

Camelot UK Lotteries Limited

**Response to the Department for Digital,
Culture, Media & Sport Consultation on
Society Lottery Reform**

7th September 2018

Table of contents

Section	Page
1. Executive summary	3
2. Introduction	9
3. Analysis of the available evidence	12
4. An efficient lottery ecosystem	19
5. 'Synthetic' national lotteries	22
6. The impact of 'synthetic' national lotteries on The National Lottery	24
7. Impact on the National Lottery Licence	34
8. Camelot's recommendations	35
9. Conclusion	36
10. Appendix <i>Gambling Compliance, Competition Authorities Approve De Lotto- Staatsloterij Merger, 11 December 2015</i>	37

1. Executive Summary

Introduction

The Department for Digital, Culture, Media & Sport (DCMS) has invited responses to a consultation on Society Lottery Reform. The Government proposes to amend the regulations for large society lotteries as follows (DCMS preferred options):

- Individual per draw sales limits – raise the limit from £4 million to £5 million;
- Individual per draw prize limit – raise the limit from £400,000 to £500,000;
- Annual sales limits – raise the limit from £10 million to £100 million.

This submission, by Camelot – acting in its role as the current operator of The National Lottery – serves to set out a clear position against the changes proposed by Government and, as an absolute minimum, maintaining the limits as they currently stand.

Based on Camelot's 24 years' experience of operating The National Lottery in the UK, and drawing on its knowledge gained through its work in international markets, this paper will demonstrate that there is a real risk that the proposals will fail to deliver the Government's desired outcome – to *“achieve a balance between enabling the sustainable growth of society lotteries on the one hand while also protecting the unique position of the UK-wide National Lottery under the National Lottery etc. Act 1993”*.¹

Our submission is divided into three sections, each with a distinct theme:

- that the evidence on which the proposals are based is insufficient to conclude with reasonable certainty that there will be no damage to National Lottery returns to society²;
- that the current lotteries ecosystem is inefficient, does not maximise National Lottery returns to society and the changes proposed would exacerbate this inefficiency;
- and that the proposals would move significantly away from the basis upon which the third Licence to operate was awarded and they are potentially damaging to the competition for the fourth Licence, which we understand is due to commence in the coming months.

Insufficient evidence

The preferred options proposed by DCMS are based on the belief that there is no evidence of a negative impact on The National Lottery from the growth of 'synthetic' national lotteries³. This unfounded expectation of positive outcomes has been reached by Government without having completed a comprehensive impact study and full Impact Assessment, placing the £2.4 billion annual returns to society from The National Lottery at great risk. Further, we would also

¹ DCMS Consultation on Society Lottery Reform, ministerial foreword, p2 (29 June 2018)

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/720930/society_lotteries_consultation_june_2018_pdf.pdf

² Returns to Good Causes and Lottery Duty

³ By 'synthetic' national lotteries, we mean society lotteries which operate on an industrial scale, are marketed under an 'umbrella' brand and compete at a national level with The National Lottery

question whether this approach is consistent with both the Secretary of State's and the Gambling Commission's statutory duty to do their "*best to secure that the net proceeds of the National Lottery are as great as possible*".

Our view is supported by an independent critique of the evidence undertaken by Frontier Economics ('Frontier'). Having reviewed the advice and supporting evidence provided to DCMS by the Gambling Commission⁴, Frontier found it to "*largely be based on assumption rather than hard evidence*". Frontier also suggests that some of the evidence is "*observational rather than econometric*", and that there are gaps in both the qualitative and quantitative analysis of the competitive relationship between The National Lottery and large-scale society lotteries in the UK, particularly the largest 'synthetic' national lotteries, for example in terms the direct material adverse impact created the marketing spend of 'synthetic' national lotteries.⁵

The advice put forward by the Gambling Commission is understandably and rightly caveated with the instruction to proceed with caution. However, we believe that the extent of the proposed changes, and particularly the ten-fold increase to the annual sales limit, is anything but cautious. It would be a risky strategy to place National Lottery Good Causes – which represent a substantial proportion of the DCMS budget and returns to HM Treasury through Lottery Duty⁶ – in further jeopardy without a full Impact Assessment. Frontier provides a number of recommendations as to how more detailed econometric analysis could be undertaken, as well as suggestions for supplementary evidence-gathering that would provide greater understanding of the lotteries ecosystem as it operates today. We urge DCMS and the Gambling Commission to pause and undertake additional analysis before proceeding with any of the proposals for large society lotteries set out in the consultation.

Beyond the limited nature of the evidence on which the Gambling Commission's policy advice is based, we also do not believe that there is any evidence that the current prize and proceeds limits are restricting growth of the society lotteries ecosystem. Indeed, the Gambling Commission's data⁷ on total proceeds from large society lotteries paints a picture of a sector in growth. In particular, the increased year-on-year sales recorded by the People's Postcode Lottery (845% over the past five years⁸) clearly highlights that the current limits are not restricting growth. Further, the data also indicates that there are very few occasions on which the current prize limits are reached, calling into question the suggestion that there is an urgent need for reform of those prize caps.

We also believe that the international evidence available has not been given due consideration throughout this process. Evidence from the Netherlands clearly shows significant harm to national lotteries from large scale society/charity lotteries – namely the Novamedia-operated

⁴ <http://www.gamblingcommission.gov.uk/PDF/consultations/Society-lottery-advice-provided-to-DCMS-002.pdf>

⁵ Frontier Economics 'Review of Gambling Commission Evidence: A note for Camelot' August 2018

⁶ 12% of total National Lottery sales

⁷ Gambling Commission Industry Statistics – May 2018, large society lotteries

⁸ Novamedia annual reports 2010 – 2017

charity lotteries⁹. In 2015, the two state-owned lotteries in the Netherlands merged in direct response to declining sales and returns to good causes resulting from an increasingly competitive charity lotteries market.

The factors set out above have led to a fundamental difference in our position to that of the Government, despite the fact that our goal, to maximise returns to society in a socially responsible way, is shared. Given the risk of potentially irreversible harm to a well-established and much-needed source of Good Cause funding, we urge that Government gathers better evidence and more granular data, undertakes a full Impact Assessment, considers international precedent, and clarifies the lotteries ecosystem to coincide with the start of the fourth National Lottery Licence competition.

Driving inefficiency at the cost of National Lottery returns to society

Returning to the objectives set out by DCMS, including to ensure “...*both society lotteries and the National Lottery are able to thrive*”, our analysis is unequivocal: the proposals put forward will neither help traditional society lotteries nor The National Lottery. In fact, we believe the opposite will happen.

Camelot has consistently supported – and continues to support – the vital work of traditional society lotteries. These lotteries operate with a clear distinction from The National Lottery, recognising differing motivations to play and offering a very different proposition to players. As acknowledged in the DCMS consultation document, “*for many societies, the good cause, rather than the prize, is the primary motivating factor for playing.*” Of these society lotteries, none utilises the current cap on jackpots and therefore would receive no benefit from the proposed prize increase – this is because players are motivated to play these society lotteries by the act of giving.

The National Lottery, in contrast, has a unique proposition in offering life-changing jackpots which serve as a powerful motivation to play. This distinction has been clear since the launch of The National Lottery and, in its purest form, serves both Good Causes and wider returns to society well. The proposed changes place the unique status of The National Lottery at risk, and blur this distinction at a significant cost while predominantly serving only one ‘synthetic’ national lottery, the People’s Postcode Lottery. The proposed changes also enable direct competition with The National Lottery and legitimise the scale of ‘synthetic’ national lotteries.

The People’s Postcode Lottery has created a ‘synthetic’ national lottery by grouping together many society lotteries under one brand. It utilises society lottery legislation in a way that was not intended by Parliament and, having achieved growth of 845% over the past five years, the People’s Postcode Lottery has established itself as a rival to The National Lottery by acquiring millions of customers and operating at national scale. As it has grown, it has become the only society lottery to offer jackpots which approach the £400,000 cap. It has also moved its proposition away from that of traditional society lotteries which promote the opportunity to give

⁹ Novamedia is the founder and (intellectual property) owner of the formats of the Dutch Postcode Lottery, the BankGiro Lottery and the FriendsLottery, and of the Postcode Lotteries in Sweden, Germany and Great Britain.

to good causes through play. Instead, its marketing is now directed squarely at the opportunity to win life-changing prizes.

Not only does this marketing shift the motivation of playing society lotteries towards winning prizes rather than giving to good causes, it also has a direct impact on The National Lottery's share of voice¹⁰. The result is to establish a marketing 'arms race' in which The National Lottery is forced to compete for share of voice in a market designed around the economically-efficient model of a 'single National Lottery operator', inflating its marketing costs and driving a cycle of inefficiency at the expense of National Lottery returns to society.

In 2010, The National Lottery represented 85% of all lottery advertising. By 2017, this share had been eroded to 44%, almost entirely due to the large-scale marketing campaigns undertaken by 'synthetic' national lotteries. The latest industry data highlights that the People's Postcode Lottery (with sales of £306 million in 2017) is now outspending The National Lottery (with sales of £6.951 billion in 2017/18) on marketing investment and has done so consistently over the period March to June 2018.

This is possible because, since the Gambling Act 2005 – when a cap on expenses at 15% for large society lotteries was removed - 'synthetic' national lotteries have been free to spend unlimited amounts of lottery revenue on overheads, including marketing. By comparison, The National Lottery retains only 5% of turnover for operating costs, including marketing (at 1.07%), and returns to its shareholder (at around 1%). This disparity in expenses distorts the lotteries ecosystem, preventing it from operating in the way in which it was designed to function and resulting in what we believe to be suboptimal returns to society.

The proposed changes would serve to exacerbate this cycle, putting National Lottery returns to society at substantial risk. A solution that would break this cycle and ensure that the lotteries ecosystem continues to operate as originally intended by Parliament would be to reinstate the cap on expenses, but at a level that recognises the scale at which 'synthetic' national lotteries now operate (e.g. between 5% and 10%).

In terms of the proposal to increase jackpots, the evidence that large jackpots drive sales is incontrovertible and it is our contention that this is a *de facto* case against the proposed increase to £500,000. Any party which disputes this fact is doing so in the face of clear evidence to the contrary – a position they are free to hold, but they cannot logically do so while maintaining that there is value in increasing the current cap. Simply put: either bigger jackpots do not drive sales, in which case there is no need for change. Or they do, in which case changes should not be introduced as they risk further cannibalising sales of National Lottery products which represent the most efficient means of generating returns to society.

