

Chapter 3

Section 3.01

Alcohol and Gaming Commission of Ontario

Casino Gaming Regulation

Background

Under the *Criminal Code* of Canada, provinces are assigned responsibility for regulating, licensing, and operating legal forms of gaming. In Ontario, two Crown agencies, with different responsibilities and an arm's-length relationship, are primarily involved in overseeing casino gaming. The Alcohol and Gaming Commission of Ontario (Commission), as the “regulator,” has a mandate to regulate, license, and inspect all gaming facilities, and to enforce gaming legislation. The Ontario Lottery and Gaming Corporation (OLG), as the “operator,” builds, manages, and operates, either directly or by contracting with private-sector operators, Ontario’s casinos and slot machine facilities at horse racetracks. During our audit, the Commission initially reported to the Minister of Consumer Services, and subsequently to the Attorney General. OLG reports to the Minister of Finance.

As Figure 1 indicates, there are 27 gaming facilities in Ontario. OLG directly operates 22 casino gaming facilities in Ontario, including 17 facilities at racetracks that have only slot machines (“slot facilities”) and five casinos with both table games and slot machines. As well, OLG has contracted with private-sector operators to run the day-to-day operations of one smaller casino and its four largest

gaming facilities, known as “resort casinos.” These resort casinos offer more gaming options, higher wagering limits, and a wide range of amenities such as hotels, entertainment venues, and meeting and convention areas. Casino gaming was first introduced in Windsor in 1994, and after that time two new gaming facilities, on average, were added each year until 2006.

In the 2009/10 fiscal year, OLG casino gaming operations generated over \$3.4 billion in revenues and incurred \$2.5 billion in operating costs, for a net profit of \$900 million for the province. Over 85% of all revenues are generated by slot machines. In addition, OLG paid \$341 million to support the horse racing industry, and OLG and private operators paid host municipalities \$78 million. Casino gaming facilities employ almost 17,000 staff.

The Commission was established in 1998 under the *Alcohol and Gaming Regulation and Public Protection Act, 1996*, replacing both the Gaming Control Commission and the Liquor Licence Board of Ontario. This act requires that the Commission exercise its powers and duties in the public interest and in accordance with the principles of honesty, integrity, and social responsibility. The *Gaming Control Act, 1992* and its regulations prescribe operating, registration, and commission-approval requirements covering key gaming suppliers and employees, the layout of gaming facilities, security, surveillance plans, controls over accounting and

Figure 1: OLG Gaming Facilities and Revenues as of March 31, 2010

Source of data: Ontario Lottery and Gaming Corporation

| | Slot Facilities at Racetracks | Smaller Casinos Operated Primarily by OLG | Resort Casinos | Total |
|---------------------------------|----------------------------------|---|-------------------------|--------------------------|
| gaming facilities | 17 | 6 | 4 | 27 |
| slot machines | 11,073 | 2,925 | 9,681 | 23,679 |
| table games | — | 129 | 375 | 504 |
| total patrons annually | 17,550,000 | 5,850,000 | 16,700,000 | 40,100,000 |
| employees | 3,800 | 2,500 | 10,500 | 16,800 |
| revenue from slot machines | \$1,685 million | \$340 million | \$960 million | \$2,985 million |
| revenue from table games | — | \$53 million | \$396 million | \$449 million |
| total gaming revenue/% of total | \$1,685 million/ 49% | \$393 million/ 11% | \$1,356 million/ 40% | \$3,434 million/ 100% |

money handling, rules of play, equipment, chips and tokens, advertising, customer credit, the exclusion of persons from gaming premises, and the Commission's investigation and enforcement powers.

The Commission operates from its head office in Toronto and nine regional offices. Its total operating expenditures for the 2009/10 fiscal year were about \$63 million, of which about \$27 million related to casino gaming. That same year, the Commission received approximately \$10 million in casino gaming revenues from fees that casinos pay to register employees, suppliers' registrations and product approvals, cost recoveries from investigations, and levying fines.

Audit Objective and Scope

Our audit objective was to assess whether the Alcohol and Gaming Commission of Ontario (Commission) had adequate policies, procedures, and systems in place to:

- ensure that gaming at casinos and slot facilities in Ontario was regulated in accordance with established policies and legislative requirements; and
- measure and report on the effectiveness of its regulatory activities designed to ensure that

gaming at casinos and slot facilities in Ontario met the principles of honesty and integrity, and were in the public's interest.

We conducted our audit work at the Commission's head office in Toronto and also visited six OLG gaming facilities, including two slot facilities at racetracks and one casino—all operated directly by OLG—and three large resort casinos operated by private companies on behalf of OLG. We interviewed commission head office and field staff; observed the activities of staff stationed at gaming facilities; conducted tests and other procedures; and examined recent policies, records, and other relevant documents that were available during our fieldwork. We also engaged an independent accredited gaming testing lab from outside of the province to assess the Commission's technical standards and the testing procedures its Electronic Gaming Branch uses to approve all new electronic gaming equipment, primarily slot machines, and to conduct random and scheduled inspections of electronic gaming equipment installed in gaming facilities.

Our audit was limited to the Commission's regulatory activities and did not include an audit of OLG's operation of casinos. Nonetheless, our audit did involve certain work at gaming facilities and we received full co-operation from OLG and its private operators. For instance, we met with

OLG management staff at their head office and at gaming facilities, and with private operators at OLG resort casinos, who gave us tours of their operations, shared their perspectives on regulatory controls over casino gaming, and described controls in casinos and the key risks and challenges facing the gaming industry.

We researched casino gaming regulations and operations in several North American and international jurisdictions. We engaged on an advisory basis the services of two independent experts in casino gaming: one having significant legal experience in U.S. gaming regulation; the other having significant Canadian executive experience in casino operations. We met with representatives from the British Columbia Lottery Corporation to discuss their perspectives on regulatory controls over casino gaming, and we attended the annual conference of North American gaming regulators, which addressed current issues, trends, and challenges facing the industry.

