

MinterEllison

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BY EMAIL

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Dear Josh

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We have had a further meeting with, and received a further report from, Hakluyt in relation to Malaysia.

Hakluyt's conclusions

1. Hakluyt's conclusions are:
 - *'The election of the Mahathir government has not worsened the regulatory environment for foreign IRs [integrated resorts]. Indeed, the situation is arguably more stable than before the election.*
 - *Provided strong operating procedures are in place to avoid contravening the unwritten rules, there appears little in the way of obstacles to you returning to VIP marketing in Malaysia, although a local presence supplemented by visiting executives may be preferable to establishing a physical office'*

Basis

2. In summary, the basis for Hakluyt's conclusions is as follows:

'Little change in regulation or enforcement so far under Mahathir...

Since Malaysian Prime Minister Mahathir Mohamad's election victory last year, there have been only minor changes to the country's regulatory framework governing gambling. These relate to lotteries and the issuing of sports betting licences.

There have been no changes to the regulatory or administrative approaches to the marketing of integrated resorts (IR) by domestic or foreign operators - and none are considered likely.

...and the government appears disinclined to make significant reforms

The government appears disinclined to make significant reforms to the regulatory environment. This is in part because of a reluctance to discuss issues such as gambling, alcohol and pork unless forced to: gambling is not something bumiputra (ethnic Malays) could profit from. Another reason may be Mahathir's long-standing closeness to Genting and the founding Lim family.

Tax rises show the government's reliance on Genting and gambling more widely



The 2019 budget, the new government's first, imposed substantial revenue increases on the casino sector, in the form of higher casino licence fees, turnover taxes and gaming machine licence fees.

Genting is known to have deep pockets and is able to meet this increased financial burden comfortably. However, the significant role played by Genting and the gambling sector more broadly – in the economy and its contribution to Malaysia's public finances only add to the government's preference to avoid the introduction of punitive regulation and, for that matter, public discussion of new marketing curbs. As such, it is unlikely that tighter rules will be introduced on top of the revenue measures – for either Genting or foreign operators.

The politics surrounding gambling, however, remain sensitive...

Nevertheless, the politics surrounding gambling remain highly sensitive, especially given the prominence of concerns about public morality detailed in our last report. And the presence of conservative parties in the governing coalition may increase pressure on the government to respond to public concern as it arises. Mahathir will therefore need to balance the need for revenue from the sector against better represented public antipathy to gambling.

...and issues of Muslim morality could yet become a catalyst for punitive action

It is important, too, not to lose sight of the risk that issues of Muslim morality can swiftly become a source of embarrassment - and economic loss - for hospitality companies, as well as a possible catalyst for punitive government action. If anything, this risk may have increased since the election. And it applies not just to gambling and curbs on promotional activity surrounding it, but also, for example, to cuisine.

In this context, several of our sources cautioned of the potential for knee-jerk reactions by the government should particular industry transgressions suffer an extended public airing.

While specific moves to regulate foreign operators are unlikely...

We heard nothing to suggest that a change in the government's attitude to foreign operators is on the cards, despite the fact that they contribute little, if anything, to public revenues through taxes and licence fees.

...it is advisable to abide by the "unwritten rules" around casino promotion

Still, given the delicate political and fiscal situation facing the government, it is advisable to abide by the "unwritten rules" around casino promotion. Additional emphasis should be placed on ensuring that marketing efforts are discreet and avoid doing anything that could be interpreted as targeting Muslim Malaysians. It is important, too, to exercise caution on the direct promotion of gambling.

Setting up a local operation remains viable...

Despite growing religious conservatism, the balance of our reporting indicates that setting up, or returning to, IR marketing in Malaysia is no less viable under the current government than before, subject to certain caveats. Conducted with due skill, planning and discretion, private marketing using local representatives and executives who fly in and out of the country poses no particular risk.

...although the current environment is not conducive to a physical office

In our June 2018 report we pointed to only low levels of concern in relation to a physical marketing office in Malaysia. Our most recent reporting suggests a subtle shift under the PH government that makes such a presence - as opposed to a more informal local operation supported by travelling executives - less advisable."

Commentary

3. Hakluyt's commentary on the above matters and the general environment in Malaysia is as follows:

'No indication that the Mahathir government is to change gambling regime

The Pakatan Harapan (PH) government under Prime Minister Mahathir Mohamad is now firmly established following its election victory in May last year. While the coalition administration depends on the support of more conservative parties (including the Islamist Parti Amanah Negara), there has so far been no indication that changes either to the regulatory regime for gambling or rules on enforcement are planned.

