



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Lee Wilcox
Edgardo Garcia

SUBJECT: CARDROOM REVENUE
MEASURE UPDATE

DATE: August 7, 2018

Approved

D. D. Syl

Date

8/7/18

RECOMMENDATION

- (a) Defer placement of a cardroom revenue measure on the 2018 Citywide ballot and direct the City Manager and City Attorney to return to Council no later than fall of 2019 with ballot language and a resolution for Council consideration for placement on the March 3, 2020 citywide primary election that would extend the Cardroom Tax to gross revenues of Third-Party Proposition Player Services Businesses and expand the definition of Cardroom Business revenues to capture some cardroom revenues not currently used in calculating gross revenues for purposes of the Cardroom Tax.
- (b) Direct the City Manager to return to Council within 60 days with an implementation plan that may include revisions to Title 16 to address the City's ability to better regulate Third-Party Providers of Player Services
- (c) Direct the City Manager to engage the State of California, specifically the Bureau of Gambling Control, California Gambling Control Commission, Governor's Office, and Legislature, on the current state of gaming in California and possible changes to the State of California's regulation of gaming in the near future and report to the Public Safety, Finance, and Strategic Support Committee in April 2019.

OUTCOME

If the Council approves this item, the Administration will return to Council in fall of 2019 in advance of the deadline for placing items on the March 3, 2020 primary ballot with ballot language and a draft resolution to amend the City's Cardroom Tax to extend the Cardroom Tax to gross revenues of Third-Party Proposition Player Services (TPPPS) Businesses and expand the definition of gross revenues.

In addition, the Administration will bring forward changes to the City's gaming program and will continue discussions with the City's two cardrooms regarding potential changes to the Cardroom Tax that would be placed on the March 2020 primary ballot, business operation changes, and the current state of gaming at the State level.

BACKGROUND

On June 27, 2018 the Council directed the Administration to analyze and develop recommendations for extending the 15 percent Cardroom Tax to the two Third-Party Proposition Player Services businesses operating in the City, engage the City's two cardrooms on alternative approaches, and return to Council on August 7, 2018.

For background, Title 16 of the San Jose Municipal Code was enacted by the City Council on November 9, 1999 and restructured the City's gaming regulations. Title 16 establishes the City's gaming control regulatory program and sets forth the local requirements associated with expanding gaming within the City. Title 16, Section 16.04.030, states that the City Council shall not take any action to expand gaming in San José without voter approval. Section 16.04.030 defines "Expansion" to include an increase in: cardrooms or cardroom tables; use of slot machines or devices; and, any form of gambling which is not allowed under the Municipal Code on or before June 30, 1996, or which is prohibited under state gambling law on or before June 30, 1996.

Gaming in San José is also regulated under provisions of the State of California Gambling Control Act (the "Act"), Business and Professions Code, Division 8, Chapter 5. There are several so-called moratorium provisions that control the expansion of cardroom gambling under Article 13 of the Act. The Act requires that an increase to the current number of gambling tables in San José requires voter approval. Additionally, under the Act, any proposed amendment to the City's cardroom regulations in Title 16, whether effectuated by a City Council adopted ordinance or a measure approved by the voters, must be submitted to the State's Department of Justice for review and comment before adoption.

It is important to note that, while the State has authority over gaming regulations and the expansion of gaming in cities such as San José, the State has no authority to review or comment on the City's Cardroom Tax.

ANALYSIS

The Administration met with both of the City's cardrooms regarding a potential revenue measure for the November 6, 2018 ballot. Per Council direction, these conversations included:

- Increasing the Cardroom Tax rate;
- Increasing the number of tables each cardroom is permitted to have; and
- Extending the Cardroom Tax to those businesses providing third-party proposition player services in the cardrooms.

While the conversations were very productive, timing has become an issue for two major reasons. First, the City partnering with each cardroom to find a path forward became difficult because of time constraints related to placing a measure on the November 2018 ballot. The cardrooms operate differently, in terms of the types of games primarily played and clientele, so an increase in tables or changes to business operations are viewed very differently. Second, through these meetings, and the independent research of City staff, the Administration has found that the statutory and regulatory structure of the entire California cardroom industry is in flux in Sacramento, with powerful lobbying voices pressuring the State. These two issues are the main reason the Administration is recommending the City delay a revenue measure for 2018 and work jointly with the City's two cardrooms and Third-Party Providers of Player Services to pursue a strategy for the March 3, 2020 primary election.

Third-Party Providers of Player Services

The Administration still believes extending the 15 percent Cardroom Tax to the TPPPS businesses is a viable path forward, in addition to several alternative approaches, including increasing the existing Cardroom Tax and updating Title 16.

A TPPPS is a separate and distinct business entity which is under contract with, and operates in, a licensed cardroom with the specific purpose of banking the various games offered. State law and the San José Municipal Code do not allow the cardrooms to serve as the "banks." These provisions are unique to California cardrooms; traditional house-banked games are only permitted in Tribal casinos. Because the cardrooms cannot bank games, the owners rely on TPPPS businesses to collect and pay-off bets when an individual player does not take the option of covering bets on the table.

The primary threat to this operating model for cardrooms throughout California is an attempt, through the Courts and Legislature, to force the State Bureau of Gambling Control (BGC) to make player-banked games illegal. Given the 2018 election cycle at the State level, little action on this issue has been discussed recently. However, the Administration believes this issue, along with other possible changes, will be discussed beginning in 2019. In addition to the questions concerning the legality of the TPPPS businesses and limits on the expansion of gaming, the U.S. Supreme Court issued a decision on May 14, 2018 that will allow states to legalize sports gambling. The Court struck down a 1992 federal law that banned sports betting in most places.

While it is unclear if the State Legislature will take up this issue in the 2019 Legislative Session, some efforts in the current Legislative Session have been made to amend the State Constitution to enable sports betting.

Regulatory Changes

As staff has delved into the issues outlined here, it has become clear that revisions to Title 16 are needed to better regulate gaming, including the TPPPS businesses, particularly in light of the changes in the industry.

Next Steps

The added complexities and ongoing flux regarding State gaming regulations require a brief pause with the proposed tax measure. The additional time will allow for a more complete review and confirmation of cardroom and TPPPS revenues, and an informed analysis of their business operations, to more successfully fashion a ballot measure that increases revenue to the City and gives the two cardrooms additional tools they deem necessary for business operations.

The deadline for placing items on the March 3, 2020 ballot have not yet been released by the Santa Clara County Registrar of Voters, however, the requirement is that ballot measures be submitted no later than 88 days in advance of an election. Given the number of holidays falling in November and December, the Administration will work with the City Clerk and City Attorney to determine the timing of bringing forward a measure to amend the Cardroom Tax in the fall of 2019. The Administration will return with proposed ballot language and recommended needed actions in fall 2019, for placement in a 2020 citywide election, that could take place as early as March 2020 with the California primary election moved from June.

EVALUATION AND FOLLOW-UP

This item will return to Council in fall 2019 with ballot language and a resolution for placement on the March 3, 2020 primary ballot citywide.

COORDINATION

This memorandum has been coordinated with the City Attorney's Office.

COMMISSION RECOMMENDATION/INPUT

No commission recommendation or input is associated with this action.

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CEQA

Not a Project, File No. PP17-001, Feasibility and Planning Studies with no commitment to future actions.

/s/
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Chief of Staff
City Manager's Office

/s/
EDGARDO GARCIA
CHIEF
San Jose Police Department

For questions, please contact Lee Wilcox, Chief of Staff, at (408) 535-4873 or Dave Knopf, Assistant Chief, at (408) 277-4214.