

Office of the City Attorney
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May 7, 2009

Senator Rod Wright
California State Senate
State Capitol, Room #5064
Sacramento, CA 95814

Re: **OPPOSITION** to Senate Bill 213 (Florez) as Amended on May 5, 2009 relating to Gambling Establishments.

Set for hearing May 12, 2009 in Senate Governmental Organization Committee

Dear Senator Wright:

This letter is being written to state the opposition of the City of San José to Senate Bill 213 as amended in the Senate on May 5, 2009. More specifically, the City wishes to put on the record its opposition to two provisions to SB 213 that were added on May 5, 2009 which encroach on the City's ability to exercise effective local control over cardrooms that are permitted to operate in its jurisdiction.

Section 1 of the bill amends Section 19854 of the Business and Professions Code to create a new subdivision (e) which would allow a portable state key employee license to serve as a temporary local license if the holder of the license transfers to a cardroom in a jurisdiction that has a local key employee license requirement when the gambling establishment gives notice to the local licensing authority. This proposed provision allows the transferring key employee and his new employer to completely circumvent the local jurisdiction's procedures for gaining a key employee license. The purpose and effect of this proposed provision is to preempt local authorities from exercising local control over cardrooms in their jurisdiction. It is well to emphasize in this regard that prior to the Gaming Registration Act, and the more current Gambling Control Act, all regulation of cardrooms was left to local jurisdictions.¹

¹ The Gambling Control Act was enacted in 1997, and its predecessor, the Gaming Registration Act was enacted in 1983. The City of San José has had local ordinances regulating cardrooms since at least the 1950's.

Section 4 of the bill would add to the Gambling Control Act a new Section 19966 to the Business and Professions Code, which would impose upon local jurisdictions that regulate cardrooms, a requirement that the jurisdiction cannot appoint a person to manage or oversee the issuance of local gambling licenses, key employee licenses, or work permits, if that person, within two years prior to that appointment, was employed or retained by, or derived substantial income from, a gambling establishment, or was a principal in a partnership or corporation that was retained by, or derived substantial income from, any gambling establishment. The proposed Section 4 is an unprecedented and needless attempt to preempt local jurisdictions in their regulation of the qualifications of their officers and employees and it also has the unfortunate and needless effect of limiting the ability of local jurisdictions to hire well qualified persons who are knowledgeable about the industry that they are regulating.

With respect to the general issue of local versus state control over cardrooms, we take note that the California Legislature, when it enacted the Gambling Control Act (GCA) in 1997, specifically stated its intention to exercise concurrent jurisdiction with local governments and to allow them to promulgate their own gambling regulations. Business and Professions Code Section 19803 states that it is the intent of the Legislature, in enacting the Gambling Control Act, "to provide for uniform **minimum standards of regulation**" and "[n]othing . . . shall be construed to preclude" any local authority "from imposing **more stringent local controls or conditions** upon gambling than those imposed by" the Act. (Emphasis added.) *Gilbert v. City of San Jose* (6th Dist. 2003) 114 Cal.App.4th 606, 616.

The plaintiffs in *Gilbert* specifically argued that the Act preempts San José's Gaming Regulatory Control Ordinance (Title 16 of the San José Municipal Code). San José's Ordinance states, at the outset, in its statement of purpose section that: "It is the intent of the city council to regulate cardrooms and gaming activities in this city concurrently with the State of California, to the extent authorized by, and as required by, the Gambling Control Act . . ." (San José Municipal Code Section 16.02.010D.) The Court of Appeal held that the GCA does not preempt local ordinances regulating cardrooms that require applicants for licenses to provide personal information, noting that the Gambling Control Act provides only "minimum standards" and permits "more stringent local controls."

As noted above, prior to 1983, virtually all regulation of cardrooms in the State of California was left to the local jurisdictions that authorized legalized gambling. The Gambling Control Act and the Gaming Registration Act both acknowledge and honored the historic role played by local governments in regulating cardrooms and indeed, in deciding whether or not to even to allow cardrooms in their jurisdictions. In fact, the GCA specifically requires local jurisdictions that allows cardrooms to have ordinances with specific minimum standards of regulation.

We acknowledge the considered judgment of the Legislature which historically has left regulation of cardrooms to local jurisdictions, and in recent years has allowed concurrent state jurisdiction side-by-side with local governments.

