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| Consultation:  Proposed changes to gambling fees  Department of Internal Affairs  March 2015 |
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# What is this consultation document about?

This document invites your comments about proposed changes to gambling fees under the Gambling Act 2003.

## Consultation requirements

Section 372 of the Gambling Act 2003 requires that, before regulations are made, persons and organisations that are likely to be substantially affected by the regulations must be consulted and given a reasonable opportunity to respond. Submissions will be given adequate and appropriate consideration.

## Sending us your submission

Please send your submission to the Department of Internal Affairs by 13 April 2015.

Please note that all submissions may be made publicly available. Even if you request confidentiality, we may have to release your submission at a later date if a request is made under the Official Information Act 1982. In your submission please highlight the information you would prefer was withheld should a request be made.[[1]](#footnote-1)

Your submission can be sent in the following ways:

Email: [gamblingfees@dia.govt.nz](mailto:gamblingfees@dia.govt.nz)

Post: Community Well-being Policy Team

Policy Group

Department of Internal Affairs

PO Box 805

Wellington 6140

Although all reasonable steps have been taken to ensure the accuracy of the information contained in this document, the Department of Internal Affairs disclaims responsibility for any inaccuracy in relation to the information; and fully excludes liability of any kind to any person or entity that chooses to rely upon the information.

# Executive summary

1. The Department of Internal Affairs (the Department) undertakes gambling licensing, compliance, and enforcement functions under the Gambling Act 2003 (the Act). These functions (and those of the Gambling Commission) are funded through fees paid by the gambling operators that give rise to the Department’s regulatory activities. The operators are Class 4 gambling societies (those that operate electronic gaming machines in pubs and clubs), casinos, and organisations that conduct Class 3 gambling (where prizes exceed $5000).
2. Currently the costs of regulation are in excess of the revenue received and are not sufficient to support the proper, effective regulation of the gambling sector. Moreover, effective regulation of the gambling sector will cost more in future than is currently recovered from the sector. The forecast deficit is not sustainable and means that the taxpayer, rather than the industry, is funding a significant amount of gambling regulation, which is contrary to the intent of the Act.
3. Fees have not changed since 2008. The effects of no fee adjustments since then are particularly stark for the Class 4 sector. Revenue from fees has fallen due to a greater than anticipated decline in the number of gaming machines in pubs and clubs to which the majority of fees revenue is linked.
4. Declining machine numbers have not corresponded with a decline in the demand for regulatory activity. There is a considerable amount of work undertaken in the Class 4 sector that does not directly relate to the number of gaming machines (for example, there has been an increase in complex investigations into fraud and illegal activity with associated costs). Current and forecast cost pressures are driven by the need to maintain the Department’s levels of regulatory activity and technical capability, while continuing to cover general cost pressures, corporate overheads and capital charges.
5. The Department’s current and projected under-recovery of costs is reflected in the growing deficit in the balance of the Department’s memorandum account that manages gambling fees. At 30 June 2014 the deficit was $9.173 million. Without a change in fees, the gambling memorandum account deficit is forecast to increase significantly. Forecasts indicate a deficit of $27.942 million by 2016/17.
6. The Department has contained costs as far as possible. Two structural reviews have been undertaken since the last review of fees to ensure regulatory activity is being undertaken in the most efficient and cost effective manner. The first review resulted in a reduction of 20 full-time equivalent (FTE) staff. The Department is unable to make meaningful savings through further staff reductions without compromising the compliance and enforcement activities required by the Act.
7. The Department is proposing to set new fees to: address the gap between fee revenue and regulatory costs; reduce the memorandum account deficit; and place the burden of costs on those that give rise to them. While some fees would increase, others would decrease or stay the same. The proposed new schedule of fees represents the minimum revenue increase required to cover the increased costs of regulation from the gambling sector (particularly the Class 4 sector) and reduce the memorandum account deficit significantly over time.
8. The proposed new fees mainly impact on the Class 4 sector where fees are proposed to increase overall by 53.62 per cent. Lower annual compliance fees are proposed for small club societies to reflect their lower compliance costs to the Department. Class 4 fees currently account for approximately 2.06 per cent of societies’ GST-exclusive gross gaming machine proceeds. With the proposed fees this is forecast to increase to 3.16 per cent of societies’ GST-exclusive gross proceeds in 2015/16.
9. The Department considers that the proposed fee increases fairly cover Class 4 regulatory costs and strike a reasonable balance in reducing the memorandum account deficit. Fee levels have not changed since 2008 and the Class 4 sector has been effectively experiencing a reduction in fees payments since then as the number of gaming machines has declined.
10. Overall revenue from casino licence fees is not proposed to change, but it is proposed that some casinos pay more or less than they currently pay, based on their relative size and the estimated costs incurred by the Department in regulating each casino.
11. Amendments to Class 3 licences will no longer be charged due to low volumes and the potential for licence amendment fees to create a barrier to compliance.
12. The main benefit of the proposed changes to fees is that they will ensure the continued operation of the compliance and enforcement activities that the Department undertakes. These activities are important for the general public, so it can be assured that current levels of regulatory oversight are maintained.
13. Your views on the proposed changes to fees and alternative options are sought by   
    13 April 2015.

