The Gambling Debate

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If we consider games of chance immoral, then every pursuit of human industry is immoral; for there is not a single one that is not subject to chance, not one wherein you do not risk a loss for the chance of some gain.... In all these pursuits, you take some one thing against another which you hope to win.... These, then, are games of chance. Yet so far from being immoral, they are indispensable to the existence of man, and every one has a natural right to choose for his pursuit such one of them as he thinks most likely to furnish him subsistence.

—Thomas Jefferson, *Thoughts on Lotteries,* 1826

Almost all these pursuits of chance [i.e., of human industry] produce something useful to society. But there are some which produce nothing, and endanger the well-being of the individuals engaged in them or of others depending on them. Such are games with cards, dice, billiards, etc. And although the pursuit of them is a matter of natural right, yet society, perceiving the irresistible bent of some of its members to pursue them, and the ruin produced by them to the families depending on these individuals, consider it as a case of insanity, *quoad hoc,* step in to protect the family and the party himself, as in other cases of insanity, infancy, imbecility, etc., and suppress the pursuit altogether, and the natural right of following it. There are some other games of chance, useful on certain occasions, and injurious only when carried beyond their useful bounds. Such are insurances, lotteries, raffles, etc. These they do not suppress, but take their regulation under their own discretion.

—Thomas Jefferson, *Thoughts on Lotteries,* 1826

Contents

Illustrations ix

Acknowledgments xi

Introduction xiii

Part I: Introduction

1 The Current Climate of Gambling in the United States 3

2 Ethical Rationales Utilized in Public Policy: The Gambling and Tobacco Industries 19

Part II: Current Issues

3 Internet Gambling: Gambling's Jackpot or Demise? 35

4 Sports Gambling: A Friendly Wager or a Threat to the Integrity of the Game? 47

5 Native American Gambling: Economic Development or Dependence? 65

Part III: Government's Role in Gambling

6 Expanding Gambling: Factors behind the Decision 83

7 Locating a Casino and Selecting an Operator: The St. Louis Experience 95

8 Playing the Revenue Game: New England's Gaming Industry 113
9 Macau: China's Entry into the World of Gambling 139

Part IV: Conclusion

10 The Role of Government and the Gambling Industry 147

Bibliography 155
Index 163

Illustrations

TABLES

Table 1.1	State Prohibitions on Gaming	12
Table 1.2	Gambling Taxes (Millions) Collected by States (2005)	14
Table 1.3	Gambling's Contributions to State Finances	16
Table 2.1	State Excise Tax Policy (1990)	21
Table 2.2	State Excise Tax Policy (2002)	22
Table 2.3	The Five Waves of U.S. Gambling	24
Table 5.1	Changes on Reservations Other than Navajo	69
Table 6.1	States Collecting More than 5% of Total Tax Revenues from Gambling Taxes	84
Table 7.1	Casino Revenue Tax Rates for Illinois, Indiana, Iowa, and Missouri	100
Table 7.2	Missouri Gaming Commission Regulations	101
Table 7.3	St. Louis City RFP Goals and Preferences	103
Table 7.4	St. Louis County RFP Goals and Policies	105
Table 7.5	Operating Results of President Casinos, Inc.'s St. Louis Subsidiary	108
Table 8.1	Seasonal Indices: Rhode Island Data, July 1997–December 2002	116
Table 8.2	Trend by Segment: Rhode Island Data, July 1997–December 2002	117
Table 8.3	Massachusetts Lottery Program	118

Table 8.4 Seasonal Indices: Massachusetts Lottery Data, January 1998–February 2006 119
Table 8.5 Trend by Segment: Massachusetts Lottery Data, January 1998–February 2006 120
Table 8.6 Trend Equations: Connecticut Lottery Sales, 1972–2002 122
Table 8.7 Trend, Percentage Collected: Connecticut Lottery, 1972–2002 122
Table 8.8 Trend Equations: Annual Contributions to the State of Connecticut, 1993–2005 123
Table 8.9 Seasonal Indices (Sales): Foxwoods and Mohegan Sun, Monthly, 1993/1997–2005 123
Table 8.10 Trend: Connecticut Casinos—Total Handle, Total Collected 124
Table 10.1 A Framework for Evaluating the Privatization Process 149

FIGURES

Figure 5.1 Revenue Sharing between States and Native American Casinos 67
Figure 6.1 Gambling Revenue Forecasts: Where Would the Money Come From? 90
Figure 7.1 St. Louis Metropolitan Area Casino Market 98
Figure 7.2 St. Louis Market Share Analysis 99

Acknowledgments

One of the public figures whose attitude toward gambling has fascinated me for over 15 years is Thomas Jefferson. As the epigraph indicates, Jefferson was quite conflicted about gambling. Although he argues that society can advance only if individuals are willing to take risks, he also realizes that many risk-takers have a tendency to lose their ability to judge that risk and thereby not only get themselves into trouble but also cause their families to suffer. So I need to state that my own attitude toward gambling has much in common with Jefferson's.

I have been quite fortunate over the years to share my ambivalence about gambling with a number of extremely bright students at Boston College, in my statistics, forecasting, and business policy classes. Without the students in these classes challenging me to think of various ways in which gambling issues could be approached, this volume would not have been possible.

A number of students have served as research assistants for this volume. Ryan Muldowney was the primary research assistant for chapter 1, on the current shape of the gambling industry, and as usual, Ryan had some interesting observations to share on the gambling industry overall. Mike Spinello did yeoman work on the chapter that covers the Internet gambling issue. Chris Robinson spent hours collecting data as well as cataloging numerous sources on the Native American gambling phenomenon. The sports gambling chapter was made possible through the work of Matt Breaux. Brian Muller, a native of the St. Louis area, facilitated the chapter on the location of a casino in St. Louis, whereas Brian Kang, a Connecticut native, did the research for the New England gambling chapter. Matt Becker toiled through a number of articles for the Macau chapter.

Finally, I'd like to thank Peter Kim for checking the references and citations. A special thanks to Matt Raffol for compiling the index as well as rereading the chapters in order to ensure that students would find them somewhat interesting!

Of course, any deficiencies in this book can be attributed solely to me. I hope that readers will be inspired to investigate further the various aspects and problems that make the gambling industry such a fascinating—and always timely—subject for discussion and further research.

Introduction

This is the third book that I have written about the gambling industry. Each of these volumes has taken a very different look at the industry. But taken together, all of them illustrate how gambling as a public policy issue has evolved over the 20-plus years that I have been studying the industry.

The first book, *State Lotteries and Legalized Gambling* (Greenwood Press, 1994), analyzed the rise of the lottery movement in the United States. In 1964 New Hampshire became the first state to operate a lottery since the Civil War era. The rationale behind this lottery was an attempt to raise revenue while avoiding the politically unpopular imposition of either a state income tax or a sales tax. New Hampshire's would become a familiar scenario, played out throughout the country, for the one constant refrain used by state officials to justify entering into the lottery business was the lottery's ability to obtain revenue for state operations without the imposition of either new taxes or tax increases. Thirty-seven states, along with the District of Columbia, have followed New Hampshire into the lottery business. The book nevertheless concluded that, because of this search for revenue, the lottery boom was ending, and a new era in the gambling industry was about to commence.

My *States and the Transformation of the Gambling Industry* (Edgar Press, 2001) described the rise of casino gambling in the United States. In 1975 New Jersey legalized casino gambling in Atlantic City as a means to revitalize that city as a tourist attraction and, of course, to raise revenue to support various benefits for the elderly throughout New Jersey. But this development did not spark a nationwide movement to legalize casino gambling in the way that New Hampshire's institution of its lottery ignited the lottery movement across the country. In 1993, however, two events did result in a boom for casino gambling. First, Iowa permitted riverboat gambling for towns on the Mississippi River. Many other Midwestern states followed Iowa's lead, and they are still competing with each other for this revenue source. But the biggest development was the establishment of the Foxwoods Native American casino in Connecticut. Although Native Americans had been permitted to operate casinos on their tribal lands since 1988, it was Foxwoods that established what a potent source of revenue Native American casinos could be, not only for the tribes but also for the states that negotiated with them what games would be permitted. *States and the Transformation of the Gambling Industry* chronicled the march of casino gambling into 27 states, recounting how casino gambling replaced lotteries as the chief form of gambling in the United States. This book also included statistical analysis investigating whether casino gambling could be as consistent a source of revenue for the states as lotteries and how states were beginning to develop overall gambling strategies.

So, six years later, why write another book on gambling? Is the gambling industry facing any new or unique issues that were not studied in the previous books? Well, the answer to that question is a definite yes! Despite its phenomenal growth over the past 40 years, gambling is still a controversial public policy issue. Public policy officials are still divided over whether to permit additional gambling and over the best means to regulate it—and, of course, profit from it.

This book differs significantly from my previous attempts to examine the gambling industry. Unlike my previous books, which featured statistical analysis examining the effectiveness of gambling revenue as a part of public financing, this current volume features a series of case studies. The book's goal is to permit readers to debate the merits of additional gambling from the points of view of the various stakeholders, such as government officials, gambling industry executives, and, of course, the gambling public.

The first of the book's three parts consists of two chapters. Chapter 1 gives the reader an insight into the current state of gambling in the United States, emphasizing the newest segments of the gambling industry. Chapter 2 contains a brief history of the various debates that have surfaced over gambling during the past few years and analyzes the ethical debate confronting public policy makers as they legislate for the gambling industry. Two ways of analyzing ethical issues are delineated, namely, the "ethics of sacrifice" versus the "ethics of tolerance." The reader is asked to consider how these two ways of examining ethical issues lead to very different attitudes toward the overall gambling issue. Finally, this chapter contrasts the gambling issue with the controversy surrounding the tobacco industry. Using the concepts of the ethics of sacrifice and the ethics of tolerance, the reader will be able to determine why the gambling industry has been able to survive many attacks on it whereas the tobacco industry seemingly has forfeited any public policy support.

Part II of the book focuses on issues that are emerging as the public debate on gambling continues. Three issues are analyzed: Internet gambling, sports gambling, and Native American gambling. All of these issues have been subjected to legislation on international, national, and local levels of government; clearly they will remain controversial parts of the entire gambling scene well into the future.

Chapter 3 examines the intense controversy surrounding Internet gambling. In many ways the controversy surrounding Internet gambling captures all of the issues that have made gambling so controversial. There is the addiction issue; there is the issue of underage gambling. How does government regulate this type of gambling? Even more important (in the eyes of many), can government raise revenue from Internet gaming? For many national governments (the United States, France, and most of the countries of the European Union), the solution to Internet gambling is simply to outlaw it. But these bans have been challenged before the World Trade Organization and by other legal means. Even the casino industry is split over the issue; Harrah's, the biggest casino operator in the world, is opposed to Internet gambling, but MGM, the second-largest casino firm, had a Web site in place ready to take Internet gambling bets. This segment of the gambling industry, too, will be a challenge to public policy officials for the foreseeable future.

Sports gambling is a form of gambling that has divided the various levels of government, yet legalization is firmly opposed by all of the professional leagues as well as by the National Collegiate Athletic Association. Chapter 4 provides a brief history of the prohibitions leveled against sports gambling. In recent years the federal government has led the charge against it, going so far as to outlawing any betting on collegiate sports. At the state level, however, many states (such as Delaware and New Jersey) are investigating the possibility of legalizing sports gambling in order to protect their gambling revenue. As a result, some states are suing the federal government in order to establish that their right to offer sports gambling supersedes any federal prohibition. Once again, this controversy involves revenue, but it also brings up issues of states' rights versus federal law. One unique argument that advocates of sports gambling have utilized is that legalizing sports gambling will cripple organized crime, which is now the primary source and beneficiary of illegal sports betting.

Chapter 5 investigates the Native American casino gambling controversy. In 1988 Congress passed a law that permitted Native American tribes to establish gaming facilities on federally recognized reservations, allowing them to offer those games that the states in which their reservations were located permitted nonprofit organizations to offer on "casino" nights. The legislation required states to negotiate with the tribes. This requirement led to many court tests in order to determine whether the federal government could require states to negotiate with tribes and whether states could profit from these negotiations by requiring tribes to contribute a certain portion of gambling revenue to the "host" states. But the controversy that continues to rage is whether Native American tribes can use proceeds from their tribal casinos to bankroll casinos or gambling sites in other states. In reaction to this development, the U.S. House of Representatives passed legislation to make these actions illegal, but the U.S. Senate has not followed suit. Meanwhile, in a search for revenue, states are negotiating with their tribes. So the controversy surrounding Native American gambling continues, and the success of Native American casinos has prompted calls—especially by operators of private casino firms—for these enterprises to be reexamined.

Part III examines all of the factors that public policy officials need to weigh when they consider expansion of gambling in their jurisdictions. Chapter 6 develops a model of such factors. Once again, the reader is given the opportunity to select those factors that ought to be emphasized as public policy officials contend with the issue of expanding gambling.

The following three chapters offer actual case studies, presenting the reader with policies or choices associated with various facets of the gambling industry. The first case, in chapter 7, describes the Missouri State Gambling Commission's deliberations regarding the appropriate location for a casino in the St. Louis area when confronted with conflicting needs for revenue and for economic development. Finally, the commission had to choose the casino firm that would offer the best opportunity to fulfill the commission's desires.

Chapter 8 explains the dilemma of Massachusetts governor Deval Patrick, who took office in January 2007 facing a one billion dollar deficit. He needs to decide whether to resort to gambling as a way of raising additional revenue to balance his budget. The two major competitors for Massachusetts's gambling revenue are Connecticut and Rhode Island. The gambling policies and revenues of each of these states are presented, along with their possible responses to any gambling initiative that Massachusetts might enact. The reader is asked to choose among various options and justify their choices to Governor Patrick.

Macau's rapid rise in the world of gambling is the focus of chapter 9. Although Chinese officials have dreams of turning Macau into the "Las Vegas of the East," the island faces numerous problems as well as opportunities. Just how far this expansion should go and how the Chinese authorities should regulate this explosion of gambling activity within its borders are the questions presented to the reader at the end of this chapter.

Finally, chapter 10 challenges the reader to summarize his or her attitude toward the gambling problem by responding to the privatization of lotteries and casinos. Recently, Illinois, Texas, and other states have moved toward privatizing their lotteries. In Canada, legislation has been filed to privatize casinos previously operated by provinces. The overarching questions of this chapter are as follows: What should be the role of government in regard to gambling? Can the regulator regulate itself? Is gambling an industry in which a firm should aim only to maximize profits?

Overall, I hope that this book will enable the reader to analyze for him- or herself the many complex issues that gambling represents and, at the same time, give the reader confidence that it is possible to make a positive contribution to the policy debates surrounding gambling.

Part I

INTRODUCTION

1

The Current Climate of Gambling in the United States

> A look at how gambling revenues stack up against revenues from other recreational/leisure time activity sectors reveals not only that the gambling revenues outweigh both music sales and movies combined, but also that the gambling industry is the only one of the industries in this study to have shown consistent growth in each of the last three years.
>
> —Joseph Greff, "U.S. Gambling" (Bear, Stearns, January 2005)

With a few notable exceptions, it is a great time to be in the gambling industry. The year 2005, for example, was a record-breaking one for Las Vegas casinos, which took in $11 billion from gamblers in casino revenues—excluding hotel, restaurant, and bar revenues.[1] In 2004 alone, U.S. gamblers spent $78.6 billion dollars on commercial gambling, a 7.6 percent increase over the year before.[2] Lottery sales increased by an average of 12.5 percent throughout the United States.[3] Tribal gambling and Internet gambling experienced double-digit growth, a rate not seen anywhere else within the gambling industry.

But can discussions about the gambling industry be painted in such broad, sweeping terms? Can one really talk about "the" gambling industry as a whole without generalizing to the point that trends become half-truths and facts and figures become meaningless? What similarities are there between an Internet sports book based on the Isle of Man and the Massachusetts state lottery's daily operations? Given the explosive rate of growth in Internet gambling and the gradual decline of horserace betting, can one ignore the fact that the various segments within the industry are at different stages in their life cycles and should therefore expect very different opportunities and threats in coming years? It is obvious that each segment deserves (or, more accurately, demands) its own assessment in order for any analysis to be fully developed, relevant, and—most important—meaningful.

There are, however, recurring themes that weave throughout each segment of "the" gambling industry and that merit special attention. The most obvious, and perhaps most important, of these themes is that of regulation. Regardless of what type of gambling is being discussed—be it Internet poker, slot machines in Vegas, or a sports book in the United Kingdom—each and every one of these various business enterprises faces some sort of regulation. In some instances, regulation creates state-held monopolies through special gambling licensing. In other jurisdictions more lax regulations allow for numerous firms to compete for consumer dollars. Finally, in the United States, ambiguous legislation and inconsistent activity by the courts regarding Internet gambling create a legal "gray area." In this type of environment, sites enjoy a surplus of consumers and a scarcity of competitors, often resulting in huge profits for the more daring Internet gambling site operators.

Monopolies in the industry, however, are becoming things of the past. A second recurring and universal theme throughout "the" gambling industry is increasing levels of competition. The forms in which this competition manifests itself are as diverse as ever. California's tribal casinos now compete with the Las Vegas Strip. Las Vegas bookmakers compete with Internet sports books based in the United Kingdom. These Internet sports books diversify their product offerings and allow users to play poker online, competing with other Internet poker sites. In many instances, gambling operators compete not only with other operators within the same segment (for example, a casino competing with another casino), but with *every other form of gambling readily available to its customers.*

INTERNET GAMBLING

The rise of Internet gambling has been the primary driver of the intensifying levels of competition within the industry. No longer is consumers' ability to place wagers limited by their geographic proximity to gambling operators (nor, in some instances, are they limited by the legislation of their country's jurisdiction—for example, China). Internet gambling operators can serve a truly global customer base, and with the financial barriers to entry relatively low in comparison with the huge profits being reaped through Internet gambling, new entrants can enter at will and attempt to compete with the market leaders. As discussed earlier, these online operators compete not only with each other, but with traditional land-based operators as well. Although both land-based and Internet gambling operators have done fairly well in recent years, given the explosive growth and successful initial public offerings (IPOs) of several online-only firms, it appears that the Internet sites will ultimately come out ahead. Indeed, players in the gambling industry must be ready to compete in the "borderless global marketplace the Internet has created."[4]

Regardless of what segment of the gambling industry a particular firm is involved in, be it market leader or new entrant, no firm can afford to underestimate the impact that the Internet will have on its business. Internet gambling has revolutionized the gambling industry, and what we have seen thus far is only the tip of the iceberg. Estimates vary, but for discussion's sake, one expert estimates that consumers spent over $8 billion on Internet gambling in 2004, and he expects that number to more than triple by the end of the decade.[5] Although this sum represents only a small portion of global expenditures on commercial gambling, certain indicators point toward a bright future for Internet gambling operators. A case in point: PartyGambling plc, operator of PartyPoker, executed a highly successful IPO and listed on the London Stock Exchange with a market cap of almost $8.5 billion. These shares have appreciated significantly since then, and PartyGambling now has a market capitalization larger than Harrah's Entertainment.[6] In light of the fact that Harrah's Entertainment is the world's largest casino operator, the true potential of Internet gambling has become apparent.

The landscape of the online gambling industry is undoubtedly the most challenging to navigate of any of the gambling industry's segments. In no other segment must an operator navigate such a web of legislative snarls or compete so ferociously for revenues. Unlike for traditional land-based gambling operators, for online casinos, poker tables, and bookmakers, barriers to entry are extremely low. With relatively little initial capital, a firm can purchase third-party software at minimal cost (royalties included) and apply for a license in any of a number of jurisdictions throughout the world. As a result, "given the portability of pure online services,"[7] jurisdictions now compete to draw online operators, resulting in attractive tax regimes for firms willing to be flexible in their location. This leads to increasing levels of competition for consumers, driving up marketing spending. The added complexity of the various legal issues regarding the jurisdiction of the consumers themselves further muddles the legal waters.

A comprehensive discussion of the various issues surrounding Internet gambling appears in chapter 3, but the following is a short summary. Current legislation in various countries runs the gamut from complete prohibition of Internet gambling to its legalization and regulation. In the United States, the Department of Justice (DOJ) holds that all Internet gambling is illegal, under the 1961 Federal Wire Act, which prohibits bets made over telephone and other "wires."[8] Although the DOJ has no intention of prosecuting casual gamers, it is adamantly opposed to allowing firms located within U.S. jurisdiction to run online gambling sites. Harrah's and MGM Mirage, for example, both formed Internet casinos, only to shut them down under pressure from the DOJ.[9] The DOJ's strategy has been to put pressure on financial intermediaries, fining them for processing illegal online gambling transactions. For example, the DOJ fined PayPal $10 million in 2003 for such violations.[10]

Interestingly enough, the legality of certain actions by the Department of Justice in restricting online gambling subsequently came under scrutiny. A case filed by the island of Antigua, a small Caribbean center for offshore Internet gambling, charged that the Department of Justice had restricted the "cross border supply of gambling and betting services" in violation of U.S. obligations under the General Agreement on Trade in Services (GATS) and World Trade Organization (WTO) regulations. The outcome proved ambiguous, with both sides claiming victory. Nevertheless, it appears that the United States ultimately will have to acquiesce to the WTO ruling—either through "total prohibition, including currently legal forms of online gambling . . . or liberalization [*sic*] and permissive regulation of online gambling."[11]

Unlike U.S. legislation, legislation within the United Kingdom was updated following passage of the Gambling Act in 2005. Although online betting had not previously been illegal in the United Kingdom, the Gambling Act explicitly legalized online gambling and clarified a number of issues regarding advertising to the U.K. audience.[12] But although the United Kingdom's stance on Internet gambling is quite clear (permissive regulation), the greater European landscape is still divided. The 1957 Treaty of Rome established free trade principles regarding services, yet the European Court of Justice "has wrestled with the conflicting claims of member state laws predicated on sovereign power over gambling and free trade principles."[13] The political structure and conflicting interests of greater Europe are immeasurably complex, but research analysts at Deutsche Bank believe that the European market ultimately "will open up to cross-border online gambling . . . through rulings from the EU (European Union) courts rather than through a directive."[14]

Regardless of the short-term developments in global regulation, the expansion of Internet gambling is inevitable in the long term. The blistering growth rates of online revenues, seemingly endless consumer demand, and market capitalization figures usually reserved for blue-chip stocks all point in one direction: Internet gambling will continue to grow as more firms enter the industry and cater to "an audience that is discovering that it actually quite enjoys casual gambling."[15] In regard to the future of Internet gambling, the competition will eventually be whittled away until, as the industry matures, only the most successful operators remain. Consolidation is also likely as smaller sites are bought up by major firms, several of which, after very successful IPOs, now have plenty of acquisition currency.

What, therefore, is in store for traditional land-based gambling operators, given the unfettered explosion of Internet gambling in the United States—despite legislation aimed at preventing American gamers from utilizing online services? Like many things in life, it all depends on whom you ask, and even then, the answer you get today is likely to change over the course of the next few years. One study that analyzed the relationship between the increasing prevalence of Internet gambling and states' casino revenues came to the conclusion that "Internet gambling has not had a statistically significant negative impact on the gambling revenues of . . . Nevada and New Jersey."[16]

Yet by the close of this first decade of the twenty-first century, the advent of Internet gambling will have had a significant impact on traditional land-based revenues, negatively *or positively.* One scenario foresees Internet gambling reducing revenues through a substitution effect. The U.K. Treasury currently holds a different view, stating that the "assumption of a substitution effect between traditional based gambling offerings and remote gambling is false. Remote gambling is a unique customer experience."[17] Although the experience is indeed different, this does nothing to imply that casual gamers will not choose one form of entertainment over the other. Internet gambling cannot replicate the experience of a weekend in Vegas, but online gambling sites offer betting services from the home. For consumers looking only to place a bet—with no interest in luxurious hotels, restaurants commanded by world-renowned chefs, or bustling nightlife—the online gambling experience may be preferable to what traditional casinos have to offer. In order to succeed in a post-Internet environment, casinos and other traditionally based gambling operations will have to evolve from being merchants of gambling services to merchants of *entertainment* services. This process has already begun, with certain casinos on the Las Vegas Strip earning less than half their revenues from gambling activities. If online gambling does negatively impact traditional operators, those operators will have to adapt their product offerings in order to replace lost revenues.

A second possible outcome scenario would find Internet gambling actually benefiting traditionally-based games operators. Internet gambling—online poker, specifically—has introduced a record number of Americans to casual gambling. The stigma attached to gambling by moral authorities is diminished every time a consumer visits an online gambling site. The trend was started when Las Vegas shed its image as a seedy gambling hotspot and began to be perceived as a more family-friendly destination. What the Internet has done is accelerate a shift in public opinion about gambling as a form of leisure, from a vice to an acceptable, and oftentimes enjoyable, pastime. Should this scenario hold true, casinos would see increases in their gambling revenues *as well as* in their other operating revenues. According to this "rising tide lifts all boats" view, casinos would see not only higher room occupancy rates *but also a greater percentage of guests actually sitting down to play at gambling tables.* Not only is there the opportunity to draw more people to casinos and other traditional gambling sites, but the opportunity also exists to encourage them to gamble more. Whereas Americans spend an average of 1 percent of after-tax earnings on gambling, Australians, for example, spend approximately 3.5 percent on gambling.[18] Clearly, the market for American gambling services is far from saturated.

For horseracing in particular, with declining purses caused by years of declining race attendance, Internet gambling may be the last hope for survival. Simulcast races and off-track betting offer two ways to stimulate the sluggish industry by increasing purse sizes. Not everyone is embracing Internet gambling, though. Betting exchanges, which operate by matching a gambler who sets odds with another willing to take the bet (the operator of a betting exchange site takes no risk), can offer better prices than traditional bookmakers. Traditional bookmakers must manage their risk exposure and are also subject to higher taxes. Therefore, traditional bookmakers are unambiguously harmed by the existence of betting exchanges because betting exchanges reduce the margins bookmakers can hope to earn.

To say that the Internet has revolutionized the gambling industry is far from an overstatement. If anything, the word "revolution" has been so overused that it fails to capture the tremendous impact Internet gambling will have on the industry for years to come.

NATIVE AMERICAN GAMBLING

Although online gambling has taken the globe by storm, it is not the only segment of the gambling industry to experience double-digit growth in recent years. Within the United States, gambling ventures operated under the Indian Gambling Regulatory Act have proven highly lucrative for Native American tribes as well as for investors lucky enough to have gotten in on the action. Collectively, the tribes now have the largest gambling industry segment in the United States, having surpassed the gross gambling revenues of the state of Nevada in 2001.[19] The climate of tribal gambling in the United States has become increasingly political, a fact that will shape the future of tribal gambling to come.

The most heated political debates revolve around tribal recognition and off-reservation casinos. Formal recognition of a tribe's legitimacy can mean the difference between financial success and poverty, and the political maneuverings employed by tribes seeking recognition, the investors backing them, casino operators, and other tribes who fear competition demonstrate the varied interests at play in tribal gambling. In 2005, the U.S. Senate Committee on Indian Affairs met to discuss the recognition process for Indian tribes. As one commentator noted, "Connecticut's governor, both its senators, and three of its congressmen showed up to testify on a matter none would have cared much about a decade or so ago."[20] Connecticut already has two well-established tribal casinos, and those in office are not interested in a third.

Senator John McCain, who then chaired the Senate committee, noted that wealthy investors have a vested interest in helping tribes win recognition because the tribes would, in turn, provide the investors with profitable investment opportunities.[21] Indeed, lobbying expenditures by tribes—whose poverty-stricken members are purportedly among the poorest in America—can total in the millions of dollars. As a matter of illustration, the Schaghticoke tribal nation spent approximately $12 million in its efforts for recognition, financed in part by the founder of the Subway restaurant chain, and the Eastern Pequots of Connecticut were supported financially by none other than Donald Trump.[22] Although it would be nice to consider these acts as particularly altruistic, partnering with Native American casino operators can prove highly profitable. Witness a recent partnership between the Creek Indians and Harrah's Entertainment Inc. in trying to expand gambling in Rhode Island.[23]

Off-reservation casinos are also a hot-button issue within the scope of tribal gambling. Whereas landless tribes maintain that restricting off-reservation gambling deprives them of opportunities to raise their socioeconomic status by opening a casino, opponents of off-reservation casinos, led by Senator McCain, argue that Congress (in passing the Indian Gaming Regulatory Act in 1988) never intended for Native Americans to build off-reservation, Vegas-style casinos.[24] Opposition can even come from a seemingly unlikely source—other Indian tribes. Many tribes oppose off-reservation casinos strictly for fear of competition with their own tribal casinos.

Future prospects for Indian gambling are similar to those for traditional land-based casinos and other gambling sites. Although rapid expansion continues, the market segment is already showing signs of slowing growth rates as tribal casinos face increased competition from private casinos, state-run gambling operations, online gambling sites, and other tribal casinos themselves. As tribal casinos become established in their marketplace, fewer tribes will seek to enter a saturated market, especially if casinos are restricted to reservations not frequented by the majority of the public. Though tribal gambling's fantastic rate of growth has been second only to that of Internet gambling, according to one economist, the "double-digit growth is over."[25]

THE EXPANSION OF GAMBLING BY STATES: SLOTS, SPORTS GAMBLING, AND PRIVATIZATION

The final segment of the gambling industry to be discussed is the state of gambling at traditional gambling operations within the United States, including casinos, lotteries, and slot machines. As mentioned at the opening of this chapter, 2005 was a banner year for brick-and-mortar casinos throughout the country. Despite the threat posed by Internet gambling and tribal gambling, casinos in Las Vegas and Atlantic City are positioned to continue their financial success of recent years into the near future. The gambling industry as a whole will benefit from a favorable demographic shift in the U.S. population. "The average gambling patron is 49 years old, placing the average U.S. gamer in an age category that is growing three times faster than the overall U.S. population."[26] It is also noteworthy that the Las Vegas Strip tends to be a supply-driven economy, in that increasing the number of rooms available in effect increases the demand for said rooms. With the addition in 2005 of the $2.7 billion Wynn Las Vegas, revenues from the hotel side of Vegas casinos could reach an all-time high.

Moving away from Las Vegas, casinos become less about profits and more about tax revenues. Permitting slot machines has become a favorite tactic of legislators seeking to raise revenue for state treasuries without raising taxes. Oftentimes, states vie for each other's residents' gambling dollars, building casinos just across their borders in hopes of luring revenues from out of state. As an example, Maryland is currently considering the legalization of slot machines in the state. James Browning, former executive director of Common Cause Maryland, which oversees campaign spending by the gambling industry, makes a deft comparison:

> If you look at the other states, Pennsylvania got slots. West Virginia is talking about table gambling. It's like an arms race between the states, and campaign contributions and lobbying expenditures are the weapons to win.[27]

Although the analogy may seem a bit overblown, it does bring to light an underlying theme of state-run gambling. The initial success of many of the first movers was a result of an inflow of out-of-state money into state-run casinos. Indiana, for example, has taken advantage of differences in legislature by allowing riverboat gambling near the border of two states that do not, those states being Ohio and Kentucky.[28] In effect, Ohio and Kentucky residents are subsidizing lower taxes for residents in Indiana—a politician's dream come true.

In a similar vein, states such as New Jersey are considering legalizing sports gambling in order to protect their current flow of gambling revenue. In 1976

New Jersey became the first state besides Nevada to legalize casino gambling. Casino gambling was confined to Atlantic City in the hope that Atlantic City would recover some its cachet as a resort community. It has been a success in that Atlantic City is the second-largest casino gambling market in the United States, yet Atlantic City casino gambling has experienced slow growth from 2001 to 2006. With bordering states such as Delaware, Pennsylvania, and New York permitting slot machines at racetracks as well as other venues, Atlantic City's prospects appear bleak. Hence, legalized sports gambling is seen as the newest weapon in New Jersey's arsenal to protect its gambling revenues by reinvigorating Atlantic City as a casino destination. This is a highly controversial move on New Jersey's part. Many professional sports leagues, such as the National Football League and the National Basketball Association, as well as the National Collegiate Athletic Association, are adamantly opposed to legalizing sports betting.

Finally, the state of Illinois, among others, has proposed selling its lottery to private operators. Currently, the state lotteries are owned and operated as government agencies. This proposal does gives rise to two series of questions: (1) Why should government have a monopoly over lotteries? Isn't our entire economy built on the merits of competition? Wouldn't the bettor be better off with competitors offering a variety of games and odds? and (2) Why is gambling regulated by government at all? If so, what is the appropriate amount of regulation, and can government really regulate an industry from which it draws so much revenue?

Of course, all of the these questions have one common denominator: revenue! As the reader proceeds to examine all of the various facets of gaming, tables 1.1–1.3 should provide an idea as to why gambling has been become such an important topic for public policy officials.

Although the threads of competition and regulation run through any discussion regarding any segment of the gambling industry, it is a daunting task to make any statement summarizing the present climate or future outlook of "the" gambling industry, for the industry is manifested in many distinct forms. What *can* be said about the gambling industry in its entirety is that each part is connected to the whole more deeply than ever before. Consumers enjoy gambling, and firms are just scratching the surface in terms of developing innovative service offerings to cater to the gambling public. Yet although the public enjoys additional forms of gambling, opposition to the expansion of gambling remains quite strong.

This chapter has focused on the current state of the various segments of the gambling industry, on why states compete for expanded gambling revenues, and on the forces expected to shape how that competition will take place. The next chapter develops the ethical concerns that public policy officials

Table 1.1
State Prohibitions on Gaming

State	*Lottery*	*Casino/ Resort*	*Native Casino*	*Video Lottery Terminals*	*Betting Tracks*
Alabama	No	No	Yes(3)	Yes	Yes
Alaska	Yes (non-profits)	No	No	No	No
Arizona	Yes	Yes	No	Yes	Yes
Arkansas	No	No	No	No	No
California	Yes	Yes	Yes	Yes	Yes
Colorado	Yes	Yes	Yes	Yes	Yes
Connecticut	Yes	No	Yes(2)	Yes	Yes
Delaware	Yes	No	No	Yes	Yes
Florida	Yes	Yes	Yes(4)	No	Yes
Georgia	Yes	No	No	No	No
Hawaii	No	No	No	No	No
Idaho	Yes	No	Yes(1)	Yes	No
Illinois	Yes	Yes	No	Yes	Yes(?)
Indiana	Yes	Yes	No	Yes	Yes
Iowa	Yes	Yes	Yes	Yes	Yes
Kansas	Yes	Yes	Yes(4)	Yes	Yes
Kentucky	Yes	No	No	No	Yes
Louisiana	Yes	Yes	Yes(3)	Yes	Yes
Maine	Yes	No	No	No	Yes
Maryland	Yes	No	No	No	Yes
Massachusetts	Yes	No	No	No	Yes
Michigan	Yes	Yes	Yes	Yes	Yes
Minnesota	Yes	No	Yes(18)	Yes	Yes
Mississippi	No	Yes	Yes	Yes	Yes(?)
Missouri	Yes	Yes	No	Yes	No
Montana	Yes	No	No	Yes	No
Nebraska	Yes	Yes	Yes(1)	Yes	No
Nevada	No	Yes	No	Yes	Yes
New Hampshire	Yes	No	No	No	Yes(4)
New Jersey	Yes	Yes	Yes	Yes	Yes
New Mexico	Yes	Yes	Yes(7)	Yes	Yes(4)

Table 1.1 *(continued)*

State	*Lottery*	*Casino/ Resort*	*Native Casino*	*Video Lottery Terminals*	*Betting Tracks*
New York	Yes	Yes	Yes(2)	Yes	Yes
North Carolina	No	Yes	Yes(1)	Yes	No
North Dakota	No	No	Yes(4)	Yes	No
Ohio	Yes	No	No	No	Yes(7)
Oklahoma	No	No	Yes(4)	No	Yes
Oregon	Yes	No	Yes(6)	Yes	No(?)
Pennsylvania	Yes	No	No	No	Yes(4)
Rhode Island	Yes	No	No	Yes	Yes
South Carolina	Yes	No	No	No	No
South Dakota	Yes	Yes	Yes(10)	Yes	No(?)
Tennessee	Yes	No	No	No	Yes
Texas	Yes	No	Yes(2)	No	Yes
Utah	No	No	No	No	No
Vermont	Yes	No	No	No	Yes
Virginia	No	No	No	No	No
Washington	Yes	Yes	Yes(20)	Yes	Yes
West Virginia	Yes	No	No	Yes	Yes(4)
Wisconsin	Yes	No	Yes(17)	Yes	No(?)
Wyoming	No	No	No	No	Home Only

Sources: http://www.gamblingandthelaw.com and http://www.naspl.org.

need to take into account before they develop a coherent gaming strategy for their states. How states formulate and implement these strategies will, of course, determine whether they are successful in achieving the goal of a delicate balance between the revenue needs of the state and the social costs that invariably accompany the expansion of gambling activity.

