National Competition Policy Review of Gaming Machine Legislation

Government Response

Purpose

This paper sets out the Government's response to the recommendations and findings of the National Competition Policy Review of Gaming Machine Legislation (the review).

The review took account of the opinions of various stakeholders as expressed in submissions by the wider community, gaming industry, community groups and local councils. The review also took into account relevant submissions received in as part of the public consultation undertaken with the *Responsible Gaming: A Consultation Paper* launched March 2000.

In developing its response, the Government considered in detail the review and the submissions received. The Government also informed itself by way of the submissions to the consultation paper.

Background

Under the intergovernmental competition principles agreement signed by the Council of Australian Governments in April 1995, Victoria agreed to remove unnecessary statutory restrictions on competition. As part of the agreement, all Governments agreed to adopt the following guiding principle:

Legislation should not restrict competition unless it can be demonstrated that:

1. *the benefits of the restriction to the community as a whole outweigh the costs; and*
2. *the objectives of the legislation can only be achieved by restricting competition.*

The guiding principle established under National Competition Policy places the onus of proof on governments to demonstrate a public interest case for the enactment or retention of statutory restrictions.

Governments agreed to review and reform all current and new legislation against the principle.

The Minister for Gaming commissioned the review in July 2000 in accordance with the Victorian Government's *Timetable for the Review and Reform of Legislation that Restricts Competition*, under the Government requirements to meet its NCP obligations.

Dr John Marsden of Marsden Jacob Associates conducted the independent review on behalf of the Government.

The terms of reference required the review to examine the case for reform of legislative restrictions on competition contained in the *Gaming Machine Control Act 1991* (GMCA) and part 2 of the *Gaming and Betting Act 1994* (GBA) as it relates to a gaming

operator's licence and relevant regulations. The review was directed to address specifically the appropriateness of the current arrangements of:

- licensing two gaming operators. The review should recognise that the Government will continue to uphold all its contractual agreements;
- gaming venue market structure. This includes the 50:50 split of gaming machines between hotels and clubs. It should also include consideration of the concentration of gaming venue ownership and the emergence of quasi-clubs;
- the allocation of at least 20 per cent of gaming machines outside the Casino to non-metropolitan Victoria;
- the numbers of gaming machines per venue; and
- betting limits on gaming machines.

Report recommendations and Government Response - Summary

Review Recommendation	**Proposed Government Response**
1. *The excessive generosity of the current licences and resulting monopoly rents should end as soon as practicable.* *The two-operator system should not be continued beyond the expiry of the current contracts and that a competitive model be based on Queensland. However, whichever model is chosen we strongly recommend that there be no profit sharing* *We recommend that the Victorian Government use the discretion provided by clause 8 of the Gaming Operator's Licence to:* *i) remove the monopoly profits above the level of payments necessary to ensure competitive or regulated provision of monitoring, servicing and machine rental;* *ii) provide the operators with a flat cost-based fee for these services to venues.* *Unlike the 1996 review, any future review should be public and transparent.* .(page 1)	The Government notes that the recommendation does not directly deal with a competitive restriction and does not require Government action for the purpose of NCP compliance. However the Government notes the findings of the review with regard to the accrual and distribution of economic rents resulting from the industry arrangements. The Government agrees that a comprehensive review should be conducted closer to the expiry of the current licences to examine the appropriate industry structure beyond 2012. Without pre-empting the review, the Government is supportive of greater competition in the industry. Any comprehensive review of the post-2012 industry structure should consider a number of the issues raised by the review, including the appropriateness of the continuation of the profit sharing arrangements, ownership structure and number of gaming operator licences. However, the review erred in presenting the option of a further 'clause 8 review' of profit sharing and taxation arrangements. Following that review, conducted in 1996, the previous Government removed that provision from the legislation and the licences. Changes to the profit sharing and taxation arrangements before 2012 would require a

Review Recommendation	Proposed Government Response
	fundamental alteration of the operating environment established for the terms of the licences. The Government has given an undertaking to honour the principles and commitments given at the time the licences were issued. In immediate response to this recommendation, and the review of State business taxes, the Government announced an additional $1200 levy per machine to provide funding for the public hospital system. This is in addition to the $333 levy per machine introduced in the 1999-00 Budget. The Government notes that in introducing the recent raft of responsible gambling initiatives it has imposed additional costs upon the operators. The Government will consult with the gaming operators and other stakeholders to determine the timetable for a review of the arrangements to apply beyond 2012.
2. *The Government and the racing industry should take the early opportunity to renegotiate the current open-ended Agreement Act to ensure on-going support independent of the existing duopoly and financing arrangements, so that agreed new arrangements can be in place when the existing contracts/licences expire in 2012.* (page 5)	The Government accepts in principle the recommendation, noting that the review identifies support of the racing industry as an objective of the legislation. The Government is committed to retaining this as an objective of the legislation.
3. *The legislation should be amended to remove the requirement that monitoring and control be a requirement of the operator's licence. There would consequently be no need to require the system to be on-line, real-time.* (page 6)	The Government accepts in principle the review findings and recommendation. While the intention is to retain the requirement that monitoring and control be a requirement of the operator's licence for the life of the current arrangements, the Government will consult with the VCGA and the industry on the most appropriate way forward for monitoring arrangements. A key consideration in examining this issue will be to ensure the absolute integrity of the on-line monitoring regime.
4. *The restriction allocating at least 20 per cent of gaming machines to non-metropolitan Victoria should be removed.*	The Government notes the recommendation and will monitor the impact of the recent, more sophisticated, reforms on the distribution of machines across the State. Until the impacts of recent policy initiatives

