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# Gambling in California

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### *I. Gambling in the United States*

*"Gambling is inevitable. No matter what is said or done by advocates or opponents of gambling in all its various forms, it is an activity that is practiced, or tacitly endorsed, by a substantial majority of Americans."*

-- *Commission on the Review of National Policy toward Gambling, 1976, p.1.*

In 1973, the Commission on the Review of National Policy toward Gambling was created to study gambling in the United States. The Commission began its report with the above statement and it is appropriate for this report. While the statement is merely the opinion of the Commission and cannot be easily proven, it is easy to understand how they formed their opinion. If you read the history section of this report, you will see that the popularity of legal gambling has waxed and waned, but has never disappeared. Illegal gambling, although we are ignorant about the full extent of it, has shown remarkable endurance. One industry observer noted, "There is a public demand to gamble, but there is no public demand for legalized gambling."<sup>1</sup> The acceptance of gambling today can be seen by the substantial numbers of players of the various state lotteries and similar illegal games.

This report will use the terms gambling and gaming interchangeably. Within the gambling industry, the term gambling has fallen into disfavor and is being replaced by gaming.

***Legal Gaming Has Expanded Greatly Throughout the Country.*** Legal gambling activities include state lotteries; parimutuel betting on horses, greyhounds, and jai-alai; sports book-making; card games; keno; bingo; slot machines; progressive slot machines; video poker machines; video keno machines; video blackjack machines; and video roulette machines. Not all of these are legal in all places. These activities have grown tremendously, especially when considering that virtually all have been only recently legal in most states. This growth of gambling has been remarkable: in 30 years gambling has transformed itself from sinful to well accepted.<sup>2</sup> But the spread has been inconsistent, with each state selecting the type of gaming that it supports or at least condones. Some states have casinos, but no lotteries. Other states have lotteries, but no casinos. Some have both.

Illegal gambling still exists and, by many accounts, flourishes.<sup>3</sup> Not surprisingly, there is not a lot of data about illegal gambling. The most popular forms of illegal games are "numbers," which is essentially a lottery, and betting with bookies, typically sports betting. Sports betting, in particular, is thought to amount to a large sum. Some analysts think it is the largest category of gambling after casino games.<sup>4</sup>

***Views on Gambling Vary.*** Gambling is regarded by some as a vice, a sinful activity which corrupts society. Others view gambling simply as a harmless form of entertainment. These contrasting views help shape the regulation of gambling. The regulation of gambling is unusual as society regulates gambling like no other business.<sup>5</sup> Overall, society has taken a cautious view of gambling. Only limited types of games are legal. Gambling is heavily regulated because of concerns about criminal involvement. Because of the large amount of cash involved, gambling is an attractive target for criminals.

Others look at gambling in economic terms. Legalized casino gambling, whether in Las Vegas, Atlantic City, or on Indian land, rose out of the desire for economic stimulus,

although other factors also played a role. Lotteries are regarded by state governments as a revenue-generating tool.

Why has gambling grown? There are a variety of possible explanations.<sup>6</sup> One explanation for the spread is that states need the revenue and are hooked on gaming funds. Another related view is that government has said it is acceptable, hence people are more willing to participate. Some observers attribute the domino effect. The domino effect of gambling occurs when one state legalizes gaming, other states legalize gambling so they do not lose money to their neighbors. The spread of lotteries can be seen as an example of the domino effect. The current wave of legal lotteries started in New Hampshire, spread to other North-Eastern states, and then across the nation. Right now, the states that do not have lotteries are clustered primarily in the South. Similarly, riverboat casinos were first legalized in Iowa, then Illinois, followed closely by Missouri, Indiana, Louisiana, and Mississippi.

Regardless of viewpoint, there is little doubt that gambling is a very popular activity in the United States. By 1994, every state except Utah and Hawaii had some form of legal commercial gambling. Casino gambling, including Indian gaming, is legal in 27 states and most of the casinos have been built in the last 5 years.<sup>7</sup>

***The Gaming Sector is a Large Entertainment Industry.*** In 1995, gambling in the United States grossed over \$40 billion in revenues. Although this total does not include illegal gaming, it is still quite large compared to some other entertainment industries. The same year, the estimated receipts for amusement parks were \$7 billion, including admission fees, sales of food and beverages, and other sales. The estimated receipts for movie theaters were \$5.5 billion.<sup>8</sup> Gambling is clearly a major form of entertainment.



Another way to look at gambling's relative popularity is through the public's participation. In 1993, the last full year before the baseball strike, 70 million fans went to the ballpark, while 92 million visited casinos.

The preceding comparisons were made using gross revenues, but the amount of money people spend gambling is usually measured by one of two methods.

- "Handle." A popular form of measurement is the handle, which is the total amount of money that a player spends purchasing lottery tickets, parimutuel bets, or playing casino table games or slot machines. Since the total amount includes winnings, it is a much larger number than what players actually lose.
- "Gross Revenues." The amount of money that bettors lose gambling is called gross revenue, or also known as consumer gambling losses. Gross revenues are the actual net income retained by the operator after the payment of prizes, but before deducting the other costs of operating the gambling establishment.

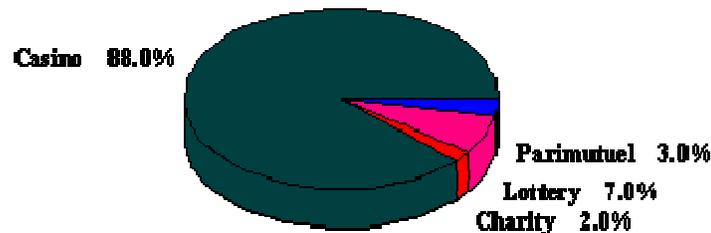
The handle is popularly used for measurement, but it can be misleading. Because it is the amount wagered before payment of prizes, the handle tends to inflate the economic importance of gambling. Gross revenues are a better measurement when comparing gaming to the rest of the economy.

An example may help illustrate the difference. A player spends a dollar playing video poker and wins \$4. The \$4 is fed back into the machine until she loses the \$4 plus her original dollar. In this example, the handle would be \$5. But the gross revenue and the amount the player lost out of pocket is only \$1.

***There Are Four Major Types of Legal Gambling.*** According to one well-known researcher, these include charitable gaming, parimutuel betting, casino gaming, and lotteries.<sup>9</sup> There is some potential confusion that may arise from these definitions. The definition of casinos include what most of us would expect, i.e. the Las Vegas-style casinos that are found in Nevada, Atlantic City, and a few other locales. In California, cardrooms advertise themselves as casinos, but they don't offer the games that one expects from casinos, namely banked games, especially slot machines. The cardrooms found in California are an anomaly and don't fit into the major categories. They are discussed later in Chapter V on "Gambling in California." The following chart shows the relative size of the different types of gambling.

## Casinos Account for Major Portion of U.S. Gambling Handle ...

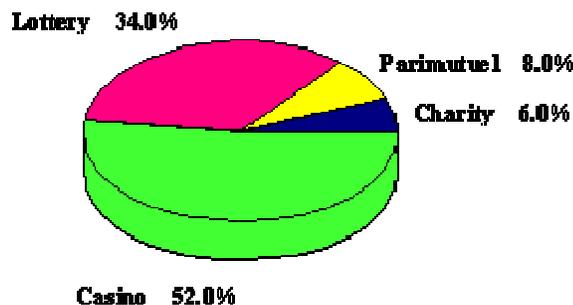
1995



Sources : International Gaming and Wagering Business, California Research Bureau

## But Relatively Greater Gross Profits go to Other Games

1995



Sources : International Gaming and Wagering Business, California Research Bureau

### *Charitable Gambling*

Charitable gambling is run for the benefit of nonprofit organizations, although the nonprofit may not necessarily be the operator of the games. Some examples of charitable gambling are PTA Monte Carlo nights and church raffles. The most popular form of charitable gambling is bingo. Charitable bingo is legal in all but five states. In California, bingo is the only charitable game that is legal.

Despite the nonprofit nature of charitable gaming, it has come under criticism. One reason is that it is the area of gambling that is the least regulated. As the tables and graphs show, it accounts for a significant amount of money even if the total is dwarfed by that of casinos. According to some industry observers, there are serious problems of fraud, theft, cheating, and accounting irregularities.<sup>10</sup> In California, charitable games have been victimized by robbers because of the large amount of cash generated by bingo.

### ***Parimutuel Wagering***

Parimutuel wagering refers to the type of gambling where the total prize pool is based upon the amount of money wagered. The more money gambled, the bigger the prize. Horse racing is the best known and widespread parimutuel betting event. Horse racing is the only form of parimutuel wagering legal in California.

Dog racing and jai-alai are less popular parimutuel betting events. Dog racing operates in 17 states, while jai-alai is legal in just three: Connecticut, Florida, and Rhode Island. Dog racing is, as suggested by the name, a race among greyhounds who chase after a mechanical rabbit. Jai-alai is a game played by two or four persons and its action is similar to handball.

Parimutuel wagering has not been able to compete well with the myriad of new forms and types of gambling. Observers attribute its decline to the complicated nature of the sports, especially for the new gambler.<sup>11</sup> The industry is changing, however, some racetracks are adding casino games. Situating casino games with the track exposes other gamblers to horses and thereby parimutuel wagering. In turn, this may lead to increased parimutuel participation.

### ***Lotteries***

Lotteries have a long tradition in this country. They were used to raise money in support of the first North American colonies. Lotteries continued to be used by the original thirteen colonies to raise necessary revenue for the development and the successful independent operation of the new settlements. Though early lotteries were successful in raising money, the scandals from crooked operations strengthened the hand of antigambling forces, eventually leading to prohibition of lotteries in many states. From 1894 to 1964 no legal government-sponsored lotteries operated in the United States. The long and colorful history of lotteries in the United States is described in more detail in the history section of this report.

***Legal Lotteries Experienced a Rebirth in the 1960s.*** The first legal lottery in the twentieth century was the New Hampshire Sweepstakes which began on March 12, 1964. Other North-Eastern states quickly followed. In 1981, Arizona became the first state west of the Mississippi to authorize a lottery. Currently 37 states and the District of Columbia operate lotteries.

### ***Casino Gaming***

Casino gaming is the largest part of the commercial gambling market. Casino gaming continues to grow in popularity, fueled by the creation of new casino destinations and the expansion of existing casino locales.

A casino is usually characterized by the offering of banked games. Banked games are where the house is banking the game and basically acting as a participant. That is, it has a stake in who wins. In contrast in a non-banked game, like the lottery, the operator does not care who wins. As noted earlier, cardrooms such as those in California are not included. They are often called casinos, but they do not offer banked games.

Currently, ten states have legalized some form of commercial, non-tribal casino gambling with banked games. These are what the typical observer would call Las Vegas style casinos.

The following chart lists the states and the year each made casino gambling legal. Note the rapid growth since 1989.

State	Form of Casino Gaming	Year of Legalization
Nevada	Unlimited Stakes	1931
New Jersey	Unlimited Stakes	1976
South Dakota	Limited Stakes	1989
Iowa	Riverboat	1989
Colorado	Limited Stakes	1990
Illinois	Riverboat	1990
Mississippi	Riverboat, Dockside	1990
Louisiana	Unlimited Stakes, Riverboat	1991
Missouri	Riverboat	1992
Indiana	Riverboat	1993

This chart does not include Indian gaming, which is discussed later.

For almost 50 years casino gaming was only legal in Nevada. There, legal state-regulated gaming was dominated by organized crime. In the late 1950s, the state first permitted publicly-held companies to own and operate gaming facilities, which eventually led to the entrance of companies such as Hilton and Ramada into the industry, improving the industry's reputation. It was at this time that intense gaming activity spread from

downtown Las Vegas to the Strip and began to grow in Reno and Lake Tahoe. Since then, gaming in Nevada, and especially Las Vegas, has become a multibillion-dollar industry that attracts millions of people each year.

Nevada enjoyed a long period with little legal competition. New Jersey's statewide referendum legalized gambling in 1976. The first Atlantic City casino opened in 1978. Since then, eight other states have legalized casino type gambling.

The first state that authorized one of the new wave of legalized casinos was in South Dakota. In 1989, South Dakota legalized limited-stakes casino gambling in the historic mining town of Deadwood. In 1990, Colorado followed when voters in that state approved limited-stakes casino gambling in three former mining towns: Cripple Creek, Black Hawk, and Central City.

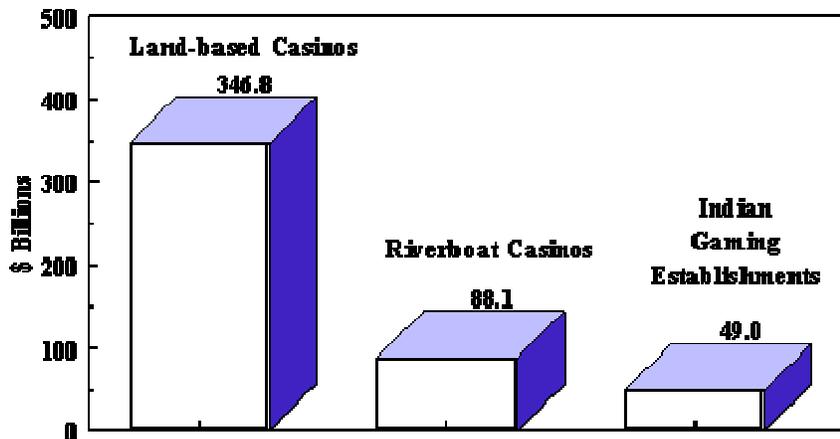
In 1989, Iowa and Illinois legalized riverboat casino gaming and, in April 1991, Iowa launched the first gaming vessel in recent U.S. history. Riverboat casinos are now legal in six states: Illinois, Indiana, Iowa, Louisiana, Mississippi, and Missouri. Currently there are about 65 boats operating in these states. The type of gaming allowed on riverboat casinos varies by jurisdiction. Generally, the states allow the playing of traditional casino games such as blackjack, roulette, and slots.

***Riverboats Present a Good Example of the Domino Theory of Making Gambling Legal.*** Illinois' statute was more liberal than Iowa's, leading to a riverboat regulation war. Gaming revenues began to decline in Iowa in 1993 when the riverboats moved out of Iowa to locations with more favorable regulations. Iowa had established a \$5 maximum wager and a \$200 per customer loss limit. Illinois did not have a wager or loss limit and the riverboat casino centers in Illinois were closer to population centers. In 1994, in an effort to reverse the industry's decline, the voters in Iowa voted to eliminate wager and loss limits.

The advent of riverboat gaming also led to increased Indian gaming, when Indian tribes were allowed to operate the same kinds of gambling allowed within a state. A Nebraska tribe even attempted to buy property in Iowa to open a casino.

***Riverboat Gaming Has Captured 20% of the Casino Market Share.*** Mississippi now has more gambling square footage than Atlantic City. The International Gaming and Wagering Business magazine reported casino revenue figures for 1995 as shown in the chart below.<sup>12</sup>

## Land-Based Casinos are Still Largest 1995



Source: International Gambling and Wagering Business  
Note: As measured by Handle.

There are two major categories of riverboat casinos, excursion and dockside. Excursion riverboats cruise along some waterway, while dockside casinos are tethered to the shore during operations. Dockside casinos are usually just a land-based casino on pilings or a floating, but not navigable, platform.

The excursion requirement was important in the beginning because it provided a subtle transition into legal gambling, giving the public an impression that the gambling could be isolated and controlled. The gambling takes place in a restricted location, namely on a boat traveling on the waterways and the amount of activity is limited by the length of the excursion. If the excursion is three hours, then the amount of gambling is limited to the three hours on the river, plus another half hour or so while the boat is tied up for loading and unloading. Many analysts believe that the perception that riverboat gambling would be physically contained made legal gambling an easier sell to the voters.

Some states are eliminating the law concerning the cruising requirement. Dockside casinos are more popular because some customers do not like to be cooped up for a set period of time, and some do not like having to leave when the ship is moored. Eliminating the cruising requirement also reduces the possibility of accidents on the waterways. Mississippi has no cruise requirements on their riverboat casinos. Other states allow for some flexibility for bad weather and choppy waters. According to a representative of Hilton Hotels Corp., which operates a riverboat casino in New Orleans, "admission revenues rise 40% and gambling revenues increase as much as 20%" when the ship is kept at the dock.<sup>13</sup> The riverboat casino industry is trying to convince other states to eliminate the cruising requirement. In this way, riverboat gambling has become an indirect path to land-based gaming.

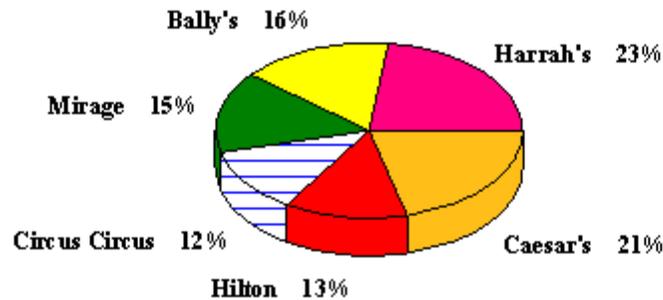
In 1992, Louisiana became the third state to legalize land-based casino gambling. Voters narrowly approved legislation to establish a riverfront facility in New Orleans. The legislation permits a single facility in downtown New Orleans and a temporary facility to be operational while the permanent facility is under construction. On November 21, 1995, the partnership that owns the casino venture filed for Chapter 11 bankruptcy. The temporary casino was closed and the construction of the new facility was halted while the organization went under restructuring. Harrah's is the lead partner in this effort. New Orleans is the first casino in a major city other than Nevada. Concerns about the industry's survival were allayed when casino gaming was ratified by a large margin of voters in a referendum in November 1996.

***Las Vegas Expands to Meet the Challenge From Competing States.*** With competition from new gaming locales and other parts of the entertainment industry, the owners of major casino properties in Las Vegas have not stood still. While other markets rely on their local population, the Las Vegas market is almost entirely reliant upon the tourist business that the casinos generate.

Many of the major developers are turning Las Vegas into a family-oriented destination resort, complete with grand spectacles and theme parks. In late 1993, Circus Circus' pyramidal Luxor opened, featuring an Egyptian theme and amusement park. Shortly thereafter, the Mirage's Treasure Island opened with a pirate theme and a regularly scheduled sea battle outside the facility. The new MGM Grand has a Wizard of Oz theme park. Las Vegas visitation in 1994 was very strong, up approximately 24% from 1993. Almost 30 million visitors came in 1994, approaching the level of Atlantic City.

As the following chart shows, the big operators in casino amusement are large publicly-owned companies. If the merger between Hilton and Bally's goes through, it will create the largest company in the country, surpassing Harrah's.

## Top U.S. Publicly-Owned Casino Companies



Source: Harrah's Casinos  
Note: Based on total casino revenues for these large companies of \$3.8 billion.

### *Indian Gaming*

Indian tribes have used their position as sovereign entities to develop a number of gaming establishments. Indian casinos operate in 22 states: Arizona, California, Colorado, Connecticut, Idaho, Iowa, Kansas, Louisiana, Michigan, Minnesota, Mississippi, Montana, Nebraska, Nevada, New York, North Carolina, North Dakota, Oklahoma, Oregon, South Dakota, Washington, and Wisconsin. This number is expected to grow.

The opportunity for economic development through gambling has piqued the interest of many Indian tribes. The U.S. Bureau of Indian Affairs reported that there are 545 federally-recognized Indian tribes in 35 states. Gambling on Indian-owned land has grown in popularity and there are approximately 150 to 175 casinos and bingo halls currently in operation.<sup>14</sup>

Gambling has represented an opportunity for tribal self-reliance and a chance to reverse some of the poverty that has affected many of the tribes. Indian tribes started offering games similar to those being offered by charities, such as bingo. In order to gain a competitive advantage, some tribes began offering high-stakes bingo, an option that was not available to the charities because of state laws. The growth of Indian gaming led to many court battles, including some important ones in California. This issue is covered in more detail in the section on Indian Gaming.

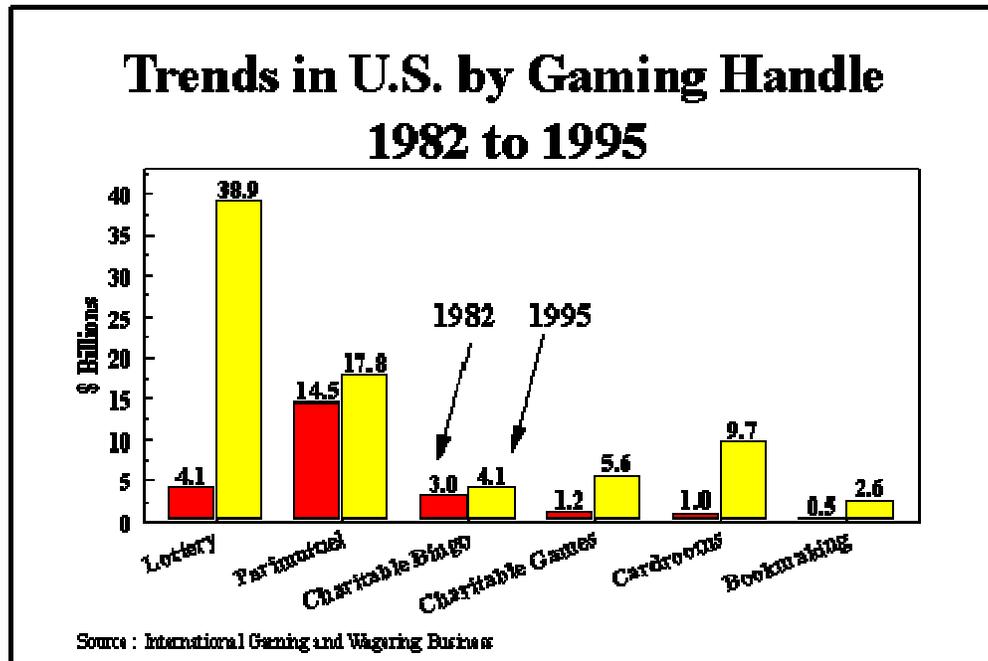
### *Illegal Gambling*

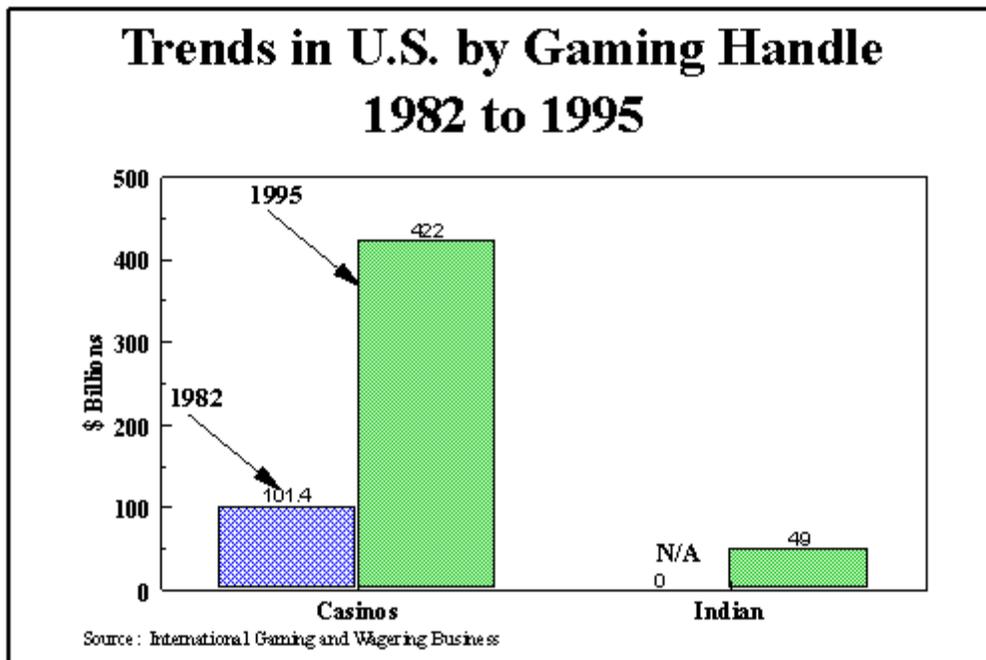
Illegal gaming is popular, though its popularity and prevalence are difficult to measure. An estimated \$32 billion was wagered illegally in 1986, resulting in gross revenues of approximately \$5.6 billion.<sup>15</sup> Another estimate places the illegal gaming handle at about

\$48 billion with gross revenues of \$2.4 billion.<sup>16</sup> The most significant forms of illegal gambling in the United States are numbers, betting with bookmakers or bookies, and sports pools or sports cards. The "numbers" game is similar to the lottery game. Bettors select numbers and hope theirs match the winning numbers that have been randomly selected.

Betting with bookies usually involves placing bets on the outcome of a certain event, such as a sporting event. Sports cards and pools are also bets involving sporting events. Most sports bets are between friends or acquaintances. A smaller amount is made with bookies and the bets are usually under \$100.

*All Types of Gambling Have Shown Growth.* Although there are numerous types of gaming, a common theme is that they are all growing. The following charts show the growth in the different categories of legal gambling.





***Gambling is Usually Regulated by a Commission Form of State Agency.*** Currently in the United States, 48 of the 50 states have legalized some form of gambling. Utah and Hawaii are the exceptions. Regulation of gambling activities across the nation is usually done by commissions.

#### ***Parimutuel Wagering***

- Forty-three states have parimutuel wagering (horse racing, dog racing, jai alai). Of these 43 states, the great majority have racing commissions whose sole purpose is to regulate parimutuel gaming.
- The exceptions are Connecticut, Florida, Iowa, Nevada, New York, South Dakota, and Wisconsin. These states have parimutuel commissions which regulate other forms of legalized gaming in that state, or have their parimutuel activities regulated by another commission. For example, parimutuel wagering in Nevada is regulated by the Nevada State Gaming Control Board, which oversees all gaming in that state. The Florida Division of Parimutuel Wagering also oversees charitable gaming.

#### ***Lotteries***

- Thirty-seven states and the District of Columbia have state lotteries. Of these states, the great majority have lottery commissions solely dedicated to regulating the lottery. The commissions also operate the lottery.
- The exceptions are Idaho, Massachusetts, Michigan, and Texas. The lottery commissions in these states also oversee charitable gaming.

### ***Card Rooms***

- There are non-casino card rooms in five states: Maryland, Montana, Oregon, Washington, and California. California's industry is by far the largest. There is statewide regulation in Montana and Washington and local regulation in Oregon, Maryland, and California.

### ***Casino Gaming***

- All of the ten states which have state-legalized casino gambling have gaming commissions which regulate casino gaming activities.
- There are a large number of gaming commissions/boards across the U.S. which regulate legal gaming activities besides casino gaming. (Excluding lottery or parimutuel wagering, which as noted is almost always regulated by a commission.)
- Louisiana had two separate commissions which regulate casino gambling in that state. One commission regulates riverboat casino and the other regulates land-based casino gambling. That was recently changed to one unified commission.
- The Nevada Gaming Control Board serves as the administrative arm of that state's gaming commission.
- There are three states that have a gaming division as part of another state agency. In Montana and New Jersey, these divisions are part of the Department of Justice/ Attorney General's Office. The Colorado Division of Gaming is part of the Department of Revenue. In Colorado and New Jersey these divisions serve the administrative functions of the gaming commission. Montana does not have a gaming commission.

***1996 Election Results Suggest Gaming Will Continue to Expand.*** Prior to the elections, there was concern within the industry that a backlash was beginning to build. As the history section of this report discusses, such a backlash has occurred in the past. There was some evidence that a backlash was starting. Factors slowing growth include:<sup>17</sup>

- Referenda to legalize gaming versus legislative action alone.
- Organized and growing opposition that employs effective lobbying and grass roots tactics.
- More conservative political climate.
- Lack of an industry success model and a fractured industry.

In a reverse for the industry, a federal study commission on gambling has been created despite the opposition of the gaming industry and gambling had failed to gain approval in new states. During 1994, the industry suffered some losses in important elections in Florida and Missouri.

However, the 1996 elections changed that view.<sup>18</sup> The industry recorded the following major victories:

- Voters in Michigan voted to allow casinos in Detroit and those in Arizona voted to allow more Indian casinos. This was the first time in American history that the citizens voted to legalize high stakes casinos *in the face of active opposition*.
- Voters in Louisiana opted to keep both land-based and riverboat casinos. In this parish by parish election, some regions opted to ban video lottery terminals while the majority parishes voted to allow them.
- Various minor local elections ended in victory for gambling interests.

Some observers have drawn different conclusions from the election as there were also losses for gambling interests.<sup>19</sup> Nevertheless, there has never been such victories for gaming interests in state-wide contested elections. The vote was even more dramatic when one considered the criminal convictions resulting from Louisiana's gambling scandals. (Discussed in more detail in the Politics and Gambling section of the report.)

The Internet may be the source for the largest growth in gambling. The World Wide Web has three hundred gambling-related sites, some of which have set up operations offshore. The Attorney General of Minnesota has filed a suit against a service that plans to offer sports bookmaking.

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## ***II. History of Gambling in the United States***

Examining the history of gambling in North America suggests important conclusions that are useful today in considering policies related to gambling.

1. The United States has had a long history of allowing some forms of legal gambling and a degree of tolerance of illegal gambling.
2. Societal tolerance and acceptance of legal gambling can change rapidly. Scandals and political control by gaming interests have led to backlashes which result in regulation and/or prohibition.

Societal standards and laws related to gambling have tended to change back and forth from prohibition to regulation. These changes in law have led one noted observer, Professor I. Nelson Rose, to describe three waves of gambling regulation during the history of the colonies and the United States.<sup>1</sup> The first wave began during the colonial period and lasted until the mid-1800s. The second wave commenced at the close of the Civil War and lasted until the early 20th century. The last wave started during the Great Depression and is still going strong. Because of the length and size of this last wave, another observer has characterized it as an explosion, not a wave.<sup>2</sup>

### *The First Wave: 1600's to mid 1800's*

The early colonies had very different attitudes towards gambling. Historians have classified the early settlers into two groups, the English who brought along the English traditions and beliefs, and the Puritans. Although the Puritans came from England, they came to the new world to create a better society and discard the values of their mother country. To them, the new world represented an opportunity for establishing a society grounded on Puritan values and beliefs.

Entire colonies were established along the guidelines and beliefs of one group or another. In particular, different attitudes towards gambling were enforced. In New England and Pennsylvania, Puritan attitudes toward gaming and play were adopted. The Puritan-led Massachusetts Bay Colony outlawed not only the possession of cards, dice, and gaming tables (even in private homes), but also dancing and singing. This stance was relaxed slightly the following year so as to allow gaming as long as it was for innocent and moderate recreation and not as a trade or calling. This hostility towards the professional gambler is a common theme that will be seen again as we look at the history of U.S. gambling.

In other colonies, English attitudes towards gambling and recreation prevailed. These settlers brought with them the view that gambling was a harmless diversion. In these colonies, gambling was a popular and accepted activity. Legal gambling tended to be those types that were considered proper gentlemen's diversions. For example, it took a long time for cock-fighting to become legal because it was not considered a suitable game for gentlemen.

One prominent researcher speculates that the appeal of gambling was probably heightened by the frontier spirit. The desire to explore new worlds is similar to gambling. Both rely heavily on high expectations, risk taking, opportunism, and movement.<sup>3</sup>

Despite the acceptance, gambling began to be blamed for the problems of the colonies. To investors and others in England, the prevalence of gambling suggested an atmosphere of idleness and vice. Financiers began to suspect that it was the root cause of the inability of the colonies to sustain themselves.<sup>4</sup> The colonies had been relying on England to supply provisions and to replace dying settlers.

***Lotteries Used to Bail Out the Early Colonies.*** Although the financial backers of the colonies viewed gambling as a source of the colonies' problems, they began to see it as the solution as well. The Virginia Company of London, the financier of Jamestown in Virginia, was permitted by the Crown to hold lotteries to raise money for the company's colonial venture. The lotteries were relatively sophisticated and included instant winners. Eventually, the crown banned the lotteries because of complaints that they were robbing England of money.<sup>5</sup> The company dissolved shortly thereafter.

This episode was not the last use of lotteries to benefit the colonies. All 13 original colonies established lotteries, usually more than one, to raise revenue. Playing the lottery

became a civic responsibility.<sup>6</sup> Proceeds helped establish some of the nation's earliest and most prestigious universities -- Harvard, Yale, Columbia, Dartmouth, Princeton, and William and Mary. Lottery funds were also used to build churches and libraries. Ben Franklin, John Hancock, and George Washington were all prominent sponsors of specific lotteries for public works projects.

Lotteries became an issue in the drive for independence of the colonies. The colonies protested the crown's rules for holding lotteries. In 1769, the crown tried to prevent lotteries from occurring without its permission. Once the war of independence started, the Continental Congress voted a \$10 million lottery to finance the war. The lottery had to be abandoned, however, because it was too large and the tickets could not be sold.