# Introduction

1. The Department of Internal Affairs (the Department) is seeking your views on proposed changes to gambling fees under the Gambling Act 2003 (the Act).
2. The purpose of the Act is to:
   * 1. control the growth of gambling;
     2. prevent and minimise the harm caused by gambling, including problem gambling;
     3. authorise some gambling and prohibit the rest;
     4. facilitate responsible gambling;
     5. ensure the integrity and fairness of games;
     6. limit opportunities for crime or dishonesty associated with gambling;
     7. ensure that money from gambling benefits the community; and
     8. facilitate community involvement in decisions about the provision of gambling.
3. In order to achieve these purposes, the Department undertakes gambling licensing, compliance and enforcement functions. These functions are funded through fees paid by gambling operators. The operators include Class 4 gambling societies (those that operate electronic gaming machines in pubs and clubs), casinos, and organisations that conduct Class 3 gambling.[[2]](#footnote-2)
4. Section 370 of the Act provides that regulations may be made prescribing fees or charges payable to enable the recovery of the direct or indirect costs of the Department, the Gambling Commission or the Police in:
   * 1. publicising and informing people about the Act;
     2. administering the Act;
     3. enforcing and monitoring compliance with the Act; and
     4. doing anything else authorised or required by the Act.
5. The current fees under the Gambling (Fees) Regulations 2007 have not changed since February 2008. The Department has reviewed the current fees and concluded that the revenue derived from them is not sufficient to cover the current and forecast costs of regulating the gambling sector.
6. The Department proposes to increase some fees to address the funding issues identified and intends to review the fees again in 2017/18.

## Types of fees paid by gambling operators

1. There are currently four broad types of fees in the Regulations. Table 1 shows the types of fees, revenue generated for 2013/14 and the relative proportion of total revenue that each fee comprises (*all figures are GST exclusive*).[[3]](#footnote-3)

Table 1: Fee types and associated proportion of gambling revenue in 2013/14[[4]](#footnote-4)

|  |  |  |  |
| --- | --- | --- | --- |
| Type of fee | Fees recovered (2013/14) $million | Percentage of total gambling revenue | Comment |
| Class 4 machine monitoring fees | $7.04 | 35.18% | Fees of $1.20/day charged for use of gaming machines that fund the Electronic Monitoring System and the Integrated Gambling Platform |
| Class 4 compliance fees | $6.46 | 32.28% | Annual fee of $378 per gaming machine charged to all Class 4 operators that covers compliance activity |
| Casino fees | $5.24 | 26.89% | Fixed annual fees charged to each of the six casinos |
| Licensing and miscellaneous fees | $1.13 | 5.65% | A range of fees primarily for issue of new or renewed licences for Classes 3 and 4 gambling |
| Total | $19.87 | 100% |  |

1. Gambling fees cover a variety of costs driven by a multitude of activities undertaken in gambling compliance and enforcement. Many of these activities are required by the Act including: responding to enquiries and complaints; conducting investigations; standards setting for gambling equipment; monitoring and auditing; and processing societies’ licence applications and amendments.
2. The Gambling Commission is also funded through the fees. Approximately 60 per cent of the Commission’s work is driven by casino applications and 40 per cent from Class 4 appeals.

# What is the problem with the current fees?

## Declining revenue leading to under-recovery of costs

1. The number of gaming machines in the Class 4 sector has declined to a level that is less than forecast. The fees review in 2007 assumed that machine numbers would stabilise at approximately 20,000 machines. However, machine numbers have continued to decline at a steady rate and at 30 June 2014 there were 17,130 licensed machines. As most of the Department’s revenue is derived from fees linked to the number of Class 4 gaming machines, the decline in numbers has had a significant impact on the Department’s financial position.
2. Declining machine numbers have not corresponded with a decline in the need for regulatory activity, particularly in the Class 4 sector. This means that the Department is under-recovering its gambling regulatory costs. The Department’s operating deficit for 2014/15 is forecast to be $3.841 million.
3. The figure below provides a breakdown of the Department’s gambling regulatory costs by activity for 2013/14. The costs are spread across the various gambling sectors, with nearly 80 per cent being driven by work associated with the Class 4 sector. The operation and maintenance of the Electronic Monitoring System (EMS), which monitors all Class 4 gaming machine-related activity, represents the largest cost. The remaining costs are driven by the casino sector and Class 3 gambling.

