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Regulating Casino Gaming: A Checklist for States Considering It

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Regulating Casino Gaming: A Checklist for States Considering It

Abstract

In his essay - Regulating Casino Gaming: A Checklist for States Considering It – by Leonard E. Goodall, Professor of Management and Public Administration, College of Business and Economics, University of Nevada, Las Vegas, Professor Goodall initially states: “Since various states are likely to continue to debate the issue of the establishment of legal casinos, and since states considering legal casinos must also decide how best to regulate them, the author discusses the similarities and contrasts in the regulatory systems already in operation.”

Certainly not all states have solicited casino gaming, or what people generally refer to as gambling, but many have and the list is growing. If casinos are to be, and indications are that many more states will endorse gaming as a source of revenue, then regulating them must follow as a matter of due course says the author. Keep in mind this essay was written in 1988, and the actuality of casino gaming has indeed come to fruition in many states.

“Nevada, having legalized casino gaming in 1931, has over a half-century of experience with the regulatory process,” Professor Goodall informs. “When New Jersey approved the establishment of casinos in Atlantic City in 1976, state officials studied the Nevada system carefully and adopted many of Nevada’s procedures.”

Professor Goodall bullet-points at least 7 key elements that states wanting to pursue gaming should, or in the cases of Nevada and New Jersey, have already addressed in regard to regulation of the industry. Goodall parses, in more detail, those essentials.

The ultimate form of regulation is ownership Goodall says. Either state run, or private are the logical options. “The arguments for private ownership have been both pragmatic and political,” Goodall says. “Legislators, like the general public, are skeptical of the ability of state bureaucracies to run big businesses in an efficient manner. Many of them also believe regulation can be more effective if there is at least an arm’s-length distance between regulation and ownership,” the professor opines.

Additionally important to consider is the purpose of legalization, says Goodall. Are the proceeds earmarked for general funds, or to be used specifically?

Geographic considerations are key, Goodall points out. “This decision will depend partly on a state’s reasons for having casinos in the first place,” he expands. “New Jersey’s policy, for example, is obviously consistent with its goal of using casinos to reinvigorate Atlantic City.”

“In both states, one of the most important functions of the regulatory agencies is that of licensing, the process of investigating individuals or organizations and then authorizing them to participate in the gaming business,” Goodall provides.

In closing, Goodall says there is no need for ensuing states to reinvent the wheel when it comes to casino gaming regulation. Nevada and New Jersey already provide two good designs from which to emulate and/or build upon.

Keywords

Leonard E. Goodall, Regulating Casino Gaming: A Checklist for States Considering It, State v. Rosenthal

Regulating Casino Gaming: A Checklist for States Considering It

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Since various states are likely to continue to debate the issue of the establishment of legal casinos, and since states considering legal casinos must also decide how best to regulate them, the author discusses the similarities and contrasts in the regulatory systems already in operation.

There are few, if any, actions which will alter a community's hospitality industry more dramatically than the establishing of legal casinos. In recent years a number of states—including Florida, California, Louisiana, New York, Michigan, and Arizona—have considered the possibility of legalizing some form of casino gaming. The usual motivation has been the enhancement of state revenues. Only New Jersey has joined Nevada as states which have full scale casinos in operation.

Nevada, having legalized casino gaming in 1931, has over a half-century of experience with the regulatory process. When New Jersey approved the establishment of casinos in Atlantic City in 1976, state officials studied the Nevada system carefully and adopted many of Nevada's procedures. In some cases, however, New Jersey adopted a different philosophy and implemented different kinds of procedures. States facing this question should look at both systems. The following are among the issues which must be considered.

- **Public or private ownership.** The ultimate form of regulation is ownership, as seen in the case of state-owned lotteries or state-run liquor stores. New York uses a quasi-public corporation to operate its off-track betting system, and former Governor Carey recommended state-owned casinos. In New Jersey there was serious consideration of state ownership, and the private ownership system resulted more from legislative compromise than from the issues themselves.¹ Nevada has long opted for private ownership.