***The Popularity of Lotteries Continued in the Early 19th Century.*** Notable among the later lotteries was a private lottery passed by Congress in 1823 for the beautification of Washington D.C. Unfortunately, the organizers absconded with the proceeds and the winner was never paid.

Lotteries were not the only form of gambling during this era. Wagering on horse racing was a popular form of gambling. Not surprisingly, it was not quite as organized nor as elaborate as modern horse racing. Rather, the gambling was limited to a few friendly bets between owners of horses and their partisans. The first racetrack in North America was built on Long Island in 1665.

Casino gaming started slowly. Taverns and roadhouses would allow dice and card games. The relatively sparse population was a barrier to establishing gaming houses. But as the population increased, by the early 1800s lavish casinos were established in the young republic.

***The United States and Gambling Move West.*** As previously mentioned, gambling and the frontier lifestyle shared similar foundations -- a spirit of adventure, opportunity, and risk taking. During the early 1800s gambling in the lower Mississippi Valley became a legitimate and organized enterprise. The Mississippi River and connected waterways were major avenues of trade for farmers and merchants and the river boats carried passengers who had lots of cash. The south tended to have a more open attitude towards gaming, reflecting the Spanish, French, and early Virginian traditions.<sup>7</sup> New Orleans became the capital for gambling.

Gambling establishments were started in the river towns and were popular haunts for both travelers and professional gamblers. These gamblers preyed upon these cash-laden travelers who were, "Seduced by the bright prospects of their business deals as well as by the transience of the river frontier..."<sup>8</sup> These professional gamblers, also known as sharps or sharpers, generally were dishonest and often turned to confidence games and cheating to make money.

During the 1830's, the actions of the professional gamblers came under growing scrutiny and southern settlers turned against the professional gambler. The professional gamblers

were blamed for limiting economic growth, interfering with business, endangering the streets, committing numerous crimes, and debasing the morality of the society. Vigilantism was one method by which the anti-professional gambler sentiment manifested itself. Groups of citizens organized to push the gamblers out of the South.

In 1835, a vigilante group lynched five cardsharps in Mississippi. Professional gamblers moved from the town into the riverboats. Lynching proved to be a successful policy option for reducing the presence of professional gamblers. In contrast to the river boat casinos of today, the old-time river boats were not floating casinos. Gambling occurred informally among the passengers. The period between 1840 and 1860 represented the glory days of the flashy riverboat gambler. The professional gamblers also moved to California, a history we cover in the next section.

***The First Wave of Legal Gambling Draws to an End.*** During the early 1800's, gambling came under increasing attack. There was always a group opposing gambling on moral grounds. This opposition was largely based on religious beliefs.<sup>9</sup> The flames of opposition were fanned, however, by the prevalence of scandals and the belief that the poor were being targeted, especially by lotteries. This opposition drew strength from the larger climate of social reform. Issues such as temperance, women's rights, educational reform, prison reform, and abolition of slavery were on the minds of many. Although there was strong sentiment to avoid interference with market forces, there was a countervailing view that people should behave in a virtuous way and that meant no gambling.<sup>10</sup>

The attack against gambling was focused particularly on lotteries because it represented a form of wagering that was offensive to both the moral sensibilities of reformers, and the Jacksonian resentment toward privilege.<sup>11</sup> The exclusive charters granted to lottery operations were examples of this form of privilege. Ironically, President Jackson was an inveterate gambler<sup>12</sup> and had such a history of problems that he must be viewed as a likely addictive or compulsive gambler. His gambling was well-known but tended to be seen as the behavior of a gentleman, hence he was reserved the disapprobation held for commercial gamblers.

***Lottery Scandals Led to Gambling Prohibition.*** As noted earlier, lottery for the beautification of the nation's capital ended in scandal with the operators absconding with the proceeds. This incident illustrated the problems with the lotteries of that time as many were crooked. Increasing evidence of fraud and dishonesty in the operations of lotteries added to the opposition.<sup>13</sup> An additional argument was that they corrupted the free press and made them captive to their huge demand for advertising.<sup>14</sup>

The antilottery forces fought against lotteries and prevailed. In 1833 Pennsylvania, New York, and Massachusetts put an end to state authorized lotteries. By 1840, most states had banned lotteries. By 1860, only Delaware, Missouri, and Kentucky still allowed state-authorized lotteries. Nevertheless, the tickets of these few states were shipped around the country by mail or smugglers. The prohibition also led to the creation of illegal lotteries.

The demise of the riverboat gambler had more to do with circumstance than direct action by the people. Emergence of railroads and the outbreak of the Civil War were the precipitating factors. Travel by steamboats declined as railroads started to supplant steamboats as the favored method of transportation. Trains were more reliable and were faster than the riverboats. The Civil War interrupted virtually all river travel and abruptly diminished gambling in that area.

The end of the first wave did not result in an end to all legal gambling. The prohibition was selective in terms of type of gambling and location. The frontier areas, California included, saw a great deal of gambling after the end of the first wave. Because of the wholesale fraud, lotteries were targeted for prohibition, but gambling in posh clubs were still legal in New York. Horse racing survived the end of the first wave relatively unscathed. As such it is more difficult to draw a clear distinction between the end of the first wave and the beginning of the second. As we shall see later, the demarcation between second and third waves are much clearer.

It was also during this time that the Grimaldis sold a concession for gaming in an attempt to keep their principality, Monaco, from going bankrupt. Monte Carlo was opened in 1858 by gambling operators who had been forced to leave Hamburg, Germany after popular opinion turned against gambling. The public disfavor in Germany occurred because of the charge that legalized gaming was turning the city into a nest of paupers.

### *Second Wave: Mid-1800's to Early 1900's*

The expansion of the western frontier spurred the second wave. As the country moved westward, the frontier spirit continued to spread. Mining booms increased the rush to the Far West. Miners lured by the promises of easy and abundant riches, personified the frontier spirit better than the explorers before them. Mining was a gamble, and risk-taking was valued for it represented an opportunity for great wealth. These were restless and ambitious people who had high expectations.<sup>15</sup> Probably nowhere was this more apparent than in California.

***Gold Rush Set Off a Gambling Boom in California.*** The gold rush brought a huge increase in the amount and types of gambling to California. San Francisco replaced New Orleans as the center for gambling in the United States. The market for gambling space was so strong that a mere canvas tent, 15 by 25 feet, cost \$40,000 annually, payable in advance with gold dust.

The apex of California gambling was from 1849 to 1855. Gambling became widespread throughout the state whether it was in Mexican towns like Monterey, mountain towns like Mariposa, or growing cities such as Sacramento. During this period, gambling tended to be integrated. Patrons included women, blacks, and Chinese. By 1850, both the state and cities were licensing gambling establishments to raise money.

As settlers spread beyond California, so did gambling. In general, gambling and the west were intimately linked. Gambling was especially widespread in the mining camps that multiplied as the miners spread across the west searching for new strikes.

***Public Opinion Quickly Turns Against Gambling.*** Laws against gamblers and gambling began to be enacted in California. As with the rest of the United States, the desire for respectability and a recognition of the social ills tied to gaming led to limits on gambling. The Legislature made most types of gambling illegal. However, the Legislature's initial aim was more to target the professional gambler than gaming in general. Gamblers were affiliated with municipal corruption and were blamed for the depression that was occurring at the time.<sup>16</sup> Lynching of professional gamblers occurred in San Francisco in 1856, in part a result of the fight for political control of the city. The gamblers were strong backers of one political faction.

Initially, the state laws were weak and had little real effect on gambling. The statutes outlawed specific games, making the laws difficult to enforce as new and unnamed variants were used and only light penalties were provided. However, the laws were gradually strengthened. In 1860, all banking games were banned. (Banking games are those where the player bets against the house.) Initially, the laws tended to focus on those who ran the games, not the players. In 1885, this was changed so that it was illegal to play. Finally in 1891, the statutes made the penalty for playing equal to the penalty for running the game.

***The Prohibition Did Not Eliminate Gambling But Drove it Underground.*** Even in California, where most gambling was illegal, the first slot machine was invented and premiered in San Francisco in 1895.<sup>17</sup> It was not specifically outlawed until 1911.

Nevada bounced between legalizing and banning gaming. Gambling was legal in Nevada between 1869 and 1910. As a result, gaming activity moved from California to places such as Virginia City, Nevada. Although legally protected, during this time gambling never reached the size in Nevada that it did in San Francisco.

Another effect of the antigambling laws was to stratify gaming activity more. One result was the prevalence of Chinese gaming houses that catered only to Chinese. There were also large Chinese-run lotteries that appealed to non-Chinese. Enforcement of the gaming laws became a method of discrimination. During times of strong anti-Chinese sentiment the gaming laws were enforced more vigorously against Chinese establishments.<sup>18</sup> One operator in San Francisco who alleged discrimination took a case to the U.S. Supreme Court, but lost because he could not show that people who were not Chinese violated the law, but were not prosecuted.

Los Angeles also had gaming activity, but it was overshadowed by San Francisco. Like the city itself, gaming in Los Angeles had more of a Hispanic flavor and occurred on a smaller scale. The city eventually banned gambling which led to a number of illegal clubs and the spread to permissive suburbs.

***Lotteries Began a Comeback.*** Following a long national tradition, the South turned to lotteries to generate revenue to rebuild the war-ravaged region. The Louisiana lottery was the most notable because of its unseemly end. In 1868, the Louisiana Lottery Company was authorized and granted a 25-year charter. A carpetbagger criminal syndicate from New York bribed the Legislature into passing the lottery law and establishing the syndicate as the sole lottery provider.<sup>19</sup> The Louisiana Lottery was an interstate venture with over 90% of the company's revenue coming from outside Louisiana. This lottery was a prolific money maker. Attempts to repeal the 25-year charter were defeated with assistance of bribes to legislators.

Scandals and antigaming sentiment led to additional state and federal legislation against lotteries. In particular, religious leaders led the move against them.<sup>20</sup> By 1878, Louisiana was the last of the legal lotteries in the country. The Louisiana Lottery survived until Congress enacted a prohibition against moving lottery tickets across state lines by any method. This act led to the abolition of the Louisiana Lottery in 1895. When the lottery was disbanded, it was discovered that promoters had made huge sums of ill-gotten gains. The Legislature was riven with accusations of bribery. By the end of the century, thirty-five states, including California, had in their constitutions prohibitions against lotteries and no state permitted the operation of lotteries.

***Lotteries Were Not the Only Source of Gambling Scandal.*** Horse racing was plagued by fraud. The odds and payouts were often faked. The parties taking the bets, known as the bookmakers, often owned horses and were able to influence the race. "Ringers," horses that were fraudulent substitutes and were either much quicker or slower than the expected entry, were often raced.

The second wave of legal gambling, was relatively short-lived. Scandals and the rise of Victorian morality led to the end of legal gambling. By 1910, virtually all forms of gambling were prohibited in the U.S. The only legal betting that occurred was in three states which allowed horse racing, but even that number shrank in the ensuing years.<sup>21</sup> The feelings against gambling ran so strong that Arizona and New Mexico were forced to outlaw casinos to gain statehood.<sup>22</sup> However, the prohibition did not stop gambling. There were many types of illegal gambling houses. Some operated openly for many years. They, of course, had to pay protection money to the law enforcement authorities.

### ***Third Wave (Early 1930's to Present)***

The great depression led to a much greater legalization of gambling. The antigambling mood changed as tremendous financial distress gripped the country, especially after the stock market crash of 1929. Legalized gambling was looked upon as a way to stimulate the economy. Massachusetts decriminalized bingo in 1931 in an attempt to help churches and charitable organizations raise money. Bingo was legal in 11 states by the 1950s, usually only for charity purposes.

Horse racing and parimutuel wagering began to make a comeback. In 1933, Michigan, New Hampshire, Ohio, and California legalized parimutuel betting. The California

Legislature adopted a statute in 1933 referred to as the Horse Racing Act. The statutes took effect upon adoption by the voters of an amendment to the Constitution in June of 1933. During the 1930's, 21 states brought back racetracks. New laws and automated systems made horse racing much more honest than during the 1800s.

Coincident with resurgence of legal gambling was a crackdown on illegal gambling, in part because illegal gambling had become so prevalent. A backlash developed and reform candidates were swept into office in New York where Fiorella La Guardia replaced Jimmy Walker and in Chicago where Anton Cermak pushed out "Big" Bill Thompson. Theater-goers were treated to newsreels of Mayor La Guardia taking a sledge hammer to slot machines and pushing them off the barge into the city's ocean dump. District Attorney Thomas Dewey ran an aggressive campaign against mobsters who were involved in gambling.

***Crackdown on Organized Crime Sent Mobsters to California.*** The crackdown in the east had implications for California. Because of the pressure from law enforcement agencies, New York mobsters, including the infamous Benjamin "Bugsy" Siegel, moved to the West Coast. His role was to expand gaming and bookmaking operations for organized crime. Eventually, publicity was directed on him during an investigation of mob ties with the film unions, forcing him to move to Las Vegas.

At the same time, scrutiny also resulted in the closing of the floating casinos. The most famous was the *Rex*, a floating casino operated by organized crime that was anchored just outside the three-mile limit of state jurisdiction. Gamblers were taken out to *Rex* in excursion boats. The *Rex* and some gaming ships that operated out of San Francisco Bay were eventually closed down by law enforcement authorities.

***Nevada Legalized Most Forms of Gambling in the State in 1931.*** The Nevada Legislature was motivated to build on the tourism boom that was expected in the wake of the completion of Boulder, now Hoover, Dam. Nevada had a flourishing, albeit illegal, gambling industry prior to the legalization. The move for making gambling legal also grew out of concerns that the flourishing illegal gambling was corrupting law enforcement and prohibition was unenforceable.<sup>23</sup> Gaming in Nevada struggled from its inception until after World War II, when the prosperity of post-war America started a boom in the fledgling industry.

The Nevada gaming industry was helped by events in California. As stated, the gambling ships that used to leave from California ports were shut down. Municipal reform in Los Angeles kicked out many of the thriving illegal gambling businesses. These establishments were run by organized crime who moved to Nevada where their skills were desperately needed to launch the new legal gambling industry.

***Organized Crime Syndicates Were Early Supporters of Gaming and Invested Heavily.*** Many casinos in Nevada were financed by mobsters. Most notable perhaps was Las Vegas' Flamingo which was opened in 1947 by Bugsy Siegel. Even though he had an extensive and violent criminal record, Bugsy Siegel was able to get a gaming license.

Most notable of his criminal exploits was his role in arranging the murder of New York mobster "Dutch" Schultz by the infamous "Murder Inc." Today, even the hint of any such activity would be sufficient to deny a license.

Part of the reason for Mr. Siegel's success was due to his connection to the underworld. Wartime shortages did not slow down his plans because of his ties to the black market and his political connections.<sup>24</sup> The lavish casino he built opened with such stars as Jimmy Durante, Xavier Cougat, and George Raft. The Flamingo helped establish Las Vegas, rather than Reno, as the destination for high rollers. Reportedly Mr. Siegel used too much of the mob's money on what was initially a unprofitable operation. Within the year, Mr. Siegel was gunned down at a Beverly Hills mansion.

***Senate Investigated Mob Influence in Casinos.*** During the 1950s, the Senate Committee to Investigate Organized Crime in Interstate Commerce held a number of hearings on criminal influence in the casino industry. The committee was chaired by Senator Estes Kefauver, and the committee is also known by his name. The committee found widespread evidence of skimming, which sheltered gambling profits from taxes. The prevalence of crime left gaming once again on the verge of a national prohibition.<sup>25</sup> The result of the committee's findings was a crackdown on criminal influence and a cleansing of the casino industry. Eventually, the mob sold their casino interests to lawful individuals and publicly-traded companies.

The link between organized crime and gambling was a factor in four state elections on legal gaming.<sup>26</sup> In 1950, voters in California, Montana, Arizona, and Massachusetts voted against legal casino gaming. The California proposition would have established a state board to run all gaming operations with the proceeds going for old-age benefits. It lost by a wide margin.

***Lotteries Begin Their Resurgence.*** From 1894 to 1964, there were no legal government-sponsored lotteries operating in the United States. This ban led to a paradox: lotteries were widely played, but always illegal. One of the most well known was the Irish sweepstakes which began in 1930 for the purpose of raising money for hospitals in Ireland. Although it was not legal to sell tickets in the U.S. or to ship them here, they were smuggled into the country. Participation was high with about 13 percent of the country having ever bought a ticket.<sup>27</sup>

Another prominent form of lottery was the illegal "numbers" game. Despite the illegality, numbers was quite popular. One author claimed that the amount being wagered on numbers was \$5 billion in 1960.<sup>28</sup> Another estimate shows that the numbers game was grossing \$20 million annually in Chicago alone during the early 1970s and the total handle was \$1.1 billion.<sup>29</sup>

Growing opposition to tax increases was a leading factor in establishing state-run lotteries in the 20th century. In 1964 New Hampshire was the first state to sponsor a lottery, followed by New York in 1967. New Jersey launched the first financially successful modern lottery in 1971. The New Jersey lottery was successful because it stressed

frequent action at low cost, and it returned a higher percentage of lottery revenues as prizes. There were also various attempts to legalize a national lottery, but they failed to be passed by Congress.

In 1978, New Jersey became the second state to legalize casino gambling in an attempt to revitalize the rundown resort area of Atlantic City. The legalization was restricted only to Atlantic City. In the late 1800's to the early 1900's, Atlantic City was a popular resort town, boosted by the new rail service which linked the Northeast. Day trips to the Jersey shore were now possible and affordable. But its popularity dwindled when air travel became easily accessible. Upscale tourists chose beach resorts in Florida, the Bahamas, and the Caribbean over Atlantic City. Visitors to Atlantic City in the 1960's and 1970's were generally elderly and/or poor. Casino gaming was expected to be a way for Atlantic City to become a popular tourist destination once again.

***What Could End Gambling's Third Wave?*** The first and second waves ended in part because of a resurgence of public concern about morality and scandals in gaming. People can live with adverse odds but not cheating.<sup>30</sup> What kind of events could lead to scandals today? If lotteries were plagued by fraud that would probably have an impact on people's perceptions. Another route is through problems and scandal in sports gambling. Pete Rose is a symbol of what gambling can do to a person. What happens if a sports hero is more interested in winning a bet than a game? Could such a scandal impact legalized gaming?

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### ***III. Lotteries***

"Hope Springs Eternal in the Human Heart," Alexander Pope.

***Lotteries Have Been Prominent Throughout History.***<sup>1</sup> Ancient India, China, Greece, and Japan all had lotteries. The emperor Nero had lotteries for prizes at parties. The Great Wall of China was financed, in part, by a lottery. The Bible is replete with references to drawing lots. Lot casting was a favored means of communication between man and god.

As early as 1420, lotteries were used in Europe for public works. High-value commodities such as land and art were often sold through lotteries. The first publicly run European lottery was in Florence in 1530. The money was raised for public works. The first public English lottery was in 1566 and was also for public works projects. In 1753 the British Museum was funded with lottery proceeds. In addition, England had private lotteries, but they became such a scandal that parliament outlawed them in 1699.

As noted in the history section, lotteries have a long and mixed history in the new world. In modern times, lotteries started their comeback with the legalization of the New Hampshire lottery in 1964. This lottery was a low-stakes low-excitement lottery, because drawings were held twice a year and the winnings were not large. The lottery was modeled after the Irish sweepstakes. The winning numbers were tied to the winner of a

horse race. However, it was not a skill-based game, as the numbers were randomly selected.

Researchers usually point to New Jersey as the first modern successful lottery. The New Jersey lottery was more successful because of the more frequent drawings and larger purses. The New Jersey lottery was administered by a commission appointed by the Governor, a model that most states use.

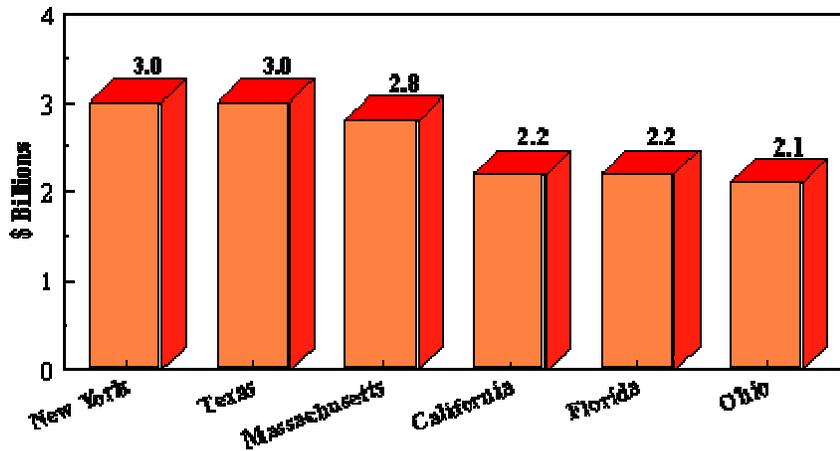
***Lotteries Enjoy Widespread Legalization.*** Lotteries are legal now in 37 states and the District of Columbia. Lotteries have spread rapidly across the country, in a way that is consistent with the domino theory of gaming regulation discussed in the introductory section. Simply put, a given state is more likely to have a lottery, if the neighboring state has a lottery. The first states with lotteries were all in the northeast. Then lotteries spread across the country. The only region in the United States where they are generally not legal is in Alaska, and Hawaii, and the southern states.

Lotteries, along with their close derivative bingo, are the most popular kinds of gambling. The popularity of lottery games is not limited to state-run lotteries. Indian tribes run lotteries and illegal lotteries still exist.

Lotteries are also legal around the world. The 1995 worldwide sales for legal lotteries were \$95 billion.<sup>2</sup> The United States leads with sales of approximately \$28.7 billion. Germany is a distant second at \$9.2 billion in sales. In all these places, lotteries are basically the same game with only minor differences that reflect the particular national culture.

Looking at some specific industry statistics, we can see that lotteries are well-established in this country and within California, although for the size of the state, California does not have a particularly large lottery. Although the chart shows California as one of the biggest lottery's state, the table at the bottom shows Californians spent less on the lottery than many other states.

## Largest State Lotteries Sales - 1995



Source: La Fleur's 1996 World Gambling Abstract.

### Per Capita Lottery Sales - 1995

Massachusetts	1	\$462
Washington, DC	2	\$404
Maryland	3	\$208
<b>California</b>	<b>33</b>	<b>\$69</b>
Montana	37	\$38

Source: La Fleur's 1996 World Gambling Abstract.

*Despite Success, Opposition Exists.* The resurgence of lotteries has not been universally welcomed.<sup>3</sup> An argument used in opposing lotteries is that they symbolize the boredom and materialism of modern life. Another argument against lotteries is that legal gambling leads to illegal gambling. Lottery critics see legalized state-sponsored gambling destroying ethical values by promoting the ethics of easy money over hard work. Critics point to the ads of employees being disrespectful to their bosses after winning the lottery.<sup>4</sup>

Another argument that is marshaled against lotteries is that they prey on the poor, the ignorant, and compulsive gamblers. The poor may be induced to spend money on lottery rather than basic necessities leaving local and state government picking up the tab through varied service programs. State lotteries are also a monopoly and some question exists whether that is proper. Another argument is that if the purpose is to make money for schools or some other worthy purpose, why shouldn't the state earn money through opening other businesses such as restaurants or brothels?<sup>5</sup>

In sharp contrast, supporters call lotteries a painless tax, even a high-minded tax. Money is raised for good causes through people having fun. Lotteries are to be celebrated because they restore consumer sovereignty, allowing people to spend money on what they choose. The argument goes on to state that gambling is prevalent whether it is legal or illegal, so why not allow people to do it legally. To prevent people from gambling is a form of paternalism and is elitist. There is no harm save for the compulsive gambler or in the crooked game, which all state lotteries go to great pains to avoid.

Two stories by modern American writers indicate the ambivalent feelings aroused by the lottery.

"Once you could send your innocent babes, hope of the future, off to the candy store to buy some chewing wax, a Baby Ruth, the new Batman comic book and a kazoo, and be secure in the knowledge that good Mrs. Chesley behind the counter would bust their little knuckles if they tried to buy a copy of The Racing Form. Not anymore. Now good Mrs. Chesley has turned her shop into a gambling hell where she greets the traffic with a leer that says, "Hello sucker" and has to keep kicking the kids out of her way so the lottery players can get their bets down."<sup>6</sup>

But there is another view. A supporter noted:

"Editorial and other criticism of legal gambling smacks of nannying ordinary working and retired folks: we the affluent, who would not dream of playing numbers whether legal or illegal, long shots on the races or for jackpots at slot machines, don't want you, the unwashed, to enjoy your simple pleasures."<sup>7</sup>

There are objections to lotteries that go beyond the arguments just presented. Some critics are concerned that state-sponsored lotteries are not just supplying a good, but trying to foster a taste for it.<sup>8</sup> In legalizing a lottery, the state is yielding to consumer preference and the argument that a little gambling does not hurt anybody. But the question remains, does the business-like behavior where sales of lottery tickets are actively encouraged through state sponsorship and huge amounts of advertising reflect the public interest?

Why have lotteries grown? There are several trends that receive credit for expanding lottery business.<sup>9</sup>

- Tickets have become cheaper, especially when adjusted for inflation.
- Number of retail outlets has increased.
- Size of grand prizes has grown.
- More consumer participation is allowed in the betting: for example consumers can choose their own numbers.
- Frequency of drawings has increased, in part because there are more types of games.
- The payout rate has increased, although compared to colonial times it has decreased.

***State Lotteries Have Two Important Attributes.*** One of these is a significant marketing and advertising campaign and the other is that the lottery is a monopoly run by state government and not by a private firm.

Lotteries are run by state government for two major reasons. One is to reduce fraud and the other is to raise money for a worthy cause. Some states deposit the proceeds into the general fund while others earmark the money for special purposes. Some interesting purposes include a gamblers aid fund in Iowa and the University of Illinois Athletic Association in Illinois. The state statutes generally call for the lottery commission to maximize profits, although some restrictions may be adopted. Because of the statutory direction to maximize profits, lotteries are run like businesses and are more like a private sector entity than a state agency. An unusual case was Missouri, where the law prohibited advertising that would induce a person to participate. Since the effect of this prohibition was to eliminate all of the advertising normally done by a state lottery, the law has since been changed.

***Critics Argue That Much of the Advertising is Misleading.*** For example, lotteries, including California, routinely advertise multimillion dollar prizes. The real value of these prizes is actually about one-half as large because they are paid out over many years. Critics charge that this is misleading advertising and the present value of the prizes should be noted in the advertisements. New York Governor Pataki has directed the lottery to advertise in a more honest way. Gone are the pictures of the new millionaire beside his pool. Now a woman from Yonkers is shown spending her \$10,000 (\$6,400 after taxes) on a variety of home appliances.

***Modern Lotteries Have Been Essentially Free of Scandals.*** Early lotteries were plagued by corruption and scandals. To protect the integrity of the games, lotteries have adopted many safeguards to protect against corruption and fraud. The lottery industry has experienced very few scandals in the more than 30 years of state-administered lotteries in North America.<sup>10</sup> The integrity of the lottery is one of the appeals of lottery gaming.

There have been some instances of fraud in modern lotteries, although the incidents pale in comparison to the experiences of the 18th and 19th century American lotteries. In 1982, there was a scandal in the Pennsylvania lottery. In a drawing where balls were used to determine the winning number, some of the balls were injected with fluid to make them heavier. Because they were heavier they would be chosen in the mechanized selection procedure. The perpetrators included the TV announcer and were quickly discovered. Another significant lottery scandal also occurred in Pennsylvania when a computer vendor printed a ticket with the winning numbers. Again the perpetrator was quickly discovered. In a slightly different kind of case, New York closed down its lottery for a period after the agency announced winning tickets that the lottery officials knew had not been sold.

***States Have Been Very Effective at Stimulating Demand.*** As noted, New Hampshire started with a couple of drawings a year. The results were not spectacular. As more states legalized lotteries, the states have become very effective at innovating and creating new

games. One of the first innovations was to increase the frequency of drawing and the size of the prizes. Another new product was the instant tickets, termed "scratchers." Then lotteries started daily drawings which are modeled after the illegal numbers game. One of the biggest booms to lotteries was the introduction of Lotto. Lotto is a game where winners are determined by matching the player's number with numbers that are drawn. If the winning numbers are not held by a player the prize rolls over and grows. The rolling over of the prize is crucial to a modern lottery's success, because it creates a large jackpot which has a significant effect in stimulating sales.<sup>11</sup>

***Lottery Players are Widespread.*** Lotteries are the most popular and broadly played form of gambling despite having the lowest payout. A large proportion, about 50 to 60 percent of adult Americans play legal lotteries in lottery states. Two-thirds of these play regularly, which means that about one-third of the adults are regular players. Heavy players are about 10 percent of all lottery players.<sup>12</sup> The poor, minority, Catholic, undereducated, and middle-aged are all more likely to play.<sup>13</sup> Two of the first 11 big winners in California were illegal immigrants.

There is substantial evidence that youths play the lottery, although they are forbidden by law. Studies have found large number of high schools kids playing lottery games. Some of these individuals have characteristics of pathological gamblers.<sup>14</sup>

The total number of all lottery players is probably greater than reflected in statistics because illegal lotteries still exist. They can exist because their payout ratio is much higher. State lotteries are a very unattractive gambling proposition as they return a relatively small amount of the money as prizes.

***The Typical Individual Spends \$100 Annually.***<sup>15</sup> This amount exceeds the amount spent directly on prescription drugs and reading materials. Also, a small number of poor families spend a very large sum on lotteries.<sup>16</sup> In general, the amount spent on lotteries per person does not vary as much as the percent of income spent. That is because higher income people spend proportionally much less on the lottery.

Research has shown that a relatively small minority of customers provide a large share of revenues. A study based on California data showed that, typically about two-thirds of the take is provided by about 10 percent of the customers.<sup>17</sup>

Lotteries have come to be seen as "implicit taxes" by researchers.<sup>18</sup> That means that they are not, of course, taxes because no one is obligated to pay them. But lotteries are similar to taxes because they raise money for public purposes. Some critics would argue that lotteries are not wholly voluntary because of the coercive nature of the advertising and the fact that people buy them on impulse.<sup>19</sup> The counter argument is that it is in fact a voluntary purchase. Even if purchased on impulse, so are candy bars and lottery tickets do not cost much more.

***Lotteries Raise a Disproportionate Share of Money From Low-Income Groups.*** Almost every study conducted by economists and researchers has found lotteries to be regressive

form of raising money.<sup>20</sup> Regressive means that as income rises, the proportion of money spent on a given product, lotteries in this case, declines. The regressivity of a lottery is heightened because of how the money is spent. The proceeds tend to go for programs that benefit the population as a whole, namely education. The regressivity could be diminished if lottery proceeds went for programs that aided lower income groups exclusively.

In other states there has been criticism that lotteries have targeted low-income people. The lottery in Illinois rented billboards in Chicago's most blighted neighborhoods with the slogan "This Could Be Your Ticket Out."<sup>21</sup> After receiving significant criticism, the ad campaign was dropped.

***Why do People Play the Lottery?*** The main reasons are availability, no skill is required to play, players have little or no fear of corruption, and gamblers can wager small amounts. People play despite the low payout compared to other forms of gambling. However, playing the lottery is a cheap way to have an opportunity of winning big dollars and become a celebrity. If you win a big lottery prize you are put in the newspapers. The celebrity status of winners may be an important aspect in encouraging play.

The odds of success in lotteries do not seem that important to players. When interviewed, consumers do not seem to know the odds or the payout rate. Researchers have found that once people believe that a low probability event can occur, they tend to overestimate the chances of it occurring.<sup>22</sup> And a small number of people do win and win large amounts of money, although the overwhelming majority lose money.

Lotteries give an illusion of control to some players. Because you can pick your own numbers in some games, you can choose your own lucky number. Tabloids feature articles about how to improve odds at picking lottery numbers, obviously a forlorn hope because the winning numbers are a product of a random process. Another attraction of the lottery is that people enjoy the non-monetary aspects of it, including talking about playing, engaging in the ritual weekly purchase, socializing with friends and coworkers to pool to buy tickets, and dreaming about winning, perhaps the favorite activity among lottery players.

According to some research, lotteries recruit people into commercial gaming, especially in states that have had little legalized gaming or exposure to such activity.<sup>23</sup> This finding is interesting because lotteries have been opposed by commercial gaming interests. Another view is that lotteries have sanitized gaming and popularized it.<sup>24</sup>

Gambling can be an addiction for some gamblers and the resulting costs from these compulsive gamblers is quite significant as discussed in Chapter IX. It is unclear what role lotteries are having on the compulsive gambler.<sup>25</sup>

***Illegal Gambling Isn't Eliminated by Lotteries.*** One justification that has been used to win approval of lotteries is that they will undercut the illegal numbers game. Nevertheless, illegal numbers still persist, although they are probably smaller.<sup>26</sup> Numbers

persist because its convenient, flexible, offers credit, and if you owe the government for taxes or welfare, it may be a better place to bet your money. And the payout is much larger than the approximately 50 percent of state-run lotteries. Although the size of numbers is not known, researchers note that estimates put drugs as a far bigger source of funds to criminal interests.<sup>27</sup>

***Economic Impact of Lotteries is Unclear.*** The lotteries help retailers that sell lottery tickets, especially the small ones. But of course by removing money from expenditure on other goods and services it can have a harmful impact on other retailers, but that has not been quantified.