In this context, it is especially important to note that a change to the top prize as recommended in the proposals would create direct competition with The National Lottery's Thunderball game, which also offers a £500,000 top prize. This game alone generated returns to society of £124 million last year, a sum greater than the total proceeds raised by the People's Postcode Lottery in 2017, and delivered in a more efficient way. Direct competition for consumer spend in this game category, supported by heavy marketing investment by 'synthetic' national lotteries will

¹⁰ A measure used to determine how big a share of advertising is compared to all other competitors

have a predictably adverse impact on The National Lottery's ability to generate returns to society.

Our evidence shows that, contrary to the Gambling Commission's view that there is no evidence of impact, competition *has* had a negative impact on National Lottery sales compared to what they otherwise would have been. Frontier Economics estimate that National Lottery sales have been cannibalised by £703 million as a result of competition over the period 2011 to 2017, leading to a reduction of National Lottery returns to society of £266 million over the same period. Further, the evidence suggests there will be a stepped increase if the prize and sales limits are raised.

The proposed reforms could have a severe and irreversible negative impact on The National Lottery model and Licence to operate, now and in the future

The proposed changes present a wider challenge to policy-makers, beyond exacerbating the existing damage to National Lottery returns to society. If implemented, the proposals would move significantly away from the basis upon which the third Licence to operate was awarded. The third Licence competition was run – and won by Camelot – on the basis that there is clear separation between The National Lottery and society lotteries.

Looking ahead, there is a significant risk that the proposed changes could weaken the forthcoming fourth Licence competition process. Without clarity around the future regulation of the lotteries ecosystem and with the full impact of these proposed reforms unclear in the near and long term based on the evidence provided, there are a number of potentially undesirable outcomes. These include increased complexity, and bidders raising prices to adjust for competitive market uncertainty, with the potential for this to result in a reduction in overall returns to society in the long term.

No changes to the prize or sales limits

In conclusion, we do not believe that the proposed changes to the draw, prize and annual sales limits will deliver the Government's stated aim of achieving "*a balance between enabling the sustainable growth of society lotteries on the one hand while also protecting the unique position of the UK-wide National Lottery*". These limits are the very measures which separate The National Lottery from traditional society lotteries and preserve the balance outlined above.

The evidence we set out in this response clearly demonstrates that there has already been a negative competitive impact from the 'synthetic' national lotteries on The National Lottery. This would therefore point to a reduction in the prize and proceeds limits as a solution. However, we recognise that Government is in a difficult position and needs to balance the needs of various stakeholders. To that end, while a reduction in the top prize would help to reduce future damage to The National Lottery, it would have a corresponding effect on the individual draw limits which might inadvertently put traditional society lotteries at a disadvantage, particularly those charities that operate on a national scale such as Macmillan Cancer Support.

As a minimum, we believe that the status quo must be maintained, in order to limit further damage to The National Lottery while complete evidence is gathered and a comprehensive Impact Assessment is undertaken. At this stage, Camelot is committed to participate fully in

a consultation which considered more 'surgical' reforms which could include legislation that decouples the prize and proceeds limits. This would reduce the competition from 'synthetic' national lotteries around the top prize and help to ensure the future health of The National Lottery and the 'single national lottery' model, and would also enable traditional society lotteries to thrive, with the focus clearly on the cause and not the top prize.

We would therefore urge Government to undertake a thorough assessment of the lotteries ecosystem, with consideration of the points raised above, before making any changes to the prize and proceeds limits. Further, we propose that a cap on expenses be introduced for 'synthetic' national lotteries at a level that recognises the scale at which those lotteries now operate (i.e. between 5% and 10%).

2. Introduction

Maximising returns to good causes must be at the very heart of any discussion about lotteries. This was a fundamental principle when The National Lottery was launched in 1994 and it remains true today. In total, The National Lottery has to date raised over £38 billion for Good Causes – which is far in excess of the original top-end Government forecast of £1 billion per year for Good Causes – and paid over £15.7 billion to the Exchequer in Lottery Duty. This has been achieved as a result of the very deliberate establishment of a highly-regulated single national lottery, and a clear distinction between The National Lottery and traditional society lotteries which has allowed both to co-exist in a complementary lottery ecosystem, thereby maximising returns for good causes and society.

It is our strong belief that the best model to achieve the maximum benefit for society remains the ‘one national lottery’ system – alongside smaller-scale, traditional society lotteries which raise vital funds for good causes in a way that is complementary to The National Lottery.

Camelot is therefore very concerned by the proposals to increase the limits on prize and proceeds for society lotteries. We would contend that the Gambling Commission’s policy advice is not supported by adequate economic evidence, and requires a full detailed Impact Assessment. The Government proposes to amend the regulations for large society lotteries as follows (preferred options):

- Individual per draw sales limits – raise the limit from £4 million to £5 million;
- Individual per draw prize limit – raise the limit from £400,000 to £500,000;
- Annual sales limits – raise the limit from £10 million to £100 million.

We do not believe that the proposed changes to the prize and proceeds limits will deliver the Government’s stated aim of achieving “*a balance between enabling the sustainable growth of society lotteries on the one hand while also protecting the unique position of the UK-wide National Lottery*”¹¹ and urge that, as an absolute minimum, the status quo be maintained to prevent exacerbating future damage to The National Lottery. These limits are the very measures which separate The National Lottery from society lotteries and preserve the balance outlined above. We also discuss in section 8 the potential to decouple the top prize and draw limit.

While we are very supportive of traditional society lotteries and the important work they do, we urge that Government undertake an updated, thorough assessment of the lotteries ecosystem – and the impact on The National Lottery – before making any changes to the prize and proceeds limits.

Our submission is divided into three sections, each with a distinct theme:

- that the evidence on which the proposals are based is insufficient to conclude with reasonable certainty that there will be no damage to National Lottery returns to society;
- that the current ecosystem is inefficient, does not maximise National Lottery returns to society and the changes proposed would exacerbate this inefficiency;

¹¹ DCMS, Ministerial Foreword, Op Cit

- and that the proposals would move significantly away from the basis upon which the third Licence to operate was awarded and they are potentially damaging to the competition for the fourth Licence, which we understand is due to commence in the coming months.

About Camelot and The National Lottery

Camelot has been the licensed operator of The National Lottery since its introduction in 1994, and the current Licence runs until January 2023. It has 24 years' experience of responsibly operating a national asset and one of the most successful lotteries in the world.

Camelot's overarching objective is to maximise returns to National Lottery Good Causes through selling lottery products in an efficient and socially-responsible way. While Camelot is responsible for generating returns to Good Causes, it plays no role in the allocation of Good Cause funding. This is the specific responsibility of 12 lottery distribution bodies, each with specialist knowledge of their sectors.

The National Lottery – a national success

The National Lottery has been an undoubted success since it was launched in 1994.

- ***Returns to society:*** To date, National Lottery players have raised over £38 billion for Good Cause projects, with more than 535,000 individual awards made across the UK – an average of 190 lottery grants for every postcode district. This is far in excess of the original top-end Government forecast of £1 billion per year for Good Causes. In addition, The National Lottery has paid over £15.7 billion to the Exchequer in Lottery Duty.
- ***Corporate responsibility:*** Camelot is internationally recognised for selling lottery tickets in a socially-responsible way. The UK National Lottery is ranked just 65th in the world in terms of per capita spend, despite being the sixth largest lottery in the world in terms of sales.¹²
- ***Leading UK brand:*** The National Lottery crossed fingers logo is recognisable to 95% of the UK population. Based on 2017/18 sales, Lotto and EuroMillions were the two biggest FMCG brand in the country, while total National Lottery sales were bigger than Cadbury, Coca-Cola, Nestle, Walkers, Heinz, Warburtons, Muller, and Purina combined.¹³
- ***Efficiency:*** Due to the competitive process for awarding the licence and the effective oversight of the Gambling Commission, The National Lottery is the most cost-efficient major lottery in Europe, with around 5% (including c.1% profit) of total revenue spent on operating costs.

¹² La Fleur's World Lottery Almanac, 2018

¹³ Britain's Biggest Brands, The Grocer/Nielsen, March 2018

- **Reach:** Around 60% of adults play The National Lottery. Accounting for over 75% of sales, retail is the largest National Lottery sales channel. Camelot now works with around 45,000 retailers across the UK, with independent outlets making up the majority.

These achievements are, in part, a direct result of the very deliberate establishment of an efficient structure with a single operator, secured through the competitive licensing process and effective regulatory oversight, deemed by Parliament to be the most efficient and effective mechanism to maximise returns to Good Causes. This model has been undermined by the entry and substantial growth of 'synthetic' national lotteries, and we believe will be exacerbated further by the implementation of the proposed changes.

3. Analysis of the available evidence

The proposals set out in the consultation are supported by two accompanying documents, the Gambling Commission's advice note and the DCMS *De Minimis* Assessment. The Gambling Commission's advice, as referenced in the consultation document, found that *"to date the growth of the society lottery sector has not been at the detriment of National Lottery sales, and that a relatively small increase in the limits is unlikely to disrupt the current balance between the two sectors"*.¹⁴ The following section considers this evidence and provides a critique of its robustness. It also considers the wider question as to whether there is a compelling need for a change in the regulation and the international evidence.

Prior to examining the specifics, Camelot has a general concern as to the basis on which the reforms are proposed. Camelot's overall position is based on extensive evidence, while in contrast the advice provided by the Gambling Commission presents an absence of evidence. We believe that Government reforms should be proposed on the basis of evidence that demonstrates a reasonable expectation of positive results not on the basis an absence of evidence to the contrary. Without a clear case to show that the reforms will deliver a positive outcome for good causes and society, we believe that the status quo should be maintained. To do otherwise would be to put at risk vital funding on the basis on unfounded expectations.

The Gambling Commission advice – a critique

The proposals to increase the prize and proceeds limits for society lotteries are predicated on the assertion that there is little evidence of competition or harm between The National Lottery and large-scale society lotteries. In contrast, a report commissioned by Camelot in 2017 – shared with the Gambling Commission and DCMS – found that there was a negative impact of competition and that there was cannibalisation of National Lottery sales resulting from 'synthetic' society lotteries¹⁵.

In order to understand the discrepancy between the advice provided by the Gambling Commission and our previous findings, we commissioned Frontier Economics to review the Gambling Commission's advice. Frontier concluded the evidence contained in the Gambling Commission advice, relied upon by DCMS, to be relying more on assumption than hard evidence. A summary of Frontier's report is included below.

