
12 Gambling policy: overview and assessment framework

Box 12.1 Key messages

- Transparent processes, careful attention to policy design and evidence-based choices among competing options are the keys to good policy.
- Governments have not always provided clear rationales for gambling policies.
- Some apparent objectives for, and outcomes of, policies do not have a strong *prima facie* basis — in particular, exclusivity arrangements, economic development, and measures which support particular groups or activities within the gambling industries.
- Policies often appear to have inconsistent objectives and variable application, illustrated by the use of strong probity controls in some gambling modes and their absence in others.
- The goal of revenue generation can have a distorting influence on policy. It is unlikely that the gambling regulatory environment would look like it does without the understandable imperative for states to meet their tax revenue needs.
- The two objectives providing the strongest rationale for special gambling policies are to ensure probity and to reduce adverse social impacts.
- The principle of consumer sovereignty and choice is important when devising gambling policy, but it does not mean that there is no role for government in trying to alleviate the harms from problem gambling.
- The overarching goal should be to maximise the welfare of the community as a whole. Measures which can reduce the social harms of gambling while maintaining the benefits find particular favour under this approach.

12.1 Introduction

The gambling policy environment is complex. It involves a highly elaborate and, at times, clashing set of arrangements for taxing and regulating the industry as well as for remedying its harmful side-effects.

This complexity reflects:

- the multiple jurisdictions and institutions involved in policymaking and administration;
- the variety of gambling modes, from racing (in all of its forms), casino table games, gaming machines, lotteries and more minor forms such as bingo, keno, and community gambling;
- apparent ambivalence in public attitudes to gambling;
- tensions between different policy goals of government; and
- the historical sequence of deregulation.

As the CIE observed:

To some extent the ‘heavy hand’ and the rich detail of regulation is a consequence of the relatively quick transition from illegal activity to legal activity. It is also shaped by the lingering perception that gambling is immoral. The large quantity of legislation can also be explained in part by the numerous moves by government in recent years to increase gambling opportunities. The current body of legislation reflects these seemingly contradictory motives to tightly control gambling, while simultaneously liberalising its availability (1997, p. 21).

Part D of this report contains a detailed examination of policies — current and potential — for regulating the gambling industry. In responding to the terms of reference and in line the requirements in the *Productivity Commission Act 1998*, the Commission’s primary aim is to identify any changes to present policy settings and institutional arrangements for gambling which could enhance the wellbeing of the community as a whole.

To this end, the Commission has used a broad framework which takes account of community wide costs and benefits. A key element of the framework is its clear delineation of the reasons individuals and markets left to their own devices may fail to maximise community wellbeing.

The preliminary steps in this approach were undertaken in part C — the assessment of the benefits and costs of gambling, including the delineation of social impacts from private impacts. The Commission found that, for certain modes in particular, the social costs are substantial. This in turn strongly suggests (but of itself does not prove) that governments need to make considerable changes to the way they regulate the industry.

Against this background, the subsequent steps involve:

- the evaluation of existing policies and institutional arrangements to determine the extent to which they adequately address either the underlying causes of the social impacts of gambling or the impacts themselves;
- where they do not, the design of alternatives to address these matters; and
- the selection of the option, or combination of options, assessed as having potential to yield the largest net benefits.

These steps are taken in the detailed analyses contained in subsequent chapters. However, the Commission has not been asked to make formal recommendations for reforms to the specific state and territory regulatory regimes applying to gambling. Hence, its approach has been to provide information and guidance for policymakers on the likely elements of a sound regulatory system for gambling or, at least, on areas where further investigation may be warranted. The Commission has explored a wide range of options for improved consumer protection and harm minimisation (chapter 16). Some of these could be implemented on the basis of existing evidence about their likely effectiveness and costs. But others require further evaluation and possible trials before implementation, a technical and empirical task that is beyond the scope of this inquiry.

Some requirements for good policy overarch the individual elements, just as some of the reasons for existing (poor) policies lay outside the gambling arena altogether.

To capture these broader issues and thereby provide a context for the detailed analyses which follow, in this chapter the Commission:

- sets out the generic policy-development processes and principles that have driven its findings and which should guide gambling policy generally; and
- provides an overview of the extent to which current approach to gambling regulation converges or diverges from these principles.