Some research on the California lottery shows that it has a pronounced impact on rural areas. The lottery raises money throughout the state, but proceeds and purchases of inputs do not benefit the state equally. An economist estimated that the lottery may take \$711 million out of rural California, in other words, it is an "anti-rural development program."<sup>28</sup>

***There are New Directions for Lotteries.*** State lottery commissions are intrigued by several new directions. These include video lottery terminals and betting at home through touch-tone phones or cable television. Another is sports betting. Sports betting may be the most popular type of betting, although much of it is illegal. Four states have used sports betting in the lotteries, but Congress acted to outlaw it at the behest of professional athletic organizations. There was a widespread concern that any legalized sports betting could make the athlete more concerned with the bet than the game.

State lotteries have not been involved in casino gaming. A different situation exists in Manitoba, Canada, where the lottery operates a casino.

Lotteries have gone to quickdraw keno and it has become quite popular. Monitors are placed in bars and restaurants and drawings are held on a very frequent basis, approximately every five minutes. Critics argue that it exposes young people to casino-type gaming. California earned more than any state on quickdraw keno.<sup>29</sup> The state's earnings plummeted sharply after the California Supreme Court ruled that the lottery's keno game was not a lottery game as authorized by the constitution and was illegal because it was a banked game. Lottery games are played against other players and not against the house, in this case the California Lottery. California law prohibits all banked games, that is those games where the house has a stake in the outcome.

As will be discussed further in the Indian Gaming section, the Coeur D'Alene Indian tribe in Idaho is proposing a national lottery. That lottery would be available in all states that have a lottery, including California. Such a lottery would allow someone to use a credit card to purchase a ticket over the phone. The person would be able to buy on credit and would not have to leave his own home. Another advantage is that the lottery does not have to earmark money for a purpose, such as the California lottery. Some lottery analysts say this could be a large advantage.<sup>30</sup> The tribe is, however, proposing to share

the revenues with other Indian tribes and states. Whether this will drive their payout to a higher or lower level than the state's is not clear.

There is a strong link between the lotteries and Indian gaming. The Indian tribes are allowed to operate whatever type of gambling that is not prohibited to everyone within a state. The games used by the lottery are often used to pave the way for expanded Indian gaming in states that do not otherwise allow casino gaming.

***Lotteries May Not Stay Public.*** Governor Rowland of Connecticut has proposed selling a portion of the state lottery to private investors to raise money for the state. It would not have a significant impact on the operation because only a minority, about 6 percent of the state lottery, would be sold.

#### Appendix I

Start-up Year	State	Authorization	Approval Rate
1964	New Hampshire	Legislation	
1967	New York	Referendum	61%
1970	New Jersey	Referendum	82%
1972	Pennsylvania	Legislation	
1972	Connecticut	Legislation	
1972	Massachusetts	Legislation	
1972	Michigan	Referendum	67%
1973	Maryland	Referendum	80%
1974	Ohio	Legislation	
1974	Rhode Island	Referendum	
1974	Illinois	Legislation	
1974	Maine	Referendum	61%
1975	Delaware	Legislation	
1978	Vermont	Referendum	66%
1981	Arizona	Initiative	51%

1982	Washington	Legislation	
1982	Washington DC	Initiative	66%
1983	Colorado	Initiative	60%
1985	Oregon	Initiative	66%
1985	California	Initiative	58%
1985	Iowa	Legislation	
1986	West Virginia	Referendum	67%
1986	Missouri	Referendum	70%
1987	South Dakota	Referendum	60%
	Kansas	Referendum	64%
	Montana	Referendum	70%
1988	Virginia	Referendum	57%
	Wisconsin	Referendum	65%
	Florida	Referendum	64%
1989	Idaho	Referendum	51%
	Indiana	Referendum	62%
	Kentucky	Referendum	60%
1990	Minnesota	Referendum	57%
1991	Louisiana	Referendum	65%
1992	Texas	Referendum	65%
1992	Nebraska	Referendum	63%
1993	Georgia	Referendum	52%
1994	New Mexico	Referendum	54%

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## *IV. Indian Gaming*

Indian gaming has mushroomed over the last three decades. Although there is agreement that it has grown dramatically, it is difficult to put an exact dollar figure on the size of Indian gaming. There are no publicly collected and released statistics figures, as there would be with a public corporation involved in gaming. Estimates of the gross revenues vary widely. A writer on gambling and economic development, Robert Goodman, quotes a \$6 billion figure.<sup>1</sup> A quick review of other articles yields estimates of \$2.3 billion,<sup>2</sup> \$8 billion,<sup>3</sup> and \$2.6 billion.<sup>4</sup> Not all these revenues are going to the tribes, however, as the management companies take a significant share. By some accounts 65 to 85 percent of the income goes to management companies.<sup>5</sup> Again, the exact figure is not known and those figures are higher than the ones seen in recent newspaper stories about signed contracts.

***Despite its Popularity and Widespread Availability, the Future of Indian Gaming is Unsettled.*** Some observers believe that despite its widespread popularity, Indian gaming could become illegal again.<sup>6</sup> The history of Indian gaming is replete with conflicts with the states. Native Americans are concerned that those conflicts could threaten what some observers are calling the "new buffalo." Indian gaming has earned that term because it is a single source capable of feeding and clothing the Indians. It has become the one economic development program that has been able to overcome the poor quality and remote location of most of their lands.

The conflict between the states and Indian tribes arises because both are sovereign entities. As such, states are severely limited from taxing and exercising jurisdiction over activities on tribal land. When the interests of the Indian tribes and the states differ, this sets up a conflict. The history of tribal-state relations have been not always been free of conflict and tension.<sup>7</sup> The states, in order to prevent the off-reservation effects of certain activities that occur on the reservation have sought to extend authority over reservations. The result has been substantial litigation between the states and tribes in an attempt to define the relationship between the two. The high stakes of gaming and the fact it is an area traditionally regulated by the state have intensified the conflicts.

Although Indian tribes are sovereign entities, they are clearly dependent and subject to federal policy and regulation. Federal policy has fluctuated dramatically over the years, alternating between forcing Native Americans to assimilate or allowing them to maintain their separate identity. During the most recent swing in policy, Congress passed the Indian Civil Rights Act of 1968 which embraces continued tribal existence. The support and promotion of gambling by the federal government is an outgrowth of the policy of supporting a separate identity for indigenous peoples.

***First Major Litigation Spurred by Indian Bingo in Florida.*** The state of Florida had legalized bingo for nonprofit entities. The state had adopted specific laws governing bingo, including prize limits and hours of operation. In 1979, the Seminole tribe opened a high stakes bingo parlor that did not comply with many of the state laws. They were the first federally recognized Indian tribe in the U.S. to operate a high-stakes bingo operation

on a reservation.<sup>8</sup> The Sheriff of Broward County, the site of the bingo parlor, threatened to close the operation down. Florida, like California, is a Public Law 280 state, meaning that Congress granted the state the authority to enforce the state's criminal laws on reservations. The tribe sued to prevent the action.

In the first important decision in a modern Indian gaming case, the U.S. Court of Appeals rejected the arguments of the State of Florida.<sup>9</sup> The Court found that the relevant question was whether gambling, or more specifically bingo, was prohibited in Florida or was it merely regulated. If it was prohibited, then clearly the state could act to prevent gaming on Indian lands. But since Florida allowed charitable bingo, then bingo was regulated rather than prohibited within the state and was a civil rather than a criminal issue. States are severely restricted in enforcing their civil jurisdiction on Indian reservations. The tribe was allowed to continue their operations. California lost a similar suit over bingo games.<sup>10</sup>

***Indian Gaming Began to Grow Rapidly.*** At that time, only five states prohibited all forms of gaming, giving the Indian tribes a great deal of latitude to expand their gaming. By 1988 over 100 tribes were engaged in bingo and one researcher put the collective revenues at over \$100 million.<sup>11</sup> Not surprisingly, the *tribes* wanted to move beyond bingo to card games and slot machines.

***Congress Supported the Spread of Indian Gaming.***<sup>12</sup> Congress was motivated by the conditions on reservations. By any standard they were grim.<sup>13</sup> In 1989, the median family income on reservations was \$13,489, while it was \$34,213 in the remainder of the country. On reservations, 47.3 percent of families lived in poverty compared to the national average of 11.5 percent. The alcoholism rate among Indians was 663 percent higher than the national average, the suicide rate was 95 percent higher.

***Objections Were Voiced Over Indian Gaming.*** The expansion of Indian gaming was not greeted with enthusiasm from all quarters.<sup>14</sup> The states, even if they have legalized gaming, have long been reluctant to open up gaming on Indian lands.<sup>15</sup> Law enforcement officials were concerned with the possibility that organized crime would infiltrate Indian gaming operations. Non-Indian gaming operations were very concerned about the competition from businesses that did not have to pay the same state and local taxes that they did. Governments were concerned about the possibility of social problems resulting from increased gaming. Another concern of government was its inability to tax gaming on reservation lands.

During this period, the federal government was not active in regulating Indian gaming. The Bureau of Indian Affairs had adopted tribal gaming ordinances for years, but generally gaming was not an issue of regulatory concern.<sup>16</sup>

The problems associated with Indian gaming began to grow.<sup>17</sup> Non-Indian managers who helped tribes establish gaming operations were taking the majority of the profits. Suspected organized crime involvement began to surface. There was also evidence of cheating and skimming. Some dishonest tribal members were involved in criminal

activities. These events began to create pressure for Congress to act, but there was not a consensus on what should be done. A major case regarding gaming in California was pending before the Supreme Court, adding to the inertia in Congress.

The pending Supreme Court case had developed when California had threatened to take criminal action against the Cabazon and Morongo Bands of Mission Indians because of their card game and bingo casino. These games were not operated in a manner that was consistent with state law. In 1987, the Supreme Court found for the Indians in the landmark case, *California v. Cabazon Band of Mission Indians*.<sup>18</sup> The U.S. Supreme Court upheld by a six to three vote the right under federal law for Indians to run gambling operations without state regulation in states where such gaming was legal for any purpose. As the court noted:

"California itself operates a state lottery and daily encourages its citizens to participate in this state-run gambling. California also permits parimutuel horse-race betting."<sup>19</sup>

The decision in the Cabazon case ultimately prompted Congress to act. After Cabazon, the states and Nevada gaming interests became the principle proponents for new gambling legislation, because they wanted more limitations and control.<sup>20</sup> Shortly after, the Indian Gaming Regulatory Act (IGRA) was passed.

***Congress Intended to Accomplish Five Objectives With the Passage of IGRA.***

- Promote self-sufficiency for the tribes.
- Ensure that Indians were primary benefactors of the gambling.
- Establish fair and honest gaming.
- Prevent organized crime and other corruption by providing a statutory basis for its regulation.
- Establish standards for the National Indian Gaming Commission.

IGRA divided gaming into the following three classes or categories:

**Class I:** Consists of social games for minimal value prizes associated with traditional tribal ceremonies or celebrations. This class is within the exclusive jurisdiction of the Indian tribe.

**Class II:** Includes limited card games, lotto, and bingo, but not the electronic form of the games. Class II games are within the jurisdiction of the tribes primarily, but is subject to oversight by the National Indian Gaming Commission. These games are only permitted in states that permit such gaming for any purpose and/or any condition. Although states almost always heavily regulate and restrict such games, many of those state restrictions do not always apply to the tribe.<sup>21</sup> For example, although Class II card games must be played in conformity with state laws and regulations on hours of operation and limitations on wager or pot sizes, state limits do not apply to bingo at a tribal reservation facility.

**Class III:** Encompasses those gaming activities such as slot machines and other games that are commonly operated by Nevada or Atlantic City casinos, lotteries, or parimutuel facilities. Class III gaming is subject to negotiations between the state and the tribe. The exceptions are those cases where the tribe already offered Class III prior to the passage of the IGRA and these were grandfathered.

In order for a tribe to offer new Class III gaming, three events must occur:

1. The state in which the reservation is located must permit the same specific gaming activities that are permitted.
2. The tribe passes an ordinance authorizing the gaming activities.
3. The gaming is conducted in conformance with a compact entered into by the tribe and the state.

The IGRA also reserves for the federal government exclusive jurisdiction over criminal prosecutions of state gambling laws at Indian facilities.<sup>22</sup> For the state to gain any say over how Indian gaming is conducted, the state must enter into a compact that allows state oversight.<sup>23</sup>

***States Unhappy With Tribal Authority Over Gaming.*** The States were interested in protecting their prerogatives and opposed the grant of authority in the Cabazon case and the IGRA.<sup>24</sup> The IGRA requires states to allow tribes to conduct gambling to a greater extent than the state allows other person and entities to gamble. At the same time, IGRA does not automatically make tribal gaming subject to state regulation intended to protect patrons and minimize the negative side-effects of gambling on nearby communities.

Furthermore, the reluctance of the states can also be understood by noting that neither the tribes nor tribal members pay state sales taxes or state income taxes on income earned on reservations nor do they have to pay property taxes. This is a long-standing prohibition that predates IGRA. To the extent that tribal gaming reduces lottery ticket sales or causes consumers to spend money on gambling that would otherwise be spent on goods or entertainment that generate sales tax, the states are direct competitors, not mutual beneficiaries of gambling on Indian reservations.

The compact provisions have proven to be a contentious element and has been the subject of much litigation. Many states have not wanted to negotiate because they did not agree with the position of tribes that certain Class III games were legal in the state. They did not believe that Congress envisioned casino gambling in states just because the state allowed charity Monte Carlo nights. Senators Inouye and McCain have indicated that if the states do not negotiate compacts, Congress might preempt and establish sole federal regulation of Indian Gaming.<sup>25</sup>

In particular, the requirement that the states negotiate with the tribes in good faith has spawned a great deal of litigation. The states were required under IGRA to negotiate in

good faith to enter into a compact with a tribe to allow Class III gaming. If they did not do so, the tribes were allowed to sue in federal court. Congress adopted this good faith requirement to ensure that the states would not stonewall but would enter into negotiations that could and would be completed.<sup>26</sup> Ironically, the compact provision was put into the bill at the behest of the states and limited the freedom that the tribes had gained in the Cabazon case. The Nevada gaming interests also pushed for the compact provisions.<sup>27</sup>

Under the provisions for negotiating a compact, if negotiations failed, each party had to submit an offer to a mediator. The mediator picked an option and submitted it to the tribe and state. If the state did not approve the mediator's option, the Secretary of the Interior could step in and approve the compact. Even with state approval, the Secretary must approve a compact for it to go into effect.

The issue of good faith, however, will be less important in the future. The Supreme Court of the United States recently decided a Florida case on the issue. The court agreed with the state's position that the 11th amendment prevents states from being sued by the tribes in federal court without the state's permission.

It is an open question of what will happen next. The compact is merely an option under federal law, perhaps leaving the tribes the ability to go straight to the Secretary of the Interior. The Secretary of Interior has issued an Advance Notice of Proposed Rulemaking for regulations that would allow that. The states oppose this and argue that such an action is bad policy, in violation of IGRA, and possibly unconstitutional.

***Connecticut Lost One of the First Significant Cases.*** Connecticut's position was that Class III games were not legal in the state. The Mashantucket Pequot Indians pointed out that a charity could have an annual Las Vegas night where casino-type games were legal. Because casino-type games were legal under certain conditions the court held the state to negotiate a compact to allow those games to be played on Indian land with or without those conditions. Thus, because charities could have a casino night one time a year, the Indian tribes were permitted to open a casino. Furthermore, even though these games were strictly limited and regulated by state, none of the state's limitations or regulation would apply, except as agreed on the compact. Because the state had failed to negotiate with the tribe, the court ordered the state to negotiate a compact within 60 days of its order.

The court settled this dispute and agreed with the tribe's position. The state was found to not be negotiating in good faith and the Indians were able to set up a casino. This was the first of several cases where the state lost the leverage that it could have gained by a compact, because it failed to negotiate. While the Supreme Court decision has eliminated the ability of tribes to take states into federal court, it still leaves states without authority unless they negotiate a compact.

There was an additional dispute in Connecticut over whether slots were allowed. The state and tribe came to agreement and the state receives a payment from the tribe of at

least \$100 million annually. This casino, Foxwoods, is now one of the largest casinos in the Western hemisphere.

***Indian Casino Gaming Has Become Widespread.*** The spread of casino gaming into states where it is generally not legal was an unforeseen result of the compact process.<sup>28</sup> In Minnesota, the federal mediator concluded that since Minnesota allows private social games such as blackjack and poker in private citizen's homes, the tribes could do these things in casinos.

### ***Significant Indian Gaming Cases***

**State of California v. Harold Monteau.** This case has been brought by the state against the National Indian Gaming Commission to compel them to shut down slot machines at tribal casinos. The state lost its case at the District Court in December 1996. The state is considering an appeal.

**Seminole v. State of Florida.** In this case, the Supreme Court held that the Indian tribes cannot sue states under the Indian Gaming Regulatory Act in federal courts without state permission. In other words the tribes cannot force states to negotiate gaming compacts. The decision was based on the 11th Amendment to the Constitution which provides that a state can only be sued in its own courts or if it consents to the suit. Basically states have a sovereign immunity from lawsuits filed in federal courts and Congress cannot abridge that immunity through passage of the Indian Gaming Regulatory Act.

**Rumsey Indian Rancheria of Wintun Indians v. Wilson.** The basic issue in this case is whether the tribe can have slot machines because the lottery operates similar games. This case was decided for the tribe, but appealed to the Ninth Circuit Court of Appeals. The Ninth Circuit held for the state and decided that Indian tribes cannot offer banked games such as slots.

**Western Telcon v. California State Lottery.** This case was decided by the California Supreme Court on June 24, 1996. The court held that the lottery's electronic keno game was not a lawful lottery game, but an illegal banked game that is prohibited in California. Hence the state lost the case although the ruling is favorable to the state's position in negotiating with Indian tribes. In non-banked games, including the lottery, the house collects a flat percentage. With a banked game the house is betting against the players and has a stake in the outcome. Although not strictly an Indian gaming case, it has ramifications over what is legal in California, hence what the tribes can operate

**Sycuan Band of Mission Indians v. Roach.** In this case, the court held that the State has no authority to prosecute tribe's employees for conducting tribal gaming.

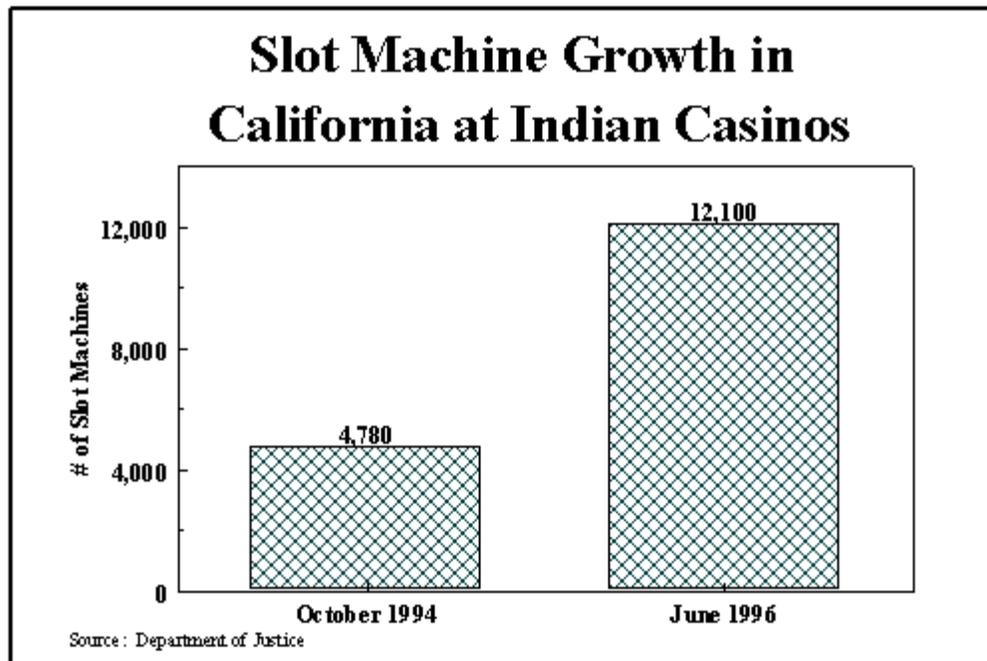
Indeed the act has been so successful in promoting Indian gaming that one observer noted:

"The IGRA may fairly be said to be the first Indian victory since the Little Bighorn."<sup>29</sup>

***When the States and Tribes Cooperate, States Have Been Able to Gain Some Concessions.*** For example, in Minnesota the 11 tribes that have entered into compacts have agreed to limit table games to blackjack. Minnesota also uses the compacts to get Indian tribes to set minimum gambling ages. As noted before, Connecticut ended up with a share of the slot machine revenues. The governor of Kansas was anxious to sign a compact and upset that the Legislature prevented him from doing that. He was concerned that without the compact, the state will have no regulatory say over Indian gaming.<sup>30</sup> Among the conditions negotiated in the compact were state inspections, background checks and an agreement to create a state gaming commission that would oversee Indian gaming. The tribes even agreed not to offer games that compete with the lottery.

The Kansas case highlights a key case in the compact process. Some observers see the negotiations to be a legislative action, hence the Governor cannot unilaterally negotiate. A decision by the New Mexican Supreme Court supported this notion.

***California Has Been Locked in Litigation With the Tribes.*** At issue is whether or not the lottery games are the same as slot machines. Despite the litigation and controversy about slot machines, there are over 12,000 slot machines in Indian casinos in California. Although the state argues that they are illegal, and that position has been upheld in the court, federal law prevents the state from acting to have them removed. Only the U.S. Attorney can act, but there has been no action pending resolution of the cases. The U.S. Attorney General has sent letters to the U.S. Attorneys encouraging a review of Indian gaming and direction to terminate any illegal gaming. The reluctance of the U.S. Attorneys to act may be explained by waiting for pending court cases to be resolved and their experience in other states where the U.S. Attorney acted against Indian casinos only to have the states reverse themselves and agree to allow slots.

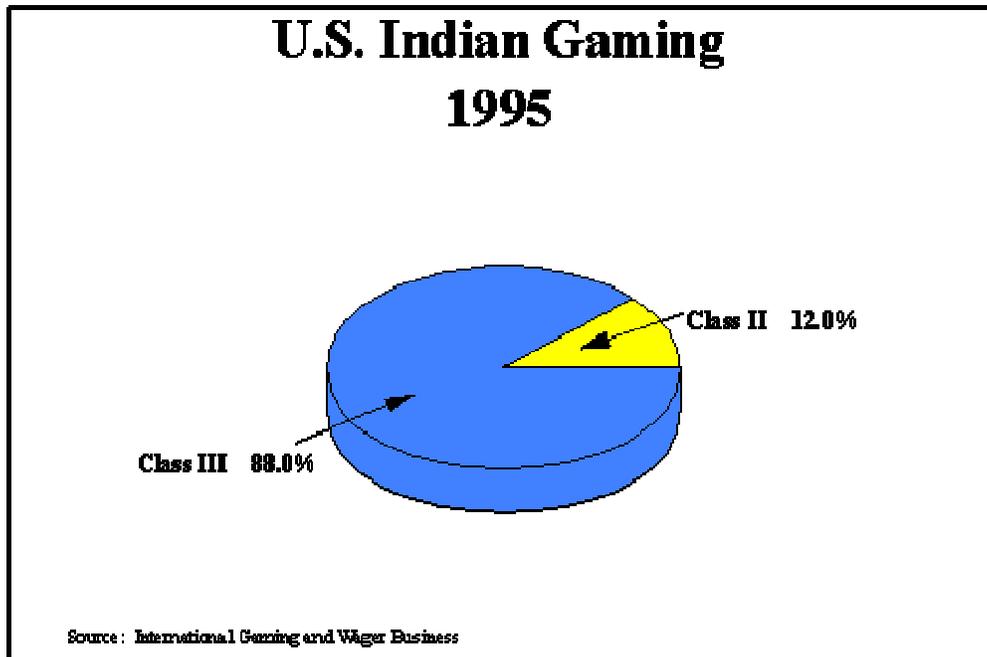


***If the Goal of IGRA Was to Promote Indian Gaming, it Has Been Widely Successful.***

As noted in the first sentences in this section, Indian gaming has become a multibillion dollar industry. Over one-half of the reservations in the country offer some kind of gaming. Fifty-nine casinos have been opened, with several more in the construction process.<sup>31</sup> Of the 550 recognized tribes, 109 have entered into high stakes gaming compacts in 20 states. Gaming operations range from huge casinos that rival or exceed any in the world to small bingo halls.

The following chart shows the growth of Indian gaming using the handle as the form of measurement. Some states in particular have seen dramatic growth. Minnesota has 17 tribal casinos, and Wisconsin has 11. One writer suggested that Minnesota is now the land of 12,000 slots.<sup>32</sup>

***Direction of Indian Gaming in California is Uncertain.*** The reason is the state's loss in the Western Telcon case. (See the Box on Major Court Cases, p. IV-7.) The case outlawed the lottery's electronic keno and definitely states that the Lottery cannot have banked games. Traditional slots are banked games. Maintaining the continued level of success in Indian gaming will require the alteration of traditional slots into non-banked lottery games, where the payout is dependent on the number of players and the house takes a cut based on the number of players, not the outcome of the game. In addition, they cannot use anything that would fall under the very broad definition of slot machines under California law. Arguments exist over how easy it is to make this change.<sup>33</sup>



After paying all costs, including management fees, wages, and winnings, the profits from Indian gaming accrue to the tribe for distribution. Consistent with the IGRA, tribes can make per capita distribution. Although the amount of money the tribes have earned varies, a significant share is going into service for members of the tribes. Indian gaming

has slowed the migratory trend of Indians moving from the reservation to urban areas and has even reversed some of the migration.<sup>34</sup> Some tribes have made direct payments to tribe members. The practice of direct payments alarm some people, for fear that the money will not be invested to improve the Indian's welfare. The evidence from earlier payments for land sales showed that they tended to be spent on consumer goods and were not invested.<sup>35</sup> This concern over how payments are spent is heightened because of the unsure future of Indian gaming.

Another issue is the sheer size of the payments. The Mdewakanton who operate a lucrative casino have distributed sixty-five percent of their net profit to 100 members. Reportedly, payments exceeded over \$500,000 each.<sup>36</sup> Other tribes invest their funds, replacing housing, protecting areas of cultural significance, and building schools. Some small tribes in California have significant gaming operations.

***Arguments Exist Over the Adequacy of Regulation of Indian Games.*** The IGRA also established a National Indian Gaming Commission made up of three administration appointments. The Commission is charged with the oversight of Class II games.

Tribal representatives strenuously argue that the regulation of gaming is adequate. They point out that because the profits accrue to them, they have every incentive to make sure that there are not diversions either from crooked players or employees. Others offer far different conclusions.<sup>37</sup> Other states have not agreed with the tribes and have increased their regulatory presence through the compact process.

In early October, the Senate Indian Affairs Committee held a hearing on oversight of Indian gaming. A Justice Department witness urged Congress to adopt standards because in some instances neither the state or the tribe would develop adequate regulatory standards.<sup>38</sup>

***States Unable to Tax Indian Gaming.*** States get some tax revenues from Indian gaming. Most casino workers are not Indian nor reservation residents, hence their income stream is taxable by the state.<sup>39</sup> Whether that represents a new income stream for states to tax is discussed in the social-economic impacts section.

The states have also used tribal gaming as a way to influence their relations with neighbors. New York threatened to legalize high stakes Indian gambling which would have competed with Atlantic City should New Jersey lure the New York Yankees away from New York.

Pacts between cash-strapped state governments and the tribes have a great deal of appeal to some states. Massachusetts Governor William Weld and the Wampanoag tribe are trying to negotiate a pact to allow casino gaming. As a condition, the state would get \$90 million per year and the revenues would be shared with affected cities and towns. Detroit would like to lure a Chippewa Indian casino to downtown Detroit.<sup>40</sup> In a different twist on revenue sharing, Washington tribes sponsored initiative 651 that would give each

registered voter a share of slot machine profits. The state was given no enforcement power. The measure was soundly defeated.

***Reservation Neighbors Often Unhappy Over Indian Casinos.*** Not surprisingly, the settled areas near reservations and rancherias complain about the Indian gaming facilities. These are usually rural areas and the people fear an onslaught of traffic and other urban ailments. The efforts by tribal members to open a casino in El Dorado County, is an example of the controversy that can occur.

Conversely, the tribes will argue that they can be a positive influence. Because of the improvement in their fiscal status, they can pay for services that weren't previously available in rural areas such as increased sheriff's patrol, and fire and ambulance revenues.

***Some Disputes Exists Between Indian and Private Gaming Interests.*** There was resistance and opposition to Indian gaming by most of the established Nevada and Atlantic City gaming interests. Harrah's at one time withdrew from the Nevada Resort Association because of the Association's opposition to Indian Gaming. Public corporations involved in casinos have changed their views as they have seen the business opportunities associated with managing Indian casinos. They see Indian gaming as a way to open casinos in states that are traditionally opposed to gambling.<sup>41</sup>

Relations between the tribe and their management contractor is not always amicable. For example Gaming World International was recently dismissed from its management contract with an Indian casino in Minnesota. The Tribal Council accused the company of gross mismanagement and misappropriating tribal funds. The company denies the accusations and says that it has been caught up in the tribe's problems. The former chairman was convicted of embezzling and conspiracy in charges related to bid-rigging when the casino was constructed. Two other tribal council members were also convicted.

Another interesting development is the widening conflict between Indian and non-Indian gaming. In New Jersey, an Oklahoma tribe wants to open a tribal casino near Atlantic City. These are Indians that were forced to move from New Jersey more than a century ago. Another interesting development is a national lottery proposed by the Coeur D'Alene Indian tribe in Idaho. That lottery would be available in all states that have a lottery, including California. The tribe has had difficulty in obtaining a long-distance carrier for the 800 number. The carriers have been threatened with criminal action by various states Attorney Generals. The matter is currently in litigation in the Coeur D'Alene tribal court.

There is, however, little direct competition between Indian and Nevada gaming in the sense that they don't own and operate casinos in the same geographic areas. The first Indian casino is opening in Nevada, but it is completely state regulated so it is not tribal gaming in the usual sense.

Not surprisingly given the number of tribes, Indian gaming is beginning to have its own conflicts. Tribes in Wisconsin and Minnesota opposed a new facility to be run by

Chippewas for fear it would encroach on the existing gaming operations of other tribes.<sup>42</sup> In California, Torres-Martinez Indians would receive funds to settle a 71-year old dispute over the loss of their lands when the Salton Sea was created by a dam break. The tribe plans to purchase new land for a casino, a move opposed by the Cabezon band, who are concerned about competition.

***California Has a Large Number of Reservations.*** Within the state, there are 104 reservations with 32,000 members, of which 12,500 live on the reservation or rancheria. California has about 12 percent of the Native Americans counted during the 1990 census. They are only 0.8 percent of California's population, about equal to the nation's share of

Native Americans. The vast majority in California do not live on the reservation.



Source: Sacramento Bee

Note: The above map shows Indian Casinos in California. There is disagreement in the accuracy of this map. No inventory of sites exist and tribes cannot be easily contacted for information as many are quite small.

The majority of people living on reservations and trust land in California did not identify themselves as American Indians in the 1990 census. Tribal membership is determined by individual tribes, and is frequently based on some minimum blood requirement and/or descent from a historical list of tribal members. Some tribes also have residency or participation requirements. The population of the tribes planning or operating in gaming facilities is small, ranging from one (The Buena Vista Rancheria of the Me-Wuk Indians) to over 4,000 (the Hoopa Valley Tribe). Eleven of the 35 gaming tribes have fewer than 100 members.

***Number of Recognized Indian Tribes Could Grow.*** Recognition petitions allow groups of Indians to become recognized as tribes. Historically, there was not a lot of concern about these petitions. Now the possibility of expanding the size of the gaming industry has increased the controversy surrounding the petitions. Within California, 37 tribes have pending petitions for recognition, 14 of these were filed after the passage of IGRA. Some of the tribes are seeking land in the most populous areas of the state. Nationwide, 165 tribes have petitions pending, some dating back to 1826. Only nine have been recognized by the Bureau of Indian Affairs and an additional seven have been restored or recognized by Congress. Another 109 tribes, including 41 in California, were once recognized but were later terminated during a time of a federal policy for assimilation.<sup>43</sup> These tribes can petition to be restored.

