

GAMBLING IN CALIFORNIA

By

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January 1997

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Acknowledgments

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I. Gambling in the United States

“Gambling is inevitable. No matter what is said or done by advocates or opponents of gambling in all its various forms, it is an activity that is practiced, or tacitly endorsed, by a substantial majority of Americans.”

-- Commission on the Review of National Policy toward Gambling, 1976, p.1.

In 1973, the Commission on the Review of National Policy toward Gambling was created to study gambling in the United States. The Commission began its report with the above statement and it is appropriate for this report. While the statement is merely the opinion of the Commission and cannot be easily proven, it is easy to understand how they formed their opinion. If you read the history section of this report, you will see that the popularity of legal gambling has waxed and waned, but has never disappeared. Illegal gambling, although we are ignorant about the full extent of it, has shown remarkable endurance. One industry observer noted, “There is a public demand to gamble, but there is no public demand for legalized gambling.”¹ The acceptance of gambling today can be seen by the substantial numbers of players of the various state lotteries and similar illegal games.

This report will use the terms gambling and gaming interchangeably. Within the gambling industry, the term gambling has fallen into disfavor and is being replaced by gaming.

Legal Gaming Has Expanded Greatly Throughout the Country. Legal gambling activities include state lotteries; parimutuel betting on horses, greyhounds, and jai-alai; sports book-making; card games; keno; bingo; slot machines; progressive slot machines; video poker machines; video keno machines; video blackjack machines; and video roulette machines. Not all of these are legal in all places. These activities have grown tremendously, especially when considering that virtually all have been only recently legal in most states. This growth of gambling has been remarkable: in 30 years gambling has transformed itself from sinful to well accepted.² But the spread has been inconsistent, with each state selecting the type of gaming that it supports or at least condones. Some states have casinos, but no lotteries. Other states have lotteries, but no casinos. Some have both.

Illegal gambling still exists and, by many accounts, flourishes.³ Not surprisingly, there is not a lot of data about illegal gambling. The most popular forms of illegal games are “numbers,” which is essentially a lottery, and betting with bookies, typically sports betting. Sports betting, in particular, is thought to amount to a large sum. Some analysts think it is the largest category of gambling after casino games.⁴

Views on Gambling Vary. Gambling is regarded by some as a vice, a sinful activity which corrupts society. Others view gambling simply as a harmless form of entertainment. These contrasting views help shape the regulation of gambling. The regulation of gambling is unusual as society regulates gambling like no other business.⁵ Overall, society has taken a cautious view of gambling. Only limited types of games are legal. Gambling is heavily regulated because of concerns about criminal involvement. Because of the large amount of cash involved, gambling is an attractive target for criminals.

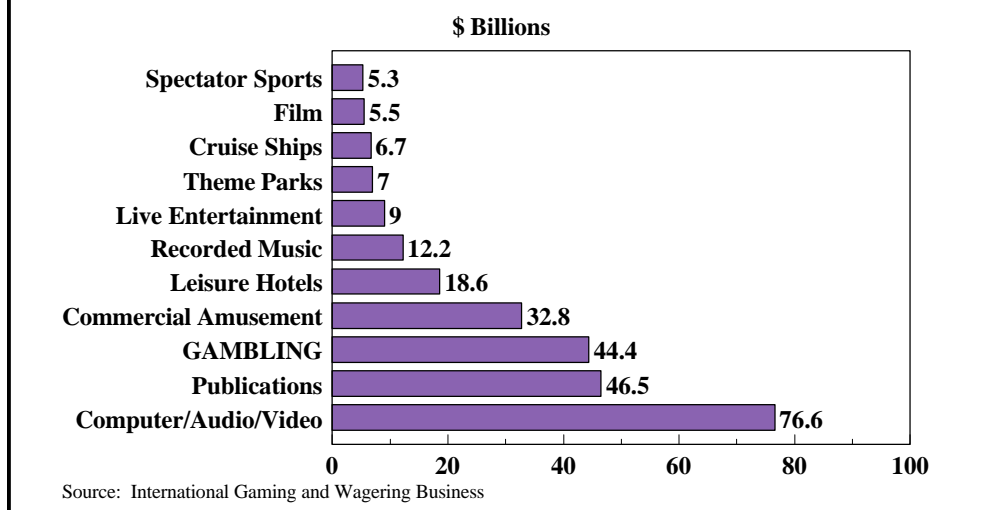
Others look at gambling in economic terms. Legalized casino gambling, whether in Las Vegas, Atlantic City, or on Indian land, rose out of the desire for economic stimulus, although other factors also played a role. Lotteries are regarded by state governments as a revenue-generating tool.

Why has gambling grown? There are a variety of possible explanations.⁶ One explanation for the spread is that states need the revenue and are hooked on gaming funds. Another related view is that government has said it is acceptable, hence people are more willing to participate. Some observers attribute the domino effect. The domino effect of gambling occurs when one state legalizes gaming, other states legalize gambling so they do not lose money to their neighbors. The spread of lotteries can be seen as an example of the domino effect. The current wave of legal lotteries started in New Hampshire, spread to other North-Eastern states, and then across the nation. Right now, the states that do not have lotteries are clustered primarily in the South. Similarly, riverboat casinos were first legalized in Iowa, then Illinois, followed closely by Missouri, Indiana, Louisiana, and Mississippi.

Regardless of viewpoint, there is little doubt that gambling is a very popular activity in the United States. By 1994, every state except Utah and Hawaii had some form of legal commercial gambling. Casino gambling, including Indian gaming, is legal in 27 states and most of the casinos have been built in the last 5 years.⁷

The Gaming Sector is a Large Entertainment Industry. In 1995, gambling in the United States grossed over \$40 billion in revenues. Although this total does not include illegal gaming, it is still quite large compared to some other entertainment industries. The same year, the estimated receipts for amusement parks were \$7 billion, including admission fees, sales of food and beverages, and other sales. The estimated receipts for movie theaters were \$5.5 billion.⁸ Gambling is clearly a major form of entertainment.

Gambling is a Major Category of U.S. Leisure Spending



Another way to look at gambling's relative popularity is through the public's participation. In 1993, the last full year before the baseball strike, 70 million fans went to the ballpark, while 92 million visited casinos.

The preceding comparisons were made using gross revenues, but the amount of money people spend gambling is usually measured by one of two methods.

- "Handle." A popular form of measurement is the handle, which is the total amount of money that a player spends purchasing lottery tickets, parimutuel bets, or playing casino table games or slot machines. Since the total amount includes winnings, it is a much larger number than what players actually lose.
- "Gross Revenues." The amount of money that bettors lose gambling is called gross revenue, or also known as consumer gambling losses. Gross revenues are the actual net income retained by the operator after the payment of prizes, but before deducting the other costs of operating the gambling establishment.

The handle is popularly used for measurement, but it can be misleading. Because it is the amount wagered before payment of prizes, the handle tends to inflate the economic importance of gambling. Gross revenues are a better measurement when comparing gaming to the rest of the economy.

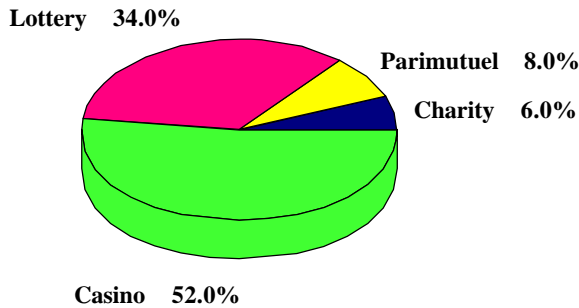
An example may help illustrate the difference. A player spends a dollar playing video poker and wins \$4. The \$4 is fed back into the machine until she loses the \$4 plus her original dollar. In this example, the handle would be \$5. But the gross revenue and the amount the player lost out of pocket is only \$1.

There Are Four Major Types of Legal Gambling. According to one well-known researcher, these include charitable gaming, parimutuel betting, casino gaming, and lotteries.⁹ There is some potential confusion that may arise from these definitions. The definition of casinos include what most of us would expect, i.e. the Las Vegas-style casinos that are found in Nevada, Atlantic City, and a few other locales. In California, cardrooms advertise themselves as casinos, but they don't offer the games that one expects from casinos, namely banked games, especially slot machines. The cardrooms found in California are an anomaly and don't fit into the major categories. They are discussed later in Chapter V on "Gambling in California." The following chart shows the relative size of the different types of gambling.



But Relatively Greater Gross Profits go to Other Games

1995



Sources: International Gaming and Wagering Business, California Research Bureau

Charitable Gambling

Charitable gambling is run for the benefit of nonprofit organizations, although the nonprofit may not necessarily be the operator of the games. Some examples of charitable gambling are PTA Monte Carlo nights and church raffles. The most popular form of charitable gambling is bingo. Charitable bingo is legal in all but five states. In California, bingo is the only charitable game that is legal.

Despite the nonprofit nature of charitable gaming, it has come under criticism. One reason is that it is the area of gambling that is the least regulated. As the tables and graphs show, it accounts for a significant amount of money even if the total is dwarfed by that of casinos. According to some industry observers, there are serious problems of fraud, theft, cheating, and accounting irregularities.¹⁰ In California, charitable games have been victimized by robbers because of the large amount of cash generated by bingo.

Parimutuel Wagering

Parimutuel wagering refers to the type of gambling where the total prize pool is based upon the amount of money wagered. The more money gambled, the bigger the prize. Horse racing is the best known and widespread parimutuel betting event. Horse racing is the only form of parimutuel wagering legal in California.

Dog racing and jai-alai are less popular parimutuel betting events. Dog racing operates in 17 states, while jai-alai is legal in just three: Connecticut, Florida, and Rhode Island. Dog racing is, as suggested by the name, a race among greyhounds who chase after a mechanical rabbit. Jai-alai is a game played by two or four persons and its action is similar to handball.

Parimutuel wagering has not been able to compete well with the myriad of new forms and types of gambling. Observers attribute its decline to the complicated nature of the sports,

especially for the new gambler.¹¹ The industry is changing, however, some racetracks are adding casino games. Situating casino games with the track exposes other gamblers to horses and thereby parimutuel wagering. In turn, this may lead to increased parimutuel participation.

Lotteries

Lotteries have a long tradition in this country. They were used to raise money in support of the first North American colonies. Lotteries continued to be used by the original thirteen colonies to raise necessary revenue for the development and the successful independent operation of the new settlements. Though early lotteries were successful in raising money, the scandals from crooked operations strengthened the hand of antigambling forces, eventually leading to prohibition of lotteries in many states. From 1894 to 1964 no legal government-sponsored lotteries operated in the United States. The long and colorful history of lotteries in the United States is described in more detail in the history section of this report.

Legal Lotteries Experienced a Rebirth in the 1960s. The first legal lottery in the twentieth century was the New Hampshire Sweepstakes which began on March 12, 1964. Other North-Eastern states quickly followed. In 1981, Arizona became the first state west of the Mississippi to authorize a lottery. Currently 37 states and the District of Columbia operate lotteries.

Casino Gaming

Casino gaming is the largest part of the commercial gambling market. Casino gaming continues to grow in popularity, fueled by the creation of new casino destinations and the expansion of existing casino locales.

A casino is usually characterized by the offering of banked games. Banked games are where the house is banking the game and basically acting as a participant. That is, it has a stake in who wins. In contrast in a non-banked game, like the lottery, the operator does not care who wins. As noted earlier, cardrooms such as those in California are not included. They are often called casinos, but they do not offer banked games.

Currently, ten states have legalized some form of commercial, non-tribal casino gambling with banked games. These are what the typical observer would call Las Vegas style casinos.

The following chart lists the states and the year each made casino gambling legal. Note the rapid growth since 1989.

State	Form of Casino Gaming	Year of Legalization
Nevada	Unlimited Stakes	1931
New Jersey	Unlimited Stakes	1976
South Dakota	Limited Stakes	1989
Iowa	Riverboat	1989
Colorado	Limited Stakes	1990
Illinois	Riverboat	1990
Mississippi	Riverboat, Dockside	1990
Louisiana	Unlimited Stakes, Riverboat	1991
Missouri	Riverboat	1992
Indiana	Riverboat	1993

This chart does not include Indian gaming, which is discussed later.

For almost 50 years casino gaming was only legal in Nevada. There, legal state-regulated gaming was dominated by organized crime. In the late 1950s, the state first permitted publicly-held companies to own and operate gaming facilities, which eventually led to the entrance of companies such as Hilton and Ramada into the industry, improving the industry's reputation. It was at this time that intense gaming activity spread from downtown Las Vegas to the Strip and began to grow in Reno and Lake Tahoe. Since then, gaming in Nevada, and especially Las Vegas, has become a multibillion-dollar industry that attracts millions of people each year.

