

# **Managing the Relations Between State and Local Government and Casinos**

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**Citizens Research Council of Michigan**

625 Shelby Street  
Detroit, Michigan 48226-4154  
(313) 961-5377

1502 Michigan National Tower  
Lansing, Michigan 48933-1738  
(517) 485-9444

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# Managing the Relations Between State and Local Government and Casinos

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## Foreword

Legalized gambling is, along with Medicaid and corrections, among the components of state and local government in the United States that have exhibited the most dramatic growth in the 1980s and 1990s. States such as Mississippi and Indiana, in which most forms of gambling were illegal only a few years ago and which were viewed by most observers as unlikely candidates for lotteries, let alone casinos, have embraced gambling as a significant part of their economic development and revenue enhancement strategies.

There are several explanations for this sudden rise. First, in their search for new sources of revenue, governmental units tend to view revenue from gambling as a popular alternative to increasing unpopular taxes, mainly the property tax. Second, certain economically distressed areas have turned to legalized gambling as a means of producing revenue that could not be obtained through more conventional economic development and public finance approaches. Third, states may authorize gambling in self-defense. If a non-lottery state is surrounded by states with lotteries, it is normally only a matter of time before the pressure to stem the flow of money to those other states results in legalization of a lottery in that state. Casinos are now generating similar pressures. Finally, casinos, once inextricably associated with unsavory elements of society, are now frequently operated by large corporations with fine reputations.

At this writing, Michigan is confronting the issue of legalizing casino gambling. The Citizens Research Council of Michigan has been asked to assist in identifying ways in which the relationship between government and casinos might be made as successful as possible, should legalization of non-Indian casinos occur. This report is the response to that request.

In producing this report, the Research Council has approached the issue of government-casino relations as a problem in public administration. *On the threshold issue of whether casinos should be legalized in Michigan, the Citizens Research Council takes no position.* The point of this report is simply that, if the establishment of casinos in Detroit, or any other Michigan jurisdiction for that matter, becomes a real possibility, there are certain practical issues that should be addressed, sooner rather than later, that will help to maximize any benefits that might be derived from this activity.

The Citizens Research Council wishes to acknowledge the contribution of Wayne A. Collier, President of EDC, New Orleans, Louisiana, who brought a rare combination of objectivity and first-hand knowledge of city-casino relations to the task. Although he prepared significant portions of the report and commented on others, the Citizens Research Council accepts full responsibility for the material contained in this report.

*Earl M. Ryan*  
*Vice President-Executive Director*

# ***Checklist of State and Local Governmental Policy Considerations in Implementing Casino Gaming***

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## I. Introduction

After a long period of rejection, casinos have come to be viewed by many governmental jurisdictions as potential avenues of economic development and governmental revenue. Casinos are, however, unlike almost every other target of economic development efforts. Because they may operate legally in only a relatively few jurisdictions in the United States, the usual economic development approach—the offering of incentives, such as tax breaks—is stood on its head. Instead of being required to offer incentives, jurisdictions willing to legalize the operation of casinos find that they are, for the time being at least, in the unaccustomed position of being able to demand concessions from casinos.

This novel situation has created both opportunities and difficulties for many jurisdictions that have contemplated the establishment of casinos. The opportunities—new employment, new tax revenue, tourist revenue, and special exactions—have in many cases been at least partially offset by some of the difficulties associated with the introduction of casino gaming. The problem of greatest concern in this report flows from two simple facts about casinos: 1) only state government can authorize the establishment of casinos, and with that power comes the power to regulate them; 2) the economic impact of casinos, both costs and benefits, will be felt primarily by the local unit in which they are located. The extent of the local economic impact will be determined in large measure by decisions made by state government and the degree of flexibility it affords to local units in which the casinos will be located. For the introduction of casinos to work smoothly, therefore, it is important that the respective roles of the state and its local units be clearly delineated. Failure to do this has created serious implementation problems in Louisiana, Indiana, and other jurisdictions that have legalized casinos.

In short, the advent of casino gaming creates issues regarding not only the relationships between government and the casinos, but between state and local government, as well. If these relationships are not carefully structured, the establishment of casino gaming may not result in the kinds of benefits envisioned for it.

This report provides an introduction to the extent of casino gaming in the United States, the forms of casinos, and the structure of the regulatory response of states to casino operations. Further, it identifies the concurrent and separate interests of the State of Michigan and a local unit, such as Detroit, in the establishment and operation of casinos. It also provides a checklist of items to consider with appropriate references to the main body of the report.

## **II. Background on Casino Gaming**

The entertainment business is one of the fastest growing segments of the national economy and legalized gaming is considered to be the fastest growing element of the entertainment industry. The 1960s witnessed the beginning of a trend towards legalization of gambling in the United States. During the 1980s, tough economic and fiscal conditions further led state and local governments to legalize forms of gambling as a means to enhance state and local revenues. Among the popular forms of legalized gambling that gained legitimacy during this period were lotteries, horse racing, and, more recently, casino gaming.

The first modern era public lottery was established in 1964 in New Hampshire. The New York Lottery was established in 1967 followed by New Jersey in 1970. At present, 36 states and the District of Columbia operate legal public lotteries. Further, 46 states have active horse racing or authorize one or more type of horse race wagering including harness, thoroughbred and quarter horse tracks. Among the 50 states, only the states of Hawaii and Utah do not permit some form of gambling as a legal activity. In addition to lotteries, horse racing and casinos, other forms of legalized gaming include off-track betting, charitable and for profit bingo, card rooms, pull tabs, raffles, sports betting, and video lottery games.

### **A. Forms of Casino Gaming**

Over the past five years, the segment of the entertainment industry which has demonstrated unprecedented growth has been casino gaming. Casino gaming occurs in three major forms: land-based non-Indian casinos; land-based Indian casinos; and riverboat casinos. While the casino gaming industry has experienced significant growth over the past five years, it has been the rapid growth of the riverboat and Indian casino market segments that have fueled the overall growth of the casino industry.

#### **1. Land-based Non-Indian Casinos**

Currently, there are five states where land-based non-Indian casinos have been authorized: Nevada, New Jersey, South Dakota, Colorado, and Louisiana. Montana has authorized limited forms of legalized “mini-casinos.”

For 45 years, from 1931 to 1976, Nevada had a monopoly on legal casinos among the 50 states until New Jersey amended its state constitution to legalize commercial casino gambling. In 1976, New Jersey became the second state to legalize casino gambling and saw 13 casino hotels licensed and opened for business. Another 12 years passed before South Dakota approved limited stakes casinos in the City of Deadwood. In the general election of 1990, Colorado voters approved similar controlled stakes casinos for the towns of Blackhawk, Central City and Cripple Creek. Finally in 1992, Louisiana authorized a single, land-based non-Indian casino in New Orleans.

According to *International Gaming & Wagering Business* in 1991, land-based non-Indian casinos accounted for \$8.6 billion of gross revenue of the total casino market of \$9.7 billion, or 89 percent of the market. By 1994, the land-based, non-Indian casino market segment had grown to \$10.1 billion, a 17 percent increase over 1991 levels. However, due to the rapid growth in both the riverboat and the Indian market segments, the land-based non-Indian casino market share dropped to 62.3 percent of the total casino market.

**Chart 1**  
**Legal Status of Casino Gaming, 1994**

<u>State Name</u>	<u>Land-based</u>	<u>Riverboat</u>	<u>Indian Compact</u>
Arizona			X
California			X
Colorado	X		X
Connecticut			X
Idaho			X
Illinois		X	
Indiana		X*	
Iowa		X	
Louisiana	X	X	X
Michigan			X
Minnesota			X
Missouri		X	
Mississippi		X	X
Montana			X
North Dakota			X
Nebraska			X
Nevada	X		X
New Jersey	X		
New York			X
Oregon			X
South Dakota	X		X
Washington			X
Wisconsin			X

Footnotes:

\* Indiana approved riverboat casinos in 1993, but the first boats targeted for Gary have not been licensed.

Source: *International Gaming & Wagering Business*; October, 1994

## 2. Land-Based Indian Casinos

In October 1988, the Federal Indian Gaming Regulatory Act (IGRA) became law, authorizing Indian tribes to operate casino gambling under certain terms and conditions. The intention of this act was to encourage badly needed economic development on Indian tribal lands and to respond to the interest of tribes in using gaming activities for that purpose.