Figure 1: Breakdown of regulatory costs by activity for 2013/14

## Increasing cost pressures on the Department

1. Forecasts indicate reduced revenue over the next ten years to 2023/24 (based on the current rate of decline in machine numbers) and increased costs. The forecast operating deficit is not sustainable and results in the taxpayer rather than the industry funding gambling regulation, which is contrary to the intent of the Act (refer to table 2 below).

Table 2: Forecast changes in revenue and costs to 2023/24 ($million)

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | 2014/15 | 2015/16 | 2016/17 | 2017/18 | 2018/19 |  | 2023/24 |
| Revenue | 18.994 | 18.619 | 18.244 | 17.869 | 17.494 |  | 15.994 |
| Expenditure | 22.835 | 23.620 | 24.120 | 24.620 | 25.120 |  | 26.480 |
| **Deficit** | -3.841 | -5.001 | -5.876 | -6.751 | -7.626 |  | -10.486 |

1. Current and forecast cost pressures are driven by the need to maintain the Department’s levels of regulatory activity and technical capability, while continuing to manage general cost pressures, corporate overheads and capital charges.

### Constant levels of regulatory activity

1. Regulatory activity has remained constant despite the decrease in the number of gaming machines. Actual gambling activity and spend has stayed at similar levels (New Zealanders are gambling roughly the same amount, just on fewer machines).
2. The Class 4 sector is continuing to evolve, with levels of non-compliance becoming increasingly systemic. The Department’s investigations, audits and venue inspections of Class 4 activity identify breaches or non-compliance approximately 50 per cent of the time with varying degrees of severity. Increasingly, non-compliance in the Class 4 sector involves complex, large scale fraud and criminal activity that increases cost pressure on the Department. Investigative and legal work in response to these activities is contributing to the Department’s under-recovery of costs.
3. The Department works closely with the Police and other law enforcement agencies, sharing information and co-operating on enforcement actions. A large scale investigation in collaboration with the Serious Fraud Office is nearing completion. The investigation suggests that a number of societies have significant grant integrity issues and that grant capture is of growing concern. Additional budget of $0.67 million in 2013/14 and $0.62 million in 2014/15 had to be sought to fund the investigation. The investigation is one of several that the Department is currently undertaking.
4. Parts of the Class 4 gambling sector tend to be highly litigious, which creates a steady flow of legal work and associated costs for the Department. Legal contestation of the Department’s decisions is increasing. Typically between five and ten cases are before the courts or the Commission at any point in time. The costs of a single judicial review can amount to approximately $70,000 – 80,000 in legal fees.

### Technical capability

1. The Department continues to invest in maintaining its technical capability from which the gambling regulatory function receives considerable benefit. As required by the Act, the Department monitors all Class 4 gaming machines through the EMS. This monitoring is fundamental to regulating the sector. The EMS connects every gaming machine in every pub and club in New Zealand to a central server. It records information such as the amount of money gambled, the amount required to be banked, whether the machine is in use and if it has been tampered with. Initially the costs of EMS were related to its design, development and implementation and the on-going costs associated with the contract provider, Intralot NZ. Now that the system has matured, the remaining costs relate to the Department’s continued management and support of EMS.
2. There are also additional development and depreciation costs associated with implementing the Integrated Gambling Platform (IGP). The additional costs range from $0.200 – $1.340 million per year over the forecast period. The IGP is an upgraded licensing management system, which the Department uses to manage licensing applications and (in the future) compliance activities. The IGP replaces and improves on a legacy licensing system that is now over ten years old. It will reduce the amount of paperwork associated with licence applications, provide more robust business processes and link licensing and compliance related information.

### General cost pressures

1. General cost pressures amount to $0.500 million per year cumulatively and includes all consumer price index adjustments and increases in salary costs for the forecast period to 2023/24.

### Corporate overheads

1. Increased corporate overhead costs amount to $0.500 million per year over the forecast period and includes the costs of upgrading aging software, and modernising processes and technology.

## Department’s memorandum account deficit

1. Treasury instructions require that where departments provide services on a full cost recovery basis, the department is required to operate a memorandum account. The memorandum account records the accumulated surplus or deficit arising from the provision of the service. The balance of the memorandum account deficit is expected to trend to zero over a reasonable period of time.[[5]](#footnote-5)
2. The Department’s under-recovery of costs to regulate the gambling sector is reflected by an increase in the deficit in the Department’s memorandum account that administers gambling fees. At 30 June 2014 the deficit was $9.173 million.
3. The deficit is forecast to increase significantly if revenue declines and costs increase at forecast levels. The forecast deficit includes capital charges that can be applied to Department memorandum accounts that run a net deficit.[[6]](#footnote-6) As the deficit increases capital charges accrue, which further exacerbate the deficit (refer to table 3 below). Capital charges amount to $4.879 million over the forecast period to 2023/24.