The ministries' and Commission's internal audit divisions had not conducted any recent audits of casino gaming activities that would allow us to reduce the scope of our audit. However, OLG and its private operators had put in place regular ongoing financial and operational audits at each casino and slot facility to verify that financial controls were in place and operating effectively, and to ensure compliance with legislative, licensing, and other regulatory requirements. The results are shared with the Commission as part of its regulatory oversight. The Commission also audits gaming facilities on a regular basis. We took these audits into consideration in reaching our conclusions.

Summary

From an overall perspective, the most important expectation that casino customers (often referred to as "patrons" by the gaming industry) have of slot machines is that the machines actually pay out the

regulated minimum payout amount. Casino patrons who participate in table games such as blackjack or craps want assurance that casino employees are honest and effectively overseen, and that the games are run fairly. The general public also expects casinos and slot facilities to be run fairly and honestly.

Overall, we concluded that the Commission had adequate systems, policies, and procedures to accomplish this. In fact, our research of other jurisdictions and expert advice indicated that Ontario's regulatory framework for casinos is not only comprehensive, but provides for one of the stronger oversight mechanisms in North America. The Commission's focus on key risks covering revenues, gaming integrity, and criminal activity involved good preventive and effective ongoing oversight. The Commission's in-house electronic gaming equipment testing lab and its electronic gaming enforcement officers working at gaming facilities use comprehensive technical standards and effective procedures for ensuring that slot machines and other gaming equipment operate as intended. This was confirmed by the independent accredited gaming testing lab that we hired.

However, we did note a number of areas in which the Commission's oversight procedures and gaming transparency could be enhanced, as follows:

- Some U.S. jurisdictions, such as Nevada and New Jersey, provide information on the actual payout ratios for slot machines in casinos and whether these payout percentages vary depending on the machine's denomination category—for instance, a one-dollar machine or a penny machine. Ontario does not provide this information, yet we believe that slot machine patrons in Ontario would appreciate having it.
- We noted that patrons would find it difficult to locate information on the maximum prize payout on certain slot machines. Aside from being useful information, this is an important disclosure should the machine malfunction and

award an erroneous jackpot. This occurred twice in the last two years, when two \$42 million jackpots were awarded by machines that were supposed to pay a maximum of \$40,000 and \$300, respectively. In addition, the Commission does not require casinos to post the odds of winning a jackpot on slot machines.

- The Commission sets no minimum training standards for key gaming employees, such as table dealers and surveillance staff, to ensure that they are aware of the many rules and procedures they must follow and to help them identify criminal activities and problem gamblers.
- During the 2008/09 fiscal year, commission inspectors at three of the four gaming facilities we tested were unable to complete their goal of inspecting all slot machines, and gaming audit and compliance inspectors were also behind schedule in verifying that gaming facilities were in compliance with approval requirements and their internal control manuals. The Commission needed to improve its risk assessments to allow it to focus more of its audit and inspection staff on higher-risk gaming facilities and less on lower-risk facilities.
- Although satisfactory procedures exist for approving new registrations for gaming suppliers and gaming assistants, we noted 12 instances where the Commission granted registration renewals to gaming suppliers even though it had not received required information from them or performed necessary investigations. Even though the Commission had not completed the renewal process for these suppliers, for more than a year after the expiry of their registration it treated them as if they had renewed; in one case, the renewal was overdue by 34 months.
- In determining registration eligibility, the Commission had no policy for dealing with conflict-of-interest situations involving related employees working in the same casino.

Instead, it relied on casino and slot facility operators to deal with these situations.

OLG has primary responsibility for operating its casinos with controls, systems, and procedures that address social and financial risks and gaming integrity in accordance with legislative requirements. Although we did not audit OLG, our discussions with its staff and visits to casinos and racetrack slot facilities indicated that it also has established extensive and comprehensive systems, controls, and verification processes to help ensure that casinos eliminate, or at least mitigate, the risks associated with the gaming industry. As a further control on the industry, the Commission has a regulatory mandate to independently control, oversee, and verify the adequacy of OLG's operations.

On a somewhat related issue, Ontario residents currently spend an estimated \$400 million annually on foreign-based Internet gaming websites. The foreign gaming operators do not provide the province with a share of these revenues, and the Commission does not have a mandate to regulate Internet gaming. The Ontario Provincial Police (OPP) is responsible for enforcing the *Criminal Code* as it applies to gaming operators that operate illegally in Ontario; however, enforcement is problematic when dealing with foreign-based gaming operations. We noted that many international jurisdictions use a range of approaches to Internet gaming, from prohibiting or restricting it to regulating and taxing its operators. British Columbia offers Internet gaming, Quebec intends to introduce it before the end of 2010, and in August 2010 OLG announced plans to introduce its own Internet gaming website in 2012.

OVERALL COMMISSION RESPONSE

We appreciate the Auditor General's overall conclusion that the Commission has adequate systems, policies, and procedures in place to ensure that casinos and slot facilities are run fairly and honestly, that casino employees are honest and are effectively overseen, and that the games are run fairly. We welcome the recommendations

in this report—especially those that help to further strengthen the Commission’s regulatory oversight over government-operated commercial gaming activities.