Review Recommendation	Proposed Government Response
(page 7)	introducing regional caps and social and economic benefit tests are known the Government will retain the current restriction.
5. *The Club-Hotel 50:50 Split restriction should be retained.* (page 8)	The Government accepts the recommendation to retain the Direction regulating a 50:50 split of gaming machine numbers between hotel and club venues.
6. This package of measures should be adopted: *(a) separate liquor and gaming licences and break the presumption that award of a liquor licence automatically qualifies the venue for a gaming licence. The legislative change has already been made, but the change needs to be signalled;* *(b) provide legislative clarity and guidance to the VCGA by explicitly listing the items to be considered in any case by case assessment of the 'reasonableness' or otherwise of commercial arrangements;* *(c) prohibit in totality profit-sharing arrangements or prohibit, subject to specifically authorised exceptions, profit-sharing arrangements;* *(d) require and resource the VCGA to undertake ex-post analysis of the sources and uses of funds from gaming and other activities in those clubs contracting external management contract services and leasing premises from related third parties;* *(e) provide and enforce penalties on companies, their directors and the club directors found to be involved in non-genuine club gaming activities. For instance, banning these persons and entities from further involvement in gaming; and* *(f) tighten direct responsibilities for clubs engaging in substantial gaming activity. For instance, amend the gaming machine*	The Government notes the suite of recommendations outlined for the club sector, while noting that this issue is not, strictly speaking, one directly concerning a competitive restriction. The Government is moving to implement initiatives to ensure accountability of club venues. In addition the Government will continue to examine these recommended options as well as other measures. The Government has already put in place measures that introduce Recommendation (a). The Government accepts in-principle recommendations (b) & (d) to provide broader scope for the assessment of club venues and the appropriateness of applying the Community Support Fund levy and to provide a mechanism for venues to demonstrate the wider community benefits of their gaming activities. The Government is considering a number of options, with the objective of ensuring that venues provide meaningful information with a minimal compliance burden on genuine club venues. The Government accepts in-principle recommendation (c). However it should be recognised that some clubs have benefited from such management arrangements. The Government will examine the issue in more detail to determine the appropriate changes to the existing regime. The Government does not accept recommendations (e) & (f) believing that the principal focus of gaming legislation should be to ensure the honesty and integrity of the gaming industry and its participants, rather than duplicate Corporations Law and other legislative governance of general commercial activities.

Review Recommendation	Proposed Government Response
control act to require directors of such clubs to be bound by the same responsibilities of directors of companies under Corporations Law. (page 9)	
7. *The restriction placing limits on machine numbers per venue should be retained pro tempore.* (page 13)	The Government accepts the recommendation.
8. *The restriction on* 24-hour Gaming *should be retained.* (page 14)	The Government accepts the recommendation.
9. *Only venues with one of: a general licence under the Liquor Control Reform Act 1998, a club licence under s.10 of the same Act or a licence under Part I of the Racing Act 1958 (or a licence issued under these sections but with conditions under s.80 of the Liquor Control Act 1987) can be approved premises (s.12A).* (page 15)	The Government accepts the recommendation.
10. The general ability to set bet limits under Ministerial Direction should be retained. We also recommend that the use of more aggressive bet limits should follow appropriate research and testing. (page 16)	The Government accepts the recommendation to retain the ability to set bet limits. The Government would wish to see research conducted into the effectiveness of bet limits to promote responsible gambling behaviour.
11. Where an applicant (or an associate) has an existing venue within 100m of a proposed venue, these venues must be independent of each other. (page 17)	The Government accepts the recommendation.
12. *The existing probity restrictions should be retained and continue to be subject to on-going independent review.* (page 17)	The Government accepts in principle the findings of the review. The Government is satisfied that the barriers to entry presented by the stringent probity arrangements are in the public interest to ensure integrity and honesty in the gaming industry.
13. More explicit guidance should be given to the VCGA on its role and responsibilities. (page 18)	The Government notes the review's comments on the secrecy provisions to which the industry is subject. While the recommendation does not strictly deal with matters of competitive restrictions, the Government supports in principle the notion of continual review of these provisions. Recent amendments to this section of the Act provide for more accountability and openness of the VCGA including the conduct of open hearings. To the extent that more public information assists competitive

Review Recommendation	Proposed Government Response
	outcomes then the Government has already acted to remove competitive restrictions.

Government Response

The review applies economic and broader policy analysis to the structure of the gaming machine industry consistent with the guiding principle for legislative reviews under national competition policy.

The review found that gaming machine legislation restricts competition in three areas:

- the principal restriction is the establishment of a two-operator industry, with a suite of interlocking restrictions underpinning the dual operator system. The review:
  - concluded that the restrictions associated with the two-operator system should not be retained; but
  - notes that Government is committed under contractual obligations to maintain the two-operator system until 2012;
- the distribution of machines; and
- certain probity and regulatory requirements the review considers competitive restrictions.

