

# Is The State Lottery The New Online Casino?

By **Michael Peacock** (May 23, 2024)

State lottery games and traditional casino games have long been easy to distinguish. For example, when one thinks of a Powerball ticket or a scratch-off ticket, those products are identified as conventional lottery games, whereas the slot machine and roulette wheel are synonymous with the casino industry.

However, with the advent of internet and mobile gaming in the U.S., the traditional lines of demarcation between lottery and casino games are eroding, as new so-called iLottery games that can be played on a smartphone are largely indistinguishable from online casino-style games to the casual gambler.



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The American Gaming Association defines "iLottery" broadly to comprise online computer sales and/or mobile device sales of lottery products, as well as online subscription services.[1] As of May, 15 states legally permit iLottery sales in some form, with New Jersey being the latest state preparing to launch its direct online lottery sales in the fall of 2024.[2]

While the appearance and gameplay of state-offered interactive lottery products may closely resemble casino-style games, lottery products are typically entitled to more protections under state law, since lotteries are a creature of the public sector.

This difference in legal treatment begs the question: Is an online turf war brewing between state lotteries and the private-sector casino industry?

## Lottery Versus Casino Gambling Under State Laws

At their core, both lottery games and casino games constitute gambling, as both types of games contain three key elements: payment, otherwise known as consideration; chance; and prize.[3][4]

State-sanctioned lottery and casino gambling products have coexisted for hundreds of years, dating back to at least the 1560s in England, where the first recorded official lottery was chartered by Queen Elizabeth I.[5]

Despite both being games of chance or gambling products, state lotteries have been legalized in 45 states plus the District of Columbia, whereas only 25 states currently offer commercial casino gaming.

Private-sector interactive and mobile casino gaming has been legally authorized in only six states to date: New Jersey, Pennsylvania, Nevada, Michigan, West Virginia and Delaware.

Why are lotteries legally authorized in the vast majority of states, whereas commercial casinos and online casino gaming are not? Primarily because of the manner in which state lottery laws are written vis-à-vis private-sector gambling laws.

While federal laws typically proscribe or criminalize certain interstate gambling activities, 10th Amendment jurisprudence coupled with state laws give the states expansive authority and jurisdiction to legalize and regulate gambling and lottery activities conducted on an

intrastate basis.

Under each state's enabling legislation, lotteries are operated and conducted by an instrumentality or body of state government, and the profits of lotteries inure to state beneficiaries such as public schools, public transportation systems and the state's general fund.

Thus, state lottery laws typically consist of a broad mandate and are generally permissive, giving the state lottery wide discretion to determine the means and manner in which intrastate lottery games may be conducted.

For example, the New Jersey Constitution expressly authorized the New Jersey Legislature to establish a state lottery so long as the "entire net proceeds of any such lottery shall be for State institutions and State aid for education."<sup>[6]</sup> The state Legislature enacted a statutory scheme creating a Division of Lottery within the Department of Treasury, as well as a State Lottery Commission.<sup>[7]</sup>

The Legislature also adopted statutory provisions setting forth the regulatory duties and powers of both the director of the Division of Lottery and the State Lottery Commission, enabling them to, among other things: authorize the type(s) of lottery to be conducted, determine the method to be used in selling tickets or shares, license agents to sell tickets or shares, and determine the number and sizes of prizes on the winning tickets or shares.<sup>[8]</sup>

By contrast, state gambling laws typically consist of a blanket constitutional prohibition on all types of private gambling, with narrowly tailored exceptions.

As a result, private casino and online gaming enterprises are required to be licensed by state gambling regulatory authorities, and operate subject to strict oversight by those authorities.

Using New Jersey as the same example, the state constitution expressly prohibits private-sector gambling unless authorized by a majority of voters via a statewide referendum.

The only for-profit gambling exceptions currently authorized in the state constitution are: wagering on running and harness horse races conducted at racetracks located within or outside of the state, and gambling at casinos located within the territorial boundaries of Atlantic City.<sup>[9]</sup>

Indeed, when the New Jersey Legislature legally authorized internet casino gambling on an intrastate basis, a statutory provision was included requiring all "facilities, equipment and personnel ... directly engaged in the conduct of Internet gaming activity, shall be located [...] within the territorial limits of Atlantic City, New Jersey," so as to not run afoul of the constitutional exception providing that casino gambling may only take place within the boundaries of Atlantic City.<sup>[10]</sup>

Both land-based and online casino operators must undergo a protracted licensing process that includes remitting substantial licensing fees — totaling hundreds of thousands of dollars — and filing invasive personal and business-level disclosures with state gambling regulators before being permitted to operate in New Jersey.

Enabled by this disparate legislative treatment, state lotteries generally have more latitude to establish a wider array of intrastate gambling products than gambling enterprises that operate in the private sector.

Recognizing that most Americans today own a mobile phone and use it to access the internet on a daily basis to engage in a variety of activities, including e-commerce purchases and gambling, a handful of state lotteries have begun to offer interactive lottery games that are played via the internet, in addition to traditional paper tickets.

These iLottery products are often similar to private-sector internet casino gambling products in terms of appearance and gameplay features. As a result, a battle for market supremacy has begun in those states that have legally authorized both internet casino gambling and iLottery.

As detailed below, this battle has already spilled over into the courts in Pennsylvania.

### **Case Study: Greenwood Gaming v. Pennsylvania**

On Aug. 22, 2018, seven casinos filed an action, Greenwood Gaming and Entertainment Inc. v. Commonwealth of Pennsylvania, in the Pennsylvania Supreme Court.