The City of San José has existing procedures for key employee applicants to obtain temporary key employee licenses during the pendency of the regular key employee licensing investigation and we note that all of the employees and owners at our two permitted cardrooms, Bay 101 and Garden City, who are required to be licensed, have either temporary or regular key employee or stock ownership licenses. There is no requirement in the City's Ordinance that the Administrator issue a temporary key employee license. Under the City's Ordinance, issuance of a temporary key employee license is completely discretionary, SJMC Section 16.32.620. However, the City has issued temporary key employee licenses after a preliminary review and investigation where the City determines that issuance of the temporary license is consistent with the public interest and the policies of the Ordinance. We see no reason for the State to preempt the ability of a locality to evaluate and judge the qualifications of persons applying for key employee positions in a cardroom that owes its existence to an affirmative legislative act by the local governing body to permit legalized gambling.

It is our understanding that Garden City is the sponsor of the amendments to this bill. The Committee should know when it evaluates the amendments proposed by Garden City that the City has had a number of regulatory issues with Garden City's new owners, including a recent settlement of a regulatory disciplinary proceeding begun by the City against Garden City, Inc. and its new stock owners for violations of Title 16 and the City's Minimum Internal Control Standards Regulations governing the operation of the cardroom. These violations were in part related to Garden City's failure to have the required experienced personnel in the day-to-day management of the business. In addition, other violations included Garden City's inadequate security surveillance system. In July 2008, the City reached a settlement with Garden City, in which Garden City agreed to pay costs and fines in the amount of one hundred ten thousand (\$110,000.00) dollars and to surrender key employee licenses held by two (2) stockowners. Garden City further agreed to "stayed penalties" which would be triggered in the event of future significant regulatory violations within one year. These stayed penalties included an additional fine of one hundred forty thousand (\$140,000) dollars and a one-week suspension of the gaming operation at Garden City. We note in this regard the assistance of the Department of Justice Bureau of Gambling Control which concurrently issued a notice of violation of the state's gambling licenses after the City initiated its regulatory action against the Cardroom Permittee and the new owners.

The City's strict control over gambling within its borders is also based upon historic problems of corruption associated with local gambling in San José. In 1987, a criminal grand jury handed down an indictment of Garden City, Inc., all of its stockholders, and various Garden City officers and employees on a host of criminal charges, including

conspiracy to defraud their landlord, tax evasion, contribution laundering and skimming (I have enclosed a copy of the Third Amended Information for your information). In February 1993 all the stockholders of Garden City, the corporation itself, and a host of employees pled to various felony and misdemeanor charges that included profit skimming from GCI, grand theft, political contribution laundering and conspiracy to cheat and defraud the landlord. There were federal taxes, penalties, and interest amounting to approximately ten to twelve million dollars for the corporation and the individual shareholder defendants. In 1987, the State of California collected eight hundred thousand (\$800,000) dollars on a jeopardy assessment against the corporation.

The Chief of Police imposed a civil penalty in the amount of five million (\$5,000,000) dollars on GCI for the felony case, eighty thousand (\$80,000) dollars for acts committed by employees in Municipal Court cases. The Chief's Notice of Decision also required all the shareholders in Garden City, Inc. to completely divest themselves of all stock in Garden City, Inc.

On a more recent regulatory issue, the City has taken action to eliminate a recent, temporary backlog of new work permit applications caused by the decision of the new owners to change Garden City's business model. The new owners decided to terminate many of the existing employees when they assumed ownership of the cardroom and to rely instead on independent contractors to perform many of the job functions previously performed by long-time employees of the cardroom. This is in stark contrast to their competitor, Bay 101, which has maintained a more traditional business model that relies on regular employees, rather than independent contractors. Although Garden City filed an ill-considered mandamus action against the City over the backlog, the City had voluntarily initiated aggressive steps to overcome the backlog in new employee work permit applications prior to initiation of the lawsuit by Garden City. In fact, Garden City itself requested a continuance of the hearing on its application for a writ of mandamus, and the judge obliged by continuing the hearing for three weeks in anticipation that the backlog would be over in that time. We have attached the City's brief in opposition to the application for a writ of mandamus to this letter.²

We also note in passing, that two years ago, Garden City raised a number of issues with the Legislature in an attempt to circumvent San José's regulation of its cardrooms, and we have attached the October 24, 2007 letter that I wrote to Senator Dean Florez at that time responding to Garden City's unfounded accusations against the City and its gaming administration.

² Exhibit B to the City's brief is a cardroom work permit activity chart that clearly shows the difference in employment practices between Garden City and Bay 101.