Nevada enjoyed a long period with little legal competition. New Jersey's statewide referendum legalized gambling in 1976. The first Atlantic City casino opened in 1978. Since then, eight other states have legalized casino type gambling.

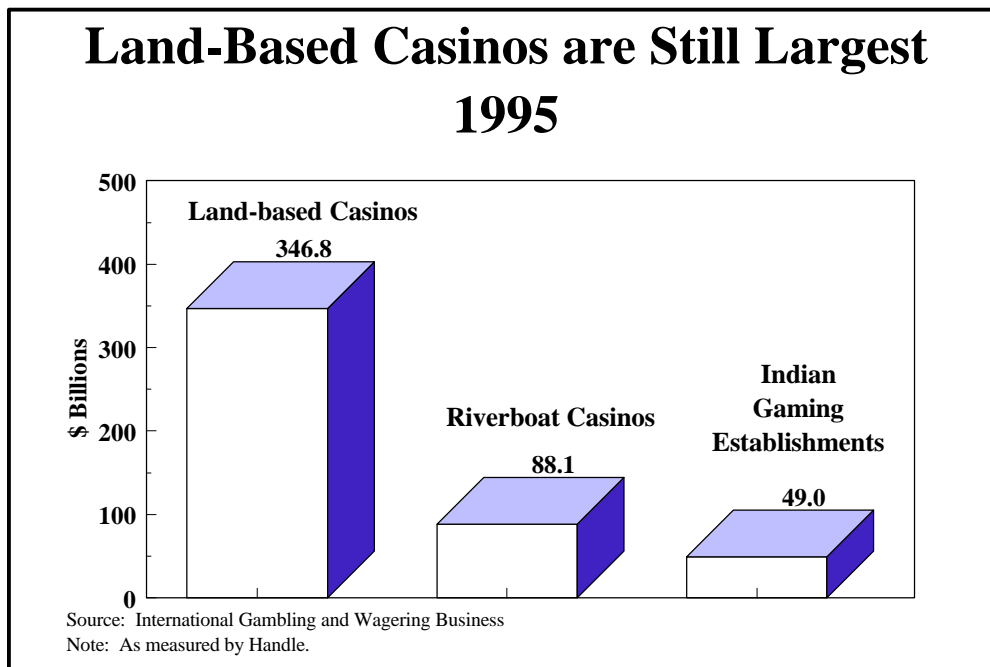
The first state that authorized one of the new wave of legalized casinos was in South Dakota. In 1989, South Dakota legalized limited-stakes casino gambling in the historic mining town of Deadwood. In 1990, Colorado followed when voters in that state approved limited-stakes casino gambling in three former mining towns: Cripple Creek, Black Hawk, and Central City.

In 1989, Iowa and Illinois legalized riverboat casino gaming and, in April 1991, Iowa launched the first gaming vessel in recent U.S. history. Riverboat casinos are now legal in six states: Illinois, Indiana, Iowa, Louisiana, Mississippi, and Missouri. Currently there are about 65 boats operating in these states. The type of gaming allowed on riverboat casinos varies by jurisdiction. Generally, the states allow the playing of traditional casino games such as blackjack, roulette, and slots.

Riverboats Present a Good Example of the Domino Theory of Making Gambling Legal. Illinois' statute was more liberal than Iowa's, leading to a riverboat regulation war. Gaming revenues began to decline in Iowa in 1993 when the riverboats moved out of Iowa to locations with more favorable regulations. Iowa had established a \$5 maximum wager and a \$200 per customer loss limit. Illinois did not have a wager or loss limit and the riverboat casino centers in Illinois were closer to population centers. In 1994, in an effort to reverse the industry's decline, the voters in Iowa voted to eliminate wager and loss limits.

The advent of riverboat gaming also led to increased Indian gaming, when Indian tribes were allowed to operate the same kinds of gambling allowed within a state. A Nebraska tribe even attempted to buy property in Iowa to open a casino.

Riverboat Gaming Has Captured 20% of the Casino Market Share. Mississippi now has more gambling square footage than Atlantic City. The International Gaming and Wagering Business magazine reported casino revenue figures for 1995 as shown in the chart below.¹²



There are two major categories of riverboat casinos, excursion and dockside. Excursion riverboats cruise along some waterway, while dockside casinos are tethered to the shore during operations. Dockside casinos are usually just a land-based casino on pilings or a floating, but not navigable, platform.

The excursion requirement was important in the beginning because it provided a subtle transition into legal gambling, giving the public an impression that the gambling could be isolated and controlled. The gambling takes place in a restricted location, namely on a boat traveling on the waterways and the amount of activity is limited by the length of the excursion. If the excursion is three hours, then the amount of gambling is limited to the

three hours on the river, plus another half hour or so while the boat is tied up for loading and unloading. Many analysts believe that the perception that riverboat gambling would be physically contained made legal gambling an easier sell to the voters.

Some states are eliminating the law concerning the cruising requirement. Dockside casinos are more popular because some customers do not like to be cooped up for a set period of time, and some do not like having to leave when the ship is moored. Eliminating the cruising requirement also reduces the possibility of accidents on the waterways. Mississippi has no cruise requirements on their riverboat casinos. Other states allow for some flexibility for bad weather and choppy waters. According to a representative of Hilton Hotels Corp., which operates a riverboat casino in New Orleans, “admission revenues rise 40% and gambling revenues increase as much as 20%” when the ship is kept at the dock.¹³ The riverboat casino industry is trying to convince other states to eliminate the cruising requirement. In this way, riverboat gambling has become an indirect path to land-based gaming.

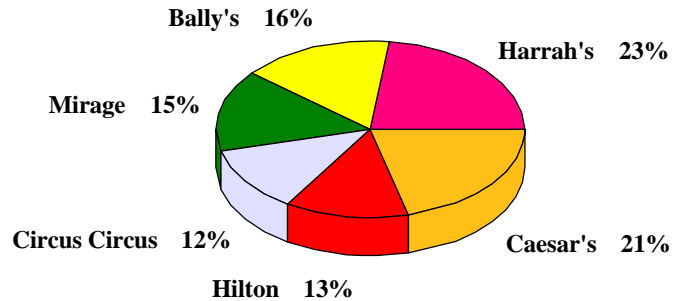
In 1992, Louisiana became the third state to legalize land-based casino gambling. Voters narrowly approved legislation to establish a riverfront facility in New Orleans. The legislation permits a single facility in downtown New Orleans and a temporary facility to be operational while the permanent facility is under construction. On November 21, 1995, the partnership that owns the casino venture filed for Chapter 11 bankruptcy. The temporary casino was closed and the construction of the new facility was halted while the organization under went restructuring. Harrah’s is the lead partner in this effort. New Orleans is the first casino in a major city other than Nevada. Concerns about the industry’s survival were allayed when casino gaming was ratified by a large margin of voters in a referendum in November 1996.

Las Vegas Expands to Meet the Challenge From Competing States. With competition from new gaming locales and other parts of the entertainment industry, the owners of major casino properties in Las Vegas have not stood still. While other markets rely on their local population, the Las Vegas market is almost entirely reliant upon the tourist business that the casinos generate.

Many of the major developers are turning Las Vegas into a family-oriented destination resort, complete with grand spectacles and theme parks. In late 1993, Circus Circus’ pyramidal Luxor opened, featuring an Egyptian theme and amusement park. Shortly thereafter, the Mirage’s Treasure Island opened with a pirate theme and a regularly scheduled sea battle outside the facility. The new MGM Grand has a Wizard of Oz theme park. Las Vegas visitation in 1994 was very strong, up approximately 24% from 1993. Almost 30 million visitors came in 1994, approaching the level of Atlantic City.

As the following chart shows, the big operators in casino amusement are large publicly-owned companies. If the merger between Hilton and Bally’s goes through, it will create the largest company in the country, surpassing Harrah’s.

Top U.S. Publicly-Owned Casino Companies



Source: Harrah's Casinos

Note: Based on total casino revenues for these large companies of \$3.8 billion.

Indian Gaming

Indian tribes have used their position as sovereign entities to develop a number of gaming establishments. Indian casinos operate in 22 states: Arizona, California, Colorado, Connecticut, Idaho, Iowa, Kansas, Louisiana, Michigan, Minnesota, Mississippi, Montana, Nebraska, Nevada, New York, North Carolina, North Dakota, Oklahoma, Oregon, South Dakota, Washington, and Wisconsin. This number is expected to grow.

The opportunity for economic development through gambling has piqued the interest of many Indian tribes. The U.S. Bureau of Indian Affairs reported that there are 545 federally-recognized Indian tribes in 35 states. Gambling on Indian-owned land has grown in popularity and there are approximately 150 to 175 casinos and bingo halls currently in operation.¹⁴

Gambling has represented an opportunity for tribal self-reliance and a chance to reverse some of the poverty that has affected many of the tribes. Indian tribes started offering games similar to those being offered by charities, such as bingo. In order to gain a competitive advantage, some tribes began offering high-stakes bingo, an option that was not available to the charities because of state laws. The growth of Indian gaming led to many court battles, including some important ones in California. This issue is covered in more detail in the section on Indian Gaming.

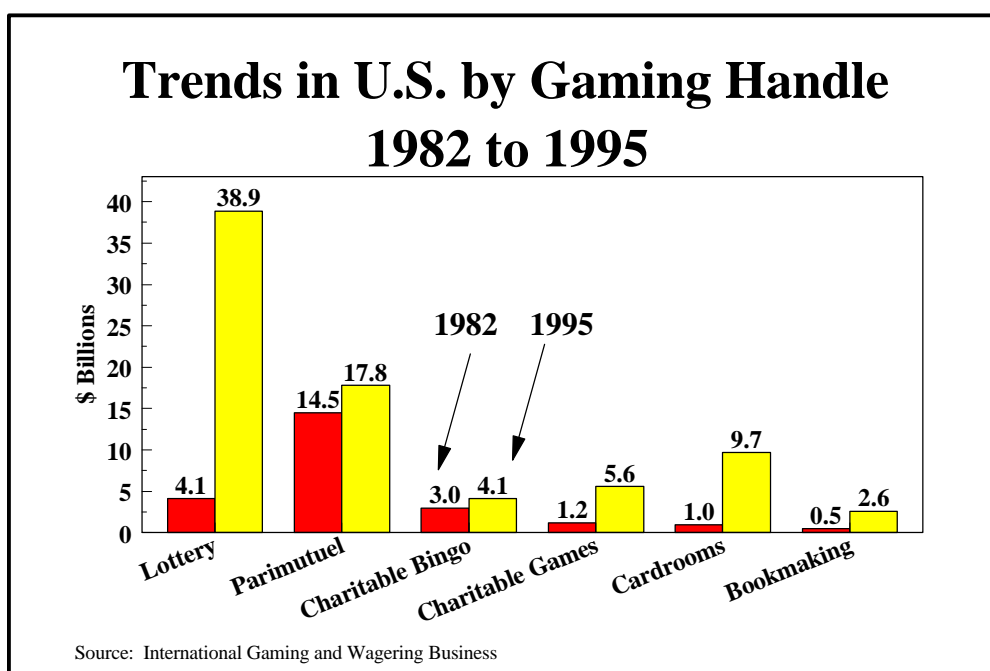
Illegal Gambling

Illegal gaming is popular, though its popularity and prevalence are difficult to measure. An estimated \$32 billion was wagered illegally in 1986, resulting in gross revenues of approximately \$5.6 billion.¹⁵ Another estimate places the illegal gaming handle at about \$48 billion with gross revenues of \$2.4 billion.¹⁶ The most significant forms of illegal gambling

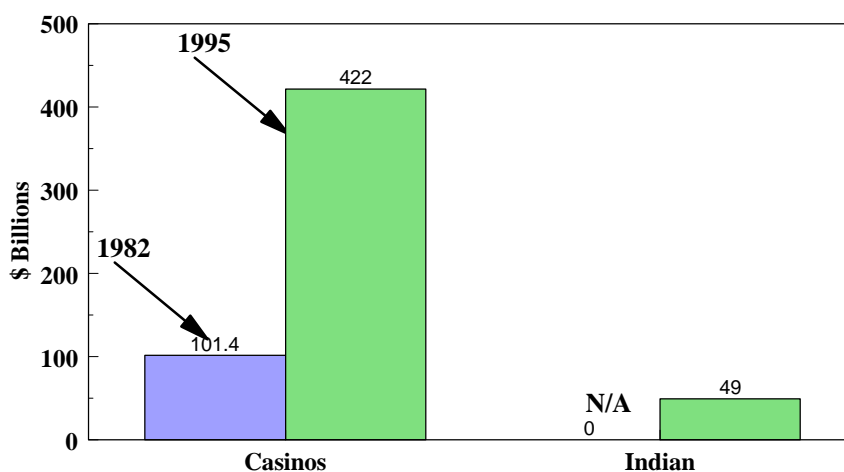
in the United States are numbers, betting with bookmakers or bookies, and sports pools or sports cards. The “numbers” game is similar to the lottery game. Bettors select numbers and hope theirs match the winning numbers that have been randomly selected.