The same applies to the promotion of foreign integrated resorts (IPs) in Malaysia. A gaming consultant in Singapore, who has been following recent developments closely, commented: "The new PH government under Mahathir, despite its claims of being more socially conservative, is likely to continue the hands-off approach to foreign IR marketers, so long as they follow the unwritten rules [which we discussed in our June 2018 report]."

A director of Genting Malaysia, similarly, noted: "The new government's outlook on gambling appears largely unchanged from that of the previous administration. The same is true of IR marketing, which to be fair is a relatively new activity in this country. Resorts World [Genting], for its part, has suffered no enforcement setbacks under the new government. Indeed, no attention of any kind has been paid to our marketing, at least not that we've detected. "

And a Genting Malaysia manager confirmed: "There is generally no change to the official position on the regulation of casinos or IRs under the new government." The same appears true of enforcement. "Thus far, no local or foreign IR group has been hauled up for operating here. Nor have their advertisements faced a backlash of any kind. And, as far as I can tell, there's no sign that this situation is about to change. "

It does not want to take action unless forced to by circumstances...

Several sources offered explanations for why the government is unlikely to take a tougher stance towards IR marketing.

A Malaysian political analyst who follows industry regulation closely made this representative observation: "Gambling in its entirety - whether casinos, 4D number forecast operators [a state-licensed lottery] or lotteries - are of little or no interest to this government or politicians. It is not something bumiputra [ethnic Malays] could profit from, hence the lack of interest from the government or bumiputra business interests in the sector. Issues such as gambling, alcohol and pork are not things anyone in the government is interested in discussing unless they're forced to by circumstances. "

A successful author in Kuala Lumpur, who has studied the Malaysian casino industry, said that Mahathir's closeness to Genting and its founding Lim family is another reason why the new government is avoiding IR regulation: "Mahathir is probably the most pragmatic, if authoritarian, prime minister Malaysia has ever had. He is no different now than he was during his first tenure. And he's also known the Lim family for decades: his original relationship with Genting founder Lim Goh Tong dates back to before his first term as prime minister began in 1981. He has known Lim Kok Thay since he was a young adult, too, before he took the reins from his father."

He added: "Mahathir understands the economic and racial dynamic involved with Genting as much as anyone in Malaysian politics, and is far too savvy to put any policy in place that could in any way rebound on Genting Group, even peripherally. "

...though some token restrictions have been put in place

Notwithstanding the government's apparent disinterest, gambling remains frowned-upon in Malaysia and has been subject to minor, additional regulatory restrictions.

According to an official at the Malaysian Ministry of Tourism Arts and Culture (MOTAC): "Apart from increased taxation [see below], the government has said it plans to reduce the number of special draws for 4D number forecast operators in 2019. This reduction is aimed at tackling gambling addiction in the middle and working classes.

"In addition, Finance Minister Lim Guan Eng has reiterated that there are no plans to reissue a sports betting licence to Vincent Tan's Ascot Sports Sdn Bhd [a prominent sports betting house operating under government licence] or any other operator. "

The government has raised taxes on casinos...

The 2019 budget, the new government's first, imposed substantial revenue increases on the casino sector, in the form of higher casino licence fees, turnover taxes and gaming machine licence fees.

The Genting Malaysia director underlined the industry's significance as a source of tax revenue: "The only change in the new government's thinking on gambling has been to increase taxation on casino and slot machine licensing, in order to increase revenue streams. Given the debt situation, gambling has become more important to this government than others before it."

A retired Malaysian CFO echoed this, observing somewhat dryly that the industry's contribution to Malaysia's public finances made it unlikely that the government would want to introduce much tougher regulation. The increase in casino taxation has exposed the government's reliance on this revenue. It seems more invested in the health of the sector than ever."

...and Genting is of national significance in revenue terms

The author with knowledge of the industry suggested that overly zealous enforcement of existing regulation was unlikely for the same reason: "Gaming, particularly Genting Resorts Malaysia, is an important part of the economy. The fear is that an attack on the sector- including foreign IR operators' marketing - could ricochet into Genting's casino licence approval and damage the whole country."