The arguments for private ownership have been both pragmatic and political. Legislators, like the general public, are skeptical of the ability of state bureaucracies to run big businesses in an efficient manner. Many of them also believe regulation can be more effective if there is at least an arm's-length distance between regulation and ownership.

From a political point of view, state officials often are not anxious to be seen as owners of a business which many members of the public frown upon and which has too often been seen as being corrupt or having underworld ties. It is also likely that officials in any state seriously considering the question will be heavily lobbied by casino owners in states having legal casinos to opt for private ownership. Existing experienced casino owners, after all, are the most likely candidates for owning and managing new casinos in other states.

• **Purpose of legalization.** While it may seem obvious, states need to consider the basic purpose for which they are considering authorizing casinos. Nevada and New Jersey, for example, differ on this point. The Nevada Revised Statutes state clearly: "The gaming industry is vitally important to the economy of the state and the general welfare of the inhabitants," thus identifying the industry with the economic welfare of the entire state.² In New Jersey the rationale was much more specific—the revitalization of Atlantic City.

Supporters of the 1976 referendum felt there was little support for something as general and nebulous as economic development or tax revenues statewide. Assemblyman Perskie said, prior to the referendum, "We must talk about the position of Atlantic City in the state's economy. I do think we can sell Atlantic City to the people of New Jersey." As the book, *Atlantic City Gamble*, puts it, "Gambling was not valued for itself but as a means to an end—the revitalization of Atlantic City."³

States considering legalization as a means of raising revenues must decide whether the new state revenues are to go into the general fund or be earmarked for a specific purpose. In Nevada the revenues go into, and comprise a major portion of, the general fund. In New Jersey, the 1976 referendum called for the revenues to be earmarked for projects to help the elderly. It is often politically popular to tie the revenue proposal to a specific purpose, such as education or the elderly. Once enacted, however, it is always difficult to determine whether other revenues have been diverted away from the stated purpose because that purpose now has its own designated revenue source.

State voters have been unwilling to approve casinos unless they clearly understand the purpose for legalization. A clear understanding of the purpose is not sufficient to assure approval, but lack of clarity on the issue will almost certainly assure rejection.

• **Geographic and other limits.** States must determine what limits, if any, they want to place on where casinos can be located. Nevada represents a very liberal approach. Casinos are allowed virtually everywhere in the state (only the city of Boulder City prohibits them), and they may be free standing with no associated hotel or other tourist facility. New Jersey permits casinos only in Atlantic City and requires that they be operated in connection with an approved hotel which meets minimum standards for numbers of rooms and amount of public space.

This decision will depend partly on a state's reasons for having casinos in the first place. New Jersey's policy, for example, is obviously consistent with its goal of using casinos to reinvigorate Atlantic City.

The decision on geographic limits will greatly affect a state's approach to casino regulation and enforcement. Regulation in a limited area can be much more intense than when regulatory responsibilities extend throughout the state.

Most of the states to consider the issue so far have preferred the New Jersey approach. Florida, for example, considered placing casinos on Miami Beach; Michigan planned to place them on Belle Isle in the Detroit River near Detroit, and Louisiana's plan was to allow them only in the French Quarter in New Orleans.

• **Organization and administrative structure.** This is an area in which New Jersey and Nevada function in very similar manners. The Nevada Gaming Commission and the New Jersey Casino Control Commission are the primary policy-making bodies for their respective states. Both are five-member boards, appointed by the governor, with general responsibility for regulation of the industry, including licensing, investigations, and the making and enforcement of regulations. Both states have requirements that no more than three of the five members may come from the same political party.

Both states also have operating agencies with responsibility for day-to-day enforcement under the general direction of the policy board. The Nevada Gaming Control Board consists of three full-time members who must represent the fields of law enforcement or law, accounting, and business or public administration. Members may not have a pecuniary interest in the gaming business, but nothing prevents them from entering the business after leaving the board.

