



NATIONAL LOTTERIES COMMISSION

a member of **the dti** group

The background of the cover features a close-up of hands holding a pen over a lottery ticket. The ticket has a grid of numbers and a 'Date:' field. In the foreground, several colorful lottery balls (orange, blue, yellow, red, green) are scattered, some with numbers like 29, 23, 28, and 27. The bottom half of the cover has a solid blue background.

# FEASIBILITY STUDY ON THE REGULATION OF ILLEGAL LOTTERIES IN SOUTH AFRICA



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# FEASIBILITY STUDY ON THE REGULATION OF ILLEGAL LOTTERIES IN SOUTH AFRICA



# EXECUTIVE SUMMARY

The National Lotteries Commission (NLC) was established in terms of section 2 of the Lotteries Act 57 of 1997 as amended (the Act). The NLC is responsible for regulating lotteries and sports pools. In terms of the Act, all lotteries are illegal unless authorised in terms thereof.

The NLC has an explicit revenue-maximizing mandate. Section 10(b) (iii) of the Act requires the Board to ensure that the net proceeds of the National Lottery are as large as possible, and to identify any risks or obstacles to the fulfilment of this objective. Other responsibilities include advising the Minister of Trade and Industry on policy matters relating to the National Lottery and other lotteries.

The comprehensive *Impact of Illegal Lotteries* study conducted in 2016 documented the proliferation of illegal lotteries in South Africa. These are defined in this report, and include totalisators offering sports pools, fahfee, bookmakers offering fixed odds bets on the outcome of a lottery (numbers betting), some promotional competitions, bets placed on international lotteries, and lottery scams.

According to this study, the amounts spent on these schemes, and the cost to the NLDTF, are as follows:

<b>Lottery Activity</b>	<b>Total (R millions)</b>	<b>% Share</b>	<b>NLDTF (R millions)</b>
National Lottery	4,559.00	65.6%	1,230.00
Totalisators offering sports pools	1,092.73	15.7%	295.04
Fahfee	725.57	10.4%	195.90
Bookmakers	531.38	7.6%	143.47
Promotional competitions	19.91	0.3%	5.37
International lotteries	5.92	0.1%	1.60
Lottery scams	10.48	0.2%	2.83
Permitted lotteries	1.60	0.0%	0.43
<b>Total</b>	<b>6,946.59</b>	<b>100%</b>	<b>1,875.58</b>

Historically, the NLC took punitive action against the operators of these illegal lottery schemes. More recently, the NLC has considered the possibility of legalising and licensing *some* additional lottery schemes. In this way, to adapt the famous US anti-prohibition saying to our current purpose, we hope to bring popular but illegal games “out of the underground and into the sunlight” where they can be appropriately monitored and regulated.

In this way, the reputation and integrity of the National Lottery can best be protected, whilst revenues for the National Lottery and for good causes are maximised.

This report assesses the feasibility of regulating these illegal schemes. At the outset, the assumption is that these schemes are all currently operational, popular, and cannot easily be closed down and prevented. The intention with legalisation is not to encourage a proliferation of new forms of gambling but, rather, to channel popular existing forms of illegal gambling into an open and transparent regulatory space, where their harmful effects can be mitigated.

In accordance with the project terms of reference, the report overviews the *modus operandi* and considers the pros and cons of regulating each scheme. Drawing on interviews with industry stakeholders, including both operators and regulators, a comprehensive literature review, and an analysis of the experience of regulating similar schemes in other jurisdictions, the report makes a number of suggestions as to the licensing and regulation of these schemes.

At a high level, the basic approach to the legalisation of each scheme can be summarised as follows:

Gambling Mode	Type of action required
Fahfee	Legalize, and develop new legal/regulatory framework Regulate, possibly in conjunction with voluntary industry associations Preserve the existing character of the game (including number selection and return to layer)
Bookmaker fixed odds numbers betting	National Gambling Amendment Bill, 2017, shifts regulatory responsibilities to the NLC Existing (provincial) legal frameworks exists, which need to be adapted to allow for (national) NLC regulation. Restrictions on advertising to preserve feel of traditional lotteries Licensing of bets on lotteries offered outside of SA only. No bets allowed on SA licenced lotteries. Guarantees needed to cover operator liability





Sports betting	National Gambling Amendment Bill, 2017, shifts regulatory responsibilities to the NLC  Existing (provincial) legal frameworks exists, which need to be adapted to allow for (national) NLC regulation.  Additional focus on integrity of underlying sports and the dangers of match-fixing
Promotional competitions	Clarify and supplement existing legal framework
Society lotteries	Clarify and supplement existing legal framework
Other unauthorized lotteries	Stricter enforcement of existing prohibitions.

*Recommendations: fahfee*

In terms of fahfee, which is presently an illegal lottery, the report makes the following recommendations:

- The Lotteries Act should be amended to legalise the game of fahfee. Fahfee should be regulated by the NLC, with licenses issued at a Provincial level.
- Voluntary fahfee operator associations should be established at a provincial level. Membership of such an association should become a condition of license.
- The NLC should explore various strategies for the licensing of fahfee operators. These include granting individual licenses (i.e. to stand alone operators, with perhaps 1-3 routes each), route operator licenses (granted to corporate entities who will then oversee the management and sub-licensing of a specified number of routes in designated areas), and licenses issued to provincial fahfee operators associations, who would, in turn, sub-license routes within each province.
- All fahfee operators to undergo a probity check, the manner and form of which should be prescribed by the NLC, and recorded on a national probity register. This is particularly important given the strong likelihood of criminal elements in the current fahfee sector.
- The issuing of licenses and the criteria used to identify potential licensees must contribute to the broad-based transformation of the bookmaker sector.

- The existing characteristics of the game of fahfee must be preserved. This includes the rules relating to number selection, pay-outs, and house edge/return to player. Similarly, it is recommended that the current system of decentralised ticket-sales, in which operators take bets at demarcated “banks” along a “route” rather than at fixed points, be retained.
- Fahfee operators must be allowed to advertise and promote the game of fahfee as well as their specific fahfee routes and banks. This should be subject to the same sumptuary limitations and restrictions that apply to the advertising of the National Lottery.
- A saturation study as well as a social impact assessment must be conducted after three years of legalisation. This study should be used to set limits to the further issuing of licenses.
- Fahfee operators licenced by the NLC must contribute a reasonable amount towards the NLDTF.
- Further research should be conducted to establish the best way to ensure tax and regulatory compliance, including the option of the NLC taking control of the printing and distributing of betting books, which can be sold directly to operators at a price commensurate with their aggregate expected contribution to the NLDTF and other gambling taxes. This would simplify compliance.

*Recommendations: Fixed odds betting on lotteries (numbers betting) and sports pools*

Provincial gambling boards currently regulate fixed odds betting on the outcome of lotteries, or numbers betting, as well as sports betting. The National Gambling Amendment Bill, 2017 (the Bill), gives the NLC sole legislative competence for the licensing of fixed odds bets on lottery results, regardless of the type or location of the lottery in question. Similarly, the Bill also gives the NLC sole legislative competence for the licensing of sports bets, other than those placed on horse races.

In terms of these new responsibilities, the report makes the following recommendations:

- Sports pool licenses should be granted on a national basis
- Bookmaker licenses should be granted on a provincial basis, subject to national compliance standards.
- The issuing of licenses, and the criteria used to identify potential licensees, must contribute to the broad-based transformation of the bookmaker sector.
- Bookmakers and totalisators licenced by the NLC must contribute a reasonable amount towards the NLDTF.



- Considerable attention needs to be paid to the dangers of regulatory confusion and overreach, as bookmakers and totalisators will now be expected to deal with separate provincial and national licensing authorities for their various betting and totalisator products. The changes mandated in the Bill should not raise transaction costs within the industry, or act as a barrier to the development of the industry. They cannot disincentivise the growth of the industry.

In terms of fixed odds bets placed on the outcome of lotteries, the report makes the following specific recommendations:

- The NLC should only license fixed odds bets on non-South African lotteries. Bets placed on the National Lottery or any other lottery licenced by the NLC should not be permitted in order to help preserve the monopolistic character of the state lottery.
- Licenses to place bets on the outcomes of lotteries should be granted subject to clear conditions pertaining to the advertising and promotion of such products, including prohibitions against the use of the words “Lottery” and “Lotto”. Players need to understand fully that they are betting on a contingency (often called hard gambling), not participating in a lottery that raises funds for good causes (soft gambling).
- A national guarantees policy should be developed, and bookmakers should lodge financial guarantees to ensure that they are able to make possible multiple pay-outs on the top fixed odds prizes they offer.

In terms of sports pools, the report makes the following specific recommendation:

Provincial gambling boards currently regulate sports pools. The Bill gives the NLC sole legislative competence for the national licensing of sports pools, other than those placed on horse races.

The issuing of national licenses for sports pools has the potential to create a more viable and profitable, national tote, as opposed to multiple regional totes, which is good for the industry as a whole.

To affect this shift in regulatory responsibility, the report makes the following recommendations:

- The NLC, in conjunction with the relevant sporting associations, and perhaps the Minister of Sport, needs to develop a national policy for the regulation of sports betting, which addresses in particular the problem of match fixing. (This applies equally to bookmaker betting on sporting events, which is regulated by provincial authorities.)

## *Recommendations: promotional competitions*

In terms of promotional competitions, the report makes the following specific recommendations:

- Promotional competitions should continue to be prohibited from requiring a subscription or consideration. The Lotteries Act, the Consumer Protection Act, and the Codes adopted by industry self-regulation bodies, should reinforce this point. Promoters should however be entitled to require participants to bear the reasonable cost of entry, subject to a stipulated maximum cost (currently R1.50).
- The provisions in section 36(3)(b) of the CPA should be clarified to allow promoters to require participants to purchase goods or services at their current market price in exchange for the right to participate in the promotional competition.
- The definition of a promotional competition removed by the Lotteries Amendment Act, 2013 should be reinserted. This should read: “‘promotional competition’ has the meaning set out in section 36 of the Consumer Protection Act, 2008.”
- The definition of a promotional competition in the Consumer Protection Act should be simplified to avoid ambiguity. The following definition is proposed: “‘promotional competition’ means any competition, game, scheme, arrangement, system, plan or device for distributing prizes by lot or chance if it is conducted in the ordinary course of business for the purpose of promoting a producer, distributor, supplier, or association of any such persons, or the sale of goods or services, irrespective of whether a participant is required to demonstrate any skill or ability before being awarded a prize”.
- The following authorising provision should be inserted in place of section 54 of the Lotteries Act, which was repealed: “A promotional competition, as defined in the Consumer Protection Act, 2008, is authorised by the Act.”
- Redundant references to section 54 (which has been repealed) should be removed from the Lotteries Act, specifically references to section 54 in section 1 (definition of a participant), section 10(d), and section 56(b) and (c) of the Lotteries Act. The relevant sections should cross reference to section 36 of the Consumer Protection Act instead.
- The threshold for the exclusion of competitions with prize values below a designated threshold should be increased to R100. Competitions with prizes falling below the stipulated threshold should be exempted from section 36 of the Consumer Protection Act’s requirements.
- Organisers of promotional competitions should be required to join an Industry Association and submit to its self-regulatory codes relating to sales promotion, in general, and promotional competitions, in particular, where such codes exist.



In addition to these schemes, the report considered international lotteries that are presently sold directly in the South African market, usually online, as well as lottery scams, where people are enticed to pay for tickets to lotteries that don't exist (so called "advance-fee fraud" schemes). In both cases, these are clearly illegal, fraudulent, and unethical. There is no reason to consider legalising such schemes, and existing enforcement mechanisms need to be supported and strengthened to minimise their negative impact in South Africa.

Finally, the legalisation of fahfee and the transfer of responsibility for fixed-odds betting on lotteries as well as sports betting is going to require a whole range of new technical, regulatory, and human resource skills. The NLC will also need to develop considerable capacity to issue and oversee licenses at the provincial level. They do not have this capacity at present. Moreover, to become an effective gaming regulator, the NLC is going to have to develop a significant inspectorate, and to ensure that this is legally and administratively empowered to actively monitor and oversee the financial affairs of all licensees. In addition, the inspectorate will have to be able to investigate and stamp out illegal/unlicensed operations, especially in the case of fahfee.



# ACRONYMS

<b>ASA</b>	Advertising Standards Association
<b>CAP Code</b>	United Kingdom Code of Non-Broadcast Advertising, Sales Promotion and Direct Marketing.
<b>CPA</b>	Consumer Protection Act No. 68 of 2008
<b>GOBA</b>	Gauteng Off-Course Bookmakers Association
<b>NGB</b>	National Gambling Board
<b>NLC</b>	National Lotteries Commission
<b>NLDTF</b>	National Lotteries Distribution Trust Fund
<b>SABA</b>	South African Bookmakers Association
<b>SAPS</b>	South African Police Service
<b>SARGF</b>	South African Responsible Gambling Foundation
<b>VRGF</b>	Victorian Responsible Gambling Foundation
<b>WASPA</b>	Wireless Application Service Providers Association



# 1 INTRODUCTION

The National Lotteries Commission (NLC) was established in terms of section 2 of the Lotteries Act 57 of 1997 as amended (the Act). The NLC is responsible for regulating lotteries and sports pools. All lotteries are illegal unless authorised in terms of the Act. The National Lottery system is a monopoly system with only one operator, currently Ithuba (Pty) Ltd, authorised to conduct the National Lottery. The National Lottery contributes 27% of the funds raised to the National Lottery Distribution Trust Fund (NLDTF), for distribution to good causes. To date billions of rands were distributed to charities, sports and recreation and arts, culture and heritage projects.

We have an explicit revenue-maximizing mandate. Section 10(b) (iii) of the Act requires the Board to ensure that the net proceeds of the National Lottery are as large as possible, and to identify any risks or obstacles to the fulfilment of this objective. Other responsibilities include advising the Minister of Trade and Industry on policy matters relating to the National Lottery and other lotteries.

The comprehensive *Impact of Illegal Lotteries* study conducted in 2016 documented the proliferation of illegal lotteries in South Africa. Of particular concern is the almost R2.4 billion spent on illegal lotteries. This diverts significant revenue from the National Lottery and, in turn, has a negative impact on the NLDTF, and the good causes which the National Lottery supports.

It is on this basis that we conducted this study to determine the feasibility of regulating these illegal schemes, and to devise regulatory strategies to inform and guide policy.

## 2 OBJECTIVES OF THE STUDY

The objectives of the study is to:

- 2.1 Assess the *modus operandi* of the illegal schemes as contained in the impact study and conduct further assessment where necessary;
- 2.2 Determine the feasibility of regulating and devise regulatory options and recommend appropriate option
- 2.3 Outline the pros and cons of regulating
- 2.4 Outline the key issues that policy and legislation should address
- 2.5 Explore the views of the industry stakeholders
- 2.6 Benchmark/analysis of other international jurisdiction on regulation of similar schemes

## 3 SCOPE OF WORK

- 3.1 Assess the *modus operandi* of each scheme as contained in the impact study and conduct further assessment where necessary
- 3.2 Determine feasibility to regulate and outline the pros and cons of regulating each scheme within the ambit of the lotteries Act, including costs benefits.
- 3.3 Outline and recommend regulatory options appropriate for regulating such schemes
- 3.4 Views of the industry and international comparative analysis.

## 4 ILLEGAL LOTTERIES SITUATIONAL ANALYSIS

Illegal lotteries pose a significant financial risk to the National Lottery.

Illegal lotteries pose significant social risks as well. Problem (disordered) gambling is a significant problem in South Africa. Many schemes specifically target lower income groups, and have a significantly more regressive impact on the poor than the National Lottery.

Unfortunately, regulators receive insufficient support from the South African Police (SAPS) when seeking to enforce gambling legislation. The SAPS generally do not consider illegal gambling a priority crime, and few resources are devoted to the investigation and prosecution of illegal gambling operations.

In particular, there is a critical lack of capacity to manage cybercrime, which is a growing threat to the integrity of the gambling and lottery sectors.

In order to determine the nature and impact of illegal lotteries, we completed a detailed study, *Impact of Illegal Lotteries to the National Lottery in South Africa*, in 2016. The report identified the main illegal lottery schemes, and established the total estimated rand value of these unlawful lotteries and the associated loss of revenue for both the National Lottery and the NLDTF (NLC 2016: 58). This gives us a basis to assess the relative risks associated with each lottery scheme, and to contextualise the associated regulatory challenges.

This report builds on these findings, and considers ways to address the challenge of illegal lotteries in South Africa.



The primary illegal lotteries identified are fahfee; fixed odds betting on the outcome of the National Lottery and various international lotteries; sports pools; promotional competitions; international lotteries; lottery scams; and various other permitted lotteries authorised by the NLC.

## **4.1 FAHFEE**

Fahfee is a popular illegal lottery scheme, which has been played for over a century in South Africa. For less affluent township dwellers and working class black punters, fahfee is the most direct competitor to the National Lottery. Fahfee is a cash only business, and operators do not pay tax on profits or make any contribution to either the NLC or the NLDTF. Fahfee players may be disproportionately at risk for problem (disordered) gambling (SARGF 2009: 28).

Attempts to close down fahfee operations have little impact, and in our view it is better to try and license and regulate fahfee than to simply prohibit fahfee.