The provisions of the IGRA are complex and have been disputed in several states that contended that they were not meant to permit Indian tribes to operate casinos within their boundaries. The intention of the IGRA was to recognize the existing state role in gaming regulation by dividing Indian gaming into three classes. Two classes of Indian gaming fall under Indian and federal control. Class I games are social games conducted for prizes of minimal value or traditional forms of Indian gaming. Class I gaming is under the exclusive jurisdiction of Indian tribes and not subject to provisions of the IGRA. Class II games include bingo and non-banking card games (where players play against each other rather than the house, or bank). Class II gaming is under extensive tribal jurisdiction, but is subject to provisions of the IGRA and oversight regulation of the National Indian Gaming Commission.

Class III, or casino-style gaming (including banking card games, slot machines, pari-mutuel racing, jai alai, and electronic games of chance, such as video poker), was acknowledged to be a state-tribal issue. In general, a tribe may engage in Class III gaming in any state that allows such gaming in any form, but a state-tribal compact must be in place before the tribe may proceed. The United States secretary of the interior has final authority to approve state-tribal agreements, and generally, the governors of states act for the state in approving such agreements.

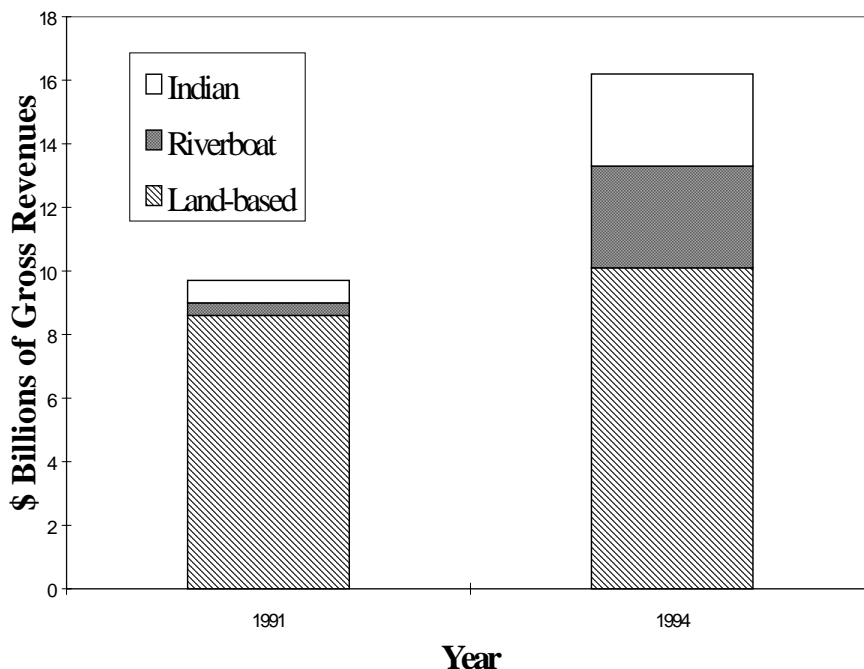
While several states have resisted efforts of Indian tribes to locate gaming facilities in their states, federal courts have essentially upheld the IGRA, particularly with respect to the right of Indians to operate any gaming activity for profit and free from regulation, as long as the state in which it is located allows the same activity to be conducted for any purpose. A recent federal court ruling held that the IGRA permits tribes to enter into compact negotiations with a state to conduct all forms of Class III gaming activity on tribal lands if the state permits any form of Class III gaming within its jurisdiction.

The effect of the IGRA has been to invite Indian tribes, operating as sovereign governments, to undertake commercial gambling activities but without the type of state regulation and oversight that exists where non-Indian gambling has been legalized. The Indian casino gaming allowed under the IGRA, and so far supported by court decisions, is not subject to state control except as agreed to in compacts. Tribal gaming activities beyond the scope permitted to nontribal entities elsewhere in the state present a challenge to policymakers who consider casino gambling contrary to the public interest.

Nonetheless, the enactment of the Indian Gaming Regulatory Act has resulted in the establishment of Indian casino establishments in 18 states since 1988. Currently, there are more than 50 Indian casinos in operation and reports that at least that number are planned in states across the nation. According to *International Gaming & Wagering Business*, 1991 gross revenues from Indian operated casinos totaled \$700 million, or 7 percent of the total national casino market. By 1994, Indian operated casinos had grown to \$2.9 billion in gross revenues, increasing the Indian casino market share of the total casino industry to 18 percent.



**Chart 2**  
**Growth in U.S. Casino Gaming Industry by Market Segment**



Source: *International Gaming & Wagering Business*; October, 1994

### 3. Riverboat Casinos

Adding to the overall growth of the casino industry has been a rapid proliferation in riverboat casinos that has taken place since 1991, when riverboat casinos were launched in Iowa and Illinois. Since 1991, more than 60 riverboat casinos have been launched and have captured 20 percent of the casino market. Currently, six states have authorized riverboat casinos: Indiana, Iowa, Illinois, Louisiana, Missouri, and Mississippi.

The first riverboats appeared in 1991 in Iowa and Illinois, and were quickly followed in 1992 by dockside casinos in Mississippi. By late 1993, the first Louisiana boats were launched which were followed by Missouri in the following year. Indiana also approved riverboat casinos in 1993. According to *International Gaming & Wagering Business*, some 20 riverboats entered service in 1992, bringing the total number of riverboat casinos to 32. An additional 24 riverboats were launched through October 1994, and another 10 new boats were anticipated by the end of 1994. Rapid growth is anticipated to continue as riverboat casino legislation has been introduced or under study or discussion in several additional states.

The rapid expansion of the riverboat casinos is evident in gross revenue data reported in 1991 and 1994. In 1991, the riverboat casinos comprised \$400 million, just over 4 percent, of a total casino market of \$9.7 billion. By 1994, the riverboat casino gross revenue exceeded \$3 billion, or 20 percent, of the rapidly expanding national casino industry.

## **B. Status of Gambling in Michigan**

The experiences of the State of Michigan with legalized gambling have been consistent with the national trend towards legalization. The State of Michigan currently authorizes several forms of legalized gaming including horse racing, lottery, bingo and charitable games. The state legalized pari-mutuel horse racing in 1933, and the constitutional prohibition against lotteries was repealed by a vote of the people in 1972. Under a federally-required compact, Class III casino gaming is permitted on certain federally recognized Indian lands in the state.

Pressure to expand legalize gaming has continued for a number of years and in August 1994, voters of the City of Detroit approved an advisory question related to the establishment of river-boat and land-based, Indian casino gaming. There were also a number of related gaming measures on the November 1994 ballot including two supporting casino gaming that did not pass, one in Flint and another in Port Huron. In addition, several Michigan communities have indicated their strong interest in entertaining proposals for casino gaming facilities.

### **1. Legal Prohibition on Gambling**

There is no constitutional prohibition against casino gambling although state law in Michigan prohibits gambling, except for licensed pari-mutuel horse racing, the state lottery and bingo games. Gambling on Indian reservations is regulated by federal law and not subject to state law or city ordinances.

An advisory opinion of the Attorney General of Michigan issued in 1975 ruled that there is no constitutional prohibition against casino gambling. The opinion pointed out that provisions in the Constitutions of 1835, 1908 and 1963 prohibited authorization of a state lottery. Lotteries were made legal by a constitutional amendment to Article 4, ratified on May 16, 1972, to authorize lotteries and permit the sale of lottery tickets in a manner provided by law, thereby removing the only constitutional gambling prohibition.

However, Michigan statutes have declared gambling of any type a crime, except for licensed pari-mutuel horse racing, the state lottery, and bingo games. Such laws have been upheld as a reasonable exercise of police power.

### **2. Indian Casinos in Michigan**

Presently, seven Indian tribes with negotiated state-tribal compacts operate eight Class III casinos in Michigan. The compacts were confirmed in November 1993 by a concurrent resolution of the Michigan Legislature, providing formal agreement between the state and the tribes for the operation of Class III gaming activities. All of the Indian casino operations are operated by the tribes. In addition to those casinos identified below, the Sault Ste. Marie Tribe operates three small satellite gaming facilities, with limited gaming options, located in Christmas, Manistique and Hessel.