Table 1.2
Gambling Taxes (Millions) Collected by States (2005)

State	*Lottery*	*Casino/ Resort*	*Racino*	*Charitable*	*Pari-Mutuel*	***Total***
Alabama	0	0	0	0	0.5	0.5
Alaska	0	0	0	0	0	0
Arizona	104.57	0	0	5.61	0.64	110.82
Arkansas	0	0	0	0	2.59	2.59
California	945.16	0	0	20.72	37.43	1,003.31
Colorado	93	95.6	0	4.68	0.52	193.8
Connecticut	270.37	0	0	1.36	4.52	275.93
Delaware	32.87	0	175.7	0.09	0.24	208.89
Florida	1,178.36	0	0	4.95	8.91	1,192.23
Georgia	768.16	0	0	1.1	0	769.25
Hawaii	0	0	0	0	0	0
Idaho	20.7	0	0	0	0.47	21.17
Illinois	578.08	719.9	0	9.21	12.01	1,319.20
Indiana	188.47	702.7	0	0	4.12	895.28
Iowa	48.85	141.3	68.4	1.18	0.19	259.93
Kansas	63.43	0	0	1.33	1.65	66.41
Kentucky	187.66	0	0	14.12	5.6	207.58
Louisiana	119.25	517.66	76.7	4.57	4.83	723.01
Maine	44.02	0	0	0	1.74	45.77
Maryland	464.59	0	0	5.75	1.89	472.23
Massachusetts	971.78	0	0	4.15	0.98	976.90
Michigan	609.75	250.2	0	12.59	11.87	884.41
Minnesota	79.17	0	0	25.26	0.17	104.60
Mississippi	0	325	0	2.7	0	327.70
Missouri	214.74	377.2	0	2.89	0	594.82
Montana	7.01	46.13	0	0.09	0.1	53.33
Nebraska	62.13	0	0	2.32	0.76	65.21
Nevada	0	776.5	0	0.34	5.01	781.85
New Hampshire	71.28	0	0	3.52	2.14	76.94
New Jersey	824.2	414.5	0	4.81	0	1,243.50

Table 1.2 *(continued)*

State	*Lottery*	*Casino/ Resort*	*Racino*	*Charitable*	*Pari-Mutuel*	***Total***
New Mexico	32.86	0	37.7	0.72	0.64	71.92
New York	2,144.51	0	n/a		27.85	2,172.35
North Carolina	0	0	0	0.89	0	0.89
North Dakota	0	0	0	5.39	4.01	9.40
Ohio	580.66	0	0	22.49	10.08	613.23
Oklahoma	0	0	0	2.15	3.33	5.48
Oregon	68.97	0	256.66	0	0.76	326.40
Pennsylvania	519.19	0	0	6.14	19.71	545.04
Rhode Island	69.75	0	188.8	0.41	3.26	262.22
South Carolina	0	0	0	3.87	0	3.87
South Dakota	6.25	11.6	138.93	0.64	0.18	157.61
Tennessee	0	0	0	0	0	0.00
Texas	1,004.74	0	0	16.85	3.38	1,024.96
Utah	0	0	0	0	0	0.00
Vermont	20.52	0	0	0.28	0	28.80
Virginia	377.58	0	0	0	2.29	379.88
Washington	63.82	93.42	0	6.1	1.84	165.18
West Virginia	54.35	0	324.6	0	1.02	379.97
Wisconsin	120.21	0	0	2.93	0	123.15
Wyoming	0	0	0	0.59	0.18	0.76
Totals	**$13,088.70**	**$4,471.80**	**$1,267.50**	**$202.80**	**$187.10**	**19,217.70**

Sources: “Insight,” *Christiansen Capital Advisors,* August 2005, http://www.cca-1.com; http://www.naspl.org.

Table 1.3
Gambling's Contributions to State Finances

State	*Gambling Revenue*	*Total Revenue*	*Percentage*
Alabama	$0.50	$5,585	0.01
Alaska	0	2,471	0
Arizona	110.8	6,031	1.84
Arkansas	2.6	3,251	0.08
California	1003.3	79,412	1.26
Colorado	193.8	6,137	3.16
Connecticut	275.9	12,016	2.3
Delaware	208.9	2,918	7.16
Florida	1192.2	21,197	5.62
Georgia	769.3	16,383	4.7
Hawaii	0	3,923	0
Idaho	21.2	1,941	1.09
Illinois	1319.2	25,161	5.24
Indiana	895.3	10,446	8.57
Iowa	259.9	4,484	5.8
Kansas	66.4	4,260	1.56
Kentucky	207.6	7,444	2.79
Louisiana	723	6,662	10.85
Maine	45.8	2,564	1.78
Maryland	472.2	10,469	4.51
Massachusetts	976.9	23,363	4.18
Michigan	884.4	8,895	9.94
Minnesota	104.6	14,180	0.74
Mississippi	327.7	3,494	9.38
Missouri	594.8	7,669	7.76
Montana	53.3	1,322	4.03
Nebraska	65.2	2,622	2.49
Nevada	781.9	2,139	36.55
New Hampshire	76.9	1,336	5.76
New Jersey	1243.5	23,223	5.35
New Mexico	71.9	4,339	1.66
New York	2172.4	40,328	5.39
North Carolina	0.9	14,271	0.01

Table 1.3 *(continued)*

State	*Gambling Revenue*	*Total Revenue*	*Percentage*
North Dakota	9.4	870	1.08
Ohio	613.2	22,558	2.72
Oklahoma	5.5	4,687	0.12
Oregon	326.4	3,969	8.22
Pennsylvania	545	20,679	2.64
Rhode Island	262.2	2,735	9.59
South Carolina	3.9	5,040	0.08
South Dakota	157.6	891	17.69
Tennessee	0	8,126	0
Texas	1025	31,064	3.3
Utah	0	3,560	0
Vermont	20.8	884	2.35
Virginia	379.9	12,204	3.11
Washington	165.2	11,666	1.42
West Virginia	380	3,139	12.1
Wisconsin	123.1	10,772	1.14
Wyoming	0.8	768	0.1
Totals	19,217.70	523,548	3.67

Sources: *Statistical Abstract of the United States for 2004–05,* State Regulatory Agencies.

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2

Ethical Rationales Utilized in Public Policy: The Gambling and Tobacco Industries

The previous chapter laid out in some detail the enormous expansion of gambling that has taken place in the United States during the past 43 years. One of the questions asked throughout this book is this: why did this occur, and what were the rationales used by public policy makers as they went about their decision-making process?

Public policy makers have never been known for their consistency in addressing the various issues that confront them during the public policy process. Some observers maintain this inconsistency merely demonstrates the highly "irrational" nature by which policy decisions are achieved. However, these inconsistencies could very well have an explanation that goes far beyond the typical cost-benefit analysis that economists might utilize in what they would term a "rational" public policy decision. One area that could provide a handle on how the public policy process has evolved over the past 40 years would be an examination of the "ethical" reasoning that public policy makers employ as they go about the task of enacting legislation.

In order to demonstrate the importance of ethical reasoning in the public policy process and how ethical argumentation has changed over the past 40 years, this chapter analyzes the changes that have occurred in two of the so-called sin industries, namely, cigarettes and gambling.

THE CIGARETTE AND GAMBLING INDUSTRIES (1964 TO THE PRESENT)

The tobacco and gambling industries have both been subjected to increasingly intense public scrutiny over the past 40 years, with very different outcomes. It should be noted that both of these industries depend on the "tolerance" of public policy makers. The ethical thinking grounding public policy as it pertains to these industries has radically changed over the course of this period. It is this shift that has determined the profound difference in the fate of these two industries in the public policy realm.

The Cigarette Industry

In 1964 the Surgeon General of the United States published the now famous report that concluded that "cigarette smoking is a health hazard of sufficient importance in the United States to warrant remedial action."[1] It was with this simple conclusion that the cigarette industry began its endless battles with government officials at all levels and branches of government.

From 1964 to 1985, the U.S. Congress passed two significant measures that it hoped would curb cigarette sales: the Cigarette Warning Label Act of 1966 and the TV and Radio Cigarette Advertising Ban of 1971. Ironically, these measures did not have their intended effects. Cigarettes sales still increased throughout the period of 1964 to 1985 (although the rate of increase was less than the rate of increase prior to 1964). Why didn't these public policy measures have their intended effect? The following reasons ought to give the readers pause before they advocate various public policy measures to regulate the gambling industry.

First, although cigarette makers could no longer advertise, the groups opposed to cigarette smoking were no longer allowed free access to play their antismoking advertisements either. The antismoking advertisements had proved to be much more powerful in persuading current smokers to quit smoking than cigarette commercials had been in making cigarette smoking appear glamorous. Second, the cigarette warning label not only has been largely ignored by cigarette smokers (as is the case with alcohol warning labels), but also has provided cigarette makers with much comfort in their legal battles concerning their liability for the wrongful deaths of cigarette smokers.

Ironically, this period of renewed regulation of the cigarette industry resulted in higher profits: the industry spent significantly less on advertising, and the cigarette firms took the opportunity to diversify into the food industry, with, for example, Philip Morris's purchase of Miller Beer and General Foods and R.J. Reynolds's purchase of Nabisco.

On December 20, 1985, Surgeon General C. Everett Koop announced the results of research into the effects of "second-hand" smoke, or the passive smoking issue (ironically, more than 20 years later, there are still articles being written about passive smoking!).[2] The most controversial finding of this report was that there was a significant increase in the rate of lung cancer among nonsmokers in households where nonsmokers were living with cigarette smokers. This report sparked off a flurry in two areas: first, state legislators became extremely active in regulating where smokers could smoke, and second, excise tax increases became much more common and pronounced. Tables 2.1 and 2.2 illustrate this renewed interest in state regulation of the cigarette industry.

Table 2.1
State Excise Tax Policy (1990)

# of Prohibitive Laws Passed	*Low Level (2–20/pack)*	*Mid Level (21–49/pack)*	*High Level (50+/pack)*
0–5	Alabama Georgia Indiana Kentucky Mississippi North Carolina Tennessee West Virginia Wyoming	Arkansas New Mexico Texas	Arizona Wisconsin
6–11	Colorado South Carolina Virginia	Idaho Louisiana Minnesota Nebraska Nevada North Dakota Ohio Oklahoma Pennsylvania South Dakota	Alaska District of Columbia Hawaii Illinois Maryland Massachusetts Michigan New Jersey Oregon Rhode Island
12–14	Missouri Montana	Delaware Florida Iowa Kansas Vermont	California Connecticut Maine New Hampshire New York Utah Washington

Source: Data assembled from www.tobaccofreekids.org.

Table 2.2
State Excise Tax Policy (2002)

# of Prohibitive Laws Passed	*Low Level (2–40/pack)*	*Mid Level (41–60/pack)*	*High Level (61–150/pack)*
	Alabama	Arizona	
	Georgia	Indiana	
	Indiana	Texas	
	Kentucky		
	Mississippi		
	New Mexico		
	North Carolina		
	Tennessee		
	West Virginia		
	Wyoming		
6–11	Colorado	Minnesota	Alaska
	Idaho	Nebraska	District of Columbia
	Iowa	North Dakota	Hawaii
	Louisiana	Ohio	Illinois
	Oklahoma		Maryland
	Nevada		Massachusetts
	South Carolina		Michigan
	South Dakota		New Jersey
	Virginia		Oregon
			Pennsylvania
			Rhode Island
			Wisconsin
12–14	Delaware	New Hampshire	California
	Florida		Connecticut
	Missouri		Kansas
	Montana		Maine
			New York
			Utah
			Vermont
			Washington

Source: Data assembled from www.tobaccofreekids.org.

These two tables certainly demonstrate the powerful effect that the "passive" smoking issue had on state public policy makers. In terms of the number of smoking prohibition laws, the vast majority of states were prohibiting cigarette smoking in public places, and the only real battleground left for the cigarette industry was whether smokers could smoke in bars and restaurants. Even international airline flights now had banned all cigarette smoking.

The other striking aspect is the incredible increase in the excise tax rates. In 1990 the state excise tax rates on cigarettes ranged from $0.02 per pack to a maximum of $0.65 per pack. By 2002 three states had excise tax rates of $1.50 per pack! In fact, the average state excise tax rate on cigarettes increased from $0.32 per pack in 1990 to $0.68 per pack in 2002 and $1.00 per pack in 2005.[3] During the same period, the federal excise tax rate on cigarettes doubled from $0.16 per pack to $0.32 per pack. Although Congress and most state legislatures were heeding a call to lower taxes throughout the 1990s, it appears that cigarette excise tax rates were exempt from this trend. Even more startling was how powerless the cigarette industry was in fighting these increases. Clearly, public sentiment had turned against the cigarette industry.

The Gambling Industry

Just as 1964 became a landmark year for the U.S. cigarette industry, that same year became a landmark year for its cousin in the "sin" industries, the gambling industry. In 1964 the gambling industry began a revival that has not abated since. Prior to 1964 gambling was confined to two venues. In 1933 Nevada legalized casino gambling, establishing Las Vegas as the mecca of casino gambling. The other outlet was pari-mutuel betting on horse and dog racing, which portrayed itself as a sport. But overall, gambling was considered an unacceptable social activity. Table 2.3 provides a brief history of gambling in the United States.

In 1964 New Hampshire voters approved a state lottery. Lotteries had been socially acceptable in the colonial period of U.S. history and again in the post–Civil War era, but they had fallen out favor because of various scandals. The rationale used to justify the New Hampshire lottery is now a familiar one: proceeds from the lottery were to fund education, thereby averting the enactment of either a sales tax or an income tax in New Hampshire. In another familiar scenario, the lottery was declared a success because most of the tickets were purchased by customers who did *not* reside in New Hampshire.

But this lesson was not lost on New Hampshire's neighboring states. Over the next 10 years, every state in the northeastern United States approved a

Table 2.3
The Five Waves of U.S. Gambling

1st Wave (1607–1840s): State-Sanctioned Lotteries

Beneficiaries: Allowed private operators or colleges to operate lotteries in order to subsidize costs of capital improvements such as buildings or roads. Lotteries were given permission to operate only during the financing of the capital improvement. The lottery ceased operation after the completion of the project.

2nd Wave (1865–1890s): National Lotteries

Beneficiaries: Southern States offered prizes through the U.S. mail in order to gather funds to reconstruct roads and railways after the Civil War. These lotteries ceased operations following numerous scandals involving the private operators.

3rd Wave (1920–1964): The Golden Age of Horse Racing

Beneficiaries: With the advent of pari-mutuel betting machines, states permitted betting on "sporting" events such as horse and dog racing. Of course, the states received a percentage of the revenue in taxes.

4th Wave (1964–1993): The Golden Age of State Lotteries

Beneficiaries: In their search for new sources of revenue, state governments began to operate their own lotteries. These lotteries differed from previous lotteries in that they were state operated and played on a continuous basis.

5th Wave (1993–present): The Triumph of Casino Gambling

Beneficiaries: As gambling became more socially acceptable, casino gambling was the logical progression in enhancing a state's ability to raise revenue. The casino industry has become more concentrated, and the federal government began permitting Native Americans to operate casinos in order to become economically self-sufficient.

lottery. Then the lotteries spread to the Midwest and the western United States, with the South being the last U.S. region to establish lotteries. By 1993 only Utah and Hawaii did not have some form of legalized gambling. Gambling had gained a social acceptance that it had never been able to achieve in any previous period of American history.

The year 1993 was also a watershed for the gambling industry in another way. It marked the first time in U.S. history that casino revenues surpassed lottery revenues, cementing gambling's claim to be the most utilized form of entertainment in the United States.

How did this expansion of casino gambling take place? Three sources contributed to this rapid expansion of casino gambling. First, there was the expansion of the number of what can be termed "national destination" markets for casino gambling. Throughout the 1980s and 1990s, Las Vegas transformed itself from a venue strictly for casino operations to a full entertainment center.

As a result of this trend, not only do visitors to Las Vegas stay longer (3.5 nights in 2005 in comparison with 2.3 nights in 1970), but in addition, the amount of money they spend in Vegas on nongaming activities has increased by more than 20 percent![4] In 1978 casino gambling was legalized in Atlantic City, and although it is not the national destination that Las Vegas is, Atlantic City has experienced a 22 percent increase in gambling revenues as well as a 24 percent increase in visitors since the advent of casino gambling.[5]

Another form of casino gambling that exploded during the 1990s was riverboat gambling. In 1989 Iowa became the first state to permit it and was soon followed by Louisiana, Illinois, Mississippi, Missouri, and Indiana. This form of casino gambling at first placed numerous restrictions on operators. For example, the boats actually had to cruise, the amount of money patrons could bring aboard was limited, and patrons had to leave the boats after the boats cruised. All of these restrictions were gradually lifted as states competed with each other for the gambling revenues. By far, the most successful state in the riverboat arena has been Mississippi, which is now the third-largest casino gambling market in the United States.

The final source of casino gambling revenues is Native American casinos. In 1988 Congress passed the Indian Gaming Regulatory Act (IGRA). This legislation permitted tribes that were recognized by the federal government to develop gaming facilities. The various issues surrounding Native American gambling are taken up in a later chapter. But to give the reader some indication of how successful Indian gaming has become, it is estimated that revenue at American Indian casinos grew to nearly $23 billion in 2005. In 2006 there were 420 Indian casinos in the United States, accounting for 310,000 full-time jobs as well as $10.5 billion in wages.[6] Hence, by any measure, Native American casinos have been an economic success for the tribes—as well as for the states in which they operate: the tribal casinos have contributed $6.9 billion to the states in tax revenues.

Casino gambling has clearly become the dominant force behind the explosion of gambling activity in the United States, and there are various proposals to expand casino gambling in new jurisdictions. State legislators give many reasons that they might approve the expansion of gambling. In particular, taxes and economic activity generated by casino gambling are useful sources of revenue and economic development; and if a neighboring state has casino gambling, a state risks losing all of the potential tourist and tax revenue to its neighbor, thereby putting additional tax burdens on its citizens.

But beyond economic considerations, there also appears to be another overarching reason for legislators to be well disposed toward gambling: the social acceptance gambling has gained over the past 40 years. The public not only tolerates additional gambling opportunities but in many ways demands that a state provide these opportunities, or the gambler will leave the state and gamble elsewhere. The final section of this chapter attempts to account for this fundamental change and provides the reader with conceptual tools to apply while exploring the various options that legislators face as they decide on the gambling issue.

THE "ETHICS OF SACRIFICE" VERSUS THE "ETHICS OF TOLERANCE"

As already recounted, gambling and cigarette smoking have experienced an almost complete role reversal in the public policy process. Why has cigarette smoking been condemned by the vast majority of public policy makers whereas gambling has seemingly become the darling of legislators as a painless source of revenues for pet projects? Why have the debates over gambling and cigarette smoking evolved so differently over the past 40 years? One way to account for this development is to examine the manner in which the merits of a public policy issue are debated. In U.S. policy debates, the conflict between the societal good and the rights of the individual historically has been the focus of ethical controversy. Advocates for both sides of controversial issues, such as Prohibition, have constantly appealed to one or the other of these ethical stances in making their cases. This conflict between the societal good and the rights of individuals remains the basis for debating the ethical merits of public policy issues ranging from gun control to environmental protection. Put another way, throughout American history, public policy makers have had to deal with conflict between the common good and the individual's right to choose freely. Arguments have aligned in what we call the "ethics of sacrifice" (or "ethics of duty") and the "ethics of tolerance."

The Ethics of Sacrifice

When "sacrifice" is used as a moral concept to advance the merits of a particular public policy issue, public policy makers must be able to persuade the public that the public must sacrifice some right (think of the "war on terror" and the right to privacy) or benefit in order to achieve a noble goal or end. Most moral arguments with a religious basis utilize this type of rationale—that is, sacrifice in order to please God. The notion of sacrifice is also employed by political leaders during times of crisis, especially times of war, as during World War II or in the "war on terror." In terms of traditional ethical or moral categories, the "ethics of sacrifice" is teleological, that is, goal- or end-oriented. This goal is the "good" of society, and one can ascertain whether a public policy measure is correct according to whether it contributes to the "good" of society.

In terms of public policy, the "good," or "end," is a harmonious society. Traditionally, the sacrifice ethic has been invoked by those who wish to maintain social institutions and structures that they deem as desirable and worthy of being maintained at any cost. Although some might associate this type of ethical thinking with conservative public policy makers, it actually has been employed by both liberals and conservatives to justify their stances on public policy measures. Certainly, President John F. Kennedy employed the ethics of sacrifice when he made his famous challenge to the American people: "Ask not what your country can do for you; ask what you can do for your country." The new president was asking the country to sacrifice in order to meet the challenges that lay ahead for the United States in the 1960s. In essence, those who invoke the ethics of sacrifice are asking the public to sublimate what is "good" for the individual for the "good" of all.

Robert Bellah and his colleagues, the authors of *Habits of the Heart: Individualism and Commitment in American Life,* recall the work of the French social philosopher Alexis de Tocqueville in order to illuminate the ethics of sacrifice. When Tocqueville analyzed American life in the 1830s, he labeled American mores as "habits of the heart" and demonstrated how they helped to mold our national character. Tocqueville singled out family life, our religious traditions, and our participation in local politics as helping to foster the kind of individual who would be willing to make sacrifices in order to sustain a wider political community and to maintain free institutions. It is this identification of the "common good" with the maintenance of societal institutions that is the hallmark of the ethics of sacrifice.[7]

In a later work, *The Good Society,* these same authors once again return to the concept of a society in need of an ethics of sacrifice, refining their analysis of the proper role of societal institutions. They define institutions as "normative patterns embedded in and enforced by laws and mores (informal customs and practices)."[8] In order to show how our understanding of institutions influences the manner in which we conduct our lives, they give various examples. One of the examples has a great deal to do with the issue of gambling. On his decision to ban Pete Rose from baseball, A. Bartlett Giamatti, then Commissioner of Major League Baseball, wrote,

> I believe baseball is an important, enduring American institution. It must assert and aspire to the highest principles—of integrity, of professionalism, of performance, of fair play within its rules. It will come as no surprise that like any institution composed of human beings, this institution will not always fulfill its highest aspirations. I know of no earthly institution that does. But this one, because it is so much a part of our history as a people and because it has such a purchase on our national soul, has an obligation to the people for whom it is played—to its fans and well-wishers—to strive for excellence in all things and to promote the highest ideals.[9]

The advocates of the ethics of sacrifice equate the preservation of institutions with the maintenance of the "good" life. From this perspective Pete Rose's decision to gamble had to be punished severely because his gambling had damaged an institution that inspires people to act virtuously. In fact, gambling should be discouraged or banned on a permanent basis because it does not promote the virtuous life. The decision about whether a person has the "right" to perform certain actions has to take into account what effect that action will have on an institution or society at large.

Those who invoke the ethics of sacrifice at its most extreme can be accused of employing the motto "the ends justify the means." The individual's ability to decide what is best for herself or himself needs to be subservient to the needs of an institution, such as the state, a corporation, or even the church. The good of society or of the institution overrides the rights and needs of the individual. This is certainly the ethic under which the military operates. When it is applied too rigorously to a society with many diverse parts, however, it can have many disastrous consequences. One only needs to recall America's Prohibition era to realize that one cannot impose virtue on an entire population. Yet the ethics of sacrifice calls forth what many would maintain is the noblest of human characteristics, the ability to give of one's self even if that giving is detrimental to that individual self.

The Ethics of Tolerance

One of the earliest virtues that every American schoolchild is taught is tolerance. Having settled in Pennsylvania in order to escape persecution in England, the Quakers are celebrated in American history texts because they permitted everyone to practice their religious beliefs. In founding Maryland, Cecil Calvert, Lord Baltimore, too established religious freedom and welcomed persecuted English Catholics (although this religious tolerance would be tested frequently throughout the colonial period). Meanwhile, the Puritans who settled Massachusetts had also fled religious persecution, but tolerance was not one of the virtues they cherished in the building of the New Jerusalem. The Separatist Roger Williams quickly found that he had to flee Massachusetts or be deported back to England, and he went on to found Rhode Island. So although there have been differences of opinion about just how tolerant American society was or is, in comparison to European societies, tolerance of various religious beliefs as well as other nationalities has been a hallmark of American society.

Tolerance entails that no person has to "sacrifice" her or his basic freedoms in order to achieve some goal of public welfare or to preserve an institution that promotes the societal good. When tolerance is promoted as one of the chief societal virtues, society must preserve the rights of minorities at all costs, even at the expense of the majority. The principle also entails that American society has to tolerate the "right" of the individual to perform actions that might very well be destructive to society, as long as the right to perform those activities is guaranteed by law. In traditional ethical thought, the ethics of tolerance would fall into the deontological mode of thinking. That is, the means a person uses to achieve a goal are more important than the goal itself.

One example of continuous public policy controversy in which the ethics of tolerance has played a part is the gun control issue. Opponents of tougher gun control laws have utilized the ethics of tolerance as the basis for their ethical argument against tighter controls on guns. They maintain that the right to bear arms is protected in the U.S. Constitution. Therefore, even if the majority of Americans favor stricter gun restrictions, their right to bear arms has to be tolerated in order to uphold the rights of the minority who wish to have no limits placed on their ability to own and use guns.

The ethics of tolerance is based on an American ideal that Founding Fathers such as John Adams and Thomas Jefferson insisted be part of the U.S. Constitution—that no citizen's rights can be violated in order to achieve an end. Government exists to protect an individual citizen's rights and must not coerce an individual to relinquish a right even to preserve an institution that has served society well. Tolerance is a guiding principle that in many ways has served a nation of immigrants very well. Immigrants had to be tolerated and protected by the majority in order to promote the diversity needed for a dynamic society.

But like most virtues and values, this conception of tolerance has its downside. At its worst, the ethics of tolerance could promote a rather narrow, selfish focus on the individual. It can be argued that the individual has to find a place in a society and that if individuals are going to live in a community, then there has to be some sort of hierarchy of "rights," but the ethics of tolerance provides very few clues about how to determine this hierarchy. The glorification of the individual that is essential to the ethics of tolerance makes it quite difficult for a society to challenge the individual to make sacrifices that are necessary in order to preserve those institutions that, in turn, help that society to function for the common good.

SECURING ETHICAL LEGITIMACY

So why did the cigarette industry fall so out of favor with public policy officials? Why has its "sin" cousin, the gambling industry, flourished even as the tobacco industry has suffered a rapid decline? In comparing the evolution of these two controversial public policy concerns, it would be instructive to analyze the role that the ethics of sacrifice and the ethics of tolerance have played in determining how public policy makers view each issue. Let us once again examine how each type of ethical reasoning is utilized by groups that either oppose or support these activities.

Advocates of increased gambling activities (whether lotteries, casinos, Internet gambling, or sports gambling) and those who wish to limit government's involvement in the cigarette industry invariably make their case in the public policy arena by employing the ethics of tolerance as their primary moral argument. For both issues their argument is simply that society must tolerate these activities because individuals have the "right" to engage in them as long as they are not harming anyone else. Of course, they also point out the economic benefits that government enjoys from these industries Although they acknowledge that these activities might be harmful to a few individuals, they hold that the states ought to be able to profit from these activities, given that the vast majority of smokers and gamblers will continue to smoke or gamble regardless of whether the state permits these activities. So why shouldn't the state use the profit from smoking and gambling for "good" causes such as education and aid to the elderly?

Meanwhile, opponents of these two "sin" industries have generally utilized the ethics of sacrifice as their primary ethical retort in their fight against these vices. They argue that any benefits society accrues by allowing these activities in no way "justifies" the activities and that, in fact, society must protect itself from these activities because they bring great harm to some segments of society. The harm done to society more than outweighs the harm done by violating an individual's right to engage in these activities, they assert. Therefore, government ought to sacrifice individuals' right to gamble and to smoke cigarettes for society's overall good.

So why has the cigarette industry become the endless target of public policy initiatives to restrict the use of cigarettes, while the gambling industry has not only withstood attacks but has actually increased its presence throughout the United States? It is because the cigarette industry has lost its ability to utilize the ethics of tolerance to defend its right to exist, whereas the gambling industry has very effectively employed the ethics of tolerance argument, so much so that a "majority of U.S. adults now favor licensed casinos in their own states."[10]

Since the advent of the passive smoking debate in 1993, opponents of the cigarette industry have taken up an ethics of tolerance argument unavailable to them prior to 1993. The opponents of the cigarette industry make the following argument: Cigarette smokers no longer have the "right" to smoke because it has been proved that nonsmokers are negatively affected by cigarette smoke. In other words, the right to smoke can no longer be tolerated because it interferes with the rights of nonsmokers to live in a smoke-free environment. Meanwhile, the vast majority of Americans seem to believe that gambling is an individual's right. Because the individual gambler is not hurting anyone else, it is quite acceptable for the state to profit from this activity.

The next three chapters will the pros and cons of the various forms of gambling, namely, Internet gambling, sports wagering, and Native American casino gambling. The reader should be able to determine which arguments fall into the category of the ethics of sacrifice and which into the category of the ethics of tolerance. The question of just how persuasive these arguments are might lead to a long and fruitful discussion with fellow students and colleagues.

At the same time, the reader will also need to ascertain whether the gambling industry will be able to maintain the current ethical legitimacy conferred by the ethics of tolerance. Under what circumstances would the gambling industry's opponents be able to make the case that gambling should no longer be tolerated? Is there a "passive smoking" argument in the gambling industry's future? Further, what should the government's role be in regulating the gambling industry? Should the government be operating lotteries and casinos at all?

But we now turn to the form of gambling that not only is currently causing immense controversy in the United States but that also has drawn international attention and has been the source of World Trade Organization controversy. Critics have called it the "crack cocaine" of gambling, whereas supporters hail it as the most democratic form of gambling. It is time to examine the world of Internet gambling.

NOTES

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2. U.S. Department of Health and Human Services, *Report of the Surgeon General: The Health Consequences of Smoking: Cancer* (Rockville, MD: U.S. Department of Health and Human Services, 1985).
3. Campaign for Tobacco-Free Kids, http://www.tobaccofreekids.org.
4. *Standard and Poor's Credit Week,* June 14, 2006.
5. *Standard and Poor's Credit Week,* June 14, 2006.
6. "The Economics of Native American Gambling," *Richmond Register,* June 22, 2006, www.richmondregister.com.
7. Bellah, Robert N., Richard Madsen, William Sullivan, Ann Swidler, Steven Tipton, *Habits of the Heart: Individualism and Commitment in American Life* (New York: Harper & Row, 1985).
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9. Giamatti, A. Bartlett, "In the Matter of Peter Edward Rose, Manager, Cincinnati Reds Baseball Club, Agreement and Resolution," quoted in Bellah et al., 1991.
10. Harrah's Entertainment, "Casino Customers: An Annual Survey," 2006. http://www.harrah.com.

Part II

CURRENT ISSUES

3

Internet Gambling: Gambling's Jackpot or Demise?

> We don't believe online gaming will have a negative impact on any resort revenues, gaming or non-gaming, because these are different businesses and will attract a different clientele. I really don't believe that anyone would make a decision to play online for an hour and then decide not to come to Las Vegas on a three-day holiday.
>
> —*High Yield Report,* 2001

These remarks, spoken at a press conference by vice president of MGM Mirage properties Alan Feldman, display the firm's stance on the issue of Internet gambling. However, these remarks also are evidence that gambling on the Internet has become a considerable enterprise. The fact that the largest casino companies in the world, such as MGM Mirage, which generated over $6 billion in revenues in 2005, would even be acknowledge the existence of Internet gambling makes it a topic worthy of study.[1]

Yet the traditional brick and mortar casinos are not the only entities that have become keenly aware of gambling on the Internet, an industry that according to the *New York Times* reached $12 billion in revenues in 2005.[2] In addition, the states that maintain their livelihood through gaming revenues, such as Nevada and New Jersey, must also be attentive to the burgeoning Internet gambling industry. As such, Internet gambling poses a considerable threat to the financial well-being of several institutions, and its prevalence could have significant consequences for taxpayers.

These far-reaching effects, coupled with the inherent difficulty in regulation and ineffectual federal legislation, have made Internet gaming an issue of intense debate in both the political and the financial realms. Legislators on both sides of the issue have been fighting to strengthen federal statutes, and financial experts for the affected parties have deliberated on the best strategic way to approach the phenomenon.

This chapter focuses on why this segment of the gambling industry has become so controversial. First, the pros and cons of Internet gambling are presented. Next is an examination of the various attempts to regulate Internet gambling. Finally, the chapter closes with an analysis of the positions of the various stakeholders, such as the traditional brick and mortar casino industry as well as Nevada and New Jersey, two states that derive a great deal of revenue from traditional casino gambling.

PRO AND CONS OF INTERNET GAMBLING

The arguments in favor of legalizing Internet gambling in many ways mirror the traditional arguments that proponents of gambling have utilized but with a very interesting twist. First, supporters of Internet gambling maintain that this form of entertainment is a result of a choice. The Internet gives people access to a world that might be closed to many, and so it is a communications tool. Ultimately, how an individual utilizes the Internet is a matter of choice and not the government's responsibility. Why should Congress or any level of government tell Americans what they can or cannot do in the privacy of their homes? After all, in a recent poll in the *Wall Street Journal,* 85 percent of those polled reported believing Congress should stop interfering with Internet gambling.[3]

Proponents of Internet gambling argue that trying to prohibit the online gambling industry is a futile exercise bound to fail and hence is a waste of resources. They see hypocrisy in the federal government's attempt to ban Internet gambling while simultaneously permitting state lotteries to open Web sites as well allowing betting on horse races. Americans account for 45 percent of the consumers who bet online. Overall, Americans wagered nearly $6 billion online in 2005, in comparison with $1.5 billion in 2001.[4] Hence, it is a business that consumers demand remain in business! Proponents of Internet gambling again remind legislators of the lesson of alcohol prohibition. You cannot ban what most of the public deems acceptable behavior.