Table 3: Forecast memorandum account deficit ($million)

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | 2014/15 | 2015/16 | 2016/17 | 2017/18 | 2018/19 | 2019/20 | 2020/21 |
| Memo a/c opening | -9.173 | -13.901 | -20.214 | -27.942 | -37.198 | -48.104 | -60.544 |
| Memo a/c closing | -13.014 | -18.902 | -26.090 | -34.693 | -44.824 | -56.365 | -68.780 |
| Capital charge | -0.887 | -1.312 | -1.852 | -2.505 | -3.281 | -4.179 | -5.173 |
| **Memo a/c closing (net)** | -13.901 | -20.214 | -27.942 | -37.198 | -48.104 | -60.544 | -73.953 |

1. A review of the gambling fees is urgent in order to rectify these financial pressures. Delaying an adjustment to fees would require a more significant increase in fee levels in future years to recover the deficit. It is also not appropriate for the burden of regulatory costs to fall on the taxpayer. The Treasury *Guidelines for Setting Charges* *in the Public Sector* note that those that give rise to costs should be responsible for covering them and that a key aim of fees is to reduce the reliance on funding from tax.

# Managing cost pressures to date

1. The Department has contained costs as far as possible. Two structural reviews have been undertaken since the last review of fees to ensure regulatory activity is being undertaken in the most efficient and cost effective manner. The first review resulted in a reduction of 20 full-time equivalent (FTE) staff.[[7]](#footnote-7) The Department is operating at the lowest number of staff positions committed to gambling compliance and enforcement work since 2004 (refer to table 4 below). Ten positions proposed in a 2012 review were not filled for budgetary reasons.

Table 4: Changes in total established staff positions since 2003/04

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | 2003/04 | May 2007 | 2007/08 | 2013/14 |
| FTE Staff | 104 | 117 | 105[[8]](#footnote-8) | 85 |

1. The level of savings achieved in each year from the reduction in established staff positions is provided in table 5 below.[[9]](#footnote-9) Approximately $14.000 million has been saved to date as a result of the reduction to 85 FTE staff. The savings generated have been used to cover cost increases.

Table 5: Level of savings achieved from staff reductions since 2007/08 ($million)

|  |  |  |  |
| --- | --- | --- | --- |
| Year | Personnel cost savings | Overhead cost savings | Total savings |
| 2008/09 | $1.60 | $0.70 | $2.30 |
| 2009/10 | $1.64 | $0.70 | $2.34 |
| 2010/11 | $1.68 | $0.70 | $2.38 |
| 2011/12 | $1.72 | $0.70 | $2.42 |
| 2012/13 | $1.77 | $0.70 | $2.47 |
| 2013/14 | $1.81 | $0.70 | $2.51 |
| Total | | | $14.42 |

1. The Department continues to make changes to business processes with a view to enhancing operational efficiency and making best use of its available resources. These changes include:

* a greater focus on risk-based checks before licences are issued or renewed;
* a greater emphasis on management of audits and investigations;
* improved intelligence services that allow for more accurate risk-based positioning of regulatory effort; and
* a greater emphasis on working with Class 4 societies to avoid sanctions that could result in litigation. (This is specifically where societies have indicated their willingness to improve their performance and cease non-compliant behaviour consistent with the requirements of the Act).

# Principles for assessing fee options

1. The Department undertook the review of fees with the objectives of:
   * 1. creating a more sustainable third party revenue framework that adequately recovers the Department’s costs based on the regulatory work required; and
     2. maintaining current levels of regulatory oversight, which are the minimum necessary to meet the Department’s statutory obligations.
2. The Treasury and the Office of the Auditor-General (OAG) list a number of principles that should be considered when setting fees and charges. This review has been undertaken with these principles in mind.[[10]](#footnote-10) The OAG notes that authority, efficiency and accountability are the principles to be incorporated in fee-setting decisions. The Treasury guidelines focus on efficient resource allocation, minimising transaction costs, equity among those that give rise to costs, and reducing costs and taxpayer burden.
3. Because of the decline in the number of gaming machines, the Department examined other measures through which Class 4 gambling fees could be charged, including coupling fees to gaming machine proceeds or to the number of venues operated by a society. Analysis showed that similar revenue could be gained by tying fees to machine numbers, gaming machine proceeds or to the number of Class 4 venues.
4. The Department proposes to continue using gaming machine numbers in fee setting because:

* it provides more certainty for gambling operators as it is easier to budget for fee costs based on the number of machines (rather than gaming machine proceeds, for example);
* it provides more certainty to the Department for financial projections, as the decline in machine numbers is more predictable than gaming machine proceeds or venue numbers; and
* is transparent to all parties, easier to administer and is already familiar to the sector.

# What are the options?

## Option one: increase fees to cover costs and reduce the memorandum account deficit over time (preferred option)

1. This option would involve fee increases that are the minimum possible to cover costs and reduce the Department’s memorandum account deficit, as shown in table 6 below. For a full list of the proposed fees under this option, refer to the Appendix. If the proposed new fees described in this option are set, the average annual contribution to reducing the memorandum account deficit would be $1.766 million. The Department’s analysis indicates that a smaller percentage increase in fees would not recover costs and facilitate a decrease in the memorandum account deficit.

