Report From Agency

PROPOSED ORDER OF THE DEPARTMENT OF REVENUE REPEALING, RENUMBERING, RENUMBERING AND AMENDING, AMENDING AND CREATING RULES

The Wisconsin Department of Revenue hereby proposes an order to: **repeal** Tax 61.085(4)(a)2.; **renumber** no sections of this rule; **renumber and amend** Tax 61.08(14)(c) and (d); **amend** Tax 61.02(6), Tax 61.08(13)(c)1., Tax 61.08(14)(bm), Tax 61.08(17)(b), Tax 61.08(18), Tax 61.08(21), Tax 61.08(21)(g), Tax 61.08 (Note:), Tax 61.085(3)(a), Tax 61.085(4)(b), Tax 61.10(title), Tax 61.10(2), Tax 63.06(11)(c)1., Tax 63.06(11)(c)2., Tax 63.06(11)(c)3., and Tax 63.06(11)(d); **repeal and recreate** no sections of this rule; **create** Tax 61.02(1m), Tax 61.08(11)(h), (j) and (k), Tax 61.08(13)(e), Tax 61.08(14)(c), Tax 61.08(15)(title) and (15)(a) and (b), Tax 61.08(17)(a)4., Tax 61.08(22)(title) and (22)(a), (b) and (c), and Tax 61.25(title), Tax 61.25(1), (1)(a), (2), (3), (3) (a) to (h), (4) and Tax 61.25 (note:), **affecting small businesses,** and **relating to** creating billing terms options for Wisconsin Lottery retailers, creating additional shipping options at cost in situations where the retailer requests those options, correcting minor requirements that currently exist in the lottery Retailer Performance Program, creating rules that satisfy the voluntary disclosure requirements of 2003 Act 145, and correcting minor technical problems in Chapters s. Tax 61 and 63 of Wisconsin Administrative Code.

Analysis by the Department of Revenue

Statutes interpreted:
ss. 565.02(4)(g) and 565.10(14)(b)3m., Stats.

Statutory authority:
ss. 227.11(2)(a) and 565.10(14)(b)3m., Stats.

Statutory small business review:
ss. 227.114(2), Stats.

Explanation of agency authority:

The proposed order is intended to improve Chapters Tax 61 and Tax 63, Wisconsin Administrative Code.

In Chapter Tax 61, the Wisconsin Lottery is proposing an amendment to the rule authority for current retailer billing terms, consistent with changes to s. 565.10 (15) and which were made as part of 2005 Wis. Act 25, s. 2427b., that amended the time period

within which the lottery must bill retailers from not less than weekly to not less frequently than once every 60 days. The lottery is also proposing language to broaden its ability to offer to retailers the option to pay the cost of additional shipping of ticket inventory should the retailer request additional shipments. Also proposed is language to amend minor requirements which currently exist in the Retailer Performance Program (RPP) and that the lottery has determined are not consistent with the program intent. The proposal will also create rules that satisfy the voluntary disclosure requirements of 2003 Act 145, and will also correct minor technical problems in both chapters.

In Chapter Tax 63, rule amendments are proposed to clarify the manner in which non-profit retailers should return product for credit with the lottery.

Related statute or rule:

The Wisconsin Lottery maintains Chapters Tax 61, 62 and 63. Further, ss. 20.75 and ss. 25.566 and ss. 565, Stats., are all relevant to the Wisconsin Lottery. This proposed rule order directly affects Chapters Tax 61 and 63, and draws on ss. 565, Stats.

Plain Language Analysis

The proposed order is intended to implement changes that will improve the methods and processes that the Wisconsin Lottery uses to serve its retailer business partners. Nearly all of the proposed changes generate no increased cost of compliance for lottery retailer small businesses, and in some cases may slightly reduce some operating costs.

The proposal enables the lottery to offer improved billing terms to retailers which are more in keeping with both lottery industry and other retail industry standards. Billing terms are the processes by which a retailer is billed for ticket inventory. Anticipated improvements in the billing terms should result in terms that are easier to understand and that require less overall labor, thereby resulting in some labor savings for retailers. The lottery is proposing the creation of a “Billing Procedure” document, drafted in plain language, to aid retailers in understanding lottery billing practices. Consistent with these changes, the agency is also pursuing electronic methods of providing billing information directly to retailers, which should increase these efficiencies.

The proposed language also permits the agency to extend to retailers the option to pay additional shipping costs should the retailer request additional shipments on dates other than the retailer’s assigned shipment date(s). Any expenses will be limited to the actual cost of the delivery, and the proposed language would only apply if the lottery implements assigned delivery dates for retailers. Currently, the agency does not assign shipment dates to retailers, but may need to do so in the future dependent upon how new billing terms or delivery methods are implemented.

The proposal amends minor requirements which currently exist in the Retailer Performance Program (RPP) and that have been determined to be inconsistent with the program intent.

The proposal also clarifies the concepts of suspension and termination of retailer contracts. Further, the proposal will create rules that satisfy the voluntary disclosure requirements of 2003 Act 145, in which the lottery must identify when it may use discretion in the event of the disclosure of a non-compliance issue.

Last, the proposal clarifies language on the manner in which non-profit retailers should return product for credit with the lottery.

Federal Regulations Review

There is no relevant outstanding federal legislation that would require comparative review for the changes proposed under either Chapter Tax 61 or 63.