Then, the argument for Internet gambling takes a slightly different twist. Proponents of Internet gambling maintain that this form of gambling is the most transparent form of gambling in the sense that every transaction is recorded and logged and can be examined by regulators. In fact, many proponents would like government to "legitimize" the Internet gambling industry by regulating it. They maintain that it is inconsistent to regulate "brick and mortar" casinos without giving the same consideration to Internet gambling sites.

This lack of regulation has had two consequences that legislators ought to take into account: first, this lack of regulation has led to a boom in illegal Internet gambling business. Currently, 64 countries have regulated Internet gambling (with Great Britain being the leading advocate of online regulation), which proves that regulation is possible. Regulation would standardize and strengthen legitimate Internet gambling sites. Finally, by regulating online gambling, government would be provided additional revenues. It could tax the sites by taking in a certain percentage of revenues and of course by taxing winnings.

Those who oppose Internet gambling counter with a variety of arguments, the first being that those who operate Internet gambling sites are simply breaking the law. When a site solicits and accepts wagers on games of chance, it violates the Wire Act and the Professional and Amateur Sports Protection Act. So why should a firm that violates the law be rewarded with government protection?

A second argument is that Internet gambling regulation cannot work like traditional casino-based regulation. Traditional casinos can check the IDs of underage children and problem gamblers at the door. This is certainly not the case with an Internet casino. Regulation of Internet gambling would not eliminate underage gambling nor would it deal with the gambling addiction problem.

Opponents of Internet gambling sites maintain that they are often operated by criminals. The potential for identity theft and fraud is high. These sites also present criminals with a haven for laundering money from other illegal activities. Some law enforcement officials equate Internet gambling sites with wholly unregulated offshore banks.

The final objection has a unique twist. Although land-based casinos have a multiplier effect on the local economy, Internet gambling sites extract money from gamblers but return nothing in the way of services to a local community. In other words, there are no long-term benefits associated with Internet gambling, so therefore it is merely a siphon to any economy and should not be permitted.

In the next section we examine the current legal status of Internet gambling as well as some of the proposals to regulate it.

THE LEGAL STATUS OF INTERNET GAMBLING IN THE UNITED STATES

The extremely high growth prospects for the Internet gambling industry coupled with the fact that virtually all of the e-gaming casinos are located outside the United States make the industry a hotbed for debate among federal and state legislators alike. This has been the case ever since 1961, when the federal government intervened in the affairs of each state and invoked the U.S. Constitution's Commerce Clause to regulate gambling across state borders. As is still the case, in the 1960s gambling was legal in some states and illegal in others. To skirt this issue, people wishing to place bets would often wire money from the states where gambling was illegal to states where gambling was legal. This money was then used for gambling purposes within those states by the persons residing in states where gambling was illegal.

Federal Legislation

In 1961 federal legislators passed the Wire Act, a bill intended to assist states in enforcing their respective laws on gambling. The Wire Act was the first and main piece of legislation to deal with the issue of gambling across state lines. Its provisions impose fines and imprisonment on those who are convicted of "knowingly [using] a wire communication facility for the transmission in interstate and foreign commerce of bets or wagers or information assisting in the placing of bets or wagers on any sporting event or contest, or for the transmission of a wire communication which entitles the recipient to receive money or credit as a result of bets or wagers."[5]

Clearly, the issue then was much the same as it is now. The federal government reacted to complaints about the negative effect of gambling across state lines much in the same manner as it is now attempting to prohibit gambling across foreign borders in the form of Internet gambling. Thus, when Internet gambling sprung onto the scene in the late 1990s, the federal government interpreted the Wire Act of 1961 to mean that the pursuit of Internet gambling was strictly illegal across the United States.

Yet there are some problems with this loose interpretation of the act that have made prosecuting the individuals involved in Internet gambling extremely difficult. First, the act applies only to placing bets on "sporting events or contests." As mentioned earlier, the popularity of Internet gambling has allowed it to encompass much more than merely betting on sports. A second issue, and undoubtedly the most troubling, is that Internet gambling can occur without the use of any wires whatsoever. Modern technology has allowed for wireless Internet, which if used in connection with gambling pursuits, would technically render the Wire Act ineffective with respect to prosecution.

With these thoughts in mind, federal legislators have been pushing a bill that will clarify the ambiguities of the Wire Act with respect to Internet gambling. The Combating Illegal Gaming Reform and Modernization Act was approved by the Judiciary Committee in July 2002. This act would amend the Wire Act to include all interstate communications, namely gambling on the Internet. In addition, the Combating Illegal Gaming Reform and Modernization Act would expand the scope of the Wire Act to apply not only to sports betting, but also to all other "games of chance." Formally, this act would require banks to refuse transactions for Internet gaming and make it illegal for banks and individuals to knowingly accept credit cards or other payments in connection with gambling on the Internet.

It is important to keep in mind, however, that the Combating Illegal Gaming Reform and Modernization Act has yet to become a law. It still needs the approval of the Financial Services Committee, the House of Representatives, and the United States Senate. Therefore, at the present time, the main act in effect governing Internet gambling in the United States continues to be the Wire Act of 1961, and although the Department of Justice contends that Internet gaming is a violation of the Wire Act, and in turn is already an illegal activity, their interpretation is quite loose and extremely difficult to enforce.

Regulation

The other alternative to the strict prohibition of Internet gambling supported by the Internet gambling industry is legalization and regulation. This approach is advocated by several institutions that feel prohibition of Internet gambling will be impossible to enforce. However, the regulation of Internet gambling will also be an uphill battle because several issues make the regulation of the industry extremely difficult.

The first of these issues deals directly with the online gaming casinos. When individuals place bets with an online gambling casino, they are not able to cash out and walk away with their winnings like at a traditional casino. Rather, the bettors must wait for their winnings to be deposited into their account or for a check to be written by the casino for payment. Since the onset of Internet gambling, there have been several reports of online gambling outfits simply disappearing into thin air. Other online gaming sites are notorious for being extremely slow to pay out winnings and others for not paying out winnings at all. This issue is compounded by the fact that unlike traditional casinos in places like Nevada, which are constantly under the watchful eye of State Gaming Commissions, online casinos are for the most part unregulated. Therefore, there is no way to ensure that the software used by these casinos for gambling pursuits is not in some way rigged to maximize profits for the firm.

A second issue with regard to the regulation of Internet gambling has to do with the location of the players in the online gambling arena. Because the U.S. government holds that Internet gambling is illegal, the inference is that it is illegal for any person within the United States to gamble over the Internet. This is not the case for citizens of other countries such as England and South Africa, where gambling over the Internet is permitted. So the problem arises when Internet gambling casinos take bets, either knowingly or unknowingly, from persons located within the United States. Many times, these casinos have no way of knowing the exact location of the bettors, thus making it impossible to strictly adhere to the laws that govern Internet gambling in the United States.

A new device has been designed to address the player location issue; however, at this point its practicality is severely limited. Engineers at http://cyberlocator.com have developed a piece of equipment that once installed into computers enables the equipped computers to be located by means of satellite sensors anywhere in the world. Theoretically, this would solve the problems associated with the location of players, but several obstacles impede the implementation of this product. Most importantly, in order for a computer to be located, it must have this device installed. Although the devise is inexpensive and easy to install, it would take a worldwide mandate for that type of technology to be successful, and that success could come only after several years, when all currently owned computers without this device have become obsolete.

A third issue impeding those attempting to regulate Internet gambling is the pervasiveness of underage players. Because of the nature of Internet gambling, there exists a problem of not knowing who is gambling on any given site. Any person with a credit card and a minimal amount of expertise in surfing the net is able to place bets on the Internet. Currently, there are no forms of virtual identification that can discern an 8-year-old from an 80-year-old with respect to gambling on the Internet.

Finally, the issue of addiction is problematic when considered within the context of online gambling. Persons addicted to gambling, often referred to as compulsive gamblers, cannot help themselves from indulging in any sort of gaming activity. It logically follows that the closer these gambling addicts are to a gaming facility, the more inclined they will be to gamble. With Internet gambling, compulsive gamblers have casino-like games literally at their fingertips. Thus, the effects of this constant 24-hour-a-day access will most likely intensify addiction to gambling. Additional losses due to gambling will also put further strain between gambling addict and his/her family and friends.

Policies of the State Governments (Nevada and New Jersey)

Generating nearly 50 percent of the aggregate revenue for the state, casino gambling is the lifeblood of Nevada. The onset of Internet gambling might put a damper on the revenue base of the Nevada state government. With a substantial portion of gaming revenues now being used via the Internet through offshore accounts, the amount of revenues produced by these casinos has likely been depressed. Because the state of Nevada garners taxes directly from these casinos, it follows that the state government and the residents of the state feel the need to address the issue of Internet gambling.

The state legislators of Nevada have realized that a great deal is on the line for them with respect to Internet gambling. They know that they cannot remain idle and continually lose a significant portion of their gaming revenues year after year on account of Internet gambling. Thus, on June 14, 2001, Nevada governor Kenneth Guinn signed Assembly Bill 466 into law. This bill "enables the Nevada Gaming Commission to adopt regulations upon the advice and assistance of the Nevada Gaming Control Board. However, before such regulations may be promulgated, the Legislature clearly instructed the Commission to first determine whether 'interactive gaming' is legal."[6] Thus, Nevada has chosen to exploit the current ambiguity of federal legislation regarding Internet gambling and utilize their regulatory body, the Nevada Gaming Commission, to determine the legality of Internet gambling.

It seems that the state of Nevada has chosen this path for two reasons. First, there exists a general sentiment among state legislators that no piece of legislation will be able to completely abolish the Internet gambling phenomenon in the near future. Thus, the state government most likely feels that Internet gambling ought to be legalized and regulated in the state in order to potentially gain a piece of the revenues that the state may lose on account of Internet casinos. Second, Nevada most likely wants to enter the Internet gambling industry as well because of its explosive growth potential. The state realizes that the trusted names of the traditional brick and mortar casinos as well as the intensely regulated nature of gaming in Nevada would give any Internet gambling initiative put in place in Nevada an edge over the competition.

Much like Nevada, the state of New Jersey receives much-needed revenues from gaming. In 2002 gambling within the state generated over nine billion dollars in revenues for New Jersey. Therefore, the topic of lost revenues to offshore Internet gambling Web sites is a real concern. However, New Jersey's legislation has not sailed along as smoothly as Nevada's.

Senate Resolution No. 48 from New Jersey's 209th legislature urged Congress to regulate Internet gambling. The resolution, introduced on May 18, 2000, states that "a number of studies have concluded that the proliferation of legalized gambling has had a detrimental impact on society." It states further that "minors who would otherwise be unable to participate in gambling activities may be particularly susceptible to gambling related problems as a result of the easy access to such activity through the Internet." Therefore, it appears that State Senator John Bennett was asking Congress to think of Internet gambling as a detriment to the citizens of the state when he introduced this resolution.

Likewise, one of the main figures behind the push toward legalization and regulation of Internet gambling in New Jersey, state legislator Anthony Impreveduto, shares similar thoughts. He has long held the belief that allowing licensed land-based casinos to offer online gambling would be a huge step toward protecting residents of his state from unlicensed and unregulated operators. In 2001 he and fellow state assemblyman Neil Cohen introduced a "safe-haven bill" that would aim to establish Atlantic City as a regulated U.S. jurisdiction for Internet casinos.[7] This legislation, according to Cohen, would be a protective measure to prevent the growth of unregulated Internet casinos and would require Internet casinos to use software that blocks minors and compulsive gamblers. In addition, the bill would not interfere with federal legislation, according to Impreveduto, because it does not allow for online sports wagering.

This bill, however, is currently at a standstill, and it does not appear it will move any time soon. Likewise, the New Jersey senate resolution has done little to sway opinions on Capitol Hill. Thus, the attempt by state legislators to legalize and regulate Internet gambling in New Jersey has had little impact on changing the laws governing Internet gambling. The statutes on the books in the state of New Jersey concur with the federal government that Internet gambling is illegal within the state, and it does not appear that legalization and regulation are on the horizon.

Strategies of Traditional Casinos (MGM Mirage and Harrah's)

In addition to the actions taken by the state governments, there is also heightened awareness of Internet gambling among the traditional brick and mortar casinos. These traditionally operated casinos are now actively weighing the pros and cons of starting their own Internet gambling Web sites in order to get their slice of the ever-growing revenues that the budding industry has to offer.

The traditional brick and mortar casinos face several concerns when deciding whether to enter into the Internet gambling industry. First, these casinos share the same revenue concerns as the state governments; they are troubled by the fact that they may be losing revenues to the offshore Internet gambling sites. This issue is tricky in that on one hand the traditional casinos would be inclined to side with the federal government in an attempt to prohibit Internet gambling and in turn preserve their revenues. Yet the problem with that approach would be the ineffectiveness of the federal government in promulgating and enforcing laws that would be construed tightly enough to entirely eliminate the threat of the loss of revenues from competitors in the Internet gambling industry.

In addition to this concern over revenues, traditional casinos also face the issue of cannibalization when deciding whether to become a player in the Internet gambling industry. Cannibalization occurs because there is only a finite amount of money that consumers are willing to spend on gambling. This money, if spent in traditional casinos, would be supplemented by other recreational activities that also provide revenues for those casinos, such as shopping, meals, entertainment, and so on. However if this money were spent at an online gambling Web site operated by these traditional casinos, there would be the possibility of a downturn in spending in those non-gambling activities, which would detract from the bottom line of the casinos. In short, cannibalization would weaken the desirability of entering into the Internet gambling industry; traditional casinos would not wish to enter into an industry that would be in direct competition with their current operations.

All of these concerns did not deter MGM Mirage, one of the major Las Vegas casino operators. This casino took an aggressive approach to entering the Internet gambling industry. The company set up an Internet gambling Web site, playmgmmirage.com, which was operated from the Isle of Man, a small island off the coast of Great Britain. MGM Mirage invested $15 million in this venture and agreed to pay the Isle of Man a licensing fee of $125,000 per year so that operations could be conducted from the island.[8] Playmgmmirage.com was able to take bets legally from several countries, including the United Kingdom, Ireland, and South Africa. However, online betting from parties located in the United States is illegal and MGM abandoned this site a few years later in response to pressure from the U.S. Justice Department.

MGM Mirage took the stance that federal legislation abolishing Internet gambling in the near future will be an extremely difficult task. The amount of money that it spent on this venture is miniscule in comparison with its possible revenues.

The marketing strategy of MGM Mirage in launching this online venture was also quite interesting. Playmgmmirage.com focused on its brand credibility to lure current users of other online gambling Web sites to come and play with them. They contended that the Internet gambling industry is based on trust and that if there is a name out there that holds some credibility and a solid reputation, then that casino will experience a great deal of success within the industry. In addition, playmgmmirage.com offered real Las Vegas–style table games in a virtual setting, such as blackjack and roulette. This is in contrast to many of Internet gambling Web sites, which rely heavily on sports betting.

The second major player in the gambling industry is Harrah's Inc. This company's strategy toward Internet gambling stands in sharp contrast to that of its competitor, MGM Mirage: Harrah's is taking a cautious stance toward entering the industry. A representative for the company, David Strow, said in a 2002 press conference that Harrah's is "essentially taking a wait-and-see attitude. We're not looking at online gaming because of the ambiguity. We won't do anything that jeopardizes our current licenses."[9] Arguably, Harrah's is concerned with the negative effects that could be brought on by entrance into the Internet gambling industry. Although plans have been made to develop Internet gambling "gamble-for-prizes" Web sites, there have been no plans for Harrah's to create any real online gambling Web sites in the near future.

Therefore, just as it has become apparent that the states of Nevada and New Jersey have different attitudes toward Internet gambling, two of the largest casino companies, MGM Mirage and Harrah's, also hold differing opinions on the topic. This may to be a peculiar discrepancy, but an examination of the general strategies of each entity shows their opposing positions to be quite rational.

RECENT DEVELOPMENTS INVOLVING INTERNET GAMBLING

Currently, the U.S. federal government appears to be employing two different tactics to deter Internet gambling. First, there is a legislative track. We have already seen that federal prosecutors currently are using the Wire Act of 1961 to prevent not only sports betting but also casino games as well as online poker. But many legal experts point out that it is far from clear that the Wire Act of 1961 was intended to cover all gambling activities.

In 2007, the U.S. House passed a bill (note: the U.S. Senate has not passed this bill) that explicitly covers these games. It also seeks to create a new enforcement mechanism by criminalizing the processing of payments for Internet gambling. It would prohibit banks, credit card companies (Visa, MasterCard, American Express, and so on) and online payment processors from engaging in any Internet gambling transactions. Hence, this bill would prohibit any American financial institution from transferring money to transfer payment processors that are known to do business with Internet gambling sites. Needless to say, it would make it quite difficult to place an online wager or bet. Proponents of this legislation maintain that it makes no moral judgments on the wisdom of gambling but merely provides an enforcement mechanism for the laws that already exist.[10]

The second prong in the U.S. federal attack is prosecutorial. In 2006, Federal agents arrested the British chief executive of BetOnSports, David Carruthers, who was in the United States on a flight layover from Costa Rica.

Mr. Carruthers is a British citizen, and his firm was listed on the London Stock Exchange. His business is legal in the United Kingdom, but it derives 45 percent of its revenues from U.S. customers.[11] According to the prosecutor, Catherine Hanaway, the U.S. attorney for eastern Missouri, the fact that this activity is legal in Britain and Costa Rica does not make it legal in the United States.[12] As a result, Carruthers faced 20 years in prison if convicted of conspiring to operate an illegal gambling operation. The value of shares in Carruthers's BetOnSports fell by 80 percent, and trading these shares was suspended on the London Stock Exchange. Carruther was eventually deported back to the United Kingdom in January 2007.

But proponents of Internet gambling have also mobilized forces in response to this assault on Internet gambling. The case that perhaps is causing the U.S. government the greatest concern is the one that Antigua and Barbuda have lodged with the World Trade Organization (WTO). Both countries have claimed that the U.S. Department of Justice illegally tried to stop betting companies based in these tiny Caribbean islands from marketing themselves to American gamblers. Both islands maintain that U.S. laws are a restraint of trade and that these prohibitions are hurting these islands' attempts to diversify their economies away from tourism. Meanwhile, the United States contends that Internet gambling should be prohibited because it violates some state laws that prohibit gambling. The legislature of Utah (where there is no legal form of gambling) passed a resolution asking the Bush administration to withdraw from the WTO unless the United States can negotiate within that organization with "states' rights in mind."[13]

The initial ruling by the WTO found in favor of the United States in part, agreeing that the 1961 Wire Act was consistent in denying sports gambling to both domestic and international operators. However, it found against the United States in ruling that the United States had failed to show that the Interstate Horse Racing Act applied equally to foreign and domestic remote betting services and that the act therefore violates international trading rules. Both sides are appealing this ruling.[14]

Hence, the Internet gambling issue remains far from settled. How this issue is eventually settled will have a profound impact on many other forms of gambling. Perhaps, the form on which it will have the greatest impact is sports betting, which is the focus of the next chapter.

NOTES

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3. "Should Online Gambling Be Banned? A Wall Street Journal Online News Roundup," *Wall Street Journal,* April 4, 2006.

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8. "MGM Mirage Starts Internet Gaming Operation in Isle of Man," *Las Vegas Review-Journal,* November 11, 2002.

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10. *New York Times* "The Gambling Is Virtual; the Money Is Real," July 25, 2006.

11. *Wall Street Journal* "Should Online Gambling Be Banned? A Wall Street Journal Online News Roundup," April 4, 2006.

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13. *Financial Times* "Antigua and US Both Claim Win in WTP Gambling Row," April 7, 2005.

14. Ibid.

4

Sports Gambling: A Friendly Wager or a Threat to the Integrity of the Game?

Sports events have played a key role in our society for millennia, and gambling has accompanied many of these events in some form. From placing bets on Roman gladiators to betting on college sports teams, sports wagering is a thriving, yet often hidden, part of sports competitions. But in other instances, it is not hidden at all. Horse racing is an example of a sport that depends on wagering for its existence.

In the United States, Nevada is the only state that legally maintains sports books, but authorities, especially the Federal Bureau of Investigation (FBI), openly recognize that the amount of sports betting far surpasses what is reported within Nevada. This implies that many people place bets either through illegal bookies or on offshore Internet gambling Web sites. To solve the issue, some organizations suggest that sports betting should be legalized because this would increase state revenues through taxes on legal winnings and would minimize illegal betting and Internet gambling. Others argue that legalization will not solve long-standing problems surrounding the legitimacy of sports events or prevent athletes from engaging in such tactics as point-shaving.

STAKEHOLDERS IN SPORTS GAMBLING

We next examine the positions of two of the major players involved in the sports gambling controversy, the National Collegiate Athletic Association (NCAA) and the American Gaming Association (AGA).

The National Collegiate Athletic Association

Betting on collegiate sporting events is a substantial area of concern for many organizations, including the National Collegiate Athletic Association (NCAA) and member colleges. The NCAA's position on sports wagering is as follows:

> The NCAA opposes all forms of legal and illegal sports wagering. Sports wagering has the potential to undermine the integrity of sports contests and jeopardizes the welfare of student-athletes and the intercollegiate athletics community. Sports wagering demeans the competition and competitors alike by a message that is contrary to the purposes and meaning of sport. Sports competition should be appreciated for the inherent benefits related to participation of student-athletes, coaches and institutions in fair contests, not the amount of money wagered on the outcome of the competition.[1]

The NCAA believes that the existence of sports wagering mars the image of collegiate sports and damages its integrity. There have been several instances in which student-athletes have affected the outcome of a sporting event because of a sports wagering issue. The NCAA believes that over the years the number of these occurrences has increased. The NCAA firmly believes that to prevent such conflicts from occurring, the federal government should outlaw sports gambling on collegiate sports.[2]

Because the NCAA desires to uphold the integrity of college sports, the member schools have adopted NCAA Bylaw 10.3, which prohibits athletic department staff members and student-athletes from participating in gambling activities as related to intercollegiate or professional sporting events:

> Staff members of a member conference, staff members of the athletics department of a member institution and student-athletes shall not knowingly: provide information to individuals involved in organized gambling activities concerning intercollegiate athletics competition; solicit a bet on any intercollegiate team; accept a bet on any team representing the institution; solicit or accept a bet on any intercollegiate competition for any item (e.g. cash, shirt, dinner) that has a tangible value; or participate in any gambling activity that involves inter-collegiate athletics or professional athletics through a bookmaker, a parlay card or any other method employed by organized gambling.[3]

Student-athletes who do not follow these guidelines are sanctioned. Punishments include the loss of remaining regular-season and postseason eligibility in all sports. Although the NCAA realizes that these regulations alone will not deter undesirable activity, it hopes that these rules will assist in maintaining the integrity of sports and prevent student-athletes from engaging in risky behavior. The NCAA has also increased communication with the FBI, the National Football League (NFL), the National Basketball Association (NBA), the National Hockey League (NHL), and Major League Baseball (MLB) concerning information related to gambling and organized crime. The association has produced a video with the FBI called *Gambling with Your Life,* which is used as an educational tool for student-athletes.[4] The NCAA also supports workshops in which college administrators educate student-athletes about the risks involved with sports gambling, televises public service announcements against sports gambling during championship games, and produces a pamphlet titled "Don't Bet on It," which informs students of the dangers of sports wagering and how to avoid undesirable situations.[5]

The NCAA has established additional measures to prevent any sports wagering. The NCAA Division I Men's Basketball Championship cannot be played in any area where gambling activities based on the outcome of the game are permitted. As stated earlier, this includes Oregon, Nevada, Delaware, and Montana. The NCAA also does not allow its committees to gather in casinos. The organization requests that corporate sponsors do not undertake promotions connected to the outcome of games. Background checks are performed on all members of the organization, including game officials who are refereeing for the Division I Men's or Women's Basketball Championships, in order to confirm that the individuals have no past history of sports gambling.[6]

The NCAA claims that much of the money from sports wagering on college campuses is used for illegal purposes, including the sale of narcotics and loan sharking. The FBI readily acknowledges that nearly all college campuses have illegal student bookies. If a student-athlete becomes indebted or addicted to gambling, a bookie may force the student-athlete to participate in point-shaving to pay his or her debts or as a means to continue his or her gambling behavior.[7] It is also believed that money from illegal sports books is laundered through the legal sports books in Nevada. Steve DuCharme, former chair of the Nevada Gaming Control Board, stated that it is not possible to know how much illegal money is indeed laundered through legal sports books. However, based on the information gained from wiretaps, it is thought to be millions of dollars.[8]

The NCAA does not feel that prohibiting sports wagering on collegiate sports is a significant threat to the Nevada economy. In 2002 the sports books produced revenue of $110 million, in comparison with $93.37 billion from other gaming revenue.[9] Hence, the elimination of collegiate sports wagering will have a small impact, if any, on casino revenues. Additionally, because the casino revenues are not greatly affected, neither is state income from these activities. The NCAA also believes that the presence of sports gambling in casinos actually limits the Nevada economy because many amateur and professional sports leagues maintain policies that prohibit them from staging events in Nevada because of the existence of sports betting. Regardless of the revenue lost because events are held at alternate sites, it is still evident that the sports wagering revenues are not significant for Nevada casinos.

Gambling studies prompt concern that college sports wagering leads to addictive gambling behavior by youth. Research conducted by the American Academy of Pediatrics indicates that over one million teens in the United States are addicted to gambling. Another study conducted by the Harvard School of Medicine reports that an estimated 6 percent of teenagers under the age of 18 have a serious gambling problem. A Gallup poll conducted in 1999 showed that nearly twice as many teenagers wager on sporting events as adults. The NCAA believes that if sports wagering throughout the United States were banned, youth would be prevented from establishing these addictive behaviors.[10] Although banning sports wagering would provide uniformity nationwide, it would not prevent the existence of other means of sports betting, such as illegal bookies and Internet gambling.

A study conducted by the University of Michigan Department of Athletics, on 3,000 NCAA Division I student-athletes (1,500 football players, 750 men's basketball players, and 750 women's basketball players), supports much of the NCAA's concerns. The research indicated that 72 percent of student-athletes have gambled in some form since entering college, with 80 percent of males gambling in some way since attending college. From all the student-athletes surveyed, it was found that 35 percent have gambled on sports while at college, including men and women. The study found that nearly 45 percent of males gambled on sports. Over 5 percent of male student-athletes provided inside information for sports gambling purposes, gambled on a game in which they participated, or accepted money for playing poorly in a sporting event. The mean amount of money bet on a single sporting event through a bookie was found to be $57.25. An average of $225 was wagered each month.[11] These findings indicate that sports wagering is a problem that cannot be ignored on the campuses of NCAA member colleges.

Research conducted at Connecticut State University highlights some important findings concerning student-athletes and the conflicts that may arise at universities. The main purpose of the study was to examine "the interaction of gambling and problem gambling with other risk-taking behaviors in students attending college in a pro-gambling culture with many legalized gambling opportunities."[12] The results of the study recognize that there are higher rates of problem gambling among student-athletes who participate in collegiate sports than among non-athletes. Student-athletes who are problem gamblers and in significant debt, notably to bookies and loan sharks, are especially susceptible to point-shaving and other game-altering actions. This study found that student-athletes gamble significantly more than non-athletes and have increased levels of problem and pathological gambling. Male students are four times more likely than females to have a gambling problem (18.3% for males and 4.4% for females). However, both male and female athletes are at greater risk than non-athletes. The study concluded that coaching staff and student-athletes should receive specialized education regarding sports wagering.[13]

Critics of the NCAA claim that the organization does not invest sufficiently in gambling prevention programs, even though they gain much revenue from college sports. The NCAA says that approximately 94 percent of all its revenue, including money received from the $6 billion CBS contract, is returned to member colleges. The money supports the nearly 363,000 men and women athletes who participate in the NCAA.[14] The number of programs the NCAA is able to support is certainly limited by the association's resources. However, critics contend that the NCAA is shirking its responsibility regarding sports wagering and placing too much blame on other parties. Perhaps with additional educational programs concerning sports wagering, the NCAA would be able to have a stronger impact on these gambling problems.

The NCAA maintains that banning sports wagering is necessary to the vitality and integrity of sports. It has adopted NCAA Bylaw 10.3 in an attempt to limit sports wagering by athletes. Though limited, the NCAA has initiated some educational programs to address this issue. The organization believes that much of the money from sports wagering is used for illegal activities and that the revenue lost from banning legal sports betting is not significant in comparison with other gaming revenues for Nevada casinos. The NCAA also cites increased gambling among youth as a major concern and believes that prohibiting legal sports wagering might stem this problem.

The American Gaming Association

The American Gaming Association (AGA) asserts that the NCAA is misled in many of its claims. The AGA "represents the commercial casino entertainment industry by addressing federal legislative and regulatory issues affecting its members and their employees and customers, such as federal taxation, regulatory issues, and travel and tourism matters."[15] This association agrees that a problem exists regarding sports wagering, but disagrees that banning the legal sports book in Nevada would have a significant effect on deterring student-athletes from gambling.[16] Although both sides concede that there are problems, they differ on how to resolve the issue.

The AGA agrees with the NCAA that a sports wagering issue exists on college campuses nationwide. But as an association that represents the industry, the AGA defends the legality of sports books based on a number of points. First, it contends that the betting that occurs in Nevada makes up only about 1 to 3 percent of the total amount of money wagered on sports. Second, Nevada sports books assist the NCAA in discovering unusual point movements. Third, newspapers would not remove point spreads from print, even if sports gambling were banned nationally. Fourth, the AGA claims that sports gambling is an important aspect of the Nevada economy. Finally, a federal ban on sports betting may conflict with states' rights. The AGA provides persuasive evidence about the effect of sports wagering, and a closer look at each of these points is warranted.

As the NCAA admits, students are able to place sports bets through illegal student bookies and Internet gambling. Eliminating the sports book in Nevada would affect only the 1 to 3 percent of people who currently use that channel. The betting in Nevada is limited to those who are over the age of 21 and physically present in the state. The state of Nevada is able to monitor and record the bets, as well as collect taxes on the winnings. Hence, the AGA claims that the true problem lies not in the legal sports books in Nevada, but in the illegal bookies and Internet gambling. The vast majority of gamblers are not affected by whether the legal sports books exist. The AGA says that focusing on the sports books only provides a face-saving measure about the overall legitimacy of sports for the NCAA and is not the answer to the larger problem of illegal sports wagering and youth gambling.[17] A large facet of the NCAA's argument to ban legal sports wagering is the "morality argument." The NCAA believes that sports gambling undermines the integrity of collegiate athletics. With an ancestral heritage that began with the Puritans, the cultural tradition of religious society contains an aspect of morality. The AGA refutes this so-called "morality argument" and asserts that between 80 and 90 percent of people in the United States support casino gaming. The association says that the attitude of those who attend church is similar to the attitude of the rest of the United States.[18]

There is disagreement regarding the ability of Nevada sports books to uncover unusual point movements. The AGA recognizes that the Nevada casinos are not able to detect and prevent every point-shaving incident. However, the casinos provide the NCAA with what information is available through a direct computer link. This offers an additional means of discovering any odd movements but is not a definite means of tracking all discrepancies. Furthermore, the AGA claims that there has not been an increase in the occurrence of point-shaving incidents since the advent of sports books. Although several scandals took place in the mid-1990s, there were more players and more teams involved in incidents during the 1940s and the 1950s, before sports books existed in Nevada in their current form.[19]

The AGA does not believe that newspapers would be pressured to stop publishing point spreads if legal sports books were banned. Nevada sports books are not the only source of point spreads. Danny Sheridan, a sports analyst for *USA Today,* is also a major source of point spreads. In addition to this, students and other gamblers would have access to the spreads from offshore Internet gambling Web sites, independent sports analysts, and toll-free phone numbers. The Newspaper Association of America reported to the House Judiciary Committee that its members would continue to publish point spreads, and they maintain that it is their constitutional right as delineated in the First Amendment. It is a service enjoyed by readers, not all of whom gamble.[20]

Although the NCAA contends that the elimination of legal sports books in Nevada would have either a neutral or a positive effect on the state's economy, the AGA states that it would have a negative impact. These are the expected assertions from each organization, given the groups they represent. The AGA says that many tourists visit Nevada during the Super Bowl and March Madness. They find it convenient to be able to place bets on these events, bets that are usually less than $50. From these visits, Nevada also generates a significant amount of money in non-gaming revenue as tourists support other local activities. The Professional and Amateur Sports Protection Act of 1992 exempted Nevada and other states that previously had some form of sports gambling because of the belief that applying the act to them would negatively impact the economy of those states. The AGA believes that this is still the case.[21]

The AGA contends that a federal ban on sports books in Nevada (and other states where it is currently legal) would create serious constitutional issues and that if Congress approves legislation banning sports books in Nevada, it will establish a perilous precedent for the federal government to intervene in state gaming policy rulings. In other words, even if a state referendum legalized sports wagering, the federal law would prohibit such actions.[22] The Tenth Amendment of the Constitution states, "The powers not delegated to the United States by the Constitution, nor prohibited by it to the states, are reserved to the states respectively, or to the people." In past precedent, gambling has been an activity decided on by the state. If new legislation is challenged, it may affect any current laws, most notably the 1992 Professional and Amateur Sports Protection Act.

The National Gambling Impact Study Commission

In June 1999 the National Gambling Impact Study Commission released its findings. The commission was appointed by Congress "to conduct a comprehensive legal and factual study of the social and economic implications of gambling in the United States."[23] The committee refers to the aforementioned Professional and Amateur Sports Protection Act of 1992 as the original legislation banning sports wagering in all states that did not have preexisting statutes legalizing sports betting. As stated in the report, only Nevada and Oregon offer a form of sports gambling. Nevada allows sports books in casinos. Oregon employs a state lottery game that is based on sporting events played in the National Football League.[24]

The Interstate Wire Act of 1961, known also as the Federal Wire Act, is used as additional leverage against sports gambling. The act prohibits gambling entities from using wire communications to transmit bets, wagers, or other information that assists in the placing of any bets or wagers, related to "any sporting event or contest," across state lines or across the national borders of the United States. Anyone who violates this law is subject to fines or imprisonment for not more than two years. The Federal Wire Act provides the federal government with a means of control over interstate and international sports gambling.

The commission highlighted several key points from its proceedings. It stated that because sports betting is illegal in many states, it is not able to provide any of the positive aspects associated with other forms of gambling, such as tax revenue and job creation. Realizing that simply legalizing sports wagering is not the answer, the commission recognized that sports gambling indeed threatens the integrity of sporting events. It places student-athletes in precarious situations when faced with indebtedness or when problematic gambling behavior emerges. This can cause great harm to individuals who become involved in scandals at universities. These claims are reinforced in the study conducted by the University of Michigan, which found that over 45 percent of male collegiate football and basketball athletes admit to wagering on games, despite the NCAA Bylaw 10.3 prohibiting such behavior. The research of the commission calls for additional studies to be conducted regarding the issue of underage gambling because evidence suggests that sports wagering leads to other forms of gambling. The National Gambling Impact Study Commission wishes to discover how this trend can be prevented and suggests that legal ramifications be adopted to discourage others from luring underage persons into addictive gambling behavior.[25]

The commission recognized that the NFL, MLB, and the NBA have each issued rules clearly stating that wagering on a player's own sport is grounds for removal of any athlete or coach from the team. Each team provides referral services for any gambling-related problems of its players or staff.[26] Although national sports certainly have had problems with sports gambling among their players, most notably Pete Rose, the issue of sports wagering is most controversial among collegiate student-athletes. Perhaps it is because there is no salary in college sports that student-athletes get involved in sports wagering with a misguided belief that it will be a good source of money. The minimum salary for a Major League Baseball player for 2004 is $300,000,[27] and the minimum salary for a National Football Player with no credited seasons is $230,000.[28] With such high salaries, there is no need to gamble on one's own sport and risk removal. On the contrary, however, student-athletes have been known to get involved in sports wagering on their own sport. This obviously causes a large source of conflict among players. The NCAA has taken action to prevent sports betting problems, though their success has been limited. The organization utilizes advertisements during popular games, such as the Division I Men's Basketball Tournament, and has established additional gambling education programs to inform the public of the risks of sports gambling. It is also in the process of developing other similar services with the ultimate goal of increasing awareness.[29] Although the commission acknowledged these programs, it did not specifically recommend further action. This will likely come after additional research is conducted concerning the problems stemming from sports wagering.

