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PGRI Introduction: The German Interstate Treaty on Games of Chance, which came into effect on January 1, 2008, banned all forms of online gaming and online betting in Germany. The main goals of this treaty were youth and player protection as well as prevention of gambling addiction. As the Interstate Treaty on Games of Chance expired at the end of 2011, a new state treaty came into force. The new treaty shifted the perspective, stating that along with player protection and preventing gambling addiction, the goals of channeling the demand into regulated offers, preventing crime and fraud, and securing the integrity of sports to be of equivalent importance. Fifteen of the sixteen German federal states signed that treaty (Schleswig-Holstein passed its own, more liberal, gambling law coming into effect on January 1, 2012), so that the new treaty came into effect on July 1, 2012. In addition to the expansion of the goals, the key issues of the new treaty were the perpetuation of the monopoly for lotteries, with the possibility to apply for special permits to sell lotteries via online and mobile channels, and implementing a testing model for liberalizing the sports betting market with 20 licenses.

Consequently, in 2012 there were two valid legislations in Germany with regards to gambling: a very liberal regulatory system in Schleswig-Holstein and a more strict regulatory system in the rest of the country. This situation did not change until January 24, 2013. On this day, two significant events occurred. First, the parliament of Schleswig-Holstein passed a law to join the treaty of the fifteen other states. This decision of Schleswig-Holstein means that there is now unanimous support among all sixteen German states for the new German

Treaty on Games of Chance.

The other event is based on a totally different issue, but is strongly connected to the case of Schleswig-Holstein. A commercial operator was sued in 2008 for offering online gambling in Germany. The private company lost its argument that the state treaty would not be in compliance with European Union laws regarding free trade. It proceeded to appeal against the court's decision by going to the German Federal Court of Justice. The Federal Court approved the prior decisions for the period of time ending December 31, 2011; and referred questions regarding the time span from the beginning of 2012 (the onset of Schleswig-Holstein gambling law) until the day of the current hearing, over to the European Court of Justice (ECJ) for review and comment. The answer is still to come.

The case of Germany is a good example of how the individual regulations of the Member States of the European Union and the laws of the Union itself can sometimes conflict. European Member States all have, and have always had, different gambling regulatory frameworks. Commercial operators are lobbying the European Union Commission to force EU Member States to open up their markets to free and open cross-border trade of gambling. The overwhelming majority of EU Member States, as represented by the European Parliament, contend that EU laws requiring free market competition and open cross-border trade do not apply to gambling and lottery. Gambling products can rather be characterized as being of a very special nature and depend highly on the culture of each country. This principle that gambling is excepted from the general EU laws that require free-market competition and open borders, along with the principle of subsidiar-

ity which confers authority over these issues to the Member States, has been re-affirmed time and again by the highest courts in the EU. Further, the European Parliament has affirmed that the matter of tax and regulatory policy as pertains to gambling and lottery should be in the competence and authority of the Member States. PGRI advocates for the position of the European Parliament – that EU Member State governments are empowered to determine the regulatory and taxation framework that best serves the interests of their citizens.

The regulatory climate within the European Union remains in a state of flux and uncertainty. Thankfully, it appears that the EU Commission is endeavoring to clarify its position on these matters. Germany is especially interesting because the German government, and the lotteries, have struggled mightily to preserve the stability of a regulatory model that effectively preserves Public Order, protects the consumer, and results also in funding for worthy causes that help society. We thank Mr. Goßner for taking the time to share his insights and for helping us to understand this complex set of circumstances, and how they affect the operation of the Westdeutsche Lotterie. Too, since we are meeting at the European Lottery Congress in Tel Aviv, we discussed how the industry has changed since the Helsinki EL Congress of two years ago.

My conversation with Mr. Antonopoulos at the European Lottery Congress in Tel Aviv included impressive demonstrations of these ideas in action which, unfortunately, can't be replicated by mere text. What does come through loud and clear is that the consumer retail experience will be transformed by the smart application of digital technology.