**Chart 3**  
**Class III Indian Gaming in Michigan**

<u><b>Tribe</b></u>	<u><b>Casino Name</b></u>	<u><b>Location</b></u>	<u><b>Tables</b></u>	<u><b>Slots</b></u>	<u><b>Date Opened</b></u>
1. Bay Mills Indian	1. Kings Club Casino	Brimley, Mi.	8	250	1984
2. Grand Traverse Band of Ottawa/Chippewa	2. Grand Traverse Band Video Palace	Peshawbestow, Mi.	-	600	1984
	Leelanau Sands Casino	Peshawbestow, Mi.	36	250	1984
3. Hannahville Tribe	3. Chip-In Casino	Harris, Mi.	38	487	1991
4. Keweenaw Bay Indian Council	4. Ojibwa Casino	Baraga, Mi	18	200	1985
5. Lac Vieux Desert Band of Lake Superior Chippewa Indians	5. Lac Vieux Desert Casino	Watersmeet, Mi.	-	269	1988
6. Saginaw Chippewa Indian Tribe	6. Soaring Eagle Casino	Mt. Pleasant, Mi.	48	823	1987
7. Sault Ste. Marie Tribe Chippewa Indians	7. Vegas Kewakin Casino	Sault Ste. Marie, Mi.	34	800	1987
	8. Kewandin Shores Casino	St. Ignace, Mi.	55	1,500	1985

Source: Smith Barney

### **3. City of Detroit Gambling Referenda**

No community in Michigan has felt the pressure to expand legalized gambling to casinos more than the City of Detroit. Starting in 1976, the question of legalization of casino gambling has been before the voters of the City of Detroit five times during an 18-year period. The voters rejected all proposals with the exception of the most recent proposals approved in August 1994.

**Previous Ballot Questions** In 1976, the City Council placed the first gambling proposal on the ballot in response to a city financial emergency. That proposal to allow up to six state licensed and regulated casinos in Detroit, with the city receiving the taxes, was rejected by a vote of 59 percent to 41 percent.

In 1981, the City Council placed another gambling proposal on the ballot in response to another financial crisis. That proposal to allow the City Council to approve a limited number of hotel casinos, with the state and city splitting the taxes, was rejected by a vote of 63 percent to 37 percent.

In 1988, an initiated ordinance to prohibit casino gambling in the city, even if casino gambling were to be approved by state law, was submitted to the voters. This proposal was a reaction to

the report of the Casino Gaming Study Commission, which was appointed by the Mayor and used a model of twelve 1,000 room hotel casinos. The proposed ordinance prohibiting casino gambling was approved by a vote of 62 percent to 38 percent.

In 1993, the voters of the City of Detroit rejected by a vote of 51 percent to 49 percent an initiated ordinance that would have repealed the ordinance prohibiting casino gambling authorized in 1988 and authorized the City Council to approve licenses for casino gambling. This proposal followed another city financial crisis and came after the Mayor's 21st Century Committee rejected a recommendation for casino gambling.

**Proposals B & C of 1994** In 1994, two separate questions were placed before the voters in a different environment, one in which legalized casino gambling was easily accessible to Detroiters. A casino, owned by the Province of Ontario, opened on May 17, 1994, across the Detroit River in Windsor, Ontario. Currently, Casino Windsor reports a daily average gross revenue take of about \$1 million and averages 19,000 gamblers per day, 80 percent of them from the United States.

Proposal B, approved by the voters, repealed the 1988 initiated ordinance prohibiting casino gambling and authorized the Atwater Recreation and Entertainment District. That district would allow access to a permanently docked riverboat gambling and entertainment facility which is proposed to be operating 24 hours a day, seven days a week. For this proposal to become operational, state legislation would be required to authorize commercial casinos.

Proposal C, also approved by the voters, repealed the 1988 initiated ordinance that prohibited casino gambling in the city and approved an Indian casino in Greektown on land owned by the Sault Ste. Marie Tribe of Chippewa Indians. The casino could only be authorized pursuant to Federal law and with the concurrence of the Governor. Under the proposed ordinance, the Mayor and City Council would be authorized to enter into contracts with the Indian tribe for the city to provide services to the casino and be paid a percentage of the gross casino revenues. Approval of these two ballot questions, while not legally significant, does express the wishes of the electorate and is a departure from the historic position of anti-gambling.

### **III. Distinguishing the Proper Roles of State and Local Governments**

The process required to authorize casino gaming and to enact legislation necessary to regulate casino gaming is an extremely complicated task. Frequently, the goals of the state and local governments are incompatible, resulting in competition between the state and local governments in the development of public policy of casino gaming. Further complicating the task are the efforts of prospective developer/operators to influence local governments in the casino selection process, which also has significant public policy implications. Thus, without a comprehensive, cooperative approach to public policy development of casino gaming, the public sector loses control of the implementation process and must react to the actions of prospective developer/operators which may result in failure to reach the best “deal.”

#### **A. State Role**

Several fundamental elements define the proper role of the state in implementing casino gaming. The most important element is the determination of the benefits and costs of casino gaming for the state. While state officials must recognize the need for significant input from local units on this issue, local officials must recognize that the overall state policy toward casino gaming is decided by the state. Once a determination has been made to authorize casino gaming, the issue of the best way to regulate the casino gaming industry can be determined. The state is uniquely positioned to perform this role since the state has the authority to enact legislation necessary to establish gaming regulations and has experience in oversight of other forms of legalized gambling.

The state is also best situated to determine the best means to maximize the benefits and minimize the costs to the state. Clearly, for the public interest to be realized in Michigan, any new casino industry must have integrity and meet with long-term economic success. Finally, the state will need to determine the best means to distribute the benefits and share the costs throughout the state.

#### **B. Local Government Role**

Local governments have great interest in the potential of casino gaming in Michigan and will position themselves to have as great an impact on shaping public policy as possible. However, there are severe limits on the authority of local governments to make policy determinations.

There are several elements central to the proper role of local units of governments in implementation of casino gaming in their jurisdiction. Perhaps the most important role is to determine the overall benefits and costs of casino gaming to a city. In this role the city may promote casino gaming to expand the local tourist industry, to stimulate urban investment or to foster urban redevelopment. Related factors such as the location of casinos in a city, minimum size of a facility and gaming areas, and whether the facility will have hotel rooms are part of this determination and will have a direct impact on the host community. The presence of a gaming

facility will present a city with additional costs for services. The local unit is best positioned to determine these costs and to propose methods to be reimbursed for these increased costs.

The public sector goal of negotiating with the casino industry is to maximize the benefits to the State of Michigan and local units. That the state and local units have competing short term goals and different levels of authority in determining this outcome is clear. What is not as obvious are the methods that might be used to assist the state and its municipalities to recognize and understand their relative roles in this process. It is clear from the experiences of other communities that greater public benefits are derived when the state and local municipalities finally establish their respective roles.

## **IV. Regulation of Casinos**

### **A. Public Interest in Casino Regulation**

The philosophy behind public gaming regulation can be summed up in two words: honesty and integrity. Gaming regulatory statutes exist to assure honesty and integrity in casino finances and operations. Should non-Indian casino gaming be approved in Michigan, it is essential that the regulatory system designed for Michigan succeed in providing sufficiently stringent provisions to maintain the integrity of the casino industry without being so restrictive as to make the Michigan locations uncompetitive.

The public interest in gaming regulation focuses on three fundamental issues: suitability; fair games; and audit controls. Public gaming regulators need to assure the suitability of those permitted to own, operate, work in, do business with and invest in casinos. In addition, regulators need to know the source of all funds provided for the construction and other development costs of a casino and be able to track the return of such funds to investors and owners. Fair games must be assured or the public will not trust the games or participate in gaming activities. Finally, public regulators want and must be able to trace all wagered dollars to ensure that proper gaming taxes are paid on gaming revenue. It is because of these suitability, fairness and financial control demands that casino regulators in other states have been empowered to exert control over the core aspects of casino gaming and over individuals involved in casino gaming.

### **B. Role of the State of Michigan**

If casino gaming becomes a reality in Michigan, it will be critical that the state ensure that the regulatory process has integrity and that the regulatory system generates public confidence. While it is important that the state government fulfill its proper role in authorizing legalized casino gaming and establishing the statutory framework to regulate the casino gaming industry, it is also desirable to build a partnership between the state and its local governments in development of public policy for the casino gaming industry in Michigan.

Currently, there is no expressly granted statutory or constitutional power granted to local governmental units to implement gambling in Michigan. Assuming that a local unit could find some implied authority under the Constitution or state law to adopt casino gaming, it would only be able to do so to the extent that the area of gambling had not already been preempted by state statute. Thus, the state finds itself uniquely positioned to establish policy to authorize legalized gaming in Michigan and to regulate the commercial gaming industry.

Should gaming be approved in Michigan, it is in the long-term public interest of state residents for the State of Michigan to assume a lead role in the authorization process for several reasons. First, the state has the primary authority to enact enabling legislation for casino gaming. In addition, the state currently has a degree of expertise in gaming regulation relative to existing forms of gambling, including the state lottery and pari-mutuel horse racing. It reasonably can be argued that the state has access to greater resources necessary for effective control, including

broad statutory powers than local units of government. Finally, the state is further removed from the pressures inherent in casino operations than a unit of local government, which would allow the state to exercise greater independence in decisions affecting the casino industry.