## **4.2 BOOKMAKERS – FIXED ODDS NUMBERS BETTING**

Worldwide, the gambling industry has witnessed a massive growth in the popularity of fixed odds betting on contingencies. One of the most popular contingency is the outcome of an existing lottery. This is often simply called numbers betting. Player's place bets on the outcome of a stipulated lottery, e.g. the Spanish Lottery, or the National Lottery in South Africa, and bookmakers offer relatively attractive fixed odds on all or some of the winning numbers selected.

In South Africa, bookmakers have been granted licenses by provincial gambling authorities to offer such schemes, often via an online platform. The National Gambling Amendment Bill, 2017, addresses this regulatory confusion.

## **4.3 SPORTS POOLS**

Sports Pools are pooled bets offered on any series or combination of sporting events. Sports betting generally (including both fixed odds and pooled/totalisator products), is the second largest gambling activity in the country, after casinos, and represent one of the fastest growing sectors of the gambling market, in both developed and developing countries.

In terms of the Act, sports pools, other than horse racing, are a national competence, and are supposed to be authorised by the Minister, in consultation with the NLC.

As with betting on the outcome of lotteries, provincial regulators have bypassed this and issued licenses within their jurisdictions. The National Gambling Amendment Bill, 2017, addresses this regulatory confusion.

#### **4.4 PROMOTIONAL COMPETITIONS**

Promotional competitions are lottery-based schemes offered for the purpose of promoting a particular person or business. These competitions are games of chance, and are treated as lottery games.

Promotional competitions are regulated according to section 36 of the Consumer Protection Act (2008), and no benefits accrue to either the NLC or the NLDTF.

In our view, promotional competitions should be defined in the Consumer Protection Act, 2008, and authorised by the Lotteries Act.

#### **4.5 OTHER AUTHORISED LOTTERIES**

The Lotteries Act makes provision for several smaller lotteries, which are authorised but not necessarily regulated by the NLC. These include society lotteries; private lotteries; and lotteries incidental to exempt entertainment. Of these, only society lotteries pose a potential risk to the monopoly of the National Lottery, or deprive the NLC and the NLDTF of revenue.

Society lotteries are lotteries promoted on behalf of a society that is established and conducted primarily for non-commercial gain. Society lotteries are licenced and regulated by the NLC.

Many society lotteries are offered illegally, without any regulatory approval. As such, no benefits accrue to either the NLC or the NLDTF. In part this is due to wilful disregard for the authority of the NLC. In part this is due simply to ignorance, as many non-commercial entities are unaware of the need for regulatory approval.

Private lotteries are lotteries run for and by members of a social or sporting club for purposes that are not connected with any form of gambling. Private lotteries are essentially self-regulated, and do not make any contribution to the NLC or the NLDTF. Organisers do not need to register with or report to the NLC, although they do have to observe certain rules in order to operate within the law. Lotteries incidental to exempt entertainment are self-regulated lotteries that are run as part of events classified as exempt entertainment.





This includes bazaars, fetes, dinners, dances and sporting events. These lotteries are essentially self-regulated, and do not make any contribution to the NLC or the NLDTF. Organisers do not need to register with the NLC or report to the NLC, although they have to observe certain rules to operate within the law. Promoters who do not operate within the framework set out in the Lotteries Act offer many private lotteries and lotteries incidental to exempt entertainment.

Private lotteries and lotteries incidental to exempt entertainment do not pose a significant threat to the national lottery. For this reason, they are not discussed further in this report.

## **4.6 OTHER UNAUTHORISED LOTTERIES**

A number of lottery schemes exist which are clearly not authorised by the NLC or any other law. These are illegal lotteries. As with fahfee, a decision has to be taken whether to legalise and regulate these, or to continue to enforce the prohibition of such lotteries. *The Impact of Illegal Lotteries Study* drew attention to two particularly prevalent schemes considered to pose a threat to the National Lottery, namely international lotteries and lottery scams.

International lotteries are lotteries offered in jurisdictions outside the Republic of South Africa. Participation in such lotteries is prohibited in terms of section 59 of the Lotteries Act.

There is no single type of lottery scam. All pretend to be lawful lotteries or competitions. Most seek to defraud people by enticing them to pay money to receive their winnings, or to stand in line to win a prize that is never actually awarded. These schemes fall outside the ambit of the Lotteries Act.

## **4.7 THE SIZE AND FINANCIAL IMPACT OF ILLEGAL LOTTERIES IN SOUTH AFRICA**

The *Impact of Illegal Lotteries* study estimates that a total of just under R7 billion is spent annually on lottery activity in South Africa. Only around two thirds of this is spent on the National Lottery. This is clearly a threat to the financial viability of the National Lottery.

The share of lottery expenditure in 2015, ordered by scheme, was as follows:

<b>Table 1: A breakdown of legal and illegal lottery activities</b>			
<b>Lottery Activity</b>	<b>Total (R millions)</b>	<b>% Share</b>	<b>NLDTF (R millions)</b>
National Lottery	4,559.00	65.6%	1,230.00
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Fahfee	725.57	10.4%	195.90
Bookmakers	531.38	7.6%	143.47
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Permitted lotteries	1.60	0.0%	0.43
<b>Total</b>	<b>6,946.59</b>	<b>100%</b>	<b>1,875.58</b>
Source: NLC (2016: 58).			

Of these, only the National Lottery, promotional competitions, and permitted lotteries, are legal schemes. Fahfee is clearly illegal, as are international lotteries and scams.

Totalisator sports betting and bookmaker numbers betting should both be considered illegal, as they operate under licenses that were incorrectly awarded by provincial regulators.

In total, almost R2.4 billion is spent on illegal lotteries. Much of the money currently spent on totalisator sports betting and bookmaker fixed-odds numbers betting will be shifted to the National Lottery now that the jurisdictional authority of the NLC has been confirmed in the National Gambling Amendment Bill, 2017 (the Bill).

Around three quarters of a billion Rands are lost to lotteries that are completely illegal.

None of the illegal lotteries identified here contribute to the NLDTF, which has a negative impact on funding for good causes, as well as considerable indirect and induced losses to the economy at large.

The *Impact of Illegal Lotteries* study estimates that the accumulated economic impact of lost NLDTF contributions for the period 2016–2020 will be:

<b>Table 2: The impact of illegal lotteries on the NLDTF</b>				
<b>Impact on:</b>	<b>Direct</b>	<b>Indirect</b>	<b>Induced</b>	<b>Total</b>
Production (R million)	644.65	854.98	1,004.98	2,504.61
GDP (R million)	265.14	363.50	429.38	1,058.02
Employment (No. of jobs)	1,702.00	1,831.00	1,852.00	5,384
Income (R million)	131.05	184.09	188.92	504.06
Source: NLC (2016: 60).				

The enormity of this projected impact—a loss of 5,384 jobs, R2.5 billion in production, R1 billion in GDP, and half a billion rand in income over 5 years—underlines the threat that illegal lotteries pose.

## 5 GENERAL PRINCIPLES OF REGULATION

Gambling is an economic activity with considerable external benefits and costs. In most jurisdictions, government claims a monopoly over gambling generally. Until the second half of the twentieth century, governments tended to ban or severely restrict all forms of gambling, typically on the basis of moralistic criteria, with a view to preventing the public from the harm caused by immoral predatory gambling operators (Clotfelter and Cook, 1991).

Attitudes began to change in the second half of the twentieth century, and regulators, beginning in Europe and North America, started to liberalise their gambling markets, seeking to promote the controlled expansion of a well-regulated and carefully controlled industry. This was as much due to changes in public morality – with gambling no longer treated as a moralistic concern – as an attempt to raise additional revenues without raising taxes (Clotfelter and Cook, 1991).

Lotteries have long been tolerated as a way to raise money for specific purposes. Famous examples include the lotteries used to partially fund the Sistine Chapel in the Vatican and Michelangelo’s ceiling, the British Museum, and Harvard University (Siemba 2018, 72). A less well-known example was used to fund the rapid industrialisation drive between 1928 and 1958 in the Soviet Union (Millar and Gentry 1980). As with gambling generally, states have increasingly sought to legalise and promote state owned or run lotteries in the post-War period, primarily as a politically attractive alternative to higher taxes.

In SA, the current regulation of lotteries is motivated by the desire to:

- protect the monopoly of the National Lottery and to enhance its revenue maximising mandate
- prevent the emergence of predatory lotteries which undermine the financial wellbeing and long term sustainability of the National Lottery
- protect players and the public alike, by ensuring the integrity of all aspects of the game, from number selection to pay-outs and the adjudication of complaints.
- protect the public from over stimulation of demand the negative effects of problem gambling (disordered gambling).

## 5.1 NEW APPROACHES TO REGULATION

Traditionally, the NLC sought to protect the integrity and financial viability of the National Lottery by taking punitive action against the operators of illegal lotteries. Provincial gambling regulators have followed a similar approach to illegal gambling operations within their jurisdiction. Sadly, this has not always been successful, and, as we see below, illegal lotteries continue to operate and grow.

At the 2015 National Indaba Roundtable (NLC 2017: 15) we debated the idea of shifting from a strictly prohibitionist style of regulation to one which is open to the possibility of legalising and licensing some additional lottery schemes. In this way, to adapt the famous US anti-prohibition saying to our current purpose, we hope to bring popular games “out of the underground and into the sunlight” where they can be appropriately monitored and regulated.

This might alternatively be described as shifting from a framework of strict protection of a state monopoly to a philosophy of carefully controlled liberalisation. In this way, the reputation and integrity of the National Lottery can best be protected, whilst revenues for the National Lottery and for good causes are maximised.

This report assesses the feasibility of regulating these illegal schemes. At the outset, the assumption is that these schemes are all currently operational, popular, and cannot easily be closed down and prevented. The intention is not to encourage a proliferation of new forms of gambling but, rather, to channel popular existing forms of illegal gambling into an open and transparent regulatory space, where their harmful effects can be mitigated.

Both the 2016 *Illegal Lotteries Study* and this report flow out of this decision to consider the feasibility of regulating illegal lotteries.



## 5.2 FACTORS TO BE TAKEN INTO CONSIDERATION OF POSSIBLE LEGALISATION OF ILLEGAL SCHEMES

When assessing whether to legalise a currently illegal lottery scheme the regulator needs to take the following factors into account:

- The history of the scheme and its popularity amongst the public.
- Whether legalising and regulating the scheme will contribute to the proliferation of gambling in South Africa.
- The social impact of the scheme, particularly whether the degree to which it contributes to problem (disordered) gambling.
- The displacement effects of the scheme on other lotteries. In particular, will legalisation of this scheme result in diminished revenues for the National Lottery.
- The actual cost and feasibility of prohibition. Is it realistically possible to prohibit the scheme? Or will operators simply ignore the NLC and continue to run their schemes illegally?
- The international experience with regulating similar schemes.
- Whether national and/or provincial authorities can effectively regulate the scheme.
- Whether the required inspectorate capacity exists, or can be developed, in order to monitor and oversee new schemes. And the cost of developing this new capacity.
- Whether the operators of illegal schemes believe that the gains from regulation—both financial and social—exceed the losses (or costs) that they will incur once they operate as legal businesses and comply with all regulatory expectations.

## 5.3 POSSIBLE APPROACHES FOR SOUTH AFRICA

The *Impact of Illegal Lotteries* study usefully identifies four possible approaches for South Africa, namely:

- **To do nothing**, and continue to incur the costs of the illegal lottery industry in the form of stagnant National Lottery ticket sales and contributions to the NLDTF. Noting the difficulties involved in prosecuting illegal lotteries, and the delays in developing appropriate legislative responses to such lotteries, the study concludes that this scenario is highly possible.



- **To enforce** the prohibition of illegal lotteries, through adjustments in the Lotteries Act and the developing enforcement capacity. Whilst noting that this is a likely outcome, the study again notes the difficulty and time-consuming nature of legislative amendment, as well as the likely delays in developing associated enforcement capacity, to take effective action against such schemes.
- **To regulate**, by offering illegal operators licenses to continue operations, and extracting a commission, fee, or share of revenue from the operators. This scenario is only plausible when illegal operators see a benefit in operating legally. Why would unlawful lottery operators choose to comply under this scenario when they have been getting away with non-compliance? In economic terms, higher transaction costs may discourage compliance.
- **To enforce and compete**, whereby the NLC and other enforcement agencies use a combination of enforcement and market-based approaches, where the NLC develops and operates alternative games which mimic the illegal lotteries and induce customers away from illegal operators.

These options, which guide the discussion that follows, are summarised in the table below.

Scenario	Approach	Rationale
1. Do nothing	<p>Continue as normal with the uncertainty between the National Gambling Act and National Lotteries Act, while the provincial gambling inspectors continue to be unable to enforce or prosecute illegal lottery operators.</p> <p>The NLC can expect to continue to incur the costs of the illegal lottery industry in the form of stagnant National Lottery ticket sales and contributions to the NLDTF.</p>	<p>The gap between policy amendments (5 years) means that the next revisions and amendments that can be made to the Lotteries Act will only come into effect in 2018 and beyond.</p> <p>Solving the issue of unlawful lotteries through legislative action is unlikely, and this scenario is therefore highly possible.</p>



Scenario	Approach	Rationale
2. Enforce	<p>To make adjustments to the National Lotteries Act, in terms of removing the ambiguity on the definition of an illegal lottery (as per activities on the ground) and the powers vested in lottery inspectors, which currently have no powers to enforce the National Lotteries Act.</p> <p>Also, in order to overcome uncertainty regarding the exact definition of unlawful lotteries, such as fahfee and other associated games that meet the definition of a lottery, such definitions must be clearly defined in the legislation.</p>	<p>In terms of a regulatory approach to illegal lotteries—where fahfee and other unlawful lotteries remain strictly prohibited—this is the most plausible option.</p> <p>However there are two concerns:</p> <ol style="list-style-type: none"> <li>1. That NLC-employed inspectors will be able to attain powers under the CPA, as with the provincial gambling board inspectors.</li> <li>2. There will be a long lead time before the necessary amendments needed to bring the legislation in line with policy can be affected in the Lotteries Act.</li> </ol> <p>Following the enforcement approach solely where only legislation is used as a tool to combat unlawful lotteries may therefore not be effective or efficient until the legislative framework can be properly addressed in the future.</p>

Scenario	Approach	Rationale
3. Regulate	<p>To offer illegal operators licenses in order to continue operations. This could take the form of various approaches, for instance fahfee operators could be offered licenses to operate on specific routes/areas/provinces/ The NLC can then receive a commission/ fee/share of revenue from the operators.</p> <p>In other instances, bookmakers could be licenced to take bets on the outcome of the National Lottery, allowing the Commission to extract rents from this on-going activity. The existing compliance and enforcement framework, operating primarily through provincial licensing authorities, could be used to monitor compliance.</p> <p>The same can be used for totalisators.</p>	<p>This option may be particularly attractive as it is seen that the NLC, due to its own constraints and loophole with the existing legislative framework.</p> <p>Enforcing the law with an inefficient framework on the one hand and highly organised criminal network on the other will be an extremely difficult exercise, where the costs of implementing enforcement will probably outweigh the benefits.</p> <p>Offering the illegal lottery operators a chance to become licenced, such as tax amnesty used to coax tax dodgers to comply, may be a wise approach. This scenario is plausible but unlikely to be effective due to the nature of illegal lotteries – why would lawful lottery operators choose to comply under this scenario when they have been getting away with non-compliance?</p>



Scenario	Approach	Rationale
<p>4. Enforce and compete</p>	<p>This approach is a hybrid enforcement approach, where the NLC uses two separate but complementary mechanisms to combat and prohibit illegal lotteries and other activities in the country.</p> <p>The one tool is the enforcement tool as stated above. The second is a market-based approach where the NLC in coordination with the NGB and provincial gambling boards as well as other stakeholders embarks on a market campaign to both educate the people about the consequences of organised crime facilitated through illegal lotteries, as well as to provide an alternative game of chance to the illegal lottery, one which maintains (read mimics) the strengths of the illegal lottery to keep the customer happy. In other words, replace fahfee with a game operated by the NLC, which covers the traditional advantages and modus operandi of fahfee.</p> <ul style="list-style-type: none"> <li>• frequency of games</li> <li>• lower ticket prices and entry requirements</li> <li>• accessibility and operation in rural areas</li> <li>• higher rewards and better chances of winning</li> <li>• use of existing networks to build relationships between runners/operators/punters</li> </ul>	<p>The main drawback with the regulatory option is that illegal lotteries most often form part of larger criminal syndicates, which are also involved in other illegal and criminal activities. It is unlikely that they will, therefore, be willing to accept regulation, given their involvement in other crimes.</p> <p>This is perhaps the most robust approach to combating and prohibiting illegal lotteries, where the dual strengths of the law and of the market are combined to fight illegal lotteries in a multi-dimensional manner.</p>

Source: NLC 2016: 66-67.

## 6 ASSESSMENT OF EACH SCHEME TO DETERMINE THE FEASIBILITY OF REGULATION WITHIN THE AMBIT OF THE LOTTERIES ACT

In this section we assess each of the major illegal lottery schemes with a view to determine the feasibility and viability of regulation. On this basis, we make recommendations as to the most appropriate way to address these schemes.

### 6.1 FAHFEE

Fahfee has historically been owned and run by South African born Chinese operators who settled in South Africa before 1994. This appears to have changed since 1994, with the entry of new immigrants from Mainland China, many of whom are believed to have connections with organised crime. Many fahfee operations controlled by New Chinese immigrants resemble organised businesses, with a central controlling office, computer based accounting systems and permanent staff, as opposed to the small family-run operations of the past.