Summary of Frontier Economics 'Review of Gambling Commission Evidence: A note for Camelot', August 2018

Camelot commissioned Frontier Economics to review the Gambling Commission's formal advice to DCMS relating to legislative reform for the society lottery sector. The Gambling Commission's advice came in three parts after the 2014 Culture, Media and Sport Select Committee inquiry into society lotteries, with phase 1 being delivered to DCMS in October 2015, phase 2 in January 2016 and updated advice being delivered in October 2017.

¹⁴ DCMS Consultation, Ministerial Foreword, Op Cit

¹⁵ Frontier Report: "The Impact of Competition on The National Lottery", June 2017

Frontier focused on those areas of the Gambling Commission's advice that most closely related to the issues around competition between The National Lottery and 'synthetic' national lotteries. They provided views on the advice around the nature of competition between The National Lottery and 'synthetic' national lotteries; the different competitive pressures exerted on The National Lottery by these lotteries; 'synthetic' national lotteries' reliance on advertising; the rapid growth of these lotteries, and the size of the proposed increases in society lottery limits.

In summary, Frontier found that the Gambling Commission's underlying conclusion – that, at current prize levels, 'synthetic' national lotteries do not compete with The National Lottery – appears to be largely based on assumption rather than evidence. In particular, the Gambling Commission asserts that, because the payout and jackpot structures of The National Lottery and 'synthetic' national lotteries are different, they attract different consumers and therefore do not compete. While it is true that many people play The National Lottery to win life-changing jackpots, there are other important drivers of play and it is certainly not inconceivable that, in the eyes of many players, The National Lottery and 'synthetic' national lotteries would be substitutable. Frontier explains that the Gambling Commission's conclusion is supported by quantitative evidence from empirical and econometric analysis which found no significant evidence that society lottery sales are negatively correlated with National Lottery sales. However, some of this evidence (for the impact of the Health Lottery's entry into the sector) was observational rather than econometric, providing no counterfactual 'no entry' scenario.

Rigorous econometric studies by Frontier Economics have found negative effects on National Lottery sales from the Health Lottery's entry to the market, and from competitor advertising. This is also consistent with academic evidence, not referenced by the Gambling Commission, that competing lottery products offered by different operators are substitutes.

The Gambling Commission notes qualitative differences between the Health Lottery and People's Postcode Lottery compared with other society lotteries, in particular in terms of scale, reach and reliance on advertising. However, Frontier says that the advice does not fully explore the potential for competitive impacts to differ between these 'synthetic' national lotteries and other society lotteries, seeming to imply that they are comparable to other, smaller, society lotteries in terms of competitive impact on The National Lottery.

For example, there is recognition in the Gambling Commission's advice of the 'synthetic' national lotteries' heavy reliance on advertising but little attention is paid to this in terms of the implications for The National Lottery even though Frontier Economics (2017; 2018) found robust evidence that competitor advertising (the Health Lottery, People's Postcode Lottery and Lottoland) is negatively correlated with National Lottery sales, even controlling for other sales drivers.

Frontier also contends that the advice understates the potential for growth of these largest 'synthetic' national lotteries. Further, the advice regularly implies that because society lottery sales are small relative to the size of The National Lottery, the impact of society lotteries must be small. However, in terms of protecting returns to Good Causes and wider society, what matters is the degree of cannibalisation and the relative returns to society. Gambling Commission data shows that the society lottery market is growing strongly. In 2008/9, National

Lottery sales were 30 times bigger than ‘synthetic’ national lotteries’ sales. By 2016/17, they were just 12 times bigger.

Moreover, the advice then remarks that the largest ‘synthetic’ national lotteries may have reached ‘saturation point’ by 2014/15, looking at the share of large society lottery proceeds coming from ELM¹⁶-managed lotteries. This neglects more recent data and the growing dominance of People’s Postcode Lottery in this share of the proceeds.

The Gambling Commission’s conclusion that DCMS may wish to “*consider introducing measures which look to limit the risk of new schemes emerging in the future, rather than limiting the existing schemes already in operation*”¹⁷, seems to be contradictory unless they consider competition to be harmful. This would simply protect the ‘synthetic’ national lotteries from future competition, while implicitly acknowledging that there must be the potential for harm.

Finally, Frontier is critical of the fact that, given the established and accepted view that there should only be a single national lottery operator, there is a surprising lack of analyses of the competitive relationship between The National Lottery and society lotteries in the UK, particularly from the largest ‘synthetic’ national lotteries. Other than econometric analysis by Frontier Economics and NERA which reach different conclusions, there appears to be no other quantitative or qualitative evidence focused on this issue. Frontier believes there is a need to fill this gap and that there should be joint interest on the part of the Gambling Commission, DCMS, Camelot and potential bidders for the fourth National Lottery licence to better understand the competitive landscape ahead of the fourth licence competition. As part of this, a full review of the scale and nature of competitor advertising is advised.

¹⁶ External Lottery Manager

¹⁷ <https://www.gamblingcommission.gov.uk/PDF/consultations/Society-lottery-advice-provided-to-DCMS-002.pdf> section 10.5

Growth of the society lotteries market under the current limits

Beyond the shortcomings of the evidence as set out above, we also do not believe that there is any evidence that the current prize and proceeds limits are currently restricting growth of the society lotteries market.

Gambling Commission data highlights that total proceeds from large society lotteries have tripled over the period from 2008/9 to 2016/7 and that this growth is predominantly being driven by ‘synthetic’ national lotteries and ELMs, as demonstrated in the table below¹⁸.

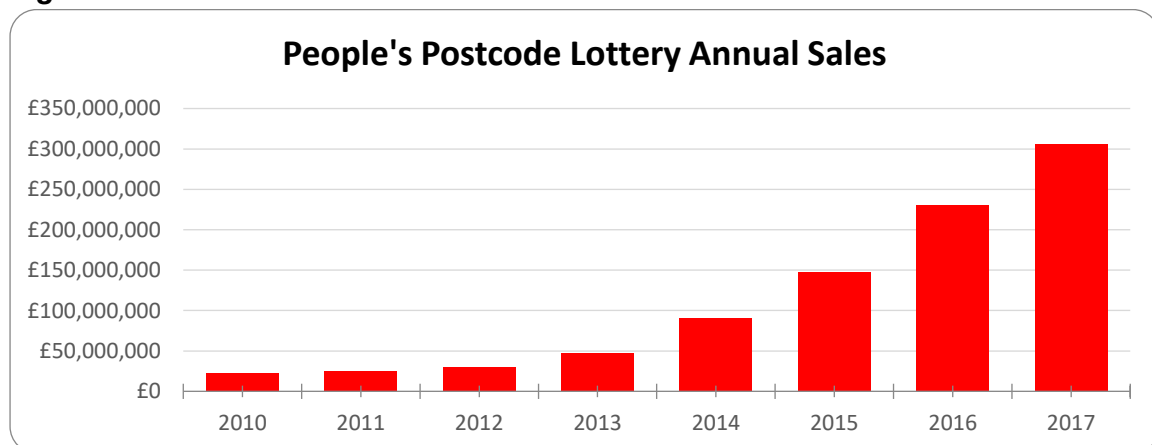
Figure 1

Year	08/09	09/10	10/11	11/12	12/13	13/14	14/15	15/16	16/17
Proceeds (£m)	178.68	194.91	208.16	300.96	345.56	376.82	446.13	493.13	586.66
% change	n/a	+9%	+7%	+45%	+15%	+9%	+18%	+11%	+19%
From ELMs	+20%	+29%	+43%	+61%	+64%	+70%	+69%	+77%	+61%

This growth was recognised by Sue Owen, DCMS Permanent Secretary, in oral evidence to the Public Accounts Committee in January 2018. She also considered the impact that this could have on The National Lottery, telling the Committee that “*the [society lotteries] sector has grown a lot — 10% or 11% annual growth rate — over the past 10 years, and if that continued it could get to a scale where it starts to impinge on the national lottery. We do not know about how saturated the market could get.*”¹⁹

It is important to understand where this growth has come from, but the significant growth of People’s Postcode Lottery of around 845%²⁰ over the past five years appears to be driving the vast majority of growth within the society lotteries market as a whole. This growth is set out in the graph below:

Figure 2:



¹⁸ Large Society Lottery Proceeds data, Gambling Commission Industry Statistics, November 2017

¹⁹ <http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/public-accounts-committee/decline-in-national-lottery-income/oral/77503.html> Q70

²⁰ Novamedia annual reports 2010 – 2017

This growth also challenges the contention in the DCMS *De Minimis* Assessment that the ‘Do nothing’ scenario would hamper society lottery growth:

“Option 0: Do nothing: *No change to sales or prize limits for society lotteries. This would continue to protect the unique space in which The National Lottery operates, but would not allow society lotteries room to grow nor generate greater returns to good causes*”.²¹

The growth of the People’s Postcode Lottery clearly highlights that this rationale is flawed. The assumption that ‘do nothing’ does not allow ‘*society lotteries to grow nor generate greater returns to good causes*’ is at odds with the way in which the society lotteries market has grown over the past five years (see figure 1 and 2 above). However, it does raise questions about where this growth has come from. We will demonstrate below in section 6 that we believe some of the growth is cannibalised from National Lottery sales.

We also note the comment by Mintel in its report of January 2018 that “*the level of growth recorded by the People’s Postcode Lottery suggests that other society lotteries may actually be experiencing sales decline*”.²²

As well as undertaking further investigation into the potential impact on The National Lottery, we would suggest there is a case for assessing the impact of the proposed changes on the wider charity lottery market and particularly the smaller society lotteries, which may see a negative impact from the increased prize and proceeds limits.

Evidence to support the top prize increase?

With regard to the specific proposal to increase the top prize for society lotteries from £400,000 to £500,000, we would again question the evidence to support this move. The Gambling Commission data included in its advice to DCMS highlights that for the last six years of available data there were only 11 occasions when a society lottery has operated within 20% of the draw proceeds limit, with no occasions in 2016/17²³ – the last year for which data was published.

Furthermore, analysis of the largest single prize offered by society lotteries highlights that only the People’s Postcode Lottery comes close to the current £400,000 limit. The Health Lottery has to date only offered a prize of up to £100,000, although we note it introduced a £250,000 monthly prize draw in September 2018.

This suggests that, of the current participants in the society lotteries market, those most likely to benefit from any increase in the top prize limit would be the People’s Postcode Lottery and the Health Lottery – not traditional, small-scale society lotteries. Given that the Health Lottery

²¹

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/720931/society_lottery_dma_pdf_final.pdf p2

²² Mintel UK Lotteries Market Report 2018

²³ <http://www.gamblingcommission.gov.uk/PDF/consultations/Society-lottery-advice-provided-to-DCMS-002.pdf> p9

has long argued for an increase in the top prize but offers a current jackpot well below the permitted limit, it can be hypothesised that it expects a very significant uplift in sales which would result from being able to offer a much larger jackpot.