These tribes have a great deal of flexibility acquiring a land base without state approval. A restored tribe in Sonoma County tried to build a casino in Santa Rosa with the backing of Japanese investors.<sup>44</sup> The deal eventually fell apart. The Mohegans in Connecticut bought land and had it approved as trust land by the Bureau of Indian Affairs (BIA). They obtained financing for a casino project with \$175 million in privately placed bonds, becoming the first tribe to get capital financing from Wall Street. Part of the settlement was that the tribe drop land claims to over 20,000 acres in return for being allowed to purchase the land for the casino.

There are at least two imminent possibilities for restored tribes to obtain land near urban areas in California. One is the Auburn rancheria. In 1994, Congress passed and President Clinton signed a bill restoring the United Auburn Indian Rancheria to federally recognized tribal status. Another band, the Mechoopda Band of Maidu is trying to buy 240 acres of land in Sutter County and declare it sovereign territory and establish a casino. The members of this tribe gave up their status as a tribe. However, the federal government did not live up to the commitment it made to provide financial help to the tribe, which played a role in band members losing the land they were granted as individuals. As a result, they sued and won a ruling reinstating them as a tribe, but they had already lost their tribal lands. The settlement allowed the tribes to acquire land anywhere in California and have it be placed in trust. The tribe is being bankrolled by Showboat Casino of Nevada.

Normally, tribes can only use land off the reservation for gaming with the approval of the Secretary of the Interior in consultation with the local community or consent must be given by the Governor to gamble on the lands. Some Native Americans have had success

operating bingo and casino halls off the reservation. The Potawatomi Tribe gained permission to operate a bingo and casino hall in Milwaukee, 200 miles south of their reservation. Such movements concern law enforcement officials. Some officials currently view Indian gaming as being more difficult for organized crime to infiltrate because of its isolated gaming centers, hence the move to urban areas could make this more of a problem.<sup>45</sup> (See the discussion in the [crime section](#).)

***Some Non-gaming Tribes Criticize Gaming Tribes.*** Criticism of the present structure of Indian gaming has come from an unexpected source, other Indians.<sup>46</sup> From the numbers presented in this section, it is clear that only a minority of tribes are involved in gaming. Of those, only a minority are doing what a Department of Interior official terms as "Fairly well."<sup>47</sup> Some tribes, because of the isolation of their reservation, are unlikely to ever benefit. These include some of the largest tribes in America. Some advocates suggest a method for pooling gaming profits to help tribes that are poorer.

There are also factions within tribes, so-called "traditionalists," that object to gaming. These differences have led to significant disputes. Approximately 25 reservations nationwide are being torn up by these problems.<sup>48</sup>

***Overall Impact of Indian Gaming is Still Uncertain.*** It is very difficult to say with authority what the social-economic impact of Indian gaming has been. Of interest to most observers are the following questions:

- What is the impact on surrounding communities? Impacts would include economic as well as social, including changes in rates of compulsive gambling.
- What is the impact on the tribe and what are the opportunities available to the tribe and its members?

Definitive answers to these questions do not yet exist. Research has been hampered by several factors:

- Indian gaming is a relatively recent phenomenon.
- Local governments have not studied it as it occurs outside of their jurisdiction.
- Casino earnings are difficult to trace, in part because the information is proprietary.

There have been several reports that have been quite laudatory, but they have been commissioned by the tribes. These are discussed more in the economic section.

***Indian Gaming Has Appeared to Lead to Greater Political Involvement by Tribal Members.*** New Mexico is another state where Indian gaming has become a major political issue. The then incumbent Governor would not sign compacts with the tribes. As a result, the gaming tribes mobilized and donated funds to his opponent, who eventually won the election. Native American turnout in the election was somewhat higher than in past elections. Native Americans have historically exhibited low levels of voter turnout even when compared to other ethnic minorities.<sup>49</sup>

***State Fears on Crime Are Not Groundless.*** In October 1995, gunfights broke out in the Elem Indian colony in Lake County over control of the tribe's casino. Seven people were wounded. This event prompted the Attorney General Dan Lungren to convene a formal briefing on enforcing laws on tribal reservations and rancherias. Similar conflicts have occurred in other states.

Another question, to what extent is organized crime a threat? Donald Trump has testified before Congress that organized crime is rampant in Indian gaming.<sup>50</sup> At the same hearing, the FBI, the Department of Justice, and the Internal Revenue Service testified that they had no evidence of widespread organized crime within Indian gaming. Critics say that their statement is evidence of how loosely they regulate and oversee Indian gaming. Senate supporters of Indian Gaming, Senators McCain and Evans, both concluded that the concern about organized crime was a smokescreen for concerns about economic competition.<sup>51</sup> Others look at some of the unsavory business connections that have been established by the tribes and suggest that a problem of "disorganized" crime is much more of a problem.<sup>52</sup>

Another concern about Indian gaming is that it leads to the legalization of other kinds of gambling, although opinions are split.<sup>53</sup> There are a lot of opinions on this issue, but few conclusions. Some argue that Indian gaming has led to increased legalization of other gaming by states. Others argue that other gaming would have been legalized anyway to gain money, stimulate the economy, and create jobs. Some people think it has helped destination gaming, such as Nevada, as people get a taste for gambling, they are more likely to opt for a gambling destination vacation.

Another criticism that has been leveled is over the low number of Native Americans that are employed in gaming. The low employment may be good or bad depending on who is looking at the situation. If the employees are not Native Americans living on the reservation, then state and local governments should get more tax revenues. Many of the tribes are so small that they can not supply a sufficient number of employees. The lack of experience is being remedied to some degree by education and training. DQU (Deganawidah-Quetzalcoatl University), an Indian college near Davis, is offering a course of studies in Indian Gaming.<sup>54</sup>

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## ***V. Gambling in California***

Californians can choose from a variety of gambling opportunities. California has legal gaming that includes a state lottery, parimutuel horse wagering, cardclubs, Indian casinos, and charitable gaming.

Much of the basic framework of gaming has been enacted by the people through constitutional amendments rather than by the Legislature. The State Lottery was enacted through a constitutional amendment as was horse racing. The Constitution specifically prohibits Nevada and New Jersey-type casino gaming.

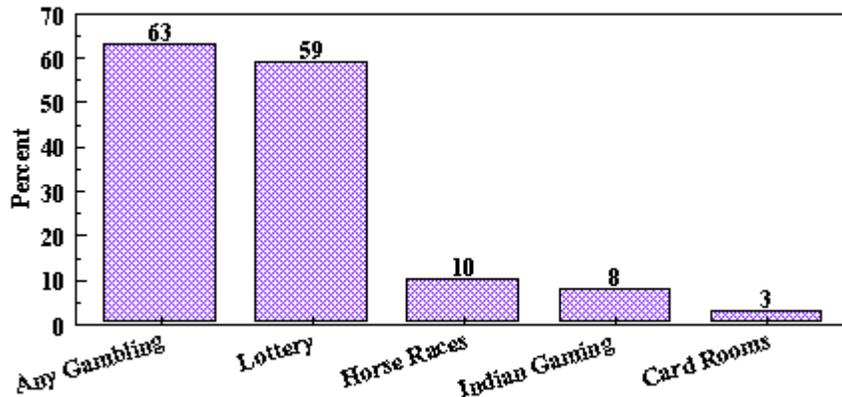
Gambling is a \$14 billion business in California as measured by the handle.<sup>1</sup> The amount actually lost by consumers is much less, approximately \$2.5 Billion. While that is a small portion of California's approximately \$700 billion economy, it is a sizable amount of money. As the following chart shows, California is the sixth largest gambling state. California is the only one of these six states that doesn't have high-stakes casinos. These totals do not include Indian gaming as there are no reliable state by state estimates.



A cautionary note is needed for the preceding chart. Handle is defined as the total amount wagered. Since much of the gaming is between players, not the house, at California cardrooms, the handle is difficult to measure but must be estimated.

The following chart shows the popularity of different games for Californians. Not surprisingly, the lottery is the most popular.

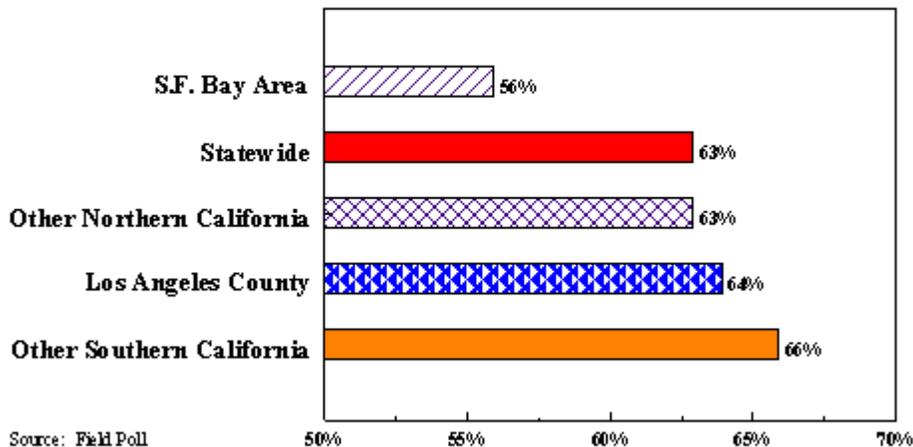
## Participation of Californians in Various Types of Gambling in 1995



Source: Field Poll  
 Note: Only gambling in California is counted  
 and only adult participation is included

There are some small regional differences in participation as the following chart shows:

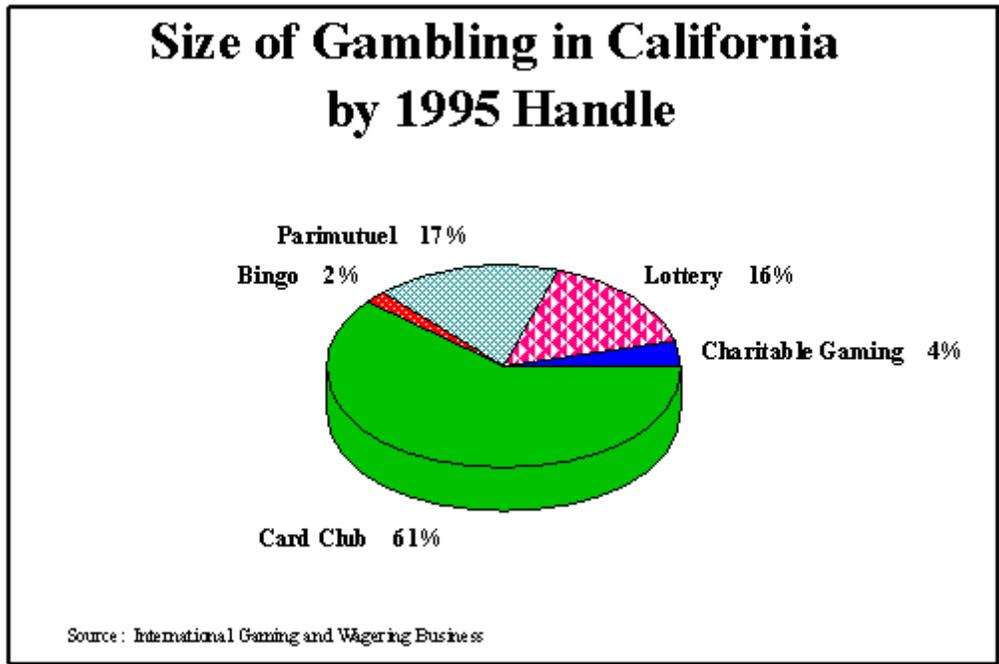
## Regional Participation of Californians in Any Gambling - 1995



Source: Field Poll  
 Note: Only gambling in California is counted  
 and only adult participation is included

No discussion of gambling in California would be complete without noting the gambling that Californians do in their neighboring state. Californians spend \$9.5 billion in Nevada each year on gambling while making 14 million casino visits.<sup>2</sup> California is the top feeder state to Nevada casinos.

Following is a discussion of the different types of gambling in California. The next chart shows the relative sizes of these gaming types. The discussion does not include the gambling that occurs on cruise ships. Owing to a recent change in federal law, cruise ships can call at consecutive California ports and allow gambling. This will be a relatively minor amount compared to the overall state total. The following graph includes estimates of charitable gaming other than bingo. While bingo is the only legal charitable gambling, the category includes charitable sweepstakes which aren't actually gambling under the California penal code. The difference is that donations are requested rather than require for the prizes.



### ***Parimutuel Wagering***

In California parimutuel wagering is limited to horse racing, which is regulated by the California Horse Racing Board. Horse racing was legalized in California in 1933 through a constitutional amendment. The amendment authorized the Legislature to regulate horse racing and to authorize parimutuel wagering at licensed racing tracks. Enabling statutes were soon enacted. The statutory authority for the board is commonly known as the Horse Racing Law.

The goal of the regulatory scheme is to:

- Assure protection of the public,
- Encourage agriculture and the breeding of horses in this state,
- Generate public revenues,
- Provide for maximum expansion of horse racing opportunities in the public interest, and
- Provide uniformity of regulation for each type of horse racing.<sup>3</sup>

The Board consists of seven members appointed by the Governor to four-year terms. The appointments are subject to confirmation by the State Senate. The Board has two main programs related to gaming. One is overseeing parimutuel wagering and the other is designed to ensure the integrity of the actual horse race. The Board has about 75 employees, including investigators, to regulate about \$2.5 billion in wagers placed at facilities in-state. Another \$1 billion is bet on California races from out of state facilities and is handled by the Board.

One recent change has been the legalization of simulcast wagering. This is parimutuel gaming at a site remote from the actual race, although most of the sites are at existing racetracks. Intrastate and interstate wagering can occur at these sites. The amount wagered at simulcast facilities now exceeds the amount wagered at races.

There are some disturbing trends for the industry however.

- The on-track handle has dropped 47 percent in the last decade.
- License fee revenue for the state has declined 27 percent in the last five years.

### ***State Lottery***

The California lottery gained approval at the November 1984 election, making California a relatively recent entrant into the lottery business. The vote was not even close as a 58-percent majority approved the lottery. Only one state has turned down a publicly-run lottery and the aye votes have been as high as 81 percent, although the mean of all states was 64 percent, slightly above California's vote. The initiative amended the California Constitution and added provisions to the California Government Code.

Prior to the initiative, five major legislative proposals on the lottery had surfaced but none of them had made it to the ballot. Circumstances changed when in 1982, the state faced a major budget shortfall. Momentum increased for passage until Governor Deukmejian said he would veto a lottery if it passed, bringing a halt to legislative efforts.<sup>4</sup>

With legislative action stymied, an initiative was started. At the time it was considered an expensive campaign to qualify and win passage, costing about \$1 million. A pro-lottery coalition led by a company that supplied lottery products qualified the measure and earned passage. The statute earmarked the proceeds for education. An interesting requirement of the statute was the extensive disclosure by firms that would get contracts. One of the leading firms was an affiliate of Bally Manufacturing Company that already had to meet this extensive disclosure requirement because of their New Jersey gaming activities.<sup>5</sup> The measure passed despite opposition by the Governor, Attorney General, and some religious leaders who were mostly Protestants. The affiliation of the religious leaders is notable because religious figures have been important opponents of gambling, although they are usually from Protestant denominations.

***The 1984 Lottery Measure Was the Second Chance Voters Had to Approve a Lottery.*** California voters turned down an initiative in 1964. That measure would have authorized

a private firm to run a lottery. The measure lost by a large margin, 31 to 69 percent. The initiative was opposed by the Governor, Superintendent of Public Instruction, and most of the state's press.

The 1984 initiative set up an autonomous five-member commission to run the lottery. The commissioners are appointed by the Governor and confirmed by the Senate. One of the commissioners must have a minimum of five years experience in law enforcement and at least one of the commissioners shall be a certified public accountant. Prior to the keno game being dropped, the lottery had about 800 employees and 30 agents to oversee \$2 billion in gross sales.

The Lottery Act limits the types of games that can be used. The specific list is drawn so as to limit competition with horse racing, cardclubs, and bingo.

The lottery in California is a government monopoly. Government was chosen to operate the lottery primarily to reduce the possibilities of corruption.

In California, about half of the revenues are returned to winning players as prizes. A minimum of 34 percent is allocated to educational institutions and the remainder covers administrative expenses including retailer commissions. California has one of the nation's largest lotteries, befitting the size of the state.

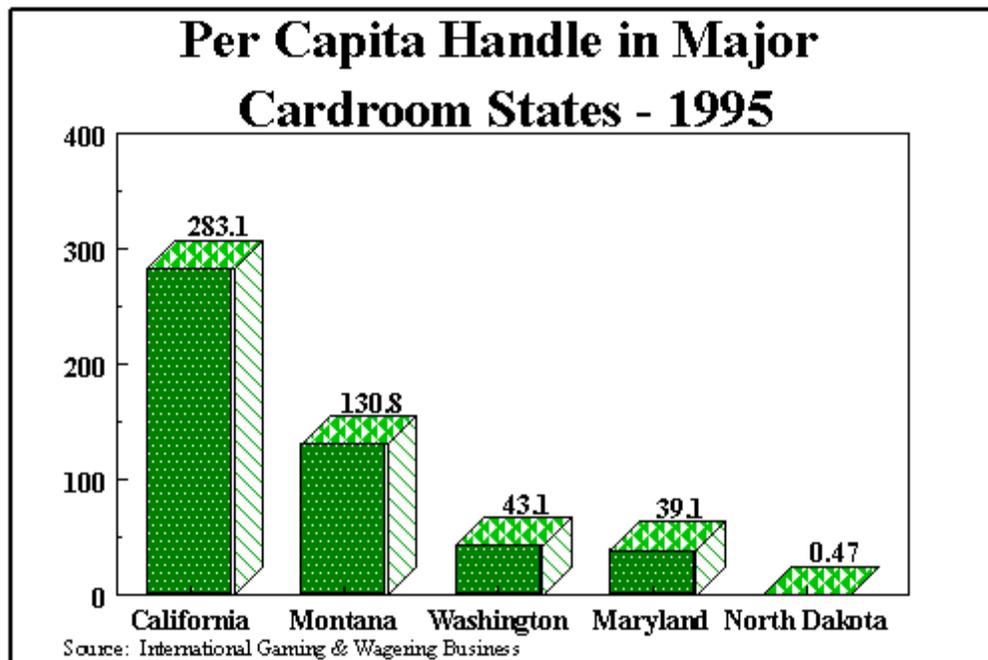
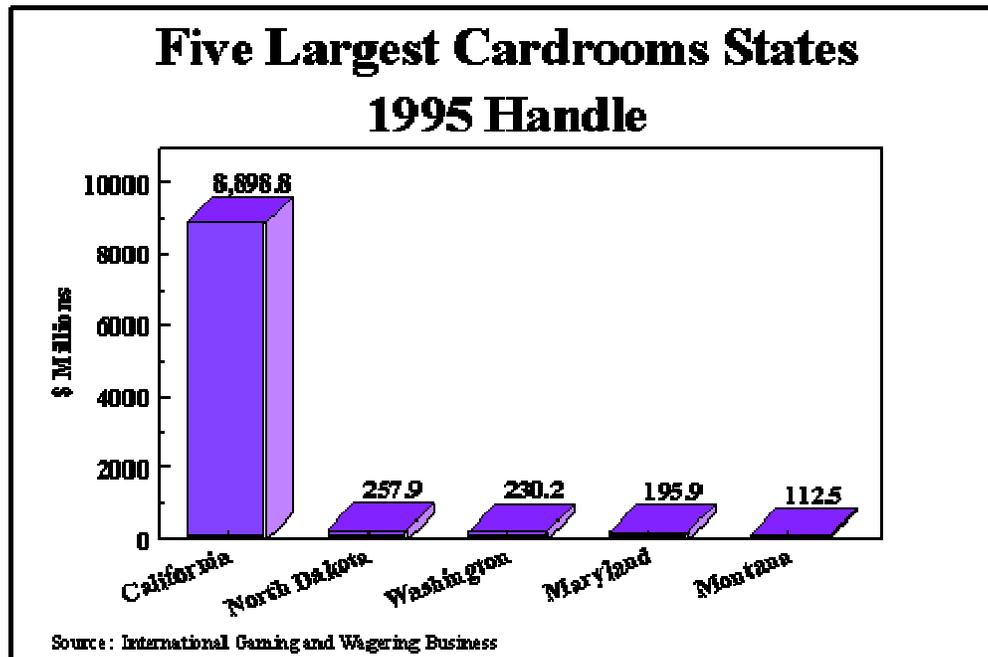
The lottery does not provide a large amount proportionately to the school districts. The average district gets about 2 percent of its general fund from the lottery. The amount varies from year to year, depending on the success of the lottery. Since 1985-86, the amount has varied from \$76.64 to \$178.63 per student. According to informal surveys compiled by the California State Lottery, the majority of the money goes for salaries and wages. (It is not clear from the survey if the respondents meant higher salaries for existing teachers or more teachers.)

***Lottery Activities Diminished by Legal Problems.*** The state lost its case in Western Telcon. The case banned the Lottery's electronic keno and definitively states that banked games are not legal within the state. Shortly after, the Attorney General advised that the Scratcher vending machine is a type of slot machine, although it is a lottery game. Slot machines are illegal in California. The Scratcher vending machines accounted for approximately \$200 million in lottery revenues annually. The keno game is significantly larger, amounting to about \$400 million annually.

### ***Cardclubs***

Cardclubs have existed in the state as long as there has been a state. State law neither specifically authorized nor prohibits these. California's gambling statutes prohibit certain types of gaming, rather than authorizing certain types of gaming. Cardclubs are legal because they have not been specifically prohibited. But only those games not prohibited can be played at these facilities. House revenues are generated by charging a seat rental fee, by time period or by hand played.

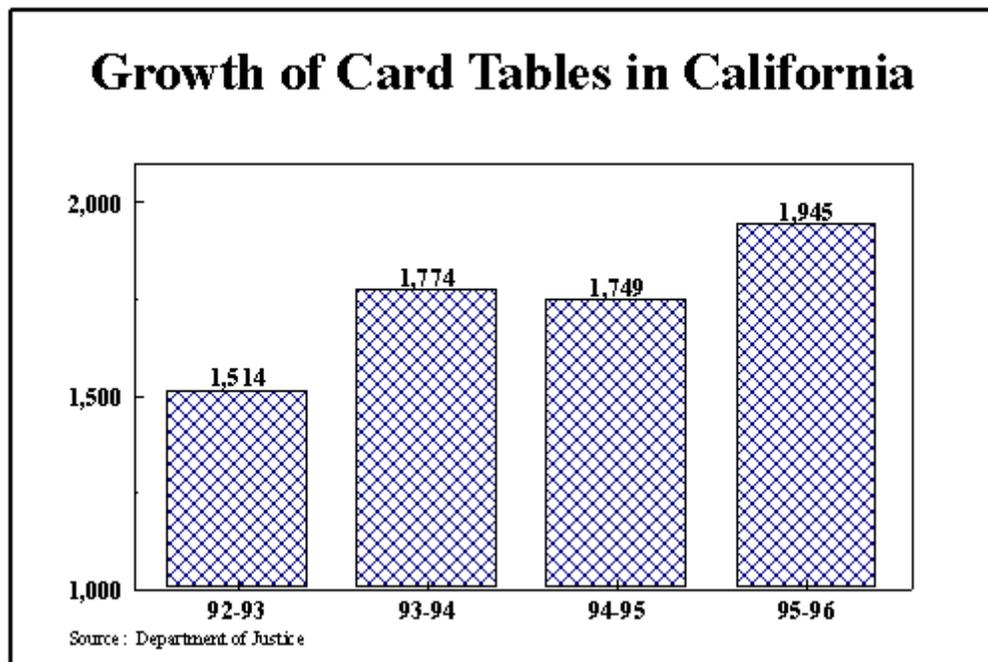
As shown in the following chart, California cardclubs are the largest nation-wide when compared to other states with free-standing cardclubs.

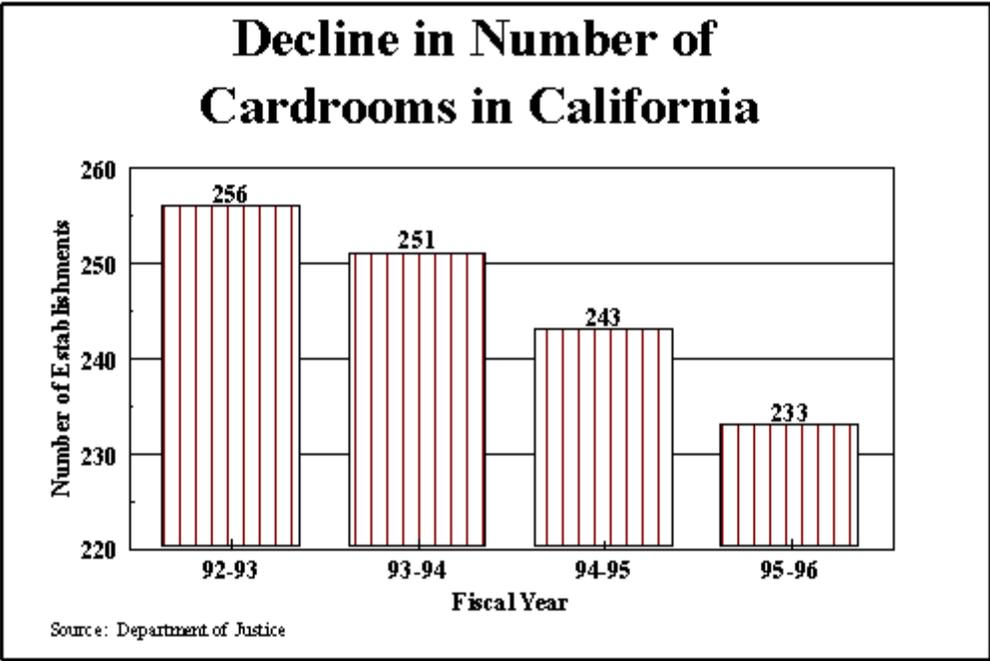


Cardclubs are approved by and licensed by local jurisdictions. Owners and operators must be registered with the Attorney General per the Gaming Registration Act.<sup>6</sup> This chapter applies to all gaming clubs in existence on or after July 1, 1984. Under the current law, the state does not tax the clubs, but local governments may negotiate a tax with the developers.

Cardclubs in California generate a great deal of gambling activity compare to clubs in other states. It may seem surprising that California allows cardclubs. There are several reasons why cardclubs are viewed differently than other types of prohibited gaming. One reason is that the club cannot directly benefit from the amount wagered. Fees can be charged only for play. In that way, money is lost to other players, not to the house, and is more likely to remain in the community. Casinos are viewed more negatively because they, like lotteries, take money from the community. Another reason is that playing cards requires an element of skill and is often viewed differently than games of chance. Cardclubs are very different than casinos. Cardclubs cannot offer the banked games such as 21 and slot machines that are normally found in casinos. The cardclub provides services such as a cashier and dealer. Players, for a fee, can play against each other, not the house.

***Cardclubs Have a Large and Growing Presence Within the State.*** It is estimated that the state's 233 cardclubs generated \$711 million in gross revenues in 1995.<sup>7</sup> Bettors wagered approximately \$8.5 billion.<sup>8</sup> Bettors wagered four times more than Californian's spent buying lottery tickets. As the following table shows, cardclubs have added almost 500 tables since 1992. Although the number of tables has increased, the number of California's cardclubs has actually shrunk as older smaller parlors have closed.





Overall, the industry has been dramatically changing. As noted earlier, the older smaller clubs are closing and new larger facilities are being opened. Despite the shift, cardclubs vary tremendously. For example, one of the owners has been quoted as saying that Sacramento has seamy, derelict-type cardclubs.<sup>9</sup> Other jurisdictions have much more extensive and elaborate facilities. The newly opened Club San Pablo drew 5,000 people to its opening. The 71,000 square foot club cost \$31 million, has 60 tables and 900 parking spaces. The club is supposed to pump \$4.6 million in sales tax and \$14-18 million in salaries into the local community.

#### California's Largest Card Clubs

Card club	Cities	# of tables	City Revenues from Card Clubs	% of Gross Revenue City Receives
Commerce Club	Commerce	217	\$13.5 million	13.0%
Bicycle Club	Bell Gardens	200	\$8.94 million	12.5%
Hollywood Park	Inglewood	140	\$5.52 million	11.0%
Crystal Park Casino*	Compton	110	\$0.32 million	10.9%
Ladbroke's Casino	San Pablo	100	\$3.73 million	12.4%
Normandie Club	Gardena	80	\$4.16 million	15.5%

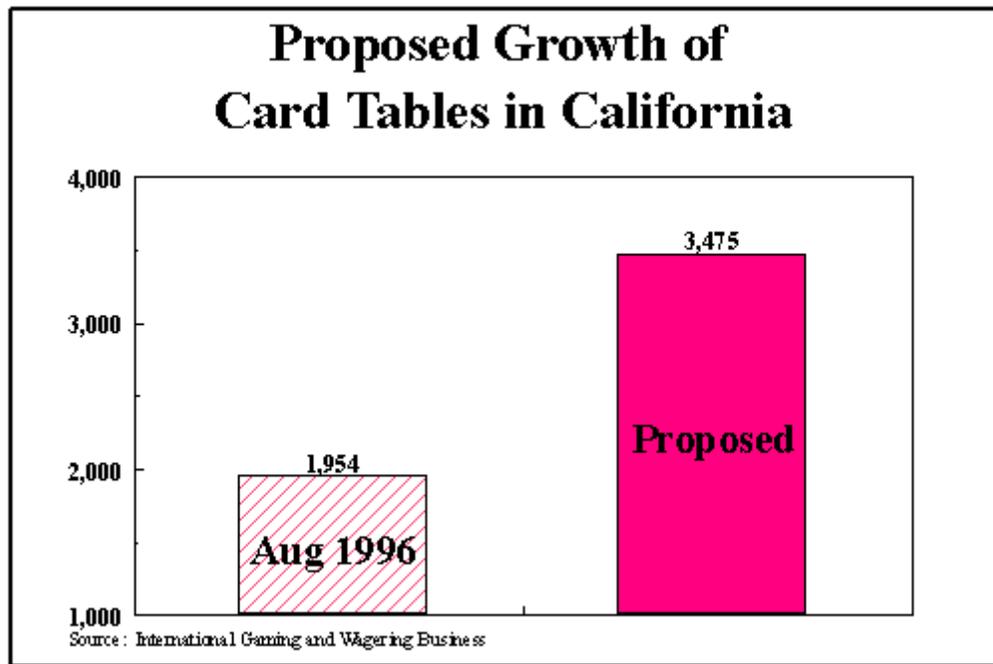
Huntington Park Casino*	Huntington Park	70	\$0.23 million	8.0%
Garden City Card Club	San Jose	40	\$3.01 million	13.0%
Bay 101	San Jose	40	\$5.51 million	13.0%
Oaks Card Club	Emeryville	40	\$1.4 million	6.5%

\*Note: the figures for Crystal Park Casino are for only November, 1996. The club opened in October, 1996.

\*Note: The figures for the Huntington Park Casino are from the 94-95 fiscal year. The casino and the city agreed to defer the payments to the city until July 1997 due to changes in management.

Sources: Department of Justice

The changes that have occurred are projected to continue. Following is a chart from a noted gaming industry publication that shows the proposed increase in card tables at California cardrooms.



Much of the increased player interest is due to fast-paced Asian games such as Pai Gow. These can generate large pots, up to \$75,000 and involve side betters. Sacramento Sheriff Glenn Craig says these situations bring "money laundering, Asian gang involvement and the actual or attempted corruption of local government."<sup>10</sup> However, because of their revenue potential, cardclubs are touted as a possible source of funds for local governments.

Despite the construction of these new clubs, the industry profitability has been hurt. In a case over what is called jackpot poker, the clubs lost. The game was ruled a lottery, which is illegal except when offered by the state. The jackpot was paid when two players got certain hands, hands that were not useful in winning the poker game that was the main object of play. The jackpot was incidental to the poker game. The jackpots were as high as \$70,000, from which the clubs got a healthy cut.

***California Has no Special State Agency to Regulate Cardclubs in the State.*** Although the Department of Justice has a role, it is not the regulator in the same sense that other states have regulatory agencies that oversee gambling activity. This situation has led some outside researchers to point to California as an anomaly. As one researcher, who overstated the number of cardclub rooms, noted:

"For a bad example of gambling regulation, California stands out. There are over 400 legal cardrooms in that state, with no special agency to regulate them."<sup>11</sup>

California's Gaming Registration Act was enacted to provide a minimum level of regulation by registering owners and operators as a prerequisite to licensing. The Gaming Registration Act is administered at the state level through the California Attorney General. Annual registration is required. This annual process involves updating of information which trigger additional background checks.

The act provides that state and local governments have concurrent jurisdiction over gaming establishments within the state and expressly disclaims state preemption of regulation. On an ongoing basis, cardclub rooms are regulated only by municipalities which develop a code for regulation. Sometimes a combined city-county ordinance is used such as in Sacramento. New cardclub rooms can only be opened after an affirmative vote of the electors within the city, county, or city and county, unless the jurisdiction had a club operating prior to January 1, 1984.