Betting with bookies usually involves placing bets on the outcome of a certain event, such as a sporting event. Sports cards and pools are also bets involving sporting events. Most sports bets are between friends or acquaintances. A smaller amount is made with bookies and the bets are usually under \$100.

All Types of Gambling Have Shown Growth. Although there are numerous types of gaming, a common theme is that they are all growing. The following charts show the growth in the different categories of legal gambling.



Trends in U.S. by Gaming Handle 1982 to 1995



Source: International Gaming and Wagering Business

Gambling is Usually Regulated by a Commission Form of State Agency. Currently in the United States, 48 of the 50 states have legalized some form of gambling. Utah and Hawaii are the exceptions. Regulation of gambling activities across the nation is usually done by commissions.

Parimutuel Wagering

- Forty-three states have parimutuel wagering (horse racing, dog racing, jai alai). Of these 43 states, the great majority have racing commissions whose sole purpose is to regulate parimutuel gaming.
- The exceptions are Connecticut, Florida, Iowa, Nevada, New York, South Dakota, and Wisconsin. These states have parimutuel commissions which regulate other forms of legalized gaming in that state, or have their parimutuel activities regulated by another commission. For example, parimutuel wagering in Nevada is regulated by the Nevada State Gaming Control Board, which oversees all gaming in that state. The Florida Division of Parimutuel Wagering also oversees charitable gaming.

Lotteries

- Thirty-seven states and the District of Columbia have state lotteries. Of these states, the great majority have lottery commissions solely dedicated to regulating the lottery. The commissions also operate the lottery.
- The exceptions are Idaho, Massachusetts, Michigan, and Texas. The lottery commissions in these states also oversee charitable gaming.

Card Rooms

- There are non-casino card rooms in five states: Maryland, Montana, Oregon, Washington, and California. California's industry is by far the largest. There is statewide regulation in Montana and Washington and local regulation in Oregon, Maryland, and California.

Casino Gaming

- All of the ten states which have state-legalized casino gambling have gaming commissions which regulate casino gaming activities.
- There are a large number of gaming commissions/boards across the U.S. which regulate legal gaming activities besides casino gaming. (Excluding lottery or parimutuel wagering, which as noted is almost always regulated by a commission.)
- Louisiana had two separate commissions which regulate casino gambling in that state. One commission regulates riverboat casino and the other regulates land-based casino gambling. That was recently changed to one unified commission.
- The Nevada Gaming Control Board serves as the administrative arm of that state's gaming commission.
- There are three states that have a gaming division as part of another state agency. In Montana and New Jersey, these divisions are part of the Department of Justice/ Attorney General's Office. The Colorado Division of Gaming is part of the Department of Revenue. In Colorado and New Jersey these divisions serve the administrative functions of the gaming commission. Montana does not have a gaming commission.

1996 Election Results Suggest Gaming Will Continue to Expand. Prior to the elections, there was concern within the industry that a backlash was beginning to build. As the history section of this report discusses, such a backlash has occurred in the past. There was some evidence that a backlash was starting. Factors slowing growth include:¹⁷

- Referenda to legalize gaming versus legislative action alone.
- Organized and growing opposition that employs effective lobbying and grass roots tactics.
- More conservative political climate.
- Lack of an industry success model and a fractured industry.

In a reverse for the industry, a federal study commission on gambling has been created despite the opposition of the gaming industry and gambling had failed to gain approval in new states. During 1994, the industry suffered some losses in important elections in Florida and Missouri.

However, the 1996 elections changed that view.¹⁸ The industry recorded the following major victories:

- Voters in Michigan voted to allow casinos in Detroit and those in Arizona voted to allow more Indian casinos. This was the first time in American history that the citizens voted to legalize high stakes casinos *in the face of active opposition*.
- Voters in Louisiana opted to keep both land-based and riverboat casinos. In this parish by parish election, some regions opted to ban video lottery terminals while the majority parishes voted to allow them.
- Various minor local elections ended in victory for gambling interests.

Some observers have drawn different conclusions from the election as there were also losses for gambling interests.¹⁹ Nevertheless, there has never been such victories for gaming interests in state-wide contested elections. The vote was even more dramatic when one considered the criminal convictions resulting from Louisiana's gambling scandals. (Discussed in more detail in the Politics and Gambling section of the report.)

The Internet may be the source for the largest growth in gambling. The World Wide Web has three hundred gambling-related sites, some of which have set up operations offshore. The Attorney General of Minnesota has filed a suit against a service that plans to offer sports bookmaking.

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- ¹William Thompson, Professor of Public Administration at University of Nevada, Las Vegas, Richard L. Worsnop, "Gambling Boom," CQ Researcher, 8 March 1994, p. 243.
- ²William R. Eadington, in William R. Eadington and Judy A. Cornelius, eds., Gambling and Public Policy (Reno, NV: Institute for the Study of Gambling & Commercial Gaming, University of Nevada, 1991), p. 3.
- ³Support for this argument can be found by Anthony N. Cabot and Richard J. Schuetz in "An Economic View of the Nevada Gaming Licensing Process," in Eadington & Cornelius, eds., p. 125.
- ⁴Worsnop, op.cit., 248.
- ⁵Cabot and Schuetz, op.cit., p. 125.
- ⁶I. Nelson Rose, "The Rise and Fall of the Third Wave: Gambling Will be Dead in Thirty Years," in Eadington and Cornelius, eds., pp. 67-69.
- ⁷"America's Gambling Fever," U. S. News and World Report, 15 Jan 1996, p. 53.
- ⁸"The United States Gross Annual Wager," International Gaming and Wagering Business vol. 17, no. 8 (August 1996), p. 45.
- ⁹Eadington, op.cit., p. 4.
- ¹⁰*Ibid.*, p. 11.
- ¹¹*Ibid.*, p. 10.
- ¹²"The United States Gross Annual Wager," op.cit., p. 45.
- ¹³Bruce Orwall, "States Take 'River' Out of Riverboat Gambling," Wall Street Journal, 18 October 1995, p. B1.
- ¹⁴Worsnop, op.cit., p. 255.
- ¹⁵Charles T. Clotfelter and Philip J. Cook, Selling Hope: State Lotteries in America, (Cambridge, MA: Harvard University Press, 1989), p. 20.
- ¹⁶Garry J. Smith, "To Do Over Sports Gambling: Sanitizing a Tainted Activity," in Eadington and Cornelius, eds., p 14.
- ¹⁷John J. Rohs and Steven M. Pinsk, Gaming Industry Update, (New York, NY: Wertheim Schroder & Co., 8 March 1995), p. 3.
- ¹⁸I. Nelson Rose, "Legal Gambling's Historic Triumph at the Polls," Gambling and the Law, 21 November 1996, p. 1.
- ¹⁹See for example, William Safire, "Essay: Political Gambling," New York Times, 21 November 1996, p. 29.

II. History of Gambling in the United States

Examining the history of gambling in North America suggests important conclusions that are useful today in considering policies related to gambling.

1. The United States has had a long history of allowing some forms of legal gambling and a degree of tolerance of illegal gambling.
2. Societal tolerance and acceptance of legal gambling can change rapidly. Scandals and political control by gaming interests have led to backlashes which result in regulation and/or prohibition.

Societal standards and laws related to gambling have tended to change back and forth from prohibition to regulation. These changes in law have led one noted observer, Professor I. Nelson Rose, to describe three waves of gambling regulation during the history of the colonies and the United States.¹ The first wave began during the colonial period and lasted until the mid-1800s. The second wave commenced at the close of the Civil War and lasted until the early 20th century. The last wave started during the Great Depression and is still going strong. Because of the length and size of this last wave, another observer has characterized it as an explosion, not a wave.²

The First Wave: 1600's to mid 1800's

The early colonies had very different attitudes towards gambling. Historians have classified the early settlers into two groups, the English who brought along the English traditions and beliefs, and the Puritans. Although the Puritans came from England, they came to the new world to create a better society and discard the values of their mother country. To them, the new world represented an opportunity for establishing a society grounded on Puritan values and beliefs.

Entire colonies were established along the guidelines and beliefs of one group or another. In particular, different attitudes towards gambling were enforced. In New England and Pennsylvania, Puritan attitudes toward gaming and play were adopted. The Puritan-led Massachusetts Bay Colony outlawed not only the possession of cards, dice, and gaming tables (even in private homes), but also dancing and singing. This stance was relaxed slightly the following year so as to allow gaming as long as it was for innocent and moderate recreation and not as a trade or calling. This hostility towards the professional gambler is a common theme that will be seen again as we look at the history of U.S. gambling.

In other colonies, English attitudes towards gambling and recreation prevailed. These settlers brought with them the view that gambling was a harmless diversion. In these colonies, gambling was a popular and accepted activity. Legal gambling tended to be those types that were considered proper gentlemen's diversions. For example, it took a long time for cock-fighting to become legal because it was not considered a suitable game for gentlemen.

One prominent researcher speculates that the appeal of gambling was probably heightened by the frontier spirit. The desire to explore new worlds is similar to gambling. Both rely heavily on high expectations, risk taking, opportunism, and movement.³

Despite the acceptance, gambling began to be blamed for the problems of the colonies. To investors and others in England, the prevalence of gambling suggested an atmosphere of idleness and vice. Financiers began to suspect that it was the root cause of the inability of the colonies to sustain themselves.⁴ The colonies had been relying on England to supply provisions and to replace dying settlers.

Lotteries Used to Bail Out the Early Colonies. Although the financial backers of the colonies viewed gambling as a source of the colonies' problems, they began to see it as the solution as well. The Virginia Company of London, the financier of Jamestown in Virginia, was permitted by the Crown to hold lotteries to raise money for the company's colonial venture. The lotteries were relatively sophisticated and included instant winners. Eventually, the crown banned the lotteries because of complaints that they were robbing England of money.⁵ The company dissolved shortly thereafter.

This episode was not the last use of lotteries to benefit the colonies. All 13 original colonies established lotteries, usually more than one, to raise revenue. Playing the lottery became a civic responsibility.⁶ Proceeds helped establish some of the nation's earliest and most prestigious universities -- Harvard, Yale, Columbia, Dartmouth, Princeton, and William and Mary. Lottery funds were also used to build churches and libraries. Ben Franklin, John Hancock, and George Washington were all prominent sponsors of specific lotteries for public works projects.

Lotteries became an issue in the drive for independence of the colonies. The colonies protested the crown's rules for holding lotteries. In 1769, the crown tried to prevent lotteries from occurring without its permission. Once the war of independence started, the Continental Congress voted a \$10 million lottery to finance the war. The lottery had to be abandoned, however, because it was too large and the tickets could not be sold.

The Popularity of Lotteries Continued in the Early 19th Century. Notable among the later lotteries was a private lottery passed by Congress in 1823 for the beautification of Washington D.C. Unfortunately, the organizers absconded with the proceeds and the winner was never paid.

Lotteries were not the only form of gambling during this era. Wagering on horse racing was a popular form of gambling. Not surprisingly, it was not quite as organized nor as elaborate as modern horse racing. Rather, the gambling was limited to a few friendly bets between owners of horses and their partisans. The first racetrack in North America was built on Long Island in 1665.

Casino gaming started slowly. Taverns and roadhouses would allow dice and card games. The relatively sparse population was a barrier to establishing gaming houses. But as the population increased, by the early 1800s lavish casinos were established in the young republic.

The United States and Gambling Move West. As previously mentioned, gambling and the frontier lifestyle shared similar foundations -- a spirit of adventure, opportunity, and risk taking. During the early 1800s gambling in the lower Mississippi Valley became a legitimate and organized enterprise. The Mississippi River and connected waterways were major avenues of trade for farmers and merchants and the river boats carried passengers who had lots of cash. The south tended to have a more open attitude towards gaming, reflecting the Spanish, French, and early Virginian traditions.⁷ New Orleans became the capital for gambling.

Gambling establishments were started in the river towns and were popular haunts for both travelers and professional gamblers. These gamblers preyed upon these cash-laden travelers who were, "Seduced by the bright prospects of their business deals as well as by the transience of the river frontier..."⁸ These professional gamblers, also known as sharps or sharpers, generally were dishonest and often turned to confidence games and cheating to make money.