We consider the wider potential impact of the proposed prize increase in further detail below.

International evidence

We also believe that the international evidence available has not been given due consideration throughout this process, and that the case study from the Netherlands should be noted²⁴:

International evidence – harm to national lotteries from large scale society lotteries

Evidence from the Netherlands clearly shows significant harm to national lotteries from large scale society/charity lotteries. In 2015, the merger of two state-owned lotteries in the Netherlands was in direct response to declining sales and returns to good causes resulting from an increasingly-competitive charities lotteries market – with the Postcode Lottery at the fore. According to an article in Gambling Compliance:

“As Postcode Lottery and other charity lotteries have mounted a marketing push, De Lotto and Staatsloterij’s [national lotteries] market share of the country’s lottery market has contracted.

De Lotto turnover declined 8.6 percent between 2010 and 2014 to €321.8m, while at Staatsloterij, turnover fell 12 percent in the same period to €737.8m.

In contrast, turnover at the country’s national charity lottery sector, which comprises Postcode Lottery, BankGiro Lottery and Friends Lottery, has been on an upward curve for a number of years with turnover in excess of €850m by the collective trio.”

Conclusion – a comprehensive impact study is required

As set out in the section above, we do not believe the evidence relied upon by Government is sufficiently rigorous. It is not sufficient to make recommendations based on the lack of evidence of damage to The National Lottery – and in the following section we refute the suggestion that there has been no damage – but there must be clear evidence that there *will not be damage* in the future. We do not believe the advice provided by the Gambling Commission, which itself urges caution, has satisfied this evidential burden.

In addition, it is not clear that a compelling case for change has been made, given that the People’s Postcode Lottery has grown by 845% over five years under the current regime. We also believe that there is merit in considering the impact of the growth of ‘synthetic’ national lotteries on traditional, small scale society lotteries.

²⁴ See Appendix 1 for full article

We would therefore urge DCMS and the Gambling Commission to undertake a thorough, updated assessment taking into account the points made in this section, before proceeding with any further action. This is a necessary next step in order to ensure that there is no reduction in the proceeds to society from the National Lottery, which exceed £2.4bn annually, nor that there is a detrimental impact on other participants in the society lotteries market.

To assist with the necessary further assessment, we highlight in the next section analysis we have undertaken which illustrates that the proposed changes are inefficient, and the subsequent impact of these changes on The National Lottery.

4. An efficient lottery ecosystem

The proposals put forward in the consultation are predicated on the assumption that they will “support the society lottery sector to maximise returns, whilst ensuring that any changes are not to the detriment of The National Lottery”.²⁵ It is our view – based on the available evidence – that this ambition will not be achieved by proceeding with the Government’s preferred options. In fact, the proposed changes carry a significant risk to any benefit that can possibly be expected to be achieved and are inefficient for maximising returns to Good Causes and society.

To understand why this is the case, it is important to revisit the economic rationale of the lotteries ecosystem in the UK.

The ‘single national lottery’ model

Going back to first principles, Parliament’s original intent was that there should be only one national lottery. The 1992 Home Office White Paper²⁶ which introduced the concept of a national lottery stated that “... *the best way forward would be to promote a single national lottery. This will have the advantage of:*

- *Ensuring large prizes which would capture wide public interest;*
- *Maximising the potential funds which could be raised for Good Causes;*
- *Minimising regulatory problems;*
- *Reducing the potential for fraud and criminal involvement; and*
- *Being less likely to encourage undesirable forms of advertising.”*

The White Paper also recognised that other lotteries (‘traditional society lotteries’) should continue to have a role in the lottery ecosystem, albeit on a smaller scale to The National Lottery, making a clear distinction between the two types of lottery. It recognised the differing purposes and motivations to play each type of lottery, with National Lottery players primarily driven by life-changing prizes and society lottery sales driven by good causes.

When presenting the White Paper to Parliament, the Government “concluded that a single national lottery is the best way forward. This would allow major prizes to be offered and it would maximise the potential funds which could be raised for good causes, while minimising the risk of fraud or mismanagement.”²⁷ A single national lottery under government licence, with efficiency delivered through the competition for the licence and effective regulatory oversight, was deemed the most efficient way to ensure consistent protection of players, the fitness and propriety of its operation, and the maximisation of returns to Good Causes and society.

²⁵

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/720930/society_lotteries_consultation_june_2018_pdf.pdf (page 5)

²⁶ ‘A National Lottery Raising Money for Good Causes’, 1992 Government White Paper

²⁷ https://api.parliament.uk/historic-hansard/commons/1992/mar/06/national-lottery#S6CV0205P0_19920306_HOC_33

This is reflected in the overriding statutory duties of both the Secretary of State for DCMS and the Gambling Commission. The Secretary of State and Gambling Commission must exercise their functions in the manner they consider most likely to secure that “*the National Lottery is run, and every lottery that forms part of it is promoted, with all due propriety, and that the interests of every participant in a lottery that forms part of the National Lottery are protected.*” Subject to this, they must do their “*best to secure that the net proceeds of the National Lottery are as great as possible.*”²⁸

The success of The National Lottery since 1994 is testament to the very deliberate establishment of a highly-regulated single national lottery, and a clear distinction between it and traditional society lotteries, which allows both to exist in a complementary lottery ecosystem, thereby maximising returns for good causes and society.

The economic case for whether Good Causes are best served by having a single national lottery provider has been revisited a number of times since The National Lottery was introduced. This includes reviews by the 2001 Gambling Review Body, the 2002 White Paper ‘A Safe Bet for Success – Modernising Britain’s Gambling Laws’ and the 2004 Culture, Media and Sport Select Committee Report, ‘Reform of the National Lottery’. All concluded that the single national lottery model should be maintained.

Nonetheless, the lotteries and gambling markets have evolved significantly since The National Lottery was introduced, particularly in the last decade. It is, therefore, worthwhile reviewing whether the single national lottery model remains the most efficient way to maximise returns to Good Causes and society. Camelot commissioned Frontier Economics (Frontier) in 2014 to look into this once again and its findings clearly support a single national lottery as the most efficient model to maximise returns to Good Causes.²⁹

Frontier Economics analysis

Frontier found nothing to alter the previous conclusions – outlined above – that returns to good causes are maximised by having one national lottery operator. Specifically, Frontier concluded³⁰:

- Multiple national lotteries lead to diseconomies of scale, as administrative and other costs are repeated across providers, reducing the revenues available for good causes.
- There is empirical evidence from a number of countries that larger jackpots attract more players. Most estimates suggest that a 10% increase in jackpot size is associated with an increase in demand of around 3% to 5%. By concentrating sales, a single lottery provider maximises the jackpots available to win and thus maximises the revenues available.

²⁸ https://www.legislation.gov.uk/ukpga/1993/39/pdfs/ukpga_19930039_en.pdf Part 1 Section 4 (1-2)

²⁹ <http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/culture-media-and-sport-committee/society-lotteries/written/13656.html>

³⁰ <http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/culture-media-and-sport-committee/society-lotteries/written/13656.html>

- National Lottery products are perceived to be substitutable, meaning that multiple operators are likely to ‘innovate’ by developing similar products and compete for market share, leading to significant cannibalisation of sales.

Further, uncertainty in the market could lead to operators being less willing to bid for future licences to run The National Lottery, or demanding increased margins to do so, which could reduce future returns to Good Causes.

Traditional society lotteries

Traditional society lotteries play an essential role in raising much-needed funds for good causes. As set out in the Gambling Act 2005, society lotteries can only be run for good causes, promoted for the benefit of a non-commercial society³¹. It is important to stress that Camelot is very supportive of traditional society lotteries and the important work that they do, as well as their role as a source of innovation in lotteries. As referenced in the Gambling Commission’s ‘Advice provided on society lotteries’, the vast majority of these are small in scale – but vital in contribution to society. They operate well within the limits as envisaged by the Gambling Act 2005 and are complementary to, not in competition with, The National Lottery.

In most cases traditional society lotteries are local and are operated to benefit a single cause. In the instance where society lotteries are larger in scale, they are distinct from The National Lottery in a number of ways: they are operated for a single cause; prizes are usually less than £30,000 and good cause returns are substantially higher than the statutory minimum of 20%; and their marketing is predominantly led by the cause, not the prize.

The ‘single national lottery’ model works

The National Lottery and traditional society lotteries have, by and large, successfully co-existed for over two decades. They are complementary to each other, and operate in separate and distinct markets. The figures show that both have grown steadily in recent years.

Funding raised by The National Lottery for Good Causes benefits a hugely diverse range of sectors. In total, 535,000 individual awards have been made over 24 years – an average of 190 lottery grants for each postcode district. Alongside the headline projects – including the Olympics and Paralympic games, Tate Modern, The Giant’s Causeway visitor centre and cliff top walk on the Antrim Coast, the Eden Project in Cornwall, the Kelpies in Falkirk, The Millennium Stadium in Cardiff and The Lowry in Manchester – it is important to note that 70% of funding awards are for less than £10,000. These are small scale local projects having a direct and life-changing impact on people across the UK every day.

These achievements can only be delivered by maintaining the distinctive features that make The National Lottery unique: its ability to reach every community in the UK, the wide range of sectors that it helps through its funding and its place in the national psyche as a trusted way to help Good Causes – and, of course, the chance to win a life-changing prize which has maintained player interest for over two decades.

³¹ <http://www.gamblingcommission.gov.uk/for-gambling-businesses/Compliance/Sector-specific-compliance/Lotteries/Society-lotteries.aspx>

5. 'Synthetic' national lotteries

When the 2005 Gambling Act was passed, the lotteries ecosystem consisted of the traditional lotteries as referenced above and The National Lottery. However, over time, the lotteries sector has evolved and a new category of 'umbrella' society lotteries has emerged. As these umbrella lotteries have grown in size, scale and reach, they have created a third tier of lottery: the 'synthetic' national lottery. These 'synthetic' national lotteries share a number of characteristics with The National Lottery:

- They are advertised and promoted nationally;
- They are marketed under a single umbrella brand; and
- The good cause funds raised are distributed on a national scale.

There are currently two major 'synthetic' national lotteries: the Health Lottery and the People's Postcode Lottery. Along with the Lotteries Council (the trade body for prize-led fundraising through lotteries and competitions), these two 'synthetic' national lotteries have been most vocal in terms of pushing for the Government to increase the society lottery limits. Both have grown in recent years, with the People's Postcode Lottery in particular recording rapid year-on-year growth. We would suggest these organisations – and their commercially operated external lottery managers – are significantly more likely to benefit from any increase in top prize or proceeds limit than the traditional society lottery sector. This will be discussed further below.