Other limitations on clubs include the types of games. Most non-banked card games are permitted, but faro, monte, roulette, lansequenet, rouge et noir, rondo, tan, fan tan, seven-and-a-half, twenty-one, hokey-pokey or any banking or percentage game played with cards, dice or devices for money or scrip are explicitly prohibited.<sup>12</sup> In non-banked games, players are not playing against the house who controls the purse such as in twenty-one at a Nevada casino. California law currently prevents publicly owned-companies from operating cardclub rooms with the exception of those companies who run racetracks. Sizes, locations and hours of operation are determined on the local level. Gambling activities that are not expressly prohibited or regulated by state law may be prohibited or regulated by local government.

***Cardclub Elections and Actions are Often Quite Volatile.*** In Folsom, the council allowed expansion of an existing cardclub, but opponents collected signatures to force a referendum of the Council's action. Some residents in Colma were gravely concerned about cardclub gambling and unsuccessfully attempted to overturn by referendum the 1993 vote to legalize cardclub gaming. In San Mateo, Bay Meadows poured more than

\$400,000 into the cardclub election but still lost by a 3-2 ratio. The Bay Meadows proposal included a provision that the City of San Mateo would get 15 cents of every dollar gambled. That would mean that the city would get as much as \$6 million annually. In addition the club would pay all of the costs associated with regulating itself that was approximately \$1 million per year. A San Jose club put in \$150,000 to attack the proposal in an attempt to squelch competition.

There were other instances of money from the existing clubs being used to finance the opposition in cardclub ballot measures. This occurred in the recent election in Pomona. The Agua Caliente Band of Cahuilla Indians sponsored advertisements opposing several new cardclubs proposed for the city. The cardclub in Bell Gardens, the one that is partly owned by the Federal government, also contributed \$200,000 to quash clubs in elections in Pomona and Pico Rivera.<sup>13</sup> Actions such as these have led to a Fair Political Practices Commission (FPPC) suit against the Commerce Club for the club's contributions against a ballot measure in nearby Pico Rivera. The FPPC alleges that the Commerce Club did not report independent contributions and was late filing other statements of contributions. The developer of the proposed Pico Rivera club has initiated a suit against the Bicycle Club for similar reasons.

A recent council action in San Jose authorized doubling the number of card tables at existing clubs. It was opposed by social workers and groups within San Jose's large Vietnamese-American community who claim that gambling-related problems are tearing apart vulnerable immigrant families and leading to more crime. The action was eventually reversed.

***Revenue Needs by Local Government Have Led to New Cardclubs.*** There was a rush of new cardclubs after the passage of Proposition 13 because of local government's desire to replace the lost property tax revenues. Small blue-collar cities were particular favorites.<sup>14</sup>

***Concerns Expressed About the Fiscal Dependence of Cities on Cardclubs.*** Local governments have the obligation to regulate, but critics question whether there isn't a conflict of interest. When a single revenue source becomes that important, the city is not just a revenue recipient but a municipal partner according to some reports.<sup>15</sup> The partnership reached a point with one club where the city considered issuing bonds to finance the purchase of the federal interest in the club by club employees.<sup>16</sup> The concern is that the city is reluctant to interfere with the club operation for fear of losing municipal funds.

The following table shows the large proportion that cardclub revenues comprise of city budgets in some cities.

<b>Portion of Cardclub Revenues for Selected Cities</b>
<b>\$ Millions</b>

City	City Revenue From Cardclubs	Total City Budget	% From Cardclubs
Commerce	13.5	36.7	36.7
Compton	0.3	76.5	.3
Huntington Park	0.2	23.6	.8
San Jose Combined	8.5	663.7	1.2
Inglewood	5.5	109.6	5.0
Emeryville	1.4	12.8	10.9
Gardena	4.2	36.8	11.4
Bell Gardens	8.9	20.1	44.3
San Pablo	3.7	8.1	45.7

Sources: California Research Bureau, Dept. of Justice Office, State Controller's Office

The fear to regulate can be heightened by the competition between cardclubs. Many cardclubs are very close to each other and so they do compete even if they are within different jurisdictions. This competition has raised questions about how effective can the local government be if stricter regulation may drive customers to other clubs in other jurisdictions, jeopardizing the regulating town's revenues.

***Ban on New Clubs Led to Numerous Elections.*** There is a statewide moratorium on new cardclubs. The ban began January 1, 1996 and lasts until January 1, 1999. The moratorium was part of SB 100 (Maddy).

The cardclub elections held in 1995 took on added importance because they were considered a barometer on a possible statewide ballot campaign to legalize casino-style gambling. Following is a table of recent elections.

#### **Cardclubs Elections and City Council Votes During 1995**

City	Proposal	Election Date	Results
South San Francisco	150-table cardclub casino on an	Sept. 12	Failed

	isolated patch of Oyster Point land just east of Highway 101		56% Y - 4461 N - 5644
Irwindale	60,000 square foot cardclub that would serve @ 3000 customers daily	Oct. 21	Failed 59% Y - 192 N - 280
San Mateo	50-table cardclub at Bay Meadows Race Track. Also proposed that the city of San Mateo receive 15 cents of every dollar gambled at the club -- the highest cardclub tax rate in the state.	Nov. 7	Failed 62%
San Jose	City council votes on allowing up to 100 additional tables at existing clubs, which now have 81 tables.	Nov. 7	Approved initially then repealed.
Marina	City council votes on whether to amend its gambling ordinance to allow additional clubs. Developers have proposed a 60-table club and resort on an old Fort Ord airfield.	Nov. 7	Approved
Coachella	Election	Nov. 7	Approved
Hesperia	Election	Nov. 7	Failed
Ontario	Election	Nov. 7	Failed
Palm Springs	Three cardclubs; one 30 table cardclub in a former department store.	Nov. 7	Approved
Pomona	One 100 table cardclub; previous measure to allow two cardclubs was defeated in April.	Nov. 7	Failed

			55% Y - 5262 N - 6452
Pleasanton	City council votes on a proposal for a cardclub at the Alameda county Fairgrounds.	Nov. 7	Failed
Suisun	Riverboat Cardclub.	Nov. 7	Approved Y-1851 N-1829
Hawaiian Gardens	Measure A.	Nov. 21	Approved Y- 965 N- 722
Lynwood	Measure L to legalize cardclub casinos.	Dec. 19	Failed Y- 609 N- 990
Pacifica	Measure B, an advisory vote that called for a single, 200-table gambling hall to be built on Mori Point.	Dec. 12	Failed 76%
Pacifica	Measure A which would change Pacifica's anti gambling ordinance to allow cardclub rooms in the city.	Dec. 12	Failed 80%
Azusa	Proposition A which would have allowed the Normandie Casino to build a gambling facility.	Dec. 12	Failed Y- 1339 N- 3511
Colton	Election	Dec. 12	Failed

Perris	Election	Dec. 12	Failed
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***Full Casino Gambling the Subject of Initiatives.*** Three statewide initiatives were being considered for circulation. One of the most prominent parties involved with an initiative is Mr. Mark Bragg, a real estate developer and president of the Palm Springs Gaming Corporation. He was one of the sponsors of the recent cardclubs measure in Palm Springs. His proposal would have designated three sites across the state that would be allowed to have Nevada-style casino gaming. An adequate amount of signatures were gathered to be submitted to the Secretary of State. It did not, however, qualify for the ballot, because too many signatures could not be verified. The sponsor disagrees and has vowed to contest the state's findings. The measure needed 694,000 but only received 588,809 confirmed signatures.

There have been some problems associated with the signature gathering for the initiative. Paid gatherers have admitted to violations of the law both in California and Nebraska. In California, a paid gatherer admitted to forging signatures. At least in Nebraska, the violations were not limited to initiatives associated with gambling.

Another initiative to allow casino gambling at five designated racetracks was being circulated in early 1997. If successful at gathering the required amount of signatures, it will be placed on the June 1998 ballot.

### ***Charitable Gaming***

Cities and counties are allowed under state law to authorize bingo. The regulator is left up to the local governments. The gross revenues are \$60 million. The total is about 2 percent of overall gaming gross revenues within the state.

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## ***VI. Regulation of Gambling***

Where gambling is legal it is very extensively regulated. There is probably not another business that has so many aspects of its operations so heavily regulated. The primary purpose of the regulation is to keep out criminals. The extent of the regulation is justified because gambling has had a long history of criminal involvement. Gambling operations also have large amounts of cash that are uncounted and unrecorded as the gambling takes place, making it convenient for criminal activities such as money laundering and skimming. Gaming regulation also protects the public by making sure that games are honestly run.

Given that the primary aim of gambling regulation is to keep out criminal elements, what does a state look for in designing an effective regulatory regime? One researcher identified two aims for effective regulation:<sup>1</sup>

- Divorce licensing from politics.
- Tighten controls by regulator and operator.

This chapter will look more closely at states that have a more involved regulatory structure than California. Because few states have cardrooms, especially of the size of California, there are not many similar models. Washington and Montana are states that will be examined. In addition, the more expanded regulatory presence of the casino gaming states will be analyzed. Although California doesn't have casino gaming, these do provide some models and lessons for California.

### ***Washington in Gaming Regulation***

The Washington Gaming Commission oversees all authorized gaming in the state. The commission is made up of nine members. Five are appointed by the Governor to six year terms. These appointees are subject to the advice and consent of the Senate. There are also four ex-officio members, two each from the Senate and the House. The commission is an autonomous agency.

Washington, like California, has cardrooms. The significant difference is that cardrooms can only be ancillary businesses designed to support a main business of a restaurant, bar or tavern. The profitability is also strictly limited by statutory limitation on the charges. Until recently the club could only charge \$3 per half hour per seat. A recent change in law allowed this to be raised.

The Gaming Commission also has responsibility for other gambling. These include sports pools, charitable gaming, amusement games and pull-tabs. There are a large number of tribal casinos within the state that are under the oversight of the commission.

The state does not tax the card clubs. However they can be taxed by localities.

The Washington Gaming Commission is large by California standards. They have about 135 staff people. They have an ongoing and open process of negotiating compacts with the Indian tribes.

### ***Gaming Regulation in Montana***

Montana has video poker, video keno, live card games, sport pools, and casino nights for nonprofits. Montana is unique in that the state has a long history of gaming including slot machines, roulette, and twenty-one. The fact that gaming was illegal was completely overlooked until the late 1940s when the practice was challenged and the State Supreme Court found that it was actually illegal. It took over 30 years for gaming to make a comeback.

In 1989, the Legislature established a Gambling Control Division within the Justice Department. This action placed the licensing, auditing, and enforcement functions under one roof.

Prior to the creation of the division, there was local control of the games. Each local government could lower the number of state-sanctioned machines in an establishment, and levy a local tax. The 1989 changes placed all revenue collection matters under one set of regulations at the state level. The taxes are split one-third to local governments, two-thirds to state government.

Local governments retain some control. They may extend the 2:00 a.m. closing hours set by the state. Local governments may also restrict gambling to certain geographical areas through zoning regulations.

The Gambling Control Division currently employs about 36 persons. The Division tests and approves machines. They also issue licenses to qualified applicants after conducting a thorough background investigation. All findings concerning the denial, granting, renewal, revocation, or suspension of a license or investigation are subject to judicial review. An auditing branch of the Division examines tax records, and investigates financial issues. Compliance with the law and record-keeping is the major focus of this group.

Besides Washington there are approximately 10 states that have gaming commissions without casino gaming. In some states the commission regulates only charitable gaming. Other states the commission regulate Indian gaming, cardclubs, or other small scale commercial gaming.

The following portions of the report look at casino gaming states and the entities that regulate such gaming. Emphasis is placed on Nevada and New Jersey because they have the longest history.

### ***Gaming Regulation in Nevada***

***Nevada Has a Major Gambling Presence.*** The state issues about 500 casino licenses and regulates 1,800 slot licenses, 1,360,000 slot machines, and 5,300 table games. Gambling revenues to the state exceed \$300 million, about 45 percent of state revenues. No other state has such a large share of state revenues or economic activity provided by the gaming industry.

Nevada is the oldest and largest legalized gaming center in the United States. Gaming was legalized in Nevada in 1931 in the middle of the Great Depression as a form of economic stimulant. The industry did not really begin to develop until after World War II. Since then, the Nevada gaming industry has survived the presence of organized crime, a U.S. Senate committee investigation, and the corresponding damage to its reputation.

***Agency Roles Have Shifted Extensively Over Time.*** The authority to license and collect taxes from gaming operations has shifted among governing bodies four times in Nevada. In 1931, the legislation gave the local county sheriff offices the authority to license and tax casinos. Soon the state moved in and assumed a role because of the threat of federal prohibition of casinos. Extensive federal investigations had exposed extensive organized

crime influence in the casinos. Local governments still exercise a concurrent right with the state over gaming regulation.

The first state agency to take responsibility was the State Tax Commission, which in 1945 was granted the authority to license and tax gaming operations. After that, the Nevada Gaming Control Act created the State Gaming Control Board in 1955 and authorized it to become the enforcement and investigating unit of gaming matters for the Nevada Tax Commission. The Board was comprised of three members appointed by Nevada's governor.

In 1959, the Nevada Tax Commission was relieved of its regulatory duties over the gaming industry by the creation of the State Gaming Commission. The five-member Commission was formed with officials appointed by the Governor for a four year term. Licensing and policy decisions comprised the bounds of authority for the Commission. In 1971, legislation expanded the duties of the State Gaming Control Board to include gaming tax collection and administrative responsibilities for the Gaming Commission.

Local governments have concurrent authority to license and regulate gaming. Both jurisdictions must approve a casino license. However, local governments seem to perceive licensing as primarily a method of taxation, and rarely utilize their powers in a regulatory fashion. A local government can prohibit or restrict gaming within its city or county limits. In the Las Vegas area, casino gaming generally is limited to areas designated as "gaming enterprise districts." Each district is established by the local government having jurisdiction over the area.

***Nevada Gaming Was Linked With Organized Crime.*** Although there are many examples of past criminal involvement in Nevada's gaming, one of the more egregious involves the famous mobster, Bugsy Siegel. Despite his reputation as a hoodlum and his history of gratuitous violence, he had no trouble getting a casino license.

Because the casinos were controlled by organized crime, enforcement was handled somewhat differently than now. If a dealer was found cheating, he or she was taken to a soundproof room to have their hands beat with a baseball bat.<sup>2</sup> Two robbers who pulled off the only successful armed robbery of a casino, until recently, were later found shot to death in Los Angeles.

The state's reputation improved with the creation of the Nevada Gaming Commission and the State Gaming Control Board. The state's image received another boost when Howard Hughes began purchasing casinos. Although he was eccentric, Howard Hughes was clearly not an organized crime figure. Nevada had reached the point where a billionaire who wore empty Kleenex boxes for slippers improved the image of the state's gaming industry. (That fact was not widely known at the time.) Big publicly-owned companies such as Hilton and Ramada followed Howard Hughes' investments.

The toughened regulatory system and the addition of respected companies and individuals eliminated the threat of federal intervention and contributed to the growth and

respectability the industry enjoys today. Gaming in Nevada, and especially Las Vegas, has become a multibillion dollar industry that attracts millions of people each year.

***Nevada Has Two Entities That Regulate Gaming.***

- The State Gaming Control Board has evolved into the primary administrative arm for casino gaming regulation. The Board has responsibility for handling investigations for licensing, collecting taxes, and enforcing gaming regulations. The State Gaming Control Board is composed of three members, one of which must be a CPA, one of which must have experience in law enforcement, and one of which must have experience in business administration or management. Board members are appointed by the Governor for staggered four-year terms and are expected to serve full-time. The Gaming Control Board oversees the granting of licenses. The Board serves as the prosecutor in disputes.
- The State Gaming Commission remains Nevada's decision-making body on gaming policy and regulations. The Gaming Commission issues, denies, restricts, limits, suspends, or revokes gaming licenses. The Commission is composed of five members, also appointed by the Governor, who serve part-time. The Gaming Commission also handles disciplinary proceedings.

***There are Two Different Types of Gaming Licenses Issued by the Nevada Gaming Commission.***

- Restricted licenses prohibit the operation of more than 15 slot machines and do not allow the licensee to operate any other type of game. Holders of these licenses are generally owners of small bars, restaurants, and grocery stores. Only a routine investigation is required for restricted licenses.
- Unrestricted licenses allow the operation of any number of slot machines, gaming devices, or table games. A thorough investigation is conducted by the Gaming Control Board, who refers its licensing recommendations to the Gaming Commission. The Gaming Commission makes the final decision on an application for a gaming license.

***Licensing is More Thorough and Intrusive Than the Highest U.S. Security Clearance Investigation.***<sup>3</sup> An applicant must pay approximately \$500,000 to \$1 million to cover the state's costs. The state takes approximately one year to complete the process and issue a license. There are two public hearings where every personal and business transgression is subject to inquiry. The State Gaming Control Board provides a recommendation on licensing to the Commission.

The basic criterion for licensing is the applicant's character. An applicant is unsuitable if they are an organized crime figure, a case that can be hard to prove. A criminal record is neither necessary nor sufficient for denial of a license. There are a number of additional criteria:

- **Financing of the Operation.** The state wants to make sure that the money is not coming from criminal enterprise, but from a legitimate source. Another concern is that of viability of the casino. Moreover, there is the concern that a troubled operation may cheat customers and not pay taxes. This portion of the licensing law was passed when Las Vegas hotels were not doing well financially.
- **Business Competency.** To protect the state's revenues and consumers, the state wants the casino operator to be sophisticated enough to deal with very skilled cheaters. Cheaters not only steal from the casinos, but also cheat the state out of tax revenues, and possibly other patrons.
- **Suitability of Location.** The state does not want casinos near activities that are not suitable such as schools or brothels. (Nearby brothels present a negative image of gaming, especially to out-of-state visitors who are not used to such businesses being legal.)
- **Multiple Licenses Criteria.** This criterion was passed shortly after Howard Hughes acquired his extensive holdings. At the time, the U.S. Justice Department had threatened to intervene if Hughes bought more properties.

Besides the casino license, a number of employees are required to have licenses. Nevada's requirements are not as extensive as New Jersey's were. However, the type of positions that are required to have a license has spread as organized crime figures have been found in ancillary positions.

*Nevada Law Permits a Wide Variety of Gaming.* The currently permitted games include faro, monte, roulette, keno, bongo, fan-tan, blackjack, seven-and-a-half, big injun, klondike, craps, poker, chuck-a-luck, Chinese chuck-a-luck (dai shu), wheel of fortune, chemin de fer, baccarat, pai gow, pai gow poker, red dog, beat the banker, pyramid dice, panguingui, and sports book (except on teams from Nevada). Raffle type lotteries are not permitted.

### *Gaming Tax Structure*

Non-restricted gaming locations (those with more than 15 slot machines) pay monthly taxes on a sliding scale that goes from 3% to 6.25%. There is also a 10% tax on admissions, merchandise, refreshments, and services provided by any gaming establishment in connection with any form of spectator or participatory entertainment. There are also quarterly and annual fees assessed according to the number of table games offered.

### *Gaming Regulation in New Jersey*

New Jersey's regulatory situation is different from Nevada's. Casinos were legalized somewhat later and the state already allowed a variety of other types of gambling. In addition, New Jersey had a long history of problems with organized crime, so there was a

special concern about keeping their gambling clean. The state wanted to avoid the perception that many people had of Nevada gaming regulation. Nevada's regulators were seen as being a captive of the industry.<sup>4</sup> New Jersey wanted the industry and workers to meet standards of behavior that were exemplary.<sup>5</sup>

New Jersey was successful in following the strategy they laid out, but at a cost. Eventually, the state significantly eased gaming regulation, allowing casinos to advertise more aggressively, reduce labor costs by eliminating some mandated functions, and offer new games. The result was increased profits for the casinos.

***New Jersey Also Has a Two-Agency Structure.*** The state role is divided into an investigating office under the Attorney General and a license, rulemaking, and quasi adjudicative function. The general structure is modeled after Nevada.

- The Casino Control Commission is responsible for licensing casinos, employees and the firms that do business with them. The commission consists of five members appointed by the Governor for a term of five years. No more than three members may be from the same political party. The Casino Control Commission (CCC) is a quasi judicial agency in the Department of Treasury. The commission has its own staff. The CCC is funded from license application fees, slot machine taxes and licenses, and permitting fees. The objective of this funding mechanism is to protect the agency from politics by not requiring a legislative appropriation to fund the agency. The criticism that results, however, is that the agency is dependent on the industry through its fees.
- The Division of Gaming Enforcement is a branch of the Attorney General's Office. The division is responsible for investigating all license applications and prosecuting violations before the Commission.

The two-agency arrangement that both Nevada and New Jersey have is valued in these states because they act as a check over the regulatory process. A disadvantage is that conflicts occur between the two agencies. In Nevada, the commission has questioned the staff of the board and the board staff has resented the commission for ignoring their judgment.<sup>6</sup>

Members and employees of both New Jersey agencies are subject to strict post-employment restrictions. The goal is to eliminate or at least reduce the possibility of a revolving door between the industry and the regulators.

New Jersey also has a lottery that is regulated through the Department of Treasury. Parimutuel gambling is regulated by the Racing Commission in the Department of Law and Public Safety.

***New Jersey Wanted to Avoid Dependence on Gambling Revenues.*** While Nevada and New Jersey both have an agency system of casino regulation, there are many subtle differences. New Jersey was concerned that the gaming industry could capture the state's

regulatory process if the state relied too heavily on gaming revenues. The state was also concerned about political participation by gambling interests. As a result, the state banned political contributions by gaming interests.

Historically, casinos are regulated much more strictly and rigidly in New Jersey than in Nevada.<sup>7</sup> The state viewed regulation of gaming as a difficult problem. As noted earlier, casinos have large amounts of cash that is uncounted and unrecorded as the gambling takes place, making skimming and money laundering quite easy. To limit such problems, New Jersey has specified control systems that are an important part of licensing and regulation. Nevada does not follow that model. Part of New Jersey's regulatory regime includes strict restrictions that prevent individuals from being hired very quickly. Licensing takes a long time which hinders the job market. Observers have characterized it as inflexible.<sup>8</sup> Because of the delays, job applicants often seek employment elsewhere rather than wait for a license.

***New Jersey Has Proportionately a Much Larger Regulatory Structure.*** New Jersey's regulating agencies have 1,100 employees and a \$60 million budget while Nevada has 392 employees and an \$18 million budget. New Jersey has a significantly smaller industry, about \$37 billion handle versus \$107 billion handle in Nevada. New Jersey's regulatory costs are paid by charging fees, while Nevada's are paid from the general fund. The result is a system that critics say has no efficiency incentives. Casinos are just billed for the costs of regulation.

***New Jersey Has Recently Evaluated Gambling in the State.*** In the mid-1980s, a Governor's Advisory Committee on Gambling was established with 19 members whose job was to examine the interrelationship between the state's various forms of gambling and their regulation. The state was concerned that there was duplication and overlap of the different regulatory agencies that oversaw each of the legal forms of gaming in the state. The Commission was also to address:

- gambling as a public policy,
- compulsive gambling,
- economic impact, and
- criminal activity.

Some of the committee's findings will be discussed in the respective sections that deal with these issues.

### ***Recent Regulatory Issues***

New Jersey recently relaxed its regulatory stance. The licensing system for employees in particular was loosened.

New Jersey has had hearings on the issue of credit. Casinos can loan money to gamblers. These loans can become a way to skim or launder money. Skimming is diverting money away from the normal controls and books. Loans can be deliberately made to a debtor

who knows that he or she does not have to repay the loan. The casino can write off the loan, the debtor gives the money back to the casino minus a reward for collusion, the loan is charged off as an uncollectable debt, and the amount of the loan has just been skimmed and is not subject to taxes. Loans in amounts as high as almost \$5 million were being made to organized crime figures.

Another related issue is that the casinos were fostering a debt problem by loaning far more than people could pay back. A supermarket clerk making \$18,000 annually and no other significant assets was granted a loan of \$300,000 from a casino. The result of the hearings was a tightening of regulations on loans to gamblers.

The New Jersey Legislature has considered taking action that would stave off competition from neighboring states. The state faces the threat of gaming in Philadelphia, New York City, and the Catskills. A bill was considered, but not enacted that would authorize New Jersey riverboats only if neighboring states authorize riverboats. Under the legislation, riverboat ownership would be limited to the companies operating in Atlantic City. The vessels would be subject to local option and each company would be permitted to own and operate up to three vessels. Governor Whitman criticized the bill, saying that she did not want to expand gaming in the state, but would rather make Atlantic City a more attractive and accessible place.

### ***Gaming Tax Structure***

Atlantic City casinos pay taxes to two different funds. One, the Casino Revenue Fund, is a traditional special fund that supports regulation and other state purposes. The other is the Casino Reinvestment and Development Authority. This fund was established to assist urban redevelopment in the state. Gaming was originally approved to help redevelop Atlantic City. Each casino must contribute 8% of gross revenue to the Casino Revenue Fund and another 1.25% of gross revenues to the Casino Reinvestment and Development Authority.

### ***Other States***

Following is a brief discussion of gaming in other states that have casino and/or cardroom gaming.

#### ***Colorado***

##### **Authorized Gaming**

In 1989, limited stakes gaming was authorized to take place in the historic towns of Central City, Black Hawk, and Cripple Creek. Only blackjack, poker, and slot machines with a maximum single bet of five dollars is allowed.

##### **Regulatory Agency**

The Department of Revenue is the oversight agency for the Division of Gaming and the Colorado Limited Gaming Control Commission. The Division issues licenses and implements, regulates, and supervises the conduct of limited gaming.

The Governor appoints the five members of the commission who are subject to confirmation by the Senate. No more than three members may belong to the same political party and no more than one may be from the same congressional district. The commission must include a law enforcement officer, an attorney, a CPA or public accountant, a business person in a management-level position, and a registered voter who is not employed in a job similar to any of the other Commission members. All members except for the registered voter must have at least five years' experience in their profession. The members' terms are staggered. No member may serve more than two consecutive terms.

The commission is responsible for promulgating all rules and regulations related to gaming, establishing the gaming tax rate, delegating budgetary authority over the Division of Gaming, and allocating money to other state departments.

The commission establishes and collects fees from licensees, and adopts rules and regulations for overseeing gaming. The commission also enforces the rules and regulations. The commission also has a research responsibility and is required to conduct an ongoing investigation of limited gaming in Colorado.

### Tax Structure

The state levies a tax of up to 18 percent depending on the size of the operations. In addition to the tax on revenues, the state levies an annual tax on gaming devices and for licenses.

### *Illinois*

#### Authorized Gaming

Illinois moved to legalize riverboat gambling shortly after seeing the success of Iowa's riverboat gambling. Passage of the measure was helped by the fact that many Illinois residents journey to Iowa to use its casinos. The Illinois Riverboat Gambling Act was passed in January 1990, authorizing gaming to begin by April 1991.

The direct competition between Iowa and Illinois riverboats affected the law in Illinois. As originally proposed, Illinois was going to adopt the same limits on gambling as those in Iowa. When the bill was finally enacted, no wagering or loss limits were imposed in Illinois.

#### Regulatory Agency

The Illinois Gaming Board regulates riverboat gaming in Illinois. The board consists of five Governor-appointed and Senate-confirmed members. The Governor designates one of the Board members as chairman. The board members must have a "reasonable knowledge of the practice, procedure, and principles of gambling operations." The board must include an attorney, a certified public accountant, and a person experienced in law enforcement. Each Board member must post a \$25,000 bond, while earning \$300 for each day of hearings or meetings. Board members serve staggered three-year terms.

The board hires its own staff. Agents of the board must be aboard the riverboats whenever gambling is taking place to certify revenue, conduct investigations, and listen to patron's complaints. Agents are supplied by the Department of Revenue and the Department of State Police.

The board issues licenses, conducts hearings on civil violations, collects fees and taxes, assesses fines and penalties, and sets rules and regulations. The board can suspend, revoke, or restrict licenses, and impose fines for violations of the act or the board rules.

Initially, the board has received about 35 percent of its funding from the general fund. This is in response to the significant start-up costs. In the future, the board will be completely funded by the State Gaming Fund with plans to transfer any surplus to the Educational Assistance Fund.

### Tax Structure

The state imposes a tax of \$2.00 per passenger and a 20% tax on adjusted gross receipts.

## ***Indiana***

### Authorized Gaming

Indiana is one of the more recent entrants to riverboat gaming. Up to 11 licenses may be issued in counties contiguous to the Ohio River, Patoka Lake, and Lake Michigan.

### Regulatory Agency

The Indiana Gaming Commission is in the executive branch and reports to the Governor. There are seven commissioners appointed by the Governor to serve staggered three-year terms. At least one member must have a background in law enforcement and criminal investigation, one must be a CPA with auditing experience, and one must be a lawyer in Indiana. Three of the members must be from a county contiguous to Lake Michigan, three from counties contiguous to the Ohio River, and the other must be from another county. No more than four can be from the same political party. The Indiana State Police are also involved because they conduct the background investigations for license applicants.

### Tax Structure

The commission will collect a \$3 per head admissions tax from each of the boats, payable on a daily basis. There is also a 20% state tax on the adjusted gross revenues.

## *Iowa*

### Authorized Gaming

In 1989, the Iowa Legislature legalized casino gambling aboard historical river excursion boats that could ply the Mississippi River, the Missouri River, and other waterways located within Iowa. The Legislature also created the Iowa Racing and Gaming Commission. Previously, the Commission was known as the Iowa Racing Commission, and was responsible for the regulation of the parimutuel industry that included three greyhound tracks and one horse track.

### Regulatory Agency

The Iowa Racing and Gaming Commission oversees parimutuel wagering and riverboat gaming. It is composed of five members appointed by the Governor and confirmed by the Senate. The term of office is three years. Iowa's Governor appoints the members based on requirements for representation by region, political party, and gender. Iowa requires county-wide referenda to approve the docking of riverboats.

The commission is part of another state agency called the Department of Inspection and Appeals. The Department reports directly to the Governor.

Iowa borrowed concepts from both New Jersey and Nevada. The Nevada model was regarded as more lenient while the New Jersey model was seen by some as guaranteeing full employment of regulators.<sup>9</sup> Since the statute requires that the cost of regulation be assessed in addition to the taxes, the New Jersey model in total was not feasible for Iowa. The cost of regulation combined with the high taxes and gaming restrictions would have been too costly for the type of casino operations allowed within the state. The state turned its focus on strict regulation in key areas such as cash control, security, and surveillance. An on-line slot machine data system was also required.

Although the state thought a balance was struck between regulation and cost effectiveness, the cost of regulation was still considered oppressive by the riverboat casino operators. The cost of regulation was increased significantly because of the decision to place relatively high-priced state police agents aboard each cruise.

### Tax Structure

There is an annual license fee equivalent to \$5 per person based on the capacity of the vessel, including the crew. There is a state head tax of \$0.50 per passenger, not to exceed \$250,000 per vessel and an optional matching local tax of \$0.50 per passenger. Gaming revenue is taxed on a graduated scale of 5% on the first \$1 million of revenue, 10% on the next \$2 million and 20% on any revenue above three million.

## *Louisiana*

### Authorized Gaming

Louisiana law now allows horse racing, a statewide lottery, video poker machines, and riverboat gambling. In 1992, a law was enacted that authorized a single, land-based casino in New Orleans. Before that, the Indian Gaming Commission had been created. At least one tribe plans to open a casino/resort complex in Louisiana. Others are expected to follow.

A casino may offer most types of games played for money or property except lottery, bingo, charitable games, raffles, electronic video bingo, pull tabs, cable television bingo, wagering on dog races, or wagering on any type of sports event.

### Regulatory Agencies

Louisiana started with a multitude of gambling regulatory agencies. The Gaming Enforcement Division of the Office of State Police regulated video poker and riverboat gaming. It is part of a larger department which also includes the Riverboat Gaming Commission. The Louisiana Economic Development and Gaming Commission regulated Louisiana's land-based casinos. All of these agencies report to the Governor.

Partly in response to the troubles in the industry, Louisiana overhauled their regulatory agencies. In the spring of 1996, a new Gaming Control Board was created to oversee riverboat, video poker, casino and Indian gaming. The governor appoints the nine-member board. He is required to obtain recommendations from different universities in the state. Some of the appointments have certain geographic, educational, or professional criteria.

The Board is nominally under the Department of Public Safety. Louisiana has a ceiling on the number of State Departments. Since the ceiling had been reached, the Gaming Control Board had to be placed within an existing department, but it functions as an independent agency. The State Police also have a role in enforcement and licensing.

The riverboat gaming legislation provides for 15 riverboat casino licenses. Licenses are granted for an initial five-year term, followed by annual renewals. There are also limitations on the amount of space dedicated to gambling, no more than 30,000 square feet on any vessel may be used for gaming activities. Riverboat gaming may only take place on certain waterways.

