determine, among other things, (1) the types of lotteries to be conducted, (2) the method to be used in selling tickets, (3) the types of locations at which tickets may be sold, (4) the manner of selecting winning tickets, and (5) the frequency of drawings or selections of winnings tickets.⁴ Further, in each state the state lottery is limited to the conduct of “lottery” games.⁵

The term “lottery” is not defined in the Indiana Constitution or lottery laws. However, in interpreting Indiana’s criminal statutes, Indiana courts have defined “lottery” to mean “a scheme for the distribution of prizes by lot or chance among those who provided or promised to provide consideration. Under this definition, there are three essential elements to a lottery, as described above: (1) a prize; (2) chance; and (3) consideration.”⁶ Indiana follows the “predominance test,” and thus for a game to constitute a lottery, chance must predominate over skill in determining the outcome of the game.⁷

Accordingly, because poker is currently considered a game of chance in Indiana,⁸ it appears that the Indiana Lottery Commission has the authority to conduct it as a state lottery game.

In New York, the Constitution prohibits all lotteries “except lotteries operated by the state and the sale of lottery tickets,” the proceeds of which must benefit education”⁹ However, as in Indiana, what constitutes a “lottery” is not defined in either the Constitution or state lottery laws. Under New York’s Penal Law, “lottery” is a subset of “gambling.” “Gambling” means wagering upon the outcome of a contest of chance (or a future contingent event not controlled by the player) and the opportunity to receive something of value in the event of a particular outcome.¹⁰ The term “lottery” similarly has three elements:

- a) the players pay or agree to pay something of value for chances, one or more of which chances are to be designated the winning ones;
- b) the winning chances are to be determined by a drawing or by some other method based upon the element of chance; and
- c) the holders of the winning chances receive something of value,¹¹

However, what constitutes “chance” under New York law is different from “chance” under the laws in Indiana. While Indiana follows the “predominance test,” in New York, a “contest of chance” means any contest, game, gaming scheme or gaming devise in which the outcome depends in a material degree upon an element of chance, notwithstanding that skill of the contestants may also be a factor therein.¹² Thus, there was no question in DiCristina that the peer-to-peer poker at issue was a game of chance under New

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spective. However, from a general business perspective Mauritius is positioned as the gateway to Africa. On that note Lottotech has been approached to operate outside of Mauritius which is why we are seriously developing our people for the future.

What would you say is unique about operating the lottery in Mauritius?

M. Carinci: The retail network is unique compared to North America. There is only one large chain as most retailers are small family owned businesses. There are four shopping malls, however the kiosk concept is new so there is opportunity for material growth. We recently expanded the distribution network from 571 to 911 retailers over a very short period of time which has had a very positive incremental impact on sales. In Mauritius there is one pay period per month which impacts the selling cycle for most products.

There have been many start-ups in the African region and a few success stories. Lottotech certainly seems to have made the cut!

M. Carinci: Oh, definitely Lottotech is a great success story. After only four years our lotto game (6/40) has very high participation rates of 69% in a given month. The sales at the base jackpot of Rs5million continue to grow. I would say Lotto has become part of the culture, almost an institution. Unaided brand awareness is 100%. The percentage of quick picks is approximately 15% which I think is one of the lowest in the world demonstrating the emotional connection of ownership towards numbers. Total lottery annual per caps are \$60+ which may seem low to mature lotteries, however considering the GDP(PPP) in Mauritius it is good reinforcing the fact that a lot of people are spending modest amounts every week, in other words playing responsibly.

What about the instant category?

M. Carinci: The category represents about 25% of the total sales and participation rates of 46% on a monthly basis from adults (18+). Last May we rolled out a growth plan which has had excellent results increasing weekly sales by 50%. The instant category sales are also impacted by the aforementioned payday cycles, again reinforcing the fact folks play responsibly. We are introducing brands that have been very successful elsewhere such as Bingo and Crossword as well as themes that are completely Mauritian. While the Dodo bird is extinct, (rumor has it that the Dutch ate them all) this would likely be a strong theme specific to Mauritius as the Dodo is a strong symbol in Mauritius. It represents a sense of pride and strength. It is actually found on the country Coat of Arms.