Fahfee enjoyed considerable popularity throughout the twentieth century. Although never widely played in the white community, there is evidence that it was widely played by working class members of the coloured and Indian communities.

Fahfee is embedded in the culture of everyday life in South African black communities, and is particularly popular amongst low-income gamblers in Gauteng (SARGF 2009: 30, 41), Mpumalanga, and Limpopo provinces. National prevalence studies suggest that fahfee is currently played by around 2.4 percent, and is the preferred gambling mode for 1.6 percent, of the general adult population (NGB 2009a: 8, 16).

According to our *Impact of Illegal Lotteries* study (NLC 2016: 23-24), R725.57 million rand is spent annually on fahfee, the bulk of which is spent in Gauteng (R380.14 million), Mpumalanga (R101.35 million), and Limpopo (R101.60 million) provinces.

Fahfee players are disproportionately middle aged and elderly working class African women (NGB 2013: 39-40).



## 6.1.1 LEGAL STATUS

Fahfee involves the sale of tickets in exchange for a chance to win a prize, and the selection of a number or symbol which determines who is entitled to a prize. This clearly fits the definition of a lottery in South African law.

Prior to the legalisation of gambling in the 1990s, fahfee was treated as a lottery offence—see, for example, *The State v Chan* 1962(1) SA 735 TPT.

Today fahfee is prohibited in terms of the *Lotteries Act* 57 of 1997, and persons who organise or participate in the game can be prosecuted in terms of Sections 57(1)(a)(b) and 57(2)(g) of this Act.

Fahfee is also considered unlawful in terms of Section 7(a) of the *National Gambling Act* 7 of 2004, as well as similar provisions in various provincial gambling acts, which prohibit the offering or participating in of any activity the outcome of which depends on a contingency related to an event which is prohibited in law.

The prosecution of offenders under gambling legislation has allowed fahfee operators to exploit ambiguities in the wording of provincial gambling acts. In Limpopo province, where the vast majority of prosecutions occur, for example, Section 77(b) of the Northern Province Casino and Gambling Act (Act No 4 of 1996) prohibits people from permitting “*any gambling activity at any place under his or her control or his or her charge*”. As fahfee almost always occurs in public spaces over which fahfee operators have no control, defence attorneys have often successfully argued that the Act does not apply to fahfee.

## 6.1.2 MODUS OPERANDI: HOW THE GAME IS PLAYED

Fahfee is a variation of a single-number lottery where players choose a number between 1 and 36 in the hope of winning a pay-out of 27 to 1 plus the return of the original bet. Number selection is often guided by dreams.

Fahfee is primarily played at “spots” or “banks”, where local players meet to place bets. Operators or “bankers” run “routes”, which consist of a number of “banks”, which they visit daily.

Operators are assisted by local bookies, called “runners”, who collect bets from players on their behalf. When operators arrive at a bank they collect the bets from the runners, and then announce the winning number. The bets are then inspected, and successful players paid out.

The operators themselves select winning numbers. Records of recent selections are displayed on boards (“madodai”) at banks, which are intended to “guide” player selection by encouraging an illusion of pattern.

Each bank operates according to rules determined by the operator. In its most basic version, all 36 numbers are played. In other versions, the numbers from the last two draws are excluded. With these exceptions, fahfee is an extraordinarily simple lottery to play and manage.

In most banks, limits are placed on bet size, but operators will sometimes include an unlimited-bet bank in their route to give players a wider choice.

Fahfee bets are typically relatively small, usually in the R2-R5 range, and seldom more than R20 (NGB 2013: 39-40). This makes fahfee appealing to its target market and, whilst similar in price to the National Lottery (R5 for a Lotto ticket, and R2 per board in Sportstake 13), considerably more financially accessible than other forms of legal gambling.

Fahfee “draws” occur frequently, usually twice a day on weekdays. Importantly, draws happen directly in front of players, which gives fahfee an “instant gratification” appeal which is highly valued by players.

### **6.1.3 KEY ACTORS: OPERATORS**

Although there are a handful of black operators, the vast majority of operators are of Chinese origin. One significant consequence of this is the fact that *ownership and control rests with community outsiders, with almost no social and limited economic links to the communities in which fahfee is played*. Thus fahfee contributes to a net out-flow of capital from black South African townships, which generates a degree of resentment in some quarters.

Compared to other illegal community-based lotteries, the “outsider” status of fahfee operators is unique. In inter-war New York and Harlem, where the most well-known numbers games were played, entrepreneurial black operators, the so-called Policy Kings, used illegal lotteries to leverage capital for a wide range of black owned community businesses, from hotels to banks.



During the segregation era, illegal lotteries were a hugely significant vehicle for black economic advancement (Haller 1991; Thompson 2006; White et. al. 2010). Similarly, in Brazil, a wide range of local business concerns, often connected to the Carnival, profit from the Jogo do Bicho or “animal game”, a popular illegal numbers game played in the streets of Brazil (Chazkel 2011).

Fahfee operators complain about police harassment, and are regularly forced to pay bribes to law enforcement officials in order to continue operating routes. Not having to pay bribes is a significant factor in favour of legalisation.

South African born Chinese operators complain bitterly about the threats posed by “New Chinese” immigrants. One operator interviewed spoke at length about the connections between the New Chinese and organised crime. In his own case, he was shot and was forced to surrender his route to a “New Chinese” gang, an experience he believes is all too common around Johannesburg and Pretoria.

It is alleged that some “New Chinese” operators are undocumented immigrants, who use fahfee as a springboard or a supplement to a variety of other criminal activities, including perlemoen smuggling, rhino horn poaching, drugs, and prostitution.

Historically, because fahfee routes were family owned and run, they were relatively small-scale business operations. There was limited room to expand, or to develop value add on products.

It is widely claimed that the entry of “New Chinese” immigrants has substantially altered this. Criminal syndicates operate from dedicated premises, and run multiple routes. It is believed that syndicates bring cheap labour over from China, and employ this labour in a variety of illegal activities.

“New Chinese” operators often do not speak much English, and are dependent on translators.

The South African born Chinese community cultivated very close relationship with black punter communities, and enjoyed a very strong relationship of trust with players. “New Chinese” operators appear to battle to maintain this trust relationship.

## 6.1.4 KEY ACTORS: RUNNERS

Runners usually live in the communities in which banks are located.

Runners process bets on behalf of operators, and serve as intermediaries between the operator and the community. This is partly for logistical reasons, and partly to shield operators from the police.

Runners are remunerated in different ways. Some operators pay a basic stipend, whilst in other cases they rely on a commission on winning bets. They do not have any job security, or guaranteed income.

Operators will sometimes employ a head runner, who will assist with the overall management of the route. In some cases, operators will also employ a driver who is able to speak English as well as local languages, who will interact with runners on their behalf.

Head runners also assist with the initial establishment of routes, advising prospective operators about local demographics and the suitability of locations for fahfee banks.

## 6.1.5 KEY ACTORS: PLAYERS

Fahfee is embedded in community structures, and is part of everyday life for most of the working class black people who play the game.

Players appreciate the social aspects of the game, and value the chance to meet their friends regularly (sometimes twice daily) to discuss number selection and strategy. Fahfee play is a collective experience, with associated rituals and gaming culture. The National Lottery, by contrast, is a largely individual game.

Fahfee players generally have considerable faith in the integrity of the game of fahfee, and of number selection in particular. Players see the Chinese operator arrive, and watch him announce the lucky number before opening the bags in which their bets have been collected. Although simple, players trust this system. By contrast, despite the sophisticated compliance requirements governing number selection in the National Lottery, fahfee players often do not trust the National Lottery, and complain that is rigged.



## 6.1.6 ARCHITECTURE OF THE GAME: HOW IS FAHFEE STRUCTURED AS A SCHEME

In this section we discuss seven key aspects of the game of fahfee, namely:

- i. Route identification and ownership
- ii. Management of routes
- iii. Management of player disputes
- iv. Number selection
- v. Return to player
- vi. Record keeping
- vii. Taxes

These aspects are all peculiar to the architecture of this particular community based informal lottery, and necessarily inform our recommendations for an appropriate regulatory structure for fahfee.

The success of regulation will depend on our ability to address these key aspects.

### ***6.1.6.1 Route identification and ownership***

Fahfee is unique, in that there is no central body or organisation regulating operators or routes, although this is starting to change with the entry of “New Chinese” operators connected to organised crime. Although some ticket sales were historically made through fixed points, usually Chinese run shops, this happens less frequently today. For the most part, entrepreneurial individuals work with a member of the local community to investigate the viability of potential fahfee routes, and to set up routes in preferred locations. As long as the proposed routes do not encroach on any existing route, the operator is free to establish a new route where and when they please.

In the event that there is a dispute between operators over routes, these are sorted out informally within the Chinese community. The fear of losing honour or offending the community is a powerful informal regulatory constraint amongst South African born Chinese operators.

This form of informal self-regulation works very well amongst South African born Chinese operators. It appears to have considerably less relevance to “New Chinese” operators, who have less incentive to cooperate with operators who are not part of their syndicate, and are more prone to settle disputes violently.

In theory, there are no obstacles preventing non-Chinese people from establishing their own fahfee routes. In practice, players associate fahfee with “the Chinaman”, and are often suspicious of local black operators.

People who establish routes may pass these onto their spouses or children. However, because fahfee is illegal, owners have no secure property rights over routes, and are not easily able to sell these or leverage their ownership rights to access credit.

### ***6.1.6.2 Management of routes***

Fahfee operators usually set up and own between one and three routes. The head of the family will oversee the general operation, and run one of the routes themselves. Family members run the remaining routes.

There is no external body currently capable of overseeing the management of routes. Families do not permit outsiders, even from within the Chinese community, to play a role in the management of the routes that they own.

This applies equally to South African born Chinese and “New Chinese” operators.

### ***6.1.6.3 Management of player disputes***

Operators have sole discretion over their operations, and players are not able to appeal their decisions. Because fahfee is illegal, players who feel cheated cannot turn to the police, as this would expose their own criminal conduct.

As with other forms of gambling, disputes between players and operators often arise when it comes to interpreting bets. Players sometimes fail to indicate their preferences clearly on betting slips, often by placing their cross outside of the preferred box, or overlapping between two boxes, much like an ambiguous or unclear bet placed on a roulette table.

In such cases, the operator is entitled to refuse to honour a win. If the player is well known to the operator or runner, and the amount is relatively small, operators will often interpret the bet in the player’s favour, to encourage customer loyalty and a relationship of trust.



The discretionary powers of the operator deserve emphasis here. Whilst the runners, like the croupier in roulette, should theoretically check all bets prior to submission, in practice this does not always happen in fahfee, and incorrect or ambiguous bets are occasionally placed. The operator, with an obvious interest in minimising the number of winning bets, clearly faces a massive conflict of interest when interpreting disputed betting slips. When betting slips are not accepted, and when operators refuse to pay out, this is known as “bet return”.

The number of disputes appears to have increased with the entry of “New Chinese” operators, who prioritise short-term profits over developing relationships of trust with players. Players and operators interviewed for the report accuse “New Chinese” operators of manipulating decisions to avoid having to make pay-outs, especially on larger bets.

Sometimes operators do not have enough cash to pay out on all winning numbers. This occurs when there are unusually large individual wins, or when an unexpectedly large number of players select the lucky number. In such cases, operators defer payment for a day or two, a process known as “carry over”. There is no mechanism to enforce payment.

#### **6.1.6.4 Number selection**

Traditional lotteries have elaborate procedures to insure the integrity of number selection. The numbers selected in the National Lottery in South Africa are carefully audited to ensure that they are completely random, and that neither the operator nor the player derives any unfair advantage from advance knowledge of the numbers chosen.

In fahfee, by contrast, the operator himself selects the winning number for each bank along his route. This is done in a way that is intended to ensure fairness. In the first instance, the runners collect bets and bring them to a central point. Depending on the size of the bank, there may be different layers of runners collecting bets, which are placed in a bag before being handed over to the operator. The operator will announce the winning number, which he will have selected earlier (a process known as *num ju*) and only then will he open the bags and separate winning tickets.

This is vulnerable to criticism, as the operator is clearly not a neutral third party. Clearly, and they admitted this openly in our interviews, operators do not seek to generate completely random numbers. Instead, they keep records of previous player choices and try to guess which numbers are least likely to be chosen by the players at each particular bank along their routes. Strategic selection is as much part of the game as it is part of the business.



Interviews with players confirm that they are fully aware of this point (Louw 2018, pp. 125-26), and enjoy the battle of wits over number choice. This is part of the allure of fahfee, and adds considerable excitement to the game.

In short: players appreciate and enjoy the informal nature of number selection. This is one of the reasons why they like fahfee, and choose to play fahfee rather than participate in the state lottery or other forms of gambling.

#### ***6.1.6.6 Return to player***

Fahfee has a fixed-odds pay-out of 27 to 1 plus the return of the original stake. When it is played with all 36 numbers, this produces a house edge of 22.2%, or a return to player of 77.8%. When the last two numbers are excluded, this improves slightly to a house edge of 17.81%, or an 82.19 percent return to player. In addition, punters usually pay hefty commissions on winning bets.

Compared to casino gambling, these are unfavourable odds for players. Roulette has a house edge of only 2.7%, and Baccarat is 1.06%.

Whilst the return to player is extremely low, the chances of winning something (albeit a small win) at fahfee are considerably greater than the chances of winning a much bigger prize in most other lotteries. In the National Lottery, the odds of choosing all six numbers required to win the Lotto jackpot are 1:20,358,520, and the odds of choosing 2 numbers plus a bonus number, which is the most likely lottery win, are 1:95.6.

Although gambling regulators would ordinarily frown upon the low return to player—certainly, no casino would be allowed to offer these odds—it would appear that players accept the return to player in fahfee, because they believe they have a greater chance of winning something than they would in the state lottery. In this sense, there is a similarity between fahfee and the fixed odds bets on the outcome of a lottery offered by bookmakers: these are both popular alternatives to the state lottery precisely because players have a better chance of winning small prizes on more likely outcomes (i.e. selecting just three of the winning six or seven numbers).



### **6.1.6.6 Record keeping**

Some operators, particularly “New Chinese” operators, employ sophisticated computer-based accounting systems.<sup>1</sup> However in most cases fahfee is run in an informal manner, and operators keep little more than handwritten records of the numbers chosen and the amounts bet at each bank. From materials seized in police raids shown to us, these transactions are recorded cryptically, or encoded to protect the operator, and are difficult for non-Chinese speaking outsiders to interpret. In this sense, fahfee is typical of many business operations in the informal economy, sustainable and oftentimes lucrative but run on the basis of trust and limited formal oversight and control. The transition to sustainable formal business practices is hampered by this dependence on informal recordkeeping and informal business practices, policies, and procedures.

### **6.1.6.7 Taxes**

Fahfee is a cash business, and operators do not pay VAT or tax on their profits, and do not contribute to the NLDTF.

Operators pay regular small bribes to police officials, either to avoid arrest or to get out of jail. This is a long-standing feature of the game.

Operators keep records of bribes paid, which they regard as a cost of doing business.

Our interviews with fahfee operators confirm that they bitterly resent having to pay bribes, and that they believe that police solicit more bribes more frequently now than ever before. Whilst most shrug their shoulders and regard this as a cost of doing business in the illegal economy, some clearly hope that legalisation will allow them to do business without having to constantly look over their shoulder and find ways to avoid being arrested.

It is not clear what the aggregate cost of paying bribes is, or whether this approximates the compliance costs operators would incur if they were forced to register as small businesses, pay tax, and make contributions to the NLDTF.

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<sup>1</sup> See National Director of Public Prosecutions v Nuanjan Liu & others. Case no. 7942/2007. <<http://www.saflii.org/za/cases/ZAGPPHC/2012/271.pdf>>

## 6.1.7 THE INTERNATIONAL EXPERIENCE WITH SIMILAR LOTTERIES

Informal lotteries are common in many countries, and authorities regularly face the choice of having to stamp these out (usually to protect a state owned lottery or to regulate them) In this section we consider, very briefly, two examples, in the acronym USA and India, where the approach has been to prohibit informal lotteries. Thereafter we consider in more detail recent proposals to legalise and regulate an informal lottery in Brazil.

### 6.1.7.1 United States of America: Numbers games or Policy

The most well-known informal lotteries are perhaps the numbers games, or “Policy”, as they were often called, widely played in black communities in many US cities in the inter-War and immediate post-War period. In the same period, Chinese migrants introduced their own lottery games, like Pák Kòp Piú (white pigeon ticket), Tsz’ Fa (word blossoming), and Gee Far, which was structurally almost identical to fahfee (on these lotteries, and their similarity to fahfee, see Louw 2018b). The widespread takeover of numbers operations by the Italian mafia make it hard for the authorities to ignore these games, and by the 1960s most numbers rackets had been closed down, largely because of a broader crackdown on organised crime, rather than gambling-specific concerns (Haller 1991; Thompson 2006; White et. al. 2010).

In 1964, an estimated 100,000 numbers runners worked in New York, with 8,000 arrests annually. Today numbers games are seldom played and, although the government cracks down on illegal gambling generally, almost no one is ever arrested for running numbers (Wilson 2013).