Table 6: Projected impact of the proposed new fees on the memorandum account deficit ($million)

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | 2015/16 | 2016/17 | 2017/18 | 2018/19 | 2019/20 |  | 2022/23 |
| Revenue | 26.267 | 27.325 | 27.211 | 27.100 | 26.994 |  | 26.700 |
| Expenditure | 23.620 | 24.120 | 24.620 | 25.120 | 25.380 |  | 25.980 |
| **Surplus/Deficit** | 2.647 | 3.205 | 2.591 | 1.981 | 1.615 |  | 0.720 |
| Memo account opening | -13.901 | -12.189 | -9.757 | -7.781 | -6.294 |  | -2.351 |
| Capital charge | -0.935 | -0.772 | -0.615 | -0.494 | -0.399 |  | -0.143 |
| Net movement | 1.712 | 2.433 | 1.976 | 1.487 | 1.215 |  | 0.577 |
| **Memo account closing** | -12.189 | -9.757 | -7.781 | -6.294 | -5.079 |  | -1.775 |

1. The impact of this option on individual fees is described below. While some fees would increase, others would decrease or stay the same.

### Class 4 annual compliance fee

1. Annual compliance fees are charged for every gaming machine operated by a Class 4 operator. This fee covers all gambling regulation activities not covered by other fees, notably information and education activities, sector monitoring, audits, and investigations and prosecutions.
2. Under this option, the annual compliance fee for non-club societies and large club societies (those with eight machines or more) would increase from $378.00 to $595.77 in the first year and in a stepped manner in subsequent years. This is to reflect forecast revenue decline and increasing costs and to reduce the deficit in the memorandum account. The annual compliance fee for small club societies (those with seven machines or less) would be lowered. The lower fee reflects the lower compliance costs that small club societies present to the Department.

### Class 4 licensing fees

1. Under this option, fees for new entrants to the sector and for the renewals of some licences would increase to more accurately reflect the costs incurred by the Department in processing these applications.
2. The Department undertakes significant due diligence to assess the suitability of gambling operators and venue operators, which is not reflected in the current fees. Therefore, under this option, an application to be approved as a *new* Class 4 non-club society would increase from $3,616 to $15,795. The fee for *new* venue licences would also increase for both club and non-club societies. Renewals of non-club society licences would increase from $2,261 to $10,246.
3. Some licensing application fees would remain unchanged. The application fee to be approved as a new club operator and fees for venue licence renewals for both club and non-club societies would not change as the current fees still cover the Department’s costs.

### Class 4 monitoring fee

1. This fee has been charged since the implementation of the EMS in 2008. From 2012, a portion of the EMS fee has been used towards the IGP. The current EMS fee was based on an assumption that gaming machine numbers would stabilise at approximately 20,000. Due to the continued decline in the number of gaming machines, the cost of the daily monitoring and operation work required and the cost of the IGP must now be recovered from a smaller number of machines.
2. Under this option, the monitoring fee would increase from $1.20 to $1.90 per machine per day (or part day) that the machine is switched on.[[11]](#footnote-11)

### Casino fees

1. Casinos pay an annual licence fee that is designed to cover the costs of the work involved in regulating them. Under this option, total revenue from casino licence fees would not change. However, some casino annual licence fees would change with the result that SkyCity Auckland, Queenstown SkyCity, and Queenstown Wharf would pay more and Hamilton, Christchurch, and Dunedin would pay less based on their relative size and the estimated costs incurred by the Department in regulating each casino. The impact of the New Zealand International Convention Centre Project and Licensing Agreement has been factored into the figures for SkyCity Auckland.
2. Casino fees currently partly subsidise the Department’s costs relating to Class 4 regulatory activity (by approximately $1.4 million per annum). The proposed Class 4 fee changes would reduce the subsidy to approximately $0.4 million per annum.
3. The existence of cross subsidies reflects the fact that levels of work undertaken by the Department between Class 4 gambling and casino gambling sub-sectors tend to fluctuate. To accommodate this, some gambling inspectors work across both areas and the potential exists for the costs of each sub-sector to vary each year, depending on what issues arise. The Department would monitor workloads and costs closely to determine if the respective costs are being allocated appropriately.

### Miscellaneous fees

1. These fees include appeals to the Gambling Commission, associated person approvals (casinos), and certificates of approval (casino employees). The two fees for casino person approvals would increase to better reflect the costs of processes such as police background checks that must be completed for the applications. The certificate of approval application fee would also increase from $292 to $836. Other amendment or notification fees for Class 4 operators would decrease in line with actual costs to the Department. The other miscellaneous fees would remain unchanged due to infrequency of use or little changes in costs.
2. Other fees in this category include those for Class 3 licences. Licences are required when conducting Class 3 gambling. Two fee levels apply depending on the value of prizes. These fees would not change due to low volumes and because the current fee still reflects the work required to issue the licences. Amendments to Class 3 licences would no longer be charged due to low volumes and the potential for licence amendment fees to create a barrier to compliance.