What are you doing to advance the lottery in Mauritius?

M. Carinci: Doing what lotteries all over the world do, take the best in class, tailor it to the market and wait anxiously for the results. We have partnered with Ipsos Canada in our market research endeavors which has worked very well, particularly in the transfer of knowledge from a company that has deep lottery experience. The recent expansion of the retailer network aligned with best practices has resulted in incremental sales. We are working towards our WLA Responsible Gaming certification with the aim to e at Level 3 this year. I am working with the regulator in Mauritius to apply the Responsible Gaming framework to all forms of gaming in the country. It has been a lot of fun using the Erewhon case studies (Thanks Guy!) to give our team the insights. We are really so lucky in our industry to be able to benefit from the successes and failures of others. GTECH has been a good partner in exposing global best

practices to the young team. Of course, I am committed to sharing my 38 years of experience with the team as well as exposing them to experts in the industry. This experience enhances my appreciation for the wonderful network our industry has globally!

Do you have plans to roll out other games and how about the internet?

M. Carinci: Mauritius still presents many serious opportunities in the traditional lottery space. While the internet is certainly an opportunity, mobile is of even greater interest as cell phone penetration is above 100% and smart phone and tablet penetration is increasing every day. While it is tempting to want to introduce all the developed proven games quickly we don't want to spoil the market by moving too quickly. The plan at the present time is to build long term sustainable growth as has been done all over the world.

What's Next?

M. Carinci: Lottotech is currently working on a very interesting initiative which I will be able to share with you in a few months, something that is a completely new experience for me. We would also like to work closely with WLA in developing the African Association of Lotteries further. Of course I am looking forward to seeing everyone in Rome this fall which is our summer!

No, I meant what is next for Michelle Carinci?

M. Carinci: You know I have been so lucky over the past 38 years in the lottery/gaming industry it is difficult to think of doing anything else. As long as I am creating value for the company and shareholders I work for and having a good time doing so, my golf game will just have to wait! ♦

York law, and this was in fact conceded by the defendant. Even if skill were agreed to predominate over chance in the outcome of play, there could be no doubt that the outcome of play depended in a material degree upon an element of chance – i.e., the deal of the cards.

Accordingly, one might argue that the New York State Lottery could offer peer-to-peer poker to its players even if skill were deemed to predominate over chance. However, the New York Court of Appeals (that state's highest court) has stated:

[T]he limited constitutional exception for state-run lotteries cannot be read to allow any casino game (such as poker, blackjack or roulette) to constitute a valid lottery if operated by the State. Thus, we agree with the Appellate Division [citation omitted] that a constitutional lottery requires something more – specifically, the use of tickets and multiple participation, as opposed to a single player competing against a single machine.^{13, 14}

The lower court, which was affirmed in the above-described decision, had even clearer language. It stated:

is a big mistake and a huge missed opportunity when a supplier does not recognize our collective buying power. What we decide to do can be rolled out to over 8,000 stores, which adds up to a lot of sales. And our personalized clerk-assisted selling model aligns with Lottery in ways that the other big-chain stores are not likely to do.

Additionally, 7-Eleven is on quite the exciting growth curve.

M. Hagen: Our store base has grown by 2,000 stores just over the last three years. That's 25 %, and we expect the growth to continue.

Isn't the entire c-store sector moving towards consolidation? And so the things that Lottery needs to do to meet your needs are really no different from what they will need to do anyway to meet the needs of larger and larger chain store operations.