The Government recognises that electronic gaming is a legitimate recreational activity available to adult Victorians, but one accompanied by serious negative social consequences that excessive or problem gambling brings to some individuals, their families and communities.

Since assuming office, the Government has instituted a range of measures to promote responsible gaming and ensuring the industry and regulatory structures better reflect community expectations. Amendments to the GMCA include a number of measures suggested in the review. As part of those changes, the Government inserted as a purpose of the GMCA the objective of fostering responsible gambling in order to:

- minimise harm caused by problem gambling; and
- accommodate those who gamble without harming themselves or others.

The Government is of the view that competitive restrictions on the industry which can effectively limit costs from problem gambling, without significantly reducing the benefits for recreational gamblers are in the public interest.

The recommendations of the review are listed below, together with a brief discussion and the proposed Government response to each recommendation.

Recommendations

1. Industry Structure

Recommendation 1: Two-Operator System

The excessive generosity of the current licences and resulting monopoly rents should end as soon as practicable.

The two-operator system should not be continued beyond the expiry of the current contracts and that a competitive model be based on Queensland. However, whichever model is chosen we strongly recommend that there be no profit sharing.(page 3)

We recommend that the Victorian Government use the discretion provided by clause 8 of the Gaming Operator's Licence to:

i) remove the monopoly profits above the level of payments necessary to ensure competitive or regulated provision of monitoring, servicing and machine rental;

ii) provide the operators with a flat cost-based fee for these services to venues.

Unlike the 1996 review, any future review should be public and transparent.

Discussion

As the review notes, the Government will continue to uphold all its contractual agreements. The early termination of a licence under the GMCA requires an order from the Supreme Court arising from either a material breach or persistent breaches of its licence. Early termination on other grounds may lead to compensation claims. Thus, the review concludes that under these constraints there is little benefit from revoking the existing licences before 2012.

The Government forms the view that the potential costs involved in a material change to the licence arrangements before 2012 would be large if compensation is payable to the two operators. Moreover, the overall economic benefits are likely to be relatively small due to the retention of the statewide cap on machines of 27 500. Therefore, the Government considers that the cost of early alteration of the licence arrangements would exceed the benefits.

The review asserts that Victorian legislation is unique in providing very substantial monopoly rents to the gaming operators. The review attributes this to the situation in Victoria where the machine operators receive a share of the profit. Indicative calculations made by the reviewer suggest that the guaranteed payment to the two machine operators is around four times larger than the payments for the equivalent functions in other states.

The review proposes that the Victorian Government:

- remove the monopoly profits above the level of payments necessary to ensure competitive or regulated provision of monitoring, servicing and machine rental; and
- provide the operators with a flat cost-based fee for these services to venues.

The Government accepts that, on the basis of the evidence examined by, and presented in, the review it is possible that operators are earning monopoly rents.

The Government accepts that the original return guidelines formulated were either fully or in part dependent on two policy goals that were of concern to policy makers, namely:

- adequate returns to the gaming operators; and

- assistance in ensuring public confidence in the probity of the industry and capital for industry set-up.

As noted above, the Government is committed to the dual operator arrangements until 2012. At some time before the expiry of the licences in 2012 a comprehensive review of the industry arrangements beyond that date will be undertaken. That review should consider the issue of profit sharing, and any rents that are generated in the industry.

However, in considering what changes, if any, the Government should make now to the current rate of tax, it must examine questions about the size and distribution of gaming machine revenues and whether Government is retaining the 'right' proportion of those revenues. This includes both in an ongoing fashion through the player loss tax rates or through the up-front payment of licence fees. It must also consider "sovereign risk" arguments.

There is little doubt that in the face of strong demand for gaming machines, the industry and regulatory structure in place generates large amounts of turnover, and therefore player loss, on a relatively limited number of gaming machines. In question is the level of any excess profitability, and how it should be distributed between venues, gaming operators and the Government.

The estimates of the monopoly rents range from:

- the figures calculated by this review (ranging from $200 to $500m pa);
- that offered by the business tax review ($120m – comprising $110m from the two operators); and
- an independent assessment commissioned by Tabcorp that concluded that the level of profitability is not above normal levels for the industry.

The review constructed its estimate of the level of excessive profits by benchmarking the two operators against the typical range of costs found across those other jurisdictions that have gaming machines. The review concludes that the arrangements provide a level of payment to the two operators well above that required to ensure provision of the service. That is, under an alternative structure there would be a much greater return to either the venues or to government.

It is the Government's view that the assumptions used in the review overestimate to a significant degree the level of overall 'rent' accruing to the operators as a result of the industry structure. Moreover, the review plays down the payment of significant licence fees (which in the case of Tattersall's is an ongoing additional payment from its profit share) and the basis upon which those licence fees were calculated. The current arrangements share the profits broadly equally across venues, the operators and the Government. The review in essence makes the judgement that the operators derive 'too much' of the player losses from the industry.

The assumptions contained in the review were examined on behalf of the review of State business taxes. Based upon an analysis of information contained in the annual financial

statements for Tattersall's (the operator with the most intensively used machines), the business tax review concluded that the review's estimates are on the very high side of the likely range of outcomes.