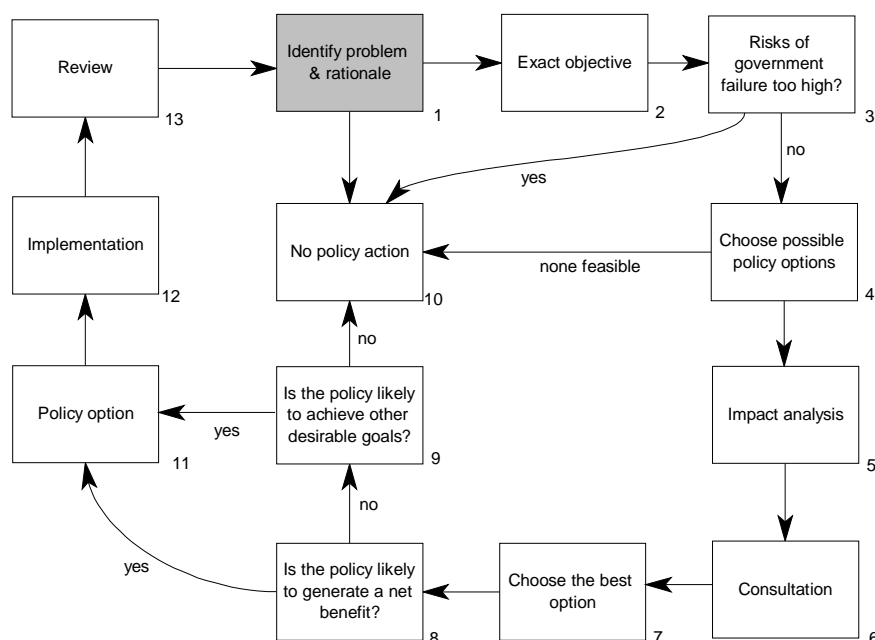
12.2 Policy processes

Because what *actually* happens in gambling policy often differs from what *should* happen, it is important to clarify how policy making should proceed, both as a way of assessing existing arrangements and as a tool for devising new approaches.

There are a number of general steps that assist good policy making (figure 12.1). These include:

- specifying clear objectives, considering alternative measures, and using transparent and consultative processes (box 12.2);
- and considering detailed design of any policy (table 12.1).

Figure 12.1 **13 steps to good policy**



Box 12.2 **Some principles of good policy process**

Identifying problems and clarifying objectives

- What is the problem that needs to be addressed and what is its risk?
- Why is government action needed to correct the problem?
- What are the objectives of government action?
- What are the risks and problems of government action?

Choosing an instrument

- What are the options for policy? (different types of regulation, including self-regulation; tax measures; financial assistance; and information provision)

Consultation

- Who are the main affected parties and what are their views? (eg industry's views about compliance costs of new regulations, community views about local changes with significant impacts).
- Are there appropriate *grievance* procedures for regulatory arrangements? (eg easily accessible, timely, fair systems).

Transparency and accountability

- Is the option clear, consistent, comprehensible and accessible to users? (eg granting licenses should be based on pre-agreed criteria and open to scrutiny).

Implementation and review

- How will the preferred option be implemented?
- How will the effectiveness of the option be assessed, including attempts to measure costs and benefits? How frequently?
- Is there a built-in provision to review or revoke the policy measure after it has been in place a certain time? For example, a regulation may become anachronistic with technological change (eg the influence of internet gambling on existing gambling modes) or altered community attitudes.
- Will any assessment of policies be independent from the policy maker or regulator?

Source: PC (1998) and ORR (1998).

Table 12.1 Impact and policy design issues

<i>Issue</i>	<i>Comments</i>
Design issues:	
Targeting	Does the policy target the problem effectively, and apply to the right groups? Does the policy apply too widely or narrowly?
Timeliness	Does the policy solve the problem in sufficient time?
Scale of resources	Does the policy apply the right scale of resources to the problem at hand?
Duration	Does the policy have the right duration?
Best-practice regulatory administration and delivery	Is it administratively efficient for government and for the client or target group? Is compliance and administration simple and low cost? Does the policy increase uncertainty? Do any paperwork requirements fit in with standard commercial practices, and with those required by any relevant regulations? Are the reporting requirements (in terms of frequency and detail) set appropriately? Is the administrative structure optimal for policy coordination, delivery and information provision? What systems are in place to ensure that the behaviour of policy administrators is fair and appropriate?
International obligations	Does it breach Australia's international obligations?
Enforcement	Is any regulatory enforcement regime appropriate (monitoring, fines, sanctions, education)? Is any penalty in proportion to the seriousness of the offence?
Flexibility	Is the policy likely to be effective as technology, markets, and community attitudes to gambling change? Is it likely to be effective for different sorts of gambling, venues or gamblers? Are any regulations flexible enough that a gambling provider has the freedom to search for lower cost ways of achieving the goals of the policy?
Cost recovery	Who should pay for the administrative and other costs of the policies (gambling providers, gamblers, taxpayers generally, a particular group of gamblers or providers, the source of any externality)?
Impacts:	
Who?	Who is affected by the problem which needs to be fixed, and who is affected by its proposed solutions?
On other policies?	How will any policy affect existing policies and regulatory institutions? Is it consistent with them?
On costs and benefits?	What are the costs and benefits of alternative options?
Distributional and social?	Who bears these costs and benefits? Does the policy unintentionally transfer significant resources from one group to another? How can these transfers be avoided or reduced? Is the policy 'unfair'? Does it conform with social norms?
Consumer and business impact tests?	Does the policy reduce competition and/or business innovation? Does it increase prices or reduce the quality of gambling? How much does it affect costs, quality or availability of inputs to the gambling industries? Does the policy require operational changes, including changes in personnel, or physical capital? Does it constrain business practices, for example, ability to attract overseas high rollers?

Sources: PC (1998), ORR (1998), Better Regulation Taskforce (1998), Ontario Red Tape Commission (1997).