He added that the scale of Genting's financial contribution and its role in the economy should not be underestimated. "It [Genting] is riddled with ethnic Malay commercial interests. It is important to tourism and brings in more revenue than any other domestic company. It has the largest cash reserves of any domestic business, and pays all kinds of money out to vested interests, political parties and charities."

"Genting is also one of Malaysia's very few global brands, with highly successful operations overseas. Doing anything that could eventually result in a challenge to the legitimacy of Genting's licence would have profound economic consequences. Its interests are synonymous with those of the country and not to be trifled with."

Muslim sensitivities remain paramount...

Nevertheless, the politics surrounding gambling remain highly sensitive, especially given the prominence of concerns about public morality detailed in our last report. This is likely to be a further reason for not drawing attention to - and promoting - the industry.

The Genting Malaysia director again: "While the government relies on revenue brought in by taxation on gambling, it remains cautious about being seen to promote gambling because of the sensitivities of the Muslim community. The new government didn't win the election with huge support from Malay Muslims and is wary about upsetting them. So, although it would like to encourage gambling and extract more revenue, this desire is offset by the need to placate the Muslims who wish to reduce, or even eliminate, such activity."

...and could yet be a catalyst for punitive government action

Indeed, it is important not to lose sight of the risk that issues of Muslim morality can swiftly become a source of embarrassment - and economic loss - for hospitality companies, as well as a possible catalyst for punitive government action.

If anything, this risk may have increased since the election. And it applies not just to gambling and curbs on promotional activity surrounding it, but also, for example, to cuisine.

The Genting Malaysia director noted: "IR operators who wish to conduct local, mass marketing have to pay attention to more than simply ensuring that they don't promote gambling. They now have to be careful about prominently promoting food that contains pork. The Muslim majority can take offence at this sort of promotion."

This anecdote about Muslim sensitivities, relayed by the Malaysian political analyst, was illustrative: “Recently, Malaysia Airlines came under fire for apparently promoting pork in their in-flight magazine. The company issued an apology, despite it turning out to be beef.”

The airline, he added, has also since announced that the word “pork” will no longer appear in its magazine.

“Any transgressions that promote gambling will not escape the watchdogs”

In this context, several of our sources cautioned of the potential for knee-jerk reactions by the government should particular transgressions by the industry suffer an extended public airing. As the Malaysian political analyst put it: “The government is usually reactive to issues, they get caught on the back foot. But first there has to be something that causes a stir in the public, often starting in the media and spreading to the internet. The government itself doesn’t promote the conflagration; it simply reacts to it. That’s how the entire government operates: reactionary and in the moment.”

The Genting Malaysia director observed: “Activities that are not considered compatible with Islam in Malaysia are well monitored by the numerous Muslim NGOs and Muslim people in general. One can be sure that any marketing transgressions that promote gambling will not escape the watchdogs and will be widely reported.”

The author with knowledge of the industry agreed: “No one in the current coalition wants to draw any attention to gaming that could unsettle the status quo. However, a sudden, publicised focus on high-roller marketing by foreign IRs could stir up the ethnic-Malay rural base, which is conservative and genuinely believes that gambling in any form is a sin. If Malay media ever decided to make an issue about foreign IR marketing, it could expand to the blogosphere and mushroom into a political issue.”

Finally, we turn to issues specific to the foreign IR industry undertaking marketing in Malaysia.

Specific moves against foreign marketing operators are thought unlikely

We heard nothing to suggest that a change in the government’s attitude to foreign operators is on the cards, despite the fact that they contribute little, if anything, to public revenues through taxes and licence fees. This comment from the Genting Malaysia director was typical: “There is no distinction between local and foreign IR marketing. This is best exemplified by Resorts World [Genting], whose marketing usually emphasises the local resort in Genting Highlands, but will also include promotion for Sentosa [Genting casino in Singapore]. There’s no dividing line between local and foreign operators that we’ve encountered.”

The managing director of a Malaysian hotel chain confirmed: “There are no restrictions on foreigners marketing tourism and IR in Malaysia except that the promotion must not be seen to promote gambling and vice. Promoting entertainment, leisure, sports and cuisine are the usual themes and the government does not draw a distinction between local and foreign IR operators.”

Other contacts suggested that any attempt by the government to make a distinction between local and foreign marketing - whether mass or VIP - could result in unwelcome internal scrutiny from conservative politicians.

