

***Nearing the  
imperfect but  
acceptable  
finish line***



Prime Minister Shinzo Abe has been committed to bring integrated resorts to Japan since the beginning of his term, but now a scandal threatens to end not only the gaming effort, but also his career

By Steve Gallaway, Brendan Bussmann and Kit Szybala

# Home Stretch in **Japan**

**F**or nearly 20 years, Japan has gone through several false starts and iterations in its attempt to legalize integrated resorts. In December 2016, Japan took its first official first step toward legalization with the passing of the IR Promotion Bill. Later this spring, Japan is poised to take the final step in this process with the introduction of two bills that will help solidify the initial act: the IR Implementation Bill and the Basics Bill on Gambling Addiction Countermeasures.

The government of Japan has been contemplating what items to include within these bills in its quest to create an environment that maximizes the potential benefit realized by the country in terms of investment and tourism as well as to attract quality operators to the market.

The decisions made within this process are vital to creating a healthy regulatory environment that both attracts operators and ensures a positive impact to the nation. However, certain aspects of regulation can prevent the ideal marketplace from coming to fruition.

As the Japanese Diet enters the tail end of its 2018 ordinary session, the Liberal Democratic Party (LDP) and the Komeito will continue to negotiate the terms and outline of both bills. As the end of the session draws nearer, stakeholders will have a clearer picture of how this new, valuable market's regulatory model will take shape.

However, as the current session is set to end on June 20, it does not provide ample time for the creation and passage of the bill, particularly when the Japanese Diet would like to pass the Basics Bill on Gambling Addiction Countermeasures before the IR Implementation Bill. As the process continues to unfold, several key aspects of the bills have been revealed.

At the beginning of April, after two months of deliberations, the LDP and the Komeito came to terms on key points that are expected to be in-

cluded within the framework of the IR Implementation Bill. These key points include a tax on gross gaming revenue, entrance levy, visitation restrictions, and gaming floor space limitations.

When regulatory limitations such as entrance levies, gaming tax rates and floor size are imposed, the bidders must reevaluate how the legal and regulatory environment would impact the feasibility of their proposed projects and reshape what they can offer to the government and people of Japan.

## **Number of Locations**

The number of locations allowed within the bill was one of the last items to be agreed upon between the LDP and the Komeito. Initially, the Komeito Party desired only two to three locations. However, the LDP sought as many as six locations.

As outlined in Global Market Advisors' (GMA) white paper "Japan: Integrated Resorts" from May 2017, the Japanese market can easily support anywhere from four to six locations. However, it was stressed at that time that the government of Japan should consider allowing multiple licenses at specific locations to meet its tourism goals. Specifically, this process could be employed in Osaka, creating the Osaka Strip.

In Osaka, the size and scope of the site require significant infrastructure improvements as well as encompassing more land than the resorts on Cotai. By allowing two or three operators to participate in the market, the operators could accommodate these necessary development costs while creating a premiere tourist destination.

After much debate, the ruling coalition decided upon three host locations. The current leading contenders vying for these locations include (in no particular order) Osaka (Osaka Prefecture), Yokohama (Kanagawa Prefec-

ture), Sasebo (Nagasaki Prefecture) and Tomakomai (Hokkaido Prefecture). However, over 25 prefectural governments have expressed interest in participating in this process.

## Tax Rate

Throughout the debate, it has been clear that the Japanese Diet is relying on the Singapore framework as a model for regulation. Given the success that Singapore has realized from IR development, this is a sound approach. As such, it appeared that Japan was going to pass a rational tax rate of 15 percent on gaming.

Recently, it became clear that discussions had changed and the LDP is leaning towards implementing a 30 percent tax rate, which is higher than tax rates in most leading jurisdictions. While IR development would still be feasible at this tax rate, operators are likely evaluating previously proposed levels of investment.

Specifically, an increased tax rate impacts an operator's ability to develop a product that is highly attractive to tourists. As the expected level of profit is lowered, operators must adjust development costs to meet return thresholds.

The first components of development that are reduced include the size and scope of non-gaming amenities (e.g., hotel rooms, food and beverage outlets, retail space, etc.), including the quality level, and aspects of the design and architecture. These items have a direct impact on potential gaming revenue, especially the ability to attract international operators. With the reduction of these components, it will be harder for the government to meet its tourism goals and we'll see an overall reduced economic impact from IR development.