Legitimacy of 'synthetic' national lotteries

Before considering the impact on The National Lottery, it is first necessary to consider the way in which 'synthetic' national lotteries have blurred the intended boundaries of the lotteries ecosystem. The National Lottery etc. Act 1993 and Gambling Act 2005 foresaw a landscape comprising two distinct but complementary types of non-exempt lotteries, and the emergence of 'synthetic' national lotteries, exploiting a loophole designed to enable individual charities to raise money through running lotteries, has been identified as a cause for concern numerous times.

In 2012, when considering the emergence of the Health Lottery, the Gambling Commission said it was *"clearly designed to circumvent the proceeds limits – the gambling equivalent of a tax avoidance scheme that exploits loopholes in the legislation"* and stated that *"the Department needs to decide whether to block the loophole or allow the limits to be breached and accept the possible damage to The National Lottery."*³²

In evidence to the Culture, Media and Sport Committee in January 2012, Jenny Williams, then-Chief Executive of the Gambling Commission, commented that *"If you're saying that this [the Health Lottery] was a scheme designed to get around the lottery limits, yes, clearly it was."*³³

³² Source: Gambling Commission evidence to court in Camelot's application for judicial review of the decision to licence the Health Lottery

³³ <http://www.publications.parliament.uk/pa/cm201213/cmselect/cmcmds/421/120119.htm> (Question 753)

The Culture, Media and Sport Committee in its report *The Gambling Act 2005: A bet worth taking?* (July 2012) commented that “...*the Health Lottery appears to us to accord with neither the spirit nor the intention of Parliament as set out in the National Lottery Act 2006 and the Gambling Act 2005*”.³⁴

Notwithstanding the concerns expressed by the Gambling Commission regarding its operation, it was determined that the Health Lottery was capable of functioning within the boundaries of the current legislation and regulations. Further, while the High Court rejected Camelot’s request to judicially review the Gambling Commission’s licensing of the Health Lottery, the Court itself said quite explicitly that the operations and legality of multiple society lotteries are a matter for Government or Parliament to determine.

Camelot has voiced concerns on a number of occasions about the precedent that ‘synthetic’ national lotteries set, and the potential for other commercial operators could be encouraged to follow the Health Lottery or People’s Postcode models.

The Charity Law Association addressed this in its written evidence to the Culture, Media and Sport Select Committee inquiry into the society lottery sector. It suggested that the Health Lottery appears to be a model that “*could be misused by unscrupulous private bodies in the future as a method of developing income at the expense of charities and in a manner that could be unfair to the operator of The National Lottery*.”³⁵

In the years following these developments, the ‘synthetic’ national lotteries have continued to grow, and in the case of the People’s Postcode Lottery, they have thrived – in direct competition with The National Lottery. In oral evidence to the CMS Select Committee in November 2014, when asked whether the People’s Postcode Lottery is a competitor to The National Lottery, Jo Bucci (Managing Director) stated “*Are we competitors [to The National Lottery]? Of course we are*.”³⁶ This is a stark contrast to the more recent messaging from the People’s Postcode Lottery that it provides “*very much a complementary source of funding [to The National Lottery] particularly for charities*”.³⁷ In addition, the Health Lottery has continuously used its marketing to make direct comparisons with The National Lottery’s Lotto game.

³⁴ <http://www.publications.parliament.uk/pa/cm201213/cmselect/cmcmums/421/42107.htm#a37> (Para 229)

³⁵ <http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/culture-media-and-sport-committee/society-lotteries/written/13618.pdf> (page 4)

³⁶ <http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/culture-media-and-sport-committee/society-lotteries/oral/15640.html> (Question 29)

³⁷ <https://www.insider.co.uk/special-reports/clara-govier-peoples-postcode-lottery-12864289>

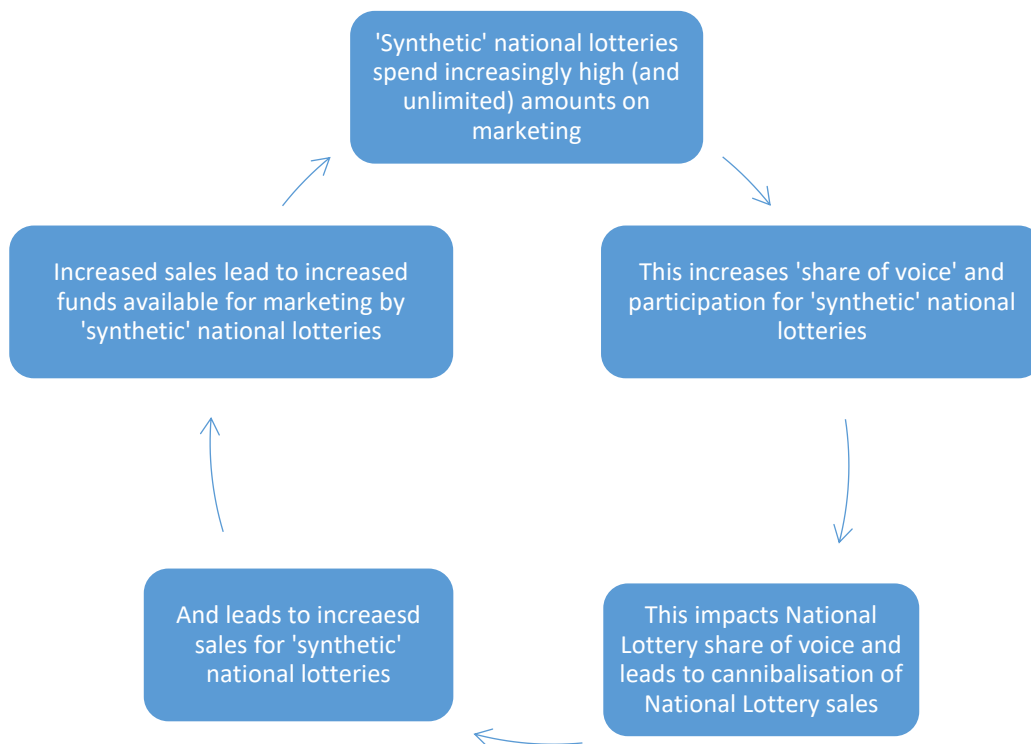
6. The impact of 'synthetic' national lotteries on The National Lottery

We believe that the impact of 'synthetic' national lotteries can be assessed in a number of ways. The assumption in the advice from the Gambling Commission is that “*there has not yet been a significant impact on the National Lottery from the [umbrella] schemes*”. As set out in section 3, we do not believe the evidence supports this – in fact, to the contrary, we believe the impact has been substantial. Further, we believe that it is necessary to look at what has driven that impact to date, and what could happen in the future. This begins with analysis of the way in which 'synthetic' national lotteries are marketed, and the levels of marketing spend – a useful proxy in assessing the impact on both sales and share of voice.

Marketing spend – driving inefficiencies in the lotteries ecosystem

Looking at the economics of the lotteries ecosystem, as there is no cap in place on the level of expenses³⁸ for society lotteries, the 'synthetic' national lotteries have invested heavily in marketing with a significant impact on The National Lottery. Marketing spend is a crucial consideration because this is where the cycle of inefficiency begins:

Figure 3:



³⁸ Society lottery expense must be 'reasonable'. However, as noted in the Gambling Commission's advice to DCMS: "Transparency regarding the fees paid by societies for the promotion and management of lotteries through umbrella brands is rooted in the 'reasonable expenses' test. The Act does not define what is deemed to be an expense 'reasonably incurred in organising the lottery' and what is deemed reasonable to one society may not be regarded as reasonable to another." We also note that there is no transparency for the public as to what "reasonable expenses" means in practice.

This can be demonstrated in real terms by looking at the marketing spend of the People's Postcode Lottery, which has seen its advertising spend increase significantly from £12.4 million in 2014 to £35.2 million in 2017 – an increase of 184%. This is possible as the People's Postcode Lottery continues to operate with very high levels of expenses. In 2017, expenses were £90.1 million compared to £93.4 million returned to beneficiaries in.

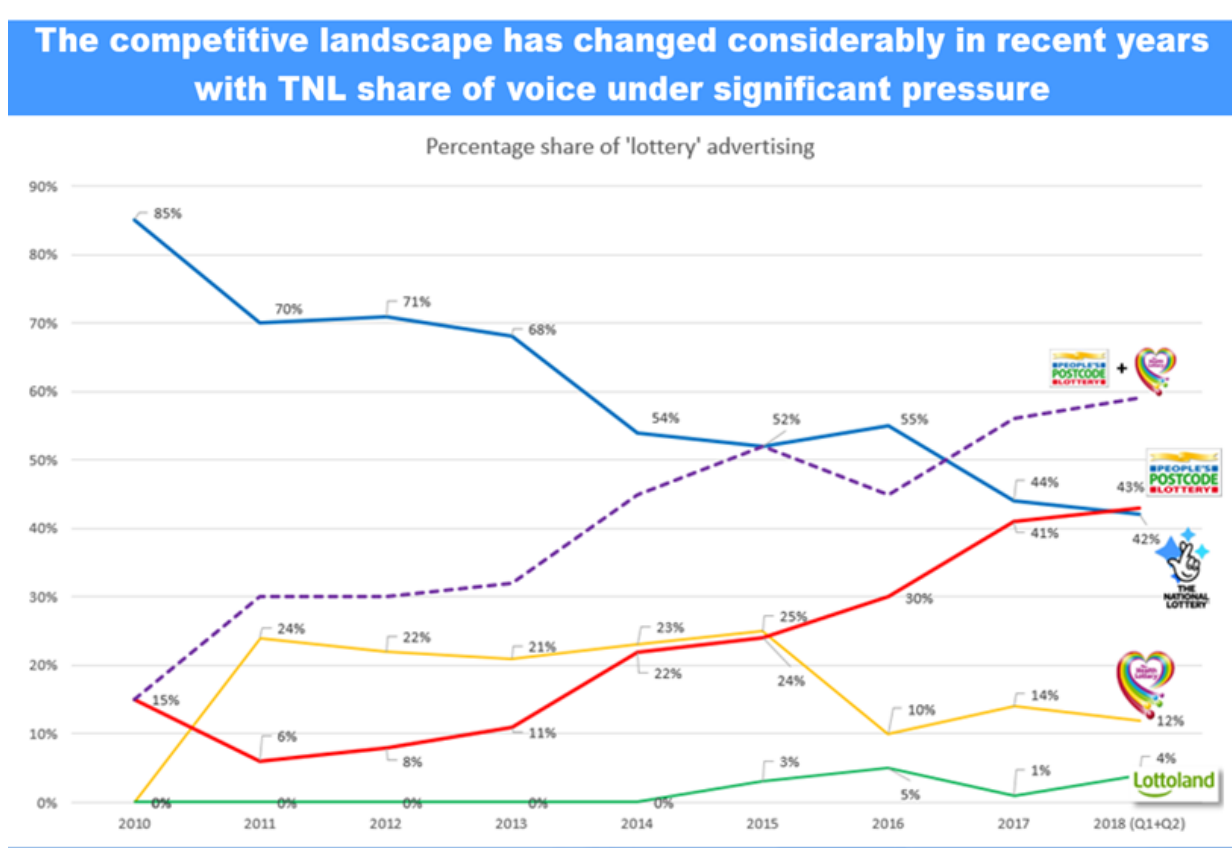
Similarly, the Health Lottery has also increased its advertising spend – in the last 5 years it increased by over 400% (from an estimated £6.9 million in 2013 to £35.2m in 2017).

