

Casino Gaming Regulation

Follow-up to VFM Section 3.01, *2010 Annual Report*

Background

Casino gaming in Ontario is primarily overseen by two Crown agencies, which have different responsibilities and an arm's-length relationship to each other:

- The Alcohol and Gaming Commission of Ontario (Commission) is the “regulator,” with a mandate to regulate, license and inspect gaming facilities, and to enforce gaming legislation.
- The Ontario Lottery and Gaming Corporation (OLG), as the “operator,” builds, manages and operates, either directly or with private-sector partners, Ontario’s 24 casinos and slot machine facilities at horse racetracks (27 casinos and slot machine facilities in the 2009/10 fiscal year).

OLG directly operates 19 gaming venues, including 14 at racetracks that have only slot machines and five casinos with both table games and slot machines (at the time of our 2010 audit, it directly operated 22 gaming venues, including 17 slot facilities and five casinos). It also contracts private-sector operators to run day-to-day operations at one smaller casino and four large “resort casinos,” which offer more gaming options, higher wagering limits and amenities such as hotels, entertainment, and meeting and convention space.

In the 2011/12 fiscal year, OLG casino gaming operations generated more than \$3.3 billion in revenues (\$3.4 billion at the time of our audit in 2009/10) and incurred \$2.6 billion in operating costs (\$2.5 billion in 2009/10), for a net profit of \$700 million for the province (\$900 million in 2009/10). More than 85% of all revenues are generated by slot machines.

The general public expects casinos and slot facilities to be run fairly and honestly. Casino and slot facility customers expect slot machines to actually pay out the regulated minimums; those who play table games, such as blackjack or craps, want assurance that casino employees are honest and properly supervised, and that the games are run fairly.

In our *2010 Annual Report*, we concluded that the Commission had adequate systems, policies and procedures in place to meet these expectations. The Commission’s gaming equipment test lab and gaming enforcement procedures were adequate to ensure the fair operation of gaming equipment, a conclusion confirmed by an independent accredited gaming test lab that we hired. Our research into other jurisdictions, and advice from external experts, also indicated that Ontario’s regulatory framework for casinos offers one of the stronger oversight mechanisms in North America.

However, we also noted in our 2010 audit several areas where the Commission’s oversight

procedures and gaming transparency could be enhanced, as follows:

- Slot machine patrons are very interested in the actual payout ratio and in whether these payout percentages vary depending on the machine type and denomination (for example, a one-dollar or a penny machine). Some U.S. jurisdictions such as Nevada provide this information, but Ontario did not.
- We noted that patrons would find it difficult to locate information on the maximum prize payout on certain slot machines—an important disclosure should the machine malfunction and erroneously award a multi-million-dollar jackpot, as occurred twice in the two years prior to our audit. In addition, the Commission did not require casinos to post the odds of winning a jackpot on slot machines.
- In the 2008/09 fiscal year, commission inspectors at three of four gaming facilities could not meet their goal of inspecting every slot machine once a year. In addition, the Commission's gaming audit and compliance inspectors were behind schedule in verifying that gaming facilities complied with approval requirements and their own internal control manuals.
- In determining registration eligibility for suppliers and gaming employees, the Commission had no policy for dealing with conflicts of interest involving related employees working in the same casino. It relied, instead, on casino and slot facility operators to deal with these situations.

In a related issue, estimates in the 2009/10 fiscal year were that Ontario residents spent about \$400 million annually on foreign-based Internet gaming websites. Foreign gaming operators do not share their revenues with the province, and the Commission has no mandate to regulate Internet gaming. To help address this, British Columbia and Quebec now offer Internet gaming, and, at the time of our 2010 audit, OLG indicated that it planned to introduce Internet gaming in 2012.

We made a number of recommendations for improvement and received commitments from the Commission that it would take action to address our concerns.