If enabling legislation is to be enacted, the state should assume primary authority to regulate all aspects of the casino industry and should consider delegation to local units only those powers related to casino gaming deemed appropriate. As seen in other states, control could rest in state agencies created specifically for the task of regulating the casino industry or it could rest in an existing body, such as the state police. Representatives from appropriate local governmental units could be appointed to positions of authority within the regulatory agencies.

### **C. Major Elements of Casino Regulation**

Establishment of legalized non-Indian casino gambling in Michigan will be a very complicated effort and will require development of public policy in a variety of specific areas. The first step toward legalization would be a determination to authorize commercial casino gaming in the state. Once this determination has been made, then four threshold policy issues must be addressed by state policymakers. These issues are:

1. Establishing the form of casino ownership;
2. Establishing the permissible number of Michigan casinos;
3. Establishing suitability criteria for selection of casino operators; and
4. Establishing the regulatory framework for monitoring the operations of casinos.

#### **1. Ownership Models**

A state considering legalizing casino gaming has essentially two choices in structuring ownership and control of gaming facilities. It can either adopt a private sector model, authorizing private sector interests to construct and operate gaming facilities, or it can choose a structure of public ownership and operation.

The most typical arrangement found among the states is private ownership and operation of casino gaming under public regulation. Private ownership and operation tends to offer a wider potential for gaming facility development, where the public model tends to confine development in order not to compete with itself. Private ownership can also be limited to a single facility (New Orleans), or can be shaped to allow multiple casino gaming facilities at one location (Atlantic City), or at several locations within a jurisdiction (Nevada). Private ownership also displaces the development cost for gaming facilities that would need to be borne or shared by the public sector to private investors.

Generally, in a private ownership model, the public sector will realize revenue from a gross gaming tax, with the potential for public revenue creation enhanced by authorization of multiple gaming facilities. If the choice is to limit gaming to one or two facilities under private ownership, and thus create a monopoly or near monopoly, a greater public share can be extracted from the developer/operator in return for exclusivity.



Public ownership tends to offer limited possibilities while private ownership and operation of casinos offers a greater range of choices and greater economic development potential. Public ownership tends to confuse regulatory scope and responsibility, while private ownership more clearly delineates the private and public responsibilities, and insulates the government from criticism of the conduct and marketing of gaming.

## **2. Number of Casinos**

A second issue is that of how many casinos should be authorized and where should they be located.

A review of current practices of other states in authorizing land-based and riverboat casinos provides some examples of the different approaches used by states. Only the states of Montana and Nevada allow gaming throughout their jurisdictions. Other states limit casino locations by statute. Colorado, New Jersey, South Dakota and Louisiana casino statutes limit facilities to specific cities. Colorado limits facilities to the central business district of Black Hawk, Cripple Creek and Central. New Jersey allows casinos only in Atlantic City and South Dakota restricts casinos to the City of Deadwood. The Louisiana casino statute not only limits casinos to the City of New Orleans, it specifically designates the building -- the Rivergate Convention Center.

Among riverboat states, Iowa alone does not limit casino operations to specific waterways. Illinois restricts the total number of riverboats to 20 and specifies the types of waterways on which a riverboat may operate and excludes Cook County (Chicago) from riverboat gaming. Louisiana limits the number of casino riverboats to 15 and restricts its riverboats from specific waterways. Mississippi and Missouri do not limit the number of casinos, but restrict riverboat operations to specific waterways. Indiana authorized riverboats in certain voter-approved locations in Lake Michigan and along the Ohio River (and even established architectural standards for those on the Ohio River.)

## **3. State Regulatory Structures**

State schemes of regulating non-Indian casino gaming have evolved from the early experiences in Nevada into sophisticated systems that cover every facet of the gaming operation. Most current state regulatory systems are patterned after those that have evolved in Nevada and New Jersey, the two principal US gaming jurisdictions.

In both states, the policy behind the regulatory framework is the need to protect the lawful casino industry from criminal infiltration or influence. There are many similarities between these two state regulatory approaches, as well as some fundamental differences. New Jersey supports a highly regulated gaming industry. On the other hand, Nevada has chosen to take a more liberal view towards regulation recognizing the competitive nature of the casino gaming industry. Nonetheless, the basic regulatory framework found in these states is essentially the same and the major features of the systems are illustrative of a regulatory framework that should be considered in Michigan, should commercial gaming be authorized.

In Nevada and New Jersey, there are dual agency control systems in which the functions of investigation and enforcement of gaming regulation are assigned to one agency, while the final administrative adjudicative review is the responsibility of a second agency. As with other types of regulation, a balance must be maintained in which casino regulation must be stringent enough to ensure integrity of the industry, without restricting the ability of casinos to effectively compete.

**Regulatory Commissions** In each state, a commission (Nevada Gaming Commission and New Jersey Casino Control Commission) was established with primary responsibilities of license granting, tax collection, and auditing. These quasi-judicial bodies also have authority over a wide variety of gaming-related matters. However, regulation of the manner in which casino games operate varies between the states. Nevada gaming regulations are stringent and comprehensive in such areas as the licensing of slot machine manufacturers and distributors, the licensing of private and publicly traded corporations, pari-mutuel wagering, sports pools and wire services. On the other hand, there is an absence of regulation in the area of game odds and payoff ratios in Nevada.

New Jersey's regulatory scheme has gone further than Nevada's in an effort to foster economic development and to establish stricter control. In an attempt to affect economic development, New Jersey regulation specifies Atlantic City as the sole community to benefit from casino gaming in the state. Further, criteria for the overall design of the gaming facility including establishing minimum casino size limits and a requirement that hotels be part of the casino development are set in regulation. The intention of these provisions is to direct the benefits gained from large scale casino-hotel gaming facilities to Atlantic City. In addition, New Jersey regulates gaming odds, credit, alcohol consumption in casinos, advertising, places state control personnel on the premises, and regulates the use of casino tax revenues.

The authority to grant gaming licenses to applicants (to establish the suitability of owners/developers) is perhaps the most significant role of the regulatory commissions of Nevada and New Jersey. These commissions essentially base their decisions regarding licensing on the reports and recommendations submitted by the enforcement agencies of the two states: the Nevada Gaming Control Board and the New Jersey Division of Gaming Enforcement.

**Enforcement Bodies** Each state established an investigative and prosecutorial body to ensure the day-to-day compliance with gaming law and regulation: the Nevada Gaming Control Board and the New Jersey Division of Gaming Enforcement. The primary duties of these agencies are to conduct background investigations on applicants for gaming licenses; enforcement of gaming laws and regulation; collection of taxes; and inspection of premises where gaming is conducted or gaming devices are manufactured or sold.

The Nevada State Gaming Control Board is organized into three separate divisions: administrative, fiscal and surveillance. The administrative division performs all general administrative and clerical functions of the State Gaming Control Board and the Gaming Commission. The fiscal division conducts economic research, collects taxes, and performs auditing functions. The surveillance division performs all enforcement and investigative functions of the State Gaming Board.

The duties and responsibilities of the New Jersey Division of Gaming Enforcement are approximately equivalent to Nevada's State Gaming Control Board. The Division of Gaming Enforcement is to investigate all applications, enforce the provisions of the Casino Control Act, prosecute before the commission all proceedings for violations of the act and provide the commission with all information necessary relating to licensing matters. The Division may prosecute criminal violations of the Act and has access to a state grand jury. This centralization of authority to investigate and prosecute is not present in Nevada.

The long term impact of the evolution of effective casino regulation by the states has lead to the legitimization of the casino industry in the eyes of the public. Over the years, the unsavory reputation of the early Las Vegas casino operations has changed to one of an ever expanding element of the growing entertainment business. Indeed, the industry has undergone a name change, from gambling to "gaming," as part of a change in image. Today, the presence of large public corporations and banks and other financial institutions in casino investments reflects the shift of public opinion away from general opposition to casino gaming.

#### **4. Suitability of Owners/Operators**

In order to ensure integrity of the casino industry, a thorough and vigorous licensing mechanism will be necessary. This is achieved by establishing a licensing mechanism so that public regulators have the ability if they choose to examine every person and business that owns, operates, invests in, works in, or sells or leases to authorized casinos.

Licensing should consist of a thorough background check on each applicant's record, including any criminal activity. Generally, broad standards are established including factors that bear on an applicant's suitability including: 1) reputation for good character and honesty; 2) sufficient business skill; and 3) financial integrity and responsibility. Prospective licensees must make themselves available for extensive investigative background checks of their personal and business activities and reputations

#### **D. Regulating Casino Operations**

In addition to establishing a thorough and vigorous mechanism to license casino owners/developers, a state considering legalization of casino gaming also needs to recognize two related public purposes of gaming regulation essential to ensure the integrity of casino gaming. First, adequate control and accountability of gaming revenue and assets to ensure an honest reconciliation of revenue for tax and other public purposes. Second, to ensure fairness and integrity in the games.