Detailed Observations

OVERALL REGULATORY CONTROLS

Casinos can provide significant economic benefits to the province and local communities, such as profits and increased local employment, business, and tourism. Yet there are also risks inherent in the casino industry. As is the case in other jurisdictions, the Ontario government set a goal to operate casinos in the public interest and in accordance with the principles of honesty, integrity, and social responsibility. In meeting this goal, there are ongoing challenges, such as the following:

- Social risks need to be managed to ensure that customers gamble responsibly within their limits to avoid dire financial and family consequences, and to prevent criminal elements from exploiting casinos with illegal activities such as money laundering and loan sharking, and from controlling goods-and-services supply chains used by casinos.
 - The cash nature of the business, especially with respect to betting on table games, and the large amounts processed daily by casinos pose a financial risk of losses from accounting and money-handling errors, and from theft by employees, customers, and criminal organizations.
 - The integrity of the game must be perceived as fair to patrons and the public at large. To prevent cheating or erroneous payouts, the necessary oversight processes must be in place to ensure that games of chance and slot machines cannot be manipulated. A loss of confidence in the fairness of the industry could significantly lower attendance and reduce revenues.
- The Commission’s regulatory measures, as prescribed by the *Gaming Control Act, 1992* (Act) and as established by its policies and procedures, include:
- registration of key gaming employees and commercial suppliers to gaming facilities following an investigation, including criminal background checks by the OPP, into all applicants to ensure that they meet high standards of honesty and integrity and act in accordance with the law;
 - approval of rules of play for games of chance to ensure that they are in accordance with the Commission’s standards, and verification that all table games and electronic gaming equipment meet the Commission’s standards and are from approved suppliers;
 - approval of the internal control manuals prepared by each casino operator for the safe and timely handling, accounting, and movement of money;
 - approval of security, surveillance, and floor plans for all gaming premises according to standards established by the Commission;
 - full-time presence of the OPP at all casinos and part-time presence at slot facilities at racetracks to help deter, identify, and investigate criminal activities;
 - cyclical audits of all gaming premises by commission staff to assess compliance with the requirements of the premises’ internal control manual, and with anti-money-laundering measures;
 - frequent inspections by compliance inspectors of gaming premises to monitor and test compliance with the Act, its regulations and licensing requirements, internal control systems, surveillance and security plans, standards and directives, and approved rules of play; and
 - pre-installation and random inspections of electronic gaming equipment and gaming

management systems, and independent verification of each large jackpot won from electronic gaming equipment.

Overall, we concluded that the Commission had adequate systems, policies, and procedures for regulating casino gaming in Ontario, and our research, including our reviews of other jurisdictions in North America, indicated that Ontario's regulatory framework for casinos was comprehensive. We did, however, identify certain areas where the Commission should either improve or reassess its systems and procedures, particularly with respect to communicating better information on games of chance to patrons, renewal of registrations, approval of electronic gaming equipment, frequency of inspections and audits, and reporting to the public and the Legislative Assembly on its performance in achieving its regulatory mandate and on the integrity of Ontario's gaming industry.

CONTROLS OVER GAMES

Electronic Gaming

We found an extensive system of controls in place to ensure the integrity and security of electronic gaming equipment, which includes some 24,000 slot machines at gaming facilities, as well as computer systems linked to slot machines, playing-card shufflers, and self-serve ticket and money-redemption machines. The Commission's controls include minimum standards for electronic gaming equipment, in-house testing of new gaming equipment proposed by manufacturers before approval is granted for its use in Ontario, verification of all new gaming equipment before installation and when changes are made, sealing of key electronic components of the equipment to prevent access once the machine has been tested, limiting access to equipment service areas, and periodic random testing of installed electronic games to identify any changes or tampering. Another key control is the testing of slot machines that have awarded a large jackpot.

Four U.S. states and Quebec are the only other jurisdictions in North America that have the capacity internally to test electronic gaming equipment. Generally, their labs are responsible for assessing all electronic gaming equipment, including slot machines and related software, for casino use. Other jurisdictions rely on private labs to test their electronic gaming equipment. The Commission's Electronic Gaming Branch (Branch) includes 10 staff in its head office and 32 electronic gaming enforcement officers who work at gaming facilities. We found that the Branch had established quality assurance measures for its lab and was working toward accreditation to an ISO standard.

We contracted a private testing lab to examine and report on testing of electronic gaming equipment carried out at the Commission's gaming lab and ongoing inspections of installed gaming equipment at casinos and slot facilities. The testing lab concluded that the Branch had satisfactory security controls in place to prevent loss, damage, or unauthorized access; technical standards were consistent with those applied by regulators in other North American jurisdictions; testing procedures adequately addressed the standards; and an effective management system and internal controls were in place to ensure accuracy and consistency in results and product approvals. In addition, the testing lab found that procedures used by field workers were adequate for testing slot machines in operation in the casinos and at slot facilities.

Slot Machines

In Ontario, the Commission has established a minimum theoretical payout of 85% of money wagered for all games played on slot machines. The result of each game played is determined using a random number generator built into the slot machine and there is no guarantee to win a prize on any given game; however, over time, the machine's total payout relative to all money played is a percentage programmed in what is known as the machine's "pay table." It may take hundreds of thousands of

plays before the pre-programmed payout rate—also called the “return to player”—is reached. A casino or slot facility in Ontario may choose an overall payout rate higher than 85%, but cannot set a machine with a lower payout. In order to change the payout rate of any slot machine, a request must be submitted to the Commission for approval and an inspection.

The Commission’s minimum theoretical payout standard of 85% compares favourably to other North American jurisdictions, which we found to have lower minimum payout rates. More importantly to players, OLG and private operators typically set slot machine payout rates at about 91% to 93%, which is similar to return-to-player rates publicly reported by some other North American jurisdictions we researched.

To ensure that slot machines pay minimum returns, the Commission conducts a quarterly review of a report on each of the 24,000 slot machines in play to assess the actual return-to-player rate. Machines paying less than 85% or over 100% are flagged for review and possibly an inspection. Slot machines paying outside the expected range are either removed from service or monitored at 30-day intervals until they are in compliance. Where a slot machine that is identified as not meeting the minimum payout is normal, this is usually due to low volumes of play and low recent prize payouts by the machine. In the quarterly reports we reviewed for the year preceding our audit, less than 0.1% of all machines paid less than 85%, and most of these were paying in the range of 84% to 84.99%. No electronic gaming enforcement officers at gaming premises we visited could recall a slot machine that needed to be taken out of play for not meeting the minimum required payout rate of 85% over time. Similarly, machines rarely overpay over time, although their payout rate might exceed 100% in the short term if they have recently paid a jackpot.

