

Regulatory Impact Statement

Multi-Year Grants from Non-Casino Gaming Machine Proceeds

Agency Disclosure Statement

1. This Regulatory Impact Statement has been prepared by the Department of Internal Affairs (the Department).
2. It provides an analysis of policy options to increase the likelihood that non-casino gaming machine societies will fund long-term strategic projects that confer significant community benefit. Societies and grant recipients report that there are barriers to funding and undertaking these projects as the law stands.
3. It also analyses a proposal to amend a regulation that allows some societies to accumulate gaming machine profits. The Department considers that the wording of this regulation aggravates the risk of misappropriation.
4. The Gambling Act 2003 (the Act) regulates all gambling in New Zealand and includes powers to make regulations to deal with matters of detail.
5. The Gambling (Class 4 Net Proceeds) Regulations 2004 (the Regulations) set out requirements for societies that operate non-casino gaming machines. Part 1 of the Regulations sets out requirements for all such societies. Part 2 sets out additional requirements for societies that operate machines mainly to distribute the proceeds to the community through grants. It is these additional requirements that are the focus of this Regulatory Impact Statement.
6. The analysis of regulatory options encompassed a review of the Regulations. Possible amendments to the Act were outside scope, and were not considered. The objectives could be achieved without such amendments.
7. Grant-making decisions remain the prerogative of gaming machine societies. The preferred option will empower societies to fund long-term strategic projects that confer significant community benefit, but they cannot be required to do so. That said, the proposed additional regulations to enhance grant-making transparency, and the resulting public scrutiny, will make it more likely that multi-year grants will largely be made only for such projects.
8. The Act requires consultation with affected groups before regulations are amended. This consultation was carried out in November and December 2010.
9. The analysis is based on the observed effects of the current gambling legislation, the results of consultation, and some assumptions about likely behaviour by gaming machine societies, grant recipients, and other entities.
10. The policy options are unlikely to: impose additional costs on business; to impair private property rights, market competition, or the incentives on businesses to innovate and invest; or to override fundamental common law principles. Compliance costs are unlikely to increase, and might even reduce.

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Problem definition

11. Current regulatory requirements mean that gaming machine societies do not have the confidence to fund, and community groups that are potential grant recipients do not have the confidence to undertake, long-term strategic projects that confer significant community benefit.
12. An additional problem, which the Department of Internal Affairs (the Department) has identified, is that the wording of one regulation permits residual gaming machine profits to accumulate in some societies' bank accounts, increasing the risk of misappropriation.

Status quo

13. All gambling in New Zealand is regulated by the Gambling Act 2003 (the Act) and related regulations. The Act's objectives include: limiting opportunities for crime or dishonesty associated with gambling, ensuring that money from gambling benefits the community, and facilitating community involvement in decisions about the provision of gambling. Under the Act, corporate societies are licensed to operate non-casino gaming machines to raise money for authorised (i.e. community) purposes.
14. Most of the 50 societies that operate machines in commercial venues, such as pubs, *distribute* their net proceeds (i.e. their profits after meeting operating costs) through grants to authorised purposes. These grants typically total more than \$250m annually. By contrast, societies that are clubs tend to operate machines in their own premises, and *apply* their profits, which typically total over \$50m annually, to their own authorised purposes.
15. A few societies *distribute* some of their profits through grants to the community, and *apply* the rest to their own authorised purposes.
16. Part 1 of the Gambling (Class 4 Net Proceeds) Regulations 2004 (the Regulations) sets out requirements for all gaming machine societies. In addition to meeting these standard requirements, societies that *mainly distribute* their profits through grants to the community are also required, by Part 2 of the Regulations, to:
 - distribute a minimum amount (at least 37.12 per cent of GST-exclusive gross proceeds) through grants each financial year (regulation 10)
 - distribute most of their grants quarterly, and the remainder within 3 months after the end of the financial year in which the profits were earned (regulation 11)
 - make grants from available funds and not on the understanding that funding will be sourced from future profits (regulation 16(g)).
17. The benefits of regulations 10 and 11 are that they help to ensure that each society to which they refer achieves a minimum return to, and regularly makes grants to, community purposes. The benefit of regulation 16(g) is that it helps to ensure that societies do not undermine the transparency of the system by earmarking future profits for selected grant applicants.
18. The main problem expressed by some societies and grant recipients is that regulation 16(g) means that they do not have the confidence to fund (in the case of societies) or undertake (in the case of grant recipients) long-term strategic projects that confer significant community benefit. This concern was confirmed in a recent consultation process.