In many US states, some form of legal lottery has been introduced in the past half century. This has undermined significantly the market for “Policy”. The combination of this, coupled to the crackdown on illegal numbers games, means that the US approach, in the terminology adopted in the *Illegal Lotteries Report*, can be described as either to **enforce** or to **enforce and compete**.

### 6.1.7.2 India: Matka

Gambling is regulated at a state level in India. With the exception of betting on horse racing, some games of skill, and the lottery, most forms of gambling are prohibited. Despite such prohibitions, there is a growing illegal gambling market, driven in large measure by underground sports betting. Matka is one such game, a popular illegal lottery, in which players bet on the face value of three cards drawn randomly from clay pots (called *matka*).

Bets are placed on either 2- or 3-digit numbers, with a payoff of up to 80 times the amount wagered (Benegal 2012, p. 2065; Dandekar, 1970). Most Matka gambling occurs in the state of Maharashtra.

Matka has always been associated with organised crime, and police have cracked down on the game because of these linkages. The fact that many overseas Indians play Matka, with bets being placed from as far afield as London and Dubai, raises serious questions about illegal money flows and money laundering.

At its peak in the 1980s and 1990s, it was estimated that around \$47 million was spent on Matka each month, with around 2,000 big and medium-sized bookies in Mumbai alone. A major police crackdown on organised crime in 1995 reduced Matka ticket sales to an estimated \$16 million a month, with fewer than 300 bookies remaining in 2008 (Parmar 2008).

A second factor driving the reduced popularity of Matka is the spread of internet connectivity, which has facilitated an unprecedented explosion in sports betting, especially on cricket.

In the terminology adopted in the *Illegal Lotteries Report*, the Indian approach to illegal lotteries can be described as to narrowly **enforce** existing anti-gambling prohibitions, as much to combat organised crime as to protect the public from the dangers of illegal gambling.

### **6.1.7.3 Brazil: The Jogo do Bicho (Animal Game)**

The regulatory debates on the Brazilian illegal lottery, the Jogo do Bicho, are more nuanced, and provide a more interesting example for our present concern.

Brazil, along with Indonesia and Saudi Arabia, is one of only three G-20 countries that currently prohibit non-state providers of gambling products (Jobim and Williams 2017, 104). Although some forms of gambling were unbanned briefly in 1993, most prohibitions were reinstated within a decade. Numerous federal- and state-run lotteries are permitted.

In the past decade, several proposals to liberalise gambling have been debated in both the state and federal legislatures. Of particular interest here is the debate over the Jogo do Bicho or “animal game”, a wildly popular numbers game or lottery, with strong similarities to fahfee. Originating in Rio de Janeiro in the 1890s, the game was banned in 1946, five years after the banning of casinos, and remains illegal in terms of federal law, and in 25 out of the 26 states. Despite federal prohibition, the north-eastern state of Paraíba regulates the game.

The Jogo do Bicho is a lottery game, where players bet on the likelihood of a number being drawn. Each number is matched against a 25 possible animals, No. 1 being an Ostrich and No. 22 a Tiger. The winning number is derived from an agreed upon external eventuality, for example, the two digits of the daily state lottery. Up to 3 draws are held daily, with prizes up to 4,000 Reals (\$1,240) (for a comprehensive history, see Chazkel, 2011).

Although the game is more complex than fahfee, with many different types of bets and prizes, the basic structure is very similar. Tickets are sold by a network of runners or bookies, who place bets at fixed points throughout the city. Although illegal, ticket sales take place openly and brazenly, and are largely ignored by the police.

The amount of money involved in the Jogo do Bicho is staggering. A Special Commission set up in 2016 to investigate the legalisation of various forms of gambling estimates that half a million people are employed in Jogo do Bicho operations, with an annual turnover of \$12 million.<sup>2</sup>

The bicheiros, who control the Jogo do Bicho, have close links to a wide range of local business concerns, often connected to the Carnival, as well as to organised crime. Unlike fahfee, in which operators or bankers operate autonomously, the Jogo do Bicho has a relatively hierarchical organisational structure, with the top bosses based in Rio de Janeiro. This structure makes for more efficient organisation, but is believed to facilitate closer integration with a variety of other illicit businesses and with organised crime. Judges and politicians are accused regularly of receiving bribes and campaign financing from the bicheiros. In the 1990 elections, bicheiros in Rio de Janeiro went so far as to print names of the candidates that they supported on the back of betting slips. In exchange, politicians would ensure that anti-gambling laws were not enforced aggressively in their areas (Speck 2013, 63).

Many bicheiros have established their own bingo halls. Although not legal, these are tolerated in many cities, and are widely used to launder money (Jobim and Williams 2017, pp.108-09).

#### *The regulatory debate: the pros and cons:*

Lawmakers concerned about the criminal networks associated with the Jogo do Bicho have consistently argued against legalisation. At one extreme, Bill 3,629 was introduced in 2008 to specifically criminalise participation in the Jogo do Bicho, with its chief proponent suggesting that:

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<sup>2</sup> Câmara Dos Deputados, “Reportagem Especial. Legalização dos jogos no Brasil: arrecadação aos cofres públicos” [Special Report. Legalisation of games in Brazil: pros and cons], 09/05/2016.

“I have always maintained that the exploitation of the so-called game of the beast only appears to be harmless, but it is a criminal activity of extreme gravity. It integrates organized crime.”<sup>3</sup>

After then-president Dilma Rousseff vetoed 2015 legislation allowing for the liberalisation of sports betting, a Special Commission of the Regulatory Framework of the Games was established to discuss gambling legislation, as part of a larger response to the economic crisis in Brazil. The most recent proposals approved by the Special Commission are contained in Bill of Law 442/1991 and PL442/119, which are being debated in the Senate and the Chamber of Representatives respectively (Rohsler 2017, pp. 82-85). Both of these support the legalisation of land-based and online casinos, sports betting, bingo halls, and the Jogo do Bicho.

The main arguments in favour of legalisation mirror many of those discussed elsewhere in this report: controlled liberalisation is a better way to maximise revenues and protect players, both directly through taxes and indirectly, by bringing money out of the shadow economy into the formal economy, whilst reducing the threat of gambling as a front for other illegal activities.

In addition to the money spend on the Jogo do Bicho, many Brazilians gamble outside the country, increasingly via online platforms. The government estimates that \$3 billion leaves the country annually because of this. Legalising and regulating gambling is one way to try and keep monies lost to gambling inside the country. Furthermore, according to the President of the Legal Gaming Institute, Magno Santos de Sousa, the legalisation (of all sectors) would create four hundred and fifty thousand formal jobs.

In a Senate debate, lawmaker Mr. Pompeo de Mattos expressed this revenue maximising sentiment clearly:

“Latin America is full of casinos. And the Brazilians are going to play there [whether we like it or not]. We will [if we legalise casinos in Brazil] place them in tourist cities and allocate the funds collected, as well as those of the Game of Bicho, for health and education. Let’s educate our people and have money for health.”<sup>4</sup>

A year later, Mr. de Mattos went further. In language that could just as easily be used to support the legalisation of fahfee in South Africa, de Mattos added:

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3 Mr. Antonio Carlos Biscaia. Speech, Chamber of Deputies, 10/30/2008, Session 258.2.53. <<http://www.camara.leg.br>>

4 Mr. Pompeo de Mattos. Speech, Chamber of Deputies, 06/10/2015, Session: 146.1.55. <<http://www.camara.leg.br>>

“I also want to legalize and regulate the game of the animal, a game as old as the history of our Country and that is being played every day. No use trying to cover the sun with the sieve. It’s hypocrisy. Sorry for the expression, but those who do not understand it are hypocrites. The game of the beast does not depend on me, it does not depend on you, it does not depend on us, it is fact, it is real. ‘Ah, behind the game of the animal there is illegality.’ Of course, he’s not cool! ‘Ah, behind it comes corruption.’ Of course, because it is not regulated and regulated, it cannot be enforced. ‘Ah, there’s prostitution behind it.’ Of course, because it is not transparent, it is not objective, it does not submit to state control. ...

So let’s legalize the games in Brazil, so that they can be controlled, supervised, and that the money raised be reverted in favor of the poorest, poorest people, so that they have more health, more education and more quality of life. This I defend, I fight for it, with the conviction that I have. I think the way out of the game in Brazil is legalization. Let’s legalize, legalize, legalize!”<sup>5</sup>

How then should the Jogo do Bicho be regulated? In Mr de Mattos’ proposals, it is important to preserve the character of the animal game, and not change any key components— “The way it works: the bicheiro remains a bicheiro, the scorer is still pointing, the banker is still a banker. Whatever name they want, it will work the same way.” In this way, gambling as recreation activity makes provision for gambling as a space to promote economic development. The bicheiros, in short, will become both “bicheiros” and “micro entrepreneurs”.<sup>6</sup>

The Brazilian regulatory debate provides some useful ideas for the debate on regulating fahfee.

In the state of Paraíba, the only state in which the game is licenced, the Jogo do Bicho is regulated by the Lottery of Paraíba (LOTEP). Bankers are licenced as “lottery agents” by LOTEP, and are allowed to sell tickets via 15 authorised points across the state. Each point is taxed based on monthly turnover. Draws for the Jogo do Bicho take place daily in the LOTEP building, and winning numbers are released on official radio. In this way, regulators ensure that number selection is free and fair.

Proposals outlined in the Bill before the Chamber of Representatives (PL442/119) follow this general direction, supporting the idea of unlimited time licenses (as opposed to fixed-term licenses for other gambling modalities).

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5 Mr. Pompeo de Mattos, Speech, Chamber of Deputies, Session: 116.2.55, 05/11/2016. <<http://www.camara.leg.br>>

6 Mr. Pompeo de Mattos, Session: 116.2.55, 05/11/2016. <<http://www.camara.leg.br>>





To limit the growth of the industry to a smaller group of larger operators, states will have the right to insist on a minimum amount of paid up capital (the report suggests 5 million reais).

*Lessons/questions for SA:*

- The idea of a state/provincial level licensing, overseen by a “lottery agent” like LOTEPI. This can be coupled to municipal-level compliance requirements.
- The idea of state/provincial level determination and publication of winning numbers, to reduce operator discretion. In considering this, it should be remembered that the Jogo do Bicho has always involved some sort of centralised number selection, and never had different numbers for each bank/point, as is the case with fahfee. We would suggest that such centralisation would undermine the essence of fahfee, and reduce its appeal and viability.
- The processing of sales (made by a network of runners across a defined area) at central points, which are licenced and overseen by state/provincial regulatory authorities. From a regulatory point of view this is tempting, as it makes it easier to bring operations into the formal economy, and to monitor them for tax and other compliance reasons. We would suggest that it is unlikely to work with fahfee, as operators are far less organised and operate far smaller routes, along which they process sales in a decentralised way. Changing this would destroy the character and feel of the game, which we do not recommend doing.

## **6.1.8 THE FEASIBILITY OF REGULATING FAHFEE: PROS AND CONS**

At this point it is possible to identify and summarise the pros and cons of regulating fahfee. On balance, we believe that the positives outweigh the negatives, and that fahfee should be legalised and regulated.

### ***6.1.8.1 Legalising fahfee: arguments in favour (the pros)***

The eight strongest arguments in favour of legalising fahfee include:

### **(1) Indigenisation of gambling.**

Most legal gambling games as well as the National Lottery in South Africa offer variants of games developed in European and North American markets, with only minor adaptation to the South African market. Fahfee by contrast is a uniquely South African game, embedded in our history and cultural landscape. Legalising fahfee would honour this history, and help to promote the indigenisation of the South African gambling industry.

### **(2) Satisfy market demand, without overstimulation of new demand.**

Although illegal, fahfee is a popular game that has been played for over a century, despite attempts by successive governments to prosecute operators and fine players. The liberalisation of gambling in the 1990s and the introduction of the National Lottery do not appear to have diminished its appeal significantly.

Legalising fahfee would have limited real impact on the aggregate number of people playing lotteries, whether the National Lottery or fahfee. It would not run the risk of overstimulation demand for gambling; it would simply channel gambling that is currently illegal but widespread into a legal space. In so doing it would make it easier to monitor the negative impacts of fahfee, along with all other lottery schemes, and to mitigate the harmful effects thereof.

### **(3) Taxation and NLDTF contributions**

As it is run presently, fahfee does not benefit either the national or the local economy directly. Taxes and NLDTF contributions are not levied on profits, whilst fahfee contributes to a net outflow of capital from the communities in which it is played. From a public interest perspective, this is a lose-lose situation.

Allowing fahfee operators to register as formal businesses and to operate legally would mitigate the financial threat that they pose to the National Lottery and the NLDTF, and help contribute to the development of the economies in which fahfee is played. From a public interest perspective, this is a win-win situation.



#### **(4) Promote B-BBEE and transformation**

Small black operators have limited opportunity to enter the gambling and lotteries market. This is unfortunate, as fahfee is a relatively low cost, low risk game, which offers good returns for operators. It is an ideal vehicle to help promote B-BBEE and small business development in the gambling sector. Actual barriers to entry for black fahfee operators are high, as the game is effectively controlled by South African born and “New Chinese” incumbents.

The legalisation of an indigenous community based South African lottery like fahfee would allow for the entry of new black operators into a sector of the gambling industry that has previously been very difficult for them to enter. Along with indigenisation, this must be considered a very strong motivation for the legalisation and promotion of the game of fahfee.

#### **(5) Leverage economic opportunities**

Licensing fahfee routes would turn illegal assets into bankable assets, and would help leverage economic and social opportunities for small entrepreneurs. This would assist in the formalisation of the shadow economy, and contribute to township revitalisation.

#### **(6) Protect and empower existing operators**

Legalising fahfee would protect incumbent South African born Chinese operators, and reduce the threat of “New Chinese” operators taking over fahfee routes and drawing fahfee into a wider network of illegal criminal activity. In terms of the operators we interviewed, this is one of the single most important steps that can be taken to protect their livelihoods.

Once fahfee is legalised, operators would be able to report threats to the police, and expect protection from criminal syndicates.

#### **(7) Protect players**

Fahfee operators have tremendous powers over the operation and management of fahfee, and players have no real way to hold operators accountable and appeal their decisions. Legalisation would help ensure the integrity of the game by providing an independent regulatory structure to which players can appeal operator decisions, and which can ensure that the game is conducted in a fair and transparent way.

**(8) Reduce criminal influences.**

Unlike the case with similar games in America and India, fahfee is not explicitly tied to organised crime. Legalising fahfee would make it easier to oversee the practices of fahfee operations, and ensure that monies are brought into the formal economy in a transparent way. Links to syndicates and other criminal networks would be easier to detect and to prevent.

***6.1.8.2 Legalising fahfee: arguments against (the cons)***

The two strongest arguments against legalising fahfee include:

**(1) Ensuring compliance: why operate legally**

One reason why fahfee has flourished despite attempts to arrest operators and close down routes is the sheer difficulty of enforcement. Because the game operates in such an informal way, with no fixed premises, it is extremely hard for authorities to monitor and control fahfee operators. For as long as fahfee operators believe they can make more money more easily by operating illegally, it will be difficult to ensure compliance.

Many operators are likely to continue to operate illegally in order to avoid paying tax and making contributions to the NLDTF.

Even if some operators choose to operate legally, and apply for licenses, others are likely to continue operating illegally. It will be necessary for the NLC and other regulatory authorities to develop ways to effectively target and close down illegal fahfee operations.

**(2) Ensuring compliance: regulating informal businesses**

Experience in the informal economy, and with small businesses generally, suggests that transitioning into the formal, legal, economy is often difficult. Formal businesses, particularly in the gambling and lotteries sector, face considerable compliance requirements, which will necessitate elaborate record keeping and professional management. The jump from an informal cash-only illegal business to a tax and regulatory compliant business is a significant one.



## 6.1.9 FAHFEE: REGULATORY RECOMMENDATIONS

Fahfee operators should be encouraged to apply for licenses to run their businesses legally. As with the Jogo do Bicho in the state of Paraíba, operators should apply to a provincial-level licensing authority, operating under the auspices of the NLC. Fahfee operators who do not apply for licenses, or whose applications are unsuccessful, should be prosecuted.

In the terminology adopted in the *Illegal Lotteries Report*, we believe that fahfee should be legalised and **regulated**. Given the peculiar cultural and social character of the game, as well as the logistics involved in running diverse routes with multiple banks over large distances, we do not believe the market based approach, **enforce and compete**, through which the NLC develops its own variant of fahfee which mimics the traditional game in order to compete with existing operators, is appropriate. Fahfee is only viable in South Africa if it operates in much the same way as it has done for the past 100 years.

Our major recommendations for the legalisation of fahfee are as follows.

- It is recommended that the Lotteries Act be amended to legalise the game of fahfee.
- It is recommended that fahfee be regulated by the NLC, with licenses issued at a Provincial level. This will allow for greater sensitivity to local conditions – market saturation, location of routes and banks, B-BBEE empowerment targets, social impact, etc.
- It is recommended that voluntary fahfee operator associations be established, preferably at a provincial level, and that membership of an association becomes a condition of license. The association would play a key role in liaising between licensees and regulator, and in helping to oversee the operations of licensees.
- It is recommended that the NLC explore various strategies for the licensing of fahfee operations. These strategies, which might be pursued in parallel or separately, could involve the issuing of the following types of license:
  - a. Individual licenses: The first strategy would allow individual fahfee operators to apply for up to three fahfee routes, with a maximum of 36 spots along each route, which they would operate in their own name, or as small proprietors. This route is particularly appropriate for existing operators, and would allow them to legalise the majority of existing fahfee routes.