It is clear that the duopoly arrangements and the statewide cap on the number of gaming machines in the State provide benefits to the operators of scarce machines, as well as those venues that have access to them. It is arguable that the size of those benefits was underestimated to a degree at the time of the development of the industry structure. However, the current market rate of return has been capitalised into the value of the companies (particularly Tabcorp), and to that extent current shareholders are not receiving supernormal returns on their investment. This situation is somewhat different for Tattersall's, where the ownership (that is, the beneficiaries of the Estate) has not significantly changed.

The impost of a levy of $1,200 per machine announced by the Government on 18 April 2001, in addition to the $333 levy per machine introduced in the 1999-00 Budget, strikes an appropriate and fair balance between the interests of investors, business and the broader community.

Government Response

The Government notes that the recommendation does not directly deal with a competitive restriction and does not require Government action for the purpose of NCP compliance.

However the Government notes the findings of the review with regard to the accrual and distribution of economic rents resulting from the industry arrangements.

The Government agrees that a comprehensive review should be conducted closer to the expiry of the current licences to examine the appropriate industry structure beyond 2012. Without pre-empting the review, the Government is supportive of greater competition in the industry.

Any comprehensive review of the post-2012 industry structure should consider a number of the issues raised by the review, including the appropriateness of the continuation of the profit sharing arrangements, ownership structure and number of gaming operator licences.

However, the review erred in presenting the option of a further 'clause 8 review' of profit sharing and taxation arrangements. Following that review, conducted in 1996, the previous Government removed that provision from the legislation and the licences. Changes to the profit sharing and taxation arrangements before 2012 would require a fundamental alteration of the operating environment established for the terms of the licences. The Government has given an undertaking to honour the principles and commitments given at the time the licences were issued.

In immediate response to this recommendation, and the review of State business taxes, the Government announced an additional $1200 levy per machine to provide funding for the public hospital system. This is in addition to the $333 levy per machine introduced in the 1999-00 Budget.

The Government notes that in introducing the recent raft of responsible gambling initiatives it has imposed additional costs upon the operators.

The Government will consult with the gaming operators and other stakeholders to determine the timetable for a review of the arrangements to apply beyond 2012.

Recommendation 2: The Racing industry and the Licence under the Gaming and Betting Act 1994

The Government and the racing industry should take the early opportunity to renegotiate the current open-ended Agreement Act to ensure on-going support independent of the existing duopoly and financing arrangements, so that agreed new arrangements can be in place when the existing contracts/licences expire in 2012.

Discussion

The review notes that the racing industry is a direct beneficiary of the on-going extraction of revenues from gaming machines as venue operators and as joint venture partners with Tabcorp. The review assumes this arrangement has contributed to the health of the Victorian racing industry.

The review argues that the retention of the duopoly in gaming machines is not necessary to achieve the legislative objective of supporting the racing industry. Uncoupling the link will ensure that support to the industry is not dependent on the health of one operator in the gaming machine market. Under more competitive conditions for machine operators and/or reduced earnings, the racing industry is likely to receive substantially lower returns.

The review recommends that support to the racing industry could be coupled to total gaming industry revenues.

The Government accepts the view that other methods exist by which the objectives of the legislation can be achieved, and that another method of support provision may be desirable in achieving the objectives of the legislation. This is of particular importance in any post-2012 industry structure materially different from the current arrangements.

The Government recognises the contribution the racing industry makes to the State's economy. The review should be cognisant of the impacts upon the viability of the racing industry when investigating options for the industry structure beyond 2012.

Government Response

The Government accepts in principle the recommendation, noting that the review identifies support of the racing industry as an objective of the legislation.

Recommendation 3: Linking Real-time On-line Monitoring to Operator's Licence

The legislation should be amended to remove the requirement that monitoring and control be a requirement of the operator's licence. There would consequently be no need to require the system to be on-line, real-time.

Discussion

The review compares the restriction for ensuring probity in gaming, and the undertaking of the function of monitoring and control of machines, against alternative methods and arrangements found in other Australian States.

The review concludes that despite the different restrictions and structures and the legislative specification of, arguably, better quality real time monitoring for Victoria, there appears to be little or no difference in the levels or threat of infiltration of organised crime between the three States.

Real-time on-line monitoring of gaming machine operations is a condition of the gaming operator's licence. The review notes that this requirement has been believed necessary to ensure probity of gaming machine operations. It states, however, that this restriction may prevent the use of alternative monitoring systems, such as the lower cost dial up system.

The review claims that the benefits of the restriction are not obvious. Other states, such as Queensland and New South Wales, have opted for dial-up monitoring and these states have not identified superior features in the practice of real-time on-line monitoring in relation to probity.

The Government accepts there is no compelling argument from the point of view of regulation to require Operators to connect all machines on-line all the time to a central monitoring system. Provided that secure data storage at each site can be maintained that allows for revenue verification and game play history, regular and frequent dial-up capabilities should be sufficient. However, on-line real-time connection is necessary if gaming operators wish to continue to offer multi-site linked jackpots.

While the dual-operator system remains a feature of the industry structure, there is little competitive benefit in modifying this requirement, as it is the prohibition on additional monitoring service providers that presents the barrier to entry, not the requirement for real time monitoring. The Government does not intend to approve additional monitoring service providers.