We believe that information on the minimum 85% payout and the actual average payouts of each casino and type of slot machine (for instance, a

one-dollar machine or a penny machine) should be made public on the Commission’s website. We noted that Nevada and New Jersey publicly report return-to-player information for each of their casinos. This would also provide the opportunity for the Commission to assure gaming patrons and the public at large of its key role in overseeing actual payouts and in ensuring the reliability of information regarding gaming in Ontario. We believe that patrons would welcome this information and that it would allow the Commission to better communicate its role in ensuring the fairness and integrity of gaming in Ontario.

Disclosure of Maximum Prize Payouts and Odds of Winning for Individual Slot Machines

The Commission sets a standard for the provision of information to customers on slot machines’ maximum possible prizes. We question, however, whether this standard is sufficient. On our site visits, we found that maximum prize amounts and prize tables were not always easy for customers to access. In many cases, either the information was not available or the player needed to navigate through multiple video screens to obtain it. For slot games that had variations of play based on the amount wagered, the screens were often complicated and unclear as to the maximum payouts. Some machines referred to credits instead of monetary payouts. When we asked both the local electronic gaming enforcement officer and the casino’s slot attendant staff to find the maximum payout information on slot machines we had randomly selected, they also had difficulty finding or could not find the information for several machines. We also noted progressive slot machines (whose jackpots grow with each play) that did not have the maximum payout sign as required by commission standards. There is also no standard and requirement for disclosing on the slot machine the odds of winning the jackpot.

We noted that there have been two large jackpot errors with slot machines over the last two years

at OLG gaming facilities. Coincidentally, both erroneous jackpots were \$42 million, whereas the maximum jackpots were intended to be \$40,000 and \$300, respectively. Some other jurisdictions also incurred similar situations. Although OLG is not legally obligated to pay out jackpots caused by equipment failure, these incidents would be easier to explain to patrons as equipment errors if the maximum prize payout were posted on the machines and relatively easy for patrons to identify.

Slot Machine Inspections

The Electronic Gaming Branch's annual risk assessments did not address inspection frequency. Our discussions with field staff identified that their goal is to inspect all 24,000 slot machines at least once per year. We reviewed inspection frequencies at four of the gaming facilities we visited. During the year ended February 2010, at one gaming facility, all slot machines were inspected; at two facilities, about 95% were inspected; and at the fourth facility, less than 80% were inspected. It is important to note, however, that historically such inspections identified only minor deficiencies, such as loose lock hardware, loose buttons and hinges, and light bulbs not working. Nevertheless, we also noted that electronic gaming enforcement officers conducted about 50,000 inspections annually over the last three years, including inspections for new machine installations, supplier notifications, and equipment malfunctions, as well as random inspections. At the casinos we visited, electronic gaming enforcement officers did not recall any instance of a jackpot involving a slot machine that had been tampered with. When an unusual jackpot win of \$42 million occurred at one slot facility, all the machines with similar software were shut down within an hour, and the cause of the error was subsequently determined to be a hardware malfunction. Slot machine suppliers notify the Commission if a problem with a slot machine or brand is identified either by them or in another jurisdiction. We understand that, in the current and previous fiscal years, the Commission

issued 17 critical supplier notifications as a result of receiving such information from suppliers. Our review indicated that all gaming sites we visited responded to these notifications by immediately taking the machines out of play or replacing defective components in a timely manner.

Seals on Sensitive Electronic Components

After each slot machine is newly installed or randomly inspected, an electronic gaming equipment officer affixes a tamper-proof serially numbered seal on its key hardware computer chip. A broken seal could indicate that the computer chip had been removed and possibly tampered with, which would be a serious incident triggering an investigation by the Commission, which could involve the OPP.

Although commission field staff record the serial number of each seal in their records, there are no periodic audits of seals. This results in a risk that seals could be misplaced, improperly recorded, or stolen and used inappropriately without being detected and accounted for. There is also a risk that a seal could be broken, the machine tampered with, and a new seal put on the machine to disguise the tampering. Our test of seal inventory at one casino noted three seals that were recorded as unused but were not in the vault. Upon further investigation, the electronic gaming enforcement officer was able to account for the seals having been used within the last three months but not recorded properly in the inventory logs. The Branch informed us that it accounts for seals sent out to electronic gaming enforcement officers and replenishes their inventory as needed, and relies on regional managers to monitor and review records on the use of seals.

Table Games

Because table games involve significant amounts of money, oversight to ensure that gaming rules are observed and the integrity of the game is maintained involves many layers of control. The cards and dice are replaced at regular and frequent intervals; a

table games supervisor and pit managers oversee dealers; surveillance cameras record the play activity; and surveillance operators may watch the play, looking for compliance with procedures and for misconduct. Plainclothes OPP officers also have camera surveillance available to them. For each table game, the casino's backroom staff will calculate the hold (the percentage retained by the casino after paying winnings) and assess whether it is within an expected range. For example, roulette games are designed to result in the casino retaining, in theory, 5.6% of the amount wagered. As with slot machines, although the hold rate will vary between individual plays, over a period of time—several thousand plays—the targeted rate should be achieved. If it is not, this may be an indicator that a customer and/or a dealer is involved in dishonest conduct and is manipulating game results.

At the time of our audit, we were informed that the Commission's Audit and Gaming Compliance Branch had just completed a pilot project that analyzed payout rates on table games at each site. Largely because the payout associated with table games depends on the "roll of the dice" or the "fall of the cards" as well as the skill level of the patrons, the Commission cannot realistically set a required minimum percentage of payout on table games. However, it does consider the expected hold rates when approving the rules of play for a game. Commission analysis of hold rates will help confirm that the rules of play are being observed and help detect fraudulent activity that the casino might not detect.