### Risks, costs and benefits

1. For modelling the level of fee increases under this option, the Department has conservatively assumed that:

* the number of Class 4 gaming machines would continue to decline at the rate they have been (approximately 500 per year) thus reducing revenue; and
* annual volumes of licensing activity would decrease because of the combined impact on non-club societies of the proposed fee increases and recent regulatory change in the Class 4 sector.

1. It is possible that the rate of decline in gaming machine numbers will slow, as the sector continues to rationalise, and reach an “optimum” number earlier than assumed (that is within three years). It is also possible that volumes of licensing activity will be greater than assumed. The effect of these scenarios is that the memorandum account reduces more quickly due to over-recovery of revenue.
2. Conversely there is also potential for under-recovery of revenue. As part of recent regulatory change in the Class 4 sector, new regulations requiring non-club societies to progressively increase the minimum amount they return to communities from gaming machine proceeds came into effect. The first increase on 4 September 2014 raised the minimum rate of return to 40 per cent of gross gaming machine proceeds. The minimum rate will increase to 41 per cent in 2016 and 42 per cent in 2018. Further changes are proposed to the Act and regulations, some of which are intended to reduce compliance costs for the Department and societies.
3. The Department’s analysis indicates that most non-club societies should comfortably afford an increase in fees and an increased rate of return to 40 per cent. However the longer term increase to 42 per cent in 2018 is likely to require more of an adjustment to the operations of non-club societies.
4. This option would increase costs for the Class 4 sector. Class 4 fees are paid from the gross proceeds earned through the operation of gaming machines. As such they form a part of a society’s overall budget and affect the amount of money available to be returned to the community as grants. If the fees are set too high, there is a risk that less money is returned to the community or that the society will exit the sector altogether. The Department would carefully monitor the financial situation and, if necessary, bring forward its planned 2017/18 review of fees to consider whether the fee levels need to be adjusted.
5. The Department considers that the fee increases proposed under this option fairly cover costs and strike a reasonable balance in reducing the memorandum account deficit. Fees have not changed since 2008 and the sector has been effectively experiencing a reduction in fees payments over time as the number of machines have declined. Class 4 fees currently account for approximately 2.06 per cent of societies’ GST-exclusive gross gaming machine proceeds. With the proposed fees this is forecast to increase to 3.16 per cent of societies’ GST-exclusive gross proceeds in 2015/16 (refer to table 7 below).
6. The main benefit of this option is that it will ensure the continued operation of the compliance and enforcement activities that the Department undertakes. These activities are important for the general public, so it can be assured that current levels of regulatory oversight are maintained.

Table 7: Total impact on Class 4 societies from the bulk of the proposed new fees (GST exclusive)[[12]](#footnote-12)

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Class 4 operator type | Total annual current fees | Total proposed fees 2015/16 | Total percentage increase | Gaming machine proceeds (2013/14) | Fee increase as a % of gaming machine proceeds |
| Small club societies  (1-7 machines) | $377,432 | $429,380 | 13.76% | $3,540,980 | 1.47% |
| Large club societies (8+ machines) | $2,656,633 | $4,042,345 | 52.16% | $88,113,413 | 1.57% |
| Small non-club societies  ( 1-9 venues) | $1,074,783 | $1,690,389 | 57.28% | $60,855,988 | 1.01% |
| Large non-club societies (10+ venues) | $10,002,990 | $15,517,194 | 55.13% | $534,122,343 | 1.03% |
| **Total** | **$14,111,838** | **$21,679,308** | **53.62%** | **$686,632,724** | **1.10%** |

## Option two: status quo

1. Under this option there would be no change to fee levels. The risk of this option is that it would lead to a significant increase in the memorandum account deficit (refer to table 3 above) and a reduction in resources to regulate the gambling sector.
2. Forecast expenditure levels for 2014/15 and beyond are in excess of current revenue. Currently the costs of regulating the gambling sector are being partially met by the taxpayer rather than the industry. Retaining the status quo is not a viable option in the medium to long term as the gap between revenue and costs will continue to grow (refer to figure 2 below). Allowing the deficit in the memorandum account to continue to increase means that the taxpayer will continue to cover the costs of gambling compliance and enforcement, rather than the operators that give rise to these activities.

Figure 2: The Department’s actual and projected revenue and expenditure on gambling regulation from 2008/09 to 2016/17 if status quo retained ($million, GST exclusive)[[13]](#footnote-13)

## Other options considered

### Larger fee increases to enable more proactive compliance work

1. During the Department’s fees review, an alternative proposal was considered. The proposal involved fees that would fund more proactive compliance work and initiatives aimed at reducing the need for enforcement action in the sector. This option was rejected on the grounds that its cost impact on the gambling sector would be too high. Option one (the preferred option) is the absolute minimum revenue increase required to cover costs and reduce the memorandum account deficit over time. It does not include any new activities or staffing.