Regular and frequent dial-up monitoring capability is less expensive than dedicated telecommunications necessary for on-line, real-time monitoring. At present, if gaming operators were allowed to adopt dial up monitoring, under the existing arrangements all the benefits would go to the gaming operators. An issue that the Government would wish to examine would be how to distribute the benefits arising from reduced operating expenses amongst the Government, gaming and venue operators and the players.

The Government will consult with the industry and the Victorian Casino and Gaming Authority (VCGA) to assess the consequences of any move away from on-line real time monitoring. The Government will only contemplate changes if it is satisfied that public confidence in the integrity of the system can be maintained.

Government response

The Government accepts in principle the review findings and recommendation. While the intention is to retain the requirement that monitoring and control be a requirement of the operator's licence for the life of the current arrangements, the Government will consult with the VCGA and the industry on the most appropriate way forward for monitoring arrangements. A key consideration in examining this issue will be to ensure the absolute integrity of the on-line monitoring regime.

2. Distribution of Machines

Recommendation 4: The allocation of at least 20 per cent of gaming machines to non-metropolitan Victoria

This restriction should be removed from the legislation.

Discussion

The review states that the objective of this restriction is to ensure that the benefits associated with gaming would be available to non-metropolitan Victorian areas. The restriction was particularly relevant in the initial rollout of the industry, when machine numbers were very low. Indeed references in the Hansard during debate of the GMCA referred to this Ministerial Direction in the context of concerns that the country areas would miss out on (scarce) machines at the expense of Melbourne.

The review questions the restriction in two areas. First, it argues that the restriction is not binding, with around 27 per cent of machines currently located outside of the Melbourne Statistical Division. Second, it asserts that the objective of the restriction conflicts, at least in part, with the new objective of minimising harm. The review concludes that there is no need to retain this direction.

The Government accepts that the primary intention of the direction was to make gaming machines available to country venues at a time of relatively small numbers of machines, and that the restriction is not currently binding. However, the Government is concerned

that recent changes making Melbourne-based venues more commercially attractive than non-metropolitan venues may bring this restriction into play. The Government would wish to see the outcome of the reforms introduced to date, before removing this ministerial direction.

Government response

The Government notes the recommendation and will monitor the impact of the recent, more sophisticated, reforms on the distribution of machines across the State. Until the impacts of recent policy initiatives introducing regional caps and social and economic benefit tests are known the Government will retain the current restriction.

Recommendation 5: Club-Hotel 50:50 Split

This restriction should be retained.

Discussion

The review finds that there are two objectives of this restriction. First, the restriction ensures that clubs obtain the benefits of gaming machines, which is an implicit, but significant objective of the legislation. The review argues that there are also benefits for the wider community, as clubs ultimately direct the money back to the community (or at least their members). Second, it is meant to reduce the harm of problem gambling.

The review recognises that the effects of this restriction include:

- ensuring that a minimum proportion of machines are located in clubs;
- preventing the vast majority of machines from being allocated to hotel venues;
- slowing the growth in numbers of electronic gaming machines in Victoria;
- keeping the level of gaming much lower than it would be if the hotel sector was able to obtain an unrestricted share of available machines; and
- increasing the competitiveness in the club sector and reducing competition in the hotel sector.

The review then considers alternatives to the restriction. It further states that the benefits and costs of the 50:50 split in machine numbers between hotels and clubs can be assessed against the benchmark of no such restriction.

Potential benefits of the restriction include:

- the mutual and co-operative objectives of clubs being less in conflict with the objectives of responsible gambling than the profit-focussed objectives of the hotel venues. Clubs should therefore be well-placed to assist in alleviating problem gambling;
- a greater focus on community objectives and higher, or more wider, distribution of revenue;

- with their mutual structure and focus on community and other objectives rather than profits, the clubs contribute to community objectives. However, in a commercial sense, the clubs are often seen to lack efficiency; and
- the spread of gaming has been slowed by the interaction of the 50:50 split between clubs and hotels in concert with the 50:50 split between Tattersall's and TABCORP and the total cap on numbers.

The review concludes that, under the current industry structure, there would be no benefit to allowing greater access for hotels to machines.

The Government accepts the view that, on the basis of the evidence presented in this and other research and under current policy settings, there is a net public benefit to the wider Victorian community in retaining this restriction.

Government response

The Government accepts the recommendation to retain the Direction regulating a 50:50 split of gaming machine numbers between hotel and club venues.

Recommendation 6:Quasi Clubs

This package of measures should be adopted:

(a) *separate liquor and gaming licences and break the presumption that award of a liquor licence automatically qualifies the venue for a gaming licence. The legislative change has already been made, but the change needs to be signalled;*

(b) *provide legislative clarity and guidance to the VCGA by explicitly listing the items to be considered in any case by case assessment of the 'reasonableness' or otherwise of commercial arrangements;*

(c) *prohibit in totality profit-sharing arrangements or prohibit, subject to specifically authorised exceptions, profit-sharing arrangements;*

(d) *require and resource the VCGA to undertake ex-post analysis of the sources and uses of funds from gaming and other activities in those clubs contracting external management contract services and leasing premises from related third parties;*

(e) *provide and enforce penalties on companies, their directors and the club directors found to be involved in non-genuine club gaming activities. For instance, banning these persons and entities from further involvement in gaming; and*

(f) *tighten direct responsibilities for clubs engaging in substantial gaming activity. For instance, amend the gaming machine control act to require directors of such clubs to be bound by the same responsibilities of directors of companies under Corporations Law.*

Discussion

The review identifies 'quasi clubs' as venues that are licensed as clubs but where the commercial arrangements are structured to transfer power, discretion and profits to other parties.