19. Projects such as building sports facilities, running sports and arts organisations, and running periodic sports events and arts festivals, typically require certainty of funding over several years, not just for the first year. However, the relevant regulation prohibits multi-year grants, denying societies flexibility and denying grant recipients a degree of certainty.
20. A second, separate, problem is that regulation 11 sets a time limit for societies to *distribute* their profits by way of grants. However, this regulation does not specify a time limit to *apply* residual profits for those societies that *distribute* most of their profits in grants and *apply* the remainder to their own purposes. The Department considers that this permits residual profits to accumulate in some societies' bank accounts, increasing the risk of misappropriation.

Objectives

Desired outcomes/objectives against which options analysed

21. The primary objective is to increase the likelihood that non-casino gaming machine societies will fund, and community groups that are grant recipients will undertake, long-term strategic projects that confer significant community benefit.
22. A further objective is to deal with the risk of residual gaming machine profits being misappropriated.

Authoritative or statutory basis for undertaking the analysis

23. The Act includes a variety of regulation-making powers. In particular, section 114(1)(d) and (f) allow regulations to be made prescribing requirements for grant applications, and prescribing other requirements about the management, application, or distribution of net proceeds. Section 372 requires prior consultation with persons or organisations likely to be affected by proposed regulations.
24. In terms of regulatory options, only amendments to regulations were considered. The objectives can be achieved without amendments to the Act. In addition, any proposal to amend the Act would be likely to elicit a considerable number and wide variety of divergent proposals for more fundamental reform of the gambling sector. Undertaking a review of that scope was not considered desirable at this time.

Regulatory impact analysis

Non-regulatory options to facilitate funding of long-term strategic projects

25. Currently, there are two ways that a society could support long-term projects.
26. A society can make a large grant for a long-term project on the basis of a single application, as long as it has the money to do so in a single quarter and puts in place accountability measures to ensure that the grant is spent as intended over the life of the project.
27. Alternatively, a society can prioritise some types of applications in the course of its annual review of its grant-making policies. For example, it could adopt a policy to grant the first 10 per cent of available funds in each quarter to qualifying applications related to the 2012 Olympics or the next biennial International Arts Festival. It could do this without formally promising to make a grant, which would be a breach of regulation 16(g).

28. The Department has publicised these options. However, it appears that societies still do not tend to fund, and community groups do not have the confidence to undertake, long-term strategic projects. Consultation suggests that the prohibition in regulation 16(g) is seen as a barrier to such projects. In addition, societies and community groups see these two non-regulatory options as largely impractical, because they are not seen as providing sufficient flexibility for societies or certainty for grant applicants.

Regulatory option to facilitate funding of long-term strategic projects (preferred)