The land-based casino legislation permits a single facility at the Rivergate Convention Center site in downtown New Orleans. A temporary facility, to be operational while the permanent facility is under construction, is also permitted. The license was awarded to a group spearheaded by Harrah's. All games using cards, dice or mechanical or electronic devices are permitted, as is wagering on race horses. Lotteries, bingo, pull tabs, dog race wagering, and sports betting are not permitted.

A number of regulatory and legislative changes have occurred recently. The Riverboat Gaming Commission voted to permit free access to gaming vessels while they are at dockside, thus eliminating the phenomenon of phantom cruises. (These are cruises which do not go anywhere, but just allow the boat to leave the dock and meet the legal requirement of being on a cruise.)

### Tax Structure

The land-based casino will pay 18.5% of gaming revenues or \$100 million to the state per year, whichever is greater.

Gaming vessels are assessed a 3.5% license fee of net gaming proceeds and a 15% franchise fee each year, plus a flat fee of \$50,000 per vessel in the first year of a vessel's operation and \$100,000 per vessel every year of the life of the vessel after that. Localities also have the option of imposing a \$2.50 per head boarding fee.

## *Mississippi*

### Authorized Gaming

Following the examples of Iowa and Illinois, the Mississippi Legislature authorized gaming on boats on the Mississippi River and its navigable tributaries. Gaming was also authorized in Oxbow Lakes bordering the river, in the waters of the Mississippi Sound, and off of the three Mississippi Gulf Coast counties. The effective date of the law was April 1, 1990. If a city or county does not want the gaming boat to dock in its ports, a petition signed by 20% or 1,500 of the registered voters may force a vote on the issue.

All forms of gaming are authorized. New games can be approved by the Mississippi Gaming Commission. Charitable bingo is also authorized under Mississippi law, and regulated by the Commission.

Gaming is not automatically legal in each of these counties. An applicant must file a notice of intent with the Commission. If no petition is filed with the County Board of Supervisors within 30 days of the last date of publication, the Board of Supervisors must adopt a resolution saying that legal gaming may be conducted in that county. If 20% or 1,500, whichever is less, of the registered voters in the county file a petition with the County Board of Supervisors within the 30-day period, an election on the issue must be held generally within 30 to 60 days after certification of the number of registered voters signing the petitions. The gaming authorities may deny a license for any location deemed unsuitable because of its proximity to a residential area, church, school, hospital, or playground, or because the location is difficult to police.

### Regulatory Agency

The Mississippi Gaming Commission, which took over the task of regulating the gaming industry from the State Tax Commission in October 1993, is composed of three

members, each serving staggered four-year terms. Members may serve no more than two terms and at least one member must have been a resident of a state that permits gaming activity for five years. Commissioners serve without pay. The Governor appoints the commissioners subject to the advice and consent of the Mississippi Senate.

The Commission is responsible for licensing, administering discipline to licensees, and adopting regulations. A full-time executive director administers the gaming laws and regulations, and makes recommendations on licensing and other matters to the Commission. The Attorney General must approve the appointment of all legal staff.

The Commission adopts rules and regulations consistent with the gaming laws. Among other subjects, the rules may provide for the;

- forms and procedures used to apply for licenses,
- procedures for all hearings,
- payment of investigative costs of applicants,
- permitted games (the statute prohibits non-banking games and wagers on athletic events, but authorizes sports pools and horse race wagering),
- the size of the gaming area on a ship or vessel, and
- procedures for issuing credit and collecting debt.

The law permits gaming only by players who are present in the casino. Players must be at least 21 years old.

Local governments cannot issue licenses, and have limited ability to regulate gaming. The Mississippi Attorney General has issued an opinion stating that a local government can adopt zoning ordinances restricting gaming to certain areas within its city or county limits. However, a local government may not prohibit gaming completely.

### Tax Structure

Persons boarding the boats must pay a \$3.50 fee. The fee is divided between the state government (60%), the county (20%), and the city (20%).

Mississippi gaming establishments are required to pay a monthly sliding tax of 4% on the first \$50,000 of gaming revenue, of 6% on the next \$84,000 and 8% on revenue over \$134,000. Local jurisdictions may opt to impose a local gaming tax of one-tenth of the state fee and a per-passenger boarding tax, or a single tax of up to 3.2% of gross revenues.

### *Missouri*

### Authorized Gaming

Although Missouri has recently approved legal gaming, legal disputes are slowing the growth of the industry. Riverboat gaming was approved by legislation and enacted in 1995.

#### Regulatory Agency

The legislation established the Missouri Gaming Commission. The commission assumed the responsibilities of the Missouri Horse Racing Commission. Although horse racing is legal in Missouri, there are not any horse tracks. The commission is composed of five members serving no more than two staggered three-year terms. The commissioners are appointed by the Governor and confirmed by the Senate.

#### Tax Structure

The state collects a \$2 per head admissions tax and a 20% tax on adjusted gross revenues.

### ***South Dakota***

#### Authorized Gaming

The South Dakota Limited Gaming Law authorized slot machines, poker, and blackjack in the City of Deadwood. It was subject to a 60% voter approval later received from the residents of Deadwood. Deadwood is an historic town with a long history of illegal gambling and prostitution that continued without significant government interference into the middle of this century.

Eventually, the historical town deteriorated. Town leaders pushed for legal gaming to save the town. They sponsored a statewide petition to place a proposition on the ballot that was approved. Gaming began in November 1989.

#### Regulatory Agency

The state regulates gaming through the South Dakota Commission on Gaming. The Commission consists of five members appointed by the Governor. Members have staggered three-year terms. The Commission members cannot all be members of the same political party.

The Commission appoints an Executive Secretary to conduct administrative matters. The Executive Secretary, who serves at the pleasure of the Commission, employs a staff to administer the gaming laws.

No Commission member may be a license holder or a resident of Lawrence County (where Deadwood is located). The Commission members may not receive anything of value from a licensee or their officers and employees. Commission members cannot gamble in Deadwood.

The Commission can (a) adopt regulations, (b) issue licenses, (c) oversee and define gaming contracts of licensees, (d) inspect and examine gaming premises and places where gaming devices are located, sold, distributed, or stored, (e) seize and examine gaming equipment or supplies, (f) require verification of licensee's or applicant's income, (g) contract for legal counsel, (h) suspend or revoke for cause any gaming license, (i) require applicants to disclose pecuniary interest in the applicant by any person, (j) carry out duties as may be imposed by the state because of a contract entered under authority of the Federal Indian Gaming Regulatory Act, (k) establish application fees, (l) fix the gaming tax after June 30, 1990, within the parameters set by law, and (m) pay expenditures.

The Commission and Executive Secretary also can investigate conduct of licensees or employees to help enforce the law and to ensure unqualified or unsuitable persons are not involved in gaming. The Commission may review any action taken by the Executive Secretary.

The Executive Secretary prescribes gaming tax return forms, and may grant limited extensions in which to report and remit taxes. The Executive Secretary can grant or deny support licenses. The South Dakota Attorney General may exercise any authority of inspection or examination allowed by the Gaming Control Act. The Attorney General also may apply to the court to enforce the Gaming Control Act or any gaming rule.

### Tax Structure

There is an annual fee of \$2,000 for every card game or slot machine. In addition, 8% percent of the gross revenues must be paid to the state.

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## ***VII. Why do People Gamble?***

Earlier sections of this report presented data on the growing popularity of gambling nationally, as well as in California. Given the popularity of gambling, this raises an obvious question: "Why do people gamble?" What is the major motivation for engaging in this activity? And why do some people gamble more than others and who are these people? Why do people gamble when it isn't a sure path to riches? As one researcher noted:<sup>1</sup>

"Yet the fact that empirical evidence strongly indicates that the best way of finishing up with a small fortune as a result of gambling is to start with a large fortune is played down."

Gambling is defined by the Webster's New World Dictionary as the following:

- to play games of chance for money or some other stake, or
- to take a risk in order to gain some advantage.

***Various Theories Exist on Why People Gamble.*** There is a debate over whether the motivation to gamble is positive or negative. A common view is that gambling is negative. In particular, this view is common among religious groups.<sup>2</sup> Others argue that the motivation is positive, that people enjoy gambling and it is usually a harmless diversion. Because people enjoy it they continue to gamble in spite of losing.<sup>3</sup>

Any discussion of the motivation of gambling usually starts with the natural comparison to life. Life is a gamble. Everyday, people are faced with situations which involve risk and chance.

Gambling activities are extensions of the risk and chance in life. The activity of gambling becomes play, it becomes a game. Gambling allows the person the choice of engaging in the activity, the amount of risk and, in many cases, the stakes. The stakes are a necessary element for many people. It turns the bet into not just an opinion but a commitment.

The concept of gambling mimicking the risk and chance of life has a parallel in the history section of this report. As noted in that portion, gambling was a popular activity during the gold mining era. Mining was a high-risk enterprise that required constant gambles by the participants. Considering that the people who accepted risk were drawn to mining, it is not surprising that gambling would become a popular leisure activity.

The fact that recreational gambling mimics life does not really help us determine why people gamble. If risk and chance are integral parts of life, why do some people seek out gambling activities and why are others content without it? Researchers have attempted to answer this question, but thus far no definitive answer has been found, but plenty of articles have been published.

Another way to determine why people gamble is to ask them. Why do people say they gamble? In a survey in Washington, those sampled reported that they gambled for fun, to win money, or they were looking for excitement and a challenge.<sup>4</sup>

Modern theories of gambling motivation are quite a change from some earlier theories. Early social scientists theorized that gambling was a way to deal with the pressures of industrialization. Karl Marx grouped it with religion as an opiate for the masses. Psychoanalysts had a different view. Sigmund Freud analyzed Fyodor Dostoyevsky's heavy gambling and diagnosed him as punishing himself for his oedipal urges.<sup>5</sup>

Different groups are more inclined to gamble than others. A review of several studies on demographic factors which relate to gambling behavior helps answer the question of who gambles the most. The following represents a synopsis of some of the research findings.<sup>6</sup>

- **Gender.** Men and women tend to have different preferences in their gambling. Men are more likely to gamble in games such as blackjack and lotteries and women are more likely to engage in bingo and raffles.
- **Age.** There is a negative relationship between the two. That is, the older one becomes, the less likely she or he is to gamble.
- **Social Class.** There have been mixed results, with gambling behavior found to be related to social class in some studies and not related in others.
- **Marital Status.** Single, divorced, and separated people were found to be more likely to gamble than married people.
- **Community Size.** Studies have found community size to be positively related to gambling propensity, meaning that residents of big cities gamble more.
- **Religion.** Catholics were found to be more likely to gamble than Protestants and other religious groups. Catholics were also found to be less likely to disapprove of gambling than other religious groups.

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### ***VIII. Why do People Gamble Too Much?--Pathological and Problem Gambling***

To many people, gambling is a simple form of entertainment. But to some others, it becomes an uncontrollable behavior. Many terms are used to describe a person who has a problem with gambling, including pathological gambler, gambling addict, compulsive gambler, or problem gambler. All of these terms are used to describe a person for whom gambling has become more than an innocent diversion.

Some of these terms lack specific meaning. This report will follow the literature and use "problem gambling" to mean an umbrella term to describe a situation where gambling activity disrupts one's life, but the extent of the disruption is not defined. Problem gambling includes pathological gambling, which is a more severe condition and is a term with specific medical meaning.

Pathological gambling is recognized as a medical disorder by the American Psychiatric Association and has elements of addiction similar to alcohol and drug addiction. It describes a gambler who loses control over gambling behavior with damaging personal, social and financial effects. Very often, the pathological gambler suffers from legal problems. Because the gambler is losing control it is referred to by mental health practitioners as an impulse disorder. Pathological gambling is a progressive disease, meaning that the symptoms will get worse over time. Mental health professionals see it as a complex disease often seen in conjunction with other disorders including depression and chemical dependency.

***Graphic Stories Exist of Those Whose Lives Were Destroyed by Pathological Gambling.*** The media readily tells the tales of those whose lives were destroyed by their uncontrollable gambling. These are some stories that have been pulled from press clippings:<sup>1</sup>

- A 40 year old Illinois woman gambled away her family's savings and her wedding ring on a riverboat casino. When she found out that the sheriff was on his way to evict her and her family for missing 17 consecutive mortgage payments, she drove to a mall parking lot and shot herself. She left a husband who did not even know that his wife gambled, let alone had a gambling problem.
- Jason Berg killed himself after running up a huge gambling loss. He left a suicide note which simply read, "I'm out of control." He was 19 years old.
- Cuong Thu Cam fatally shot two friends and later committed suicide. He was despondent over his gambling debts and owed as much as \$200,000.
- A bank robbery occurred in San Jose. The robber was found within a couple of hours waiting for a seat at the gaming table inside a club.
- In Oregon, a County Commissioner was recalled in 1995 after pleading guilty to embezzling county funds to fuel his compulsive gambling.
- For those who have forgotten, probably the best-known pathological gambler is Pete Rose. A record-breaking hall of fame player was banned from the game he loved for life because of his gambling problems.

Tragic examples such as these receive an enormous amount of publicity and are often used by anti-gambling groups to fight the spread of legalized gambling. Industry observers credit attention from these stories as blocking laws that would have relaxed betting limit regulations in Missouri.<sup>2</sup>

Describing the behavior is much simpler than explaining why the problem gambler persists in behavior which is so damaging.<sup>3</sup> There are several models that are used to describe the problem gamblers.

Mental-health professionals prefer the term "pathological gambling" because it stresses the disease aspect of the issue. Pathological gambling is a progressive and chronic disorder that is clearly distinguished from social gambling. Psychiatrist Richard J. Rosenthal, who has written the official medical definition, defines it as:

"a progressive disorder characterized by a continuous or periodic loss of control over gambling; a preoccupation with gambling and with obtaining money with which to gamble; irrational thinking; and a continuation of the behavior despite adverse consequences."<sup>4</sup>

The results can be quite devastating. The disorder is incapacitating. The pathological gambler is unable to maintain solvency or provide basic support for themselves or their family. Further, as noted in the American Psychiatric Association description of the condition, "When the individual's borrowing resources are strained, the person may resort to antisocial behavior to obtain money."<sup>5</sup> That is a vague medical term for theft, embezzlement, fraud, and other crime. A significant percentage of pathological gamblers have a second addiction to drugs or alcohol.

***Pathological Gambling Recognized as a Medical Problem.*** In 1980, the American Psychological Association included pathological gambling in their Diagnostic and Statistical Manual of Mental Disorders, Third Edition (DSM-III). By including pathological gambling, it gave official medical recognition as a disease. Pathological gambling is also identified as a disease by the World Health Organization.

Since 1980, the definition of pathological gambling has undergone some major changes. At first, the emphasis was on the damage and disruption caused by the disease. The motive was of little importance. Subsequent versions have changed this description and revised the diagnostic criteria for pathological gambling, emphasizing the addictive nature of the disease. It mentions issues concerning tolerance and withdrawal, suggesting a physiological basis for the disorder. In the case of the pathological gambler, tolerance refers to their increasing need for gambling and usually gambling with greater risks to get the same emotional effect. As with chemical dependency, withdrawal refers to the pain and discomfort associated with not practicing the behavior.

According to the latest version of the manual, DSM-IV, a person who exhibits at least five of the following behaviors may be a pathological gambler.<sup>6</sup>

- Preoccupation with gambling (e.g., preoccupied with reliving past gambling experiences, handicapping or planning the next venture, or thinking of ways to get money with which to gamble).
- Needs to gamble with increasing amounts of money in order to achieve the desired excitement.
- Repeated unsuccessful efforts to control, cut back or stop gambling.
- Restlessness or irritability when attempting to cut down or stop gambling.
- Gambles as a way of escaping from problems or of relieving dysphoric mood (e.g., feelings of helplessness, guilt, anxiety, or depression).
- After losing money gambling, often returns another day in order to get even ("chasing" one's losses).
- Lies to family members, therapists or others to conceal the extent of involvement with gambling.

- Has committed illegal acts such as forgery, fraud, theft or embezzlement, in order to finance gambling.
- Has jeopardized or lost a significant relationship, job, or educational or career opportunity because of gambling.
- Reliance on others to provide money to relieve a desperate financial situation caused by gambling.

Researchers consider pathological gambling an invisible problem with symptoms that are hard to distinguish from non-pathological gambling.<sup>7</sup> This contrasts with drug or alcohol addiction where there are obvious symptoms of intoxication. Further, individual cases will vary greatly.<sup>8</sup>

***Who is Most at Risk For Becoming a Pathological Gambler?*** Research has shown that there are factors that increase the risk of being a pathological gambler. Surveys of pathological gamblers show a greater proportion of:<sup>9</sup>

- males,
- children of pathological gamblers,
- people with the attitude that money causes and is also the solution to all their problems,
- individuals with a poor education,
- single persons, and
- individuals whose household income is below the mean.

These findings are from prevalence surveys, not from studies of who is in treatment. White middle-aged males are the pathological gamblers most likely to end up in treatment.<sup>10</sup>

Researchers have been less successful in determining what causes problem gambling and what the differences are between problem and normal gamblers. There are many people who have a variety of risk factors but don't become problem gamblers.

***Studies Indicate That There is a One to Five Percent Incidence of Problem Gambling in the Adult Population.***<sup>11</sup> Specifically, the studies usually show the following results:

- Over their lifetime, about 1 to 5 percent of the population are problem gamblers. This includes individuals who are currently experiencing problems as well as those who may have experienced problems in the past.
- A subset of the problem gamblers, a group that may be as large as one to three percent of the total population, are pathological gamblers. This figure is from the DSM-IV, the most recent encyclopedia of mental illnesses, but there is some dispute over the actual level.

These incidence figures are surveys for the adult population as a whole. The rate of compulsive gambling among teens may be higher, reaching seven to eleven percent.<sup>12</sup>

One of the most comprehensive research projects on compulsive gambling prevalence was conducted by Rachel A. Volberg with funding by the National Institute of Mental Health.<sup>13</sup> In this study, randomly selected individuals in five states were interviewed by telephone, using a survey instrument that detects pathological gamblers. California was one of the five states surveyed. There have been surveys of other states.

### Prevalence over Lifetime

	Total	Problem Only	Pathological
California, 1990	4.1	2.9	1.2
Average of 13 States	3.9	2.5	1.3

### Current Gambling Problems

	Total	Problem Only	Pathological
Average of 6 States	2	1.3	.7

**Controversy Exists Over the Accuracy of the Surveys.** The survey instrument used is the South Oaks Gambling Screen (SOGS). This survey instrument is a twenty-item scale that was derived from the diagnostic criteria for pathological gamblers published in DSM-III.<sup>14</sup> Critics of the SOGS say that the instrument is too broad and vague, and it overstates the persuasiveness of the problem.<sup>15</sup> They point out that one incident of an argument with a spouse and some remorse over losses from exceeding gambling limits can lead to a positive result on the screen. The potential for false positives may be increased because gambling may be more likely to lead to occasional problem elements by normal individuals.<sup>16</sup> In other words, there may be some low or occasional incidence of distress that cannot truly be considered problem or pathological, but does result in a positive score according to the test.

Another criticism is that the screen doesn't accurately detect problem gambling in the young. The screen was developed from response and behavioral patterns of adult pathological gamblers. There is also a concern that it based on the criteria in the DSM-III, not the DSM-IV. Those that use the screen retort that it is accurate for many different groups.<sup>17</sup> The screen is in the process of being updated to the new DSM-IV definitions.

Some critics argue, however, that the screen doesn't detect enough problem gamblers. Some observers are concerned that researchers can't realistically conduct phone surveys of problem gamblers. They point out that problem gamblers are at the clubs or afraid to answer the phone because the gamblers don't want to talk to somebody they owe money.<sup>18</sup> Another point of interest is that there is a large rate, 27 percent in the California study, of people who refuse to answer a telephone survey. That is similar to other telephone surveys regarding sensitive questions.<sup>19</sup>

***Controversy Exists Regarding Whether Prevalence Studies Suggest a Link Between Pathological Gambling and Legal Gaming.*** Results of the Volberg study suggest that problem gambling is a greater problem in those states where legal wagering has been available for some time.<sup>20</sup> This conclusion is arrived at by comparing rates in different states. Drawing conclusions from comparisons of one state over time or a cross-sectional study of multiple states is difficult. Such comparisons are based only on the prevalence rates and not by looking at population differences that could explain the different rates.

Another way that prevalence studies attempt to shed light on the same question is by conducting the studies over time. In South Dakota, prevalence studies show that despite the legalization of casinos, the prevalence did not change in a statistically significant way over time. A study in Iowa came to quite different conclusions. It showed a dramatic increase from 1.7 percent in 1989 to 5.4 percent in 1995.

Mental health professionals who treat pathological gamblers tend to believe that legalization leads to increased compulsive gambling.<sup>21</sup> The DSM specifically notes that the onset of pathological gambling can result from greater exposure to gambling.<sup>22</sup>

Counselors form this belief based on their experience and the nature of addiction. They tend to hold the view that some people may be predisposed to an addiction. If a person was predisposed to have a drinking problem, but never came into contact with alcohol, she or he would not become an alcoholic. The pathology of their predisposing factors may still cause some damage to them and others. They might also be some other kind of addict, but they would not be an alcoholic. In the same way, a person with a predisposition to problem gambling may not see it manifested until access to gambling becomes available. Another element of this is that legalization leads to greater acceptance of gambling and greater exposure for the average person.<sup>23</sup>

This behavioral pattern occurs because pathological gambling is a problem of impulse control. The more accessible gambling is, the harder it is to maintain the control. Despite the logic of this line of reasoning, there are no prevalence studies that prove the notion that expanded gambling will lead to increased problem gambling.

Another theory of problem gambling counselors is that electronic games such as slots and video lottery terminals are especially addictive.<sup>24</sup> They refer to these as the "crack cocaine of gambling," because of the low cost per wager and their rapid play.<sup>25</sup> This connection is disputed. Those disagreeing point to survey results from South Dakota. The

amount of video lottery sales in the state increased, but prevalence of gambling problems remained unchanged.<sup>26</sup>

Regardless of any possible links, legal gambling probably cannot be blamed for all pathological gambling. Research in Texas before the lottery began operating showed that a small percentage of Texas had gambling problems.<sup>27</sup> Conversely in Louisiana, a recent study showed a very high rate of gambling problems and that problem gamblers tended to spend more than those in other states.<sup>28</sup> Louisiana has a great deal of accessible legal gambling.

If gambling were prohibited, would problem gambling stop? Probably not. According to Jean Falzon, executive director of the National Council on Problem Gambling, "Problem gambling is going to exist despite the availability of legalized gambling or the lack thereof. Many problem and compulsive gamblers have problems with sports betting which is predominantly illegal in this country."<sup>29</sup>

***Social Costs in California Could Easily be \$5 Billion.*** The following table shows how the cost estimates are derived, and shows social costs that range from \$1 billion to \$10 billion. These are derived from cost estimates from other states and prevalence studies both from California and other states. It is not known with accuracy either the social costs or the actual number of problem gamblers. Hence, the table presents a range. The social costs per pathological gambler are in the low range as other studies have shown costs as high as \$50,000 to \$80,000 per gambler.

<b>Estimated Social Costs of Pathological Gaming in California</b>			
Percentage and Number of Pathological Gamblers		Cost Per Pathological Gambler	Total Cost
.5	105,000	\$8,000	\$844 Million
		\$15,000	\$1.6 Billion
1	210,000	\$8,000	\$1.7 Billion
		\$15,000	\$3.2 Billion
1.5	316,000	\$8,000	\$2.5 Billion
		\$15,000	\$4.8 Billion
3	633,235	\$8,000	\$5.0 Billion
		\$15,000	\$9.5 Billion

gambling are explained in more detail in the economics chapter.

The State of Florida estimated that crime and social costs attributable to casinos would total \$2 billion at a minimum. For California, with slightly over twice the population, the total would then exceed \$4 billion, a figure in line with the above estimates.

***Pathological Gamblers Play a Number of Different Games.*** Surveys have shown that some play a number of games. A study in a state with casinos showed that the majority of problem gamblers were having problems with non-casino gambling, including the state lottery.<sup>30</sup> The study also looked at the reasons that people called a help-line. Among these, a small majority said their problem was related to casino gambling. But, significant numbers said that their problem was lotteries or sports and race betting.

***There are Two Main Types of Pathological Gamblers.*** With so many different types of gambling opportunities, the course of the disease can be broken into two types:

- The Escape Gambler: This is the gambler who prefers slot machines, bingo, and lotteries. They are often female and are married to men who are addicts of some kind. They tend to be depressed and use gambling to numb themselves.
- The Action Gambler: These prefer cards, dice, racing, sports, and stocks or commodities. They are competitive and concerned about status. They see themselves exercising skill in their gambling. They are more likely to be male and gamble for much longer before seeking treatment than the escape gambler.

***Pathological Gambling and Gamblers Exist Outside of Gaming Establishments.*** One article points to Donald Trump and Robert Maxwell.<sup>31</sup> Both men were gambling that their empires would emerge unscathed from the challenges they faced. Both men gambled incorrectly as subsequent events have shown. They are identified because of the nature and size of the risks they took. Experts in pathological gambling point to some of the more notorious financial market trading scandals as evidence of pathological gambling outside of gaming establishments.<sup>32</sup>

***Resources for Treating Problem Gamblers Have Grown.*** Historically, problem gambling was regarded as an individual failing rather than as a medical or social problem.<sup>33</sup> As such, little treatment was available.

The original treatment for problem gamblers was Gamblers Anonymous. It is also known by the shorthand GA. GA was established in 1957 and until the 1970's, it was the only treatment program in the United States for problem gamblers. The program of Gamblers Anonymous is based upon Alcoholics Anonymous. AA is a spiritual program that uses twelve steps as a guide to help program participants recover from alcoholism and its effects. GA uses the same basic twelve steps for treating uncontrolled gambling. The program is supported entirely by member contributions. The only requirement for

membership is a desire to stop gambling. Like alcoholics, GA members attend meetings and talk of their experiences. GA members believe that they cannot control their gambling and must abstain. They learn to avoid gambling establishments and also learn that gambling won't solve their problems. For the problem gambler, the fellowship of GA represents a source of comfort, friendship, and social activities rather than turning to gambling.

***Since its Inception, the Number of Gamblers Anonymous Chapters Has Grown Rapidly.*** In 1960, there were 16 chapters in the U.S. This number grew to 130 in 1970, and by 1988, 600 chapters existed.

The National Council on Compulsive Gambling (now called the National Council on Problem Gambling) was founded in 1972. The first inpatient treatment program for compulsive gambling was established at the Veterans Administration Hospital in Ohio in that same year.

With the inclusion of pathological gambling in the DSM-III in 1980, people started to look at this problem as a disease, and paid more attention to treatment. There were an increasing number of treatment programs for compulsive gambling. Some programs were established by state legislatures in response to concerns voiced by the opponents of legalized gambling. There are also a number of private practitioners whose private practices are focused on compulsive gamblers. Generally, treatment is modeled on the treatment of alcoholism and other drug addictions. That consists of 12-step programs, behavioral modification and counseling, including individual, group, and family therapy, although, a review of the literature shows that a variety of treatment forms have been tried, including electric shock treatment and aversion therapy.

Treatment is complicated by the nature of the disease. Addicts are in denial of their disease, hence they cannot be relied upon to accurately report their condition. Many GA members were in therapy prior to joining GA, usually for depression, anxiety, and marital conflict, but their gambling problem was not admitted, recognized, or discussed. The employer can be a valuable tool in requiring an employee receive treatment. But because gambling is a disease that involves loss of control over money, any pathological gambler who is handling money is especially reluctant to let their employer know that they have a problem.

Another complicating factor is that pathological gamblers often don't have insurance to cover treatment. Many are having financial and employment problems so they don't have health insurance. If they have health insurance it may cover alcohol or drug treatment but only rarely gambling.

***Effectiveness Rate of Treatment is Not Accurately Known.*** Although individual pathological gamblers can be quite successfully treated, little is known about the effectiveness of treatment programs. Self-help programs such as GA don't keep track of their success. One study showed that 8 percent of the members haven't gambled two years after joining the program. It is likely the effectiveness is greater because some

members take longer than two years to completely refrain from gambling. When GA is combined with outpatient and/or inpatient treatment, the success rate is thought to be more like 50 percent.<sup>34</sup> However, many members leave GA because they don't want to abstain or they have difficulty with the concept of admitting a lack of control and having to decide to turn their life over to a power greater than the individual.

There is a school of researchers that argue that prevention is much more cost-effective, because of the high treatment costs and the uncertain success. Prevention programs include public awareness advertising and programs in the schools to make individuals aware of the disease. Again, despite the questions about the overall success rate, clinicians describe the disease as very treatable for any particular individual who has the appropriate motivation and receives the proper treatment.

***Very Small Minority of Pathological Gamblers Seek Treatment.*** Although accurate figures are not known, the consensus of researchers is that it is a small minority. The best estimate for the population of Gamblers Anonymous is about 80,000. There are about 1 to 2 million pathological gamblers in the United States. A much smaller number gets professional treatment without going to GA.

One gambler who did seek treatment was Chet Forte, who was better known as the director of "Monday Night Football." He also was producer-director of the 1984 Olympics. Mr. Forte won 11 Emmy awards. But he also gambled away nearly \$4 million including his million-dollar home. He was spared from prison only because the judge recognized his cooperation and his efforts in gaining treatment for his gambling addiction. According to press accounts, he paid back his debts, including back taxes, and continued attending Gamblers Anonymous meetings up until his untimely death from a heart attack in May 1996.

***Some States Have Directed Significant Resources to the Problem.*** California is not among their number. Some examples include Texas where the agency that administers alcohol and drug abuse programs also has a gambling responsibility. The agency sponsored a pathological gambling prevalence survey in Texas. Massachusetts funds the Massachusetts Council on Compulsive Gambling with unclaimed lottery winnings. The State of Texas contributes to the Texas Council on Problem and Compulsive Gambling. Other states have sponsored extensive prevalence studies or provided funds directly for treatment and public education. Some states fund their programs through a portion of the lottery proceeds or fees on gaming activities.

***The Gaming Industry Has Responded to the Issue of Problem Gambling.*** Though there is debate over the prevalence of problem gambling, the industry generally accepts that there are problem gamblers. Some gaming companies are participating in programs aimed at educating the public about problem gambling and providing information about the help that is available to those who need it. But participation is far from uniform. One observer has characterized the industry as doing surprisingly little.<sup>35</sup>

There are different approaches to educating the public about problem gambling. Toll-free help-lines have become popular and one can see posters or stickers with the 1-800 number posted in casinos. Public service announcements on television and radio have also become popular. These announcements are often sponsored by the casino industry or a specific casino company.

While the industry is taking some responsibility and has been an active participant in the education effort, it does not feel its responsibility extends to treatment. The industry view is that pathological gambling should be treated like any other medical condition. Individual members of industry may have donated to charitable organizations that promote the counseling and treatment of problem gamblers.

Could casinos do more? One researcher noted that it is possible that seasoned casino personnel can be quite effective in identifying pathological gamblers. However, once a pathological gambler is identified it is not clear what is the appropriate response. Industry action is complicated by the concern that a gambler may walk down the street to a competing casino or facility.<sup>36</sup>

***There are Regulatory Strategies That Might Reduce Pathological Gambling Problems.*** The situation is quite different in European countries than in the United States. In Europe, individuals can request to be banned and even family members can request that an individual not be allowed in the casino. Some areas go so far as to prohibit locals from entering casinos.

The British experience with casinos provides an interesting contrast. This discussion is drawn from an article by the noted University of Nevada researcher Dr. William Eadington.<sup>37</sup> British casinos are run on a club basis with members and guests as the only allowed patrons. Credit is not granted and alcohol is prohibited. There is not any advertising for the general public. Casinos are required to provide printed material to advise patrons of wise gambling strategies.