The Government notes the concerns, highlighted in the review, that arise where the regulatory and legislative framework allows quasi clubs to exist. The Government is opposed to these quasi clubs because it believes that the benefits derived from gaming machines in club venues should accrue to the club, its members and the wider community, rather than to private management groups or individuals.

The Government also accepts that some clubs and club members have benefited from management arrangements through injection of capital, efficient modes of management and, more generally, provision of expertise from the commercial sector.

The Government is of the view that the main reason that 'quasi clubs' occur is because of the restrictions on the overall number of machines in the State and the direction that 50 per cent of machines must be located in club venues. A second factor is that club venues do not have to contribute to the Community Support Fund (although there is scope for this levy to be applied to clubs in certain circumstances).

Given that the Government has accepted that the statewide cap and the 50:50 club-hotel split are in the public interest, and has made public commitments not to remove these restrictions, it is keen to ensure that machines are provided to legitimate clubs.

Another particular concern of the Government was to examine the apparent concentration of control over club venue management in the hands of a relatively small number of agents. While this issue is also of concern in the hotel sector, the review concludes that this issue is most apparent in the club sector. Recent changes to legislation have allowed the publicising of associates of venue operators and gaming operators. This information is now available from the VCGA, including on its Internet site.

In general, the Government will continue to review approval and operating procedures to ensure the transparency, accountability, integrity and independence of the club as gaming licensee but without compromising efficient commercial practice. The Government believes that such an approach would be consistent with the NCP framework and be in the best interests of club membership and the wider community.

In relation to the specific suite of recommendations, the Government takes the following views.

(a) *Breaking the presumption that award of a liquor licence automatically qualifies the venue for a gaming licence*

As the review identifies, the Government has legislated to remove the presumption that award of a liquor licence is a necessary pre-requisite to the consideration by the VCGA of

the granting of a gaming licence. The Government is of the view that the significant shift in the licensing regime for venues is becoming instilled in the industry. This recommendation is already in place.

(b) Provide legislative clarity and guidance to the VCGA by explicitly listing the items to be considered in assessing commercial arrangements

(c) Prohibit profit-sharing arrangements either altogether or subject to specifically authorised exceptions

It should be noted that that section 136A of the GMCA already provides a means of looking behind the commercial arrangements at a club and applying the hotel rate of tax if the club is found in substance to be a hotel. However, the Government will consider ways of providing increased scope for the VCGA to make such determinations.

The imposition of the hotel rate of tax to non-conforming clubs may not act as enough of a deterrent to the continuation of quasi club arrangements. The Government is keen to provide an industry structure that meets the spirit and intent of the restrictions. That is to ensure that at least half of the number of machines permitted in the State is available for legitimate clubs. The review does not provide a convincing case that the best way to address this issue is through Government micro-regulation of commercial agreements between venues and management service providers. However, it will examine ways to enhance controls on the allocation of machines, for example by Ministerial Direction, to ensure that outcome.

(d) Require and resource the VCGA to undertake ex-post analysis of the sources and uses of funds from gaming and other activities in those clubs contracting external management contract services and leasing premises from related third parties

This recommendation is strongly linked to (b), above, which the Government accepts in principle. This approach is one option available to Government to broaden the scope of the VCGA in examining such arrangements. In broad terms the options include:

i. applying the CSF levy to all venues, then providing them with scope to apply for funding from the CSF for worthwhile projects for the community benefit;

ii. providing a clear checklist of activities that club venues must undertake to justify why they should avoid the levy. For example a periodic community benefit statement might indicate not only the commercial, financial and community activities the club has undertaken, but also what it has done in terms of the promotion of responsible gaming measures and behaviour; and

iii. giving the VCGA enhanced powers to examine the commercial and financial structure and nature of the venue and its activities for the express purpose of deciding whether the levy should be imposed.

The Government will consider all options in the context of achieving the objectives of ensuring access to 50 per cent of gaming machines to legitimate clubs and demonstrating to the community the wider benefits of a gaming industry that is conducted responsibly. The Government would also wish to introduce a regime that imposes as small as possible compliance burden upon legitimate clubs.

(e) Provide and enforce penalties on companies, their directors and the club directors found to be involved in non-genuine club gaming activities. For instance, banning these persons and entities from further involvement in gaming

(f) Tighten direct responsibilities for clubs engaging in substantial gaming activity. For instance, amend the gaming machine control act to require directors of such clubs to be bound by the same responsibilities of directors of companies under Corporations Law

The Government will not consider imposing controls designed for directors and companies upon those that are not. The focus of gaming legislation and investigation should remain focussed upon probity and related checks as well as dishonesty and integrity.