Before closing, I would like to address Section 4 of the bill again. The proposed amendment to the bill is an unnecessary and unwarranted preemption intrusion into the City's authority to regulate the qualifications of its employees and officers, a task that should be left to existing state law that is applicable to all jurisdictions and to further specific regulation by individual jurisdictions that are tailored to local needs and concerns. There is no provision in the current Gambling Control Act that imposes on local jurisdictions statewide standards for the qualifications of its employees who are involved in gaming regulation. There is no need for this novel provision and it does not conform to the concurrent jurisdiction policy of the Gambling Control Act. We note that the City of San José has in its current Ordinance a code of ethics provision, see SJMC Section 16.46.010.³ Moreover, San José's civil service rules strictly regulate and restrict outside work employment by City employees. City employees cannot accept any outside employment unless it is preapproved by the City and no employee can engage in any outside work that is detrimental to the service, prevents or impedes the efficient performance of the employee's duties in his or her city employment, or which in any way is in conflict with his or her City employment, SJMC Section 3.04.1710.

In addition, Title 8 of the San José Municipal Code is devoted to ethics regulation. This title includes, for example, a gift ordinance applicable to all employees that is stricter than the gift regulations in the Fair Political Practices Act, SJMC Chapter 12.08. Chapter 12.10 of the Municipal Code details revolving door restrictions to prevent former officials and designated employees from using their positions with the City for personal gain and to prevent private for-profit business entities from gaining a real or

³SJMC Section 16.46.010 Code of Ethics

No City employee directly involved in the regulation of Cardrooms or the enforcement of any of the provisions of this Title shall knowingly engage in any of the following conduct:

- A. Accept any gift, favor, complimentary service or other item of value from any Cardroom Permittee, Licensee, or Work Permittee.
- B. Participate directly or indirectly in any Gaming activity on the premises of a permitted Cardroom, or obtain any service from any restaurant, club, or other business located on the premises of a permitted Cardroom except in the course of his or her official duties as a City employee.
- C. Pursue any outside business or employment on an off-duty basis that would conflict with his or her official duties as a City employee respecting the regulation of Cardrooms.
- D. Have any interest, financial or otherwise, direct or indirect, or engage in any business or professional activity which is in substantial conflict with the discharge of his or her official duties as a City employee respecting the regulation of Cardrooms.

Senator Rod Wright

Re: Position of City of San José in Opposition to Senate Bill 213 (Florez) as Amended on May 5, 2009

May 7, 2009

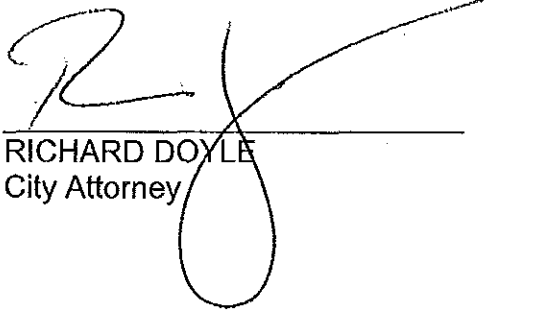
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perceived unfair advantage in dealing with the City by hiring former officials and designated employees.

As a matter of policy, the proposed Section 4 will have very negative effects on serious regulation of gambling at the local level by making it extremely difficult for cities and counties with legalized gambling to attract and hire well qualified applicants to manage local regulation of gambling establishments. The proposed provision would virtually eliminate from the pool of qualified applicants, the very persons with sufficient knowledge and expertise in the gambling industry to effectively administer and enforce strict local regulatory controls on gambling. Local governments must have access to persons who understand the business workings of the industry that they are going to regulate. Otherwise, regulation will be ineffective and fail in its purpose of protecting the public safety, health and general welfare of the people of the State of California.

For all of the reasons given above, the City of San José strongly opposes this bill as currently amended and requests your "no" vote.

Very truly yours,



RICHARD DOYLE
City Attorney

Attachments

cc: Senator Dean Florez
Members, Senate Governmental Organization Committee
Chris Lindstrom, Committee Consultant
Mayor and City Council
Roxanne Miller, Legislative Representative
Debra Figone, City Manager
Chris Shippey, Asst. City Manager
Robert Davis, Chief of Police
Richard Teng, Gaming Administrator

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May 22, 2009

Honorable Christine Kehoe, Chair
Senate Appropriations Committee
State Capitol, Room 2206
Sacramento, CA 95814

Re: **OPPOSE** - Senate Bill 213 (Florez) relating to Gambling Establishments
(cardrooms); Set for Hearing on May 26 in Senate Appropriations Committee