Detailed base expectations must be written in control systems to establish minimum norms of business activity and behavior. Deviations from the norm will alert both the private owner/operator and the government to potential or real violations of the gaming control code. Enforcement of the gaming control code will assist in the maintenance of honesty and integrity in all aspects of the gaming operation.

## **1. Licensing**

Licensing should be required for all persons and organizations capable of directly or indirectly affecting the industry. Experience in Nevada and New Jersey indicate that particular attention be given to the licensing of unions, vendors and junket operators. The basic premises that should underlie the licensing system are: 1) a license constitutes a revocable privilege, not a vested right; and 2) the burden of proof for providing evidence of qualification for a license rests upon the applicant. The closer an applicant's responsibilities lie to direct casino operations, the more extensive should be the scrutiny.

The heart of regulating the casino business is the licensing process. State authorities are given broad discretion to issue licenses to categories of persons engaged in casinos and ancillary operations. States establish mandatory suitability and disqualifying criteria, and grant the agency broad discretion beyond these mandatory criteria. Some states specifically mandate licensing for all categories of applicants while other states explicitly require only some applicant categories to be licensed, delegating other licensing to the discretion of the regulatory agency.

The regulatory systems protect the integrity of gaming operations principally by background investigations of prospective licensees. All of the states provide for background investigations as part of the licensing process for different actors in a casino operation. Typically, a state will require licensing of the owner or operator of a casino, key management employees, gaming employees, and manufacturers and distributors of supplies and equipment. However, significant variations exist in the breadth of licensing and the extent to which statutes mandate a licensing process as opposed to authorizing the administrative agency, in its discretion, to require a license.

## **2. Operational Controls**

As suggested in the prior discussion of regulatory frameworks available to the state to monitor the casino gaming industry, there is wide variation among the states regarding operational controls of the games offered in casinos. A brief review of similarities and differences is useful as the State of Michigan contemplates legalization of casino gaming.

There are a number of operational restrictions applied to casino gaming that are part of the regulatory framework found in the states that have authorized legalized gaming. These factors include restrictions on the hours of operation, minimum age limit of patrons, maximum limits on bets and loss limits, minimum slot payout ratios, limitations on credit, and whether a patron exclusion list is maintained.

Of the ten states that have authorized commercial casino gaming in the forms of land-based and riverboat casinos, all impose an age restriction on gambling patrons. Generally, the age limit is 21; however, Iowa and Montana have established an age limit of 18. The next most frequently used restriction is the exclusion list which is present in all the states with the single exception of Montana. The exclusion list is an official list of patrons that are excluded from the gaming premises due to a criminal record or other undesirable background factors.

Minimum slot machine payouts is the next most frequent operational restriction, found in five of the ten states. Of the states with land-based casinos, only Nevada has not established a minimum payout for slot machines. Among the riverboat states, only Missouri has established such minimums. Bet limits are imposed in four of the ten states, Colorado, Iowa, Montana and South Dakota, and loss limits are present in only two states, Iowa and Missouri.

### **3. Regulatory Costs and Fees**

Experience in other states shows that effective regulation of casino gaming is very costly. A standard approach used in other states is that the costs of regulation be borne by the casino industry. Application fees, license fees, license renewal fees and other fees should be set so that the sum total of the fees pays for the costs of the regulatory agencies.

### **4. Enforcement Powers**

Generally, state regulatory bodies utilize a wide range of investigatory and enforcement powers to ensure integrity of regulatory framework established to monitor the casino gaming industry. Should casino gaming be legalized in Michigan any proposed regulatory scheme should consider empowerment to do the following:

1. Investigate violations of statutory and regulatory provisions;
2. Initiate civil and criminal proceedings before administrative tribunals and courts of law;
3. Conduct continuing review of casino operations; and
4. Perform casino audits.

In fulfilling regulatory responsibilities, state regulators must be vested with all powers not inconsistent with the State and Federal Constitutions. Examples include having access to broad use of subpoena powers and the authority to conduct search and seizure on gaming premises. Authority for electronic surveillance and the sharing of police information with federal offices and officers in other states should also be considered.

Finally, extensive provisions should be considered which establish a wide range of conduct including unlicensed operations and employment, cheating and skimming. Sanctions should be included for proscribed conduct that could include fines and imprisonment. Regulators should have authority to establish remedies best suited for a violation including authority to revoke, modify or suspend a license; assess civil penalties; enter cease and desist orders; and issue letters of reprimand and censure.

## **V. Local Government Interests and Key Issues**

### **A. State/City Concurrent Interests and Concerns**

State government has the exclusive power to authorize and regulate casino gaming. Local government, therefore, has a direct interest in any state action that permits gaming in local venues. State authorization to conduct casino gaming will result in increased costs to any host city in the form of increased services to the casino and its customers. The manner in which state legislation is drafted will also affect the economy of the city and its ability to maximize the economic benefits of gaming. City government can achieve both benefits and protections through state actions.

Conversely, if the state and its municipalities do not act as partners in decisions related to gaming, local governments may lose the ability to shape these new venues in a manner that will help achieve economic revitalization in their communities. If local government is placed in a position where it can exercise only local governing power, such as zoning and permitting, to gain some control of the decisions regarding gaming, it has substantially diminished its capacity to achieve local objectives. Where local policy conflicts with state legislation, local government can only resist and limit, not change; and its only tool comes in the form of zoning and land use restrictions.

There are six principal issues that city governments seek to resolve through state casino legislation:

1. Reimbursement for increased costs of city services;
2. Participation in the recurring revenue paid to government by the casino;
3. Policies governing the number, size, type and statewide distribution of casino locations, both within the city boundaries and the surrounding economic market served by the city;
4. Mandated resident employment and open access for disadvantaged and minorities (including vendor preference);
5. Policies to promote new businesses and protect existing businesses; and
6. Social programs for problem gamblers.

In the following sections, each of these issues will be addressed.

#### **1. Reimbursement for increased cost of city services**

Unlike traditional open market business enterprises, casino gaming exists solely as a result of state authorization and is not a universally favored industry. Cities benefit from job creation, but are also burdened by the incremental cost. There is a rational basis for the state to adopt laws to ensure that the city government is paid for the incremental increased costs occasioned by a state-authorized casino. In such cities as Atlantic City and New Orleans where state government has authorized casino gaming, the state has also recognized the direct impact on city services and has mandated compensation. To ensure the license to operate, the industry is willing to pay.

Historically, it is not the principle of reimbursement that is typically at issue in the state debate, but the amount and the procedure to verify it.

The procedure to determine the incremental payments requires a policy and a mechanism that assures both the city and the state that the amount is accurate and fair. The three methods most commonly used are: 1) computation of an annual sum by the city, subject to state verification, 2) determination of a fixed sum, subject to periodic adjustment, and 3) a percentage of the gross win from the casino.

Many local governments have policies that identify and mandate "development impact fees." These fees are designed to require new developments to pay for increases in costs to the city for services necessitated by the development. The concept has been expanded in its application to casino development. Due to a variety of factors unique to casinos -- special licensure requirements, the large amount of investment in these developments, accelerated development timetables for opening, the unique and largely unquantified impact of a casino in a community -- the industry has been willing to accept the imposition of costs that exceed normal "impact fees." For example, operators have been known to fund a wide range of public safety activities, from increased police manpower to specialized crime units and on-site and off-site security units. In addition, casino impact fees support improved street lighting and beautification, sanitation and waste removal, city finance and treasury activities, legal department expenses, and other local government functions potentially impacted by the casino. Casino operators also fund specialized monitoring, planning and evaluation of casino impacts.

Timing of the receipt of funds is also a critical issue. The city will incur costs prior to the opening of the casino. These costs are related to planning and preparing both public infrastructure and personnel to meet the increased demands directly related to the casino. As few cities are able to carry these increased costs within their operating budgets, the city will need to receive reimbursements in advance of, or simultaneous with, incurring the costs.

## **2. Participation in the recurring revenue paid to government by the casino**

The principal motivation for state governments to authorize casino gaming is to create a new source of state revenue. A 1995 report, *Economic Impacts of Casino Gaming on the State of Michigan* (Deloitte & Touche LLP), estimated the market for gaming to be about \$1 billion per year. States receive revenues from a casino for granting it a license to operate. States have also authorized gaming to create jobs and economic growth, to increase private investment, and to maintain a competitive position for conventions and tourism within the state. The principal reasons for state resistance to casino gaming are moral concerns, quality of life issues, fear of increased crime, potential for corruption, and business competitiveness issues.