- b. Fahfee route operator licenses: The second strategy would allow small companies to tender for up to thirty fahfee routes, with a maximum of 36 spots along each route. These could then be sub-licensed to up to ten individual operators, who would operate these routes under a shared management and revenue sharing agreement with the primary licensee. The holder of the route operator license would be responsible for setting up and training new operators, and assisting them to comply with all relevant laws. This strategy is analogous to the route operator strategy employed by the Limited Pay-out Machine (LPM) industry, and is particularly appropriate for the development of new fahfee businesses, and for promoting transformation within the industry. This route is probably the easiest way to promote transformation and license new non-Chinese entrants.
  - c. Alternatively, licenses could be issued via provincial fahfee operators associations. The NLC would issue the license, on the recommendation of the association, who would be responsible for assisting applicants to apply, and the basic vetting of applicant suitability. Responsibility for probity checks would rest with the NLC. This route is likely to have the greatest buy in from Chinese operators.
- It is recommended that fahfee route operator licenses be offered to new entrants to the fahfee sector, in areas where there are few if any established routes, only. This is in order to maximise the opportunity for new business development and small black business empowerment, and to prevent the sector from being taken over by large existing gambling operators. This strategy should be adjusted at a provincial level, once the market appetite for such licenses has been determined.
  - It is recommended that license fees be kept at a minimum in order to encourage compliance. This can be reassessed once the demand for licenses has been determined.
  - It is recommended that fahfee operators would have to undergo a probity check, the manner and form of which should be prescribed by the NLC. All probity reports should be filed in a national probity register, to be developed and maintained by the NLC.
  - It is recommended that the number and size of fahfee licenses be determined at a provincial level and reviewed on a regular basis, once the market appetite for such licenses has been determined.



- It is recommended that B-BBEE empowerment targets are set at a provincial level, and that the issue of licenses is in accordance with the Broad-Based Black Economic Empowerment Act, 2003 (Act 53 of 2003) as amended, as contemplated in the applicable sections and the Codes. Particular attention needs to be paid to encouraging black South Africans to apply for licenses to operate fahfee.
- It is recommended that the NLC develops capacity at the provincial level to oversee the licensing of fahfee, as well as the adjudication of all disputes between players and operators. Players need to have access to an independent third party to whom they can refer queries and complaints about all aspects of the game. This includes adjudication over disputed bets.
- It is recommended that the current system of number selection, in which operators themselves rather than neutral third parties, choose numbers be retained.
- It is recommended that the current system of decentralised ticket-sales, in which operators take bets at demarcated “banks” along their routes be retained. We do not support a shift to centralised ticket-processing points.
- It is recommended that the current odds, pay-out, and house edge, in fahfee schemes be retained. This should be monitored carefully, and adjusted on the basis of a fuller understanding of the actual amount spent on fahfee.
- It is recommended that operators be required to identify and display prominently any numbers excluded from a draw (i.e. the last two numbers drawn) to prevent player selection of “dead numbers”.
- It is recommended that operators be required to display prominently acceptable bet size or denominations, as well as any limitations on bet size.
- It is recommended that fahfee operators be allowed to advertise and promote the game of fahfee as well as their specific fahfee routes and banks. This should be subject to the same sumptuary limitations and restrictions that apply to the advertising of the National Lottery.

- It is recommended that both a saturation study and a social impact assessment be conducted after three years of legalisation. This study should inform the Minister and the NLC, and be used to set limits to the further issuing of licenses, if required and appropriate. The legalisation of fahfee cannot be allowed to over stimulate demand for gambling or contribute disproportionately to problem gambling.
- Getting fahfee operators to convert from a cash only business, where taxes are seldom if ever paid, to become formal registered tax paying businesses, will be extremely difficult. A number of options might be considered to facilitate this process. In our view, the simplest way to do this would be to find ways to control the printing and distributing of betting slips. If the national and/or provincial regulator takes over the responsibility for printing betting tickets, these could be sold on to fahfee operators at a set price. The money paid for the book would cover all relevant gambling taxes, including NLDTF contributions. The operator would make his or her profit selling lottery tickets from these books, and would keep all profits from fahfee draws. This would simplify the cost of collecting taxes.
- Operators should pay personal income taxes in the same way and on the same scale as any other person in South Africa.
- It is recommended that fahfee licensees contribute a reasonable amount towards the NLDTF. Such amount will be determined by the Minister, communicated to license holders by way of notice, from time to time, as contemplated in the Lotteries Act. As with tax rates generally, the amount should be kept low in the beginning to help ensure compliance, and monitored as we gain better insight into the actual size and strength of the fahfee economy.
- It is recommended that fahfee operators who, for whatever reason, continue to offer fahfee without a license, be prosecuted. Voluntary fahfee operator associations could assist to identify unlicensed operations.
- The NLCs inspectorate needs to be improved, resourced, and empowered, both legally and administratively, to ensure that cases can be investigated and prosecuted without significant additional involvement of the already overcommitted South African Police Services.
- It is recommended that prosecutions be pursued in terms of the Lotteries Act, as opposed to Provincial Gambling Acts. It is generally easier to obtain a conviction under the Lotteries Act than under Provincial Gambling Acts.





## 6.2 BOOKMAKERS ACTIVITIES: FIXED ODDS BETTING

Many licenced bookmakers offer fixed odds bets on the outcome of existing lottery schemes, including the National Lottery and various international lotteries. This is variously described as “numbers betting”, “lottery betting”, a “parasitic lottery”, or a “synthetic lottery”.

This new type of bet has proved to be very popular in gambling jurisdictions throughout the world, in both developed and developing countries (Chung and Hwang, 2010). South Africa is no exception to this trend. In addition to the wide range of product offerings, numbers bets offer punters a range of massive potential jackpots, as well as the more realistic possibility of smaller wins for selecting three or more correct numbers. Pay-outs on these smaller wins are generally higher than they would be in the National Lottery, which attracts players away from the National Lottery.

The popularity of numbers betting has had an adverse effect on the NLC’s revenue. We estimate the cost to the NLC to be R531, 38 million rand annually, with a loss of R143, 47 million rand annually to the NLTDF (NLC 2016: 8). Bookmakers in Gauteng are reported to make around 60% of their revenue from numbers betting.

The issue that the NLC faces here is that the Provincial gambling regulators have licenced numbers betting for many years. We consider this to be in direct contravention of Sections 56 and 57 of the Lotteries Act, and therefore consider these schemes, as they are presently licenced and operated, to be illegal lotteries.

### 6.2.1 MODUS OPERANDI: HOW THE GAME IS PLAYED

There are more than 435 operational bookmaker outlets across the country. Betting on the outcome of the National Lottery and foreign lotteries occurs at both the registered premises of the bookmaker, telephonically, or, increasingly, online.

Typically, punters place bets by filling in a ticket slip. More commonly, punters place bets verbally, which are immediately loaded onto the betting system. A receipt is printed, similar to the National Lottery and other associated schemes, which details the date, time, place, numbers selected, and the total value of the bet. Punters use this receipt to check whether they have won or claim their winnings once the draw has taken place.

Draws for betting on the outcome of the National Lottery, international lotteries, and in-house lottery games, are either connected to official draws, which usually takes 2-3 times per week in the case of the National Lottery and international lotteries, or weekly, as in the case of the in-house lottery games.

Punters have a variety of options to choose from in terms of betting on the outcome of the lottery. This can include for instance:

- Betting on the total value of the balls that are drawn, where each total category has different odds attached to it;
- Betting on whether the total value of the balls that are drawn are odd or even;
- Betting on individual balls;
- Betting on the value of the bonus ball;
- Betting on whether the individual balls drawn are above a certain threshold or below (i.e. below 20);
- Betting on number groups; and
- Betting on the number of the first and last ball to be drawn.

These bets are available on official lotteries that include the following:

- National Lottery and Powerball on South Africa;
- UK National Lottery;
- Irish Lotto;
- Greek Lotto;
- Italian Lotto; and
- Spanish Lotto. (NLC 2016: 25)

Numbers betting is not restricted to the placing of bets on the outcome of existing state lotteries, and can be based on almost any eventuality. In South Korea, for example, there is a very popular sports lottery, which offers odds on the outcome of the final scores in English Premier League soccer matches. This product is offered alongside a variety of other lottery bets, which offer odds on a variety of different state lotteries (Chung and Ho: 2010).



### **6.2.1.1 Taxation**

Bookmakers are currently taxed by provincial regulatory authorities, at rates determined on a provincial basis. Whilst these rates have remained stable for some time, some provinces are seeking to raise these. Bookmaker associations are contesting such attempts.

### **6.2.1.2 SARGF contributions**

Bookmakers, like all other hard gambling licensees, make a voluntary contribution of 0.1% of Gross Gambling Revenues (GGR's) to the South African Responsible Gambling Foundation (SARGF). This money is used to monitor and mitigate the harmful effects of gambling in South Africa.

### **6.2.1.3 Transformation**

The bookmaking industry has, over the past decade, moved from an industry centred on individuals to one dominated by larger bookmaking companies with multiple licenses across the country.

Bookmakers are rapidly moving into an online space, which complicates the provincial regulation of their product offerings.

Transforming the bookmaker industry remains a challenge, which has been addressed unevenly by provincial gambling regulatory authorities.

## **6.2.2 LEGISLATION**

The relevant legislation is the Constitution, the Lotteries Act and Regulations and the Lotteries Amendment Act, the National and Provincial Gambling Acts, and the National Gambling Amendment Bill.

Fixed odds betting is currently authorised by provincial gambling legislation. For example, "Lotto Star", probably the most well-known bookmaker offering numbers bets, is licenced under the Mpumalanga Gambling Board. As Lotto Star accepts the placement of online bets, it effectively operates at a national level.

Although provincial legislation makes provision for bookmakers to offer fixed odds betting on eventualities, it does not make provision for bookmakers to offer fixed-odds betting on the outcome of lotteries. Section 55 of the Gauteng Gambling Act 4 of 1995 says that the only form of betting permitted by a bookmaker's licence is "fixed odds bets on sporting events". Section 1(1) defines a "sporting event" as "any ball-game, race (including a race involving vehicles or animals) or any other athletic or sporting contest, competition, or game, including a beauty contest, usually attended by the public". This clause does not include a lottery in its definition.

In our view, this means that bookmakers may not offer fixed odds bets on the outcome of either the National Lottery or any other local or international lottery.

### 6.2.3 THE NATIONAL GAMBLING AMENDMENT BILL, 2017

Clause 2 of the National Gambling Amendment Bill, 2017, addresses any possible regulatory confusion by amending the definition of permissible "Bets and Wagers" in Section 4 of the National Gambling Act, 2004. The amendment, indicated in the highlighted portions of the extract cited below, clearly makes it impossible for provincial gambling authorities to continue licensing fixed odds bets on the outcome of lotteries. (Sports pools, discussed in more detail in section 6.3 below, are also excluded.)

- "4. (1) A person places or accepts a bet or wager when that person—
- (a) being a player, stakes money or anything of value on a fixed-odds bet, or an open bet, with a bookmaker on any contingency, excluding bets on national lottery, foreign lottery, lottery results and sports pools; or
  - (b) being a bookmaker –
    - (i) accepts a stake of money or anything of value on a fixed-odds bet, or an open bet, from a player on any contingency, excluding bets on national lottery, foreign lottery, lottery results and sports pools; or
    - (ii) stakes money on anything of value on a fixed-odds bet, or an open bet, with another bookmaker on any contingency, excluding bets on national lottery, foreign lottery, lottery results and sports pools;
  - (c) stakes or accepts a stake of money or anything of value with one or more other persons on any contingency, excluding bets on national lottery, foreign lottery, lottery results and sports pools".



Furthermore, the National Gambling Amendment Bill inserts a new clause into the National Gambling Act, which confirms the NLC's regulatory responsibility for both "numbers betting" and sports pools.

"44C Bets on lottery and sports pools

(1) Bets on lottery, lottery results and sports pools are only permitted under the licence and licensing conditions issued by the Board of National Lotteries Commission, with the requirement that –

(a) licensees contribute a reasonable amount towards the National Lotteries Distribution Trust Fund;

(b) such amount will be determined by the Minister, communicated to license holders by way of notice, from time to time, as contemplated in the Lotteries Act, 1997 (Act 57 of 1997), as amended; and

(c) provisions listed under schedule (2) of this Act shall remain applicable under the Lotteries Act, 1997 (Act 57 of 1997), as amended."

Finally, Schedule 2 of the National Gambling Amendment Bill amends sections 1, 2, 3, 4, 5, 6, 12, 13, 14, 15, 16, 17, 19, 20, 21, 22, 23, 24, 25, 28, 29, 46, 47, 48, 49, 50, 51, 52, 53, 54, 55, 56, 57, 58, 59, 60, 76, 77, 78, 79, 80, 81, 82, 83, 84, 85 and 86 of the National Lotteries Act to make these sections of the Lotteries Act applicable to bookmakers and totalisators when they are licenced by us.

Together these amendments give us (the NLC) sole legislative competence for the licensing and regulation of all forms of lotteries, and remove any regulatory confusion over the competencies of provincial gambling boards.

This will result in substantial additional revenue for both the NLDTF and us once the Bill is passed into law.

## **6.2.4 THE INTERNATIONAL EXPERIENCE**

Parasitic lotteries of this ilk are increasingly common throughout the world, as bookmakers seek to capitalise on market demand for this type of product offering. Whilst they are less common in the US, where bookmaking is largely illegal, it is ubiquitous across Europe and in Australia.

Numbers bets are offered directly by licenced bookmakers falling within a particular regulator's jurisdiction, and also online, by both domestic and offshore betting companies. In Ireland, for example, *Premier Lotteries Ireland*, the operator of the National Lottery, have identified 15 predatory betting companies, namely BoyleSports, LottoLand, William Hill, Bet365 and Unibet, based in Gibraltar; My Lotto 24, based in the UK; Playlottery.com and World Lottery Club, based in the Isle of Man; and Jackpot.com and MultiLotto, based in Malta.

The bookmakers offering these lotteries sometimes intentionally mislead the public about the nature of the bets that they place. In Premier Lottery Ireland's opinion, "They utilise the names of 'Lotto' and 'EuroMillions', potentially leading players to believe they are participating in National Lottery games and contributing to good causes. In fact, they are just betting on the outcome of games" (*The Irish Sun*, 18 February 2018).

British law prohibits the sale of bets on UK-licenced lotteries, but allows betting on lotteries registered outside of the UK. Bookmakers exploit this distinction to sell versions of the EuroMillions that are offered by other EU-member countries, rather than the UK version of the same lottery.

Under pressure from licenced lotteries, regulators have begun to address such loopholes, and are looking for ways to protect licenced lotteries. In particular, attention is drawn to the advertising and promoting of lotteries betting, and to the need to educate the public about the difference between participating in a lottery which raises money for good causes, and betting on the outcome of a lottery, which, like sports betting, is a distinct form of "hard gambling" (Alaeddini 2015).

Camelot, in its submission to the British Department for Culture, Media and Sport, review of society lotteries in 2015,<sup>7</sup> called for a clearer distinction between "pure lotteries" and "hard gambling", and called on the regulator to:

1. Prohibit betting on lotteries either in betting shops or online
2. Prohibit the use of branding and imagery intended to give numbers bets the look and feel of a licenced lottery product
3. Prohibit the use of words like "lotto" and "lottery" in the advertising of numbers bets
4. Insist that adverts for numbers bets include the word "bet" in the title

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<sup>7</sup> "Society Lotteries", Department for Culture, Media and Sport, 25 March 2015. <<http://www.gamblingcommission.gov.uk/>>



In addition, to help make a clearer distinction between “pure lotteries” and “hard gambling”, Camelot called on the regulator to redefine bets on lotteries as “pure lotteries”.

In Australia, the Gibraltar-based company, Lottoland, sells bets on the outcomes of both domestic and over 30-licenced overseas lotteries to its 650,000 plus registered Australian members.

This “synthetic lottery”, as it is known in Australia, has attracted considerable backlash, and Lottoland has already been banned in the state of South Australia, whilst four other states, Victoria, Western Australia, New South Wales, and Queensland, look set to either ban or restrict betting on Lottoland (Williams 2017; *Casino News Daily*, 22 September 2017). On 30 November 2017, the Northern Territory introduced a restriction prohibiting the sale of bets on Australian lotteries, although Lottoland is still able to take bets on international lotteries (Marsh 2017).

Two primary objections are raised to Lottoland’s operations. The first, similar to those raised by the NLC in South Africa, is that this is a predatory lottery that draws customers away from licenced state lotteries. Whilst Lottoland pays an annual registration fee of Aus. \$500,000, and pays tax on its profits, it makes no contributions to good causes. Secondly, one of the draw cards of Lottoland is the frequency of its offerings, with players able to choose between several different lotteries, and to place bets several times a day. This contributes to the proliferation of gambling in Australia. A 2014 study by the Victorian Responsible Gambling Foundation (VRGF) had already raised concerns about lottery contribution to problem gambling, after it found that over two-thirds (67.4%) of people with “significant gambling problems” played the Lotto, Powerball and the Pools; more than any other gambling modality. The VRGF is particularly worried about the possibility of lottery betting contributing to this worrying trend, and notes that: “While lottery is a popular form of gambling for many people, the bets are usually small and infrequent. With Lottoland, the opportunities and incentives to bet are much higher than in traditional lotteries. It is still too early to observe the effects of this product, but, logically, there are good reasons to be concerned” (Shaw 2016).