In the chapters that make up part D, the Commission shows that some of the above principles have not been well observed in policy making for gambling.

Some of the elements which need particular attention for gambling policy are examined below.

12.3 Clear rationales?

Part C of the report outlined the key social impacts of gambling which might justify government involvement. Clarifying these rationales is important because, in their absence, gambling would be like many other entertainment and recreational industries, and there would be no grounds for what has been called the ‘complex regulatory web’ (sub. 155, p. 142).

Unfortunately, governments themselves send unclear signals about the underlying objectives for their gambling policies. This is because the objectives are often implicit rather than stated, are not always consistent, and the trade-offs among them are not specified. For example, governments have generally not revealed why there are variations in tax rates among gambling forms and venues, or why they themselves own some forms of gambling and not others.

The CIE (1998), in preparing a framework for Victoria’s NCP reviews of gaming legislation, argued that the stated objectives of governments provide only a partial understanding of the range of objectives which the regulations are intended to meet:

One reason for this is that nine different principal acts covering the industry have been enacted over the past 39 years and there are resulting inconsistencies, overlapping controls and gaps (CIE 1998, p. 20).

In this respect, Victoria is little different from other jurisdictions.

However, a number of objectives emerge as important (CIE 1998, p. xi; IPART 1998), as discussed below. The purpose of this discussion is not to detail *what* regulations and policies governments implement (which is in chapter 13). Rather it is to see *why* these are implemented, and whether such objectives have a *prima facie* rationale, as a basis for more detailed consideration in later chapters.

Generating government revenue

In no other group of industries today do policies appear to be driven so strongly by revenue needs — so much so that it is commonly observed that the states have become ‘addicted’ to gambling revenue. These revenue needs have contributed to the willingness by governments to liberalise formerly prohibited forms of gambling, such as gaming machines and casinos (for example, note the case of Queensland in box 12.3). Indeed, liberalisation displaced formerly illegal activity that gave governments no tax revenue, but occasioned liabilities (eg policing costs).

For example, the Western Australian Government said that:

... it seems certain that the revenue motive would have played a bigger role in the more recent rapid expansion of legalised gambling in most parts of Australia (in the last 10-20 years)... (sub. 76, p. 39).

Similarly, Tattersall's observed that:

... given gambling's effectiveness as a revenue raising device, governments have not long been able to maintain a policy of prohibition and non-involvement. The potential for revenue loss to other jurisdictions has also been a strong factor encouraging the spread of gambling services... (sub. 156, p. 56).

While revenue needs have contributed to liberalisation in the *availability* of gambling, they have also led to an overall regulatory and taxation regime that is far from liberal when compared with other entertainment products. Revenue needs have:

- encouraged monopoly practices that generate large economic rents, which are (partly) appropriated by governments through licence fees or specific gambling taxes; and
- led to high tax rates relative to other industries.

In some cases, the prominence of revenue generation in gambling policy is explicit. For example, lotteries have long been used to raise revenue for particular public purposes — these are sometimes seen as 'voluntary' taxes (the Opera House lottery being an obvious example). Western Australia and South Australia still depend on lottery revenues to fund specific activities. Queensland governments used the Golden Casket to fund their hospital system for many years, although the Government now simply directs funds to consolidated revenue (sub. 128, p. 12), as does New South Wales for its lottery.

In other cases, the revenue motive is more implicit in policy. For example, the persistence of monopoly (or 'exclusivity') arrangements in the gambling industries appears to be mainly driven by revenue considerations. Revenue collection, by itself, provides an unconvincing rationale for creating such exclusive rights. *If* it were accepted that governments should raise significant revenue from the gambling industries, then explicit taxes, through their greater transparency, accountability and flexibility, are preferred measures for collection (recognising that they may not *maximise* revenue from the industries in some cases).

However, even the goal of raising significant revenue from gambling may not be appropriate. That would depend on whether this was an efficient and equitable way of collecting tax revenue (compared to other sources) — an issue analysed in chapter 19.

**Box 12.3 Introducing gaming machines into Queensland:
some stated objectives**

According to the Queensland Government:

Gaming machines were introduced to:

- provide an avenue by which participating clubs could improve their financial position in order to provide enhanced recreational facilities and services for their members and patrons;
- provide additional employment opportunities in the States;
- provide direct funding to community groups, recreational and welfare programs;
- encourage the growth of tourism by the improvement of club facilities, services and entertainment;
- create extra revenue for the State; and
- meet the legitimate wish of those who are attracted to playing gaming machines by legalising access to such machines.

The Government added that gaming machines were legalised within a regulatory environment designed to ensure probity and integrity, and a range of policies was implemented to achieve this.

Source: sub. 128, p. 9 and Queensland Government (1996), p. 1.

The special weight given to revenue needs in governments' policies towards gambling reflects two factors.

First, the imperative for gambling revenue is driven by the imbalance in taxation powers between the Commonwealth and the states and territories. The Western Australian Government, for example, sees gambling taxes as a symptom of:

... the States' excessive reliance on Commonwealth grants (commonly known as Vertical Fiscal Imbalance ...) and substantial cuts in those grants; and very limited own source revenue raising options for the States (sub. 76, p. 39).