It cannot be correct that two 'synthetic' national lotteries with a combined turnover of c. £365 million spend more on advertising than The National Lottery (with sales of £6.95 billion).

Share of voice

Share of voice – related to marketing spend – is another important factor to consider when evaluating the lotteries ecosystem and assessing potential impact of the proposed changes on The National Lottery. This is omitted from the Gambling Commission's advice, which looks at the growth of the markets but not the impact of marketing on the share of voice. Before looking at the changes in share of voice over time, we must consider this point in the context of the 'single national lottery' model. Given that The National Lottery is licensed as a 'single operator', it follows that it should command a significant share of voice in lottery marketing – prior to the growth of 'synthetic' national lotteries, the National Lottery enjoyed a share of voice of around 85%. However, the increasing marketing spend of the 'synthetic' national lotteries has eroded The National Lottery's share of voice significantly. The chart below shows how combined 'synthetic' national lotteries share of voice has grown from 15% in 2010 to 55% in 2017 and how the National Lottery's share of voice has fallen from 85% to 42% in the same period.

Figure 4:



The marketing 'arms race'

In contrast to the 'synthetic' national lotteries, which spend around 29% (People's Postcode Lottery) and c.40-50% (the Health Lottery) of total revenues on expenses, Camelot operates The National Lottery at a margin of around 5%. This consists of 4% expenses – 1.07% of which accounts for marketing spend – and c.1% in profit. The result of this fundamental difference is to drive a distortion in the relationship between share of voice and market share. This exerts a competitive threat on The National Lottery which is disproportionate to the relative scale of the synthetic national lotteries and establishes a critical dilemma as to how to respond. Either The National Lottery will have to accept a decline in its market share as a result of being outspent by its smaller, synthetic competitors with a resultant reduction in returns to society. Or, it must respond in kind by committing additional investment in marketing using funding that would otherwise flow directly to Good Causes.

In effect, this distortion has led to a marketing 'arms race' between The National Lottery and the 'synthetic' national lotteries. To give a sense of scale of the harm that has already been caused as well as the potential for further harm as a result of the changes proposed by Government, it would be necessary to increase The National Lottery's marketing outlay by more than 600% per year to £280 million to return to an 85% share of voice that it had, by statutory design, in 2010. This is a scenario that could never be recommended by a responsible and efficient operator, but the long term impact is unequivocal. Failing to maintain The National Lottery's single operator position undermines returns to society. On this basis alone, the government should not proceed with its proposed reforms as they would clearly be

in conflict with the statutory duty of the Secretary of State to ensure that the net proceeds of the National Lottery are as great as possible.

Comparing National Lottery and People’s Postcode Lottery efficiencies:

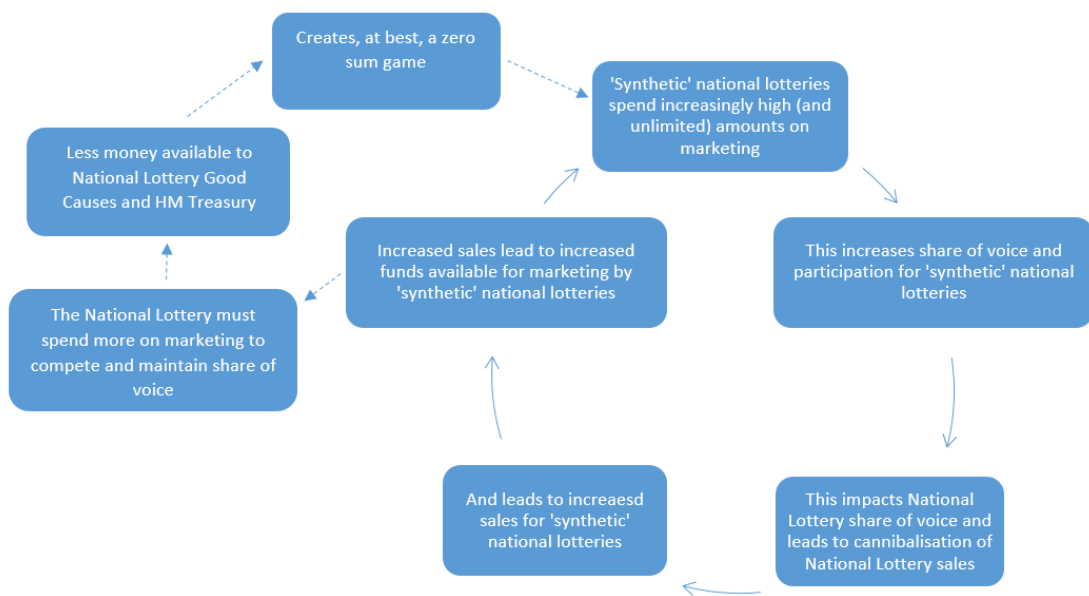
In the latest financial year, both The National Lottery and People’s Postcode Lottery spent a similar amount on marketing. As a result:

- The National Lottery returned **£1.6 billion** to Good Causes and **£834 million** in Lottery Duty
- People’s Postcode Lottery returned **£93 million** to Good Causes

Taking this to its logical conclusion, the unchecked growth of ‘synthetic’ society lotteries will continue have a direct impact on both National Lottery returns to Good Causes and also to the Exchequer and society more widely. The National Lottery will be forced to increase its marketing spend in order to protect its share in a market where it should be the ‘single operator’ and this will unavoidably impact on returns to National Lottery Good Causes. This conflicts directly with the duties of the Secretary of State and Gambling Commission to maximise the net returns to society, because it enables damage to The National Lottery while allowing marketing spend to increase to levels that compromise returns to National Lottery Good Causes. It also has implications for the Exchequer, as any reduction in National Lottery sales will automatically lead to a reduction in Lottery Duty (at 12% of turnover). This also trickles down to local high streets, where retailers will feel the effects of reduced commission from National Lottery sales.

The result is a zero sum game, where National Lottery returns to society are at risk:

Figure 5:



Participation in ‘synthetic’ national lotteries

The impact of increasing marketing spend and share voice for the People’s Postcode Lottery can also be clearly seen in the increase in the number of players in recent years. Over the period 2012 to 2017, the number of People’s Postcode Lottery players has increased by around 900% from 237,000 to over 2.4 million³⁹. In addition, it is also instructive to look at the increase in monthly Webtraffic visits to the People’s Postcode Lottery’s website (www.postcodelottery.co.uk). For the period January 2017 to July 2018, monthly visits increased by 43%⁴⁰.

Cannibalisation of National Lottery sales – Frontier Economics Analysis August 2018

Following the publication of the DCMS Consultation on Society Lottery reform and the Gambling Commission’s advice provided to DCMS which found that large society lotteries do not compete with The National Lottery, Camelot asked Frontier Economics (Frontier) to update its 2017 analysis of the effect of competition on National Lottery sales. We also asked Frontier to consider the future impact of competition on The National Lottery over the rest of the current licence period.

Frontier’s analysis is based on a robust econometric framework incorporating competitor advertising by ‘synthetic’ national lotteries the Health Lottery and People’s Postcode Lottery, along with betting-on-lotteries company Lottoland to determine the effect on National Lottery sales, and a forward-looking scenario model drawing on this econometric evidence.

Frontier continues to find that competition has had a negative impact on National Lottery sales compared to what they otherwise would have been. Frontier’s analysis shows that total National Lottery sales have been reduced by a cumulative £703 million as a result of competition over the period 2011 to 2017 – leading to a reduction in National Lottery returns to society of £266 million over the same period. Given competitor sales of around £1.4 billion, this suggests an average cannibalisation rate of almost 50% over the 7-year period.

³⁹ Novamedia / People’s Postcode Lottery Annual reports 2012 to 2017

⁴⁰ Hitwise web traffic data, August 2018

Figure 6: Competitor sales and impact on National Lottery sales

	2011	2012	2013	2014	2015	2016	2017	Total
Competitor sales (£m)	62	139	125	178	222	296	380	1402
Impact on National Lottery sales (£m)	-49	-61	-66	-88	-135	-143	-161	-703
Impact on TNL returns to society	-20	-24	-25	-34	-51	-53	-59	-266
<i>of which Good Causes</i>	-14	-17	-18	-23	-35	-36	-40	-182
<i>of which Lottery Duty</i>	-6	-7	-8	-11	-16	-17	-19	-84
Implied cannibalisation	80%	44%	53%	50%	61%	48%	42%	50%

Source: Frontier Economics estimates based on econometric model results, National Lottery sales data and estimates of competitor sales data.

Looking ahead, Frontier estimates in its central scenario⁴¹ that over the period from 2018 to 2022 National Lottery sales are reduced by £1.6 billion and National Lottery returns to society by £591 million.

Figure 7: Impacts over time on National Lottery sales and returns to society in the central scenario (£m)

	2018	2019	2020	2021	2022	2018-22
Competitor sales (£m)	478	578	670	745	791	3262
Impact on National Lottery sales (£m)	-239	-289	-335	-372	-396	-1631
Impact on TNL returns to society	-87	-105	-122	-135	-143	-591
<i>of which Good Causes</i>	-58	-70	-81	-90	-96	-396
<i>of which Lottery Duty</i>	-29	-35	-40	-45	-47	-196
Assumed cannibalisation	50%	50%	50%	50%	50%	50%

Source: Frontier Economics analysis

The Frontier analysis provides compelling evidence that, contrary to the assertion in the DCMS consultation document and the Gambling Commission's advice, the growth of 'synthetic' national lotteries has had a direct and material adverse impact on The National Lottery.