We noted during our visits that OLG casinos require potential table game dealers to pass a four-to-six-week in-house training course before they work on the gaming floor. In addition to rules of play and dealing procedures, the training covers counterfeit currency detection, responsible gaming, customer services, and gaming security. Resort casino operators informed us that they generally hire experienced dealers who must first pass a test, followed by up to one week of training. We noted that neither the Act nor any regulation requires a specific level of competency or certification for deal-

ers. The Commission does not specify minimum training requirements for dealers, although such requirements would be appropriate given dealers' direct involvement with customers and the expectation that they can identify issues pertaining to gaming integrity, money handling, and responsible gaming.

Surveillance

A Commission-approved surveillance plan requires a floor plan of the premises showing the placement of all surveillance equipment and a description of the operator's policies and procedures. Minimum standards set out surveillance requirements such as types of equipment, areas to be covered by surveillance, minimum camera coverage over gaming areas, recording requirements, minimum staffing levels in the surveillance room, and backup procedures should surveillance systems fail.

The Commission sets minimum surveillance staffing levels for each gaming facility based on square footage of the gaming floor; however, this method does not take into consideration varying risk at different casinos depending on the games played and the number of patrons during peak times of operation, such as on weekends. At several locations, we were informed that if the casino followed the Commission's minimum surveillance staff requirement, it could not operate effectively—it therefore used higher staffing levels. Casino staff informed us that table games posed the greatest risk to the operator, and surveillance staff generally focused a significant portion of their time on live viewing of table game activities. The risk of the operator being defrauded by a customer using slot machines was generally low because of their proven and mature technology.

We were informed that surveillance rooms themselves are not covered by surveillance cameras and recording. Although there is a requirement that surveillance operators always work in the presence of a supervisor, surveillance recording of the surveillance room itself would permit the commission

compliance officer to randomly check previously recorded video to verify that the minimum number of surveillance staff were present and performing their surveillance duties, and that no unauthorized casino staff were in the surveillance room.

The Commission does not set minimum training requirements for surveillance staff, who would be expected to know the rules of each game, proper security measures, and operational procedures. For instance, in addition to monitoring table games, surveillance staff monitor security checkpoints, such as the casino entrance, and cash-handling procedures, such as activity in the money-counting rooms. One gaming operator informed us that its surveillance staff spend five days in the classroom, followed by 100 hours with an experienced surveillance operator, and that people who are hired have prior experience in security and loss prevention. At another location, surveillance staff undergo up to five weeks of training, and must achieve at least 75% on a final test. We were informed that OLG is considering creating a standardized training program for surveillance staff across the province, as British Columbia already has in place.

RECOMMENDATION 1

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

- make public the minimum 85% slot machine payout percentage, a range of actual payouts, and the Commission's role in overseeing this, similar to the public disclosures made in Nevada and New Jersey; and
- review its standards and approval processes for new and existing slot machines to ensure that the maximum prize payouts and odds of winning are clearly disclosed or readily obtainable on each machine.

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

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

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

COMMISSION RESPONSE

The Commission agrees with the principle that there be adequate, appropriate, and easily understood disclosure to consumers on how casino games, including slot machines, function and on enhanced payout disclosure. The Commission undertakes to consult with the OLG, gaming suppliers, government, and other interested stakeholders on how best to achieve the appropriate balance between this objective and the potential impact on business operations. The Ontario Lottery and Gaming Corporation, casino operators, and gaming equipment manufacturers have been aware of the minimum theoretical payout requirements since 1994,

and these have always been publicly available upon request. In addition, the Commission has recently included on its website the Electronic Gaming Equipment Minimum Technical Standards.

We agree with the audit recommendations on inventory control and have updated our procedures accordingly. In addition, the Commission will continue to implement its risk-based approach to slot machine inspections, including taking into consideration the Auditor General's recommendations.

The Commission will continue to review its approval requirements for surveillance plans and will consult with stakeholders on how to best address this recommendation.

GAMING AUDIT AND COMPLIANCE

Before a gaming facility is opened and for any changes thereafter, a regulation under the Act requires that operators obtain commission approval for the facility's layout, security equipment, games played, staffing and operating procedures, and financial controls. Commission approval is required for floor, surveillance, and security plans; all electronic and non-electronic gaming equipment; each type of game of chance played and its rules; chips and tokens; and internal control manuals covering compliance-related operating, accounting, and financial controls.

Commission-trained audit staff and regional compliance staff assess the ongoing compliance with the approved internal control manual, floor plan, security plan, and other requirements of the Act and its regulations. In addition, casino operators are required to report to the Commission any significant incidents of non-compliance or breach of approval requirements. Considering the size of Ontario's gaming industry, there are very few significant incidents identified by the Commission or brought to its attention by gaming operators

or customers. As well, the OPP informed us that instances of criminal activity related to gaming, such as cheating, in gaming facilities are infrequent and are typically small and isolated cases.

As outlined in the following sections, we found approval requirements, ongoing compliance inspections, and other commission controls to be effective for ensuring that gaming premises are designed with proper security and financial controls, and for ensuring the integrity of games played.

Audits of Gaming Facilities

The Commission has a goal of auditing each gaming facility every 18 months for its compliance with the approved internal control manual. These commission audits take into account audit reports from OLG and resort casino operators' internal auditors, site auditors, and annual audits carried out by an external auditor. Operators of the gaming premises have 30 days to respond to the findings and must follow up on any significant issues within six months.

We noted that the Commission's audit section was behind schedule in auditing 15 of the 27 casino gaming sites, including all four resort casinos. More significantly, two of the four large resort casinos had not been audited more than two years after their 18-month due date—that is, more than three-and-a-half years after their previous audit. Although our review of commission reports from several recent audits carried out by the audit section and our discussions with staff at gaming sites indicated that these audits typically do not identify significant findings, the Commission needs to catch up on the audit backlog. Alternatively, the Commission should reassess its inspection frequency from a risk perspective, which we discuss under Risk Assessments later in this report.