Second, governments' ability to tax is reinforced by the widespread perception that gambling is a 'questionable' pleasure. Ambivalent public attitudes allow governments to tax gambling with little adverse response. Governments can also mollify opposition to gambling itself, by taxing it heavily and channelling some of the revenues raised into socially worthwhile uses (chapter 20). It is politically much more difficult to oppose a measure if a significant proportion of the revenue raised is payable to a children's hospital.

Economic development and promoting tourism

Casinos, in particular, are promoted as agents for economic development and increased tourism. In Australia, every jurisdiction has adopted the policy of issuing casino licences only for hotel-casino complexes. And in many cases, the casino has involved large scale local redevelopments of partly derelict land: Jupiters, Crown, and Burswood are examples, while Adelaide and Brisbane both involved major renovation of heritage buildings.

The Queensland Government said that one of its objectives was to ensure:

... that the State benefits by the development and operation of hotel-casino complexes and associated community infrastructure. In particular ... casino licensees must have the financial resources to ensure the continuing viability of the hotel-casino complex (sub. 128, p. 8).

But while tourism and economic development are explicit objectives of some governments, the Commission found in chapter 5 that the wider economic development benefits of gambling are overplayed. It might have some relevance to destination gambling sites aiming to meet tourist needs, but most gambling does not fit this mould.

Special treatment for certain industries

Some gambling policies incorporate as a policy objective the favourable regulatory and tax treatment of particular groups, such as the racing and ‘club’ industries.

TABs commonly involve arrangements under which the racing industry receives funding from wagering revenues. For example, the joint venture between Tabcorp and VicRacing provides that the racing industry receive a share of all profits from Tabcorp’s gaming *and* wagering licences. The CIE (1997, p. 23), in its study of the Victorian regulatory framework, argued that ‘this is unlikely to have been negotiated in an unregulated market’.

In many jurisdictions, governments explicitly provide special advantages to clubs in the way they allocate gaming machine licences (chapter 13). Clubs also benefit to some extent from arrangements in jurisdictions such as Victoria and South Australia, where they are permitted the same maximum number of gaming machines as hotels, but where the greater demand is for hotel gambling. Clubs also benefit from advantageous taxation arrangements, partly as a matter of policy and partly in view of their mutual status (chapters 19 and 21).

In the absence of subsidiary rationales, the objective of tailoring regulatory and tax arrangements for segments of the gambling industries is unpersuasive. For example,

the Queensland Government introduced gaming machines to clubs (on a more favourable basis than hotels), in part, to

... provide an avenue by which participating clubs could improve their financial position in order to provide enhanced recreational facilities and services for their members and patrons (sub. 128, p. 9).

This begs the question of why gaming, among all possible services, should be chosen as the medium for the favourable treatment of clubs. Clubs would also improve their financial position from favourable treatment in providing cinemas, alcohol and other recreational and entertainment services, but most people would not see this as a proper basis for selective regulation.

It is possible that there are rationales for selective treatment, but that they are not articulated clearly by governments. This is problematic because it makes it difficult for policy evaluators to ask and test the right questions. Some *possible* rationales for selective treatment of different gambling forms could be that:

- clubs may represent less hazardous environments for gaming machine and TAB gambling than other venues (CIE 1997, p. 23);
- there may be other social advantages in favourable treatment of clubs — such as a more equitable distribution of resources in local communities;
- exclusivity may be a way of efficiently enhancing the pool size for parimutuel gambling modes (such as the TAB and lotteries); and
- in competitive wagering markets (where there are a number of gambling suppliers) no individual supplier has an incentive to pay anything towards the costs of the racing industry on whose outcomes they wager — the so-called ‘free-rider’ problem. In this case, it may be optimal for gambling suppliers to bind each other to pay a levy to the racing industry.

Whether in fact these provide a good basis for selective treatment is taken up in chapter 14.

Addressing the social costs of gambling

In practice, governments aim to limit the adverse social impacts of gambling through a range of policies, including preventative measures, harm minimisation and help services, and also through restrictions on the availability of gambling.

For example, the AHA (Victoria) indicated that the regulatory environment with respect to gaming machine licensing aims, in part, to address a number of social costs associated, or potentially associated, with gambling:

The rationale for licensing venue operators appears to be consumer protection, eliminating criminals and maintaining and protecting the government's revenue base. The rationale for linking the gaming licence to a liquor licence appears to be to restrict use of the product to those over 18 years of age, and to entrust the delivery of the product to a section of the community which is practiced in the responsible delivery of potentially harmful products (sub. 154, p. 9).

Gambling clearly does have severe social impacts for some people (chapters 6 to 9), so the objective of ameliorating or preventing these harms has a strong foundation.

Uncertainty about the social impacts of gambling have also led to a conservative attitude towards liberalisation of gambling. Governments have feared that some formerly illegal modes of gambling — gaming machines and casinos — might, when liberalised, have significant adverse effects on the community.

In reporting the reviews of gambling legislation undertaken thus far under the National Competition Policy agenda, the National Competition Council said that:

Traditionally, gambling has been far more regulated than most other industries, and free competition has not been an objective ... The approach of governments has reflected their views that there is significant community concern about the potential economic and social costs associated with a more competitive gambling market (NCC 1998b, p. 123).