Adjacent States Review

Regarding the changes to Chapter Tax 61, the statutes and administrative rules of Illinois, Iowa, Michigan and Minnesota (all of which have state lotteries) were researched, and each state codifies more or less lottery retailer policy of import to small businesses. As a consequence, the Wisconsin Lottery's administrative rules may be more or less detailed when compared to a given state. The following state's laws were reviewed:

- State of Michigan: s. 432.1 – 432.38, Stats., and R432.1 – 432.38, Admin. Code.
- State of Minnesota: s. 349A, Stats., and 7856, Admin. Code.
- State of Illinois: s. 20 ILCS 1605, Stats. (taken from Chapter 120, various para.), and Section 1770, Admin. Code.
- State of Iowa: s. 99G, Statutes.

This analysis addresses the five major changes that are contained within the body of this rule order, which are retailer billing terms, discretion of enforcement per 2003 Act 145, ticket distribution controls, the industry development of reselling tickets, and retailer contract termination.

First, with regards to retailer billing terms, found as Sections 1 and 8 to 10 of this rule order, the adjacent states address the topic as follows:

- Michigan does not appear to make substantial statements in statutes or administrative rules, regarding retailer billing.
- Minnesota makes the following statement: "*Lottery retailers shall deposit in a bank account all money received by the retailer from the sale of lottery tickets, less the amount retained as compensation for the sale of tickets and credit for direct payment of prizes. The lottery shall have access through electronic funds transfer (EFT) to all money required to be deposited by lottery retailers.*" Significantly, no time period is identified in this rule.
- Illinois maintains significant statutory and administrative rule language regarding billing procedures, due payments that are missed, and serious delinquency. The language can be found under 20 ILCS 1605/21 (from Ch.120, par. 1171), and under Section 1770.90, Admin. Rules. While extensive, the fact that the entire procedure appears to be promulgated as administrative rules makes it potentially difficult to keep up-to-date with changes in banking, sales practices or other relevant technological developments.
- Iowa does not appear to make substantial statements in statutes or administrative rules, regarding retailer billing.

With regard to discretion of enforcement, created in Section 25 of this rule order and consistent with the requirements of 2003 Act 145, the adjacent states do not maintain a similar clause in lottery statutes or administrative code.

With regard to distribution of ticket inventory, affected by Section 17 of this rule order, the adjacent states address the topic as follows:

- Michigan, Minnesota and Iowa do not appear to make substantial statements regarding distribution of inventory in statutes or administrative rules.
- Illinois makes few substantial statements in statute or administrative rules. Generally, it appears that Illinois defines agents to potentially include distributors, such that it may have business partnerships with retailers who inventory and sell to other retailers, a practice not uncommon among larger state's lotteries. Rules addressing significant delinquency of payment (by agents or distributors) are maintained under 20 ILCS 1605/21, Stats. The lottery does not intend to pursue distributor relationships, as they do not fit well with our smaller population and market.

With regard to restrictions on the act of reselling, affected by Section 12 of this rule order, the adjacent states address the topic as follows:

- Michigan permits the Lottery to suspend, revoke or not renew a contract, if "...there is reasonable cause to believe that the retailer is engaged in fraud, misrepresentation, or illegal gaming." The statement does not directly identify reselling as fraudulent or illegal, but re-selling may be determined to be illegal dependent upon the facts of the particular situation.
- Minnesota makes general statements in statutes and substantial statements in administrative rules, regarding restrictions on the act of reselling. Similar to Michigan, Minnesota also has relevant general language. Under s.349A. Subd. 11, Stats., the director shall cancel the contract if a retailer "(a)(2) has committed fraud, misrepresentation, or deceit.", or if a retailer "(b)(4) violates a law or a rule or order of the director." Both these statements, while general, may also apply to reselling dependent upon the circumstances. Further, administrative rule 7856.6010, subpar. 2, clarifies the authority of the director, who may cancel, suspend or not renew a contract for a retailer who…" sold lottery tickets to a person who the retailer knows or has reason to know will resell the tickets to other persons." Notably, this language may restrict lottery players from buying tickets for friends, family or co-workers who have provided the buyer with the dollars necessary to make the face-value purchase. This could effectively ban the behavior used by a group of Wisconsin citizens who were employees of a Sargento, Inc. cheese processing facility near St Cloud, WI. The co-workers had organized a spokesperson to buy tickets for them on a frequent and regular basis, and as a group eventually won and shared the Powerball jackpot of August 5, 2006. Wisconsin's proposed rule order is drafted so that it would not ban this practice, provided all players fairly pay the stated ticket price for their ticket(s).
- Illinois makes a substantial statement in administrative rules, regarding restrictions on the act of reselling. Specifically, Section 1770.60 i) states in relevant part …"No 'service charge', 'handling fee' or other cost shall be added by any person to the established price of a ticket or share. No person shall charge a fee to redeem valid winning tickets or shares." Further, subsection l) also states, "Licensed agents shall….not conduct sales to off-premises

customers by telephone, mail, parcel, delivery service, or through an agent-sponsored vehicle such as a club, players' association, or similar entity".

- Iowa does not appear to make substantial statements in statutes or administrative rules, regarding the act of reselling.