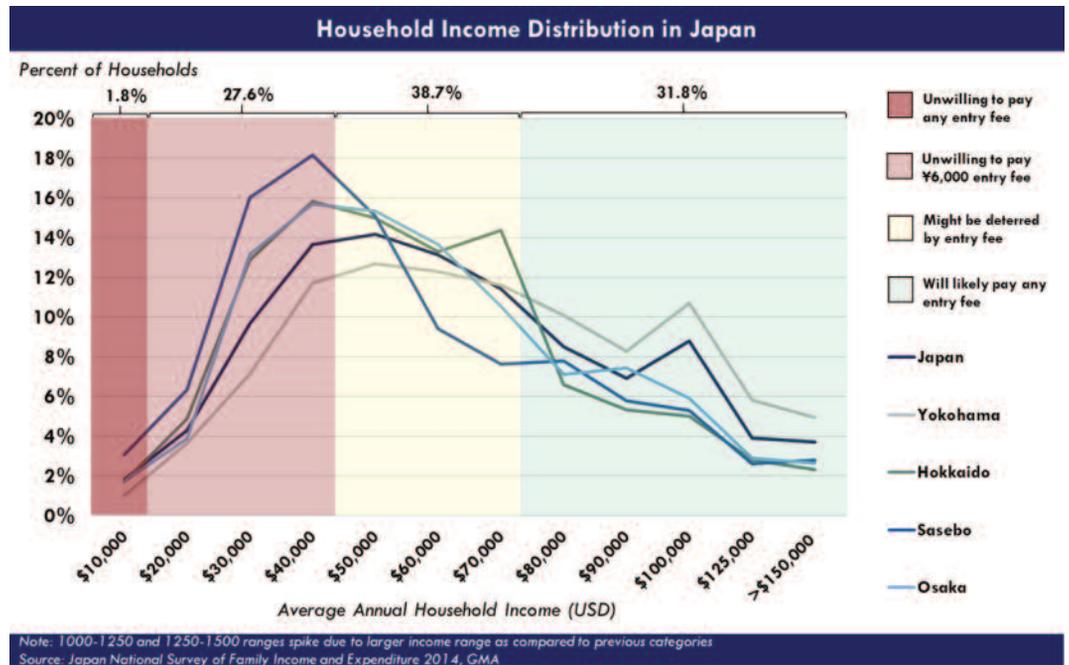
## Entry Levy, Visitation Restrictions

Singapore was one of the first jurisdictions to introduce a casino levy for locals. Regulators in Singapore set a fee of SGD100 (equivalent to US\$76 or JPY¥8,000). Recent announcements indicate that the LDP will likely use this aspect of the Singapore model as well. This issue was heavily debated between the LDP and Komeito, with the LDP pushing for a JPY¥2,000 levy and the Komeito lobbying for a levy closer to the Singaporean level.

After negotiation, the parties agreed to a compromise and proposed an entry levy of JPY¥6,000 (USD \$56), which is higher as a percentage of GDP than the levy imposed in Singapore. Additionally, the Japanese entry levy, as with the Singapore levy, is only applicable to local market patrons, thus allowing foreigner access to the gaming area free of the tax.

Alongside this provision, visitation restrictions will be put into place that limit the amount of times that a local market patron can visit a casino within a given time period. Specifically, the proposed restrictions would prohibit local patrons from visiting a casino more than three times a week with a maximum of 10 visits per month. This will be tracked through an ID card system, or the "my number" card as it is known in Japan. These visitation restrictions also do not apply to foreigners.

While the actual regulations governing these measures still need to be written, the entrance to gaming floors in Japan will likely resemble those at Marina



Bay Sands and Resorts World Sentosa in Singapore. However, it may be difficult to use the "my number" system, as most Japanese do not carry this new ID.

This entry levy is expected to impact gaming revenue to a large degree, as the percentage of the population that would have the means to frequent the casino would shrink considerably. While some suggest that entry levies help curb problem gaming, there has been no conclusive research conducted to support that hypothesis. Simply put, the entry levy is nothing more than an additional tax that encourages lower-value patrons to gamble in unregulated markets like pachinko parlors.

The entry levy, which is suggested to help curb problem gaming, would instead make it more difficult to prevent problem gaming.

The IRs will have internationally accepted problem gaming programs in place that have been proven to address incidence of problem gaming among a population. The entry levy will likely result in fewer problem gamblers being identified by the operators, and could result in gamers spending more than they can afford to gamble in an attempt to gain back their sunken dollars spent on entering the facilities.

From a revenue standpoint, the tripling of the proposed entry levy from JPY¥2,000 to JPY¥6,000 will reduce the percentage of the local population that has the means to gamble by about 27.5 percent in the wealthier regions, to nearly 40 percent in less affluent regions, such as Hokkaido. This reduction is a result of an entry fee simply too high in relationship to the amount of money a given gamer may be willing to risk in a given day.