The action sought declaratory and injunctive relief to prohibit the Pennsylvania Lottery from "offering iLottery games that contain certain features, such as reveal all, auto play, bonus games, adjustable bets, and unlimited play/non-depleting prize pools," all of which "customers associate with slot machines." [11]

During discovery, and in June 2019, the casinos filed an application for a preliminary injunction, seeking to enjoin the lottery from offering iLottery games that were "uniquely characteristic of slot machines." Following a two-day preliminary hearing, the court denied the casinos' application, concluding they failed to meet their heavy burden of proof.

Central to the court's analysis in Greenwood were two provisions of the Pennsylvania Lottery Law. Section 303(a.1) of the Pennsylvania Lottery Law forbids the secretary of revenue and, in turn, the Pennsylvania Lottery, from allowing "any Internet-based or monitor-based interactive lottery game or simulated casino-style lottery game, including ... slot machines." [12]

Section 502 defines iLottery games as "Internet instant games and other lottery products offered through iLottery ... [excluding] 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." [13]

The court observed that the crux of the case boiled down to two questions: "(1) whether the legislature intended iLottery games to merely be online versions of instant tickets ... and (2) what the legislature intended to authorize and prohibit when it described the prohibition as relating to the simulation of 'casino-style' games." [14]

Finding that a plain reading of the statutory provisions at issue provides that the Pennsylvania Legislature did not intend to limit iLottery games to that of online instant tickets, the court analyzed whether the following game features are unique to slot machines: reveal all; autoplay; bonus games; adjustable bet; unlimited plays and nondepleting prize pools; and other features, e.g., a random number generator and return-to-player.

The court ultimately held in May 2021 that:

the features of the iLottery games challenged by [the casinos] are not signature, iconic, or key features particular to casino slot machines. Rather, they are features that; related to technological advances in online gaming; are based on online entertainment and gaming, as well as existing entertainment sources like television and board games, which have indisputably inspired both iLottery game and slot machines game designers; or existed in the same or similar fashion in traditional lottery products that were translated into a new online medium.[15]

The court in Greenwood further held that:

It cannot have been the intent of the legislation for [Sections 303(a.1) and 502] to be read to preclude either one of these newly authorized online games, iLottery or interactive gaming, from taking advantage of technological advances, changes in gaming and entertainment, or features that are found in existing popular entertainment.[16]

As a result, the Pennsylvania Lottery may continue to offer its iLottery products, pending a likely appeal by the casino-plaintiffs.

## **Conclusion**

The Greenwood case in Pennsylvania is likely a harbinger of similar cases to come in other states that legally authorize both iLottery products and private-sector interactive casino gaming.

iLottery products will continue to evolve as more state lotteries enter the online market. In many cases, the courts will ultimately decide how closely new and emerging iLottery products may resemble private-sector online casino gambling products.

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[1] See "State of the States 2023, The AGA Analysis of the Commercial Casino Industry" at 14, URL: <https://www.americangaming.org/wp-content/uploads/2023/05/AGA-State-of-the-States-2023.pdf>.

[2] Id. At 13-14. See also <https://www.nj.com/lottery/2023/08/nj-lottery-plans-to-sell-tickets-online-direct-to-players.html#:~:text=While%20lottery%20tickets%20can%20already,2024%2C%20a%20spokeswoman%20said%20Thursday>.

[3] See *Soto v. Sky Union, LLC*, 159 F. Supp. 3d 871, 878 (N.D. Ill. 2016) (citing *People ex rel. Green v. Grewal*, 61 Cal.4th 544, 564, 189 Cal.Rptr.3d 686, 699, 352 P.3d 275, 286 (2015) (quoting *Trinkle v. Stroh*, 60 Cal.App.4th 771, 782, 70 Cal.Rptr.2d 661, 667 (1997)

(Trinkle 1)). First, the machine or device must be activated by "the insertion of money or [some] other object." *Trinkle v. Cal. State Lottery*, 105 Cal.App.4th 1401, 1410, 129 Cal.Rptr.2d 904, 910 (2003) (Trinkle 2). Second, "the operation of the machine [must be] unpredictable and governed by chance." *Id.* Third, "by reason of the chance operation of the machine, the user may become entitled to receive a thing of value." *Id.*

[4] See also *FCC v. American Broadcasting Co., Inc.*, 347 U.S. 284, 290 (1954) ("All the parties agree that there are three essential elements of a "lottery, gift enterprise, or similar scheme": (1) the distribution of prizes; (2) according to chance; (3) for a consideration.") (citing *Stone v. Mississippi*, 101 U.S. 814 (1879) (a typical "lottery" is a scheme in which tickets are sold and prizes are awarded among the ticket holders by lot)).

[5] See John Ashton, *A History of English Lotteries* (1893).

[6] See N.J. Const., Art. IV, Sec. 7, Par. 2., Subpar. C.

[7] See N.J.S.A. 5:9-1 to -7.

[8] See N.J.S.A. 5:9-7 and 5:9-8.

[9] See N.J. Const., Art. IV, Sec. 7, Par. 2., Subpar. D through F.

[10] See N.J.S.A. 5:12-95.22.

[11] *Greenwood Gaming and Entertainment, Inc. v. Commonwealth of Pennsylvania, Department of Revenue*, Pa. Cmwlth No. 571 M.D. 2018 (Filed May 25, 2021), slip op. at 3.

[12] 72 P.S. § 3761.303(a.1).

[13] 4 Pa. C.S. § 502.

[14] *Greenwood Gaming and Entertainment, Inc. v. Commonwealth of Pennsylvania, Department of Revenue*, Pa. Cmwlth No. 571 M.D. 2018 (May 25, 2021), slip op. at 29.

[15] *Id.* at 44-45.

[16] *Id.* at 45.