With regard to retailer contract termination, affected by Section 18 of this rule order, the adjacent states address the topic in significant depth, as follows:

- Michigan maintains substantial statements in s. 432.23 (7) to (10), including language providing authority for probation, fines, removal of lottery terminal, assurance bonding, licensure requirements and revocation. Further, the above authorities are clarified under R 432.4 of administrative rules, with language that includes immediate suspension, revocation or denial of renewal, and provides a list of reasoned causes for the lottery to act.
- Minnesota maintains substantial statements in s. 349A. Subd. 11., Stats., regarding cancellation, suspension and refusal of renewal of retailer contracts. The language indicates that the director shall cancel the contract of a retailer who engages in any of a list of reasoned causes. Further, these authorities are clarified under 7856.6010 CANCELLATION, SUSPENSION, AND NONRENEWAL OF CONTRACT. Both the mandatory and discretionary authorities of the lottery director are noted, and the reasoned causes for both types of action are listed. Also provided is a clause that states that cancellation may occur if there is a material change in the qualifications for a retailer's contract or other considered factors.
- Illinois maintains little statutory language, but significant administrative rule language, regarding contract termination. Specifically, under Section 1770.40 License Revocation Without Prior Notice, language exists that covers how to define a person who is "ineligible for a license", and that the director may suspend or revoke the license of an agent for cause, and reasoned causes are listed. Language is provided for an appeal hearing, and relevant factors to be reasonably considered are listed.
- Iowa maintains little administrative rule language, but some substantive statutory language, regarding contract termination. Specifically, language is found under s. 99G.27 Lottery retailer licenses – cancellation, suspension, revocation, or termination. Authority for cancellation, suspension, revocation and termination are provided, and the reasoned causes are listed.

Summary of Adjacent State Review

In summary the adjacent states have a range of approaches to address retailer billing terms, from general to specific (and potentially unwieldy) language. Addressing discretion of enforcement, the states do not maintain similar language. In consideration of distribution of ticket inventory, the states maintain little language, and where present it controls distributor/agent authority, a practice less useful in Wisconsin's somewhat smaller market. Reviewing termination of contracts, the adjacent states have significant language, often providing one or more sections in both statute and administrative rules on the subject. Further, there appear to be separate considerations for suspension versus termination of contract, the separation of which are consistent with the language updated within this rule order.

In summary of the changes to Chapter Tax 63, the adjacent states do not maintain language that addresses the manner in which non-profit organizations are to conduct product returns.

Factual Data and Analytical Methodologies

Analytical methods were applied where necessary and possible. However, not all areas required analysis, and in cases where quantitative research was not feasible, anecdotal or related subject mater data was reviewed. For example, the issue of discretion of enforcement is driven by actions of the Legislature found in 2003 Act 145. The language created by the Act is clear, so no analysis was necessary.

Similarly, the language that clarifies suspension and termination of retailer contracts is considered a basic part of the due process of retailer licensing. The lottery's intention to separate the two issues improves clarity for the retailers, with no substantial change in the associated methods or practices. As the language is being separated for clarity and there is no substantial change, no analysis is needed.

The proposed language to address ticket distribution required review of administrative expenses over time as well as consideration of unit delivery costs. Both issues are discussed below under "Analysis of the effect on small business".

Regarding the issue of reselling of tickets, there is little quantitative data. Instead, a review was conducted of anecdotal information, supported by data from a Likert scale survey question. The question was written to generate psychographic responses to the query of the propensity of a lottery player to buy tickets for someone else, and the results are discussed.

Last, the remaining issue of billing terms has received, and continues to receive, significant analysis. A review of current billing terms versus new terms ideas was conducted, and a number of lottery retailers and industry groups were surveyed. The lottery has also conducted a review of the effects of billing terms changes on its expenses and revenue stream. Further, a fiscal impact on "average retailers" was conducted, to determine how changes of various billing terms options would effect the retailer's experience. Last, the lottery also modeled the affects of other factors (such as pack size) on the cash handling needs of retailers. The results are summarized.

Analysis of the Effect on Small Business

Generally, this portion of the analysis is given over to the impact of the proposed rule order upon small businesses. Specifically, any effect upon a lottery retailer is effectively an impact upon a small business, so the phrases 'small business' and 'lottery retailer' are effectively synonymous for purposes of this analysis. Each of the major substantive changes in this rule order is addressed separately.

Distribution Controls, proposed

Since fiscal year 2000, the lottery's instant ticket sales have increased significantly. Accordingly, a review of ticket distribution controls has been conducted, which include analysis of expenses over time, and review of the cost of delivery per unit. The result of the analysis is that ticket distribution expenses have grown, from $317,700 in FY2000 to $626,700 in FY2006, an estimated 49% increase. This is directly related to three factors: 1) increased gross sales of instant ticket inventory, 2) the increased number of price points of tickets desired by the marketplace, resulting in the shipping of

more packs of tickets, and 3) an increase in the number of orders per week the lottery is delivering to some retailers. The cost of a delivery is broken out as the set-up cost (currently an estimated $3.09 per order), and an additional $.04 to $.10 per extra pack of tickets, depending on the weight of the pack. Due to the set-up costs of an order, it is almost always less expensive to deliver 10 packs once a week, rather than delivering five packs in one order and then five packs in another order, on different days. In an effort to slow the growth of shipping costs, the lottery is considering improvements to how it delivers and monitors ticket inventory at retail.

Option 1: Consideration is being given to the market trend toward diverse price points, and to opportunities for just-in-time inventory control. One possibility is a restructuring of our ticket ordering, fulfillment and delivery systems, while another is the possibility of passing on costs of shipments beyond those shipments that are normally necessary. The first option has been pursued as a budgetary initiative proposal in 2007 SB 40, the goal of which is the implementation of new software and business processes.

Option 2: The second option requires a clarification of authority, which is being provided in Section 7 of this rule order, as the authority to charge retailers for the delivery expense of extra orders they request. The rule has been drafted using conditional phrasing that states that a retailer can only be charged up to the delivery cost, and only in cases where the retailer has requested the extra order. The lottery is pursuing both the options of improved inventory control systems and of expanded authority to charge retailers for extra orders, as they conceptually reinforce each other and permit the addressing of the broadest range of causes of increased costs. However, the lottery has no plans to implement this particular language on the date of promulgation of this rule order, or for the foreseeable future beyond that date. Rather, the language is being drafted to ensure that it is in place and ready if fiscal circumstances should warrant its implementation. If the language is implemented, the retailer will not pay for the first order shipped per week. With proper planning retailers can work with Lottery staff to avoid any additional shipping expenses.