It is also worth noting that 'synthetic' national lotteries may have cannibalised sales from other society lotteries, who typically return even larger shares of sales to good causes. We would further urge further investigation of this by the Gambling Commission.

⁴¹ This scenario assumes 50% cannibalisation from competitors, medium competitor growth, equal impact propensity between Draw Based Games and Instant.

The relevance of the top prize

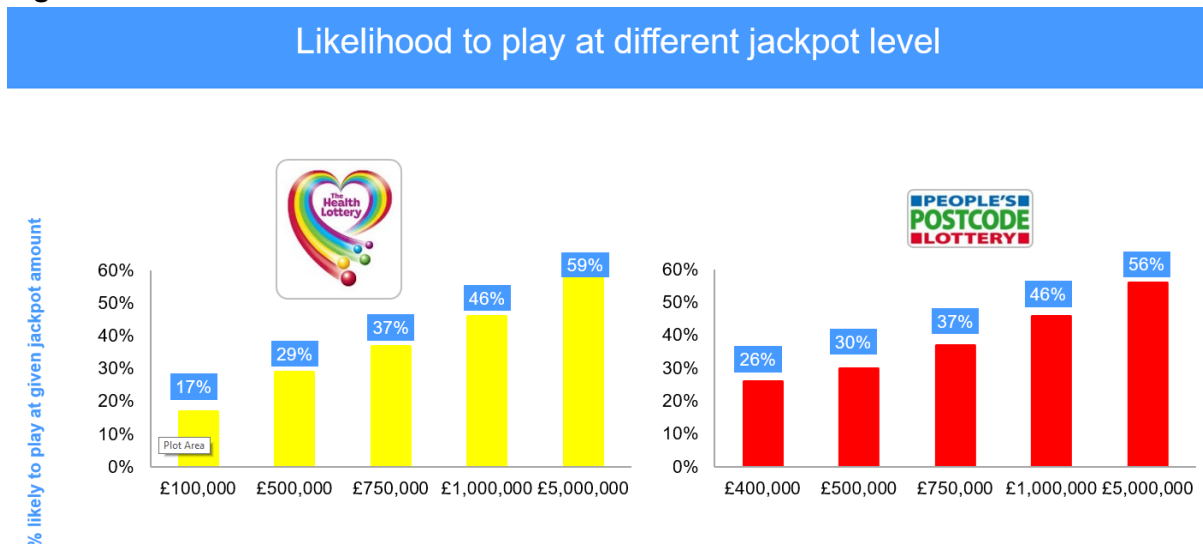
This situation set out above is likely to be exacerbated if the top prize for society lotteries is increased.

Life changing prizes are the preserve of The National Lottery and many games in its portfolio offer prizes of £500,000 or £1 million. This includes draw-based games like Thunderball, which has a top prize of £500,000, and many National Lottery Instant Win games offer top prizes of £500,000 or £1 million.

We are continuing to develop new and existing games with prizes in the £500,000 to £1 million range. These prize levels are therefore key National Lottery territory and it remains paramount that the £500,000 to £1 million prizes remain the exclusive preserve of The National Lottery to ensure the games are successful and maximise returns to Good Causes.

Camelot recently commissioned research⁴² with 1,673 consumers to identify the impact of increasing the jackpot to £500,000 and £1 million (options considered in the consultation document and accompanying advice) for society lotteries on player participation. As the below chart clearly shows, higher jackpots materially increase the likelihood that consumers will play 'synthetic' society lotteries. For example, the likelihood of playing People's Postcode Lottery at jackpots of £500,000 and £1 million increases by 15% and 77% respectively (vs. the current £400,000 jackpot). The results for the Health Lottery are even starker with likelihood of playing increasing by 71% for a £500,000 jackpot and 171% for a £1 million jackpot (vs. its current top prize of £100,000).

Figure 9:

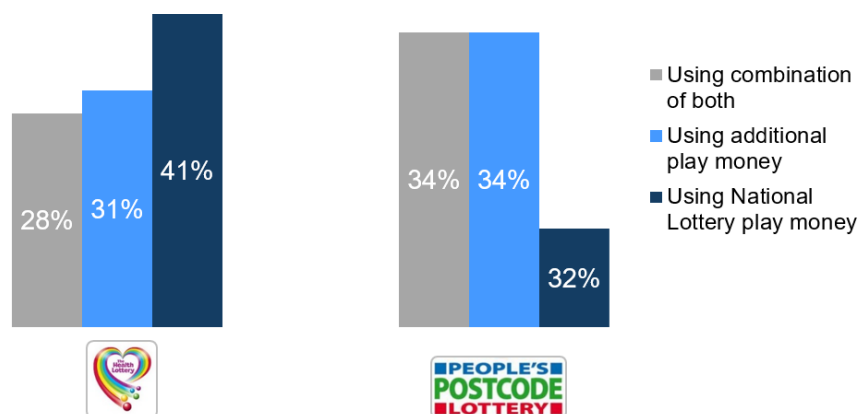


The same research also identified the source of funding for the increased play. As the chart below illustrates, the research found that around two thirds of consumers expect any additional play to come at the expense of The National Lottery.

⁴² Verve Research, Society lotteries online survey , 1 to 6 August 2018, amongst 1,673 PlayerHub members

Figure 10:

Source of increased play funding



It is also important to note that a change to the top prize as proposed would create direct competition with the National Lottery game Thunderball, which also offers a £500,000 top prize. This game alone generated returns to society of £124 million last year, a sum greater than (and more efficiently than) the returns to society generated by the People's Postcode Lottery. Direct competition for consumer spend in this game category, supported by heavy marketing investment by 'synthetic' national lotteries will have a predictably adverse impact on the National Lottery's ability to generate returns to society.

Further, the intentions as stated by DCMS in the consultation materials are to support 'fundraising by society lotteries while maintaining the distinct nature of the sector from the National Lottery.' The consultation document cites the intent of the Gambling Act 2005:

'The Act deliberately imposes strict limits on the annual and individual draw sales, and on the prizes they can offer, which ensures that the primary purpose of society lotteries is to raise funds for good causes and that they remain distinct in size from the National Lottery.'

We believe that by enabling direct competition between society lotteries and the £295 million National Lottery Thunderball game, DCMS's recommendations to increase prize limits are at odds with its declared objectives.

Motivation to play society lotteries shifts from charitable giving to winning prizes

Not only would increasing the jackpot for umbrella society lotteries increase consumers' likelihood to play at the expense of The National Lottery, it also appears to change the motivation behind *why* they play.

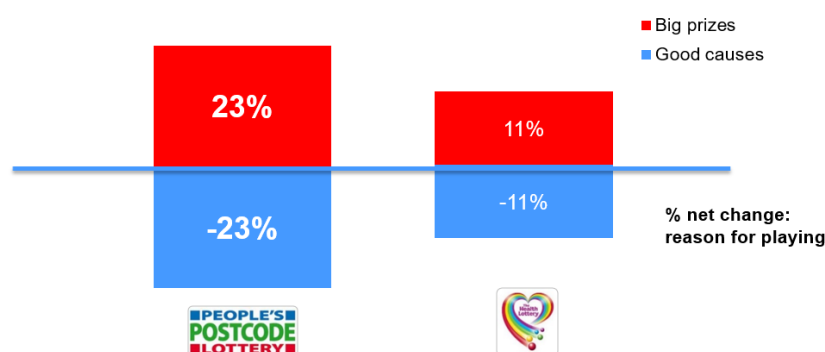
Previous governments have recognised that The National Lottery and society lotteries fulfil different roles with people playing society lotteries primarily because they wish to contribute to the good causes concerned. For example, when Government last considered changing the top prize for society lotteries (in 2008) it noted that there is “a significant risk that increasing the limit on proceeds of lottery draws, and hence the top prize available by too great an amount could significantly change the character of a society lottery by appealing to players for whom winning such a prize would be a greater attraction than supporting the charitable cause in question.”⁴³ More recently, the Gambling Commission’s advice to DCMS on regulatory policy for the lottery sector (October 2017) referenced the characteristics that separate the different types of lotteries in the UK, with the level of top prize being a key differentiator and means of protection for The National Lottery, along with generally limited distribution and specific good cause association.

We know that members of the public are motivated to play society lotteries based on the desire to support a specific cause or charity, and historically society lotteries have been specific to a local region or specific charity. For The National Lottery the prime motivation for most players is the chance to win life-changing prizes – which are the preserve of The National Lottery – with the secondary motivator being the prospect of giving to Good Causes.

Our research shows that the motivation shifts from good cause to prize when the prize limits are increased:

Figure 11:

Main reason for playing if jackpots increased to £1,000,000 – current projected, net change



Advertising – focus on top prize versus motivation to support good causes

Along with increased levels of marketing as set out above, the focus of the ‘synthetic’ national lotteries’ advertising has also shifted over time. Returning to the distinction between society lotteries and The National Lottery, as intended by Parliament, the motivation for playing The National Lottery is driven primarily by the possibility of winning significant, life-changing prizes, whereas society lotteries are generally characterised by lower prize, low frequency draws and a primary focus on the good causes they support. Looking at the recent marketing (advertising) of the People’s Postcode Lottery, this distinction is not evident. This is demonstrated by the People’s Postcode Lottery marketing materials below:

⁴³ 16 July 2008 DCMS Ministerial Written Statement, Society Lottery limits



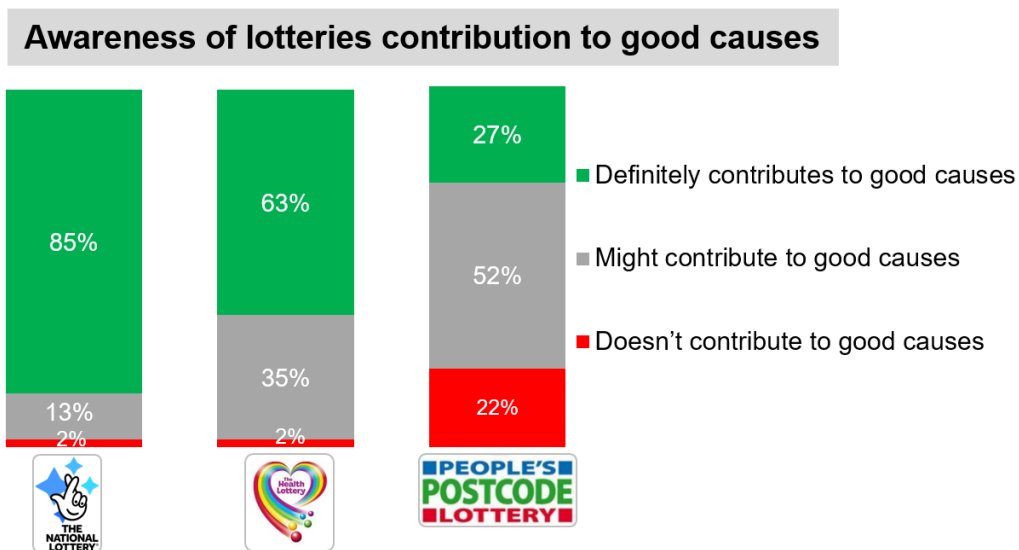
In addition, our analysis of People’s Postcode Lottery adverts found that almost all of its TV advertising is focused on winners and highlights the largest prizes in that month. Mentions of Good Causes are often passing references.