Status of Actions Taken on Recommendations

At the time of our follow-up, the Commission had taken action on several of the recommendations we made in 2010; however, others are taking more time to implement. The Commission is in the process of implementing a new approach to regulating gaming that aims to target higher-risk areas and to set standards while increasing operational flexibility for gaming operators by allowing them to develop their own control activities and business processes. The Commission has completed a series of risk assessments related to casino gaming facilities and expects to begin introducing new standards and requirements by 2013. As a result of the Commission's development of a new regulatory approach, which is an ongoing and evolving process, a few of our recommendations have yet to be substantially addressed.

The current status of action taken on each of our recommendations is as follows.

CONTROLS OVER GAMES

Recommendation 1

To provide more useful information to slot machine patrons and better communicate its role in ensuring the integrity of gaming in Ontario, the Alcohol and Gaming Commission of Ontario (Commission) should:

- *make public the minimum 85% slot machine payout percentage, a range of actual payouts, and the Commission's role in overseeing this, similar to the public disclosures made in Nevada and New Jersey; and*

- *review its standards and approval processes for new and existing slot machines to ensure that the maximum prize payouts and odds of winning are clearly disclosed or readily obtainable on each machine.*

To enhance its already strong controls over electronic gaming equipment, the Commission should:

- *assess the reasons for its Electronic Gaming Branch not meeting its goal of inspecting all slot machines annually and, using a risk-based approach, assess the implications of this but also the need for an annual 100% inspection practice; and*
- *regularly audit its inventory controls over security seals intended to prevent tampering with electronic gaming equipment to ensure that proper accounting is in place and that unaccounted-for seals are immediately detected and investigated.*

In addition, to ensure consideration of key risk factors relating to table games, the Commission should reassess its approval requirements for surveillance plans, including minimum surveillance staff levels at gaming facilities. To ensure that gaming operators' staff who work in key risk areas, such as table game dealers and surveillance staff, have sufficient training, the Commission should consider whether it should require casino staff to meet predefined standards of training and competency.

Status

The Commission advised us at the time of our follow-up that it was still reviewing current policies on casino gaming facilities. It also said that the new standards and requirements that casino operators must meet would begin being implemented in 2013, although a date for establishing a standard for communicating maximum prize payouts and odds of winning to slot players had not been set. In the meantime, information on the minimum 85% expected payout percentage is now currently available to the public on the Commission and OLG websites.

The Commission also developed risk-evaluation criteria for identifying slot machines that require

inspection. We were advised that the Commission does not have a policy to physically inspect 100% of the devices annually. Instead, using the risk-based approach, it carries out targeted inspections of machines identified as high priority. These include new machines, those that have been converted or changed in any way that might affect the integrity of the game, and those being removed from service. In addition, the Commission conducts risk-based random inspections on installed gaming equipment. We were informed that the Commission is up to date on its risk-based inspections of gaming equipment.

The Commission has also updated its control procedures over security seals to include new procedures at every gaming facility. At the end of each month, an electronic gaming inspector physically counts all unused seals, and a regional manager reviews a report that identifies all currently applied seals and highlights any suspicious numbers for further investigation. In addition, the Commission updated the Slot History System database in July 2011 to keep a historical record of all seals entered into the system so as to be able to reconcile them. We visited one slot facility and found that new inventory controls over seals were in place as required.

The Commission has initiated a number of pilot projects in the development of the standards-based approach to gaming regulation, including a regulatory review of surveillance plan requirements. While the standards and requirements being developed do not specifically address surveillance staffing levels or casino staff training and competency, the Commission did change existing requirements so that performance reporting of employees now includes their adherence to required procedures. We were also informed that risks related to the competency of table game dealers have been identified, with further relevant standards and requirements to be developed as part of the Commission's review of policies over gaming facilities taking place at the time of our follow-up.

GAMING AUDIT AND COMPLIANCE

Recommendation 2

Given that Ontario's gaming industry is mature and there is a high level of gaming facility compliance with its regulatory requirements, the Alcohol and Gaming Commission of Ontario (Commission) should develop comprehensive control-risk frameworks that would allow gaming facilities to be assessed individually for risk. Such a framework would allow the Commission to cost-effectively focus more of its regulatory oversight on higher-risk facilities and less on lower-risk ones and yet still achieve a prudent level of oversight. In developing these frameworks, the Commission should also assess the reasons for and the potential impact of its audit and compliance staff not achieving the targeted number of audits and inspections of gaming facilities.