Impact on small business: It is difficult to estimate exactly how much a given retailer would experience in charges for additional order(s) in a given week. However, the expenses would be consistent with those currently experienced by the lottery. For example, an additional order of 6 packs might cost $3.44 total ($3.09 for the first pack, and $.07 for each pack after the first.) Variations in the count and weight of packs in each order, as well as the current pricing structure itself, will cause some variation in the expense per order shipped. The variations will be generally limited to less than an estimated 10% of current cost, for the foreseeable future.

It is important to note that the lottery currently *does not* have plans to implement this rule language regarding retailers paying for additional orders. To do so would require the lottery to have delivery day assignments in place as of the promulgation date; this will not be the case. Instead, the rule order has been drafted using conditional language, and is being proposed now to ensure that the authority is available should the improvements under consideration prove workable. For example, computer software is being reviewed that offers the potential to track extra orders per week, for which the cost could be programmed to be billed to the retailer. Having the authority clearly stated well before implementation will provide the lottery with useful preparation time, in which retailers can be notified and given ample opportunity to review the initiative.

Conclusion: As of the date of promulgation, and for at least a calendar year after, there will be no effect on lottery retailers. Any intended activation of the rule would only be completed after significant notice of the event to all retailers, with retailers being given meeting opportunities with Lottery administration.

Reselling Controls, proposed

The issue of restricting the act of reselling of tickets to others, found in Section 12, is not easily quantified. However, there is anecdotal information that indicates many lottery players engage in some form of 'buy-tickets-for-friends' behavior. For example, husbands buy for wives and vice versa when they go fill up the car with gas, co-workers buy for each other when they stop at a store for a soda, and neighbors pick up an extra ticket for the neighbor that mowed their lawn when they were on vacation. Sometimes these purchases are gifts, and other times the buyer is doing the other person a favor to save time, and is reimbursed for the ticket.

To determine the extent of public awareness of this practice, the lottery gathered data on a Likert scale rating question as part of a recent market segmentation study. The question asked respondents if they strongly agree, somewhat agree, slightly agree, have no opinion, slightly disagree, somewhat disagree, or strongly disagree with this statement: "*I sometimes buy scratch games as gifts for friends or family.*" Respondents were asked pick the answer that best matched their behavior.

Public perception: Of 327 valid respondents, the top three "boxes" (responses ranging from slightly agree to strongly agree) show that 63.9% of respondents do in fact feel that they buy a lottery ticket for someone else at least sometimes, while only 21% responded that they have virtually no propensity to buy tickets as gifts. The question was not researched particularly in support of this rule order, but rather was part of a much larger market segmentation study which is refreshed every two years by an independent, contracted research firm. The data was collected during the month of June, 2006, in a state-wide survey process. While not strongly quantitative, the result does reinforce the notion that a lottery ticket is viewed by the majority as a potential gift or favor to someone else. Implementing a ban on this would not only prove effectively impossible to enforce, but also appears contrary to lottery culture as viewed by player citizens.

Illicit behaviors noted: In contrast to the positive perceptions noted above, it has unfortunately come to the attention of the lottery industry that there are 'subscription services' forming via telephone, postal mail and on the Internet. These services offer to wager on behalf of a player, usually at the price of a ticket plus a service charge, and send him or her tickets either via some electronic means or through the mail. Depending on circumstances, mailing lottery tickets ordered by telephone or via the Internet may violate federal laws. Worse, the services are often structured so as to act as an "agent" or "retailer" of lottery products without actually holding a valid lottery retailer license in the state in question. Further, the industry occasionally uncovers unscrupulous practices, wherein players do not receive the promised ticket or instead receive a 'ticket' that somehow violates one or more of the fair lottery concepts of random chance, consideration or prize.

Impact on small business: It is difficult to identify the number or range of impact these self-styled 'retailers' have upon lottery retailers or players, but some loss of retail sales opportunity is occurring. The Wisconsin Lottery has proposed language that permits 'friend and family' purchasing but bans subscription services, and has also adopted language from the adjacent states to address issues of "service fees" and "charging to validate", found under Sections 3, 4 and 5.

Conclusion: The impact upon lottery retailers of this language change should be negligible to slightly positive. The language does not ban 'friend or family' purchases as gifts (which would be sold by retailers), but does clarify that it is illegal for unscrupulous parties to pretend to be a legitimate retailer when they are not or to apply service fees or validation charges to players.

Billing Terms Authority, proposed

The remaining issue of billing terms as proposed under Sections 1 and 8 to 10 has been analyzed at several levels. The lottery is clarifying authority with respect to being able to offer new, more retailer-friendly billing terms, consistent with changes to s.565.10(15), made as part of 2005 Wis. Act 25, s. 2427b. The lottery will maintain the new document, called the "Billing Procedure" document, which will outline billing terms and procedures in concise and retailer-friendly terminology. This document will be maintained similar to lottery's current product "Features and Procedures" documents, under s.565.27 (1), Stats. The document will draw its authority from the language in this rule order.