During the 1830's, the actions of the professional gamblers came under growing scrutiny and southern settlers turned against the professional gambler. The professional gamblers were blamed for limiting economic growth, interfering with business, endangering the streets, committing numerous crimes, and debasing the morality of the society. Vigilantism was one method by which the anti-professional gambler sentiment manifested itself. Groups of citizens organized to push the gamblers out of the South.

In 1835, a vigilante group lynched five cardsharps in Mississippi. Professional gamblers moved from the town into the riverboats. Lynching proved to be a successful policy option for reducing the presence of professional gamblers. In contrast to the river boat casinos of today, the old-time river boats were not floating casinos. Gambling occurred informally among the passengers. The period between 1840 and 1860 represented the glory days of the flashy riverboat gambler. The professional gamblers also moved to California, a history we cover in the next section.

The First Wave of Legal Gambling Draws to an End. During the early 1800's, gambling came under increasing attack. There was always a group opposing gambling on moral grounds. This opposition was largely based on religious beliefs.⁹

The flames of opposition were fanned, however, by the prevalence of scandals and the belief that the poor were being targeted, especially by lotteries. This opposition drew strength from the larger climate of social reform. Issues such as temperance, women's rights, educational reform, prison reform, and abolition of slavery were on the minds of many. Although there was strong sentiment to avoid interference with market forces, there was a countervailing view that people should behave in a virtuous way and that meant no gambling.¹⁰

The attack against gambling was focused particularly on lotteries because it represented a form of wagering that was offensive to both the moral sensibilities of reformers, and the Jacksonian resentment toward privilege.¹¹ The exclusive charters granted to lottery operations were examples of this form of privilege. Ironically, President Jackson was an inveterate gambler and had such a history of problems that he must be viewed as a likely addictive or compulsive gambler.¹² His gambling was well-known but tended to be seen as the behavior of a gentleman, hence he was reserved the disapprobation held for commercial gamblers.

Lottery Scandals Led to Gambling Prohibition. As noted earlier, lottery for the beautification of the nation's capital ended in scandal with the operators absconding with the proceeds. This incident illustrated the problems with the lotteries of that time as many were crooked. Increasing evidence of fraud and dishonesty in the operations of lotteries added to the opposition.¹³ An additional argument was that they corrupted the free press and made them captive to their huge demand for advertising.¹⁴

The antilottery forces fought against lotteries and prevailed. In 1833 Pennsylvania, New York, and Massachusetts put an end to state authorized lotteries. By 1840, most states had banned lotteries. By 1860, only Delaware, Missouri, and Kentucky still allowed state-authorized lotteries. Nevertheless, the tickets of these few states were shipped around the country by mail or smugglers. The prohibition also led to the creation of illegal lotteries.

The demise of the riverboat gambler had more to do with circumstance than direct action by the people. Emergence of railroads and the outbreak of the Civil War were the precipitating factors. Travel by steamboats declined as railroads started to supplant steamboats as the favored method of transportation. Trains were more reliable and were faster than the riverboats. The Civil War interrupted virtually all river travel and abruptly diminished gambling in that area.

The end of the first wave did not result in an end to all legal gambling. The prohibition was selective in terms of type of gambling and location. The frontier areas, California included, saw a great deal of gambling after the end of the first wave. Because of the wholesale fraud, lotteries were targeted for prohibition, but gambling in posh clubs were

still legal in New York. Horse racing survived the end of the first wave relatively unscathed. As such it is more difficult to draw a clear distinction between the end of the first wave and the beginning of the second. As we shall see later, the demarcation between second and third waves are much clearer.

It was also during this time that the Grimaldis sold a concession for gaming in an attempt to keep their principality, Monaco, from going bankrupt. Monte Carlo was opened in 1858 by gambling operators who had been forced to leave Hamburg, Germany after popular opinion turned against gambling. The public disfavor in Germany occurred because of the charge that legalized gaming was turning the city into a nest of paupers.

Second Wave: Mid-1800's to Early 1900's

The expansion of the western frontier spurred the second wave. As the country moved westward, the frontier spirit continued to spread. Mining booms increased the rush to the Far West. Miners lured by the promises of easy and abundant riches, personified the frontier spirit better than the explorers before them. Mining was a gamble, and risk-taking was valued for it represented an opportunity for great wealth. These were restless and ambitious people who had high expectations.¹⁵ Probably nowhere was this more apparent than in California.

Gold Rush Set Off a Gambling Boom in California. The gold rush brought a huge increase in the amount and types of gambling to California. San Francisco replaced New Orleans as the center for gambling in the United States. The market for gambling space was so strong that a mere canvas tent, 15 by 25 feet, cost \$40,000 annually, payable in advance with gold dust.

The apex of California gambling was from 1849 to 1855. Gambling became widespread throughout the state whether it was in Mexican towns like Monterey, mountain towns like Mariposa, or growing cities such as Sacramento. During this period, gambling tended to be integrated. Patrons included women, blacks, and Chinese. By 1850, both the state and cities were licensing gambling establishments to raise money.

As settlers spread beyond California, so did gambling. In general, gambling and the west were intimately linked. Gambling was especially widespread in the mining camps that multiplied as the miners spread across the west searching for new strikes.

Public Opinion Quickly Turns Against Gambling. Laws against gamblers and gambling began to be enacted in California. As with the rest of the United States, the desire for respectability and a recognition of the social ills tied to gaming led to limits on gambling. The Legislature made most types of gambling illegal. However, the Legislature's initial aim was more to target the professional gambler than gaming in general. Gamblers were affiliated with municipal corruption and were blamed for the depression that was occurring at the time.¹⁶ Lynching of professional gamblers occurred in San Francisco in 1856, in

part a result of the fight for political control of the city. The gamblers were strong backers of one political faction.

Initially, the state laws were weak and had little real effect on gambling. The statutes outlawed specific games, making the laws difficult to enforce as new and unnamed variants were used and only light penalties were provided. However, the laws were gradually strengthened. In 1860, all banking games were banned. (Banking games are those where the player bets against the house.) Initially, the laws tended to focus on those who ran the games, not the players. In 1885, this was changed so that it was illegal to play. Finally in 1891, the statutes made the penalty for playing equal to the penalty for running the game.

The Prohibition Did Not Eliminate Gambling But Drove it Underground. Even in California, where most gambling was illegal, the first slot machine was invented and premiered in San Francisco in 1895.¹⁷ It was not specifically outlawed until 1911.

Nevada bounced between legalizing and banning gaming. Gambling was legal in Nevada between 1869 and 1910. As a result, gaming activity moved from California to places such as Virginia City, Nevada. Although legally protected, during this time gambling never reached the size in Nevada that it did in San Francisco.

Another effect of the antigambling laws was to stratify gaming activity more. One result was the prevalence of Chinese gaming houses that catered only to Chinese. There were also large Chinese-run lotteries that appealed to non-Chinese. Enforcement of the gaming laws became a method of discrimination. During times of strong anti-Chinese sentiment the gaming laws were enforced more vigorously against Chinese establishments.¹⁸ One operator in San Francisco who alleged discrimination took a case to the U.S. Supreme Court, but lost because he could not show that people who were not Chinese violated the law, but were not prosecuted.

Los Angeles also had gaming activity, but it was overshadowed by San Francisco. Like the city itself, gaming in Los Angeles had more of a Hispanic flavor and occurred on a smaller scale. The city eventually banned gambling which led to a number of illegal clubs and the spread to permissive suburbs.

Lotteries Began a Comeback. Following a long national tradition, the South turned to lotteries to generate revenue to rebuild the war-ravaged region. The Louisiana lottery was the most notable because of its unseemly end. In 1868, the Louisiana Lottery Company was authorized and granted a 25-year charter. A carpetbagger criminal syndicate from New York bribed the Legislature into passing the lottery law and establishing the syndicate as the sole lottery provider.¹⁹ The Louisiana Lottery was an interstate venture with over 90% of the company's revenue coming from outside Louisiana. This lottery was a prolific money maker. Attempts to repeal the 25-year charter were defeated with assistance of bribes to legislators.

Scandals and antigaming sentiment led to additional state and federal legislation against lotteries. In particular, religious leaders led the move against them.²⁰ By 1878, Louisiana was the last of the legal lotteries in the country. The Louisiana Lottery survived until Congress enacted a prohibition against moving lottery tickets across state lines by any method. This act led to the abolition of the Louisiana Lottery in 1895. When the lottery was disbanded, it was discovered that promoters had made huge sums of ill-gotten gains. The Legislature was riven with accusations of bribery. By the end of the century, thirty-five states, including California, had in their constitutions prohibitions against lotteries and no state permitted the operation of lotteries.

Lotteries Were Not the Only Source of Gambling Scandal. Horse racing was plagued by fraud. The odds and payouts were often faked. The parties taking the bets, known as the bookmakers, often owned horses and were able to influence the race. “Ringers,” horses that were fraudulent substitutes and were either much quicker or slower than the expected entry, were often raced.

The second wave of legal gambling, was relatively short-lived. Scandals and the rise of Victorian morality led to the end of legal gambling. By 1910, virtually all forms of gambling were prohibited in the U.S. The only legal betting that occurred was in three states which allowed horse racing, but even that number shrank in the ensuing years.²¹ The feelings against gambling ran so strong that Arizona and New Mexico were forced to outlaw casinos to gain statehood.²² However, the prohibition did not stop gambling. There were many types of illegal gambling houses. Some operated openly for many years. They, of course, had to pay protection money to the law enforcement authorities.

Third Wave (Early 1930's to Present)

The great depression led to a much greater legalization of gambling. The antigambling mood changed as tremendous financial distress gripped the country, especially after the stock market crash of 1929. Legalized gambling was looked upon as a way to stimulate the economy. Massachusetts decriminalized bingo in 1931 in an attempt to help churches and charitable organizations raise money. Bingo was legal in 11 states by the 1950s, usually only for charity purposes.

Horse racing and parimutuel wagering began to make a comeback. In 1933, Michigan, New Hampshire, Ohio, and California legalized parimutuel betting. The California Legislature adopted a statute in 1933 referred to as the Horse Racing Act. The statutes took effect upon adoption by the voters of an amendment to the Constitution in June of 1933. During the 1930's, 21 states brought back racetracks. New laws and automated systems made horse racing much more honest than during the 1800s.

Coincident with resurgence of legal gambling was a crackdown on illegal gambling, in part because illegal gambling had become so prevalent. A backlash developed and reform candidates were swept into office in New York where Fiorella La Guardia replaced Jimmy

Walker and in Chicago where Anton Cermak pushed out “Big” Bill Thompson. Theatergoers were treated to newsreels of Mayor La Guardia taking a sledge hammer to slot machines and pushing them off the barge into the city’s ocean dump. District Attorney Thomas Dewey ran an aggressive campaign against mobsters who were involved in gambling.

Crackdown on Organized Crime Sent Mobsters to California. The crackdown in the east had implications for California. Because of the pressure from law enforcement agencies, New York mobsters, including the infamous Benjamin “Bugsy” Siegel, moved to the West Coast. His role was to expand gaming and bookmaking operations for organized crime. Eventually, publicity was directed on him during an investigation of mob ties with the film unions, forcing him to move to Las Vegas.

At the same time, scrutiny also resulted in the closing of the floating casinos. The most famous was the *Rex*, a floating casino operated by organized crime that was anchored just outside the three-mile limit of state jurisdiction. Gamblers were taken out to *Rex* in excursion boats. The *Rex* and some gaming ships that operated out of San Francisco Bay were eventually closed down by law enforcement authorities.

Nevada Legalized Most Forms of Gambling in the State in 1931. The Nevada Legislature was motivated to build on the tourism boom that was expected in the wake of the completion of Boulder, now Hoover, Dam. Nevada had a flourishing, albeit illegal, gambling industry prior to the legalization. The move for making gambling legal also grew out of concerns that the flourishing illegal gambling was corrupting law enforcement and prohibition was unenforceable.²³ Gaming in Nevada struggled from its inception until after World War II, when the prosperity of post-war America started a boom in the fledgling industry.

The Nevada gaming industry was helped by events in California. As stated, the gambling ships that used to leave from California ports were shut down. Municipal reform in Los Angeles kicked out many of the thriving illegal gambling businesses. These establishments were run by organized crime who moved to Nevada where their skills were desperately needed to launch the new legal gambling industry.

Organized Crime Syndicates Were Early Supporters of Gaming and Invested Heavily. Many casinos in Nevada were financed by mobsters. Most notable perhaps was Las Vegas’ Flamingo which was opened in 1947 by Bugsy Siegel. Even though he had an extensive and violent criminal record, Bugsy Siegel was able to get a gaming license. Most notable of his criminal exploits was his role in arranging the murder of New York mobster “Dutch” Schultz by the infamous “Murder Inc.” Today, even the hint of any such activity would be sufficient to deny a license.