The most direct impact of a casino is felt by those in the city in which the casino is located. Thus, it is reasonable to expect the city government to receive direct revenue from the casinos affecting its citizens, above its costs. Historically, states have been resistant to sharing direct revenue with political subdivisions. A balance of interests is at issue, and the state does have the exclusive authority to license casino gaming. The city government alone is not in a strong position to bargain for this revenue. Unless the legislators representing the city have the will and

voting strength to require direct city participation, the city government will have only its powers of limitation or exclusion to leverage in negotiations for its fair share of new revenue.

In states with casino gaming, if there is a direct revenue sharing between the state and the city, the percentages favor the state, at a ratio of about 4 to 1. Typically, the means for sharing recurring revenue include: 1) a fixed direct annual payment to the state and city, and/or 2) a percentage of gross win, payable periodically, but computed annually.

A review of current practice reveals two ways in which the amount of revenue to be paid to state government has been established. The first states to license gaming (Nevada and New Jersey) instituted a license fee for doing business, similar to other business licensure practices. The state determined the amount the casino must pay to secure the privilege to operate. The state also regulated the number of licenses to be given out, creating the opportunity for a limited monopoly. In these states, the fees were not instituted with the sole intent of maximizing state revenues. From the 1930s until 1990, casino gaming was called gambling and was perceived largely as a regulated evil. The fee for licensing a casino in Nevada and New Jersey was 6 to 8 percent of the gross win. In these states, state government revenue was increased by granting additional licenses, not by raising the fees. Decisions about the granting of additional licenses were driven by requests from suitable operators, who were in turn responding to perceived increases in market demand.

The recent wave of casino growth has revolutionized the fee structure. States are now seeking to increase state revenues through their involvement with this new industry. The object is to extract as much revenue as prudent from the gaming operators, up to that limit in which such extraction becomes a barrier to market entry. Simply put, government wants more of the profit in exchange for the right to operate a casino. For states seeking to balance their budgets or provide tax relief to individuals and businesses, while at the same time creating hundreds of entry level jobs, the casino industry is very attractive. The "magic number" that approaches the sum the casino will pay to operate in any given market at any given time under competitive conditions is not easily determined by government statisticians, operators or economists. However, an 8 to 10 percent share for government does not appear to approach that number.

In Europe, the casino industry is structured differently from American land-based and riverboat casinos. There, a gross win fee of 40 to 80 percent is common. American casinos operate on a different, and more intensely cost competitive model. Even with these economic constraints, casinos continue to demonstrate a willingness to pay at least double the 10 percent fee common prior to 1990, as well as additional costs and benefits, in a limited monopoly marketplace.

For example, in 1990 the state of Louisiana passed a limited monopoly for fifteen riverboats, with limited geographic distribution and limited size. The state arbitrarily charged operators 18.5 percent of gross win for the state and \$2.50 per head to be paid to the host city. That bold step to double the prevailing fee-based rates could have proven to be too aggressive. The applications for licenses exceeded the number to be authorized by nearly 3 to 1, even though the application process costs an average of \$750,000 to prepare and file.



In 1992, Louisiana also authorized a single monopoly land-based casino in New Orleans at a site owned by the city. A bid process for a license to operate at that site was established, with a guarantee of \$100 million per year, against a minimum bid of 18.5 percent. The winning bid was \$125 million per year, against a sliding scale of up to 22.5 percent of gross win. Likewise, the city of New Orleans held a worldwide competition and secured \$15 million per year, plus up to 7 percent of gross win, and a 5 percent participation in net income and other benefits. The message for the state and the city is simple. The industry can and will pay more under certain conditions. The message for local government is that the state may not be willing to permit the city to share in revenues above a threshold percentage.

In contrast, Mississippi adopted an open market policy, at a fixed fee of 6 percent for the state, and percent for the city, for an unlimited number of dockside "riverboats" (no sailing required). The desire to attract immediate investment worked, and the market is now saturated. The centers of gaming activity in Mississippi and Louisiana are only 40 miles apart, and they share some of the same market area. The difference in approach between these two states will result in interesting case studies in the years to come. The lesson learned from both approaches is that the industry is not deterred by government-imposed fees, if it perceives high profit potential in the marketplace.

### **3. Policies governing the number, size, type and statewide distribution of casino locations, both within the city boundaries and the surrounding economic market served by the city**

The number, size, type and distribution of casinos is determined by state statute, and thus within the exclusive jurisdiction of state government. However, cities have intense interest in the economic impact of that state policy upon their ability to maximize the local benefits of gaming. If the state policy is non-protective of the city economy, then the city can become a victim, and not a beneficiary. The city and the state may not have the same policy goals or economic development objectives, but clearly, the state does not prosper if the city's local economy is further drained, rather than enhanced by casino gaming.

Some states have authorized unlimited casinos and left growth to competitive market forces. In other states, legislation authorizes a specific number of casino licenses, and may specify site-specific casino locations. The concern for local government is how mandated sites or numbers of casinos in and around the city impact local economic development within that city. If the state approach is not supportive of or consistent with city policy, then the city has limited recourse. The city has the exclusive authority for local zoning and permitting. That authority can be used to limit or even exclude mandated sites by refusing to approve casino land use. It can also be used to so limit development as to render it economically infeasible. The city cannot create a casino, but may be able to stop it. However, having to take this position results in an economic loss to the city of any casino benefits.

The city has an interest in ensuring that the state action accords the city the opportunity to realize gaming's economic development potential for the city. The state, in turn, has an interest in ensuring that the maximum benefits to the state will be realized through regulation of the location, size and number of authorized casinos. If state and local officials are able to work together in policy development, both stand to benefit from the outcome. The following are

examples of state/city coordinated approaches to gaming regulation that recognize the legitimate interests of both parties:

1. State selected site-specific authorizations, subject to city approval;
2. City selected site-specific locations, subject to state approval;
3. Non-site specific locations, but limited as to number and casino size and subject to city approval, state approval or both;
4. A bid process with state approval, a bid process with city approval, or a bid process with both state and city approval; or
5. Unrestricted casino locations, subject to state licensing only, or subject to state licensing and city approval.

Typically, casino operators do not want a competitive bid process. They seek direct access to governors and mayors to secure support for their proposal before state and city policy decisions have been made. This is currently occurring in Detroit. The operators will assemble land, assemble partnerships, prepare extraordinary development plans, and seek negotiated approval to be enacted into a state selection process. The executive branch and often key members of the legislative branch are brought into a negotiation to respond to a proposal. The legislation and authorization follow the selection of an operator. There is no open process for bid or competition.

By contrast, both New Orleans and the state of Louisiana utilized a bid process in selecting an operator for the state's only land-based casino. The state controlled access to the operating license, and the city controlled the only land-based casino site in the state. Unfortunately, there was no city/state coordination of the bid activity. It could be argued that this diminished the negotiating power of both governmental entities. There are no examples of a state joining with one of its local municipalities to first determine the policy requirements and economic potential for casinos, and then conducting a coordinated bid solicitation process, where a certainty exists regarding the limitation of the market and the unity of selection. Were that process to be used, it offers the potential to realize a bid even higher than the combined 30 percent achieved in New Orleans.

Regardless of the method of selection of an operator, Detroit has a special need concerning site location and distribution. It must protect its economy from border pressure. Detroit has already experienced the impact of the temporary casino in Windsor. Detroit and Michigan dollars are flowing across the river with little or no return to the city or state economy. In recent years, Detroit, like many other urban areas, has experienced a decline in population and an economic disinvestment. Outmigration has become the pattern for those economically mobile. Casino gaming near, but outside Detroit city limits will further induce outmigration of dollars and jobs. This is a problem the city and state can prevent.

The city has a direct interest in ensuring that the geographic distribution of casino locations in Michigan, outside of Detroit, are not within Detroit's economic market area. There are two levels of risk: 1) casinos outside Detroit will take part of the Detroit market and economic base, and 2) casinos outside Detroit may have a market advantage that will render the Detroit casinos non-competitive. Among the ways the state might ensure that the city has a net economic gain from casino gaming are to: 1) locate casinos in Detroit and not locate casinos surrounding

Detroit, 2) locate casinos in Detroit and limit the number and size of casinos surrounding Detroit, 3) require casinos that are located in the Detroit market area, but outside Detroit city limits, to contribute to Detroit city government to off-set the economic outflow.

#### **4. Mandated resident employment and open access for disadvantaged and minorities (including vendor preference)**

The principal non-revenue reason for gaming is economic development. Economic development impact is measured by net new jobs and investment for both the state and the city. State and city employment goals are a proper condition for granting the right to operate casinos in Detroit and in Michigan. There are at least two means of job creation, and two classes of policy considerations.