### Reduce costs further

1. The Department also considered the option of reducing costs further. The Department considers that meaningful cost savings (i.e. savings that would significantly reduce the proposed level of fee increases) could only be achieved by further reducing the number of staff employed in gambling regulation. The risk of this option is that further reducing staff numbers to levels that create meaningful savings would severely affect the Department’s ability to meet its statutory obligations, and lead to poorer regulatory outcomes.
2. As noted above, the Department is already operating at the lowest number of staff committed to gambling compliance and enforcement work since 2004 [refer paragraphs 40 to 42 above]. This is despite the fact that the gambling sector continues to pose significant and complex regulatory challenges. As discussed, non-compliance in the Class 4 sector increasingly involves complex, large scale fraud and criminal activity [refer paragraphs 28 to 31 above]. This means that more resource intensive background and financial analysis is required, for example when assessing the suitability of a new Class 4 operator or issuing a new venue licence.
3. The purposes of the Act include an emphasis on the prevention and minimisation of gambling-related harm and the limiting of opportunities for crime and dishonesty associated with gambling. A further reduction in staff numbers is likely to result in a reduction in the level of regulation. Organised crime, increased grant fraud, problem gambling and the proliferation of crime to meet gambling debts are all potential results from unregulated gambling operations.
4. The Department’s view is that further reductions in staff numbers would be unworkable, given the objectives and requirements of the Act and the public interest in a well-run gambling sector. The large amount of money spent by gamblers on Class 4 gambling ($808 million in 2013/14) and subsequent proportion returned to the community through grants ($242 million in 2013/14) underlie the importance of ensuring that the regulatory system is effective and has integrity.
5. Other cost savings have been considered and discounted. The maintenance of the EMS and the implementation of the IGP, coupled with the modernisation of processes and technology, are critical to undertaking regulatory activity. These investments and ongoing maintenance requirements represent fixed costs that are difficult to reduce. Similarly the Department’s response to non-compliance and legal contestation are mandated by the Act. As the primary regulator of the gambling sector, the Department must investigate non-compliance and defend the decisions of the Secretary of Internal Affairs and/or the Commission.

## Implementation

1. If new fees are approved, it is proposed that they will come into effect from   
   1 October 2015. Information will be provided to those affected to inform them of the new fees. There are no proposed changes to methods of payment at this time.

## Monitoring, evaluation and review

1. The Department will be monitoring the effect of any proposed new fees on the sector, particularly as the increases in the minimum rate of return take effect. A key factor would be whether the fees are recovering the required amounts and not under-recovering or over-recovering. The number of venues changing hands or societies struggling to meet their maximum returns to the community would also be monitored to assess the impacts. As noted earlier, the Department’s intention is to review the fees regime again in 2017/18, or earlier if necessary.

## Questions for you

How will these proposals affect you?

Are there other options for funding that we have not considered? If so, what?

Under the preferred option, have the costs to the sector and the benefits of effective regulation been correctly identified?

Is the basis for the Class 4 compliance fee the right one? Should something other than machine numbers, gaming machine proceeds or venue numbers be considered as the basis for this fee?

Should smaller clubs (with less than seven machines) pay a lower compliance fee than other clubs and non-club operators?