Indeed, in explaining its approach to restricting gambling opportunities, the South Australian Government (sub. D284, pp. 1–3) emphasised that it sees gambling as a matter of social policy, not competition policy, (although it should be noted that there is not necessarily any conflict between the two, as social policy considerations are integral to the assessment of the merits of restrictions on competition under the National Competition Policy principles).

In the Commission's view, uncertainty justifies a cautious approach to liberalisation, but it does not justify protecting the interests of entrenched gambling providers (for example, by *long-term* exclusivity arrangements — chapters 13 and 14).

Whether the other instruments chosen to ameliorate the social harms of gambling work well or are applied consistently across jurisdictions and modes is, again, far from clear — an issue analysed in chapters 16 and 17.

Quality control and probity

One objective of governments is to implement regulations and oversight to ensure that games are 'fair' and that criminal provision of gambling — once the hallmark of parts of the industry — is avoided.

IPART observed that most developed countries regulate gaming primarily for social reasons and to deter crime:

The only product that exchanges hands in gaming is money. As a consequence, if gaming is not properly controlled, it is susceptible to criminal activity, fraud and dishonesty. Individuals can, and in some cases do, become addicted to gaming, with adverse effects for themselves, their families and society in general (IPART 1998, p. ii).

This is consistent with the views of the Western Australian Government, which said that the way in which it provides the public with access to gaming activities:

... has been influenced by the recognition that the gaming industry is an industry particularly attractive to unscrupulous operators and to organised crime. In an effort to protect the consumer from fraudulent activity, and to ensure that organised crime does not have an interest in operating or owning gaming activities, governments have determined that it is in the public interest to have a legislative regime requiring licensing and strict regulation of the gaming industry. These are long standing views which have been maintained by successive governments ... (sub. 76, p. 15).

Similarly, the Queensland Government said that its two major policy objectives are:

- to suppress illegal gambling by offering a legal equivalent; and
- to ensure the probity of the persons and the integrity of the systems involved in gambling by licensing the providers of the gambling product (sub. 128, p. 6).

The Queensland Government also noted that:

- the *Interactive Gambling (Player Protection) Act 1998* seeks to protect players by licensing providers, controlling advertising and marketing, ensuring privacy of personal information etc;
- its proposed new regulatory regime for art unions is heavily focused on ensuring probity;
- lotteries are run under stringent guidelines to ensure a high level of public confidence in the integrity of their operations; and
- the creation of the TAB was intended to stamp out illegal SP bookmakers and ensure that a significant proportion of the profits of offcourse wagering were returned to the racing industry (sub. 128, p. 12).

While probity appears to constitute a sound basis for government regulations, there are a number of subtleties:

- Probity is often in the interest of suppliers themselves. Good operators would, in the absence of regulation, still wish to signal their quality in this respect to consumers. For example, Star City Casino considered casino probity controls to be a reflection of residual concerns about casinos and organised crime, which

paid insufficient attention to the incentives which casinos have to operate as reputable businesses. Governments may, however, be more efficient at signalling and ensuring probity than individual operators.

- As noted in chapter 13, probity regulations apply extensively in some gambling modes (casinos and lotteries) but hardly at all in others (clubs). Probity regulations are rarely in place for non-gambling businesses.

The question of whether probity is an appropriate basis for special regulations in the gambling industries has to rest on evidence that the risks or consequences of lack of probity are likely to be noticeably higher without them (an issue which is examined further in chapter 16).

Summing up

Australian governments generally agree on the broad objectives of gambling policy. Foremost among these are the desires to maximise revenue, to minimise social impacts, to ensure product integrity and to deter criminal involvement.

However, not all of governments' objectives for gambling policies are clear, consistent, or have a persuasive economic or social rationale. Of governments' objectives, only two provide a strong *prima facie* basis for any special policies directed at the gambling industries — probity and ameliorating social harms. Four others have an uncertain basis, while the remaining four appear to have little rationale.

Nor do the objectives — when scrutinised closely — fit with the Competition Principles Agreement, the agreed framework for State and Territory reviews of regulatory arrangements. For example, when formulating the objectives of their gambling policies, jurisdictions have largely ignored their impacts on the efficient allocation of resources and, apart from probity, they appear to have often disregarded the interests of consumers (which goes beyond prices to consumer protection issues).

The view that implicit and explicit objectives set down by governments are flawed is echoed by others. The NCC, for example, expressed some doubts about some of the justifications provided for restrictions on competition (1998b, p. 124), taken up in chapter 14. ACIL, in a report commissioned by major providers from three States, was even more critical of both the objectives and sweeping nature of the regulatory and policy regime:

Regulation of gambling in Australia ... is an accretion resulting from historical attitudes and events (especially in periods in which gambling was illegal) that bear no relation to

either current reality or an overall and properly considered policy framework (sub. 155, p. 142).

In part it attributes this to ‘policy gridlock’ in all jurisdictions, noting that, notwithstanding National Competition Policy reviews:

... the various state and territory jurisdictions have found it difficult to undertake very searching reviews of their gambling laws (sub. 155, p. 143).