Potential Tax Revenue from Collegiate Sporting Events

As noted earlier, the revenue derived from the sports book in Nevada for 2002 was over $110 million. Approximately $40 million, or 35 percent, of this was wagered on collegiate sports. Other gambling revenue in Nevada for 2002 was $93.37 billion. This means that the sports book in Nevada accounted for only 1 percent of total casino revenue. Christiansen Capital Advisors estimates that the U.S. revenue from the Internet sports books was about $1 billion for 2002. Further, the company approximates that $370 million was wagered on college sports. The Internet gambling sites would benefit if the NCAA were successful at banning legal sports wagering. This would purportedly move the current sports gambling in Nevada to offshore Internet Web sites, increasing revenues for those sites by an estimated 10 percent.[30]

Although the NCAA argues that the integrity of the sports must be maintained, the organization has surely viewed the effects of legalizing sports gambling as a way to increase state tax revenue and to regulate sports wagering. Christiansen Capital Advisors estimates that the total sports revenues including legal and illegal sources, is $1.1 billion. Applying Nevada's gaming tax rate of 6.5 percent for simplicity (not accounting for local taxes), the estimated tax revenue from the proposed legal betting on collegiate sporting events would be $70 to $80 million. Would this amount be a worthwhile reason to legalize sports gambling on a national level? The amount of that revenue provided to each state and local government would be significantly diminished, considering that regulatory agencies would need to be established. Additionally, the NCAA would lobby for part of this revenue to fund programs aimed at helping educate student-athletes and others about the problems of sports wagering. With so many stakeholders of this small amount, it would seem difficult to justify legalizing sports gambling solely for the purpose of increased tax revenues.[31] Proponents of legalization would still contend that it would severely limit the amount of betting through bookies or Internet gambling, allow the government to track wagers much more easily, increase jobs, and help the local economy. Critics, including the NCAA, would not recognize these economical factors, but rather would point to the rise in underage gambling and the problem of point-shaving and other scandals by student-athletes. The NCAA desires to maintain the integrity of intercollegiate sporting events and is adamant about this position.

Overall Potential Tax Revenue

What is the potential tax revenue if all forms of sports wagering are legalized, not just from the viewpoint of collegiate sports? This is a slightly more complex issue. It is claimed that legalized sports gambling would not create any new gambling, but simply legalize that which already occurs. Two main tax issues have prompted gamblers to use bookies and Internet gambling. The federal wagering excise tax used to be a significant issue concerning sports betting. On the recommendation of the Commission on the Review of the National Policy toward Gambling, it was lowered to a nominal 0.25 percent, in an effort to stimulate betting. A significant increase in the sports book of Nevada from 1982 to 2001 showed this to be effective. Furthermore, the commission called for the repeal of the income tax on legal winnings. Removing this tax would weaken one of the main advantages of a bookie; this has not occurred as of yet.[32] "Sports gambling" is actually made up of two different games: multiple-choice sports pools and head-to-head betting on the outcome of a single sporting event. Multiple-choice sports pools are high-takeout games that are financially safe for the operator and expensive for the gambler. Oregon's game called Sports Action falls into this category. Sports Action has an effective takeout rate, the percentage of the handle that Oregon keeps, of 38 percent. Takeouts from illegal pool cards are significantly higher and can range up to 65 percent. Sports pools are for the casual bettor who does not closely follow the specific sport. The national revenue potential for a game that is structured similarly to Sports Action is $205 million.[33]

Sports bookmaking is the other form and is a head-to-head bet against a bookmaker, or bookie, at a fixed price on a singe sporting event. Estimates of illegal sports bets are extremely varied—from $80 billion to $500 billion. The hypothetical takeout percentage for an evenly balanced sports book, as noted by the Commission on the Review of the National Policy toward Gambling, is 4.6 percent. The takeout percentages for Nevada sports books varied from 1.85 percent in 1982 to 5.79 percent in 2001. The exact reason for the rise in takeout percentages is unknown. However, Nevada sports books are clearly functioning better than they previously were. If the theoretical legal sports books handled the lower estimate of $80 billion, and the takeout rate was 4.6 percent, as mentioned previously, the potential revenue would be $3,680 million. Using the same parameters with a takeout rate of 5.79 percent, which was the takeout rate for Nevada sports books in 2001, the potential revenue would be $63.2 billion.[34]

Part of the $3.68 billion to $6.32 billion in potential gross revenue would be allocated to operating expenses for handling the $80 billion in wagers. The remaining cash flow would be used for profit and taxes. This assumes that bookmakers in the United States would operate as private sector, for-profit firms. In Nevada, 6.5 percent of gross gambling revenue is paid to the state, and an estimated additional one percentage point is paid to the local government in the form of levies and licenses fees. The large Nevada sports books are owned by casino companies, so it is assumed that the effective tax rate is 7.5 percent. The tax proceeds from gross gambling revenue of $3.68 billion at a tax rate of 7.5 percent are $276 million. The tax returns from gross gambling revenue of $6,320 million at a tax rate of 7.5 percent are $474 million. Combining the tax receipts from pool cards, the total potential tax revenue for a takeout percentage of 4.6 percent is $481 million. The total potential tax revenue for a takeout percentage of 5.79 percent is $679 million. Although income of $481 million to $679 million is considerable, it is not the answer to solving significant monetary needs. The media often ambitiously asserts that legalizing sports gambling would solve long-standing issues such as the size of the federal budget deficit. However, the revenue is significant enough to merit consideration regarding the usefulness of this money and where it can logically be employed to resolve financing issues.[35]

Success of Sports Wagering Abroad

Other countries have had sports gambling on a national scale for a number of years. The closest comparison to the United States is with the United Kingdom. Several large private-sector companies offer sports gambling to the public there, which in turn provides additional tax revenue to the government. The Camelot Group, for example, operates the U.K. National Lottery. The company produced revenues of $6.9 billion for the fiscal year ending March 2002. Roughly 30 percent of the company's income goes to worthy causes throughout the United Kingdom. Camelot maintains 0.5 percent as profit. Ladbrokes is the country's largest off-track bookmaker. The company generated $5.4 billion of revenue for the fiscal year ending December 2002. Ladbrokes maintains shops in the United Kingdom, Ireland, and Belgium. William Hill is the second largest bookmaker in the United Kingdom, generating $5.3 billion in revenues for the fiscal year ending December 2002. The company has 1,500 stores in England, Scotland, and Wales.[36] The United Kingdom has been able to use tax revenues from sports wagering toward public projects and to fund projects for sports.[37] Nearly $700 million in tax revenue was provided by sports wagering locations in the United Kingdom for 2002.[38]

Although sports wagering has been highly successful from a tax receipt standpoint, the United Kingdom has run into some problems relating to betting exchanges, which are "a novel form of betting that cuts out the middleman by allowing punters [betting parties] to match bets directly placed by other punters, one backing and the other laying on any given event."[39] It is argued that these exchanges, which are wildly popular and highly profitable, increase the occurrence of cheating and corruption in sports wagering by presenting irregular wagers to its customers, such as "the number of catches taken by fielders wearing sunglasses" in an Ashe Series cricket match that took place in England during 2004.[40] Because these types of wagers can be easily manipulated by the athletes, many of the professional sports leagues argue that bets should be standardized and regulated by the Gambling Commission with input from the leagues themselves. The Betting & Gaming Group concluded that "greater transparency and disclosure" by the exchanges as well as increased regulation and scrutiny by the Gambling Commission would increase the integrity of the athletic events and decrease instances of cheating and profiting from inside information.[41]

Though the United States may be doubtful about legalizing sports gambling nationally, the United Kingdom has implemented a relatively successful model that has increased regulation of sports wagering and benefited the government through the increase in tax receipts.

ATTEMPTS TO BAN SPORTS WAGERING AND CURRENT LEGISLATION

Nevada started licensing bookmakers in 1949. They were restricted from receiving bets on amateur sports events held in Nevada or on events held outside the state in which a Nevada team played.[42] In 1992 Congress passed the Professional and Amateur Sports Protection Act, which made most forms of sports wagering illegal, except in those states where it already existed: Nevada, Oregon, Delaware, and Montana. Nevada is often the target of attacks on sports wagering because it is the only state that currently has sports books (Oregon maintains a sports lottery). The NCAA claims that Nevada is a main factor in the ongoing sports wagering problem, whereas other organizations, such as the American Gaming Association, claim that banning legal sports betting would only increase the use of illegal bookies and Internet gambling.[43]

The 1992 Professional and Amateur Sports Protection Act

Section 3702 of the Professional and Amateur Sports Protection Act states,

> It shall be unlawful for a governmental entity to sponsor, operate, advertise, promote, license or authorize by law or compact, or a person to sponsor, operate, advertise, or promote, pursuant to the law or compact of a governmental entity, a lottery, sweepstakes, or other betting, gambling or wagering scheme based, directly or indirectly, on one or more competitive games in which amateur or professional athletes participate, or are intended to participate, or on one or more performances of such athletes in such games.

Recent attempts by Congress to ban sports wagering on college sports have been executed through the use of proposed amendments to the 1992 Professional and Amateur Sports Prevention Act.

Several attempts have been made to ban gambling on collegiate sporting events. The first attempt was made in 2000 with the Student Athlete Protection Act, H.R. 3575, and the Amateur Sports Integrity Act, S. 2340. The former Act, sponsored by representatives Lindsey Graham and Tim Roemer, petitioned for the banning of sports wagering on collegiate sports nationwide because of its undesirable effects, such as undermining the integrity of college athletics. The Amateur Sports Integrity Act is the Senate version of the aforementioned Student Athlete Protection Act. The legislation essentially aims to remove the grandfather clause from the 1992 Professional and Amateur Sports Protection Act. The first attempt was not successful and was never considered on the Senate floor.[44]

The Amateur Sports Integrity Act, S. 718, was reintroduced to the Senate on April 5, 2001. The bill was presented by Senator John McCain, and its supporters hoped to achieve the same goals as before. Both sides, including the NCAA and the AGA, have passionately voiced their arguments regarding this issue. The bill for consideration in the House of Representatives is known as the Student Athlete Protection Act, H.R. 1110. This act was introduced on March 20, 2001, by representatives Lindsey Graham, Tim Roemer, Tom Osborne, and Ron Kind and 22 cosponsors.[45] The bill was not successfully passed.[46]

In 2003 Senator John McCain renewed his effort to ban Nevada sports books from accepting wagers on college or amateur sporting events. The issue was raised nearly two years after previous legislation had not passed. McCain was quoted as saying, "Congress must take action to close the loophole in current law that allows just a handful of states to serve as national clearinghouses for betting on our youth."[47] Senator Harry Reid stated that he would continue to battle against McCain's bill, believing that a ban on betting is misguided.[48] The NCAA and the AGA again battled over this controversial topic.

On the national level, the previous momentum for action against sports gambling has diminished. In March of 2004, McCain, long a leader of the anti–sports gambling effort, declined a renewed attempt to further legislation. He recognized that a betting ban is not likely to advance in Congress until new evidence opposing it is discovered. From the time of the legislation's undertaking in 2000, the AGA and Nevada's congressional delegation launched strong resistance and successfully impeded McCain and his committee.[49] Further, at the NCAA meeting in 2006, there was no mention of continuing to push for a ban. Although the association still asserts that this issue is a top priority, it states that it is waiting for the bill to gain momentum in Congress.[50]

Sports betting received attention at the state level in New Jersey in 2004, as the state searched for methods to increase lagging state budgets. Under the proposed plan, which has been moved to the New Jersey General Assembly, the state would tax sports wagers made in person at a casino, and a portion of the tax would be allocated to reimburse hospitals for the cost of medical care for the working poor and uninsured. The proposed increase in tax receipts is estimated at $90 million and does not include the increase in business for Atlantic City hotels and restaurants.[51] New Jersey has stated that no betting would be allowed on college or other amateur sporting events. If this bill is approved by the New Jersey General Assembly, the state will present a referendum to the voters and begin to work on a challenge of the 1992 Professional and Amateur Sports Protection Act. Backers of the proposed legislation maintain that, because the 1992 Professional and Amateur Sports Protection Act allowed New Jersey until January 1, 1994, to approve sports wagering for Atlantic City, the state has a reasonably strong case to overturn the act. Previously, the legislature failed to place the issue on the ballot because it was heavily opposed by Senator Bill Bradley and the National Basketball

Association.[52] Although New Jersey politicians claim that the legislation will help the economy and lead to job creation, and outlook on overturning the 1992 act is optimistic, the referendum has a high likelihood of being defeated in the general assembly because of the negative publicity that may result from the state's stance on sports gambling.

CONCLUSION

As with most disagreements involving gambling, the sports betting argument will not be resolved easily. With the strong forces of the NCAA and its member schools disagreeing with the AGA and casinos, neither side will be able to achieve progress if concessions are not made. The NCAA has stated, and studies have shown, that gambling among student-athletes is an issue of concern. However, any action taken to ban sports wagering will not have a significant effect on this problem because of the prevalence of illegal bookmakers and Internet gambling. It can be argued that the legalization of sports gambling might lead to increased gambling problems with student-athletes because of accessibility; however, legalization would also allow for much more regulation than having it in the hands of bookies and Internet gambling Web sites. While the NCAA argues for a ban, it should concurrently strengthen its own educational programs to inform student-athletes of the pitfalls of sports gambling and such tactics as point-shaving.

Federal legislation during the past few years has focused only on banning collegiate betting on sports books in Nevada. Laws that would legalize sports betting have not formally entered the congressional arena. With increasing federal budget deficits and possible tax increases, the potential tax revenues from sports gambling, though not staggering, might be considered as a way of increasing funding for educational programs and assisting the government with financing problems. If the federal ban is lifted, local economies might also benefit, and jobs could be created. The AGA may not be able to assist in extending sports gambling nationwide, but certainly it has many valid arguments against the banning of sports wagering.

Sports wagering will always exist, whether bettors visit a Las Vegas casino, the well-known bookie, or the new Internet gambling Web site. Regardless of the path that legislation takes, action should be taken to increase awareness of the problem of sports gambling among student-athletes. Without a solution to this problem, point-shaving scandals will always be a threat. Sports gambling can always have a potential negative effect on the integrity of sporting events. Through public debate of the issue and careful deliberation over the social, political, and ethical ramifications of sports wagering, legislators will be able to determine the correct outcome.

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5

Native American Gambling: Economic Development or Dependence?

There are over four million Native Americans living in the 567 federally recognized Indian Tribes in the United States. Over the past 20 years, the quality of life for American Indians living on reservations has increased tremendously. However, the economic welfare statistics of these tribes still consistently place them far behind the rest of the American population. Although the cultural and historical reasons for this discrepancy are important, they will not be the focus of this chapter. This chapter concentrates purely on the rationale for Native American gambling. More specifically, this chapter concentrates on the effects that the Indian Gaming Regulatory Act (IGRA, 1988) have had on the Native American population in the United States.

This issue is of importance because many financial and political effects must be considered during development of plans for new casinos, creation of tax codes, or drafting of federal legislation, for example. States cannot impose taxes on American Indian casinos, but the IGRA allows states to negotiate compacts for exclusive rights with tribes for a share of their revenues. One-third of the 22 states that permit “Las Vegas–style” games on American Indian land receive significant revenue from the tribes.[1] Although certainly many other aspects must be considered when these political tasks are undertaken, the effects that tribal casinos have had on the welfare of the Native American population, if significant, should be weighed heavily. And if not, then the claims that tribal casinos have been a huge success need to be examined more closely. Although the data available limit the scope of this study, it should be recognized that concerns over the social welfare of Native Americans since the passing of the IGRA (drafted as a direct result of the decision of the *California v. Cabazon* case) have even served as an impetus for a recent push for Congress to draft further legislation. Some of these proposed bills call for more closely measuring the negative effects that casinos have had on Native Americans, altering the legal uses for Indian casino revenue, and changing the way the oversight committee operates. Further, in light of the recent Jack Abramoff lobbying scandals, the political associations of tribal leaders have been called into question, thereby implicating the casinos that they run.[2]

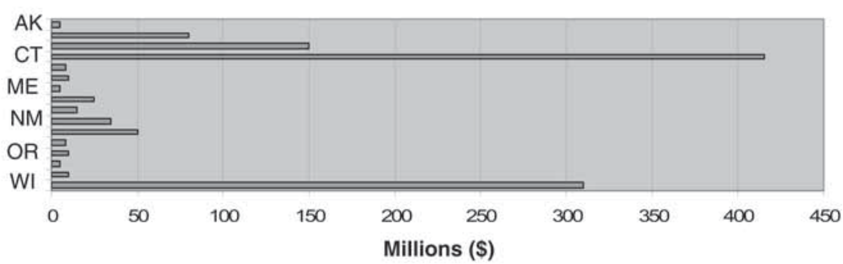
Tribal gaming is a $19.6 billion per year industry, and it is getting larger,[3] as reports from February and June 2005 indicate with headlines such as, "Tribal casino takes are soaring, surpassing those in Nevada."[4] According to excerpts from Dr. Alan Meister's study on Indian gaming, the growth rate of Indian casino revenues from 2003 to 2004 exceeded 15 percent.[5] The number of tribes with gaming facilities grew about 3 percent in 2004 (from 221 to 228), and the number of Indian gaming facilities saw growth at about 5 percent in 2004 (from 385 to 405).[6] Although they are highly correlated with the development of new gaming facilities, the numbers of gaming tables and gaming machines have seen tremendous growth as well. In 2004 the number of gaming machines grew by 10.7 percent, and the number of table games grew by 9.4 percent. These numbers are significantly larger than the percentage of growth we see in new gaming facilities; therefore, the currently existing gaming facilities clearly are continuing to grow. In 2004, for instance, in California there were no new tribes with gaming facilities, and there were no additional Indian gaming facilities in the entire state. However, California saw a 4.5 percent growth in the gaming machines and saw 16.9 percent growth in the amount of table games within its already existing 54 Indian casinos.[7]

Even non-gaming revenue at Indian gaming facilities saw significant growth in 2004. This revenue includes money spent by casino patrons on food, beverages, hotel stays, retail purchases, and other entertainment at the gaming facilities. If it were possible to measure the contribution these patrons made to neighboring facilities as a direct result of their visit to the casino, then this revenue would be included as well. However, because this data is practically nonexistent, the reported non-gaming revenues have the effect of underestimating the total economic contribution of expenditures at casinos. Non-gaming revenue grew by 7.6 percent in 2004 or, from $1.79 billion to $1.93 billion dollars. However, as discussed in following sections, the stipulations of the IGRA are less strict about non-gaming revenue than they are about revenue directly created and received from gaming expenditures at casinos. Therefore, the effects that these revenues have on Native American welfare are much less than the effects of revenues received from gaming. Also, non-gaming revenues make up less than 10 percent of gaming revenue. In general, it can be asserted that non-casino revenue does not play an important role for Native American casinos.

Furthermore, in the economic impact analysis that Dr. Alan Meister performed, he estimated several effects that tribal gaming has had on the overall economy. In total, the claim is that Indian gaming in the year 2004 contributed about $53.1 billion in output, $19.7 billion in wages, and 545,000 total jobs and helped create about $6.3 billion in tax revenue. Indian gaming in the year 2003 saw about $45.3 billion in output, $17.3 billion in wages, 489,000 jobs, and $5.7 billion in tax revenue. When the revenue-sharing agreements that each state has developed are considered, totaling $889 million, the total tax revenue garnered in 2004 reaches $7.2 billion. Of the 545,000 jobs supported by Indian casinos in 2004, 279,000 of those jobs were directly induced, and 266,000 were indirectly supported by the output of Indian gaming. The $6.3 billion of tax revenue mainly comes from secondary economic activity as estimated by the input-output analysis that Dr. Alan Meister conducted. In his study, Meister used the Impact Analysis for Planning (IMPLAN) method, which has been in use since 1979 and is used by the Federal Emergency Management Agency (FEMA) and the Bureau of Economic Analysis; it is also very similar to the format used by the United Nations. For most of the economic estimations such as tax revenue, jobs created, and wages distributed, IMPLAN came into use.

Figure 5.1 shows the amount of revenue shared by the tribes and states according to their compact agreements in 2004. As one can see, states such as Connecticut, Wisconsin, and California have reasonably substantial revenue-sharing agreements with their tribes, whereas the governors of states such as Minnesota and Washington often receive flak for failing to

Figure 5.1
Revenue Sharing between States and Native American Casinos



Source: Analysis of the Economic Impact of Indian Gaming in 2004, National Indian Gaming Association (January 2005).

negotiate successful compacts for their states. At this time, the IGRA does not explicitly mandate that states receive a portion of the revenue from the tribes. However, it is pervasively assumed that changes to the IGRA will be made in the future and that among those changes will be an additional clause that provides the framework for adopting revenue-sharing agreements in new compacts.[8]

The issue surrounding revenue-sharing agreements is a tricky one. From the states' perspective, they are permitting such activity to go on within their borders, and most likely their residents are the patrons of Indian casinos on reservations in their state. Therefore, as with any other commercial activity, the states should have the right to receive some portion of the profit from these casinos. However, from the Native American viewpoint, they are a sovereign nation and not subject to the laws and taxation principles of the states in which they are located. Also, a fear often expressed by politicians who side with Indian tribes is that the states will basically coerce the tribes rather than meet them as equals at the bargaining table.[9] Hence the issue is once again whether the tribes are truly sovereign or have become merely wards of state government. Two well-versed political scientists have raised the question of whether compacts are "*compromises,* or are they *compromised?*"[10] The focus of Steven Light and Kathryn Rand's work is the political consideration of the impact of Indian gaming, mainly on sovereignty of the tribes. Their work is considered further throughout this chapter and more specifically when we consider the pros and cons of tribal gambling.

Clearly, given the preceding facts and figures, Indian gaming is becoming a significant factor in the U.S. economy, in addition to being the most significant contributor to the Native American economy. Although commercial casinos brought in just under $30 billion in revenue last year, Indian casinos grew to nearly $20 billion. The growth rate of Indian casinos has also significantly outpaced commercial casino development—even since the year 2000—as the establishment of Indian casinos has become more complete. Dr. Alan Meister sees no reason to assume that the growth of Indian casinos will stop and even predicts that they will continue to grow faster than their commercial counterparts. Obviously, as these markets, mature and the base of revenue becomes much larger, Indian growth rates will have to decline. However, as more and more states begin to negotiate casino development with the tribes located within their states, continued expansion is to be expected.[11] Another reason it is important to consider the influence of casinos on Indian welfare is that at first glance there appears to be a significant relationship between casinos and expedited improvement in quality of life. Table 5.1 shows a chart created by a group at Harvard when they looked at some of the simple observable results from the 2000 U.S. census.

Table 5.1
Changes on Reservations Other than Navajo

(Changes 1990–2000 presented in points unless indicated as %; OTSAs excluded)			
	Non-Gaming	*Gaming*	*U.S.*
Real per capita income	+21%	+36%	+11%
Median household income	+14%	+35%	+4%
Family poverty	-6.9	-11.8	-0.8
Child poverty	-8.1	-11.6	-1.7
Deep poverty	-1.4	-3.4	-0.4
Public assistance	+0.7	-1.6	+0.3
Unemployment	-1.8	-4.8	-0.5
Labor force participation	-1.6	+1.6	-1.3
Overcrowded homes	-1.3	-0.1	+1.1
Homes lacking complete plumbing	-4.6	-3.3	-0.1
Homes lacking complete kitchen	+1.3	-0.6	+0.2
College graduates	+1.7	+2.6	+4.2
High school or equivalency only	-0.3	+1.8	-1.4
Less than 9th grade education	-5.5	-6.3	-2.8

Source: Taylor, Jonathan B. and Kalt, Joseph P. *American Indians on Reservations: A Databook of Socioeconomic Change between the 1990 + 2000 Censuses.* Cambridge, MA: Harvard Project on American Indian Economic Development, 2005. See: www.ksg.harvard.edu/hpaied/pubs/pub_151.htm.

These numbers suggest that there might be a significant correlation between gaming and a stronger performance of welfare improvement over time. In 13 of the 15 categories, gaming tribes performed better than non-gaming tribes. Although at first glance it is apparent that Native Americans' lives have improved since the inception of the IGRA, will advances and growth in Indian Gaming result in comparable gains in Native American welfare in the future? Does this improvement in the lives of Native Americans justify the costs of gambling in the communities that surround these casinos? Are states using Native American casinos as an agent for revenue while leaving these casinos largely unregulated?

INDIAN GAMING REGULATORY ACT

The impetus to address the Indian gaming situation came from a court case involving a tribe of Native Americans from California called the Cabazon Band of Mission Indians. In 1953 Congress passed a law that authorized states to extend state criminal laws to Native Americans. This law, known as Public Law 280, was often used by the state to justify regulation of activity on reservations. However, when states began to impede the rights of tribes to operate gaming facilities on their reservations, the Cabazon tribe forced the state of California to take them to the Supreme Court. In *California v. Cabazon* (1987), the Supreme Court ruled that Indian tribes had the inherent right to self-rule and that Public Law 280 applied only to limited circumstances, particularly when criminal activity was taking place between Indians and non-Indians. Specifically, the courts ruled that Public Law 280 was not enough justification for states to impede on tribal sovereignty in civil terms.[12] Noticing this glaring legal omission, Congress quickly acted to draft legislation that would help fill this void of confusion, whence came the Indian Gaming Regulatory Act.

In the time between the *Cabazon* decision and the adoption of the Indian Gaming Regulatory Act (IGRA), gaming sprung up nationwide on tribal reservations. This helped charge the atmosphere surrounding debate on the IGRA. In drafting the IGRA, Congress sought to balance tribal rights to sovereignty with the right of a state to regulate what sort of activity takes place within its borders, thereby affecting its citizens. One of the major considerations and justifications for federal intervention in this matter was the issue of organized crime. One major fear that came in discussions of gambling was the concern about organized crime gaining a foothold in the casino industry. Because the business involves transactions with large amounts of cash, many spectators were suspicious that Indians, without private-run management interference or federal intervention, would turn to the realm of organized crime to help them run their businesses and gain political influence. This was definitely something that legislators kept in mind when drafting earlier forms of the bill and that influenced legislators' decision to allow private firms to help run Indian casinos.[13]

According to the opening section of U.S. Code Title 25 Chapter 29, Congress had five main things in mind when considering the IGRA: (1) tribes had begun to utilize the revenue drawn from casinos to generate governmental funding; (2) tribes had turned to outside management, but existing law provided no standards by which those management contracts could be regulated or approved; (3) existing federal law did not provide any clear stipulations for regulation of Indian gaming; (4) at that time, the goal of federal policy involving Indians was to "promote tribal economic development, tribal self-sufficiency, and strong tribal government"; and (5) Indian tribes had the right to wholly regulate any gaming activity on their land that is neither prohibited nor strictly regulated by the state or federal governments.

The major provisions of the IGRA sought to create three separate classes of gaming, and a different regulatory scheme for each class, and put stipulations on the use of casino revenue. The first thing that the IGRA established, the three classes of gaming, are still used today to define various types of gaming in both commercial and Indian casinos. Class I gaming refers to traditional social games with minimal prizes, clearly targeted toward ceremonial Native American forms of gaming. The regulatory authority over these types of games is vested exclusively in tribal governments and is not subject to any of the requirements in the IGRA. Class II gaming refers to bingo and other similar games of inter-player chance, such as lotto, pull-tabs, and punchboards, if played at the same location as bingo. Also included in this are card games where the establishment is not banking any of the money. The regulatory authority over these types of games is vested in the tribal governments insofar as the state in which the tribe is located permits such gaming for any purpose and the tribal government adopts a gaming ordinance that is approved by the National Indian Gaming Commission (which is also established later in the IGRA). Class III gaming refers to every other type of gaming, including slot machines, banked card games, and typical casino games such as blackjack, roulette, craps, any wagering games, and electronic facsimiles of any game of chance. There are three main clauses regarding the regulatory authority of such gaming: the particular form of gaming must already be permitted by the state in which the tribe is located, the tribe must negotiate a contract with the state and have it approved by the Secretary of the Interior, and the tribe must have a tribal gaming ordinance that has been approved by the National Indian Gaming Commission.

Further, the IGRA limits the use of any casino revenue to three major categories: (1) to fund tribal government operations or programs, (2) to provide for the general welfare of the Indian tribe and its members, or (3) to promote tribal economic development. Of course, the tribes are also allowed to make donations to charitable organizations or help fund the operations of local government agencies.

The tribal compacts described in the text of the IGRA are very vaguely outlined. The IGRA does not require the compacts to have any specific terms except that both parties approach the negotiations in good faith—particularly the state, given that the Indian tribe is the party that initiates the negotiations. If this disposition of good faith is in question, the Indian tribe has the right to sue the state in federal court. Many procedures, detailed in the IGRA, are in place to handle these types of situations as they develop. The procedures are not as important as the implications for tribal and state sovereignties, but in general, government mediators step in and utilize loosely constructed general principles, the goal of which is to establish a well-balanced compromise between both parties. It is through these mediums that states are able to negotiate revenue-sharing agreements and other issues of taxation. Although these work on a state-by-state basis, as is evident by the disparity among revenues collected by states, in general they provide a means to mitigate the cost that the casinos incur to the state, and they often times go above and beyond this inferred cost.

In particular cases, it is in the Indian tribe's interest to agree to pay more if the state will promise to help keep commercial casinos banned or kept far away from the prime location of the tribal casino. For instance, in 1992 the Mashantucket Pequot Tribe negotiated such a contract with the state of Connecticut. In exchange for the tribe's promise to share with the state 25 percent of the revenue generated from the Foxwoods Resort Casino's slot machines, Connecticut effectively guarantees them exclusive rights (along with Mohegan Sun, which now has the same contract) to operate slot machines within the state. Since the precedence of this revenue-sharing agreement, many other tribes have offered similar terms and come to settlement on them. Quite recently, Harrah's Entertainment offered similar commercial revenue-sharing terms with the states of Rhode Island and Pennsylvania if they were to grant them exclusive slot machine rights. In Rhode Island, Harrah's has agreed to pay 25 percent of slot revenue up if revenues do not surpass $400 million and a higher percentage to be determined if revenues exceeded $400 million while in Pennsylvania, Harrah's has agreed to pay a whopping 53 percent excise tax on slot revenue.[14] The justification that this commercial entertainment giant offers to Rhode Island legislators is that the facility to be developed in Rhode Island is more of a resort; therefore, it needs fewer taxes to operate its smaller casino. Harrah's Entertainment assists in the management of as many as nearly 200 Indian casinos in North America.

Also established by the IGRA was the National Indian Gaming Commission (NIGC). As an oversight committee on tribal gaming in the United States, with limited regulatory powers, the NIGC was to be funded by a minuscule tax on the revenues of Indian casinos. With the commission's funding limited to 2.5 percent of the first $1.5 million in revenues and 5 percent thereafter, with a cap of $8 million, the effectiveness of this committee has been questioned at every level of government (U.S. Code Title 25). In 2005, Senator John McCain (R-AZ), then chair of the Senate Indian Affairs Committee, introduced the legislation regarding the NIGC. This bill, S.1295, would have forced the NIGC to be held more accountable and would also provided an increased amount of funding, to the tune of .08 percent of Indian casino revenue without any cap. Under this setup, the revenues received by the commission would have increased to about double what they are now and then would have proportionally increased relative to the growth of the industry. This bill would have also allow the NIGC to crack down on off-reservation gaming, which is often seen as a scam that allows the tribes to illegitimately profit by creating and supporting commercial casinos under the guise of tribal sovereignty. In 2006, this bill passed the Senate Indian Affairs Committee but still remains on the agenda of the House Resources Committee awaiting approval for vote.[15]

PRO-INDIAN CASINO ARGUMENTS

There is a lot of literature supporting the propagation of Indian casinos. The study with the most data to back its conclusions was conducted by the Harvard Project for American Indian Economic Development. Authored primarily by Jonathan Taylor, a leading research expert on Indian welfare, *American Indians on Reservations: A Databook of Socioeconomic Change between the 1990 and 2000 Censuses* provides a summary glimpse into the changes in welfare that American Indians experienced during the explosion of tribal casinos. Basically providing two snapshot images of the state of Native American welfare, this study looked at the empirical census data from both 1990 and 2000, breaking it down by every single federally recognized reservation. But aside from the fact that this study neglected to use econometric analysis or examine the revenue-side data, the institution that funded this study receives massive donations from the National Indian Gaming Association (NIGA) to run its research. The NIGA is a non-profit organization of all the Indian tribes that have casinos—it is clearly in their best interest to promote the expansion and growth of the Indian casino industry. Therefore, the research that the NIGA conducts, though mainly objective, often has suspect results that appear to maintain an optimistic outlook on Indian gaming. The *Cabazon* project, one that specifically focuses on economic development with regard to Indian gaming and of which the previously mentioned study is a part, on the whole manifestly supports the expansion of tribal sovereignty and rights—issues that are not so clearly defined on the national political stage. "Essentially, the research of the Harvard Project finds that poverty in Indian Country is a political problem—not an economic one."[16] Their claim is that the economic development of the tribes, which is bolstered by Indian gaming, is merely the means to the end of achieving full tribal sovereignty and self-reliance. In 2004, the NIGA produced their *Analysis of the Economic Impact of Indian Gaming*. This report details much of the alleged success that tribes have had with casinos. Although much of the evidence is anecdotal or qualitative, the report does provide some firm statistical support for its very optimistic outlook for Indian gaming. The NIGA touts statistics such as the fact that in 2005, 69 percent of Americans thought that Indian nations deserve their help, or that 86 percent of Americans thought that Indian tribes benefit from having casinos.[17] The *Analysis of the Economic Impact of Indian Gaming* clearly states that the mission of NIGA is to "protect and preserve the general welfare of tribes striving for self-sufficiency through gaming enterprises in Indian Country."[18] Also included in the association's analysis is a mention of every positive outcome that Indian gaming could have ever possibly influenced, from jobs to roads to schools. In order to further garner sympathy and support, the NIGA points out that there are various shortfalls among the Native American community when it comes to keeping up with national norms and includes notations of various education, poverty, health, and crime statistics.

Other published books that may give the reader a clearer picture of the effects of Native American gambling are *Gambling and Survival in Native North America* by Paul Pasquaretta (2003) and *Indian Gaming and Tribal Sovereignty* by Steven Andrew Light (2005). The latter provides a very thorough analysis of the political implications of casinos through the lens of tribal sovereignty. Again, the researchers behind *Indian Gaming* clearly favor the expansion of tribal sovereignty, and their book is predominately anecdotal and historically based. Information from this book is referenced throughout this chapter.