## **6.2.5 OTHER RELEVANT REGULATORY EXPERIENCE**

An alternative and possibly more effective way to manage fixed odds lottery bets is to develop a rigorous guarantees policy, which will make it difficult if not impossible, to offer the type of massive fixed odds prizes advertised by companies like LottoStar in Mpumalanga.

Ordinary lotteries, like the National Lottery in South Africa, are pooled bets, totalisator-type products in which a stipulated percentage of ticket sales is reserved for prizes and distributed to winners according to a predetermined formula.

It does not matter how many people win prizes, or what type of prizes people win. The money is always available for distribution. The operator is not at risk of having to honour bets that they cannot afford to pay. And players are not at risk of finding that their wins cannot be honoured.

In the gambling sector, it is customary for regulators to insist that the operators of all gambling products, other than totalisator products, lodge financial guarantees that confirm their ability to pay out should a punter win a particularly high prize, or, more likely, should an unusually large number of punters win high prizes on the same night. The guarantees are determined on the basis of a risk-based formula, and are game/seat specific. For example, regulators might insist that operators lodge a guarantee sufficient to cover 15 times the maximum pay-out on each table game offered in a casino (assuming the game has less than 15 seats), and/or an amount equal to several months gambling taxes. The total guarantee required adds up quickly.

Fixed odds bets on the outcome of a lottery expose both the operator and the player to the same sort of risk. Because the bets are not part of the pooled prize money, and are instead fixed odds pay-outs, it is quite possible that the operator will find herself in a position where she has to pay out several top prizes at the same time. Hypothetically, if several punters predicted the winning combination in the Africa Millions draw on the same night, LottoStar might have to pay out several prizes of €100 million each. Which it clearly cannot do.

Fixed odds operators mitigate their risk by taking out insurance on higher bets. A large part of the ticket price goes to covering this insurance. However regulators are never sure what level of risk the operators pass onto players. The likelihood of a bookmaker having to make massive pay-outs is extremely small, and they are often willing to take this risk, as the consequences of not paying out are relatively low. This leaves the player vulnerable.

To mitigate this risk, and to protect the gambling public, some provincial gambling regulators insist that bookmakers have to lodge guarantees on fixed odds lottery bets. This is consistent and fair, and treats such bets in the same way as they would treat a bet on the outcome of the spin on a roulette wheel, or a slot machine. Because the amount needed to lodge a guarantee on a massive pay-out, as in Africa Millions or Euro Millions, is so large, this effectively forces operators to limit their bets to a stipulated maximum pay-out.

Bookmakers get around some of these restrictions by migrating from provinces with higher restrictions, and license their online operations in provinces with fewer if any restrictions.





If a national operator like the NLC took responsibility for the regulation of all fixed odds lottery bets, a single national guarantees policy could be enforced. This would drastically disincentive the offering of massive fixed odds bets that compete with the National Lottery.

## **6.2.6 THE PROS AND CONS OF NLC REGULATION**

Unlike *fahfee*, which is clearly illegal, the licensing and regulation of fixed odds lottery betting is relatively easy to understand and to prepare for. In large measure, we will take over a regulatory responsibility that is presently being performed by provincial gambling boards, on the basis of legislative amendments that will soon be in place once the National Gambling Amendment Bill becomes law.

The most likely positive outcome of our regulation of fixed odds bets on the outcome of lotteries is additional revenues, which will accrue to us and to the NLDTF.

A significant potential “con” is the danger of regulatory overlap and overburden for bookmakers, who will now have to deal with separate regulatory authorities when licensing different betting products. This is a very real concern. It is important to minimise this problem, so as not to jeopardise the profitability of the industry we are seeking to promote and regulate.

Voluntary associations representing the broad interest of bookmakers can provide an important vehicle to reduce the potential “silo effect” of having different regulators license different parts of the bookmaking business. These can assist all parties to identify and address potential regulatory overlap between the NLC, provincial gambling regulators, and bookmakers. Important issues to address here include the granting of probity certificates, the establishment of tax rates, transformation objectives and targets, the identification and response to problem gambling, and the continued development of all aspects of the bookmaking industry.

Some but not all provincial gambling regulators presently require membership of voluntary bookmaker associations.

A secondary “con” is resistance to the change in regulatory responsibility by licenced bookmakers. Both the South African Bookmakers Association (SABA) and the Gauteng Off-Course Bookmakers Association (GOBA), have already indicated that they oppose this move, citing perceived capacity shortcomings at the NLC, as well as likely regulatory overlap and overburden, as key concerns. It is clear that this is significant challenge.

Finally, a shift to national regulation by the NLC will result in a significant loss of revenues for the SARGF, and have a negative impact on the identification and treatment of problem (disordered) gambling in South Africa. Coupled to the likely increase in hard gambling attributable to the spread of numbers betting, this is a problem worth noting.

### 6.2.7 BOOKMAKER NUMBERS BETTING: RECOMMENDATIONS

Bookmaker numbers betting is a lucrative market, which should fall under the jurisdiction of the NLC and not provincial gambling boards.

In the terminology adopted in the *Illegal Lotteries Report*, we believe that this type of bet should be **regulated**, and that the NLC should license bookmakers to offer this product. It is equally feasible for the NLC to develop its own products which **compete** directly with those offered by bookmakers. This market-based approach should be considered in the medium to long term.

Our major recommendations for the regulation of bookmaker bets on the outcome of lotteries are as follows.

- It is recommended that the National Gambling Amendment Bill should be supported as it removes any regulatory uncertainty and clearly gives the NLC sole legislative competence for the licensing of fixed odds bets on lottery results, regardless of the type or location of the lottery in question.
- It is recommended that the NLC should only license fixed odds bets on non-South African lotteries. Bets should not be placed on the outcome of the South African National Lottery, which should enjoy a higher level of protection than other lotteries.
- It is recommended that any licenses granted are subject to clear conditions pertaining to the advertising and promotion of numbers betting products. This should promote public awareness about the nature of the product, and avoid the blurring of lines between traditional or “pure” lotteries (to use the British term) and bets placed on the outcome of a lottery.
- The advertising of numbers betting products needs to avoid the use of the words “Lottery” and “Lotto”, and similar terms. Adverts for a numbers bet cannot have the look or feel of an advertisement for the lottery or lotteries on which the bet is placed.



- It is recommended that a national guarantees policy be developed, and that operators lodge financial guarantees to ensure that they are able to make possible multiple pay-outs on the top fixed odds prizes in each bet on each lottery draw they provide. These guarantees need to supplement but not replace any insurance that bookmakers take out on bet outcomes.
- It is recommended that the NLC urgently develop capacity to exercise this licensing function. This capacity is needed at both a provincial and a national level.
- It is recommended that the NLC urgently develop the capacity required to inspect and monitor the operations of licenced bookmakers offering fixed odds numbers bets in order to ensure that all required taxes and levies are collected. The NLCs inspectorate needs to be improved, resourced, and empowered to ensure that cases can be investigated and prosecuted without significant involvement of the already overcommitted South African Police Services. This capacity is needed at both a provincial and a national level.
- It is recommended that licenses be granted on a provincial basis, subject to national compliance standards. Online betting should be subject to the same geographic limitations, and operators should be required to use geolocation software, to enforce such limitations. This technology is widely available, and employed in other jurisdictions.
- It is recommended that the issuing of licenses, and the criteria used to identify potential licensees, must contribute to the broad-based transformation of the bookmaker sector and advance the objectives of the Broad-Based Black Economic Empowerment Act, 2003 (Act 53 of 2003) as amended, as contemplated in the applicable sections and the Codes.
- Bookmakers will now have to deal with both provincial gambling regulators and the NLC in order to obtain licenses for their different product offerings. In order to simplify this process and reduce compliance costs, it is recommended that probity checks currently conducted by provincial gambling boards as a condition of license be considered sufficient for the granting of licenses for fixed-odds bets on lottery outcomes. Alternatively, we need to conduct an equivalent probity check on bookmakers applying only for a license to place fixed odds bets on lottery outcomes.
- Bookmaker probity should be recorded in a national probity register, to be developed and maintained by the NLC, and made available to all provincial gambling regulators as required.

- It is recommended that bookmakers be required to be members of a voluntary association representing the collective interest of bookmakers. This association would consider all matters pertaining to bookmakers, not only fixed odds betting on lottery outcomes.
- It is recommended that bookmakers contribute a reasonable amount towards the NLDTF. Such amount will be determined by the Minister, communicated to license holders by way of notice, from time to time, as contemplated in the Lotteries Act, 1997 (Act 57 of 1997), as amended.
- It is recommended that the taxation of revenues derived from betting on the outcome of a lottery be determined by the NLC, and that a national rate be applied across the industry. In determining this rate, we should take into consideration the additional burden of NLDTF contributions, which bookmakers did not previously have to make.
- In the medium- to long-term, it is important to understand why fixed odds betting on lotteries have become so popular. Simply put, it is a very attractive product, which punters, worldwide, increasingly prefer to traditional (pooled) lottery products. It is recommended that the NLC consider entering this market directly, and encourage the operator of the National Lottery to offer fixed odds bets on the outcome of both the South African and various international lotteries.
- Unlike the National Lottery, which is a pooled lottery product and a protected monopoly, it is recommended that this market-based response allows for competition between the operator of the National Lottery and bookmakers licenced to offer such products by the NLC.

## 6.3 SPORTS POOLS

Sports betting has become the second largest gambling activity in the country, comprising nearly 14% of total GGR's in 2014, second only to casinos which accounted for 72% of GGR's (NLC 2016: 32-33). This represents a significant loss of potential revenue for the NLC, and in contributions to the NLDTF. We estimate the cost to the NLC to be R1, 092.73 million annually, with a loss of R295.04 million annually to the NLDTF (NLC 2016: 8).



## 6.3.1 MODUS OPERANDI: HOW THE GAME IS PLAYED

Totalisators are presently licenced by provincial gambling authorities. Licences are granted based on a number of conditions, one of which states that the premises of the totalisator must be specified in the license. Research shows that as at 2015, there were 402 operational totalisator outlets across the country, with the Western Cape accounting for more than 78% of the total (NLC 2016: 32).

### 6.3.1.1 Taxation

Totalisators are taxed by provincial regulatory authorities, at rates determined on a provincial basis. Whilst these rates have remained stable for some time, some provinces are seeking to raise these. This is being contested.

### 6.3.1.2 The SARGF

Totalisators are expected to make a voluntary contribution of 0.1% of revenues to the SARGF. This money is used to monitor and mitigate the harmful effects of gambling in South Africa.

## 6.3.2 LEGISLATION

Sports pools are defined in terms of the Lotteries Act as:

*“any scheme, excluding any scheme or competition in respect of horse racing which is authorised by the board, or which is conducted in the same format and manner and under the same circumstances as a scheme or competition in respect of horse racing that existed prior to 18 June 1997, under which-*

- (a) any person is invited or undertakes to forecast the result of any series or combination of sporting events in competition with other participants: and*
- (b) a prize is to be awarded to the competitor who forecasts the said result correctly or whose forecast is more nearly correct than the forecasts of other competitors, or a number of prizes are to be awarded on the basis aforesaid, and for the purposes of this definition the forecast of a result includes not only the forecast of the person, animal, thing or team that will be victorious or otherwise, but also any forecast relating to the system of scoring employed in the sporting event in question, or to the person who will be responsible for that score.”*

A sports pool is a form of a lottery. Unlike fixed-odds betting, the amounts wagered are placed in a common pool where monies are first deducted to cover expenses and then the remainder of the amount is allocated to the winning ticket holders.

The National Lottery is a classic example of a pooled bet. This is one of the reasons why sports pools are supposed to be regulated by the NLC.

The Lotteries Act permits sports pools that have “been authorised by or under this Act or any other law” (s 57(1)(b)). Provincial gambling authorities do not believe that this gives the NLC sole jurisdiction over sports pools. For one thing, many sports pools were authorised by provincial authorities and became operational before the Lotteries Act came into effect. Provincial authorities therefore believe that those licenses remain valid. Secondly, the provincial authorities believe that the NLC has sole jurisdiction over the issuing of licenses to conduct *national* sports pools, which are contemplated in s 55(1) of the Lotteries Act. The NLC does not have sole jurisdiction over the licensing of all possible sports pools. Thirdly, and related to this last point, provincial regulators believe that the reference to the licensing of sports pools under “any other law” allows them to continue to authorise sports pools after 1997. Section 2(1) of the Gauteng Gambling Act, 1995, for example, says that the National Gambling Act does not apply in Gauteng in relation to anything for which a licence is required in terms of the Gauteng Act. It thus excludes the National Act from the regulation of gambling, including totalisator betting, in Gauteng.

This dispute is currently the subject of a legal challenge, *KwaZulu-Natal Bookmakers Society and others v Phumelela Gaming and Leisure Ltd and others* (Case no. 38728/2015, North High Court of South Africa), in which various bookmakers are seeking to have Phumelela and Gold Circle sports betting operations declared contrary to the Lotteries Act. In all likelihood this case will be finalised before the Amendment Bill is voted upon. This will bring some clarity to the debate on the licensing and regulating of sports pools in South Africa.

The operators of sports pools are instructed by law to contribute to the NLDTF. Section 55(2) of the Act authorizes the Minister to determine what percentage of sales should be allocated to the NLDTF in terms of section 26(3) of the Act.

### **6.3.3 THE NATIONAL GAMBLING AMENDMENT BILL, 2017**

The discussion here is a summary of the fuller discussion in 6.2.3 above, which applies equally to sports betting and fixed odds numbers betting.



The National Gambling Amendment Bill, 2017, clarifies responsibility for the regulation of sports pools, and removes any legislative obstacles to the transfer of responsibility for regulation of sports pools to the NLC.

Clause 2 of the National Gambling Amendment Bill, 2017, addresses any possible regulatory confusion by amending the definition of permissible “Bets and Wagers” in Section 4 of the National Gambling Act, 2004 to exclude bets on sports pools from the categories of activities regulated by either the national or provincial gambling authorities.

Section 44C of the National Gambling Amendment Bill confirms the NLCs responsibility for the issuing of licenses for sports pools, and directs licensees to contribute a reasonable amount towards the NLDTF; such amount to be determined by the Minister, and communicated to license holders by way of notice, from time to time, as contemplated in the Lotteries Act, 1997 (Act 57 of 1997), as amended.

Together these amendments give the NLC sole legislative competence for the licensing and regulation of sports pools.

This will result in substantial additional revenue for both the NLC and the NLDTF once the Bill is passed into law.

### **6.3.4 SPORTS BETTING: THE INDIAN EXPERIENCE**

Sports betting, other than horseracing, is banned in India, although there is a thriving illegal betting industry, both land-based and online, worth an estimated \$150 billion annually (Ranjan and Vasavda 2017).

Legislators, supported by sections of the judiciary, seeking to deal with this growing problem acknowledge the government’s inability to control the growth of this sector, and the dangers of allowing criminal syndicates to control betting in India. Legalisation allows bookmakers to be drawn into a transparent space, where they can be effectively monitored. This is similar to the recommendations of the Wiehahn Commission, which led to the liberalisation of gambling in South Africa after 1994.

A key issue that would need to be addressed here is money laundering. Bookmakers accept bets from all over the world, with transfers made via the informal hawala system. This further opens possibilities for organised crime to use sports betting to launder money, both in and outside of India.

Of greater concern to the South African debate is the focus on the relationship between sports betting and the underlying sport. The question of match fixing and corruption is a major issue in Indian sport, and bookmakers are believed to have an inordinate influence over the results of games, sometimes even games played outside of India.

The Lodha Commission of enquiry set up to investigate a range of issues affecting Indian cricket made a number of important recommendations which have helped frame the debate on legalisation. The discussion here focuses only on issues of relevance to the debate in sports betting in South Africa.

In addition to the legalisation of betting, and establishment of the necessary gambling regulatory authorities, the Commission called the promulgation of specific Sports Regulation Law and a Central Sports Regulator Authority (Lodha Commission, Vol 2, 2016, pp. 22-23).

This was presented as a means to address the problem of match fixing, and the relationship between sports betting, bookies, and the underlying sport. It is a constructive suggestion, and speaks to a growing regulatory challenge in all jurisdictions, not just in India.

Summarising the problem at hand, the Commission noted:

“There is a fundamental difference between betting and match/spot-fixing. The latter interferes with the integrity of the game and attempts to change the course of the match. It is tampering the game by the cricket players to benefit a few. On the other hand, betting is a general malaise indulged by different sections of society, not only with reference to cricket but other games also. While the issue of betting can be effectively dealt with by providing a legal framework, match/spot-fixing is neither pardonable nor a matter for regulation. The only way to deal with it is by making it a criminal offence punishable by law. The Committee recommends appropriate amendments by the legislature” (Lodha Commission, Vol 1, 2016, p. 60).

To help create a transparent gambling and sporting environment, the Commission recommended that players, administrators, and other officials close to the sport, would be required to furnish details of their incomes (Lodha Commission, Vol 1, 2016, p.62).

A second recommendation drew a distinction between the regulation of land-based and online betting, and recommended that these be treated separately. Licenses for land based betting should be issued by state authorities, whilst an (unspecified) central authority would issue a national license for internet gambling.