Part of the reason for Mr. Siegel’s success was due to his connection to the underworld. Wartime shortages did not slow down his plans because of his ties to the black market and his political connections.²⁴ The lavish casino he built opened with such stars as Jimmy

Durante, Xavier Cougat, and George Raft. The Flamingo helped establish Las Vegas, rather than Reno, as the destination for high rollers. Reportedly Mr. Siegel used too much of the mob's money on what was initially a unprofitable operation. Within the year, Mr. Siegel was gunned down at a Beverly Hills mansion.

Senate Investigated Mob Influence in Casinos. During the 1950s, the Senate Committee to Investigate Organized Crime in Interstate Commerce held a number of hearings on criminal influence in the casino industry. The committee was chaired by Senator Estes Kefauver, and the committee is also known by his name. The committee found widespread evidence of skimming, which sheltered gambling profits from taxes. The prevalence of crime left gaming once again on the verge of a national prohibition.²⁵ The result of the committee's findings was a crackdown on criminal influence and a cleansing of the casino industry. Eventually, the mob sold their casino interests to lawful individuals and publicly-traded companies.

The link between organized crime and gambling was a factor in four state elections on legal gaming.²⁶ In 1950, voters in California, Montana, Arizona, and Massachusetts voted against legal casino gaming. The California proposition would have established a state board to run all gaming operations with the proceeds going for old-age benefits. It lost by a wide margin.

Lotteries Begin Their Resurgence. From 1894 to 1964, there were no legal government-sponsored lotteries operating in the United States. This ban led to a paradox: lotteries were widely played, but always illegal. One of the most well known was the Irish sweepstakes which began in 1930 for the purpose of raising money for hospitals in Ireland. Although it was not legal to sell tickets in the U.S. or to ship them here, they were smuggled into the country. Participation was high with about 13 percent of the country having ever bought a ticket.²⁷

Another prominent form of lottery was the illegal "numbers" game. Despite the illegality, numbers was quite popular. One author claimed that the amount being wagered on numbers was \$5 billion in 1960.²⁸ Another estimate shows that the numbers game was grossing \$20 million annually in Chicago alone during the early 1970s and the total handle was \$1.1 billion.²⁹

Growing opposition to tax increases was a leading factor in establishing state-run lotteries in the 20th century. In 1964 New Hampshire was the first state to sponsor a lottery, followed by New York in 1967. New Jersey launched the first financially successful modern lottery in 1971. The New Jersey lottery was successful because it stressed frequent action at low cost, and it returned a higher percentage of lottery revenues as prizes. There were also various attempts to legalize a national lottery, but they failed to be passed by Congress.

In 1978, New Jersey became the second state to legalize casino gambling in an attempt to revitalize the rundown resort area of Atlantic City. The legalization was restricted only to

Atlantic City. In the late 1800's to the early 1900's, Atlantic City was a popular resort town, boosted by the new rail service which linked the Northeast. Day trips to the Jersey shore were now possible and affordable. But its popularity dwindled when air travel became easily accessible. Upscale tourists chose beach resorts in Florida, the Bahamas, and the Caribbean over Atlantic City. Visitors to Atlantic City in the 1960's and 1970's were generally elderly and/or poor. Casino gaming was expected to be a way for Atlantic City to become a popular tourist destination once again.

What Could End Gambling's Third Wave? The first and second waves ended in part because of a resurgence of public concern about morality and scandals in gaming. People can live with adverse odds but not cheating.³⁰ What kind of events could lead to scandals today? If lotteries were plagued by fraud that would probably have an impact on people's perceptions. Another route is through problems and scandal in sports gambling. Pete Rose is a symbol of what gambling can do to a person. What happens if a sports hero is more interested in winning a bet than a game? Could such a scandal impact legalized gaming?

¹I. Nelson Rose, "The Rise and Fall of the Third Wave: Gambling Will be Outlawed in Forty Years," in Eadington & Cornelius, eds., Gambling and Public Policy (Reno, NV: Institute for the Study of Gambling & Commercial Gaming, University of Nevada, 1991), p. 70.

²*Ibid.*, p. 70.

³John M. Findlay, People of Chance, (New York, NY: Oxford University Press, 1986), p. 4.

⁴*Ibid.*, p. 12.

⁵*Ibid.*, p. 14.

⁶Charles T. Clotfelter and Philip J. Cook, Selling Hope: State Lotteries In America (Cambridge, MA: Harvard University Press, 1989), p. 20.

⁷Findlay, *op.cit.*, p. 51.

⁸*Ibid.*, p. 58.

⁹Gabrielle A. and Reuven Brenner, "Gambling: Shaping an Opinion," in Eadington and Cornelius, eds., p. 482.

¹⁰Findlay, *op.cit.*, p. 49.

¹¹*Ibid.*, p. 40.

¹²Such a statement cannot of course be made precisely because such a diagnosis requires a professional opinion that can't be made with a president long-since dead. For more information on his astounding gambling record see Findlay, p. 38.

¹³Clotfelter and Cook, *op.cit.*, p. 37.

¹⁴Findlay, *op.cit.*, p. 41.

¹⁵*Ibid.*, p. 82.

¹⁶*Ibid.*, p. 97.

¹⁷John Scarne, Scarne's Complete Guide to Gambling (New York, NY: Simon and Schuster, 1961), p. 386.

¹⁸Sylvia Sun Minnick, Samfow: The San Joaquin Chinese - Legacy (Fresno, CA: Panorama West Publishing, 1988), p. 108.

¹⁹Tara L. Lavery, "Commercial Speech Suffers a First Amendment Blow in *United States v. Edge Broadcasting Co.*," 14 Northern Illinois University Law Review, p. 551.

²⁰Clotfelter and Cook, *op.cit.*, p. 37.

²¹Rose, *op.cit.*, p. 75.

²²*Ibid.*, p. 75.

²³Anthony N. Cabot and Richard J. Schuetz in "An Economic View of the Nevada Gaming Licensing Process," in Eadington & Cornelius, eds., p. 126.

²⁴James F. Smith, "Bugsy's: Flamingo and the Modern Casino-Hotel," in Eadington & Cornelius, eds., p. 502.

²⁵Thomas Harris, "Winner Take All: Expansion of the Gaming Industry," Western Wire, Fall 1994, p. 18

²⁶"Gambling Proposals Lose in Four States," Christian Century vol. LXVII, no. 47 (22 November 1950), p. 1380.

²⁷Clotfelter and Cook, *op.cit.*, p. 38.

²⁸Scarne, *op.cit.*, p. 164.

²⁹Clotfelter and Cook, *op.cit.*, p. 40.

³⁰Rose, *op.cit.*, p. 74.

III. Lotteries

“Hope Springs Eternal in the Human Heart,” Alexander Pope.

Lotteries Have Been Prominent Throughout History.¹ Ancient India, China, Greece, and Japan all had lotteries. The emperor Nero had lotteries for prizes at parties. The Great Wall of China was financed, in part, by a lottery. The Bible is replete with references to drawing lots. Lot casting was a favored means of communication between man and god.

As early as 1420, lotteries were used in Europe for public works. High-value commodities such as land and art were often sold through lotteries. The first publicly run European lottery was in Florence in 1530. The money was raised for public works. The first public English lottery was in 1566 and was also for public works projects. In 1753 the British Museum was funded with lottery proceeds. In addition, England had private lotteries, but they became such a scandal that parliament outlawed them in 1699.

As noted in the history section, lotteries have a long and mixed history in the new world. In modern times, lotteries started their comeback with the legalization of the New Hampshire lottery in 1964. This lottery was a low-stakes low-excitement lottery, because drawings were held twice a year and the winnings were not large. The lottery was modeled after the Irish sweepstakes. The winning numbers were tied to the winner of a horse race. However, it was not a skill-based game, as the numbers were randomly selected.

Researchers usually point to New Jersey as the first modern successful lottery. The New Jersey lottery was more successful because of the more frequent drawings and larger purses. The New Jersey lottery was administered by a commission appointed by the Governor, a model that most states use.

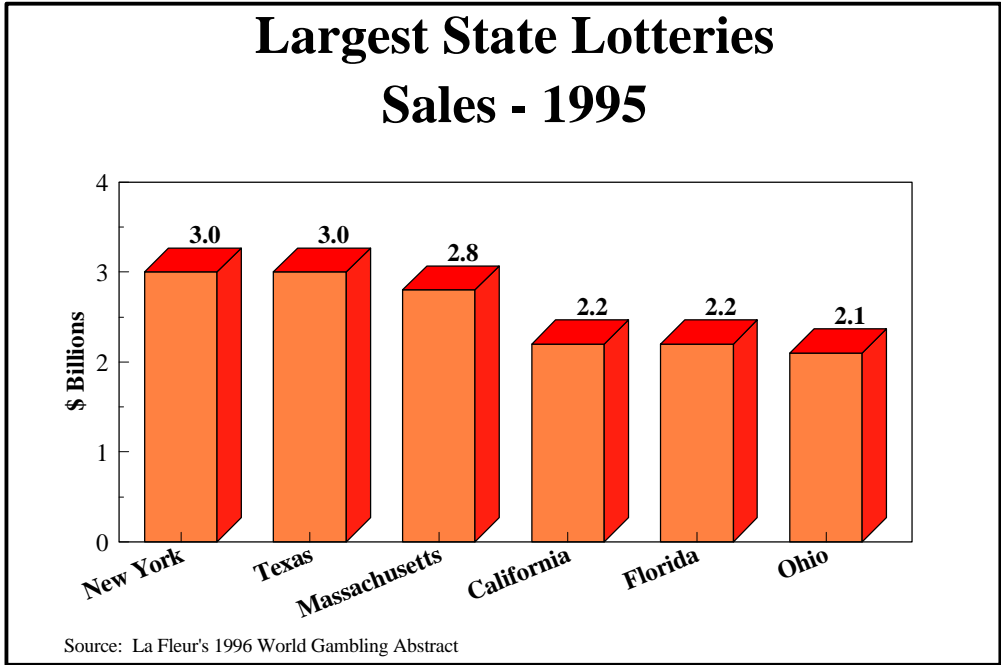
Lotteries Enjoy Widespread Legalization. Lotteries are legal now in 37 states and the District of Columbia. Lotteries have spread rapidly across the country, in a way that is consistent with the domino theory of gaming regulation discussed in the introductory section. Simply put, a given state is more likely to have a lottery, if the neighboring state has a lottery. The first states with lotteries were all in the northeast. Then lotteries spread across the country. The only region in the United States where they are generally not legal is in Alaska, and Hawaii, and the southern states.

Lotteries, along with their close derivative bingo, are the most popular kinds of gambling. The popularity of lottery games is not limited to state-run lotteries. Indian tribes run lotteries and illegal lotteries still exist.

Lotteries are also legal around the world. The 1995 worldwide sales for legal lotteries were \$95 billion.² The United States leads with sales of approximately \$28.7 billion. Germany is a distant second at \$9.2 billion in sales. In all these places, lotteries are

basically the same game with only minor differences that reflect the particular national culture.

Looking at some specific industry statistics, we can see that lotteries are well-established in this country and within California, although for the size of the state, California does not have a particularly large lottery. Although the chart shows California as one of the biggest lottery's state, the table at the bottom shows Californians spent less on the lottery than many other states.



Massachusetts	1	\$462
Washington, DC	2	\$404
Maryland	3	\$208
California	33	\$69
Montana	37	\$38

Source: La Fleur's 1996 World Gambling Abstract.

Despite Success, Opposition Exists. The resurgence of lotteries has not been universally welcomed.³ An argument used in opposing lotteries is that they symbolize the boredom and materialism of modern life. Another argument against lotteries is that legal gambling leads to illegal gambling. Lottery critics see legalized state-sponsored gambling

destroying ethical values by promoting the ethics of easy money over hard work. Critics point to the ads of employees being disrespectful to their bosses after winning the lottery.⁴

Another argument that is marshaled against lotteries is that they prey on the poor, the ignorant, and compulsive gamblers. The poor may be induced to spend money on lottery rather than basic necessities leaving local and state government picking up the tab through varied service programs. State lotteries are also a monopoly and some question exists whether that is proper. Another argument is that if the purpose is to make money for schools or some other worthy purpose, why shouldn't the state earn money through opening other businesses such as restaurants or brothels?⁵

In sharp contrast, supporters call lotteries a painless tax, even a high-minded tax. Money is raised for good causes through people having fun. Lotteries are to be celebrated because they restore consumer sovereignty, allowing people to spend money on what they choose. The argument goes on to state that gambling is prevalent whether it is legal or illegal, so why not allow people to do it legally. To prevent people from gambling is a form of paternalism and is elitist. There is no harm save for the compulsive gambler or in the crooked game, which all state lotteries go to great pains to avoid.