The New Jersey Division of Gaming Enforcement is a part of the state's Department of Law and Public Safety. The director is also to be an assistant attorney general and works under the general supervision of the attorney general.

• **Licensing.** In both states, one of the most important functions of the regulatory agencies is that of licensing, the process of investigating individuals or organizations and then authorizing them to participate in the gaming business.

In understanding the licensing process, it is essential to know that Nevada and New Jersey both declare participation in gaming to be a revokable privilege and not a right. Both states give their regulatory agencies very broad (in Nevada, almost unlimited) discretion in granting, renewing or revoking gaming licenses.⁴

This broad regulatory authority was strongly reinforced in 1977 in the Nevada court case of *State v. Rosenthal*.⁵ In that case, the Nevada Gaming Commission found Frank Rosenthal unfit for licensing based on allegations he had attempted to bribe athletes. Rosenthal claimed the case was based on hearsay evidence and other information that in no way would meet any court standards for rules of evidence or procedural due process. He appealed on the grounds that his constitutional rights had been violated.

A state district court ruled in favor of Rosenthal, but the Nevada Supreme Court, in a broad and sweeping decision, overturned the district court and upheld the Gaming Commission. The supreme court ruled that the Gaming Commission need not establish uniform standards, that the burden of proof is on the applicant and not the commission, that participation in the gaming business is a privilege and not a right, and that the commission may regulate without regard to constitutional rights so long as the regulation is "reasonable."

In affirming the lack of constitutional rights, the court differentiated between gaming, which it referred to as a "non-useful trade with deleterious tendency," and the "useful trades," which are subject to much more limited state regulation. The court states that gaming is a matter reserved to the states under the Tenth Amendment, and there is thus "no room for federally protected constitutional rights."

The U.S. Supreme Court, in a very significant decision (or perhaps non-decision), refused to hear the case, thus letting the state decision stand. Professor Nelson Rose, in commenting on the decision, said, "The Nevada Supreme Court is undoubtedly wrong; the Supremacy Clause and 14th Amendment in the United States Constitution do not allow a state government to deny federally created civil rights." Nevertheless, the Rosenthal case still stands.

The New Jersey Supreme Court seems to take a more limited view, having heard cases involving charges that state gaming regulations violate federal constitutional rights. The state courts have upheld such individual rights as due process and the right to privacy.⁷

The U.S. Supreme Court's refusal to hear the Rosenthal case suggests it is likely to leave gaming regulation to the states, giving the states far broader discretion in this area than in others. States, therefore, need to be prepared to provide statutory protection to protect individual rights where gaming regulations are concerned. The alternative is to rely on the state constitution and state courts to assure such protection.

The licensing process itself relies heavily on an investigatory process to determine which individuals or corporations are "suitable" to receive a license. The investigation may look at such items as financial responsibility, prior business experience, criminal records, past associations with alleged underworld figures, etc. The broad discretion granted by the Rosenthal decision gives regulators authority to consider whatever matters they consider appropriate to the investigation.

There is some difference in the definition of who must be licensed in the two states. Both states require licensing of the casinos themselves, of the ownership corporations, executives, major stockholders, key employees, etc. New Jersey goes beyond Nevada and requires licensing of such others as the employees of suppliers, employees of adjacent hotels, the unions of casino employees, etc.⁸

One procedural difference between the two states is that in Nevada the Gaming Control Board, after completing its investigation, must provide a report and a specific recommendation to the Gaming

Commission. New Jersey, in contrast, requires the Division of Gaming Enforcement to provide a report to the Casino Control Commission, but no recommendation is made.

An effective licensing process is essential to the successful operation of legal casinos, and licensing law is rapidly becoming a speciality within the field of gaming law. States considering the possibility of authorizing casinos would be well advised to consult with specialists in licensing when preparing their enabling legislation.

• **Regulation.** After states have licensed casinos and casino personnel to do business, they must establish a process for their ongoing regulation. Regulation involves many activities including the proper operation of slot machines, the fairness of the table games, procedures to prevent skimming, assurance of honesty among employees, etc.