This is the same for the Health Lottery, where the launch of the new monthly £250,000 raffle has seen advertising focus almost entirely on the prize and not the good causes.

Awareness of lotteries’ contributions to good causes

Given that, as explained above, that ‘motivation’ to play society lotteries is primarily as a means to give to charity, we considered the extent to which players of the two largest ‘synthetic’ national lotteries were aware that there was a good cause element when they bought a ticket or subscribed to play. Our research found that, when asked whether the People’s Postcode Lottery gives to good causes, 22% of players believed that it makes no contribution to good causes and a further 52% thought that it *might*. Only 27% of People’s Postcode Lottery player correctly identified that it does contribute to good causes.

Figure 10:



7. Impact on the National Lottery Licence

Aside from the short-term damage to The National Lottery that we believe will result from the proposed changes, there are some more fundamental short-term and long-term issues that must be considered.

A departure from the basis on which the Third Licence was awarded

The proposed changes not only risk increasing the already proven negative impact on The National Lottery, but also move significantly away from the basis upon which the Third Licence to operate was awarded. The Third Licence competition was run – and won by Camelot – on the basis that there is clear separation between The National Lottery and society lotteries. As described above, this distinction has already been significantly blurred, but the proposed changes would represent an even greater shift from the Licence as awarded.

Impact on Fourth Licence competition

We understand that the competition for the Fourth Licence to operate The National Lottery is due to commence in early 2019. The DCMS consultation materials appear to contemplate successive relaxations for the society lottery market.⁴⁴ As noted elsewhere, we believe such an outcome would reduce overall returns to society. It may also weaken the forthcoming fourth Licence process.

Decisions about whether and how to bid for the National Lottery licence are inherently complex and uncertain, but are based on an understanding of the current and likely future competitive context. Any increase in regulatory uncertainty arising from a current (or possible expected future) relaxation of the caps on large-scale society lotteries could therefore be associated with a reduction in the willingness for providers to bid, or at least an increase in the margins expected as a result. Any reduction in competition, or increase in margin, could threaten the returns to society from the next licence period.

In conclusion, if DCMS is unable to offer clarity around the regulation of the UK lottery ecosystem, it may result in a number of undesirable outcomes:

- bidders raising prices to adjust for competitive uncertainty, reducing overall returns to Good Causes
- increased complexity of Licence negotiations to manage risk of adverse regulatory or policy changes

In summary, changes to the prize and proceed limits at this time could have potentially serious consequences for the forthcoming fourth National Lottery Licence competition.

⁴⁴ The Gambling Commission has developed a series of triggers to determine when future reviews of sales and prizes should take place, DCMS Consultation, Op Cit p7

8. Camelot's recommendations

Proposed solution: Reinroduce a cap on expenses for 'synthetic' national lotteries

As can be seen from the analysis above, the 'synthetic' national lotteries have significant cost ratios. This analysis contradicts the assertion in the DCMS consultation that *"umbrella schemes ... can provide marketing efficiencies"*.

To counter the marketing 'arms race' set out above, reset the 'share of voice' and to ensure that National Lottery Good Causes are not impacted in the future, Camelot continues to argue that an expenses cap should be reintroduced for 'synthetic' national lotteries, ensuring that the level of expenses remains proportionate. We suggest that the cap should be reinstated at a level that recognises the scale on which 'synthetic' national lotteries now operate (i.e. between 5% and 10%). For the avoidance of doubt we are not suggesting that this cap applies to traditional society lotteries. Should an expenses cap not be introduced for 'synthetic' national lotteries we believe it is vital that The National Lottery is enabled to spend more itself on marketing.

Prize and individual draw limits – at a minimum, maintain the status quo

The evidence we set out in this response clearly demonstrates that there has already been a negative competitive impact from the 'synthetic' national lotteries on The National Lottery. This would therefore point to a reduction in the prize and proceeds limits as a solution. However, we recognise that Government is in a difficult position and needs to balance the needs of various stakeholders. To that end, while a reduction in the top prize would help to reduce future damage to The National Lottery, it would have a corresponding effect on the individual draw limits which might inadvertently put traditional society lotteries at a disadvantage, particularly those charities that operate on a national scale such as Macmillan Cancer Support.

As a minimum, we believe that the status quo must be maintained, in order to limit damage to The National Lottery. However, a more 'surgical' option would be deregulation in the shape of legislation that decouples the prize and proceeds limits. This would reduce the competition from 'synthetic' national lotteries around the top prize and help to ensure the future health of The National Lottery and the single national lottery model, and would also enable traditional society lotteries to thrive, with the focus clearly on the cause and not the top prize.

No change to annual sales limits

The consultation also proposes to increase the annual limits for society lotteries from £10m to £100m. As noted above, we see scale as an important differentiator between The National Lottery and the society lotteries sector. We have already highlighted the current impact and future threat to returns to society from 'synthetic' national lotteries. While we support the proposal to reduce administrative burdens for traditional society lotteries, we have concerns that increasing the annual limit to £100m will enable 'synthetic' national lotteries that compete directly with The National Lottery by spending even more on marketing. Finally, the recommended ten-fold increase in annual turnover caps is a major change and seems to contradict the objective of the consultation, which is to preserve the balance between society lotteries and the National Lottery, while taking a cautious approach.

9. Conclusion

We do not believe that there is a compelling case to justify the proposed increase to society lottery prize and proceed limits. The preferred options proposed by DCMS are based on the belief that there is no evidence of a negative impact on The National Lottery from the growth of 'synthetic' national lotteries. This unfounded expectation of positive outcomes has been reached by Government without having completed a comprehensive impact study and full Impact Assessment, placing the £2.4 billion annual proceeds to society from The National Lottery at great risk.

Further, we do not believe that there is any evidence that the current prize and proceed limits are restricting growth of the society lotteries market. Indeed, the Gambling Commission's data on total proceeds from large society lotteries paints a picture of a sector in growth.

It is also clear from Camelot's evidence that moving away from the 'single National Lottery operator' model will undermine returns from The National Lottery to society. Our evidence shows that, contrary to the Gambling Commission's view that there is no evidence of impact, competition *has* had a negative impact on National Lottery sales compared to what they otherwise would have been. Frontier Economics estimate that National Lottery sales have been cannibalised by £703 million as a result of competition over the period 2011 to 2017, leading to a reduction of National Lottery returns to society of £266m over the same period. Further, the evidence suggests that this will only increase over time, and that there will be a stepped increase if the prize and sales limits are raised.

The proposals move further away from the efficient 'single operator' model as originally intended by Parliament towards an increasingly fragmented, inefficient ecosystem where competition to The National Lottery is growing, creating a 'marketing arms race'.

This not only has a negative impact on National Lottery returns to society but also moves significantly from the basis upon which the Third Licence to operate was awarded. Further, it could weaken the competition for the fourth National Lottery Licence.

In conclusion, and as a minimum, we believe that the status quo must be maintained, in order to limit damage to The National Lottery. However, a more 'surgical' option would be deregulation in the shape of legislation that decouples the prize and proceeds limits. This would reduce the competition from 'synthetic' national lotteries around the top prize and help to ensure the future health of The National Lottery and the single national lottery model, and would also enable traditional society lotteries to thrive, with the focus clearly on the cause and not the top prize.

Appendix 1

International evidence – harm to national lotteries from large scale society lotteries Competition Authorities Approve De Lotto- Staatsloterij Merger

11TH DEC 2015 | WRITTEN BY: DAVID ALTANER, GAMBLING COMPLIANCE

The Dutch State Lottery (Staatsloterij) and De Lotto have been given approval to merge by competition regulators, in a potential combination that would create a €1bn (£725m) lottery operator.

The possible merger would help the state-owned operators reverse sliding turnover and prepare for the opening of the licensed Netherlands online gambling market, probably in 2017. The merger proposal now goes to parliament for approval after passing the Council of Ministers in October.

A Staatsloterij spokesman said approval from the Authority for Consumers and Markets (ACM) was an "important next step". "After the merger the new organisation has a known position on the Dutch offline lottery-market," he said. It will be able to develop online lottery- and gambling-games, with proceeds going to Dutch society, sports and charities, he added.

The competition regulators said they see no risk of the combined company dominating the market because there will be sufficient domestic and foreign competition. "It appears that the State Lottery and the Lotto in practice rarely compete with each other", partly due to strict regulation of the companies, said Chris Fonteijn, ACM chief executive. "Our research shows this merger has only a limited effect on the gaming market," he said in a statement this week.

Previously, the ACM had said the merged group would control about half of the Dutch lottery market, with Postcode Lottery, BankGiro Lottery and Friends Lottery controlling most of the rest.

State secretary for finance Eric Wiebes said the merged company would generate more money for social causes and sports.

As Postcode Lottery and other charity lotteries have mounted a marketing push, De Lotto and Staatsloterij's market share of the country's lottery market has contracted.

De Lotto turnover declined 8.6 percent between 2010 and 2014 to €321.8m, while at Staatsloterij, turnover fell 12 percent in the same period to €737.8m.

In contrast, turnover at the country's national charity lottery sector, which comprises Postcode Lottery, BankGiro Lottery and Friends Lottery, has been on an upward curve for a number of years with turnover in excess of €850m by the collective trio.

If the merger raises more funding for sports, "obviously that would be a good thing," said a spokeswoman for the three charity lotteries.

"However, since a major competitor will arise on the Dutch market, we will follow its proposition and profiling with great interest," the spokeswoman told GamblingCompliance. She also called

for "a level playing field for the Dutch lotteries, in order to be able to contribute even more to society all together".

The Dutch government is extending lottery and gambling licences for an extra two years to 2017, as the country updates its 50-year-old licensing legislation. A fuller account of the competition board's decisions usually comes about a week after an announcement of a resolution.