1. Schedule of proposed fees (GST exclusive)

| Fee type | Current fee ($) | Proposed fee 2015/16 ($) | Proposed fee 2016/17 ($) | Proposed fee 2017/18 ($) | Proposed fee Out years  2023/24 ($) | Estimated volume of transactions (2015/16) |
| --- | --- | --- | --- | --- | --- | --- |
| **Class 3 Operator Licence**  New or renewal (prizes not exceeding $50,000)  New or renewal (for prizes of $50,000 or more)  Amendment to licence | 88.89  628.44  305.78 | 88.89  628.44  0 | 88.89  628.44  0 | 88.89  628.44  0 | 88.89  628.44  0 | 56  20  7 |
| **Class 4 Operator Licences**  New (club societies)  New (non-club societies)  Amendment or notification (key person)  Amendment or notification (other)  Renewal (club societies)  Renewal (non-club societies)  Operator’s annual fee (non-clubs) | 3,616  3,616    565.33  225.78  1,129.78  2,260.44  3,611.56 | 3,616  15,795  565.33  169  1,129.78  10,246  3,611.56 | 3,616  15,795  565.33  169  1,129.78  10,246  3,611.56 | 3,616  15,795  565.33  169  1,129.78  10,246  3,611.56 | 3,616  15,795  565.33  169  1,129.78  10,246  3,611.56 | 6  2  446  2,932  200  35  35 |
| **Annual compliance fee (per gaming machine) – non-clubs and larger clubs** | 377.78 | 595.77 | 627.27 | 661.13 | 930.35 | 13,810 |
| **Annual compliance fee (per gaming machine) – small clubs** | 377.78 | 295.50 | 304.50 | 313.50 | 368.30 | 320 |
| **Class 4 venue licences**  New venue licence (club)  New venue licence (non-club)  Renewed venue licence (club)  Renewed venue licence (non-club) | 678.22  904  112.89  169.78 | 2,054  2,567  112.89  169.78 | 2,054  2,567  112.89  169.78 | 2,054  2,567  112.89  169.78 | 2,054  2,567  112.89  169.78 | 6  133  200  765 |
| **Daily monitoring fee** | 1.20 | 1.90 | 1.90 | 1.90 | 1.90 | 360 days x no. of EGMs x 90% |
| **Certificate of Approval (casino staff)** | 291.56 | 836 | 836 | 836 | 836 | 400 |
| **Associated person approval** | 293.33 | 836 | 836 | 836 | 836 | 2 |
| **New casino operator’s licence** | 302,222.22 | 302,222.22 | 302,222.22 | 302,222.22 | 302,222.22 | 0 |
| **New casino venue agreement** | 20,444.44 | 20,444.44 | 20,444.44 | 20,444.44 | 20,444.44 | 0 |
| **Amendment to casino operator’s licence, venue agreement and venue licence** | 888.89 | 888.89 | 888.89 | 888.89 | 888.89 | 0 |
| **New or renewed promoters’ licence**  **Temp licensed promoter authority** | 1,222.22  88.89 | 2,567  88.89 | 2,567  88.89 | 2,567  88.89 | 2,567  88.89 | 0  0 |
| **Filing appeal with Gambling Commission** | 222.22 | 222.22 | 222.22 | 222.22 | 222.22 | 5 |
| **1-day, half day and part half day hearing** | 400 | 400 | 400 | 400 | 400 | 0 |

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Casino fees | Current fee ($million) | Proposed fee 2015/16 ($million) | Proposed fee 2016/17 ($million) | Proposed fee 2017/18 ($million) |
| **Auckland** | 2.573 | 2.852 | 2.852 | 2.852 |
| **Hamilton** | 0.652 | 0.550 | 0.550 | 0.550 |
| **Christchurch** | 1.114 | 0.813 | 0.813 | 0.813 |
| **Dunedin** | 0.495 | 0.446 | 0.446 | 0.446 |
| **Queenstown Sky City** | 0.211 | 0.304 | 0.304 | 0.304 |
| **Queenstown wharf** | 0.197 | 0.278 | 0.278 | 0.278 |
| **Total** | 5.242 | 5.242 | 5.242 | 5.242 |

1. While you may indicate the information you would like withheld, it can only be withheld if it meets the relevant criteria under the Official Information Act 1982. [↑](#footnote-ref-1)
2. Class 3 gambling is gambling where prizes exceed $5000 (including housie, large raffles and some instant games) and requires a licence from the Department. [↑](#footnote-ref-2)
3. The current published Regulations include GST at the previous rate of 12.5 per cent. To avoid confusion all figures will exclude GST unless otherwise stated. It is proposed that any new regulations be made exclusive of GST so that any future tax changes will not affect figures used in the Regulations. [↑](#footnote-ref-3)
4. A full list of current fees can be found in the Appendix. [↑](#footnote-ref-4)
5. Treasury circular 2011/10 *Guidance for the operation of departmental memorandum accounts*. [↑](#footnote-ref-5)
6. For more information please refer to <http://www.treasury.govt.nz/publications/guidance/instructions/2014/22.html> [↑](#footnote-ref-6)
7. At December 2013 there were 85 FTE staff committed to gambling compliance and enforcement work compared with 105 in 2007. [↑](#footnote-ref-7)
8. In 2007, it was projected that 111 FTE staff would be involved in implementing the regulatory regime for gambling. The actual number from 2007/08 was 105 FTE staff. [↑](#footnote-ref-8)
9. The table assumes $80,000 per annum for the average FTE and $35,000 for overheads.  A 2.5% annual increase in salary costs is included. [↑](#footnote-ref-9)
10. For more information about the Treasury guidelines see <http://www.treasury.govt.nz/publications/guidance/planning/charges> and for more information about the OAG principles see <http://www.oag.govt.nz/2008/charging-fees>. [↑](#footnote-ref-10)
11. The Department has assumed that 90 per cent of licensed gaming machines will be operated over 360 days per year. [↑](#footnote-ref-11)
12. Based on societies and venues operating as at 30 June 2014 and includes licensing, monitoring and compliance fees but does not include other amendment or notification fees which are proposed to decrease. [↑](#footnote-ref-12)
13. Note that fee revenue was higher in 2012/13 due to an accounting change that saw some revenue not treated correctly in earlier years. [↑](#footnote-ref-13)