Dear Senator Kehoe:

This letter is being written to emphasize the City's position opposing SB 213 (Florez). The City has a history of local regulation of permitted cardrooms going back to the 1950's. The City's authority to regulate pre-existed state regulation of cardrooms and the state Gambling Control Act enacted in 1996 specifically recognizes the exercise of concurrent jurisdiction over gambling by local governments. Business and Professions Code Section 19803 specifically authorizes local governments to impose more stringent local controls and conditions on gambling than those imposed by the Act. The City's regulation of its cardrooms culminated in the 1999 adoption by the City Council of our Gaming Control Ordinance that comprehensively and strictly regulates the persons, locations and practices of permitted cardrooms. The current Gaming Administrator has been employed by the City since 2002. The Gaming Administrator reports directly to the Chief of Police and is tasked with implementing the 1999 Ordinance. The Chief of Police makes all licensing decisions.

The 1999 Ordinance required the Administrator to develop and promulgate regulations establishing minimum internal controls over all areas of cardroom operations. In 2004 – 2005, the Administrator implemented Minimum Internal Control Standards and Auditing Regulations for San José's cardrooms. Gaming revenues and City tax revenues rose dramatically after promulgation of the Regulations. Needless to say, it is the City's position that San José has an effective Gaming Administrator and an effective regulatory system.

The City agrees with the Gambling Control Commission that there is no basis for the employment restrictions in this bill. San José's employees are already subject to comprehensive local ethical restrictions on city employment. For example, former

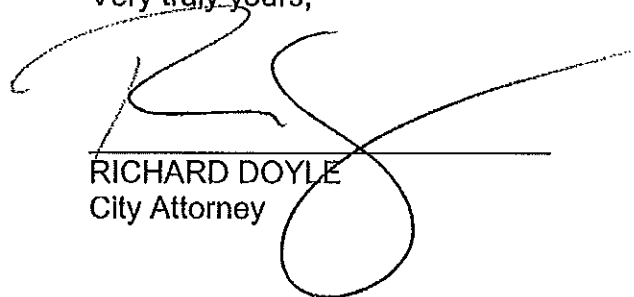
officials and designated employees are already subject to a two year revolving door work prohibition when they leave City office or employment, as is proposed for State employment in Section 3 of SB 213. Moreover, the City's own restrictions on officers and designated employees receiving gifts are stricter than the State's monetary reporting regulations under the Fair Political Practices Commission.¹

Although the Gambling Control Act has a pre-employment restriction on Commissioners to the Gambling Control Commission, the Act currently does not impose a pre-employment restriction on Department of Justice employees who work in the Bureau of Gambling Control, nor does this bill propose to impose pre-employment restrictions on applicants for employment with the Bureau. Only local governments would be subject to the pre-employment restrictions proposed in Section 2.

The pre-employment restrictions proposed for applicants for managerial positions in the local regulatory bodies will adversely impact the pool of qualified applicants who may apply for managerial positions regulating cardrooms at the local level by making it difficult to select persons who have substantial professional experience both in government regulation and in the regulated industry. It makes little sense to force local governments either to look at candidates with one-sided experience only in government or to have to look outside the State for applicants who have some balance of experience in the gambling industry and in government regulation of that industry.

We would remind the Committee of the importance of thoughtful and effective regulation. One need only look at the breakdown of federal regulation of the nation's financial institutions to see what can happen when professional regulation of the marketplace is hamstrung. The City urges the Committee to oppose this bill and continue to allow local governments to retain their historic primary role in defining and regulating the qualifications of applicants for local government employment.

Very truly yours,



RICHARD DOYLE
City Attorney

¹Under the City's Civil Service Rules, no employee can engage in any outside work without written authorization of the Department head. No City employee may engage in any outside work that in any way would conflict with City employment. The Chief of Police is responsible for approving any outside work request by the Gaming Administrator. Employees involved in the regulation of cardrooms are also subject to additional ethical limitations that are part of the City's Gaming Control Ordinance.

Honorable Christine Kehoe

Re: Position of City of San José in Opposition to Senate Bill 213 (Florez)

May 22, 2009

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cc: Members, Senate Appropriations Committee
Honorable Dean Florez
Maureen Ortiz, Senate Appropriations Committee Consultant
Matt Osterli, Senate Republican Fiscal Consultant
San José Legislative Delegation
Mayor and City Council
Roxanne Miller, Legislative Representative
Robert Davis, Chief of Police