Some also argue that the mix of objectives is unbalanced, with the revenue objective dominating that of reducing the social costs of gambling:

- some fear that social costs may increase over time if a preoccupation with tax revenue deters governments from policies which may constrain gambling; and
- there is also concern that measures which seek to legitimise high taxes, like the earmarking of revenue for particular purposes, also serve to promote gambling.

12.4 Allowing for ‘government failure’

As noted, while there are a number of poor reasons given for government regulation of gambling, there remain some strong *prima facie* rationales for regulation of gambling and other government policies.

But these provide only a *contingent* basis for government policies in the gambling industries — they are not sufficient.

Policies intended to deal with one problem can create other problems and greater costs. For example, one strand of harm minimisation aims to reduce problem gambling by changing the designs of gambling technology and venues. For this to be worthwhile, the benefits from reducing problem gambling have to be greater than the costs for recreational gamblers. Some design changes will not pass this test.

Measures based on social norms and ethics pose questions about *whose* norms and ethics should apply, with risks of paternalism and excessive social control.

Similarly, it is possible that some measures aimed at curbing criminal problems associated with gambling (such as money laundering) may simply lead to criminal behaviour elsewhere, with little aggregate impact. And as IPART pointed out, there are limits to the extent to which governments can regulate gambling, because of the need to avoid increasing the appeal of illegal forms of gaming and providers of gaming in other states and countries (IPART 1998, p. ii).

The industry submission prepared by ACIL gave particular emphasis to the likelihood of such ‘government failure’, citing probable regulatory capture of public

officials, likely ‘lowest common denominator’ outcomes from government sponsored activities, populism and the distortions of raising taxes to fund government measures. It concluded that:

The key issue is that even if the market clearly fails in the provision of gambling services, this does not of itself justify the existence of public funding, regulatory and institutional arrangements to combat market failure. At the very least, the market failure must outweigh any government failure that may be reasonably expected to be associated with fixing it. This apparently straightforward point is often forgotten by proponents of government intervention and stands as an important reason why the current array of interventions, including tax policy, in Australia’s gambling industry deserves review (sub. 155, p. 5).

Governments’ failure to follow good regulatory process and design principles, compounded by and combined with revenue raising imperatives, may well have led to perverse regulatory outcomes in gambling.

12.5 Good process and design

There appears to be scope for process and policy design reforms that would reduce the risks of government failure. One of the key advantages of following something akin to Regulation Impact Statements (for regulations or other policies) is that they provide a framework for considering whether policy is susceptible to government failure.

Transparency, appropriate consultation and grievance procedures, combined with the explicit design of policy and the recurring independent assessment of the public benefit of policies, maximise the likelihood of an efficient and effective policy regime.

The right instruments and settings

In the gambling industries, a large range of instruments is used to achieve government objectives:

- taxes are levied or license fees exacted (at different rates for different gambling forms and venues);
- gambling venues are given exclusivity in some domains (casinos, lotteries, licensing of venues able to offer gambling);
- prices have regulated floors and sometimes ceilings;
- information is mandatorily collected and probity checked for some games and some venues;

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- gambling technology is rationed (caps at various levels);
 - governments provide help services to people who come forward as problem gamblers or their family members;
 - there are a small range of preventative measures, such as the development of curriculum materials and awareness raising of some of the risks of problem gambling; and
 - harm minimisation strategies are developed, sometimes by the gambling industry on a self-regulatory basis and sometimes through legislative requirements (such as the ban on bill acceptors in South Australia).

The following chapters in part D assess the usefulness and justification of these instruments.

The internet and a range of other emerging technologies present some new challenges for policy (chapter 18). They raise the possibility that policy instruments that worked in other gambling modes will be ineffective in the new ones. It is also possible that if there is strong substitution between new and old gambling technologies, then it will undermine the effectiveness of policies used in the old modes. The story which unfolds from internet and interactive gambling may in this sense resemble that of banking in the early 1980s, where the protective web of regulations entangling the banks was unravelled by the vigorous growth of non-bank financial institutions.

A policy framework, whether it be for health, defence or gambling, should consist of a coherent set of arrangements which are coordinated to achieve their aims. However, policies for the gambling industries are fragmented, inconsistent, and even in conflict.

Policy inconsistencies can arise both because of poorly defined rationales for policy and because of the ad hoc way in which policies are developed (typically by different institutions) for the different modes of gambling. They often also reflect historical accident and the evolving nature of the industry. In many cases, only now are the gambling industries being seen as a coherent group of activities, which require a consistent set of policies and the need for, if not one, at least a coordinated group of institutional overseers (as demonstrated by the thrust of submissions to the New South Wales IPART inquiry). The Commission assesses in chapter 22 the procedural and governance arrangements which might provide better outcomes.