29. The regulatory option is to revoke regulation 16(g). This option is preferred because it provides more flexibility for societies wishing to make lawful, in principle, multi-year commitments, and a little more certainty for grant applicants, than the non-regulatory option. The regulatory option also entails making additional regulations to support the purposes of the Act and to ensure compliance with sections 53 and 109.
30. Section 53 limits a gaming machine society's operating licence to a maximum term of 18 months. In practice, licences are issued for terms of 1 year at a time. Therefore, unless a society has complied with all relevant regulatory requirements, it might not have an operating licence to enable it to honour a multi-year grant arrangement beyond the first year.
31. Section 109 requires a society that mainly distributes its profits through grants to, at least annually, review the criteria, methods, systems and policies it uses to consider grant applications. Again, this means that a society might not be able to honour a multi-year grant arrangement beyond the first year, because its policies must be able to change as a result of a review.
32. Even if regulation 16(g) was revoked, it would be at best imprudent, and at worst unlawful, for the trustees or directors of a gaming machine society to make a fully-binding multi-year grant. Revoking regulation 16(g) would allow a society to make an *in principle* commitment to a multi-year grant.
33. Therefore, for societies that mainly distribute their profits through grants, the following additional regulations are proposed as safeguards (to support the Act's accessibility, transparency and accountability objectives, and to ensure that societies do not inadvertently fall foul of section 53 or section 109):
- a) A requirement that future instalments of a multi-year grant be conditional on the society still having a licence, funds being available, and the grant otherwise being lawful.
 - b) A requirement that each instalment of a multi-year grant be re-confirmed before payment, allowing a society to withdraw if, for example, its trustees or grant-making policies change.
 - c) A requirement that, at the time of seeking future grant instalments, a recipient of a multi-year grant provides evidence that earlier instalments of the grant were spent for the purposes for which they were provided.
 - d) A limit on the term of any multi-year grants to a maximum of 4 years, to help mitigate risk and to fit in with the typical cycles for large sports and cultural events (e.g. 4-yearly sports events and biennial arts festivals).
 - e) A requirement that a society discloses multi-year grants in its publicity about available funds and grants made, and in the annual report required by the Act.
 - f) A requirement that a society publishes its annual report on the website that it is already required by regulation to maintain.

34. If the Regulations are amended as proposed, the Department will advise societies about the long-term monitoring, and additional reporting, requirements in respect of multi-year grants. It will also advise societies to make recipients of multi-year grants aware of the conditions set out in the additional regulations, and that it would be unwise for a grant recipient to make binding, unconditional commitments on the basis of an in principle grant. Finally, the Department will publicise the amendments and their implications directly to community groups (e.g. through a few key publications).
35. Revoking regulation 16(g) might make it slightly more difficult for the Department to take compliance action, because groups promised multi-year grants are likely to lobby for non-compliant societies to retain their licences. However, published advice will help ensure that groups promised multi-year grants are aware that future instalments are conditional, among other things, on the society still having a licence. Prudent grant recipients will, therefore, make contingency plans.
36. Regulations made under the Act cannot require gaming machine societies to give priority to one type of authorised purpose over another. Grant-making decisions will remain the societies' prerogative. Revoking regulation 16(g) will empower societies to fund long-term strategic projects that confer significant community benefit, but it does not guarantee either that they will fund long-term projects, or that the long-term projects they do fund will be strategic projects that confer significant community benefit. That said, the proposed additional regulations to enhance grant-making transparency, and the resulting public scrutiny, will make it more likely that multi-year grants are largely made only for such projects.
37. There is a risk that multi-year funding and most available funding will be granted to a limited number of grant applicants. Once again, public scrutiny will militate against this happening, but will not guarantee that it does not. It is worth noting, however, that this risk already exists. The additional regulations will at least ensure that communities know, or are able to find out, what funds are available and what funds have already been committed in principle, and to whom multi-year commitments have been made and for what.
38. There is also a risk that societies will be unable to make grants to projects that they might see as a priority in future (e.g. grants to assist in the recovery from a major earthquake) because most of their funding is tied up in multi-year grants to projects that they have seen as a priority in the past. The requirement that each instalment of a multi-year grant be re-confirmed before payment will afford societies some leeway in such cases, albeit to the detriment of those community groups previously promised multi-year grants.
39. Despite these caveats associated with the regulatory option, it is the preferred option. Societies and community groups that are grant recipients have made it clear that they do not see the status quo as workable, and as a result few grants are made for long-term strategic projects. They have also indicated that the regulatory option will increase the likelihood that societies will fund, and grant recipients will undertake, such projects.
40. It is anticipated that the costs to societies of complying with these regulatory amendments will not change. The recent consultation (discussed below) indicated that there would be little or no effect on those costs. Some societies thought their costs would reduce because there would be fewer annual grant applications to administer.