Securing jobs for state and local residents and attracting new resident workers is a goal of economic development. With the power to license, resident employment is a policy that might be imposed both for employment of state residents for all casinos in the state as well as city residency for casinos in the city. If the state enabling legislation provides adequately for city as well as state residency, then the city needs may be satisfied. If not, the city may have the authority to impose their own regulations through city-controlled portions of the selection processes and procedures for operators and sites, assuming these are consistent with state legislation. Careful consideration should be given to the extent to which it is realistic to impose prior residency requirements on an industry that has not previously existed in the city.

In some instances, cities and states have chosen to mandate minimum levels of worker benefits, including health and day care. State and city policies regarding a drug-free workplace can also be required. Both the city and the state may have policies for improving access to employment for disadvantaged and minority workers.

Jobs and economic development also occur through the purchase of goods and services by the casino. Both the state and the city have an interest in vendor preferences for state and city businesses. The state legislation can recognize and establish regulations and policies for both. Likewise, the city may have the independent authority to mandate preference under some selection options.

In contrast to other competitive industries where states and cities must aggressively bid to win new jobs, the casino industry will pay for the initial right to operate. At the time of selection, and only then, in order to win the right to operate casinos in the state and in the city, operators can be mandated and will be willing to provide additional economic development benefits to both governmental units. Types of direct payments include: fixed guaranteed annual payments, percentage of gross win, percentage of net income, bonus or up-front payments and direct payments to various agencies, or the sponsorship of various projects or programs. A "redevelopment" or "investment fund" can be established and administered separately from the general fund, to enable the city and/or state to achieve economic development goals. These direct payments can be mandated for statewide benefit or targeted to a specific city or zone within the city or state.

Operators may be mandated and should be willing to provide the state and/or city with additional funding and commitments for projects and improvements, both on and off-site. These may be directly related to the casino enterprise, but can also be of "general benefit" to the community unrelated to the casino. Among the types of projects included in this category are infrastructure improvements normally funded by the state or city, acquisition and rehabilitation of properties or buildings within targeted areas of the community, the development of affordable housing as well as housing to attract new resident employees of the casino.

## **5. Policies to promote new businesses and protect existing businesses**

The city has an interest in protecting its existing businesses and its business climate. Some states have enacted specific prohibitions or limitations for casino-related enterprises to aid in the growth of non-casino support businesses. These limitations are not without controversy. The operator prefers to have a self-contained site and provide for all of the needs of his customers. Examples of the contained casino environment have been viewed differently by planners and economic developers with mixed results. Those contained environments that have attracted more visitors, like the newer properties in Las Vegas, are lauded. Those contained environments that have captured the customer and provided no additional attraction or benefit are seen as disastrous to the local communities. The corridor Boardwalk in Atlantic City is a good example of the latter. Among the businesses that are often cited for protection are local restaurants, lodging, meeting halls and convention centers, specialized transportation, retail and entertainment venues.

Both the state legislation and city zoning regulations can be used to establish public policy on these issues. The operators and governmental units will be concerned that regulation and limitation may also render the casino at a competitive disadvantage with other casinos in the market area. The extent of impact and concern about these issues is largely a function of existing market strength and commitment to policies that support and encourage new growth policy. For example, if the state and the city desire to increase the appeal of Detroit and Michigan as a convention or tourism venue and there is an insufficient supply of hotel rooms or meeting places, then public policy can permit or require casino investment in such businesses. If existing providers can absorb the growth and benefit from market expansion, then limitation on casino operator involvement in these ancillary businesses may be appropriate.

## **6. Social programs for problem gamblers**

Problem gamblers are a state as well as a city problem. The advent of a casino in any community brings to public consciousness social problems that exist in all communities. It further presents the community with an opportunity and resources to address the problem proactively. Many of the current citizens of Detroit can benefit from this assistance, and many of those who need help may well become Detroit residents. The state act should ensure that the operators of casinos have the responsibility to support counseling and social service programs to address this problem.

## **B. Local Development Issues**

Within limits, the city has the right and responsibility to regulate the site, size and scope of the development occasioned by casinos within its jurisdiction. In reality, many of the factors that affect the extent of the development and subsequent regulation, may be preempted by the state act. Thus, the potential for a city/state conflict is created. To the extent that such conflicts can be eliminated, or minimized, both state and city governments stand to benefit. This reduction in conflict also assists in creating a reasonable regulatory environment in which the casino operators can function, giving assurances to those who will be providing the significant investment required for casino developments.

Unless regulated through the state act, the city will have the opportunity to determine or influence the physical development and economic impact of the casino. The state may permit a process that calls for city involvement in the determination of a casino site. Even without enabling legislation, the city maintains the ability to exercise its prerogatives related to land use and development.

The tool for local government involvement is zoning and land use regulation. The objective should be to maximize the economic development potential of a casino development. Rather than creating enclaves of casino operations, most cities desire to use the casino attraction and investment to improve the local economy and positively affect the surrounding environment. The issues and options are complex and, because of the huge amounts of investment and activity involved, have the potential for substantial and longstanding impact.

### **1. Site selection**

If the state does not mandate a site, then the city will have exclusive authority to determine where casinos may be located. The city may choose to accept proposed developments from operators and create a "permitted use" or "casino zoning" district. The city can also opt to select its own site or zone, and authorize casinos only in that area. The city may permit operators to compete for the right to operate, including the site and development plan as part of the bid process. One of the most critical decisions a city may make is to determine whether the economic development and investment impact of a casino is to be used to revitalize a depressed area, or to further enhance an emerging growth area that may have some supportive infrastructure and associated entertainment attractions already in place. The former may have a greater incremental impact for the immediate area, but the total impact may be greater in an emerging area because the investment risk will be less and the growth potential may be greater. Site selection is the single most important decision that will shape the impact of the urban casino.

There is also another factor in the urban casino site selection process -- business climate. Resistance to locating casinos in the areas of the city with heavy concentrations of office workers and company headquarters is likely. Whether the impact of a casino on business is actually negative or only perceived as negative is irrelevant. As with many business climate issues, perception is reality. Unless and until perceptions change, this is an issue with which governmental leaders must grapple in determining the casino location.

## **2. Attraction of associated development**

Will a particular casino at a particular site attract additional economic development to the area? Some economic development professionals suggest that, like other large scale, high volume developments, "build a casino and they will come." They will come not only to the casino, but to the surrounding area to eat, to sleep, to party, to live and to work. Some have suggested specifically that the Windsor casino would result in a rush of spin-off development in Detroit, as well as in Windsor; that Detroit could get the benefit without the evil. To date, there is no evidence that this has, or will, occur.

The casino industry has flourished through use of the concept of a self-contained venue to "capture" the customer. "They play where they stay" mandated hotels were an essential element of the successful casino in Nevada and New Jersey. These mega-facilities now cater not only to the gambler, but to the entire family. They provide lodging, restaurants and entertainment, all on-site. This type of casino operates on a market theory similar to that of the large theme parks. They strive to meet all of the customers needs, and take all of their money, by providing whatever they desire -- slot machines, Tomorrowland, rides, gifts, golf courses, concerts and elaborate stage shows. But all of the money is spent on their property. The total casino development with all amenities in a mega-facility may result in the greatest return to the casino and may also be the greatest attraction for market share, investment and job growth. As a result of its success, it may represent the greatest potential for payment of fees and revenues to the government.

Conversely, the greatest incremental economic impact may be realized by adding a casino to the existing city economy and creating the associated business opportunities off-site and through local enterprise. This spreads the economic opportunity and the wealth -- as well as the control of that wealth and opportunity -- more evenly throughout the community.

Another factor to be considered is the impact of rapid induced growth versus market driven slower growth. Off-site development, not directly part of the casino development, will be market driven, and thus slower to develop. Mega-development owned, operated and financed by the casino can be mandated in advance of natural growth.

The city has a high stake in making the correct planning choices. One factor often overlooked until the end of the process is the ability of the developer to secure financing. Lenders are not risk takers, even in the casino industry. A well-positioned site and mega-development will be easier to finance through casino revenues than a pioneer urban revitalization project.

## **3. On-site infrastructure improvements and requirements**

The economic model for any casino requires the requisite infrastructure to accommodate, attract and keep the customer. The relationship between the customer market and parking, traffic and transportation issues are the most important limiting elements for any casino development. They also have the greatest potential impact on the city's ability to function smoothly.

Local governments can mandate that the casino create a master plan for its current and future development, specifically requiring it to plan and fund adequate public infrastructure, including transportation and parking. Not so readily apparent, but equally important, is the need to require the casino to provide for adequate utility, water and sewer service for the development, without the local government incurring additional costs.