Paul Jason, Public Gaming: *The “German State Treaty on Games of Chance” was established almost five years ago and revised at the end of 2011. Can you describe the main differences between the two treaties and explain why a revision was necessary?*

Theo Goßner: First of all, the goals of the new state treaty have changed from the old treaty. The overarching goals of the original treaty focused on the youth and player protection, and the prevention of gambling addiction. For this purpose, the old treaty set strict regulation for advertising and forbade online gambling, for example. The problem was that, due to some judgments of the ECJ questioning the compatibility of the German State Treaty with EU law, public authorities were hampered in executing this regulation. The lack of effective means of enforcement allowed the grey and black market to develop in a very strong way. Evidence of that is the fact that the German state lotteries had a market share of only 3 % in sports-betting in spite of having a monopoly on sports-betting.

Therefore, the German authorities revised the State Treaty when it expired in 2011. Along with the goals of player protection and prevention of gambling addiction, the goal of channeling the demand away from unauthorized operators and over to the state-authorized operators came into force. The regulatory authorities want to allow the regulated companies to offer more attractive products to attract customers, hoping that will keep consumers away from unregulated offerings in the grey and black market. That is why there are very strict conditions for player protection and addiction prevention. Against this background, the German authorities began to accept applications for permits to do Online marketing and TV and Online advertising. In addition to allowing more attractive products and promotion, the market for sports-betting is being re-organized. Formerly, sixteen regional state monopolies, similar to those in the lottery market, existed to offer product for sports bets with fixed odds. As this market model eroded during past years, the new State Treaty installed a license model for a multi-year test. Included in this test, twenty sports-betting licenses are currently in the process of being awarded.

I wonder if our political stakeholders recognize and appreciate that lotteries are already performing to a much higher standard than private commercial operators?

T. Goßner: For us, responsible gaming has evolved to include the more expansive concept of Sustainable gaming. Our political stakeholders and regulators already expect us to employ the highest standards of responsible gaming. Now we are looking at how the Lottery can align even more closely with the interests of society and support a broader range of societal goals. I think that regulators are well aware of the fact that state-regulated lotteries already fulfill a standard of responsibility and sustainability that is much higher than the private companies. But that conviction is not necessarily adequate to allow them to take action against the private offerings, or even to compel the private operators to comply with the same standards as Lottery is held to.

It does not seem reasonable to hold the lottery to a different standard than operators competing in the same gaming categories.

T. Goßner: The government is the primary stakeholder of the state lottery and so the Lottery will, as a matter of course, embrace the rules and expectations and standards of performance that is expected of it. That is not necessarily so with private operators, especially those that are based outside of Germany. We can all see that there are effective methods of enforcement, like requiring the banking system to block funds transfers that are done in the course of illegal gambling. Even so, EU laws and German national laws make some of these enforcement mechanisms difficult to implement. Advertising restrictions are hard to enforce on operators which are based outside of the national jurisdiction. And Internet operators are contesting the rights of the EU Member States to require compliance with all manner of rules and requirements. These are complicated issues that make it difficult to implement a regulatory framework that is enforceable.

The source of the confusion is the lack of clear guidance from the EU Commission?

T. Goßner: Not in the first instance. The primary source of the problem in Germany is the old interstate treaty which expired at the end of 2011. As already mentioned the treaty justified the monopoly for lotteries and sports-betting with the need for youth and player protection as well as preventing gambling addiction. Parallel to this very restrictive ruling, a much less restrictive set of regulations was applied to gambling halls and other sectors of the industry. As slot machines in gambling halls are proved to show a much higher danger

of gambling addiction, the EU Court of Justice determined that the set of regulations in the overall view was inconsistent. Thus, the need for the market constraints by the monopoly were not justified in an adequate manner and the ECJ came to the conclusion that the state treaty was not in compliance with EU laws.