Two stories by modern American writers indicate the ambivalent feelings aroused by the lottery.

“Once you could send your innocent babes, hope of the future, off to the candy store to buy some chewing wax, a Baby Ruth, the new Batman comic book and a kazoo, and be secure in the knowledge that good Mrs. Chesley behind the counter would bust their little knuckles if they tried to buy a copy of The Racing Form. Not anymore. Now good Mrs. Chesley has turned her shop into a gambling hell where she greets the traffic with a leer that says, “Hello sucker” and has to keep kicking the kids out of her way so the lottery players can get their bets down.”⁶

But there is another view. A supporter noted:

“Editorial and other criticism of legal gambling smacks of nannying ordinary working and retired folks: we the affluent, who would not dream of playing numbers whether legal or illegal, long shots on the races or for jackpots at slot machines, don't want you, the unwashed, to enjoy your simple pleasures.”⁷

There are objections to lotteries that go beyond the arguments just presented. Some critics are concerned that state-sponsored lotteries are not just supplying a good, but trying to foster a taste for it.⁸ In legalizing a lottery, the state is yielding to consumer preference and the argument that a little gambling does not hurt anybody. But the question remains, does the business-like behavior where sales of lottery tickets are actively

encouraged through state sponsorship and huge amounts of advertising reflect the public interest?

Why have lotteries grown? There are several trends that receive credit for expanding lottery business.⁹

- Tickets have become cheaper, especially when adjusted for inflation.
- Number of retail outlets has increased.
- Size of grand prizes has grown.
- More consumer participation is allowed in the betting: for example consumers can choose their own numbers.
- Frequency of drawings has increased, in part because there are more types of games.
- The payout rate has increased, although compared to colonial times it has decreased.

State Lotteries Have Two Important Attributes. One of these is a significant marketing and advertising campaign and the other is that the lottery is a monopoly run by state government and not by a private firm.

Lotteries are run by state government for two major reasons. One is to reduce fraud and the other is to raise money for a worthy cause. Some states deposit the proceeds into the general fund while others earmark the money for special purposes. Some interesting purposes include a gamblers aid fund in Iowa and the University of Illinois Athletic Association in Illinois. The state statutes generally call for the lottery commission to maximize profits, although some restrictions may be adopted. Because of the statutory direction to maximize profits, lotteries are run like businesses and are more like a private sector entity than a state agency. An unusual case was Missouri, where the law prohibited advertising that would induce a person to participate. Since the effect of this prohibition was to eliminate all of the advertising normally done by a state lottery, the law has since been changed.

Critics Argue That Much of the Advertising is Misleading. For example, lotteries, including California, routinely advertise multimillion dollar prizes. The real value of these prizes is actually about one-half as large because they are paid out over many years. Critics charge that this is misleading advertising and the present value of the prizes should be noted in the advertisements. New York Governor Pataki has directed the lottery to advertise in a more honest way. Gone are the pictures of the new millionaire beside his pool. Now a woman from Yonkers is shown spending her \$10,000 (\$6,400 after taxes) on a variety of home appliances.

Modern Lotteries Have Been Essentially Free of Scandals. Early lotteries were plagued by corruption and scandals. To protect the integrity of the games, lotteries have adopted many safeguards to protect against corruption and fraud. The lottery industry has experienced very few scandals in the more than 30 years of state-administered lotteries in North America.¹⁰ The integrity of the lottery is one of the appeals of lottery gaming.

There have been some instances of fraud in modern lotteries, although the incidents pale in comparison to the experiences of the 18th and 19th century American lotteries. In 1982, there was a scandal in the Pennsylvania lottery. In a drawing where balls were used to determine the winning number, some of the balls were injected with fluid to make them heavier. Because they were heavier they would be chosen in the mechanized selection procedure. The perpetrators included the TV announcer and were quickly discovered. Another significant lottery scandal also occurred in Pennsylvania when a computer vendor printed a ticket with the winning numbers. Again the perpetrator was quickly discovered. In a slightly different kind of case, New York closed down its lottery for a period after the agency announced winning tickets that the lottery officials knew had not been sold.

States Have Been Very Effective at Stimulating Demand. As noted, New Hampshire started with a couple of drawings a year. The results were not spectacular. As more states legalized lotteries, the states have become very effective at innovating and creating new games. One of the first innovations was to increase the frequency of drawing and the size of the prizes. Another new product was the instant tickets, termed “scratchers.” Then lotteries started daily drawings which are modeled after the illegal numbers game. One of the biggest booms to lotteries was the introduction of Lotto. Lotto is a game where winners are determined by matching the player’s number with numbers that are drawn. If the winning numbers are not held by a player the prize rolls over and grows. The rolling over of the prize is crucial to a modern lottery’s success, because it creates a large jackpot which has a significant effect in stimulating sales.¹¹

Lottery Players are Widespread. Lotteries are the most popular and broadly played form of gambling despite having the lowest payout. A large proportion, about 50 to 60 percent of adult Americans play legal lotteries in lottery states. Two-thirds of these play regularly, which means that about one-third of the adults are regular players. Heavy players are about 10 percent of all lottery players.¹² The poor, minority, Catholic, undereducated, and middle-aged are all more likely to play.¹³ Two of the first 11 big winners in California were illegal immigrants.

There is substantial evidence that youths play the lottery, although they are forbidden by law. Studies have found large number of high schools kids playing lottery games. Some of these individuals have characteristics of pathological gamblers.¹⁴

The total number of all lottery players is probably greater than reflected in statistics because illegal lotteries still exist. They can exist because their payout ratio is much higher. State lotteries are a very unattractive gambling proposition as they return a relatively small amount of the money as prizes.

The Typical Individual Spends \$100 Annually.¹⁵ This amount exceeds the amount spent directly on prescription drugs and reading materials. Also, a small number of poor families spend a very large sum on lotteries.¹⁶ In general, the amount spent on lotteries per person does not vary as much as the percent of income spent. That is because higher income people spend proportionally much less on the lottery.

Research has shown that a relatively small minority of customers provide a large share of revenues. A study based on California data showed that, typically about two-thirds of the take is provide by about 10 percent of the customers.¹⁷

Lotteries have come to be seen as “implicit taxes” by researchers.¹⁸ That means that they are not, of course, taxes because no one is obligated to pay them. But lotteries are similar to taxes because they raise money for public purposes. Some critics would argue that lotteries are not wholly voluntary because of the coercive nature of the advertising and the fact that people buy them on impulse.¹⁹ The counter argument is that it is in fact a voluntary purchase. Even if purchased on impulse, so are candy bars and lottery tickets do not cost much more.

Lotteries Raise a Disproportionate Share of Money From Low-Income Groups.

Almost every study conducted by economists and researchers has found lotteries to be regressive form of raising money.²⁰ Regressive means that as income rises, the proportion of money spent on a given product, lotteries in this case, declines. The regressivity of a lottery is heightened because of how the money is spent. The proceeds tend to go for programs that benefit the population as a whole, namely education. The regressivity could be diminished if lottery proceeds went for programs that aided lower income groups exclusively.

In other states there has been criticism that lotteries have targeted low-income people. The lottery in Illinois rented billboards in Chicago’s most blighted neighborhoods with the slogan “This Could Be Your Ticket Out.”²¹ After receiving significant criticism, the ad campaign was dropped.

Why do People Play the Lottery? The main reasons are availability, no skill is required to play, players have little or no fear of corruption, and gamblers can wager small amounts. People play despite the low payout compared to other forms of gambling. However, playing the lottery is a cheap way to have an opportunity of winning big dollars and become a celebrity. If you win a big lottery prize you are put in the newspapers. The celebrity status of winners may be an important aspect in encouraging play.

The odds of success in lotteries do not seem that important to players. When interviewed, consumers do not seem to know the odds or the payout rate. Researchers have found that once people believe that a low probability event can occur, they tend to overestimate the chances of it occurring.²² And a small number of people do win and win large amounts of money, although the overwhelming majority lose money.

Lotteries give an illusion of control to some players. Because you can pick your own numbers in some games, you can choose your own lucky number. Tabloids feature articles about how to improve odds at picking lottery numbers, obviously a forlorn hope because the winning numbers are a product of a random process. Another attraction of the lottery is that people enjoy the non-monetary aspects of it, including talking about

playing, engaging in the ritual weekly purchase, socializing with friends and coworkers to pool to buy tickets, and dreaming about winning, perhaps the favorite activity among lottery players.

According to some research, lotteries recruit people into commercial gaming, especially in states that have had little legalized gaming or exposure to such activity.²³ This finding is interesting because lotteries have been opposed by commercial gaming interests. Another view is that lotteries have sanitized gaming and popularized it.²⁴

Gambling can be an addiction for some gamblers and the resulting costs from these compulsive gamblers is quite significant as discussed in Chapter IX. It is unclear what role lotteries are having on the compulsive gambler.²⁵

Illegal Gambling Isn't Eliminated by Lotteries. One justification that has been used to win approval of lotteries is that they will undercut the illegal numbers game. Nevertheless, illegal numbers still persist, although they are probably smaller.²⁶ Numbers persist because its convenient, flexible, offers credit, and if you owe the government for taxes or welfare, it may be a better place to bet your money. And the payout is much larger than the approximately 50 percent of state-run lotteries. Although the size of numbers is not known, researchers note that estimates put drugs as a far bigger source of funds to criminal interests.²⁷

Economic Impact of Lotteries is Unclear. The lotteries help retailers that sell lottery tickets, especially the small ones. But of course by removing money from expenditure on other goods and services it can have a harmful impact on other retailers, but that has not been quantified.

Some research on the California lottery shows that it has a pronounced impact on rural areas. The lottery raises money throughout the state, but proceeds and purchases of inputs do not benefit the state equally. An economist estimated that the lottery may take \$711 million out of rural California, in other words, it is an "anti-rural development program."²⁸

There are New Directions for Lotteries. State lottery commissions are intrigued by several new directions. These include video lottery terminals and betting at home through touch-tone phones or cable television. Another is sports betting. Sports betting may be the most popular type of betting, although much of it is illegal. Four states have used sports betting in the lotteries, but Congress acted to outlaw it at the behest of professional athletic organizations. There was a widespread concern that any legalized sports betting could make the athlete more concerned with the bet than the game.

State lotteries have not been involved in casino gaming. A different situation exists in Manitoba, Canada, where the lottery operates a casino.

Lotteries have gone to quickdraw keno and it has become quite popular. Monitors are placed in bars and restaurants and drawings are held on a very frequent basis, approximately every five minutes. Critics argue that it exposes young people to casino-type gaming. California earned more than any state on quickdraw keno.²⁹ The state's earnings plummeted sharply after the California Supreme Court ruled that the lottery's keno game was not a lottery game as authorized by the constitution and was illegal because it was a banked game. Lottery games are played against other players and not against the house, in this case the California Lottery. California law prohibits all banked games, that is those games where the house has a stake in the outcome.

As will be discussed further in the Indian Gaming section, the Coeur D'Alene Indian tribe in Idaho is proposing a national lottery. That lottery would be available in all states that have a lottery, including California. Such a lottery would allow someone to use a credit card to purchase a ticket over the phone. The person would be able to buy on credit and would not have to leave his own home. Another advantage is that the lottery does not have to earmark money for a purpose, such as the California lottery. Some lottery analysts say this could be a large advantage.³⁰ The tribe is, however, proposing to share the revenues with other Indian tribes and states. Whether this will drive their payout to a higher or lower level than the state's is not clear.

There is a strong link between the lotteries and Indian gaming. The Indian tribes are allowed to operate whatever type of gambling that is not prohibited to everyone within a state. The games used by the lottery are often used to pave the way for expanded Indian gaming in states that do not otherwise allow casino gaming.

Lotteries May Not Stay Public. Governor Rowland of Connecticut has proposed selling a portion of the state lottery to private investors to raise money for the state. It would not have a significant impact on the operation because only a minority, about 6 percent of the state lottery, would be sold.