The Government is of the view that there is no benefit from a duplication of Corporations Law in State gaming legislation. This may well be outside the powers of the State Government in any case.

Changes to accountability of associates of venues, etc, coupled with other changes to remove the incentives to form quasi clubs should able to be designed to meet government objectives in this area without the need for such an approach.

Government response

The Government notes the suite of recommendations outlined for the club sector, while noting that this issue is not, strictly speaking, one directly concerning a competitive restriction.

The Government is moving to implement initiatives to ensure accountability of club venues. In addition the Government will continue to examine these recommended options as well as other measures.

The Government has already put in place measures that introduce Recommendation (a).

The Government accepts in-principle recommendations (b) & (d) to provide broader scope for the assessment of club venues and the appropriateness of applying the Community Support Fund levy and to provide a mechanism for venues to demonstrate the wider community benefits of their gaming activities. The Government is considering a number of options, with the objective of ensuring that venues provide meaningful information with a minimal compliance burden on genuine club venues.

The Government accepts in-principle recommendation (c). However it should be recognised that some clubs have benefited from such management arrangements. The Government will examine the issue in more detail to determine the appropriate changes to the existing regime.

The Government does not accept recommendations (e) & (f) believing that the principal focus of gaming legislation should be to ensure the honesty and integrity of the gaming industry and its participants, rather than duplicate Corporations Law and other legislative governance of general commercial activities.

Recommendation 7: Limits on machine numbers per venue

This restriction should be retained pro tempore.

Discussion

The review notes that Victoria currently imposes a uniform limit of 105 machines total per venue. The genesis of the restriction is that it is part of the exclusivity arrangements made by the previous Government with the casino operator (at the time of negotiations for the commercial arrangements relating to the casino). The Casino Management Agreement prohibits, until 2005, the existence of venues larger than 105 machines within 100km of the Melbourne casino.

The current ministerial direction extends that prohibition to cover the entire State.

The review notes the impacts of the restriction include:

- preventing large venues "mini-casinos" from being established in the country;
- lowering the total level of gaming;
- ensuring that geographic location within the State does not advantage any other venue or group of venues;
- lowering the competitiveness of Victorian venues located near the NSW border across which larger and possibly more attractive venues may be operated; and
- potentially, to slow the relocation of machines from small venues.

The review analyses the benefits of the restriction against alternatives and sets the analysis in the context of other restrictions. The alternative chosen for this evaluation is the situation of no restriction on machine numbers per venue outside the 100km radius of the casino.

The impacts, benefits and costs of this restriction and its removal outside the 100km radius are heavily impacted by the new requirements applying to venues outside the zone. Venues outside of the zone that wish to increase their machine numbers must now meet the net social and economic benefit criteria. At the time of the writing of the review the net social-economic impact tests had not been fully implemented. Therefore, there had been little

demonstration of its effectiveness or otherwise in reducing the level of gaming or the level of problem gambling.

Larger venues tend to obtain greater revenue from each machine, which may indicate that consumers prefer larger venues. However, greater gambling expenditure is thought to be associated with higher levels of problem gambling. Again, as a very blunt instrument, by limiting the efficiency of venues and restricting turnover, the limit on venue numbers appears to reduce the harm from problem gambling. In contrast, the alternative of no restrictive venue limit may increase the machine turnover and problem gambling.

The review notes that a limit on numbers of machines per venues may interact with other restrictions producing varying effects on revenue and the allocation mix between hotels and clubs.

The Government notes that various options exist. These include raising the venue limit (or removing the restriction altogether) on the number of machines in venues outside the 100km radius of the casino; or lowering the venue limit for some or all venues.

The Government notes Productivity Commission research, cited by the review, which states that *"On balance, venue caps can play a role in moderating the accessibility drivers of problem gambling from gaming machines…"*

The main advantage from a competition policy perspective in retaining the statewide 105 limit – applied to club and hotel venues equally – is that it provides for a level playing field for all venues (excluding the casino). This is in contrast to some other jurisdictions that discriminate between clubs and hotels with regards to limits.

There may be some modest benefits from removing restrictions on machine numbers for venue efficiency, consumer satisfaction and competitiveness with large venues inside NSW. However, the Government considers that such benefits are outweighed by the benefits from maintaining a common machine limit for all venues across the State.

The Government at this stage is not inclined to follow a path of liberalisation of gaming machine numbers in venues and will consider any future course of action in the context of its interaction with current and future Government policy.

Government Response

The Government accepts the recommendation to retain the 105-machine cap on venues.

3. Other Restrictions

Recommendation 8: 24-hour Gaming Restrictions

This restriction should be retained.

Discussion

The review examines the new restrictions introduced in the *Gambling Legislation (Responsible Gambling) Act 2000* which set a maximum 20 hours of continuous gaming (with a minimum 4 hours break following this period) for venues that do not have approval for extended hours. Extended hours are only allowed for venues that have approval from the VCGA to operate up to 24 hours on specified days.

The effects of the restriction are to:

- limit and eventually phase out 24-hour venues outside the Melbourne Statistical Division (MSD); and
- allow venues within the MSD to operate 24-hours only where they can demonstrate to the VCGA a net social or economic benefit from being permitted to do so.