The Commission provides no real explanation for this distinction, or details as to how this would operate in practice. They do not appear to have considered the practicalities of this distinction, or the experience of regulation elsewhere in reaching this decision. Presumably this is to prevent a situation where state-licensed betting outlets (like LottoLand in the Northern Territories) sell their product nationally via the internet, despite objections from other state authorities to the licensing of the product in question. But how would such restrictions work in practice? Once a national license is issued, then surely this would mean that anyone anywhere in India could place a bet, and the rights of states to decide on their own licensing policy would be completely eroded? An alternative, which might be more appropriate in South Africa, would be to allow state authorities to license online operations, and insist that they use geolocation software to restrict sales outside their jurisdiction.

It is expected that India will proceed legalise sports betting within the next two years.

In Australia, sports betting has raised considerable social and ethical concerns. These led to the passing of a National Policy on Match-fixing in Sport in 2011, and the establishment of a specialised National Integrity in Sport Unit, which is tasked with protecting sport from the dangers of corruption, doping, and match fixing.

The functions of this Unit are extensive, and are of considerable relevance to the debate in South Africa. The Australian Sports Commission emphasises the need to link the regulation of sport closely to the regulation of betting, and lists these responsibilities as to:

- “coordinate legislation, regulation, policies and administrative practices between the Commonwealth and the States to allow governments to adopt appropriate measures to ensure sport is drug-free
- provide national coordination, monitoring, reporting, and strengthen relationships between state and territory governments, regulators, sporting organisations, law enforcement agencies, and other agencies as appropriate
- work with like-minded nations, the international sports movement, betting operators and regulators on match-fixing and fraudulent betting issues and advocate for a global response to match-fixing
- work with relevant sports governing bodies and local organising committees to develop integrity strategies

- provide advice and work with individual sports to ensure a robust framework is adopted across the sporting codes and there are no gaps for criminal groups to use as soft targets
- develop and maintain a website as a resource centre for key stakeholders to access up to date information including integrity tools, education, contacts and research
- compliance audits of sports to ensure policies continue to be effectively implemented
- support sports through Match-fixing crisis situations (i.e. advice, issues management)
- introduce mechanisms for whistle-blowing in the area of manipulation of sports results to ensure disclosure of information
- investigate complaints made about the integrity processes and systems of a sports controlling body, and
- undertake research and provide information on latest best practice to support international, state and territory governments, regulators, sporting organisations law enforcement agencies, regulators and other agencies as appropriate to promote consistent and effective approaches to protect the integrity of sport.”<sup>8</sup>

Despite this, match fixing appears to be a recurring problem in Australia, most recently highlighted in a Fairfax Media investigation into three National Football League matches (*Sydney Morning Herald*, 7 September, 2016). Various specific areas of concern have been flagged, including the ease with which Australian citizen place bets on international bookmaker and totalisator sites, in-play betting, and the number of micro-bets being offered on the outcome of small events within a game—for example, the outcome of each serve in tennis, or whether the next ball bowled in cricket will be a “no ball” in a single over in cricket (VRGF 2013, p. 2). Although these latter products are only really applicable to fixed odds betting, it is important to note the danger of betting on events that are more easily manipulative within a game.

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8 [https://www.ausport.gov.au/supporting/integrity\\_in\\_sport/match\\_fixing](https://www.ausport.gov.au/supporting/integrity_in_sport/match_fixing)



The massive growth in sports betting has also prompted renewed concerns about the proliferation of gambling in society. In an effort to curb this, and to weaken the growing association between sports and betting generally, the government has recently announced (effective 30 March 2018) a national ban on gambling adverts during sports events between 5am and 8:30 pm each night (igaming.com, 28 March, 2018).

Lessons/questions for SA:

- should there be a distinction between the licences offered for online and land based sports betting?
- what and if any geolocation restrictions should be applied?
- should in-play betting and micro-betting be allowed?
- should the regulation of sports betting be linked to the regulation of the underlying sport to help address issues of match fixing? And if so, what levels of coordination between national sporting organisations and gambling authorities are required to address this.
- how should the negative social impacts of the growth of sports betting (both in-play and outcome betting) be mitigated?
- should advertising which reinforces a link between sports and betting be restricted?

### **6.3.5 THE PROS AND CONS OF NLC REGULATION**

Unlike fahfee, which is clearly illegal, the licensing and regulation of sports pools is relatively easy to understand. The NLC will simply take over a regulatory responsibility that is presently being performed by provincial gambling boards, on the basis of a legal framework that is either already in place or which will soon be in place once the National Gambling Amendment Bill becomes law. On the positive side, this will mean that substantial additional revenues will accrue to the NLC, and additional contributions will be made to the NLDTF.

From the industries perspective, the possibility of being able to run a single national tote, as opposed to nine stand-alone totes, has been cautiously welcomed by stakeholders, who see this as a considerably more viable long-term gaming product, which will allow them to offer a more competitive product, increase returns to punter, and expand their gaming operations.

On the negative side, this may result in significant regulatory overburden for totalisators or anyone offering a sports pool, who will now have to deal with separate regulatory authorities when licensing different betting products.

Totalisators, for e.g., will still apply to provincial regulatory authorities for licences for horseracing pools, and any legacy sports pools still licenced by the provincial authorities, whilst applying to the NLC for national licenses for sports pools. It is important to minimise this potential duplication of effort and associated burden, so as not to jeopardise the profitability of the industry we are seeking to promote and regulate.

Voluntary associations representing the broad interest of totalisators can provide an important vehicle to reduce the potential “silo effect” of having different regulators license different parts of the totalisator (and horse racing) business. These can assist all parties to identify and address potential regulatory overlap between the NLC, provincial gambling regulators, sporting associations (including horseracing associations), and totalisators. Important issues to address here include the development of the underlying sport on which sports pools are offered, the granting of probity certificates, the establishment of tax rates, transformation objectives and targets, the identification and response to problem gambling, and the continued development of all aspects of the bookmaking industry.

Industry stakeholders express concern about the NLC’s current capacity to license and regulate sports pools. In particular, they are concerned about a lack of capacity at the provincial level.

Finally, a shift to national regulation by the NLC could result in a significant loss of revenues to the SARGF, and have a negative impact on the identification and treatment of problem (disordered) gambling in South Africa. At present, the NLC does not require its licensees to make a contribution to the SARGF. This loss of SARGF revenues should be flagged as a potential reputational risk for the NLC.

### 6.3.6 SPORTS POOLS: RECOMMENDATIONS

Sports pools are a lucrative market, which should fall under the jurisdiction of the NLC and not provincial gambling boards.

In the terminology adopted in the *Illegal Lotteries Report*, we believe that this type of bet should be **regulated**, and that the NLC should provide national totalisator licenses to offer this product.

Our major recommendations for the national regulation of sports pools are as follows.



- It is recommended that the National Gambling Amendment Bill should be supported as it removes any regulatory uncertainty and clearly gives the NLC sole legislative competence for the national licensing of sports pools, excluding any scheme or competition in respect of horse racing.
- It is recommended that the NLC urgently develop capacity to exercise this licensing function. This capacity is needed at both a provincial and a national level, even if licenses are issued at a national level.
- It is recommended that the NLC urgently develop the capacity required to inspect and monitor the operations of totalisators offering sports pools in order to ensure that all required taxes and levies are collected and paid to the relevant provincial and national authorities.
- The NLCs inspectorate needs to be improved, resourced, and empowered to ensure that cases can be investigated and prosecuted without significant involvement of the already overcommitted South African Police Services. This capacity is needed at both a provincial and a national level.
- It is recommended that the issuing of licenses, and the criteria used to identify potential licensees, must contribute to the broad-based transformation of the totalisator sector and advance the objectives of the Broad-Based Black Economic Empowerment Act, 2003 (Act 53 of 2003) as amended, as contemplated in the applicable sections and the Codes.
- Totalisators offering sports pools will now have to deal with both provincial gambling regulators and the NLC in order to obtain licenses. In order to simplify this process and reduce compliance costs, it is recommended that probity checks currently conducted by provincial gambling boards as a condition of licence be considered sufficient for the granting of licences for sports pools. Alternatively, the NLC needs to conduct an equivalent probity check on totalisators applying only for a licence to offer sports pools.
- Totalisator probity should be recorded in a national probity register, to be developed and maintained by the NLC, and made available to all provincial gambling regulators as required.
- It is recommended that totalisators contribute a reasonable amount towards the NLDTF. Such amount will be determined by the Minister, communicated to licence holders by way of notice, from time to time, as contemplated in the Lotteries Act, 1997 (Act 57 of 1997), as amended.

- It is recommended that the taxation of revenues derived from sports pools be determined by the NLC, and that a national rate be applied across the industry. In determining this rate, the NLC should take into consideration the additional burden of NLDTF contributions, which totalisators did not previously have to make.
- It is recommended that a national policy dealing with match fixing be developed, and that a common task force or unit, involving the NLC, all national sporting codes, and the SAPS, be established to protect sports betting and the underlying sport from the dangers of corruption, doping, and match fixing.

## 6.4 PROMOTIONAL COMPETITIONS

Promotional competitions are intended to promote or advertise products, and are currently regulated in terms of section 36 of the Consumer Protection Act No. 68 of 2008. Prior to 2011, they were regulated in terms of Section 54 of the Lotteries Act.

Promotional competitions are always difficult to regulate, as they are both a form of lottery and a tool to promote business.

Section 36 of the Consumer Protection Act (CPA) defines promotional competitions as “*any competition, game, scheme, arrangement, system, plan or device for distributing prizes by lot or chance*”. This definition applies regardless of whether participants need to demonstrate any skill or ability in order to win a prize. Due to the element of chance, promotional competitions are often categorised as lotteries or gambling.

The CPA expects promotional competitions to be “conducted in the ordinary course of business for the purpose of promoting a producer, distributor, supplier or association of any such persons, or the sale of any goods or services”.

The massive expansion in social media in South Africa has made promotional competitions an increasingly popular way for businesses to interact with potential customers.

Promotional competitions may not charge a consideration or subscription as a condition of entry. As such, they are not supposed to compete with the National Lottery, and are not intended to be money-making schemes in their own right.



The *Impact of Illegal Lotteries* study confirmed that this does not always occur, and that many promotional competitions “either charge too high an entry fee, sell more than the allowed number of tickets, or have a prize where the value exceeds a prescribed limit. As a result, these promotional competitions are being run more for commercial gain than for promotional purposes” (NLC 2016: 38).

It is clear that promotional competitions are abused, and that many illegal schemes are offered under the guise of promotional competitions. Some form of regulation is needed to protect consumers from this abuse.

#### **6.4.1 MODUS OPERANDI: HOW THE GAME IS PLAYED**

Promotional competitions are offered using a variety of traditional and electronic media platforms, the most popular being SMS, social media, and e-mail. Less frequently these days, competitions are offered via the postal service.

Promoters are not allowed to charge premium rates for SMS entry fees, and Regulation 11(1) of the CPA Regulations establishes a maximum permitted cost of R1.50 per competition entry. No consideration for play is allowed.

Our research suggests that this stipulation is often abused, and that promoters sometimes raise monies through the charging of premium SMS fees, or by directly requiring a consideration. The *Impact of Illegal Lotteries* study found that “the use of premium rated SMS competitions is pervasive and extensive across South Africa and [it is] likely that the combined value of the individual schemes is considerable” (NLC 2016: 37).

##### ***6.4.1.1 Consideration or entry fee***

One difference between ordinary lotteries and promotional competitions is that lotteries require entrants to pay a consideration in order to participate—and fund the prize in whole or part out of this consideration—whilst promotional competitions do not usually require a consideration in order to enter.

Whilst some jurisdictions allow for a consideration, South Africa does not.

Section 63 of the Lotteries Act, 1997, states that the Act does not apply “*in relation to any lottery, sports pool or competition in respect of which there is no subscription*”.

In terms of section 54 of the Lotteries Act, the payment of a consideration was explicitly prohibited, although promoters were entitled to require entrants to purchase their goods and services at the normal retail price in order to participate in a competition.

This remains unchanged with the repeal of section 54. In terms of sections 36(3)(a) and 36(4) of the CPA, promotional competitions may not charge an entry fee or a consideration for entering, that is to say, there is no additional cost attached to entering the competition, other than the cost of submitting an entry. As such, the organisers of promotional competitions cannot fund the prize through the cost of entry tickets.

Strictly speaking, this means that only two of the three elements usually stipulated in the definition of lottery gambling—a consideration, chance, and a prize—are present. As Strachan (2016: 52), commenting on promotional competitions in general, points out; this allows national regulators to exempt such competitions from the more onerous requirements of ordinary gambling legislation, whilst at the same time restricting competition in order to protect the monopoly of licenced state lotteries.

#### **6.4.1.2 Prizes**

Section 36(11) of the CPA allows the Minister to determine a low value threshold, and excludes competitions with prize values below this threshold from the definition of a promotional competition. At present, the threshold for excluding competitions with low value prizes is R1, which, as Strachan (2016: 300) notes, means that no competition is ever excluded. As such, the stipulation has no practical effect, and imposes an unnecessary regulatory burden

In Strachan's view, it would be better to raise the threshold to a meaningful level—he suggests R100—to allow the regulator to focus their efforts on a more limited range of more consequential promotional competitions.

At the same time, it is important to ensure that competitions with low value prizes falling below the designated threshold are not excluded from the definition of a promotional competition and become unauthorised competitions by default. Strachan (2016: 299) recommends that such competitions are instead *exempted* from section 36 of the CPA's requirements. This is sensible. The CPA has broadened the category of prize that can be offered. Promoters are no longer prohibited from offering prizes and competitions that are in any way similar to the National Lottery, or from requiring winners to pay fees to third parties to obtain licences, authorisations, or the like, in order to use the prize (Strachan 2016: 208).





### **6.4.1.3 Self-regulation**

Various voluntary codes provide a degree of self-regulation for the organisers of promotional competitions. The Advertising Standards Association (ASA) Codes, for example, prohibit promotional competitions from using misleading language when describing prizes, for example by implying that people who enter would win a prize when they will in fact merely be *eligible* to win (see the *Sowetan BMW / S Zwane* ruling) or for failing to display the closing date of a competition clearly (see the *Brooks Sweeto / GH Smith Ruling*). These codes are only binding on ASA members.

Similarly, the Wireless Application Service Providers Association (WASPA), which self-regulates mobile based value added services in South Africa, has detailed provisions for the self-regulation of promotional competitions. Section 18(2) of the WASA Codes, for example, confirms the CPA stipulation that the maximum permitted cost of a competition entry is R1.50, whilst section 18(4), mirroring section 36(5) of the CPA, details the information that has to be provided in any offer made to enter a promotional competition. These codes are only binding on ASA members.

WASPA actively monitors the advertising of members, to ensure compliance with the WASPA Codes, and appoints independent adjudicators to adjudicate on any complaint made by members of the public or WASPA members.

Although he praises the high level of self-regulation in the marketing and advertising industry in South Africa, Strachan (2016: 275) concludes that, with the exception of the WASPA Codes, the provisions in most industry self-regulatory codes pertaining to promotional competitions are limited. Most Codes simply require promoters to comply with applicable law, rather than set out in detail proactive ways to regulate promotional competitions. On this, Strachan sees the United Kingdom Code of Non-Broadcast Advertising, Sales Promotion and Direct Marketing, or CAP code, as a model worth following.

### **6.4.1.4 Independent professional certification**

According to Regulation 11(5) of the CPA Regulations, a promoter has to ensure that the conducting of a promotional competition is overseen and certified by an independent accountant, registered auditor, attorney, or advocate.

This is a costly compliance requirement, which imposes a significant barrier to entry, especially for small competitions offering small prizes (De Stadler 2013: 74-75), and is likely to discourage small businesses and entrepreneurs from using promotional competitions to attract customers.

It is not entirely clear what this “oversight” requirement entails, or whether the overseer is expected simply to witness and verify the random draw, or to supervise the entire competition from inception (Strachan 2016: 243).

Clarifying and simplifying the certification and compliance requirements could be a good way to achieve the twin objectives of:

- encouraging the use of promotional competitions for the purpose for which they are intended, i.e. as a means to grow businesses, and to reduce the compliance costs, especially for emerging and small businesses.
- Getting the independent professional to certify a few key aspects of the scheme only, particularly the fairness of number selection, the fact that no consideration or entry fee was required, and that prizes were not made conditional on any additional payment, would go a long way towards combating the proliferation of illegal promotional competitions.

## 6.4.2 LEGISLATION

In the past, the Lotteries Act made provision for the authorisation of promotional competitions under Section 54. The CPA has repealed this section, and the NLC can no longer authorise promotional competitions.

Promotional competitions now governed by section 36 and regulation 11 of the Consumer Protection Act (2008). The National Consumer Commission has been established by the Consumer Protection Act (2008) to enforce the legislation and to ensure that the consumer is protected by curbing unfair marketing and business practices.

Strachan (2016: 297) argues that it is unclear whether promotional competitions are indeed authorised and lawful, due to the fact that sections 56 and 57(1) of the Lotteries Act prohibit the conducting of promotional competitions and other competitions *unless they are authorised by the Lotteries Act*; whilst the Lotteries Act does not expressly authorise promotional competitions. Although the CPA regulates promotional competitions, it does not expressly authorise them. As such, Strachan recommends that the term, “promotional completion” is reinserted into the Lotteries Act.