Compliance Inspections

Commission compliance inspectors spend most of their time at larger gaming premises and attend

part-time at smaller sites, where they respond to incidents, monitor gaming facilities, and conduct tests to verify that casinos operate in accordance with approval requirements. The Commission sets a minimum number of visits that its compliance inspectors must make to a gaming facility each year. It also requires that each gaming facility's site and operations be tested each year to ensure that all the key requirements of the approved plans and the internal control manual are adhered to. In addition, compliance inspectors assess gaming facilities under the *Liquor Licence Act* and its regulations, and ensure that gaming facilities comply with federal reporting requirements targeting money laundering.

In the 2008/09 fiscal year, compliance inspectors completed 2,400 out of 2,800 planned inspections, or about 86%. However, we noted that they did not complete all their required inspection tasks at nine of the 27 gaming premises; tasks completed at these nine sites ranged from 62% to 93% of the total required. Additional details about inspections were not recorded that could indicate whether certain types of inspections, such as evening and weekend visits, were carried out less frequently than planned.

Given that gaming facilities have many significant controls and verification procedures to ensure a very high level of compliance and oversight, the added risk of not completing all visits and inspection tasks might not be significant. Compliance inspectors cited commission staff shortages as the most common reason they did not meet their annual requirements.

Compliance inspectors informed us that operators consistently complied with issues identified in commission corrective action reports. We noted that the appropriate corrective action reports had been completed for the 124 breach reports for 2008/09 and 2009/10, which typically related to minor internal control breaches, such as access to the gaming floor by a minor and violations under the *Liquor Licence Act*. Only seven warning letters were issued over the same period to seven different gaming premises for such things as an operator

failing to ensure that operations were conducted in compliance with the approved security, internal-control-system, floor, or surveillance plans; or an operator allowing employees to play games of chance on gaming premises. Monetary penalties for such infractions were implemented in January 2009 as an additional tool to achieve compliance for an incident where a warning is insufficient and a suspension or revocation of a registration is too severe. As of March 31, 2010, the Commission had issued one such monetary penalty to a casino operator.

Risk Assessments

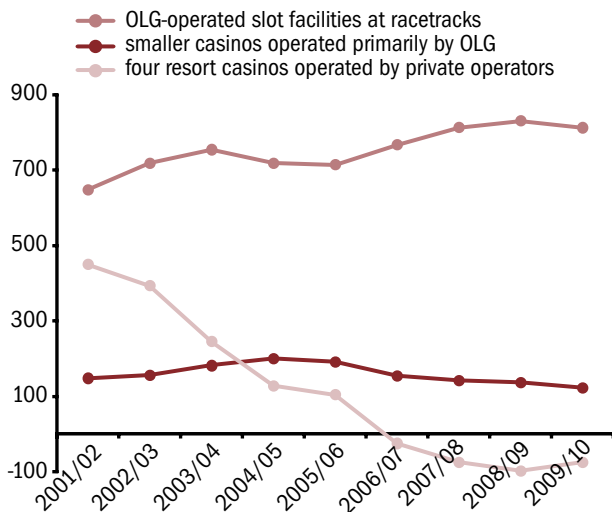
Ontario gaming facilities are under the control of the Ontario Lottery and Gaming Corporation (OLG); however, OLG contracts out the four largest casinos and one smaller casino to private operators. There is little difference in the level of controls the Commission has put in place at casinos operated directly by OLG and those that are privately operated, and all gaming facilities undergo similar inspection and auditing procedures and at the same frequency. Because Ontario's casino gaming industry is about 16 years old, its control systems are mature, and commission inspections generally do not find significant errors. As a result, there may be an opportunity for the Commission to revisit its procedures on an individual basis for each gaming facility by developing a control-risk framework that helps it decide on the level of scrutiny needed for adequate and cost-effective oversight. An assessment of risk should consider:

- previous history of incidents, complaints, and violations;
- recent changes to the casino's operations and management;
- types of games played, wagering limits, and new games introduced recently; and
- profits or losses of each casino.

For instance, Figure 2 indicates that OLG casinos have been consistently profitable over the last eight years, whereas resort casinos' profits have steadily declined. This information could indicate a greater

Figure 2: Profits Generated by Ontario Gaming Facilities Operated by OLG and Private Operators, 2001/02–2008/09 (\$ million)

Source of data: Ontario Lottery and Gaming Corporation



risk at resort casinos as a result of any cost-cutting measures they introduce to address revenue declines, and the impact of these decisions on their ability to meet stringent operational requirements necessary under their approvals.

The Commission's risk assessments were not sufficiently comprehensive to focus its resources more on gaming facilities that have higher risk factors and allow less monitoring of other gaming facilities. This would affect decisions such as whether all operations of casinos are to be reviewed annually, whether commission compliance inspectors are stationed at casinos full-time or part-time, and whether OPP personnel need to be stationed at certain casinos full-time. Lower-risk gaming facilities would also benefit from fewer regulatory procedures.

Ontario is one of the few jurisdictions in North America that maintains an on-site police presence at gaming facilities. For resort casinos, OPP presence is maintained 24 hours a day, 7 days a week. In the 2008/09 fiscal year, the OPP dealt with almost 6,000 incidents at casinos and slot facilities, but only 29 criminal charges were laid at gaming premises. Cheating at play has been relatively rare in Ontario facilities. Other crimes committed at

casinos, such as assault and petty theft, are turned over to the local police by the OPP, and suspicious money transactions from criminal activity or potentially for financing terrorist activity are investigated federally. We were informed by casino security staff that they can deal with most incidents, such as assaults and petty thefts, and local police can be called in if needed.