ANTI-INDIAN CASINO LITERATURE

Legalized Gambling (2006), edited by David Haugen, provides a collection of abridged articles on various gambling topics, such as Indian gaming, Internet gaming, social consequences, personal stories, and a general overview of gaming in the United States. Although not every article in this collection is anti-casino—in fact, it attempts to provide an equal amount of articles for each side—it is one of the only available sources that clearly try to present this point of view. In these articles, once again, we see that the evidence provided is largely anecdotal and subjective. Although this is clearly an important component of the consideration as to whether casinos are a viable and good option for Indian tribes to gain economic independence, anecdotal evidence is very difficult to include in any quantitative analysis or econometric study. Some of the interesting things for legislatures and concerned citizens to keep in mind about Indian casinos are the alleged social burdens that they place on the public: costs to local communities in the form of upkeep, roadway paving, and police patrols and other implied public costs. There are claims that casinos lead to increased crime in the surrounding areas, that the people who are drawn to visit communities with casinos are not the most upstanding citizens of this country, and finally, that the harmful effects on addicted gamblers and ordinary, but excessive, gamblers are not nearly outweighed by the benefits that Indian casinos receive from the economic independence they gain. And these concerns do not consider the larger moral question as to whether gambling should be legalized in the first place, which, as a democratic society, America has determined it should, viewing it as an acceptable form of business practice.

Finally, there is the story about the famous Mashantucket Pequot founder who, on his marriage license, claimed to be "white." Many people point to this as evidence of Native Americans simply taking advantage of a crooked system that seeks to pay reparations to a people that no longer necessarily deserve them. It is true that there were only four registered members of this tribe in 1990; today, however, there are several hundred members. The Mashantucket Pequots now host the largest Native American casino in the country and hence are flourishing as operators of one of the most successful casinos in the world. There are two sides to every story. The next section gives the reader a chance to ascertain whether the advent of Native American Casino gaming has really made a difference in the welfare of tribal members.

COMPARING GAMING AND NON-GAMING TRIBES IN 2005

One fundamental question that needs to be addressed is this: has Native American gambling improved the plight of Native Americans? One way to explore this question would be to test different sets of welfare statistics on two groups: those with gaming and those without. The method that was utilized to determine whether or not there was a statistically significant difference exists is called the unpaired (independent) samples "t" test. The categories (which refer to American Indians on reservations, including Navajo, unless otherwise noted) to be tested included:

(1) median income,
(2) family poverty, unemployment,
(3) percentage of houses that lack kitchen facilities,
(4) actual number of houses that lack kitchen facilities,
(5) aggregate income of tribe,
(6) average aggregate income,
(7) percentage over the age of 25 who are college graduates,
(8) percentage over the age of 25 who have a high school degree,
(9) percentage over the age of 25 who have less than a ninth-grade education,
(10) the actual numbers for each of the preceding three statistics,
(11) percentage of families living in poverty, percentage of population that owns houses,
(12) percentage of occupied houses that are actually owned by the Indians occupying them,
(13) percentage of homes that are occupied by American Indians that are overcrowded,
(14) the percentage of all races on reservations that are self-employed, and
(15) percentage of American Indians that live in deep poverty.

Results of Independent Samples Tests

Out of the various categories that were tested, only six of them came out statistically significant (a "t" test value of 2 or greater), with a seventh one reasonably close. Median income produced t-scores of 3.086 and 3.094; percentage of houses lacking kitchen facilities produced t-scores of –2.391 and –2.304; average aggregate income produced t-scores of 1.797 and 1.873; actual number of college graduates came really close, producing a t-score of 1.320; percentage of American Indians over the age of 25 with a less than ninth grade education produced t-scores of –2.045 and –1.991; percentage of occupied homes that are owned by its American Indian residents produced t-scores of –2.370 and –2.346; and the percentage of population of all races on reservations that are self-employed produced t-scores of 2.069 and 2.049. The rest of the statistics produced t-scores that ranged from .344 to .998, none of them being significant at even the 10 percent level.

CONCLUSIONS

From these analyses, it appears as though the only welfare statistic that has been significantly influenced by casino revenue in the past 16 years is average aggregate income of American Indians. When you take this result and compare it with the fact that median income has not seen an equivalent impact, it appears as though a lot of the money could be staying at the top. If some of the wealthiest tribal members were keeping a lot of the profits for themselves, it would explain why the average income is much higher than the median. This is being addressed in various political circles. In particular, Senator John McCain's bill addresses the issue of tribal casinos using profits to reinvest in commercial casinos or build other casinos in off-reservation locations. Although tribal leaders argue that oftentimes, building a casino away from their reservation can provide opportunities that otherwise would not be economically feasible, opponents to this argue that it also has the potential to cause a great deal of trouble. No one imagined that Indian casinos would have expanded to the extent that they already have, and this is just one more way that they could grow even more—which is undesirable to many.[19]

Whereas commercial casinos grew at a rate of 6.7 percent in 2004, according to the American Gaming Association,[20] Dr. Alan Meister's numbers show us that Indian casino revenue grew at 15.2 percent.[21] This beats even Las Vegas's growth rate of about 10 percent. These significant increases mean that the influence that Indian tribes have on politics and the welfare of their citizens is only going to increase over time. In 1999 Indian tribes donated a total of $2,000 to politicians in the United States. In 2004 that number had surged to $7 million.[22] Although in the wake of the Jack Abramoff scandals, this tremendous increase should slow down, the contributions are not expected to stop any time soon. As their economic well-being increases more and more, Indian tribes are going to become steadily more influential. Real per capita income of gaming tribes increased 36 percent between 1990 and 2000, whereas the income of non-gaming tribes and the rest of the nation grew at 21 percent and 11 percent, respectively, during that same time period. This seems significant considering that American Indians received the lowest amount of per capita income assistance out of all Americans.[23] Obviously, it is also possible that the tremendous growth we see is merely a result of the historical setbacks that American Indians have faced over time—that any improvement we see is a result of the relative weakness of their starting point. However, this is not always the case, and if one looks at mere percentage point changes in the census data, there are still significant differences on the surface between the data for Indian reservations and the data for the nation as a whole.

Between the years 1990 and 2000, Indian tribes on the whole increased their overall income at an astoundingly higher rate than the rest of the United States, as described earlier in this chapter. Yet, the differences between Indian tribes with gaming and without do not seem to be significant at this time. There are many things to consider when recognizing the lack of influence that gaming has had in 17 years. Many of the effects that are calculated would take much longer than these 17 years to have a massive measurable impact on the Indian population as a whole. Welfare statistics that are related to education and housing, for example, would take a lot longer to be affected by casino income than the aggregate income numbers. The time it takes to receive an education must be considered, and additionally, the investment in infrastructure and way of life definitely does not occur successfully over night. Aside from the fact that it took about 8 years for Indian casinos to take off and about 10 years for those tribes to gain any significant political influence, schools have to be built, a culture of education has to be established, and pupils that are of the appropriate age need to pass through these newly established learning systems. For instance, take the Mashantucket Pequot Tribal Nation; this tribe profits so substantially from its world-renowned Foxwoods Resort Casino that it pays for any tribal member to attend college. Assuming that a person begins high school at the age of 14, that same person probably decides whether he or she is going to attend college by about age 17. Because the education statistics are not measured for anyone under the age of 25, at which age education levels become standardized and typically no longer change, this effect would take anywhere from 8 to 11 years to have any significant effect and much longer to make up a significant portion of the 25-and-older population. Considering this, it is not hard to see why the positive effects that many claim economic independence is having on the tribes might not yet be showing themselves . Either this is the case, or tribal leaders are, to date, making poor investment decisions or restricting the flow of money downward to the rest of the members of their tribes.

Finally, it is always important to look at the big picture when critiquing policy decisions. It is therefore difficult to gauge the specific impact that casinos have had—even more so for the Indian gaming industry because of its perceived isolation on reservations and mysterious reporting practices that are not subject to the same transparency laws as commercial casinos in the rest of the country. More specific to this chapter, it is even more difficult to estimate the negative effects that casinos have had on the Native American populace. Although studies may provide hard statistical evidence of negative effects in the future—one such study is soon due to produce the results of research on the use of methamphetamines by Indians on reservations—at current time there is no such evidence.

Therefore, in coming years, we can only hope that the size and power of the Indian gaming industry influences public and private parties to engage in further studies of the effects that Indian gaming has had on the Native American population as well as the American population at large.

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Part III

GOVERNMENT'S ROLE IN GAMBLING

6

Expanding Gambling: Factors behind the Decision

The supply of gambling is controlled and regulated by each individual state government in the United States. As the gatekeepers of the gambling industry, state governments determine the forms and amount of gambling that will be legal in their respective states. Although politics are a significant consideration, demographics, geography, and competition are key determinants of whether a particular form of gambling will be successful in a given state. The primary question of this chapter is this: what factors must states account for when they contemplate expanding gambling?

The question of what is possible for state governments in the realm of gambling has been made interesting by several new developments over the last decade. As casino-style gambling has expanded, the industry has become dominated by corporations that have promoted and popularized gambling. The emergence of poker tournaments on cable television with events such as the World Series of Poker on ESPN has boosted the awareness and acceptance of the gaming industry. The popularity of such shows and events makes the topic and analysis of gambling expansion very interesting. Harrah's Entertainment studies have shown that greater than 50 percent of Americans find gambling personally acceptable, whereas less than 20 percent of people find it not acceptable at all.[1] The majority of Americans want to know when and where gambling will turn up next.

It is important to understand why state governments are pursuing this controversial industry. In addition looking at the quantitative analysis that projects gambling tax revenues, examining the motivation that state governments have for expanding and regulating the gambling industry is necessary.

The simple answer to this inquiry about motivation is that states need tax revenues for their ballooning state budgets. A more complicated analysis would show that states began the legalization of gambling not only to increase state tax revenues without the political backlash of raising sales or income taxes, but also to spur economic development in regions of the state experiencing economic hardship.[2]

Economic development was the basis used to garner government support when gambling was legalized in Atlantic City, New Jersey.[3] The expansion of casino gambling that began in the early 1990s along the Mississippi river in the form of riverboats also targeted economically depressed areas. Now, as casino-style gambling has been legalized for many years, states are coming to rely more heavily on gambling tax revenues than ever before (see Table 6.1). They are beginning to expand gambling and loosen regulations on it solely to protect these tax revenues on which they have become reliant.

Table 6.1
States Collecting More than 5% of Total Tax Revenues from Gambling Taxes

State	*Gambling Revenue*	*Total Revenue*	*Percentage*
Delaware	208.9	2,918	7.2%
Florida	1192.2	21,197	5.6%
Illinois	1319.2	25,161	5.2%
Indiana	895.3	10,446	8.6%
Iowa	259.9	4,484	5.8%
Louisiana	723	6,662	**10.9%**
Michigan	884.4	8,895	9.9%
Mississippi	327.7	3,494	9.4%
Missouri	594.8	7,669	7.8%
Nevada	781.9	2,139	**36.6%**
New Hampshire	76.9	1,336	5.8%
New Jersey	1243.5	23,223	5.4%
New York	2172.4	40,328	5.4%
Oregon	326.4	3,969	8.2%
Rhode Island	262.2	2,735	9.6%
South Dakota	157.6	891	**17.7%**
West Virginia	380	3,139	**12.1%**
Total United States	19,217.70	523,548	3.67%

Sources: Statistical Abstract of the United States for 2004–2005; State Regulatory Agencies.

STATES RELYING ON GAMBLING TAX DOLLARS

In 2004 gambling tax revenues accounted for over 5 percent of total tax revenues in 17 states. Although it might not surprise anyone to learn that Nevada collects just over one-third of its tax revenues from casino gambling taxes, states such as South Dakota and West Virginia are also heavily dependent on gambling tax revenues, accounting for 17.7 percent and 12.1 percent of total tax revenues. Many of the states with the greatest reliance on gambling tax revenues are also home to commercial casinos and riverboats, including Michigan (9.9%), Louisiana (10.9%), Mississippi (9.4%), and Indiana (8.6%).

It is not only commercial casino states that reap gambling tax dollars; states such as Rhode Island (9.6%), Delaware (7.2%), and Oregon (8.2%) have been able to garner their fair share of tax dollars by expanding their lotteries through video lottery terminal (VLT) machines. Many of the remaining states with gambling revenues over 5 percent of their total tax base have found success with their original lotteries. This preliminary data indicates that states have many options to leverage their tax revenues on gambling, and their specific game of choice may be influenced more by demographics and politics than by the profitability of any one form of gaming.

The concern with states' new reliance on gambling tax revenues is growing as more states consider expansion of the industry. The expansion throughout the United States is a threat to each state that currently relies on gambling tax revenues. With limited flexibility of demand, the significant potential increase in supply will hurt states that currently rely on gaming, putting them in danger of budget shortfalls. Gaming tax policies that were once meant to cover state budget deficits may in the future create them.

THE CURRENT COMPETITION FOR TAX DOLLARS

The growth of states' reliance on gambling tax dollars has led to heated competition between states for the existing demand for gambling. With tax dollars at stake, state governments are competing with their neighbors to capture gambling tax dollars from their own citizens and citizens of neighboring states. This is particularly true in the Northeast, where lotteries began in the 1960s and 1970s. Starting with New Hampshire, lotteries were introduced one by one, moving westward, as Massachusetts, New York, and Connecticut quickly followed suit.[4]

Ballooning budget deficits and declining growth rates for lotteries have led states in the Northeast to pursue a variety of non-lottery forms of gaming, making them an optimal case study for this topic. Since 1993, northeastern states have implemented their gaming strategies while states in other sections of the country have faced political opposition to gambling expansion. But as political opposition lessens, and states find an increased need for new tax revenues to fund state budgets deficits, new developments in the supply of gaming are sending shock waves through the Northeast gaming market.

Examples from the Northeast

In 2006, Pennsylvania passed legislation that permitted up to 61,000 slot machines to be spread throughout the state at racetracks, resorts, and slot parlors in major cities including Philadelphia and Pittsburgh.[5] The competitive effects on neighboring states are considerable. Maryland, a state with a historic horse racing industry, stands to lose significantly if it does not quickly act and allow slot machines within its state boundaries.[6] States with a high concentration of gambling that formerly enjoyed pseudo-monopolies, such as New Jersey, Delaware, and West Virginia, will witness an erosion of their market power and, thus, tax revenues.

New Jersey's Atlantic City casinos also face threats from neighboring states. The introduction of Native American casinos in the Catskill region of New York, a priority for former New York governor George Pataki, and his successor, Eliot Spitzer, would directly compete with Atlantic City for New York metro casino patrons.[7] The three projected casinos in southern New York would not only potentially seize Atlantic City customers but also pose a threat to Foxwoods and Mohegan Sun, the two most successful Indian casinos in the country, from neighboring Connecticut. All along the East Coast, states are positioning themselves to gain their maximum gaming tax revenues.

THE CHOICES OF GAMBLING EXPANSION

Commercial Casinos

State governments have shifted from lotteries to casino-style gambling for expansion. The first of these forms of gambling is commercial casinos, made popular by Las Vegas and Atlantic City before the lotteries spread across the nation. Nevada, the birthplace of commercial casino gambling, for many years owned an unchallenged monopoly throughout the country.[8] With low excise tax rates on casinos and few limitations, casinos have thrived and created a unique gambling market littered with non-gaming attractions and amenities. Regardless of the casino gambling expansion of the last decade, Las Vegas remains the nation's top casino market with solid growth rates.

Atlantic City casinos in New Jersey followed the success of commercial casinos in Las Vegas. However, supply restrictions and competition from neighboring states have limited the Atlantic City casinos' success and growth. commercial casinos have also been approved by Mississippi and Michigan with restrictions similar to those in Atlantic City. Commercial casinos are typically targeted for urban areas, as evidenced in Michigan (Detroit), Mississippi (Tunica and Biloxi), and New Jersey (Atlantic City).[9] Commercial casinos are generally not an option for most state governments because many state constitutions forbid them. Casinos bear the greatest political and legal hurdles of all gaming choices throughout the industry.

Riverboat Casinos

Riverboat casinos served as the primary reintroduction of casino expansion in the United States in the early 1990s. They were built throughout the Midwest as an acceptable form of gambling because of the historical nostalgia associated with casino riverboats.[10] Riverboats, however, fundamentally differed from commercial casinos because their original amenities were limited, and restrictions were placed on the dollar amount people could gamble.[11]

Riverboats were required to leave the dock and sail along the Mississippi River for gambling to take place. In many states there were limits set on the amount of money customers could lose in a given time frame, and customers were not permitted to reboard consecutive riverboat cruises. As time has passed and legislators have realized that restrictions stifle casinos and thus tax revenues, many of the limitations on riverboats have been lifted. They no longer sail along the Mississippi River, and most are permanently docked and linked with land-based resorts.[12]

Iowa was the first state to legalize riverboats in 1989, with many Midwestern states such as Illinois and Missouri quick to follow. States compete with one another in location and price, with some states having higher tax rates on casino revenues than others. Nowhere else is this more true than in Chicago, where both Indiana and Illinois have casinos positioned nearby. Tax rates proved to be an important driver of revenues as casino operators shifted their marketing foci toward Indiana casinos when the state of Illinois raised their revenue tax rate to a relative tax rate of 70 percent.[13]

Indiana has positioned its remaining casinos along its southern border to directly compete with and draw customers from neighboring Kentucky. Each casino is targeted to compete with a specific horse racing track, for which Kentucky is famous. The positioning of such casinos has led Kentucky gamblers to cross the border and has caused its racetracks to lose revenue.[14] This has prompted many discussions and debates in the legislature about legalizing slot machines at each of the state's racetracks.[15] The goal of such an expansion would be to bring back Kentucky gamblers and their tax dollars.

Indian Casinos

With the passing of the Indian Gaming Regulatory Act (IGRA) in 1988, state governments were helpless to prevent the expansion of Indian casinos. The act did, however, give the states a loophole by which to profit from these casinos. The IGRA classifies gaming into three separate classes. Although Indian casinos have complete sovereignty over Class I and Class II gaming, consisting of bingo and traditional Indian gaming for small prizes. Class III gaming, which includes slot machines, roulette, blackjack, and craps is the most lucrative of the classes. Class III gaming is allowed at Indian casinos only when it is allowed in other jurisdictions throughout the state.[16] This forces Indian tribes to negotiate gaming compacts with state governments that have restricted such forms of gambling, allowing states to take a piece of the pie.

Although Connecticut is home to the two most successful Indian casinos in the country, Foxwoods and Mohegan Sun, they are not the only state using Indian gaming to expand their tax revenue base. Former governor George Pataki of New York aggressively pursued compacts with several Indian tribes to develop a series of casinos from the Catskills to Buffalo, and this policy has been continued by his successor, Governor Eliot Spitzer. Rhode Island is in a heated competition with Massachusetts for gambling revenue. However, voters would not approve a Native American casino because of the negative effect it might have on existing gambling revenues.[17]

The use of Indian casinos, however, is not a strategy of expansion for many states with Indian tribes owning sovereign land. States that consider expanding casino-style gaming through slot machines or resort casinos must recognize the supply risks that Indian tribes pose. Legalizing such gaming options within the state would give the opportunity for Indian reservations to request and force a gaming compact for similar gaming options.

VLTs and Slot Machines

Casinos, whether commercial, riverboat, or Indian, are not the only options for state governments. The horse racing industry has long stood as a respected form of entertainment and gambling characterized by traditional pageantry. Very few people, however, would consider opening new racetracks for the expansion of pari-mutuel wagering on the horse races, but rather would do so to capitalize on the growing trend of placing slot machines or VLTs (video lottery terminals) at them. As the horse racing industry has suffered negative growth rates, an expense incurred from other forms of expanded gambling throughout the country, states have introduced VLTs and slot machines at these fledgling sites to rejuvenate them.[18]

Slot machines, the revenue drivers of casinos, have a significant effect on racetracks by drawing bigger crowds and increasing the amount of money wagered. They are operated independently of one another and are significantly different from their sister machines, VLTs. Slot machines are, by definition, Class III gaming machines that are independent.[19] Video lottery terminals, which may look nearly identical to slot machines, are primarily unique because they operate in a connected system like a lottery and are thus regulated by the lottery commission of the given state.

The Importance of the VLT–Slot Machine Difference

The distinction between the two types of casino-style machines (VLTs and slot machines) is noteworthy for both political and competitive reasons. States such as New York, with a longstanding lottery, are able to introduce VLTs with minimal legislative hurdles in comparison with the obstacles faced when slot machines and casinos are considered. Slot machines, because of their independence, are more attractive to consumers, and operators have more flexibility in their placement, all of which makes them more profitable.

Slot machines are rare among states because of both the political hurdles and the threat of competition from Indian casinos. Legalizing slot machines would force a state government to negotiate a gambling compact with any Indian reservations, thus further increasing the supply of gambling. Thus, slot machines have been pursued rarely, with the notable exception of Pennsylvania, a state with no Indian tribes wishing to build casinos.

The combination of potential Indian casinos and the legalization of slot machines would introduce an explosion in the supply of gambling within a state. This is one particular reason for the recent legislative battle in Florida, a state with many Indian tribes, over slot machines at racetracks. Relative tax rates of 65 percent were added to the voter-mandated gambling resolution, limiting the building expansion plans for slot machines in the state and creating a hurdle to actual development.[20] This was one of the political efforts of conservatives in the state legislature who recognized the potential expansion of gambling within the state from such a resolution.

THE FUTURE IN GAMING EXPANSION FOR STATES

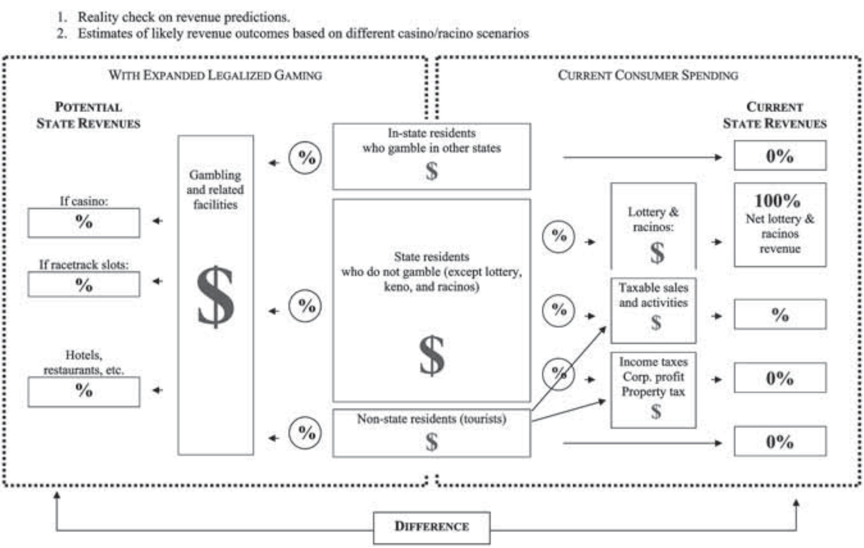
As gambling becomes more acceptable across the country and the supply of gambling increases, the logical economic result is decreasing gambling revenues in the current gaming states, as a result of cannibalization. Those states with large gaming investments have the most to lose from competition and expansion, as evidenced by Atlantic City's position. States combat their fear of losing gambling tax revenues by further solidifying their position in the gambling market with supplementary gambling expansion. Figure 6.1 provides a summary of the various factors that policy makers need to account for as they determine whether expand gambling in their jurisdictions.

Thus, current strategies, if undertaken by multiple states, may cause a self-fulfilling prophecy in which states are destined to lose a portion of their tax revenues to their neighbors. Although this may prove to be a more equitable distribution of gaming tax revenues among states, those states that heavily rely on gambling revenues will lose out as their potential for growth declines. Recognizing the competitive nature of gambling expansion is necessary not only for understanding the motivations of state governments but also for quantifying the impact of their expansion choices.

Competition within the Industry: Casinos versus Lotteries

Understanding the relationships between the different forms of gambling is crucial to understanding the impact that expansion will have on the existing gambling industry. Many economic studies have sought to determine whether gambling industries (casinos and lotteries) are complementary or partial substitutes. This determination is critical to measuring the effect of gambling expansion and quantifying the tax revenues a state can gain from gambling.

Figure 6.1
Gambling Revenue Forecasts: Where Would the Money Come From?



A study by gambling researchers Douglas M. Walker and John D. Jackson, titled "The Relationships among US Gambling Industries," seeks to understand the impacts gambling industries have on one another. Their work is noteworthy for not only its results but also its approach. Their specification of variables employed to test the effects of cross-border competition successfully simplifies and captures a difficult variable. In addition to their variable specification, Walker and Jackson included demographic variables such as poverty level and religion, using the number of Baptists because Baptists are a well-organized interest group. Expectedly, increases in the number of people in poverty correlated with decreased casino revenues, but ironically, an increase in the number of Baptists increased casino gambling.

The most important results to consider from this study are the competition and intrastate relationships between gambling industries. The authors found that casinos and lotteries within the same state are partial substitutes and cannibalize each other. In studying the interstate competition, they found similar results of cannibalization and substitution with one notable exception: casinos in neighboring states did not substitute each other in a statistically significant respect.[21]

Explaining Recent State Casino Gaming Adoptions

Edward Furlong's "A Logistic Regression Model Explaining Recent State Casino Adoptions" presented four rationales that a state has for legalizing casinos: revenue, political, competitive, and economic development. His results exposed many false notions about casino adoptions, mainly that indicators of fiscal stress were insignificant and that casino-adopting states were in better financial health than non-adopters. Although many political variables failed, state ideological identifications had strong effects, as did job growth, with poorly performing states more likely to adopt gaming.[22]

Furlong may not have been able to garner any significant variables to defend his revenue and political rationales for casino adoptions, but this does not discount their importance. One of the flaws inherent in his study, however, is that it was limited to riverboat casinos and did not include considerations for racinos (race tracks that are permitted to operate slot machines) and VLT machines run by the state lotteries. The other reason that Furlong was unable to capture these rationales is that they are extremely difficult to quantify in an econometric model.

Measuring the Casino Cannibalization of State Lotteries

The competition between gambling industries within the United States is just as important as the competition between states for the gambling tax dollars. As casino gambling is expanded, such casinos will encounter competition not only from neighboring states but also from other gambling sources within the state. Thus, it is crucial to understand how different forms of gambling compete and specifically how the two major forms—casinos and lotteries—cannibalize each other.

Many studies have been conducted to find the cannibalization effect casinos have on lotteries, In 2003, Stephen Fink and Jonathan Rork published an article titled, "The Importance of Self-Selection in Casino Cannibalization of State Lotteries."[23] Their study stands out from previous papers that attempted to measure the same effect by controlling for negative selection bias. Their analysis yielded somewhat expected results, showing that the cannibalizing effect is 56 percent, which, though significant, is much less than previous studies have showed. Nonetheless, the body of research has shown that casinos and lotteries are not complementary goods but partial substitutes.

CONCLUSION

This chapter has described for the reader some of the complexity that is involved in determining what gambling policy a state should pursue. This chapter may not provide legislators with a dollar figure for the expansion of casino-style gaming, but it does give significant insight into the issues and factors states must consider. In the next three chapters, we examine and analyze situations where public policy makers are faced with the decision to authorize changes in venue or additional gambling. Hopefully, the reader will be able to recall the various options that public policy makers have available as they seek additional gambling revenue.

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7

Locating a Casino and Selecting an Operator: The St. Louis Experience

Pierre Laclede landed on the banks of the Mississippi River in 1764 and endeavored to build "one of the finest cities in America." President Casinos, Inc.'s Casino on the Admiral, which, 300 years later, would occupy his landing point, was certainly not part of his dream. The casino, marred by rows of broken slot machines and warped floors, lends credence to the assertion made by one developer that it is "a dingy barge that is barely afloat." Also, with only 1,200 slot machines and 15 table games, the President Casino is dwarfed by its newest competitors, Harrah's and the Ameristar Casino St. Charles, which both boast well over 3,000 slot machines and 70 table games. After years of poor management and stiff competition and after defaulting on a $37 million mortgage repayment, President Casinos, Inc., filed for Chapter 11 on June 20, 2002.[1] The failure of the President Casino left a void in the heart of historic St. Louis and contributed yet another example of the urban decay that had engulfed the once-flourishing city.

HISTORY OF ST. LOUIS

In 1876 the city of St. Louis seceded from the county of the same name, making it the first home-rule charter city in the nation. At the time, the move appeared to be a good idea. The underpopulated and underdeveloped county exerted a disproportionate amount of political influence and siphoned off financial resources from the affluent city in the form of subsidies and tax aid. For years, the newly chartered city prospered under this arrangement. The city's prestige and power culminated when it hosted the 1904 World's Fair and Olympic

Games. However, the strategic advantages of this port city diminished because of manufacturers' increased use of trucking and railroads to ship goods. In addition, the tenement housing and subtle smell of hops from the many breweries in the area hardly made it an ideal environment to raise children. Consequently, many wealthy citizens began to move into the surrounding countryside, ridding themselves of the city's congestion. Soon, businesses started to follow the wealthy families, forming a second center of commerce in the suburb of Clayton. This trend, which began in the early twentieth century, continues to this day. Without the support of affluent residents and with a gradual decrease in the number of businesses paying taxes, the city of St. Louis began a downward spiral, while the county of the same name flourished. Crime and corruption became so prevalent that large sections of the city were just abandoned. Without drastic action, the city was expected to continue on its downward course.

THE PIONEERS

Lawrence Biondi, S.J., president of Saint Louis University (SLU), led the charge to change the city. Seeking to revitalize SLU's campus and the surrounding areas, Biondi, in conjunction with various civic leaders and regional developers, helped revamp much of the area with the goal of creating a safer, more aesthetically pleasing campus in the heart of St. Louis. Biondi had his hand in many notable projects, including the redevelopment of the Continental Building, a beautiful art deco landmark bordering the SLU's campus, and an initiative for a $45-million, 13,000-person stadium to house the SLU Billiken basketball teams. In addition, Francis Slay, mayor of St. Louis, helped to orchestrate a deal that would keep the St. Louis Cardinals in the downtown area, and Senator Jack Danforth spearheaded an initiative to provide more low- and middle-income housing in the city. Although the bankruptcy of President Casinos, Inc., was a cold reminder of the remaining work to be done, many civic leaders saw the bankruptcy as an opportunity for the city. If a new luxury casino could be built in the area to replace its antiquated predecessor, it would be the capstone of St. Louis's rebirth. If the initiative failed, however, it would most likely lead to more lost jobs and urban blight for the city. By 2003 it had become apparent that action had to be taken quickly because St. Louis County was considering development of a rival casino in South County, the only untapped region in the area.

THE MARKET

The Midwestern riverboat casino gambling market is dominated by four states: Illinois, Indiana, Iowa, and Missouri. Because of the possible negative societal impacts of casino gambling, each state closely monitors its casino-gambling activities and licensing procedures through an independent gaming board or commission. However, many specific regulations governing riverboat gambling are still controlled by the state legislatures. Because of the highly regulated nature of the industry, each individual state's restrictions play a prominent role in regional market dynamics. In response to loosened restrictions in neighboring states, it is important to note, Missouri and Illinois have tended to relax their initially more stringent regulations.

The battle to legalize gaming in both Illinois and Missouri was fierce. Proponents believed that legalizing gambling would bring in greater revenues for the state and depressed river towns, but opponents feared that gambling would increase instances of crime and prostitution. As a compromise, the states agreed to legalize riverboat gambling as long as the riverboat casinos would operate only while the boat was out on the river and piloted by a licensed captain. If problems did arise, the boats could be sold or moved away. This riverboat concept was shared by the earliest casinos in the market, the President Casino and the Casino Queen, across the Mississippi River in East St. Louis, Illinois. But in response to loosened requirements in neighboring states and complaints from casino operators about river conditions, Missouri and Illinois law gradually evolved. Boats are no longer required to be *on* the river; being *near* a river will suffice. Further, regulations now require that only the gaming floor be on water. This allowed a casino to build four walls that are anchored to the ground while pumping running water underneath the floor of the casino, allowing the base of the casino to float. As a result, the casinos became larger and more luxurious than previous riverboats, one reason many people view the President Casino as antiquated. As a result of these water requirements, the casinos in St. Louis arc in a semicircle-like pattern along the waterways surrounding the city and county (see Figure 7.1). These "boats in moats" became the design of the luxury casinos in St. Charles, Missouri (Ameristar's Casino St. Charles and Harrah's), and would become incorporated into the proposals submitted for the casino at Laclede's Landing.

In addition to design regulations, Missouri also imposes a $500 loss limit during a two-hour period, whereas Illinois has no loss limit. As a result, most high rollers in the St. Louis market gamble in Illinois, which helps to explain why the Casino Queen has had continued dominance over the President Casino in both market share and profits. Former Missouri governor Bob Holden proposed lifting the ban in response to pleas from President's management and in an attempt to boost revenues for the state, but the motion has yet to pass.

Missouri and Illinois gaming laws also differ in the gaming size requirement. Illinois allows a casino to have no more than 1,200 gaming positions

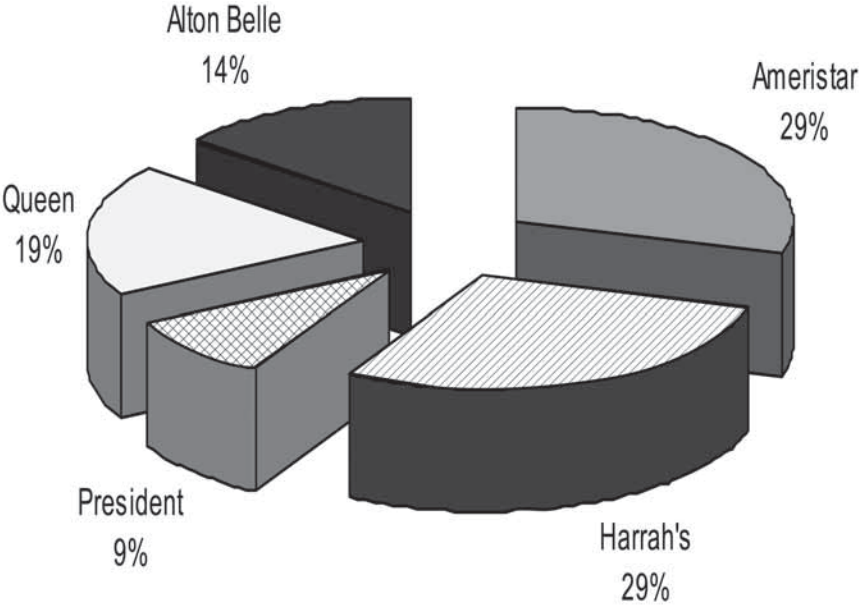
Figure 7.1
St. Louis Metropolitan Area Casino Market

Map Key

1. President's Casino on the Admiral.
2. Casino Queen in East Saint Louis, IL.
3. Proposed Site of Harrah's and Isle of Capri's South County Bid.
4. Proposed Site of Pinnacle's South County Bid.
5. Harrah's Casino in Maryland Heights, MO.
6. Casino Saint Charles operated by Ameristar Inc. in Saint Charles, MO.
7. Argosy's Alton Belle Casino in Alton, IL.