Regulatory option to deal with the risk of residual gaming machine profits being misappropriated

41. Under regulation 11, there is a time limit for societies to distribute their profits by way of grants. However, for those societies that *distribute* most of their profits through grants and *apply* the remainder to their own purposes, there is no specified time limit to *apply* those residual profits. The Department considers that this permits residual profits to accumulate in some societies' bank accounts, increasing the risk of misappropriation. There is no non-regulatory option to deal with this issue.
42. Regulation 11 could be amended so that such a society would have to apply any residual profits to its own authorised purposes in the same timeframe as for the distribution of profits through grants.

Consultation

43. On 10 November 2010, the Cabinet Domestic Policy Committee (DOM) approved the public release of the *Consultation on Gambling (Class 4 Net Proceeds) Regulations 2004* document. The major sporting, non-casino gaming machine gambling, problem gambling, community, arts and cultural, and local government organisations were consulted. The consultation closed on 17 December 2010.
44. The 56 submissions received confirmed the perceived problem with regulation 16(g). Most (50 of 56) submitters were in favour of allowing in principle multi-year grants by revoking regulation 16(g). The issue with regulation 11 was less clear-cut, with opinions divided, but most of the organisations (44 of 56) did not make a submission on this.
45. Some disadvantages of revoking 16(g) were cited (in some cases, by those in favour of revocation). For an applicant, there was no guarantee of a multi-year grant because it depended on the society having a licence, and trustees and grant policies not changing. For a society, a multi-year grant could restrict the policies of future trustees if community needs changed, and was also contingent on sufficient funds being available and the society having an operating licence.

Conclusions and recommendations

46. Under the present gambling legislation, a gaming machine society can fund a long-term strategic project through a large grant. To do this, a society must have the money available in a given quarter and establish suitable accountability measures to ensure the grant is spent as intended.
47. In addition, a society can review and change its grants criteria and policies to give preference to long-term strategic projects.
48. However, to allow gaming machine societies a little more flexibility to fund, and grant applicants a little more certainty of funding to undertake, long-term, strategic projects that confer significant community benefit, it is recommended that regulation 16(g) of the *Gambling (Class 4 Net Proceeds) Regulations 2004* be revoked. Revoking regulation 16(g) would allow societies to make *in principle* commitments to multi-year grants. Additional regulatory safeguards should also be made to ensure continued compliance with the gambling legislation, and to help mitigate some risks of revoking regulation 16(g).

49. It is also recommended that regulation 11 be amended so that a society that has accumulated residual profits is required to spend those profits on its own purposes in a timely fashion, specifically, within the same timeframe as for the distribution of profits through grants. While the risk inherent in the current wording of this regulation does not yet seem to have been realised, making this amendment would reduce the risk of those residual profits being misappropriated.

Implementation

50. If the Regulations are amended as proposed, the Department anticipates they will be notified in the *Gazette* no later than 25 August 2011.
51. The Department will advise societies about the long-term monitoring, and additional reporting, requirements in respect of multi-year grants. It will also advise societies to make recipients of multi-year grants aware of the conditions set out in the additional regulations, and that it would be unwise for a grant recipient to make binding, unconditional commitments on the basis of an in principle grant. Finally, the Department will publicise the amendments and their implications directly to community groups that are potential grant recipients, for example through items in a few key electronic or paper publications.

Monitoring, evaluation and review

52. The Department administers and monitors the gambling legislation, licenses non-casino gaming machine activities, ensures compliance with the legislation, and provides public information and education. The Act and regulations made under the Act, and the behaviour of societies and grant recipients, are subject to ongoing review in the course of these processes.
53. The Gambling Commission (an independent quasi-judicial body), among other things, considers and deals with complaints about the Department's handling of non-casino gaming machine issues. It also considers and determines appeals against the Department's regulatory and licensing decisions.