Appendix I

Start-up Year	State	Authorization	Approval Rate
1964	New Hampshire	Legislation	
1967	New York	Referendum	61%
1970	New Jersey	Referendum	82%
1972	Pennsylvania	Legislation	
1972	Connecticut	Legislation	
1972	Massachusetts	Legislation	
1972	Michigan	Referendum	67%
1973	Maryland	Referendum	80%
1974	Ohio	Legislation	
1974	Rhode Island	Referendum	
1974	Illinois	Legislation	
1974	Maine	Referendum	61%
1975	Delaware	Legislation	
1978	Vermont	Referendum	66%
1981	Arizona	Initiative	51%
1982	Washington	Legislation	
1982	Washington DC	Initiative	66%
1983	Colorado	Initiative	60%
1985	Oregon	Initiative	66%
1985	California	Initiative	58%
1985	Iowa	Legislation	
1986	West Virginia	Referendum	67%
1986	Missouri	Referendum	70%
1987	South Dakota	Referendum	60%
	Kansas	Referendum	64%
	Montana	Referendum	70%
1988	Virginia	Referendum	57%
	Wisconsin	Referendum	65%
	Florida	Referendum	64%
1989	Idaho	Referendum	51%
	Indiana	Referendum	62%
	Kentucky	Referendum	60%
1990	Minnesota	Referendum	57%
1991	Louisiana	Referendum	65%
1992	Texas	Referendum	65%
1992	Nebraska	Referendum	63%
1993	Georgia	Referendum	52%
1994	New Mexico	Referendum	54%

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- ¹Much of the history of lotteries comes from John Scarne, Scarne's Complete Guide to Gambling (New York, NY: Simon and Schuster, 1961).
- ²International Wagering and Gaming Business vol. 18, no. 5 (May, 1995), p. 1.
- ³Charles T. Clotfelter and Philip J. Cook, Selling Hope: State Lotteries In America (Cambridge, MA: Harvard University Press, 1989), p. 20.
- ⁴I. Nelson Rose, "The Rise and Fall of the Third Wave: Gambling Will be Outlawed in Forty Years," in Eadington & Cornelius, eds., Gambling and Public Policy (Reno, NV: Institute for the Study of Gambling & Commercial Gaming, University of Nevada, 1991), p. 78.
- ⁵*Ibid.*
- ⁶Russell Baker, "Big Rot Candy Lesson," New York Times (8 September 1984) in Charles T. Clotfelter and Philip J. Cook, eds., p. 10.
- ⁷Dick Netzer, "Legal Gambling, Now That We Have Lots of It," New York Affairs vol. 8 (1984), p. 66.
- ⁸Clotfelter and Cook, *op.cit.*, p. 11.
- ⁹*Ibid.*, p. 51.
- ¹⁰William R. Eadington, "The Legalization of Casinos: Policy Objectives, Regulatory Alternatives and Cost/ Benefit Considerations," Journal of Travel Research vol. 34, no. 3 (Winter 1996), p. 6.
- ¹¹Clotfelter and Cook, *op.cit.*, p. 59.
- ¹²*Ibid.*, p. 93.
- ¹³*Ibid.*, p. 96.
- ¹⁴*Ibid.*, p. 134.
- ¹⁵*Ibid.*, p. 24.
- ¹⁶Todd A. Wyett, "State Lotteries: Regressive Taxes in Disguise" The Tax Lawyer, Spring 1991.
- ¹⁷Clotfelter and Cook, *op.cit.*, p. 93.
- ¹⁸See Charles T. Clotfelter and Philip J. Cook, in "Selling Hope," p. 216 and Todd A Wyett, in "The Tax Lawyer," Spring 1991.
- ¹⁹Wyett, *op.cit.*
- ²⁰Summarized in Wyett, Table IV.
- ²¹U. S. News and World Report, 15 January 1996, p. 60.
- ²²Clotfelter and Cook, *op.cit.*, p. 77.
- ²³*Ibid.*, p. 104.
- ²⁴William R. Eadington, in William R. Eadington and Judy A. Cornelius, eds., Gambling and Public Policy (Reno, NV: Institute for the Study of Gambling & Commercial Gaming, University of Nevada, 1991) p. 3.
- ²⁵Clotfelter and Cook, *op.cit.*, p. 126.
- ²⁶*Ibid.*, p. 132.
- ²⁷*Ibid.*, p. 133.
- ²⁸George Goldman, "The California State Lottery and Rural Areas," Western Wire, Fall 1994, p. 21.
- ²⁹Paul Doocey, "Quick Draw Dilemma," International Gaming and Wagering Business, 1 June 1995.
- ³⁰Matt Connor, "National Indian Lottery Takes Shape," International Gaming and Wagering Business vol. 18, no. 6 (1 June 1995), p. 24.

IV. Indian Gaming

Indian gaming has mushroomed over the last three decades. Although there is agreement that it has grown dramatically, it is difficult to put an exact dollar figure on the size of Indian gaming. There are no publicly collected and released statistics figures, as there would be with a public corporation involved in gaming. Estimates of the gross revenues vary widely. A writer on gambling and economic development, Robert Goodman, quotes a \$6 billion figure.¹ A quick review of other articles yields estimates of \$2.3 billion,² \$8 billion,³ and \$2.6 billion.⁴ Not all these revenues are going to the tribes, however, as the management companies take a significant share. By some accounts 65 to 85 percent of the income goes to management companies.⁵ Again, the exact figure is not known and those figures are higher than the ones seen in recent newspaper stories about signed contracts.

Despite its Popularity and Widespread Availability, the Future of Indian Gaming is Unsettled. Some observers believe that despite its widespread popularity, Indian gaming could become illegal again.⁶ The history of Indian gaming is replete with conflicts with the states. Native Americans are concerned that those conflicts could threaten what some observers are calling the “new buffalo.” Indian gaming has earned that term because it is a single source capable of feeding and clothing the Indians. It has become the one economic development program that has been able to overcome the poor quality and remote location of most of their lands.

The conflict between the states and Indian tribes arises because both are sovereign entities. As such, states are severely limited from taxing and exercising jurisdiction over activities on tribal land. When the interests of the Indian tribes and the states differ, this sets up a conflict. The history of tribal-state relations have been not always been free of conflict and tension.⁷ The states, in order to prevent the off-reservation effects of certain activities that occur on the reservation have sought to extend authority over reservations. The result has been substantial litigation between the states and tribes in an attempt to define the relationship between the two. The high stakes of gaming and the fact it is an area traditionally regulated by the state have intensified the conflicts.

Although Indian tribes are sovereign entities, they are clearly dependent and subject to federal policy and regulation. Federal policy has fluctuated dramatically over the years, alternating between forcing Native Americans to assimilate or allowing them to maintain their separate identity. During the most recent swing in policy, Congress passed the Indian Civil Rights Act of 1968 which embraces continued tribal existence. The support and promotion of gambling by the federal government is an outgrowth of the policy of supporting a separate identity for indigenous peoples.

First Major Litigation Spurred by Indian Bingo in Florida. The state of Florida had legalized bingo for nonprofit entities. The state had adopted specific laws governing bingo, including prize limits and hours of operation. In 1979, the Seminole tribe opened a high stakes bingo parlor that did not comply with many of the state laws. They were the

first federally recognized Indian tribe in the U.S. to operate a high-stakes bingo operation on a reservation.⁸ The Sheriff of Broward County, the site of the bingo parlor, threatened to close the operation down. Florida, like California, is a Public Law 280 state, meaning that Congress granted the state the authority to enforce the state's criminal laws on reservations. The tribe sued to prevent the action.

In the first important decision in a modern Indian gaming case, the U.S. Court of Appeals rejected the arguments of the State of Florida.⁹ The Court found that the relevant question was whether gambling, or more specifically bingo, was prohibited in Florida or was it merely regulated. If it was prohibited, then clearly the state could act to prevent gaming on Indian lands. But since Florida allowed charitable bingo, then bingo was regulated rather than prohibited within the state and was a civil rather than a criminal issue. States are severely restricted in enforcing their civil jurisdiction on Indian reservations. The tribe was allowed to continue their operations. California lost a similar suit over bingo games.¹⁰

Indian Gaming Began to Grow Rapidly. At that time, only five states prohibited all forms of gaming, giving the Indian tribes a great deal of latitude to expand their gaming. By 1988 over 100 tribes were engaged in bingo and one researcher put the collective revenues at over \$100 million.¹¹ Not surprisingly, the *tribes* wanted to move beyond bingo to card games and slot machines.

Congress Supported the Spread of Indian Gaming.¹² Congress was motivated by the conditions on reservations. By any standard they were grim.¹³ In 1989, the median family income on reservations was \$13,489, while it was \$34,213 in the remainder of the country. On reservations, 47.3 percent of families lived in poverty compared to the national average of 11.5 percent. The alcoholism rate among Indians was 663 percent higher than the national average, the suicide rate was 95 percent higher.

Objections Were Voiced Over Indian Gaming. The expansion of Indian gaming was not greeted with enthusiasm from all quarters.¹⁴ The states, even if they have legalized gaming, have long been reluctant to open up gaming on Indian lands.¹⁵ Law enforcement officials were concerned with the possibility that organized crime would infiltrate Indian gaming operations. Non-Indian gaming operations were very concerned about the competition from businesses that did not have to pay the same state and local taxes that they did. Governments were concerned about the possibility of social problems resulting from increased gaming. Another concern of government was its inability to tax gaming on reservation lands.

During this period, the federal government was not active in regulating Indian gaming. The Bureau of Indian Affairs had adopted tribal gaming ordinances for years, but generally gaming was not an issue of regulatory concern.¹⁶

The problems associated with Indian gaming began to grow.¹⁷ Non-Indian managers who helped tribes establish gaming operations were taking the majority of the profits.

Suspected organized crime involvement began to surface. There was also evidence of cheating and skimming. Some dishonest tribal members were involved in criminal activities. These events began to create pressure for Congress to act, but there was not a consensus on what should be done. A major case regarding gaming in California was pending before the Supreme Court, adding to the inertia in Congress.

The pending Supreme Court case had developed when California had threatened to take criminal action against the Cabazon and Morongo Bands of Mission Indians because of their card game and bingo casino. These games were not operated in a manner that was consistent with state law. In 1987, the Supreme Court found for the Indians in the landmark case, *California v. Cabazon Band of Mission Indians*.¹⁸ The U.S. Supreme Court upheld by a six to three vote the right under federal law for Indians to run gambling operations without state regulation in states where such gaming was legal for any purpose. As the court noted:

“California itself operates a state lottery and daily encourages its citizens to participate in this state-run gambling. California also permits parimutuel horse-race betting.”¹⁹

The decision in the Cabazon case ultimately prompted Congress to act. After Cabazon, the states and Nevada gaming interests became the principle proponents for new gambling legislation, because they wanted more limitations and control.²⁰ Shortly after, the Indian Gaming Regulatory Act (IGRA) was passed.

Congress Intended to Accomplish Five Objectives With the Passage of IGRA.

- Promote self-sufficiency for the tribes.
- Ensure that Indians were primary benefactors of the gambling.
- Establish fair and honest gaming.
- Prevent organized crime and other corruption by providing a statutory basis for its regulation.
- Establish standards for the National Indian Gaming Commission.

IGRA divided gaming into the following three classes or categories:

Class I: Consists of social games for minimal value prizes associated with traditional tribal ceremonies or celebrations. This class is within the exclusive jurisdiction of the Indian tribe.

Class II: Includes limited card games, lotto, and bingo, but not the electronic form of the games. Class II games are within the jurisdiction of the tribes primarily, but is subject to oversight by the National Indian Gaming Commission. These games are only permitted in states that permit such gaming for any purpose and/or any condition. Although states almost always heavily regulate and restrict such games, many of those state restrictions do not always apply to the tribe.²¹ For example, although Class II card games must be played

in conformity with state laws and regulations on hours of operation and limitations on wager or pot sizes, state limits do not apply to bingo at a tribal reservation facility.

Class III: Encompasses those gaming activities such as slot machines and other games that are commonly operated by Nevada or Atlantic City casinos, lotteries, or parimutuel facilities. Class III gaming is subject to negotiations between the state and the tribe. The exceptions are those cases where the tribe already offered Class III prior to the passage of the IGRA and these were grandfathered.

In order for a tribe to offer new Class III gaming, three events must occur:

1. The state in which the reservation is located must permit the same specific gaming activities that are permitted.
2. The tribe passes an ordinance authorizing the gaming activities.
3. The gaming is conducted in conformance with a compact entered into by the tribe and the state.

The IGRA also reserves for the federal government exclusive jurisdiction over criminal prosecutions of state gambling laws at Indian facilities.²² For the state to gain any say over how Indian gaming is conducted, the state must enter into a compact that allows state oversight.²³

States Unhappy With Tribal Authority Over Gaming. The States were interested in protecting their prerogatives and opposed the grant of authority in the Cabazon case and the IGRA.²⁴ The IGRA requires states to allow tribes to conduct gambling to a greater extent than the state allows other person and entities to gamble. At the same time, IGRA does not automatically make tribal gaming subject to state regulation intended to protect patrons and minimize the negative side-effects of gambling on nearby communities.