(a gaming position is calculated by multiplying the number of slot machines by 0.9 and table games by the number of seats available). Illinois is currently considering changing this requirement because neighboring states (Missouri, Indiana, and Iowa) have no size requirements, and border casinos are having trouble competing with casinos in neighboring states. The size requirement explains why Harrah's and Casino St. Charles have quickly displaced the Casino Queen, which once was the third most popular tourist destination in the St. Louis area and the largest gaming operation in the market (see Figure 7.2). In addition to size requirements, the high tax rates assessed by Illinois have placed it at a strategic disadvantage in the Midwest market, which favors large casino development in Missouri over Illinois (see Table 7.1).

Figure 7.2
St. Louis Market Share Analysis



THE MISSOURI GAMING COMMISSION

As already noted, Illinois, Indiana, Iowa, and Missouri each established independent boards or commissions to enforce their respective state's gaming regulations. In Missouri, for example, the Missouri Gaming Commission (MGC) was established in 1993 to regulate excursion riverboat gambling. The MGC is made up of five members, appointed by the governor, who serve a term of three years. To maintain balance, no more than three members can be affiliated with the same political party, and members serve for a maximum of six years. Members must be residents of Missouri and commonly represent an array of large political bases from across the state. As of 2006 two members hailed from Kansas City, two from Jefferson City, and one from St. Louis County. Typically, casino operators submit proposals to the local governing bodies in the jurisdiction of the proposal before the commission begins licensing hearings because community support is one of the main criteria of approval. The local governing bodies generally accept one of the bids and make their recommendation to the MGC.

Table 7.1
Casino Revenue Tax Rates for Illinois, Indiana, Iowa, and Missouri

Illinois
15% on first $25 million of gambling revenue
22.5% on next $25–50 million of gambling revenue
27.5% on next $50–75 million of gambling revenue
32.5% on next $75–100 million of gambling revenue
37.5% on next $100–150 million of gambling revenue
45% on all gambling revenues in excess of $150 million
Indiana
15% on first $25 million of gambling revenue
20% on next $25–50 million of gambling revenue
25% on next $50–75 million of gambling revenue
30% on next $75–150 million of gambling revenue
35% on all gambling revenue in excess of $150 million
Iowa
5% on first $1 million of gambling revenue
10% on next $1–3 million of gambling revenue
32% on all gambling revenue in excess of $3 million
Missouri
20% on all gambling revenue (2% for local governments)

The MGC reviews all accepted bids proposed in a development area and has the power to license as many or as few casinos as it chooses in a given area (licensing requirements are listed in Table 7.2). In 2003, the Gaming Commission issued a press release elucidating its insights about the St. Louis market. In it, the Gaming Commission stated that it believed the St. Louis market was underserved, citing its "St. Louis Market Analysis" study as support. The St. Louis Market Analysis shows that although only 14 percent of the population within the proximity of downtown St. Louis lives closer to East St. Louis than to the President Casino, 68 percent of the gaming revenue goes to the Casino Queen, which rests in East St. Louis. The press release went on to explain specific criteria the Gaming Commission uses in its approval process not listed in the licensing requirements. The additional criteria were as follows:

(1) support of opposition of the location's governing body; (2) the suitability of the location; (3) the financial resources of the applicant; (4) the applicant's experience in managing a gaming operation; (5) the economic impact to the state; (6) the economic impact on the home dock jurisdiction and the surrounding region, including competing casinos, local businesses and local governments; (7) the quality and scope of the proposed development and (8) the status of governmental actions required for the facility.

Table 7.2
Missouri Gaming Commission Regulations

11 CSR 45-4.080 License Criteria

(1) The commission may issue a Class A license if it determines on the basis of all the facts before it that the applicant meets the criteria contained in Chapter 313, RSMo.

(2) In making the required determinations, the commission may consider the following factors and indices, among others:

(A) The integrity of the applicant and any personnel employed to have duties and responsibilities for the operation of gaming. This determination shall include considerations of—

1. Any criminal record of any individual;
2. The involvement in litigation over business practices by the applicant or any individuals or entities employed by the applicant;
3. The involvement in proceedings in which unfair labor practices, discrimination or regulation of gambling was an issue; and
4. Failure to satisfy any judgments, orders or decrees of any court;

(B) The types and variety of games which the applicant may offer;

(C) The quality of the physical facility together with improvements and equipment;

(D) The imminence of completion of the facility or any of its improvements;

(E) Financial ability to develop and operate a facility successfully, including:

1. Ownership and control structure;
2. Amounts and reliability of development costs;
3. Certainty of site acquisition or lease;
4. Current financial conditions;
5. Sources of equity and debt funds, amounts, terms and conditions and certainty of commitment;
6. Provisions for cost overruns, nonreceipt of expected equity or debt funds, failure to achieve projected revenues or other financial adversity; and
7. Feasibility of financial plan;

(F) The statue of governmental actions required by the applicants facility including:

1. Necessary road improvements;
2. Necessary public utility improvements;
3. Required governmental approvals for development, ownership and operation; and
4. Acceptance of any required environmental assessment and preparation of any required environmental impact statement;

(G) Management ability of the applicant including:

1. Qualifications of managers, consultants and other contractors to develop and own a gaming facility and the likelihood of projected operation;
2. Security plan;
3. Plans for marketing, promotion and advertising;
4. Concession plan;
5. Plan for training personnel; and
6. Equal employment and affirmative action plan;

Table 7.2 *(continued)*

11 CSR 45-4.080 License Criteria *(continued)*

(H) Compliance with applicable statutes, rules, charters and ordinances;
(I) The impact of the facility including:
1. The economic impact-
A. The employment created;
B. The purchases of goods and services, including Missouri goods and services;
C. Public and private investment; and
D. Taxes generated;
2. Ecological impact;
3. Social impact; and
4. Cost of public improvements;
(J) The extent of any public support or opposition;
(K) The plan adopted by the home dock city or county; and
(L) Effects on competition, including:
1. Number, Nature and relative location of other Class A licensees; and
2. Number, nature and relative location of gaming facilities in other states.
(3) The commission may also consider any other information which the applicant discloses and which is relevant or helpful to a proper determination by commission and any information disclosed during the background investigation.

The licensing requirements and these criteria were used as the basis for the St. Louis approval process.[2]

The MGC has ultimate authority over accepting and rejecting casino licenses and requires no additional approval from the legislature, the governor, or local communities. Because the board rejects more proposals than it accepts, and a rival project in South County was being considered in 2003 the ability of a casino operator in the city to receive a gaming license in a timely manner was a crucial factor in deciding which bid to go ahead with.

REQUEST FOR PROPOSALS

The first step in the process of building a new casino in Missouri is issuance of a Request for Proposals (RFP) document. An RFP is a memorandum drafted by an executive body explaining the project being considered by a community, and it typically explains the location and nature of the project, the requirements for bidding applicants, the criteria for evaluating the project, required respondent information, and timetables for project approval. The body then reviews the bids received and ranks them in order of preference using the criteria found in the RFP. This first step was executed by the St. Louis

Development Corporation (SLDC) in the fall of 2003, when the Missouri Gaming Commission indicated that it would begin to consider new gaming proposals. The RFP submitted by the SLDC was for development and operation of a gaming facility and related mixed-use establishment in the city of St. Louis. The goals and preferences of this RFP are outlined in Table 7.3.

Table 7.3
St. Louis City RFP Goals and Preferences

Goals

1. Secure the maximum possible economic benefit for the City in the form of tax and other direct revenues (taxes, fees, lease payments, property sales proceeds, etc., in particular as a result of the developments gaming component) as well as in the form of indirect economic benefit through the creation of employment opportunities and a quality environment at or near the riverfront that will attract residents, visitors, and workers to downtown St. Louis.
2. Select a gaming operator with the quality and capacity to be readily licensed by the Missouri Gaming Commission and to assist in persuading the Commission to select the proposed site as its immediate priority for licensure of a gaming facility, thus enabling the proposed casino to move ahead.
3. Select a developer or developers with the quality of track record, financial and organizational capacity and willingness to directly or indirectly produce a quality mixed-use environment that includes residential and retail development on the proposed site that can become a nationally recognized gaming/convention/tourist/entertainment are in the Central Riverfront that complements planned residential development and builds on and enhances existing City and Downtown resources.
4. Ensure that the proposed development will achieve the goals and preferences set forth herein.

Preferences

1. A gaming facility and surrounding development that is attractive and job-intensive, and which enhances the surrounding community and/or mitigates any potentially detrimental aspects.
2. A gaming facility and surrounding development which maximizes taxes, fees, rent, and other revenues to the City and the State of Missouri.
3. A gaming facility and surrounding development likely to be selected for licensure by MGC as a result of best meeting the established goals and evaluation factors of MGC and the State of Missouri, including but not limited to those listed in 11 CSR 45–4.080 (See Exhibit 3).
4. Positive long-term economic impact on the City of St. Louis in general and the downtown area in the immediate vicinity of the proposed site in particular.
5. Creation of business opportunities for persons residing and businesses located in the City. This shall include compliance with the Mayor's Executive Order 28 to encourage minority and women owned business participation.
6. Proposals that result in direct or indirect implementation of the following community and economic development projects and address the following goals:

Table 7.3 *(continued)*

Preferences *(continued)*

a. The development should create a high quality, financially and operationally successful gaming facility that will attract gaming customers and other visitors to the City and that will directly or indirectly produce a mixed-use project including retail, residential, and other uses in the area of or adjacent to the gaming facility;
b. The proposed gaming facility should balance the needs of gaming operations, hospitality, entertainment, and recreation, with job growth, long-term economic growth, infrastructure improvements, and direct and indirect benefits to the surrounding community;
c. A compatible operational relationship among gaming operations and the surrounding community;
d. A high level of design excellence and innovation in all proposed facilities and development;
e. Significant levels of job training and creation, including a plan for achieving diversity in recruiting, training and hiring in all employment classifications;
f. The inclusion of a capital infrastructure improvements program for the proposed site, and if possible, also for areas in the vicinity of the proposed sit; and
g. The inclusion of an interior drainage plan for the site, including appropriate solutions for any portions of the site that are located in the floodplain and/or the floodway.

To facilitate the decision making process, the City of St. Louis also established a selection committee for evaluating the project. The selection committee assigned to the proposed casino included members of the Port Authority, the mayor's office, the Board of Aldermen, the SLDC, and other prominent civic bodies. The selection committee then appointed a finance subcommittee to review the economic implications of each proposal. The committee, comprising prominent community business leaders, had the task of submitting its findings to the selection committee, which in turn ranked the bidding firms and submitted its recommendations to the MGC. Concurrently, the St. Louis County Economic Council drafted an RFP for a rival casino in South County. Their criteria, elucidated in Table 7.4, were being evaluated by the St. Louis County/St. Louis County Port Authority Gaming Selection Committee.

THE ENTENTE

St. Louis county executive George R. "Buzz" Westfall epitomized the St. Louis spirit. Born in a housing project in north St. Louis City, he went

Table 7.4
St. Louis County RFP Goals and Policies

Goals

1. A gaming facility and surrounding development that is attractive and job-intensive, and which enhances the surrounding community and/or mitigates any potentially detrimental aspects.
2. A gaming facility and surrounding development which maximizes the taxes, fees, rent and other revenues to South County, St. Louis County, SLCPA, and the State of Missouri.
3. A gaming facility and surrounding development likely to be selected for licensure by MGC as a result of best meeting the established goals and evaluation factors of MGC and the State of Missouri, including but not limited to those listed in 11 CSR 45-4.080 License Criteria.
4. Positive long-term economic impact on St. Louis County in general and South County and the community in the immediate vicinity of the proposed site in particular.
5. Creation of employment and business opportunities for persons residing and businesses located in St. Louis County.
6. Implementation of the following community and economic development projects:
   a. capital infrastructure improvements fund for the areas in the vicinity of the proposed site;
   b. a neighborhood stabilization fund for residential housing code enforcement, rehabilitation loans and grants, and down payment assistance for targeted areas within St. Louis County;
   c. small business loan funds;
   d. resources for redevelopment of older, inner-suburban commercial corridors;
   e. resources for the establishment of recreational and open space uses along the Mississippi River, preferably for SLCPA or County-owned or controlled property.

Policies

1. The proposed gaming facilities should balance the needs of gaming operations, hospitality, entertainment, and recreation with job growth, long-term economic growth, infrastructure improvements, and direct and indirect benefits to the surrounding community.
2. A compatible operational relationship among gaming operations and the surrounding community is required.
3. A high level of design excellence and innovation is required for all development.
4. Interior drainage must be addressed for all sites. If a proposed site is in the floodplain and/or the floodway, proposals must realistically address appropriate solutions.
5. Job training and creation must be a significant part of any proposal, including an affirmative action plan for recruiting, training and hiring of minorities and women in all employment classifications.
6. St. Louis County desires the creation by a developer of a financially and operationally successful gaming facility that will attract residents and out-of-county visitors.

on to receive his bachelor's and law degrees from St. Louis University before becoming one of the most influential civic leaders in St. Louis politics.[3] However strong his city roots may have been, as county executive, Westfall was responsible for overseeing the development of a casino in South St. Louis County. The South County market is the most coveted area for casino developers in the St. Louis market because there is no direct area competition and, according to 2003 data, South St. Louis residents frequent casinos most often. Further, a properly placed casino in South County would be the closest casino for over a quarter of the St. Louis market, the largest gamer base of any casino in the area to date. A casino in South County would cause a huge surge in job opportunities and tax revenues. In addition, because one of the commissioners at the time, Judy Hinrichs, was a resident of St. Louis County, the community connection could have facilitated area casino development.

However, one major problem with the South County proposal existed. Four years earlier, in 1999, the county had tried and failed to obtain approval for a new casino in same area. In its decision, the MGC had cited its concerns that a rival casino in South County would siphon off revenues from the President Casino, which derived a large portion of its revenues from the South County market. Conversely, a new luxury casino in the city of St. Louis would draw even more disposable income out of the county because residents would be more likely to visit a refurbished city casino in their leisure time. These concerns, coupled with his St. Louis ties, prompted Buzz Westfall to contact St. Louis mayor Francis Slay in the hope that a symbiotic relationship could be formed. After negotiations, the two tepidly formed an agreement whereby bidding firms could submit joint proposals for the two projects. It was believed that, with the support of both the county and the city, both projects stood a better chance to be approved by the MGC. As part of the agreement, the county agreed to accept the same bidder as the city, and the door was left open for possible revenue sharing arrangements. However, this agreement was not enforceable. To further complicate matters, Buzz Westfall died in late October 2003, before the county could consider project proposals. With their loose entente nevertheless in place, the city and the county were ready to welcome bidders.

THE BIDDERS

Harrah's Entertainment Group

According to its own Web site, Harrah's Entertainment is the most recognized and respected name in the casino entertainment industry.[4] Harrah's was by far the largest and most recognized bidder in the fray. In 2003 the company operated 26 casinos in 13 states under the Harrah's, Harvey's, Rio, and Showboat brand names. Harrah's operated two casinos in Missouri, Harrah's St. Louis in Maryland Heights and Harrah's North Kansas City in North Kansas City. Harrah's St. Louis is the largest casino in the St. Louis market, with a 29 percent market share.

Harrah's chose to remain on the sidelines of the City of St. Louis bidding process. Instead, the company proposed a $275 million gaming facility on 16 acres of land in South County, next to the Jefferson Barracks Bridge. The proposed casino would feature 90,000 square feet of gaming space adjoining an 180,000-square-foot, land-based structure. The facility would boast a 125-room hotel tower and a 2,200-spot parking garage. In addition, the gaming area would include approximately 2,000 slot machines and 25 to 40 table games. Harrah's estimated that the project would create 580 construction jobs; 1,300 to 1,350 full-time positions; and 914 indirect jobs. Finally, a 27-month construction period was projected. The company would use its existing capital structure to finance the project.

Isle of Capri Casinos, Inc.

Isle of Capri Casinos, Inc., with its unique "Isle of Capri" brand, has quickly grown to be one of the 10 largest publicly held gaming companies in the United States. The first gaming company to open in Mississippi, in 1992, Isle of Capri Casinos, Inc., in 2003 owned and operated riverboat, dockside, and land-based casinos at 14 locations throughout Mississippi, Louisiana, Colorado, Iowa, Missouri, and Nevada, in addition to a horse racing track in Florida. At the time of its bid, Isle of Capri operated two casinos in Missouri, the Isle of Capri–Boonville and the Isle of Capri–Kansas Riverboat in Kansas City. In addition, Isle of Capri has made a proposal for a third Missouri facility in Jefferson County, which lies just south of St. Louis County. However, community opposition to the proposed development surfaced, and Isle modified the original proposal to appease residents. With its billion-plus annual revenues, Isle was the second largest of the casino bidders.[5]

Isle of Capri made joint bids in both the city and the county of St. Louis. The city proposal had two distinct options for development. The first option called for a $146 million casino to be built at Laclede's Landing. The city casino would feature approximately 1,100 slot machines and 35 table games under an island theme. It would be possible to expand gaming operations by 50 percent if gaming demand rose. Because weekend hotel occupancy rates in downtown St. Louis were hovering at around 65 percent, Isle decided to purchase the fledgling Embassy Suites and renovate it rather than build a new hotel. After refurbishment, the hotel included 280 rooms, an entertainment area, and an exhibition hall. Because the city had dabbled in hotel development and held a partial interest in the struggling convention center hotel at the America's Center, Isle believed that renovating a preexisting hotel would not add to the city's burdens. In addition, Isle proposed $114 million in ancillary residential and retail development that was subject to non-compete agreements with other casino operators. The mixed-use residential and retail space would form a promenade around the casino, and Isle would grant an $8 million revolving credit line to the developers. The principal partners in this venture would be Steve and Mike Roberts of Roberts Brother's Properties and Steve Trampe of Owen Development. Of the $114 million, Mike and Steve Roberts, two phenomenally successful entrepreneurs, proposed $84.5 million in developments, including a pedestrian mall, an apartment complex, and a "Dave and Buster's" entertainment facility. Additionally, Steve Trampe proposed a $22 million apartment complex on Morgan Street. The bulk of the remaining development proposed by Isle would come from partners Bob Saur and Jerry Glick. Finally, on condition of approval for a gaming license and a recommendation from the city, Isle agreed to buy the defunct President Casino out of bankruptcy court for $50 million and keep the casino operating until the new Isle casino development was completed. Although Isle did not guarantee that the President Casino would remain open after the new casino was finished, the company pledged to incorporate the current casino's employees into their new operations. Past financial results for the President are listed in Table 7.5. The second option proposed by Isle was basically the same as the first, except Isle proposed building a new hotel with 300 suites to adjoin the casino rather than refurbishing the Embassy Suites. This option would have a budget of approximately $166 million.

The county proposal made by Isle called for a $167 million "Rhythm City" casino to be built on 10.3 acres of land near the Jefferson Barracks Bridge. The casino would include 1,600 slot machines and 40 table games over 70,000 square feet of gaming space. Also, an11-story, 228-suite hotel

Table 7.5
Operating Results of President Casinos, Inc.'s St. Louis Subsidiary

Twelve Months Ending February 28/29	2002	2001	2000
		(in millions)	
St. Louis, Missouri, Operations			
Operating revenues (1)	$79.1	$62.4	$63.8
Operating income (loss)	6.1	(0.7)	1.6

featuring 4 restaurants and a banquet hall would adjoin the casino. The proposal would create approximately 600–700 construction jobs; 1,265 permanent jobs; and 1,895 indirect jobs. Isle's proposal had the support of the AFL-CIO, the South County Chamber of Commerce, and 11 state representatives. Also, of particular importance, Isle has donated approximately $500,000 annually to charities surrounding its other casino developments. Both county and city proposals would be built simultaneously and have a 24-month construction period. They would be financed with approximately 80 percent debt and 20 percent equity. Isle secured $500 million in revolving credit to help fund the two proposals.

Pinnacle Entertainment

Pinnacle Entertainment is a diversified casino operator with facilities in Indiana, Louisiana, Mississippi, Nevada, and Argentina. As of 2003, Pinnacle has operated seven casinos under the brand names Boomtown, Belterra, and Casino Magic in addition to receiving lease income from two Los Angeles area casinos. Although much smaller than its two competing bidders, Pinnacle boasted an experienced management team formerly integral to Steve Wynn's successful team at Mirage Resorts. The team was responsible for developing numerous premier Las Vegas casinos, including the Bellagio, Treasure Island, and Monte Carlo. At the time of its bid, Pinnacle did not have any gaming interests in the state of Missouri.[6]

Pinnacle's success, however, had not come without controversy. Pinnacle experienced a serious scandal in 2001 after the former chairman of the board, R. D. Hubbard, hosted an invitational golf tournament over June 26–29 for senior management and high rollers at the Belterra Casino and Resort and Spa in Vevay, Indiana. Ominous signs were apparent from the beginning when a plane leased by Pinnacle flew 8 or 10 "ladies of ill repute" to the event to entertain the guests. The Indiana Gaming Commission leveled a litany of gaming infractions against Pinnacle stemming from this tournament. The most serious of these infractions included the removal of chips, tokens, and money from the cage without proper authorization and alleged sexual harassment. The commission also contended that these events were not reported in a timely manner to authorities. To settle the complaint, Pinnacle agreed to pay a $2.26 million fine—the largest fine ever imposed by the Commission—and to suspend gaming operations for three days in 2002. During the suspension, the company had to pay wages and taxes it would have incurred during normal operations. In addition, Pinnacle agreed to build a 300-room guest tower within two years and adopt a corporate code of conduct. R. D. Hubbard resigned, along with president and CEO

Paul Alanis. Pinnacle worked to expunge all employees that were involved in or knew of the infractions and replaced them with managers with sterling reputations. The company was confident that the scandal would not affect licensing proceedings in Missouri.[7]

Pinnacle also proposed joint proposals in the county and the city. The city proposal called for a $200 million casino to be built at Laclede's Landing. The proposal called for a 75,000-square-foot gaming area with approximately 2,000 slot machines and 40 table games. The adjoining hotel and retail development would feature a health club, an event center, retail shopping, restaurants, a 300-room hotel, and an 80-room condominium tower. The proposal would create 1,300 direct jobs and approximately 750 indirect jobs. As part of their proposal, Pinnacle would agree to add $50 million in residential real estate within five years of the casino opening.

Pinnacle's county proposal called for a $300 million facility to be built in Lemay, Missouri, on 80 acres near the confluence of the Des Peres and Mississippi Rivers. The proposed location was the former site of the National Lead Plant, and Pinnacle agreed to clean up the area if its proposal was accepted. The facility would be flanked by a 24-acre public park and feature approximately 3,000 slot machines and 60 table games housed in 90,000 square feet of gaming space. The 280,000-square-foot facility would include an indoor ice rink, a movie theater, a bowling lane, a spa and salon, a nightclub, restaurants, and a 100-room boutique hotel with prime views of the Mississippi River. The proposal is expected to create 800 to 1,000 direct jobs and approximately 750 indirect jobs. Further, Pinnacle agreed to donate $4 million to build an aquatic community center in the surrounding area in addition to annual contributions to local charities. The company also stated its preference for using local businesses owned by minorities or women as vendors for its operational maintenance, which was projected to run around $50 million annually and which boasted the support of numerous local unions. The projects would be built simultaneously with a construction period of 18 months. In 2003, the company had $250 million in revolving credit for a development in Lake Charles, Louisiana. Pinnacle stated it would raise the additional capital necessary for the two projects using a combination of debt and equity to be determined by the dynamics of the market at the time of approval.

CONCLUSION

The agreement between the city and county of St. Louis to pursue casinos together in order to facilitate better deals essentially eliminated Harrah's proposal from the beginning. This elimination was made official on January 14, 2004, when the St. Louis County Gaming Selection Committee named the two finalists: Pinnacle Entertainment and Isle of Capri Casinos, Inc.[8] On January 15, 2004, the St. Louis Development Corporation chose Pinnacle Entertainment's $254 million casino development plan for downtown St. Louis's Laclede's Landing over the proposal of rival Isle of Capri Casinos, Inc.[9] The Pinnacle proposal was chosen partly because "it proposed to build on a much larger scale than Isle of Capri."[10] Additionally, on February 10, 2004, the St. Louis County Port Authority commissioners approved the Pinnacle's $300 million casino complex in south St. Louis County. The county chose Pinnacle because the city had already approved its downtown casino proposal, and the company's county site choice of Lemay, Missouri, was more ideal than Isle's proposed site.[11] Also, the county believed that "state gaming regulators were more likely to approve a two-boat, city-county project from the same company than a single, county-only casino," given that "gaming officials [had] previously expressed concern that a new casino in south St. Louis County would hurt revenues at a downtown one."[12]

Now that the casino proposals were accepted by the county and city committees, Pinnacle needed only MGC licensing before the company's plans could come to fruition. However, even before the company began its campaign for licensing, certain political considerations had to be satisfied. Because the planned county casino was only eight miles south of the proposed downtown casino, the city requested the following "additional sweeteners" in its contract with Pinnacle:

> To accommodate the city, Pinnacle agreed, among other things to open its city casino at least a year before it opens a Lemay casino, to pay St. Louis $1 million a year to help make up for money that may be lost to the potential operation in Lemay, and to pay a fine if it does not build a promised $50 million residential or retail project within five years of opening the downtown casino.[13]

Although Pinnacle made a few more concessions to the city, the company also received an option to lease up to seven acres of city-owned land to expand its casino, housing, or retail buildings at Laclede's Landing and flexibility in its $50 million construction promise.

After months of tireless negotiations with the City of St. Louis, St. Louis County, and the MGC, Pinnacle Entertainment's hard work finally paid off. On September 2, 2004, the commission approved Pinnacle's two casino proposals for licensing priority, effectively removing Isle of Capri's and Harrah's proposals from the running. The commission "judged Pinnacle to have enough financial strength to carry through on the project" and "also acknowledged that the development at Laclede's Landing probably would mean the demise of the President Casino on the Admiral."[14]

Clearly, whether this was the "right" decision will be revealed in the long run. However, what can be debated now are the following questions: (1) Did the MGC make the correct decision without political pressure? (2) Were the right criteria employed? Was there too much emphasis on revenue rather than economic development? (3) Finally, should the government be involved at all in casino development? Why is opening a casino different, for example, from opening a restaurant?

NOTES

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8

Playing the Revenue Game: New England's Gaming Industry

With the prospect of increasing budget deficits, many state governments are now considering the introduction of casino gambling within their states to raise revenues. The amounts projected for these budget deficits are staggering. In the New England region, general revenues, especially those from the personal income tax, fell sharply in every New England state except New Hampshire in fiscal year (FY) 2006. All six New England states closed the fiscal year with deficits. According to the Boston Federal Reserve Fiscal Facts, Massachusetts collected nearly $30 billion in revenues in FY 2005, but is still faced with a $1.2 billion deficit for FY 2007. Connecticut ended FY 2005 with a budget deficit of $817 million, or 6.8 percent of general fund spending. Maine closed FY 2005 with a $93 million deficit in its general fund budget; an additional $150 million deficit is predicted for FY 2007. Maine will likely end its biennial budget cycle in June 2007 with a $243 million insufficiency in its $5.3 billion general fund budget, making up roughly 5.5 percent of the state's general fund expenditures. Vermont's general revenues declined by 10 percent from FY 2005 to FY 2006 and caused a budget gap for FY 2007 of $25 million or 3 percent of general fund spending. Finally, New Hampshire will end FY 2006 with a $62.6 million deficit (2.7 percent of budgeted expenditures), and Rhode Island experienced shrinking revenues for FY 2005 and FY 2006 by $92.9 million and $74.6 million, respectively.[1]

The increasing deficits have prompted many states to review the revenue streams of nearby states to see if there might be any chance for additional in-state revenues. A driving factor in states' entrance into the casino industry is the success of a nearby state coupled with a desperate need for a larger revenue stream. Within the New England region, Connecticut, having made a compact with the Indian tribes who have operating rights for Foxwoods and Mohegan Sun, received nearly $400 million from casino payments to the state in the FY 2005, and that payment rate had an annually compounded growth of 18.6 percent over five years.[2] Citing the success that Connecticut has had, a majority of the remaining New England states are now considering the introduction of casinos. Massachusetts has contemplated various gambling legislation ranging from permitting slots machine at racetracks to allowing privately operated casinos, whereas Rhode Island is examining casino gambling.

In 2005 Massachusetts residents spent an estimated $820 million at Connecticut's two casinos—Foxwoods and Mohegan Sun—and they are dropping an additional $726 million at other out-of-state gambling facilities each year.[3] If this sum were to be spent in-state, Massachusetts might be able to reap a significant percentage of that amount for its state revenues. The same can be said for Rhode Island. West Warwick, Rhode Island, is merely 45 minutes away from Foxwoods, and Mohegan Sun is about an hour away, and for a state with a huge deficit, the profit that Rhode Island could reap from an in-state casino could make the introduction of casinos a worthwhile venture.

Given this gambling scenario, Massachusetts's governor, Deval Patrick, faces the dilemma of introducing additional gambling in Massachusetts. He could advocate for the introduction of Video Lottery Terminals or slot machines, approve Native American casinos, or legalize casino gambling. Of course, he could also want to maintain the status quo.

DATA ANALYSIS

If additional gambling were introduced, what revenue could Massachusetts and Rhode Island expect to obtain? In order to explore this question quantitatively, it is first necessary to examine the states' current tax structure regarding casino gambling. Second there needs to be an analysis of the current contributions to revenue that the forms of gaming are providing to Rhode Island, Massachusetts, and Connecticut. Finally, this chapter discusses the external factors and issues that may impact a state's revenues from gaming operations.

Taxation of Casinos

In the appendix of this chapter, there is a listing of all of the tax rates on the various forms of gambling permitted by state governments. As the appendix shows, different states collect taxes at different rates, with the range being between about 7 and 30 percent. It is important to note that the states that have higher gaming revenues generally have lower tax rates, in some cases much lower. Furthermore, in addition to the direct taxes on, or contributions from, gambling activities, casinos bring in further tax revenues through taxes on hotel room rentals, meals, and shopping sales. This amount can be collected at both the local and the state level. Furthermore, when private-firm casinos are introduced, the states need to spend money on regulating these casinos. In comparison with the potential for tax revenues using the private-firm format, the earnings of Indian casinos, of the tribes operating the endeavors on tribal land, and of individual tribal members cannot be taxed. Therefore, any state that is considering placing new gambling sites within its borders should consider the various options for additional gaming revenues.

In addition to choosing the group to operate additional gambling sites, policy makers also need to consider whether these sites will be large destination sites or smaller convenience sites. National casino destinations, such as Las Vegas and Atlantic City, offer more possibilities of outside tourists visiting the area, which will result in positive gains. Also, large casinos might benefit the region by recapturing the amount of money that local residents would otherwise spend outside the region. Convenience or localized casino gambling aims to capture a limited geographic market and may not result in any significant earnings. According to the National Gambling Impacts Study Commission's (NGISC) final report, "no economic benefit to either place or a person was advanced by proponents of convenience gambling. There are no national statistics that indicate the specific impacts of neighborhood gambling."[4] If a casino is not a destination draw, then the NGISC study shows that the convenience casinos simply recirculate local dollars.

Current Contributions

Rhode Island

In the 2006 election, Rhode Island's voters turned down a proposal for placing a casino within its borders. When considering the possible benefits and costs that casino gaming could have added to Rhode Island revenues, it is important to first examine the current contributions that the state is receiving from its gaming operations.

Rhode Island receives money from its traditional lottery system, keno, and Video Lottery Terminals (VLTs) that are operational in its two racinos, located in Lincoln Downs and Newport Jai Alai. Total gambling revenue for

Rhode Island includes: VLTs, keno, and nine forms of traditional lottery (instant tickets, Powerball, Wild Money, Roll Down, Numbers, Instant Match, Money Roll, Easy Win, and Daily Millions).

The introduction of VLTs into Rhode Island in July 1997 has had a substantial effect for Rhode Island because the vast majority of gaming revenue that Rhode Island receives comes directly from the VLT contributions. As will be shown there is clearly a high correlation between the VLTs and total revenues.

The following is a breakdown of the components of Rhode Island gambling revenue. This analysis (monthly data from 1993 to 2005 for all gaming revenue) incorporates a trend component will determine the actual forecasted effect of each component on the total revenue. The general mathematical representation of the model for decomposition approach is as follows:

$$Y_t = f(S_t, T_t, E_t)$$

where Y_t is the time series value (actual data) at period t,
S_t is the seasonal component (or index) at period t,
T_t is the trend-cycle component at period t, and
E_t is the irregular (or remainder) component at period t.

Table 8.1 shows the seasonality of the Rhode Island data. It is notable that the data is surprisingly seasonal.

The seasonal components reveal that the warm weather months have higher indices—translated as higher revenues. In establishing a casino or promoting the current racinos, that time period is optimal because it is the time period where the majority of vacation time is spent. If an introduction of a casino will bear similar seasonality, then a destination casino will be an option that is worth considering. The trend component of the data is shown in Table 8.2.

Table 8.1
Seasonal Indices: Rhode Island Data, July 1997–December 2002

July	105.677	November	96.069	March	106.583
August	103.266	December	92.947	April	103.504
September	98.213	January	94.750	May	104.730
October	100.388	February	95.035	June	98.837

Table 8.2
Trend by Segment: Rhode Island Data, July 1997–December 2002

Total:	922,372 t + 45,136,455	(t = time in months)
Video:	821,517 t + 31,505,650	(t = time in months)
Lottery:	55,362 t + 9,755,577	(t = time in months)
Keno:	48,147 t + 3,846,858	(t = time in months)

Analyzing these equations confirms that the total revenue is driven by the video component. During the period of analysis, total gaming revenues showed an average increase of about $925,000 per month, and 90 percent of this increase was attributed to the video component. The trend equations for the lottery and keno numbers further support the view that lottery and keno have shown relatively limited growth and do not represent a majority of the growth in the Rhode Island gaming revenue.

It is evident that Rhode Island currently is very reliant on the VLTs as a source of revenue. Therefore, it is imperative that the effect of the introduction of casinos on VLTs play be considered. This potential for "cannibalization" of existing gaming opportunities is a major factor in whether casinos offer a viable option for greater revenues. Cannibalization is the deterioration of one product's sales as a result of the introduction of another product or, conversely, the increase in sales of one product (game) at the expense of another.[5]

Currently, the Rhode Island state government collects 51 to 57 percent of revenues at Lincoln Downs and Newport Jai Alai, with 1 percent given to the local town or city that hosts the various sites. It is evident that no states currently benefit at those high rates and that casinos will not be able to compensate the states at that level! This is why Rhode Island voters wisely turned down the proposal to establish a casino in the state.

Massachusetts

Massachusetts is another state in the New England region considering the introduction of additional gambling. Massachusetts could face the highest absolute deficit, projected at a figure well over $2 billion if various proposed programs are approved without additional revenues. Also, it is important to note that Massachusetts residents spend over $1.3 billion at out-of-state gambling facilities each year.[6] (This considers the estimated $700 million spent at Connecticut's two casinos—Foxwoods and Mohegan Sun—and an additional $600 million spent at other gambling facilities and venues.) It has been argued by pro-gambling factions that if this amount could be spent in-state, then the state would be able to recoup gaming revenues in the hundreds of millions of dollars.

Currently, Massachusetts collects significant amounts of revenues from different forms of the traditional lottery. See Table 8.3 for a breakdown of the lottery segments. On a per capita basis, Massachusetts is a national leader in lottery per capita sales, exceeded only by the District of Columbia.[7] Table 8.3 shows some data about the state's lottery program.