Status

The Commission has implemented a three-phase risk-based approach for conducting audits of gaming facilities.

First, it developed an industry-wide risk assessment in November 2009 for all gaming sites, leading to the creation of a risk profile for each individual site. Based on the risk profiles, more frequent audit cycles were established for higher-risk sites. We were informed that the risk profiles are also updated on a quarterly basis using the latest available information.

Second, various operations within a specific gaming site with a greater risk of non-compliance were identified to allow the Commission to focus its resources not only on sites determined to be higher risk, but more specifically on the internal operations, such as surveillance, table games, and cashiering, of each site deemed to be higher risk.

The Commission informed us that in June 2012, it implemented the third phase of the updated audit approach, which involves determining the key controls to be selected for testing. In light of the government's 2012 Budget, which announced the government's intention to explore the further privatization of OLG casino facility operations, the

Commission advised us it would take new operators into account in developing its new risk-based audit approach, with implementation planned for 2013.

In addition, the Commission has been developing an integrated audit model in conjunction with OLG's internal auditors to enhance audit efficiency and effectiveness and to minimize overlap of the overall audit function between the two agencies. We were informed that, because of shifting government and OLG priorities, the time frame for completion of this integrated model had not been finalized.

GAMING SUPPLIER AND EMPLOYEE REGISTRATION

Recommendation 3

To ensure that registration and renewal processes meet adequate standards for timely completion and consistent quality, the Alcohol and Gaming Commission of Ontario should:

- *complete its risk-based assessment for streamlining procedures, and establish benchmarks and management tracking reports for registration and renewal processing times; and*
- *establish a policy defining what could constitute potential conflict-of-interest situations involving gaming assistants and what situations could prove problematic.*

Status

The Commission implemented a new three-stage risk-based process in September 2011 to streamline the registration and renewals process for gaming suppliers and employees. The first stage establishes basic eligibility and determines whether further investigation is required using a scorecard to assess risk. If an applicant's level of risk is scored high, the Investigations and Enforcement Branch conducts a more rigorous inquiry, collecting more in-depth information through interviews and/or a full background review. The final stage involves a decision about whether to issue the registration or renewal. We were informed that the Commission will undertake a comprehensive assessment of the

new streamlined process after it has been in place for one year.

The Commission also developed the Casino Gaming Performance Measures Dashboard as a performance management tracking and benchmarking tool. The Dashboard is used to report on the overall performance of the Commission against key indicators, including registration and renewal processing times. Benchmarks for the performance indicators have been established, and when targets are not met, management investigates the causes and makes operational adjustments as required. In addition, monthly reports using information from the Dashboard—such as the number of licences and registrations issued as well as average turnaround times for processing—are prepared for the Commission’s Board of Directors and also distributed to senior management.

The Commission has yet to establish any policies covering potential conflicts of interest involving gaming assistants. We were advised that these standards and requirements are being developed as part of the Commission’s overall move toward a standards-based approach to regulation.

SELF-EXCLUSION PROGRAM

Recommendation 4

To ensure that gaming facilities adequately deal with patrons who may have a problem with or an addiction to gambling and those who participate in a self-exclusion program, the Alcohol and Gaming Commission of Ontario should develop minimum standards, policies, and procedures related to self-exclusion for use in Ontario’s gaming facilities. It should also implement a process of periodically reviewing gaming facilities’ compliance with these requirements.

Status

The Commission advised us that it consulted with key stakeholders regarding various elements of self-exclusion and whether those elements should be included in policies and programs approved by the Board. We were informed that as a result of the con-

sultations and a scan of best practices across various Canadian and foreign jurisdictions, Responsible Gaming Standards are currently being developed that will also address self-exclusion programs. For example, the standards will require gaming operators to offer a voluntary self-exclusion program, terminate the OLG accounts of self-excluded persons, remove them from mailing lists, and withhold all incentives and promotions for OLG products and services during the period of self-exclusion. The Commission expects the new standards to begin being implemented in 2013, although a date for a standard on self-exclusion programs has not been set. In the meantime, we were informed that all sites currently operate a self-exclusion program that is largely consistent with the standards and requirements that will ultimately be put in place.

