June 10, 2016

The Honorable Adam Gray, Chair
Assembly Governmental Organization Committee
1020 N Street, Room 156
Sacramento, CA 95814

RE: OPPOSE – AB 2863 (Gray) as amended June 7

Dear Chairman Gray,

We deeply appreciate your leadership in bringing stakeholders together to try to resolve the outstanding differences regarding Internet poker legislation. Although we have made some progress under your leadership, we regret that your amendments of June 7 to AB 2863 related to suitability standards and taxation force us to oppose the bill.[1]

Suitability Standards

Our coalition remains committed to the policy principle that unlawful online gaming, whether in the past, present, or future, must not be incentivized. The federal Unlawful Internet Gambling Enforcement Act (UIGEA) clarified the legal status of online gaming in 2006, which caused all publicly traded online poker operators to withdraw from the U.S. market. However, as most online poker operators exited the market due to UIGEA several privately held offshore gambling websites made a conscious decision to continue operating in order to capture market share and grow their companies and brands by unlawfully accepting bets from U.S. players after October 13, 2006, when the UIGEA was enacted.

Not until 2011, when the FBI seized three of the biggest offshore gambling websites — Absolute Poker, Full Tilt Poker, and PokerStars — on allegations that from at least November 2006 through March 2011 those operators violated the UIGEA and the Illegal Gambling Business Act, did those firms stop accepting bets from U.S. players. Criminal indictments were handed down against certain owners and executives, including the founders of PokerStars who, to this day, continue to be fugitives under indictment by the U.S. government.

At a time when California was making painful budget cuts to education, public safety, and social services, these and other offshore poker sites evaded paying tens of millions of dollars in California taxes while breaking the law by taking bets from consumers in California and the U.S.

[1] As we have noted previously, we have other concerns with various provisions of AB 2863, but we believe that it is important to resolve the fundamental suitability and tax issues first.

California has an important public policy interest in ensuring that gaming licenses are not issued to persons or entities that have engaged in any form of unlawful or unauthorized gaming. In fact, one of the world's leading experts on gambling law, Professor I. Nelson Rose, recently opined:

> "The common law and public policy of every state hold that gambling is an illegal activity. State-licensed gaming is an exception to the general rule. Like any other exception to common law, gaming, including Internet poker, is strictly construed in favor of limiting the activity. This allows the state to deny licenses to applicants who do not comply with the state's requirements."

Furthermore, some of the same parties who now oppose robust suitability standards have previously testified to Congress that illegal foreign websites that violated federal laws should be disqualified from licensure. As the vice chairman of the Commerce Casino (PokerStars coalition member) told the House Committee on Financial Services on federal Internet gambling legislation:

> "For years, overseas sites beyond the reach of US law enforcement have offered Internet gaming to American customers in violation of US laws. In doing so, they have built brand name recognition and a strong customer base at the expense of American casinos and Indian tribes, who would have been shut down had they engaged in the same activities…Unfortunately, HR 2267 does not address this unfair situation because it allows illegal foreign sites to be licensed despite their past actions, when in fact <u>they should be deemed ineligible to ever be licensed</u>."

In March and again in May of this year, in the spirit of compromise, we proposed language that attempts to strike a balance between no meaningful suitability standards and more rigorous standards by providing applicants that may be deemed unsuitable due to prior acts the opportunity to rebut the unsuitable designation. This would allow an applicant to present clear evidence to the California Gambling Control Commission that the acceptance of illegal wagers was not knowing or intentional. This language should be acceptable and redeeming to persons and entities confident their activities were legal.

Unfortunately, the proposed language fails to provide any meaningful mechanism to assure that unsuitable entities are prevented from participating in the California market. Instead, the language would establish a rebuttable presumption specifically for those that accepted wagers from U.S. residents before the legislation's effective date, but sets a cutoff date of December 31, 2011.[2] This date is over five years <u>after</u> UIGEA was enacted, nearly 10 years after the U.S. Justice Department first opined that Internet gaming was illegal, and months after the FBI seized websites belonging to Absolute Poker, Full Tilt Poker, and PokerStars. In our view, using such a recent date grants a free pass to the most egregious foreign offenders that continued accepting online U.S. bets illegally after 2006 from offshore tax havens.

Further, the proposed language would allow the presumption that an entity is unsuitable for a license to be rebutted by simply showing that the activity "occurred within a reasonable time period in order to cease those activities in the United States." Simply put, we do not believe that it was reasonable for any entity to have continued accepting wagers five years after UIGEA's enactment. No other jurisdiction has adopted such a recent date. Doing so would serve only to reward those persons and entities that chose to violate U.S. law long after their competitors left the market.

---

[2] We understand that the December 2011 date was used because e the U.S. Department of Justice published its September 20, 2011, legal opinion on December 23, 2011, regarding the lawfulness of proposals by New York and Illinois to use the Internet to sell lottery tickets to in-state adults. However, that opinion is irrelevant to the legal status of Internet poker offered to U.S. residents by offshore companies. The opinion was very limited in scope (it expressed "no view about the proper interpretation or scope of UIGEA"), and opined about a different subject altogether: whether the federal Wire Act prohibits the intra-state sale of lottery tickets via the Internet.

With respect to the use of "tainted assets", the proposed language is even less effective. Rather than imposing a bar to the use of such assets or even imposing a rebuttable presumption, the proposed language would merely note that the Commission "may" impose limitations and conditions on the use of such assets. Thus, the proposed language could result in a situation where entities that violated U.S. law are able to use the fruits of their illegal activity, such as customer lists and brands, to unfairly compete against others in the market. We strongly believe that the legislation must be absolutely clear that no entity will be allowed to gain unfair competitive advantage, and thereby benefit from its past illegal acts. This should be a matter of State public policy – not a matter of discretion for regulators.[3]

Fees and Taxation

We also believe it is important that tax policy strike an appropriate balance between immediate revenue gains and sustained economic growth for the State.

Poker by nature is a social game – perhaps the quintessential American social game – and social games by their nature demonstrate lower margins than casino table games or slots. Social games rely on a high volume of small transactions to generate revenue and poker is no different. These games are characterized by low margins compared to casino style games; operators would be negatively impacted by high gross gaming revenue taxes.

We appreciate your thoughtful approach to this specific section; however we believe the proposed tax amounts require modification. While a tiered structure would allow the industry to launch, we note the only jurisdiction in the U.S. to offer only online poker is Nevada, which has set its tax rate at 6.8%.

Furthermore, that the upfront license fee of $12.5 million would no longer be subject to future tax credits undermines the viability of this new industry.

Sincerely,

Jeff Grubbe
Tribal Chairman
Agua Caliente Band of
Cahuilla Indians

Clifford LaChappa
Tribal Chairman
Barona Band of
Mission Indians

Margie Mejia
Tribal Chairwoman
Lytton Band of
Pomo Indians

Mark Macarro
Tribal Chairman
Pechanga Band of
Luiseño Indians

Robert J. Welch, Jr.
Tribal Chairman
Viejas Band of
Kumeyaay Indians

Leland Kinter
Tribal Chairman
Yocha Dehe Wintun
Nation

cc: Members of the Assembly Appropriations Committee

[3] We note that Nevada, which is widely respected as the leader in gaming regulation, also included a suitability clause in its Internet poker statutes. Specifically, Nevada created the classification of "covered assets" meaning, "any tangible or intangible asset specifically designed for use in, and used in connection with, the operation of an interactive gaming facility that, after December 31, 2006, knowingly and intentionally operated interactive gaming involving patrons located in the United States." Californians deserve suitability standards no less stringent.