12.6 The policy goal: maximising net community benefits

The Commission's approach for examining policies, such as the regulatory and taxation arrangements which pervade the gambling industries, emphasises as its ultimate goal the notion of maximising overall community welfare or well-being. This encompasses those who benefit from, and those who are disadvantaged by, any policy measures. Where social and distributional issues are important, the Commission also considers the role that equity and social norms play in good policy making. In general though, given that weights for distributional considerations and values for achieving community norms can be incorporated with economic analysis, this goal can be broadly characterised as one of maximising net community benefits.

Chapter 11 indicated that, conceptually, one way to represent this objective in gambling policy is for government to set policy so as to achieve an optimal industry size. This size would be the level at which the marginal costs of gambling (comprising social and production costs) equal the marginal benefits to gamblers (box 11.4 in chapter 11).

One, unambitious, stance of government could be to take everything about the gambling environment as given (such as the design of gambling technologies, accessibility and monopoly provision), *except* the quantity of gambling allowed. Government would then simply try to maximise the social benefits of gambling by relaxing or tightening the quantity constraint.

However, such a stance would ignore all of the other possible policies and instruments discussed in the preceding sections. By re-designing these policies, it will often be possible to achieve higher net benefits by reducing social harms — and this, in turn, may allow the safer liberalisation of gambling.

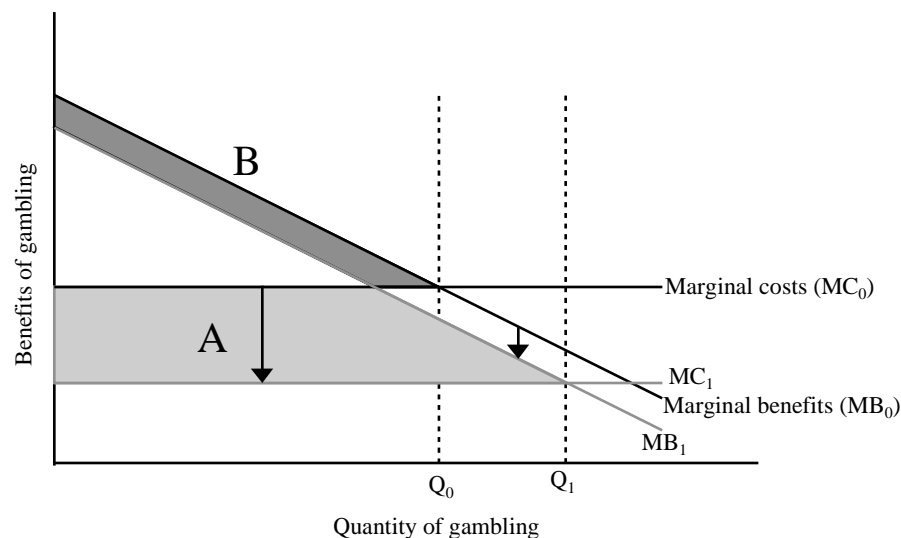
The principle is illustrated in box 12.4.

An analogy is motor vehicles. If cars were very unsafe, it might be reasonable for governments to limit their number. However, in the presence of the accident prevention and harm minimisation standards present today, there is no need to control vehicle numbers.

Box 12.4 Using policy to maximise benefits — some theory

The gambling industry produces both benefits and costs. These costs and benefits are likely to change as the industry grows or declines in size. The changes in costs and benefits associated with incremental changes in the size of the industry are referred to as *marginal* costs and benefits. While the graphical depiction of these marginal costs and benefits below is only hypothetical, they provide some useful policy insights.

Say that governments were to introduce some policies which improved prevention, harm minimisation and assistance, leading to less problem gambling — thus lowering the marginal social costs of gambling (from MC_0 to MC_1). Suppose that these also had some adverse impacts on the marginal benefits — pushing marginal benefits down from MB_0 to MB_1 (for example, because some recreational consumers found some of the measures decreased the convenience from playing). In the example given here, there is a clear net benefit from these measures (A, the gain, is bigger than B, the loss). Also, effective harm minimisation *increases* the optimal amount of gambling from Q_0 to Q_1 — so that policies which deal effectively with the adverse social consequences of gambling need not be counter to the interests of gambling suppliers.



Of course, the example in box 12.4 is an illustration only. Different movements in the marginal benefits and marginal costs will have other outcomes than shown in the example. However, the point is that government policy-making should take account of how it shifts the marginal benefits of gambling to consumers *and/or* the marginal costs of gambling (to problem gamblers and the community in general).

The role of consumer sovereignty

An overarching issue for the evaluation of gambling policies is how to determine which mix of gambling activities (and constraints on activities) actually maximises gamblers' net benefits. This can seem a perplexing task given the myriad of possible

activities and variations on activities that could be made available for gamblers, and the difficulty for the outside observer of determining which of these would bring the most net benefits for any one gambler, let alone for each gambler in the population.

A common benchmark is that people's revealed preferences are the best guide to these issues — the notion of 'consumer sovereignty':

One basic economic tenet is the 'consumer sovereignty' principle that individuals are generally best placed to assess for themselves the benefits that they receive and the costs that they incur from engaging in an activity. A corollary of this that, generally, an individual will only engage in an activity to the extent that the benefits of doing so outweigh any costs involved. Another is that the activities we observe can be safely assumed to represent the set which gives greatest possible satisfaction to those engaged in them, given the constraints of income, time available, information and so on (sub. 155, p. 2).