***Pathological Gamblers Leave High Costs in Their Wake.*** People seek treatment for compulsive gambling, but not just because of the losses they run up. Pathological gambling is not just a problem of lost money. Compulsive or pathological gamblers seek treatment when other addicts do, when their life is an absolute mess and they can't take it anymore. Mental health professionals point to factors such as widespread borrowing, deception, and crime making the lives of pathological gamblers uncontrollable. Reportedly, a large number of compulsive gamblers are involved in white-collar crime. Not surprisingly given the pathological gambler's need for funds, a significant proportion of those incarcerated may be pathological gamblers.<sup>38</sup>

These problems don't even begin to detail the impact of their behavior on their family, including children. In other words, pathological gambling is not victimless. Research has shown that children of pathological gamblers had a variety of problems and were much more likely to be abused. In the parlance of the mental health professionals, "Children of pathological gamblers show more signs of serious psycho-social maladjustment."<sup>39</sup>

Asians and Native Americans (as well as the young) have been identified as being particularly sensitive to pathological gambling problems.<sup>40</sup> Another study identified the elderly, the poor, minorities, and housewives.<sup>41</sup> Asians have been identified because gambling is a more accepted part of their culture and participation tends to be much higher. The young are at risk because of their immaturity, which can lead to excess.<sup>42</sup> Those involved in treating pathological gamblers also note large numbers of senior citizens, although this may reflect their high participation rate in gambling.<sup>43</sup>

***Underage Gambling Shows Worrying Trends.*** Some who are concerned about the issues say that gambling-related problems are overtaking drug addiction as the most prevalent problem among teenagers.<sup>44</sup> Surveys among young people show that a very large number gamble. The surveys show that about 80 percent responded that they have gambled by the time they were 15.<sup>45</sup> Approximately one-eighth of the nation's compulsive gamblers are teenagers.<sup>46</sup>

An alternate point of view is that young people engage in a variety of experimental behavior of which gambling is but one example, and can be viewed as relatively normal.<sup>47</sup>

A survey of teenagers in New Jersey showed that 64 percent of high school students had gambled at the casinos.<sup>48</sup> As reports note, there are tragic stories behind the figures:

- The captain of the football team with a \$5,000 gambling debt.
- A college student drops out 20 units short of graduation because his tuition was gambled away.
- A 16-year old was comped gourmet dinners and front row show seats. She was allowed in even after her father distributed her picture to the casinos. Caesar's and four other casinos eventually paid fines and donated funds to compulsive gambling programs.

A recent story that received considerable press attention involved three students at a New Jersey high school who ran a betting ring. They were charged with extortion, kidnapping and terrorists threats. The ring came to the attention of authorities when they kidnapped a 14-year old student who owed \$500. The student was dropped off at a housing project. The ring took in \$5,000 to \$7,000 per week.

Many played games that were illegal for minors to play and a significant number also bet on sports. Problem gambling counselors find this pattern of behavior worrying because it is illegal, hence it may have implications for those caught and convicted. Second, gambling among minors may lead to increased levels of problem gambling when they become adults.<sup>49</sup> A significantly larger percentage of pathological gamblers than the population as a whole report starting when they were young. At least some mental health practitioners view problem gambling, like alcoholism, as a family disease.<sup>50</sup> That is, there is a definite link between parental problem gamblers and their dysfunctional household and a higher level of addiction in their children, including pathological gambling.

The prevalence studies seem to show a consistently higher rate for youthful gambling than adults.<sup>51</sup> One study of college students showed that 87 percent had gambled at some point, 26 percent gambled weekly, and 11 percent said they had gambled more than \$100 in one day. In that study, 5.7 percent were pathological gamblers, a higher figure than that found in adult prevalence studies.

There is some question about the actions taken by regulators and the casinos to deal with the problems of underage gambling. Although there are figures on the thousands of underage patrons that were turned away or escorted from a casino, according to one researcher, no casino has even been fined for allowing minors to gamble.<sup>52</sup> His article is several years old, however, and there are recent press reports of such fines, but it is not known how widespread they are.

***Recent Louisiana Study Showed High Proportion of Young Problem Gamblers.*** The study released in July of 1996 showed that one in seven state residents between the ages of 18 and 21 are problem gamblers.<sup>53</sup> The rate was three times the adult rate. Technically these are not underage gamblers, because 18 is the legal age for most gambling in Louisiana. They are also not yet pathological gamblers.

***Legal Treatment of Pathological Gambling Varies.*** Despite the recognition of pathological gambling as a medical condition, it is specifically excluded from the Americans with Disabilities Act. It is at least theoretically possible that a pathological gambler could claim disability under social security. Such a claim would not likely be for the gambling itself, as it isn't clear how that would make an individual disabled and unable to work. However, the gambling would probably be an indicator of another disorder. Many pathological gamblers also suffer from another mental illness.

California law has protected the pathological gambler by not allowing enforcement of the collection of gambling debts. The reasoning of the Supreme Court in a recent case was that, "...the law should not invite them to play themselves into debt. The judiciary cannot protect pathological gamblers from themselves, but we can refuse to participate in their financial ruin."<sup>54</sup>

The liability of gaming proprietors is largely unexplored. The courts have been quite ready to hold dispensers of alcoholic beverages liable for damages to third parties from accidents caused by drunk drivers. There have not been any lawsuits yet for third-party damages from pathological gamblers, but the analogy has not been lost on observers.

### ***Test for Gambling Addiction***

If you answer yes to any of these questions, you might reconsider your gambling, according to experts on problem gambling.

- Do you ever borrow to pay for your gambling?
- Have you ever sold something in order to gamble?
- Do you have trouble sleeping due to your gambling?

- Do you gamble to escape worry or trouble?
- Do letdowns or disputes make you want to gamble?
- Whenever you feel good, do you want to gamble?
- Has your gambling led you to want to hurt yourself?
- After losing do you start over as soon as possible to win back your losses?
- Do you gamble to pay off other bills?
- Does your gambling money come from your everyday budget?

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### ***IX. Economic Impacts of Gambling***

According to one report, there is little reliable information on the social and economic impacts of gambling.<sup>1</sup> A great deal of research does exist, but often it is prepared by groups advocating one position or another and is biased or suffers from such basic flaws as to render it virtually unusable. In short, much of what has been done is not sound.

***There is a Debate Over Whether or Not Gambling Can be Good For an Economy.*** Proponents of the view that gambling is harmful use a quote of Nobel Laureate Paul Samuelson.<sup>2</sup>

"(Gambling) involves simply sterile transfers of money or goods between individuals, creating no new money or goods. Although it creates no output, gambling does nevertheless absorb time and resources. When pursued beyond the limits of recreation, where the main purpose after all is to kill time, gambling subtracts from the national income."

Other economists have taken exception to Samuelson's characterization of gambling. They point out that his criticism could be applied to movies or Disneyland. These are products that don't add to the ability of the economy to produce more. But they still have value because they provide satisfaction, or utility in the economist's jargon, to consumers. These economists are more concerned about the costs of banning gambling, that is the ensuing enforcement costs and the incentives to lobby and bribe public officials to allow illegal gambling to occur.

***Gambling Can be a Powerful Economic Development Tool.*** Las Vegas is a testament of the powerful ability of gambling to foster economic development. Because of gambling, Las Vegas has shown impressive job growth, developed into a major city with a low tax burden that many state and local governments look at with envy, and has spawned significant private and public sector investment. But can the Las Vegas model be duplicated?

There are other questions:

- Are there costs involved that exceed the obvious economic development benefits?
- Who actually gains and who loses?

- If Las Vegas is a model of economic development through gaming, are there any other costs that need to be looked at? Las Vegas tends to have a wide variety of social ills associated with it.<sup>3</sup> There is some controversy of the true level of these given the high tourist population. No studies have examined whether those are associated with gambling, the transient population, the growing population, or the low level of social services provided by the state.
- How widespread are the economic benefits? Las Vegas has grown into a large diversified city, but others have not. Atlantic City is a different case.

"But look at Atlantic City. It used to be a slum by the sea, and now, it's a slum by the sea with casinos."<sup>4</sup>

Research has attempted to answer these questions. Before we look at the research results, this report will lay out how a gambling development project may affect a local area. For those that are uninterested in the theoretical discussion, there are some conclusions that begin on page IX-7 that may be more interesting. This discussion also tends to focus on casinos but it is true for any type of gambling facility operation.

***The Basic Criteria For Economic Development Success is For a Project to Increase a Region's Net Exports.*** Specifically, the amount of goods or services that are exported needs to be increased or the amount that are imported decreased. This is the only way that income can increase. Projects can certainly be an overall economic success in terms of profit without doing either of these, but those profits come at the expense of other businesses.

***Various Factors Come to Play in Determining if Gaming Has a Positive or Negative Economic Impact.*** A full accounting of all costs must be done and it is difficult. The economic impacts of legalized gambling are tangible and quantifiable. The basic economic impacts include the construction of a casino which leads to many jobs for construction employees and suppliers, employees to staff the casino, and the suppliers for an ongoing casino. Multiplier effects then ripple throughout the overall economy. But just because a gambling project creates a lot of jobs and a large facility is built doesn't mean the economic impacts are positive. Non-economic impacts such as social costs are usually intangible, difficult to measure, and on balance negative.

Building a casino creates new jobs, such as a card dealer, in the sense that they did not exist before. But they may not be new jobs for the economy. Money spent on a gambling facility is money that already existed but was spent on other things. That is probably an obvious point, but one that needs to be made. Building and running a gambling facility doesn't create wealth, it merely transfers it. The benefit for a region is if the transfers are from outside of the region. In contrast, there is not a stimulus or net benefit if development of the casino leads to more money being spent outside of the region.

This stimulus or beneficial impact could happen two main ways:

- Tourists from abroad spend more time and money within the region. For example, if foreign tourists changed their travel patterns so that rather than coming to both California and Las Vegas, they only go to California.
- Local residents who used to travel outside of the region and gamble now stay within the region.

There are also ways that building a casino could result in no increased benefits for the region:

- Local residents who used to go to restaurants now spend their money in the casino. Then the casino has no net economic benefit.
- Tourists who used to spend money on other activities within the region now go to a gambling facility within the region.

Constructing a casino could hurt a region if either of the following occurred:

- Locally-owned businesses go bankrupt because consumers have changed their expenditures to casinos that happen to be owned by out-of-state interests.
- Casinos buy more products from out of state than the businesses they replace.
- Casinos result in increased social costs including police and other public services as well as the costs of pathological and problem gamblers. These issues will be addressed shortly.

### ***Economic Development and Impact on Communities***

There is debate about whether or not gambling is an appropriate economic development tool. The argument against using it is that although the number of jobs associated with new gambling facilities is significant it is not a compelling reason to be legalized. For example, one commentator wrote after the Mayor of Chicago proposed a gaming project:<sup>5</sup>

"Ten thousand construction jobs are supposed to be created by this project. This may very well be true. However, we could create plenty of construction jobs by building brothels and opium dens."

***Gambling is Often Legalized to Promote Economic Development of Depressed Areas.*** That was an important motivation in Las Vegas, Atlantic City, New Jersey, and many of the other locales for casinos.

Gaming in Atlantic City, like Las Vegas, has been a successful economic development tool. It has resulted in the building of many large facilities and over forty thousand jobs have been created. The success of gambling in Atlantic City, however, has done little to

revitalize the rest of Atlantic City and its business community. Atlantic City has been described as two cities.<sup>6</sup> One is the casinos and the other is a city of boarded-up buildings with a unemployed minority work force.<sup>7</sup> Gambling has largely failed in achieving the objectives of job growth for local residents and city-wide economic development.<sup>8</sup>

Another criticism of gaming in Atlantic City is that it doesn't support complimentary businesses in the community such as restaurants because these facilities are all in the casinos. In Atlantic City, the number of restaurants dropped 40 percent since 1977. Most people associated with the industry note that people don't venture far from the casinos. Because of this concern, Louisiana legalized a casino but it cannot have restaurants and hotel facilities.

In Mississippi, the Legislature legalized gambling, in part to promote development in the Mississippi delta. One county, Tunica, was the poorest county in Mississippi, the poorest state. Tunica was once called "America's Ethiopia." Since gambling was made legal, the welfare rate was cut by a third and the proportion of people receiving food stamps has fallen. Unemployment is down to 4.9 percent, its lowest rate in nearly two decades.<sup>9</sup> On the negative side, crime skyrocketed and by some reports most jobs went to workers from Memphis.<sup>10</sup>

Many of the areas that casinos are being sited in Mississippi are heavily minority, almost solely African-American. Most industry observers note that casinos are making more of an effort to hire minorities than other industries.<sup>11</sup>

One study showed little change in unemployment rates in counties where Illinois casinos are sited.<sup>12</sup> But the study did document substantial numbers of people being employed. The study suggested that the new jobs were just substitutions and/or that out-of-area workers were hired. But another explanation is that people who were unemployed but not looking for work, hence not counted in the labor force became more hopeful and led to increased labor force participation and employment but no change in the unemployment rate.

Localities report that the industry will pressure the communities to rewrite the rules for casinos once they are established.<sup>13</sup> The casinos are trying to maximize profits as any business should, but this complaint does raise questions about the claims that are made by proponents prior to legalization. Examples of recent liberalizing moves are the extension of Atlantic City gambling hours on weekends at first and then on weekdays. Also, changes in Iowa regarding riverboat gambling rules are another example.

***Local Governments have had Difficulty Controlling the Size and Scope of Gambling.***<sup>14</sup> Colorado legalized limited stake casinos in October, 1991. These facilities were sited in old mining towns that were in need of funds to preserve their historic structures. Within three years the towns were reaping large sums of money. Residents complained about traffic, crime, and noise and air pollution.<sup>15</sup>

Attempts were made to control the impact of gaming. Bets were limited and casinos had to be a small portion of the floor space. However, within a short period there were 7,000 gaming devices and 68 casinos. By December 1992, 21 casinos closed their doors, since then more have moved into bankruptcy.

The growth of the casinos and rising property tax rates lead to a decline in non-casino businesses. The town quickly found that it didn't have a grocery store, laundromat, or filling station as a result of increased taxes which had driven out these other businesses. There was also a considerable strain on the small town's infrastructure.

The City Manager of Central City, one of the cities with legal gaming, was quoted as saying:

"I'd tell anyone who was thinking of opening their community to casino gambling to have his head examined."<sup>16</sup>

South Dakota has a limitation on the number of machines per building. Tax revenues have accomplished the goal of restoring old buildings and repaving downtown. Retail sales growth within the community outpaced the state average.<sup>17</sup>

***California Horse Racing Industry Has Major Impact.*** In a study prepared for the horse racing industry, the following impacts were noted:<sup>18</sup>

- The industry generates more than \$3 billion each year for the agribusiness, tourism and entertainment economies of California.
- Nearly 25,000 Californians work either directly or indirectly in the industry.
- The industry has declined in recent years as horse racing activity has shifted to states with lower state and local taxes or fees.
- The state's share of pari-mutuel receipts is three times higher than the national average.
- Approximately 4,000 jobs have been lost in the last five years.

***Wisconsin Study Shows Major Economic Impact of Indian Gaming.***<sup>19</sup> This study attempted to describe the size of Indian gaming in Wisconsin. The major conclusions were:

- The revenues to the gaming operations were \$275 million.
- Employment at the casinos totaled 4,500. A significant portion, 1,400, were unemployed prior to obtaining casino employment and 20 percent came from the welfare rolls. Tribal employment supported by casinos constituted 70 percent.
- The multiplier effect led to another 1,500 jobs.
- Employees paid \$2 million in federal income taxes and almost \$4 million in Social Security and pension funds.

This study, along with many other studies supported by the Indian tribes, show the large economic impact of Native American gaming. These studies accurately and exhaustively

calculate the direct economic impact of Indian gaming. The Indian casinos pay out wages, social security and Medicare taxes, and federal taxes. Even though the tribes are exempt from state and local taxation, many of their employees pay state and local taxes.

The economic impacts can flow outside of the reservation. A study in Minnesota found an increase in the wages of those in the amusement industry as well as an increase in sales in casino areas.<sup>20</sup> Typically, these are smaller rural areas. Little overall impact to the state was noted, however. An interesting spin-off from the construction of Foxwoods at Mashantucket, Connecticut led to a marked increase in the profitability of area savings and loans.<sup>21</sup>

The problem with these types of studies are that they don't document all of the benefits and costs of gaming. They look at the size of the industry, which in many areas is quite significant. They leave unanswered, however, if costs exceed the benefits and what is the impact on a larger area, such as the state or nation. Another problem of the studies is that they are somewhat suspect because they are paid for by groups that have an obvious interest in continued gaming.

Gaming can have a negative impact on rural areas also, depending on the pattern of sales. One study showed that the California state lottery was in effect a \$711 million anti-rural development program.<sup>22</sup> This figure was arrived at by totaling the amount of money taken out of rural areas through lottery ticket sales, minus the funds that come back into the schools in those areas.

As noted in the discussion of Colorado, gaming enterprises can impact property values. According to industry material, casino gaming leads to higher property values.<sup>23</sup> This is supported anecdotally by stories of non-gaming firms leaving towns. The closing of small businesses may be another symptom, although both could be a product of a substitution effect as well, meaning that expenditures for gambling were substituted for other goods. The data and anecdotes from Colorado suggest that the impact can be disruptive and create a land-rush type atmosphere, at least initially.

Australia is a good laboratory for determining the socio-economic impacts. The country legalized a very limited number of casinos, allowing for a thoughtful look at the impacts of new casinos.<sup>24</sup> One notable and unsurprising impact is that the casinos took more of the gambling dollars, relative to other gambling enterprises. For most of the casinos, the bulk of revenues came from locals. Some casinos have been good at targeting international visitors and most have appeared to help tourism. But some casinos were placed in locations that were not big destination spots before, hence they did not have a significant impact. There was a boom to local restaurants, but a significant harmful impact on other trade. There were harmful effects like congestion, noise, and traffic. Also, the change in the aesthetics was noted. For the small towns it did appear to slow out-migration. It was difficult to ascertain the impacts to the compulsive gambler. The conclusion was that there was not a casino-led regional tourism boom.

***Important Conclusions from this Economic Development Discussion Are:***

- **Small Regions Benefit More than Large Ones.** The smaller the region the more likely a gambling project will be a benefit to the region. This statement is true for the simple reason that the smaller the region, the more likely the gamblers will come from outside of the region. That suggests that an urban casino will have a much different impact than a rural casino. Also the smaller the region, the greater chance that the costs of gambling, especially those of pathological or problem gamblers will occur outside of the region. Hence, gaming is likely to benefit an Indian reservation or a small city more than an entire state or country.
- **Any Industry that Draws Money From Outside is Helpful.** This is the pattern that Las Vegas followed. It fostered an industry that appealed to tourists and was unique. Gaming is not the only way to follow that pattern. Orlando, Florida owes much to Disney World, another tourist-oriented business that brought in a significant amount of money from outside of the region.
- **The Las Vegas Model can be Copied.** There are stories of success in Atlantic City; Tunica County, Mississippi; Joliet, Illinois; and the Pequot Mashantucket tribal lands in Connecticut to name a few. Clearly all of these places have seen an influx of investment and many new jobs being created. There is some dispute, however, about the positive effects in some of these places. What is in dispute are the social costs and the extent to which the original residents of these communities were helped.
- **How Many Places can Follow Las Vegas?** The fact that others have been able to follow the model makes many more places want to adopt the strategy. How many areas can be successful in luring large numbers of tourists to gamble?
- **Desire to Attract Out-of-State Residents Leads to Competition Between Jurisdictions.** Since the economic benefits occur in attracting out-of-state residents or preventing in-state residents from gambling in another state, legalization has led to competition between states. Once one state sees its residents crossing the river to gamble it creates pressure to make gambling within their own state legal. This pressure on regulating is referred to as a domino theory. A good example of this has been the legalization of riverboat casinos along the Mississippi river basin states.
- **The Freedom of People to Gamble is Worth Something.** Economists believe that the satisfaction of those who want to gamble and now can is worth something. Economists measure this and call it consumer surplus and can, in theory, estimate the dollar value of consumer surplus.
- **Many Claims of Industry Success in Economic Development do not Meet the Strict Criteria for Success.** Again, the criteria is that exports increase or imports decrease. With criteria for success this rigid, you must attract net additional dollars from out of the region, and these additional dollars must pay for any

increased social costs. Many claims of success by proponents, especially when pushing new facilities, are false.

- **Claims that Gambling Never Pays its Way Cannot be Disproven.** As discussed above, the claims that gambling never pays its way appear to be contradicted by the Las Vegas model. However, the assertion that gambling never pays its own way cannot be conclusively refuted because of the difficulty of accurately measuring social costs.

### ***Public Finance***

Politicians and the public are naturally attracted to an industry that is willing to pay 20 to 30 percent of its gross revenues as taxes. Also, gambling is seen as a source of money that is easier to obtain because it is not a tax on individuals.<sup>25</sup> Gambling has become a very accepted way for governments to raise funds.

***Nevada Stands as an Envious Example of what Gambling can do for Public Finances.*** Casino industry revenues make up close to half of the state's tax revenue. But that is not a goal that states can realistically shoot for. Economists doubt that any other state can match that.<sup>26</sup> Casino operators agree. The following quote is from a Harrah's publication:

"Despite casino gambling's promise as a source of economic development and tax revenue, gaming should not be viewed as a panacea for the fiscal woes of a state or local jurisdiction. Casino gaming is more appropriately viewed as an amenity that in smaller metropolitan areas can be a cornerstone in the local tourism/entertainment market, and in larger metropolitan areas as simply another component of a regional tourism/entertainment package."<sup>27</sup>

***Outside of Nevada, Gambling Taxes are a Small Share of State Revenues.*** The next largest gambling presence is in New Jersey, but there the proportion of state revenues provided by gambling is only about 2.5 percent of total tax revenues because the state is so large. The next largest gambling contributions to state revenues, in absolute numbers, are in Louisiana and Mississippi. Because they are small states, gambling revenues can make a larger proportion, about 8 percent of both states' budgets.

<b>Estimated State &amp; Local Government Revenue From Casinos</b>	
<b>\$ Millions</b>	
Nevada	\$556
New Jersey	\$296
Illinois	\$286
Louisiana	\$204

Mississippi	\$609
Missouri	\$130
Colorado	\$51
Iowa	\$46
South Dakota	\$4
Source: Harrah's	

**Lotteries Don't Supply a Large Portion of Revenues.** Compared to overall tax revenues, lotteries are small, they constitute only about 2.5 percent of total taxes.<sup>28</sup> Despite the sizable volumes being wagered, only about 40 percent of the lottery revenues are available for state programs after prizes and administrative costs are paid.

Even in California with more modest facilities, there can be substantial amounts of money earned by local governments. In 1993, the U.S. Conference of Mayors conducted a survey.<sup>29</sup> San Jose reported that \$5 million was contributed by cardclubs and charitable gaming. Another 500 jobs were reported in the industry, while Gardena reported 1,000 jobs. Although the City of Los Angeles had reported that bingo declined, in 1992 over 750,000 residents engaged in this activity and the city earned about \$2 million.

With some states earning large sums, other state and local governments look at how they can get a share of the gambling revenues. Because of the state money flowing to New Jersey and Colorado, New York Governor George Pataki has gone on record that gaming would be a way to keep the money at home, reduce income taxes, and control projected budget deficits.<sup>30</sup>

**Could Indian Gaming Help California?** California might be able to get revenues from Indian casinos if it signed agreements regarding Indian gaming. Connecticut gains around \$200 million annually from slot machines in an Indian casino. There are about three times as many slot machines in California as in Connecticut. If individual slot machines in Indian casinos in California are as profitable, then California might be able to gain around \$600 million annually. The figure is derived from the profits in Connecticut multiplied by the three-fold greater number of slot machines in California.

This estimate is highly speculative and is based on the following calculations:

	Slots	Profit Per Machine	Revenues to State
Connecticut	4,000	\$120,000	\$200 Million

California	112,000	
As profitable as Connecticut	\$120,000	\$600 Million
As profitable as Atlantic City	\$89,000	\$445 Million
Lower profitability scenario	\$60,000	\$300 Million

The estimate is also based on the following assumptions:

- The tribes must be able to get around the prohibition on banked games and slot machines or be able to offer lottery and non-banked games that are as profitable. Slots and banked games are currently not legal in California.
- If they offer slots under a compact, these may be significantly less profitable in California. There are many more competing opportunities in California. If Indian casinos cannot have banked machines, that could also have an impact on profitability.
- The demand for gambling may be less in California than in New England.

It needs to be pointed out that the state cannot tax or even ask for money from the tribes. The funds must be offered, then the state can accept.

If Indian gaming grows along the lines of what some researchers claim, California could stand to gain even more.<sup>31</sup> Dr. Marilyn Whitney modeled different scenarios for gambling growth in California. Under one scenario, Indian gaming more than doubled in size. The growth of Indian gaming led to a relative decline in cardroom and lottery activity and state and local revenues fell when adjusted for population growth and inflation. Under that scenario, the state could gain approximately \$1 billion if they could negotiate an agreement similar to what the state of Connecticut was able to negotiate and slots have the same popularity. The tribes would have to meet all the conditions described in the preceding paragraphs.

***Ability of Governments to Gain Funds is Dependent on Industry Profitability.*** As recent events in Louisiana have shown, not all gambling is profitable. Last year, two new riverboat casinos opened in New Orleans. They both closed within nine weeks. The City of New Orleans was left to fight with other creditors over collecting \$3 million in taxes and fees. The City's problems aren't limited to the riverboat casinos. The land-based casino has netted only about one-third of its projected revenue.<sup>32</sup> The closing of the land-based casino led to the layoffs of as many as 1,000 city workers and a 5 percent cut in the city budget.<sup>33</sup> In Iowa, the town of Fort Madison was left with a \$2.5 million bond for dock improvements, but the boat left because of lack of profitability.

### ***Iowa County Became Owner of Gambling Hall***

When the local racetrack stumbled into bankruptcy, county supervisors converted the clubhouse into a casino. The result is that the county has pulled in a tremendous amount of money. The value of the casino, if it was to be sold, is estimated at \$300 million.<sup>34</sup> According to one report, the county has gone from "rags to riches."<sup>35</sup>

Reliance on gaming revenues can be problematic because of changing consumer preferences. Parimutuel wagering is one of the oldest sources of gambling revenues. In most states it is from betting on horses, but it includes dog racing and jai alai. Parimutuel revenues are declining and for all states is 17 percent less than in 1980.

***The Reaction of Neighboring Jurisdictions is also a Risk Factor in Gaining Public Revenues.*** The domino theory plays a large role in whether or not governments get their funds. Iowa was initially quite successful in earning gambling funds. Then Illinois legalized riverboat casinos without some of the restrictions that Iowa had adopted. Traffic declined and two of the five boats moved out of Iowa. Revenues also dropped off.

Iowa responded by relaxing rules that limited operating hours and dropped a restriction that limited each gambler's loss to \$200 a visit. But Iowa's countermove had an impact on Illinois. A nearby casino in Rock Island, Illinois had to lay off 200 people and the city now receives only a fraction of the revenues it received last year. These events suggest that gambling can provide a lot of money if you are the first state in the region to legalize gambling, but revenues may be at risk if neighboring states legalize gambling.

***Casinos May Hurt State Lottery Revenues.*** The competition between gaming interests isn't just between states. Competition also occurs within industries within the state. This competition does have public finance implications. During a battle over casinos in Maryland, the restaurant and horse racing industries united against casinos.<sup>36</sup> Studies have shown that wagering on horse races clearly declines when casino-style gaming is made available in the same market.<sup>37</sup> A Florida study projected that gaming revenue would be between \$300 and \$450 million while sales tax would decrease about \$85 million and parimutuel and lottery would fall by a small amount.<sup>38</sup> In general, for states that rely more on consumption taxes the impact of increased gambling is likely to be greater than for states that rely on income taxes.

There is some debate about the competition between casino gaming and lotteries. Some research suggests that the casino gambler is much different than the lottery gambler.<sup>39</sup> That may change as casinos become more widespread. When Illinois opened up riverboat casinos, lottery revenues fell off by about 25 percent.<sup>40</sup>

Similarly, the research for California that forecasted a possible doubling in the size of Indian gaming also showed a decline in lottery revenues.<sup>41</sup> Local government revenues would also fall.

Another issue of competition that is of concern to some observers is the possible competition between legal commercial gaming and charitable gaming. Some hypothesize that charities will have less money as a result.<sup>42</sup>

***Another Element of the Public Finance Discussion is Public Service Costs.*** University of Illinois commerce professor John Kindt states that for every dollar of taxes, taxpayers spend three on infrastructure, problems gamblers, police, etc.<sup>43</sup> This contention is hotly disputed. Additional research has claimed that gambling can pay for services but because of the actual costs to consumers, it is a very expensive way for governments to raise funds.<sup>44</sup>

For example, according to this research a ten thousand dollar police squad car really costs \$120,000 if the funds are received from gambling. That figure is arrived at by adding up how much money must be lost by consumers to earn enough gambling profits to pay \$10,000 in gambling taxes. By using that logic, a ten thousand dollar police squad car costs \$129,000 in meals in California. That is how many meals must be purchased to buy the car with sales tax. Figures such as these make it seem that the public services came at an exceptionally high price, but they ignore the fact that people like to gamble or eat out. They suggest the tax burden is the entire expenditure for the entertainment, not the small portion that it really is.

### ***Social Costs***

Problem and pathological gambling may be an invisible or silent disease but it is not a costless disease. Social costs are the costs borne by society as a whole that result from the behavior of the problem gambler. Social costs includes such items as fraud, theft, bad loans, bad checks, lost work time, unemployment and welfare benefits, insured or publicly supported medical costs, and criminal justice system costs. Those types of social costs are easier to quantify than other types of social costs that result from gambling such as increased rates of suicide, car accidents, and incidence of child abuse.<sup>45</sup> Another study says that social costs should include lost productivity of spouses, impaired judgment and efficiency on the job, divorces, added administrative costs for unemployed, and the costs of depression and physical illness related to the stress and lower quality of family life.<sup>46</sup>

***Any Attempt to Quantify Social Costs is Highly Speculative.*** Most of the studies have asked pathological gamblers who are in treatment or recovery of some kind to make an estimate of what they cost society. The studies look at those social costs that are easier to quantify, such as employment costs, loss of work, bad debts, civil court costs, criminal justice costs, therapy, and welfare. The problem of this research approach is that people in treatment are not representative of the entire population of pathological gamblers.

For example, in the Wisconsin study, 92 of the 95 members of Gamblers Anonymous who responded to the survey were white. This contradicts what is found in prevalence surveys that show a larger incidence proportion among minorities. Another sign of the unrepresentative nature of these surveys is that 52 percent of those responding were married, again that is inconsistent with the prevalence surveys. The second problem with surveying for determining costs is that it requires accurate reporting by the individuals. These are individuals who clearly have some problems or else they would not be diagnosed with this disease. It isn't known how this problem may affect their reporting.

Nevertheless, the results are interesting and, even if not representative, illustrate the high costs of pathological gambling. The lifetime estimates of losses by each gambler ranged from as little as \$100 to \$20 million. The latter high figure was from gambling on the stock market and it included \$8 million of embezzled funds. A study in Wisconsin shows that the social costs were about \$8,600 per year per problem gambler, a figure that is on the low end of the range of available research.<sup>47</sup> In Grinols and Omorov, a range of \$15,000 to \$33,500 per problem gambler per year is discussed from a survey of other studies.<sup>48</sup> There are other studies showing different figures and some of the cost figures are much higher, up to \$100,000 per pathological gambler.

### ***Consumer Sovereignty***

The economic studies have tended to ignore a very important economic component. That component is what economists call consumer surplus, that is the benefit to people who want to gamble. Economists can and do use methods that attach a dollar value to that consumer surplus. Consumer surplus may sound like a theoretical tool that is not useful, but a simple example may help the reader see that it does exist.

Assume an individual goes to the movies and is planning to pay the normal entrance fee of \$7.00. Upon arriving the individual finds that entrance can be obtained at the matinee price of \$4.00. The individual pays \$4.00 but clearly the movie was worth more since the person was prepared to pay \$7.00. Consumer surplus then is at least \$3.00, the difference between the matinee price and the full price. At least, because maybe it was a movie the person really wanted to see and would have been willing to pay even more.

This concept of consumer surplus is especially relevant in valuing publicly-provided projects such as freeways where a toll is not collected. The value of the freeway can be established by estimating what people would be willing to pay.

***Studies also have Neglected the Incidence of Costs and Benefits.*** Those who are paying the costs are the compulsive gamblers and those whose lives are touched by them. The benefits go to those who enjoy gambling. Also, certain groups of taxpayers may not be well compensated. Typically, Indian gaming doesn't result in the tax revenues from the establishments. Local governments may have to provide services for which they are not paid for. The people who gain from this subsidy are the people who enjoy gambling and the Native Americans, not a small issue given their history of poverty and difficulty in fostering economic development on the reservation. Consistently it has been shown that the poor spend a greater portion of their wealth on gambling. It is still, however, a small amount and generally their gambling is not why they are poor.<sup>49</sup>

### ***Bottom Line--Do Gaming Facilities Pay Their Way?***

A Chicago Sun-Times headline said it best:

"Studies of Gambling Deal Few Answers--Conclusions Elusive on Social, Economic Impact of Casinos."<sup>50</sup>

The article follows with a discussion and a conclusion that ultimately, a decision on how to weigh all the costs and benefits is essentially subjective and moral. How does one weigh a shattered life of a pathological gambler against new jobs for people whose only hope had been welfare?