We were advised that along with the development of standards, self-exclusion programs will be examined on an ongoing basis using appropriate regulatory assurance activities such as audits and inspections.

PERFORMANCE REPORTING

Recommendation 5

In order to provide the public, including gaming facilities’ patrons, with meaningful information on its regulatory activities, the Alcohol and Gaming Commission of Ontario should research other gaming jurisdictions’ best practices in public reporting, and expand the information published in its annual report and website to ensure that it provides information of use to gaming patrons and to the public with respect to its key regulatory activities and results, as well as performance information that demonstrates the Ontario gaming industry’s competitiveness and integrity.

Status

Although no research was undertaken by the Commission on best practices in public reporting in other jurisdictions, the Commission has developed a Casino Gaming Performance Measures Dashboard that it now uses to report on its overall oversight of

the industry. Benchmark data from the Dashboard is used in the Commission's annual report, which was expanded in the 2010/11 fiscal year to include information such as the number and results of compliance inspections, testing of electronic gaming equipment and systems, and number and results of occurrences investigated by casino enforcement. We were informed that other key communication vehicles such as the Commission's website will be reviewed to enhance the information that is available to stakeholders.

OTHER MATTER

Internet Gaming

Recommendation 6

Although the Alcohol and Gaming Commission of Ontario (Commission) does not have a mandate to regulate Internet gaming, there are proactive measures the Commission could take to protect the interests of Ontarians in this area until such time as a decision is made as to whether Internet gaming should be regulated. Given the estimated nearly \$400 million that Ontarians gamble each year with unregulated foreign Internet gaming operators that do not pay fees or taxes to Ontario, and the recent decision that the Ontario Lottery and Gaming Corporation will offer Internet gaming in 2012, the Commission should:

- *conduct research into regulatory, technological, and oversight best practices used in other jurisdictions over Internet gaming available in their respective jurisdictions;*
- *develop strategies for possible action that can effectively regulate and tax or charge fees on foreign operators doing Internet gaming business in Ontario; and*
- *consider forming alliances with other provinces and the federal government to address Internet gaming, as is currently being done by some other international jurisdictions.*

Status

In November 2011, the Commission conducted a survey of regulatory bodies around the world to

assess best practices in regulation, technology and oversight and governance as they relate to Internet gaming. The review identified jurisdictions where knowledge-sharing and collaboration should be explored because their established regulations align with the Commission's own regulatory direction for Internet gaming. The Commission also released a request for proposals for consulting services to develop a regulatory assurance model for Internet gaming. The request closed in June 2011. A resulting contract was executed in September 2011, and work on the model began at that time. As of July 2012, the OLG was in the process of selecting a provider of Internet gaming as a result of its request for proposals completed in February 2012.

We were advised that since the Commission lacks the legal power and mandate to regulate foreign operators who conduct Internet gaming in Ontario, it had not developed strategies or proposals at the time of our follow-up to regulate and tax these operators, or charge them fees.

We were informed that while the Commission has formed no new formal alliances with other provinces to address Internet gaming, the Commission remains in regular contact with other Canadian jurisdictions and regulatory bodies through the Regulatory Review Committee and other organizations such as the Canadian Gaming Regulators Association and the North American Gaming Regulators Association. The Commission also advised us that it is in the process of entering into memorandums of understanding with other internationally based gaming regulators, including those involved in Internet gaming, to share information on applicants and on regulatory processes and standards. For example, the Commission signed a memorandum of understanding in March 2012 with the Gambling Commission in the United Kingdom, which regulates Internet gaming, to allow sharing of information and documentation for eligibility assessments of applicants, licensees or registrants, and for providing joint inspections, investigations, and other compliance and regulatory assurance activities with respect to gaming.