The Lotteries Amendment Act, 2013 removed the definition of a promotional competition from the Lotteries Act, despite the fact that the term is still used in sections 1, 56, and 57 of the Lotteries Act. This means that promotional competitions that meet the conditions of a lottery cannot be authorised in terms of the Act.

Despite the fact that the CPA repealed Section 54 of the Lotteries Act, several references to Section 54 remain in the Act; section 1 (definition of a participant), section 10(d), and section 56(b) and (c). These should be removed. In so far as it is necessary to cross reference in these sections, the relevant sections should cross reference to section 36 of the CPA instead.

The Consumer Protection Act sets out basic rules for the running of promotional competitions in Section 36. These include a ban on misleading communication, a prohibition of entry fees or payment to participate in the competition, restrictions on prize-winners, the organisers' responsibility to publish the rules for the competition, and rules protecting the rights of participants.

### **6.4.3 THE PROS AND CONS OF NLC AND CPA REGULATION**

Promotional competitions are a legal lottery-type scheme for the promotion of a product or service. They are not an illegal lottery scheme *per se*. However it is clear that these schemes are sometimes abused, that many promotional lotteries are run illegally, and that many illegal lottery schemes are offered under the guise of promotional lotteries.

This distinction is important: the issue we face here is not, primarily, the definition of promotional competitions, or the regulatory framework developed to oversee promotional competitions. Indeed, the most comprehensive assessment of promotional competitions in South Africa concludes that, "South Africa's law relating to promotional competitions is in fact quite evolved and comprehensive. Accordingly, a drastic review or redrafting of the existing legislation was not proposed. However, it was found that there are some defects and inconsistencies and these need to be addressed in order to make it easier to interpret and apply the law and enforce it properly" (Strachan 2016: 278).

At present, it is not clear where or how promotional competitions are authorised. Because promotional competitions are a game of chance, they are a lottery, and the Lotteries Act should be amended to make provision for the authorisation of such competitions.

One advantage of this is that a violation of the provisions of the Lotteries Act would attract criminal sanction, whereas promoters who violate the provisions of the CPA are unlikely to face more than an administrative penalty (Strachan 2016: 208).

The more difficult question is whether promotional competitions should be regulated directly by the NLC (as they were before 2011), or under the CPA (as they have been since 2011).

The argument in favour of the NLC regulating promotional competitions directly is that the NLC has a better understanding of the workings of lottery schemes, and is therefore better placed to regulate this particular game of chance and to protect the consumer.

From this perspective, the Lotteries Act should be amended to make provision for both the authorisation and the regulation of promotional competitions. Section 36 of the CPA, under which promotional competitions are currently regulated, should be repealed, and much of the former section 54 of the Lotteries Act should be updated, clarified, and reinserted into the Lotteries Act.

This approach has similarities to the regulation of “sales promotion schemes” under section 19 of the New Zealand Gambling Act.

An alternative and more viable option is to amend the Lotteries Act to make provision for the authorisation of promotional competitions *as defined in the CPA*, and to govern promotional competitions in accordance with consumer protection rather than gambling legislation.

If this conclusion is shared, then the Lotteries Act should be amended to authorise promotional competitions *as defined in the CPA*, and to allow these to be regulated in accordance with the provisions in section 36 of the CPA.

This approach is similar to that adopted throughout the EU, and incorporated into UK law through the Consumer Protection From Unfair Trading Regulations, 2008.

In our view, this is the more pragmatic, administratively effective, and cost-effective approach. It is correct that the NLC be required to authorise all lotteries, including promotional competitions; however the CPA has greater enforcement and inspectorate capacity, and is better placed to coordinate the efforts of business and industry self-regulatory bodies, than the NLC.

As promotional competitions are not allowed to generate a profit, it is difficult to see how the regulation of these schemes can generate significant revenues for the NLC, or what contributions to the NLDTF might be levied.



## 6.4.4 RECOMMENDATIONS

In the terminology adopted in the *Illegal Lotteries Report*, we believe that the solution to the misuse of promotional competitions requires a combination of **enforcement** and **regulation**, involving the combined efforts of the NLC, the CPA, and industry self-regulation bodies like ASA and WASPA.

Our major recommendations are as follows:

- It is recommended that promotional competitions continue to be prohibited from requiring a subscription or consideration, and that the Lotteries Act, CPA, and Codes adopted by industry self-regulation bodies, all reinforce this point. This is important in distinguishing promotional competitions from other forms of gambling.
- Whilst maintaining the prohibition of a consideration for entry, it is recommended that the provisions in section 36(3)(a) of the CPA, in terms of which promoters are entitled to require participants to “bear the reasonable cost of posting or otherwise transmitting an entry form or device”, be maintained, and that such costs (currently a maximum of R1.50) be maintained, and reviewed on an annual basis.
- Whilst maintaining the prohibition of a consideration for entry, it is recommended that the provisions in section 36(3)(b) of the CPA be amended to clarify that promoters are allowed to require participants to purchase goods or services at their current market price in exchange for the right to participate in the promotional competition.
- Following Strachan (2016: 296), we suggest that the definition of a promotional competition removed by the Lotteries Amendment Act, 2013, should be reinserted, and that this should read: “‘promotional competition’ has the meaning set out in section 36 of the Consumer Protection Act, 2008”.
- Following Strachan (2016: 300), we suggest that the definition of a promotional competition in the CPA is clarified and simplified to avoid ambiguity. The following definition is proposed: “‘promotional competition’ means any competition, game, scheme, arrangement, system, plan or device for distributing prizes by lot or chance if it is conducted in the ordinary course of business for the purpose of promoting a producer, distributor, supplier, or association of any such persons, or the sale of goods or services, irrespective of whether a participant is required to demonstrate any skill or ability before being awarded a prize”.

This definition succeeds in capturing both the chance and gambling component as well as the broad business promotion objectives and characteristics of promotional competitions.

- Following Strachan (2016: 298), we suggest that the following authorising provision be inserted in place of section 54 of the Lotteries Act, which was repealed: “A promotional competition, as defined in the Consumer Protection Act, 2008, is authorised by the Act.”
- It is recommended that redundant references to section 54 (which has been repealed) are removed from the Lotteries Act, specifically references to section 54 (which has been repealed) in section 1 (definition of a participant), section 10(d), and section 56(b) and (c) of the Lotteries Act. These should be removed, and the relevant sections should cross reference to section 36 of the CPA instead.
- It is recommended that the threshold for the exclusion of competitions with prize values below a designated threshold be increased to R100.
- It is recommended that competitions with prizes falling below the stipulated threshold are exempted from section 36 of the CPA’s requirements. Following Strachan (2016: 299), section 36(12) of the CPA should be amended to read: “The provisions of section 36 do not apply to a promotional competition unless the value of any prize in that competition exceeds the monetary threshold prescribed in terms of subsection 11”.
- It is recommended that Regulation 11(5) of the CPA Regulations be amended to clarify the oversight and certification requirements for promotional competitions. The independent professional employed to certify the competition should not be required to supervise all aspects of the competition. Instead, they should only be required to certify that the draw was random and fair; and that the relevant provisions of the CPA, including the prohibition of a consideration, and stipulations regarding marketing and prize size, have been complied with.
- It is recommended that the requirements in Regulation 11(5) of the CPA Regulations for the oversight of promotional competitions by an independent professional should be clarified and simplified to reduce the cost of compliance. Certification need not focus on all aspects of the scheme, but rather key aspects, which are often not properly monitored, including the integrity of number selection and confirming that no consideration or subscription was required, that marketing did not make any unrealistic or unreasonable promises, and that prizes were not made conditional on any additional payment.



- It is recommended that independent industry self-regulation be encouraged, and that industry bodies are encouraged to develop their own codes of practice for promotional competitions, along the lines outlined in the WASPA Code, and the UK CAP Code. These self-regulatory bodies should be encouraged to actively monitor their members and resolve complaints from the public efficiently.
- It is recommended that organisers of promotional competitions be required to join an Industry Association and submit to its self-regulatory codes relating to sales promotion, in general, and promotional competitions, in particular, where such codes exist.

## 6.5 SOCIETY LOTTERIES

A society lottery means a lottery promoted on behalf of a society that is established and conducted wholly or mainly for purposes not for private gain or commercial undertaking.

Any society wishing to promote a lottery must be registered with the NLC.

### 6.5.1 MODUS OPERANDI: HOW THE GAME IS PLAYED

Society lotteries are used primarily by schools, churches and charities for fund raising purposes.

A society is defined in the Lotteries Act as *“including any club, institution, organisation or association of persons, and any separate branch or section of such a club, institution, organisation or association”*.

There are strict criteria governing the uses to which a society lottery might be put. The total proceeds of a society lottery after deduction for amounts of expenses and prizes, must be applied solely to the following:

- (a) recognized charitable purposes;
- (b) participation in or support of sport or cultural activities;
- (c) other purposes not described in (a) or (b) but which the NLC approves and which are purposes neither of private gain nor of any commercial undertaking.

Organisations may not conduct more than six society lotteries annually, and the maximum value of both tickets and prizes are prescribed by the Minister.

## 6.5.2 REGISTRATION AND MANAGEMENT OF SOCIETY LOTTERIES

The criteria for registering and managing society lotteries are very onerous; and are set out in sections 41-52 of the Act. These include detailed requirements for the certification of lottery managers, and complex audit requirements.

There is plenty of paperwork to get through and a fee to be paid.

## 6.5.3 NON-COMPLIANCE

Society lotteries are not particularly successful. The Illegal Lotteries Study estimates that only R1.6 million was collected over a two-year period in 2012-14, with an average ticket price of R150. Schools conducted most society lotteries.

This does not pose a threat to the National Lottery.

There appears to be high levels of non-compliance, and it is clear that many organisations conduct lotteries without applying for a licence. These lotteries are unauthorised, and are therefore illegal lotteries.

Whilst these illegal society lotteries are unlikely to pose a financial threat to the National Lottery, the lack of respect for the law, and a widespread belief that no one is likely to enforce the provisions in the Lotteries Act, is concerning.

In part, this is due to ignorance. Organisers believe that because their scheme is very small, and used only for charity, there is no need to apply to the NLC for a licence.

Some societies claim that the cost of applying for a society licence (to raise money) is prohibitive.

## 6.5.4 THE PROS AND CONS OF REGULATING

Society lotteries are a good way for deserving societies to raise money. They have the potential to help promote the sustainability of many not-for-profit organisations.

As these are lottery schemes, it is correct that they are regulated in terms of the Lotteries Act. Our biggest concern is that the cost of regulating society lotteries is greater than the benefits incurred.





From the NLC's perspective, very little money is collected in application fees.

From the not-for-profit organisation's perspective, the application procedures are too onerous, and it is only relatively affluent institutions, like private schools, that are able to engage the services of an attorney to apply for their licences.

## 6.5.5 RECOMMENDATIONS

In the terminology adopted in the *Illegal Lotteries Report*, we believe that the existing legislation should be **enforced**, with minor amendment.

- (1) It is recommended that the application process be redesigned to make it user-friendly. If possible, it should be entirely online.
- (2) It is recommended that the NLC embarks on a proactive education drive, in which it reaches out to schools, churches and related organisations, and teaches them about the benefits of registration, and the process that has to be followed.
- (3) It is recommended that a system of exemptions be introduced for society lotteries with a total prize value below a stipulated threshold.
- (4) It is recommended that application fees be reduced or scrapped.
- (5) At the same time as we relax the criteria to apply for a licence, it is recommended that the NLC increase its capacity to inspect and monitor society lotteries.

## 6.6 OTHER UNAUTHORISED LOTTERIES

Unauthorised lotteries are, by definition, illegal lotteries, as they are not authorised by the Lotteries Act or any other law. Part of the rationale for this report is to investigate the feasibility of regulating some of these lotteries. Where the benefits of regulation exceed the costs of prohibition, and where the regulation of these schemes will not expose the public to significant harm, then, as with fahfee above, a case can be made to license and regulate particular schemes. This is not the case with either of the schemes discussed here.

### 6.6.1 INTERNATIONAL LOTTERIES

International lotteries are lotteries offered in jurisdictions outside the Republic of South Africa. Unlike bets placed with bookmakers on the outcome of a foreign lottery, here players participate directly in the lottery, as their subscription becomes part of the prize pool.

### **6.6.1.1 Modus operandi: How the game is played**

The market for foreign lotteries is growing rapidly, driven by a massive expansion in internet access and the ease of online monetary transactions.

In most cases, bets are placed via the internet. Players open an account with a service provider, and transfer funds into this account prior to play. The service provider will purchase tickets and resell them to players outside the jurisdiction in question, for a small fee.

Service providers collect prize money on their customer's behalf, and will transfer this back to the player's account in South Africa on instruction.

Players are at the mercy of service providers, and usually have very little protection should any queries arise about any aspect of the game or the processing of payments.

According to the *Impact of Illegal Lotteries Study* (NLC 2016: 58), players spend a total of R5.92 million annually on international lotteries, money that is diverted away from the National Lottery, depriving the NLDTF of R1.60 million.

### **6.6.1.2 Legislation**

Participation in foreign lotteries is prohibited in terms of section 59 of the Lotteries Act, which states:

*“In a prosecution arising from anything done or not done in the Republic in connection with a lottery or sports pool, it shall not be a defence merely to prove that the management, conduct or business of or concerning the lottery or sports pool in question is or was wholly or in part carried on at a place outside the Republic.”*

It is an offence to receive payment for any gambling winnings outside the Republic. In terms of section 16(4)(b) of the National Gambling Act, confiscated winnings are to be handed over to the Unlawful Winnings Trust, and the Board may apply to the High Court to have such winnings forfeited to the state.



The need to apply to the High Court for forfeiture has proved cumbersome. The National Gambling Amendment Bill, 2017, enhances the powers of the regulator, and replaces section 16(4)(b) with a clause stating that unlawful winnings confiscated “shall be automatically forfeited to the National Gambling Regulator after the investigation is concluded”.

Greater pressure is placed on banks and internet service providers to monitor transactions, and to prevent their clients from making payments to, or receiving payments from, online lottery and gambling providers. Section 76A(2) of the National Gambling Amendment Bill, 2017, states that:

*“No financial institution is allowed to process payment transactions for illegal gambling activities to which this Act applies and which is prohibited under the Financial Intelligence Centre Act (Act 38 of 2001).”*

### **6.6.1.3 The pros and cons of regulating**

It is difficult to imagine how either the NLC or the NLDTF might benefit from the authorisation of foreign lotteries in South Africa.

From the perspective of the National Lottery, this represents a growing and unwarranted challenge to their monopoly. Money spent on foreign lotteries is money lost to the country. Operators do not pay South African tax, and do not make any contribution to the NLDTF.

Players enjoy very little protection when participating in foreign lotteries, and even less so when bets are placed via service providers or intermediaries.

### **6.6.1.4 Recommendation**

In the terminology adopted in the Illegal Lotteries Report, we believe that such schemes should never be authorised by the NLC, and believe that existing prohibitions should be **enforced**.

- (1) It is recommended that all prohibitions pertaining to participation in foreign lotteries remain.
- (2) It is recommended that the NLC work closely with the National Gambling Regulator, banks, the Reserve Bank, the Financial Intelligence Centre, and SARS, to identify and take action against illegal online gambling and lottery transactions.
- (3) It is recommended that the NLC work closely with Internet Service Providers (ISP’s) to better understand the operations of such schemes, and to develop strategies to close these down.

## 6.6.2 LOTTERY SCAMS

The growth in Internet connectivity and social media platforms has facilitated a cottage industry of lottery scams, and it is almost impossible to imagine someone who has not received an email or an SMS inviting them to participate in a fantastic sounding scheme.

According to the *Impact of Illegal Lotteries Study* (NLC 2016: 58), players lose a total of R10.48 million annually on lottery scams, money that is diverted away from the National Lottery, depriving the NLDTF of R2.83 million.

In addition to their direct financial impact, lottery scams help to undermine the public's trust in lotteries generally.

### ***6.6.2.1 Modus operandi: How the game is played***

Lottery scams seek to entice unsuspecting members of the public to respond to an invitation to collect a prize. In order to receive the prize, players are expected to pay an advance fee, which is then stolen by the operator. The term “advance-fee fraud” scheme is often used to describe such scams.

Most but not all lottery scams originate from outside the country.

### ***6.6.1.1 Legislation***

Lottery scams are clearly fraudulent, and fall outside the ambit of the Lotteries Act. They are best dealt with in terms of The Prevention of Corrupt Activities Act (No. 12 of 2004).

### ***6.6.1.2 The pros and cons of regulating***

There is nothing to be gained from regulating advance fee type schemes.

Even if we wanted to, criminal activity can never be authorised by any regulatory authority.



### **6.6.1.3 Recommendation**

In the terminology adopted in the *Illegal Lotteries Report*, we believe that such schemes are inherently fraudulent, and that all prohibitions against such schemes be **enforced**.

- (1) It is recommended that all prohibitions pertaining to advance fee schemes remain.
- (2) It is recommended that the NLC work closely with the National Gambling Regulator, banks, the Reserve Bank, the Financial Intelligence Centre, and SARS, to identify and take action against the operators of such schemes.
- (3) It is recommended that the NLC work closely with Internet Service Providers (ISP's) to better understand the operations of such schemes, and to develop strategies to close these down.

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