Hence, provided a judgment can be made that the production side of an industry is responsive to consumer demand, policymakers can normally sidestep the conundrum of having to value different activities by taking those observed in the market place to be the ones that maximise consumers' welfare.

In the case of gambling, the blanket application of this principle would imply an attenuated role for government. Some submissions to the inquiry took this viewpoint, arguing that gambling was a matter for the free choice of the consumer, and that regulations which restricted choice were, at best, paternalistic.

There is an important caveat in the above passage, however. It is the use of 'generally' in the phrase 'generally best placed'. Taken to its extreme, the concept of consumer sovereignty means that suicide, self-abuse, and heroin addiction all represent the desirable state of affairs for the person concerned. Of course, most consumption does not fall into these extremes, but for problem gambling this is exactly the issue. What generally holds for most goods may not hold for some gamblers.

In any case, the assumption that effective choice can only be restricted by policy is not always sound. Policies which allow informed consent typically widen, not narrow, consumer choice. For example, government requirements for information about product quality, cooling-off periods and measures to reduce supplier deception or entrapment, generally give consumers more power to make informed choices about what they buy.

And of course, the 'consumer sovereignty' principle is of no help where external benefits and costs are involved.

Overall, the Commission acknowledges that many policies that are consistent with the goal of maximising net (consumer) benefits will also be consistent with the principle of consumer sovereignty. The principle is also of value when devising gambling policy, particular for the large majority of (non-problem) gamblers.

However, that does not mean that there is no role for government in trying to alleviate the harmful social impacts of gambling, whether it be on gamblers themselves or on others. The notion of consumer sovereignty does not, therefore, short-circuit the policy assessment process laid out in figure 12.1.

The role of harm minimisation

The Commission has drawn on the principles of harm minimisation in developing several of its policy suggestions for gambling regulation. Harm minimisation strategies are a more ambitious, and a potentially more beneficial, way of dealing with the adverse social impacts of gambling than by simply imposing or tightening a constraint on the amount of gambling (box 12.4). They seek to meet the recreational demand for gambling, while reducing the social costs associated with each unit thereof.

It is important to recognise that the Commission's approach is more one of harm *minimisation* (or, perhaps more accurately, risk *optimisation*) than harm *prevention*. That is, the Commission does not favour measures which would reduce the social costs of gambling *no matter what the sacrifice to the private benefits*. Rather, its approach is to seek ways that, *as far as practical*, reduce the social costs of gambling without reducing the benefits.

This contrasts with the philosophy sometimes evident in public debate which, at the extreme, claims that any measure that reduces or eliminate a harm, no matter how costly the measure nor how small the harm, is justified: "One family destroyed is one too many", as one participant put it (City of Boorondara, trans. 1277).

While such claims are understandable and have obvious emotive appeal, they are also untenable in practice because they inevitably lead to the banning of anything that causes a harm, including things that entail substantial net benefits to the community. In the case of cars, for example, a philosophy of harm *elimination* would require their removal from the road.

Hence, in considering the role for harm minimisation strategies, the Commission has retained the flexibility to tradeoff the benefits of such measures with any costs they may impose on regular gamblers.

Characterising the Commission's approach

The Festival of Light interpreted the Commission's approach as involving a conflict between two mutually exclusive policy goals. It said:

...the draft report commits public policy to pursuing, simultaneously, two mutually exclusive agendas. On the one hand, a politically-correct, ultra-libertarian tendency to uphold the rights of individuals to engage in forms of pleasure seeking behaviour irrespective of their known destructive consequences is consistently upheld. On the other, a desire to establish a comprehensive social 'safety net' that protects individuals and society from the adverse consequences of such behaviour is simultaneously evident, in the form of 'minimising the harm' inflicted by problem gamblers. (sub. D213, p.3).

However, the Commission's approach is not based on absolute consumer sovereignty on the one hand, or absolute consumer safety on the other. Rather, the Commission's approach recognises that consumer choice and freedom involves some costs and benefits, as do varying regimes of consumer protection. The policy goal, difficult as it may be, is to find an approach that tries to achieve the overall best outcome.

Indeed, it should be noted that the approach developed in the following chapters involves a suite of measures, including:

- *consumer protection* measures for the benefit of all gamblers;
- proactive *harm minimisation* measures (such as voluntary self-exclusion measures) to reduce the extent of problems suffered by problem gamblers; and
- reactive *harm alleviation* measures (such as help services) for any problem gamblers, and their families and others affected by them, who suffer severe problems.

Hence, it is misleading to characterise the Commission's approach as being simply one of 'let the market rip but put a safety net in place to catch the losers'.

So in summary, the Commission has examined the merits of measures to address the pros and cons of gambling at a range of levels. In doing so, while recognising the importance of principles such as consumer sovereignty, harm minimisation and harm alleviation, it has not relied exclusively on any of these. Rather, it has been guided by the over-arching principle of maximising net community benefits. Any measure — whether it be interventionist or market-based — which can reduce the social costs of gambling while maintaining its benefits, will be particularly favoured under this approach.