#### **4. Off-site infrastructure improvements and requirements**

The casino may or may not be projected to have an impact on the surrounding area. Planning and zoning is an effective tool to evaluate land use issues, transportation issues, and growth policy with the addition of a casino in the area. Zoning and land use requirements in the casino area, if restricted to the casino site alone, can have unpleasant consequences. In an otherwise depressed area, a casino zone with a full service mega-development can not only focus huge investment on the casino site, but can also create a dead zone around it, with no potential for development. There is no impetus for the surrounding property to be developed, awaiting a "me next" windfall from anticipated acquisition by the next casino expansion. Property values in the immediate area tend to become inflated, having the undesired effect of stifling spin-off development. Atlantic City suffers from this phenomenon. On one side of the street is the casino property with high value. Across the street, unrealistic expectations have resulted in artificially inflated property values, without an economically viable use.

#### **5. Zoning to permit and prohibit**

Land use planning and zoning contemplate a master plan for a city that identifies the areas of the city where certain kinds of development are permitted. If local planning had envisioned casinos on riverboats or on land, then arguably the sites for casinos would already be part of the existing land use policy. This is not the case. With the rapid expansion of casino gaming, local governments will need to establish new zoning regulations for casinos on water or land.

More often, the proposed casino site has been determined by another process and the zoning regulations follow. Zoning procedures are widely varied and peculiar to each local jurisdiction, but the basic principles underlying use are similar. Once the casino site, zone or district is drawn, then the criteria for development both on-site and in the surrounding area is defined. Some cities use text definitions with a zoning classification to permit casino use. Others create special casino districts. Associated land uses, such as hotels, restaurants, entertainment venues, theaters and parking garages, are established. Many of the casino operators' economic development commitments, made to gain selection, are embodied in the zoning law.

In addition to permitting casinos in certain zones, many cities have likewise expressly excluded casinos from other zoning classifications. Cities that desire to further restrict and deter later casino expansions, expressly prohibit casinos in all areas of the city, except the adopted zone. New Orleans even adopted a city charter revision to limit its land-based casino to one site.

As important as the zoning and land use regulations are to establish development boundaries for a casino site or a casino district, equally helpful is an assessment of land use, development, traffic and design issues that prohibit or restrict undesirable development. Pawn shops are

probably not a preferred use, but will be economically viable and supported by problem gamblers if not prohibited. Detroit can learn from the experience of other local governments in this regard. Many have found the need to adjust prohibitions in surrounding land uses, but often after the damage has been done.

## **6. Operator and site selection process**

Depending on the decisions that may be preempted by the state legislation, the city has a direct interest in the process leading to the selection, as well as the actual selection of casino developers and sites. The potential for conflict between state and city policy is greatest prior to the actual opening of a casino. Once the sites and developer/operators are selected, then the city is left with a regulatory, rather than a policy-making role.

If the state allows the local government to have a voice in the site selection process, then the city has many options to implement policy and enhance the direct benefits to the city. If the state were to designate property owned by the city, then the city has an entirely new set of rights to negotiate benefits and shape the development. The premier example of this process is the world's largest casino, to be built in the heart of downtown New Orleans. The Rivergate site, the outmoded convention facility, was designated as the monopoly land-based casino site. To the dismay of the state, the city took a very proactive approach, soliciting proposals worldwide for a lease on the site, in advance of the state initiating the licensing process. The city was able to secure direct revenue benefits in terms of direct lease payments, up-front bonus payments, net cash flow participation and percentage rent. As landlord and not as the city, the city/landlord was authorized to negotiate a contractual open access plan for employment and vendors, and to establish local residency requirements in excess of state mandates. The enforcement and assurance of performance by the tenant is effective because a default can be a breach of valuable lease, as opposed to a violation of policy subject to penalty. Even if the city does not currently own the casino site, the state may permit the city to require that the casino operator donate the site to the city, and permit the city to negotiate a leaseback.

If the state designates only the size and number of casinos within the city, the city has several options it can pursue to participate in the development process and impose its economic development policy. In most jurisdictions, the city will be presented with "done deals" by developer/operators and be requested to approve the site and the development. The state will license its approved operator, conditioned on securing a land site or berth for riverboats. Thus, to complete the licensure process, the developer/operator must have both a site and development plan acceptable to the city.

The city may opt to open the process by calling for a "request for proposals." It can designate certain property as the site or zone for casinos and require the operator to secure property and propose a plan. The city can leave the proposals for sites entirely up to the proposers, or it can establish proposal requirements with very specific criteria. As a third option, the city can permit the proposers to make a best offer, without indicating minimum requirements, in the hope of inducing higher and more creative bids. In response to border pressure and the current loss of revenue and market growth inside the city, the state and the city can even consider permitting a



temporary casino development as a separate proposal or as part of the permanent casino development.

Based upon the experiences in other cities, the types of benefits that the city can set forth as selection criteria include the following regardless of the process for selection, whether negotiated bid, minimum requirements bid or open bidding:

1. Recurring direct revenue payments to the city;
2. Other forms of payments to government, such as up-front bonus, revenue sharing; cost reimbursements;
3. Site and development plan;
4. Financial capacity to perform;
5. Time required to open;
6. Resident employment commitments;
7. Open access plan for employees, vendors, and contractors;
8. Cost reimbursement for government increased services;
9. Mitigation of social impacts of gambling;
10. Commitments for reinvestment and redevelopment;
11. Employee training and career development programs;
12. Specific additional public projects or programs; and
13. Associated economic development impacts.

## **7. Special issues for the urban Indian casino**

Michigan has experience with Indian casinos on reservations, and has a compact for other Indian casinos that may be off-reservation land held in trust. The issues of state/Indian regulations are governed by those agreements. The issues for an "urban" Indian casino may have some notable differences. The Indian off-site or land-in-trust casino can create some specific legal and planning issues for the city. Unless there is an expressed contractual requirement the Indian casino may not be subject to city land use regulations. If this is the case, the city may have its hands tied, even in the face of potential adverse impacts. The Indian casino is normally a finite parcel of land held in trust. There is not necessarily sufficient infrastructure to serve the site. There is no guarantee that the site meets economic development goals and is located where off-site development can and will occur. There is no guarantee that the traffic and transportation infrastructure serving the site can accommodate current and future expansion needs. The city may be powerless to ensure that these and similar issues are resolved.

In addition, the nature of Indian proposals deals with limited land area, not subject to expansion by private or non-Indian enterprise. The site limitations may create development problems for the city that lessen potential spin-off economic development benefits, and may create limitations to the market competitiveness of the project. For example, if the urban site has size limitations, casino development may, by necessity, be vertical rather than on one level. Many in the industry still believe that multi-storied casinos are not economically viable, although a number of the new land-based and riverboat casinos are multi-level facilities. Whether this style of casino can survive in the highly competitive marketplace remains to be seen. Indian land-in-trust casinos may also face more problems if they chose to expand than their non-Indian owned competition.

Further, if a site is chosen that does not have the surrounding infrastructure to accommodate increased economic development, then the spin-off development potential of gaming may be lost or substantially reduced. Finally, there is the issue of market competitiveness of Indian casinos versus non-Indian casinos in the same economic market. Will Indian casinos be able to compete effectively with an urban resort destination casino?

Timing, as it relates to the opening of a casino in the marketplace, also becomes a factor. In most jurisdictions, an Indian casino development will take longer than riverboats or land-based non-Indian casinos, due to the mandated federal approval process. In Michigan and in Detroit, the opposite may be true. It seems more likely that an Indian casino can be authorized and developed faster than a non-Indian casino, due to the existing compact and approvals. A non-Indian casino development will require state legislation. If Detroit and Michigan desire to accelerate casino development to begin to capture some of the dollars currently flowing to Windsor, then the Indian casinos may offer that advantage both in Detroit and elsewhere in Michigan.

#### **8. Policy, process and procedures for monitoring issues of casino expansion or reduction, modification or termination**

Once the state has authorized a casino industry, the state will be forever in the process of regulation of operations. Once the city has operating casinos as part of its economy, the city will be affected by the growth, expansion or reduction of the casino market. There are both development and social impacts. There are traffic and transportation issues. There are competitive and non-competitive business conflicts. The city has the greatest opportunity to ensure the right to monitor and demand resolution of social and physical planning issues before the first casino opens. Once the casino is licensed and operating, the city as a regulator has diminished power to mandate corrective actions by the casino owners. The city can best negotiate a procedure for modification, expansion and even termination only in the beginning. Thereafter, any city-mandated actions that may not be accepted as necessary by the casino will be resisted.