Background: The lottery currently bills a retailer this week for a pack of tickets delivered last week. Most retailers' accounts are then swept by banking electronic file transfer (EFT) within 5 days of the day the liability is recognized. To help offset the amount of cash the retailer must keep on hand to pay for the packs, the lottery discounts from the price the full value of the retailer's commission, and also discounts an estimate of the amount of guaranteed low-end prizes (or GLEPS), those prizes which are worth $49 or less and randomly enclosed in the pack.

For example, a pack of 400 tickets is priced at $400, but the retailer is first credited $25 (equal to the 6.25% commission) and then an additional credit estimated at roughly $162.50 when the pack is billed, to cover the GLEPS prizes of that game which the retailer will likely pay out in the future. The retailer then owes $212.50 the week after the pack is delivered for sale, calculated as $400 – ($25 + $162.50). While the GLEPS value is a necessity of product design, it varies by game and can cause confusion for retailers.

This GLEPS Discount process was once considered industry-standard, but is now significantly outdated. Several industry developments have occurred since 1989, including cross-validation, the ability of one retailer to redeem winning tickets sold by another retailer. These developments have caused GLEPS Discount billing to be difficult to learn and sometimes confusing. Further, the current billing practices do not lend themselves to cash accounting, and do not align well with incentive promotions and other business practices of Lottery retailers.

New Billing Terms considered: The lottery is moving forward with new billing terms, and has researched and discussed terms including "*net 45 days, 75% validation*", "*net 30 days, 75% validation*" and "*net 30 days*", among other options. The concept of terms of *net X days* is well known to retailers, as many of their wholesale suppliers offer very similar terms. Under this concept, a retailer has x days from delivery to sell a unit of product, before being asked to pay the wholesaler for it. The concept of "*75% validated*" is a similar process unique to the lottery industry, wherein a pack is billed when the lottery identifies that 75% of the tickets in the pack have been computer-scanned for validation. Therefore terms of "net X days or 75% validated" would mean that a retailer is billed for the pack when X days have passed or when the pack is 75% validated, whichever comes first.

Consistent with s.227.114(4)(b), Stats., the lottery has contacted representative trade associations as well as corporate and independent retailers, to receive feedback about the billing terms options. The intent to change the terms has been discussed, both regarding changes to the time between delivery and billing, as well as regarding the types of mathematic terms the retailer might experience. The agency also reviewed the impact upon its revenue stream, by considering a range of alternative billing terms.

Feedback: The responses from lottery retailers thus far have been generally very positive, with few negative comments focused primarily in one area. In particular, retailers

with headquarters or outlets in adjacent states have experience with net X days and 75% validation tracking. From their feedback, retailers prefer by a wide margin the net X days, with no validation percentage tracking. Their reasoning is that the validation percentage causes confusion, as retailers don't know and can only guess when the pack will come due for payment. It may come due earlier than expected if a large number of validations occur, thereby making planning for the payment and related cash handling more difficult. Ideally, billing terms that are purely net 30 days allow retailers to plan that in the fourth week, the payment of a pack will be due, regardless. This style of billing is consistent with many of the other wholesaler/ distributor relationships that retailers maintain. It also allows the retailer significantly more time to sell the product and retain the cash necessary to meet the future obligation of the pack cost.

Impact on small business: While retailers receive more time, under new terms, to sell through a pack of tickets, they could in theory be responsible for a somewhat larger sticker price for each pack. This is because lottery intends to greatly simplify the accounting of lottery packs by eliminating the discounting of GLEPS that normally occurs when the pack is billed. This, and its related cross-redeem calculations, are the source of much confusion among retailers accountants. The lottery intends to keep the commission discounting on the pack price, but not GLEPS discounting. Therefore, instead of a pack of 400 tickets that costs $212.50 the week after it is shipped, the retailer will be billed for a pack of 400 tickets that costs $375.00 the fourth week after it is shipped, allowing more time for the retailer to sell the product. Also, the retailer will still be receiving credits each week for winners actually scan-validated, consistent with how the current system provides credits. The combination of more time to sell the product and the continuation of currently-offered credits for validations will help ease the financial impact of the perceived sticker price of a pack.

Related improvements to aid retailers: To further alleviate the financial impact on retailers, the lottery has changed the base ticket count of all $1 dollar scratch ticket packs. The lottery identified 300 count packs as a better fit with the product life cycle of $1 games, rather than the 400 ticket packs currently used. This change will help retailers sell through the pack faster, thereby avoiding having too many tickets unsold when the billing comes due. As of Game #711 *Moola Tripler,* launched in June of 2007, the count of tickets dropped from 400 tickets to 300 tickets per pack, for $1 game titles.

Continuing the comparison above, a 300-count pack of $300 under the current billing method would cost an estimated $162 instead of $212.50. Further, a pack valued at $300 and offered at net 28 days (possible new terms) would cost $281.25 the fourth week after it is shipped. When a 400 count pack and a 300 count pack are compared, using net 28 days, the difference is $93.75 less in cost to the retailer ($375.00 vs. $281.25), for the same price point and same amount of time to sell. Ultimately, for a 300-count pack with net 28 days terms, a retailer would have an additional three weeks in which to sell the pack and will still be receiving the validation credits as noted above. Given current selling behaviors, the lottery anticipates that an average retailer will sell through the pack mid-week 3, well before the expense comes due, and therefore have the cash already on hand to pay the bill. Overall, the potential change in billing terms to a 28-day cycle will not have a negative effect on the winning credits the retailer receives, nor will it have a negative effect on the retailer's commissions.