### *California-Nevada Gambling Relationship*

With the discussion in this section of the economic success of an area being dependent on a place's ability to get out-of-region residents to gamble, it is fitting to discuss California and Nevada. To many observers, it is probably obvious and not worth discussing. The relationship is simple: California sends gamblers and Nevada receives them. A recent newspaper report gives an idea of how most people view the relationship:

"But there is something vaguely parasitical about Nevadans, who try their damndest to suck money from Californians."<sup>51</sup>

With California exporting so much money to Nevada, there are obvious questions as to what might happen if California made gambling legal. A report by the Governor's Office of Planning and Research estimated that it would increase net income in California by about \$1.5 billion.<sup>52</sup> Any estimate would have to be speculative as nobody knows how attached Californians are to going to Tahoe or Las Vegas. Also, if a California casino was developed it would allow more types of games to be offered in Indian casinos. What effect that might have on gambling behavior and where the dollar is spent is uncertain. Nevertheless, it is possible that California would bear added social costs such as those arising from the pathological gambler if casinos are legalized.

An interesting point to ponder is that California may gain from having the gambling center of North America so near its borders. Although Californians drop a large amount of money in the neighboring state, Nevada orders goods and services from California and California workers bring money or send remittances from Nevada. Nevada orders could never cancel out California spending alone, but when one considers the gambling activity of all the other visitors and all of the orders it generates, that could well be a net plus for California.

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## *X. Politics and Gambling*

The relationship between politics and gambling receives considerable attention. One reason is that people's voting behavior often reflects their attitude about gambling. Another reason is the concern about the possible impact on the political process of contributions from gaming interests.

***Voting Patterns on Gambling Issues Have Definitely Changed.*** Before 1989, only one casino legalization effort was successful during the 1970s and 1980s. The vote to legalize casinos in Atlantic City was the only one out of nearly 20 state elections on casino

gambling issues to pass. However, there was a much different record on lotteries. Every state but one, North Dakota, has voted yes on stand-alone lotteries.

Since 1989, eight new casino states have emerged. The success of gambling measures is attributed to economic issues which have appeared to drive out morality issues as the major concern of voters and politicians when it comes to gambling. Gambling has been seen as a way to boost the economy and gain public revenues.<sup>1</sup>

The authors of the book on casino campaigns, The Last Resort, have suggested that a model for casino campaigns is what they call a veto model.<sup>2</sup> What they mean is that voters will not approve a casino if there is a significant negative among any of several important factors. These factors include opposition by a Governor or other major political figure, or morality and crime becoming significant campaign issues. The 1996 election has seemed to overturn that rule. Elections on casino gaming were won despite strong negative campaigns and gubernatorial opposition in Michigan, Louisiana, and Arizona. It is surprising that crime did not become an issue that shaped the Louisiana election given the great number of gaming scandals in the state.

Casinos have not required a vote of the people to be approved in every instance. Popular votes occurred in New Jersey, when residents voted for casinos in Atlantic City. Missouri had a statewide election in 1992. Local referenda were required in Missouri, Mississippi, Indiana, and Iowa at various times. These measures passed and paved the way for riverboat gaming's expansion.

***Gaming Companies and Tribes Are Large Political Contributors.*** Evidence of the size and scale of political contributions can be seen in California. In California, the gaming lobby has spent over \$10 million since 1990.<sup>3</sup>

The 1994 gubernatorial election saw significant Indian tribal involvement. The tribes contributed more than \$1.5 million to the Democratic party in order to support a gubernatorial candidate who they believed would be more receptive to their gaming efforts.<sup>4</sup> Their gubernatorial involvement was part of a larger effort to elect officeholders who would be friendly to their interests. Tribal contributions made to Democrats went from \$33,000 in 1992-1993 to \$2.4 million in 1994-95. The tribes donated \$740,000 to the Umberg campaign for attorney general alone. However, they have also begun to increase their contributions to Republicans.<sup>5</sup>

The donations of the tribes are not limited to political causes. The tribes also have made donations for symphonies in San Diego and Sacramento.

Following is a table of political donations in California from gambling organizations.

### **Political Spending**

<b>Company</b>	<b>Lobbying</b>	<b>Campaign Contributions*</b>	<b>Total</b>
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Hollywood Park Operating Co.	\$430,391	\$1,420,000	\$1,850,391
California Commerce Club	\$606,349	\$654,360	\$1,260,709
Bell Gardens Bicycle Club	\$372,204	\$773,077	\$1,145,281
Oaks Card Club		\$207,051	\$207,051
Ladbroke Racing Association and affiliated entities	\$240,302		\$240,302
Table Mountain Rancheria	\$52,878	\$146,394	\$199,272
Rumsey Indian Rancheria	\$54,580	\$146,500	\$201,080
Barona Band of Mission Indians, Barona Casino	\$117,774	\$210,951	\$328,725
Viejas Band of Kumeyaay Indians	\$73,559	\$228,600	\$302,159
Sycuan Gaming Center		\$253,745	\$253,745
Los Angeles Turf Club	\$378,607	\$242,720	\$621,327
Bay Meadows Operating Co.	\$84,593	\$178,022	\$262,615
De Bartolo Entertainment, Eddie De Bartolo Jr.	\$10,000	\$167,725	\$177,725
Oak Tree Racing Association	\$69,998	\$207,401	\$277,399
Del Mar Thoroughbred Club	\$52,500	\$175,324	\$227,824
<b>Totals</b>	<b>\$2,543,735</b>	<b>\$5,011,870</b>	<b>\$7,555,605</b>

Source: Sacramento Bee

\*including local initiatives

On the national level, gambling interests are quite active. The top 10 donations in terms of dollar amount from gambling interests are topped by the Mashantucket Pequot tribe followed by casino companies and technology firms. Gambling is among the top five interest group givers, just below the National Rifle Association.<sup>6</sup>

The amount of campaign money donated by gaming interests has led to press attention on the issue. In the words of two observers, the candidates are "...raking in Las Vegas money as never before."<sup>7</sup> In certain state races, there have been similar patterns of major contributions by gaming interests. In Louisiana, one-third of the campaign contributions are from the gaming industry.<sup>8</sup>

***Gambling Donations and Political Scandals Have Occurred.*** Because entry into gambling is limited by regulation, there is a potential for corruption in the licensing decision. In Missouri, the attorney general alleges that the house speaker broke the law by accepting funds from casino companies. The aim of the companies, according to the attorney general, was to influence licensing decisions. The result was a grand jury investigation.

In Louisiana, there has been significant criticism of the licensing decisions for casinos. As the economics section notes, there have been several projects that have not been successful.<sup>9</sup> Critics blame it on those who received the licenses and the fact that they received the licenses for political reasons rather than merit.<sup>10</sup>

***Scandals in Louisiana Related to Gambling.*** Louisiana has been seized by a number of scandals related to the gaming industry.

**Influence-Peddling Scheme in the Video Poker Industry.** The scandal has led to the resignation or electoral defeat of several legislators. The senate president, the senate's most senior member, and the chair of the house committee which deals with gambling bills were all defeated in election campaigns as a result of the gambling scandal. As a result of the scandal, the new governor proposed a referendum on gambling in Louisiana. The election, which is discussed elsewhere in this section, was held on November 5. Each parish had the opportunity to vote on continuing to allow video poker machines and casino gaming within the parish.

The scandal has also led to an FBI investigation. Affidavits based on FBI tapes portray some lawmakers accepting payoffs or campaign donations from gambling lobbyists. Some of the newly-elected legislators that have ousted the incumbents are distinctly anti-gambling. Twenty-one men were convicted or have pleaded guilty to crimes. Many are connected to New Orleans or New York organized crime families.

**Skimming on Construction Contracts:** A crony of former Governor Edwin Edwards named William Broadhurst, is awaiting trial on charges he skimmed money off of a construction contract for a riverboat casino.

**Improper Influence For Casino License:** The State licensing agency conducted its own investigation into the case and then voted to close it without issuing a report. The FBI subpoenaed the records the day after the vote. There are allegations that the licensing agency was improperly influenced through campaign contributions.

Interestingly, many in the industry don't expect that events in Louisiana will have an effect on gambling elsewhere. The reason is the "Louisiana Factor," which to industry observers means a notorious political structure and a haphazard gambling regulatory regimen.<sup>11</sup>

As a result of the scandals, binding referendums on continuing gaming were placed on each of the 64 parish ballots. Each parish had the option of banning the gaming that was currently legal within the parish. In 30 of the parishes video poker was banned. The most important elections were on the continuation of river-based and land-based casinos. These all passed in the parishes that had casinos. In Orleans parish, the home of the land-based casino, two-thirds of the voters favored maintaining the casino.

***Louisiana is not Alone in Having Scandals.***

- The speaker of the House in Missouri had to resign because of gambling corruption charges.
- The FBI conducted "Operation Lost Trust" in South Carolina. It resulted in the conviction of 17 legislators and lobbyists for bribes related to votes to legalize parimutuel racing in 1990.

- In the same year, six members of the Arizona Legislature pleaded guilty for accepting bribes on a bill to legalize casino gambling.

***There Have Been Some Scandals Associated with California Cardrooms.*** In Irwindale, a city mayor's enchilada was spiked in 1972 by a then cardclub proponent who was later convicted of trying to drug the mayor in an effort to blackmail him and win his support for a casino.<sup>12</sup> A scandal has recently occurred in California. A former chairman of the California Republican Party was indicted on charges of trying to influence a GOP Assembly Member. He offered the lawmaker a share of a proposed cardroom in Colma.

More recently, a member of the Compton City Council was indicted. She was charged with extorting money from a company seeking permission to build a cardclub in Compton.

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## ***XI. Gambling and Crime***

Gambling is often associated with crime. The relationship is easy to understand. Many types of gambling have been, indeed still are, illegal. Hence, by definition, criminals were the only operators of games. When gambling restrictions were relaxed, criminals were the first to open up legal gambling establishments. A lax regulatory framework in Nevada did not prevent members of organized crime from openly owning and operating casinos. To some degree, Nevada needed the criminals to make gambling viable because no one else had their expertise and experience.<sup>1</sup>

***Up to the 1960s, Nevada had a Difficult Time Keeping Mobsters out of the Casinos.*** Nevada was plagued by teamster financing, hidden ownership, employment of individuals of questionable character and background, and the clear links to organized crime.<sup>2</sup> In this context, organized crime doesn't just mean Mafia.<sup>3</sup> Nevada improved its regulation only under the threat of federal intervention.<sup>4</sup> The federal government believed, with good reason, that Nevada casinos were fueling organized crime throughout the country.

Because of this history, the concern about organized crime usually is raised whenever legalizing gambling is discussed. Even when New Hampshire began its state lottery in 1964, there was concern that organized crime would take over.<sup>5</sup>

Much has changed since the days when Bugsy Siegel started the first modern casino in Las Vegas. Organized crime has become part of the mystique of gambling but it is without significant influence today. Las Vegas and the Flamingo are part of an historical association with organized crime.

***Modern Casino Gaming Has Safeguards to Protect Against Organized Crime.*** Casino gaming has become one of the most highly regulated industries in America. The companies and individuals involved are very carefully scrutinized and held to extremely

high standards. The organized crime scare is simply that, a scare according to many observers.<sup>6</sup> Gambling is indeed associated with crime, specifically political corruption.

The casino companies suggest that they are devoid of organized crime influence because they are:

- Dominated by publicly-held companies, many with household names like Hilton and Sheraton.
- Answerable to their shareholders who are thousands of individuals and institutional investors.
- Answerable to the Securities Exchange Commission.
- Indistinguishable from any other business with accountants, attorneys, payroll specialists, auditors, and market researchers.
- Licensed and tightly-regulated by state governments.

Nevertheless, there remains an ever present concern about organized crime. The sheer volume of money, cash in particular, that is generated by gambling, makes it a tempting target. Organized crime has been successful infiltrating ancillary businesses such as machine maintenance or those that provide other services.<sup>7</sup> Often labor unions are used as the vehicle to carry out the infiltration.<sup>8</sup> There are examples of organized crime infiltration. For example, as discussed in the section on gambling and politics, the FBI is investigating allegations that Louisiana state legislators took multimillion dollar payoffs to approve an expansion of video poker. The individuals attempting to buy influence were connected to organized crime families.

Researchers state that organized crime is more of a product of illegal or poorly regulated gambling than well-regulated gambling.<sup>9</sup> That is especially worrisome because gambling isn't just done within the large casinos. There are many other gambling opportunities and not all are as well-regulated or as free of organized crime influence as casinos. In California, cardrooms and Indian casinos have been a focus of concern about criminal infiltration.

***The Role of Organized Crime and Indian Gaming has Been a Controversial One.*** As noted in the section on Indian gaming, the charge that Indian gaming has been infiltrated by organized crime has been made. Competitors and antigambling interests use that charge as an attack on Indian gaming. Some researchers and industry observers are quick to point out that, however, there is no evidence that organized crime has significantly infiltrated Indian gambling operations.<sup>10</sup> Others counter that inadequate regulation and oversight make it harder to find evidence. But there is ample evidence of attempts, some of which have met with success.

The Los Angeles Times ran a lengthy article on Mafia attempts to take over an Indian gaming operation in California.<sup>11</sup> The attempts were ultimately unsuccessful. The information used in the article was from a long-running federal investigation. The same investigation eventually ended with the conviction of Richard Silberman, the former State Director of Finance, on charges unrelated to the gambling infiltration attempt.

There have been other incidents.<sup>12</sup> Two tribal leaders who had complained that Indians weren't getting a fair share of gambling profits at another facility were later murdered. At the Barona Reservation, a bingo manager was caught rigging games so that skills in the audience could win. Later, he testified about mob involvement in a number of Indian casinos throughout the country. Some of what he said has been substantiated. These events did occur, however, during the earlier years of Indian gaming.

***Gambling is a Natural Target for Criminals Because of the Large Amounts of Cash.***

Gambling operations, including cardrooms, earn large amounts of cash and present particular opportunities for skimming and money laundering. Dealers don't have to continually inventory their chips and money while they are working, providing opportunities for fraud. In addition, cheats are drawn to casinos and cardrooms because of the large amount of money generated by the facilities. Dealer skimming of chips by palming or collusion is probably the greatest risk.<sup>13</sup> Clubs allow employees to gamble when they aren't working, a situation that can lead to collusion. Other risks include credit abuse, card cheaters, and currency transaction violations. Because of these factors, proper operations and security are very important.

Skimming has been a significant problem. The Kefauver committee found that it was widespread. There were indictments in the early 1960s of casino owners for tax evasion. Skimming can also occur with the granting of credit. Credit can be granted to individuals who aren't required to repay all of the loan. One solution is to prohibit credit, but that can increase the problem of loan sharking.

Money laundering is another problem. Bettors can come in with a large amount of cash and purchase chips. The chips can then be cashed in, labeled as "winnings" and the money is now legal. In California cardrooms, where the house is not the banker, it is harder to dispute claims of large winnings. Federal regulations require that currency transactions of \$10,000 or more must be reported including multiple transactions that exceed \$10,000. Employees have to be alert to the time periods and possibility of multiple transactions.

Another issue is kickbacks. These occur in a variety of different situations. Operators can receive kickbacks for allowing money laundering. Employees can be pressured into giving kickbacks for preferred assignments.

***Crime has Been an Issue for Cardclubs.*** Although there has not been an overall comprehensive study, information is available from a report by the Attorney General, new reports, as well as a report by the City of San Jose Police Chief.<sup>14</sup> According to these sources, there have been robberies and assaults of patrons who had left the cardclubs after making money. In the news reports, the criminals and victims are usually Asian and have been playing Asian games which frequently have high stakes.

There is debate about the role of the clubs and crime. The City of San Jose produced a memorandum showing dramatic increases in crime in the area where a new club opened.<sup>15</sup> But it is hard to know if that is a result of more people coming into the

neighborhood or criminals following the money. The police chief of San Bruno states that the club there presents no crime problem.

Some of the crime may be unrelated to the gambling that occurs at the cardclubs. Rather, the club is a suitable place to meet individuals who are willing to buy stolen property, drugs, or cars without registration. Other activities such as loan sharking and credit card/check fraud have been noted. Unfortunately, some of these crimes are difficult to prosecute. There is some belief that gambling crimes are victimless. This thinking ignores the role of organized crime behind some of these. Loan sharking can be difficult to prosecute because the victim doesn't want to be involved.

In the City of Commerce, seven individuals linked to a Chicago crime syndicate were indicted by a federal grand jury for racketeering, extortion, and conspiracy. The loansharking and bookmaking operations occurred in the California Bell Club before the Gaming Registration Act was fully implemented in 1984.

Since then, however, there have been other incidents. A Santa Clara grand jury indicted 14 individuals associated with the Garden City cardclub. Skimming of approximately \$4 million in club revenues occurred. The subjects were eventually convicted of filing false income tax returns, making illegal campaign contributions, theft of club assets, and perjury. This is a case where upper level management of the club was involved. While less frequent than participation by low or mid-level employees, the scope for criminal activity is greater when upper level management is involved. Another example was the attempted effort of Chinese organized crime figures to purchase a cardclub.

Detailed information about the cardclub in Bell Gardens, the Bicycle Club, sheds light on criminal acts in cardclubs. The Federal government was a part owner. The club had been seized because it was financed through ill-gotten gains. Following is a listing of some important developments at the club:<sup>16</sup>

1. In 1986, Asian games were introduced and club revenues went from around \$12 million per year to \$60 million, then \$80 million annually.
2. One of the club's pit bosses was arrested and eventually plead guilty to seven counts of extortion and weapons' violations.
3. Wall Street Journal article identified the Asian Games manager as a member of an Asian crime family.
4. The Internal Revenue Service fined the club \$4.2 million for ignoring laws designed to prevent money laundering.
5. Government audits turned up a lack of adequate cash reporting and internal accounting controls.
6. The Attorney General alleged that the founder is skimming millions in the form of kickbacks from the manager of the Asian games.
7. Three more employees were arrested involving possession of automatic weapons and heroin smuggling. They provided evidence that led to the arrest of the manager for Asian games on conspiracy and extortion charges.

8. A new Asian Games Manager was hired. Part of the job was for her to grant credit to gamblers and pay operating expenses. Her money came from an organized crime figure.
9. The sale of the club was discussed with organized crime figures. One is in Nevada's "Black Book," meaning he is barred from even walking into a casino. The deal eventually fell through.
10. The casino manager suspends the next Asian games manager. The City of Bell Gardens then forced the manager to reverse the action and canceled the work permit of the club security manager. The Department of Justice suspended the license of Asian games manager and that of the Casino manager.
11. The Attorney General alleged that the federal trustee had knowingly allowed illegal activities at the club, including loan sharking, kickbacks, and cheating.

The television news show, "60 Minutes" did a report on the club. They were able to catch on camera the laundering of money at the club.

Loan sharking has also been an issue for the clubs.<sup>17</sup> This crime is particularly dangerous for the problem gambler who needs money for gambling. Because of their compulsion it is easy to end up in debt to a loan shark.

The purpose of detailing some of the crime is to give a general sense of some of the problems that have occurred. A more detailed listing of cardclub crime can be found in the information available from the Department of Justice.

***Federal Concern for Money Laundering Evidence by New Regulatory Requirements.*** During 1996, the U.S. Department of Treasury's Financial Crime Enforcement Network proposed to more tightly regulate cash transactions at California cardrooms and Indian casinos. The federal regulation adds cardclubs and Indian casinos to the definition of financial institutions under the Bank Secrecy Act. The purpose is to prevent fraud and tax evasion. Under this rule, the facilities will be required to maintain a comprehensive record keeping program and establish anti-money laundering safeguards. Part of the justification that the Treasury provided was that California is unable to monitor and regulate the activities of cardclubs absent additional resources and a gaming commission.

***Another Crime Issue Associated with Gambling is Street Crime.*** U.S. News and World Report did a comparison of crime rates in cities with gambling versus those that do not. The crime rates were significantly higher in the places that allowed gambling.<sup>18</sup> Industry researchers dispute the view that cities with gambling have higher crime rates and assert that the rates aren't higher when the tourist population is considered.<sup>19</sup> The article failed to consider that these cities are vacation destinations and their population is swollen by the influx of tourists.

Atlantic City showed a jump in crime when gambling was legalized. The city went from 50th in the nation in per capita crime to first.<sup>20</sup> But when the number of tourists are taken into account, Atlantic City doesn't appear to have a crime rate that is much different from other cities.

In Deadwood, there were significant increases in crime and violence when gambling was legalized.<sup>21</sup> The researcher acknowledges that the influx of people may be the cause. Another possible cause is the boom-town atmosphere.

Another researcher has pointed out that the crime that is attributable to compulsive gamblers is often underreported.<sup>22</sup> This includes bad checks, embezzlement, check forgery and fraud. The crime rate is usually for street crimes, which aren't typically attributed to compulsive gamblers.

As noted in the economic section, Australia legalized a number of casinos. As such it offers a kind of a laboratory to see the results of expanded legal gaming. There was a noted increase in minor crimes, including vandalism and property damage by casino patrons. That may just reflect the growing number of tourists. There was not a big crime wave or any infiltration by organized crime.

***Illegal Gambling is Still a Significant Problem.*** How big is illegal gambling? It may run as high as \$100 billion per year.<sup>23</sup> Other estimates put the figure even higher.<sup>24</sup> That may seem like a very large figure, but as noted earlier, sports betting is immensely popular and most of it is illegal. The large extent of illegal sports betting is one of the reasons that some used to advocate its legalization. Others claim that business with illegal bookies would not decline because they offer better odds, credit, tax free payouts, and greater convenience in placing bets and collecting winnings.<sup>25</sup>

Sports books are not the only component of illegal gambling. In San Jose, police raids led to the confiscation of 60 illegal slot machines at 14 different business establishments.

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## ***XII. Outlook and Options***

It is difficult to forecast what will happen with gambling in California. After years of an almost unbroken string of growing gambling participation and opportunities, two events have intervened to bring the trend to a halt.

- A court case that severely cut back lottery games and threatened to drastically limit Indian casino gaming.
- A moratorium on cardclub expansion.

Added to this is the possible creation of a gaming commission to regulate cardrooms. What effect that might have on the industry is difficult to say.

Another emerging development that may have an impact on California is:

- Federal legislation that would establish a study commission to look at all aspects of gambling.

Gambling may be changing radically for other reasons. Minnesota announced a joint plan to allow gambling at home. Massachusetts also tried a one-year experiment with a telephone lottery system. There is considerable discussion of at home betting on the Internet.<sup>1</sup> Reportedly current Internet gaming operations are quite profitable.<sup>2</sup> Although illegal in the United States, they are legal in their offshore havens, typically in the Caribbean. If the casinos are outside of the United States it is difficult to prohibit or regulate play. For right now the volume of play is limited because of problems of legality, security and trust.

Nevertheless, there are some successful examples. There is a lottery based in Liechtenstein that is on the World Wide Web. Tickets are purchased with credit cards. It is one example of many that include betting on racing and casino games. Because of the ease of setting up a site the number may grow to thousands soon. In some sense, it is merely an outgrowth of an already existing in-home gambling market through the telephone and cable television. In the United States, it is limited to some off-track betting. Because of the rigorous requirements, it is small.

As gambling seems to find new areas for its growth, airlines have weighed in. British Air is putting gaming machines on their international flights from London to non-U.S. destinations. It is banned on all flights that originate or end at a U.S. destination. The FAA did a study and found that if gambling was offered on foreign carriers only it could be a \$500 million market.

Although the extent and types of gambling in and around California may be changing, it is clear that gambling has already made a major presence in the state. Following is a list of options for the state to consider adopting to deal with some of the impacts and issues raised by gambling. These are only options and not recommendations. The California Research Bureau does not develop recommendations, merely options for policy makers.

## *Options*

### *Research Options*

Although this paper covers a lot of material, it is evident that there are many things that are unknown about the impacts of gambling, especially as they relate to California. Major issues related to gambling that need more research include pathological and problem gambling, underage gambling, economic impacts, public finance, and crime. Other states are in a similar situation and have tried to resolve the problem in various ways.

- New Jersey, Oregon, and Maryland have set up Commissions charged with studying the entire issue and making recommendations to the Governor. A commission such as those would not necessarily have to look at whether or not to expand gaming, but attempt to identify the impacts and how best to deal with them. Minnesota has an Advisory Council on Gambling. Its charge is to study the conduct of all forms of gambling in Minnesota and advise the governor and legislature on all aspects of state policy on gambling.

- Michigan had a blue ribbon commission that was entitled, "The Governor's Blue Ribbon Commission on Michigan Gaming." The commission was asked to assess the issue of expanded gaming. The Commission recommended expanding limited gaming. Their logic was that the state was already having to bear the social costs without any of the benefits. The Governor did not agree with their recommendation.
- Since there is a cardroom moratorium in California, such research could look at the arguments over the appropriate policy once the moratorium ends.
- The state could encourage federal studies which address areas of research needs. Such action would be particularly timely given the federal legislation that sets up a research commission.
- The state could conduct a study that discerns the number of pathological gamblers within the state. Many other states with gaming have conducted such studies.
- The Oregon Commission specifically recommended additional research. It was clear to the commission that very little was known about the costs of gambling. In the words of one of the members:

"Right now, we in Oregon do not know if we have created a monster. Nor do we know the real cost of state-run gambling, social and economic. But we do know we are going to pay the price."<sup>3</sup>

### ***Regulatory Options***

This paper discusses the regulatory regimens in different states. There are marked differences between states. At one extreme are Utah and Hawaii, where no gambling is legal. At the other extreme is Nevada, where casino gambling is allowed at many locations throughout the state, but of course still subject to state and local regulation.

- Both examples are options for California. California could remove many of the restrictions on gambling in California or increase the restrictions on gambling.

Most states with as much gambling as California have a greater state regulatory presence, including a gaming commission of some kind. California could increase regulation of gambling several different ways.

- Establish a gaming commission to oversee all types of gambling. The jurisdiction could be as broad as cardrooms, charity gaming, and the lottery. The lottery is already state-operated and regulated. One option would be to establish a separate regulatory body to oversee the operations. The commission could also negotiate to gain some oversight of Indian gaming. Another option would be to limit the commission to cardrooms.

- Such a state gaming commission could preempt or share jurisdiction with the existing regulators of charitable gaming and cardrooms, primarily local governments.

Publicly-traded companies are subject to requirements of both federal law and the listing stock exchange. These requirements for audits can eliminate some of the criminal activity that can occur in connection with gambling establishments. Also, these companies have greater access to funding from banks and other mainstream business sources.

- Eliminate any restrictions on the number of cardrooms that publicly-traded companies can own and operate.

In some sense, California law is less strict than Nevada's. Nevada prohibits all gambling unless specifically authorized. California law allows gambling except when prohibited. As a result, the prohibitions contained in California law can be ineffective as new variants of the prohibited activity are developed. Twenty-one is outlawed, but the game of 22 can be played.

- Make all gambling illegal in California unless specifically authorized. The point is not to prohibit more types of gambling, but to make it easier to enact a prohibition of particular activities. This can also allow for standardization of games which can facilitate enforcement and regulation.

### ***Pathological Gambling***

Pathological gambling is a serious medical condition that with the proper intervention can lead to recovery for the individual.

- Ensure that there is available a continuum of services that people with gambling problems can take advantage of.
- Require that all gaming establishments post a 1-800 number for gamblers to call for assistance with gambling problems. The number could also be printed on the back of all lottery tickets. The province of Nova Scotia requires an information sticker on all gaming machines.
- Require all Internet information supplied by gambling interests have a direct link to a site that provides information and help for pathological gambling. If this could not be required of private interests, the state sites, such as for the lottery could have such information. The Florida regulatory agency has this feature. The Minnesota State Lottery has a site that contains information to help individuals make choices about whether or not to gamble, help set guidelines for healthy gambling, and talk with someone about gambling problems.
- Institute public education and awareness programs about problem gambling in schools and elsewhere. Part of the motivation for these programs is that problem

gamblers are harder to spot than drug addicts or alcoholics. Other states support such programs.

- Fund treatment programs and/or education for mental health professionals. Iowa, New York, and Texas have supported treatment as does New York. Illinois is spending state funds to train gambling addiction counselors.
- Examine whether unclaimed lottery prizes or a fee on current gambling activities could fund pathological gambling programs.

There is disagreement over how best to help the pathological gambler. There are examples of public policies that have been adopted in other areas.

- Fund pathological gambling treatment programs to allow treatment on demand. This suggests a larger government role, but that may not be the case. If the treatment is successful, then those who use the program could end up paying back the money that goes for funding the program.
- Allow gamblers to sign a pledge that requires a casino to refuse entrance. Options could include play limits, rather than complete banning. Illinois and Missouri have such programs in their casinos.
- Gaming establishments may be more supportive of self exclusion programs if their liability is limited. That is, their liability if they make a mistake and allow an excluded gambler entrance to their premises. Conversely this could reduce the effectiveness of such limitations.
- Ban severe problem gamblers from entering gaming establishments.
- Ban advertising of gambling, including the state lottery. There is a significant chance that such a ban would not be constitutional.
- Ban credit card machines in casinos and gambling establishments. Other similar options would be to require ATMs to take deposits so winnings can be put safely away to discourage further gambling. Another option would be to establish limits on withdrawals from ATMs at gaming facilities.
- Ban gaming establishments from cashing checks, or at least government checks.
- Gaming establishments could follow the lead of Harrah's Casino and establish in-house programs to give services to employees and their families if they suffer from compulsive gambling behavior.
- Gaming establishment employees could be trained to recognize compulsive players, to intervene to stop compulsive play, and to direct players to help

services. Such training could be expanded for everyone who sells gambling products, including lottery tickets.

- Require closing of gaming establishments for a few hours during a day to break up binges. This is roughly analogous to requiring bars and liquor stores to not sell during certain hours. The rationale behind the option is that a pathological gambler would be forced by the closing to examine his or her behavior.
- Require checks written by gambling patrons to be deposited as soon as possible. Check writing can be a form of lending if the check is not quickly processed.
- Ensure an adequate budget in the Department of Corrections for treating incarcerated pathological gamblers. The State of Wisconsin spends \$500,000 for counseling inmates on gambling problems.<sup>4</sup>
- Don't allow sales of liquor where gambling occurs. This option could apply even to the lottery. In Texas, bars cannot sell lottery tickets.
- Require compulsive gambling education in high schools.
- Ensure that public assistance cannot be accessed at gambling venues through ATMs.

In California, gambling debts cannot be enforced by the courts. There is disagreement over whether this is wise public policy that protects the pathological gambler or poor public policy that encourages loan-sharking.

- Allow gambling debts to be collected.

### ***Economic Development***

Gambling facilities are often used to promote economic development.

- Earmark gaming revenues for economic development areas such as enterprise zones. Such a policy would ensure that the money is targeted to those areas that need it.
- Just as Indian casinos have been used for economic development for the tribes, casinos could be allowed in other economically depressed areas.

### ***Underage Gambling***

- Making the minimum age for gambling 21 or older for all kinds of gambling within the state.
- Ensure that there are effective penalties for underage gamblers and the establishments that sell to them, including those that sell lottery tickets.

## ***Crime***

- Ensure that exclusions lists of known undesirables, petty thieves, and card cheats are shared between jurisdictions.

## ***Indian Gaming***

This has been a rapidly growing area without significant state involvement. Some states have increased their say over Indian gaming through state-tribal compacts. The compacts have been agreed to in part because of widespread concern that Indian gambling is not adequately regulated, although tribal leaders disagree.

- Enter into compacts and ensure Indian tribes address such issues as minimum gambling ages and revenue sharing.
- Prohibit sales of alcohol where there is gambling.
- Enter into a compact with Indian tribes to provide for a state regulatory role in Indian gaming.
- Petition the federal government to improve regulation of Indian gaming, including compilation and release of industry statistics.

## ***Fiscal Impacts***

- Negotiate voluntary revenue sharing agreements with Nevada. In that Nevada may be less than excited about sharing money, negotiations would probably have to be backed with the threat of casino legalization in California. One option would be to allow intercept casinos within a specific geographic zone, such as within 30 miles of the Nevada border and within 30 miles of a Nevada casino.
- Withhold lottery prizes for more than child support and delinquent taxes. Other states will withhold prizes for compliance with a judicial order or any moneys owed to city, county, state or federal governments.

## ***Lottery Advertising***

There is controversy over how lotteries advertise. Critics charge that the advertisements are misleading, suggesting that the lottery is an easy path to riches and promotes a society that believes that you can get something for nothing. Some states have tried to regulate the content of advertisements, the most recent being New York which makes its advertisements portray winners more honestly. It should be pointed out that advertising does help sales which in turn provides funds for California public education.

- Require the California State Lottery to advertise more typical winners than people who win millions.

- Require lottery ads, like those for prizes, show the odds of winning the advertised prize. Wisconsin requires the odds to be shown.
- Prohibit lottery advertising altogether.
- Limit lottery advertising to that which doesn't induce people to play. Wisconsin doesn't run promotional ads, but limits ads to those that are purely informational about how to play the games and what the top prize happens to be.

Recent court cases and Attorney General opinions have sharply reduced the ability of the lottery to raise money.

- Allow the lottery to run banked games and slot machines.
- Allow the lottery to open a casino with profits earmarked for the same worthy cause as presently supported by the California State Lottery.
- Allow private lotteries.

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