Clearly, the sales amount for the lottery program is significant. Furthermore, a significant percentage of the lottery sales is returned to the Massachusetts general fund.

Revenue generated from lottery sales is used for three purposes.

1. A minimum of 45 percent of revenues stays in the state lottery fund to be paid out in prizes. Currently, the lottery's prize percentage is over 69 percent.
2. A portion of revenues is transferred to the commonwealth's general fund for the expenses incurred in administering and operating the lottery. The administrative and operating expenses of the lottery are appropriated by the legislature as part of the annual state budget. Operating expenses cannot exceed 15 percent. Currently, operating expenses are under 8 percent. These operating expenses include 5.8% percent in commissions and bonuses paid to the sales agents who sell the tickets and under 2 percent in administrative expenses due to lottery operation.

Table 8.3
Massachusetts Lottery Program

Year Lottery Founded	March 1972
Sales FY 2001	$3,969 million
Sales FY 2002	$4,211 million
Sales FY 2003	$4,292 million
Sales FY 2004	$4,339 million
Sales FY 2005	$4,483 million
Games Offered	Instant games, 3-digit game, 4-digit game, the Big Game, keno, cash lotto (Mass Cash / matrix: 5/35), Pulltabs, Megabucks (matrix: 6/42), and Mass Millions
Beneficiaries	Approximately 25% to 30% goes to cities and towns, compulsive gambling treatment, the arts council, and the state's general fund.
Jurisdiction	State of Massachusetts

3. After prizes and expenses, the remaining lottery revenues (approximately 23 per cent) are transferred to the state's general fund, which can be used to finance the local aid fund and returned to the cities and towns of the commonwealth in the form of local aid.

In FY 2005, Massachusetts received about $936 million from the state's lottery program. The lottery sales data from January 1998 to February 2006 is used for analysis on the current contributions of Massachusetts gaming revenue. This includes all the component games of the lottery program: instant tickets, Mass Millions, Megabucks, Mass Cash, the Big Game, keno, and Daily Numbers. Just as with the Rhode Island data, the total gaming revenue is affected primarily by just one component. In Massachusetts's case, instant tickets clearly constitute the vast majority of lottery revenue. The other components of the lottery program remain relatively steady and do not show any significant fluctuations. The significance, in terms of introduction of casinos, of the dominance of instant tickets in the total lottery sales is discussed in a following section.

Once again, the data is analyzed using a seasonal decomposition and a trend analysis. This allows existing Massachusetts revenues to be analyzed in the same manner as Rhode Island. Table 8.4 shows the seasonal indices for the Massachusetts Lottery program.

From the seasonal analysis, it becomes clear that the lottery data is seasonal. The higher revenue months are clearly the cold weather months. As in the case with Rhode Island, this seasonality pattern is favorable. If a casino's seasonal index is geared for higher revenues in the warm weather months, Massachusetts might be able to take advantage of the lottery program in the colder months and casino revenues in the warmer months, thereby giving the state a chance to maximize revenues for the entire year.

The trend component offers further analysis. The trend equations are displayed in Table 8.5.

During the period that was analyzed, Massachusetts government saw lottery revenues increase by an average margin of over $1.5 million per month. And

Table 8.4
Seasonal Indices: Massachusetts Lottery Data, January 1998–February 2006

January	108.353	May	94.409	September	90.897
February	94.882	June	97.250	October	96.227
March	105.926	July	91.440	November	101.326
April	106.921	August	90.742	December	121.627

Table 8.5
Trend by Segment: Massachusetts Lottery Data, January 1998–February 2006

Total:	1,514,072.6 t + 266,000,000.00	(t = time in months)
Instant:	1,402,655 t + 170,000,000.00	(t = time in months)
All other games:	194,085.3 t + 94,860,591.00	(t = time in months)

as was expected from Table 8.4 an increase in instant ticket games revenue constituted about 93 percent of the total revenue increase. Instant games are clearly the dominating factor in driving the lottery revenue. All other games remain steady; however, the significance of their contribution to the overall lottery revenue has decreased over time.

Once again, the cannibalization of existing gaming revenues is a concern when considering the introduction of a new avenue of gaming opportunity. If cannibalization exists between lottery games and additional gambling, then the introduction of additional gambling sites will negatively affect existing lottery sales.

Massachusetts's lottery program is clearly one that is dependent on instant games. The chief worry for Massachusetts legislators is whether the Mass Lottery will suffer a decrease in sales when additional gambling is introduced.

In 2006 Massachusetts collected about 23 percent of the lottery revenues for the state's coffers. Because some states collect more than 23 percent of casino tax revenues (including compacts with Native American tribes), it is conceivable that depending on the size of the expected of additional gambling revenue, Massachusetts could recuperate all lost lottery revenue and receive more tax revenues as a result. However, with instant ticket revenues of over $3 billion for the year 2005, any additional gambling operation has to be able to make a substantial contribution to overall gaming revenues.

Connecticut

Connecticut's foray into the gambling industry has been phenomenal. Since 1972, the first year of the state's lottery program, the Connecticut government has allowed the introduction of pari-mutuel facilities (1976–1977), both greyhound racing in two locations and Jai Alai in two locations, off-track betting, and finally Indian-run casinos. Foxwoods opened its doors in 1993, and Mohegan Sun followed in 1997. Since 1972, when the lottery program contributed $8.15 million to the Connecticut general fund, the contribution from gaming has exploded. In FY 2002, Connecticut collected nearly $650 million, with the two casinos contributing about $370 million to that total. Table 8.6 shows the contributions of all the component games for the state of Connecticut. It is important to note that the lottery program dominated the revenue stream for the state coffers until the inception of the casinos in 1993.

Pari-Mutuel Facilities

In Connecticut there are greyhound racetracks in Plainfield and Bridgeport. There are also two Jai Alai locations in Hartford and Bridgeport. Until 1987 pari-mutuel revenue steadily increased, but with the introduction of Native American casinos, there has been a decline in the amount that the state has been able to collect. From 1993, when Foxwoods opened, the state has collected between 1 and 2 percent of total sales. When one compares this figure to the pre-casino era, when the state had been able to collect over 6 percent, it becomes clear that the competition that the pari-mutuel venues face from the casinos has driven down their sales and the state's revenues. In fact, the state of Connecticut has had to subsidize some of these venues to keep them from closing.

Lottery

Connecticut's lottery program began in 1972. The data used to analyze the state's lottery program is annual data from 1972, both sales data and the amount contributed to the state for all the component games of the program: weekly numbers, instant tickets, Daily Numbers, Lotto, Cash Lotto, and Powerball It is important to note that until 1993, total lottery sales have been driven by a combination of Lotto, Daily Numbers, and instant ticket sales. Since 1993 there has been a direct correlation between the total lottery sales and the sale of instant lottery tickets, signifying that the increase in lottery sales revenue is largely a result of instant ticket sales growth. The trend equations in Table 8.6 quantify this correlation

It is important to note that over the whole period from 1972 to 2002, instant ticket sales accounted for 60 percent of total sales. From 1993 a greater portion of total lottery sales were due to the sales of instant ticket sales. This indicates that, like Massachusetts's program, Connecticut's lottery program is mainly driven by instant ticket sales.

So what happened to Connecticut's lottery sales with the introduction of casino gambling? In Connecticut's case, lottery sales have essentially achieved a steady state. In response to the introduction of casino gambling, the Connecticut lottery introduced a new approach for instant ticket sales. In this

Table 8.6
Trend Equations, Connecticut Lottery Sales, 1972–2002

Total sales =	32,233,330 t – 104,000,000	(t = time in years)
Instant ticket sales =	(23,783,305.89)^(.1135 t)	(t = time in years)

Table 8.7
Trend, Percentage Collected: Connecticut Lottery, 1972–2002

Total =	0.481 – 4.877E-03 t	(t = time in years)
	(.5% decline each year)	

approach, Connecticut released higher-priced games (up to $10 per game) and returned a greater percentage as winnings. This approach might explain the growth of instant ticket sales, even with the competition coming from the casinos. This growth in instant sales enabled the Connecticut lottery to stabilize any overall decline in lottery sales.

However, it is important to note that the competition has had an effect on the state's coffers. Although the total amount of lottery sold increased by a large margin ($552 million in 1993 to $907 million in 2002), the amount that the state has been able to get from these games has not shown significant growth ($221 million in 1993 to $271 million in 2002). In fact, the trend for percentage of lottery collection has had a steady decline. This is because instant lottery tickets give the lottery a lower payback than the other two forms of lottery play (see Table 8.7).

Casinos

No matter how much the lottery has influenced Connecticut's revenues, since the inception of both Foxwoods and Mohegan Sun, it is apparent that the contributions from the casinos are the main factor in the amount of transfers to the general fund. Examining the annual data from 1993 quantifies this statement (see Table 8.8).

These trend equations show that casino collection made up over 92 percent of the total contribution growth to the state annually from 1993 to 2005. In comparison, the amount that the lottery provides has meant very little in terms of growth.

Table 8.9 shows Connecticut's casinos' monthly contributions to the state. It becomes evident that there is a steady growth in these numbers. The multiplicative seasonal decomposition shows that the data is seasonal for warmer weather months. It is interesting to note that like the VLTs in Rhode Island,

Table 8.8
Trend Equations: Annual Contributions to the State of Connecticut, 1993–2005

Total =	39,301,370 t + 265,000,000	(t = time in years)
Lottery =	4,556,523 t + 226,000,000	(t = time in years)
Casino =	36,183,521 t + 20,439,971	(t = time in years)

Table 8.9
Seasonal Indices (Sales): Foxwoods and Mohegan Sun, Monthly, 1993/1997–2005

Foxwoods		*Mohegan Sun*	
January	88.505	January	88.715
February	92.191	February	95.895
March	100.108	March	101.737
April	100.526	April	100.090
May	102.174	May	103.353
June	98.788	June	99.904
July	117.391	July	111.056
August	114.829	August	110.577
September	103.126	September	98.682
October	102.119	October	102.559
November	95.327	November	94.805
December	84.915	December	92.626

Connecticut's casinos gather more revenue during the warmer months, which is in line with the idea that the warmer months see more visitor traffic. Table 8.10 gives the trend equations for the de-seasonalized data casino revenue data. It is significant to note the growth of the contributions to the state, which grew at a combined $200,000 per month over 10 years of casino operations.

The analysis of Connecticut's gaming data illustrates that casinos did indeed cannibalize the other components of the state gaming venues. Pari-mutuel facilities have seen steady decreases, with the venues having to be subsidized to be kept open. Lottery, even though it has seen some growth in terms of overall sales, has seen the contribution to the state shrink to merely 10 percent of total growth. As it becomes clearer that Connecticut is dependent on casinos, a reexamination of both Rhode Island and Massachusetts is in order to decide whether a casino would mean the optimization of revenues for each state.

Table 8.10
Trend: Connecticut Casinos—Total Handle, Total Collected

Trend: Total Handle—Connecticut Casinos		
Foxwoods:	4,172,427 t + 399,000,000	(t = time in months)
Mohegan Sun:	6,280,385 t + 297,000,000	(t = time in months)
Trend: Total Collected—Connecticut Casinos		
Foxwoods:	77,017 t + 8,533,312	(t = time in months)
Mohegan Sun:	132,435 t + 5,628,013	(t = time in months)

CONCLUSION

Rhode Island

It has been shown that Rhode Island relies heavily on the revenues from the VLTs from its two racinos. Collecting 51–57 percent of the EGD revenues, 90 percent of the state's gaming revenues come from this source. If Rhode Island voters had approved Native American gambling, Rhode Island legislators would have had to consider the answers to the following questions:

1. What rate of taxation is necessary for maximum realization of revenues?
    - How much revenue should be expected of a casino that is introduced?
    - Will this rate allow the casino operator a fair rate of return?
    - What type of casino (regional or national) should be introduced?
2. What effect will the casino have on the existing revenue stream from the VLTs?
    - What level of decline will be shown for the VLTs?
    - Will the rate of collection have to be lowered in the future for the VLTs?
3. Will these measures keep Rhode Island gaming competitive with gaming in neighboring states?

Massachusetts

Massachusetts relies on its lottery program, mostly driven by instant ticket sales, for gaming revenues. If Massachusetts could be compared to Connecticut, a valid argument could be made that the importance of the lottery program to Massachusetts's gaming revenues will experience a decline. The casinos' contribution to Connecticut grows at a much higher rate than does Connecticut's lottery program. The legislature in Massachusetts, then, also has to decide between existing revenues from the lottery, which in

FY 2005 amounted to nearly a billion dollars, and the potential benefits a casino may provide.

As in Rhode Island, Massachusetts policymakers should answer a similar line of questioning before they deem additional gambling to be a viable option for their state.

1. What rate of taxation is necessary for maximum realization of revenues?
    - How much revenue should be expected for a given form of gambling that might be introduced?
    - Will this rate allow the gambling operator a fair rate of return?
    - What type of gambling should be introduced?
2. What effect will the casino have on the existing revenue stream from the lottery program, especially instant games?
    - What level of decline will be shown for instant games?
    - Will this additional gambling be able to compensate for the loss in instant games, and if so, by how much?
3. Will these measures keep Massachusetts gaming competitive with gaming in neighboring states?

Other Implications

Since the early 1990s, the movement authorizing various additional forms of gambling has picked up a great deal of momentum. This movement was spurned possibly by the need for greater revenues. The success of Connecticut in realizing positive returns from its Indian casinos, Foxwoods and Mohegan Sun, has made other states in the New England region, Rhode Island and Massachusetts among them, considering following suit.

Currently, Connecticut's niche as the only state in the New England region with large casinos allows the state to earn a significant amount of revenue. Connecticut has sacrificed its pari-mutuel industry in establishing this niche. Meanwhile, Rhode Island has utilized VLTs at its tracks to greatly enhance its gaming revenues. Finally, Massachusetts's lottery is undoubtedly one of the most successful in the nation and has succeeded in giving a steady rate of return that appears to have plateaued. If Massachusetts permits additional gambling, then Foxwoods and Mohegan Sun will probably experience a decrease in its revenues. The size of this decrease would depend on type and location of additional gambling sites. Similar statements could be made about VLT revenue in Rhode Island. But Massachusetts is also taking a risk with its lottery revenue if it enters the gambling sweepstakes.

OPTIONS

So let us return to the options faced by Governor Deval Patrick of Massachusetts. He has five options:

1. Clearly, he could choose to oppose any additional gambling sites in Massachusetts and hope that the lottery can continue its slow but steady growth.
2. He could negotiate with the Wampanoags, the only federally recognized tribe in Massachusetts, to build a casino on their reservation and collect revenue, in a deal similar to the one worked out by Connecticut with its two tribal casinos. One consideration that needs to be taken into account is how this might affect lottery sales.
3. Governor Patrick could call for allowing the state's track owners to operate slot machines at their tracks, thereby saving the tracks and the jobs associated with those tracks. Once again, there has to be a concern over lottery sales.
4. The most radical proposal that Governor Patrick could proposed would be to allow a private casino in the Boston area. This would clearly maximize casino revenue, depending on the tax rate that the legislature would impose on the casino operators, but once again this might negatively affect lottery sales.
5. Finally, the fifth option and the most viable option politically would be to follow the Rhode Island example and set up VLTs in four Massachusetts race tracks. The lottery commissioner would operate these VLTs, and therefore there would be no question about cannibalizing the lottery as long as the revenue was shared as it currently is with the towns and cities. Because VLTs are not slot machines, this solution would enable the state to deny any additional gambling by Native American tribes. However, this proposal does involve the state even more heavily in gambling and in the addiction and social costs associated with gambling. Hence, if this option is chosen, it would behoove legislators to put aside additional funds to deal with the compulsive gambling issue.

What still needs to be ascertained is just how much revenue could be raised with any of these options and how both Rhode Island and Connecticut might respond to any additional gambling initiatives launched by Massachusetts. Finally, there is the ever-present concern of how additional gambling opportunities would affect the most successful lottery in the United States.

APPENDIX FOR TAXATION SUMMARY: RIVERBOATS, CASINOS, AND VIDEO LOTTERY

Arizona

Tribal Casinos

1% of the first $25 million of Class III net win
3% of the next $50 million of Class III net win

6% of the next $25 million of class III net win
8% of Class III net win in excess of $100 million

Colorado

Casinos

0.25% tax on adjusted gross proceeds up to $2 million
2% tax on adjusted gross proceeds exceeding $2 million, up to $4 million
4% tax on adjusted gross proceeds exceeding $4 million, up to $5 million
11% tax on adjusted gross proceeds exceeding $5 million, up to $10 million
16% on adjusted gross proceeds exceeding $10 million, up to $15 million
20% on gross proceeds exceeding $15 million
City of Blackhawk device fee of $750 per machine and table game
City of Cripple Creek device fee of $1,200 per machine and table game
Central City device fee of $1,160 per machine and table game

Connecticut

Tribal Casinos

25% tax on gross revenues of slot machines, or $160 million ($80 million per casino), whichever is more (as long as the tribes have a monopoly on slot machines)

Delaware

12.5% of the average daily win (the amount remaining after all payments to players) not exceeding $25,000
15% of the average daily win exceeding $25,000 but not in excess of $50,000
20% of the average daily win exceeding $50,000 but not in excess of $75,000
30% of the average daily win in excess of $75,000
The state receives an additional 12.27% of the proceeds attributable to licensees that conducted 40 or fewer days (at least 1 day) of live harness horse races during 1992, 12.59% of such proceeds of licensees that conducted more than 40 days of live harness racing during 1992 or that conduct thoroughbred racing under Title 28, and 12.73% of such proceeds of licensees that conduct thoroughbred horse racing pursuant to Chapter 101 of Title 3.

Illinois

Riverboats

15% tax on adjusted gross revenues less than $25 million
22.5% tax on adjusted gross revenues of $25 million–$50 million

27.5% tax on adjusted gross revenues of $50 million–$75 million
32.5% tax on adjusted gross revenues of $75 million–$100 million
37.5% tax on adjusted gross revenues of $100 million–$150 million
45% tax on adjusted gross revenues of $150 million–$200 million
50% tax on adjusted gross revenues in excess of $200 million
$3 per passenger ($2 per passenger at Casino Rock Island)

The state also imposes a required base amount payment from all Illinois casinos with the exception of Casino Rock Island. If a casino failed to meet its base payment amount by June 15, 2006, and June 15, 2007, a lump sum payment had to be paid to the state. The base amounts are as follows:

For a riverboat in Alton, $31 million
For a riverboat in East Peoria, $43 million
For the Empress Casino in Joliet, $86 million
For a riverboat in Metropolis, $45 million
For Harrah's Casino in Joliet, $114 million
For a riverboat casino in Aurora, $86 million
For a riverboat casino in East St. Louis, $48.5 million
For a riverboat casino in Elgin, $198 million

The base amount portion of the wagering formula was to terminate July 1, 2007, or when the state's dormant casino licensee became operational or if a licensee under the Illinois Horse Racing Act conducts gaming operations with electronic gaming devices or slot machines.

Indiana

Cruising Riverboats

22.5% tax on adjusted gross revenues
$3 per patron/per cruise admission fee
$25,000 initial licensing fee; $5,000 renewal thereafter

Dockside Riverboats

15% of first $2.5 million of adjusted gross revenue (AGR) based on state fiscal year
20% of AGR in excess of $25 million, but not exceeding $50 million, based on state fiscal year
25% of AGR in excess of $50 million, but not exceeding $75 million, based on state fiscal year
30% of AGR in excess of $75 million, but not exceeding $150 million based on state fiscal year

35% of AGR in excess of $150 million
$3 per patron admission fee
$25,000 initial licensing fee; $5,000 renewal thereafter

Iowa

Tax Rate

22%—riverboats and tracks with a boat in the same county and no table games and receipts under $100 million
24%—racetracks without a boat in the same county or with table games and adjusted gross receipts over $100 million

Games of Skill for Tracks—Application Fee

$3 million if the track has an AGR under $100 million
$10 million if the AGR is over $100 million
Prohibits table games at the Dubuque track until the boat there converts to a barge and agrees to allow the track to hold table games
The table license fee can offset taxes for up to five years

Fees

Infrastructure Fund fee for FY 2004 of $1.6 million for the Dubuque Greyhound Track, $10.1 million for Bluffs Run, and $11.9 million for Prairie Meadows; recoverable as a tax credit
Total fee of $30 million ($15 million in FY 2005 and $15 million in FY 2006) from the riverboats, based on 2.152% of their AGR; recoverable as a tax credit
Licensing fee for new licenses based on home county population, to be paid over five years—$5 million if the county population is less than 15,000; $10 million for home counties with populations between 15,000 and 100,000; and $20 million for home counties with a population in excess of 100,000
No more admission fees

Louisiana

Riverboats

21.5% of gross revenues (except boats on the Red River and Bally's in New Orleans)
Boats on the Red River

New tax rate of 21.5% phased in over 25 months. Rate beginning April 1, 2001, was 19.5%; beginning April 1, 2002 was 20.5%; then to 21.5% on April 1, 2003.

Bally's New Orleans

If monthly revenues are below $6 million, tax rate is 18.5%
If monthly revenues are between $6 million and $8 million, tax rate is 20.5%
If monthly revenues are greater than $8 million, tax rate is 21.5%

$2.50 per passenger local option fee

Casinos

21.5% of gross revenues or $50 million (in 2001), then $60 million (henceforth), whichever is greater

Video Lottery

Restaurants and bars pay $250 per machine per year and 26% tax
Truck stops pay $1,000 per machine per year and 32.5% tax
Racetracks and OTBs pay $1,250 per machine per year and 22.5% tax

Michigan

Tribal Casinos

10% tax on slot machines revenues (8% goes to the state, and 2% goes to the local municipality) while they have a monopoly on casino gaming; nothing thereafter (a couple of tribes who signed compacts in 2006 agreed to continue paying the tax after the Detroit casinos are operational)

Detroit Casinos

24% tax on gross revenues (55% to city of Detroit, 45% to state of Michigan)

The rate will roll back to 19% once permanent facilities are operational. If they are not complete by 2009, the rate will increase 1 point per year for three years, or until they are completed.

Municipal service fee—the greater of 1.25% or $4 million to be paid annually on the date the casinos open for operation.

Annual assessment (city and state regulatory costs): $25 million the first year and subsequently adjusted each year by multiplying the annual assessment for the preceding year by the Detroit consumer price index for the preceding year. This is shared by all three casinos.

Mississippi

Riverboats

Monthly state fees of 4% of gross gaming revenues for amounts less than $50,000 per month

6% on gross revenues from $50,000 to $134,000 per month

8% on gross revenues in excess of $134,000 per month

Local governments can impose up to a 4% tax on gross revenues
Table game fee ranging from $50 to $3,000 for up to 10 games: for the first 16 games, $500 per game; for 17 through 26 games, $4,800 per game; for 27 through 35 games, $2,800 per game; in excess of 35 games, $100 per game
Annual license fee of $5,000

Missouri

Riverboats

20% on annual adjusted gross receipts
Annual license fee of $5 per passenger capacity
Admission tax of $1 per passenger
Local option fee of 50 cents per passenger

Montana

Video Lottery

15% of net video lottery machine revenues, which are defined as those revenues received from machine play after pay-outs. Also called "net win" or "win."
Annual state device fee of $200
Operator-only fee of $1,000 (after January 1, 1994)
Manufacturer license fee of $1,000
Distributor license fee of $1,000
Operator fee of $1,000

Note: State does not purchase or lease any machines and does not operate a central computer system. Assesses a $1,000 license fee per operator per year. A manufacturer can distribute machines without buying a distributor's license, but if a manufacturer or a distributor wants to operate, an operator's license must be purchased.

Nevada

Casinos

3% of adjusted gross taxable gaming revenues up to $50,000
4% of adjusted gross taxable gaming revenues from $50,000 to $134,000
6.75% of adjusted gross taxable gaming revenues over $134,000 (beginning in 2004)

Note: Nevada casinos are additionally subject to a number of quarterly and annual taxes on the number of table games and slot machines in use as well as a 10% (of food and beverage sales) casino entertainment tax.

General definitions as used in this report:

In Nevada, the total *gaming wagered* amount is equal to the sum of all game and table wagering (the “Drop”) plus all slot machine (to include reel-type and video games) wagering (the “Handle”).

Thus, for slots the wagered amount includes all cash played as well as play from credits won.

The (casino) *win* amount is used synonymously with the term *gaming revenues* and equals the total wagering (drop plus handle) less all pay-outs as winnings to players.

Also for slots, the win percentage is the ratio of the (casino) win amount to the total wagered amount.

Taxable gaming revenues (applicable to Nevada casinos only) consist of the casino win or gaming revenue amount minus credit extended to customers by the casino, plus credit repayments, minus a bad debt allowance.

New Jersey

Casinos

$200,000 minimum for initial one-year license
$100,000 minimum for every two-year renewal

8% of gross gaming revenues. An additional 1.25% local reinvestment tax rate paid directly to or given credit by the Casino Reinvestment Development Authority.
4.25% of the value of free rooms and meals offered to patrons.

Scheduled to be phased out beginning in 2006
7.5% net income tax

Note: Gross gaming revenues for Atlantic City casinos consist of the gaming win less the bad debt allowance only. It is this figure—gross taxable gaming revenues—to which specific state gaming taxes are applied.

Explanatory Notes: Atlantic City casinos also pay an annual $500 slot tax for each machine. Casinos (corporations) may also be subject to a state corporate income tax of 9%.

Atlantic City casinos also pay an hourly regulatory enforcement fee (as set by the budget of the NJCCC) to pay for on-site gaming regulation.

Note: In New Jersey, the fee for a casino license is based on the costs of investigation, but is a minimum of $200,000 for an initial one-year license and a minimum of $100,000 for a two-year renewal. Casinos must pay an 8% tax on gross casino revenues and an additional $500,000 tax on every slot machine.

In addition, casino licensees must either pay an additional tax of 2.5% of casino gross revenues or purchase bonds from or make investments in projects approved by the Casino Reinvestment Development Authority in an amount equal to 1.25% of casino gross revenues.

All other fees are set by regulation. Casino service industry licensing fees are $3,000 for a one-year gaming-related license and $1,500 for a three-year non-gaming-related one.

Three-year junket enterprise license fees are also $3,000. Casino key employee and junket representative license fees are based on the cost of investigation, but are a minimum of $500 and a maximum of $3,000. Casino key employee licenses are valid for an initial term of one year, and the renewal fee is $500. Junket representative licenses are valid for a three-year term, and the renewal fee is the same as the initial issuance fee. The issuance and renewal fees for three-year casino employee licenses range from $180 to $275 depending on the position applied for. Casino hotel employee registration costs $30 and remains in effect until revoked.

New Mexico

Tribal Casinos

Quarterly regulatory fee of $6,250 per gaming facility plus $300 per gaming machine plus $750 per gaming table or device other than a gaming machine. These amounts shall increase by 5% each year beginning on the first day of January occurring after the compact has been in effect for at least 12 months.

8% of net win

Electronic Gaming Devices at Tracks, Veterans Clubs, and Fraternal Clubs

10% of the gross receipts of manufacturer licensees from the sale, lease, or other transfer of gaming devices in or into the state

10% of the gross receipts of distributor licensees from the sale, lease, or other transfer of gaming devices in or into the state

25% of the net take of every gaming operator licensee

New York

Tribal Casinos

25% tax on gross revenues of slot machines

VLTs at tracks

61% to the state (to aid education)

10% to the lottery (to administer the games; any balance left over after regulatory costs goes to education)
20.24% to racetracks in years 1–3; 20.01% in years 4–5; 17.487% in years 6–10
1.247% to breeders in years 1–5; 1.508% in years 6–10
7.511% to purses in years 1–3; 7.743% in years 4–5; 10% in years 6–10

Oregon

Video Lottery

65% of net video lottery machine revenues, which are defined as those revenues received from machine play after pay-outs. Also called "net win" or "win."

Note: The state purchases and maintains all machines and operates a central computer system.

Pennsylvania

Slot Machines at Tracks (Category 1), Stand-Alone "Slot Parlors" (Category 2), and Small "Resort" Slot Parlors (Category 3)

$50 million one-time slot machine licensing fee (categories 1 and 2 only); $5 million one-time licensing fee (category 3)
34% daily tax on daily gross terminal revenue
4% of daily gross terminal revenue as a local share assessment

Category 1 license that is a harness track located in:

- 3rd class county—2% of gross terminal revenue to host county
- 3rd class county with 3rd class city—1.2% of gross terminal revenue to host county
- 4th class county—2% of gross terminal revenue to host county

Category 1 license that is a thoroughbred track located in:

- 4th class county—2% of gross terminal revenue to host county

Category 2 license located in:

- 1st class county—4% of gross terminal revenue to host county
- 3rd class county with 3rd class city—1.2% of gross terminal revenue to host county
- 4th class county—2% of gross terminal revenue to host county

5th–8th class counties—2% of gross terminal revenue to host county

Category 3 license shall pay 2% of gross terminal revenue to the host county.
Category 1 or 2 license that is located in:

2nd class city—2% of gross terminal revenue or $10 million annually, whichever is greater, to host city
2nd class A city—2% of gross terminal revenue or $10 million annually, whichever is greater, to host city
The amount allocated to the designated cities shall not exceed 50% of their total budget for FY 2003–2004, adjusted for inflation.

3rd class city—2% of gross terminal revenue or $10 million annually, whichever is greater (unless there was a prior written agreement between the licensee and the city to provide additional compensation to the city in excess of the 2% or $10 million)
3rd class city that is located in more than one 3rd class county—2% of gross terminal revenue or $10 million annually, whichever is greater, to host city
1st class township—2% of gross terminal revenue or $10 million annually, whichever is greater, to host township

The amount allocated to the designated townships shall not exceed 50% of their total budget for FY 2003–2004, adjusted for inflation.

2nd class township—2% of gross terminal revenue or $10 million annually, whichever is greater, to host township

The amount allocated to the designated townships shall not exceed 50% of their total budget for fiscal year 2003–2004, adjusted for inflation.

Borough—2% of gross terminal revenue or $10 million annually, whichever is greater, to the host borough
The amount allocated to the designated borough shall not exceed 50% of their total budget for fiscal year 2003–2004, adjusted for inflation.
Incorporated town—2% of gross terminal revenue or $10 million annually, whichever is greater, to host incorporated town.

The amount allocated to the designated incorporated town shall not exceed 50% of their total budget for fiscal year 2003–2004, adjusted for inflation.

Category 3 license located in any municipality—2% of gross terminal revenue to host municipality

The amount allocated to the municipality shall not exceed 50% of their total budget for FY 2003–2004, adjusted for inflation.

Rhode Island

Video Lottery

Lincoln Greyhound Park keeps 27%; Newport Jai Alai keeps 26%
Purses: 3.4% (dog track only)
Technology providers: 7%
Host community: 1%
Balance goes to the state

South Dakota

Casinos

$2,000 per card game or slot machine annually
8% adjusted gross gaming revenues

Video Lottery

50% of net machine revenues, which are defined as those revenues received from machine play after pay-outs. Also called "net win" or "win."

West Virginia

Video Lottery (at racetracks)

30% of net video lottery machine revenues, which are defined as those revenues received from machine play after pay-outs. Also called "net win" or "win."

Video Lottery (at bars and fraternals)

30% of net video lottery revenues until June 1, 2002
Following June 1, 2002, the Lottery Commission shall calculate the aggregate average daily gross terminal income for all operating VLTs during the preceding six-month period and use the following schedule for the next year:

- 30% of net video lottery revenues, if aggregate average gross terminal income per day is $60 or less
- 34% of net video lottery revenues, if aggregate average gross terminal income per day is between $60 and $80
- 38% of net video lottery revenues, if aggregate average gross terminal income per day is between $80 and $100
- 42% of net video lottery revenues, if aggregate average gross terminal income per day is greater than $100

Sources: Compiled from state Web sites and Insight Volume 5, Issue 1 (2006).

NOTES

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9

Macau: China's Entry into the World of Gambling

Gaming in Macau is not a new penomenon. Its history traces back to before the Portuguese colonized the island in the sixteenth century. When the Portuguese did arrive, they did not attempt to change the customs of the indigenous people. However, gaming was not officially legalized until the 1850s, and the industry did not start booming until the end of the nineteenth century.

In 1930 the decision to auction off a monopoly on gaming was made by the Portuguese Colonial rulers to the Hou Heng Company, headed by Fok Chi Ting.[1] It was then awarded in 1937 to the Tai Heng Company, which narrowly lost the right to it in 1962 to STDM. The Portuguese government contemplated four special licenses in 1982, which would have given groups a specific geographic region over which they would have a monopoly. However, this proposition did not pass, and STDM's monopoly existed until 2002. In 2002, Portugal handed over control of Macau to the Chinese Government. Since 2002 the Chinese government has made many concessions and subconcessions to gaming companies. The first resort to open as a result of these moves was the Sands in May 2004. Another achievement in 2004 for the gaming companies was the new law that gave them the ability to grant credit and enforce gaming debts, a practice previously not allowed because of the cultural ideals of the residents. However, this new law was so important that Steve Wynn (owner of a premier Las Vegas casino) announced that he would not plan on buying property or opening a casino in Macau until the law was in effect.

MACAU'S GAMBLING EXPLOSION

Recently, Macau has been dubbed the "Monte Carlo of the Orient."[2] This nickname is becoming well-deserved. There were only 11 casinos in 2002. As of August 2006, there were 21 casinos operating on the island. This number is expected to more than double, to 45, in the subsequent three years. As of 2006, 60 new hotels were being planned or built to provide rooms for the upcoming influx of gamblers. However, according to locals, only two of the casinos are actually flourishing. Despite these reports, Macau's gross domestic product (GDP) grew 14.2 percent in 2003 and 28.3 percent in 2004. These factors help the younger locals to be optimistic about Macau's future.

This increase in casinos and hotels has resulted in a similarly strong increase in visitors to the island. In 2005 Macau welcomed 10.5 million visitors from China, 2.5 times as many as it had seen in 2002. Chinese visitors accounted for 56 percent of all visitors in 2005, up from 37 percent in the same time frame. Macau has growth potential in a variety of areas. According to the American Gaming Association, the acronym MICE describes the facets on which Macau should concentrate: meetings, incentives, conventions, and exhibitions. Almost every hotel planned for Macau is looking to specialize in at least one of these growth areas. For instance, the Venetian Macau plans on having 35 percent of their rooms filled by conventioneers. The Macau government has stated publicly that it intends to double its number of visitors to approximately 37–38 million by 2010.[3] Although most indicators are positive, many difficulties need to be addressed. First, there are still various issues with the Chinese government, mainly China's strong tendency to have inconsistent policies. Also, locals have some major concerns for Macau. One obvious concern is that they will become, if they have not already, too dependent on casinos. In a similar vein, they are somewhat bothered by their overreliance on gamblers coming from the Chinese mainland. Also, they realize that the rapid growth of the casino industry in Macau in the recent past and near future cannot continue given restrictions on not only demand, but also, and more importantly, land. Last, local authorities have been citing a sharp increase in casino-related crimes, such as money laundering, but others feel that the numbers are inflated because the grouping "casino-related crimes" is vaguely defined. Clearly, there is a fair amount of unease about Macau's long-term development.