Intended implementation: The agency has considered the positive retailer feedback regarding retailer accounting and cash handling, as well as the impact that net X days terms has on the cash handling of retailers, and has committed to drafting the first Billing Terms Procedure document in such manner as to offer net 28 day terms without validation tracking as the new retailer billing terms, consistent with retailer feedback. Net

28 days is easier to understand and is as close as the lottery can match to the "net 30 days" terms of similar retail wholesalers. This will allow retailers at least 28 days to sell through a pack before it is billed, and will result in simpler accounting methods. This change also allows the lottery to consider shorter terms for retailers who may be at financial risk or who fail to maintain good payment history, which in turn will reduce the lottery's exposure to the financial risk that less well organized or less responsible retailers may pose. The document will also address relevant issues such as electronic funds transfer (EFT) banking options, and the rights of retailers with respect to ticket inventory returns. Other subject matter will be added as necessary. A first draft of the document will be available for public review the week before the public hearing for this rule order, and can be requested via the contact information that follows.

Conclusion: Ultimately, the combination of new billing terms, reinforced by new pack size, should help ease the financial and labor burdens that lottery billing currently places upon retailers. The impact will ultimately be a reduction in expense per pack, once all the aspects of net 28 days billing terms are in place. Therefore, the impact on lottery retailers will be slightly to significantly positive, depending on each retailer's sales history.

Agency contact person:

Regarding either this proposed rule order or other related rules, the public may contact James Amberson, Lottery Budget/Policy Analyst, at (608) 267-4840. Alternately, the public may e-mail Mr. Amberson at jjambers@dor.state.wi.us.

Submission of comments:

Any person or organization that wishes to submit comments may do so, and are encouraged to identify the section number, below, of this rule order to which each comment applies. Comments should be submitted by October 24, 2007. Persons or organizations may submit those comments by e-mail to the attention of Mr. Amberson at jjambers@dor.state.wi.us with the subject of "Billing Terms Admin Code". Alternatively, comments may be mailed to:

Wisconsin Lottery
Attn: James Amberson, Billing Terms Admin Code
P.O. Box 8941
Madison, WI 53708-8941

SECTION 1. Tax 61.02(1m) is created, to define 'Billing Procedure.'

SECTION 2. Tax 61.02(6) is amended, to add detail to the definition of 'Selling location.'

SECTIONS 3., 4. and 5. Tax 61.08 (11)(h), (j) and (k) are created, to clarify authority regarding the proper selling and validating of lottery products by licensed retailers.

SECTION 6. Tax 61.08 (13)(c)1. is amended, to add a circumstance under which the director may reimburse for tickets returned by the retailer to the lottery.

SECTION 7. Tax 61.08 (13)(e) is created, to identify the authority of the lottery director with regards to additional orders requested by a retailer.

SECTION 8. Tax 61.08 (14)(bm) is amended, to align the administrative rule to the relevant statutory language regarding the new 60-day billing window.

SECTION 9. Tax 61.08 (14)(c) is renumbered Tax 61.08 (14)(d) and amended, to provide language that will develop retailer billing policies consistent with other changes enacted in this rule order.

SECTION 10. Tax 61.08 (14)(c) is created, to align the administrative rule to the relevant statutory language regarding the new 60-day billing window.

SECTION 11. Tax 61.08 (14)(d) is renumbered Tax 61.08 (14)(e) and amended, to clarify how much a retailer can be assessed for a dishonored payment.

SECTION 12. Tax 61.08 (15) is created, to restrict retailers from bulk reselling activities, and to define the practice and an exception to it.

SECTION 13. Tax 61.08 (17)(a)4. is created, to provide language that permits retailers to return unsold tickets for credit in the event the lottery identifies a date for the complete settlement of a game.

SECTION 14. Tax 61.08 (17)(b) is amended, to clarify the requirements of redemption of lottery tickets or shares for prizes.

SECTION 15. Tax 61.08 (18) is amended, to add language consistent with new statutory requirements concerning the notice of the availability of top prizes.

SECTION 16. Tax 61.08 (21) is amended, to remove terminology that is being recreated in another section of this rule order.

SECTION 17. Tax 61.08 (21)(g) is amended, to remove terminology that is being recreated in another section of this rule order.

SECTION 18. Tax 61.08 (22) is created, to develop language that separates the concepts of retailer contract suspension and termination, clarifying and improving the meanings of both issues for retailers.

SECTION 19. Tax 61.08 (Note:) is amended, to add a proper statutory citation.

SECTION 20. Tax 61.085 (3)(a) is amended, to remove language that is being recreated in another section of this rule order.

SECTION 21. Tax 61.085 (4)(a)2. is repealed.

SECTION 22. Tax 61.085 (4)(b) is amended, to recreate language regarding the minimum sales level for a retailer to qualify for retailer performance program incentives.

SECTIONS 23. and 24. Tax 61.10 (title) and (2) are amended, to remove words that are overly restrictive of the circumstances under which a retailer can appeal to the director.

SECTION 25. Tax 61.25 is created, to provide language on Discretion of Enforcement as required by 2003 Act 145.

SECTIONS 26. and 27. Tax 63.06(11)(c)1. and 2. are amended, to improve the manner in which retailers return product for credit.

SECTION 28. Tax 63.06(11)(c)3. is also amended to improve the manner in which retailers return product for credit.

SECTION 29. Tax 63.06(11)(d) is amended, to clarify the authority of the administrator with respect to retailers' dishonored payments for lottery product.

SECTION 1. Tax 61.02(1m) is created to read:

Tax 61.02(1m) "Billing procedure" means the procedures used to collect revenue due the lottery by retailers consistent with s. 565.10 (15), Stats.

SECTION 2. Tax 61.02(6) is amended to read:

Tax 61.02(6) "Selling location" means each cash register or instant ticket vending machine at a Wisconsin lottery retail outlet where a lottery ticket is sold.