M. Hagen: That's very true. 7-Eleven just happens to be one of the most progressive of all the c-store operators. Lottery can learn a lot from working with us to create new avenues for cooperation. We are pleased to work with Lottery, share ideas for ways to improve the business, forge new initiatives that will help Lottery grow. And, yes, I would suspect that Lottery will get lots of fresh ideas that could be introduced in some fashion in other c-stores. And the challenges of meeting our needs for better and more organized performance data will be well worth the trouble because other large chain store operations will require the same thing.

You just referred to the need for data and reporting that is more organized, formatted in ways that our usable by you, and standardized across all states. There are limi-

tations to the ability to standardize for the simple reason that lotteries all sell different products. So we all get that Lottery can't do everything that is desirable on this front. But is lottery doing everything they can to make their reporting as useful to you as possible?

M. Hagen: We talked about this at the PGRI conference in November. 7-Eleven sells lottery products in 33 different states, and we have 16 accountants that have to manage the data we get from lotteries in 33 different formats. I'd like to think that we can do better than that. I understand there may be limitations to what can be done, but I'd like to think that if we work together we can develop a more standardized approach for reporting lottery sales to retailers that is ultimately more efficient for us and more efficient for the lotteries. It will take a concerted effort on the part of all the states to produce a more organized system for reporting sales data and all I'm asking for is that we start the dialog. Lottery is not the only category where we have multiple suppliers. The CPG products throughout our stores come from thousands of different companies but for the most part they provide sales/invoice data in a consistent format. All I am really asking for is recognition of the problem and a more proactive approach from more state lotteries. To get started, all we would need is eight or 10 lotteries to work with us to figure out how to standardize the reporting in a fashion that meets the needs of all of them. We know how this is done because we work with all the CPG companies to do it. So we could help Lottery do this. We want to help Lottery to do it.

Switching gears, what is the average daily commission per store from lottery for

7-Eleven?

M. Hagen: I can't share specific numbers but I can tell you that our daily commissions, while they vary widely by state, are a meaningful number for us. In addition when Powerball or Mega Millionsjackpots get over \$300MM, that number can go up significantly. When that happens we also benefit from all those additional lottery-ticket guests who buy more than just lottery when they visit our store.

The lottery category is already one of our top 10 traffic drivers. When the jackpot gets over a certain threshold, the number of lottery customers can increase dramatically. While those guests may be coming to the store primarily to buy a Powerball or Mega Millions ticket, roughly half of them also buy something else which helps our total sales.

In fact, one of the things that the lottery could do to help us is have more \$300MM plus jackpots, we should all be so lucky. While we may not be able to control the jackpot, one thing we can control is doing a better job of capitalizing on the increased traffic that large jackpots generate.

One of the things I would like to see us work on is how to quickly execute some cross-promotions with Lottery during those high jackpot times. There is no way we can ship a physical coupon to 8,000 stores quickly enough to take advantage of a large jackpot. However, with the lottery's help we might be able to use the lotto terminal to print out a coupon during high jackpot periods.

Our goal is to give the incremental lottery customer a coupon to bring them back into the store the next day or the next week. That would be huge for us. There is no reason it can't be done if we work together to make it happen. ♦

Pursuant to the definition advanced by [the NY Governor and others], any game of chance – including such casino games as poker, blackjack, craps and roulette – could be a lottery if operated by the state. Such a broad interpretation would expand the constitutional exception permitting state-run lotteries to such an extent that it would swallow the general constitutional prohibition on gambling. [citations omitted] N.Y. Constitution, article I, section 9 cannot support such a broad reading.¹⁵

Thus, while it appears that peer-to-peer poker likely could be of-

ferred as a lottery game by the Indiana State Lottery, the same game could not be operated by the state lottery in New York.

In summary, differences in state laws, both statutory and as developed through court decisions, will result in curious differences in the types of lottery games that may be conducted by state lotteries in different states. These differences are likely to become more noticeable and significant as state lotteries expand their game offerings online, and in particular, as they compact with each other in order to combine players and prize pools. ♦