The new interstate treaty and gaming laws correct this problem, removing the inconsistencies. The new Treaty applies not only to lotteries and sports betting, but also to gambling halls. It is our expectation that if the European Court of Justice is again asked to assess the German regulatory framework, the ECJ will agree that the inconsistencies are removed such that the German regulatory system is now compliant with all EU laws.

Nevertheless there is a need for the German regulators to enforce the new legislation.

The main thing is that the government preserved the monopoly over lottery, correct?

T. Goßner: That is most important, of course, because it helps to achieve the goals of the interstate treaty, especially player and youth protection, in the best way. The old legislation granted the German lotteries a state monopoly in sports-betting, too. The problem was that the underground market grew to control 97% of the sports betting market. The monopoly was not very meaningful since the German lotteries had only 3% of the market. Our political leaders and the regulator realized that if they couldn't prevent illegal offerings, especially on the Internet, then it would be better to license, tax, and regulate them as a second best solution. At least the canalization of the demand will be improved. This is what all our neighboring countries have done and so it made sense for Germany to do it, too. So the new interstate treaty established a licensing model, allowing up to twenty licenses to offer sports-betting. This issue is not completely settled, though, since operators which are not granted a sports-betting license may choose to contest the legality of the new treaty.

So, problem solved? The basic Lottery model remains intact and viable and the license model for sports-betting channelizes the demand to regulated offers.

T. Goßner: A treaty which corrects the inconsistencies and establishes a framework that is compliant with EU laws is an important start. But there are still obstacles faced by German lotteries to carve out a relevant role for themselves in a modern

market-place for recreational gaming. One of the difficulties, for instance, is our precise and exacting way we conduct all business. Not that we should have it any other way, but it does put a burden on our distribution partners, the retailers who must comply with lots of formal bureaucratic requirements in order to sell our products, and then be willing to follow time-consuming procedures as a vendor of the product. The Lottery way of doing business is a lot more burdensome to the retailer than the alternative goods and services and gaming options that they vend. On the other side of the street are gambling halls that do not have to comply with the complicated systems that we impose, making it very easy for them to get set up to do business and process transactions. The irony is that lottery games are much more benign, much less likely to cause problem gambling or appeal to problem gamblers. The games offered in the gambling halls are much more likely to result in increased social problems like problem gambling. That is the inconsistency that our legislators and regulators were required to reconcile. The new legislation does that, imposing regulatory standards and procedures that are proportionate to the nature of the game, proportionate to the potential for the game to lead to problem gambling and such. In a perfect world, the result should be that it is easier for the consumer to buy lottery tickets and the retailer to sell lottery products than it is for them to buy and sell casino and poker games or products in the gambling halls. But it isn't.

For instance, the current discussion is about the requirements for the consumer to be able to buy lottery tickets over the internet. It is being proposed that the person register and provide their personal passport for identification. Some are protesting that the requirement for passport information is not proportionate to the nature of a lottery purchase that may cost 3 or 5 or 10 euros. Lottery should be easier for the consumer to play, and for the retailer to sell, because it poses little risk to the consumer.

Did the treaty also give you more flexibility in the area of advertising?

T. Goßner: Yes. It gives us more flexibility to use different media, like the Internet and TV, which were prohibited under the old treaty. Too, the old treaty prohibited anything other than the communication of basic information. Nothing that could be seen as making the lottery attractive to the consumer was allowed. This requirement to avoid any kind of promotion that

appeals to consumers has been modified. There are still restrictions, but at least we now have the flexibility to do more than communicate basic information.

I never did understand how informational advertising could be differentiated in a legal context from promotional advertising.

T. Goßner: There was in fact some confusion over that. The more important factor, though, was that legislators realize that if one wants to channelize demand away from underground operators and over to the legal authorized operator, we need to be able to advertise, to promote the products. From a responsible gaming and public policy point of view, we will always need to have a conservative approach to advertising and promotion. But more flexibility was needed to communicate the attributes of the product and why it is fun to play. Without that, the consumer will go to the gambling halls or illegal internet operators and be more likely to lose much more money than they do playing the lottery. We have to at least make our product visible to the consumer, and that means communicating what it is, how to play, and why it's fun to play.