SECTIONS 3., 4. and 5. Tax 61.08 (11)(h), (j) and (k) are created, to read:

Tax 61.08(11)(h) The retailer may not add any service fee, handling fee or other expense to the purchase of a ticket or share without the written permission of the administrator.

Tax 61.08(11)(j) The retailer may not charge any service fee, handling fee or other cost when validating a ticket regardless of whether the ticket or share is a winning or non-winning ticket or share, without the written permission of the administrator.

Tax 61.08(11)(k) The retailer may not conduct sales of lottery tickets or shares to off-premises customers by telephone, email, instant messaging or similar electronic

means, or by mail, parcel, delivery service or similar service, without the written permission of the administrator.

SECTION 6. Tax 61.08 (13)(c)1. is amended to read:

Tax 61.08(13)(c)1. The tickets became unsalable due to any malfunction of lottery equipment used in the sale of the tickets or if the tickets are deemed to be misprinted or void, consistent with the features and procedures document of the game to which the ticket or share belongs.

SECTION 7. Tax 61.08 (13)(e) is created to read:

Tax 61.08(13)(e) The administrator may charge a retailer for shipments delivered on a date different than the retailer's scheduled order delivery date or shipped on a date other than the retailer's shipment date. If a retailer is charged, the expense shall be limited to the cost of the delivery.

SECTION 8. Tax 61.08 (14)(bm) is amended to read:

Tax 61.08(14)(bm) The retailer's electronic fund transfer account shall be debited no less often than every 60 days for tickets received within the last 60 days.

SECTION 9. Tax 61.08 (14)(c) is renumbered Tax 61.08(14)(d) and amended to read:

Tax 61.08(14)(d) If the retailer failed to place sufficient funds in the electronic fund transfer account for the tickets received, the retailer may not receive more tickets until the retailer pays the amount due the lottery consistent with pars. (bm) and (c), or until the retailer has signed an agreement with the administrator which indicates an alternative schedule of payment for outstanding debts consistent with s. Tax 61.02(1m). The administrator shall determine whether to offer an alternative payment agreement to a retailer on a case by case basis, taking into consideration the retailer's previous payment history.

SECTION 10. Tax 61.08 (14)(c) is created to read:

Tax 61.08(14)(c) A retailer shall remit to the lottery, no less frequently than every sixty (60) days, the proceeds from the sale of lottery tickets received since the last remission of proceeds. The terms of billing processes shall be set by the administrator.

SECTION 11. Tax 61.08 (14)(d) is renumbered Tax 61.08 (14)(e) and amended, to read:

Tax 61.08(14)(e) The administrator may assess the retailer a surcharge, an interest penalty, or both, for each dishonored retailer's check or electronic fund transfer. The surcharge shall be equal to the costs incurred, incident to each dishonor. Interest may be charged only in the event that a retailer account is referred for overdue collection, and may be assessed at a rate not to exceed 8.5% of the overdue amount.

SECTION 12. Tax 61.08 (15) is created to read:

Tax 61.08(15) BULK RESELLING WITHOUT PERMISSION IS PROHIBITED (Title).

(a) A retailer may not intentionally resell, or aid in the act of reselling, bulk tickets without the written permission of the administrator.

(b) For purposes of this section, “reselling” means selling or aiding in the selling of multiple tickets to anyone engaged in the business of selling lottery tickets for profit. Persons who participate in ticket buying pools among friends, family or co-workers are not involved in reselling, provided that all tickets are purchased by all participants at the price set by the lottery administrator.

SECTION 13. Tax 61.08 (17)(a)4. is created to read:

Tax 61.08(17)(a)4. If the lottery administrator announces a settlement date for a game, a retailer may return tickets for credit on or before the date provided that the retailer returns the tickets using the original packaging materials, or in a manner acceptable to the lottery administrator.

SECTION 14. Tax 61.08 (17)(b) is amended to read:

Tax 61.08(17)(b) The retailer shall redeem all prizes from tickets purchased at the retailer's outlet unless the features and procedures document for the game state otherwise.

SECTION 15. Tax 61.08 (18) is amended to read:

Tax 61.08(18) POINT-OF-SALE MATERIAL. The retailer shall maintain and display prominently lottery point-of-sale material, including the door decal, current game poster, current game player brochures and the ticket dispenser. The retailer shall maintain and display a sign provided by the lottery that indicates which games no longer have a top prize.

SECTION 16. Tax 61.08 (21) is amended to read:

Tax 61.08(21) GROUNDS FOR SUSPENSION . The retailer's contract may be suspended without prior notice by the Wisconsin lottery for any of the following reasons:

SECTION 17. Tax 61.08 (21)(g) is amended to read:

Tax 61.08(21)(g) The retailer failed to remit money owed to the Wisconsin lottery or failed to make payment on or before the settlement date.

SECTION 18. Tax 61.08 (22) is created to read:

Tax 61.08(22) GROUNDS FOR TERMINATION. The retailer’s contract may be terminated by the Wisconsin Lottery, regardless of whether the retailer has been previously suspended. Any issue which is grounds for termination may be considered instead for suspension, at the discretion of the administrator. The administrator may consider whether a retailer acted to promptly cure a cause within a reasonable time after notice, when reviewing the grounds for termination. The retailer’s contract may be terminated for the following reasons:

(a) The retailer failed to meet one or more of the qualifications for being a retailer under s. 565.10, Stats., or under this chapter.

(b) The retailer endangered the security of the lottery, or engaged in fraud, deceit, misrepresentation or other conduct in a manner that would cause perceptions prejudicial to public confidence.