Furthermore, the reluctance of the states can also be understood by noting that neither the tribes nor tribal members pay state sales taxes or state income taxes on income earned on reservations nor do they have to pay property taxes. This is a long-standing prohibition that predates IGRA. To the extent that tribal gaming reduces lottery ticket sales or causes consumers to spend money on gambling that would otherwise be spent on goods or entertainment that generate sales tax, the states are direct competitors, not mutual beneficiaries of gambling on Indian reservations.

The compact provisions have proven to be a contentious element and has been the subject of much litigation. Many states have not wanted to negotiate because they did not agree with the position of tribes that certain Class III games were legal in the state. They did not believe that Congress envisioned casino gambling in states just because the state allowed charity Monte Carlo nights. Senators Inouye and McCain have indicated that if

the states do not negotiate compacts, Congress might preempt and establish sole federal regulation of Indian Gaming.²⁵

In particular, the requirement that the states negotiate with the tribes in good faith has spawned a great deal of litigation. The states were required under IGRA to negotiate in good faith to enter into a compact with a tribe to allow Class III gaming. If they did not do so, the tribes were allowed to sue in federal court. Congress adopted this good faith requirement to ensure that the states would not stonewall but would enter into negotiations that could and would be completed.²⁶ Ironically, the compact provision was put into the bill at the behest of the states and limited the freedom that the tribes had gained in the Cabazon case. The Nevada gaming interests also pushed for the compact provisions.²⁷

Under the provisions for negotiating a compact, if negotiations failed, each party had to submit an offer to a mediator. The mediator picked an option and submitted it to the tribe and state. If the state did not approve the mediator's option, the Secretary of the Interior could step in and approve the compact. Even with state approval, the Secretary must approve a compact for it to go into effect.

The issue of good faith, however, will be less important in the future. The Supreme Court of the United States recently decided a Florida case on the issue. The court agreed with the state's position that the 11th amendment prevents states from being sued by the tribes in federal court without the state's permission.

It is an open question of what will happen next. The compact is merely an option under federal law, perhaps leaving the tribes the ability to go straight to the Secretary of the Interior. The Secretary of Interior has issued an Advance Notice of Proposed Rulemaking for regulations that would allow that. The states oppose this and argue that such an action is bad policy, in violation of IGRA, and possibly unconstitutional.

Connecticut Lost One of the First Significant Cases. Connecticut's position was that Class III games were not legal in the state. The Mashantucket Pequot Indians pointed out that a charity could have an annual Las Vegas night where casino-type games were legal. Because casino-type games were legal under certain conditions the court held the state to negotiate a compact to allow those games to be played on Indian land with or without those conditions. Thus, because charities could have a casino night one time a year, the Indian tribes were permitted to open a casino. Furthermore, even though these games were strictly limited and regulated by state, none of the state's limitations or regulation would apply, except as agreed on the compact. Because the state had failed to negotiate with the tribe, the court ordered the state to negotiate a compact within 60 days of its order.

The court settled this dispute and agreed with the tribe's position. The state was found to not be negotiating in good faith and the Indians were able to set up a casino. This was the first of several cases where the state lost the leverage that it could have gained by a

compact, because it failed to negotiate. While the Supreme Court decision has eliminated the ability of tribes to take states into federal court, it still leaves states without authority unless they negotiate a compact.

There was an additional dispute in Connecticut over whether slots were allowed. The state and tribe came to agreement and the state receives a payment from the tribe of at least \$100 million annually. This casino, Foxwoods, is now one of the largest casinos in the Western hemisphere.

Indian Casino Gaming Has Become Widespread. The spread of casino gaming into states where it is generally not legal was an unforeseen result of the compact process.²⁸ In Minnesota, the federal mediator concluded that since Minnesota allows private social games such as blackjack and poker in private citizen's homes, the tribes could do these things in casinos.

Significant Indian Gaming Cases

State of California v. Harold Monteau. This case has been brought by the state against the National Indian Gaming Commission to compel them to shut down slot machines at tribal casinos. The state lost its case at the District Court in December 1996. The state is considering an appeal.

Seminole v. State of Florida. In this case, the Supreme Court held that the Indian tribes cannot sue states under the Indian Gaming Regulatory Act in federal courts without state permission. In other words the tribes cannot force states to negotiate gaming compacts. The decision was based on the 11th Amendment to the Constitution which provides that a state can only be sued in its own courts or if it consents to the suit. Basically states have a sovereign immunity from lawsuits filed in federal courts and Congress cannot abridge that immunity through passage of the Indian Gaming Regulatory Act.

Rumsey Indian Rancheria of Wintun Indians v. Wilson. The basic issue in this case is whether the tribe can have slot machines because the lottery operates similar games. This case was decided for the tribe, but appealed to the Ninth Circuit Court of Appeals. The Ninth Circuit held for the state and decided that Indian tribes cannot offer banked games such as slots.

Western Telcon v. California State Lottery. This case was decided by the California Supreme Court on June 24, 1996. The court held that the lottery's electronic keno game was not a lawful lottery game, but an illegal banked game that is prohibited in California. Hence the state lost the case although the ruling is favorable to the state's position in negotiating with Indian tribes. In non-banked games, including the lottery, the house collects a flat percentage. With a banked game the house is betting against the players and has a stake in the outcome. Although not strictly an Indian gaming case, it has ramifications over what is legal in California, hence what the tribes can operate

Sycuan Band of Mission Indians v. Roach. In this case, the court held that the State has no authority to prosecute tribe's employees for conducting tribal gaming.

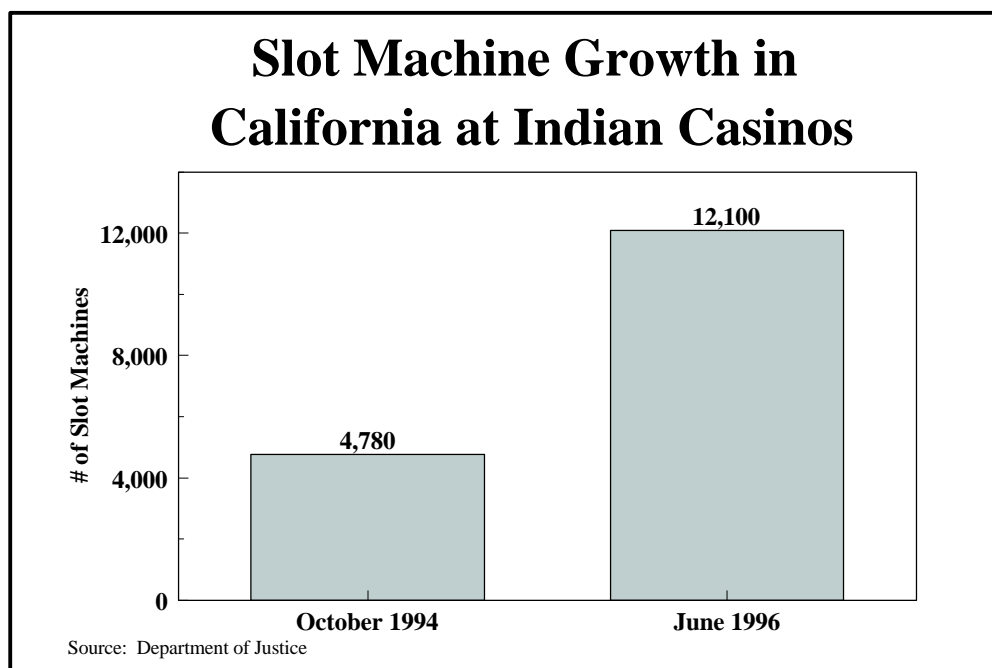
Indeed the act has been so successful in promoting Indian gaming that one observer noted:

“The IGRA may fairly be said to be the first Indian victory since the Little Bighorn.”²⁹

When the States and Tribes Cooperate, States Have Been Able to Gain Some Concessions. For example, in Minnesota the 11 tribes that have entered into compacts have agreed to limit table games to blackjack. Minnesota also uses the compacts to get Indian tribes to set minimum gambling ages. As noted before, Connecticut ended up with a share of the slot machine revenues. The governor of Kansas was anxious to sign a compact and upset that the Legislature prevented him from doing that. He was concerned that without the compact, the state will have no regulatory say over Indian gaming.³⁰ Among the conditions negotiated in the compact were state inspections, background checks and an agreement to create a state gaming commission that would oversee Indian gaming. The tribes even agreed not to offer games that compete with the lottery.

The Kansas case highlights a key case in the compact process. Some observers see the negotiations to be a legislative action, hence the Governor cannot unilaterally negotiate. A decision by the New Mexican Supreme Court supported this notion.

California Has Been Locked in Litigation With the Tribes. At issue is whether or not the lottery games are the same as slot machines. Despite the litigation and controversy about slot machines, there are over 12,000 slot machines in Indian casinos in California. Although the state argues that they are illegal, and that position has been upheld in the court, federal law prevents the state from acting to have them removed. Only the U.S. Attorney can act, but there has been no action pending resolution of the cases. The U.S. Attorney General has sent letters to the U.S. Attorneys encouraging a review of Indian gaming and direction to terminate any illegal gaming. The reluctance of the U.S. Attorneys to act may be explained by waiting for pending court cases to be resolved and their experience in other states where the U.S. Attorney acted against Indian casinos only to have the states reverse themselves and agree to allow slots.



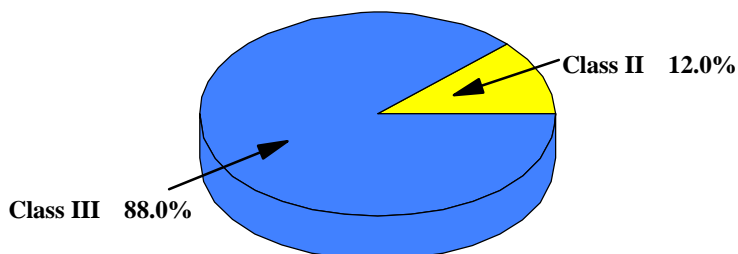
If the Goal of IGRA Was to Promote Indian Gaming, it Has Been Widely Successful.

As noted in the first sentences in this section, Indian gaming has become a multibillion dollar industry. Over one-half of the reservations in the country offer some kind of gaming. Fifty-nine casinos have been opened, with several more in the construction process.³¹ Of the 550 recognized tribes, 109 have entered into high stakes gaming compacts in 20 states. Gaming operations range from huge casinos that rival or exceed any in the world to small bingo halls.

The following chart shows the growth of Indian gaming using the handle as the form of measurement. Some states in particular have seen dramatic growth. Minnesota has 17 tribal casinos, and Wisconsin has 11. One writer suggested that Minnesota is now the land of 12,000 slots.³²

Direction of Indian Gaming in California is Uncertain. The reason is the state's loss in the Western Telcon case. (See the Box on Major Court Cases, p. IV-7.) The case outlawed the lottery's electronic keno and definitely states that the Lottery cannot have banked games. Traditional slots are banked games. Maintaining the continued level of success in Indian gaming will require the alteration of traditional slots into non-banked lottery games, where the payout is dependent on the number of players and the house takes a cut based on the number of players, not the outcome of the game. In addition, they cannot use anything that would fall under the very broad definition of slot machines under California law. Arguments exist over how easy it is to make this change.³³

U.S. Indian Gaming 1995



Source: International Gaming and Wager Business

After paying all costs, including management fees, wages, and winnings, the profits from Indian gaming accrue to the tribe for distribution. Consistent with the IGRA, tribes can make per capita distribution. Although the amount of money the tribes have earned varies, a significant share is going into service for members of the tribes. Indian gaming has slowed the migratory trend of Indians moving from the reservation to urban areas and has even reversed some of the migration.³⁴ Some tribes have made direct payments to tribe members. The practice of direct payments alarm some people, for fear that the money will not be invested to improve the Indian's welfare. The evidence from earlier payments for land sales showed that they tended to be spent on consumer goods and were not invested.³⁵ This concern over how payments are spent is heightened because of the unsure future of Indian gaming.

Another issue is the sheer size of the payments. The Mdewakanton who operate a lucrative casino have distributed sixty-five percent of their net profit to 100 members. Reportedly, payments exceeded over \$500,000 each.³⁶ Other tribes invest their funds, replacing housing, protecting areas of cultural significance, and building schools. Some small tribes in California have significant gaming operations.

Arguments Exist Over the Adequacy of Regulation of Indian Games. The IGRA also established a National Indian Gaming Commission made up of three administration appointments. The Commission is charged with the oversight of Class II games.

Tribal representatives strenuously argue that the regulation of gaming is adequate. They point out that because the profits accrue to them, they have every incentive to make sure that there are not diversions either from crooked players or employees. Others offer far