Advertising is not an issue relevant to the EU Commission, is it?

T. Goßner: No. These advertising issues are relevant to the German federal state governments. The EU Commission focuses on maintaining legality in the ways that gaming operators conduct business across Member State borders.

Compared to other parts of the global market, especially the United States, Instant scratch tickets comprise a very small percentage of your sales. Why is that?

T. Goßner: Lotto has been the traditional game for the German consumer for many decades. They know it and like it and it is just what they happen to prefer. Another reason for low Instant ticket sales is that we are very restricted in offering scratch games. We were limited to four scratch games at the same time. That has been increased to six scratch games at any one time, but we are still limited in how we can market the games. And we do not have much of the flexibility that U.S. lotteries have with brand-licensing to drive consumer affiliation and price points that vary from \$1 to \$20 or even more. And those are some of the very techniques that have driven the growth of Instants in the U.S.

How important will be digital channels like Internet for you?

T. Goßner: It is difficult to project right now because we just started online gaming a couple months ago. And the kind of identification required of the consumer for online purchasing has still not been clarified. Too, just like everywhere else, we need to help land-based retailers understand how online sales will help their businesses, or at least not hurt their sales. We need to eliminate, or at least minimize, conflict between the different channels.

Is Eurojackpot going to be a meaningful addition to your portfolio of games?

T. Goßner: We think so. It has been a long discussion with our political stakeholders because Germany has restrictions on the jackpot size. The largest jackpot allowed is 90 million euros. I realize that is not much compared to the jackpots you have in the U.S. But it is for Germany and, from a public policy point of view, our legislators do not want to create a jackpot-driven mentality. They do not want consumer excitement to be over-stimulated by super-large jackpots. So that is the issue with Eurojackpot.

Too, it is a high priority for us that our whole portfolio of games works well together, as a product category. We want to avoid cannibalization and integrate a new game like Eurojackpot, or any new game, so that it complements the other games and augments overall sales. We expect that Eurojackpot might appeal to younger demographics and otherwise expand the customer base.

Maybe it will be a blessing to have the jackpots capped so you do not get caught up with rising consumer expectations and jackpot fatigue syndrome. In fact, given the goal of building a sustainable business that encourages healthy and responsible recreational gaming, it seems like there are many reasons to be quite optimistic about the future. The German lotteries have always had more political and regulatory challenges than anywhere else in the world, and I'm not sure that has changed. But the new Treaty does set a more rational foundation that enables the different gaming sectors to co-exist, doesn't it?

T. Goßner: While it's true we have more to be optimistic about than in years past, there are still many obstacles, some formidable and some intractable. There is still the problem with enforcement of the laws against unlicensed Internet gaming operators. But the new Treaty does go a long way towards rectifying the inconsistencies and allowing the German lotteries to con-

duct business in a way that enables us to deliver value to the consumer and continue to generate funds for good causes.

It is still not certain, though, the direction that the EU Commission will take with regards to the rights of member states to determine regulatory policy. We know we need to comply with EU laws regarding consistency and other requirements; and we feel that the new treaty does comply with all EU requirements. But we do not know for sure how the EU Commis-

sion will regard the protestations of operators based in low-tax havens that want the EU to impose a pan-European regulatory framework. The EU Commission has already acknowledged that there is no reason to create a pan-European system that would result in a race to the bottom of minimal taxation. The EU Commission has stated that their focus is on consumer protection and responsible gaming. So, we are hopeful that the EU Commission will recognize that we, and our counterparts in

other EU nations, are taking every measure to deliver the highest standards of consumer protection and responsible gaming and to have a fair regulatory system. And we hope the EU Commission recognizes that bowing to the pressure of the few small Member States which want free and open borders would be devastating to the causes that depend on funding from lotteries, and would most definitely not contribute to the goal of protecting the consumer. ♦