Given the JPY¥6,000 entry levy, GMA estimates that 32 percent of adults would not be impacted by the existence of an entry levy in deciding whether or not to visit the casino, 39 percent would be influenced by the levy, and the remaining 29 percent would likely be unwilling to pay the levy as they simply cannot afford it. Those who are influenced negatively by the levy but still choose to gamble will likely visit the local pachinko parlors.

## Casino Sizing Limitations

The government of Japan wishes to limit the size of the casino gaming floor. This provision was also borrowed from Singapore, as the facilities in that market have regulatory guidelines that limit them to 15,000 square meters

of gaming space. In Japan, the ruling coalition has decided that the casino gaming floor cannot exceed 3 percent of the total facility size.

As the casino gaming floor is the engine that supports non-gaming amenities within an IR and allows operators to develop facilities with iconic design, this limitation could certainly impact the bids received by certain host markets. For example, given the comparatively low incomes in Hokkaido, some developers may find that there is not enough profit to build out the remaining 97 percent of the development, and will choose to not submit a proposal if a formal RFP is issued.

## Responsible Gaming Considerations

Meanwhile, the Japanese Diet is still contemplating the Basics Bill on Gambling Addiction Countermeasures and what responsible gaming measures it will set into place. This bill will allow for the creation of a non-government organization similar in nature to the National Council on Problem Gambling in Singapore. This council addresses all forms of gaming in Singapore, including Toto, 4D and Sweep as well as casino gaming.

Today, gaming already exists within Japan in the form of pachinko and other forms of gambling. So far, Japan has modeled its system off the same social safeguards that Singapore implemented. However, it will be important that the employed regulatory items address all forms of gaming, including pachinko.

Strong operators have already drafted effective responsible gaming programs and have started to educate and implement resources in Japan to assist the small percentage of the population that may develop a problem with gaming. The Japanese Diet should look at the scientific research model, as well as the models employed by qualified operators and regulators globally, to develop the ideal framework for addressing responsible gaming.

## Looking Forward

The current political climate in Japan has made the timeline of IR implementation uncertain, as the Prime Minister's office combats several issues regarding public opinion and the Japanese Diet deals with the PM office's heavy legislative agenda.

The political situation for Prime Minister Shinzo Abe is one that has been very tremulous over the last several months. The overall approval of Abe and the cabinet has dipped considerably since the start of 2018, with ratings dropping to levels in the low 30 percent range in March and rebounding to the low 40 percent range in April. These fluctuations are likely tied to the several scandals that continue to surround Abe and his cabinet. One major scandal involves the state's approval of land sales for a school operated by Morimoto Gakuen in Osaka.

Other notable scandals include the approval of a veterinary school, which showed the potential for favoritism toward Kake Gakuen, which is chaired by Kotaro Kake, one of Abe's closest friends; and the controversy regarding the ministry's civilian control over the Self Defense Force (SDF).

Abe has several items on the agenda that he would like to address before the June 20 end of the ordinary session. The controversy surrounding the gaming measures may force the IR issue to take a back seat during the ordinary session. Instead, the bills could be addressed in an extra ordinary session later this summer/fall or further into 2019. Additionally, the PM's office will face a party election in the fall that could play a role in the timeline of IR-related events.



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Assuming that no major roadblocks occur due to shifting political dynamics, the timeline of IR development in Japan is largely contingent upon the passage of the IR Implementation Bill and Basics Bill on Gambling Addiction Countermeasures. Once those two bills have been passed through the Diet, the timeline becomes much more prescribed in nature. Following each bill's passage, several items will begin to unfold: a casino control commission will be formed, additional regulations will be set, an RFP process will be outlined for operators and prefectures, an NGO will be created to handle responsible gaming issues, operators will be selected, design and construction of IRs will begin, and the first IR will open its doors.

Japan offers the opportunity to create the world's next destination for premiere integrated resorts. The opportunity still exists for Japan to set a reasonable stan-

dard that balances its desire to expand its tourist base to reach the goal of 60 million visitors, up 20 million visitors from its 2020 goal spurred in part by hosting the Summer Olympics.

However, the market needs to be framed appropriately in two ways—the first allowing the partnership to occur between the government and the groups formed between operators and the consortium. It must also balance the size difference between urban facilities and more remote, regional facilities. A one-size-fits-all approach does not work because of the difference in GDP within regions as well as what each market can support.

There is still a significant path to overcome with the passage of two significant pieces of legislation and the regulatory framework that must follow. However, Japan has the opportunity at hand to address concerns across all forms of gaming while investing in additional tourism to the country. If crafted appropriately, the race for integrated resorts in Japan will allow operators to invest billions of dollars to create iconic venues that will be models for locals and visitors to appreciate.

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