Both OLG and private operators have raised concerns regarding the extent of regulatory requirements in Ontario compared to other jurisdictions. As illustrated in Figure 2, profits generated by the four large resort casinos have declined significantly in recent years. In November 2008, the Commission created a Centre of Gaming Excellence that is responsible for researching, developing, and supporting the implementation of regulatory best practices. A new Regulatory Review Committee was established in November 2009 to provide a forum for resort casino operators, OLG, and the Commission to discuss casino industry issues, escalate key areas of concern, and provide advice to the Commission on existing and proposed policies and regulations.

RECOMMENDATION 2

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

COMMISSION RESPONSE

The Commission will continue to use a risk-based approach to conducting casino audit and compliance activities. This risk-based approach coupled with the Commission's current gaming modernization initiative are designed to achieve a balance between enhancing regulatory efficiency and effectiveness while addressing the operational and business-flexibility needs of the industry.

GAMING SUPPLIER AND EMPLOYEE REGISTRATION

The Act requires that suppliers of goods and services, trade unions, and certain employees at gaming facilities be registered with the Commission and have their registrations renewed every four years. Suppliers are differentiated as “gaming related” and “non-gaming related.” Gaming-related suppliers include operators of casinos under contract to OLG and businesses that manufacture, provide, install, maintain, or repair gaming equipment, surveillance equipment, or gaming management systems. Non-gaming-related suppliers provide to gaming premises goods and services that are not directly related to gaming, such as construction, furnishings, repair, or maintenance. A more in-depth investigation and registration process is undertaken with the 43 gaming-related suppliers than with the over 2,400 non-gaming-related suppliers, owing to the higher degree of risk with the former to the gaming operations.

A regulation of the Act establishes two categories of gaming assistants: “gaming key employees” and “gaming employees.” Gaming key employees are those individuals who exercise significant decision-making authority over the operations of the gaming premises, such as credit managers, cashier supervisors, and table game managers. Gaming employees are those employed in the operation of a casino whose regular duties require access to any areas

of the premises used for gaming-related purposes (such as dealers, security personnel, and cashiers) but who do not supervise other employees. As of March 31, 2010, there were approximately 2,800 gaming key employees and 12,900 gaming employees in positions that required they be registered with the Commission.

Depending on the position applied for, the Commission's registration process includes a criminal background assessment and may also include a financial assessment of the applicant by commission staff and an investigation by OPP staff assigned to the Commission. The Commission maintains memoranda of understanding with 33 jurisdictions in North America to share investigative information for the purpose of assessing gaming registration applications. The Commission charges fees for initial registrations and registration renewals; in the 2009/10 fiscal year, it collected approximately \$5.5 million.

We noted that satisfactory procedures were in place and used by gaming registration officers for approving new registrations. With respect to registration renewals, we found some incidents that indicated certain procedures could be improved:

- Gaming-related suppliers are normally granted what are known as “deemed renewals” when there are delays in the renewal process, which are often due to the complexity of a case or deficiencies in the application. Based on a sample of renewals, we noted 12 instances where such suppliers continued to be deemed renewed even though more than a year had passed since the registration renewal date. At the time of our audit, one renewal was still not completed 34 months after the renewal date; this included 14 months to gather information from the registrant, followed by 20 months of ongoing investigation. In a similar case, the deemed renewal was ongoing for 27 months. The Commission has set no maximum time period during which deemed renewals are allowed.

- In two instances, we found that detailed investigations were not carried out on corporate directors employed by gaming-related suppliers, even though the Commission's policy manual requires such investigations. In one case, a director was also a significant shareholder.
- The Commission has not established a policy for gaming registration officers to follow when gaming employees may be in conflict-of-interest situations. Instead, the Commission relies on OLG and private operators to determine what constitutes a conflict of interest and how to deal with such situations. We noted some situations where employees who were related to one another worked at the same gaming facility. This was not flagged for follow-up with the casino during the individuals' registration and renewal, to ensure that the situations were handled properly.

We were informed that delays and backlogs in registrations and renewals were caused by staff shortages and high volumes. In addition, we noted that the Commission's registration information system captured data on registrants' key information, including renewal requirements, but did not track the progress of the registration and renewal process, such as the date of receipt of the application, date when all necessary information is received, date an investigation is requested, and date completed. We understand that this information is either informally tracked by the gaming registration officers or recorded in the information system as notes, although neither of these two methods can be used for producing management reports on the status and timeliness of the completion of registrations or renewals on a monthly, quarterly, or annual basis.

At the time of our audit, the Commission was aware of backlogs in registrations and renewals, as well as the limitations of its registration information system, and was in the process of reviewing and redesigning its registration process to strengthen and streamline procedures.

We were informed that complaints about and sanctions imposed on suppliers are rare, and that no notices of proposed revocations or suspensions have been issued within the past three years. Concerns involving gaming assistants were also infrequent. For instance, during the 2009 calendar year, the Commission identified and investigated registration issues with one gaming key employee and 51 gaming employees and applicants.

RECOMMENDATION 3

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

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

COMMISSION RESPONSE

The Commission intends to continue its implementation of a risk-based approach to its registration function, and will assess appropriate benchmarks for this activity that also ensure the Commission's legislative responsibilities are being met.

The Commission will consult with the Ontario Lottery and Gaming Corporation and other stakeholders on how best to manage real or perceived conflicts of interest.

SELF-EXCLUSION PROGRAM

To address social risks inherent in casino gaming, the Act and its regulations restrict from gaming facilities persons who are under 19 years of age or

who appear intoxicated, and gambling in gaming facilities by employees of the Commission, OLG, private operators, and gaming employees' trade unions. The Commission ensures that casinos have proper security for restricting these individuals from gambling.