The political analyst explained: “The government is not going to make much of an effort to distinguish between foreign and local operators in order to avoid any accusations of promoting gambling. Even drawing up rules and properly regulating what is a mostly unregulated sector would be painted by mischievous politicians on the fringe as the government promoting the sector. The government would prefer to let this sleeping dog lie.”

Vigilance over the “unwritten rules” is more important than ever

Still, given the delicate political and fiscal situation facing the government, it is advisable to abide by the “unwritten rules” around casino promotion. Additional emphasis should be placed on ensuring that marketing efforts are discreet and avoid doing anything that could be interpreted as targeting Muslim Malaysians. It is important, too, to exercise caution on the direct promotion of gambling.

The political analyst summarised the current situation succinctly: “The most important thing is not to make a public show of marketing. If you keep it quiet, and provided all laws are followed, appropriate licences acquired, taxes paid and work permits sought, it will be treated much like any other business. The authorities are unlikely to pay much attention. ”

The Genting director also cautioned on marketing to non-Muslims and gambling promotion: “Foreign IRs shouldn’t come to the conclusion that there is no risk. High-roller marketing to non-ethnic Malays must continue to be undertaken cautiously, and the casino component of foreign IRs should not be referred to directly. This is no time to push the envelope. ”

Other sources likewise noted that a discreet approach to VIP marketing is more important under the new administration.

Said the Singapore gaming consultant: “The MOF’s [Ministry of Finance] legal division will not act against foreign and domestic IR operations so long as they keep a low profile and abide by the informal understanding that only ethnic Chinese and other non-bumiputra groups are targeted. Nothing has changed in that regard other than a heightened importance. Visiting, foreign IR marketing executives obviously need to exercise discretion and closely follow the guidance of their local representatives. Openly discussing VIP gaming with potential Malay Muslims is a risk that shouldn’t be taken.”

And a senior Genting executive who has worked directly with the Lim family for several decades said: “Everybody knows that foreign IRs are marketing here through local reps, with occasional visits from marketing executives from the property itself. But these meetings are kept low profile, generally occurring in people’s homes or Chinese restaurants and other establishments that Malays tend not to patronise.

“In this way, the marketing is segmented and discreet and will continue to work well under the PH government. ”

Setting up local operations remains viable...

The balance of our reporting indicated that setting up, or returning to, IR marketing in Malaysia is no less viable under the current government than before - albeit with the cautions and caveats detailed above.

The managing director of the Malaysian hotel chain had no legal or regulatory concerns: “Foreign representatives have always visited Malaysia to promote industry and trade. There is nothing to stop them from coming to Malaysia to promote an IR, either to the mass market or selectively to people they have targeted. They are allowed to stay as long as they don’t break the law.”

The Genting director elaborated: “A foreign IR can easily set up a marketing operation as long as this unit is not engaged in trading, business or any form of commercial activity. Its entire operations must be funded by the parent company and it must not derive any income locally. ”

There remains no formal body for the regulation of foreign IR marketing, and thus no bureaucratic structures through which marketing activities can be formalised.

The political analyst commented: “There is no formal pathway to setting up a marketing operation in Malaysia as there is no regulator to approach. There is no gaming commission or anything close to its equivalent. Most of the laws passed in parliament regarding gambling are from decades gone past, from both a simpler time and a more liberal era. Evolution of the laws and regulations for gambling to keep up with the times has been limited in Malaysia, and the current government has had little interest in discussing anything to do with gambling in any official setting.”

It should be stressed, however, that the lack of a formal framework for such marketing activity does not reduce the need to behave discreetly. Said the Genting manager: “There are no laws governing this [marketing] specifically. But it will gather adverse attention if it comes to the public’s attention, and that is in nobody’s interest. ”

...but seeking a physical presence is now less advisable

In our June 2018 report we pointed to only low levels of concern in relation to a physical marketing office in Malaysia. Our most recent reporting suggests a subtle shift under the PH government that makes such a presence - as opposed to a more informal local operation supported by executives flying in and out - less advisable.

The gaming consultant, for example, cautioned: I'd be nervous about setting up a formal office for IP's non-gaming activities. It makes little sense to expose yourself in this way after a change of government, particularly given the change was brought about by concerns over corruption and rectitude. If the Malaysian media got wind of an application, let alone the approval of an application, and made an issue of it, the story could move online, stirring up rural Malays. The government would likely be forced to put the fire out rapidly. In the current political environment, it is in no one's interest for a foreign IR to bring attention to themselves by trying to open an office."