While it would be impossible to go into detail on the casino regulatory process, it can be pointed that there is a fundamental difference in the basic approaches used by Nevada and New Jersey. New Jersey utilizes an "in-house" regulatory process that involves having casino control agents physically present in casinos all the time they are open. Such an approach obviously provides intense scrutiny of the industry.

Nevada has long used an approach that might be called the unannounced audit technique. Somewhat like bank regulators who make surprise visits to banks, Nevada's gaming control officers can visit casinos without notice. A wide variety of other investigatory techniques are used, including having agents actually play the games while watching for irregularities, but a continual "in house" presence is not part of the Nevada regulatory process.⁹

The approach a state takes may be determined to some extent by the nature of gaming in the state. New Jersey, with only about a dozen casinos all concentrated in one city, can provide for a very intense approach to regulation. The fact that New Jersey's casinos are not open 24 hours a day also makes it easier to provide the staffing necessary for such scrutiny. Nevada has well over a thousand gaming locations scattered throughout a very large state, many of them open around the clock. It would be virtually impossible to use the New Jersey approach throughout Nevada.

There is no conclusive evidence yet that one approach is necessarily better than the other. The New Jersey plan would seem to provide for tighter controls, but New Jersey's casinos have complained, almost from the day they opened, about over regulation. The violations and problems in both states suggest that neither scheme is foolproof.

Since most states considering legal casinos seem to be leaning toward confining them to specific areas, they will have the flexibility of experimenting with either approach. Additional time and more research may shed more light on the strengths and weaknesses of each.

Future Casinos Should Build on Past

It is unlikely that Nevada and New Jersey will remain the only states with casino gaming. As other states debate whether to move in this direction, they must address several key policy decisions:

- Will casinos be privately or state owned?
- Is it clearly understood why casinos are being authorized? To encourage tourism? To rehabilitate a specific area, like Atlantic City? To provide revenues for a specific purpose, like education or senior citizens? To provide more revenues in general? Is this purpose for legalizing casinos clearly understood by the press and the public?
- What are to be the geographic limits within which casinos may operate?
- What other limits are to be imposed? Must they be attached to a hotel, and must the hotel have a minimum number of rooms?
- What kind of state administrative structure will be established to regulate casinos? A board or commission? A new agency headed by an individual director? An existing agency such as the attorney general? Some combination of the above?
- Who should be licensed and how extensive should licensing procedures be? What steps will be taken to protect individual rights in the licensing process?
- Will regulation follow the New Jersey pattern of in-house regulation or the Nevada pattern of less intensive oversight?

There is no need for states considering casinos to have to reinvent the wheel. New Jersey learned much by studying the Nevada pattern. Other states can observe both states and build their own regulatory systems based on their evaluations of each. It appears that many states will continue to be addressing the issue of legal casinos in the future, and they should use the experience of the past for their own benefit.

References

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- ² Nevada Revised Statutes 463.0129
- ³ Sternlieb and Hughes, *op. cit.*, p. 49.
- ⁴ For a thorough discussion of the legal aspects of casino regulation in Nevada, see John R. Goodwin, *Gaming Control Law: The Nevada Model*, (Columbus, Ohio: Publishing Horizons, Inc., 1985). For an analysis and comparison of regulatory law in Nevada and New Jersey, see Alvin J. Hicks, "No Longer the Only Game in Town," *Southwestern University Law Review*, (1980-81).
- ⁵ State v. Rosenthal, 93 Nev. 36, 559 P.2d 830 (1977)
- ⁶ I. Nelson Rose, *Gambling and the Law*, (Hollywood, Calif.: Gambling Times, Inc., 1986), p. 185.
- ⁷ *Ibid.*, 186.
- ⁸ Hicks, *op. cit.* pp. 599-604.
- ⁹ For an interesting first-hand discussion of Nevada gaming regulation by a participant observer, see Jerome H. Skolnick, *House of Cards: Legalization and Control of Casino Gambling*, (Boston, Mass.: Little, Brown and Co., 1978).