Many companies are vying for a strong foothold in Macau, and some have a set strategy already. There are two basic strategies that casino-hotels can follow, embodied by two Hong Kong–listed companies. First, Melco International Development will compete directly with the U.S. gambling heavyweights Wynn Resorts, Las Vegas Sands, and MGM Mirage on the basis of grandiose luxury.[4] Melco is planning on building Macau's first six-star hotel, the Crown Macau, in 2007 as well as the City of Dreams (a series of casinos that Macau hopes to rival the Las Vegas strip) marketed to both VIP and mass-market gamblers, in 2008 in a joint venture with Australia's Publishing and Broadcasting. Melco has a leg up in the race for supremacy in Macau because of the familiarity of its CEO, Lawrence Ho, the son of the casino monopolist Stanley Ho, with the gaming industry in Macau.

Galaxy Entertainment Group, on the other hand, intends to pursue casual visitors from mainland China who are on a budget. This is the less popular of the two strategies, but it has its advantages because there is less competition with the U.S. companies, and Melco is looking for a higher-end customers. With this strategy, Galaxy does not have to invest as much in extravagant architecture and other amenities. However, Galaxy cannot afford to save on real estate, so the company is investing heavily in some of the best real estate on Macau. Either way, any new casino must have a good conception, a good location, and imagination because copycat casinos will suffer.

The growing popularity of the Macau gaming industry is aided in many ways. First, the government is improving the infrastructure in the hope, as noted earlier, of doubling visitation from 18.7 million in 2005 to 37 million in 2010. Second, the most profitable game, slots, is surprisingly popular with the Asian gamblers in Macau. Also, they have taken a liking to electronic table games, which are preferred by casinos over live table games because they take up less space and do not require paying dealer salaries. This is a key point because there are currently major labor shortages, including for dealers, in Macau, and this could signify a shift in Macau into Vegas-style gaming. This shortage of a labor supply exists because Macau's population is less than 500,000, but its residents protest the hiring of Chinese and Philippine workers, slowing the growth ability of the gaming industry in Macau. Many new casinos now poach some of the best employees from competing casinos and start wage wars. All of these developments are creating growing concerns about wage inflation among gaming companies. The average Macau gambler is searching for convenience and value. Most of them will not travel beyond the Macau peninsula center of mass, and despite the cheap hotel rates (US$20–40 per night), a decent percentage will stay just off the island for the slightly cheaper rates and then commute to the casinos, making Macau extremely dependent on gaming revenues. Because this market is geared to a low-end gambler, Macau's government does not want any permanent residents, but would like to see some time shares, second homes, and vacation suites.

COTAI—THE RICH MAN'S ALTERNATIVE

Currently, Macau is generating the majority of buzz in the gaming industry, but much of that attention may soon be shifting to its neighbor island, Cotai. Right now, Cotai mainly attracts "Macau rejecters"[5] and some conventioneers, but the island plans on attracting more developers and gamblers from Macau beginning around 2009. These "Macau rejecters" are affluent gamblers who have already become disinterested in Macau and want Cotai to become a high-end resort. The geographical area that Cotai would target has 120 million residents, giving it a large population from which to draw. This target audience will travel great lengths and pay premium prices (approximately US$200 per night) for a quality product. Also, nearby Hangquin Island is waiting for government approval to begin development of residential and leisure resorts. It is hoped that by 2010, Cotai can reach its full potential with many high-quality casinos and improved access to the area.

However, many pitfalls could arise and lessen Cotai's ability to match or surpass Macau's gaming potential. There is currently a lack of critical mass of casino venues on and access to Cotai, which will not be improved until at least 2008. This means that only "must see" casinos will have any chance to succeed. The most difficult of these problems to improve is the projected extra nine million land visitors coming through already saturated border crossings and congested roadways. Once the critical mass and access issues are resolved, the casinos of Cotai have to convince the gamblers of Macau to change their preferred casino, so that they can add them to their current group of "Macau rejecters." The optimistic view points to the surprising change in Asian preferences toward slots as a possible precedent for gamblers switching from Macau to Cotai. A bad sign for Cotai is that the opening of the Grand Waldo Cotai fell short of all expectations and has spooked investors for other potential Cotai casinos. However, optimists in this case focus on the differences between the unsuccessful opening of the Grand Waldo Cotai and the successful opening of the Venetian Macau. A few of the reasons for these differing results are that the Grand Waldo Cotai did not have as strong of a marketing strategy, and it also lags behind the Venetian Macau in size and amenities. Many companies, including Wynn, are taking a wait-and-see approach to get a better feel for the market, its customers, and the progress on Cotai's infrastructure, delaying many openings until 2009 or 2010. The casinos are not the only industry struggling on Cotai. As in Macau, the short supply of land in Cotai has started a land scramble that is sending real estate prices through the roof.

If all of Cotai's needed changes occur in a timely fashion, and the pitfalls are avoided, then Cotai has the ability to become one of the top casino resort locations in Asia. The projections for Cotai predict that it could have double or triple the number of casinos that Macau has sometime between 2012 and 2015.[6] This could make it the dominant casino resort destination in the world.

Another potential revenue driver is the availability of retail on both Macau and Cotai. Many investors are skeptical because of the difficulty that the Fisherman's Wharf is having. However, this area has some of the lowest rents on the island and attracts a low-end shopper. Two planned casinos will court high-end retailers. in order to be attractive to high end customers. The Wynn Macau is planning on opening 10,000 square feet of retail space to satisfy its gamblers. The Venetian Macau is pulling out all of the stops to open up a retail mall that will rival its Grand Canal Shoppes in Las Vegas. However, many retailers do have reservations, so they are signing short-term leases to take a wait-and-see approach toward the viability of retail at the Venetian Macau before signing a long-term lease. Most indicators suggest that both of these endeavors will thrive, and investors should not be concerned with the Fisherman's Wharf struggles.

QUESTIONS

Clearly, Macau has achieved the greatest growth of any recent market for additional gambling. Yet some interesting questions need to be asked about whether this growth can be sustained. The first consideration is, of course, the attitude of Chinese officials. If they fear that they are losing control of these islands, they can easily deny the remaining available land parcels on both Macau and Cotai. This could easily happen given their fear of being too dependent on one industry—namely, casino gambling. And after all, the Chinese government has made no firm commitment to the concept of private property, especially for casino operations.

Another concern of Chinese officials is the possibility of wage inflation because of the labor shortage on the island. Finally, it will be interesting to see how the governing Communist Party will reconcile its previous ban of all types of gambling in China with this establishment of another Las Vegas. If the party's authority is ever threatened on the mainland, would the Communist Party crack down on gambling on Macau in an effort to reestablish its "purity" and authority? So far, the Chinese government has "tolerated" this gambling exception, but whether or not it would sacrifice Macau as its gambling capital in times of need has yet to be tested.

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5. J. P. Morgan, "Macau Update" (newsletter), June 12, 2006.
6. Ibid.

Part IV

CONCLUSION

10

The Role of Government and the Gambling Industry

Recently, a number of states have expressed interest in "privatizing" their lotteries. For example, Democratic Illinois governor Rod Blagojevich would like to lease the state lottery to a private firm for the next 10 years for $10 billion in upfront cash. The proceeds from this windfall would go to Illinois schools so that the schools would receive at least $1 billion per year for those 10 years.[1] Meanwhile, Connecticut would like to adopt a partial privatization of its lottery whereby it would "outsource" many operations to a private firm to reduce its operating costs.[2] Certainly the rationale behind these moves is to raise revenue as well as enable lotteries to compete with other forms of gambling such as casinos, Internet gambling, and sports wagering.

But this privatization question does raise an interesting question: what role should government play in the gambling industry? The libertarian position is that government should play no role in this industry. Gambling is a form of entertainment like movies, plays, or any sort of sports. Does the governor operate movie theaters or sports teams? This approach says to let the market rule the industry, and it will provide the betting public the best possible odds and returns.

The opposite position would be that government should be the sole provider of gambling in order to protect the common good. Government has the duty to protect the consumer, and because gambling has the potential to be an addictive activity, the only way to ensure that the consumer is protected is to have the government own and operate any gambling activity. This is the Canadian attitude toward gambling; Canadian provinces operate both lotteries and casinos.

Certainly, these are two diametrically opposed opinions about the role of government in the gambling industry. For the libertarian, government has no role, and for the socialist, government's role is total control and ownership. The reader can decide on the merits of each of these positions.

However, in the United States and most countries throughout the world, there is a middle position between these two extreme positions. Although most public officials would not want a gambling industry that maximizes profits, they are also aware of the potential conflict in regulating an industry that is owned by the regulator. What follows in this final chapter is an attempt to give the reader a framework for an approach that would allow a society to achieve a balance between the efficiency needed to raise revenue and a concern for the common good, which is demanded by critics of the gambling industry.

A FRAMEWORK FOR EVALUATING THE ROLE OF GOVERNMENT IN THE GAMBLING INDUSTRY

As shown throughout this book, a government's (or state's) decision to either permit or expand gambling is usually based on whether it is an efficient way of raising revenue. In other words, would the additional revenue come at the expense of other sources of revenue? Would the introduction of a lottery hurt existing restaurants, movie theatres, and so on? Would the establishment of casino gambling merely siphon off an existing lottery?

But with any issue involving gambling, any preoccupation with economic efficiency fails to measure the political consequences that any expansion of gambling might have. To deal with this deficiency, one analyst, Ellen Pint, has proposed a "rational-choice" framework that is based on the view that interest group members and politicians act as rational-makers.[3] Although gambling is not an industry where efficiency is always the primary rationale utilized by groups or stakeholders, this approach certainly has merit. However, developing a formula to quantify the economic and political benefits and costs would be a daunting task.

One way of dealing with this problem would be to make a distinction between short-run revenues and costs and long-run revenues and costs. Hence, the short-run measurements of economic and political consequences that policy makers need to consider as they contemplate any form of gambling would be have to be continued as they decide whether it has been in the government's long-term interest to permit gambling in any of its forms.

The purpose of the framework (shown in Table 10.1) is to provide the reader with a four-step process to evaluate any proposed form of gambling. The rest of this chapter is used to explain the model and to illustrate

Table 10.1
A Framework for Evaluating the Privatization Process

	Short-Run Results	*Long-Run Results*
Economic	1 Business efficiency increase	3 Corporate options increase
Political	2 Gains by various stakeholder groups	4 Stakeholder options increase

this framework by example of one of the cases previously discussed in the book.

Cell 1 of the framework is concerned with efficiency or the increase in revenue that would result from any gambling initiative. Any addition in gambling would have to be able to either increase revenue or capture revenue from another state or jurisdiction. Has this new form of gambling allowed the state to capture "market share" or additional gambling revenue from previously illegal gambling? Has the overall gambling market expanded?

There is also need for what can be termed "political" efficiency. This short-run political need is the concern of cell 2. Although many political processes are thought to be zero-sum games (if one stakeholder "wins," the other has to lose by an equal amount), any increase in gambling must benefit the majority of stakeholders. Besides the government receiving additional revenue, taxpayers ought to receive better-quality services, property tax relief, or additional health care benefits. Other stakeholders such as local governments receive reimbursement (e.g., better access roads, funds for police) for additional services, and unions must be satisfied that workers are paid well and have job security.

Cell 3 represents the long-run economic interest of an increase in gambling. This cell demands that the state or government develop an overall gambling strategy that will provide other gambling options. The diversification of gambling opportunities has as its chief concern that the state or government not become too dependent on one source of revenue (the reader might recall the Macau case). Besides increasing revenue, any additional forms of gambling should also result in a multiplier effect for the entire economy where additional shops and restaurants are opened near venues for gambling. The reader should recall the St. Louis case.

The evaluation in cell 4 involves giving the various stakeholders "freedom" to make changes or adaptations to their gambling strategies. Government and the gambling firms need to retain some measure of power and influence over the future of any gambling operations. Government must decide the amount of power it will exercise over a gambling operation in order to satisfy all of the constituencies to which it is responsible. Again, the reader should recall that the Chinese government's reluctance to give casinos full rein in Macau could force casino firms to scale back future plans, and thus the full potential of the Macau might not be realized.

This framework for evaluating gambling proposals requires that policy officials ask a series of questions about the economic and political effects that any gambling proposal will have both in the short run and in the long run. In the short run, the new gambling enterprise not only must be able to provide additional revenues for the government, but it also must convince the vast majority of stakeholders, that this revenue will be utilized for the common good. The long-run criterion for a new gambling venture is that it provides options for all of the stakeholders. The government needs to ascertain that other economic bases for a community have broadened as a result of additional gambling and that the other stakeholders have gained a measure of freedom from government interference. This framework points out that stakeholders need to pay attention to both the economic and the political tradeoffs if additional gambling is to be successful. We utilize the framework in this next section to reexamine the situation faced by Massachusetts governor Deval Patrick.

EVALUATING ADDITIONAL GAMBLING FOR MASSACHUSETTS

Cell 1

This is the cell that places an emphasis on economic efficiency or the ability of a new gambling proposal to raise revenue. As mentioned earlier in the book, Massachusetts has the following five options: (1) do nothing; (2) establish a private casino; (3) negotiate with a Native American tribe to build a casino; (4) permit the existing racetracks to operate slot machines; or (5) allow the lottery commission to rent space off the tracks in order to establish Video Lottery Terminals (VLTs).

Clearly, option 1 would produce the least revenue for Massachusetts, and essentially, Governor Patrick would have to deal with the slow decline in lottery revenue. The ability of the next three options to raise revenue depends on the rate of taxation that the state would impose on the profits of these ventures. Clearly, a private casino could be a revenue bonanza depending on where the casino was located. The Native American option has the same drawback as a private casino, especially in regard to its location, which would not be near a large population center. Meanwhile, placing slot machines at the existing tracks would certainly increase revenue but would also permit the Native American tribes to operate slot machine without any permission from the state. Option 5 is the one option that guarantees the state a certain amount of revenue, although it would not maximize potential gambling revenue. It also keeps gambling completely in the control of the state.

Cell 2

For cell 2, we examine which of the five options is the most politically attractive to the various stakeholders involved in any expansion of gambling. Although the revenue question is a bit clouded, one option clearly has the greatest political payoff. Option 1 does have a cost with no additional revenue. The status quo does not address either the revenue needs of the state or the issue of keeping the tracks open. It also does not satisfy critics who maintain that the state is already losing revenue to neighboring states while those states are exporting any addiction problems back to Massachusetts.

Option 2 would open up all kinds of regulatory problems for the governor. First, a commission would need to be established to determine how a firm would qualify for a casino license and how many licenses or sites would be selected to have casino gambling. There would be opposition from city mayors fearing that these casinos would "cannibalize" lottery sales so that cities and town would receive less revenue from the lottery. Although this option would satisfy the "libertarian" sentiment in the state, it would generate a great deal of opposition from those who think that gambling ought to be highly regulated.

Option 3 would face a bit less opposition than option 2 because many residents think that permitting Native American gambling is justified in order to compensate Native Americans for the harsh treatment they have received in the past. But it would still be opposed by the mayors of cites and towns as well as unions, who would not be permitted to unionize the employees of Native American casinos.

Option 4 would certainly generate more support than the previous options, yet it also would have substantial opposition. Again, mayors of cities and towns would oppose this option unless they were assured that funds would be put aside to compensate for any decrease in the lottery. But another factor is that this option would permit Native American tribes to have slot machines on their reservations. If this occurred, the state would be in no position to force these tribes to negotiate sharing a certain percentage of the slot machine revenue, as has occurred in Connecticut. Hence this option is also politically unviable.

Option 5 appears to be the only option that can satisfy all of the major stakeholders for additional gambling. First, the state would operate the VLTs, thereby ensuring revenue flow to the state. Second, the mayors of town and cities would be assured not only traditional lottery revenue but also a large percentage of the additional revenue that the VLTs would raise for the Massachusetts State Lottery Commission. Unions would be satisfied because any additional jobs would be unionized, and of course the tracks would be kept alive as would the jobs that these tracks currently provide. Even the anti-gambling forces could be some be somewhat mollified with an offer of 1 percent of the revenue for compulsive gambling treatments.

Hence, at least in the short run, option 5 is the only option that both satisfies the majority of stakeholders and has the potential to raise a substantial amount of revenue. Now we need to establish whether option 5 would have long-term viability.

Cell 3

Would VLTs be a long-term source of revenue for Massachusetts? Are VLTs a "base" to diversify a gambling policy? The answer to that question is certainly yes if one uses the Rhode Island example. We saw in chapter 8 that growth of revenue from VLTs has continued unabated since the installation of VLTs in Rhode Island.

Other states such as Delaware and West Virginia have shown that VLTs do provide a "base" for additional gambling. Both states, in response to neighboring states legalizing additional gambling, have introduced "table" games such as black jack, craps, and roulette in order to attract additional gambling revenue. These tables are operated and regulated by their respective lottery commissions. In the case of Pennsylvania, even before the first slots were in operation, there was already a call to permit various table games in the state's facilities for slots. Clearly, critics of expanded gambling who view slots/VLTs as the start of the slippery slope to full-scale casino gambling may be justified in their concern.

Cell 4

Are VLTs politically viable in the long run? Again, the answer to this question appears to be yes. Rhode Island voters turned down a proposal for Native American casino gambling because it was argued that the state's revenue from the VLTs would be cannibalized if Native American gaming was permitted.[4] Because VLTs are owned and operated by a state's lottery commission, the issue of losing power to operators is of course a nonissue. The one criticism that can be made is how dependent a state becomes on this gambling revenue. Although a state should be concerned about the addictive effects that additional gambling can have on a region, one must wonder whether a state itself becomes addicted to gambling revenue.

CONCLUSION

In Chapter 2 it was argued that gambling as a form of entertainment must be tolerated, and introducing additional gambling activities appears to increase this tolerance level. Gambling may be a prime example of what ethicists term the "slippery slope" argument—that is, if one permits even the smallest opening, then the floodgates are eventually opened. In many ways, permitting full-scale gambling is the logical conclusion to the ethical dilemma that gambling poses. Once one form of additional gambling, such as VLTs or slot machines (one of the "small" openings), is legalized to support a good cause, it does seem only a matter of time until sports gambling and Internet gambling are legalized in order to protect that revenue stream that supports a good cause.

Indeed, gambling has become an integral part not only of American society but also of most other societies throughout the world, even Communist China. Gambling appears to be here to stay, and the chief question is how much control government will keep over this industry. Whether the spread of gambling will continue at its present pace depends on the public's acceptance of an ethic that places a premium on the freedom of the self over the common good.

Although the rise of gambling has and will have many implications for American society and many other countries throughout the world, perhaps these societies' greatest gambling-related challenge will be developing a system of regulatory control over an industry that can use the free market as a model but in which the government cannot be the beneficiary of its regulatory activity. It is this evolution that will pique the research interests of both economists and political scientists.

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Index

Abramoff, Jack, 66, 77
Addiction, 40, 126, 151
Addictive gambling behavior, 50, 54
AGA. *See* American Gaming Association
Alanis, Paul, 110
Amateur Sports Integrity Act, 59
American Gaming Association (AGA), 47, 51–53, 59–61
American Indian. *See* Native American
American Indians on Reservations: A Databook of Socioeconomic Change between the 1990 and 2000 Censuses, 73
America's Center, 108
Ameristar, 95, 97
Analysis of the Economic Impact of Indian Gaming, 73
Antigua, 6, 45
Argentina, 109
Arizona, 126
Assembly Bill 466, 41
Atlantic City: and sports gambling, 10; taxes in, 132; threats to, 11, 25, 42, 86–87, 89
Australians, 8
Australia's Publishing and Broadcasting, 141

Baltimore, Lord. *See* Cecil Calvert
Baptists, 91
Barbuda, 45
Baseball, 27
Bellah, Robert, 27
Bennett, John, 42
BetOnSports, 44, 45
Betting & Gaming Group, The, 58
Biloxi, 87
Biondi, Lawrence, S.J., 96
Blagojevich, Rod, 147
Bradley, Bill, 60
Bridgeport, 121
Browning, James, 10
Buffalo, 88
Bureau of Economic Analysis, 67

Cabazon Band of Mission Indians. *See* *California v. Cabazon*
Cabazon project, the, 73
California, 66–67, 69–70
California v. Cabazon, 66, 69–70
Calvert, Cecil, 28
Camelot Group, 57
Canadian attitude toward gambling, 147
Cannibalization of revenue: in Connecticut; 123; by expansion of gambling nationwide, 83; by internet gambling, 43; from lotteries by casinos, 91–92; in Massachusetts 120, 151–52; in Rhode Island, 117

Carruthers, David, 44–45
Casino Queen, 97–98, 100
Casinos: in Atlantic City, New Jersey, 11, 25, 84, 86–87; in Cotai, 142–43; and ethics, 30; and the Internet, 5, 6, 35, 37, 39–44; in Las Vegas, Nevada, 3, 10, 23, 50–52, 55, 57, 61, 86; and lottery competition, 90–92; in Macau, 139–41; in Missouri, 95–112; Native American, 4, 9, 25, 31, 65–78, 86, 88–89; in New England, 113–17, 119–26, 150–153; revenue from, 7, 8, 24, 55, 57, 66, 84–85, 114; and riverboat gambling, 25, 87; and sports gambling, 50–52, 57, 60–61; taxes on, 127, 128, 130, 131, 133, 136
Catskill, 86, 88
CBS Corporation, 51
Chicago, 87
China, 139–43, 153
Cigarette, 19–21, 23, 26, 29–30
Cigarette Warning Label Act of 1966, 20
City of Dreams, 141
Cohen, Neil, 42
Colorado, 107, 127
Combating Illegal Gaming Reform and Modernization Act, 38
Commerce Clause, 38
Commission on Review of the National Policy toward Gambling, 56–57
Common Cause Maryland, 10
Common good, 26–27, 29, 147–48, 150
Communist Party, 143
Compulsive Gamblers, 40, 42, 152
Congress (U.S.): and cigarettes, 20, 23; and internet gambling, 36, 41–42; and Native Americans, 9, 25, 66, 69–70; and sports gambling, 53, 58, 59–60
Connecticut: and casino revenue, 67, 72, 114, 123; history of gambling in, 9, 85, 120–21; and lotteries, 121–22; and privatization, 147
Constitution, U.S., 29, 38
Cotai, 142–43
Creek Indians, 9
Crime, 49, 70, 74, 96–97, 140
Criminals, 37
Crown Macau, 141
Cyberlocator.com, 40

Danforth, Jack, 96
Dave and Buster's, 108
Delaware, 49, 59, 85, 86, 127
Department of Justice (DOJ), U.S., 5–6, 39, 45
Detroit, 87, 130
District of Columbia, 118
DOJ. *See* Department of Justice
DuCharme, Steve, 49

Eastern Pequots, 9
Economic development, 25, 70–71, 73, 84, 91
Education: funding of, 23, 30; of Native Americans, 74, 76; about sports wagering, 49, 51, 55, 61
EGD. *See* Electronic Gambling Device
Elderly, aid to the, 30
Electronic gambling device (EGD), 124
Embassy Suites, 107
ESPN, 83
Ethics, 26, 204; establishing legitimacy, 29–31; of sacrifice, 26–28; of tolerance, 28–29
European Court of Justice, 6
European Union, 6

FBI. *See* Federal Bureau of Investigation
Federal Bureau of Investigation (FBI), 47, 49
Federal Emergency Management Agency (FEMA), 67
Feldman, Alan, 35
FEMA. *See* Federal Emergency Management Agency
Female gambling, 51
Fink, Stephen, 92
Fisherman's Wharf, 143
Florida, 89
Foxwoods Resort Casino: and college tuition, 77; and competition, 86, 117; and the state of Connecticut, 72, 114, 120, 125
Furlong, Edward J., 91

Galaxy Entertainment Group, 141
Gambling Act (2005), 6
Gambling and Survival in Native North America, 74

Gaming Control Board, Nevada, 41, 49
General Agreement on Trade in Services (GATS), 6
Giamatti, A. Bartlett, 27
Glick, Jerry, 108
Good Society, The. *See* Robert Bellah
Graham, Lindsey, 59
Grand Waldo Cotai, 142
Greyhound racing, 120, 121, 129
Guinn, Kenneth, 41
Gun control, 26, 29

Habits of the Heart: Individualism and Commitment in American Life, 27
Hanaway, Catherine, 45
Hangquin Island, 142
Harrah's Entertainment Inc.: and government, 72; and internet gambling, 5–6, 42, 44; in the Midwest, 95, 97–98, 106–7, 110–11; and Native Americans, 9; studies by, 83
Hartford, 121
Harvard Project for American Indian Economic Development, 73
Haugen, David, 74
Hinrichs, Judy, 106
Ho, Lawrence, 141
Holden, Bob, 97
Horseracing: and casinos, 88; and internet gambling, 8, 36, 45; and slot machines, 86; and sports gambling, 47
Hotels: in Atlantic City, 60; in Las Vegas, 3, 10; in Macau, 140–41; in the Midwest, 107–108, 110, 115; Native American, 66
Hou Heng Company, 139
House Judiciary Committee, 53
Hubbard, R. D., 109

IGRA. *See* Indian Gaming Regulatory Act
Illinois, 11, 25, 87, 96–99, 127–28, 147
Impact Analysis for Planning (IMPLAN), 67
IMPLAN. *See* Impact Analysis for Planning
"Importance of Self-Selection in Casino Cannibalization of State Lotteries, The," 92
Impreveduto, Anthony, 42
Indian. *See* Native American
Indiana: and Pinnacle Entertainment, 109; and riverboat gambling, 10, 25, 96, 98; and tax revenue, 85, 87, 128
Indiana Gaming Commission, 109
Indian Gambling Regulatory Act (IGRA): effects of, 8, 25, 65, 88; explanation of, 66–71
Indian Gaming and Tribal Sovereignty, 74
Instant tickets, 116, 119, 121
Internet gambling: and casinos, 42–44; growth of, 3; and legislation, 4, 37–42, 147; overview of, 4–8, 35–36; pros and cons of, 36–37; recent developments of, 44–45; and sports gambling, 47, 50, 52–53, 55–56, 59, 61
Interstate Horse Racing Act, 45
Iowa, 25, 87, 96, 108–9, 129
Isle of Capri Casinos, Inc., 107–9, 111
Isle of Man, 43

Jackson, John D., 91
Jai Alai, 115, 117, 120, 121, 136
Jobs: in Massachusetts, 126, 152; in Missouri, 96, 107, 109, 110; for Native Americans, 25, 67, 74; from sports gambling, 56, 61
Judiciary Committee, 38

Kennedy, John F., 27
Keno, 115–17
Kentucky, 10, 87
Kind, Ron, 60
Koop, C. Everett, 20

Laclede, Pierre, 95
Laclede's Landing, 97, 107, 110–11
Ladbrokes, 58
Lake Charles, 110
Las Vegas: history of, 23–25, 86; and internet gambling, 4, 10, 35; and revenue, 3, 7, 76
Las Vegas Sands, 141
Legalized Gambling, 74
Light, Steven, 68, 74
Lincoln Downs, 115, 117
Los Angeles, 109

Lotteries: in competition with casinos, 90–92, 201–2; in the District of Columbia, 153; growth of, 3; in New England, 23, 112, 115–26; and privatization, 147; and video lottery terminals, 85–86
Louisiana: and Isle of Capri Casinos, Inc., 107; and Pinnacle Entertainment, 109–10; and riverboat gambling, 25; and tax revenue, 85, 129

Macau, 139–44
Maine, 113
Major League Baseball (MLB), 27, 49, 54
Male gambling, 50–51, 54
March Madness, 53
Maryland, 10, 28, 86
Mashantucket Pequot Tribe, 72, 75, 77
Massachusetts: and the expansion of gambling, 85, 114, 117–20, 124–26, 150–52; history of, 28; and the state budget, 113
Massachusetts State Lottery Commission, 152
McCain, John, 9, 59–60, 72, 76
Meister, Alan, 66–68, 76
Melco International Development, 141
MGC. *See* Missouri Gaming Commission
MGM Mirage, 6, 35, 42–44, 141
Michigan, 85, 86, 130
Minnesota, 67
Mirage Resorts, 109
Mississippi: history of gambling in, 25, 84, 87; and Isle of Capri Casinos, Inc., 107; and Pinnacle Entertainment, 109; and tax revenue, 85, 130
Mississippi River, 84, 87, 95, 97, 110
Missouri: and Harrah's Entertainment Inc., 107; history of gambling in, 25, 87; and legislation, 97–98, 102; and Pinnacle Entertainment, 109–111, 141; and taxes, 131
Missouri Gaming Commission (MGC), 99–104, 106, 111–12
MLB. *See* Major League Baseball
Mohegan Sun, 72, 86, 88, 114, 120, 125
Monopolies: in Macau, 139; Native American, 127, 130; state-held, 4, 11, 86
Montana, 49, 59, 131
National Basketball Association (NBA), 11, 49, 54, 60
National Collegiate Athletic Association (NCAA), 11, 48–56, 59–60, 61
National Football League (NFL), 11, 49, 54–55
National Gambling Impact Study Commission (NGISC), 53–54, 115
National Hockey League (NHL), 49
National Indian Gaming Association (NIGA), 73–74
National Indian Gaming Commission (NIGC), 71–72
Native American casinos: in California, 4; debate on, 65–77; growth rates of, 2; and the Indian Gaming Regulatory Act, 95–99; in New England, 88, 114, 121, 125–26, 151–52; in New York, 86; overview of, 9, 25; and slot machines, 89; taxes on, 115, 126, 127, 130, 133
NBA. *See* National Basketball Association
NCAA. *See* National Collegiate Athletic Association
Nevada: and internet gambling, 7, 35, 40–41; history of gambling in, 23, 114; and sports gambling, 47, 49–61; and tax revenue, 85, 86, 131–32
New England, 147–48
New Hampshire, 23, 85, 113
New Jersey: economic development in, 86; and the expansion of gambling in the Northeast, 86–87; and internet gambling, 7, 35, 40, 41–42; and sports gambling, 10, 60; and taxes on gambling, 132
Newport Jai Alai, 115, 117
Newspaper Association of America, 53
New York, 85, 86, 88, 133
New York Times, 35
NFL. *See* National Football League
NGISC. *See* National Gambling Impact Study Commission
NHL. *See* National Hockey League
NIGA. *See* National Indian Gaming Association
NIGC. *See* National Indian Gaming Commission

Ohio, 10
Oregon: and sports gambling, 49, 54, 56; and tax revenue, 85, 134
Osborne, Tom, 60
Owen Development, 108

Pari-mutuel, 23, 88, 120, 121, 125
PartyGambling, 5
PartyPoker, 5
Pasquaretta, Paul, 74
Pataki, George, 86, 88
Patrick, Deval, 114, 126, 150
PayPal, 6
Pennsylvania: history of, 28; and slot machines, 10, 72, 86, 89; and taxes, 134
Pequots. *See* Eastern Pequots; Mashantucket Pequot Tribe
Philadelphia, 86
Pinnacle Entertainment, 109–11
Pint, Ellen, 148
Pittsburgh, 86
Plainfield, 121
PLAYMGMMIRAGE.com, 43
President Casino, Inc.: and competition, 106, 111; history of, 95, 96, 97; and Isle of Capri Casinos, Inc., 108; and market analysis, 100
Privatization, 10, 147
Professional and Amateur Sports Protection Act, 37, 53, 54, 58, 59–61
Public Law 280, 69
Public policy: 11, 19–21, 23, 26–27, 29–31
Puritans, 28, 52

Quakers, 28

Racinos, 91, 115, 116, 124
Rand, Kathryn, 68
Regulation: of the cigarette industry, 20–21; of internet gambling, 5, 6, 35, 37, 39, 41–42; of Native American casinos, 69–71; purpose of, 4, 11; of riverboat gambling, 97; of sports gambling, 48, 58, 61; and tax revenue, 84; by the World Trade Organization, 6
Reid, Harry, 60
"Relationships among US Gambling Industries, The," 91
Request for Proposals (RFP), 102
Revenue sharing, 67, 106
RFP. *See* Request for Proposals
Rhode Island: and Native American casinos, 9, 88, 113–14, 124; and tax revenue, 72, 85, 115–17, 136
Rhythm City, 108
Riverboat gambling: in Indiana, 10; history of, 25, 84, 85, 87; and Isle of Capri Casinos, Inc., 107; regulation of, 97; taxes on, 126, 127–31
Roberts, Steve and Mike. *See* Roberts Brother's Properties
Roberts Brother's Properties, 108
Roemer, Tim, 59
Rork, Jonathan, 92
Rose, Pete, 27–28, 54

St. Charles, 95, 97
St. Louis, 95–112
St. Louis County Economic Council, 104
St. Louis County Gaming Selection Committee, 110
St. Louis Development Corporation (SLDC), 103, 111
St. Louis University (SLU), 96, 106
Sands, The, 139
Saur, Bob, 108
Schaghticoke, 9
Senate Committee on Indian Affairs, U.S., 9, 99
Senate Resolution No. 48, 41
Sheridan, Danny, 53
Slay, Francis, 96, 106
Slot machines: in Asia, 141, 142; legalization of, 10–11, 71–72, 86–89, 114, 150–53; number of, 95, 98, 107, 108, 110; taxes on, 127, 128, 130, 131–32, 133, 136
Smoking. *See* Cigarette
Sociedade de Turismo e Diversoes de Macau, 139
South County, 96, 102, 104, 106–7, 109
South Dakota, 85, 136

Spitzer, Eliot, 86, 88
Sports Action, 56
Sports gambling, 10–11, 47–61
STDM. *See Sociedade de Turismo e Diversoes de Macau*
Student Athlete Protection Act, 59
Student-athletes, 48–51, 54–56, 61
Super Bowl, 53
Surgeon General, 20

Tai Heng Company, 139
Taxes: and Atlantic City, 84; excise, 23, 86; and internet gambling, 8, 35, 37; and Maryland, 10; and the Midwest, 95, 98, 106, 109; and Native American casinos, 25, 67–68, 71–72, 88; and New England, 23, 86, 113–15, 124–25, 149–50; and riverboat gambling, 10, 87; and sports gambling, 47, 51–52, 54–58, 60–61; and state budgets, 84–85; summary of taxes on riverboats, casinos, and video lottery, 126–36
Taylor, Jonathan, 73
Teenagers, 50
Ting, Fok Chi, 139
Tobacco, 19, 29
Tocqueville, Alexis de, 27
Trampe, Steve, 108
Treaty of Rome (1957), 6
Tribe. *See* Native American
Tunica, 87
TV and Radio Cigarette Advertising Ban of 1971, 20

U.K. *See* United Kingdom
United Kingdom (U.K.): and internet gambling, 4, 8, 43, 45; and legislation, 6; and sports wagering, 4, 57–58
Urban areas, 87, 95, 96
Utah, 45

Venetian Macau, 140, 142–43
Vermont, 113
Video lottery terminal (VLT): and the expansion of gambling, 88–89, 114, 126, 150–53; in Rhode Island, 115–17, 122, 124–25; taxes on, 85, 124, 133, 136
VLT. *See* Video lottery terminal

Walker, Douglas M., 91
Wall Street Journal, 36
Wampanoag, 126
Washington, 67
Westfall, George R. "Buzz", 104, 106
West Virginia, 10, 85, 86, 136
William Hill, 58
Williams, Roger, 28
Wire Act (1961), 5, 37–39, 44–45, 54
Wisconsin, 67
World Series of Poker, 83
World Trade Organization (WTO), 6, 31, 45
WTO. *See* World Trade Organization
Wynn, Steve, 109, 139
Wynn Las Vegas, 10
Wynn Macau, 143
Wynn Resorts, 141, 142

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