Another significant social risk is that of gambling by players who may have a problem with or an addiction to gambling. A regulation under the Act states that the Commission can require an operator to implement and comply with a process approved by the Commission's board of directors for identifying players who may have a problem with or an addiction to gambling and a process for players to exclude themselves from playing games of chance. We noted that the Commission's board of directors had not approved a self-exclusion policy or program, but that programs were in place at gaming facilities to identify self-excluded persons.

The Commission's security and surveillance approvals all require that gaming facilities put in place controls, such as stationing security personnel at entrances, that restrict access to the casino by excluded persons. In addition, all gaming facilities had a self-exclusion program, and OLG operated a database of about 14,000 persons who had notified OLG of their desire to exclude themselves from the gaming facilities. At the OLG and private-operator gaming facilities we visited, we observed that security measures to identify self-excluded persons who attempt to enter the facilities were generally consistent. All gaming facilities used electronic measures that would alert security staff if self-excluded persons used their player cards. OLG informed us that it detects in gaming facilities every year about 1,000 self-excluded persons, who are evicted and may be charged with trespassing and have any large winnings forfeited. During our audit, OLG was also in the process of testing facial-recognition technology to help identify registered self-excluded persons.

Although the Commission has not reviewed or audited self-exclusion programs put in place by OLG beyond ensuring that approval requirements are met, its new Centre of Gaming Excellence recently

conducted research on self-exclusion programs in other Canadian and international jurisdictions. In November 2009, the Centre noted that OLG's self-exclusion program is generally consistent with best practices in other jurisdictions. However, the Centre noted that the Commission does not have policies or programs to guide its staff's oversight of OLG or private-operator self-exclusion programs.

RECOMMENDATION 4

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

COMMISSION RESPONSE

The Commission has undertaken a formal consultation process with key stakeholders on a proposal to develop both a policy and a program related to self-exclusion, pursuant to the *Gaming Control Act* regulations. The Board will consider all views on this subject and decide on an appropriate course of action, including the need for periodically reviewing self-exclusion programs at gaming facilities.

PERFORMANCE REPORTING

Although the primary responsibility of the Commission with respect to casino gaming is to ensure that casinos operate fairly, with integrity, and in the public interest, the Commission's annual report and website do not provide meaningful performance information on its success in achieving these objectives. The Commission could demonstrate its regulatory efforts as being comprehensive and effective

by reporting on its activities, including the number and results of its compliance inspections and audit activities, number of gaming equipment inspections and their results, number and types of incidents responded to, enforcement actions over registrants and operators, fines levied, and complaints addressed. As discussed previously, providing information on gaming activities such as minimum and actual payout ratios for slot machines would also increase public confidence in the integrity of gaming facilities. Such information could, for example, include actual return-to-player rates paid from electronic gaming machines and table games and by each gaming facility, and the number of jackpot investigations successfully conducted by the Commission. Our research indicated that other jurisdictions reported such information, although no one jurisdiction provided all of it.

RECOMMENDATION 5

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

COMMISSION RESPONSE

The Commission's current benchmarks and performance measures are published in its annual report and on its website. In order to improve our reporting in this area, the Commission is currently implementing a significant "performance measurement" initiative. This initiative establishes a baseline and benchmark for all rel-

evant sectors under the Commission's mandate, including reporting on commercial gaming.

OTHER MATTER

Internet Gaming

Since 1995, when the first Internet gaming websites were created, there has been a steady increase in their public acceptance and use; some estimates put their annual revenues globally at \$25 billion. No Internet gaming websites originate in Ontario, as far as the Commission and the OPP know, and the Commission does not have a mandate to regulate the use of such sites by Ontarians. There are an estimated 2,000 Internet gaming operators worldwide, but just two or three large operators account for over 50% of all revenues. Unlike the OLG, Internet gaming operators do not pay fees or taxes to Ontario, nor do they share profits from the estimated nearly \$400 million they receive each year from Ontarians using their websites. Unregulated Internet operators are not subject to Ontario legislation that is intended to ensure that gaming is conducted in accordance with the principles of honesty, integrity, and social responsibility. In fact, provision of Internet gaming in Ontario by foreign operators is illegal under the *Criminal Code* and subject to enforcement by the OPP, although enforcement is problematic when dealing with operators that do not reside or operate in North America. As a result, foreign sites continue to operate in Ontario, although as of January 1, 2008, Ontario legislation came into effect that prohibits the advertising of Internet gaming sites, where the advertising originates in Ontario.

We noted that many international jurisdictions have used a variety of approaches to address Internet gaming. These approaches include totally prohibiting Internet gaming by private operators and declaring such operators unlawful; restricting advertising, banking services, and the provision of Internet services for foreign operators; or allowing

Internet gaming but requiring that equipment used be located in their jurisdiction, imposing licensing requirements, and taxing revenues or imposing fees.

In Canada, the approach generally taken has been for governments to establish their own legal Internet gaming sites. British Columbia introduced its own Internet gaming site in August 2010, and Quebec planned to do so in the fall of 2010. In August 2010, Ontario announced that it will also do so in 2012. In operating its own Internet gaming site, Ontario will be competing with large, well-established foreign Internet gaming operators that will continue to offer their services in Ontario without regulation or taxation, and thus with far less overhead. In this respect, it will not be a level playing field, with Ontario clearly at a disadvantage. Nevertheless, Internet gamblers may well be attracted to a government-run site, given the higher level of gaming fairness that such sites would be perceived to have.

RECOMMENDATION 6

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

pay fees or taxes to Ontario, and the recent decision that the Ontario Lottery and Gaming Corporation will offer Internet gaming in 2012, the Commission should:

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

COMMISSION RESPONSE

The Commission would like to thank the Auditor General for his observations about Internet gaming and will undertake to consider these and any other suggestions brought forward as the framework for Internet gaming in Ontario is developed. Although Internet gaming does not currently fall within the Commission's legislated mandate or regulatory authority, the Commission has been proactive in preparing, and will continue to prepare and work to identify, appropriate processes and best practices for regulating existing and emerging gaming activities in this province.