The review finds that the restriction is relevant to the legislative objectives of harm minimisation and responsible gaming. The potentially discriminatory impact of this restriction between venues approved to gamble for greater than 20 hours and the remainder does not appear to be material.

Under the GMCA the conduct of gaming for longer than 20 hours will only be approved where the venue can demonstrate there is no net social and economic detriment to the municipality. Each application for extended hours is therefore effectively subject to a public interest test.

The policy of allowing appropriate 24-hour venues in metropolitan Melbourne was to ensure that the casino was not bestowed a material competitive advantage. The eventual ban in non-metropolitan Melbourne has less impact on the competitiveness of gaming venues relative to the casino. The non-metropolitan ban policy was developed following community consultation by the Government in Opposition. The policy formed an important part of the Government's gaming policy platform. The Government believes that the policy conforms to community expectations in the affected areas and indicates it is in the public interest.

Government Response

The Government supports the recommendation to retain the restrictions on 24-hour trading.

Recommendation 9: Gaming Venues restricted to Licensed Premises only

Only venues with one of: a general licence under the Liquor Control Reform Act 1998, a club licence under s.10 of the same Act or a licence under Part I of the Racing Act 1958 (or a licence issued under these sections but with conditions under s.80 of the Liquor Control Act 1987) can be approved premises (s.12A).

Discussion

The Government does not consider it is in the public interest to extend the provision of gambling facilities beyond the current licensed premises. The barrier to entry of non-licensed premises is considered an appropriate restriction and in line with community standards and expectations. The Government also considers the restriction to licensed premises to be the most effective way of restricting minors from access to gaming opportunities.

By restricting gaming to licensed premises, gambling is better placed to remain one of a suite of recreational activities available to the club or hotel patron. This is more likely to encourage responsible gambling behaviour than, for example, dedicated gaming parlours.

Such restrictions conform to community expectations and standards about the availability of gambling venues while not materially limiting the accessibility of gambling opportunities to those that wish to gamble for recreation.

Government Response

The Government accepts the recommendation to restrict gaming to licensed club and hotel venues.

Recommendation 10: Denominations and Betting Limits

The general ability to set bet limits under Ministerial Direction should be retained. We also recommend that the use of more aggressive bet limits should follow appropriate research and testing.

Discussion

The review notes that betting limits previously existed only for machines in unrestricted areas. Machines in unrestricted areas had a bet limit of $2.00. These restrictions have been effectively removed with the banning of machines in unrestricted areas. Machines in restricted areas do not currently have a bet limit.

The review supports the ability to set betting limits because of the impact on problem gamblers. It draws from the Productivity Commission report statement that problem gamblers tend to increase the intensity of play, and that setting bet limits will invariably have an impact on intensity of play. However, the evidence on this point is equivocal. The Government accepts the need for more research into the effectiveness of such measures.

In the interim the Government will retain the ability to impose restrictions on bet limits.

Government Response

The Government accepts the recommendation to retain the ability to set bet limits. The Government would wish to see research conducted into the effectiveness of bet limits to promote responsible gambling behaviour.

Recommendation 11: Venue Operator Cannot Have Two Premises Within 100m

Where an applicant (or an associate) has an existing venue within 100m of a proposed venue, these venues must be independent of each other.

Discussion

This restriction is intended to protect against the development of *de facto* venues larger than 105 machines. The Government believes this restriction increases competition, rather than fettering it. There is no intention to remove the restriction.

Government Response

The Government accepts the recommendation to retain the restriction.

Recommendation 12: General probity requirements

The existing probity restrictions should be retained and continue to be subject to on-going independent review.

Discussion

These restrictions and conditions are common across Australian jurisdictions. Moreover they apply equally to both gaming operators and all venues and venue staff.

To the extent that these barriers to entry present a restriction on competition the review forms the view that they can be justified in the public interest. The Government will continue to monitor and, where appropriate, modify the probity requirements and procedures. For example, recent changes to provide for fingerprinting services for regional and rural-based applicants for special employee licences is one way the Government has moved to remove barriers to entry while maintaining the integrity of the probity arrangements.

Government Response

The Government accepts in principle the findings of the review. The Government is satisfied that the barriers to entry presented by the stringent probity arrangements are in the public interest to ensure integrity and honesty in the gaming industry.

Recommendation 13: Secrecy restrictions under Section 139

More explicit guidance should be given to the VCGA on its role and responsibilities.

Discussion

The review notes that free and competitive markets depend upon the free flow of information. The review asserts that the effect of the secrecy restrictions is to constrain the flow of information to market participants. The benefit of this restriction appears to accrue with the gaming operators who already have most of this information. Full information is also necessary for effective regulation and policy formation.

The Government supports fully the independence of the VCGA. Any 'explicit guidance' from the Government to the VCGA on its roles and responsibilities would be in the form of legislative change.

Government Response

The Government notes the review's comments on the secrecy provisions to which the industry is subject. While the recommendation does not strictly deal with matters of competitive restrictions, the Government supports in principle the notion of continual review of these provisions.

Recent amendments to this section of the Act provide for more accountability and openness of the VCGA including the conduct of open hearings. To the extent that more public information assists competitive outcomes then the Government has already acted to remove competitive restrictions.