(c) The retailer engaged in any practice identified under s. Tax 61.08 (21)(a) to (i).

SECTION 19. Tax 61.08 (Note:) is amended to read:

Note: Section Tax 61.08 interprets ss. 565.02 (3) (j), 565.10 (7) to (15), and 565.12, Stats.

SECTION 20. Tax 61.085 (3)(a) is amended to read:

Tax 61.085(3)(a) The retailer honors the current retailer contract, including any applicable addenda.

SECTION 21. Tax 61.085 (4)(a)2. is repealed.

SECTION 22. Tax 61.085 (4)(b) is amended to read:

Tax 61.085(4)(b) *Sales goals incentive.* The sales goals incentive component of the RPP shall pay a retailer an incentive based on an increase in the amount of sales over the appropriate sales history. The incentive shall be tracked, measured and paid separately for each product type. For each product type, a retailer shall satisfy eligibility requirements in sub. (3), sell a minimum amount of instant tickets as indicated under s. Tax 61.08 (11) (c), and qualify for the product type under sub. (5).

SECTIONS 23. and 24. Tax 61.10 (title) and (2) are amended to read:

Tax 61.10(title) Appeal procedure.

Tax 61.10(2) Within 30 calendar days of the mailing of the notice, the retailer may request a reconsideration by filing with the administrator a written statement setting forth the retailer's legal, factual or equitable arguments and submitting any supporting

documents. The request for reconsideration shall be deemed filed on the date it is received by the administrator.

SECTION 25. Tax 61.25 is created to read:

Tax 61.25 Discretion of enforcement.(title)

Tax 61.25(1)(intro.) Consistent with s.895.59, Stats., the lottery shall exercise the following discretion in the enforcement of rules and guidelines against a small business:

(a) For purposes of this section the definition of small business, under s. 227.114 (1), Stats., shall include any retailer who holds a contract under s. Tax 61.08, so that all retailers may expect the same treatment with respect to this section.

(2) If a retailer voluntarily discloses an actual or potential violation of lottery rules, guidelines, or terms of a contract with the lottery, the retailer shall be entitled to a reduction or waiver of any penalties associated with the disclosed potential violation. The amount of the reduction or the extent of the waiver shall be determined by the administrator on a case-by-case basis.

(3) Notwithstanding the provisions of sub. (2), no reduction or waiver may be granted for any of the following situations:

(a) The agency discovers the violation before the small business discloses the violation.

(b) The violation is disclosed after an agency audit or inspection of the small business has been scheduled.

(c) The violation was identified as part of the monitoring or sampling requirements that are consistent with the requirements under an existing permit.

(d) The violation results in a substantial economic advantage for the small business.

(e) The small business has repeatedly violated the same rule or guideline.

(f) The violation may result in an imminent endangerment to the environment, or to public health or safety.

(g) The violation is determined to be an act of deceit, fraud, misrepresentation or other conduct prejudicial to public confidence in the lottery.

(h) The violation may give the retailer an unfair economic advantage over another retailer.

Tax 61.25(4) A retailer may appeal a determination of inappropriate use of discretion as outlined in section s. Tax 61.10. The administrator shall review each appeal on a case by case basis.

Note: Section Tax 61.25 interprets ss. 565.10, 565.12, and 895.59, Stats.

SECTION 26. Tax 63.06(11)(c)1. is amended to read:

Tax 63.06(11)(c)1. If the tickets are defective, the administrator may allow the nonprofit organization retailer to make a return. The retailer shall return as many of the suspected defective tickets as is possible, using packaging that is opaque and can be readily sealed.

SECTION 27. Tax 63.06(11)(c)2. is amended to read:

Tax 63.06(11)(c)2. If the order was filled incorrectly by the Wisconsin lottery, the administrator may allow the nonprofit organization retailer to make a return. The retailer shall return any incorrectly shipped break-open tickets using packaging that is opaque and can be readily sealed.

SECTION 28. Tax 63.06(11)(c)3. is amended to read:

Tax 63.06(11)(c)3. If the shipment of tickets is unopened by the nonprofit organization retailer, the administrator may allow the retailer to make a return. To be considered unopened, the package shall contain all the tickets that it contained when delivered to the retailer and have the shipping seals intact and unopened.

SECTION 29. Tax 63.06(11)(d) is amended to read:

Tax 63.06(11)(d) The administrator may assess the retailer a surcharge, an interest penalty, or both, for each dishonored check or electronic fund transfer. The surcharge shall be equal to the costs incurred, incident to such dishonor. Interest may be charged only in the event that a retailer account is referred for overdue collection, and may be assessed at a rate not to exceed 8.5% of the overdue amount.

The rules contained in this order shall take effect on the first day of the month following publication in the Wisconsin administrative register as provided in s. 227.22(2)(intro.), Stats.

Final Regulatory Flexibility Analysis

This order does not have a significant economic impact on a substantial number of small businesses or lottery retailers. Retailers may experience a slight reduction in labor as improvements in billing methods are implemented. Also, a retailer may experience a new cost for extra shipments of lottery tickets, but only if the lottery determines that it is necessary to activate the language contained in Section 7 of this Rule Order. In that case, the cost will only be the expense to deliver any extra order, and will only be incurred by retailers who request the extra order.

Ultimately, this order does simplify and clarify a number of small business processes between the state and lottery retailers, and also improves the retailer performance program in ways which make the expected performance clearer and more consistent with state policy and lottery retailer activities.

DEPARTMENT OF REVENUE

Dated:_____

By:_____
Roger M. Ervin
Secretary of Revenue