



Memorandum

TO: PUBLIC SAFETY, FINANCE, AND
STRATEGIC SUPPORT COMMITTEE

FROM: Lee Wilcox

SUBJECT: STATE OF CALIFORNIA GAMING
REGULATION STATUS REPORT

DATE: April 3, 2019

Approved

Date

4-10-19

RECOMMENDATION

Accept a status report on the current state of gaming in California and possible changes to the State of California's regulation of gaming in the near future, based on discussions with the State of California, specifically the Bureau of Gambling Control, California Gambling Control Commission, Governor's Office, and Legislature.

BACKGROUND

On August 7, 2018, as part of its action to defer consideration of placing a cardroom revenue measure on the ballot, the City Council directed the City Manager to engage the State of California on potential changes to State regulation of gaming and to report back to the Public Safety, Finance, and Strategic Support Committee in the spring of 2019.

Two permitted cardrooms operate in the City of San Jose: Sutter's Place, dba Bay 101 Cardroom and Garden City, Inc., dba Casino M8trix. The City levies a Cardroom Business Tax on these two establishments, which is set at 15% of all cardroom gross receipts in excess of \$10,000. In 2017-2018, the City collected \$18.9 million in cardroom taxes. This revenue goes into the City's General Fund and is used to support City services.

The State Bureau of Gambling Control regulates the gambling industry in California, including San José cardrooms, under provisions of the State of California Gambling Control Act. The Act empowers the Bureau of Gambling Control to regulate several aspects of gaming in California, including reviewing and approving rules of games and gaming activities in all California cardrooms.

ANALYSIS

State Regulatory Activity and Tribal Lawsuit

Over recent months, the Bureau of Gambling Control has contemplated new regulations that would govern the types of games that can be played in cardrooms. State law does not allow cardrooms to offer house-banked games, where players wager against the house, and the house collects losing bets and pays winnings. Tribal casinos, on the other hand, are allowed to offer house-banked games pursuant to an approved gaming compact with the State.

As a result, many cardrooms rotate the dealer position among the players of a game, instead of having the house serve as the bank. Because recreational players often decline this player-dealer position when it is offered to them, Third-Party Providers of Proposition Player Services (TPPPS) often fill the player-dealer role in cardrooms. 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. 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.

In August of 2018, the Bureau of Gambling Control sent an email to the gambling industry expressing its intent to consider new rules for cardrooms that could potentially have an effect on the business model described above. In particular, the email expressed the Bureau's intent to "promulgate regulations to address rotation of the player-dealer position" and to "rescind game rules approvals for games too similar to 21/Blackjack that are prohibited by state law."

Potential new rules governing the rotation of the player-dealer position are of interest to the City because rule changes that undermine the role of TPPPS businesses in banking games could have consequences for San José's cardrooms and for City revenues. Beginning in October 2018, the Bureau organized a series of public workshops to solicit input on the rotation of the player-dealer position prior to starting a formal rulemaking process on the topic. City staff testified during one such workshop in Antioch on December 11, 2018 to urge caution on any significant changes to the rules governing the rotation of the player-dealer position, and to explain how the revenue from the City's two cardrooms funds City services.

The Bureau has held a total of six workshops on this issue so far. It intends to hold one additional workshop where it will provide draft rules language for public review and comment. The date and location of that workshop has not been set, but it is expected to be held in Sacramento.

The Bureau has also indicated its intent to withdraw game approvals for games that are "too similar to 21/Blackjack" games. These potential changes arise from concern that some versions of Blackjack offered in cardrooms are too similar to games that are exclusive to Tribal Casinos under state law. The two cardrooms in San Jose, Casino M8trix and Bay 101, estimated a loss of \$25.7 million in annual gaming revenue as well as over 150 jobs if cardrooms were not allowed

to offer Blackjack games. This loss of revenue to the cardrooms translates into an approximately \$3.85 million reduction in the City's General Fund revenue. In December, the City sent a letter to Attorney General Xavier Becerra expressing concern about the Bureau of Gambling Control's consideration to withdraw the approvals for certain variations of Blackjack. To date, the Bureau has not taken action to rescind approvals for Blackjack games. Bureau staff indicate that they are still reviewing the games with the Indian and Gaming Law Section of the Attorney General's Office. The Administration will continue to monitor any rulemaking activity on both the player-dealer rotation issue and the Blackjack issue and engage as appropriate to protect cardroom revenue.

On January 3, 2019, the Yocha Dehe Wintun Nation, the Viejas Band of Kumeyaay Indians, and the Sycuan Band of the Kumeyaay Nation filed a breach of contract lawsuit against the State of California, stating that "California's cardrooms have devised an ingenious four-prong system by which, under the guise of 'player-dealer' games, they offer banked card games like those played at Indian casinos, in violation of the California Constitution and California Penal Code." The Tribal Casinos maintain that they have exclusive right to offer Las Vegas-style gaming under Proposition 1A (2000). This lawsuit is still in its initial stages. On March 18, 2019, the State filed a motion to dismiss the lawsuit.

Currently, the legislature has not introduced any bills on changes to the player-dealer rotation or prohibiting cardrooms from offering Blackjack. The Administration will continue to monitor and engage on legislation that would significantly impact city cardroom revenue.

Sports Gambling Developments

Another notable development in gaming at a federal level involves sports betting. In May of 2018, the U.S. Supreme Court ruled in favor of the State of New Jersey in *Murphy v. National Collegiate Athletic Association*. The ruling overturned the Professional and Amateur Sports Protection Act prohibiting state-sanctioned sports gambling. Prior to this ruling, Nevada was the only state to offer a wide variety of legal sports betting. Currently, eight states now permit sports gambling, including Delaware, Mississippi, New Jersey, New Mexico, Nevada, Pennsylvania, Rhode Island, and West Virginia.

In California, proponents of an initiative to legalize sports betting, known as the "California Sports Wagering Initiative" started to gather signatures in August 2018 for the 2020 ballot. The initiative would have allowed licensed gambling establishments, such as cardrooms, to conduct on-site sports wagering; however, this campaign did not gather enough signatures to qualify the initiative for the ballot by the February 2019 deadline.

On the Federal level, at the end of the last congressional session, Senators Orrin Hatch (R-Utah) and Minority Leader Chuck Schumer (D-New York) introduced the Sports Wagering Market Integrity Act of 2018 to set federal standards and establish a framework for states around legalized sports betting. The legislation included language that would restrict online wagers to individuals living in the state, prohibiting wagering on amateur athletic competitions (excluding

PUBLIC SAFETY, FINANCE, AND STRATEGIC SUPPORT COMMITTEE

April 3, 2019

Subject: State of California Gaming Regulations Status Report

Page 4

Olympics and college sports), prohibiting wagers by those under 21 years-old, all athletes, coaches, and officials of sports organizations. The bill did not pass, but it is anticipated that the Sports Wagering Market Integrity Act will serve as a starting point for future legislation. The Administration will continue to monitor and analyze any federal legislation.

COORDINATION

This memorandum has been coordinated with the City Attorney's Office, the City Manager's Budget Office, and the Finance Department.

/s/

LEE WILCOX
Chief of Staff
City Manager's Office

For questions, please contact Bena Chang, Assistant to the City Manager / Director of Intergovernmental Relations, at (408) 975-3240.