The senior Genting executive who works for the Lim family agreed: "I don't think [the Prime Minister's Office] would appreciate the matter being brought to its attention and might well deny the application, which would increase the exposure of the IP's marketing network. It's just a bad idea. The current government doesn't want to be put in a position where it must look at the foreign IR marketing issue. So long as IPs quietly focus on Chinese and foreign residents there won't be a problem. "

Monitoring

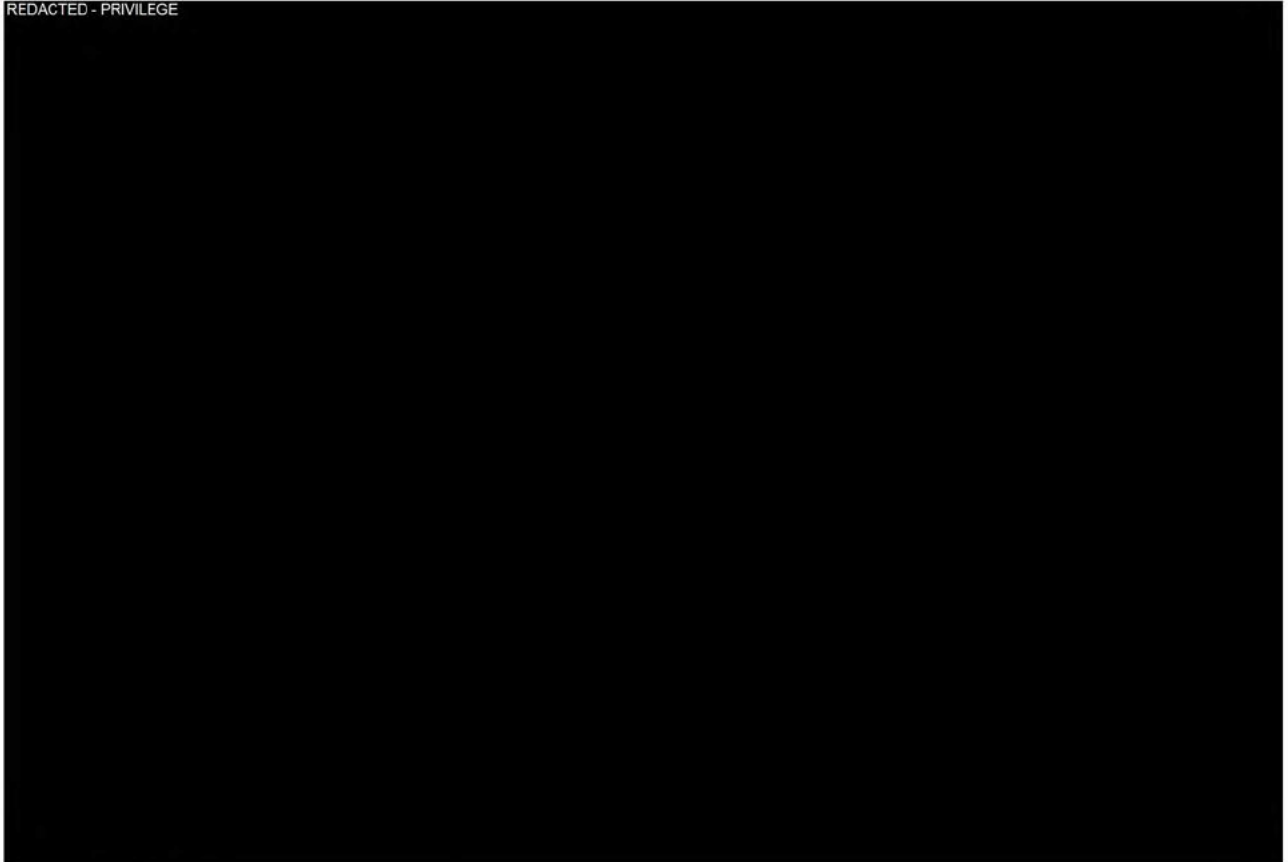
4. One further point of significance which emerged from our meeting with Hakluyt is that, unlike China, it is unusual in Malaysia for there to be a major shift in enforcement priorities, or targeted enforcement action, without some forewarning. Hakluyt suggested quarterly monitoring, at least for this calendar year, to stay abreast of any evolution of the risk of action being taken against any foreign casino or local staff.

Malaysian law advice

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Yours faithfully
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